Via email to infrastructure.regulation@comcom.govt.nz

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Default price-quality paths for electricity distribution businesses from 1 April 2025 – draft decision

Mercury welcomes the opportunity to provide feedback to the Commerce Commission (the Commission) on its *Default price-quality paths for electricity distribution businesses from 1 April 2025 – Draft decision* (Reasons Paper), 29 May 2024.

Mercury is committed to an energy transition that is affordable, secure, resilient and supports economic development and productivity growth while recognizing the challenges.

Given the regulatory tools available to the Commission, Mercury agrees in general with the draft decisions on the default price-quality path (DPP) for non-exempt electricity distribution businesses (EDBs) that would apply from 1 April 2025 (DPP4).

The implementation of the determination over the five-year regulatory period is a key concern for Mercury, particularly focusing on managing the impact of the determination on consumers. Even though the Commission's effort to mitigate the magnitude of the price increases are reasonable given its available regulatory tools, it does not obviate the impact of the increases. As a result, these price increases may be substantial for some consumers throughout the five-year regulatory period.

Mercury, therefore, submits:

- Consumers need a clear view of the potential impact of changes to retail prices throughout the regulatory period
- We need to have an open conversation about the effectiveness of the Commission's regulatory tools throughout the energy transition
- EDBs need appropriate incentives to invest in innovation and enable smart systems throughout the energy transition

Mercury expands on each of these points in turn.

Consumers will need a clear view of the impact of changes to retail prices throughout the regulatory period

Mercury endorses the clarity of the Commission's communications on the expected significant impact of the draft decision on consumers' bills and requests that the Commission continue to provide this level of clarity. This will help with planning the implementation of the DPP4 determination. Mercury's focus now is to identify how the impact of DPP4 on consumers' bills can be further mitigated, including by offering options around retail tariffs as well as identifying and supporting vulnerable customers.

The Reasons Paper provides an overview of the impact of the draft determination on consumers. It highlights that the forecast network allowable revenue allowance of $12 billion over the five-year regulatory period represents an increase of 50% in real terms compared to the five-year DPP3 regulatory period. To manage the financial impact to consumers, the Commission has limited the initial nominal increase in distribution revenue to an average of 24%. This equates to approximately $15 per month (or $180 in the first year), excluding GST, on average for a household consumer electricity bill. A more detailed analysis of the draft determination indicates that the impact of increases in allowed revenue on consumers differs significantly between distributors for each year through the regulatory period.

How each EDB implements the determination will also add a further layer of complexity driving differences in network prices they charge retailers. These differences may be impacted by EDB ownership structures, treatment of dividends by community owned EDBs, through to where EDBs are in their process of moving to cost reflective tariffs. This means that retailers are unlikely to have certainty of network prices until 3 to 6 months before they are due to be reflected in retail prices.

Mercury is fully aware of these challenges and is working to address them. This starts by ensuring changes are communicated in a clear and cohesive way and empowering customers to make informed decisions about their energy consumption. In addition, Mercury has begun investigating a Time of Use option, which would involve giving participating customers pricing that varies across the week to encourage them to shift their energy use away from peak periods for financial benefits. We also have a comprehensive customer care programme for those most in need.

We need to have an open conversation about the effectiveness of the regulatory tools throughout the energy transition

The significance of the current draft decision's impact over the DPP4 regulatory period serves as an indicator of how in subsequent regulatory periods consumers might be exposed to a similar changes to their bills and/or the possibility that EDBs might be exposed to financial hardship.

That is, Mercury is concerned with how the current regulatory tools for determining allowed revenue might expose consumers and/or EDBs to the risk of shocks in the future. This concern is motivated by the effect of potential future bill increases and/or EDB financial hardship on affordability of electricity, the rate of electrification, and ultimately support for the energy transition. Our general view is that this risk is best managed by maintaining a smoothed consistent approach to pricing that avoids significant changes that could detrimentally impact consumer confidence in electricity pricing as well as EDBs' efficient investment decisions.

Mercury, therefore, proposes that the Commission conduct a review after the commencement of DPP4 to assess the effectiveness of its regulatory tools for balancing consumer bill impacts and EDB financial hardship over multiple regulatory periods that takes into consideration the energy transition over multiple regulatory periods.

EDBs need an incentive to invest in innovative smart systems throughout the energy transition

Mercury considers that enabling the shift to a 'smart system' can play a central role in helping to alleviate some of the need for investment in traditional poles and wires that is anticipated to drive costs in future regulatory periods by maximising the use of existing infrastructure and allowing more targeted future infrastructure investment. Recent work by the Boston Consulting Group identified that enabling the smart system on its the preferred pathway for New Zealand's electricity transition would save $10b NPV in total system costs and reduce average household energy bills by around 45% in 2050.[1]

We strongly support the Commission enabling the smart system through focusing on removing the regulatory barriers. For example, we support equalizing EDB's financial incentives between opex and capex solutions, the Innovation and Non-traditional Solutions Allowance (INTSA), Incremental Rolling Incentive Scheme (IRIS), and requirements to improve quality of performance.

However, these regulated solutions do not necessarily address a regulatory drag on innovation. An EDB may still be exposed to a regulatory risk if it chooses to deviate from a tried-and-tested treatment of its expenditure. In other

[1]. BCG report *Climate Change in New Zealand: The Future is Electric*, October 25, 2022, page 10.

words, the regulated measures do not necessarily emulate a dynamic process of innovation observed in a workably competitive market.[2]

Unlocking the benefits of the smart system will deliver better outcomes for consumers overall, but requires a coordinated, multi-year work programme across a number of regulatory and government agencies. We encourage the Commission to continue to take up its leadership in ensuring that this can occur and that progress at pace is achieved.

Mercury looks forward to engaging with the Commission and industry stakeholders further on DPP4.

Yours sincerely,

[redacted]

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[2] Commerce Act, section 52A(1)(a) requires the determination to "*… promote the long-term benefit of consumers in markets referred to in section 52 by promoting outcomes that are consistent with outcomes produced in competitive markets …*"