



**Domestic Energy
Users' Network**

Grey Power
NEW ZEALAND FEDERATION INCORPORATED



**SUBMISSION TO THE SELECT COMMITTEE ON THE ELECTRICITY
INDUSTRY BILL 2009.**

BY

**GREY POWER FEDERATION IN ASSOCIATION WITH THE
DOMESTIC ENERGY USERS' NETWORK**

This submission is supported by:

The Royal New Zealand Returned and Services Association

Age Concern New Zealand

Rural Women New Zealand

Public Health Association of NZ

Child Poverty Action Group

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Summary

1. **The Electricity Industry Bill would return electricity regulation to the pure-competition model of the mid 1980s. It is portrayed as being a benefit to consumers, making the regulator more independent of Government, and improving supply security. These claims are all misleading or simply incorrect.**
2. **Domestic consumers will not be represented on the regulatory authority. Any compensation for shortages would not exceed a tenth the profits gained.**
3. **Electricity regulation will not be independent of Government. Forecasting and planning to support investment (now the Statement of Opportunities) would be done by MED officials. The Minister will unilaterally decide the most contentious issues if they have not been resolved within a year.**
4. **Supply security will be reduced by the Waitaki asset swap, and scarcity is profitable to gentailers because of the market pricing structure.**
5. **The balancing principles, "fair" and "environmentally sustainable", introduced after the 2000 Ministerial Inquiry, were never implemented. The Bill will remove these principles, leading to higher prices and higher asset values, and making privatisation attractive.**
6. **The Bill proposes an asset swap to promote competition. This will increase costs of supply and reduce security. The Bill fails to address the conflict between Government's interests as owner of profitable electricity assets, and its interests in long-term consumer benefit.**
7. **The competitive deregulated electricity market has failed domestic and other small consumers. An independent regulator should control the market, with full representation of domestic consumers on the regulatory body. Retail should be split from generation, to reduce opportunity to abuse market power.**

We submit that Parliament should:

8. **Amend the Commerce Act to restore the concept of "essential service", so that electricity supply is cost-minimising not profit-maximising.**
9. **Modify the Statements of Corporate Intent of the State-Owned Enterprises to require cost minimising not profit maximising.**
10. **Retain the objectives "fair" and "environmentally sustainable" in electricity and gas legislation, to put a focus on effective resource utilisation for the long-term benefits of all New Zealanders**
11. **Regulate gentailers under Part IV of the Commerce Act, and begin the groundwork needed to separate generation from retail businesses.**
12. **Meanwhile, progressively improve the existing regime for consumer and national benefit, instead of forcing a pure competitive market.**

The Bill would return NZ to a pure-competition model for electricity

13. The Bill's proposals would return electricity regulation to the pure-competition model of the mid 1980s. It would remove the objectives "fair" and "environmentally sustainable" from the objectives of electricity regulation (Clause 17), leaving them for politicians to decide.
14. These extreme market-based policies have in fact been in action since reforms began in the 1980s. The balancing principles were introduced after the 2000 Ministerial Inquiry,¹ but completely ignored. The new Bill would only confirm in law what is happening now.
15. Peter Rutledge (Grey Power) and Molly Melhuish (DEUN) are members of Advisory Groups of the Commission. They have been told, every time they raised matters relating to "fair" or "sustainable", that those matters are "out of scope". The Decision that authorised the Electricity Commission² stated that Government would require compulsory compliance with rules where needed to give effect to government policy. This has happened rarely if ever.
16. Many legal decisions confirm that the Commerce Act 1986 removed the concept of "essential service" from New Zealand law, and replaced it by a "broad legislative landscape" based on economic principles.³ These principles are allowing monopolies to extract all possible monopoly rents. This led, after a decade of litigation, to a change in the Commerce Act to allow threshold price regulation of network monopolies. Even threshold regulation took another decade to be implemented – and only the worst offenders, Vector and Powerco, were actually regulated.⁴

Misleading portrayal of Bill's position on key issues

17. The Bill is portrayed as being good for consumers, as making regulation independent of Government, and as increasing security of supply.⁵ Each of these claims is misleading or simply incorrect.

No benefits to consumers

¹ <http://www.comcom.govt.nz//BusinessCompetition/Anti-competitivePractices/Applications/ContentFiles/Documents/EGBL%20Final%20determination.pdf> , section 57

² [ibid](#), section 59

³ www.victoria.ac.nz/law/documentation/.../21%20White%20-%20edited.pdf also

<http://www.comcom.govt.nz//MediaCentre/Speeches/ContentFiles/Documents/Utility%20Regulation%20in%20NZ%20-%20Dr%20A%20E%20Bollard.PDF>

⁴ <http://www.comcom.govt.nz//IndustryRegulation/Gas/CommissionReportsandDocuments/ContentFiles/Documents/%5BPUBLIC%5D%20Gas%20Authorisation%20-%20Decisions%20Paper%20-%2031%20October%202008.pdf>

