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## TRUSTPOWER SUBMISSION: MORE EFFICIENT DISTRIBUTION PRICES

### 1 Introduction and background

- 1.1.1 Trustpower thanks the Electricity Authority (**Authority**) for the opportunity to provide feedback on its proposal to:
- a) amend the Distribution Pricing Principles (**Principles**) to clarify the Authority's expectations for efficient distribution prices; and
  - b) monitor and rate the efficiency of distributors' prices and their progress on price reform.
- 1.1.2 We note the Authority also wishes to hear how else the Authority and other stakeholders might be able to assist distributors to progress distribution price reform. Trustpower has submitted to the Electricity Pricing Review (**EPR**) on the opportunities to seek further efficiencies within the current regime, and believe there would be benefit in reading that work in conjunction with this submission, acknowledging the fairness lens being applied by the EPR is broader than the Authority's statutory objective.
- 1.1.3 Trustpower's submission in response to questions raised by the Authority is provided in Appendix A to this letter.

### 2 Trustpower's views

- 2.1.1 Trustpower is supportive of the Authority's increased scrutiny on the speed of change being undertaken by the Electricity Distribution Business (**EDBs**) and believes there is an opportunity to improve efficiency beyond the current arrangements which allows numerous disparate pricing structures.
- 2.1.2 Based on the slow pace of reform to date, we are uncertain that the Authority's proposal will be sufficient to promote more efficient distribution prices being introduced in a timely manner. More broadly, we remain concerned that the Authority's continued market facilitation approach will likely continue to result a patchwork of arrangements for distribution pricing and a patchwork of transition arrangements.
- 2.1.3 We are also concerned that the application of the proposed Principles and monitoring arrangements will potentially further exasperate what is already a complicated situation for consumers, through favouring the introduction of more complex cost reflective pricing

structures, rather than supporting simple tariff structures which can be understood by customers.

2.1.4 We consider it is important to recognise that not all customers will be able to understand overly complex signals or be interested in responding to real time price signals. In our view many customers prefer price certainty and so it is important that retailers are still able to offer this group of customer's plans that suit them, including plans that insulate them from price volatility. For this reason Trustpower agrees with the Authority's views around mandated retail pass-through and notes that:

- a) A workably competitive retail electricity sector provides consumers with choice.
- b) Benefits to customers occur when retailers have the ability to offer innovative services and plans that better match customers' circumstances and preferences.
- c) It is better to rely on competition to stimulate solutions and innovation, rather than imposing a mandatory requirement for retailers to pass through pricing structures.

2.1.5 We consider it is also important that new cost-reflective price structures are introduced in a measured way, that is mindful of the impacts of the new default price-quality path (due to be implemented on 1 April 2020) and the potential that price shocks may arise for some customers.

2.1.6 We recommend that:

- a) To mitigate the likelihood of price shocks arising, the Principles being amended to include of a reference to how the transition to new pricing structures should be managed; and
- b) To assist in timelier tariff reform, the Principles should be made mandatory, rather than remaining voluntary.

## **2.2 The Electricity Pricing Review ("EPR")**

2.2.1 We note that a number of important matters relating to Authority's work programmes are being considered by the EPR Panel, including distribution pricing.

2.2.2 Following the EPR Panels advice, the Government's decisions may have implications for some or all of the Authority's current work programmes, including through potentially providing direction on matters relating to fairness (which are currently outside the Authority's mandate).

2.2.3 While we appreciate that the Authority is an independent regulator, to avoid operational inefficiency the Authority should give thought to how direction from the Government following the outcomes of the EPR could impact on its current work programmes.

2.2.4 Otherwise there is the risk that the Authority will proceed with this current process to provide guidance around distribution pricing, only to have this overwritten by the outcomes of the EPR. This would result in unnecessary regulatory costs being inefficiently incurred.

2.2.5 We support the Authority considering how it can ensure 'joined-up-thinking' between its work programmes and the EPR.

Lastly, Trustpower holds the view that retailers could potentially also offer some insight into the signals customers are likely to respond to. I am happy to discuss this in more detail. If you have any questions, please do not hesitate to contact me directly.

Regards,



**Fiona Wiseman**  
**Senior Advisor - Strategy and Regulation**

## APPENDIX A: RESPONSES TO THE AUTHORITY'S QUESTIONS

Q#	Question	Response
Q1	Do you agree that distributors need to reform their prices? What is the reason for your answer?	<p>Yes, reform is necessary.</p> <p>We consider that the current consumption-based pricing approach is likely to become increasingly unsustainable, as consumers who can afford to invest in distributed energy resources, will do so, leaving costs to be progressively shifted on to those customers who are least able to make the same investment. This has also been recently highlighted by the EPR.</p> <p>As the EDBs embark on the journey of reforming their distribution pricing structures to be cost reflective, we consider an important underlying driver should be seeking greater consistency in the tariff structures offered by each EDB, along with simpler tariff structures. We acknowledge that the efficiency gains that may be achieved by this exercise will differ amongst the EDBs.</p>
Q2	How important and urgent are the issues identified by the Authority?	<p>The issues are very important and the need for action is increasing with time and technology advancements.</p> <p>While we agree that change needs to occur, we consider that it is paramount to the success of the reform process that a reasonable amount of time is allowed for transition to the new pricing structures by both distributors and retailers (this is explored further in response to question 3). Likewise we note that hasty changes may need to be reversed, this would be counter-productive and jeopardise confidence in the reform process.</p> <p>We support the views presented in ERANZ's submission on this important matter.</p>
Q3	Do you agree with the proposed Distribution Pricing Principles?	<p>Partially.</p> <p>Although Trustpower agrees with the need for distribution pricing reform, the proposed Principles appear to be overly technically-focused. We consider that the Principles need to also provide guidance around transitional matters in order to address the potential impacts of price shocks<sup>1</sup>.</p> <p>We suggest it would be valuable for the Authority to provide further clarity as to how it would anticipate the EDB's apply Principle (a)(iv)<sup>2</sup> in practice, as it is potentially unclear what types of costs the Authority considers could be</p>

<sup>1</sup> We note that broader considerations of fairness and wellbeing are outside the remit of the Authority. This will limit the ability of any principles to be included which directly capture the impact on vulnerable regions or groups of consumers.

