meridian

POWERSHOP

19 February 2019

Submissions
Electricity Authority
PO Box 10041
By email: submissions@ea.govt.nz

More efficient distribution prices – Meridian / Powershop submission

This submission is provided by Meridian and Powershop. We appreciate the opportunity to submit on the Authority's '*More efficient distribution prices: What do they look like'* consultation proposals.

Appendix A details our responses to specific consultation questions. In summary, Meridian:

- broadly supports the Authority's revised distribution pricing principles.
- generally supports the Authority's proposed star-rating monitoring system. While we take a more favourable view towards time-of-use charges, Meridian agrees with the ratings-based monitoring concept proposed. We suggest, however, qualitative assessments should also extend to how distributors communicate intended plans and progress and that road maps and monitoring reports are made readily available.

Please contact me if you have any questions regarding this submission.

Yours sincerely

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Appendix A Responses to specific consultation questions

Question	Response
Q1. Do you agree that distributors need to reform their prices? What is the reason for your answer?	Yes. Meridian agrees it is critical that distribution charges are adjusted to provide the correct price signals. The longer existing distortions are prolonged for, the longer inefficient consumer charges and impaired signals for investment will persist. This is not tenable for consumers, who will continue to pay charges which are neither fair nor cost-reflective, and ultimately will be exposed to the costs of over-investment (valued at $2.7-$5 billion over 25 years for solar over-investment alone, according to NZIER estimates[1]). In addition, it is also important that reforms are carried out to ensure efficient investments are not deterred. The scale of this effect could be particularly significant for electric vehicles, with Concept research indicating distribution pricing distortions, together with supressed carbon prices, may reduce electric vehicle uptake by 2% – at an overall economic cost of $560 million over 20 years.[2]
Q2. How important and urgent are the issues identified by the Authority?	Meridian agrees there is an urgent and pressing need for distribution pricing reforms to be progressed. As our Q1 response discusses in more detail, the current prevailing (typically flat, and time invariant c/day, c/kWh) price structures are not sustainable or ultimately in consumers' interests generally. The Authority has been pursuing reforms for three years now. On 1 April 2020, the Commerce Commission will implement a change to a weighted average revenue cap, under the revised default price quality path (DPP3) for non-exempt distributors. The change – which will replace the weighted average price cap (WAPC) method previously used – removes a key perceived barrier to reform cited by distributors.[3]

[1] NZIER 2015, *Effects of distribution charges on household investment in solar*, available at www.ea.govt.nz

[2] Concept 2016, *Electric cars, solar panels, and batteries in New Zealand Vol 2: The benefits and costs to consumers and society,* available at: http://www.concept.co.nz/uploads/2/5/5/4/25542442/new_technologies_economic_report_v2.0.pdf

[3] A WAPC caps average within-period prices. A revenue cap in contrast guarantees average revenues, irrespective of energy volumes.

Question	Response
Q3. Do you agree with the proposed Distribution Pricing Principles?	Meridian generally agrees with the amendments proposed. At a high level, we believe the revised principles should ensure a sufficiently broad and complete perspective on the changes needed to achieve efficient charges. We consider principles (d) requiring consideration of transaction costs – and (e) – promoting predictability in particular will assist with this. Meridian, however, queries the intent of principle (b)(ii) – providing for non-standard prices and services, obtained through negotiation with stakeholders. In particular, we are unclear why this provision is considered necessary, given it is our impression direct negotiations are only rarely carried out currently and would not seem to be otherwise prevented. As a supplementary provision, it also risks complicating and potentially compromising broader objectives of service-based and cost-reflective pricing outcomes. In relation to principle (a)(i) (targeting 'subsidy free' pricing), Meridian notes the Authority is proposing to maintain exclusions for legislative compliance. It's not clear what legislation the Authority has in mind. The Authority's 2016 guidance relating to the low fixed charge regulations endorses a wide variety (peak demand, capacity, and time-of-use) of pricing structures as permissible under the regulations.[4] The Authority should either clarify what legislation it is thinking about here, perhaps by way of footnote, or should amend the draft principles. The current wording is apt to create confusion. Meridian shares the Authority's concerns that retailer pass-through requirements will inhibit the ability of retailers to respond to the diverse preferences of consumers (including in relation to price stability) and risk interfering with the ability of retailers to compete. We note, in addition, there are already examples where distributors have implemented pricing reforms without retailer restrictions of any form (WEL networks' time-of-use charges, for example). We therefore oppose any interventions to mandate retailer pass-through.
Q4. What, if any, changes would you recommend are made to the proposed Distribution Pricing Principles, and why?	As detailed in our Q3 response, Meridian has some specific questions on aspects of the Authority's revised principles. We invite further details on the Authority on these questions in the first instance.

