

COVID -19 Retailer Debt Deferral Scheme proposal to close

Decision

20 October 2020



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1 We have decided to close the retailer debt deferral Scheme early

- 1.1 The Electricity Authority (Authority) has decided to amend the Electricity Industry Participation Code 2010 (Code) to remove clauses 12A.5B to 12A.5E of the Code.
- 1.2 These provisions constitute the retailer debt deferral Scheme (Scheme), which was enacted by urgent amendment to the Code during the COVID-19 lockdown on 20 May 2020.
- 1.3 We have considered the ongoing need for the Scheme against its original objectives and the current customer debt levels in the industry.
- 1.4 We sought feedback on whether the Scheme was needed and whether it should be closed ahead of its expiration on 20 February 2021. The feedback was broadly supportive of closing the Scheme early.

We consider that, given the limited objectives for which the Scheme was originally put in place, the Scheme is no longer needed and believe that closing the Scheme early has net benefits.

2 Background

- 2.1 On 1 September 2020 we published a Consultation paper titled *Retailer Debt Deferral Scheme feedback on proposal to close - Consultation paper*.¹ We consulted on whether the Scheme was needed and whether it should be closed early. The key logic in that consultation paper was the Scheme was only ever intended to be a limited and targeted solution to the unprecedented and unexpected impacts of the first COVID-19 lockdown that began in April 2020:
 - (a) The Scheme sought to address immediate cashflow concerns for retailers should they arise as a consequence of the lockdown and materially increased customer non-payment of bills.
 - (b) Entry into the Scheme was deliberately limited – retailers needed to be otherwise financially sound, and the Scheme sought to direct them first to their shareholders for further cashflow support.
 - (c) For qualifying applicants, the Scheme provided deferral of two months of distribution charges from the six largest distribution companies until 20 February 2021. The deferral would account for about half of an average retailer’s distribution cost. To qualify, a retailer would have to demonstrate it had a 25% increase in overdue receivables and needed the funds to remain viable.
- 2.2 This paper sets out the Authority’s decision to amend the Code to close the Scheme and confirms the reasons for that decision, consistent with the consultation paper. Details on the option to close the Scheme early are contained in the consultation paper.

¹ [Consultation paper](#)

- 2.3 Closing the Scheme early involves revoking clause 12A.5B to 12A.5E of the Code.
- 2.4 The amendments will come into force 28 days after the date of the Gazette notice. We anticipate the Code will be revoked mid-November 2020.
- 2.5 More information about the Scheme is available [here](#).

3 Feedback from submissions supports early closure of the Scheme

- 3.1 We consulted on the option of closing the Scheme early or leaving the Scheme in place until it expires on 20 February 2021. We carefully considered the seven submissions we received, along with up-to-date information from industry.
- 3.2 Feedback from the consultation to close the Scheme early has been largely supportive. Eight submitters (representing the Electricity Networks Association, four Electricity Distribution Businesses (EDBs), and three retailers) supported the closure of the Scheme². One submitter (Electric Kiwi) opposed.

Feedback in support of Closing the Scheme.

- 3.3 Six submissions supported the proposed amendment with Vector noting:

“The Scheme was ... intended to avoid cascading retailer failure that would reduce retail competition and choice for consumers.

“Given there has only been one application to access the Scheme, which was unsuccessful, we agree with the Authority that the likelihood of retailers accessing the Scheme going forward is very low. We also agree that, with residential and commercial electricity debt continuing to remain within historical levels, the likelihood of cascading retailer failure is very low. As such, the continued existence of the Scheme has become unnecessary and unwarranted.”³

