Insolvent Retailers Working Group: Meeting 1

Date: Wednesday 16 October 2013

Time: 11.00 to 13:15

Venue: Gas Industry Co, Level 8, the Todd Building, 95 Customhouse Quay, Wellington

Minutes

Present

Members

- Joan Purdie
- Anna Carrick
- Andrew Maseyk
- Mark Hermann
- Rod Crone
- Jim Raybould *

In attendance from Gas Industry Co

- Ian Dempster
- Andrew Walker
- Pamela Caird
- Marianna Pekar
- Pip Kerfoot

* connected via conference call

1 Introduction and Gas Act context

The meeting opened at 11:00.

Ian Dempster welcomed members of the Insolvent Retailers Working Group (IRWG) and reviewed the background of the Insolvent Retailers workstream.

Ian reminded the group that following a consultation in December 2012, Gas Industry Co prepared a letter to the Minister of Energy and Resources in April 2013. Gas Industry Co's advice was that permanent backstop regulation is not necessary for retailer default, but that Gas Industry Co should develop drafting instructions for backstop regulations with the industry which could be tailored and implemented under urgency in the rare circumstances they are needed. The Minister approved Gas

Industry Co's recommendation on 17th September 2013.

Ian provided insight into how standard retailer insolvency would work, based on the Castalia Report's timeline.[1]

It was questioned by a member whether the Gas Governance (Insolvent Retailers) Regulations 2010 ('2010 Regulations') would have been robust if triggered, considering the compressed timeline for drafting. It was agreed that the 2010 Regulations provided a good starting point, but can be improved upon.

Ian pointed out that the output of the workstream is to produce 'drafting instructions' for the Parliamentary Counsel Office ('PCO'), which has the ultimate responsibility for drafting regulations.

Ian reviewed the empowering provision from the Gas Act and emphasised that Gas Industry Co cannot recommend regulations for a potential or likely insolvency. Regulations may only be made which apply once a retailer becomes insolvent.

Several comparisons and contrasts were made with the parallel workstream being carried out by the Electricity Authority ('EA').

2 Terms of reference

Marianna called for comments on the Terms of Reference.

There were no suggested changes to the Terms of Reference. However a few issues relating to customer transfers were raised by members including that:

- A recipient retailer would likely need access to additional gas supplies as its existing portfolio would be tailored to its existing customers. It was noted that in ordinary circumstances this shouldn't be a problem as the producer would want to sell the gas that was previously being sold to the insolvent retailer. It was also noted that there should be greater short term liquidity once the new trading markets mature.

- Use of System Agreements may allow a distributor to start its own customer transfer process and this could result in only a subset of customers being re-allocated under regulations.

- There is a risk of confusion in communications going out to the industry and customers if more than one process is being run (i.e. regulations in conjunction with either a separate distributor process or the process proposed by the EA)

[1] available here, Figure 2.1, page 4.

3 Issues raised in previous consultations

Marianna provided the group with a short list of issues raised by previous submissions on the 2012 Options Paper and invited members to raise any other issues.

The following points were raised by members of the group and discussed:

- Managing orphaned customers: the insolvency practitioner needs to be aware that it has a responsibility for all of the insolvent retailer's ICPs in the Gas Registry, not just those that are currently contracted. If the liquidator just sells off the contracts (as was the case with the E-Gas insolvency), this leaves a residual set of active-vacant and inactive ICPs with no responsible retailer (which has implications under the Gas (Safety & Measurement) Regulations 2012). There was discussion around how these residual ICPs should be handled as they wouldn't be deemed by the liquidator to be an asset and may be disclaimed rather than sold.

- It was suggested that all ICPs of the insolvent retailer (including active-vacant and inactive) should be transferred to recipient retailers. While allocating orphaned customers may expose recipient retailers to some credit risk, if retailers were allowed to pick and choose then it would be likely that some customers would not be transferred and an undesirable situation would eventuate. It was generally accepted that a random allocation to all recipient retailers remains the most effective and efficient way to deal with orphaned customers (and sites).

- There was a subsequent discussion on whether retailers should be able to opt-out of the customer transition. Comparisons were drawn between the 2010 Regulations (under which retailers with more than 10% market share were obliged to receive customers but those with less than 10% could also opt-in) and the EA approach, which includes an opt-out option for any retailer likely to encounter financial stress. Further background on the approach to retailer insolvency in the electricity industry was discussed. However, it was acknowledged that allowing retailers to opt out may have unintended consequences as remaining recipient retailers would receive greater numbers of customers (and that might cause more opting out).

