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20 August 2013

Retail Advisory Group
Electricity Authority
Wellington

Re : Discussion Paper – Improving Transparency of Consumers' Electricity Charges

Please see attached ETNZ submission on the above paper.

Yours faithfully

A handwritten signature in black ink, appearing to read 'K Sherry', written over a horizontal dotted line.

Karen Sherry
Chair

RAG: Improving transparency of consumers' electricity charges

ETNZ considerations

NZIER report to Energy Trusts of New Zealand
August 2013

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NZIER was established in 1958.

Authorship

This report was prepared at NZIER by John Yeabsley

It was quality approved by Mike Hensen

The assistance of Jessica Mathewson is gratefully acknowledged.



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The question

The setting

The Retail Advisory Group (RAG) provides advice to the Electricity Authority (EA). On 9 July 2013 the RAG released an issues and options paper (IOP), part of a response to a request by the EA that the Group:

“review whether there should be more transparency about consumers’ electricity charges, and to identify and recommend alternatives that promote competition by ensuring consumers have timely access to sufficient information so that they can understand their bills, see what is driving price changes and make choices about their retailer.”

Submissions on this paper are due with the EA by 5pm 20 August 2013.

The submitter: ETNZ

Energy Trusts of NZ¹ is the national organisation for 21 energy trusts, the majority of whom own shares in companies that operate electricity networks (lines businesses). Member trusts have investments of more than \$5 billion in these lines companies.

The trusts that own most of the lines industry on behalf of communities or consumers are not involved in day-to-day management. However, like any group of shareholders, have rights to appoint suitably qualified directors to the boards of the companies they own.

Consumer ownership allows local businesses, industry and individuals to have input on issues like the supply stability of the networks and the pricing mechanisms of their local lines company.

This submission is relatively high level; it approaches the key question – what should be the degree of transparency of consumers’ electricity bills – from the ETNZ perspective and makes a firm proposal.

¹ See ETNZ website (<http://www.etnz.org.nz/>)

Key issues – ETNZ view

Benefits

ETNZ takes the benefits of increased transparency to be those coming from providing enhanced national interest via the ability of consumers to promote competition in relevant markets, in the round.

Electricity charges are a hybrid of fixed and variable cost elements for products and services supplied by generators, transmission operators, lines companies and retailers. Lines company prices and those of Transpower are regulated by the Commerce Commission while prices charged by generators and retailers are not subject to regulation.

Direct

If consumers want to understand the benefit/cost trade-off of changes to their use of energy they need to have access to sufficient information about the fixed and variable costs of the energy they consume. Similarly if consumers want to compare the price competitiveness of energy retailers they need to have access to information about the regulated and unregulated price components of the price they pay for energy.

This recognises that the benefits of consumers understanding their bills include the ability to make informed decisions, where there is a real choice. This allows them to improve their welfare by selecting among electricity retailers, based on the information they have readily to hand.

Wider

And, as a body representing consumer/community owned trusts ETNZ is also conscious that there is potentially a wider set of benefits associated with appropriate information. These stem from consumers being able to use such information about what is happening in markets to consider the wider questions. This allows consumers to contemplate what might happen in these markets beyond just their own ability to churn among retailers.

One aspect is the setting. Competition is affected by the operational rules of the market concerned. This includes their effect on efficiency and the degree of ease they bring to underpinning consumers' behaviour. It is now recognised that consumers do not always necessarily respond to small differences in supply conditions². This is one reason that public resources and regulatory interventions have been dedicated to selected activities in specified markets.

In the case of electricity these include: supporting easy access to an open supply of information; and facilitating supplier switching. This has happened despite it

² This is because they typically have to expend resources. See, for instance, the classic discussion in Zeithaml VA (1988) "Consumer perceptions of price quality and value: A means-end model and synthesis of evidence," *Journal of Marketing*, July, 52, 3, pp2-22, including, at 18:

"Nonmonetary costs – such as time and effort – must be acknowledged. Many consumers ... consider time an important commodity. Anything that can be built into products to reduce time, effort and search costs can reduce perceived sacrifice and thereby increase perceptions of value."

occurring in situations when it seems consumers could have relatively straight forwardly gathered data and changed suppliers, without any assistance.

Another is that electricity consumers have various ways of changing their behaviour in response to views about the likely course of events. One potential choice is to invest in alternative energy sources, including energy saving projects. The return on such investments will depend on the future consumer price of energy. Assessing what this may be is assisted by an understanding of the movements in components of current prices.

So consumers' access to readily useable and relevant information potentially has both direct and wider benefits.

The rest of this submission is largely organised around these two aspects of the information consumers can use to their advantage.

