23 April 2021

Submissions
Ministry of Business, Innovation, and Employment
By email: energymarkets@mbie.govt.nz

Compliance Framework: Electricity

Meridian Energy Limited ("**Meridian**") welcomes the opportunity to submit on the Ministry of Business, Innovation, and Employment's ("**MBIE**") consultation regarding the electricity industry compliance framework published in March 2021. Nothing in this submission is confidential.

Meridian agrees with the Electricity Price Review's suggestion that review of the electricity industry and, in particular, the Electricity Authority's ("**Authority**") compliance framework has long been overdue. The Authority and the Rulings Panel ("**Panel**") and the legislative and regulatory framework that they operate within are crucial to a well-functioning electricity industry. So too is industry participants' confidence in the integrity and fairness of the system that governs them. However, Meridian believes the current institutional settings of the Authority and Panel undermine this confidence. It therefore supports measures to more clearly separate the Authority's ruling making and rule enforcing functions and establish greater independence of the Panel from the Authority.

In relation to the amendments to the Electricity Industry Act 2010 proposed in section 3 of the consultation paper, provided the above institutional issues are addressed, Meridian supports the increase to the maximum penalty (but to $1,000,000 not $2,000,000) and the introduction of additional penalties for continuing breach. That said, Meridian wishes to note that it believes MBIE overstates the deterrence of a penalty and understates the more powerful incentives for compliance (for example, serious risk to the health and safety of employees, damage to assets, reputation, and more severe intervention by the Authority or the Government).

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Finally, in relation to the amendments to the Electricity Industry (Enforcement) Regulations 2010 proposed in section 4 of the consultation paper, Meridian has mixed views about some of the proposed amendments. Some of the amendments have merit. For example, Meridian agrees it would be helpful to expressly allow the Authority to report to itself an alleged breach of the Electricity Industry Participation Code ("**Code**") rather than wait for an industry participant to allege or self-report a Code breach. Other proposals, however, require more consideration. For example, Meridian believes the proposal to allow industry participants to lay formal complaints with the Panel if the Authority does not decide to investigate an alleged Code breach would undermine the Authority's gatekeeper role in dismissing frivolous and vexatious claims and could lead to a proliferation of complaints being laid with the Panel.

In **Appendix 1**, Meridian has used the template provided by MBIE to set out its submissions in greater detail.

Please do not hesitate to contact us if you have any queries regarding this submission.

Yours sincerely

Sam Fleming
Manager Regulatory and Government Relations

Fayez Shahbaz
Legal Counsel

Appendix 1

Compliance Framework: Electricity - Have your say

Introduction

* 1. **Name (first and last name)**

Sam Fleming and Fayez Shahbaz.

* 2. **Email**

Sam.Fleming@MeridianEnergy.co.nz and Fayez.Shahbaz@MeridianEnergy.co.nz

* 3. **Is this an individual submission, or is it on behalf of a group or organisation?**

☐ Individual
☒ On behalf of a group or organisation

* 4. **Which group do you most identify with, or are representing?**

☐ Industry or industry advocates
☐ Market operation service provider
☐ Metering equipment provider
☐ Metering equipment owner
☐ Operator of an approved test house
☐ Load aggregator
☒ Ancillary service agent
☒ Electricity trader
☒ Electricity retailer
☐ Electricity distributer
☒ Electricity generator
☐ Line owner
☐ Transpower
☒ Electricity consumer with direct connection to the grid
☒ Person who generates electricity that is fed into a network
☒ Person who purchases electricity from a clearing manager
☐ Other (please specify)

*5. **Business name or organisation (if applicable)**

Meridian Energy Limited.

*6. **Position title (if applicable)**

Manager Regulatory and Government Relations and Legal Counsel.

7. **We intend to upload submissions to our website at www.mbie.govt.nz. Can we include your submission on the website?**

☒ Yes

☐ No

* 8. **Can we include your name?**

☒Yes

☐No

* 9. **Can we include your organisation (if submitting on behalf of an organisation)?**

☒Yes

☐ No

10. All other personal information will not be proactively released, although it may need to be released if required under the Official Information Act.

