

The Electricity Price Review
Secretariat, Ministry of Business, Innovations and Employment
15 Stout Street
PO Box 1473
Wellington 6140
By email: energymarkets@mbie.govt.nz

14 November 2018

Dear Sir/ Madam

Electricity Price Review Submission

Thank you for the opportunity to submit on the Electricity Price Review.

Simply Group either fully or partial owns

- Simply Energy – an electricity retailer focusing on commercial and industrial consumers, independent generators and provision of white label retailing services
- Tenco – that operates ~ 250 private electricity, gas and water networks across New Zealand
- Axos Systems – the provides time of use meter data management and billing systems used by local network companies and retailers across the country
- Ampli – a data analytics business that helps network companies get value out of advanced meter consumption and event data.

Simply Group employs ~ 35 people and has actively participated in electricity market over the last 12 years. Within the group we invoice over 75,000 utility connection points each month, have provided white label services ~ 10 new entrant electricity retailers and have implemented numerous structured supply arrangements including supply and invoicing of the international airlines at Auckland and Christchurch airports and direct sales of electricity from independent generators to end consumers. We have actively contributed to the development of industry regulation including the overhaul of the onerous network and electricity prudential regulations. This history shows an active contribution to the vibrancy of the market today and we see that we have a larger role to play promoting innovation and disruption over the coming decade.

From our perspective and experience we think there is a lot right with the NZ Electricity Market. Barriers to starting up a new retailer are low, we have an operating hedge market that can be accessed by parties outside of the big five generator-retailers, embedded generators have access to regulated dispute processes that are economically viable to pursue, prudential security requirements are manageable and switching is easy,

There is of course still much to be done. Retailers and networks are still learning how to make better use of advance meter data, the standards for access to and exchange of information are poor and often not adhered to, switch win-backs and lack of depth and liquidity in the hedge market undermining retail competition. There is a lack of competitive

pressure on local networks to consider alternative asset investment and operational approaches to running their networks. It is also very important not to forget the large number of New Zealanders that are vulnerable and need help to keep their electricity connected.

We are very optimistic and excited about the future of the NZ Electricity Market. We see a future where there are 100s of new retailers, each focused on a set of customers where they can provide more value than just electricity supply. Networks that can use the rich data sets from advanced meters to respond faster to outages and storm events and make better decisions on both what to invest in and when to make an investment. We see an opportunity for housing and social welfare agencies to work with the electricity industry lower energy costs and improve outcomes for vulnerable New Zealanders with a positive economic benefit to the country.

We have responded to questions posed in the Electricity Price Review through the lens of supporting a better future for NZ and where we think we have a perspective that can contribute. We know that it is very easy to focus on negatives – but think it is important not to lose sight of the good work that has been done over the past 10 years that has contributed to NZ being considered a world leader in terms of renewability, reliability and accessibility to electricity.

We would appreciate the opportunity to talk to you about the solutions we have proposed especially in respect of addressing the issue of affordability.

Yours Sincerely
Stephen Peterson



Director of Innovation and Growth
Simply Group



ELECTRICITY PRICE REVIEW

SUBMISSION FORM

How to have your say

We are seeking submissions from the public and industry on our first report into the state of the electricity sector. The report contains a series of questions, which are listed in this form in the order in which they appear. You are free to answer some or all of them.

Where possible, please include evidence (such as facts, figures or relevant examples) to support your views. Please be sure to focus on the question asked and keep each answer short. There are also boxes for you to summarise your key points on Parts three, four and five of the report – we will use these when publishing a summary of responses. There are also boxes to briefly set out potential solutions to issues and concerns raised in the report, and one box at the end for you to include additional information not covered by the other questions.

We would prefer if you completed this form electronically. (The answer boxes will expand as you write.) You can print the form and write your responses. (In that case, expand the boxes before printing. If you still run out of room, continue your responses on an attached piece of paper, but be sure to label it so we know which question it relates to.)

We may contact you if we need to clarify any aspect of your submission.

