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20 August 2020

Commerce Commission

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Infrastructure New Zealand is the peak industry body for the infrastructure sector and promotes best practice in national infrastructure development through research, advocacy and public and private sector collaboration. Infrastructure New Zealand members come from diverse sectors across New Zealand and include infrastructure service providers, investors, and owners.

This submission represents the views of Infrastructure New Zealand as a collective whole and may not necessarily represent the views of individual member organisations.

## **Infrastructure New Zealand submission on Aurora Energy's investment plan for a Customised Price Pathway**

Infrastructure New Zealand supports Aurora Energy's application for a Customised Price Pathway (CPP) and their investment plan.

The CPP is a necessary step to ensure Aurora's vital assets are maintained and that customers in Otago have a reliable and efficient supply of electricity.

We believe the price increases to consumers, while high, are reasonable, given that existing charges are low in comparison to many other distributors.

We recognise that this CPP is necessary due to the critical importance of a safe, reliable and sustainable electricity network which meets the needs of current and future users. We encourage the Commerce Commission to continue assessing the asset management practices of distributors to avoid similar situations in future.

**Beneficiaries of infrastructure should pay wherever possible**

Delta, which operated Aurora's assets on behalf of Dunedin City Council, was clearly challenged to responsibly manage Aurora's electricity distribution network.



The result was that consumers and Aurora's shareholder experienced cheaper electricity prices and reliable dividends for much longer than their neighbours.

We believe that users of infrastructure should, wherever possible, shoulder the costs of infrastructure which they benefit from, in proportion to the benefits received.

In this case, users of Aurora's networks are the appropriate, efficient, and fair party to shoulder the costs of the work now needed.

### The costs of the CPP are noteworthy, but not unreasonable

Electricity users in New Zealand generally receive reliable and highly renewable electricity at some of the lowest prices in the world<sup>1</sup>.

Aurora's CPP will increase electricity distribution charges by 48-66%. However, these charges are typically less than half of an electrical bill and, in Aurora's instance, have been kept artificially low through lack of investment.

While distribution costs vary between 7.4 and 21.6 c/kWh across the country (averaging 11.1 c/kWh), Aurora currently charges between 8.7-9.6 c/kWh<sup>2</sup>. Moving Aurora's line charges from the bottom half of providers to a higher level may be appropriate given the scale of additional investment required.

Aurora is proposing to invest \$130-140 million each year for its CPP<sup>3</sup>, equivalent to roughly 1% of Otago's regional GDP per year (\$13.6 billion)<sup>4</sup>. We believe this amount is proportionate relative to the amount of economic activity that relies on a stable and reliable distribution network.

The Commerce Commission estimates that the net total electrical bill increase for average customers will be +10-17% or between \$240-360 per year<sup>5</sup>.

It is also important to consider the 'opportunity cost of inaction'. Aurora's assets are in poor condition and continuing to deteriorate. Failure to pay for this investment now will likely lead to larger costs in future. Prudent increases now will be necessary for long-term well-being.

We believe Aurora's proposed price increases are reasonable and the benefits to its network far outweigh the costs.

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<sup>1</sup> New Zealand Government (2019) *Electricity Price Review Final Report*

<sup>2</sup> Ministry of Business, Innovation and Employment (2020) *Quarterly Survey of Domestic Electricity Prices to 15 May 2020*

<sup>3</sup> Aurora Energy (2020) *Customised Price-Quality Path Consultation Report*

<sup>4</sup> Stats NZ (2020) *Regional Gross Domestic Product – RNA, Gross domestic product, by region and industry (Annual-Mar)*

<sup>5</sup> Commerce Commission (2020) *Have your say on Aurora Energy's investment plan – Key issues paper*



### Aurora's needs

Aurora and the Commerce Commission have made it clear that significant investment is needed over many years to firstly stop the deterioration of Aurora's assets and secondly to upgrade them to recommended standards.

It is possible that Aurora will need more than one regulatory period to do this work. It may also be preferable for customers to have all the major repairs and maintenance to the network done during a concentrated multi-year period.

Certainly Aurora, customers, and the Commerce Commission would benefit from going through the contentious CPP process as few times as possible.

We encourage the Commission to consider what mix of CPP and/or DPP will result in the best outcomes for both users *and* the long-term health of the distribution network.

### Future system requirements and opportunities

Over the next decades, we expect that distributors will need to invest in their networks to: increase resilience to earthquakes, flooding, storms, and more; allow for higher demands and different demand patterns due to electric vehicles, electrification of process heat, etc.; and allow for distributed generation to feed electricity into the network from homes and businesses.

It is unclear if Aurora will have the time or resources to adequately address these future-proofing challenges through its CPP.

We have a general standing concern that current DPP settings may not allow for the long-term planning, flexibility, or significant up-front investment needed to make upgrades to New Zealand's distribution infrastructure.

We encourage the Commission to work with distributors to ensure they are not caught flat-footed by changes in electricity demand, technology and opportunities.

### Asset management and regulation

New Zealand's historical investment in infrastructure in the post-war period has paid dividends as users have paid little for infrastructure that was largely functioning as required. However, governments and institutions, in some instances, have deferred important infrastructure maintenance in favour of cost savings.

These challenges are not unique to electricity sector and affect our roads, rail, schools, hospitals, and water infrastructure to vary degrees.

It is possible that Aurora's failures are not unique among electricity distributors.



To this end, we are pleased that the Commerce Commission is taking a more active role in reviewing distributor's asset management practices<sup>6</sup>.

We believe this work to be very important, as conventional means of regulating prices and quality may not fully capture the state and long-term health of assets.

We encourage the Commission to continue this work, which may prevent future situations like Aurora's.

### Flexibility in regulation

A CPP is an exceptional process that may be long, expensive, and contentious. It is likely best suited to truly exceptional investments, such as Orion faced in the wake of the Christchurch earthquakes.

For situations such as Aurora's, a CPP would ideally not be necessary.

Increasing prices by 48-66%, while dramatic, is not unacceptable. Under good scrutiny, it is possible that distributors should be able to use a DPP to achieve these increases.

Regardless, we observe that a CPP is an exceptional process with financial and reputation costs, and an alternative arrangement such as a more flexible DPP may reduce the barrier to entry for distributors to undertake significant investment.

We are concerned that the burden faced by distributors in seeking a CPP may discourage other distributors from coming forward to seek the significant upgrades they need.

### Summary

We believe Aurora is justified in seeking a CPP to raise distribution prices to fund its much-needed network repairs and investments. Indeed, we are more concerned that the CPP process will not provide Aurora enough flexibility and funding to make the upgrades and future-proofing for the next century's needs.

We encourage the Commerce Commission to continue assessing the asset management practices of distributors to avoid similar situations in future.

If you have any questions regarding this submission, please contact Infrastructure New Zealand's Policy Director, Hamish Glenn, at [hamish.glenn@infrastructure.org.nz](mailto:hamish.glenn@infrastructure.org.nz).

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<sup>6</sup> Commerce Commission (2019) *Open letter – Our programme of work for reviewing electricity distribution businesses asset management practices*