MAJOR ELECTRICITY USERS' GROUP

2nd June 2015

Dr John Rampton
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Electricity Authority
By email to submissions@ea.govt.nz

Dear John

Consultation Paper – Transpower's proposed variation to the TPM

1. This is a submission by the Major Electricity Users' Group (MEUG) on the Electricity Authority (EA) consultation paper[1] "Transpower's proposed variation to the Transmission Pricing Methodology" 21st April 2015. Attached and to be read as part of this submission is a report by the New Zealand Institute of Economic Research (NZIER) "Transmission pricing, Assessment of Transpower's proposed variation" 2nd June 2015.
2. MEUG members have been consulted in the preparation of this submission. This submission is not confidential. Some members may make separate submissions.
3. MEUG has previously made submissions to Transpower on prior proposed variations on 8th August 2014 and 19th December 2014. The latter submission by MEUG included a memorandum from NZIER.
4. The consultation paper states (paragraph 2.3.13):

   > "Transpower states that the five original components of its proposed variation are straightforward to implement, low-cost, incremental, and broadly supported by the industry (though not necessarily by consensus)"

5. We think Transpower has miss-read the picture if it believes the original variations were broadly supported. MEUG is not aware of any consumer that supported the more contentious of the proposals made by Transpower.
6. MEUG has been supportive of Transpower seeking to improve the quality of evidence and analysis for changes that in some cases might materially change behaviour of a range of participants and have risks of unintended consequences. However we never accepted that the quality of evidence and analysis by Transpower was sufficient to justify our supporting all of Transpower's proposals.

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[1] Refer web http://www.ea.govt.nz/development/work-programme/transmission-distribution/transpower-tpm-operational-review/consultations/#c15231 and document URL http://www.ea.govt.nz/dmsdocument/19327

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7. The conclusions of this submission on Transpower's latest proposed changes to the TPM are:

   a) Based on the analysis by NZIER of the problem definition, CBA methodology and assumptions used in the CBA MEUG is not convinced a change to N=100 for UNI and USI is unambiguously going to result in outcomes that will be welfare enhancing. There are plausible scenarios where there is no change in static efficiency or even worse outcomes. There will though be wealth transfers between consumers in different parts of New Zealand. From the analysis by NZIER and MEUG members we don't think a change to N=100 across all of New Zealand will actually affect the large grid and near grid consumers; but it will affect other classes of consumers.

      In the absence of a demonstrable net economic gain for all reasonable scenarios but full and non-contested knowledge there will be wealth transfers between different classes of consumer in different parts of New Zealand, MEUG suggests the Authority therefore cannot agree to Transpower's proposal to change from N=12 to N=100 for the UNI and USI.

   b) MEUG supports the exploration of the 2 new generic proposals to overcome lost manufacturing opportunities due to poor RCPD signals exemplified by Pacific Aluminium not producing over summer months when it would be welfare enhancing for New Zealand if it were to do so. MEUG cannot see any downside to either or both the new proposals although we have no view on which or both should be implemented.

   c) MEUG's support in the submission of 8th August 2014 for an amendment to overcome the paralleling issue is unchanged.

8. Four further observations are noted below on this first ever proposed variation to the TPM by Transpower within the TPM guidelines.

9. First MEUG has concerns that Transpower's characterisation of its proposed variations as "straight forward" risks undermining the need for robust cost-benefit-analysis. As noted in paragraphs 4 to 6above we have not viewed the problem definitions and options analysis underpinning some of the proposed variations as straightforward. NZIER demonstrate that the Cost-Benefit-Analysis (CBA) falls short due to lack of evidence supporting assumptions and many incomplete aspects of what should be included in a robust CBA. Some of those may be solvable; nevertheless the outcome may be that a change perceived as being "straight forward" may with the best but still incomplete evidence available, be unable to pass the test of being convincingly net welfare positive. Our concern is twofold.

   a) First that Transpower may have raised expectations about variations being straight-forward and therefore the likely winners will be incentivised to lobby to have those changes made perfunctorily rather than be justified with a robust analysis.

   b) The second concern is that proponents of variations proposed by Transpower and characterised by Transpower as "straight forward" may seek a lesser standard of CBA. In effect they may argue Transpower has a right to make variations with the Authority simply saying yes or no irrespective of the broader requirement in the Act for processes and outcomes for the long-term benefit of consumers. MEUG is wary of back-door major changes to TPM being masqueraded as straightforward variations within the guidelines.

10. Second MEUG welcomed the EA referring back the diluted HAMI proposal to Transpower. After reading the submissions of other parties to Transpower on that proposal we are even less inclined to support the diluted HAMI approach and definitely not the MWh approach for HVDC charges. It was therefore both surprising and disappointing that Transpower has subsequently and without change re-submitted that proposed variation. The comments in the preceding paragraph definitely apply to the proposed diluted HAMI approach.

11. Third MEUG suggest only clear cut problems with the TPM that have no downside for other parties not directly affected can be considered as variations within the existing TPM guidelines. An example of those types of issues is the paralleling issue. Every other problem with the existing TPM affects a wide range of parties. A primary issue for all such problems is Transpower's statutory right to charge for transmission services even though no party receives any benefit from them. MEUG notes that charges even for such stranded assets are at a cost of capital above the expected mid-point range. A lot of the debate on who should pay for transmission services is hung up on the problem that somebody currently has to pay for such uneconomic services rather than Transpower bearing the cost. Until the Electricity Authority, Commerce Commission and Transpower's owners address this problem possible changes to TPM will continue to be contentious.

12. Fourth and following on from the above point on treatment of stranded assets; MEUG note that stranding risk is a whole of system issue affecting transmission and distribution services and across the regulatory regimes governed by the Electricity Authority and Commerce Commission. A solution as to who should pay for stranded assets needs to be consistent across both regulators otherwise a disconnected approach will lead to less than optimal outcomes as the monopolies either forum shop or exploit gaps between the regimes. NZIER in their advice to MEUG in relation to the Commerce Commission consultation on scope of the review of Input Methodologies noted[2]:

> "Our key observation is that the scope of the IM review needs to be expanded to consider the risks of stranded assets posed both by the slow response to the flattening of electricity demand and the potential for disruptive technologies to shift load patterns in the network."

13. We look forward to the Authority announcing next steps.

Yours sincerely

Ralph Matthes
Executive Director

[2] NZIER memo to MEUG, Input Methodologies review – Commission Scope letter, 20th Match 2015, paragraph 67, document URL file:///C:/Users/Ralph/Downloads/Memo%20re%20scope%20of%20IM%20review%20(final)%20(7).pdf