Email your submission to energymarkets@mbie.govt.nz or post it to:

Electricity Price Review

Secretariat, Ministry of Business, Innovation and Employment

15 Stout Street

PO Box 1473

Wellington 6140

Contact details

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Use of information

We will use your feedback to help us prepare a report to the Government. This second report will recommend improvements to the structure and conduct of the sector, including to the regulatory framework.

We will publish all submissions in PDF form on the website of the Ministry of Business, Innovation and Employment (MBIE), except any material you identify as confidential or that we consider may be defamatory. By making a submission, we consider you have agreed to publication of your submission unless you clearly specify otherwise.

Release of information

Please indicate on the front of your submission whether it contains confidential information and mark the text accordingly. If your submission includes confidential information, please send us a separate public version of the submission.

Please be aware that all information in submissions is subject to the Official Information Act 1982. If we receive an official information request to release confidential parts of a submission, we will contact the submitter when responding to the request.

Private information

The Privacy Act 1993 establishes certain principles regarding the collection, use and disclosure of information about individuals by various agencies, including MBIE. Any personal information in your submission will be used solely to help develop policy advice for this review. Please clearly indicate in your submission whether you want your name to be excluded from any summary of submissions we may publish.

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Summary of questions

Part three: Consumers and prices

Consumer interests

1. *What are your views on the assessment of consumers' priorities?*

2. *What are your views on whether consumers have an effective voice in the electricity sector?*

3. *What are your views on whether consumers trust the electricity sector to look after their interests?*

Prices

4. *What are your views on the assessment of the make-up of recent price changes?*

We think the analysis of price changes needs further work.

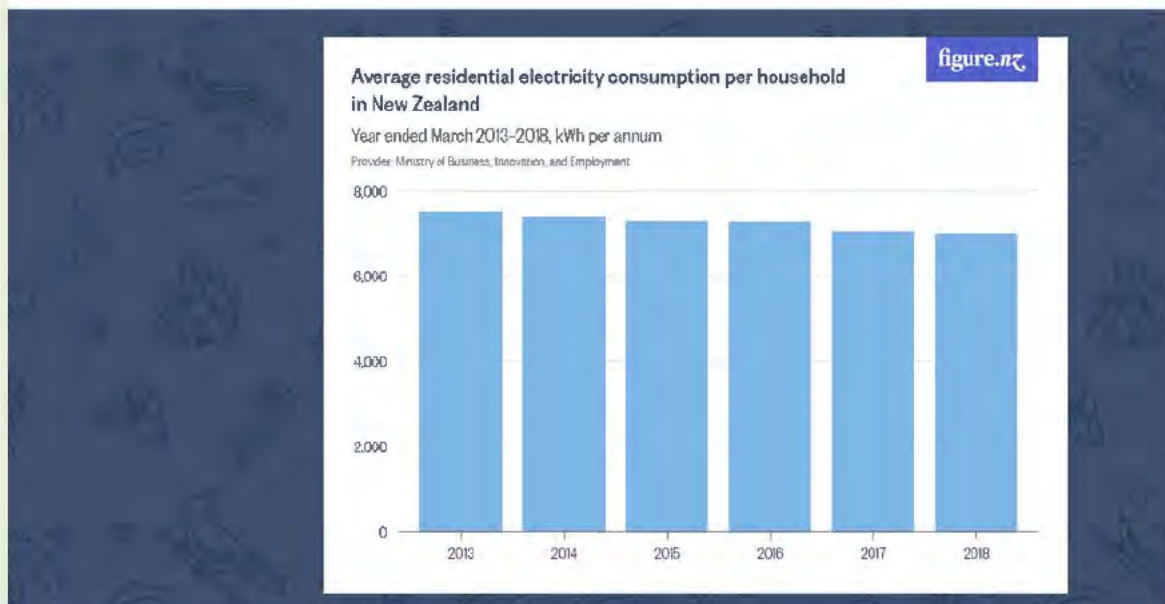
- The analysis of pricing does not take into consideration the capital contribution often made by commercial and industrial consumers towards connection costs – where they effectively prepay network charges. As such it understates the amount paid by these commercial and industrial consumers for network services.
- The Low Fixed Daily Charge regulations came into effect in 2004. This had the impact of forcing retailers to offer tariffs that didn't mirror the underlying cost structure to supply electricity and therefore to take on more risk. Ultimately this risk pushed up retail costs and will have contributed to retail price increase seen from 2005 onwards.
- Residential consumers use relatively small volumes of energy. Energy consumption per household has been declining (see following figure showing a decline in energy consumption between 2013 and 2018). A decline in consumption with no change in a tariff will lead to a price rise because residential prices include fixed charges.

