Electricity Authority
2 Hunter St
Wellington 6011

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Emailed to: submissions@ea.govt.nz

To whom it may concern,

More efficient distribution prices, what do they look like? Consultation Paper

Flick is pleased to submit on the Electricity Authority consultation paper '*More efficient distribution prices; What do they look like?*'. Our submission includes this letter and answers to the questions posed in the consultation paper.

We enthusiastically welcome the sentiment of the paper that pricing reform is required. Network companies are adopting more efficient pricing at different speeds: some networks have proactively implemented trials and new pricing structures while others have shown little impetus. From experience in other areas (eg UOSA) we know lagging network companies often have limited management capability and will not change until they are required to do so. As a result we consider that the Electricity Authority needs to actively manage an ongoing program of work on distribution pricing reform rather than leaving this work to be led by network companies. This work should include:

- Establish phased targets for all networks eg all networks must offer a TOU tariff option by 2020.
- Monitor progress and enforce compliance with any mandatory changes.
- Overseeing trials and disseminating knowledge and learnings from them in a timely and coordinated way. We believe strongly in the value of networks trialling new pricing approaches, but in many cases trials don't need to be replicated by each network. Further it's important that there are clear protocols around the form and use of customer data.
- Balancing customer and retailer considerations. What works for a network might impose increased costs on consumers and/or retailers. The Electricity Authority needs to ensure that a fair and efficient balance is struck.
- Approving tariff structures and business rules. In the interests of expediency and operational efficiency (and to avoid a proliferation of different tariff structures and business rules) we consider the EA should approve a set of structures and business rules. For example there may need to be a standard approach for communicating dynamic peak pricing signals to avoid customer confusion and replication of capability.

Please contact me if you would like to discuss the points raised above and our responses to the questions you've posed in the Consultation Paper.

Yours sincerely,

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Q1 Do you agree that distributors need to reform their prices? What is the reason for your answer?

Network investment costs are largely driven by the periods of highest demand. As a principle we support the allocation of costs in proportion to use that drives them. On this basis we believe all network companies should be required to offer the option of a cost reflective/ time of use based tariff.

Further, over the coming years there is potential for a rapid uptake in new technologies (solar, EV) that has the potential to significantly impacts to network operation and network security. To manage this transition it maybe necessary for networks to signal prices/cost and work with customers and retailers to directly control/coordinate network use in order to manage networks security.

Q2. How important and urgent are the issues identified by the Authority?

We believe immediate attention is required because more cost reflective pricing (together with education) can improve energy affordability for many consumers.

It is important to note that some networks (including WEL Networks, Vector, Unison, Waipa and Electra) already have cost reflective time of use tariff options, and we commend their proactiveness. Many of the networks that are lagging behind generally lack impetus to change business practices unless there is a requirement to do so. Therefore we believe that change needs to be backed by a regulatory obligation, soft principles and guidelines will not spur the action that is needed.

There is significant value at stake for consumers. We have observed that time of use tariffs allow consumers to make significant savings by shifting their consumption. This is obviously most relevant to customers who elect to be on spot market pricing products. It is also important to note the time of use pricing is also the best 'building block' for traditional pricing models - and the optimal in terms of allowing for pricing innovation.

We also note that some tariff structures are driving significant cost for consumers, for example Orion's unpredictable ex-post pricing means retailers are typically pricing in an additional 'risk premium' for customers in this network. This is an unfortunate example of negative customer outcomes that have arisen because of network focused tariff design; that minimises the risk to the network - only to increase the costs/risks faced by retailers and end consumers. To ensure customers needs are met into the future this type of structure must to disallowed.

Q3 Do you agree with the proposed Distribution Pricing Principles?

We generally agree with the principles as described however we do not support 'b)' in isolation from other regulatory backstops. Principle 'b' is the idea of negotiating a solution based on specific circumstances. We appreciate the logic behind this is that a one size fits all approach is unlikely to be efficient - however as the Electricity Authority will have heard from numerous parties for numerous years negotiating with monopolies can be fraught (or even impossible). Risks and costs can be shifted away from the network in an unworkable or unreasonable manner due to the imbalance of power that arises with network controlling access.