- A group member also warned that there could be a mismatch between the records in the Gas Registry and in the insolvent retailer's system and that while this could be audited (ie an audit of the insolvent retailer's ICPs could be included in the regulations) this would only be a snapshot and would not prevent ICP statuses from changing over time post-audit. The discussion led back to the idea that assigning **all** residual ICPs to other retailers would be the

best way to ensure that they continue to be monitored.

- A further point was raised that the residual inactive ICPs would still incur network and GMS charges and the receiving retailer would have to cover these costs. Other members noted that this was part of the general 'pain' that should be shared between all retailers. A general process/method of identifying and distributing these ICPs in case of insolvency would be useful.

- Following on from the discussion on the insolvency practitioner's lack of appetite for dealing with uncontracted ICPs, it was suggested that the responsibility could be made clear via an amendment to the Gas (Switching Arrangements) Rules 2008 ('Switching Rules').

The issue of a preferred allocation of the insolvent retailer's dual-fuel customers to the same recipient dual-fuel retailer was raised by group members. Although dual fuel customers are not identified by the Gas Registry, they are likely to be recorded/linked in the insolvent retailers' billing system. However, that would be a major complication for any allocation algorithm and might not be feasible given that the EA process would likely precede any process for gas customers. It was noted that due to the existence of several large electricity-only retailers who would be included in any EA process there could be no guarantee that dual-fuel customers could maintain a single supplier.

Action:

- Gas Industry Co to organise meeting with EA to touch base again about dual-fuel retailer insolvency.

- Gas Industry Co to consider ways of incorporating the allocation of disclaimed ICPs due to retailer insolvency into the Switching Rules.

4 Framework for backstop regulations

Andrew provided the group with an overview of the 2010 Regulations and asked members to suggest changes to parameters found in the expired regulations.

(a) Triggers for invoking regulations

The discussion started with clause 10, "What happens if liquidator disclaims contracts." This clause describes the event that triggers the invocation of the regulations. It was agreed that while this remains an appropriate trigger for core parts of would-be regulations, there is also a subset of information that would be useful before this time so a double-trigger system could work:

- a pre-trigger, either when the retailer ceases trading or when a liquidator is appointed, which would allow Gas Industry Co access to information necessary

for customer transition should this be required. It was suggested that this pre-trigger could be placed in the Switching Rules; and

- the trigger for formal insolvency regulations which would be kept as the liquidator disclaiming customer contracts.

(b) Insolvent retailer providing information to Gas Industry Co

Clause 6 in the 2010 Regulations sets out that – once the regulations are triggered – the insolvent retailer must provide the industry body with information required by the industry body.

As noted above, Gas Industry Co will need information from the defaulting retailer before the regulations are triggered to prepare a customer/ICP allocation plan so ICPs are allocated to recipient retailers without delay if the insolvent retailer ceases trading. Gas Industry Co would like to avoid going through an information gathering process when the timing is pressed following insolvency and the insolvency practitioner will be focussed on other priorities. A logical way of ensuring that necessary information is received in time is to include rule(s) in the Switching Rules.[2] It was suggested that the level of information needed by Gas Industry Co concerning the defaulting retailer's customers would be equivalent to that contained in the EIEP4 (customer info) file in electricity. It was also noted that information concerning capacity reservations, meter reads, and the identity of the retailer's producer or wholesaler would be valuable to any transition process. It was then noted that some of this information would fall under the Privacy Act so should be suitably protected.

(c) Process for transferring contracts

Clause 8(2) of the 2010 Regulations sets out that Gas Industry Co must identify the recipient retailers, who must have more than 10% of the total number of ICPs for which the registry shows the status "active-contacted." Any other retailer can opt in if it wishes to be a recipient retailer.

Gas Industry Co is of the opinion that retailers should not be able to opt out from receiving orphaned customers. Submitters agreed that the 10% threshold is appropriate to maintain; lowering or abolishing this threshold could cause serious problems for small retailers who lack the systems and capacity to multiply their customer base caused by the allocation of a large number of orphaned customers. It was further noted that, if the insolvent retailer is particularly large (say 45% of the market), then even retailers above the 10% threshold may struggle as the transition could potentially double their customer base.

The scope of the customer transition was discussed by the group ie how large TOU customers (including those at direct connect gas gates) would be dealt with. It was

[2] if necessary, also in the Gas (Downstream Reconciliation) Rules, 2008 ('Reconciliation Rules')

generally assumed that if a large customer becomes orphaned, it can make its own arrangements to find another supplier, although the retailer insolvency would inconvenience this customer. It was agreed that a fair transition period should be given to large customers to negotiate supply contract with a new retailer. Group members agreed that 30 days should be a long enough time to find a new retailer. One member noted that distribution service providers would be reluctant to disconnect a large customer considering the effects of the disconnection.

