Mid-point Review of the phase-out of the LFC regulations

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Executive summary

1. In 2004 the Low Fixed Charge (LFC) regulations were introduced with the aim of supporting lower use households with their electricity bills. Although not stated in the regulations, the decision papers confirm the regulations were particularly intended to help low-income households.

2. However, in 2019, the independent Electricity Price Review found that the Low Fixed Charge (LFC) regulations had significant unintended consequences – including a cross-subsidy paid by larger (including low-income) households to smaller households – and recommended that they be phased-out. A further reason was that the LFC regulations may reduce the availability of innovative pricing plans that should create new ways for households to save by flexing their demand and reducing overall costs throughout the electricity system.

3. The Mid-point Review has assessed the impacts of the phase-out on household electricity prices, looked for evidence on whether the aims of removing the LFC are likely to be achieved, and considered whether additional support measures may be necessary. This report summarises analysis of retailers' and distributors' pricing data, as well as qualitative feedback provided by consumer groups, regulators, and other interested parties.

This Review's key findings are:

4. The phase-out is delivering the benefits expected from it. More consumers bills have been reduced than increased by the fall in cross-subsidies imposed by the LFC regulations. The phase-out reduced the bills of approximately 45 per cent of household's bills by an average of $62 a year, while the impact on a further 15 per cent of households was essentially neutral.

5. A small minority of consumers are facing higher bills due to the reduction in cross-subsidies triggered by the phase-out. The six per cent of consumers who use the least amount of electricity (who are most likely to be single-occupancy households) may have seen their disposable income decrease by up to 0.6 per cent between 2021 and 2024 during the phase-out. Some consumers in this group may be at increased risk of experiencing energy hardship with the removal of the LFC.

6. The industry-funded 'Power Credits' scheme has been available to cover the losses that a low-use household may experience during the phase-out. Approximately only 1.04 per cent of consumers bills have been impacted by more than the $110 available in Power Credits.

7. Targeted initiatives should be used to assist low users at increased risk of energy hardship, rather than broad pricing regulations that affect many or all customers. The Review found that other cost drivers are having a greater impact on bills than the phase-out, even among very low users who are most affected by removal of the cross-subsidy imposed by the LFC. As a result, it is important that work across MBIE, Electricity Authority (EA), and Commerce Commission (Commission) prioritise opportunities to ensure wholesale markets are competitive and efficient, network prices are efficient, and to ensure households can take advantage of newer and more substantial means of reducing their bills. Removing the LFC regulations should assist several programmes of work that aims to drive down these wider costs.

1. Objectives, scope, and approach of the Mid-point Review

The Review has focused on the phase-out's impacts on different consumers

8. When the phase-out of the LFC regulation began it was acknowledged that there was some uncertainty over how the industry would choose to structure its pricing plans and what impact those plans would have on different consumer groups. Therefore, the then-Government decided that there should be a Mid-point Review of the phase-out.

9. In completing this Mid-point Review, MBIE has:

    - assessed the impacts of the phase-out on low-income households
    - considered whether additional support measures for specific household types may be necessary.

The Review has used a combination of quantitative and qualitative analysis

10. To carry out this assessment, the Review addressed the following questions:

1) How have prices changed and to what degree was this driven by the phase-out?	• How have fixed and variable prices changed? • To what extent have other factors influenced prices? • How have specific demographic groups been impacted?
2) Are the aims of the phase-out being achieved or likely to be achieved?	• Assess if expected benefits are occuring, or are likely to occur by the time the regulations are removed. • Whether underlying conditions have changed such that the phase-out would not have been agreed to.
3) Are additional support measures necessary now or from 2027?	• Consider the effectiveness of the Power Credit Scheme. • The impact of other electricity market initiatives.

11. To address the question focussing on how prices have changed, Sense Partners was commissioned by MBIE to undertake quantitative analysis of both distribution and retail pricing data from 2021 to 2024. During the phase-out, the expectation was that fixed charges on low use plans would increase while variable charges on low use plans and both fixed and variable charges on standard plans would decrease (all other things being equal). However, there have been concerns that variable charges have not reduced to the extent that may have been expected. This analysis, covered in section 3 of this report, has unpicked how prices have changed and to what extent other factors, such as inflation and higher wholesale prices, have influenced power prices during this period. The impact on superannuitants and larger, lower-income households has also been considered and is covered in section 5 of this report.

12. To address the second question, MBIE has assessed whether the benefits outlined in advice to the Government to support its decision to phase-out the LFC regulations are occurring as expected, or, are likely to occur when (or soon after) the regulations are completely removed from 1 April 2027. The Review also assessed whether any underlying conditions have changed such that a different decision might be considered. The expected benefits of the phase-out of the LFC regulations are outlined in section 2.

13. To address the third question, section 5 of the Review compares the scale of the Power Credit scheme (introduced at the start of the phase-out) to the impact of removing the cross-subsidy for low users. It also considers the potential adverse impacts of increasing fixed charges on low-income low users, against the wider cost pressures on electricity bills and the other supports available to households at risk of energy hardship.

2. Overview of the LFC regulations

The LFC regulations were introduced over 20 years ago and were intended to assist low-income households

14. In the early 2000s, there were growing concerns about the increasing size of fixed charges as a proportion of consumers power bills. In 2004, after an industry-led solution was deemed to be insufficient, the then-Government introduced the Electricity (Low Fixed Charge Tariff Option for Domestic Consumers) Regulations 2004 – the LFC regulations.

15. The objective of these regulations was to make consumers who used less than the then annual national average of 8,000kWh, better off. In particular, they were designed to help low-income households and "older New Zealanders on fixed incomes who are typically frugal users of power".

The regulations require plans to be structured and marketed in specific ways

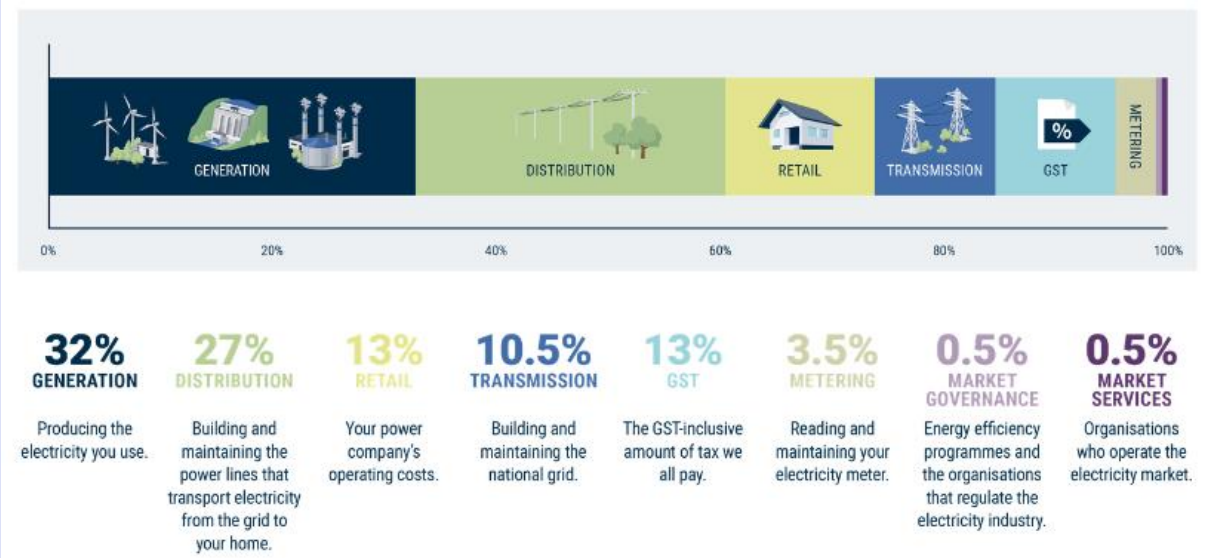
16. The LFC regulations require that, for each electricity plan a retailer has available, it must offer a low use equivalent of that plan with a fixed charge of no more than 30 cents per day (excl. GST). At the retail level, low use plans also needed to include the following features:

    - The variable charge must be at a level that a household using less than 8,000kWh (or 9,000kWh in the lower South) would always pay less on the low use plan than the equivalent standard plan.
    - Low use plans only need to be made available to households that are a primary place of residence (i.e., the regulations do not apply to baches).
    - Low use plans must be advertised at the same time and manner as other plans and households must be informed at least annually whether they would benefit from switching to a low use plan.
    - Retailers must make low use plans genuinely available, irrespective of the usage and/or meter configuration of the household.

