Better together.

Trustpower Limited

Head Office
108 Durham Street
Tauranga

Postal Address:
Private Bag 12023
Tauranga Mail Centre
Tauranga 3143

F 0800 32 93 02

Offices in
Auckland
Wellington
Christchurch
Oamaru

Freephone
0800 87 87 87

trustpower.co.nz

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Energy Markets Policy
Building, Resources and Markets
Ministry of Business Innovation and Employment
PO Box 1473
WELLINGTON 6140

By email: energymarkets@mbie.govt.nz

TRUSTPOWER SUBMISSION: COMPLIANCE FRAMEWORK: ELECTRICITY

1. Introduction and overview

1.1. Background

1.1.1. Trustpower Limited (**Trustpower)** welcomes the opportunity to provide a submission to the Ministry of Business Innovation and Employment (**MBIE)** on its *March 2021 Compliance Framework: Electricity* consultation paper (**the Consultation Paper**).

1.1.2. The Consultation Paper is MBIE's response to the suggestion from the Electricity Price Review that a review of the compliance framework is long overdue as important elements of its design dates back to the days of self-regulation in the 1990s.

1.1.3. We strongly support MBIE undertaking this review and note that we made a similar suggestion in our submissions during the Electricity Price Review process.

1.1.4. The Consultation Paper invites comments on the appropriateness of elements of the:

a) Institutional structure including the allocation of rule-making and enforcement functions between the Electricity Authority and the Rulings Panel;

b) Enforcement provisions in the Electricity Industry Act 2010 (**Act**) including in relation to penalties, liabilities and awarding of costs; and

c) Electricity Industry (Enforcement) Regulations 2010 (**Regulations**).

1.1.5. Our submission makes the following key points:

a) A more complete separation of rule-making and rule enforcement functions between the Electricity Authority and the Rulings Panel will improve institutional integrity and enhance the efficacy of the compliance function;

b) There is a case for increased penalty provisions and more flexibility to award costs but this should be accompanied by institutional separation; and

c) There are a number of refinements which can be made to the Regulations to improve the efficiency of the compliance process, promote transparency and better manage non-performance. Some aspects of the process detailed currently in the Regulations are only required because of the lack of institutional separation.

1.1.6. We strongly support MBIE considering these key points as part of the current opportunity to ensure a fit-for-purpose compliance regime for the electricity sector.

2. Institutional structure

2.1. Context for this consultation

2.1.1. New Zealand is fortunate to have a world class judiciary, which has an important constitutional role in ensuring the rule of law is upheld. This includes appropriate separation between the rule-making and rule-enforcement arms of government. The judiciary also plays an essential role in interpreting legislation made by Parliament.

2.1.2. However, the court process is costly and can be time intensive. For this reason, the industry during the time of self-regulation elected to appoint a specialist tribunal to facilitate the speedy resolution of disputes in relation to compliance with the industry rules. This specialist tribunal remains a feature of the present regulated industry environment.

2.1.3. Both the Electricity Industry Participation Code (**Code**) and the market have developed significantly since the 1990s when the Market Surveillance Committee was first established to oversee compliance with the rules which used to govern the wholesale and retail markets.

2.1.4. We now have a more complex supply chain, more sophisticated rules to accommodate new and diverse technologies and many more industry participants. These trends will continue as the industry embraces further digitalisation and decentralisation.

2.1.5. An inevitable consequence of the new trends is more market regulation affecting more organisations. It is also possible the complaints resolution process becomes part of the competitive interactions between market participants.

2.1.6. It is important that the increasing levels of market regulation are accompanied by a compliance regime which is fit for the evolving environment. This will ensure there is a timely and transparent resolution of claims; processes which reflect the complexity and significance of the subject matter; and an impartial, competent and well-respected decision-maker that is able to develop expertise over a range of similar decisions.

2.2. Separation of functions

Rule-making vs rule-enforcement

2.2.1. The Consultation Paper asks if separating rule-making and rule-enforcing functions is necessary to achieve a robust compliance regime for the electricity sector. Separation could involve the Authority transferring its rule investigation, early resolution, settlements and/or prosecution function to another agency.

2.2.2. The Consultation Paper forms an initial view that separation is not desirable as it might lead to a loss of cohesion and increased costs. We disagree and think an institutional separation will improve the integrity and focus of both organisations and enhance the overall efficacy of the compliance function.

2.2.3. Rule-making and rule enforcement are fundamentally different tasks, requiring different capabilities, processes and systems. Rule-making is concerned with net benefits and the achievement of statutory objective, whereas rule-enforcement is much more focussed on an

individual industry participant's behaviour and its consequences. A separate agency will allow both institutions to focus on the competencies and values most relevant to their tasks.

