Please direct replies to the TPM Group via:

Alan McDonald, EMA Northern
Private Bag 92066
Victoria Street West, Auckland 1142
Alan.McDonald@EMA.CO.NZ

Miriam R Dean CNZM QC
Chair
Electricity Pricing Review Expert Advisory Panel
C/O Panel Secretariat
Ministry of Business, Innovation and Employment
PO Box 1473
Wellington 6140
Email: energymarkets@mbie.govt.nz

17 July 2018

Dear Ms Dean

We are deeply concerned that the Electricity Authority (EA) is pushing forward with its plans to change the transmission pricing methodology (TPM). The proposed changes create serious issues around fairness and equity and therefore run counter to aims of the to the Government's Electricity Pricing Review (EPR).

We are a group of TPM affected parties, formed in 2016, comprising organisations from right across the electricity sector. We include large consumers, energy consumer trusts, stakeholder groups, electricity network companies, and electricity generators and retailers.

As chair of the Expert Advisory Panel for the EPR we are writing to outline to you our concerns about the EA's proposals and to request that:

(a) We meet with you as a matter of priority to outline our concerns in person.
(b) The EPR consider and advise on fact that an independent regulatory agency, the EA, can increase residential charges through the TPM with no government oversight.

We have also written to Minister Woods and asked that she:

(a) Write to EA under section 18 of the Electricity Industry Act to ask them how they consider consumers would benefit from amending the current TPM as an input into the EPR.
(b) Give serious consideration to transferring the role of setting transmission pricing methodology guidelines from the EA to the Commerce Commission, which has more robust and transparent processes.

Background

We are supportive of the Government's Electricity Price Review, which aims to run a 'fairness and equity' ruler over the electricity sector.

The terms of reference for the EPR state that "It will also assess whether the electricity regulatory framework will continue to be appropriate as we look to the future". As you know the EA interprets its objective as requiring a focus on the overall efficiency of the sector, not fairness and equity issues.

Last month, the EA announced that it was pressing ahead with its TPM proposals. These have the potential to disrupt the Government's aims in establishing the EPR, by attaching penalties to sunk investments and by creating new fairness and equity issues. In addition, the continuation of a project to set TPM Guidelines which are not supported by Transpower, the operator of the grid, is also troubling.

Changing the rules after investment has been made is problematic

In its public statements on 26 June, the EA said unless it changes the TPM, rapidly changing technology (especially batteries), could incentivise poor investment in the future. If it were proposing to do so simply to guide future investment, there would be much less concern.

However, what the EA's media statements gloss over is that it intends to restart its previous TPM with a goal of reallocating the costs of existing assets, back to 2004 (six years before its own creation).

This is extremely unhelpful, as of course all past investment decisions were made on the basis of the transmission methodology at the time, which spread costs more evenly across regions and consumers. Consumers made investment decisions based on those rules: where they chose to locate, their levels of electricity consumption vs alternative fuels and so forth. If different rules had been in play, different decisions may have been made. Regulatory certainty is a core requirement for investment in life-long assets and the EA's proposal does not meet that test.

We also know from the Productivity Commission's report that the Government's climate change aspirations involve "electrifying the economy." Achieving this will require a significant increase in investment across the supply and demand chain.

Ability to pay

The parallel review of TPM by the EA on the basis of its statutory objective of competition, reliability and operational efficiency, at the same time as the EPR is assessing the regional aspects of transmission pricing and how network pricing impacts end users from the perspective of fairness, is deeply problematic and seems to be an inefficient use of regulatory and government resources. It certainly risks leading to contradictory outcomes.

The EA says the solution to transmission pricing is an 'asset-based beneficiary-pays' approach. Of course, not all beneficiaries are created equal. Based on its last proposals back in 2016, the EA's own data showed that consumers connected to electricity lines companies would be worse off to the tune of $115m a year, while those who would be better off were only better off to the tune of $46m a year. Thousands of low-income pensioners, many small businesses, DHB's and schools, would be hit with an unexpected increase in payments without any compensating arrangement. Estimates show some households could be hit with electricity bill increases of around $100 per year if TPM changes were made, which represents more than 20% of the Government's winter energy payment for single people.

Large businesses (the Tasman paper mill in Kawerau, and the Kaitaia mill for instance), already on tight margins, could be pushed into unsustainable positions, affecting hundreds of employees and many small towns. Back in 2016 it was calculated that Northlanders would lose $15M more a year in increased power prices, significantly more than they would gain in regional development assistance.

The EA's singular focus on an asset-based beneficiary pays methodology for long life interconnection assets, where it is actually very difficult to ascertain who the beneficiaries are given the long life of these assets, is also very unhelpful in arriving at an equitable solution. This is exacerbated by the fact that these decisions made on historic transmission investments did not consider any changes in cost allocation and the financial impact on customers.

Absence of evidence and support

You will be aware that the EA halted its TPM work over a year ago when major errors in its cost-benefit analysis were discovered. For example, their analysis had concluded that their proposals would benefit the country by $13.7m over 30 years. However, our group uncovered calculation errors that showed the exact opposite: that the TPM changes would actually cost $13.7m. That meant New Zealand would be better off leaving things the way they were. The failure to produce a robust CBA in five years (2012-17) has damaged stakeholder confidence which we consider would be best restored by an independent expert preparing a CBA, which should then be road-tested via an industry advisory committee process, prior to formal consultation. This aligns with section 21(1) of the Act and the code amendment principles.

Deeply held concerns around the process

In the group's experience, good process leads to good decisions. Poor processes, by contrast, only serve to undermine trust and confidence.

The EA's first major TPM proposals, in 2012, were strongly challenged, and no decisions were made. The EA then ceased using any expert advisory groups, and they were never re-instated. In 2016 it released new proposals. These turned out to be largely a re-run of the 2012 ones. Submissions on the 2016 proposals were roughly 2 to 1 against.

In 2017 we commissioned an independent review by Covec Consulting. It analysed the total of 60 expert reports over 11 consultation rounds from 2012 to 2016 that were submitted to the EA. It showed the vast bulk of expert opinion was heavily weighted against the EA's plans, but at no stage in those four years did the EA address the criticisms contained in the expert reports, leaving submitters completely in the dark as to its thinking.

It now looks like we will again see a repeat of the same 'propose-respond' approach favoured by the EA. We have asked them many times to engage in a more iterative process (eg using cross-submissions) and to reconvene working groups, to no avail.

These concerns have resulted in the group forming the view that the role of the EA in determining transmission pricing methodology guidelines would be better transferred to the Commerce Commission as we consider they run more robust and transparent processes and it links in well with the Commerce Commissions role in considering electricity transmission and distribution input methodologies and price-paths under Part 4 of the Commerce Act.

In summary, we welcome the Government's focus on reviewing the electricity sector in order to ensure prices are fair and equitable for consumers, and that our regulatory framework is future-proofed. The EA's proposals have real potential to undermine these efforts.

Yours sincerely

Kim Campbell
Chief Executive
EMA Northern

James Carmichael
Trustee
Entrust

Richard Gardner
Senior Policy Advisor
Federated Farmers of New Zealand

Andrew McLeod
Chief Executive
Northpower

Susan Flay
Director
Norske Skog Tasman Ltd

Darren Glichrist
Energy Manager
Oji Fibre Solutions

Russell Shaw
Chief Executive
Top Energy Group

Vince Hawksworth
Chief Executive
Trustpower

Simon Mackenzie,
Group Chief Executive
Vector

Ajay Anand
Chief Executive
Horizon Networks

Judy Nicholl
Chief Executive
Counties Power