17. The LFC regulations also required electricity distribution businesses (EDBs or distributors) to make low use plans available. EDBs' low use plans were required to have a fixed charge of no more than 15 cents per day (excl. GST) and keep variable charges set at a level so that a household using less than 8,000kWh (or 9,000kWh in the lower South) would always pay less on the low use plan than the equivalent standard plan.

Explainer - Elements of a power bill

Retailers are the consumer-facing end of the electricity industry. Their role is to package up all the various costs from the entire system and pass those through to consumers. Although it may not always be clear, the bill covers all the costs a household incurs for using the electricity system. An average household power bill contributes to the following costs:



Source: Electricity Authority

Network costs, comprising distribution charges and transmission charges, contribute to building and maintaining the infrastructure (pylons, substations, poles, and wires) required to take power from generating stations to homes and businesses. This infrastructure cost represents around 37.5 per cent of household power bills. Transpower and EDBs are natural monopolies, as it wouldn't be efficient for there to be two or more competing national grids or local networks, and so are regulated by the Commerce Commission. Every five years, the Commission sets the maximum revenue they can recover from consumers.

The costs of generating and retailing electricity make up around 45 per cent of the typical bill. These parts of the industry are competitive. GST, metering, and market fees (which fund the Electricity Authority's work to regulate the market and fund market operations), make up the remainder.

Fixed and variable charges on a power bill

Electricity tariffs in New Zealand generally comprise of two key components – a fixed charge and a variable charge. The fixed charge component is designed to recover the 'fixed' costs (i.e., not dependent on how much electricity is used) associated with delivering electricity to households. Transmission and distribution costs are generally fixed and ideally are recovered through a fixed charge. Fixed charges are generally charged at a flat daily rate (e.g., $1.20 per day).

The variable charge is designed to recover costs that change with the amount of electricity consumed. Generation costs can be recovered through variable charges as greater demand means more supply is needed which increases costs for the generator. Variable charges are generally charged at a cents per kilowatt hour rate (e.g., $0.28 cents/kWh). Increasingly, power bills are using multiple different variable rates which are used to signal the difference in cost depending on time of day or use of the system (i.e., electricity can be more expensive when it's in high demand during peak periods so differing variable charges can signal this changing cost).

The LFC regulations were found to have unintended consequences and began being phased-out in 2021

The 2019 Electricity Price Review recommended phasing-out the regulations

18. In 2019, the independent Electricity Price Review found that the LFC regulations were having significant unintended consequences and recommended phasing them out. Despite lowering costs for some households, it has long been acknowledged by industry analysts that the LFC regulations were poorly targeted at helping low-income households.

19. The LFC regulations began to be phased-out in 2021. A five-year phase-out was specifically chosen to reduce the impact of sudden changes to consumer bills.

20. An industry-funded '*Power Credits*' scheme was put in place (intended to run 2021-2027) to provide financial support to households facing higher power bills as a result of the phase-out. The then-Government also decided that there should be a Mid-point Review of the phase-out.

The regulations created a cross-subsidy paid by larger (including low-income) households to smaller (including higher-income) households

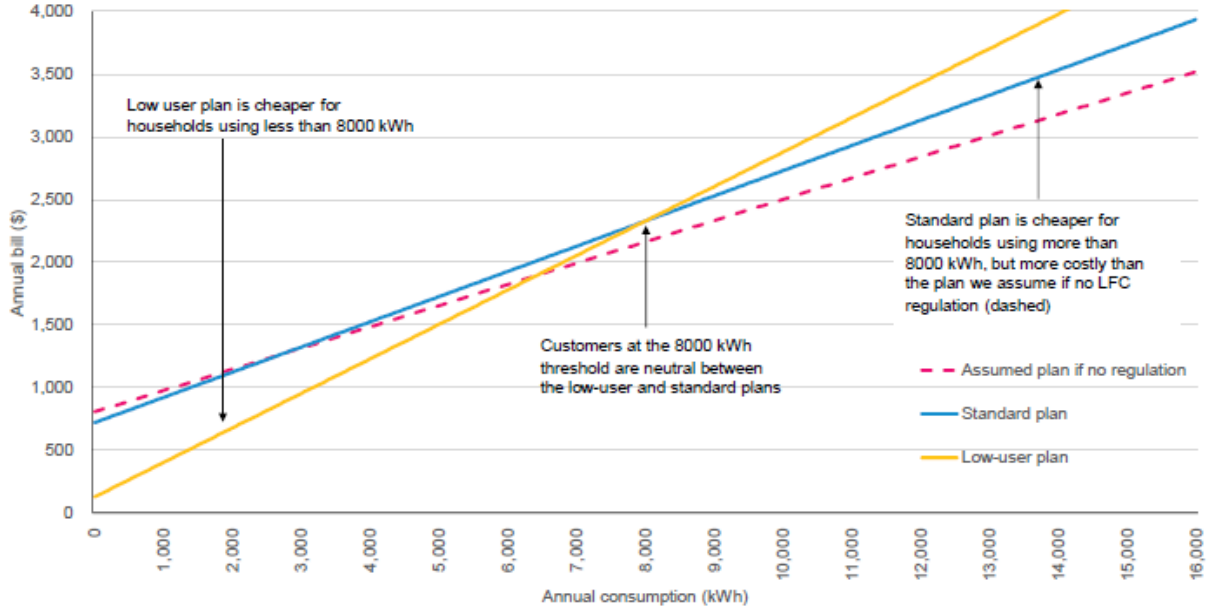
21. The LFC regulations reduced fixed charges for households on low use plans but have resulted in higher charges for standard plans. The Electricity Price Review found that, while households on low use plans do pay a higher variable charge, this is not sufficient to recover the shortfall from the artificially (regulation-mandated) lower fixed charge. As a result, households on standard plans are paying more for their electricity to offset the under-recovery of fixed costs from those households on low use plans.

22. Figure 1, below, shows annual bills of consumers on low use and standard plans compared to what the same bills would be in the absence of the LFC regulations. This illustrates the cross-subsidy that the LFC regulations introduced: households with higher consumption are cross subsidising households with lower consumption.

23. Electricity use is a poor indicator of income level, which has resulted in the LFC regulations being a poorly targeted intervention for those with limited means. The number of people living in a home, especially the number of children, is a stronger indicator of electricity use. Many higher use households, which now face higher bills as a result of the LFC regulations, are large, lower-income households, whereas lower consumption households can be higher-income households with double-glazed windows and good insultation.

24. The regulations have also, on average, increased power bills for households who are on low use plans but use more than 6,500kWh a year.

Figure 1: Annual bills of low use and standard plans compared to bill if there were no LFC regulations (illustrative only)



Source: Electricity Price Review: First Report

The regulations disincentivise household electrification

25. When the LFC was introduced energy conservation was a leading energy policy priority. Before smarter retail plans (with time-of-use pricing) and electric alternatives to fossil-fuelled resources (such as petrol cars and gas heating systems) became more commonly available, reducing electricity usage was one of very few ways households could save on their energy bills. Reducing overall power demand was also more important to supporting the security of, and reducing the emissions from, the electricity system.

