From the Electricity Networks Association

Contribution to the Productivity Commission's Regulatory Institutions and Practices Inquiry

24 October 2013

The Electricity Networks Association makes this submission along with the explicit support of its members listed below.

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Top Energy Ltd
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Vector Ltd
Waipa Networks Ltd
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Executive summary

1. The Electricity Networks Association (ENA) welcomes the opportunity to contribute to the Productivity Commission's inquiry into regulatory institutions and practices. The ENA represents the 29 electricity network businesses (ENBs) in New Zealand. ENBs are subject to industry-specific regulation by the Electricity Authority (EA) and price regulation by the Commerce Commission (Commission).

2. In this submission, we draw on our experience of price regulation by the Commission to illustrate some issues relating to the design and implementation of regulation, specifically:

    - the importance of predictability and certainty in terms of the methods and calculations that the Commission uses to implement price regulation;
    - accountability issues and options for performance assessment of the Commission; and
    - the overlaps in the regulatory regimes enforced by the EA and Commission in the areas of pricing methodologies and information disclosure.

3. The legislative changes made to the regulatory regime under Part 4 of the Commerce Act in 2008 were intended to increase the predictability and certainty of price regulation applying to ENBs. This was through the adoption of input methodologies (IMs) that are intended to set out the rules, processes and requirements relating to the regulations. However, in practice significant gaps remain between what is covered by legislation and the input methodologies, and the practice of setting and reviewing price-quality paths. These gaps have at times been filled in ways that have surprised ENBs, and this lack of predictability and procedural accountability creates regulatory costs, which is ultimately detrimental to consumers. In some countries the development and implementation of regulatory rules are undertaken by separate entities, and this approach provides a useful test for the completeness of the rules: is there sufficient detail and clarity in the regulatory regime that another agency could implement the rules.

4. Linked with this issue of the predictability of the regulator's decisions are the issues of regulator accountability, governance and culture. These features (raised in the Productivity Commission's paper) all bear on the predictability of the regulatory outcomes. There is no structured way to engage with the Commission to find a solution to the lack of procedural and substantive accountability: while the IMs are subject to merits review, default price-quality paths (DPP) and information disclosure determinations themselves are not (customised price-quality path (CPP) determinations are). The ENA supports merits review as a useful discipline on regulator decision making, but notes that it does require support from the Courts for it to be a timely discipline, which has so far not been the case. Finding ways to jointly develop solutions to issues is also a way of improving input into regulatory determinations and providing a shared understanding of the outcomes (a current example of this is the ENA has initiated research projects on specific regulatory issues and the Commission is participating in those projects as an observer).

5. In addition, the ENA considers that there is a gap in the accountability of the Commission in terms of how easy it is to deal with, organisational culture, timeliness of

responses, issues it chooses to focus on and the quality of determinations made. This gap could be reduced through increasing the formal requirements for gathering and responding to feedback from stakeholders, and instituting regular, periodic performance reviews (e.g. by the Ministry of Business, Innovation and Employment).

6. Finally, the ENA notes that there are overlaps and links between the regulatory regimes of the EA and Commission relating to lines services. These overlaps are currently managed through legislative direction that the Electricity Industry Participation Code (administered by the EA) should take precedence over Parts 3 and 4 of the Commerce Act (enforced by the Commission); and a memorandum of understanding between the two parties that agrees how other issues will be dealt with. While it may be appropriate for regulations with different purposes (for example a social or distributional purpose, as compared to an efficiency purpose) to be enforced or administered by different agencies, the ENA considers that where regulations have a common purpose they should be within the mandate of a single agency.

7. The ENA would be happy to develop these lessons and insights into more developed case studies, if that is useful.

1. Introduction

8. The Electricity Networks Association (ENA) welcomes the opportunity to contribute to the Productivity Commission's (PC) inquiry into regulatory institutions and practices.[1] The ENA is pleased the PC is giving attention to this important issue of the design and practice of regulation in the economy.

9. The ENA represents the 29 electricity network businesses in New Zealand.

10. The ENA agrees with the PC that while some features of good regulatory design are likely to be universal, it is useful to classify regulators or regulation by institutional structure and/or regulatory purpose (e.g. economic or social).

11. In this submission we draw on the design and experience of price regulation of the electricity network service over the last twelve years to identify a small number of lessons and insights to do with the design and implementation of regulation. These topics are:

- the importance of predictability and certainty in the implementation of price regulation, and experience in trying to achieve those qualities;
- accountability and performance assessment of the regulator, various ways of achieving this and experience to date; and
- overlapping regulatory mandates.