Please indicate if there is any other information you would like withheld.

Compliance Framework: Electricity – Discussion paper questions

Institutional Structure

Options and impacts

1

Should the rule making and enforcement functions of the Authority be split?

*Meridian Energy Limited ("**Meridian**") believes there would be clear benefits if the Electricity Authority's ("**Authority**") rule making and enforcement functions were split.*

The primary benefit would be enhancing industry participants' confidence in the integrity and fairness of the overall regulatory framework that governs them. A single Crown Entity responsible for making and enforcing the rules is not optimal and is susceptible to a perception that in enforcing the rules it may be unduly influenced by a desire to compensate for deficiencies or gaps in the rule making process.

The combination of rule making and enforcement functions also falls foul of orthodox administrative law principles: those who make rules should not also have the responsibility for interpreting or determining whether they have been breached. Consider, for example, the fundamental separation of powers between Parliament, which makes the rules, and the Courts, who interpret those rules and determine whether they have been breached.

Therefore, Meridian recommends that the Authority's enforcement division be transferred to a new independent agency. That agency would be entirely separate from the Authority in a legal, administrative, and operational sense (e.g. have its own legal personality, founding documents, office, funding, board, employees, performance objectives, and so on). To continue the analogy above regarding Parliament and the Courts, this agency would function like the Police. It would monitor compliance with the Code and investigate alleged breaches of the Code and either decide to discontinue any investigations or lay a complaint with the Panel.

Meridian acknowledges MBIE's concern that separation may entail a loss of cohesion and communication and result in additional administrative cost. However, Meridian believes these risks are small and that such concerns are outweighed by industry participants having enhanced confidence in the integrity and fairness of the overall regulatory framework that governs them.

Alternatively, if concerns about cost and a loss of cohesion remain, Meridian considers that greater confidence in the integrity and fairness of the overall regulatory framework can be better achieved by ensuring that there is stronger internal separation between the Authority's rule making and enforcement functions. To the extent they do not currently do so, the Authority could ensure that there are appropriate and robust information barriers between the rule making and enforcement functions In particular and at a minimum, Meridian would expect such teams to be based in different parts of the building, have separate reporting lines, and encouraged to avoid discussing their day-to-day functions with each other. This would enhance confidence in the integrity and fairness of the overall regulatory framework while mitigating some of MBIE's concerns.

Are there any examples of problematic 'blurring of functions' by the Authority in its decision making?

Meridian believes that there are at least two recent examples where the Authority may have problematically blurred its rule making and enforcement functions in its decision making.

*One concerns the high standard of trading conduct ("**HSOTC**") rule which the Authority now concedes is vague and open to interpretation.*

At page 8 of the Authority's consultation paper regarding its proposal to replace the HSOTC provisions with a new trading conduct rule, it referred to the investigation into Meridian's offers on 2 June 2016 and stated that: "The Authority decided this behaviour did not comply with a high standard of trading conduct and issued a warning letter to Meridian but did not lay a formal complaint with the Rulings Panel".

*In Appendix F of the same consultation paper at page 44 the Authority stated that: "In past decisions, the Authority has made it clear that [the behaviour in question] is prohibited under the trading conduct provisions." The Authority made this statement even though it has no responsibility for making decisions on whether matters breach the Code. That responsibility is given to the Rulings Panel ("**Panel**"). And the Panel has never consider that set of facts.*

*Under the Electricity Industry Act 2010 ("**Act**") and Electricity Industry (Enforcement) Regulations 2010 ("**Regulations**"), the Authority's role is to decide whether to commence an investigation into alleged breaches of the Code and appoint an investigator to try and reach settlement. If settlement is not reached, then the investigator will report a recommendation to the Authority. The Authority must then decide whether to discontinue the investigation or lay a formal complaint with the Panel "against the industry participant allegedly in breach".*

Accordingly, when the Authority makes statements to the market that certain conduct is prohibited by the Code and refers to its own previous commentary as "decisions" or "findings" it does so without any legal weight, and is problematically blurring its functions with that of the Panel.