26. However, kiwi households' energy use has become more efficient in the past decades. Despite more electric appliances entering homes, average residential power use has fallen 10 per cent since 2010, from 7,903 to 7,088kWh.[1] Moreover, as cheaper, cleaner, but more intermittent renewables sources increasingly underpin New Zealand's electricity system, flexible demand (the ability to shift usage away from peaks in demand and troughs in supply) has become more critical to support energy security, affordability, and sustainability, than blunt measures that aim to reduce a household's total demand.

27. Households now have more options to save money by electrifying their vehicles, cooking, and heating systems. Research by Rewiring Aotearoa, using data from the Energy Efficiency & Conservation Authority (EECA), suggests that New Zealanders could save approximately $1,637 a year (over 15 years) from choosing an electric, rather than petrol vehicle. Furthermore, by fully electrifying, households could potentially save between $1,485 and $4,699 per year on their overall energy bills.[2]

[1] Source: MBIE (June 2024). Household sales-based electricity costs data. www.mbie.govt.nz/building-and-energy/energy-and-natural-resources/energy-statistics-and-modelling/energy-statistics/energy-prices/electricity-cost-and-price-monitoring

[2] Source: Rewiring Aotearoa (2024), Electric Homes Report www.rewiring.nz/electric-homes-report
The statistics on full electrification are based on an average home of 2.8 people with 1.8 vehicles switching

28. However, as the LFC regulations force retailers and distributors to recover more costs through variable charges, it penalises households who increase their electricity use. This decreases the financial benefits of electrifying. It will be counterproductive if regulations discourage retailers from supporting and rewarding consumers who invest in and utilise new smart technologies that reduce demand for peak generation, and help delay or avoid network investments, and so help lower the overall cost of electricity. Electrification is also a key path towards meeting New Zealand's emissions commitments.

The regulations are a barrier to more efficient distribution pricing and tariff innovation

29. Networks charge distribution prices to cover the costs of maintaining, upgrading, and developing the lines and other equipment that delivers electricity from the transmission system (or local generation) to homes and businesses. The majority of a distributor's costs are fixed, although the total amount of electricity used at peak times influences whether network investments will be needed to meet demand.

30. Cost-reflective price signals allow networks to signal network constraints and encourage usage away from peak times. This helps avoid inefficient network overbuild, and so limit household power bills for all consumers.

31. Cost-reflective pricing and further tariff innovation can help support electrification. Retailers who offer a variety of plans ensures that households – who opt-in to, for example, time-of-use (ToU) plans – to respond to these signals by managing when and how they use electricity, and so enables them to better control their power bills. However, the LFC regulations have been described by industry as 'a handbrake' on innovation as they restrict the introduction of new tariffs which better signal higher wholesale costs or when the network is constrained.

32. To support distributors to move towards cost-reflective pricing in a timely manner, the EA publishes 'Pricing Principles' to guide how distributors should set their pricing methodologies. In essence, the guidelines encourage distributors to set charges that reflect underlying costs, and also where appropriate, contain an element of 'signalling' that reflects the cost of future network investments. Such signalling aims to encourage customers to shift demand in a manner that will delay or avoid the need for investment in more poles and wires. Retailers also seek to offer tariffs to meet different customers' consumption profiles – what suits one family might not suit a similar family next door, given slight variations in total, and timing of, consumption.

33. However, the LFC regulations work against the EA's pricing principles: the regulations limit distributors' ability to align with the regulator's guidance (for cost-reflective prices and signalling). Moreover, the regulations' requirement that a low use tariff is offered to parallel with every standard-use tariff, which can become a barrier to tariffs that are designed for specific or larger consumption profiles.

their space heating, water heating, cooking, vehicle type, and taking advantage of rooftop solar and home batteries over 15 years. The range is influenced by whether investments are supported by low interest finance.

34. The LFC regulations also create an incentive on households to reduce electricity consumption, which can distort consumers' investment decisions. As we move to electrify, households will increasingly choose options which increase their electricity use, such as buying an EV instead of an internal combustion engine or electrifying gas heating and cooking systems. Regulations that increase the costs of using electricity run counter to wider government objectives to support, for example, uptake of EVs in New Zealand.

The phase-out was expected to deliver several benefits to consumers

35. When the decision to phase-out the LFC regulations was taken, a number of benefits were identified as likely to eventuate from the removal of the regulations. These benefits were to:

    - limit barriers to distribution tariff reform
    - limit any unintended price distortions for consumers which could result in artificial incentives to over-invest or under-invest in particular technologies
    - enable a more equitable electricity market particularly for vulnerable consumers
    - reduce the levels of complexity and confusion in the electricity market for both consumers and industry
    - support movement towards greater electrification.

36. In terms of the financial impact on household bills, it was acknowledged that the phase-out would increase bills for some households, including some superannuitants and low-income households. It was anticipated that the phase-out would result in lower bills for approximately 60 per cent of consumers while approximately 40 per cent of consumers were expected to face an increase to their power bills.

37. As the LFC regulations have not yet been removed, and retailers are still required to offer low use versions of every plan, the potential barrier to retail and distribution pricing innovations can be expected to remain until April 2027.

38. Given this, we have considered which outcomes could provide a clear signal that the phase-out is not resulting in the anticipated outcomes. If found, the following outcomes would indicate that the phase-out is having an unacceptably negative impact:

    - both fixed and variable charges on low use plans rise significantly with no clear evidence of impacts from other factors
    - no reduction in prices for those households which were paying more for their electricity as a result of the LFC regulations.

39. The analysis carried out for this Review does **not** indicate these negative outcomes are occurring. This is discussed further in sections 3 and 4.

3. Quantitative analysis of the phase-out's impact on prices

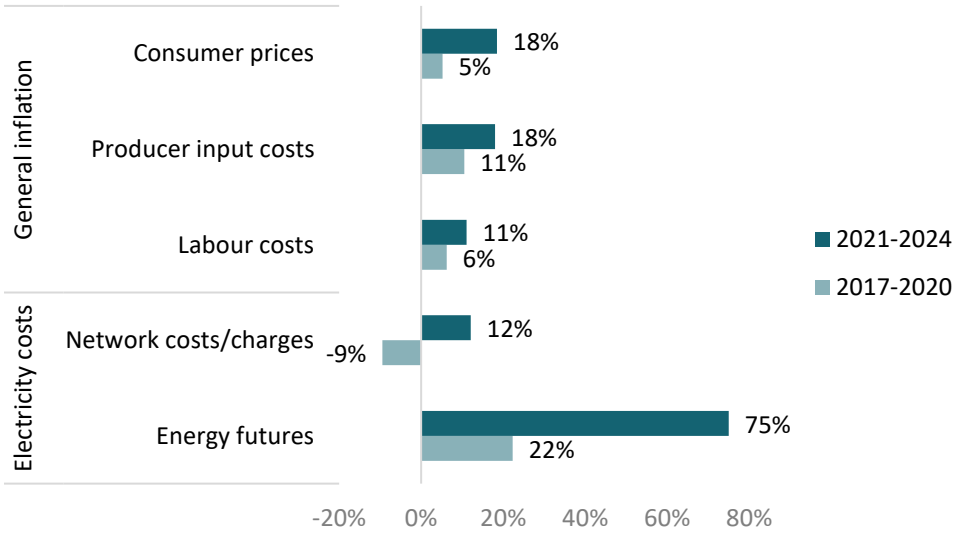
40. Sense Partners' analysis of pricing data from retailers and distributors suggests that the phase-out is delivering the expected benefits. There is evidence that cross-subsidies from average and higher users to lower users are reducing, resulting in 'more winners than losers'. A small minority of consumers, the six per cent who live in households with the lowest usage, will see real term increases in their bills because of the phase-out and wider electricity cost changes. The impacts on this group, and the wider supports available to them, are discussed in more detail later in this report.

