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Follow-up consultation – proposed changes to the default distributor agreement

31 July 2024

1 Submission and contact details

Consultation	Follow-up consultation – proposed changes to the default distributor agreement
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2 Release of information

This report contains no confidential information and can be publicly disclosed.

3 Introduction

Wellington Electricity Lines Limited (**WELL**) appreciates the opportunity to respond to the Electricity Authority's (**EA**) proposed changes (**Proposed Amendments**).

While we understand the intent of the proposed changes, they will not achieve the expected benefits. The changes will increase costs and long-term prices and provide no incentives to improve the quality of distribution services. Especially:

1. Any refunds for service outages will cost more to refund than the value being refunded. While customers experiencing outages will have a small refund (about \$1.20 per day for residential customers on the Wellington network), the operation of the revenue cap under the Default Price Path (DPP) means that future prices will be increased to recover the refund – other customers will pay for the refund through future price increases. Furthermore, customers will also have to pay for the retailer (keeping up to 50% of the value of the refund) and distribution administration costs (by increasing allowances and distribution prices). The net impact will be an overall increase in long-term prices to consumers.

2. Refunding customers for service outages over 24 hours will not incentivise EDBs to improve service quality. Last year, five customers experienced HV¹ outages longer than 24 hours on the Wellington Network. Customers would have been refunded ~\$30² or \$1.20 each day for the fixed daily charge. If retailers keep 50% for administration cost then the refund would have been \$3 which will then be recovered in future price increases. EDBs already have strong incentives to avoid outages and restore power quickly. The \$3 refund is small when compared to the equivalent quality penalty rate under the DPP (currently worth approximately \$190 per customer per day for the Wellington Network) or up to a \$5m fine for a quality breach that is applied under Part 4 price/quality regulation.
3. Wellington Electricity's current DDA has set the 'use of money adjustment' to zero after consulting with retailers. The reason we removed it was the administration costs of applying the adjustments are high for both retailers and distributors, and the unders and overs from the reconciliation process offsets most cashflow differences. Its removal reduces costs overall which in turn reduces prices to consumers. We consulted with retailers on this change and no retailer objected.

While the EA has the authority to apply quality targets and incentivise a level of quality, we strongly disagree that it is appropriate to do so via the Electricity Industry Participation Code. An essential premise of price/quality regulation is the ability to trade-off and choose what level of quality a customer wants at a price they are willing to pay for. The Commerce Commission (Commission) is responsible for making this explicit trade-off when they reset the price/quality path every five years. Applying quality mechanisms and incentives outside of the Commission price/quality path reset means that customers cannot decide whether they want to pay the additional cost for a quality improvement.

4 Consultation questions

4.1 Do you consider the revised proposed approach in 9.10 is workable, efficient, and effective? Would you propose any alternative approaches?

No, we do not think the proposed changes to clause 9.10 will provide any new benefit to consumers. Consumers will pay more in the long run and the change will not incentivise EDBs to improve service quality.

We also question what the Authority is trying to correct or improve with the changes. We are not aware that customers have said that they want to pay for an improved level of service. We survey some customers after each outage asking if they would pay for fewer outages. Most customers have said they would not.

¹ Like many other networks, Wellington Electricity does not have visibility of its low-voltage network. Some information is available from field service staff but it cannot be verified and does not provide a robust data source from which to base quality measures.

² One customer's power was out for 16 days.

We would note that price/quality regulation applied under Part 4 of the Commerce Act already has a strong incentive to restore power after an outage. EDBs face SAIDI minute penalties under the DPP, and up to a \$5m fine per quality breach for exceeding their quality limits.

4.1.1 Is the proposed change workable?

Wellington Electricity could not practically implement the change:

1. Most EDBs do not have visibility of their low voltage (LV) networks and would not be able to accurately assess LV outage times. We have some information from field staff, although the data is not complete and is not stored in a system that can be reliably scrutinized and apply quality incentives.