12. The ENA would be happy to develop these lessons and insights into more developed case studies, if that is useful.

13. In section 2 we provide a brief history of price regulation of the electricity lines service in order to provide context for the above topics.

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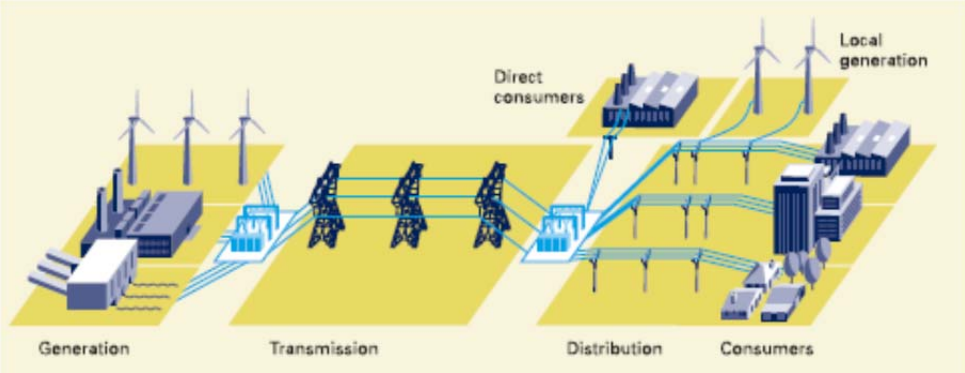
[1] Productivity Commission, *Regulatory Institutions and Practices: Issues Paper*, August 2013

2. Brief history of price regulation of the electricity lines service

15. The electricity sector can be characterised as comprising the following four functions, which are illustrated in the figure below:

- Generators, that generate the electricity, and which may be connected to the transmission system or directly to a distribution network;
- A transmission network, that transports the electricity from the point of generation to distribution networks;
- Distribution networks, that transport the electricity from (and to) the transmission network to consumers (including households and businesses); and
- Retailers, who manage the interface with the consumer (not shown explicitly in the illustration below).



16. Prior to 1998, the distribution networks and retailer functions in most cases resided in the same businesses; transmission was a standalone business; and the generation businesses were generally also standalone, but included a limited amount of retail.

17. With the passage of the Electricity Industry Reform Act 1998 the combined distribution network and retail businesses were required to separate these two functions. In practice most of these businesses divested their retail businesses, and in most cases these retail businesses were purchased by generation businesses. We refer to the remaining distribution network businesses as electricity network businesses (ENBs), which in most cases became standalone network businesses.

18. At the time of separation ENBs were subject to information disclosure requirements, but not price regulation. In 2001, Part 4A of the Commerce Act was passed, which imposed a form of price regulation on ENBs, the key features of which were:

- the Commerce Commission (the Commission) was empowered to set "price thresholds" for the electricity lines service provided by the ENBs;
- an ENB could set prices above its price thresholds, but if it did it opened itself to the possibility that the Commission would investigate its pricing practices, and if it considered it appropriate, the Commission could set enforceable price caps for the ENB; and

- these arrangements were supported by the continuation of an enhanced set of information disclosure requirements.

19. The Commission at the time was responsible for administering the Commerce Act, with its work being dominated by competition policy issues, and the Fair Trading Act. It did not at the time administer price regulation for other sectors.

20. In 2004, the Electricity Commission (EC) was formed. The EC had a wide ranging regulatory mandate within the electricity sector. In relation to ENBs it was empowered to impose price constraints of various forms in relation to the electricity lines service, and it did so (via the Minister of Energy) in the form of the low fixed charge tariff regulations. These regulations require that an ENB provides a tariff option to residential consumers that has a daily fixed charge no greater than 15c plus GST per day, and that the variable portion of the tariff crosses over other tariff options at no lower than average level of consumption (deemed to be 8,000 kWh per annum in most parts of New Zealand). These regulations remain in force today.[2] The EC was also empowered to review the pricing methodologies of ENBs and, if needed, to determine those pricing methodologies.