41. As expected, quantitative data provided limited insights into whether removing the regulations will unlock greater pricing innovations, although qualitative information from retailers and distributors gives more reason to be optimistic about future innovation. Within traditional pricing structures there is initial evidence that retailers are beginning to differentiate their plans in ways that should offer meaningful choices to more lower users.

Average electricity prices have not increased because of the phase-out

42. The LFC regulations do not limit the overall prices that distributors and retailers can charge consumers, only the way they spread their costs between the fixed and variable charges and between higher and lower users. All other factors being equal, electricity consumers as a whole should not pay more as a result of the LFC regulations being phased-out. However, all the other factors that influence electricity prices have not been equal during the phase-out. Since 2021 New Zealand has experienced unusually high inflation and a sustained increase in wholesale electricity prices, which has begun passing through into retail prices. Figure 2 summarises how these costs have broadly risen between 2021 and 2024.

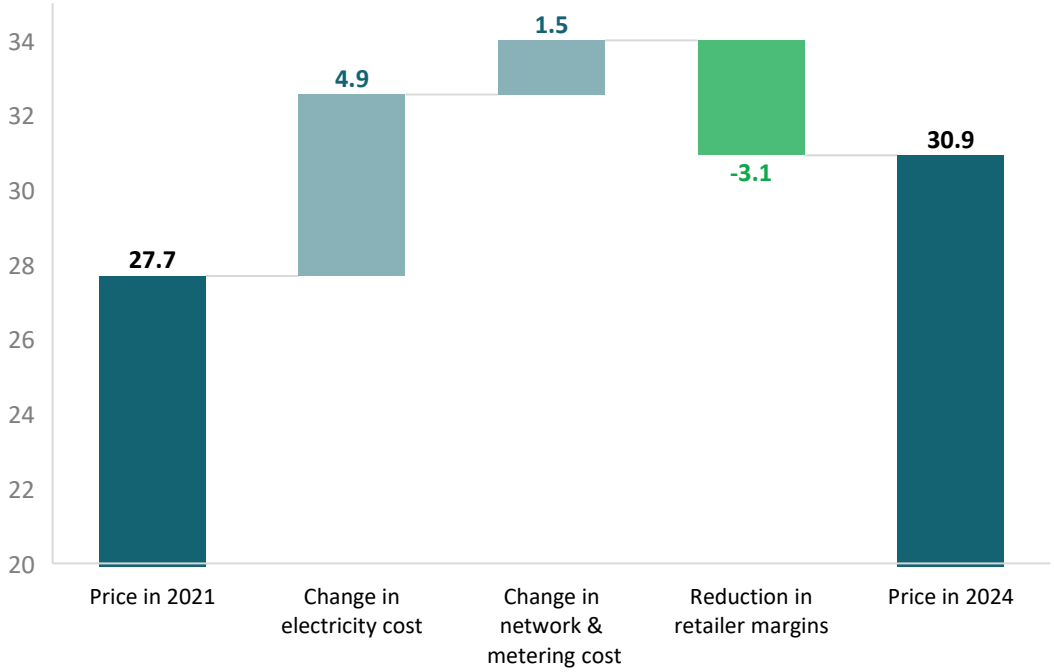
Figure 2: Indicators of industry costs changes (to nominal prices) during and before the phase-out



Source: Sense Partners (2024), Phase-out of the Low Fixed Charge regulations: Quantified price effects for the first 3 years

43. Concerns that retailers might use the removal of the LFC to increase their profits at consumers' expense have not materialised. In fact, if retailers have completely passed through rising wholesale, network and metering costs during the phase-out, the average household electricity price would have been approximately 10 per cent higher than it was in 2024. Instead, it appears retailers have seen their margins fall, as illustrated in figure 3.

Figure 3: Impact of cost increases on retail prices and margins. Approximate effects in cents per kWh.



Source: Sense Partners (2024), Phase-out of the Low Fixed Charge regulations: Quantified price effects for the first 3 years

44. The apparent reduction in retailers' margins during the phase-out could have been influenced by several factors, some of which are briefly discussed in Sense Partners' report. However, it is clear that retailers have not used the phase-out to increase their overall revenue at consumers' expense.

45. When controlling for the wider costs of goods and services in New Zealand, Sense Partners found that household electricity bills have fallen by seven per cent on average since 2021. With the exception of very low users (the six per cent of consumers that use under 4,000kWh a year) the vast majority of energy bills have risen more slowly than other prices in the economy, median household disposable income, and superannuation rates during the phase-out.

There have been more winners than losers from the phase-out

46. It was anticipated that the phase-out would see a rebalancing between the bills of lower and higher users, addressing the cross-subsidisation warned of by the 2019 Electricity Price Review. As expected, distributors and (to a lesser extent) retailers have rebalanced more of their costs from variable to fixed charges, which generally reduced the bills for higher users and increased those for lower users.

47. Sense Partners' analysis indicates that more consumers have seen their bills reduced by the phase-out than increased. In total dollar terms, the savings for average and higher users exceeds the additional charges faced by lower electricity users.

48. As figure 4 illustrates, annual bills for most users, with consumption close to the average household usage of 7088 in 2024,[3] stayed very similar or fell slightly due to the phase-out. Key findings are:

    a. Households who used more than 7000 kWh – roughly 880,000 or 45 per cent of all households – saw their bills decrease, on average, as a direct result of the phase-out.[4]

    b. The impact on households using between 6000 and 7000 kWh – roughly 280,000 or 15 per cent of households – was effectively neutral.

    c. Households using less than 6000 kWh a year – roughly 790,000 or 40 per cent of households – saw their bill increase due to the phaseout.

    d. Roughly one in five of the households that would have been considered low users when the LFC was introduced have since seen their bill reduce, due to the phase-out.

49. The impacts of the phase-out are most noticeable for consumers with particularly high or low usage:

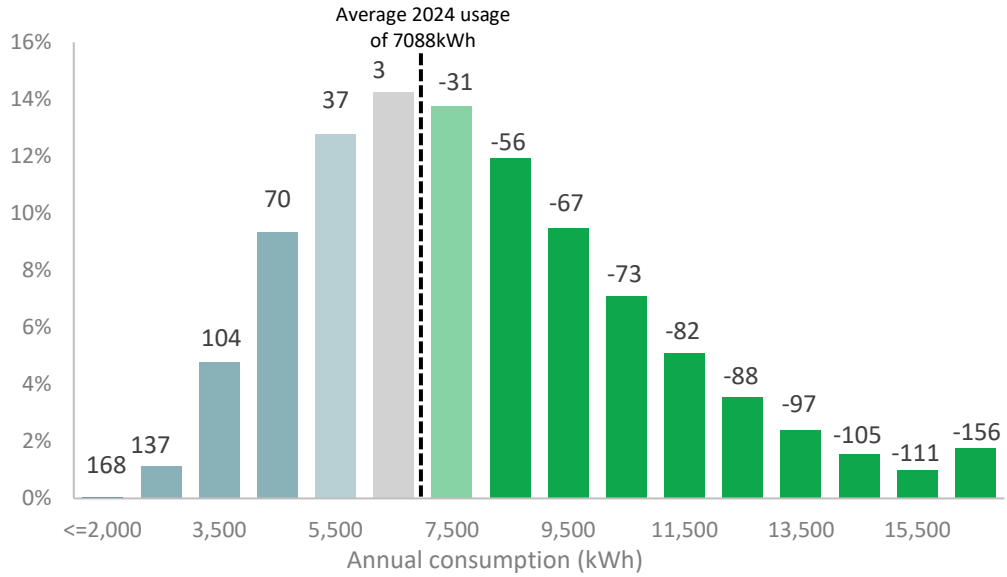
    a. Bills for approximately 22 per cent of consumers who live in households using over 10,000kWh fell by $90 on average, when wider electricity costs are accounted for.[5]

    b. In contrast, bills for the six per cent of consumers living in households with the very low usage, under 4,000 kWh a year, rose by $125 on average.