EDBs are in various stages of developing LV visibility which would allow a network to see LV outages. However, this requires allowances to purchase smart meter data, LV management software and resources to operate the new function. It also requires easy access to meter data which is owned by retailers and meter providers.

2. We estimate it takes 5 min to manually process one refund. For a normal number of refunds we can do this with existing staff. However, we would not have the resources to process a large outage like a storm. For example, 2,000 customers out for longer than 24 hours would take two weeks to process. We could automate the process. We would need to ask for a quote to make the change but past changes have cost \$50-100k.

We can invest in the systems and capability that will allow us to identify all outages and the specific households that will need refunding. However, the cost will be significant and the changes will take time.

4.1.2 Is the proposed efficient

The change is not efficient because the refund is not reflecting a loss of service. Customers don't pay for a continuous level of service and the services aren't funded to return power within 24 hours. Our service levels are designed to minimise the length and frequency of power outages. Each outage is different and repair times will vary depending on the fault. The 24-hour limit assumes all faults are the same, which they are not. Customers are still receiving a service even when the power is off – we will be restoring power and repairing the network.

The proposal is also not efficient because the proposed change will increase prices to consumers.

- Customers experiencing outages will have a small (about \$1.20 per day for residential customers on the Wellington network) refund. Under the revenue cap applied under Part 4 regulation, future prices will be increased to recover the refund. Other customers will subsidise the customers who have been refunded and prices overall will not change.
- Customers will also have to pay for the retailer (keeping up to 50% of the value of the refund) and distribution (via increasing allowances and distribution prices) administration costs.

The EDB cost of applying the change will depend on what changes are required and how many outages there are in a year. For example:

- Developing visibility of the LV network is expected to cost \$1.7m p.a. (we recently provided this estimate as part of the Part 4 DPP4 reset process).
- We estimate it will take 5 minutes per refund to process by the billing team. This can be provided by existing staff for a normal number of outages (we had five customers out for more than 24 hours last year). However, for a storm event, this could require additional resources. For example, a storm with 2,000 customers out would take one person two weeks to process the refunds. This cost will increase as storms become more common because of climate change.

Revenue to customers remains unchanged while costs will increase. The net impact will be an overall increase in long-term prices to consumers.

4.1.3 Is the proposed effective

The proposal will not improve service levels to consumers and therefore will not be effective. EDBs will be made whole for any refunds under the DPP and so are not incentivised to change their service levels.

More importantly, EDBs already have strong incentives to restore power as quickly as possible. The SAIDI quality incentive and up to \$5m per quality breach applied under Part 4 regulation provide much stronger incentives than refunding the fixed daily tariffs. Wellington Electricity's \$23k per SAIDI minute quality incentive rate under DPP3 translates to \$190 per customer per day that power remains off. This penalty cannot be recovered from the revenue cap and is paid from regulatory profits. This already provides a much stronger incentive to restore power than refunding the \$1.20 per day fixed daily change to residential consumers.

4.1.4 An alternative approach

We are unsure what the proposed change is correcting or improving. Customers don't appear to be asking for an improvement in service quality and are willing to pay for it. Last year on the Wellington network we had five customers who had outages for longer than 24 hours. Refunding the fixed daily fee would have provided \$1.20 per customer per day or \$30 (20 customer days) in total.

4.2 Do you consider it would incentivise distributors to restore electricity supply to consumers more quickly if they did not need to reduce charges for a longer outage period than 24 hours?

No – the refunded revenue is recoverable through the revenue cap and washup account so the change provides no incentives to restore power more quickly.

More importantly, EDBs already have strong incentives to restore power and will do so as fast as possible. The quality incentives under Part 4 regulation provide a greater incentive for HV outages longer than 24 hours.

4.3 If so, what time limit would you consider reasonable before charges should be reduced (eg, a maximum of 48 hours interruption)?

As highlighted in the previous answer, EDBs already have strong incentives to restore power and will do so as fast as possible.

While Part 4 quality incentives are not based on time to restore, they do incentivise EDBs to restore power as quickly as possible. They are designed to minimise the length and frequency of power outages.

