

## OVERSIGHT OF RETAIL GAS CONTRACTS – PROPOSED AMENDMENT TO THE INTERPRETATION OF BENCHMARK 16

Gas Industry Company Limited (Gas Industry Co) oversees the alignment of retail gas supply arrangements with a set of outcome-based benchmarks that were approved by the Associate Minister of Energy and Resources in 2010. In September 2010, Gas Industry Co published the Baseline Assessment against those benchmarks and, this year, we published the Transitional Assessment. The next assessment of retail gas contracts will be undertaken as at 1 July 2012.

With two assessments completed, Gas Industry Co has revisited the benchmarks and, more particularly, their interpretation as set out in *Retail Gas Contracts Benchmarks – Restatement 2011*.<sup>1</sup> Gas Industry Co is proposing to amend the interpretation of Benchmark 16, which currently sets out reasonable retailer liability limitations. It is proposed that the amended interpretation be applied by the independent reviewers in the 2012 assessment.<sup>2</sup>

Benchmark 16 states “Any exclusion of liability in the gas supply arrangements must be clearly specified and reasonable”. While it is relatively straightforward to assess whether an exclusion of liability is clearly stated, assessing the reasonableness of any such limitation can be more difficult. Gas Industry Co developed a straw man set of limitation levels to assist the independent reviewers in determining whether limitations of liability were reasonable.

Results for alignment with this benchmark have been low, although this may be indicative of the interpretation rather than actual non-alignment of contracts with the outcomes sought by the benchmarks. Retailers have suggested that the risks that would lead to a loss of supply are better mitigated by other industry participants (such as producers and pipeline owners), while customers are also able to protect their interests through insurance. Some retailers have also noted that no concerns with the reasonableness of the provisions have been raised in the retail electricity contract review process. Gas Industry Co has reconsidered the interpretation of this benchmark and has used the Electricity Authority’s similar contract review scheme as a guide.

Broadly speaking, the requirements set by Gas Industry Co and the Electricity Authority in relation to limitations of liability are similar. The Electricity Authority’s requirements<sup>3</sup> include:

**Principle 4.1:** *a Consumer Contract is to:*

- (c) *clearly set out the rights and obligations of both the Company and the Consumer...*

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<sup>1</sup> This benchmark was Benchmark 13 in the original Recommendation to the Minister in [month] 2010. A restatement of the benchmarks was issued in June 2011 following the Baseline Assessment and resulting in a change to benchmark numbering (see [http://gasindustry.co.nz/sites/default/files/u180/retail\\_gas\\_contact\\_benchmarks\\_feb\\_2011\\_155227.2.pdf](http://gasindustry.co.nz/sites/default/files/u180/retail_gas_contact_benchmarks_feb_2011_155227.2.pdf))

<sup>2</sup> The current Benchmark 16 and its interpretation are attached as appendix 1 to this letter.

<sup>3</sup> See <http://www.ea.govt.nz/our-work/programmes/market/consumer-rights-policy/domestic-electricity-retail-contracts/>

(g) *be fair and reasonable*

**Minimum Term 4.2:** *a Consumer Contract is to clearly set out:*

(d) *the Company's liability to the Consumer for damages and losses, and any liability caps that apply.*

While the electricity and gas assessment processes differ, Gas Industry Co supports harmonisation with the Electricity Authority's requirements wherever appropriate.

In light of these considerations, Gas Industry Co intends to amend the interpretation of Benchmark 16. The proposed revised wording is set out below:

Revised GIC Interpretation of Benchmark 16
<p>Liability exclusions are used to allocate the financial risk of certain events between contracting parties. Gas Industry Co interprets "exclusions" in this sense as including "limitations of liability" and "indemnities" that benefit the Retailer. It does not consider this benchmark currently addresses exclusions to the benefit of Consumers.</p> <p>The benchmark requires that allocations of financial risk be "reasonable". In this case, reasonableness depends on factors such as:</p> <ul style="list-style-type: none"><li>• what financial risks are involved (their impact and likelihood)</li><li>• who is best placed to manage the financial risks (including by way of insurance)</li><li>• what premium has been included in the charges to address the risk.</li></ul> <p>At this stage, Gas Industry Co has not performed a comprehensive analysis of these factors in the retail gas supply market. Until such time as this analysis is performed, an "exception approach" is to be applied to the assessment of reasonableness. Under this exception approach the reviewers are to assume that an exclusion of liability is not unreasonable and meets the benchmark, except where:</p> <ul style="list-style-type: none"><li>• the contract limits all of the Retailer's liability for all acts or omissions; or</li><li>• the Consumer is asked to indemnify the Retailer from any loss the Retailer may suffer as a result of the gas supply.</li></ul> <p>Gas Industry Co considers that a complete exclusion of all liability and/or requiring a customer to provide a full indemnity is clearly unreasonable, and in some cases may even breach the Consumer Guarantees Act 1993.</p> <p>As a consequence of this assessment approach, it is expected that the assessment of clauses limiting liability will primarily focus on whether any such limits are clearly stated.</p>

There is no change to the benchmark per se.