21. In 2008, Part 4A was replaced with what is now Part 4 of the Commerce Act, following a review by the then Ministry of Economic Development. That review in turn was triggered by concern on the part of the Ministry and the sector as to how Part 4A was being implemented (which we discuss in the later sections). The key features of the Part 4 regime are:

- price control is imposed on the electricity lines services provided by ENBs (and on other services such as gas network services and electricity transmission) and the Commission is empowered to administer it.[3] Consumer-owned ENBs are exempt from these price control provisions;
- the price control mechanisms applicable to ENBs include a default price-quality path (DPP) that applies to all ENBs by default, and a customised price-quality path (CPP) that can be triggered by an ENB should they be dissatisfied with the DPP; and
- information disclosure requirements, that have been significantly revised and are now much more detailed than hitherto.[4]

22. In 2010 the EC was disbanded, with many of its functions taken up by the newly formed Electricity Authority (EA). Most of the price constraint and pricing methodology powers of the EC that relate to ENBs were transferred to the EA.

23. In the following sections we draw out lessons and insights that have emerged over the last twelve years in relation to:

- the importance of predictability and certainty in the implementation of price regulation, and experience in trying to achieve those qualities;

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2 Electricity (Low Fixed Charge Tariff Option for Domestic Consumers) Regulations 2004

3 Price control only applies to non-exempt ENBs.

4 Information disclosure requirements apply to all ENBs.

- accountability and performance assessment of the regulator, various ways of achieving this and experience to date; and
- overlapping regulatory mandates.

3. Predictability and certainty

24. The issue of predictability and certainty emerged as an issue with the price thresholds regime under the then Part 4A early on in its implementation. ENBs are capital-intensive businesses with assets (e.g. poles, cables, ducts and transformers) that have physical lives of around 40 to 60 years. Most of these assets have limited value in alternative use (that is they are sunk with respect to the electricity lines service). Management and boards of these businesses work to long time frames and large investments are required at periodic intervals. In order for this long term planning and decision-making to operate efficiently, and for these businesses to be willing to commit to the necessary long-term investments, the way in which the business is allowed to price its services needs to be predictable and certain.

25. The combined 29 ENBs have assets of $9.3b, annual revenues of $1.5b, and undertake capital expenditure of approximately $0.6b each year.

26. Predictability and certainty feature prominently in the regulatory economics literature and in the concerns of those that are regulated.[5]

27. We mean by "predictability" that the regulated entity is able to predict, for a given set of circumstances, how to calculate the prices or the limits on prices, that an ENB is able to charge over the medium to long term.

28. We mean by "certainty" that the regulated entity has a high level of confidence that the regulator will use the predicted methods and calculations to set regulated prices, and therefore the regulated entity will know the risks they are exposed to.

29. Both of these features are critical to an efficient form of price regulation.

3.1 Progression of Part 4 relative to Part 4A

30. Under Part 4A, ENBs found that the regulatory regime was implemented in a way that was neither predictable nor certain. Further, there were no mechanisms under Part 4A to hold the regulator accountable to implement a regime that improved predictability and certainty.

31. For example, under the Part 4A regime two key regulatory determinations were:

- setting the price thresholds, and deciding the methods to be used to make that determination; and

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5 See for example: Levy, Brian & Spiller, Pablo T, 1994, "The Institutional Foundations of Regulatory Commitment: A Comparative Analysis of Telecommunications Regulation," *Journal of Law, Economics and Organization*, Oxford University Press, vol. 10(2), pages 201-46, October. Yarrow, George & Decker Christopher, 2008, *Reflections on policy issues raised by next-generation access networks in communications*, Regulatory Policy Institute, 2008.

- undertaking an investigation of an ENB that had breached the thresholds and determining whether or not to place that ENB under price control, and deciding the methods that would be used to make that determination.

32. In both of these cases the regulator chose to develop the methods for making these determinations in the course of making the determination itself. Further, these methods changed from one determination to the next. Thus it was not possible to predict, for a given set of circumstances, the methods and calculations that would be used to set the price thresholds, or the method and calculations that would be used to investigate an ENB and determine whether or not the ENB would be placed under price control.