(d) Transfer contracts

At the transfer time, the insolvent retailer's customers are transferred to the recipient retailers allocated by Gas Industry Co. According to the 2010 Regulations the customer contract's terms apply until the end of the transition period or the customer's switching, whichever occurs first. Transition period was specified by the regulation as 30 days following notification by the recipient retailer of that retailer's terms, conditions and price. This clause[3] was debated by group members who argued that integrating the insolvent retailers' tariffs into their system for a short period of time is at best difficult and may even be infeasible. Moreover, it can be detrimental if the prices were set too low by the insolvent retailer, which could have caused that retailer's insolvency. Additionally, even small customers can be on non-standard contracts; this would further complicate the recipient retailer's tariff system if terms and conditions need to be retained for the transition period. Group members suggested that offering these customers the recipient retailer's standard contract or 'better' for the transition period may be the best solution (this is the proposal in the electricity industry). There was an associated discussion about whether it is possible for retailers to compel customers to pay a different price to the one in the contract with the insolvent retailer.

Members suggested that the liquidator's letter informing customers that their contract is disclaimed should also contain the name of their new retailer, (new tariff) and notify them that they are able to switch/shop around.

(e) Effect of transfer on customers

Clause 12 of the 2010 Regulations sets out that the recipient retailer must not charge the customer any fee or penalty relating to the cancellation or the switch, while clause 13 explains that after the transfer time, any dispute that a former customer of the insolvent retailer has or had with the insolvent retailer must be dealt with between the insolvent retailer and the customer. During the transition period, a recipient retailer need not continue or commence any review processes that are required or authorised under customer contracts transferred to it.

The members noted that accepting the transitioned customers into their systems

[3] clause 9 in the 2010 Regulations

would not be a simple process, including because failed credit checks usually block switching and the creation of the customer account in the CRM system. One member reminded the group of a previous submission to the SoP that suggested orphaned customers must be subject to the same credit screening process as any other customers. However, a simple and random transfer of customer contacts results in retailers not being able to proceed with such a process. It was repeated that all retailer have to share the pain.

(f) Information to be provided after transfer time

Clause 15 and 16 of the 2010 Regulations request the insolvent retailer to provide Gas Industry Co and the Allocation Agent, respectively

- meter reading history covering the last 12 billing cycles for each transferred customer; and

- consumption information in accordance with rule 29-40 and rule 52 of the Gas (Downstream Reconciliation) Rules 2008 ('Reconciliation Rules').

Group members considered that the insolvent retailer might no longer have employees or systems in place by the transfer time and requesting the insolvent retailer to provide this information to Gas Industry Co upfront (ie part of the pre-trigger information) would be more effective. Gas Industry Co could pass on the information it receives in respect of any customer to the recipient retailer.

(g) Transmission capacity, enforcement, revocation

Group members believed that ensuring transmission capacity for recipient retailers might not be as easy as suggested by clause 17 of the 2010 Regulations. Some retailers might not need extra capacity, while others do, and the insolvent retailer may have benefitted from offsetting demand amongst its customers or may not have booked capacity to cover the combined load of its customer base. However, the formula in clause 17 provides for all of the insolvent retailer's reserved capacity to be transferred to those recipient retailers requesting such capacity. In addition, a shipper may have to request Vector to offer a Supplementary Agreement for transmission of gas in respect of specific end-users if they were being supplied under a Supplementary Agreement.

(h) Other issues to consider

The 2010 Regulations did not specify whether the regulations are only triggered by en masse disclamation of consumer contracts or even if a small amount of customers become orphaned. Further, it is debatable whether allocation group ('AG') 1 and 2 orphaned customers should be treated differently from AG4-6 customers.

The question emerged, how much time should be allowed to lapse between Gas

Industry Co notifying the insolvent retailer and all other retailers proposing to transfer the insolvent retailer's customers and the beginning of the transition period, starting with the transfer time, at which the insolvent retailer's customer contracts are transferred to recipient retailers.

Action:

- Gas Industry Co to incorporate group members comments into the draft 'drafting instructions' circulated prior to the next meeting.

5 Wrap up and next steps

Minutes will be circulated amongst members for comments.

Gas Industry Co will draft 'drafting instructions' and circulate it amongst members before the next meeting.

The meeting closed at 13:00.

Next meetings
Wednesday 27 November 11am-2pm