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Submissions  
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## **SUBMISSION ON DISTRIBUTION PRICING**

The Electricity Retailers Association of New Zealand ('ERANZ') welcomes the opportunity to provide feedback on the Electricity Authority's discussion document 'Supporting reform to efficient distribution pricing: a refreshed Distribution Pricing Practice Note' from September 2021.

ERANZ is the industry association representing companies that sell electricity to kiwi households and businesses. Our members supply over 90 per cent of New Zealand's electricity. We work for a competitive, fair, and sustainable electricity market that benefits consumers.

### **Summary of submission points**

#### **Overall objective**

ERANZ supports the Authority's overall objective to see "faster progress with distribution pricing reform to realise consumer benefits and to facilitate an efficient transition to a low emissions economy". It is apparent from the Authority's distributor pricing scorecards that the sector is not where it needs to be yet. Particularly considering the large-scale change required to facilitate higher electricity usage across New Zealand as we reduce our reliance on fossil fuels.

Retailers support further distributor pricing reform crystallised through this guidance note. A clear articulation from the Authority of "what good pricing looks like" will benefit the sector and provide confidence for the infrastructure investments required to cater for increased electricity supply.

Consumers will also benefit from greater choice in retail prices. Those who wish to reduce their electricity bills by changing their behaviour should be rewarded for doing so. However, those consumers who do not want to, or cannot, change their behaviour should be able to choose a pricing plan suited to them.

#### **Constraints**

The presence of the 'Low fixed charge' is a constraint to pricing reform. ERANZ has long supported removing the regulations and is actively working with MBIE officials on the phase-out. The regulations were not fit for purpose and penalised low-income households who live in poor quality housing. It disadvantages households who can least afford it and subsidises families living in modern, well-insulated homes that do not require much power to heat. Removing the low fixed

charge will encourage households to transition from fossil fuels to electric power, delivering a climate change benefit to New Zealand.

Some industry participants point to a lack of consumption data availability as a constraint on further pricing innovation. ERANZ notes the extensive efforts of retailers and distributors to enter into default distributor agreements ('DDAs') with a specific data sharing template. Following a period of transition, this process is generally working well. Of course, the sector can do more. However, retailers are intermediaries and not the primary holders of customers' consumption data. Efforts for further reform should focus on where the data is generated and how customers can access and share their data.

### **Pass through of price signals**

The most relevant issue to retailers is the issue of "direct" or compulsory pass-through of distribution pricing. ERANZ's position is that pass-through of distribution pricing should be at the discretion of retailers as they respond to consumer demand.

Consumers' preferences, as expressed through the pricing they choose to purchase, is an important signal to the market. It is the role of retailers, who are most exposed to consumer preferences, to design different pricing and product packages to appeal to the cross-section of consumers.

Customers' preferences are not homogenous. Similarly, electricity provision is not a homogenous product, despite some outside appearances to the contrary. Beyond the straightforward consumption of electrons, customer's value derived from their electricity use will vary depending on a range of factors, including the complexity (or simplicity) of prices they face and customer service provided by the retailer.

It is reasonable for different customers to place a different value on having a simple, easily understood pricing structure that shields them from some of the complexity of the electricity market. Customers that place a high value on simple pricing should have the ability to choose a plan that reflects their preferences.

ERANZ agrees with the Authority's overall views, expressed in paragraphs 57-59 that there are multiple ways in which a retailer can reflect peak pricing to their customers, for example, through peak tariffs, flexible load demand, or just higher average prices. In addition, there are multiple ways for the sector to manage periods of peak demand, for example, through the use of ripple controls, the entry of flexibility traders, or 'smart' technology that can flex supply or demand.

Flexibility traders, in particular, will rely on their ability to stand between customers and the market to manage such pricing fluctuations. If they are denied this opportunity, the market for 'multiple trader relationships' and 'distributed energy resources' will struggle to succeed.

Distributors do not need to discourage demand from all consumers during periods of congestion. Distributors just need to prevent enough demand to ensure it remains within their capacity to supply while providing them with the revenue they need to improve infrastructure capacity over time in response to market forces.

Customers who choose to be highly engaged and seek the lowest possible prices can do so, as per the Authority's paragraphs 52-56. But some customers should have the ability to choose NOT to be as engaged; and, if that means they face higher than usual average prices, that is their choice. This reveals their preference for alternative priorities such as quality of service, ease of use, or the ability to consume electricity at any time.

Some customers without the ability to respond to variable distributor pricing will be vulnerable. A key provision of the newly refreshed Consumer Care Guidelines is ensuring customers have a plan that works for them and they can budget accordingly. For some customers, this means choosing a plan smoothed over twelve months to provide predictable bills. Any requirement for direct pass-through of distribution pricing would disadvantage some of these vulnerable consumers.

Should sufficient customers choose a plan where they are not exposed to complex, cost-reflective pricing, this could be a signal to distributors that customers value more capacity on the network and trigger additional investment. The cost-reflective pricing still has value, because it could generate the revenue distributors can use to fund such investment. ERANZ recommends the Authority focus its work programme on regulations allowing distributors the flexibility to respond to these demand signals, rather than on regulations mandating pass-through.

Customers, including commercial, thinking about reducing their greenhouse gas emissions will seek to replace fossil fuel appliances, or even cars, with electric. However, this often comes with a high upfront capital cost, so customers will calculate the payback period of their investment. In an environment with direct pass-through, these customers' bills could be highly variable, leading to them losing confidence in electricity as a stable, reliable fuel source. This, in turn, could chill investment in electric conversions at the very time the country is seeking to reduce its emissions rapidly.