- 3.4 While supportive of the closure of the scheme, a number of submitters such as Trustpower, did not believe the scheme was necessary in the first place.
- 3.5 The Authority is moving to close the scheme as it is no longer needed, however our view is that the Scheme was appropriate and measured given the potential for a more serious economic outcome at that time, and that it would have been too late to act if we had waiting for such an outcome to manifest itself.
- 3.6 Ecotricity, Flick, and Pulse Energy agreed with this one aspect: *“an effective ‘insurance’ mechanism is in place before it is needed.”* However, they also submitted that the scheme was poorly targeted.⁴
- 3.7 Ecotricity, Flick, and Pulse also stated they *“do not agree that the potential for consumers to suffer acute or severe financial impacts from this pandemic has passed / no longer exists”*.⁴ Concerning this point, the Authority had not stated that the potential for customers to suffer severe impacts has passed. The Authority acknowledges these

² [Three retailers submitted jointly](#).

³ [Vector submission, 15 September 2020](#).

⁴ [Joint submission, Ecotricity, Flick, Pulse, 15 September 2020](#).

risks, however we consider retailers have now had time to prepare and that the larger issue is an income issue which is beyond the scope of this Scheme to address.

- 3.8 Submitters who supported closing the scheme also highlighted a desire for a concerted effort to address some remaining systemic risks. PowerCo stated *“Looking ahead, the prospect of further disruption to the economy from Covid19 is anything but negligible. It would be no surprise to see increased pressure [for] market mechanisms to manage bad debt – especially if there are income-related combined with an expectation that retailers need to maintain electricity supply to their customers.”*⁵

Feedback opposed to closing the scheme

- 3.9 The submitter (Electric Kiwi) who opposed closing the Scheme early raised a number of points to support their position:

- (a) The benefits proposed in the cost-benefit analysis are not material and therefore not a justification
- (b) The basis for needing the Scheme – “including the risk of ‘revers[al of] decades of progress to establish robust retail competition’ – have not gone away”⁶
- (c) The delay of the release of the consultation paper as Auckland moved back into lockdown is a relevant consideration
- (d) The lack of successful applicants does not demonstrate lack of need
- (e) The Scheme should be extended and criteria liberalised
- (f) If the Scheme were to be closed, it poses the question of ‘what then to protect competition?’

- 3.10 Staff carefully considered the submission supportive of continuing the Scheme. These points are addressed below.

- (a) We agree that the estimated monetary costs and benefits are not material, but we consider the larger benefit gained by closing the Scheme early is in allowing parties to focus their resources on other activities, and removing an ongoing, unknowable, potential financial exposure for the six distributors involved.
- (b) While we agree that financial challenges arising from COVID-19 are ongoing, we consider that the nature of these challenges is different from those which the Board considered when approving the urgent Code amendment. Traders have had time to adjust to the residual and emerging risks discussed by the submitter. We continue to monitor retailers and consumers for material changes in debt levels. Current debt levels are in line with debt levels for the previous year.
- (c) The potential for parts of New Zealand to go back to COVID-19 lockdown was considered. We view this condition as part of the risk environment in our ‘new normal’ and note that participants have taken steps to mitigate financial impacts.
- (d) We agree that the lack of successful applications does not, in itself, provide definitive evidence that the Scheme is not needed. However, the small number of applications (successful or not) is a useful indication. This data point was

⁵ [PowerCo submission, 15 September 2020.](#)

⁶ [Electric Kiwi Submission, 15 September 2020.](#)

considered alongside other evidence, including submissions, with only one submitter supporting continuation of the Scheme, and information obtained through the section 46 on the overall level of debt and the capacity of retailers to manage this.

- (e) With regard to any extension or modification of the Scheme, we consider the Scheme in its current form is no longer needed to protect against mass retailer exit so we are not considering extensions or modifications. If the situation changed to the point where a new Scheme were required, our normal practice would be to do this through a standard Code development process. This would include industry consultation.

3.11 Submitters raised a number of views not directly related to the potential closure of the Scheme which are contained in their submissions and the Authority’s summary of submissions.

