

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

19 December 2023

Default price-quality paths for electricity distribution businesses from 1 April 2025 (DPP4)

Mercury welcomes the opportunity to provide feedback to the Commerce Commission (the Commission) on its issues paper *Default price-quality paths for electricity distribution businesses from 1 April 2025* (Issues Paper), 2 November 2023.

Mercury is committed to ensuring the energy transition is affordable and the energy system is secure, resilient and supports economic development and productivity growth.

Mercury agrees with the Commission's approach for considering how the regulatory tools within the DPP can be best used to promote the long-term benefit of consumers. In particular, we agree with focusing on forecasting efficient expenditure; incentivizing continued innovation and efficiency during the energy transition; and managing price shocks and the ability for EDBs to invest.

Our submission builds on Mercury's previous submission on the Commission's *Part 4 Input Methodologies (IMs) Review 2023, draft decisions*, 19 July 2023.¹ Mercury proposed in that submission that the IMs in general should support the electrification of the New Zealand economy for the long-term benefit of consumers by:

1. Enabling investment in network capacity ahead of demand that underpins confidence in the electrification of the economy;
2. Enabling investment in emergent, innovative flexible demand-side resources that in turn reduce the need to invest in network capacity; and
3. Minimizing price shocks and ensuring that the transition is affordable now and into the future.

The Commission's Issues Paper on DPP4 addresses these points in general, and as such we refer the Commission to our prior submission.

Our present submission, in turn, expands on the need to minimize price shocks, ensuring that the transition is affordable now and into the future.

Greater collaboration and collective action is crucial for success

Mercury proposes the draft Sector and Government Energy Transition Framework (the Framework) will promote greater collaboration and collective action between the government and the energy sector to enable an energy transition that is at the pace and scale required to maintain security and affordability.²

The electricity sector is crucial for Aotearoa New Zealand's energy transition and is undergoing transformational investment and sector change of unprecedented pace and scale.

¹[Mercury-Submission-on-IM-Review-2023-Draft-Decisions-19-July-2023.pdf\(comcom.govt.nz\)](#)

² Mercury supports the draft Sector and Government Energy Transition Framework's submission to the Commerce Commission on the DPP4 Issues Paper.

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The way that Aotearoa navigates the global energy transition will be critical to our country's prosperity. To date, Aotearoa's energy system has been ranked one of the best in the world for its combined equity, security and sustainability. To continue this over the coming decades will require good 'whole of system' decision making. A joint Government and sector approach is crucial to enable collective action at the pace and scale now required.

The electricity sector will need to make significant investments in the coming decades, starting with an estimated \$42bn through to 2030.³ The Government can create the conditions that best leverage this investment by removing the barriers to supply side investment in new renewable generation, transmission and distribution, and ensure that policy actively supports demand side changes.

Collective action is crucial for the success of the transition, and the Framework's current priority themes get us started on the items that are 'no-regrets' to set up for the transition. Once up and running, the Framework can help work through other key priorities and create options for the longer term elements of the transition.

The Framework proposes the following priority themes for collective action that get us started:

Support accelerated renewables development

- *Effective consenting frameworks*: Ensuring consenting frameworks encourage rapid deployment of renewables and enabling infrastructure (high priority), both through optimising existing assets and new developments, while maintaining competitive neutrality.
- *Efficient market mechanisms*: Ensuring wholesale electricity market arrangements to enable electricity to play its role, fully and efficiently, in decarbonising New Zealand. In particular, developing market mechanisms to improve security of supply (particularly during winter peak periods).

Scale up transmission and distribution investment

- *Investment incentives for networks*: Enabling investment incentives and funding to networks to support the transition via network enhancement, expansion, and non-network alternatives.

Support people and the workforce

- *Workforce strategy*: Ensuring sector workforce development so that there is improved diversity and capacity to deliver on the transition to a decarbonised energy system.
- *People experiencing hardship*: Ensuring meaningful and enduring support for consumers experiencing hardship.

Drive electrification at pace

- *Electrification*: Drive decarbonisation through electrification by ensuring EV charging infrastructure can be successfully rolled out and electrification projects for households, businesses and large-scale initiatives can be implemented, encouraging load flexibility where possible.

Enable a smart electricity system

- *Smart system*: Enable the 'smart system' to maximise the use of existing infrastructure, to minimise future infrastructure investment, reducing whole-of-system costs and delivering better consumer outcomes.

³ BCG report The Future is Electric: A Decarbonisation Roadmap for New Zealand's Electricity Sector, page 2.



- *Network resilience*: Improve the ability of networks to adapt to the effects of climate change and build greater network resilience.

Encourage the right energy and capacity mix

- *Resilient transition*: Recognising the role of appropriate transition fuels (for example, natural gas) and supporting the interconnection between gas, electricity and other fuels in achieving a resilient transition.

Mercury supports taking a whole of system view of the energy transition out to 2050. The priority themes, as noted above, get us started on the 'no-regrets' actions that should be taken now.

