

# MODEL RETAIL CONTRACT PROJECT:

## FRAMEWORK ISSUES

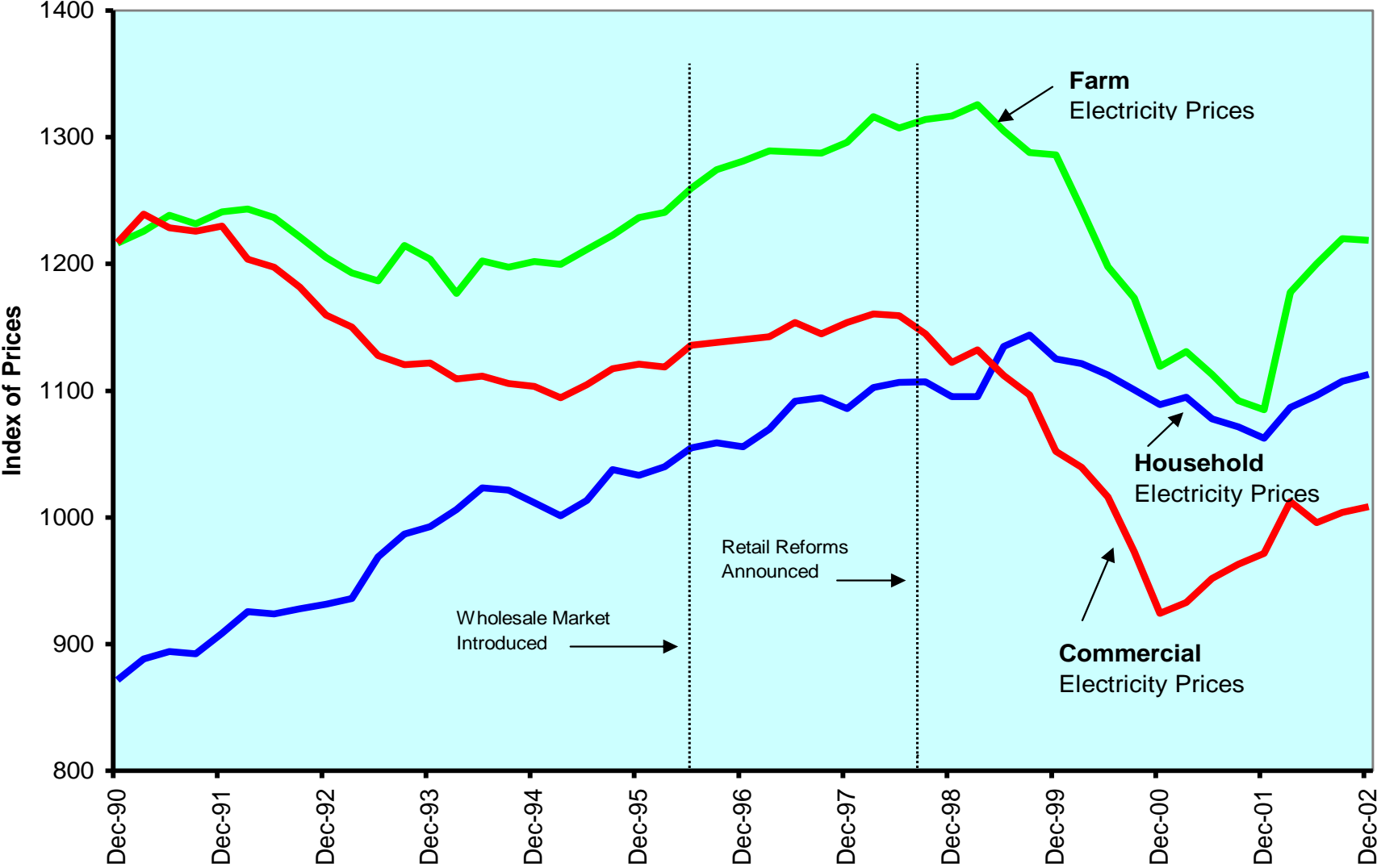
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27 August 2003