A second example where the Authority has sought to use its enforcement function to compensate for apparent deficiencies in the rule making process relates to the industry transitioning to new dispatch software in late 2020 and early 2021. Clause 13.83 of the Code requires each generator to ensure it has appropriate personnel or facilities (emphasis added) to receive, acknowledge, and comply with dispatch instructions issued by the system operator. The existing software, GENCO, was scheduled to be decommissioned in December 2020 and industry participants were encouraged to transition to the new software before 1 January 2021 because GENCO would no longer be maintained and, therefore, would not be an "appropriate" facility for the purpose of clause 13.83.

Due to events related to Covid-19 and the availability of Transpower time for testing, Meridian was not able to transition to the new software before 1 January 2021. As a result, Meridian continued to use the GENCO software for a short time after 1 January 2021, with the system operator's support. This meant it arguably did not have appropriate facilities in place. However, it still had "appropriate" personnel in place to receive, acknowledge, and comply with dispatch instructions.

Despite this, the Authority's enforcement team advised Meridian that it was in breach of clause 13.83 of the Code. Meridian disagreed with this interpretation and considered that while the system operator was continuing to use GENCO to issue dispatch instructions during the transition, GENCO was an "appropriate facility". More importantly even if Meridian

didn't have appropriate facilities, the use of the disjunctive "or" in clause 13.83 between "appropriate personnel or facilities" meant the Code requirement could be satisfied by having "appropriate personnel" in place which Meridian did. The Authority's enforcement team disagreed and strongly indicated Meridian should self-report a breach. This was inappropriate and appeared to be an attempt by them to force a particular desired result despite the plain wording of the Code. Ultimately, Meridian self-reported the breach, despite not believing any breach had occurred. Concerningly, the Authority did not seem to act consistently as it did not put any pressure on the system operator to self-breach for continuing to use GENCO, despite the Code explicitly requiring the system operator to use an "approved system" to issue dispatch instructions and GENCO no longer being an approved system.

Is there a case for a separate agency approving and publicising settlements?
No. Meridian has not experienced any issues with the Authority being responsible for investigations, approving, and publicising settlements. However, as noted above, Meridian would like to see either a separate agency responsible for the Authority's enforcement functions or strengthened internal separation.

2

Do the Regulations provide sufficient transparency and definitive guidance for industry through the requirements to publicise approved settlements and decisions by the Authority? If not, what additional measures would you suggest and why?

Meridian believes that while there is sufficient transparency and definitive guidance at the settlement and decision stages, there remains a lack of transparency and definitive guidance by the Authority much earlier in the breach process, specifically, in relation to the process the Authority undertakes when filtering and investigating alleged Code breaches.

Meridian considers it is not enough to merely describe the Code breach process at a general level on its website (available here). The problem is once an alleged Code breach has been made or a breach self-reported, industry participants have little oversight or understanding of how the Authority is assessing the alleged breach or self-reported breach. It can take several months or in some cases over a year for a decision to be made (either discontinuance or appointment of an investigator) and in the intervening period industry participants just have to wait. The industry is also not informed of those alleged breaches or self-reported breaches that do not proceed to appointment of an investigator and a notice of investigation.

Meridian considers it would be helpful for industry participants to understand how the Authority undertakes its initial filtering of alleged Code breaches or self-reported breaches and have that available on the existing Compliance Database.

Meridian believes industry participants should see:

- *when they have self-reported a breach;*
- *when they have made a Code breach allegation against another industry participant or a Code breach allegation has been made against them;*
- *in respect of the above, what steps the Authority is taking, decisions made, and/or resources allocated (all pre the Authority's decision to appoint an investigator or not).*

There may be good reason for information about initial filtering decisions to not be public – unfounded allegations that do not proceed to an investigation could harm those participants against whom they are made. However, use of the Authority's Compliance Database would manage this risk while providing transparency for participants.