50. Rebalancing costs from variable to fixed charges should also help households looking to electrify. For example, if a household with average consumption invested in electric vehicles it might increase their usage by 3,465 - 5,277 kWh a year, taking it from around 7,088 to between 10,553 - 12,365 kWh a year. Based on the pricing data collected for this Review, that household would save approximately $73 - 88 more a year due to the phase-out.

[3] Source: MBIE (June 2024). Household sales-based electricity costs data. www.mbie.govt.nz/building-and-energy/energy-and-natural-resources/energy-statistics-and-modelling/energy-statistics/energy-prices/electricity-cost-and-price-monitoring
[4] As more people live in higher using households, this represents an overall majority of individual consumers.
[5] The average bill reduction per households was $102. The average per consumer is lower as there are typically more people living in higher usage households.

Figure 4: Effects of the phase-out on household electricity bills in 2024



Source: Sense Partners (2024), Phase-out of the Low Fixed Charge regulations: Quantified price effects for the first 3 years.[6]

A minority of households are negatively impacted by the phase-out

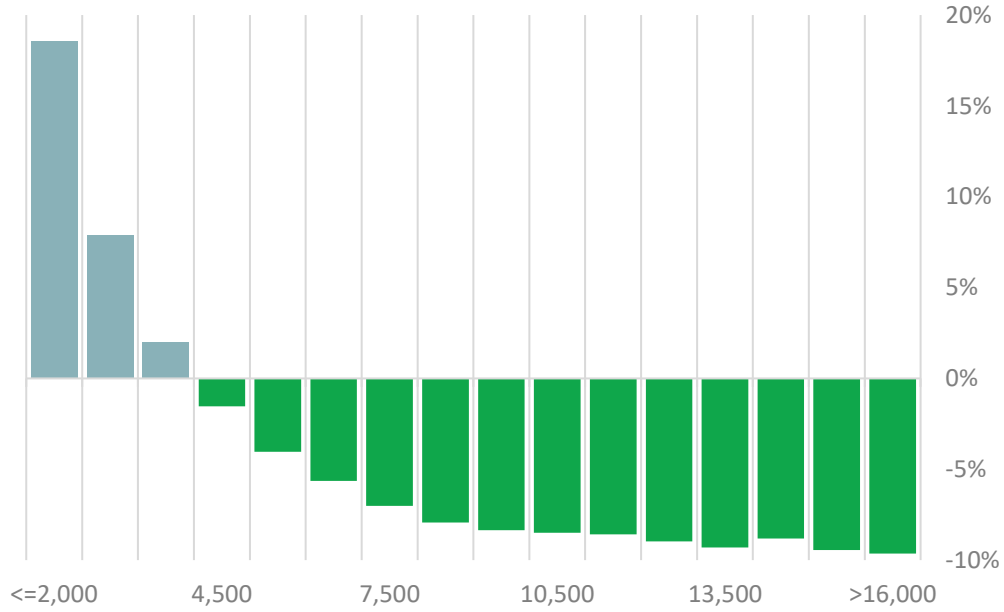
51. Roughly one in five consumers have seen their nominal electricity bills increase by tens of dollars a year due to reduction in cross-subsidies from the phase-out, while a further six per cent with the lowest usage (under 4,000 kWh a year) may have seen their bills rise by an average of $125 a year.

52. However, it is only the latter group who have experienced a real increase in their electricity bills since 2021 (as figure 5 shows), when changes in general inflation and trends in disposable income are taken into consideration.

53. As discussed in section 5 of this report, electricity use is a limited predictor of a household's vulnerability or risk of experiencing energy hardship. However, some of the users most affected will include people at risk of financial hardship. Support available to help this group, including the industry's Power Credits Scheme, is discussed further in this report.

[6] Values above the bars are changes in annual expenditure in 2024 at 'sticker' prices, and do not control for general inflation. Bars represent the percentage of all New Zealand consumers. Labels showing the arithmetic mid-points of 1000 kWh bands.

Figure 5: Real changes in bills for different levels of usage between 2021 and 2024



Source: Sense Partners (2024), Phase-out of the Low Fixed Charge regulations: Quantified price effects for the first 3 years

Consumers have still been able to choose plans with lower fixed charges

54. Sense Partner's analysis found that retailers have increased fixed charges at different speeds and degrees during the phase-out, with some offering fixed charges lower than those they are paying to distributors on behalf of customers. In 2024, just over 300,000 households (15 per cent) were on the maximum permitted fixed charge of 120cents per day while over 230,000 households (12 per cent) were on a fixed charge of 60cents per day or less.

55. This suggests that some retailers are looking to differentiate themselves from competitors and appeal to lower users. If this continues following the phase-out, low users should still be able to find pricing plans that are designed to benefit them.

The effects of the phase-out have been similar across most regions

56. Sense Partners found few headline differences in the effects of the phase-out across most regions. Otago is the one major exception where the distribution business, Aurora, has chosen to only use low fixed charges and, in some of the areas it serves, has comparatively high variable charges so that few customers really benefitted from the low fixed charges as they were before the phase-out. Headline similarities do however cover more nuanced differences in regional cost changes, household usage levels, and local distributors pricing decisions. For example, in Northland, where there are more low use households, the impacts of the phase-out appear to have been limited by the pricing decisions of local distributors.

4. Qualitative analysis of stakeholders views on the phase-out

57. In addition to collecting data on prices over recent years, the Mid-point Review invited retailers, distributors, consumer groups, regulators, and any other interested parties to share their views on the impact of phasing-out the LFC regulations. The following section briefly summarises some of the key themes from different stakeholders.

58. Copies of responses to the Review have been published alongside this report. As retailers and distributors views were provided alongside confidential pricing data, a separate summary of their qualitative responses has been prepared.

Stakeholders had different overall perspectives on the phase-out

59. Distributors, retailers, the EA, and the Infrastructure Commission (Te Waihanga) all strongly supported the continued phasing-out of the LFC.

60. In contrast, several of the consumer and community groups that responded to the Review proposed that the phase-out should be reversed or that other alternatives interventions should be introduced instead. Their proposals are discussed later in this section.

Stakeholders' commentary of price aligns with the quantitative analysis

61. Retailers' and the EA's commentary of pricing changes during the phase-out closely matched Sense Partners' analysis. They reported that more customers had benefitted from the phase-out and that variable charges would have fallen if wider factors (wholesale prices, network costs, and inflation) had not increased.

62. Similarly, the vast majority of distributors reported that variable charges, for both standard and low users, had decreased as fixed charges increase, in some instances significantly. This aligns with the rebalancing of costs expected during the phase-out.

63. Several consumers and community groups raised concerns about the risks to low users of the phase-out but these were mostly in the context of wider overall cost pressures facing households. Notably, FinCap, a charity representing financial mentors, reported frustrations that the Power Credits Scheme has been delivered inconsistently between retailers, with some consumers believing they need to go into arrears before they can access support.

64. Most distributors thought the phase-out had not yet had sufficient opportunity to influence peak demand and so has yet to avert major network expenditure. However, some initial evidence of peak demand reductions was noted, and distributors thought the removal of the regulations would reduce investment required in future.

65. The Infrastructure Commission and EA emphasised that removing the LFC will, and is beginning to, allow more cost-reflecting distribution pricing. They noted that removing the LFC was important for enabling their wider work programme to develop a more flexible electricity system and unlocking wider savings for consumers.

