

29 June 2010

Electricity Commission  
Level 7, ASB Bank Tower  
PO Box 10041  
Wellington 6143

*by email:* Jackie.ashley@electricitycommission.govt.nz

**SUBMISSION ON THE DISCUSSION DOCUMENT FOR PHASE 2 OF DISTRIBUTION PRICING STANDARDISATION**

- 1 Orion New Zealand Limited (**Orion**) welcomes the opportunity to comment on the Commission's discussion document Phase 2 – "Addressing the policy direction as outlined in the Ministerial Review and the "more standardised line distribution tariff structures and use of system rules" objective in the Electricity Industry Bill" (**the paper**) released by the Commission in May 2010.
- 2 Our submission comprises the following sections:
  - general comments on the paper,
  - comments on "Compliance" with the model UoSA in Appendix 1,
  - our response to the specific questions 2 to 28 raised in the paper, which we set out in a schedule.

**General comments**

- 3 The paper has been released within two months of the Commission publishing, on 1 March 2010, its "Distribution Pricing principles and information disclosure guidelines" which are the culmination of a significant amount of work including three rounds of consultation and two workshops.
- 4 While we appreciate that the Commission's decision to adopt a principles-based approach does not purport to meet the requirements of clause 45(2)(e) of the Electricity Industry Bill 2009, we note the Commission's comments that:

*“In deciding on a principles based approach to distribution pricing, the Commission has noted clause 45(2)(e) of the Electricity Industry Bill 2009...” and*

*“Hopefully however the work in deciding on a principles-based approach will assist the proposed Electricity Authority in its consideration of any further work to be done in this area.”<sup>1</sup>*

- 5 We also note that the Commission has formed an industry group (the Distribution Pricing Administrative Issues working group) to consider issues that could be characterised as “low level elements” and related to standardisation of nomenclature and information exchange between retailers and distributors.
- 6 The Commission expected the recommendations from this Distribution Pricing Administration Issues working group would inform a number of initiatives the commission has to increase the level of standardisation in respect of the inter-related issues of reconciliation process and use-of-system agreements.
- 7 The objective of this new paper is to gather information to help determine the likely costs and benefits of distributors adopting standard price structures. We are concerned about a number of aspects of the Commission’s new process.

- *Approach*

- 8 In our view the Commission has not followed a reasonable process either in restarting work on this subject - when it has only recently signalled it had finished it - or in the way it has decided to go about this new process. The Commission is not obliged to carry out this work at all, so it cannot argue that it is under time pressures. The Electricity Bill (the Bill) cannot be seen as a rationale for the Commission to embark on this work, since it has not been passed, and in any case it places requirements on the Electricity Authority that do not have to be met until a year after the Bill is passed. The Commission must therefore be relying on the decidedly insubstantial ‘arguments’ contained in the ETAG<sup>2</sup> report and the Cabinet Paper<sup>3</sup> supporting the Bill.

---

<sup>1</sup> Para 14 Electricity Commission *Distribution pricing principles and information disclosure guidelines* February 2010.

<sup>2</sup> Improving Electricity Market performance: A preliminary report to the Ministerial Review of Electricity Market Performance by the Electricity Technical Advisory Group, August 2009, Volume 1 pp 5, 6 and 56. Volume 2 p 110.

9 We are also concerned that the process of collecting information from retailers and then seeking distributor comment on it is flawed and unreasonable. At the very least a terms of reference or project scope should have been consulted on first.

- *Ignoring other workstreams*

10 The Commission has not explained why other Commission workstreams, some of which have been progressing for some time, and which address some of the matters unearthed in Phase 1 of the new process, have been cut across by this new process. Three key examples are:

10.1 The model use of system agreement workstream

10.2 The loss factor panel

10.3 The Distribution pricing administrative issues working group.

11 At the very least the Commission needs to explain how this new workstream interacts with the existing workstreams.

- *Shifting the rationale for intervention*

12 We are pleased to see that the commission appears to accept that retailer costs are no longer the primary rationale for considering standardisation. The new rationale appears to be driven by the objective set for the Electricity Authority in the Electricity Industry Bill (the Bill), which is: "...to promote competition in, reliable supply by, and the efficient operation of, the electricity industry for the long-term benefit of consumers."

13 While we generally support the broader objectives outlined in the Bill, in this case it merely serves to highlight that the rationale underpinning clause 45(2)(e) of the Bill itself lacks any substance, a fact which should lead the Commission to prepare advice to this effect for the Electricity Authority and terminate this workstream. Instead the Commission has sought to identify new reasons to persist with it.

14 In discussion with the Commission it would appear that it is interpreting the Electricity Authority's objective quite widely and hence refers to a need to consider such matters as demand side response, energy efficiency and emissions reductions not just generally, but also specifically as they relate

---

<sup>3</sup> Ministerial Review of the Electricity market, a paper to the Cabinet Economic Growth and Infrastructure Committee, p18, para 60.

to distribution pricing within the electricity industry value chain. In regard to this we would note:

- 14.1 it is a real stretch to turn “...efficient operation of...the industry...” into a requirement to consider matters such as energy efficiency (and we note that the Electricity Authority will not be responsible for energy efficiency),
- 14.2 we do not think it is appropriate for the Commission to either define the focus of the Authority or interpret the Authority’s legislated objective,
- 14.3 in any case a more obvious interpretation of the efficiency component of the objective would be that it refers to general operational efficiency and/or dynamic economic efficiency, not energy efficiency,
- 14.4 even if its interpretation is appropriate, the Commission has things the wrong way around: if the Bill implies a change in focus, then this should inform the Authority’s overall priorities and work programme, not be taken as a way to reinterpret existing Commission work programmes,
- 14.5 the interpretation should in any case not be taken to mean that every workstream must somehow address *all* the matters the Authority (or the Commission on its behalf) deems to be important, and
- 14.6 even if the new criteria are accepted, and they are not by Orion, they might lead to a very different standard than one that might be designed to reduce retailer costs.

