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TLC Submission on the Issues Paper on Targeted Reform of Distribution Pricing

The Lines Company (TLC) appreciates the opportunity to submit on the topics raised in the Electricity Authority's (Authority) Issues Paper on Targeted Reform of Distribution Pricing. This letter provides TLC's high-level comments on the topics covered and the attached submission responds to the detailed questions about peak and off-peak pricing.

TLC has directed significant resources to distribution pricing to date. We consider distribution pricing reform important and are committed to continuing to improve and refine our pricing. However, we also think there is a need for the Authority to identify priorities so that distributors can appropriately focus their efforts because the topics covered in the Issues Paper could give rise to a very substantial work program.

Distribution pricing regulatory options

Pricing initiatives of distributors, collaborative ENA and sector working groups, consumer engagement, and Authority engagement with the sector have provided substantial learnings on distribution pricing. The sector is undergoing significant change in the way that consumers use and store energy, and distributors, retailers and regulators need to continue to learn and adapt over time. In that context, TLC considers that it is important that the approach taken for the regulation of distribution pricing needs to be flexible and adaptable to respond to learnings and changes in circumstances. After all, what may be an appropriate pricing structure or methodology at one point in time may not be optimal later. As a result, TLC is of the view that mandating requirements that hardcode pricing structures or price levels is not good practice for distribution pricing.

Target revenue allocation

Target revenue allocation will inevitably involve a degree of judgement in the choice of allocators – there is no "right" approach. The accounting-based allocation has so far provided TLC with a reasonable and defensible methodology. TLC is open to other approaches to revenue allocation however, we highlight that changes in allocations create winners and losers among customers, and therefore any required or recommended change should be justified.

Moreover, allocation approaches that are based on efficiency (e.g. Ramsey pricing where more cost is allocated to the consumers who are least likely to reduce usage if prices increase) are challenging. Furthermore, the responsiveness of customers to pricing may differ within pricing groups and may also be difficult to identify.

Connection pricing

TLC has not experienced significant growth in connections in the recent past however, connection pricing is becoming more important to our network in the context of electrification. As a result, we have recently commissioned an external review of our connection pricing, which includes examining issues of consistency. The discussion on connection pricing in the Issues Paper is informative for that review.

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We do not consider that the Authority would be justified in mandating or prohibiting specific approaches as there has not previously been sufficient clarity around what practices are desirable. We would also be concerned about the potential for inconsistencies between mandates/prohibitions and the constraints that price-quality path regulation places on non-exempt distributors.

Retailer response

TLC agrees with the Authority's comment that monitoring retail pricing would provide a better picture of retailer response – doing so would also help distributors to:

- better understand what retail price signals consumers face;
- assess how customers respond to pricing signals; and
- account for likely consumer responses to price signals in network planning.

All our customers (with capable metering) experienced TLC's TOU pricing signals from 1 October 2018 to 30 September 2021 (when TLC was direct billing). TLC still prices the same, but we have no visibility of our prices to our customers from retailers.

We would be happy to discuss our submission to provide further clarification on TLC's views.

Yours sincerely

Craig Donaldson
Pricing & Regulatory Specialist

Responses to selected questions

Peak period price signals

Q3A. Do you agree that a combination of TOU tariffs and load control (appliance) tariffs would be useful for the smart management of peak demand?

The combination of TOU prices and load control prices is a pragmatic approach and is the strategy that TLC has adopted. However, as discussed in our letter, the optimal pricing solution may change over time as changes occur like electricity demand, technology, and consumers' ability to respond to price signals. As a result, the regulatory framework needs to be flexible.

Q3B. Do you consider that TOU pricing could have unintended consequences for congestion on the LV network?

TLC considers that significant unintended consequences are highly unlikely to occur at present. All of TLC's customers (aside from Capacity and Dedicated Asset customers) with capable metering directly faced TOU pricing signals during the period 1 October 2018 to 30 September 2021. We did not observe unintended consequences for congestion on our LV network because of TOU price signals.

In theory, sharp price differentials between time periods combined with a high uptake of EVs, batteries, or other technologies to shift load could create congestion on the LV network in future. However, whether these unintended consequences occur, depends on a range of factors including the prices that consumers face (rather than simply the network prices charged to retailers), how engaged consumers are with pricing, EV charging patterns, how much discretionary or movable load there is, and the effectiveness of other non-price load management tools. TLC considers that TOU pricing is currently an appropriate pricing structure for most customers, but that it can be supplemented, as needed, by other pricing and non-pricing tools to manage load (including load control options).

We understand that the Authority's question relates to residential and small commercial load – we note pricing considerations, including responses to TOU pricing, could be different for large customers.