33. The Part 4 regime aimed to improve predictability and certainty with the introduction of a requirement on the regulator to publish "input methodologies" (IMs), the purpose of which is (section 52R):

> *The purpose of input methodologies is to promote certainty for suppliers and consumers in relation to the rules, requirements, and processes applying to the regulation, or proposed regulation, of goods and services under this Part.*

34. And (section 52T(2))

> *Every input methodology must, as far as is reasonably practicable, -*
>
> *(a) set out the matters listed in subsection (1) in sufficient detail so that each affected supplier is reasonably able to estimate the material effects of the methodology on the supplier; and*
>
> *(b) set out how the Commission intends to apply the input methodology to particular types of goods or services; and*
>
> *(c) be consistent with the other input methodologies that relate to the same type of goods or services.*

35. The regulator developed its IMs over an intensive two year period and published the resulting IMs in late 2010. The ENA considers this requirement to publish IMs has improved the predictability and certainty of price regulation applying to ENBs. However, significant issues have arisen since then in the implementation of Part 4 that have highlighted gaps in the expectations of the ENBs and the regulator as to the appropriate scope of the IMs, and appropriate implementation of the regime more widely. Two examples illustrate this gap in expectations.

36. First, the regulator decided to not develop an IM to cover the methods for resetting prices under the DPP. The ENA and a number of ENBs contested this approach, arguing that the purpose and requirements of the IMs could not be achieved if there was such a fundamental gap in the IMs. The issue of whether the law required the regulator to publish such an IM was tested in the Courts, which found on appeal in favour of the regulator that such an IM was not required legally. Thus ENBs are now in a position that, a year out from when the existing DPP needs to be reset, they do not know the methods that will be used to undertake that reset.

37. The second example has to do with how the regulator deals with issues on which it has made statements and set expectations, but for which no IMs have been published. This

example emerged following the Canterbury earthquakes where the main ENB in that region, Orion New Zealand Ltd, decided to apply for a CPP to reset its prices and service quality levels as a consequence of that very difficult period. All ENBs understood from statements made by the regulator in the development of the IMs (including in the IM Reasons Paper that was issued by the Commission) that an ENB would be able to recover from consumers (after the event) its additional network costs and business interruption costs (losses in revenue) from a catastrophic event. The logic for this approach is sound. ENBs perceive that it is not cost effective to fully insure lines and cables and it is difficult to procure appropriate insurance. For these reasons, full insurance cover is not in place for such events, nor was there any explicit compensation in the price-setting process for an ENB to self-insure these risks.

38. In the regulator's draft determination[6] on Orion's CPP application it has decided to not allow Orion to recover its full network costs or any of its business interruption costs in future prices. Thus to Orion's and all ENBs' surprise, the understanding they perceived to be in place proved to be incorrect, and the regulator has not explained (and is not required to explain) what it did mean by the statements in the IM Reasons Paper that led to ENBs holding a different understanding.

39. The ENA views this issue as a matter of how the regulator fills in the inevitable gaps that emerge in practice between what is stated explicitly in legislation and IMs, and what is understood by the industry to be the regulator's position on certain matters. The Commission endeavours to provide some clarity through its rationale (e.g. Reasons Papers) although this is not mandatory and does not have the status of the legislation or IMs.

40. This is a matter of how the regulator performs when faced with a degree of ambiguity as to what the "rules" state it must do. Viewed from this perspective it becomes a matter of regulator accountability, and in this instance the ENA considers it raises questions of how the regulator is governed and its culture. We discuss these issues of accountability, governance and culture in section 4 below.

41. One possible way of improving the scope of the Commission's rule-making activities would be to separate the implementation of the rules (or IMs) from their formulation. This is the approach taken in Australia where the Australian Energy Market Commission (AEMC) makes rules for implementation by the Australian Energy Regulator (AER). Such a step may not be warranted given the economic size of New Zealand, but the principle provides a useful test of the completeness of the Commission's rule-making activities: is there sufficient clarity and direction in the rules that they could be implemented by a separate party?

3.2 Summary

42. Predictability and certainty are critical features of any regulatory price regime. Over the last twelve years the regulatory price regime applying to ENBs has undergone two

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6 *Orion New Zealand Limited Customised Price-Quality Path Draft Determination,* September 2013 (www.comcom.govt.nz/regulated-industries/electricity/cpp/orion-cpp/)

legislative changes; first in 2001 when what was an information disclosure regime was broadened to include "price thresholds" and the possibility of the regulator placing an ENB in breach under price control, followed by a reworking of that regulatory price regime in 2008 to introduce, amongst other things, a higher level of predictability and certainty.

43. Thus far the ENA considers the legislative changes in 2008 under Part 4 have increased the predictability and certainty of price regulation applying to ENBs. However, in practice it has become evident that there remain significant gaps between what legislation and the regulator's IMs cover, and the content of important decisions that form part of a price determination. A useful test of the completeness of rules or regulations is whether they provide sufficient clarity and direction that they could be implemented by another party. The current IMs fail that test.