- *Introducing new matters / scope*

- 15 We consider that the Commission is investigating issues that go well beyond the mandate provided to the Authority in the Bill, and in particular the set of “customer service” matters listed in para 2.1.11 of the paper. These matters may or may not be worthy of investigation, but most of them are a very distant remove from distribution pricing. There is nothing in the Bill that provides a mandate to consider them now.

- *No substantiation of cost*

- 16 Having gone to the trouble of attempting to establish the costs associated with the variety of distribution pricing arrangements the Commission

presents very little information about what these are. The paper includes just one three-line sentence saying these costs, driven by headcount and IT system costs “...could be of the order of \$5/customer/year...” but are “...subject to a significant margin of error.” We then learn that these costs relate to four key (but quite diverse) areas, but not what the relative importance of these areas is.

- 17 Turning to whether \$5 is material, if we assumed that all of this cost could be removed completely from the industry via standardisation (and not just transferred to other parties), that this change could itself be achieved costlessly, and that the full benefit flowed through to consumers then we note that \$5 per year represents around 1% of the delivery cost faced by a typical domestic consumer. We can conceive of indirect cost impacts and efficiency impacts of standardisation easily exceeding 1%, and thus making consumers worse off overall despite the cost reduction.
- 18 Perhaps most remarkable in relation to cost is the reported criticism by retailers of the direct billing approach taken by The Lines Company. For retailers to claim this is a barrier to competition when it completely relieves them of the requirement to deal with distribution pricing is at best contradictory. At worst it completely undermines the argument: we should see significant competitive activity on The Lines Company network **if** the variety of distribution pricing arrangements is a material barrier. Based on a quick perusal of Commission retail statistics we do not see any significant change in switching activity following The Lines Company’s move to direct billing. This needs to be explained by officials, the Commission and retailers. We also note that the Finance and Expenditure Committee has just amended the Bill to specifically exclude distributors who direct bill from the any standardisation under 45(2)(e), and so we presume the Commission will terminate this particular line of enquiry.

- *Integration with Commerce Commission*

- 19 As the Commission is aware, there are significant overlaps between its work in this area, and the Commerce Commission’s responsibilities under Part 4 of the Commerce Act. The Bill proposes changes to Part 4 of the Commerce Act 1986 to clarify that the Commerce Commission should not develop pricing methodologies (as an Input methodology (IM)) where an industry specific regulator has a mandate to do so.
- 20 Upon the proposed amendment being passed, the new Electricity Authority (once established) would have responsibility for setting pricing methodologies for electricity distribution services. The Commerce Commission will continue to develop its IM for pricing methodologies until the proposed amendment to part 4 is made, at which point it would act in

accordance with the amendment as regards the implications for the pricing methodologies IM. The Commerce Commission's draft decision is to adopt a principles-based approach to pricing methodologies, based largely on the EC's approach to distribution pricing (under its distribution pricing project) with some minor adjustments as necessary to ensure consistency with the Part 4 regime.<sup>4</sup>

21 We believe that, in the event the Part 4 amendment is passed, the Authority should adopt a very cautious approach to making any changes to distribution pricing methodologies, as these will directly affect regulation of distributors by the Commerce Commission. The twelve month period that the Government is providing the Authority to consider its approach provides a useful breathing space for the Authority to consult with both the Commerce Commission and the industry.

22 Should the Authority decide to make changes to distribution pricing methodologies it needs to work with the Commerce Commission to ensure that any downstream impacts – such as additional financial risks placed on EDBs – are appropriately accounted for in the Commerce Commission's IMs and more general regulatory approach.

- *No standard specified*

23 The Commission is attempting to determine the costs and benefits of standardisation, but has not given any indication of what the standard might be. We do not believe the discussion can proceed meaningfully, or very far, without some reasonable indication of what the standard is. We also consider that the appropriate counterfactual to any standard is the principles-based approach determined by the Commission in March. The standard must be a better approach than that.

- *Absence of analysis*

24 There are a number of areas where the Commission could have carried out some fairly straightforward analysis to shed some light on aspects of this workstream, rather than rely on hearsay and retailer assertion. Examples of analysis that the Commission could have carried out are:

24.1 developing a model of retailer market entry that identifies and ranks the various considerations that influence retailer decisions,

---

<sup>4</sup> Ibid, para 7.3.1

- 24.2 attempting to identify the actual diversity of distribution pricing structures: based on a quick perusal we would say there are only a handful of distinct methods – perhaps no more than six. For example the methods used by Electricity Invercargill and The Power Company are exactly the same, while the approaches of OtagoNet, Waitaki and Alpine are very similar to each other. To the extent that these and other “GXP” distributors’ pricing requires rebundling or mapping, the models to do this will be conceptually similar across all of them,
- 24.3 identifying the variety of retail offerings, and the extent to which they are driven by distribution pricing. We think the relationship is very close and that the current number of such offerings is quite small, which suggests that it is a relatively straightforward exercise to apply the same or very similar structures across the various distributor areas. (Note this is not the same as saying that the prices, or price relativities, are or should be the same across distributors. Nor is it saying what an appropriate number of retail offerings is: in a competitive market we may well see more!),
- 24.4 the extent to which complexity is driven by regulation, and in particular the low fixed charge regulations (which, for example, forced Aurora to abandon an innovative approach to distribution pricing for residential consumers),
- 24.5 an attempt to identify if there are any particular distributors whose pricing is unusual, or unusually complicated, and whether this can be correlated with competitive activity,
- 24.6 an examination of what has happened when distributors have in the past tried or been forced to change pricing structures,
- 24.7 an examination of other markets where there might be some lessons, for example how do telecommunications providers sell their services to other providers / retailers?
- *The impact of AMI*
- 25 Most retail pricing options reflect metering and load management arrangements that have been in place for twenty years or more. There is nothing wrong with these arrangements, but standardisation of distribution pricing runs the risk of locking these in, making it very difficult to design offerings more suitable to the capabilities of new technology such as AMI.