Q#	Question	Response
		<i>attributable to a specific user of group of users.</i>
Q4	What if any changes would you recommend are made to the proposed Distribution Pricing Principles, and why?	<p>Trustpower is generally supportive of the Principles.</p> <p>However as outlined above we consider the Principles would benefit from inclusion of a reference as to how the transition to new pricing structures will be managed, including:</p> <ol style="list-style-type: none"> <li>1. A requirement for a transitional arrangement to be put in place when a change in tariff structure will likely lead to a large increase or decrease in current charges; and</li> <li>2. Clarification that transitional arrangement should be developed in a way that avoids price shocks, and limit the potential for unintended consequences.</li> </ol> <p>We note that network costs, including transmission costs, can make up 30-40% of a customer's bill. Under the proposed Principles, fixed charges may take up a significant portion of the total charge for distribution networks. Any variable / demand charges will only amount to a small portion of a customer's final electricity bill as a result. Given the small potential overall impact of variable/demand charges it is important that the ability for consumers to potentially change their overall electricity charges as a result of responding to pricing signals is not overstated. Ensuring undue complexity with respect to the tariff structures is not introduced should be considered as part of this exercise.</p>
Q5	What if any changes would you propose to the star-ratings to better reflect the relative efficiency of distribution prices?	<p>While we are supportive of the Authority monitoring progress with distribution tariff reform, we caution that the proposed monitoring approach and choice of metrics could distract attention and effort to certain areas and overlook other important ones. For example, there appears to be no weight given to customers' ability to respond to price signals, with the major focus being on assigning the highest ranking to the most economically efficient pricing structures.</p> <p>Trustpower's view is that any new pricing structure must be simple for customers to understand and respond to, or retailers will be unlikely to pass them through. Charging high prices for consumption in a period that a consumer did not know about or was unable to respond to (or both) would be a potentially negative experience and counterproductive.</p> <p>New pricing structures will likely require advanced metering infrastructure and/or involve easily understood tariffs</p>

<sup>2</sup> Charging costs to a specific user of group of users where those costs can be attributed to that specific user or group of users

Q#	Question	Response
		<p>such as simple Time of Use (“TOU”) pricing. Considering the transition period for new pricing structures, and ensuring arrangements are in place to mitigate price shocks will be an important element of the exercise.</p> <p>More broadly, given the slow pace of reform to date, we have reservations as to whether a monitoring approach alone will drive the required outcomes. For this reason we recommended that the Principles be made mandatory.</p>
Q6	How long do you think distributors would reasonably need to introduce the different price structures discussed above?	<p>Whilst Trustpower believes the Principles should be mandatory, we do not consider that a prescribed timeframe for implementation is necessary. Transitions may need to occur over a number of years and this should be enabled to ensure customers are not adversely impacted as a result of the reform process.</p> <p>Trustpower notes that large customers in particular are likely to have made investments on the basis of the pricing methodology which applied when they connected. Not transitioning appropriately could erode investors’ confidence, potentially creating perverse outcomes, as investment in solutions may be delayed that could otherwise enable customers to respond to the new methodologies.</p>
Q7	Can you illustrate how and to what extent the LFC regulation hinders price reform?	<p>We note that the status of the LFC Regulations is under consideration by the EPR Panel. Any changes suggested by the EPR Panel should be considered alongside approaches for more efficient distribution prices.</p> <p>We do not consider that the suggested tariff structures are implementable while the current LFC Regulations in place, so these must be removed in order to progress with distribution pricing reform. This is because for distribution prices to be more efficient it is likely that the largest share of the total tariff structure will be fixed, as a result the tariff structure will only contain a small variable component. However, the LFC Regulations means that for a significant portion of the population achieving these more efficient tariff structures isn’t possible, with unduly high variable charges as a result providing incorrect signals for electricity usage.</p>
Q8	How accurately has the Authority categorised distributor revenues and costs? How could this be done more accurately?	This is unknown to Trustpower.
Q9	What if any would be better indicators of the efficiency of distribution prices, or the	The opportunity and indicators for efficiency gains could vary network to network. We note that although the star-ratings provide a way to compare pricing structures, it unclear they will be sophisticated enough to account for the significantly different network characteristics for EDBs.

Q#	Question	Response
	ambition of and progress being made by distributors on their price reforms?	As outlined above it is also unclear how the star rating system will incentivise EDB's to develop reformed pricing structures in a timely manner. The star-ratings in themselves may not be sufficient for encouraging the necessary action by EDBs. Our view is that mandatory pricing principles are required.
Q10	What assistance could the Authority (or other stakeholders) offer distributors in order to speed up the reform process, or help to remove or reduce barriers to distribution price reform?	<p>The EA could offer assistance by mandating the Principles, subject to inclusion of details around how the transition should be managed.</p> <p>It is Trustpower's view that retailers could potentially also offer some insight into the signals customers are likely to respond to.</p>