# Role of Retail Contract in Wider Economic Context

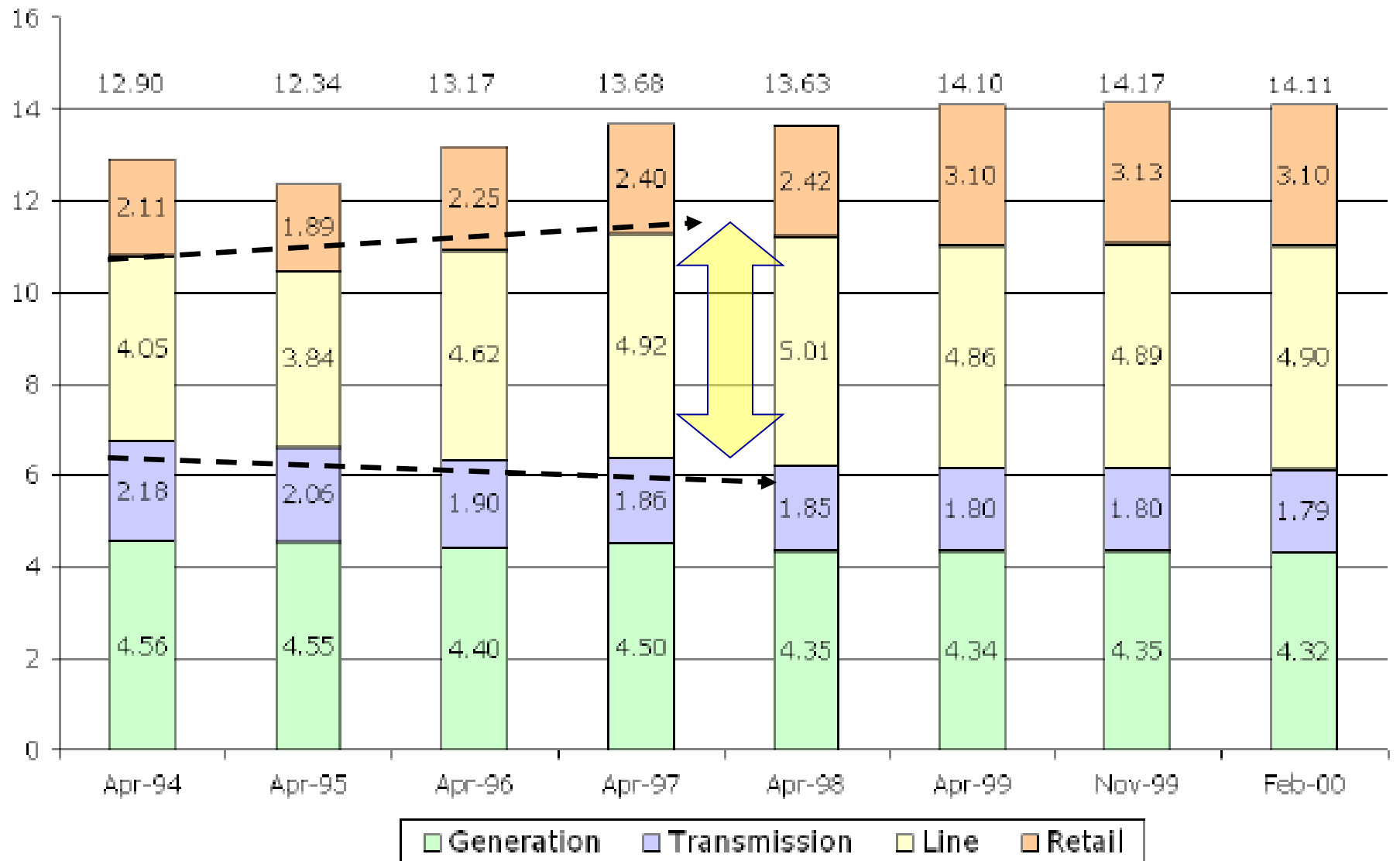
# ECONOMIC OBJECTIVES FOR INDUSTRY

- Strong downward pressure on costs
- Strong downward pressure on prices to reflect costs
- Strong pressures to innovate