⁵ <http://beehive.govt.nz/release/energy+sector+transformation+benefit+consumers>

18. The proposed return to uncontrolled competition will entrench the market pricing methodology that has caused domestic consumer prices to rise at least twice as fast as prices to large consumers.⁶ Ramsey pricing charges the most captive consumers the highest prices: it is condoned by the Commerce Commission⁷. The Electricity Commission supports the principle of Ramsey pricing, though saying it is difficult to implement⁸.
19. Retail consumers are excluded from the activities of the new Energy Authority (clauses 7, 9(1 and 2)). This means that the objective of the Authority, which includes “long term benefit of consumers” (clause 17), will be interpreted within a structure that has no domestic consumer representatives.
20. Compensation of consumers in the event of hydro shortages, provided for in Clause 45 (2) (a), would cost companies no more than \$128 million. This estimate assumes \$10/week paid to each of 1.6 million connected customers during a very long, 2-month, hydro shortage. This compares to \$4.3 billion excess profits taken by companies in three hydro shortages, as calculated by Professor Wolak⁹ – or \$1.4 billion per shortage – more than 10 times the cost of the proposed compensation. Any costs of one year’s compensation will be passed on to consumers subsequently.

Regulation involves Ministers closely

21. The Bill is portrayed as making the regulator more independent of Government. However Clause 45 has a list of contentious issues on which industry participant hold strongly divergent views. Any that the Authority cannot resolve within a year can be decided by the Minister Clause 46(2), after consultation procedures with significant loopholes (Clause 43).
22. Even more important is that forecasting and analysis to support investment planning (at present called the “Statement of Opportunities”) is removed from the regulator, and given back to Government officials (clause 126 (3) (g)).
23. Transmission investment will be regulated by the Commerce Commission (clause 148). Though formally independent of Government, the Commerce Commission will presumably only be able to rubber-stamp grid upgrade

⁶ <http://www.issues.co.nz/fairelectricity/The+truth+about+electricity+pricing> click on the underlined words “twice as fast”

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<http://www.comcom.govt.nz//IndustryRegulation/Electricity/PriceQualityPaths/ContentFiles/Documents/IM-final.pdf> , section 2.43 ff, 5.3, and especially 9.11 ff

⁸ <http://www.electricitycommission.govt.nz/pdfs/opdev/transmis/pdfsconsultation/draft-pricing-principles-guidelines.pdf> section 3.2, also pages 23-26

⁹

<http://www.comcom.govt.nz//BusinessCompetition/Publications/Electricityreport/ContentFiles/Documents/Electricity%20investigation%20report.pdf> executive summary section ii

proposals, as it will not have the technical knowledge, or be funded (clause 126 (3)) to compare transmission with alternative investments, including energy efficiency.

Changes compromise security of supply

24. The asset swap between Genesis and Meridian will lead to poor management of the hydro resource. This will reduce security of supply. Also, the cost of the asset swap will far outweigh any consumer benefit from companies trying to attract customers in a wider area.
25. Hydro shortages have given massive profits to gentailers, as shown by the Commerce Commission inquiry on market power, supported by the Wolak reports.¹⁰ Spot prices rose last year, one of the wettest ever, because of unexpected thermal outages.¹¹ Scarcity is profitable.
26. Load management is being compromised by introduction of smart meters.¹²
27. Opportunities for network pricing to reduce overall supply security and costs will be compromised by the requirement in clause 45 (2) (e) for simplified tariffs.
28. In each of these cases, the primary goal of competition is overriding goals of security and cost reduction.

Conflict of interest

29. Government, as owner of two thirds of generation assets and all transmission assets, has a great fiscal interest in price rises. Gentailers can maximise profits by raising retail prices to whatever level the Minister condones. They can manage both hydro resources and thermal generator availability to hike spot prices, and pass these price rises on to captive consumers subsequently.
30. Government's regulatory interest relates to affordable electricity for long-term benefits to consumers, and the efficient supply of electricity to service New Zealand's economic and social needs. These are public-interest goals, not

¹⁰ <http://www.comcom.govt.nz/BusinessCompetition/Publications/Electricityreport/DecisionsList.aspx>

¹¹ <http://www.electricitycommission.govt.nz/pdfs/submissions/pdfssecurity/asa-2009/DEUN.pdf>

¹² http://northpower.com/news/entry/smarter_meters_in_new_zealand/ . also http://www.pce.parliament.nz/reports_by_subject/briefing/response_to_submitters_on_smart_meters_report

pure business goals. Electricity is not just another commodity, “like baked beans”, as was argued in the mid 1980s.

31. The Bill does nothing to mitigate Government’s conflict of interest. This conflict can only be addressed by a return to the concept of electricity as an essential service.

