Meridian.

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Commerce Commission
By email: infrastructure.regulation@comcom.govt.nz

Common cost of capital Input Methodology review

Meridian appreciates the opportunity to provide feedback on the Commerce Commission's draft decision reasons paper on the common cost of capital Input Methodologies (IM) review. Meridian was amongst the group of businesses that submitted a joint letter to the Commission in August 2025 raising concerns about price volatility and step changes that have occurred at the start of recent regulatory periods under the current Part 4 rules. Along with these other businesses, we requested that the Commission consider changes to the cost of capital methodology which might help reduce price shocks and deliver better outcomes for end consumers. Meridian's specific concerns relate to the significant uplift in distribution prices which occurred between the third and the fourth Default Price-Quality Path periods (i.e. DPP3 and DPP4). These price increases occurred at a time of wider cost pressures in the industry and general cost of living pressures faced by all New Zealanders.

In March, the Commission responded to the joint letter, setting out how it had considered the issues raised but ultimately noting its draft decision was that the current cost of capital rules are largely fit for purpose and should remain in place. We are grateful for the Commission's specific consideration of this issue (including undertaking empirical analysis) and how it has communicated its thinking on this to the stakeholders concerned. We nevertheless remain concerned about the impact of significant price shocks on electricity consumers arising under the current IM rules. Such impacts can undermine confidence not only in the Part 4 regime but also in the wider industry. In our view, these consumer impacts continue to call into question whether the current approach can indeed be considered 'fit for purpose'.

Adoption of a trailing average approach to the cost of debt calculation

The Commission has identified that moving to a 'trailing average' to determine the risk-free rate under the cost of debt calculation would be the most likely means of smoothing prices for consumers under the cost of capital IM. However, it has concluded that:

- the real risk-free rate is a small part of total costs so changing that piece would have only a minor impact on allowed revenues;
- adopting a trailing average would likely add complexity to the regulatory regime; and

- there are already other tools that can smooth revenues effectively across regulatory periods, which reduces the need to change this part of the framework.

Meridian's view is that, even if the potential impact is moderate, current pressures on consumers mean that the Commission should do all that it can to pursue measures that would help alleviate future price volatility, such as that which occurred at the start of DPP4 and in each subsequent year of DPP4. We therefore encourage the Commission to reconsider this change in making its final decision on the cost of capital IM.

While we acknowledge such a change may result in additional complexity, this is already a highly complex regulatory regime and both the Commission and regulated businesses are sophisticated enough to manage this complexity. The fact that Electricity Networks Aotearoa (ENA) is one of the parties that has advocated for such a change provides a strong indication that regulated businesses are willing to trade off any additional complexity for the resulting consumer benefits. We also understand such an approach has been adopted in other jurisdictions including Australia and the United Kingdom, suggesting it is workable.

With regard to the Commission's point that other tools are available to smooth revenues, Meridian's view is that all available means should be utilised to manage the price volatility that consumers are experiencing. That is, adoption of a trailing average approach to the cost of debt calculation should be an 'and' and not an 'or'. Further, existing price smoothing tools appear to be more useful in smoothing price changes *within* DPP periods, while adopting a trailing average approach could also be useful in smoothing price changes *between* DPP periods. We would therefore view these mechanisms as being complementary rather than substitutes.

Consideration of wider changes

We have focussed our comments above on the option of adopting a trailing average cost of debt as a means of smoothing consumer price impacts as this is what the Commission identified as being the most likely means of achieving this goal. However, we also encourage the Commission to consider any wider options that might be available to achieve this aim, including any options:

- within the current cost of capital IM review;
- within the wider Part 4 regulatory framework; and
- outside the current Part 4 regulatory framework (i.e. which might require legislative change).

It is difficult to underplay the impact of the cumulative price increases on consumers that is resulting from the current Part 4 regime. We encourage the Commission to keep all options on the table in considering how it might support consumers through this and future periods.

The Commission's role in communicating price impacts

Meridian acknowledges the significant public communication undertaken by the Commission at the time of the DPP4 reset in November 2024. This included consumer-friendly collateral and online presentations to stakeholders and media, in addition to the Commission's comprehensive decision documents. However, the consumer impacts of these decisions are subsequently felt in April each year when distribution price increases tend to flow through to retail price changes. By the time these prices increases are communicated to consumers, most will have forgotten the Commission's earlier explanations (if they were ever aware of them). The end result is that electricity retailers generally need to front and explain the reasons for consumer price changes, including any price adjustments arising as a result of the DPP decisions.

In our view, it would be helpful if the Commission continued to follow through on communicating its DPP decisions throughout the DPP period, particularly at those times when consumers are likely to see resulting price increases. This would improve consumers understanding of the various contributions to annual price changes, ensure the Commission remains accountable for its decisions, and support wider confidence in the sector. This is particularly important at a time when cost of living pressures are heightened along with scrutiny of the sector.

Please contact me if you have any queries regarding this submission. This submission can be published in full.

Nāku noa, nā

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