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We don't have consumption figures going back to 2004 the following figure illustrates how reduced consumption will lead to an increase in the average price of energy before any change in the tariff offered.

Example impact of kWh saving impacting average Pricing

		Lower energy		
		Base case	consumption	Difference
kWh per year		8,000	7,000	(1,000)
Daily Price	\$	1.000	\$ 1.000	-
Variable Price	\$	0.224	\$ 0.224	-
Daily Charge	\$	365	\$ 365	-
Variable Charge	\$	1,795	\$ 1,571	(224)
Total Charge	\$	2,160	\$ 1,936	(224)
Average Price	\$	0.270	\$ 0.277	0.007
Apparent Price Increase				2.4%

5. *What are your views on the assessment of how electricity prices compare internationally?*

6. *What are your views on the outlook for electricity prices?*

Affordability

7. *What are your views on the assessment of the size of the affordability problem?*

- It isn't clear what is considered the boundary of the affordability problem. We assume you mean (and agree with) all households that can't afford to maintain a healthy home which result in serious consequences including reducing heating that result in unacceptable living conditions and significant health costs and that may scrimp on food, transport and clothing to pay their power bill.
- We think it would be useful to quantify the second order impacts of energy hardship. For example, what are the cost of doctor visits, missed school attendance, poor academic performance from insufficient food, etc. This information would help quantify the benefits of addressing affordability vs the costs of any intervention.
- It would be useful to understand how interventions or programmes could be targeted to reach those most impacted. For example we might find that a large proportion of the 103,000 households impacted by an affordability problems are also clients of Housing NZ (64,000 units) or Council housing services.



Managed Housing New Zealand Properties by Number of Bedrooms
30 June 2018

Housing New Zealand
Housing the Zealand Corporation

	Number of bedrooms						Total
	Bedsit*	1	2	3	4	5+	
State Rentals	392	5,229	23,830	24,739	6,149	1,522	61,861
Community Group Housing ¹	1	281	390	146	200	474	1,492
Emergency/Transitional Housing ²	348	61	103	91	25	15	643
Total	741	5,571	24,323	24,976	6,374	2,011	63,996

8. *What are your views of the assessment of the causes of the affordability problem?*

9. *What are your views of the assessment of the outlook for the affordability problem?*

We think the affordability problem has many dimensions and contributing factors.

The electricity industry has an important role to play in addressing this problem, but not the only role. Working together with social welfare and housing agencies we think there is an immediate opportunity to materially reduce the affordability problem and improve the lives of vulnerable New Zealanders.

We suspect that this can be achieved with a net positive economic benefit to New Zealand.

Summary of feedback on Part three

10 Please summarise your key points on Part three.

Solutions to issues and concerns raised in Part three

11 Please briefly describe any potential solutions to the issues and concerns raised in Part three.

9(2)(b)

[Redacted content]

Part four: Industry

Generation

12 *What are your views on the assessment of generation sector performance?*

13 *What are your views on the assessment of barriers to competition in the generation sector?*

We work with generators up to from 1kW to 10MW in capacity that are typically embedded within local networks. These generators will be increasingly important as NZ attempts to transition to a carbon neutral economy to provide new sources of generation that are geographically diversified and

Smaller generators require predictable, standardized and low transaction cost connection processes to support economic deployment of generation and storage. However we have seen:

- Arbitrary connection standards imposed by local networks e.g. a local network that has refused connection of solar and batteries if the battery could be charged from the grid. This not only undermines the economic case for solar-battery projects but represents uneven handed treatment of third parties that can provide load management services to that network.
- Post construction a local network modifying technical connection standards and imposing new line charges on a generation project. These charges have been disputed through Part 6 of the Code but the process has taken many years and has undermined confidence in undertaking further projects.
- The resource consent requirements for new projects is very unpredictable and increasingly costly.

