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Submissions
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Submission on Electricity Authority Paper
"More efficient distribution prices – What do they look like?"

1. Introduction

Thank you for the opportunity to submit on the paper *"More efficient distribution prices – What do they look like?"*

The Lines Company (TLC) has a unique perspective due to the diversity of our network, a rural base, and corresponding low density of connections, no cities and is the only distributor that directly bills all of its customers.

In September 2016, the TLC Board commenced an independent review of the service-based pricing approach TLC had applied. The review recommended that we move away from the then current approach which was based on a 'variable demand charge' to a 'variable time of use' charge, also referred to as 'Time Of Use' (TOU), which simplistically means that pricing for lines is applied based on the time of day customers use energy.

During the review process, TLC conducted extensive customer workshops from which key pricing principles were developed. The key themes sought by customers were simplicity and transparency.

While the demand-based system is arguably a better way to recover the costs of network growth under service-based pricing, the review concluded that TOU would be more equitable, have greater simplicity, and be more transparent – and therefore a better fit based on the criteria set through the customer engagement process.

This is not the end of the pricing roadmap for us, and we will continue to engage and listen to our customers.

2. General Comments

TLC believes that our industry needs to focus more on customers. We consider the key mechanisms to achieve this are to give customers both a ***voice*** and a ***choice*** in how distribution services are priced and delivered. To achieve this, our industry needs to engage customers more often and more meaningfully, to improve understanding of the electricity supply chain, and to enable customers to manage their costs if they choose to do so.

TLC's recent engagement with customers has indicated that while some are engaged, many are indifferent about their electricity supply. We believe that this may change rapidly with emerging technologies, smart appliances and more pricing options for customers. There is, therefore, an imperative for distributors, and all electricity participants, to actively involve customers in the reform process.

Our industry also needs to consider how the interactions between participants can be optimised to enable reform. For example, more efficient distribution prices inherently rely on sound and timely information from both metering and customer data sources, both of which are generally held or controlled by retailers. This can limit the visibility distributors have and constrain their ability to make informed planning and pricing decisions.

3. The following are our responses to the questions in the paper:

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

The need for reform has been recognised by distributors and worked on by the industry groups for quite some time. The need for price reform was detailed in the ENA consultations in 2015 and 2016 and published in their 2017 publication "A Guidance paper for Electricity Distributors". The Authority has stated in their paper that there is broad agreement that distribution prices need to change, and TLC agree with this.

TLC recognised the need for price reform about 12 years ago because of the characteristics of our network. Amongst other things, we needed transparency of distribution pricing signals to our customers, and this remains the case. To be truly effective, reform needs to consider the transparency available to customers, customer behaviour and customer's ability and willingness to react to price signals.

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

TLC has recently been through a process of pricing reform driven by customer feedback. Our own experience was that, although the imperative for change implied urgency, we found that significant consideration needed to be given to the impact on customers, and the transition options available.

Our change process required trialling, engagement with customers, extensive consultation and consideration of customer responses. Customer engagement and consultation cannot be compromised for urgency.

The process was complex, impacted systems and technology, and required extensive engagement, not only with customers but also other industry participants. This included metering equipment providers (MEPs), retailers, and regulators. Working through this process took time, and needed to be planned carefully. Extensive analysis was required to understand the possible impact on customers, particularly in relation to affordability.

3. Do you agree with the proposed Distribution Pricing Principles?

TLC supports principle-based regulation rather than prescriptive requirements. This enables distributors to be flexible with pricing to reflect the unique aspects to distributor's networks, i.e. a one-size fits all approach is not appropriate.

Concerning the individual principles, we comment as follows:

Being time and location specific

TLC supports both time and location-specific principles, although we acknowledge that our view is different from other distributors. However, consideration needs to be given to affordability and fairness of location-specific pricing, the ability of distributors and the industry to engage customers and to enable them to react.

TLC does have location specific pricing, pricing customers based on high and low density. We reflect this is our fixed, daily charges and we believe that customers, in general, are accepting of this.

Being subsidy free:

We agree, in theory, but our experience has been that this is not always achievable nor desirable in practice. A pure application of this approach ignores the issue of energy poverty which can be significant and wide-ranging.

The issue relates to affordability, and unless there is cross subsidisation, there needs to be some form of government intervention or assistance to support these customers. Affordability is a national issue and not solely related to distributors and their customers.

Simplification of principle (d) now principle (c):

The removal of *stability and certainty* as a criterion is a concern. Our experience is that although some customers are extremely engaged and are responsive to price signals, other customers prefer simplicity, stability and certainty.

TLC has sought to achieve both by offering customers a methodology that gives a choice (through its demand, and now TOU methodology), and through payment options (such as Smoothpay) that provide certainty on monthly bills.

