

electricity

January 2001

Traditionally there is an easing back into work in the New Year, but the electricity industry must hit the ground running in 2001. Unless industry solutions which satisfy the Government's objectives are sufficiently progressed by the end of February, the Government has stated that it will use its powers under the Electricity Industry Bill to regulate the industry. It is a Bill with bite!

Further Wakeup Call for the Electricity Industry

OVERVIEW

First there was the Ministerial Inquiry, which was followed by the Government's "Power Package" response. Then, in early December 2000, the final version of the Government Policy Statement was released and the Electricity Industry Bill was introduced into Parliament.

The Electricity Industry Bill:

- Provides the Government with regulation and rule-making powers to establish an Electricity Governance Board (EGB) should the industry fail to create its own electricity governance organisation which satisfies the criteria stated by the Government in its Policy Statement;
- Provides the Government with regulation and rule-making powers for aspects of the electricity industry even if the industry establishes its own electricity governance organisation; and
- Amends existing electricity legislation and gives specific new powers to the Commerce Commission.

GOVERNMENT POLICY STATEMENT

The changes from the draft version of the Statement (released in October 2000) are not substantial, but include:

- A new Guiding Principle requiring the quality of electricity services, in particular any trade-off between quality and price, to, as far as possible, reflect customers' preferences;
- A requirement that generators disclose reasons for hydro spill, as well as the amount, timing and location; and
- Clarification of the process for imposing fines for breach of market rules, with a specific

provision that any fines imposed are to take account of any awards or compensation made by the consumer complaints resolution scheme.

The Statement contains the Guiding Principles. These Guiding Principles set out the specific outcomes the Government is seeking, including that:

- Energy and other resources are used efficiently, in particular hydro spill is minimised;
- Risks relating to security of supply, in particular the risk of dry years and inadequate transmission and distribution security, are properly and efficiently managed;
- The full costs of producing and transporting each additional unit of electricity are signalled so that investors and consumers can make decisions consistent with obtaining the most value from electricity;
- Delivered electricity costs and prices are subject to sustained downward pressure;
- The quality of electricity services, in particular trade-offs between quality and price, should, as far as possible, reflect customers' preferences;
- Transmission losses and constraints are signalled to ensure that overall costs to the economy, including the costs of insufficient competition in local regions, are minimised; and
- Greenhouse gas emissions are minimised.

The rules to be developed by either the EGB or the industry-created electricity governance organisation must be consistent with these Guiding Principles and in particular the rules are to:

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vantagepoint

“The Bill is designed to encourage the electricity industry to develop its own solutions to ensure that electricity is delivered in an efficient, fair, reliable and environmentally sustainable manner to all consumers.”

- Promote and enhance competition wherever possible and, where it is not, seek outcomes that mirror, as far as possible, those that would apply in competitive markets;
- Facilitate and promote active demand-side participation;
- Ensure that the use of new electricity technologies and renewables, and distributed generation, is facilitated and that generators using these approaches do not face barriers; and
- Be consistent with Government policies on climate change and energy efficiency.

ELECTRICITY INDUSTRY BILL

The Bill has had its first reading under urgency and has been sent to the Select Committee. Closing date for submissions is 14 February 2001.

The Bill is designed to encourage the electricity industry to develop its own solutions to ensure that electricity is delivered in an efficient, fair, reliable and environmentally sustainable manner to all consumers. The Bill provides the Government with regulation and rule-making powers to be exercised if the industry fails to deliver those solutions.

The unusual and unprecedented structure of the regulation and rule-making powers has come in for some comment. These powers are set up in the following way:

- Regulations may be made to create:
 - fixed charges for domestic consumers; and
 - codes of access for beneficiaries of community and consumer trusts.
- Regulations and rules may be made for the wholesale market and transmission of electricity, *only if* the EGB is established and then either for transitional purposes or to implement the effect of an EGB recommendation.
- Regulations and rules may be made for:
 - a complaints resolution system for consumers;
 - prepayment meters;
 - the ability of consumers to choose a preferred electricity retailer;
 - transition arrangements for insolvent electricity retailers;
 - the connection of generation to distribution lines;
 - hydrospill;
 - hedge prices;

- dispute resolution procedures for disputes between industry participants; and
- the enforcement of electricity governance regulations, whether or not the EGB is established, but if it is established these regulations and rules can only be made after having had regard for any EGB recommendation.

The Bill also contains clauses which details the establishment of the EGB including:

- its functions;
- its role in relation to electricity governance regulations and rules;
- membership;
- financing; and
- accountability requirements.

These clauses will not be brought into force with the rest of the Bill. They will be held in abeyance for use only if the Government decides that the electricity industry has failed to establish an electricity governance organisation and deliver industry rules that meet the Government's expectations. If these provisions are brought into force, the EGB will be established as a Crown entity.

Whether, ultimately, the industry establishes an electricity governance organisation or the EGB is created by statute, there is potential for tension between any such body and individual industry participants. When any independent body has the right and indeed obligation to govern industry participants, there may be conflict with the concept of self-governance by the individual industry participants.

The Bill also provides for the accountability of either the EGB or any electricity governance organisation. The Minister may set objectives and outcomes for this organisation. Annual performance reports are required together with assurance audits by the Audit Office and the Parliamentary Commissioner for the Environment.

The Regulation and Rule-Making Powers

Regulations as subordinate legislation are made by the Governor General in Council on the recommendation of Cabinet and are not made by Parliament. This removes the opportunity for any Parliamentary debate on, or scrutiny of, the contents of the regulation or rule. Rules may be made for any of the purposes for which a regulation may be made. Ministerial rules are made simply by the Minister publishing a notice in the Gazette and the notice itself need not

contain the rules but must state where copies of the rules are available for inspection and purchase.