- (a) A group of three retailers submitted that it would not be efficient for retailers to price in the full expected impact of future bad debt, noting that under the current market structure, retailers manage all customer debt. They suggested such risk be spread about the industry. While we acknowledge this issue, it is well beyond the scope of this decision paper and the urgent timeframe the Scheme was operating over.
- (b) Some submitters have suggested that there is a continuing and developing need for measures to address the broader income issue which is expected to face the sector. Submitters agree that the targeted and temporary nature of the Scheme is not suited to that task.

3.12 We consider that these points are at a policy level better dealt with by Government. While there may be structural, retail competition or customer service issues which arise because of previous or ongoing COVID-19 disruption, the Scheme was not targeting these issues.

There has been no material change to market conditions since the consultation paper was published

3.13 In addition to considering submissions, we have also monitored debt levels. Figure 1 and 2 below show the aggregate levels of debt as a percentage of revenue for the commercial and residential sectors respectively. The illustrations show that, as at 13 September 2020, overall debt levels are not far from historical levels.

Fig. 1. Residential debt

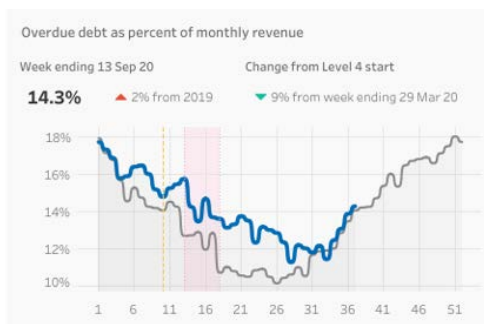


Fig. 2. Business debt



- 3.14 Since the publication of the Consultation paper there have been no new applications to the Scheme. This fact, together with the stable debt levels, means that conditions are similar to when the consultation paper was published.
- 3.15 In summary, our view remains the Scheme as designed is no longer needed. The Authority stands by the decision to implement the Scheme in May 2020 to provide some urgent cashflow protection to retailers, given that the level of increase in customer debt caused by the first COVID-19 lockdown was unknowable, but potentially large, and could occur with little or no notice. However, that immediate material increase in unpaid customer bills has not occurred, allowing retailers time to adapt. The Scheme is not suitable for dealing with any longer-term customer debt issues arising from the economic impact of COVID-19 and ongoing lockdowns.

4 The amendment promotes our statutory objective

The amendment promotes efficiency but has little effect on competition and reliability

- 4.1 After considering all submissions on the Code amendment proposal, the Authority considers the final Code amendment will deliver benefits to consumers.
- 4.2 While the Scheme contributed to the statutory objective when it was first introduced, given the risk and uncertainty at that time, the situation is now changed (managing with the impacts of COVID-19 is the new normal) and the Scheme is no longer needed.
- 4.3 The Code amendment will contribute to the efficient operation of the electricity industry by avoiding retailers and distributors diverting resources to considering utilising the Scheme when the Scheme is no longer needed.
- 4.4 Closing the Scheme also promotes efficient operation by providing regulatory certainty with respect to the ongoing operation of this Scheme. Distributors will no longer need to monitor the programme or consider the risk incurring the financing costs of providing debt deferral. Due to the tight targeting of the scheme, it will become more difficult for a retailer to qualify as the 20th of February end date approaches. By closing the Scheme early, potential applicants won't need to allocate resource to applying for a scheme they are unlikely to qualify for. These benefits are not quantified.
- 4.5 The Authority does not expect the Code amendment to have a material effect on competition or reliability. Evidence indicates that debt levels are within historical levels and that retailers have adequate arrangements in place to manage this. Accordingly, the immediate threat to retail competition is not present or protected against by the Scheme at this point. Early removal of the Scheme therefore will not reduce competition. Any longer-term recessionary impacts will not and should not be dealt with by the Scheme.

The proposed amendment's benefits are expected to outweigh the costs

- One submitter correctly pointed out that the estimated net benefit of \$3,000 is not material.
- 4.6 Far outweighing the nominal expected financial benefit outlined above are the intangible benefits related to regulatory certainty and organisational focus as discussed in Section 4.4 above.

