Treasury Report: MOM Bill: Notes for Second Reading Speech

Date: 8 June 2012

Action Sought

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<td>Minister of Finance (Hon Bill English)</td>
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<td>Associate Minister of Finance (Hon Steven Joyce)</td>
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<td>Minister for State Owned Enterprises (Hon Tony Ryall)</td>
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Contact for Telephone Discussion (if required)

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<th>Name</th>
<th>Position</th>
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<td>[Withheld under s. 9(2)(a)] ✓</td>
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<td>Chris White</td>
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Minister of Finance’s Office Actions (if required)

None.

Enclosures:  
(MOM Bill: notes for second reading speech:2365585)  
(FEC briefing material on comparative debt statistics (May 2012):2335052)
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Executive Summary

We enclose some material for use in developing second reading speeches. With a very few exceptions, this is material already provided to FEC during its involvement with the Bill.

We also enclose information provided to FEC comparing New Zealand’s central government gross and net debt, and a variety of other indicators. We are reviewing other data to see what is available; we would like to discuss this further with Minister Ryall on Monday at our 9.30 a.m. meeting.

Recommended Action

We recommend that you note the attached documents before you meet with Treasury officials on Monday 11 June 2012.

Chris White
Manager, Commercial Transactions Group

Honi Tony Ryall
Minister for State Owned Enterprises
Execution goal #2 – the Government has to be satisfied that industry-specific regulations adequately protect New Zealand consumers

10. Competition between firms is the primary form of protection for consumers in New Zealand. Competition is safeguarded through general competition law in the Commerce Act 1986, which is enforced by the Commerce Commission.

11. The regulatory regime that is most relevant to consumers in the context of the Mixed Ownership Model is the electricity sector. The Government reviewed this sector thoroughly in 2009 and made the changes through the Electricity Industry Act 2010 to strengthen competition and improve security of supply. Those changes included:
   • disestablishing the Electricity Commission and setting up the Electricity Authority whose statutory objective is to ‘promote competition in, reliable supply by, and the efficient operation of, the electricity industry for the long-term benefit of consumers’;
   • providing customer compensation and a floor on spot prices during public conservation campaigns;
   • providing for “virtual asset swaps” (by way of long-term contracts) between the SOEs and transferring Tekapo A and B power stations from Meridian to Genesis; and
   • providing for more standardised line tariffs.

12. Beyond those protections, consumers have access to the Electricity and Gas Complaints Commissioner. The Commissioner has jurisdiction over complaints up to $20,000, or $50,000 with the agreement of all parties. Common issues include billing, disconnections, damaged property and switching companies. The Commissioner can also consider complaints about actions of staff or contractors while on land, as well as access to and use of land on which there is electricity or gas equipment.

13. To encourage competition in the electricity market, the Electricity Authority is running the “What’s My Number” campaign, and continues to provide funding for the Ministry of Consumer Affairs’ Consumer Powerswitch website. From June 2011 to the end of February 2012, 306,711 consumers switched power suppliers. The Authority has estimated the average annual household savings available by switching to the cheapest retailer in the region, is $150: those switches, then, represent domestic savings of around $46M. Of course, this switching activity will also provide incentives for the electricity companies to compete on price.
There is not adequate consumer protection in the electricity market, and therefore prices will increase

81. Under the SOE Act, the proposed MOM companies are already expected to act commercially and generate profits for the shareholder. Electricity prices are not constrained by the Act’s corporate social responsibility provisions, but by market regulation and competition between companies. Competition law and electricity market regulation will continue to protect consumers of electricity in New Zealand, irrespective of company ownership.

82. The regulatory regime and the “What’s My Number” campaign are covered in more detail at paragraphs 10 - 13, at page 6.

83. Molly Melhuish has suggested that the average residential consumer in a contract with a SOE gentailer will be paying $240 less per annum than if they are supplied by a privately-owned firm. As at February 2012, that number appears broadly accurate (Ms Melhuish’s calculation significantly understated the number of customers of Mercury Energy; although that overstates the gap between SOEs and public companies, the corrected calculation does not materially decrease the $240 figure). Having said that:
   • there is a competitive market, and a significant number of customers switch electricity retailers each month, helped along by the Government funded “What’s My Number” campaign;
   • as you would expect, prices move around to reflect competition between retailers. A snapshot will give you a picture, but only at a moment in time. Power companies do reduce their tariffs in the face of competitive pressure – for instance, Contact increased its prompt payment discount from 12% to 22% after it had lost a significant number of customers over a period of time. In addition, companies do not only compete on price;
   • the fact that the average residential consumer in a contract with a SOE gentailer was paying less in February 2012 than if they were supplied by a
privately-owned firm does not imply that this was because the SOEs were 100% owned by the Crown. Nor does it imply that the situation will change simply because up to 49% of the companies are sold to private investors. Companies target different segments of the market and different regions of New Zealand, and this is likely to have an impact on their pricing. For example Trustpower’s customer base is primarily in smaller provincial centres where the cost of delivering electricity to retail customers is typically higher;

- 49% private ownership should not result in these companies changing their pricing strategies. Ministers currently don’t decide on pricing. That is a matter for the board. SOE boards are required to operate their companies as successful businesses and, to this end, to be as profitable and efficient as comparable businesses that are not owned by the Crown;
- the suggestion that boards will have an obligation to the minority shareholders, which will require them to increase prices, is not correct. Boards have an obligation to act in the best interests of the company regardless of who the shareholders are, and this will not change after the IPOs; and
- finally, increasing prices is not the only way to increase profits, and often increasing prices does not actually increase profits, it results in customer losses, as Contact has demonstrated.