Background

As the IOP makes abundantly clear (pages 5-7) the existing information arrangements are characterised by the existence of many different relevant codes and rules. In addition, there are already a number of (web-based) sources (some based on 'representative customers') available to assist consumers in understanding their energy prices.

But for these tools to be of assistance to consumers they need to be comparable and relevant to the actual energy use patterns of the particular consumer. Moreover, some retailers are said to break down the information given to consumers in ways that others do not. The difference in approach to disclosure makes it difficult for consumers to authoritatively determine the level and drivers of energy costs that might apply to them.

So the problems include:

- information is provided in a number of different forms and different places;
- consumers have different use patterns; and
- time series and causative data is not easily or simply available.

Corresponding to these issues there are at least three areas where consumers could benefit from having additional information readily to hand:

- sufficient simple data to enable them to check their bills (which is not seen as a significant issue, and so is neglected in what follows);
- a breakdown of the contributing components to their bill to allow them to isolate and establish the "variable" costs (retailing); and
- a general indication of the way various causative components are moving to provide a simple (and regular) indication of the drivers of the overall size of the bill for wider purposes including possible investments.

Retailing

The retail price paid by the consumer for energy typically is a "two part tariff" which includes a fixed connection charge and a variable cost for the amount of electricity used by the consumer. Retailer definition of fixed and variable costs seems to reflect

how retailers choose to package energy cost to consumers rather than a common objective definition of the actual fixed (network charges and retailing infrastructure) and variable (payments to generators) of the cost of supplying electricity. The potential variation in retailer approaches to setting prices may hinder consumer comparison of retailer offers.

Consumers can optimise their energy costs by seeking the combination of fixed and variable prices that provides the lowest total costs for their energy use profile. To compare total costs and potential savings between retailers, consumers need comparable information on the fixed and variable costs elements for different suppliers.

Understanding price changes

Our analysis of the drivers of recent price changes suggests that there have been wide differences between the rates of increase in the prices charged by generators for supplying electricity (unregulated) and the prices charged by lines companies for distributing electricity (regulated by the Commerce Commission).

The Commerce Commission regulates lines company prices to ensure that they behave as if they were operating in a competitive market. Showing lines company charges as a separate component of electricity retailer invoices is an important mechanism for the following:

- ensuring that the result of this intervention is visible to consumers;
- informing consumers about how much of the change in lines company charges the retailer passes on to consumers;
- giving consumers a sense of the competitiveness of retailers using the same lines company for distribution.

Overall – what to do?

This brief assessment suggests that there are potential consumer benefits, in both the ways discussed, if retailers were to provide a standardised suite of information to their customers.

Proposal

A proposal that provides the consumers with the information they need would involve the mandatory inclusion of the following information in every invoice:

- included transmission costs;
- included distribution costs;
- rents for equipment;
- included generation costs;
- included retailing costs;
- included regulatory levies.

Obviously, retailers could offer more information if they wished.

Costs and benefits

For a national welfare analysis the possible set of benefits should be evaluated against the cost of meeting them.

In terms of the costs we see economies of scale in mandating a minimum level of information. This will largely involve a one-off cost to redesign the invoice presentation. The choice of mandatory is to minimise costs by providing a standard methodology.

We see few obvious indications of the scale of the benefits. But we note there have been continued demands to have better information and explanations of the causes of electricity price changes, alongside the existence of the multitude of sources offering assistance in understanding the drivers for specific bills. One interpretation of this is that, at least some consumers see significant benefits in having more readily available information.

And over the last 25 years or so different governments have spent time and resources fostering workable competition, and assisting consumers. It is clearly in the national interest for citizens to be able to play their part in understanding their own price positions. And as citizens they wish to be informed about what is actually happening in the market so as to be able to take part in the wider debate about what might be needed to ensure the right outcome.

It also suggests that these consumers are not satisfied that the current alternatives are meeting the need – perhaps because they are not readily at hand.

Conclusion

The IOP poses a series of questions. But overall, from an ETNZ perspective there are two significant aspects of the transparency question seem worthy of a submission.

Consumers' choice

First that it is important to improve the ability of consumers to understand the retail portion of their bill, as this is potentially able to be changed by switching retailers as part of the wider campaign to encourage competition. Assessing possible alternatives starts with meaningful data about the current situation.

At the least, this means a mandated presentation that isolates the movements of key components of the total cost including separately providing lines and transmission charges – as these are subject to special regulation. This should be easy to design into every bill, to allow concerned consumers to have regular opportunities to examine their positions.

Citizens' activity

Second there is the chance to inform citizens by providing regular information on the time path of the components of their bills. This provides the basis of being able to understand the drivers of prices and decide what action they think is appropriate.

Meeting both of these requirements will entail costs, particularly to set up the systems. But the national benefits from workable competition and an informed population are attested by the actions (a series of laws and institutions) by successive governments.