# MAJOR ELECTRICITY USERS' GROUP

25 May 2006

Janet Humphris
Resources and Networks Branch
Ministry of Economic Development

By email to electricity@med.govt.nz

Dear Janet

**Submission on discussion paper "Investment in Electricity Generation by Lines Companies"**

1. This is a submission by the Major Electricity Users' Group (MEUG) on the Ministry of Economic Development (MED) discussion paper *Investment in Electricity Generation by Lines Companies*, published 26 April 2006.

2. Paragraph 4 of the discussion paper states, "*The primary purpose of the paper is to promote a further discussion with the industry on the issues of lines and energy separation*." The paper considers seven suggestions by parties in response to the prior year consultation round on the MED discussion paper *Facilitating Investment in Generation by Lines Companies: a discussion note*, March 2005.

3. Hon Trevor Mallard, Acting Minister of Energy, in a covering media statement when releasing the discussion paper, said:

   "*These options could potentially help create a better environment for much-needed investment in generation. However, it's also important that we balance any changes against the risk of lessening competition in the electricity market*."

   MEUG agrees with the Ministers summary of the key policy trade-off.

4. The discussion paper recommends, after considering the above policy trade-off, that five of the seven options should not be considered further. A summary of the MED conclusions is set out in table 2 on page 23 of the discussion paper. MEUG agrees with the discussion paper assessment and conclusion on those five options.

5. The discussion paper concludes there is a good case for two of the seven options:

   a) Allowing lines companies to trade in hedges and other financial instruments; and

   b) Removing the requirement for lines companies to comply with arms length rules when generation and customers are outside the lines company network.

**Allowing lines companies to trade in hedges**

6. The first of these preferred options was the basis of the consultation round last year and the discussion paper includes an appendix setting out the MED response to submissions. The discussion paper (paragraph 48) argues the risk of anti-competitive behaviour should lines companies be allowed to trade in hedges is minimal because, amongst other things, lines companies will continue to be subject to appropriate corporate separation and arms length rules. New rules will be needed to monitor this trading activity. The need for new monitoring rules is noted in the discussion paper when commenting on issues from the consultation round last year (page 29). MEUG suggest that until details of how this new trading activity of lines companies will be monitored to ensure compliance with the corporate separation and arms length rules; it is difficult to completely accept the discussion paper conclusion that the benefits of the proposal outweigh the risks.

7. In the experience of MEUG some lines companies have a propensity to take advantage of any crack in the regulatory framework. Recent evidence of this has been the tardiness of some lines companies to pass through the interim rebate from Transpower to offset the average 19% increase in transmission charges effective 1 April 2006. If consumers can't trust lines companies to implement this simple pass through as quickly and as transparently as possible; it's difficult to see how consumers could trust lines companies to enter into trading activities without understanding how that will be monitored.

8. Monitoring lines companies will not be a trivial matter because the expectations of some lines companies is that one of their competitive advantages is a strong balance sheet – clearly a case of them expecting to leverage of the lines assets and hence breaching the corporate separation and arms length rules. MEUG would like to see further details of how monitoring for this and other risks might work before reaching a decision on allowing lines companies to trade in hedges and other financial instruments.

**Remove arms length requirements for generation not connected to own network**

9. An example of the second preferred option in the discussion paper was the application by Unison for an exemption by the Commerce Commission. The Commission granted the application subject to various caveats.

10. MEUG suggest retaining the status quo whereby each case is considered by the Commerce Commission on its own merits rather than making a blanket change to primary legislation.

11. If the number of such exemption applications was to increase and it became clear they could all be treated exactly the same, then the cost of drafting a change to the legislation, having select committee hearings etc might be justified. However MEUG expects the number of applications for exemptions by lines companies seeking to invest in generation not connected to their own grid will be very small and the administrative cost of retaining the status quo exemption application and consultation process will be much lower than the cost of making a legislative change.

Yours sincerely

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