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OPINION

Time to look at new power pricing model

Why are Central Otago residents overpaying for power, asks Richard McKenzie, of Alexandra.

DEREGULATION of New Zealand's power industry was meant to be good for consumers — competition would drive down prices.

The opposite has happened. Since deregulation, our annual power bills have increased at four times the rate of inflation. Despite being endowed with abundant electricity-generating capabilities, we're paying as if we were shipping this stuff from Cape Reinga.

Before deregulation in 1999, we were well served by a local company, the Otago Central Electric Power Board (OCEPB). It owned and operated a few small power stations, distributed power and sold the energy to the consumers. The cost of electricity was around 10c per unit — just as it still is in parts of Canada that are similarly endowed, where the industry has not been deregulated.

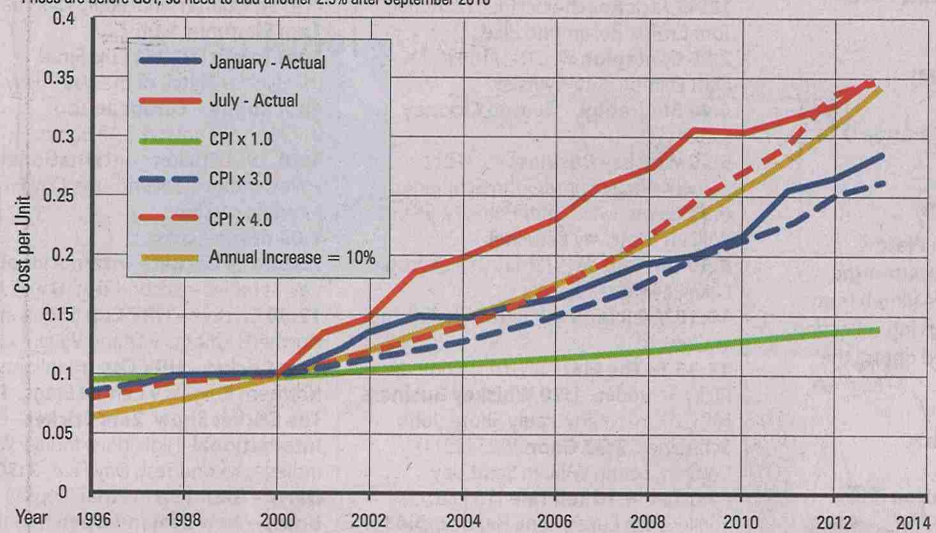
The ideology behind the deregulation of the industry was that the three arms of electricity supply (generation, lines, and retail) needed to be separated to encourage competition. Under deregulation, Central Electric decided to divest its lines and retail components. The Central Lakes Trust was set up to manage the windfall, and the redistribution of those funds has been hugely beneficial to the region as a whole. So, there's been at least one positive outcome.

But at what cost? Since deregulation in New Zealand, the price has ramped up at several times the inflation rate (as shown by the graph).

It's more expensive in winter because the energy retailers are charged more for the lines in winter than in summer. This particular company, TrustPower, passes those line costs on directly to consumers (some other retailers average these out over the year). Since deregulation, TrustPower's summer prices have increased at three times the inflation rate, and in winter they have increased by about four times the inflation rate (see graph). Most domestic power is used in winter heating, so prices have increased by around 10% a year, compared with annual inflation of about 2.5%.

So why have electricity costs been increasing sharply?

The National government's reforms of the 1990s may have resulted in lower power prices at the generator. But unfortunately, the power has to get from the generators to the consumers through power lines. Even though ample electricity for the whole of Central Otago is generated on our doorstep (like Clyde and Roxburgh), these reticulation costs dominate the overall bill.



Increases in domestic energy charges, as recorded by an Alexandra resident who has used the same supplier throughout. The green line shows the price changes that would have been required to track inflation. The blue and red dashed curves show changes for three and four times the CPI rate, and the yellow curve shows the changes that would have occurred if there had been an annual increase of 10%.

Our problem is there is only one set of power lines. The company that owns them, Aurora Energy, is a subsidiary of the Dunedin City Council, so the high prices paid in Central Otago prop up the Dunedin City Council.

In the winter months, about two-thirds of the bill is just paying for these lines charges. Aurora Energy, can get away with demanding such a high fee because there's no competition.

> Deregulation is not supposed to encourage monopolies, such as the one enjoyed by Aurora Energy. But that's what has happened.

If that was the intended outcome of deregulation, then it is a strange one. If the reforms had worked, there would be several competing lines companies. But that would mean multiple sets of power lines for each consumer, which doesn't make sense.

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Central Otago is large with a thinly spread population, so you might well expect higher lines charges than in urban areas. But Central Electric delivered power for a reasonable price. Why not now? Do other regions have the same problem?

It may be in Alexandra our lines charges pay for the energy to first be transported from Clyde to Dunedin, and then back to Alexandra. If that was the case, there would be bottlenecks on the way there and back, which the lines company could use as an excuse to hike its rates. Transport costs should be cheapest closer to the source. Here we see the opposite.

I'm a scientist, and in science we develop theories, or models, to explain our measurements. We then use these models as predictors of future change. But if the future reality differs from the model predictions, then it's time to change the model.

In this case, an economic model — was it based on any measurements at all? — predicted that electricity prices would fall, but in fact they have risen. It's time to change the economic model.

But there is hope. A local company, Pioneer Generation, is in the process of changing from being solely a generation operation to one that also sells electricity to consumers. If the company, a remnant of Central Electric now owned by the Central Lakes Trust, can find a way to add lines to its operations, then we may see a return to the pre-deregulation days, when Central Otago got a fairer deal on electricity prices. If Pioneer Generation can't manage it, then perhaps the Central Otago District Council can assist with the lines take-over.

Failing that, our best hope would be for a return to a time when the lines infrastructure, like the roads, was in government hands. Yes, that was still a monopoly. But its responsibility was to fairness for the many and not the economic gain of a few.