2.2.4. We think there is also a real risk that matters can be "held up" in the Authority where there may be competing demands for resources and/or other priorities. Without separation we are concerned about the potential for staff with overlapping rule-making and rule-enforcement responsibilities to influence the views of investigators, particularly on matters such as rule interpretation. There is also a possibility of influence over the timing of investigations. This could impact on administration matters as well as the speedy referral of rule breaches to the Rulings Panel.

2.2.5. We note it has taken ten years for the Rulings Panel to have its own website setting out current cases, decisions, procedures and performance reports. This suggests its activities have not been a high priority for the Authority.

2.2.6. It is also relevant that in relation to the investigation into the claim that Meridian and Contact Energy may have breached the High Standard of Trading Conduct (**HSOTC**) and undesirable trading situation (**UTS**) rules in late 2019 (**Haast UTS claim**), the Authority appears to have had resources to:

a) Investigate and issue the draft and final decisions on the Haast UTS claim;

b) Develop and consult on remedial action for the Hasst UTS claim;

c) Consult on replacement provisions for the HSOTC rules; and

d) Develop and advise its stakeholders on other policy processes aimed at assessing or curtailing market power;

but only announced that there was no breach of the HSOTC component of the claim on 22 April 2021.

2.2.7. A cynic might consider that the timing of this announcement was deliberately timed to occur after the progress made on the other matters. Even if this is not the case the delay in progressing this matter is demonstrably not fair on either the claimants or the defendants. Nor did the rest of the industry have any transparency as to the causes of this delay. We consider it would be preferable if the Rulings Panel had direct oversight of the progress of significant investigations.

2.2.8. The Consultation Paper refers to the importance of cohesion. However, the most important value for a rule enforcement agency is impartiality. This will be enhanced if there is institutional separation.

2.2.9. We accept that there will be some costs involved in separation. We think that these are justified. However, if this is of paramount concern, an alternative approach might be to have the Rulings Panel contract for administrative, investigation and settlement services from the Authority. This would enable it to set appropriate service levels for the delivery of the services and/or engage third parties (such as an independent barrister) to oversee certain cases as it sees fit.

2.2.10. Over the longer term it might even be possible to have less prescription in the Regulations as to how the investigation and early settlement process needs to take place. This is currently needed as a result of the co-location of roles that would normally be separated.

Scope of current compliance roles

2.2.11. Both the Authority and the Rulings Panel have decision-making roles in relation to the compliance framework.

2.2.12. Currently the Rulings Panel only has jurisdiction over the matters which are referred to it following an investigation process undertaken by the Authority. If the Authority decides that no

action is to be taken, the matter will not proceed. If the Authority negotiates a settlement or withdrawal of a claim, then that action does not need to be approved by the Rulings Panel.

2.2.13. In addition to separating rule-making and compliance investigations, we think it is essential that there is a separation between investigations and settlement approval. This would occur if the Rulings Panel, instead of the Authority, needed to approve all settlement agreements.

2.2.14. The effect of the current allocation of work is that the Rulings Panel currently considers very few cases each year[1]. Often only one case. There is a risk that such a low volume of work will adversely impact on the pool of people prepared to make themselves available for this specialist role, given the high standards of independence required. Consequently, if a choice is to be made as to whether the enforcement role should sit with the Authority or the Rulings Panel (as opposed to a new agency), we think it should sit with the Rulings Panel.

2.2.15. More broadly we note the Consultation Paper expresses reservations about the "number of legislative amendments" required to institute institutional separation. This needs to be assessed against the value invested in the businesses and assets which are being regulated.

Problematic dual jurisdiction

2.2.16. Currently the Rulings Panel is responsible for most but not all compliance decisions. This anomaly is not discussed in the Consultation Paper.

2.2.17. For example, the Rulings Panel does not have jurisdiction over the declaration of, and corrective action related to a UTS under Part 5 of the Code although it does have jurisdiction over the extent to which the HSOTC rules might have been breached – a matter which is often pleaded at the same time as a UTS.

2.2.18. This allocation of roles dates back to the period of time when UTSs needed to be resolved in the period between provisional and final prices. However, now that this no longer applies it is important that the responsibility for the determination of all Code breaches rests with the specialist tribunal formed for that purpose. We note that it would also be far more efficient if two sets of proceedings on the same facts can be joined as would occur in the court system.

Financial independence

2.2.19. The Authority administers and funds the Rulings Panel. The Rulings Panel reports to the Authority. This is because Regulations 113 to 115 provide for the Rulings Panel to be accountable to the Authority in relation to its annual budget, performance objectives, monthly costs, cost variations, and to provide it with quarterly and annual performance reports.

2.2.20. We do not consider this arrangement is appropriate. Instead we agree with the recommendation of the Authority – first made in 2014- that the Rulings Panel should be administered by, and accountable to, the Ministry of Justice.