Retailers and distributors have signalled an eagerness to introduce more pricing innovations when the phase-out is complete

66. Retailers and distributors emphasised that the LFC regulations continue to inhibit innovation. As noted above, during the phase-out they are still required to offer low use versions of all their plans and that low use customers are no worse off regardless of the design intention of the plan. The EA has highlighted that adherence to this requirement may be impractical for more complex tariffs, resulting in them simply not being offered to consumers.

67. Retailers, distributors, and the EA highlighted some examples of innovations benefitting households being introduced or piloted during the phase-out, including time-of-use tariffs that rewards households for shifting usage to off-peak times, bonuses for providing power back to the grid at peak-times, and retailers engaging in hot water control. For example, Electricity Networks Aotearoa noted that electricity distribution businesses now offered time-of-use pricing for 94 per cent of residential consumers, compared to 84 per cent in 2022-23.

68. However, retailers and distributors offered considerably more examples of innovative plans they could, and are eager to, introduce when the LFC requirements ended. Examples include:

    a. Subscription pricing – similar to broadband or mobile plans which provide different levels of plans for a set monthly fee.

    b. Stepped pricing – households pay a set rate for a certain level of use and higher rates for use above the agreed level.

    c. Capacity based pricing – charge based on the size of a household's connection to the network, or a household's real-time load.

    d. Backward-looking peak demand charges – leading to real-time or dynamic peak demand charges.

69. These (more nuanced) tariff designs are accepted internationally as best practice as they seeks to reduce the costs throughout the electricity system, to the benefit of all consumers.

Explainer – Capacity-based pricing

A household's 'use' of the distribution network is based on the size (or capacity) of its connection to the network rather than on the amount of electricity used. The size of a household's connection to the network is defined by the size of the fuse, which determines the amount of electricity that can be used at any one time. Households generally have sufficiently large fuses so that they can run a number of high-energy appliances simultaneously. However, for small, single occupancy households this may well be oversized.

It is important to understand the distinction between consumption and capacity, as these are not necessarily the same.

- A household's **consumption** is the amount of electricity used over a certain period.
- A household's **capacity** is the amount of electricity that can be used at one time.

Households that have very low consumption **may** be able to downsize their connection capacity without disrupting their supply and pay a lower fixed charge. Having very low annual consumption does not mean that a household doesn't require a high-capacity connection. A household may have a number of high-energy appliances that, although used very infrequently, if turned on simultaneously will outstrip the capacity and blow the fuse.

However, single occupancy households, which have been found to be hardest hit by the phase-out of the LFC, are most likely to be able to benefit from capacity-based pricing.

Distributors have reported that the LFC phase-out is incentivising households to consider whether their connection capacity is oversized. Some distributors have already introduced low-capacity plans and have moved qualifying households onto these plans, which have lower fixed charges. Other distributors have signalled their intent to introduce capacity-based pricing.

If households are interested in a low-capacity plan, they can check if their distributor offers this type of plan by looking at the distributor's price schedule, which is publicly available online. Households are also encouraged to check with an electrician to understand if downsizing their connection is suitable for their needs. Consumer awareness of such plans currently appears to be low.

Consumer groups raised concerns about increasing plan complexity

70. Retailers and the EA noted that the phase-out had resulted in new retail offers that were providing consumers with more choices, although they believe differentiation between plans will increase when the LFC requirements end. As discussed previously, Sense Partners' analysis also suggests that some retailers have begun to differentiate their plans by offering lower fixed charges than allowed under the phase-out.

71. However, several consumer groups warned that the increasing complexity of plans could make it harder for consumers to understand their choices and identify the plan best suited to them. For example, FinCap reported instances of consumers getting confused and switching to more expensive plans. Similarly, a survey by the Consumer Advocacy Council found that 24 per cent of consumers on bundled plans struggled to know if they were getting a good deal.

72. The feedback to this Review suggests that some households may need help to take advantage of new pricing innovations. The next section of this report discusses wider work underway to make it easier for consumers to know what plans will best suit their needs.

Some stakeholders proposed additional supports or alternative regulations

73. Several stakeholders proposed alternative interventions they believe the Government should consider to support low users or address energy affordability challenges more generally.

74. Two social retailers, Toast Electric and Grey Power, argued for regulation to centrally direct how prices are structured for low-income households. Grey Power, specifically argued that a targeted version of the LFC regulations should be retained, requiring low-fixed charges of 30 cents for low-income homes using under 7,200 kWh a year. Grey Power have kept fixed charges for their approximately 15,000 low use customers at 75 cents below the maximum allowed during the phase-out but above the original 30 cent limit they have proposed.

75. The Infrastructure Commission provided an alternative view, noting that broad tariffs regulations were an ineffective way to deliver assistance to people in need. Instead, Te Waihanga recommended that concerns about energy hardship should be addressed through non-price policies. Some examples of existing non-price supports are discussed in section 5.

76. The Consumer Advocacy Council, which formerly held a role to advocate for household electricity users, submitted to this Review just prior to its closure. It proposed strengthening requirements on retailers to financially support customers experiencing payment difficulties. The EA has been considering similar measures as part of their work to strengthening Consumer Care Obligations. On 3 December 2024 the EA announced two additional protections would come into force from January 2025, prohibiting retailers from disconnecting medically dependent customers for non-payment and requiring any fees or charges to be reasonable.[7] The remaining Consumer Care Obligations will also become mandatory obligations in the Electricity Industry Participation Code 2010 (Code) and take effect from April 2025.

77. Ecobulb, a company which delivers energy efficiency projects, warned that the phase-out was eroding incentives for households to invest in energy efficiency. They proposed that the Government create additional funds for household energy efficiency and require the sector to fund similar initiatives. Ecobulb has previously received grants from MBIE's Support for Energy Education in Communities (SEEC) programme. The SEEC programme will continue funding projects to help households become more energy-efficient. It and other government support are discussed further in next section.

[7] EA (December 2024) Electricity Authority publishes new consumer protections www.ea.govt.nz/news/press-release/electricity-authority-publishes-new-consumer-protections/

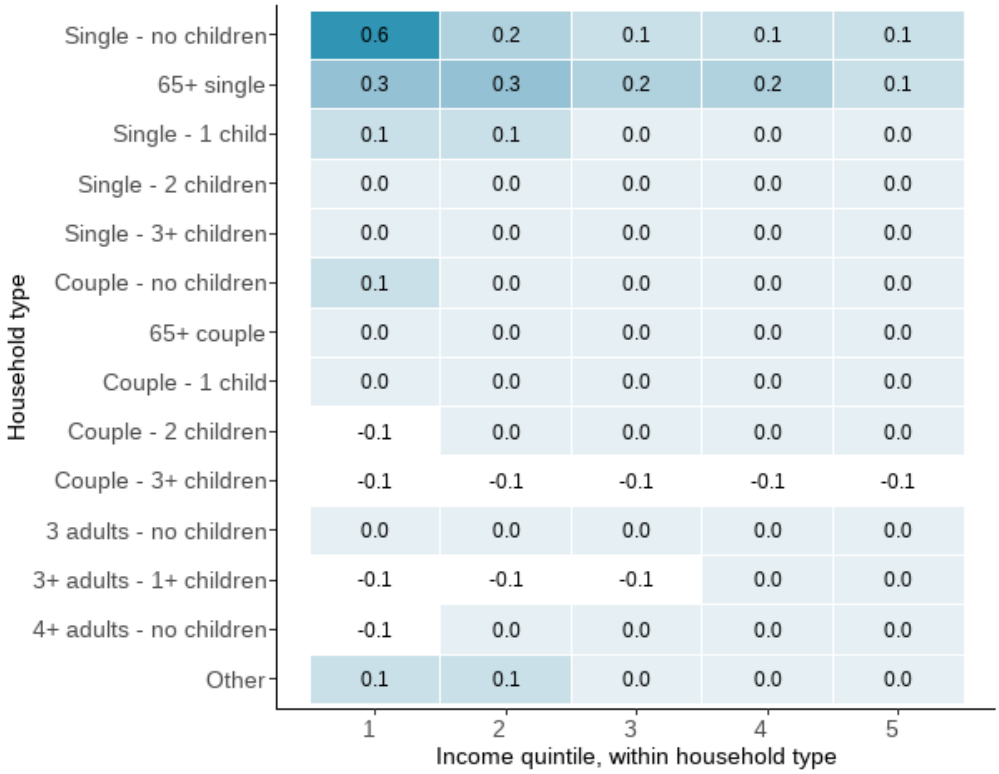
5. Options for additional support

Low-income or older people living alone are likely be most affected

79. As discussed in section 3, the Review has found there have been more winners than losers from the phase-out. However, as explained above, six per cent of lowest users' bills have risen more than general inflation and trends in disposable income.