- 26 We can easily conceive of standards that would require distributors to come up with a new price for every new product that retailers devise. That seems both impractical and undesirable. Many distributors already have pricing (often called “TOU” pricing) that applies to connections where interval data is available, and it seems much more sensible to us that a form of this be applied for charging retailers - who may or may not repackage it – than for distributors to be entangled in retail product design.
- 27 On this note, we have a solution to the problem identified by a retailer (in para 3.3.3 of the paper) that retailer innovation (to the extent it has a distribution component) must be offered to all other retailers. The solution is that distributors charge retailers on a wholesale basis (which may or may not use GXP quantities). This frees retailers to design innovative products without even needing to consult the distributor, let alone worry about the distributor having to offer anything to other retailers.
- 28 However, **if** the Authority believes it is appropriate for distributors to effectively design retail offerings, then it needs to seriously consider what the role of retailers is. It may be that the consumer connection and service relationship should be with the distributor, with the energy component a (competitive) add-on to distribution charges. We note this is the regulatory approach in some overseas electricity markets.

### **Orion’s approach**

- 29 While some of the retailer concerns collected in Phase 1 are quite general, some are clearly aimed at Orion’s pricing. We take the view that for a business – any business – to lose control over its pricing or, more widely, its business model is a very negative outcome. However this does not mean that we do not make any changes. Examples of changes that we have made over the last 10 years are:
- 29.1 simplification of time zones for volume charges (from around ten to two).
- 29.2 the change in the definition of night from being 11pm to 7am to being 9pm to 7am (benefitting 40% of households and improving our ability to manage network loadings ).
- 29.3 the creation of an Irrigation connection category that not only allows us to more accurately reflect the costs of supplying this type of load, but also means retailers no longer have to complete a time consuming washup calculation. Our irrigation pricing also offers irrigation consumers discounts if they are prepared to experience occasional short interruptions.

- 29.4 simplification of loss factors – from 24 to just four.
  - 29.5 a change in the measurement of general connection peak period demands from kVA to kW.
  - 29.6 removal of zone B (a summer peaking zone) – there is now only one zone when there were two. This change reflected the changes to the transmission pricing methodology endorsed by the Commission.
  - 29.7 spreading peak recovery over twelve months, which significantly smoothes out retailers' cash flows.
- 30 These changes have not been motivated primarily by an attempt to simplify our pricing, although most have had that affect.
- 31 Regarding a key aspect of Orion's pricing, the dynamic peak component for General connections, it is true that retailers in most cases need to rebundle this in some way, and this does involve risk. It is also true that an entrant retailer may have limited information about the consumption attributes of customers. However, we note that:
- 31.1 this information asymmetry will be true to some extent irrespective of distribution pricing,
  - 31.2 an entrant also has an advantage in that it can learn from what other retailers have done, and also can seek to leverage market niches,
  - 31.3 Orion is prepared to work with, and has indeed worked with, retailers to ensure they understand the risk,
  - 31.4 this risk needs to be seen in the light of the other risks a retailer faces, in particular wholesale market risk. We estimate that the variation in delivery cost from expected cost is within the range +/- 3% in any year, and
  - 31.5 to the extent we have relevant information, we share this with retailers.
- 32 Regarding the Orion Delivery Services Agreement, as discussed with the Commission we acknowledge that key aspects of this will no doubt be seen by entrant retailers as less than welcoming. However, while we warmly welcome new entrants, the purpose of the agreement is to set out the parties' rights and obligations and manage and allocate risk appropriately. Specifically:

- 32.1 our prudential requirements mimic those of the wholesale market, so any entrant will already have to have met those in order to be entering the market. Why Orion should have lower standards than the wholesale market needs to be explained. In discussion the Commission seems to think that our business having monopoly characteristics immunises us from risk. Aside from the fact that we don't agree, we note that the Commerce Commission's regulatory regime does not allow us to price in risk, or automatically recover any losses that we incur in running our business, and
- 32.2 the prudential requirements have been met by the other retailers, so it would be unfair to them to have different requirements for entrants, and arguably we could not maintain the same requirements of the others if we were softer on entrants.
- 33 While we note the changes to the Bill regarding transferring retailer liability under the Consumer Guarantees Act to distributors, we consider that this is not a sensible solution to what we acknowledge is an unusual situation. We believe that the courts have established an appropriate obligation on distributors with respect to the delivery service, but that the higher standard then imposed on retailers is either a wrong decision by the High Court, or calls into question the application of the Act to electricity. Either way the 'solution' included in the Bill falls well short of optimal from an economic perspective. It would also in effect impose a higher obligation on distributors under the Bill than that determined as appropriate by the courts under the Act.
- 34 Overall regarding the Model Agreement, we note that we are being asked to compare 'compliance' with the 2008 consultation draft. Because this draft was never promulgated, we have not, recently, assessed the alignment of that Model and our DSA. However we have tried to carry out an assessment in the time available, at least for what we take to be the key areas.

### **CONCLUDING REMARKS**

- 35 In Orion's view the Commission should:
- 35.1 prepare advice for the Electricity Authority that there is in fact no evidence that the variety of distribution pricing structures or use of system business rules represent material problems that require changes to the code as anticipated in clause 45(2)(e) of the Bill, and then
- 35.2 terminate this workstream.

- 36 Thank you for the opportunity to make this submission. If you have any questions relating to this submission, please contact Bruce Rogers (Pricing Manager) DDI 03 363 9870 email [bruce.rogers@oriongroup.co.nz](mailto:bruce.rogers@oriongroup.co.nz).

Yours faithfully

A handwritten signature in black ink, appearing to be 'BR', written in a cursive style.

