



29 January 2007

Manager, MCE Secretariat
Department of Industry Tourism and Resources
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Canberra ACT 2601
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Dear Sir /Madam

RE: National Framework for Distribution and Retail Regulation’ – Working Paper 2

The Energy Retailers Association of Australia (ERAA) welcomes the opportunity to comment on the Retail Policy Working Group’s, ‘National Framework for Distribution and Retail Regulation’ – Working Paper 2.

The Energy Retailer Association of Australia (ERAA) has been concerned for some time about the nature of retailer and distributor relationships. This is primarily as a result of the asymmetrical bargaining power in the retailer-distributor relationship, arising from the role of the distributor as a monopoly service provider with no commercial incentive to negotiate on a fair and reasonable basis with retailers.

To date we have seen varying practices across jurisdictions as to how this relationship is managed, however we note that the general practice, is for regulators to inevitably impose a deemed “Use of System Agreement” upon the parties following an impasse in negotiations.

The term “agreement” is therefore misleading, because such instruments usually represent a default arrangement and, as a contractual rather than regulatory instrument, there is little innovation or variance that is available to retailers to capture and pass onto the customers.

The default agreements generally only serve to further limit distributors obligations with respect to service levels and liabilities, and essentially place distributors in an extremely strong position and diminish the sanctions available to retailers in the case of distributor non-compliance.

The ERAA believes that a more pragmatic approach would be to recognise that retailers and distributors would (in all likelihood) not reach an agreement and would usually rely on the model or default terms and conditions.

Reflecting their imposed rather than agreed nature, the model or default terms should be limited to commercial arrangements (such as billing, payment and credit support). Operational obligations should be included in the Rules, whereby the regulator's enforcement and compliance framework would apply, rather than requiring retailers to rely on lengthy and costly dispute resolution processes under the terms of the contract in the case of distributor non-compliance.

To the extent that an existing framework is adopted as a model, the Queensland Electricity Co-ordination Agreement should take that role. It is the most recently completed arrangement, and builds upon the industry's experience in other jurisdictions.

The ERAA has provided some detailed comments on relevant sections are provided below.

Should you require any further information in relation to this matter please feel free to give me a call on (02) 9369 3263.

Yours sincerely,

[\[Transmitted electronically\]](#)

Cameron O'Reilly
Executive Director
Energy Retailers Association of Australia

Section 4 – Contractual models for distribution services

The ERAA supports a triangular model for the provision of services, consistent with the position of the previous (Gilbert + Tobin) Consultation Paper. A direct distributor-customer contractual relationship appropriately allocates rights and liabilities related to the provision of distribution services in accordance with the parties best able to manage the risk and the associated issues, which, from the supply-side, is the distributor.

We are concerned that the Working Paper suggests that a pure triangular model is unworkable in the absence of any supporting evidence.

It appears as though regulators have ‘ruled out’ the triangular framework, often citing the inability of distributors to undertake billing and receipting functions. However this appears to be a narrow view of the role of a triangular model, and rather than concentrating on this particular aspect of service we would encourage the RPWG to examine how successful triangular arrangements operate at the moment.

We note that in jurisdictions such as South Australia, a triangular model exists, whereby the distributor essentially novates the billing, and receipting functions to retailers through the Agreement.

The only concern with the triangular model, to the extent that it is explicitly stated, is that the retailer should “take the customer credit risk,” and that such an arrangement is inconsistent with the triangular model. However, whilst this view of customer credit risk reflects conventional wisdom, it does not appear to be based on any rational assessment, or upon the examination of a model which has been tried and failed elsewhere.

The retailer is equally dependent upon the provision of distribution services, in particular metering, as the distributor is upon the retailer for customer billing. The distributors have fought long and hard to retain monopoly rights over the provision of metering service to small customers. The ability of the retailer to charge customers relies upon the provision of accurate and timely metering data, and it is only reasonable that with this reliance should rest a corresponding level of exposure. Compensation for that risk could easily be addressed through distribution pricing arrangements.

In addition, existing jurisdictional arrangements reflect the historical nature of the stapled distributor-retailer business, whereby it mattered little where the credit risk was located. Now over 60% of customers in NEM markets are supplied by an independent retailer.

6.4 (a)(i) How does the contract arise

The ERAA supports option 1, whereby a contract between the distributor and retailer is deemed to arise when any retailer supplies to a customer connected to the distributor's network. Options 2 & 3 are not supported on the grounds detailed above, that retailers are not in a position to negotiate with distributors acting as monopoly service providers.

Whilst there may be some instances requiring distributor-specific variations, these will be extremely limited, (often reflect individual customer connection agreements or retailer credit support issues), and if distributors are able to draft such variations they will do so, acting commercially, and in their own favour. In such a case, the distributor should be required to make an application to the AEMC for a variation to the default terms, with the AEMC determining whether to approve the application in accordance with the standard rule-change process.

6.4 (a)(ii) How are the terms and conditions of the contract regulated

The ERAA does not support providing distributors with the initial responsibility for defining the terms & conditions. Distributors will act commercially to draft the terms in their own favour. This will leave retailers in an untenable position whereby they will have little or no bargaining power.

The only realistic method of achieving a fair and reasonable outcome is, consistent with option 5, for the regulator to conduct a consultation process with retailers and distributors, balancing the competing interests, and determining the contract terms and conditions.

The working paper does not appear to recognise the reality of the retailer-distributor relationship with the use of phrases such as "the distributor and the retailer should have the flexibility to negotiate," and "if the parties are unable to agree." To date, retailers and distributors have been unable to reach an agreement, and the underlying blockage, i.e. the monopoly position of distributors, will not change to suggest that agreement will be any more likely in the future.

6.4 (a)(iii) What terms & conditions should apply?

The ERAA members have found that historically, regulators have been reluctant to intervene in disputes between retailers and distributors on the grounds that the Use of System Agreement is a commercial agreement. This is despite no agreement being reached (i.e. it is a default arrangement) and that retailers have no basis upon which to negotiate. As a consequence, when faced with distributor non-compliance, retailers must rely on lengthy and costly dispute resolution procedures, rather than regulatory sanctions were the obligations imposed by codes or rules.

This reflects an inappropriate view of such agreements being a contractual rather than regulatory instrument, the outcome of negotiations between two parties, each with a degree of bargaining power. In reality, retailers have no little power when dealing with distributors operating as monopoly service providers.

For this reason the ERAA recommends that the ensuing document be renamed the “Use of System Arrangement” and that it only deal with the commercial aspects of the arrangement, such as invoicing, payment and credit support. Other obligations, such as the provision of distribution services, connection, and disconnection should be included within the rules. This would ensure that the obligations placed upon distributors are subject to the enforcement and compliance regime consistent with other regulatory obligations and that retailers would not be forced into a lengthy and costly dispute resolution process when dealing with distributor non-compliance.

With respect to the actual drafting of clauses, we support the use of the recently completed Queensland Electricity Co-ordination Agreement, as the most current version of such arrangements, built upon experiences in other jurisdictions.