2.3. Transparency on settlements

2.3.1. As noted above we do not think it is appropriate that settlements should be approved by the same body undertaking the investigation (i.e. the Authority). Instead we think settlements should be approved by the Rulings Panel. The Rulings Panel would then be well placed to provide guidance to participants on any problematic areas of the Code – using anonymised cases if required. This would be in addition to the obligation under the Regulations to publish approved settlements.

[1] We note that the Rulings Panel may be required to consider more cases in the future as a result of the new regulated Default Distribution Agreement arrangements.

3. Penalties, Code breach events, liability limits, and costs

3.1. Adequacy of maximum penalty

3.1.1. We agree that the potential consequences of a failure to follow the Code could run into the tens of millions of dollars, whether as a result of a security of supply event or abuse of market power. It is for this reason that we favour enhancing the institutional independence and capability of the Rulings Panel. If this is done, we would also support an increase to the maximum penalty to $2,000,000.

3.1.2. We also agree that the maximum penalties for failing to comply with a compliance or suspension order appear low.

3.2. Continuing and recurrent breaches

3.2.1. We agree that a series of closely related events arising from the same cause or circumstances should be dealt with as a single event and only attract one penalty. If the events are not closely related than clearly multiple breaches may have occurred.

3.2.2. We are not concerned about the prospect that a party might deliberately continue a breach for an extended period, noting that the duration of an offence is a matter which is considered when the penalty is determined.

3.3. Limits on Liability

3.3.1. We note the Authority commissioned an expert report from TDB Advisory in 2014 which undertook a first principles review of the liability arrangements that should apply for market operation service providers, ancillary service agents, asset owners, and in respect of (electricity) metering standards and metering information.

3.3.2. TDB Advisory's review concluded there were net benefits in having a specific liability limit for the relevant service providers, structured using a combination of per event liability and absolute liability caps. It also set out suggested limits for each category of service provider.

3.3.3. We recommend the advice in this expert report be adopted.

3.4. Costs

3.4.1. We note that there is no charge for access to the enforcement service. Currently the Rulings Panel may make orders against a party found in breach "regarding the reasonable costs of any investigations and proceedings". However, we think the Rulings Panel should also be able to award costs against the party laying a complaint which is not upheld.

3.4.2. We acknowledge that a balance needs to be struck between ensuring the Code is complied with and the deterrence of claims without merit but believe that the Rulings Panel should be entrusted with exercising its discretion appropriately.

4. Procedural requirements in Regulations

4.1. Direct complaints

4.1.1. We do not think the Authority, or any substitute enforcement agency, should be the gatekeeper for making complaints direct to the Rulings Panel on Code breaches. Participants should be able to lodge complaints themselves if the enforcement agent elects not to do so. The possibility of an award of costs should deter complaints which have no basis in fact or law.

4.1.2. We agree that the Authority should be able to report a breach under the Regulations.

4.2. Settlements

4.2.1. We agree that not all alleged Code breaches are amenable to a settlement process. In some cases it will be more efficient to refer a matter directly to the Rulings Panel. This will particularly be the case where there is a wide range of parties affected, or parties have strongly opposed interests. Rather than a mandatory requirement to seek settlement within thirty days we would prefer it if the enforcement agent operated to guiding principles which stressed the importance of early resolution of complaints and seeking settlement in suitable circumstances.

4.2.2. We have suggested that the Rulings Panel should have the power to approve settlements. It follows that they should also have oversight and control over enforcement of settlements they have approved. We consider that a breach of an approved settlement agreement should be a breach of the Code.

4.3. Publication of information

4.3.1. We agree that information provided or disclosed to the enforcement agent in relation to reported breaches which is not confidential in nature should be allowed to be published. This will enhance transparency of the compliance process.

4.3.2. We agree that publication obligations in the Regulations should be amended to clearly permit confidential information to be redacted from published reports.

4.3.3. We also agree that there should 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.

4.4. Mandatory reporting obligations

4.4.1. We agree that a breach of the mandatory reporting obligations should be treated as though it were a breach of the Code.

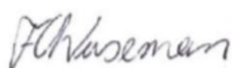
5. Concluding remarks

5.1.1. In a number of places, we have found the Consultation Paper has insufficient information for those not familiar with the detail of the current regime and its prior reviews. For this reason, we would have found it helpful if this consultation was preceded by a workshop which worked through case examples of the core matters from the perspective of market participants and regulatory practitioners as well as the Authority and the Rulings Panel.

5.1.2. The consultation is an important opportunity to reset the current compliance regime. This is an opportunity which must be seized to ensure the industry is supported by a fit for purpose compliance regime going forward. We look forward to continuing to engage with MBIE on this important topic.

5.1.3. For any questions relating to the material in this submission, please contact me directly on 027 549 9330.

Regards,



Fiona Wiseman
Senior Advisor, Strategy and Regulation