Finally, Meridian notes that the Compliance Database would benefit from a substantial upgrade. Meridian's experience with the Compliance Database is that it is not intuitive nor updated frequently enough by the Authority. For example, investigations that Meridian has joined should have all relevant correspondence from the investigator and interested parties attached and stored in the database. There are many gate closure revisions that have been submitted years ago to the Authority but still have the status 'query'. Furthermore, we are uncertain if anyone at the Authority is closing off recent gate closure revisions. Email alerts of when an investigator has prepared their recommendation and what that recommendation to the Compliance Committee will be, would also be useful.

3	**Should the Authority continue to be responsible for administrative arrangements for the Panel?** *Meridian believes the Authority should not be responsible for the administrative arrangements for the Panel. The Panel is meant to be an independent specialist decision making body. However, there are features of the institutional design that undermine the Panel's independence:* • *the Authority must fund the Panel (s 26, Act);* • *the Authority and Panel must agree on a budget and performance objectives on an annual basis (reg 113, Regulations);* • *the Panel reports quarterly to the Authority (reg 114, Regulations);* • *the Panel provides an annual report to the Authority (reg 115, Regulations).* *There are also other more subtle features of the relationship between the Authority and the Panel that tend to undermine its independence. For example, until 20 April 2021, the Panel did not have its own website. We note, as at the date of this submission, Google searches for "rulings panel" do not return results for this site and direct users to the Authority site. The establishment of a separate website for the Panel is a welcome, albeit overdue acknowledgement of the need for greater independence. Meridian would like to see this level of independence reflected in the legislative and regulatory settings and processes.* *Industry participants need to have confidence in the integrity of the regulatory framework that governs them. The features noted above tend to undermine that confidence by giving rise to a perception of a lack of independence. Orthodox legal principle establishes that it is not only a lack of actual independence that can erode confidence, a perception of a lack of independence can be equally eroding. That principle and concern should be case enough for the administrative arrangements to be moved away from the Authority.* *For these reasons, Meridian considers that the best model would be for the Panel to be entirely independent from the Authority with the administrative arrangements to be handled by MBIE.*

Amendments to the Act

Limits on liability

4	**Should the maximum penalty set out in s 54 of the Act be increased, or are current penalty levels adequate to deter harmful behaviour?** *While Meridian agrees with MBIE that, in principle, the maximum penalty in s 54 of the Act could be increased to better deter harmful behaviour, it has some reservations about the proposal and some of the rationale that underpins it.* *In particular, Meridian is interested in whether there is any evidence of industry participants flagrantly disregarding the Code because of the current level of the maximum penalty. We are not aware of this being a problem.* *Meridian considers MBIE overstates the deterrent effect of penalties and understates the other and more powerful incentives for compliance. Most industry participants strive for compliance because non-compliance can, among other things:* • *pose a serious risk to the health and safety of employees;* • *result in damage to assets;* • *damage reputation (which, in a highly competitive market where switching is relatively easy, can have other significant commercial consequences); and* • *lead to more severe intervention through Code amendments or legislative intervention by central government.* *Meridian considers the proposed increase from $200,000 to $2,000,000, an increase of 1,000%, goes too far Meridian suggests a more appropriate figure would be $1,000,000 per breach. That figure gives appropriate recognition to the deterrent effect of a penalty (and still represents a 500% increase) as well as the other incentives for compliance.* *Finally, if the maximum penalty is increased and additional penalties for continuing breach are introduced, then this would strengthen the case for greater independence of the Panel from the Authority (discussed in responses 1 and 3) and greater transparency of the Authority's internal filtering of complaints (discussed in response 2).* **Should additional penalties for a continuing breach be introduced?** *Meridian agrees that additional penalties for a continuing breach along the lines suggested by MBIE should be introduced. This would bring the regime in line with the other statutes noted by MBIE and increase the deterrent factor (noting that there are still other more powerful incentives for compliance).* **Are there alternative approaches to penalties which you would recommend?** *No.*
5	**If either or both of the above changes are introduced, should any changes be made to the limits to liability set out in the Regulations?** *If either or both of the above changes are introduced, then we agree with MBIE (at [50]) that the limits on liability set out in the Regulations should nevertheless remain at their current level.*