44. The Commission has argued that maintaining flexibility and discretion is more important than providing regulatory certainty. This approach places pressure on the accountability of the regulator, and on the way in which the regulator is governed and its culture, illustrating that these features form an important aspect of the predictability and certainty of the overall regime. We discuss these issues of accountability further in the next section.

4. Accountability and performance assessment of the regulator

45. The PC's Paper identifies three forms of accountability; financial, procedural and substantive. We discuss the second two in this section.

4.1 Procedural issues

46. Probably the most concerning procedural issue for ENBs under Part 4A was not knowing in advance of a determination being undertaken (e.g. the setting the price thresholds, or an investigation as to whether price control would be imposed) the methods the regulator would use to make the determination. When setting prices under regulation it is usual to reference prices to some measure of cost. The relevant costs, however, can be specified and measured in a number of different ways using a number of different methods, and the difference in results from differing methods can be substantial.

47. Thus without knowing the methods that are to be used, it is not possible to establish an informed view of the likely result. For example, for an ENB that was the subject of an investigation under Part 4A it was not possible to calculate in advance of the investigation with any confidence whether the ENBs price levels would result in its breaching the regulator's expectations of a reasonable profit level, or not. Procedurally that seemed flawed and unreasonable, but under Part 4A there was no legal mechanism to require the regulator to adopt a better procedure.

48. Part 4 addressed this procedural issue to some extent by including a legislative requirement that the regulator must publish IMs, and must use those IMs in making its determinations. To the extent that the IMs cover all substantial points in a determination, this requirement has addressed this procedural issue. However, where there are substantive gaps (e.g. not knowing the method to be used for the DPP reset; how an ENB would transition from a CPP to a DPP, or a gap in understanding as regards the allocation of catastrophic risk) there continues to be no means to engage with the regulator in a structured and purposeful manner to find a solution workable for both the regulator and those subject to regulation.

49. One way to improve input into regulatory determinations and provide a shared understanding of the outcomes is to find ways to jointly develop solutions to issues. A current example of this is that the ENA has initiated research projects on specific regulatory issues and the Commission is participating in those projects as an observer.

50. An additional procedural concern relates to the lack of any guidelines relating to enforcement under Part 4. Part 4 is rule-based: the price path provides a bright line, while the service quality is specified as a cap. However, there are no guidelines around how the Commission will enforce these rules if an ENB does not comply. The nature and extent of breaches of the DPP, CPP or information disclosure can very significantly depending on the circumstances that led to the breach. It is therefore appropriate that the Commission provide guidance on its intended approach to and process for responding to breaches such that regulated suppliers know how the Commission will undertake its enforcement activities relative to the nature and extent of any breach.

4.2 Strategic leadership

51. The practice of regulation requires significant discretion on the part of the regulator, because it is not practical to legislate the required level of detail to respond to all situations. Economic regulators have a limited set of resources with which to address a wide range of potential issues. Where the regulator chooses to place its effort has a significant effect on the outcomes for regulated entities.

52. While the purpose of the relevant legislation provides guidance on these choices, the scope of regulator discretion means that a change in the leadership of regulator (e.g. change of Commissioners in the case of the Commerce Commission) may result in a significant change in regulatory approach. This places pressure on the appointment process for the regulator. Improvements to the selection and appointment processes for regulators would be valuable, as would improved accountability provisions (as suggested below) for performance over time.

4.3 Substantive issues

53. Under Part 4A there was no mechanism to test the substance of the regulator's determination with the purpose of the regulation. ENBs found this situation very frustrating.

54. Part 4 provides for merits reviews in some aspects, such as the IMs and CPP determinations, but not others, for example the setting of the DPP or information

disclosure requirements. Some aspects of the initial IMs that were published in later 2010 were appealed (within twenty working days of them being published) and the result of that appeal remains outstanding. Thus the full cycle of the appeal process has yet to run its course. It has however proven to be a very slow process, taking thus far over two and half years with still no decision.

55. The ENA supports the merits review approach to strengthen the accountability of the regulator. To be a timely discipline it does require the necessary support from the Courts, which in this first set of reviews has been slow.

