NEW ZEALAND INSTITUTE FOR THE STUDY OF COMPETITION AND REGULATION INC.

NEW ZEALAND'S ELECTRICITY LINES COMPANIES: AN OWNERSHIP ANALYSIS

Presented at the New Zealand Association for the Study of Co-Operatives and Mutuals international conference *Building a Better World: the Role of Co-operatives and Mutuals in Economy and Society*, Wellington, June 22 2012

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JOINT WORK WITH TALOSAGA TALOSAGA

New Zealand's Electricity Lines Companies: an ownership analysis

http://iscr.org.nz/f747,20610/20610_Electricity_Lines_Ownership_v2_BH_TT.pdf

OUTLINE

Work undertaken with Talosaga Talosaga

Electricity Lines Businesses

- industry dynamics

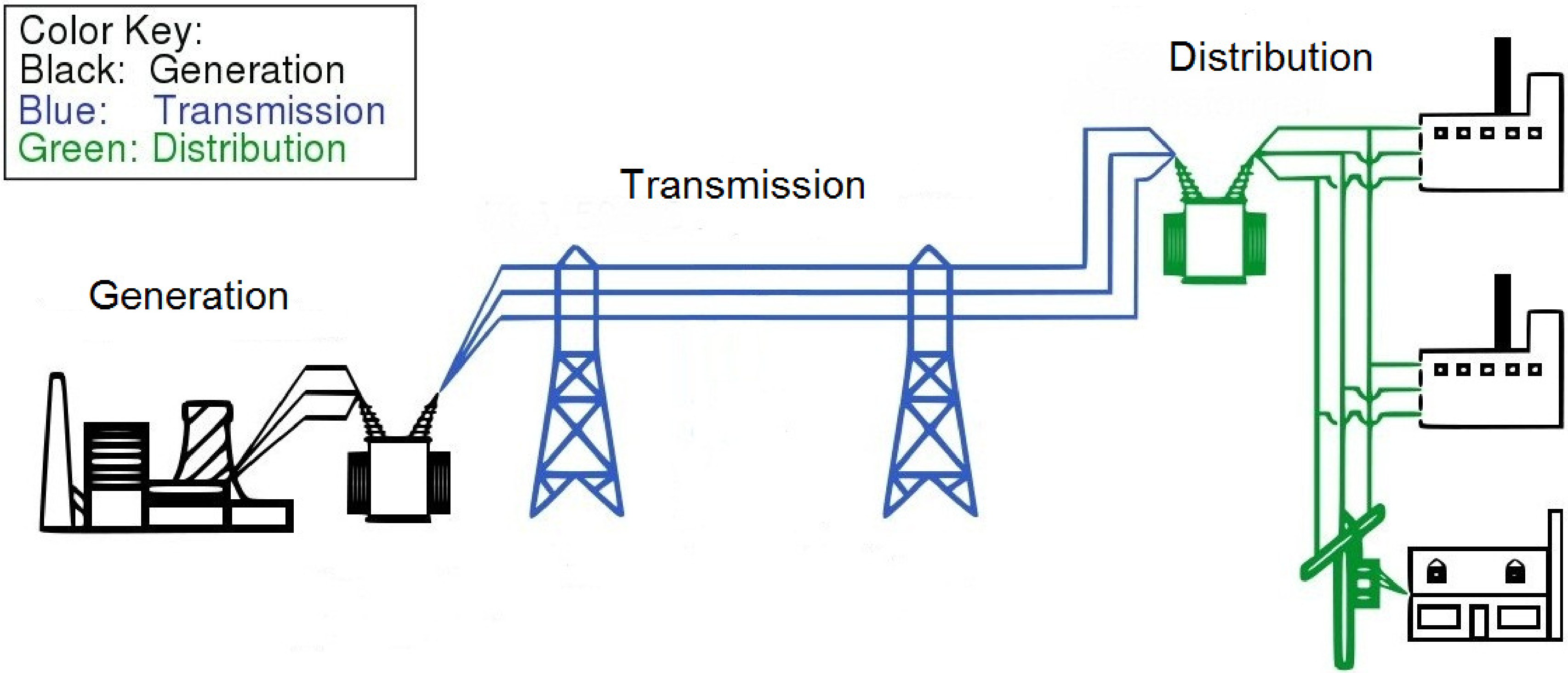
Restructuring in the 1980s and 1990s

- a default ‘trust’ (co-operative?) establishment structure
- a bias towards privatisation/corporatisation

The outcome:

- not quite what was expected
- but predictable using transaction costs and ‘incomplete contracts’ approach

THE ELECTRICITY NETWORK



ELECTRICITY LINES BUSINESSES

30 across the country

Combined assets $8.86 billion

Structurally separate from retailing, generation

- bill retailers, who then on-bill consumers
    - though some bill direct (e.g. The Lines Co)
- mixture of fixed fee and usage charge (electricity consumed)

Local ‘natural monopolies’

Subject to price-quality regulation

- unless ‘consumer-owned and having fewer than 80,000 customers, in which case only disclosure obligations apply

1980S AND 1990S REFORMS

Over 60 Electricity Supply Authorities

- Electric Power Boards (statutory bodies)
- Municipal Electricity Departments (Local Government)
- retail and local distribution

Labour Government (1989-90) Electricity Task Force

- proposed restructuring into a corporate form
  - separation of operations and shareholding (as per SOEs)
  - better incentives for cost minimisation, managerial performance, productive efficiency
  - privatisation a secondary consideration, but nonetheless 'on the table'
- but highly controversial
  - EPBs had 'no owners' (Crown Law) – how to allocate shares equitably?
  - MEDs 'council-owned' => privatisation = forced deprivation of property

1980S AND 1990S REFORMS (cont)

Compromise #1 (apparently no-one thought of a co-op!)

- MEDs and EPBs become companies
- shares vested in newly-formed Trusts for benefit of the community
- at least 90% of dividends returned to customers as rebates

Between the conception and the action came the election

- National government liked corporatisation but not trusts
- former EPB members lobbied strongly for the Trust model
    - local communities would retain ‘control’ of assets
    - wider community is beneficial if not legal owner
- but advocates of ESAs favoured full privatisation

1980S AND 1990S REFORMS (cont)

Compromise #2

- establishing authorities could decide their own form
  - indecision => local bodies would get to decide what happened
- but if Trust form adopted, an ownership review must be held at least once every five years
  - because surely consumers would prefer certain ‘cash in the hand’ now to uncertain future annual electricity bill rebates? If not now, then almost certainly at the first ownership review ….

WHAT HAPPENED?

In 2012, two thirds of ELBs are fully or partially consumer-'owned'

Ownership Structure	Number of ELBs	Number of ICPs	Percent of total customers
Investor	4	505,323	25.30%
Investor/Consumer	2	635,308	31.81%
Consumer	16	467,433	23.40%
Consumer/Municipal	2	48,067	2.41%
Municipal	5	316,802	15.86%
Nonprofit/Investor	1	24,504	1.23%

HOW TO EXPLAIN?

1. Trusts give 'unaccountable' Trustees 'too much' control (McKinlay, 1999)
    - but what about mandatory ownership reviews?
2. Consumer 'ownership' is economically rational, at least for some EPBs
    - Hansmann's 'ownership of enterprise'
        - firm will be owned by the stakeholding interest with the least combined costs of ownership and market contracting
        - can be consumers or investors (suppliers of capital)

Some evidence that (2) is a plausible explanation

- given initial starting point and ongoing industry changes

COSTS OF OWNERSHIP AND MARKET CONTRACTING

Ownership

- costs of collective decision-making increase with number of owners and customer heterogeneity
  - suggests private ownership more likely for larger, urban ELBs
- ‘disadvantage’ of non-tradability is less when consumer interests in the trust/co-op are aligned with other investments
  - long-term commitment to community e.g. home ownership investments => more stable community, fewer renters more likely to persist with Trust model (e.g. rural areas)

Market contracting

- lower regulatory burden for consumer-’owned’ ELBs
  - benefits per account greater for small ELBs as regulatory costs largely invariant to consumer numbers

THE EVIDENCE: RURAL V URBAN

PERCENTAGE OF CUSTOMERS SERVED BY ELB TYPE

Ownership Structure	Rural	Urban
Investor	3.94%	30.24%
Investor/Consumer	0.00%	39.16%
Consumer	76.60%	11.11%
Consumer/Municipal	12.82%	0.00%
Municipal	0.11%	19.50%
Nonprofit/Investor	6.53%	0.00%

CONCLUSION

A mix of ownership forms has emerged and persisted

- despite policy preference and bias towards investor ownership

Reflects different costs, incentives, facing consumers in different ELB constituencies

- distinct rural-urban; size split

Obligation to revisit ownership grants consumers an ongoing right of choice

- arguably more decision-making power over ownership than granted under standard co-operative terms
- at same time as they participate in rebates normally associated with co-ops