As noted above, the next assessment scheduled to commence on 1 July 2012. There will be full transparency in the 2012 assessment regarding each retailer's compliance and each arrangement will be published on a named basis.

Gas Industry Co also welcomes any comment on the revised interpretation of Benchmark 16. Please provide any comment to Jacki Eves at [jacki.eves@gasindustry.co.nz](mailto:jacki.eves@gasindustry.co.nz) by Monday 30<sup>th</sup> January 2012. Following consideration of any comments, Gas Industry Co will publish the amended interpretation in February 2012.

## Appendix 1

Existing interpretation of Benchmark 16, as previously circulated to retailers.

### **Benchmark 16: Reasonable retailer liability limitations**

“Any exclusion of liability in the gas supply arrangements must be clearly specified and reasonable.”

#### **GIC Interpretation in 2010 baseline assessment and 2011 transitional assessment**

##### *Background*

Liability exclusions are used to allocate the financial risk of certain events between contracting parties. Gas Industry Co interprets “exclusions” in this sense as including “limitations of liability” and “indemnities” that benefit the Retailer. It does not consider this benchmark currently addresses exclusions to the benefit of Consumers.

The benchmark requires that allocations of financial risk be “reasonable”. In this case, reasonableness depends on factors such as:

- what financial risks are involved (their impact and likelihood)
- who is best placed to manage the financial risks (including by way of insurance)
- what premium has been included in the charges to address the risk.

At this stage, Gas Industry Co has not performed a comprehensive analysis of these factors in the retail gas supply market. Instead it proposes the following approach as a “straw man”. This approach allows an initial comparison between Retailers that can be refined in subsequent reviews.

##### *Straw Man – Complete Exclusions*

Gas Industry Co considers that certain complete exclusions of liability are inherently unreasonable. Accordingly, the liability “exclusion” aspect of this benchmark will be scored as follows:

<b>Benchmark Score</b>	<b>Exclusion</b>
<b>Full</b>	No exclusions other than as permitted below.
<b>Substantial</b>	No liability for damage <i>to any other person</i> , as it is misleading for arrangements to purport to exclude liability in ways it is not possible to do. No liability for events that are <i>unforeseeable</i> , as they may still be within the Retailer’s control.
<b>Moderate</b>	No liability for damage <i>notified to the Retailer outside a specified time</i> , if that time limit is unreasonable.

**GIC Interpretation in 2010 baseline assessment and 2011 transitional assessment**

	No liability for the <i>quality or character of gas supplied</i> , as Retailers have regulatory obligations to provide quality gas.
<b>Low</b>	No liability for anything <i>other than its negligence or deliberate act or omission</i> , as ordinary breach should be actionable.  No liability for <i>all acts and omissions of subcontractors</i> (including network operators and meter readers), as Gas Industry Co considers that the Retailer should accept responsibility for subcontractors to the extent the Retailer would be liable had the Retailer committed the act / omission. The Consumer will not necessarily know what services are subcontracted.
None	No liability for <i>any of its acts or omissions</i> .

*Straw Man – Liability Caps*

Partial limitations of liability are harder to assess, particularly because of the many different approaches that Retailers can take. For example, a cap may apply to single events or to the contract in aggregate. Caps may apply to individual Consumers, or across multiple Consumers.

The liability “cap” aspect of this benchmark will be scored as follows:

Benchmark Score	Single Consumer		Multiple Consumers
	Per event or series of related events	In aggregate (including in 12 months)	
Full	\$500k +	\$600k +	\$100m +
Substantial	\$100-499k	\$150-599k	\$10m-\$99m
Moderate	\$50-99k	\$80-149k	\$2-9m
Low	\$10-49k	\$15-79k	\$100k-\$1.9m
None	\$0-9k	\$0-14k	0-99k

*Straw Man – Permitted Exclusions*

Benchmark not failed merely because:

- the Consumer Guarantees Act 1993 is excluded to the extent the Consumer is acquiring gas *for the purpose of a business*
- liability is excluded for:
  - *economic loss* (including loss of profit)

#### GIC Interpretation in 2010 baseline assessment and 2011 transitional assessment

- *indirect loss*
- *consequential loss*
- reasonable *force majeure events* (including events indirectly beyond the Retailer's control) except to the extent the force majeure purports to exclude events that may (in fact) be squarely within the Retailer's control (such as malicious acts of its employees)
- damage caused to *sensitive appliances*
- damage caused by the Consumer failing to *switch off appliances prior to reconnection*
- any interruption or reduction in the *supply of gas into the gas network*
- *risk* in gas supplied passes to the Consumer at the point of supply
- the Consumer indemnifies the Retailer against:
  - fines and other penalties due to any *failure of the Consumer's meter* to comply with industry codes or standards
  - failing to obtain the landlord's permission to install, modify, remove or replace any part of the network or metering equipment on your property, if the Consumer in fact agreed to this work
- liability limitations also benefit lines companies, network operators, meter readers and meter owners
- multiple Consumers under an arrangement are jointly and severally liable
- the Retailer may choose to replace any damaged property or goods, up to the same maximum amount, instead of paying cash.