Bruce Rogers  
**Pricing Manager**

## Appendix 1 Compliance with Model UoSA

MUoSA Elements <sup>5</sup>			Please indicate whether you currently comply with the MUoSA for each of the elements below	For elements where you are not compliant:		Please indicate the likely business impacts to comply with the MUoSA*	Other comments
				Please indicate why you are not compliant	Please indicate what you are currently doing instead		
<b>Tariff structures</b>							
Price category and tariff options (including schedule 10). Intention to adhere to new Pricing Principles (or not).			Not known.	NA	NA	Not known	As we develop our pricing changes for April 2011 we will review our approach against the principles. To the extent that there appears to be

<sup>5</sup> A copy of the model use of system agreement is available from:  
<http://www.electricitycommission.govt.nz/pdfs/opdev/retail/consultationdocs/pdfsconsultation/model-contracts2008/Appendix-5.pdf>

							any discrepancy we will consider whether it is appropriate to change our pricing approach.
Losses and loss factors (including schedule 11)			With respect to loss factor monitoring, reporting and investigation, no.	We consider that we have nothing useful to add to the information provided by the Reconciliation Manager, and the information available to retailers.	We do monitor UFE as reported by the RM. UFE is small and negative on the Orion network.	Significant business impact in terms of costs if we had to develop the capability. No benefit to consumers.	Orion intentionally calculates loss factors based on our estimate of <b>technical</b> losses. We note that under global reconciliation loss factors are just a seed for the process, and that, in the absence of a case of special factors for specials cases (eg high voltage connections) the reconciliation process would achieve pretty much the same result if all factors were unity.  With the loss factor panel still working on this we have little to

							add. We believe the current structure of our loss factors strikes a reasonable balance between precision and implementability.
<b>Commercial Terms</b>							
Process for setting and applying prices			Yes. We don't think there is anything unusual about our approach.				When we do make structural changes we consult extensively, and well in advance.
Prudential requirements			Yes. The model includes credit rating as a parameter with a suggestion of BBB (Standard and Poors). We use A-.			None if credit rating is treated as a parameter.	Orion's requirements reflect the requirements imposed on purchasers under the EGRs.  Orion requires only one month's estimated charges as security because we

							bill partly in advance.
Events of default			We don't think this is a major issue?				
Termination of agreement			We don't think this is a major issue?				
Confidentiality			We don't think this is a major issue?				
Force majeure			We don't think this is a major issue?				
Amendments to agreement			Any variations must be offered to all other retailers. Our experience is that these have not usually been taken up.				

Dispute resolution procedure			We don't think this is a major issue?				
Liability			There are some differences as to maximum liability, however we note that one figure in the Model is a parameter for negotiation.				
Consumer agreements			Broadly yes.				
<b>Service Delivery Terms</b>							
Service standards (schedule 1)			Not in the form in schedule 1	We believe our regulatory reporting covers off the relevant aspects.			
Service interruptions (including schedule 6) and Outage Management			Generally yes.				

(planned and unplanned) Generally							
Load management (including schedule 9)			Our agreement is less prescriptive.				
Service performance reporting			No	We believe our regulatory reporting covers off the relevant aspects.			
Momentary fluctuations			Our agreement does not require this, although we agree it is sensible inclusion in retailer agreements with consumers.				
<b>Operational</b>							
Billing and payment (including Reconciliation methods)			Partially	Orion carries out wash-ups but does not calculate a use of money		We believe the cost of developing the capability to calculate	Billing and Payment is actually in Part II, Payment obligations?

				<p>adjustment.</p> <p>Orion requires payment of the full amount of a disputed invoice.</p>		<p>interest on wash-ups would be significant, and exceed the value involved in the wash-ups, which by definition are largely a zero sum game amongst retailers, and can be in favour of either the distributor or any individual retailer.</p>	
Access to consumer's premises			Yes				
Interference and theft			Yes				
Network connection standards (including schedule 7)			Broadly yes.				

Consumer service lines			No.	Orion maintains these free of charge. This is not standard.	Orion maintains these free of charge. This is not standard.	It would disadvantage consumers if we moved to the standard.	
Tree trimming							We believe this is now covered by legislation so can be removed from the MoUSA
Connections and disconnections			Broadly, yes.				
Information exchange (including schedule 4) and information received e.g. as-billed, normalised, etc			Broadly yes.			Some of the EIEPs do not align well with our processes.	
<b>Other</b>							
Conveyance versus interposed models (impacts)			Interposed for all but a few large connections.				

<p>Processing Rebates for trusts / networks</p>			<p>NA</p>				
<p>Model UOSA – intention to move towards it (or not)?</p>			<p>Depends to some extent on the model, and whether indeed a model is the right approach.</p>				<p>Generally we would be comfortable aligning in those areas that do not materially adversely impact on cost or risk.</p>
<p>GST versus ICP pricing (efficiency, market signals and risk transfer)</p>			<p>Presumably GXP not GST? We are not quite sure how this relates to the model agreement? See comments in body of our submission.</p>				<p>We do not think there is a necessary relationship between where quantities are measured, and efficiency or the ability to provide pricing signals.</p> <p>AMI blurs the boundary by allowing retailers to choose how the meter and reconcile quantities. It effectively allows them to access ICP pricing by reconciling ICP interval</p>

							quantities.
Embedded Network effects			Embedded networks are inconvenient, but that itself is no rationale for intervention.				