A barrier to growth in small scale generation and storage projects in New Zealand we need access to fast, cost effective, standardized and informed dispute resolution services in respect of resource consenting and connections into local networks.

14 *What are your views on whether current arrangements will ensure sufficient new generation to meet demand?*

We support using contract markets to support the development of sufficient generation to meet capacity requirements.

To the extent that a Government is concerned that there is insufficient generation capacity in the electricity market they could become a regular purchaser of cap products that could provide cash flow certainty to developers (that would sell the caps) who could develop, commission and maintain plant to meet capacity and hydro shortfalls.

Retailing

15 *What are your views on the assessment of retail sector performance?*

16 *What are your views on the assessment of barriers to competition in retailing?*

In our experience we see win-backs as a problem. They increase the cost to acquire for new entrant retailers and undermine the incentive on incumbents to provide competitive pricing to their existing customer base.

We strongly support the introduction of an industry code that addresses this problem, for example, as per the experience in the telecoms industry.

Vertical integration

17 *What are your views on the assessment of vertical integration and the contract market?*

We concur that well-functioning contract market underpins a competitive electricity market which our retail electricity business depends on.

We don't believe the hedge market is functioning well enough to support a vibrant electricity market. Our observations include

- The current stress in the spot market is resulting in extremely wide bid-offer spreads (c/f figure 19 Spread between contract buy and sell prices), anecdotally \$100 per MWh, on monthly baseload contracts. The increase in spread during periods of physical market stress undermines confidence, participation and liquidity in the contract market.
- We have seen a major generator-retailer offer variable-volume supply tariff at an equivalent price as the fixed-volume contract market (and we are happy to share our analysis with you that demonstrates this). The observed pricing meant that there was zero margin to meet the retail cost-to-serve, risk premium or net profit.
- Anecdotally we hear many complaints that the contract market prices are higher than tariffs for physical supply making it impossible for retailers that sources hedges from the contract market to compete with a vertically integrated retailer.

We note that some market makers complain that they lose money because of their market-making requirements. We are skeptical and contend that this is likely a function of internally set risk management policies that force traders to immediately close out a position rather than holding a trade for a short amount of time so that it can be sold when the bid-offer spread can be captured.

18 *What are your views on the assessment of generators' and retailers' profits?*

Transmission

19 *What are your views on the process, timing and fairness aspects of the transmission pricing methodology?*

We think that the Electricity Authority resources could be put to higher value uses than the work that has been done and continues to be done on the transmission pricing methodology. We think it would be instructive to review the benefits achieved and costs incurred from the recent work on Avoided Cost of Transmission (closely related to the transmission pricing methodology) vs the predicted benefits and costs, and also a comparison with the benefits of other projects.

Distribution

20 *What are your views on the assessment of distributors' profits?*

21 What are your views on the assessment of barriers to greater efficiency for distributors?

If distributors are not able to get access to meter data at ICP and hhr granularity they could miss the opportunities to right size investments to meet network growth, miss opportunities to move to performance (rather than time) based maintenance and replacement regimes and be less able to effectively respond to events e.g. storms, as illustrated by the effective response Counties Power was able to deliver using its meter data and the INDI platform.

This means we strongly support the provision of meter data to networks on a reasonable commercial basis. In addition, we think

- Retailer concerns on privacy, competition and potential liability do need to be considered and could reasonably be addressed by using a trusted third party (like Ampli Ltd) to provide data anonymization services and standardized delivery of data.
- That metering data should also be available to the Regulator to support more fine grained monitoring of quality and outage standards and to test asset investment decisions
- That metering data be made available to Stats NZ and other agencies to support development of better evidenced based policy.