Q3C. Do you consider that use of shoulder pricing as part of the TOU price structure could be an effective way to mitigate this risk? What other ways could be effective?

TLC implemented TOU with three time periods (peak, shoulder and off-peak) as recommended by an external pricing review in 2017. We consider that the shoulder period would likely mitigate the risk of congestion on the LV network to some degree by giving consumers an option on whether to shift load to the shoulder or off-peak period. However, as noted above, how consumers will charge EVs and use batteries in future is unknown.

We consider that TOU pricing with a shoulder period is a good approach for now, but the industry needs to observe and learn from consumer behaviour as demand evolves with increased uptake over time of EVs and other batteries.

We note that there are also other reasons to adopt shoulder periods – for example, to reflect times when network peaks may sometimes occur, though are not as frequent as during defined peak times.

Q4. Do you agree with the assessment of the current situation and context for peak period pricing signals? What if any other significant factors should the Authority be considering?

The Authority makes observations based on distributors' existing peak pricing signals. TLC notes that our distribution roadmap includes a stream of work during 2023/24 and 2024/25 to better understand and signal the economic cost of peak network use, including updating our previous Long Run Marginal Cost (LRMC) estimates. We understand that many other distributors have similar workstreams either underway or planned.

While LRMC can form an important input into peak pricing, TLC considers that there are other factors to consider including customer impacts, expected customer responses, and uncertainties in how and when peak loading on networks will be affected by evolving demand. For example, a network that does not have existing or forecast congestion may still prefer to have peak pricing to guard against unexpected congestion in future if unexpected EV (or other battery) uptake leads to congestion on parts of the network.

Our pricing strategy, set out in our pricing roadmap, identifies a range of objectives that we attempt to balance when making pricing decisions, including peak pricing:

- Gradual – allowing thorough consultation and data analysis;
- Limit price shock to its customers;
- Consider future expenditure and demand on the network;
- Be cognisant of new technology being used more broadly on the network;
- Transition towards prices that reflect the future economic costs of the network;
- Be affordable for its customers, and consider customer energy equity;
- Use price as one of the tools to signal network constraints to customers;
- Work alongside customers to understand non-price drivers including customer usage patterns and behaviour.

Q5. Do you agree with the problem statement for peak period pricing signals?

We suggest that the Authority also have regard to distributors' pricing roadmaps and other feedback on work in progress, rather than only considering the pricing that is currently in place. Distributors' pricing is typically updated once per year, so existing prices will not reflect the work that distributors have undertaken in 2023.

Q6. Do you have any comments on the Authority’s preferred pricing for peak periods?

As discussed in response to question 4, TLC’s view is that network cost consequences of usage are an important guiding factor for peak pricing decisions, but not the only factor. Among its list of preferences for peak pricing, the Authority refers to “platform-agnostic prices that signal the value of flexibility - for example, through access to off-peak rates for controlled appliances. These prices should not be tied exclusively to a distributor's own ripple control, and should at least cover hot water cylinders and EV wall chargers.”

TLC highlights that not all networks have the separate metering of controlled load that enables usage prices for controlled load to be distinct from usage of uncontrolled load. TLC’s connections generally have all-inclusive metering, which means that separate pricing cannot be applied to controlled vs uncontrolled load. TLC charges lower kWh rates for connections that do have load control than for those that do not.

Q8. Which if any of the above options do you consider would best support distribution pricing reform around peak pricing signals and why?

Option B – worked examples and guidance are useful.

Off-peak pricing signals

Q11. Do you have any comments on the Authority’s preferred pricing for off-peak usage?

The proposition that off-peak pricing should be zero is intuitively appealing and may be appropriate in many cases. However, we would caution against a blanket requirement to have off-peak rates at zero, for example, because:

- Zero off-peak prices may result in fixed prices that are so high that they impose hardship on consumers, and cause distributors and industry to lose social license;

- Prices and load are inherently related – the timing of peaks can change as a result of pricing and sharp price TOU price differentials could cause unintended customer responses;
- Times of network peak loads may differ within pricing areas – for example, midday in summer may be an off-peak period for a feeder that serves a residential suburb in a town, but a nearby feeder that serves a farming area may peak when irrigation is used on hot summer days. It may not be practical to have separate pricing signals for residential customers on the two feeders;
- For large customers, load shifting by an individual customer in response to a zero off-peak network price could create a peak on a particular part of the network.

We consider it more appropriate that distributors demonstrate that there is a strong rationale behind their choice of pricing, rather than that requiring that pricing adheres to inflexible rules or mandates.