6	**How should closely related events be dealt with for breach and penalty purposes? Should the Act clarify that "a series of closely related events" would be treated as a single breach?** *While Meridian agrees with MBIE at [46] that the increase to the maximum penalty and the introduction of additional penalties for continuing breach may be sufficient to deal with this issue, there is nevertheless some merit clarifying that "a series of closely related events" would be treated as a single breach.*

Awarding of costs

7	**Should s 54 of the Act be amended to allow the Panel greater discretion to award costs?** *Meridian considers that s 54 of the Act should be amended to allow the Panel greater discretion to award costs.* *The ability of the Panel to award costs when it has found a breach of the Code is too narrow and limited. Meridian agrees that an industry participant that is responding to a complaint brought by the Authority or another industry participant which is found not to be a breach can impose significant legal cost, and the responding (and vindicated) industry participant should be able to recover that cost.* *Therefore, Meridian recommends that the Panel be given the same discretion to award costs as the High Court pursuant to the High Court Rules 2016. This could occur by simple amendment incorporating the costs regime of the High Court Rules.* *These rules are well understood and applied in practice. In short, under the High Court Rules, the general rule is that costs should follow the event. This means the successful party should obtain costs (whether that is the complaining industry participant, Authority, or responding industry participant).*

Amendments to the Regulations

Options and Impacts

8	**Should participants be able to lay complaints directly with the Panel if the Authority, after making preliminary inquiries, decides not to investigate an alleged breach?** *No. Currently, the Authority fulfils an important "gatekeeper" role to dismiss alleged Code breaches that are frivolous or vexatious. A decision not to investigate is not reached lightly and the Authority brings to that decision all the disciplines of being a subject-matter expert and a public body exercising public power (the same cannot be said of industry participants). The Authority's important role would therefore be undermined if dissatisfied participants were able to lay complaints directly with the Panel if the Authority decides not to investigate an alleged breach. It would also likely lead to a proliferation of complaints being laid with the Panel which would clog up the Panel.*
9	**Do mandatory attempts to settle create needless administrative burden and cost, and on-going uncertainty? Should the Regulations provide that an investigator "may", rather than "must", attempt to effect a settlement as part of the enforcement process?** *Meridian does not have a strong view on this issue. This is because, in practice, the administrative burden and cost of attempting to settle can be modest and the parties nevertheless have autonomy to refuse to settle (refer to "by agreement" in regulation 22) in which case the investigator can promptly proceed to write a report to the Authority together with a recommendation.*
10	**Does the Authority need more oversight and control of the enforcement of settlements?** *In principle, Meridian would support the Authority having more oversight and control of the enforcement of settlements. However, before Meridian can offer more support, it would be helpful to understand the extent to which this is a real issue. The implicit proposition that participants would flagrantly ignore settlements is to Meridian's knowledge unsupported.* **Should a breach of a settlement be enforceable as though it were a breach of the Code?** *If MBIE identifies evidence that there is a pattern of flagrant non-compliance with settlements, then Meridian would support some measures to introduce more oversight and control including amendments to make clear that breach of settlement be enforceable as an alleged breach of the Code enlivening the jurisdiction of the Authority and the Panel with the ordinary alleged Code breach process to follow.*

11	**Does the requirement for the investigator to endeavour to reach a settlement within 30 working days (or longer period agreed in writing by the investigator) create incentives for efficient process, given that it is rarely completed within this time?** *While the 30 working days does create an incentive for the investigator to encourage the parties to settle, the incentive is not a strong one in practice as it is relatively easy for the investigator to agree a longer timeframe. Given the limited compliance resources of the Authority and the fact that investigations of alleged Code breaches are often complex and difficult, this flexibility to extend the timeframes for settlement seems reasonable.* *The issues with compliance backlogs and delays in settlement processes, and delays in investigation reports and decisions (to discontinue or refer an investigation to the Panel) are, in Meridian's experience, attributable to a lack of compliance resources at the Authority rather than the legislative and regulatory settings.* **Should the requirement to endeavour to reach a settlement within 30 working days (or longer period agreed in writing by the investigator) in Regulations 22(2) and 23(1) be removed?** *No. Even if the timeframes are often extended it is better to have an upfront expectation of an efficient process rather than no timeframes at all (which seem to be the alternative proposed by MBIE). If the Authority considers 30 working days to be an unrealistic timeframe then the regulations should be amended to include a realistic timeframe alongside the option to extend. This would be preferable to no timeframe.*
12	**Are there circumstances where mandatory settlement is inappropriate?** *Meridian does not have a strong view on this issue and does not think characterising the process as "mandatory settlement" is accurate or that there is much cost or administrative burden associated with it. See response 9 above. The regulations only mandate the Authority to attempt to settle. Parties have autonomy to refuse to settle (and are aware of any competition law limitations on settlements) and the Authority can reject a proposed settlement even if the parties accept it.* **Should the Regulations be amended to provide that an investigator "may", rather than "must", attempt to effect a settlement as part of the enforcement process?** *See response 9 above.*