4.4 Other accountability issues

56. From the perspective of those that are regulated, there appears to be a gap in the accountability framework on issues of how the regulator goes about its business. In practice a regulator has (appropriately) a wide discretion as to how it performs its tasks on a day to day business. The choices it makes and the culture of the organisation affects how easy it is to deal with, the timeliness of its responses, the issues on which it focuses its scarce resources, and the quality of determinations made. Ultimately those leading the regulator (i.e. the Commissioners) are called on to exercise significant judgement on these matters. What seems to be missing is a structured way to engage with the regulator on these matters in a way which enables honest feedback to be provided and which places some obligation on the regulator to take such feedback into account. The ENA considers this gap in accountability could be reduced in possibly two ways.

57. The first is for the Commission to incorporate greater feedback and reporting processes in its annual cycle, that involve direct engagement with stakeholders and an obligation on the Commission to report back to stakeholders on how it has responded to feedback. The Commission has of recent years conducted stakeholder surveys, which we think is a step in the right direction.

58. The second is for the performance of the regulator to be reviewed periodically, for example every five years. We consider the Ministry of Business, Innovation & Employment (MBIE) to be the appropriate review agency, or that MBIE appoints a reviewer. As far as we are aware the performance of the Commission has not been reviewed by an external party since it was allocated price regulation functions in 2001 for electricity and telecommunications, and these responsibilities have grown significantly since then. The ENA considers periodic reviews (e.g. every five years) would be a useful addition to the accountability framework applying to the Commission.

5. Overlapping regulatory mandates

59. There is an overlap in the functions of the Commerce Commission and the Electricity Authority with regard to the regulation of lines services. For ENBs the areas of overlap relate to pricing methodologies and information disclosure requirements. It is not apparent why these areas of overlap exist, and they create unnecessary cost and complexity for both regulator and those subject to regulation, as well as the potential for inconsistent outcomes. This section describes the background to the current

regulation of pricing methodologies and suggests that where regulations have a common purpose they should be within the mandate of a single regulatory agency.

60. The Electricity Industry Act 2010 established the EA and sets out the framework within which it works. Section 32 of that Act sets out the possible content of the Electricity Industry Participation Code (the Code). Section 32(2)(b) states:

> *The Code may not – purport to do or regulate anything that the Commerce Commission is authorised or required to do or regulate under Part 3 or 4 of the Commerce Act 1986 (other than to set quality standards for Transpower and set pricing methodologies (as defined in section 52C of that Act) for Transpower and distributors)*

61. This section and section 52T of the Commerce Act, which excludes the Commission from setting pricing methodologies where the EA has the power to, describe the overlap between the functions of the Commission and the EA with respect to regulating the price of electricity lines services.

62. This overlap was first created with the establishment of the Electricity Commission and its precise treatment has varied since that time. The Electricity Amendment Act 2004 created the ability for the EC to recommend regulations "providing for a price methodology or methodologies for recovery of the revenue requirements of electricity distributors" (s.9(9)). At that time, the Commission administered the price thresholds regime relating to ENBs, but was not responsible for administering price regulation for other sectors.

63. Parliament recognised the overlap it was creating and inserted a requirement into the Commerce Act (s.57MA), which sets out the powers of the Commission, directing how this overlap should be treated. This required the Commission to take account of any electricity governance rule or regulation, or decision made under those rules and regulations that related to the areas of overlap.[7] It also required the EC to advise the Commission after recommending any regulation or rule, or making a decision that was likely to affect the Commission's powers.

64. At the same time, the Government also requested the EC and the Commission develop a memorandum of understanding on how they would operationalize their respective roles. This requirement was set out in the Government Policy Statement on Electricity Governance (October 2004).

65. The Commerce Act was further amended to create a provision that would allow the transfer of the Commission's responsibilities under Part 4A to the EC by Order in Council if the Minister of Energy was satisfied that to do so would result in more efficient and effective achievement of Part 4A or the Electricity Act as it applied to ENBs or lower compliance costs in distribution and transmission markets (s.57DD).

66. It seems then that Parliament had specifically created the overlap in mandates, and chosen to give precedence to the EC and its regulatory framework; it had gone as far as

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[7] Specifically, the areas of overlap noted are Transpower's quality standards, pricing methodologies applying to any lines owner and any levy payable by Transpower and ENBs to the EC.

to allow for a relatively easy transfer of the Commission's powers to the EC. This appears to be a relatively robust consideration of the issues that might arise from the overlap. The reason for separating the two functions is not clear, but may have related to the historical basis of the two regulators, and the relatively light-handed approach of the Commerce Commission at that time.