We need an open conversation about how retail prices may change through the energy transition

Mercury considers that it is crucial for the government to form an ongoing, forward-looking view of the potential effect of changes in the price of input factors on electricity retail prices. The Commission should be involved in this process by providing transparency regarding its expectations of the impact of DPP4 regulatory settings on retail prices.

The Commission consultation highlights the importance of the conversation where it notes it anticipates *consumer bills for electricity distribution services will significantly increase for the DPP4 regulatory period given expected increases in the inputs we use for calculating revenue allowances*.⁴

The Commission notes that it has the discretion to determine the rate of change in EBDs' allowed revenue in order to minimise any undue financial hardship to the supplier or to minimise price shock to consumers. Exercising this discretion may become increasingly challenging as there are an increasing number of other input factors that may impact on electricity retail prices.

For instance, Transpower's recent submission on its expenditure plan for the regulatory period starting 1 April 2025 highlights another factor that may place upward pressure on retail prices. It notes that its proposed increase in network expenditure would increase average household electricity bills by around \$7 per month during 2025.⁵

Other input factors that could impact retail electricity prices include near term inflation as well as impact on the cost of capital, growth in intermittent generation resulting in increased spot market volatility, the price of NZ ETS units, as well as skilled worker shortages and supply chain issues.

The Commission implicitly acknowledges this challenge in part, where it notes that there is a risk that both a price shock and financial hardship may go beyond the DPP tools, suggesting that a CPP may be a better alternative. Even here though, it is not clear that CPP would be sufficient.

In addition, a more general concern we have is that the full range of factors highlighted above span the Commission, the Electricity Authority, MBIE, and the Ministry for the Environment, which then impact distributors', Transpower's, retailers' and generators' investment and pricing decisions. Presently, there is no single view of how these decisions might come together and impact in total on retail prices.

Even though these changes may be considered individually, it is also important to consider both the cumulative impact of these changes on electricity prices and the fact the impact may be front loaded in the early stage of the energy transition. The cumulative effect of price changes has the potential to also impact affordability of electricity, the rate of electrification, and ultimately support for the energy transition.

⁴[Default-price-quality-paths-for-electricity-distribution-businesses-from-1-April-2025-Proposed-process-25-May-2023.pdf \(comcom.govt.nz\)](#) paragraph X35.

⁵[Transpower spending proposal focused on retaining a reliable national grid | Transpower](#)



With respect to DPP4, the Commission indicates that it may hold specific issues-based workshops following receipt of cross-submissions on the present consultation and before the end of March 2024. Mercury suggests that the Commission should hold an issues-based workshop on its approach the risk of undue financial hardship to EDBs and price shocks to consumers.

Discretion to minimise any undue financial hardship to the supplier or to minimise price shock to consumers

BCG's forecast growth of 30% in distribution network investment in the period 2026–2030 compared with 2021–2025 is not incremental. This investment, as highlighted above, is expected to be made under conditions of higher uncertainty and ahead of time – i.e. ahead of demand.

As Mercury has highlighted previously, the Commission has addressed analogous economic issues – i.e. where network investment is made under conditions of higher uncertainty and ahead of demand – in case of price-quality regulation of Chorus' regulated asset base under Part 6 of the Telecommunications Act 2001. As a part of the Government's ultrafast broadband initiative, local fiber companies, including Chorus, were required to deploy a fiber access network to meet specified deployment targets that were ahead of demand. Furthermore, the price of wholesale services for access to Chorus' fiber network were capped at levels agreed between Chorus and the government.

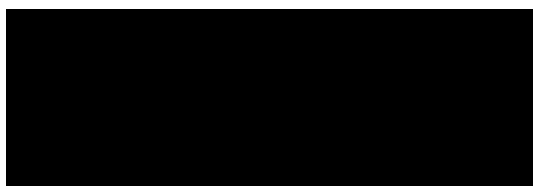
The deployment of fiber ahead of demand coupled with the cap on the price of wholesale services resulted in Chorus incurring a financial loss, which is captured in Chorus' initial RAB value as a financial loss asset. Furthermore, the Government provided financing to enable the deployment of the UFB network.⁶

Mercury notes that while Part 4 of the Commerce Act and Part 6 of the Telecommunications Act have similarities, Part 4 of the Commerce Act does not provide the same mechanisms as Part 6 as the Telecommunications Act for addressing network investments made under conditions of higher uncertainty and ahead of demand.

This example, however, suggests that the Commission should give thought to the application of its available tools so that its decisions enable investment in network capacity that would underpin confidence in the electrification of the economy.

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

Yours sincerely,



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⁶ Commerce Commission's Reasons paper, Chorus' initial regulatory asset base as at 1 January 2022 – Draft Decisions, date 19 August 2021, paragraph 2.49 states: *The background to the FLA is that it was expected that Chorus and the other LFCs that deployed fibre access networks under the Government's UFB initiative would incur financial losses during their initial period of operation. That is, despite the provision of partial funding via concessionary Crown financing, it was expected that the initial uptake of UFB services would generate insufficient revenue to cover the costs that the LFCs incurred during that period.*