The proposed amendment is preferred to other options

- 4.7 The Authority has evaluated the other means for addressing the objectives and the net benefits from the proposal appear to exceed the net benefits from the alternatives. The reasons for keeping the Scheme open has ended, so on that basis it would be appropriate for it to be closed. Doing so promptly would provide retailers and distributors the regulatory certainty to focus on their businesses in the post-COVID environment.

The proposed amendment complies with section 32(1) of the Act

- 4.8 The Authority's objective under section 15 of the Act is to promote competition in, reliable supply by, and efficient operation of, the electricity industry for the long-term benefit of consumers.
- 4.9 The Code amendment is consistent with the requirements of section 32(1) of the Electricity Industry Act 2010.
- 4.10 The amendment is also consistent with the Authority's Code amendment principles: it is lawful and it will improve the efficiency of the electricity industry for the long-term benefit of consumers. More detail on this aspect are included in the consultation paper.

Appendix A Amendment

Part 12A

Distributor agreements and arrangements

...

12A.5B Application of clause 12A.5C

- (1) ~~Clause 12A.5C applies to a **trader's** agreement with a **distributor** for the provision of **distribution** services if—~~
- ~~(a) an accountant appointed by the **Authority** has certified that the criteria specified in subclause (2) are met in relation to the **trader**; and~~
 - ~~(b) the **distributor** is one of the following:~~
 - ~~(i) Orion New Zealand Limited;~~
 - ~~(ii) Powerco Limited;~~
 - ~~(iii) Unison Networks Limited;~~
 - ~~(iv) Vector Limited;~~
 - ~~(v) Wellington Electricity Lines Limited;~~
 - ~~(vi) WEL Networks Limited; and~~
 - ~~(c) the **trader** was not, as at 1 May 2020,—~~
 - ~~(i) a listed company or a **subsidiary** of a listed company; or~~
 - ~~(ii) a **subsidiary** of a company that has capacity to provide additional capital or loans sufficient to address the situation described in subclause (2)(b)(i) so that the criteria in subclause (2) would not be met, as determined by an accountant appointed by the Authority.~~
- (2) ~~The criteria referred to in subclause (1) are—~~
- ~~(a) the value of receivables invoiced by the **trader** to **consumers** for **electricity** but not paid to the **trader** by the due date for payment (“overdue receivables”) in a month is at least 25% greater than—~~
 - ~~(i) the **trader's** overdue receivables in the same month in 2019; or~~
 - ~~(ii) if the **trader** was not trading in the same month in 2019, or the **trader's** revenue has increased by more than 25% since the same month in 2019, the **trader's** overdue receivables in March 2020; and~~
 - ~~(b) in the opinion of the accountant giving the certificate—~~
 - ~~(i) the **trader** has, or in the next 6 months immediately following the date of the certificate is likely to have, significant liquidity problems; and~~
 - ~~(ii) the liquidity problems are, or will be, a result of the effects of COVID-19 on any one or more of the **trader**, the **trader's** creditors, and the **trader's** debtors; and~~
 - ~~(iii) the **trader** satisfied the solvency test as set out in section 4 of the Companies Act 1993 as at 31 December 2019; and~~
 - ~~(iv) it is more likely than not that the **trader** will be able to pay its due debts within 12 months.~~
- (3) ~~For the purposes of this clause—~~
- ~~(a) “accountant” means a chartered accountant as defined in section 2 of the New Zealand Institute of Chartered Accountants Act 1996; and~~
 - ~~(b) “listed company” means a company whose shares are quoted on NZX Limited or on an official list of a recognised exchange in New Zealand or overseas.~~