80. Even among the most affected lowest users a minority of a household's finances are likely to be put under strain as a direct result of the phase-out, although it is difficult to determine the impacts with precision. The 2019 Electricity Price Review recognised that electricity use is a poor predictor of a household's risk of experiencing energy hardship. Sense Partners also found that low users made up 48 per cent of the highest two income quintiles, as well as 64 per cent of the bottom two quintiles. Their analysis suggests that, on average only single-occupancy households in the lowest income quintile, or single-person households where the occupant is aged over 65 years and in the lowest two income quintiles, will see their disposable income fall by more than 0.2 per cent as a result of the phase-out.

Figure 6: The direct expenditure effects of the phase-out, as a percentage of income



Source: Sense Partners (2024), Phase-out of the Low Fixed Charge regulations: Quantified price effects for the first 3 years
This figure shows the average increase in electricity bill in 2024 as a percentage of 2023 average disposable income by household type and income quintile.[8]

[8] Electricity is a smaller share of total expenditure for larger households. Therefore, the average savings they get from the phase-out are a smaller share of total household spending, despite being higher in dollar terms.

81. Income itself is only a proxy of households' access to resources. For example, while some superannuants may be more likely to have assets such as property that do not register as income, some will also have health conditions or debts that could strain their finances. At least some of the lowest users are at risk of energy hardship, although more granular data is not currently available to determine exactly how many.

The Power Credits Scheme can largely cover losses during the phase-out

82. In 2022, major electricity retailers and distributors funded a $5 million Power Credits Scheme to support low electricity-use households struggling to pay their power bills during the phase-out. Customers are eligible to receive a $110 power credit (up to two Power Credits ($220) in a 12-month period) from their electricity provider if they:

    a. are finding it difficult to pay their electricity bill

    b. have been on a low use electricity plan within the last six months

    c. have had a recent price rise.

83. The Electricity Retailers' Association of New Zealand (ERANZ) reported that, as of September 2024 approximately 20,000 Power Credits have been distributed so far, totalling $2.17 million. Although ERANZ do not have detailed data on the demographics or income-levels of recipients, the percentage of Power Credits distributed in each region has been broadly correlated with the percentage of low-income households in that area.

84. The $110 Power Credits should have been sufficient to completely cover the cost of phase-out for almost all low electricity users to date. Sense Partners analysis suggests that only 1.04 per cent of consumers (those using less than 3000 kWh a year) have seen their bills rise by more than $110 on average due to the phase-out.

85. The Power Credits Scheme is due to run until the end of the phase-out. From 2027 low users, including the 6 per cent of lowest users who would have otherwise seen real terms increases in their bills, will no longer be able to access this support.

Other support is available for households struggling with electricity bills

86. There are several government support programmes, summarised below, which will remain available to help households struggling with power bills when the Power Credits Scheme ends.

The Winter Energy Payment

87. The Winter Energy Payment is an extra automatic payment to support consumers to pay their winter energy costs from May to October every year. Consumers are eligible if they receive a main benefit, pension, or jobseeker support. Payment rates differ between single people with no dependent children ($20.46 per week) and couples or people with dependent children ($31.82 per week).

Support for Energy Education in Communities (SEEC) programme

88. SEEC is an initiative to support consumers experiencing energy hardship in achieving warmer, healthier, and more energy-efficient homes and lowering their energy bills. The aim of the SEEC programme is to expand the capacity of existing energy hardship initiatives in New Zealand communities by funding energy hardship projects delivered by community-based groups, businesses, and organisations. Projects that are granted funding prepare and deliver education material, provide personalised advice, resources and devices to households, and train community-level energy advisors. Since 2021, more than 28,000 households have been supported through the SEEC programme.

Warmer Kiwi Homes

89. Warmer Kiwi Homes provides payment that covers up to 90 per cent of the costs to purchase and install insulation and an efficient heater, to help consumers save money on their power bills. Eligible households for this payment are homeowners that live in a home built before 2008; have a community services card or live in an area identified as low-income; and do not have ceiling or underfloor insulation, or an efficient heater. Warmer Kiwi Homes has installed more than 450,000 heaters and insulation to date.

Healthy Homes Initiative

90. The Healthy Homes Initiative aims to increase the number of households living in warm, dry, and healthy homes, to enhance health and wellbeing, and reduce the number of housing-related hospitalisations. The Healthy Homes Initiative contracts providers who work with eligible households, government agencies, and local partners to provide education and access to interventions for consumers. Some interventions given to households include accessing insulation, heating sources, minor repairs, ventilation, and support with power bills. Targeted consumers for this initiative include low-income families with children aged between 0 and 5 who have been hospitalised with a specified housing related condition; families that are receiving a benefit; pregnant people; and individuals at risk of rheumatic fever or who have rheumatic fever. Through the Healthy Homes Initiative, more than 147,900 interventions have been received.

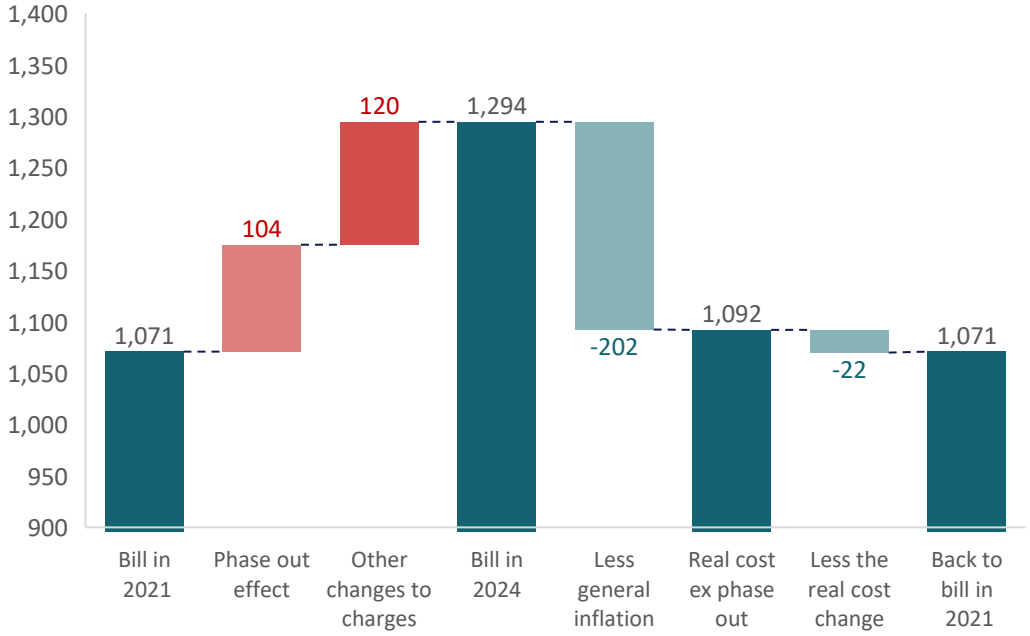
Work is also underway to reduce electricity costs more generally

91. Wider increases in electricity costs have had a significantly larger impacts on household bills, even among those most impacted by the phase-out. For example, as figure 7 shows, Sense Partners estimate that:

    a. A very low user (between 3000 and 4000 kWh a year) would have seen their bill rise by $104 due to the phase-out (in nominal terms), while wider increases in wholesale, network and metering costs would have added approximately $120 to their bill since 2021.

    b. Only 1.04 per cent of households are estimated to have seen their bill rise more than this group because of the phase-out, while most if not all consumers will have seen their bills increase due to the wider electricity cost pressures.