### **Economic literature analysis to support our position**

The importance of allowing retailers to set their own pricing plans led ERANZ to commission a report from independent consultants TBD Advisory. Their analysis is attached as an appendix to our submission. The purpose of this report is to examine the available literature and draw conclusions on how pricing pass-through could impact consumers and market efficiency.

TBD's key conclusion is that:

*“Our analysis finds that the effectiveness of transparent distribution price signalling does not depend on a mandated pass-through to end-consumers of distribution prices by the retail sector. Sufficient market response can come from the proportion of the retail market that is most willing to respond to such price signals without requiring the price signals to be conveyed directly to all consumers.”*

Based on these findings, ERANZ's strongly held view is that reform of distribution pricing is necessary and beneficial to the market; but requiring a direct or compulsory pass-through of distribution pricing by retailers is detrimental to consumers.

If we are to put consumers at the heart of the electricity system, consumers should drive the evolution and shape of the industry – not the other way around.

## Questions

ERANZ has answered below selected questions from the consultation paper that are most relevant to our members.

| Consultation themes for feedback |   |
|----------------------------------|---|
| <b>9</b>                         | <p><i>Engaged customers are more likely to respond and in a more predictable manner than disengaged customers. What role do you see the Authority has in supporting consumer engagement on pricing?</i></p> <p>Customers will choose the level of engagement that best suits them and their preferences must be taken into account. Some customers, particularly vulnerable customers, already find retail pricing complex and challenging to navigate. Consumer advocates raise this as an issue, and it was identified last year by the Authority through the Consumer Care Guidelines development process.</p> <p>Retailers make extensive efforts to guide customers through different pricing plans so they can find one that best suits their needs. However, any proposal to make retail pricing plans even more complex, with a direct pass-through of variable distributor pricing, will add a potentially overwhelming level of complexity.</p> <p>Standing between the market and customers is a service retailers, and flexibility providers give to their customers. It allows tailored pricing plans that suit customers, whether it is highly variable time-of-use plans or consistent, smooth prices over a year – customers should have this choice.</p> <p>The role of the Authority is to encourage the development of diversified retail pricing plans and a multiple trading relationships ('MTR') regime. Direct pass-through will stifle MTRs by denying them the ability to arbitrage between different players in the sector. Instead, by encouraging MTRs, the Authority can gain the benefits of distributor pricing reform without requiring end customers to be fully engaged because they have outsourced this to their flexibility provider.</p> |
| <b>10</b>                        | <p><i>Ensuring that targeted pricing signals impact decision-makers is important in distribution pricing reform. What role do you see the Authority has in supporting an industry discussion on ensuring price signals reach consumers, taking into account the need to comply with the Commerce Act 1986?</i></p> <p>Consumers who are highly engaged and price-sensitive will respond to price signals from distributors. Their resulting behaviour change will be enough to avert chronic congestion across many parts of the network. In addition, innovation in the MTR marketplace will further alleviate congestion. ERANZ supports distributor pricing reform for these reasons.</p> <p>ERANZ submits, however, that forcing customers, or “decision-makers”, to experience distributors’ pricing signals directly is counterproductive to many of the Authority’s goals, including consumer care and encouraging a new MTR marketplace – as described in answer to question 9.</p> <p>It is equally important that consumers’ price preferences reach the sector, including retailers and distributors.</p>  |
| <b>11</b>                        | <p><i>Complexity in pricing structures could slow reform efforts. How do you see the Authority working with the sector to strike the correct balance?</i></p>   |

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|           | Existing retail pricing complexity is already overwhelming for some vulnerable customers – as described in answer to question 9. Requiring further complexity is untenable and will work against many of the recent consumer-focused reforms, including the Consumer Care Guidelines.  |
| <b>12</b> | <p><i>Can you provide feedback on how bill shock can be managed by industry and the Authority, to support ongoing reform of prices and not unduly impact on groups of customers?</i></p> <p>Retailers perform a valuable role in shielding customers from the volatility of the market. The only way to avoid bill shock is to allow retailers (and other flexibility traders) to continue to stand between customers and the market. Allowing retailers to perform this function means any requirement for direct pass-through of distributor pricing falls down.</p> <p>As stated in previous sections of this submission, almost all of the benefits from distributor pricing reform can be achieved without compulsory pass-through. Compulsion will introduce hard to mitigate customer harm while creating only marginal benefits through additional deferred infrastructure investment.</p> |
| <b>13</b> | <p><i>Are there aspects of LFC and its announced phase out that you see as an ongoing impediment to pricing reform?</i></p> <p>While ERANZ prefers a shorter LFC phase-out period, the currently proposed five-year transition is manageable.</p>  |

## Conclusion

ERANZ supports the Authority examining whether its regulatory settings support New Zealand's transition to a low-carbon economy. However, we consider the Authority further exploring the question of compulsory pass-through of distribution pricing to customers a low priority that is not supported by clear evidence of a problem to solve.

Thank you again for undertaking this review of distribution pricing guidelines. We are available to discuss our submission further if required.

Yours sincerely



**Cameron Burrows**  
Chief Executive

## Appendix One:

“The determination of retail prices in the NZ electricity market”, TDB Advisory, November 2021.