**Schedule: Responses to specific questions**

<b>Q No.</b>	<b>Question</b>	<b>General comments</b>
2	<p>With regard to EIEPs:</p> <p>a) what would be the impact on your business (for example, in terms of administration costs) if compliance with the various EIEPs was made mandatory;</p> <p>b) are there some EIEPs which you consider to be more / less appropriate for a mandated approach to be adopted;</p> <p>c) how long do you think it would take before you could become compliant; and</p> <p>d) if there is significant variation in implementation issues between the various EIEPs, please indicate which would cause you the biggest issues.</p>	<p>a) Little or none for those that relate to pricing and billing. We do not believe the impact in relation to the others would be significant, however, see our answer to d).</p> <p>b) Not really. Mandated formats can still accommodate some optionality.</p> <p>c) We are already largely compliant with respect to pricing and billing.</p> <p>d) Those that relate to new connections may require us to change business processes.</p> <p>More generally we urge the Commission to leverage its working groups in developing the EIEPs, as this gives the parties a proper forum to develop such ideas.</p>
3	<p>What issues do you see with standardising:</p> <p>a) tariff coding conventions; and</p> <p>b) the methods by which tariffs and tariff changes are provided to retailers (e.g. via a pricing notification</p>	<p>a) By distributors or retailers? There is scope to achieve standardisation via mapping of the register content codes, eg “IN20”. However those codes themselves are, rightly, dynamic, and should become more so as AMI develops.</p> <p>b) We are not sure what value this would add: very few distributors have</p>

	EIEP)?	many prices. However we have no objection to the SDFWG considering and proposing changes if there seems to be value.
4	Do you see storing distribution tariff categories at a meter register level on the registry being beneficial? What issues do you see with such an initiative?	<p>No, there are numerous reasons why this should not be the case, just a few are:</p> <ul style="list-style-type: none"> <li>▪ It may limit innovation.</li> <li>▪ The inclusion of the register information itself will provide most if not all of the benefit in terms of retailers being able to make offerings to consumers.</li> <li>▪ The concept of meter register level will become (and is rapidly becoming) obsolete, and with AMI the equivalent of “meter register level” is a software or firmware construct. It may also become something that can be dynamically changed in consultation with the customer, in which case the retailer will need to know what it will be, not what it is.</li> <li>▪ It would impose a completely unnecessary requirement on distributors to maintain information on the Registry that is driven by retailer offerings to consumers.</li> </ul> <p>We need to distinguish between the registry as a repository for metering information and the registry as a place where distributors provide information. While some sort of mapping by retailers is useful, and probably necessary in a number of cases, we see no reason to have distributors maintain this mapping at the meter register level, or indeed on the Registry.</p>
5	What arrangements do you think should be implemented to improve the consultation process around tariff changes?	<p>We believe that Orion follows a reasonable process.</p> <p>We note the Commerce Commission’s interpretation in relation to consultation and the principles specified by the Court of Appeal in <i>Wellington International airport Ltd v Air New Zealand</i> [1993] 1 NZLR 671<sup>6</sup></p>

<sup>6</sup> <http://www.electricitycommission.govt.nz/pdfs/opdev/consultation-protocol-Sep07.pdf>

		<ul style="list-style-type: none"><li>▪ there are no universal requirements as to the form of consultation: any type of interaction (whether oral or written) that allows adequate expression and consideration of views will be sufficient;</li><li>▪ consultation must be allowed sufficient time, and genuine effort must be made;</li><li>▪ consultation involves the statement of a proposal not yet finally decided on, listening to what others have to say, considering their responses, and then deciding what to do;</li><li>▪ for consultation to be meaningful, the decision-maker must make available sufficient information to enable parties who are consulted to be adequately informed to make “intelligent and useful” responses; and</li><li>▪ the word “consultation” does not require agreement (although it does require more than mere telling or presenting). The Commission recognises that this principle is particularly relevant in relation to its functions. In relation to many of the issues that the Commission is required to deal with, industry stakeholders have widely divergent views and the issues have gone unresolved for many years. The Commission recognises that it is charged with breaking such deadlocks by making decisions in relation to those matters;</li><li>▪ “consultation” cannot be equated with “negotiation”. Negotiation implies a process that has as its objective arriving at agreement (although in consultation the tendency is at least to seek consensus);</li><li>▪ the decision-maker must approach the matter with an open mind: the decision-maker must be prepared to change or even start the process afresh.</li></ul>
--	--	---

---

6	<p>Do you believe:</p> <p>a. the current structure of your distribution tariffs is fundamentally consistent with the Commission's voluntary distribution pricing principles?</p> <p>b. the principles will result in a significant level of standardisation of tariff structures between distributors?</p>	<p>a) we have not conducted a review of our current structure. We will be reviewing our pricing methodology against the principles as we develop our pricing changes for April 2011.</p> <p>b) as this question is open to interpretation and is subjective it is difficult (impossible) to answer. What does the Commission mean by “a significant level of standardisation” and in whose opinion. We note the papers comment about the risk of standardising on the ‘wrong’ approach. So from the retailers’ perspective standardisation per se is not the answer. We are concerned that the paper may be confusing standardisation with simplicity. Simplicity is the enemy of long term consumer benefit.</p>
7.	<p>To the extent that the structure of your distribution tariffs is not consistent with the principles:</p> <p>a) are you intending to change them to be compliant; and</p> <p>b) do you believe it will require significant restructuring to be compliant?</p>	<p>a) we will need to assess compliance as part of our next price review. Any areas of non-compliance will require us to review such non compliance in terms of materiality, and available options for addressing it.</p> <p>b) until we actually review our pricing against the principles we do not know.</p>
8	<p>Do you believe that the current distribution pricing principles could be a practical way to address the retail competition and efficiency issues identified by retailers? Are there additional principles that should</p>	<p>The principles-based approach – which the Commission came to only a few months ago after extensive consultation – represents a compromise between the <b>possible</b> benefits of increased competition, and the possible adverse efficiency effects of standardisation. We have still not seen any evidence that distribution</p>