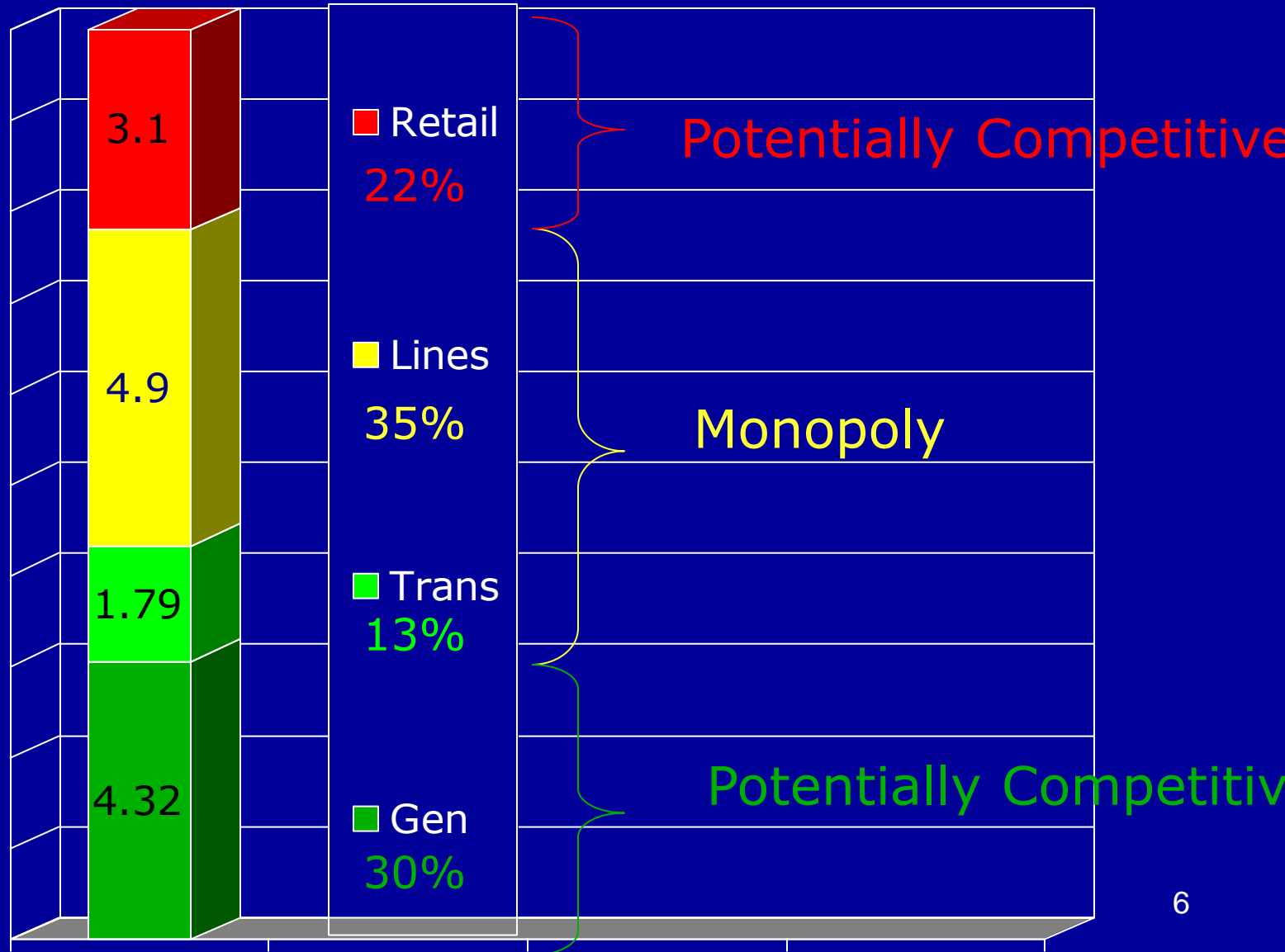
# Real Electricity Prices for Consumers 1990 - 2002