67. In 2008, the Commission's role in terms of regulating prices for electricity lines services was changed to a price control regime. Part of the method for regulating prices for a particular service is the specification of input methodologies, which detail rules, processes and requirements relating to the regulation. The input methodologies included pricing methodologies. This change deepened the scope of the overlap between the functions of the Commission and the EC and caused the Government to require further protocols on their coordination. The resulting memorandum of understanding specifically noted the dual responsibility for an electricity distribution pricing methodology, and included a pledge to coordinate initiatives in this and other areas of overlap.

68. In 2010, this area of distinct overlap was removed as the Commission was explicitly excluded from making pricing methodologies for ENBs and Transpower for as long as the EA has this power (s.52T(1)(b)).

69. The Commerce Act retains the provisions requiring the Commission to take account of any provision of the Code, or decision under it, relating to pricing methodologies for ENBs (s.54V(4)(b)). It does not, however, have any provisions allowing the transfer of functions between the two agencies.

70. Precedence continues to be given to the EA's decisions and powers. The question is whether this still makes sense given the deepening and broadening powers of the Commission with respect to price regulation.

71. Part 4 of the Commerce Act is intended to promote outcomes consistent with those produced in competitive markets, such that specific incentives and restrictions are placed on suppliers of regulated goods and services. Pricing methodologies are explicitly within this purpose, and the Commission has the power to develop them for other regulated goods and services.

72. It is not apparent that any good reason exists to separate the development of pricing methodologies for some regulated services to a different regulator than the one responsible for the setting of price or revenue levels. It is more complex and costly for both the regulated suppliers and the regulators themselves to deal with and coordinate between two different decision-makers, and potentially could give rise to inconsistent decisions. In general, where an aspect of regulation is consistent with the purpose of the primary agency regulating price (the Commerce Commission) it should be administered by that agency.

73. Where the regulation has some other purpose then there may be good reason to provide for it separately. However, good practice would be to specify the purpose of that regulation. This applies for example, to the regulation of tariffs under s.113 of the Electricity Industry Act. The Minister is able to recommend regulations for the purpose of:

(a) Regulating the type of tariffs for fixed and other charges that must or may be offered to domestic consumers; and

(b) Promoting the fair treatment by distributors and retailers of domestic consumers and small businesses; and

(c) Enabling the protection of rural consumers, and consumers supplied with electricity from an alternative source under section 105, from unfair rates of change in the prices charged to them.

74. While the first prong of this purpose statement is somewhat vague, given the context of the rest of the purpose and examples of regulations made under this provision (which include the low fixed charge tariff regulations), the ENA infers that these regulations are intended to have social or distributional goals. Such goals may differ from those of Part 4 of the Commerce Act, which relate to efficiency and a benefit to consumers overall. However this rationale does not apply to the development of pricing methodologies for lines services.

75. In addition to this specific overlap, there have been occasions when the industry regulator has made policy recommendations that are not aligned with the Commission's regulatory regime. For example:

- the EA released a transmission pricing methodology (TPM) that would have given rise to volatility in transmission costs to ENBs. Transmission costs are a pass-through for non-exempt ENBs, and the way the DPP is structured for pass-through costs does not allow for volatility. This meant that the proposed TPM would not work with another part of the regulatory regime; and
- the EA proposed using the structure of its levy to create incentives for participants, without understanding that these are a pass-through cost for non-exempt ENBs. This means that ENBs are not directly affected by EA levies.

76. Such disconnects between the regulatory regimes impose costs and impair overall effectiveness for no apparent advantage.

5.1 Summary

77. An overlap in regulatory mandates creates additional cost and complexity for both those subject to regulation and regulators; it also creates the possibility of inconsistent decisions. The Electricity Authority and Commerce Commission have overlapping mandates in areas related to the regulation of lines services.

78. This is currently managed through:

- legislative direction in section 54V of the Commerce Act that precedence is given to the Code and decisions made under it; and
- a memorandum of understanding between the Commission and the EA that acknowledges section 54V and agrees how other issues will be dealt with, for example, the EA will "take into account…information disclosure requirements imposed by the Commission". The memorandum also agrees that the EA will consult the Commission on certain matters.

79. While it may be appropriate for regulations with different purposes to be administered by different agencies, such as those with social or distributional goals rather than efficiency goals, the ENA suggests that where regulations have a common purpose they should be within the mandate of a single agency. In this case, the Commission should have responsibility for price methodologies and other price-related regulation where the purpose is to promote efficient market outcomes.