	be considered?	<p>pricing is a material barrier to retail competition.</p> <p>Since the principles were only finalised a few months ago, we see no need to change them at this time.</p>
9.	What would be the impacts from consolidating tariffs you have that are only open to a few customers?	The only pricing categories we have that apply to a “few customers” are very specific and cost reflective arrangements with very large connections. They are also subject to contractual obligations to those customers that would limit the scope for consolidation.
10	Why do you believe there are such apparent significant differences in approach between distributors with regards to the signals for load management & energy efficiency, and with regards to the extent of differentiation / grouping of customers into customer categories?	<p>This is an area where the Commission could actually do some analysis, as we do not know how much variation there is. We believe most distributors provide pricing signals that reward the provision of load management. However the signal would not obviously have the same magnitude across distributors due to different network dynamics, for example fuel substitution possibilities, different growth rates, extent of existing network constraints etc.</p> <p>Most network load management relates to shifting energy consumption to other times, or encouraging the use of non electrical energy at peak times. As such the relationship between efficient network pricing and energy efficiency is somewhat unclear. If this is a reference to the proportion of distributor revenue that is recovered on a “fixed” basis, then we can say that there is a reasonable economic rationale for a significant fixed component, both with respect to recovering the (largely sunk) cost of a (largely fixed) investment) and to reduce the variable cost of using the network most of the time (the short run marginal cost of using an electricity network is typically near zero most of the time). Having said that, Orion’s pricing has no fixed component for most connections.</p> <p>On the other hand we note that the transmission pricing methodology is</p>

		effectively entirely fixed.
11	Do you believe there are any <i>inherent</i> reasons why two networks with similar characteristics should have different tariff structures?	This begs the question about whether networks have similar characteristics, and how similar they are. These ‘characteristics’ must go far beyond the technology used in the construction of the network, and must also include the characteristics of the customer connected to the network; their requirements, expectations, understanding and historical investments. A strong focus on the future is also required.
12	<p>What would be the potential concerning impacts on your business of a move to standardised tariff structures? Please indicate if these impacts relate to:</p> <p style="padding-left: 40px;">ability to recover allowed revenues; efficiency of pricing signals in placing downward pressure on distribution and transmission costs (for example, are there cost drivers on your network that are not common to all distributors);</p> <p style="padding-left: 40px;">bill impacts (within customer classes and between customer classes),</p> <p style="padding-left: 40px;">customer service levels;</p>	<p>We cannot answer this precisely without knowing what the standard is. We can conceive of standards that would have no impact, and standards that would turn our business upside down. The impacts could be very significant in all of the areas listed. We have thus answered the questions assuming the “worst” standardisation.</p> <p>Allowed revenues: standardisation could significantly alter out profitability by increasing short and medium term costs with revenue unchanged. If we wish to maintain profitability we would have to seek a customised price path (CPP), which is likely to be an expensive process with an uncertain outcome. There is currently no mechanism under the DPP to enable us to recover such increased costs. However we note that if we were able to do so, these costs would inevitably find their way to consumers. Depending on the extent of any restructuring required to meet the standardised approach it could be very costly for us to demonstrate to the commerce commission that our new price structure remains consistent with the price path.</p> <p>Pricing signals: these signals would be completely at risk. Leaving aside short</p>

	<p>implementation costs; etc.</p>	<p>term security of supply issues, this would mean that the capacity of the Orion network and supporting transmission infrastructure could have to increase by up to 150MW, around 25%. For no increase in energy volumes our costs would increase by up to 15%. Again this would probably find its way to consumers, although we would probably have to apply for a CPP to recover the increased cost.</p> <p>Bill impacts: rate shocks could very easily be significant both within and between customer classes.</p> <p>Customer service levels: Should any changes result in the increased peak demand mentioned above, it is unlikely we could increase the size of the network in a timely manner, this could cause a reduction in customer service levels. Also customers may find that investments they have made – for example in large hot water cylinders - no longer make sense.</p> <p>Costs: If we had to move to a fully connections based billing system able to deal with data for every ICP we would need a completely new IT system, which we suspect would cost a few million dollars. We suspect approximately two more FTEs would be required.</p>
<p>13</p>	<p>When you develop tariff structures, to what extent do you consider whether a particular structure will facilitate retail competition and place downward pressure on customer’s bills from a whole of market perspective (for example, by promoting energy</p>	<p>A number of changes we have made in recent years have simplified our pricing from a retailer perspective, although that was not always the main rationale for the changes. We carefully consider any changes we make to our pricing structure, acknowledging that retailers have effectively sunk costs in administering existing arrangements. We note however that there appears to be</p>

	efficiency investments).	<p>significant competitive activity on the Orion network, with examples of aggressive retailer discounting and acquisition campaigns, and also pricing innovation that leverages our pricing. Finally we note that the Commission's analysis shows retail margins in Christchurch to be amongst the lowest in the country. [Market Design Review analysis picked up by ETAG]</p> <p>As noted above our pricing is driven primarily by network economics, not the promotion of energy efficiency.</p>
14	<p>Regulatory framework:</p> <p>a) Does your regulatory framework provide incentives to develop tariffs that place downward pressure on consumer bills from a total market perspective?</p> <p>b) Do you believe that different network ownership structures (and the nature of any subsequent regulatory price control) result in different incentives on network companies with regards to load management and energy efficiency?</p>	<p>a) the framework's focus is set out in the purpose statement of the Commerce Act. A key element of this is the long-term benefit of consumers, but there is also an objective of encouraging innovation and investment. Pricing standardisation could well compromise both innovation and investment. Note that the Commerce Commission is limited by Part 4 of the Commerce Act to only consider the "market" for electricity distribution and transmission. It cannot take an all of market perspective.</p> <p>b) this is another area where the Commission could do some analysis to establish whether there is any relationship. We have no information to support such a belief, but we can certainly conceive that it might be true. We note that a number of consumer owned distributors are exempt from price control.</p>
15	<p>With respect to 'GXP' pricing:</p> <p>a) to the extent that the motivation behind GXP pricing</p>	<p>a) we believe we could apply our "GXP" pricing structure to the HH data from AMI metered installations at an ICP level without making any</p>