- (4) ~~The costs of an accountant appointed by the Authority under this clause must be paid as follows:~~
- (a) ~~by the **trader** requiring the certificate, \$500 plus \$1 for each **ICP** for which the **trader** is responsible, up to a maximum of \$7,500 (all amounts exclusive of GST); and~~
 - (b) ~~if the costs are greater than the amount that the **trader** must pay under paragraph (a), the remainder by the **Authority**.~~

12A.5C Amendments to payment terms for COVID-19 response

- (1) ~~Subject to subclause (2), any requirement under a **trader's** agreement with a **distributor** to which this clause applies, that the **trader** pay an amount to the **distributor** in respect of the supply by the **distributor** of **distribution** services by a date, is deemed to be amended so that the payment is due 60 days after that date.~~
- (2) ~~Subclause (1) does not prevent the **distributor** and the **trader** from agreeing that the payment is due on any other date.~~

12A.5D Prudential requirements during COVID-19 period

- (1) ~~This clause applies to a **trader's** agreement with any **distributor** for the provision of **distribution** services if the **trader** is a **trader** to which clause 12A.5C applies.~~
- (2) ~~If an agreement to which this clause applies requires the **trader** to provide security or additional security as at 1 May 2020, the **distributor** must not increase the amount of security or additional security from the amount that the **trader** was required to provide on that date.~~
- (3) ~~If an agreement to which this clause applies did not require the **trader** to provide security or additional security as at 1 May 2020, the **distributor** must not require the **trader** to provide security or additional security.~~
- (4) ~~If a **distributor** has, before the commencement of this clause, required a **trader** to provide security that, if required after that commencement would have breached this clause, the **distributor** must refund or release the amount of any security that exceeds what is permitted under this clause.~~
- (5) ~~A **distributor** must make the refund or execute the release required under subclause (4) no later than 5 **business days** after the commencement of this clause.~~

12A.5E Revocation of clauses 12A.5B to 12A.5E

~~— Clauses 12A.5B to 12A.5D, and this clause, are revoked on 20 February 2021.~~

Appendix B Gazette notice

Notice of the Electricity Industry Participation Code Amendment (Revocation of COVID-19 Deferred Payment of Distribution Charges) 2020

- 1 Pursuant to section 38(3)(b) of the Electricity Industry Act 2010, and having complied with section 39 of that Act, the Electricity Authority gives notice of the making of the Electricity Industry Participation Code Amendment Removal of COVID-19 Deferred Payment of Distribution Charges ("amendment").
- 2 The amendment comes into force into force 18 November 2020.
- 3 The amendment removes the COVID-19 Deferred Payment of Distribution Charges provisions which came into force by way of urgent Code amendment on 20 May 2020. The scheme was introduced to mitigate the potential for multiple retailer defaults in the context of the then rapidly emerging implications of COVID-19 in New Zealand. The risk of multiple retailer defaults has not been realised and no retailer has successfully applied to be covered under the scheme. As an urgent Code amendment, the provisions would otherwise have expired on 20 February 2021, being the date 9 months after coming into force.
- 4 A copy of the amendment and the Electricity Industry Participation Code 2010 ("Code") is available on the Electricity Authority's website
<http://www.ea.govt.nz/code-and-compliance/the-code/>
- 5 A copy of the amendment and the Code may also be inspected free of charge or purchased from the Electricity Authority, Level 7, Harbour Tower, 2 Hunter Street, Wellington.

Dated at Wellington this 12 day of October 2020.