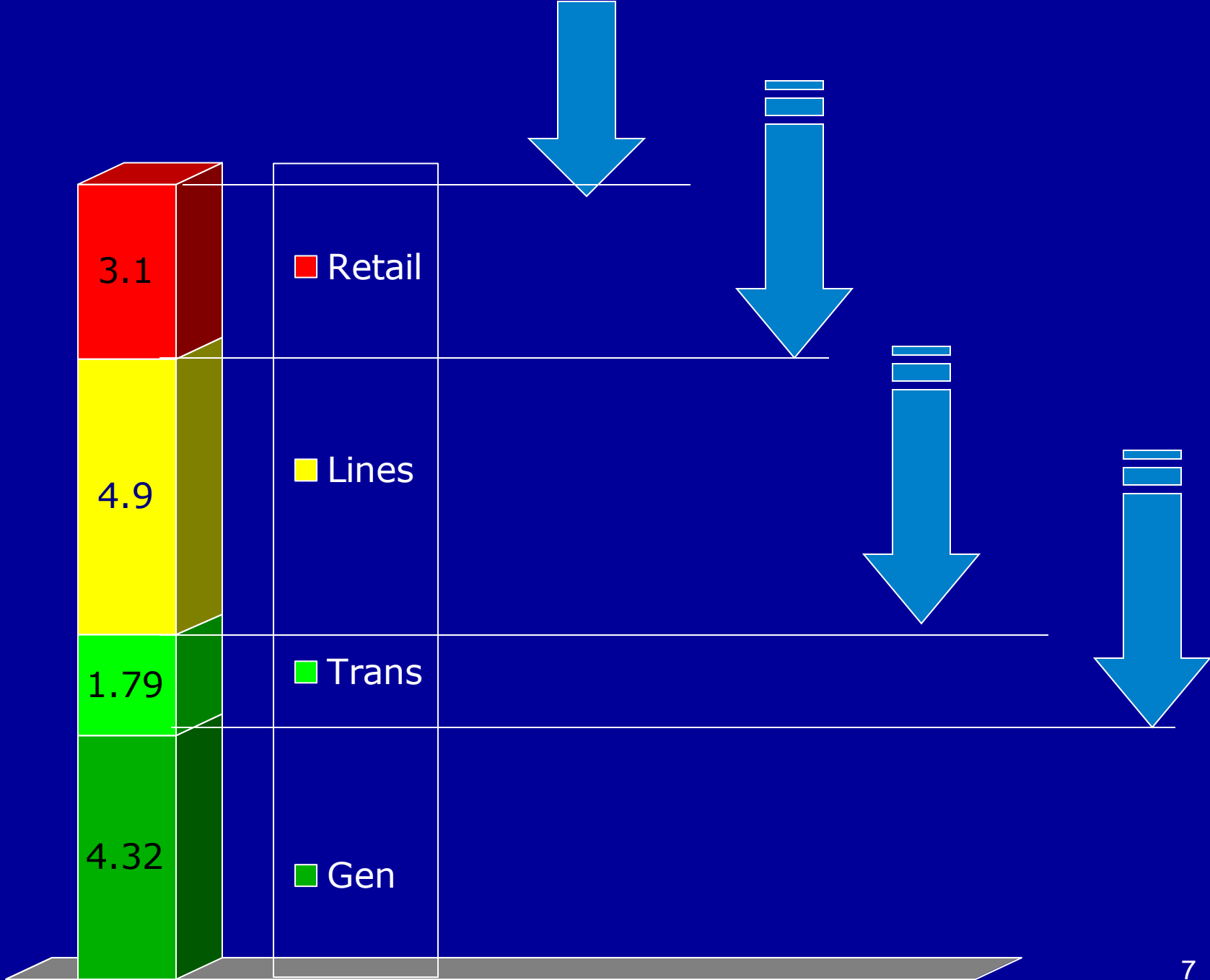


# Domestic Electricity Costs



# Costs for Consumers' Electricity





# KEY MECHANISMS

Effective retail competition

If not, then regulation



# EFFECTIVE RETAIL COMPETITION

*Two key components –*

- Real threat of customer switching
- Real threat of new retail entry

# NEW RETAIL ENTRY

## *Some key conditions -*

*In place:*

- Neutral access to lines Yes
- Ability to hedge nodal pricing differentials No
- Access to competitive wholesale supply contracts No
- Certainty of regulatory environment No
- Demand from customers for competitive retail services (particularly risk management on price and reliability) Limited

# CONSUMERS SWITCHING

*Some key conditions -*

*In place:*

- Retailer alternatives Some
- Easy consumer data transfer between retailers Yes?
- No inefficient restraints on consumer terminating contract ?
- Clear and timely information disclosure by retailer to consumer (particularly on prices) ?
- Active performance comparisons by independent agents Some
- Demand from customers for competitive retail services (particularly risk management on price and reliability) Limited

# OTHER RELEVANT FACTORS

- Culture of 'consumer sovereignty' is still relatively new and weak among retailers
- Consumers' relatively weak contractual bargaining position (with occasional media exceptions), due to fragmentation, poor information and lack of expertise
- Inelasticity of consumer demand – gives rise to fears of exploitation

# OTHER RELEVANT FACTORS

- Low awareness among consumers of supply and pricing risks
- Strong assumption by consumers of public provision and therefore government management of risks
- Weak retail competition – due to lack of transmission hedging + portfolio balancing by ‘gen-tailers’ = *de facto* regional monopolies
- Poor prospects of future retail competition – causes wider than issues relating to retail contract