	<p>is to send strong load management signals, do you believe similarly strong signals could be sent via ICP approaches? Similarly, do you believe that for customers without TOU metering, GXP pricing is no better, or potentially worse, at sending load management signals;</p> <p>b) alternatively, to the extent that the original intent behind GXP pricing was to manage distributors' UFE risk associated with ICP pricing, do you believe improvements in recent years have substantially reduced this risk; and</p> <p>c) to the extent that the main concern from retailers with regards to GXP pricing is the risk they face from having to re-package / forecast their pricing exposure, do you believe there are ways in which this risk can be reduced whilst continuing with GXP pricing?</p>	<p>material changes to it. In fact it is entirely up to retailers how they meter, profile and reconcile data, so they effectively already have access to ICP pricing on the Orion network if they want it via the <u>standardised</u> reconciliation process. We observe significant ongoing response to our ripple signals, and significant ongoing penetration of “day / night” style retail pricing options. However we can see no necessary relationship between the point of measurement and strength of load management signals.</p> <p>b) although management of UFE was not a key consideration in Orion’s move to use reconciled quantities for calculating charges, we do not believe there has ever been a significant UFE problem on the Orion network, and it appears there certainly is not one now. However we remain of the view that the best parties to manage this “risk” are retailers.</p> <p>c) we think this risk needs to be seen in the overall context of the risks that retailers face, and in the general requirement they have to repackage and forecast. The same repackaging risk could apply with ICP pricing. We also note that distributors inevitably face this risk themselves in repackaging transmission charges, including the risk of breaching their price path under a DPP.</p>
<p>16</p>	<p>What would be the impact on your business of a move</p>	<p>Has the Commission analysed the variation in loss factor structure? How many different structures / approaches are there?</p>

	<p>to a standardised approach for</p> <p>a) loss factors - is there any inherent reason why different distribution networks should have different approaches; and</p> <p>b) structures for loss factors, ie a single 'all-year' number versus splitting the year into various time blocks, and the extent to which differentiation by customer voltage levels and other factors (e.g. rural / urban) is appropriate.</p> <p>c) is there any inherent reason why different distribution networks should have different approaches?</p>	<p>a) we have recently simplified the structure of our loss factors. We are not sure that it matters much <b>how</b> loss factors are calculated?</p> <p>b) we believe there is a reasonable justification for loss factors for different voltage levels, for different geographic parts of the network ("zones") and indeed for specific connections in some cases. Our recent simplification removed the seasonality and time of day aspects as we judged these to be immaterial in the case of the Orion network</p> <p>c) this appears to be the same as a). So is our answer.</p>
17	<p>With regard to different billing / reconciliation approaches:</p> <p>a) what do you believe are the key pros and cons of the different approaches?</p> <p>b) what would be the implications for your business if the industry were to standardise on a particular approach?</p>	<p>a) we are not quite sure what this is referring to. We can imagine that distributors could have identical pricing structures, but different billing approaches, and vice versa.</p> <p>b) again it depends on the approach. We note that Orion actually uses the results of a standardised approach - reconciliation – to establish chargeable quantities.</p>
18	<p>With regards to billing risk:</p> <p>a) which billing platform do you use (e.g. Gentrack, NCS, in-house bespoke etc);</p> <p>b) do you agree or disagree with the retailers' general assertion that they should have certainty in network</p>	<p>a) Out-sourced bespoke. (How is this relevant? In the paper the concern seems to be about <u>retailers</u> having to develop bespoke systems?)</p> <p>b) We do not know what "post ante charges" are. As noted above uncertainty needs to be seen in the context of whole of market risk. There is no obvious reason why risk should be zero in relation to</p>

	<p>pricing to avoid billing risk in not being able to recover post ante charges: and</p> <p>c) a number of retailers have said that where there is no pricing certainty on a network they add a risk premium to the network charges (or will not enter that market at all) which means that consumers may be paying more than they might have otherwise. Who do you think is best placed to manage that uncertainty risk: the network company or the retailer?</p>	<p>distribution charges, and indeed there is no certainty in any areas as far as we are aware. For example retailers face credit risk, the risks associated with billing and metering errors, vacant property consumption etc.</p> <p>c) The retailers via their pricing option design to end consumers have at their disposal a wide range of options for managing risk. We note that on the assumption that the risk is equal for both parties, and distributors are adequately compensated for taking on a risk they do not currently face, consumer prices should be unchanged.</p>
<p>19</p>	<p>If communication protocols for outage information reporting between participants were standardised:</p> <p>a) would an EIEP based approach be best for this, or a central web based tool; and</p> <p>b) what would be the implications on your business (for example, in terms of costs, customer service levels, etc)?</p>	<p>We presume this is referring to planned outages? This is well beyond the scope of the matters mentioned in the Bill. We believe these arrangements are already largely standardised from a distributor perspective via EIEP 5. We note however that retailer communication to consumers is not standardised (an observation, not a criticism)</p> <p>a) This is a very technical question, but we can say that if the industry agrees to move to a particular standard we will seek to comply.</p> <p>b) We doubt these would be material.</p>
<p>20</p>	<p>If prudential requirements were standardised:</p> <p>a) what would be the implications on your business (for example, in terms of administration costs, business risks etc);</p> <p>b) what level of prudential requirements do you consider provides the right balance between bad debt protection and reducing barriers to retail competition; and</p> <p>c) are there any other solutions in this area (for</p>	<p>Once again it depends on the standard. Orion’s requirements are aligned to the standard in the EGRs for wholesale market participation.</p> <p>a) Obviously a lower standard increases our risk.</p> <p>b) Since our requirements align with the EGRs, there is no additional barrier to market entry, as any participant that meets our requirements has already had to meet the requirements of the wholesale market. This is actually an example where at least some retailers would seem to prefer non standard arrangements.</p> <p>c) The lock box looks to us like a very peculiar and non-standard approach when there are perfectly satisfactory and well established commercial arrangements in place which leverage the expertise of appropriate</p>