This recognises each outage is different and repair times will vary depending on the fault. A time-bound incentive assumes all faults are the same, which they are not.

4.4 How would this longer period incentivise quick restoration of electricity supply and balance the disruption to the consumer and the consumer's right to receive the electricity they are pay for?

It is important note that consumers do not pay for a continuous power supply. We check with consumers after each power outage whether they would be willing to pay for a higher level of service (fewer and shorter outages) and they have said they would not. We publish the results of these surveys annually in our Pricing Methodology³. Eight percent of customers surveyed after an outage said they would pay more for fewer power cuts.

The Commission set the price/quality path to balance service levels with the cost to provide that level of service. The quality incentives that are part of the price/quality path already balance service quality with price.

Applying further quality incentives to the existing Part 4 quality incentives implies a level of quality customers have said they do not want to fund. Price/quality regulation excludes major events that cause long outages to avoid EDBs building networks that are beyond customers' expectations (too expensive). Networks would have to make a significant investment to ensure power is always restored within 24 hours and customers may not be willing to pay the additional cost.

4.5 Do you consider new clause 9.11 effectively addresses the identified problem? Would you propose any alternative approaches? If so, please describe these approaches in your answer.

We agree with the intent of the change but disagree with the proposed application. EDBs do not hold customer information (including addresses) and will not be able to verify the identity of the customer or which ICP relates to a customer's address. All notifications must come from a trader who has the direct relationship with consumers.

We also disagree with using the 'inactive flag in the registry because an ICP can be identified as being inactive but still have a live electricity supply. In line with the ENA's suggestion, we think there should be a separate registry code showing an ICP has been disconnected due to a state of emergency.

³ Page 53, <https://www.welectricity.co.nz/disclosures/pricing/2024-pricing/document/330>

4.6 Do you consider new clause 12A.6 is practical to implement and will deliver benefit to consumers?

The new clause limits how much is passed through to consumers which means consumers will pay more for the refund in the long term. Any refunded amount will be funded by future price increases to consumers and any additional cost (like the portion of the refund retained by retailers) will add new costs to the consumer. The proposed changes will increase long-term prices for consumers (as discussed in section 2.1.2).

4.7 Do you see any issues or have alternative ideas?

As highlighted above, EDBs are already incentivised to restore power quality and the proposed changes provide no additional benefits – rather they increase long-term prices to consumers. Relying on Part 4 regulation to incentivise EDBs to provide the level of quality customers want will avoid retailers (and ultimately the consumer) from incurring additional administration costs.

4.8 Is the revised approach to clause 33.2 appropriate and practical to implement without the need for significant system changes? Please explain your views.

Yes, the revised approach can be implemented, but at an increase in costs for both retailers and EDBs.

4.9 Does the revised approach to clause 33.2 reduce potential implementation costs? Please explain your views.

No, the revised approach will significantly increase implementation costs for both retailers and EDBs.

Wellington Electricity's current DDA has set the 'use of money adjustment' to zero. The reason we removed it was the administration costs of applying the adjustments are high and the application provides little benefit. The unders and overs from the reconciliation process offset cashflow differences and any cost and benefits from applying interest costs is offset.

Its removal reduces costs overall which in turn reduces prices to consumers. We consulted with retailers on this change when we established the DDA and no retailer objected.

4.10 Do you agree with the analysis presented in this Regulatory Statement? If not, why not?

No, we do not agree with the analysis provided in the regulatory statement. The analysis focused only on mitigating implementation issues and did not analyse whether the overall change was needed, including whether the benefits exceeded the costs from making the change. For example:

- What issue is being solved by rebating customer revenue for outages longer than 24 hours and is this change in service something that consumers are willing to pay for?
- Will the benefits of rebating revenue for outages greater than 24 hours exceed the cost of making the payments?

- Is the high administration cost of applying 'use of money' adjustment less than the cost to fund the net reconciliation cashflow differences (the net cashflow differences between retailers and EDBs)?