Practically there may be ways to address this - by having default arrangements and then allowing parties to negotiate from that point. While not perfect this would at least provide network users some bargaining power and mean that 'negotiated' arrangement are at least more beneficial to the user and network than a strict default arrangement.

Q4 What, if any, changes would you recommend are made to the proposed Distribution Pricing Principles, and why?

Refer the comments above in Q3 regarding negotiated arrangements, the problem is with the Electricity Authority's regulatory approach rather than the principle.

In addition as with the previous principles, there is plenty of room for differences in interpretation of them. As discussed above we believe pricing structures need regulation, principles alone are too soft and leave too greater scope for unnecessary variations in structures. It is the variations that drive operational inefficiencies for retailers - and the associated increased cost to be borne by consumers. By way of example, if dynamic peak tariffs were adopted and every distribution company required retailers to communicate price signals in different formats/channels and at different notice intervals this would be unwieldy and costly for retailers to manage. So there needs to a balance struck between the freedom of distributors to develop new pricing arrangements and the workability of them for customers and retailers.

We believe it would be appropriate for a standard set of pricing structures/ business rules to be approved by the Electricity Authority for use. Beyond this a set alternative tariff structures and business rules should require approval from that Electricity Authority and only be permitted where it's clear that a fair and efficient allocation of costs can not be achieved by a standard structure - and that the proposed tariff be consistent with the Distribution Pricing Principles. Developing a comprehensive set is obviously necessary so that the arrangements are not unduly restrictive for distributors, and we would expect this set to evolve over time.

Q5. What if any changes would you propose to the star-ratings to better reflect the relative efficiency of distribution prices?

Flick acknowledges the good intention behind the star-rating, however we are concerned the rating grading is to heavily biased toward economic theory and does not place enough weight on customer considerations and how workable the tariff is. Customer considerations will evolve, they should reflect customer preferences, customer tools (eg availability of information tools/ alerts and control devices for managing consumption) and service delivery (eg are customers on a smart meter, what information is available from it and what frequency of information can they provide).

It’s also really important to distinguish rating of tariffs for different user groups. Large consumers who can justify investment in technology and resources to manage their usage can deal with more complex pricing. For smaller users simpler tariff structures should be favoured as complexity increases ‘transaction costs’ for users and may lead to confusion that drives inefficient behaviours. Accordingly, we would expect the rating of a dynamic critical peak tariff to be high for a large commercial customer group, however believe it should not be a highly rated option for small consumers given the limited penetration of smart meters, limited availability of demand data, limited availability of ‘live’ usage information etc (over time as smart metering improves and more cost effective control devices come to market this rating may change).

Q6. How long do you think distributors would reasonably need to introduce the different prices structures discussed above?

We acknowledge that some of these tariffs structures may require significant system and process changes however this should be considered a priority. We believe a phased approach could be taken - eg all distributors must offer all customer a time of use tariff from 2020, with more complex tariffs implements by 2022.

Q7. Can you illustrate how and to what extent the LFC regulation hinders price reform?

LFC regulations mean that if fixed daily network charges are passed through metering costs are not fully recovered. Metering costs 25.5 cents per day on average.

Q8. How accurately has the Authority categorised distributor revenues and costs? How could this be done more accurately?

No comment.

Q9. What, if any, would be better indicators of the efficiency of distribution prices, or the ambition of and progress being made by distributors on their price reforms?

As discussed above on Q4. we believe an approved set of standard structures tariffs would be preferable. This would help improve operational efficiency for retailers. We believe a set of standard structures would also support operational consolidation/ shared service arrangements to be made by distributors, this too would have efficiency benefits.

Q10. What assistance could the Authority (or other stakeholders) offer distributors in order to speed up the reform process, or help remove or reduce barriers to distributions price reform?

As discussed above Q2. we believe regulation is required to ensure all Networks move as quickly as necessary, relying on principles alone is unlikely to yield the necessary progress from all Networks.

As outlined in Q4. we also advocate for a set of standard tariff structures (and accompanying business rules) be developed by the Electricity Authority this may reduce design time and effort for Networks and would reduce the uncertainty and potential work required by retailers to implement new tariff structures.

As outlined in Q6. we support a phased approach so that ‘quick wins’ to remove known significant efficiencies, through the implementation of TOU pricing, are actioned as soon as possible.