13	**Should the Regulations expressly provide that the Authority can report a breach under Regulation 9?** *Yes. If the Authority has identified a potential breach of the Code, then it should not have to wait for the participant potentially in breach to self-report or for another participant to allege a Code breach. If neither of those circumstances occur, then the Authority would be powerless to act. That is a peculiar outcome. That said, before expressly providing that the Authority can report breaches to itself, participants need to have the confidence that the rule-making and enforcement divisions of the Authority are truly independent. Therefore, the changes suggested in response 1 should be implemented alongside this change.* *To implement the change, Meridian recommends that the definition of "industry participant" in s 7 of the Act not be changed to include the Authority, as that would expose the Authority to the mandatory reporting obligations in the regulations and potentially trigger excessive reporting of potential breaches no matter how minor or frivolous. This would be a burden and impose unreasonable costs on the Authority and on the industry with no commensurate benefit. Instead, a new clause of the regulations should specify that the Authority may (rather than must) report potential breaches of the Code.*
14	**Are the Authority's obligations in relation to the treatment of information sufficiently balanced?** *Yes.* **Should the 'must keep confidential' obligations in Regulations 10 and 15 expressly provide that information which is not confidential in nature may be published?** *Yes. As long as confidential information is treated confidentially, then Meridian thinks it would be helpful to clarify that information that is not confidential in nature may be published. However, a process should be designed to cover a scenario where participants and the Authority disagree about whether a particular piece of information disclosed is confidential.* **Should the 'must publish' obligations in Regulations 28 and 30(3) expressly provide that where appropriate confidential information can be redacted from published reports?** *Yes, Meridian considers this would be a helpful change.*
15	**Should there be an express obligation on parties who receive confidential information during the investigation of a complaint or Panel process to hold that information in confidence?** *Yes, Meridian considers this would be beneficial to industry participants. This change would reflect the fact that settlement processes are not public processes but are visible to affected parties. The change would also give industry participants greater confidence to provide full and frank disclosure to the Authority and investigators.*

16	**Is it inappropriate that enforcement of the mandatory reporting obligations in the Regulations are undertaken by the Courts? Should the Regulations be amended to allow enforcement by the Panel of the mandatory reporting obligations as though it were a breach of the Code?** *Meridian disagrees that it is "inappropriate". The Courts are the appropriate decision-maker for breaches of primary legislation and regulations. However, Meridian agrees with MBIE that because the maximum penalty for a breach of a mandatory reporting obligation is $20,000, it is difficult to justify Court action. Therefore, Meridian also agrees there is merit in amending the Regulations to provide that a breach of the mandatory reporting obligation be treated as a breach of the Code thereby enlivening the jurisdiction of the Authority and Panel with the ordinary compliance process to follow.*
17	**Have we correctly characterised the impact of the changes, in terms of additional compliance costs?** *If this question is referring to Section 4 changes only, then Meridian agrees the impact in terms of additional compliance costs are likely to be modest.* *However, further cost benefit assessment may be needed if the question is referring to all of the proposed changes in this consultation paper, then Meridian disagrees and considers the additional compliance costs are likely to be significant.*

Any other issues

18	**Are there any other issues that we need to consider in relation to the compliance framework for the electricity industry?** *At this stage, Meridian has not identified any other issues for consideration.*