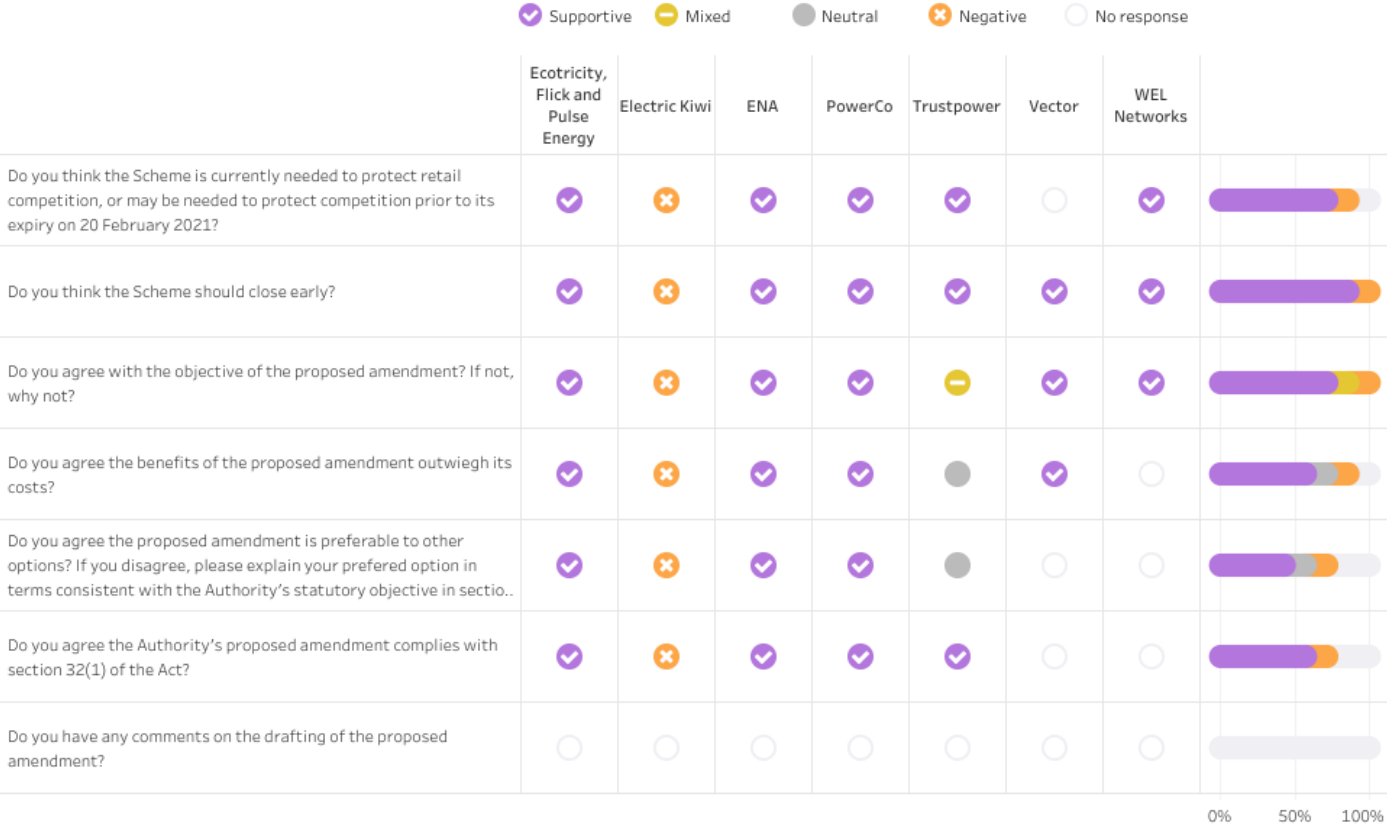
DR THOMAS BRENT LAYTON, Chair,
Electricity Authority.

Appendix C Graphical representation of submissions

DEBT DEFERRAL SCHEME CLOSURE

A summary of responses to 'Proposal to close the Retailer Debt Deferral Scheme' consultation paper

This matrix shows the sentiment of respondents in their feedback on the proposal to close the retailer debt deferral scheme. Hovering over each entry (orange negative, purple positive, yellow mixed support/support with caveats and grey neutral, no colour no comment) links to particular comments in submission on that point (there is also a link to the individual submissions to see the comment in context).



About: This summary of submissions has been created to provide visibility of the sentiment ex..