New Principle (e) - Consumers should be able to know or predict prices they will face when making decisions to connect to or use the network:

We make several observations regarding this principle:

- The electricity industry is going through unprecedented change driven by emerging technologies, electric vehicles, distributed generation, batteries, etc. On that basis, it is unclear to us how distributors would provide medium to long term price certainty without materially restricting our ability to embrace these changes;
- As the Authority highlights, there is an imperative for distributors to continuously reform, and consequently, we see this as contradicting the proposed principle;
- Long term prices for distributors are not fixed in perpetuity, e.g. pass-through costs change, network costs change over time;
- TLC currently provides direct transparency of its costs to customers through direct billing. In our view this provides customers with optimum transparency given our prices are not bundled with retailer bills. Consequently, customers are currently able to assess investment options based on prices and the influence that their behaviour has on their distribution costs.

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

TLC would like to see a principle that considers customers, and the need to balance the ‘economics’ of pricing reform with customer requirements, specifically around flexibility, transparency, and simplicity based on customer feedback.

At a fundamental level, distributors exist to provide services to customers. Consequently, customer needs should drive the service and price combination that is delivered. Customer needs are not static, but change over time. We expect the diversity of customer needs to grow as supply options develop technology. Hence, including a principle directly related to customers, and their requirements, should be a key driver for the industry.

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

The proposed star rating methodology is intended to encourage distributors to focus their efforts to reform prices. We feel that this would work if you were able to change prices quickly. However the current regulatory environment and the process of consultation with stakeholders, trialling of new plans, risk assessment, modelling the efficiency of any proposed changes, updating technology to provide data, changes to billing systems required and implementation of these changes through retailers means that, in reality, it may take a long time for price changes to take effect and for any star rating score to change. Hence it is not likely to be an active method to encourage progress on price reform.

We also feel that the proposed star rating system is fairly broad-based and cannot reflect the fact that not all networks are the same, e.g. comparing highly dense urban networks to low-density rural networks in the same methodology, with no adjustment for the differences between them.

If the Authority persists with the star rating, we would like to see a star that considers distributors pricing in terms of customer impact.

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

Our experience with our recent change in pricing indicates that it would likely be at least a two-year process from initial modelling through to implementation, with consideration of consultation and engagement with customers and other stakeholders.

Pricing may or may not also require changes to metering. If required, this can add 12 to 18 months to the timeline and requires universal support from MEPs and retailers.

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

It is comprehensively acknowledged that the LFC regulations are not fit-for-purpose, and TLC believes that they require immediate consideration, both industry-wide and politically.

It is appreciated that the Authority released the guidelines dated 9 August 2016, "Variable charges under the low fixed charge Regulations", but distributors remain hesitant and cautious with their pricing as they relate to the regulations. TLC believes that this caution is well founded and, in part, inevitably relates to the investigation TLC went through in 2014. This investigation was resource hungry, and expensive for TLC and our customers.

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

TLC has no comment on this question.

9. 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?

The efficiency of distribution prices would be better reflected by measurement of how well pricing aligns with customer needs. As previously noted customer needs are not static and are expected to grow in diversity over time. This implies an imperative on distributors to engage meaningfully with customers to find out what they require, and we consider this engagement would be an appropriate measure of distributor pricing performance.

Under the interposed model where retailers bundle prices, customers may not have any visibility of distribution prices and how their behaviour influences (positively or negatively) the associated cost drivers. We consider this absence of transparency inhibits customers in making informed decisions on their electricity usage or associated investments, and as such distributor pricing performance may be meaningless.

We, therefore, consider that an annual discussion with distributors about the progress of their pricing roadmap, its alignment with customer needs, and its meaningful delivery through retailer products, would be a more useful model to progress price efficiency reform.

10. What assistance could the Authority (or any other stakeholders) offer distributors to speed up the reform process, or help to remove or reduce barriers to distribution price reform?

We believe that the Authority, and industry, need to engage customers better. It would be useful for the Authority to involve the retailers in this discussion as they (in most cases) are the key link to the customer. The actions taken by retailers in developing their pricing plans could enhance or conversely inhibit the impacts on customers of price structures developed by distributors.

Consideration also needs to be given about the availability of metering and customer data and the relationships between participants – particularly the role that metering equipment providers play. MEP's are no longer just asset owners; they need to turn their thinking to being data providers as data is the key to understanding customers and their behaviour.

This review should also be taken in context with the Transmission Pricing review and the Electricity Price Review to ensure any changes to methodology would have the enduring long term impacts envisaged in this review.

Thank you for the opportunity to submit our view on the draft pricing principles and proposed star rating methodology. We trust that this submission provides valuable insights for the Authority.

Yours sincerely

Signed by
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On behalf of
Sean Horgan
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