[4] Available: https://www.ea.govt.nz/dmsdocument/21123-guidelines-variable-charges-under-the-low-fixed-charge-regulations

Question	Response
Q5. What if any changes would you propose to the star-ratings to better reflect the relative efficiency of distribution prices?	Meridian's view is that time-of-use (ToU) charges will play an important role in achieving more efficient distribution pricing and that the Authority's assessed ratings may understate the potential efficiency benefits of this form of charge. There is every prospect in our view that ToU pricing options will deliver the vast majority of efficiencies that are needed, with no material reduction in overall benefits. The simplicity of ToU charges, as compared with other forms of service-based and cost-reflective pricing, will also make for reduced costs and scale of transition – for retailers, distributors, and consumers – and provide pricing signals retailers are readily able to reflect to consumers. Meridian agrees locational marginal prices are currently an impractical option that should not feature in the Authority's assessments. We are concerned that the paper's analysis[5] understates the significance of metering impediments (and therefore data availability limitations), with these impediments likely to persist for some time – given the long-life span of metering assets (typically 15-20 years). Metering Equipment Providers, if they haven't already, should be able to provide further advice. Meridian supports the proposals for supplementary qualitative assessments. In addition to the areas identified for assessment by the Authority[6], how distributors have communicated their road maps and timeframes for reform should also be monitored. Allowing a lead time of at least 12 months prior (that is, well in advance of April price change consultation processes) should apply as a minimum standard for the assessment. Meridian considers star rating reports and road maps should be made easily accessible by being prominently displayed e.g. on the front page of distributors' websites.

[5] Refer paragraph 3.9 of the Authority's paper.

[6] To include, indicated by paragraph 6.16 of the Authority's paper, (a) an interpretation of the star-ratings for each distributor (b) comments on the quality and ambition of distributors' reform roadmaps (c) compares the progress each distributor has made against their own published road maps and against distributors overall.

Question	Response
Q6. How long do you think distributors would reasonably need to introduce the different price structures discussed above?	A number of distributors are already introducing such structures on an optional basis. We believe that the mandated roll out of such structures should be signalled well in advance, with retailers given plenty of time to in turn communicate with customers, but provided that is done we see no reason why, for example, ToU price structures could not be in market within the next 2 years.
Q7. Can you illustrate how and to what extent the LFC regulation hinders price reform?	In our view LFC regulation definitely hinders reform. Around 60% of residential customers are on the low fixed charge option and around 50% of total ICPs. This means distributors are currently restricted to under-recovering their fixed costs for half their customers and they compensate for this by inflating variable charges. This pattern of pricing has been well-established for some years now and, while the LFC regulations remain on the statute book, it arguably remains official Government policy when it comes to retail electricity pricing. Distributors may perceive significant reputational risk in moving away from current pricing structures while the LFC regulations remain in force. More pragmatically, it is not easy to reconcile certain forms of service-based and cost-reflective pricing with a straightforward reading or interpretation of the LFC regulations. We are aware of correspondence between the Electricity Authority and the ENA in which the Authority takes the position that, applying a purposive approach, it is possible to implement any type of service-based and cost-reflective pricing consistently with the regulations and therefore that the regulations should not be seen as a barrier or hindrance – see the Authority's letter of 17 August 2017. As the body charged with enforcing the LFC regulations it is helpful that the Authority is prepared to issue guidance of the kind contained in such letters and distributors (and retailers) can take some comfort from them. However, it also seems clear that the practical steps distributors will need to take, consistently with the Authority's guidance, in order to remain LFC compliant (e.g. to remain compliant with the prohibition against tiered or stepped charges) at least complicate to a significant degree the process of price reform. Against the background of widespread uptake of LFC pricing we believe this means that the LFC regulations are a significant hindrance to price reform.
Q8. How accurately has the Authority categorised distributor revenues and costs? How could this be done more accurately?	We believe this is a question best answered by distributors.

Question	Response
Q9. What, if any, would be better indicators of the efficiency of distributor prices or the ambition of and progress being made by distributors on their price reforms?	Refer suggestions detailed in Q5 response.
10. What assistance could the Authority (or other stakeholders) offer distributors in order to speed up the reform process, or to help remove or reduce barriers to distribution price reform?	Constraints of the low fixed charge regulations appear to remain a key perceived barrier. It is important the Authority further investigates how such concerns can be alleviated. The Authority in its paper also invites further feedback from retailers on the concept of a standardised approach to distribution prices. Consistent with previous submissions[7], Meridian's view remains that material efficiency benefits can be obtained from consistency in pricing formats, naming, and parameters (in relation to 'peak' and 'off-peak' periods, for instance). Consistency across distributors in addition will alleviate the costs of market participation – with wider potential competition benefits. The benefits from standardisation must be appropriately balanced with other efficiency-related objectives through the distribution pricing reform process. Cost-reflective and service-based pricing must, however, not be compromised by this in any significant way.

[7] Refer Meridian's 2 February 2006 '*Implications of evolving technologies for pricing of distribution services'* submission, available: https://www.ea.govt.nz/dmsdocument/20455-meridian-energy