Figure 7: Estimated cost increases for a low electricity user



Source: Sense Partners (2024), Phase-out of the Low Fixed Charge regulations: Quantified price effects for the first 3 years. This figure illustrates the annual bill, evaluated at the mean consumption above 3,000 kWh but below 4,000 kWh.

92. MBIE and electricity regulators have several key work programmes underway to reduce electricity costs and empower consumers to navigate the market.

Consumer Data Right for electricity

93. One of the most effective ways households can reduce their power bills is by finding and switching to the retail plan that is best suited to them. In July 2024 Consumer NZ estimated that switching through Powerswitch saved households on average $524 a year.

94. However, there are concerns that it may be too difficult for consumers to identify the best plan for their needs. Several consumer groups suggest this could become an increasing problem as plans become more complex, with prices that vary depending on how and when electricity is being used. These more innovative plans should help create new ways for households to save and reduce overall costs for all consumers, by helping to limit the additional investment needed to cover future peaks in demand. However, as stakeholders highlighted to the Review, some plans can also increase bills if they do not match the way a household is willing or able to consume energy.

95. MBIE is currently exploring designating a consumer data right (CDR) for the electricity sector under the Customer and Product Data Bill to enable households to take advantage of the innovations that are expected to become available when the LFC regulations are lifted. A potential CDR would ensure households can access data about their electricity usage and approve third parties to use it on their behalf. As a result, it should become considerably simpler for households to use comparison websites or other services to pinpoint which plans best suit their patterns of usage, secure personalised budgeting advice, and switch seamlessly.

Electricity Authority's consumer protections work programmes

96. The EA also has work programmes underway to empower consumers to take full advantage of the energy market.

97. In 2021, just before the phase-out began, the EA introduced new Consumer Care Guidelines to encourage power companies to improve the level of service they were providing to their customers. Having monitored retailer alignment with the Guidelines the EA concluded that making the Guidelines mandatory was needed to enhance consumer protections. The EA are now amending the Electricity Industry Participation Code 2010 to introduce the Consumer Care Obligations (Obligations). The Obligations are minimum standards that all retailers must comply with – and provide annual compliance reports to the EA on – if they sell electricity to residential consumers. The COOs will take effect from 1 April 2025, except the following two obligations which apply from 1 January 2025:

    a. Prohibiting retailers from disconnecting post-pay customers where a medically dependent consumer is known to be residing at that premises. If such a disconnection occurs, the retailer must notify the EA immediately.

    b. Requiring any fees charged by a retailer to be reasonable and reflective of actual costs.

98. The EA recently consulted on several options to improve the comparison and switching tools available to households. They will continue to support and improve a comparison and switching website service for consumers (currently Powerswitch), by mandating retailer participation, standardising bill information, and enhancing access to usage data in line with the CDR. They also exploring broadening support beyond the website service by making community advisors available to support vulnerable consumers who struggle to switch and requiring retailers to regularly Review and advise consumers of the most cost-effective and appropriate plan for their household.

99. The EA has also begun to enhance their monitoring of retail data to ensure they can identify issues with the retail market and potential risks to consumers.

Energy Competition Task Force

100. The EA and Commission recently setup an Energy Competition Task Force, with MBIE as an observer, to investigate ways to improve the performance of the electricity market in the short- to medium-term. It's Package One workstreams are considering measures to enable more new generators and independent retailers to enter and compete in the market, to put downward pressure on wholesale and retail prices. As figure 7 above illustrated, wholesale electricity costs have been the biggest driver of price increases since the phase-out began.

101. The Task Force's Package Two workstreams focus on providing more options to electricity users (including households) to lower their costs and rewards their contributions to the power system. This includes measures to ensure more innovative plans are available, like those with time-of-use pricing, to help households take advantage of new ways to save, for example by shifting their usage to cheaper times of day. As previously discussed, there are concerns that LFC regulations may limit plan innovations and discourage the uptake of new electric products, like smart-charging EVs, that can be managed more flexibly.

6. Conclusions and recommendations

The phase-out of the LFC regulations is achieving its intended aims, so should continue

102. This Review has found that the phase-out is delivering the benefits expected from it. More New Zealander's bills have been reduced than increased by the fall in cross-subsidies imposed by the LFC regulations.

103. The analysis also shows that increases in electricity costs, caused by factors beyond the LFC, are having a significant impact on household bills. Even among very low users who are most affected by the phase-out, other electricity cost increases have typically had a bigger impact on their bills.

104. As a result, it is important that regulatory settings prioritise opportunities to make wholesale and network prices more efficient and ensure households can take advantage of newer and more substantial means of reducing their bills. Removing the LFC should assist several programmes of work to drive down these wider costs.

It will continue to be important to help households navigate the deals available to them

105. There is evidence to suggest that lower users will continue to be able to find competitive plans that suit their needs, as some retailers have begun to differentiate themselves by offering fixed rates below the limits allowed by the phase-out. The lowest users may also benefit from taking steps to right-size their power connections to reduce their fixed costs.

106. Consumer groups have made convincing arguments that the increasing complexity of pricing tariffs – which is a desirable outcome from the phase-out – could make plan choices more confusing. It is critical that households are supported to identify the pricing plans that are best suited to the ways they use electricity. While time-of-use and other innovative pricing approaches will provide new ways for households to make significant savings on their bills, they could also increase some bills if a consumer is unable to respond to their price signals.

107. MBIE and the EA already have work underway to ensure that services, like comparison and switching websites, are able to give much more personalised information about the plans that best suit households usage patterns. This work will be critical for ensuring households are empowered to take advantage of innovative deals that should be more available once the phase-out is complete.

Low-income, low use households should be assisted through targeted support, rather than broad price regulations

108. Although most consumers will benefit from the phase-out, a small minority (six per cent) with the lowest usage, are likely to experience real increases in their bills from 2027 when the industry-run Power Credits Scheme ends. Single-occupancy households in the lowest income quintile, or single-person households where the occupant is over age 65 and in the lowest two income quintiles, are more likely to see their disposable income fall as a result of the phase-out (by 0.3 to 0.6 per cent).

109. Targeted initiatives, like the support already available from Government, should be used to assist low users at increased risk of energy hardship, rather than broad pricing regulations. As discussed throughout the Review, retail pricing regulations have several additional knock-on consequences to other consumers (including vulnerable higher using households) and policy priorities (such as electrification). As the EA and the Commission noted, broad regulations like the LFC could prohibit work to make the electricity system more flexible and efficient. That work will be critical to reducing wider electricity costs, which have presented a greater threat to households (including low and high using households at risk of energy hardship) than changes to the LFC.

Regulators should continue monitoring for signs of pricing innovations

110. As expected, there is only initial evidence available of new pricing innovations and cost-reflective plans being rolled out during the phase-out.

111. However, retailers and distributors have committed (in statements provided to this Review) that they will introduce more innovative pricing plans that will benefit households and avert costly infrastructure investments when the LFC requirements are removed. The Government and regulators should continue monitoring for additional evidence of new flexibility products and averted network investments in future.