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Submissions
Electricity Authority
PO Box 10041
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Dear Sir/Madam

Re: Electricity Authority appropriations and work programme 2016/17

This is Powerco Limited's submission on the Electricity Authority's 2016/17 levy-funded appropriations and proposed work programme. Thank you for the opportunity to make this submission. We have focused our comments on areas of particular interest to Powerco.

Overview

We appreciate that the Authority has not increased the size of its proposed appropriation for 2016/17, but submit that it would be reasonable to expect actual reductions in future years, as the scope for incremental efficiency gains from further regulatory intervention can reasonably be expected to diminish now that much of the "low-hanging fruit" has been harvested. Bringing the long-running transmission pricing methodology (TPM) review to a close is an obvious area where savings could be made.

One area where an expanded Authority budget would be justified would be to make greater use of external experts to test proposals before publishing them for general consultation. This approach could save the industry as a whole significant unnecessary effort and expense. Currently, the onus often falls on industry members to fund the expert analysis required to test the Authority's policy proposals and, in practice, this can mean that analysis is effectively duplicated by multiple contracted experts. The extensive contract work undertaken in order to respond effectively to the various iterations of the TPM review is an example of this problem.

Omitted work areas

We believe that the following two work areas that have been omitted from the Authority's work programme should be progressed in 2016/17.

Promotion of and efficient distribution sector structure

We recommend that the Authority reinstate its previously signalled project aimed at reviewing the efficiency of the structural arrangements for electricity distribution. We believe there is substantial potential for efficiencies to be gained from promoting the amalgamation of electricity distribution businesses (EDBs) and identifying and removing disincentives to amalgamation. The concentration index hurdle that was proposed to be applied to the deeper connection charge concept that formed part of the latest set of TPM proposals is an example of a potential distinctive to EDB amalgamation. We recommend that the Authority include in its 2016/17 work programme a project to investigate how to incentivise a more efficient distribution sector structure that would deliver long term benefits to consumers.

Consultation on the implementation of the new disconnection policy

New Code provisions (clause 14.49) have been created that require direct purchase customers to be disconnected if they default in the wholesale market, but, despite the significance of this requirement, the Authority has created no policy or procedure to guide the exercise of this power.

The Authority has previously advised that it intended to undertake further consultation on the disconnection procedures and the role of court injunctions in those processes, but this project appears to have been dropped from the Authority's work programme. We recommend that this work area be reinstated.

Review of low user fixed charge (LFC) regulations

The Authority's current distribution pricing consultation paper[1] states that "the Authority considers that demand charges and capacity charges (both of which are measured using kW) … are variable charges under the LFC regulations"[2]. Hence, the Authority is suggesting that the regulations permit a practicable "work around" that enables what would otherwise be fixed charges to take the form of variable charges for the purposes of the regulations. To create certainty for EDBs prior to embarking on tariff reform, we recommend that the Authority seek clarification from MBIE that this view is a correct interpretation and then publish on its website the alternative charging forms that would comply with the regulations. (The IRD's "binding rulings" could be referred to as a useful comparator.) This would give distributors greater comfort that alternative tariff forms are legally permissible.

We note that the Retail Advisory Group's draft paper *Research project: Effects of low fixed charges* states, at paragraph 6.3.6, that "the overall implication of this analysis is that consumers, in aggregate, pay more for less under the regulations than under the notional efficient tariff". This conclusion suggests that further work by the Authority to advocate change to the regulations, or their rescinding, would be consistent with the Authority's statutory objective to promote the efficient operation of the electricity industry for the long-term benefit of consumers, and we urge the Authority continue with such work.

Distribution pricing review

Powerco agrees with the broad direction the Authority is pursuing with its distribution pricing review, as expressed in its current consultation paper[3], which is to encourage EDBs to implement more cost-reflective or "service-based" charging structures.