22 What are your views on the assessment of the allocation of distribution costs?

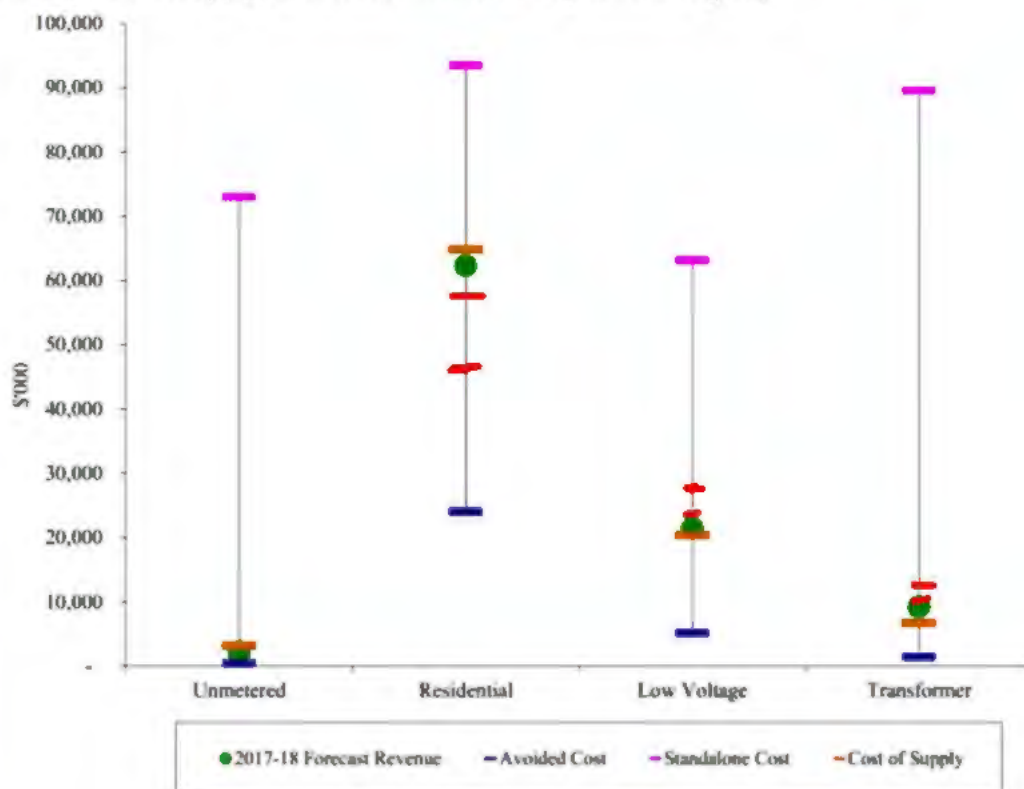
While your analysis (in the technical report) shows that residential connections are generally more than the average of the mid-point between incremental and standalone costs your analysis excludes network operations and maintenance costs that make up the cost to supply. This means that the mid-point is not the economic benchmark against which network cost allocation should be considered.

Intuitively it makes sense that residential customers cost more to service per GWh than business customers. This is because residential connections are geographically spread out and have lower energy intensity than businesses.

This point is supported by Appendix A of Wellington Electricity's analysis which shows that once cost of supply is considered that residential connections are paying marginally less than their cost to supply while businesses are paying marginally more.

Appendix A: Wellington Electricity's incremental versus stand-alone analysis

Figure 6: Wellington Electricity's comparison of avoided costs, stand-alone costs, costs of supply, and forecasted revenue by consumer group



Source: Wellington Electricity Lines Limited, 2017/18 Pricing Methodology Disclosure, figure 2.

We have added red lines to Wellington Electricity's figure to show the proposed impact of cost reallocations and note that there would be a non-economic and material shortfall in residential cost recovery.