# VALUE OF MODEL RETAIL CONTRACT

However, a good retail contract could:

- Reduce some of the barriers to effective retail competition (*promoting the economic efficiency objective*)
- Create stronger incentives for costs and risks to be managed within the contract in an economically efficient manner (even in a framework of weak competition) (*promoting the economic efficiency objective*)
- Counter-balance concerns relating to consumers' weak bargaining position (*promoting the fairness objective*)

# MRCPT AND ECC CODE PROCESSES

# HISTORY

- **June 2000:** Caygill Review notes problems in retailers' consumer services (particularly on billing). Concerned about lack of confidence in credibility of competition as an effective discipline on retailers
- **August 2001:** ECC scheme established
- **February 2002:** GPS calls for:
  - an industry code of practice with standards for contracts, particularly on billing, disconnection and metering (*paras 7, 29 + 30, GPS*) (*ECC responsible*)
  - a model domestic consumer contract covering charging, billing, dispute resolution, outage protection and retailer insolvency (*para 30, GPS*) (*MGB responsible*)



# HISTORY

- **October 2002:** Minister suggests ECC and MGB develop a joint working plan for model contract and code review processes
- **October 2002:** ECC starts code review process, governed by ECC constitution
- **Nov 02 – Feb 03:** Independent review of code
- **April 03:** ECC decides on proposed code changes

# HISTORY

- **May – Aug 03:** ECC consults with members + consumer groups
- **July 03:** MGB establishes MRCPT. No joint action plan with ECC

# NEXT STEPS

- **Possibly Sept 03:** ECC to recommend changes to Board of Council
- **Within 2 weeks:** Board required to establish Scheme of Amendment Committee (SAC). Appointments: 6 by Board + 6 Consumers Institute. SAC can only vote yes or no. Can't amend changes. Vote reported to Board.
- **Within 40 days:** Council members vote – only yes or no. Can't amend changes. Revised Code not likely to take effect before November 03.
- **Aug 04:** ECC constitution requires whole scheme to be reviewed