However, we note that the consultation paper does not refer to studies that show that consumers prefer simple and easily understandable prices. For example, a recent CSIRO study[4] concluded that all the demographic and socio-economic groups surveyed preferred flat c/kWh charges over all other methods. This sort of result suggests that retailers will find themselves under competitive pressure to re-bundle cost-reflective distribution tariffs into a form that their customers prefer, which studies such as the CSIRO work have found to be a flat rate volumetric charge. Consequently, we urge the

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[1] *Implications of evolving technologies for pricing of distribution services,* Electricity Authority, 3 November 2015.

[2] Op cit, para. 7.4.5, p.72.

[3] Op cit.

[4] Stenner, Karen – *Understanding likely customer response to future electricity tariff designs: Insights from behavioural economics*, CSIRO, 29 May 2015.

Authority to place greater emphasis on consumer communication strategies in relation to tariff reforms as well as retailer incentives or regulatory measures that may be needed to ensure that more cost-reflective distribution charges are actually passed through to end consumers and are acceptable to them.

Review of the pricing principles in Schedule 6.4 to Part 6 of the Code

We welcome the inclusion, in the Authority's work programme, of a project to review the distributed generation pricing principles in Part 6 of the Code. The Authority has recognised that small scale photovoltaic generation can drive additional network costs due, in particular, to over-voltage problems[5], but it is not clear whether or not the recovery of such additional costs via an injection tariff is permitted by Schedule 6.4 of the Code. In addition, we consider the provisions in the pricing principles that prevent distributed generation from bearing a share of the common costs of the network (and hence force these costs entirely onto other network users) to be unreasonable. We recommend that the review re-examine these requirements.

We further submit that the review project should extend to include the prescribed maximum fees set out in Schedule 6.5 of the Code. Some of these fee maxima are less than the actual costs of providing the specified services and are consequently inconsistent with the Authority's policy that charges should be service-based and cost reflective.

Transmission pricing methodology review

Given the length of time since the commencement of the TPM review and the amount of analysis that has been undertaken, we believe there must now be very little to be gained from engaging in further analysis or developing additional alternative revenue allocation methodologies. The ongoing TPM reviews have consumed significant industry resource and, in our view, the process must now be brought to an expeditious close in order to remove the prevailing uncertainty and associated cost to the industry that the current apparently open-ended review exercise has created.

Default distribution agreement

The Authority is aware that a substantial number of distributors are continuing to negotiate use of system agreements (UoSAs) with retailers despite the high risk that regulatory intervention may ultimately render their efforts pointless. These negotiations are largely based on the model use of system agreement (MUoSA), which seems to us to indicate that the voluntary framework is achieving the Authority's objectives. Consequently, we submit that the proposed project to mandate a default agreement is unnecessary.

However, if the Authority does decide to proceed to introduce mandatory requirements, we look forward to working with the Authority to ensure that some provisions in the current MUoSA that appear to be commercially and operationally impracticable, particularly the clauses relating to even-handedness, load management and liability, are modified to make them fit for purpose. We refer the Authority to our previous submission of 20 May 2014 on the Authority's consultation paper *More standardisation of use-of-system agreements*.

Retail data project

The retail data project is a positive initiative. The Authority has previously advised verbally[6] that one outcome of this project should be an improvement in distributors'

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[5] *Implications of evolving technologies for pricing of distribution services,* Electricity Authority, 3 November 2015, para. 5.2.35, p.49 refers.
[6] Verbal advice from Craig Evans at the Electricity Authority's regulatory managers and consumer representatives' meeting, 11 December 2014.

ability to access retailer metering data. Such improved access could assist the transition to more cost-reflective charging by EDBs and also improve the accuracy of distributors' demand forecasts. Consequently, we strongly support this work area.

If you wish to discuss any points raised by this submission, please contact Ross Weenink, ross.weenink@powerco.co.nz , ph. (04)978-0522 in the first instance.

Yours sincerely

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