We note that networks are expected to follow pricing principals (<https://www.ea.govt.nz/operations/distribution/pricing/>) that are designed to gather revenue in proportion to underlying costs. We think it is unlikely that there would be a systematic error in the detailed application of these principals across all networks and assert that it is more likely that the high level model does not account for the appropriate cost considerations.

23 *What are your views on the assessment of challenges facing electricity distribution?*

Summary of feedback on Part four

24 *Please summarise your key points on Part four.*

Solutions to issues and concerns raised in Part four

25 Please briefly describe any potential solutions to the issues and concerns raised in Part four.

Meter data

To facilitate access to meter data for the broader benefit of NZ we suggest tasking the Commerce Commission with facilitating the establishment of (an) independent third party that can create data flow between retailers, networks, regulators and policy makers while addressing legitimate privacy, competition and liability concerns.

Vertical Integration and Hedge Contract Markets

We think the contract market has become less effective over the last two years and that interventions to improve its function are likely to be justified. We would like to see consideration of:

- Enhancing transparency of the OTC and tariff pricing relative to the hedge market by enhancing the existing hedge disclosure system to include the equivalent price implied by the hedge market. This would create transparency into systematic cross-subsidization between a wholesale and retail business unit within a vertically integrated business that could be then be further investigated by regulators.
- A requirement on the the large generators to sell a minimum percentage of their generation through the ASX contract market over a period of at least three years into the future where the percentage would ramp up if key performance indicators on liquidity, price discovery (see prior point) and long-term price volatility were not met.
- That generators could trade their market making obligations to other parties so that the lowest cost generators would make the market and an empirical benchmark could be established for the cost of market making.

If these measures don't work, then we would suggest addressing the underlying problem of vertical integration directly through corporate separation of generation and retail business units.

Allocation of Distribution Costs

We don't believe that price review has identified that there is a problem with the allocation in distribution prices.

We are concerned that the analysis as it stands could lead to interventions and outcomes that are non-economic and have un-intended consequences like we have seen with the Low Fixed Daily Charge regulations.

If the problem is affordability we believe this can be addressed in a targeted and rapid manner as outlined earlier in our submission which we assert would be much lower cost than forcing networks to reallocate distribution costs from business to residential consumers.

Note that changing network prices takes years and risks undermining the considerable work that has been done by networks, retailers and the Electricity Authority to bring in more cost reflective network charges that will support the economic deployment of new technology across our grids to meet growing and more volatile demand.

Part five: Technology and regulation

Technology

26 *What are your views on the assessment of the impact of technology on consumers and the electricity industry?*

We think

- that consumers will be able to respond much more effectively to price signals
- that the majority of electricity will be delivered to consumers via non-traditional retailers using white label retailing platforms as an add on to an existing product or service

27 *What are your views on the assessment of the impact of technology on pricing mechanisms and the fairness of prices?*

We think

- prices should be set to reflect costs, so they can be bundled by retailers or aggregators into products that customers want and
- fairness addressed through targeted interventions to support vulnerable customers.

28 *What are your views on how emerging technology will affect security of supply, resilience and prices?*

Regulation

29 *What are your views on the assessment of the place of environmental sustainability and fairness in the regulatory system?*

30 *What are your views on the assessment of low fixed charge tariff regulations?*

We agree with the assessment of the low fixed charge regulations.

We note that these regulations add cost and complexity to new retailers who are put off entering into the market for residential supply.

31 *What are your views on the assessment of gaps or overlaps between the regulators?*

32 *What are your views on the assessment of whether the regulatory framework and regulators' workplans enable new technologies and business models to emerge?*

33 *What are your views on the assessment of other matters for the regulatory framework?*

Summary of feedback on Part five

34 *Please summarise your key points on Part five.*

Solutions to issues and concerns raised in Part five

35 *Please briefly describe any potential solutions to the issues and concerns raised in Part five.*

Additional information

36 *Please briefly provide any additional information or comment you would like to include in your submission.*