	example, the 'lock box' idea) that could be adopted?	institutions, eg banks' ability to evaluate the value of possible collateral.
21	<p>Regarding liability clauses:</p> <p>a) what are your views on the liability clause in the draft Model UoSA; Does it provide the right balance between bad debt protection and reducing barriers to retail competition, and if not, why not;</p> <p>b) what would be your recommended approach; and</p> <p>c) do you believe that the obligations by retailers under the Consumer Guarantees Act should be made back-to-back in UoSAs where the service or quality of supply failure and liability are a result of a lines issue? If so, why and if not, why not?</p>	<p>a) we do not believe the liability clause is about bad debt protection. Assuming the key point here is the amount of liability that retailers are exposed to...</p> <p>b) the courts have established that retailers have some liability for the quality of supply beyond the obligations of distributors. We can see that retailers may wish to challenge this decision and / or lobby for legislative change. We do not see that an appropriate solution is for distributors to take on additional liability.</p>
22	Please provide your views on the issues raised above by retailers.	<p>a) unless the amendment is required by law or regulation, our DSA requires the amendment to not be "materially detrimental to the retailer's business".</p> <p>b) as a practical matter it is probably necessary to have such links. In Orion's case changes to such documents are covered by the amendment criteria mentioned in a)</p> <p>c) we are not sure how this relates to the dispute resolution procedure?</p> <p>d) whose contract are we talking about here: the UoSA or the retailer's contract with the customer? Retailers are generally exposed to consumer credit risk in interposed arrangements.</p> <p>e) we don't think this is directed at Orion, but in any case we are not sure if this an information problem or a financial problem? Retailer contracts, like most contracts, have clauses covering the ability to enforce -</p>

		following termination - obligations that arose before it.
23	<p>Please provide your views as to:</p> <p>a) what extent separate billing by distributors supports the Authority’s objectives (i.e. promoting competition, reliability, and industry efficiency); and</p> <p>b) whether direct billing is required in order to ensure retailers pass through efficient distribution pricing signals, and if so:</p> <p>i) do they actually result in customer responses that are efficient from a ‘whole of market’ perspective and so place downward pressure on customers’ bills; and</p> <p>ii) could the same level of benefit be achieved without resorting to direct billing (for example, through innovative ICP pricing)?</p>	<p>a) separate billing, which Orion itself does, but only for a few large customers, is an interesting innovation. For retailers to claim this is a barrier to competition when it completely relieves them of the requirement to deal with distribution pricing is at best contradictory. At worst it completely undermines the argument: we should see significant competitive activity on The Lines Company network IF the variety of distribution pricing arrangements is a material barrier. Based on a quick perusal of Commission retail statistics we do not see significant competition on this network.</p> <p>b) Assuming direct billing is the same as separate billing, then retailers will by definition not be passing on distribution pricing signals?</p> <p>i) This appears to be a general question about whether customer responses are efficient. We believe they unambiguously are.</p> <p>ii) We don’t think this has anything to do with direct billing. Our observations based on looking at a number of network areas are that retailers preserve distribution pricing signals in their retail pricing.</p>
24	<p>With regard to connections:</p> <p>a) what would be the impacts (for example, with regard to administration costs and competition) of standardisation of information exchange for new connections (noting that there is an existing EIEP for this);</p> <p>b) although most new connections are straightforward</p>	<p>Once again this is introducing new matters not included in the Bill.</p> <p>a) What standard?</p> <p>b) Assuming new connections are an important issue, we would judge they are worthy of their own workstream to attempt to identify process improvements</p> <p>c) Yes .We provide for competition in this area.</p>

	<p>many are not. What process could be used to handle these variations if the bulk of new connections (and change to connection status) information exchange were able to be standardised; and</p> <p>c) does your company allow pre-qualified contractors to work on your network that are able to be directly contracted by retailers for connection services? If so, why, and if not, why not?</p>	
25	How should trusts receive the correct incentives to minimise retailer call centre and administrative costs in processing trust rebates?	No comment.
26	Are there any aspects of the UoSA which could be simplified, and if so, which ones and how?	<p>Which UoSA? Orion's, the existing "approved" 2005 model? The 2008 consultation draft?</p> <p>The real question is can the model be simplified without materially changing parties rights, obligations or the allocation of risk. Given the extensive consultation and discussion over many years, we suspect not.</p>
27	In your view, would a framework (with principles, milestones and a mediation process) be an appropriate mechanism to address negotiation delays, or would finalisation of the model UoSA be sufficient to speed up the process?	<p>If retailers are prepared to execute our standard agreement, which by definition treats them all equitably, there is no reason for any delay. We are not sure the model will ever be final, but completion of the 2008 consultation process would be a useful step.</p> <p>However care must be taken. We have advised the Commission over a number of years that the 'model' is unsuitable as a standard approach as it is backward looking, conceived before smart meters and lobbied for by incumbent large generator / retailers. It fails to take cognisance of the legislated distributor commitment to deliver long term benefits to consumers - not retailers.</p>
28	Do you have a view as to whether:	

<p>a) there is a need for a mandatory UoSA for embedded networks (a Commission-facilitated voluntary embedded network UoSA is already in progress);</p> <p>c) there should be a requirement that the price and / or tariff structure charged by the embedded network should be benchmarked to the 'main' network; and</p> <p>d) there would be a net benefit for simplification of the embedded model UoSA versus having the full Model UoSA?</p>	<p>a) We are unsure why embedded networks should be treated differently from other networks. Otherwise gaming is incentivised.</p> <p>b) There is no b)?</p> <p>c) We see no reason for this requirement. It seems to us that embedded networks will generally only exist where the 'main' network pricing creates an arbitrage opportunity. As such we do not think it is likely that such prices will be higher than they would otherwise be. Are there examples where they are?</p> <p>d) Net benefit for who? Perhaps the Commission could attempt to determine what drives the perceived proliferation of embedded networks. Is it the EIRA?</p>
---	---