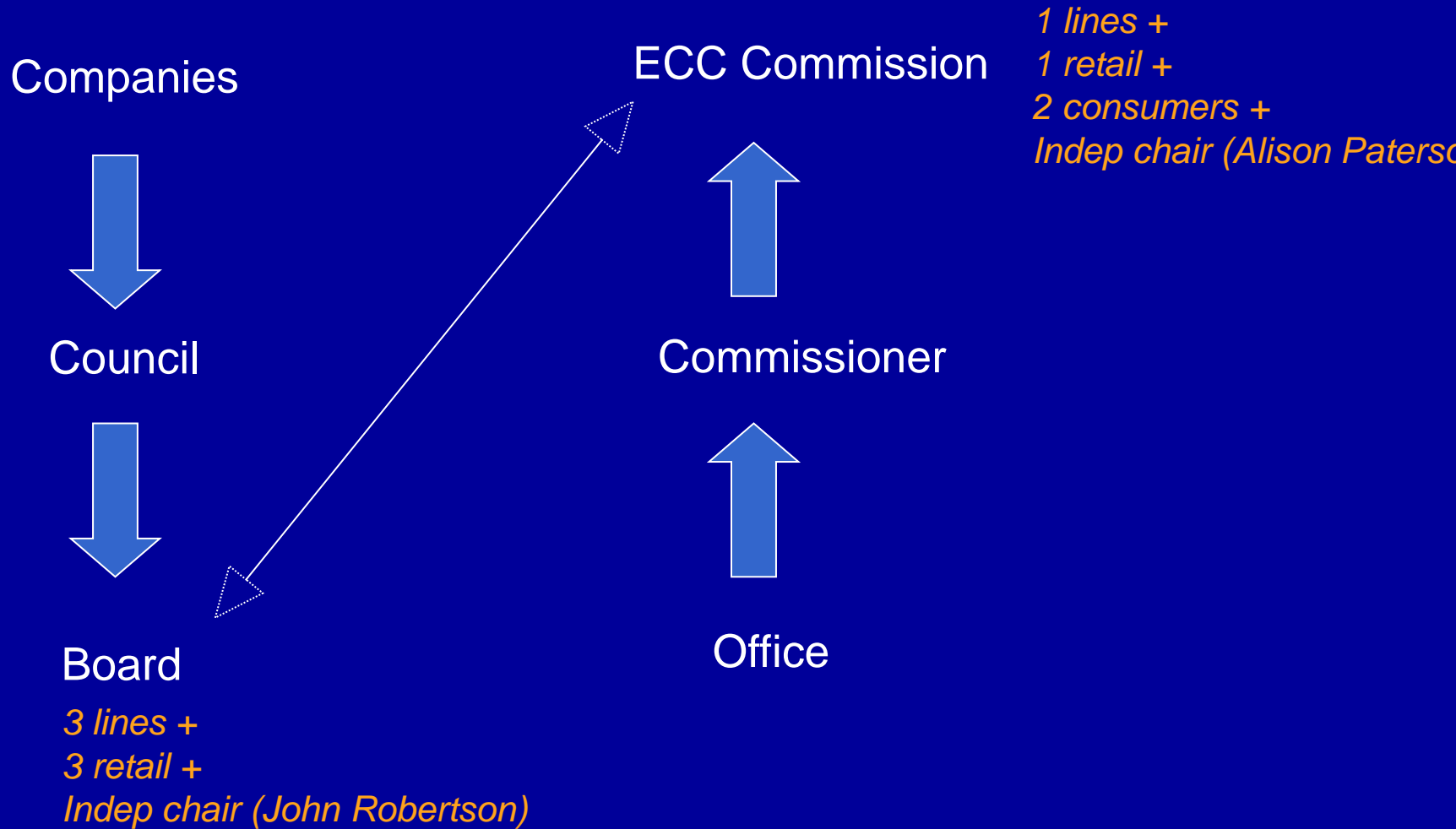
# NATURE OF CODE

- Largely a set of disclosure obligations. Only about 10 of 54 clauses set substantive minimum operating standards eg:
  - 7.1: 30 days notice of changes to contracts
  - 8.3: Quality of service to meet ‘good industry standards’ – to be established by a survey process
  - 10.1: Entitlement to refunds
  - 10.4: Self-meter reading
  - 13.6: 7 days notice of disconnection
  - 15.1: 4 days notice of planned shutdown
  - 19.2: Cap on retailer liability
- In concept, the Code is a set of principles, with details in contracts

# ECC COMMISSIONER'S ROLE

- Makes recommendations as to fair and reasonable settlement after applying:
  - Statute and common law
  - Contract between retailer and consumer
  - ECC Code (which prevails over contract if conflict)
  - 'Good industry practice' (GIP) (based on survey of retailers)
- GIP is, in effect, a means of amending the Code between formal reviews

# ECC SCHEME STRUCTURE



# OBSERVATIONS

- Concept of Code and Model Contract not clear at start, particularly how 'dove-tailed' and how specific
- Driven by concern to build public confidence in credibility of retail competition as a discipline on costs and prices
- Based on assumption of industry self-regulation – no longer valid (Govt threat to regulate if not delivered)
- Part B of draft EGB Rules left blank
- Poor planning and co-ordination between ECC and MGB – ironic given common membership

# ECC ISSUES

## August 04 Review - Possible Outcome:

- Council is dissolved
- ECC changes name to Electricity Ombudsman's Office – role narrowed to dispute resolution
- New Commission becomes responsible for Code – with minimum contractual requirements
- New Commission could also prescribe a model contract under Ministerial direction (giving legal force to GPS)



# ECC ISSUES

Current Code Review:

Should ECC pause to see shape of MRCPT work before recommending Code changes to Board of Council?

# MGB Issues

- How does MGB respond to:
  - Govt's call for a Model Contract
  - Possible role of new Commission
  - ECC Code review

# MGB Options

1. **No Change:** Continue current independent MRCPT process
2. **Seek to Integrate:** Option 1 as above, but try to dovetail with ECC Code review process (means ECC pauses). MRCPT continues if not possible
3. **Freeze:** Put MRCPT process *on hold* now pending completion of ECC Code review (recognising that ECC Council members have final vote)
4. **Abandon:** Cancel MRCPT process and promote single Code and/or wait to deal with new Commission on model contract

# COMMENT

- Options 3 + 4 involve:
  - Explanation to Government as to why no model contract
  - Risk new Commission will impose more prescriptive minimum requirements on retailers with less scope for retailer input
  - Perception within Government and new Commission of retailer failure of leadership and responsibility