The Bill does not set out what the content of these regulations and rules might be. It only, in broad terms, outlines the areas the regulations and rules may cover.

A rule is not a regulation for the purposes of the Regulations (Disallowance) Act 1989 and, therefore, cannot be disallowed on the grounds set out in that Act. For some of the regulations, the safeguard of disallowing a regulation on the ground that it contains matter more appropriate to Parliamentary enactment has also been removed.

The regulation and rule-making regime in this Bill is set up in such a way that the ability for Parliamentary scrutiny and judicial challenge is minimal. It will be interesting to see whether the judicial implications of such a regime are debated and whether the current set-up survives the Select Committee.

Amendments to Existing Legislation

- As announced in the Power Package, the Commerce Commission is given:
 - power to impose price control over line companies including TransPower;
 - responsibility for administering information disclosure;
 - power to carry out valuations of fixed assets of every line owner;
 - power to review valuation methodologies; and
 - power to determine TransPower's pricing methodology.
- The Electricity Industry Reform Act 1998 is amended to:
 - revive the option of complying with ownership separation rules through a mirror trust; and
 - provide for distributed generation, particularly for renewable energy resources.
- The Electricity Act 1992 is amended to (amongst other things):
 - define the point of supply by reference to the boundary of a consumer's property;
 - address the definition of existing works; and
 - address the statutory right of access to land in order to maintain existing works.

Fixed Charges for Domestic Consumers

The section of the Bill concerning fixed charges for domestic consumers ensures that domestic consumers have available one or more tariff options, including fixed charges for electricity supplied at not

more than a specified amount calculated by reference to the total charge of the average or medium domestic consumer. What is clarified in the Bill, and which was not evident in the earlier announcements, is that the regulations may apply to *all* or *any* aspects of a tariff offered by persons (other than TransPower) who *convey* or *supply* electricity to or for domestic consumers (regardless of whether or not they contract directly with the domestic consumer).

These provisions allow for both the retail and the line charges to be subject to regulation in order to create a fixed charge.

Consumers Guarantees Act Amendment

Proposed amendments to the Consumers Guarantees Act 1993 have not eventuated in this legislation. It may be that the Government has realised that the quick fix solution of adding "electricity" to the definition of goods and services creates specific difficulties for the application of the Act's warranties and remedies. Several industry participants presented submissions on this point. With the introduction of a complaint resolution system for consumers (which may take the form of an Ombudsman) it may be that the need for the Consumers Guarantees Act to apply to electricity is no longer as pressing.

INITIATIVES CONSEQUENT UPON THE POWER PACKAGE

Commerce Commission

The Commission has initiated its own price control investigation of electricity line companies, under section 54 of the existing Commerce Act 1986. The investigation will be conducted with a view to putting the Commission in a position where it can report to the Minister of Energy on price control for electricity line services. In particular, the Commission proposes to investigate the degree to which electricity line function services are supplied in a market(s) where competition is limited and whether it is necessary or desirable for the prices of those services to be controlled in the interests of users, consumers, or the suppliers of the services.

A preliminary issues paper, released by the Commission in October 2000, outlined the steps the Commission proposes to take and the procedures it proposes to adopt in conducting its inquiry. The submissions received by the Commission were generally supportive of the Commission's approach. The Commission has since initiated preparation of two discussion papers (price control methodologies and asset valuation methodologies). It has issued Requests for

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Proposals from consultants to assist it in preparing material for the discussion papers, which it intends to release by 31 March 2001. Once submissions to the papers have been received the Commission proposes to prepare reports in relation to each of them. These reports will identify decisions to be made and issues that require further work, and recommend the future course of action (with an intended deadline of 30 June 2001).

The final stage in the Commission’s inquiry is to undertake further investigations, call for further submissions, hold conferences as appropriate and to consider what further action to take. The Commission has said that it will, throughout the inquiry, be as open and transparent as possible and make all submissions publicly available.

In considering asset valuation methodologies, the merits of Optimised Deprival Value (ODV) will again be debated extensively. The impact of ODV or any alternative methodology on pricing is such that the Commission’s pronouncements will be of significance.

Progress by Industry Participants

The Industry has established:

- a steering group for the implementation of a complaints resolution system for consumers, including an Ombudsman and codes of practice; and
- an Electricity Governance Establishment Committee for the consideration of governance, rationalisation of existing rules, and transport and distribution.

TIMEFRAMES

The Government has set some timeframes within which it expects the industry to have fronted up with its own solutions. In the absence of

acceptable solutions it has been made clear that the Government will step in.

- The first report of the Chair of the Electricity Governance Establishment Committee was provided to the Minister in December 2000.
- The Minister has requested a specific report by 28 February 2001 on progress in establishing the electricity governance organisation.
- Industry agreement on the consumer complaints resolution system and commencement of recruitment procedures for the principal office holder are required by 31 March 2001.
- The first annual report of the Governance Committee on whether and to what extent the outcomes the Government has specified in its Policy Statement have been delivered effectively is required in October 2001.

WHERE TO FROM HERE?

One of the key questions for industry participants to consider is what form of control they want over their industry.

The choices seem clear – either come up with industry solutions or accept quasi-governmental control.

In making this assessment, does the industry see the statutorily-created EGB operating as a traditional regulator (i.e. where industry members have the opportunity of dialogue with the regulator) or will the Government’s wide regulation and rule-making powers lead to a more prescriptive approach?

Another factor to consider is whether, to successfully meet the Government’s criteria and objectives, any industry-established electricity governance organisation will have to operate in the same way as a statutorily-created EGB.

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