Proposed measures: regulate, then restructure

32. We describe the gentailer oligopoly as a cartel, legalised by the Decision that authorised the Electricity Commission¹³ because the wholesale electricity market could not be created without agreements between the industry participants.
33. Undue price raising by cartels transfers wealth from consumers to investors to an extent that can cause real economic harm.¹⁴ After almost two decades, the Commerce Commission finally regulated electricity networks that had been price gouging, under Part IV of the Commerce Act.
34. The market power of the gentailer cartel might be greatly reduced by separating retail from generation businesses. This should be part of a comprehensive redesign of the electricity market, which must be done with due deliberation. The result must be to simplify rather than atomise New Zealand’s electricity system.
35. Retailing could be transferred to a “single buyer” who buys generation output to minimise costs. Generation would remain fully competitive. A simple range of tariffs should be offered to domestic consumers, tariffs which can be adapted for specific networks where there are constraints, to improve security at minimum cost. Retailing by lines companies should remain an option, as this would enable them to reduce their network costs through special tariff offers.
36. International experience supports our call for major change. An analysis by major electricity users in the U.S. found that liberalised electricity markets in the US, Europe and Australia were neither competitive nor sustainable. If the problems are not fixed, “a return to traditional regulation ... must be considered.”¹⁵

¹³ <http://www.comcom.govt.nz/BusinessCompetition/Anti-competitivePractices/Applications/ContentFiles/Documents/EGBL%20Final%20determination.pdf>

¹⁴ <http://www.med.govt.nz/upload/70683/Cartel-Criminalisation.pdf> , paras 9, 10 on page 19

¹⁵ Anderson, John A. “Electricity Restructuring: A Review of Efforts Around the World and Customer Response. The Electricity Journal, April 2009, pages 70-86ß

37. In the UK, for example, the pure competitive electricity market has failed to deliver on promises, and the regulator, Ofgem, proposes to replace its “New Electricity Trading Arrangements” (now a decade old) by one of five options up to and including a central buyer on its electricity market.¹⁶
38. Insofar as New Zealand’s gentailer cartel remains, its regulatory authority must have full representation of domestic consumers, commensurate with their producing 32% of electricity demand and 45% of electricity revenues, and comprising 86% of customer connections.

Other relevant issues: energy efficiency

39. The removal of energy efficiency from the regulatory structure will mean that regulator’s analyses of costs and benefits of new supply would not include a comparison of these with costs and benefits of energy efficiency. New supply will be considered and costed in isolation from consideration of more sustainable strategies. This will make it easier to build new power stations and transmission and distribution lines. One consequence will be that companies will be able to increase their asset values – justifying the case for price increases and potentially making them attractive to privatisation. Grey Power Federation and DEUN both oppose any further privatisation of electricity assets, as do a large number of New Zealanders.
40. The removal of the objective “environmental sustainability” will further promote investors’ goals over environmental goals. Both energy and economic efficiency must be relevant matters in all resource management considerations of new electricity supply.

Support for matters in the Bill

41. We support the retention of restraint on lines price increases for domestic and rural consumers (Clause 111-114).
42. We also support allowing lines companies to become retailers, so long as there is sufficient protection for both consumers and shareholders. Trust-owned lines companies have real opportunities to use the electricity market to promote sustainable economic development in their regions.
43. We strongly support the provision in clause 119 (1) (c) for the Authority to require information from industry participants. We have made much use of the Centralised Data Set, for which information is not always reported in a consistent form, resulting in real gaps in our analyses. This is a world-class

¹⁶ <http://www.ofgem.gov.uk/Media/PressRel/Documents1/Ofgem%20-%20Discovery%20phase%20II%20Draft%20v15.pdf>

reporting system, and deserves to be maintained to a high standard of accuracy.

Conclusion:

44. The Bill would drive New Zealand's electricity industry back to the pure market philosophy of the 1980s, even though both electricity restructuring and market pricing have failed to meet their promise of long-term benefit to consumers. Electricity must now be treated as an essential service, for consumer benefit and the economic and social development of New Zealand. Today's profit-maximising objectives must be replaced by cost-minimising. Gentailers are acting as a cartel and should be regulated under Part IV of the Commerce Act. Their market power might be greatly reduced by separating retail from generating businesses. In the meantime the regulator must fully represent domestic consumer interests, with special attention to the most vulnerable, who are so disadvantaged by continuing price rises.

We submit that Parliament should:

- 45. Amend the Commerce Act to restore the concept of "essential service", so that electricity supply is cost-minimising not profit-maximising.**
- 46. Modify the Statements of Corporate Intent of the State-Owned Enterprises to require cost minimising not profit maximising.**
- 47. Retain the objectives "fair" and "environmentally sustainable" in electricity and gas legislation, to put a focus on effective resource utilisation for the long-term benefits of all New Zealanders**
- 48. Regulate gentailers under Part IV of the Commerce Act, and begin the groundwork needed to separate generation from retail businesses.**
- 49. Meanwhile, progressively improve the existing regime for consumer and national benefit, instead of forcing a pure competitive market.**