

22 March 2019

Miriam R Dean CNZM QC  
Chair  
Expert Advisory Panel  
Electricity Price Review  
Wellington

Dear Miriam

### **Response to Options Paper**

We welcome the opportunity to respond to the Electricity Price Review's Options Paper. As we have discussed with you, we think the Panel's Options Paper crisply identifies key issues in the sector, and proposes meaningful change.

Transpower agrees that a policy reset is timely. The Government has committed to ambitious 2050 climate change goals that have significant implications for the electricity sector. Industry participants will need to make a lot of new investment, and take risks with the adoption of new technology. Demand for electricity will increase and become harder to predict.

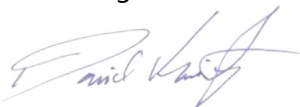
At the same time, the sector must address head on the issues of energy affordability and hardship. These are tightly linked to the pathway to our climate change goals, and the policy issues must be considered together.

We are pleased the Panel has highlighted the role a Government Policy Statement (GPS) could play in co-ordinating key policy drivers, setting the direction for the sector, and dealing with specific road blocks. We are conscious that other submitters will add their contributions to the discussion draft we have previously tabled. Once all contributions are in, we think a useful next step is that parties share their submissions and meet to establish for the benefit of the Panel as broad a consensus on the GPS as is possible.

Transpower has provided specific feedback on the proposals identified in the Options Paper using the web-based tool established by the Panel.

The proposed changes ahead of us could make a significant difference for electricity consumers in New Zealand. We look forward to engaging with the Panel, and other sector participants, on the next phase of the Electricity Price Review.

Kind Regards



David Knight  
General Counsel & Company Secretary

## TRANSPOWER'S RESPONSE

to

### ELECTRICITY PRICE REVIEW OPTIONS PAPER

#### **A STRENGTHENING THE CONSUMER VOICE**

##### **A1 Establish a consumer advisory panel**

*Transpower's view:* we support this option.

*Commentary:* we endorse the Panel's focus on consumer voice. The Panel has rightly highlighted how outcomes for consumers in the electricity sector are not good enough. Giving consumers greater voice in the development of policy and regulation will help change that.

The art will be in the design choices, some of which are highlighted by the Panel. We need to get better at framing issues that consumers can relate to and contribute to, rather than expecting consumer groups to submit on technical regulatory proposals. We should avoid a proliferation of different consumer panels. And we need to find ways for a consumer panel to contribute without being overwhelmed by the number of processes happening at any one time, or making consultation processes onerous. These are all solvable issues that can be worked on if this initiative progresses.

##### **A2 Ensure regulators listen to consumers**

*Transpower's view:* we do not support this option as currently framed.

*Commentary:* regulators should listen to consumers and have regard to their views. This happens now.

The issue raised in the Options paper is what a regulator should do when it is running a consultation process, and no consumer or consumer group has contributed.

In our view, the right way to respond to this concern is the option discussed at A1 - a consumer advisory council that is resourced to participate in key regulatory processes.

The alternative of imposing an obligation on the regulator to consult with consumers in every regulatory process raises too many unnecessary hard issues. It will be difficult for the regulator to identify representative consumer voices, and convince them to invest time participating in a regulatory process they have up until now chosen not to invest in. Harder still if it is a technical regulatory process that consumers, including potentially the consumer advisory panel, have rationally decided is not a good investment of their time.

Rather than imposing resource and time demands on consumer groups and the regulator, it seems more constructive to invest in a well-functioning consumer advisory council that can choose for itself, from a consumer perspective, how and where to participate.

#### **B REDUCING ENERGY HARDSHIP**

##### **B1 Establish a cross-sector energy hardship group**

*Transpower's view:* we support this option.

*Commentary:* we endorse the Panel's focus on energy hardship and the position of vulnerable energy consumers in New Zealand today. This is a moral and policy issue for the sector. Transpower is keen to support this work and play its part.

## **B2-B8**

*Transpower's view:* we support these options

*Commentary:* refer to our response to B1.

## **C INCREASING RETAIL COMPETITION**

### **C3 Make it easier to assess electricity usage data**

*Transpower's view:* we support this option.

### **C6 Help non-switching consumers find better deals**

*Transpower's view:* we support this option.

### **C7 Introduce retail price caps**

*Transpower's view:* we do not support this option.

*Commentary:* We agree with the Panel that a retail price cap would do more harm than good. If set too low it would stifle investment and resource availability. We are also concerned that a retail price cap would give rise to a proxy wholesale cap.

## **D REINFORCING WHOLESALE MARKET COMPETITION**

### **D1 Toughen rules on disclosing wholesale market information**

*Transpower's view:* we support this option.

*Commentary:* good, timely, easily available information is vital to the functioning of a market, and for participants to have confidence in the market. It is the reason why consumer markets have the Fair Trading Act and why share markets require continuous disclosure. The wholesale electricity market – one of the important price finding mechanisms in the economy – should be no different.

The continuous disclosure obligations of listed entities is a useful reference point. Material information relevant to price discovery must be disclosed. It is not optional, the rules are enforced rigorously, and participants play by the rules. People looking to invest in shares have confidence that the price is true, and the market is not skewed in favour of those with an information advantage.

The same should apply in the wholesale electricity market. New Zealand will need investors to commit to significant hedge arrangements and significant capital investments if we are to stay on the pathway to a low emissions economy in 2050. Those investors will want the same confidence as investors in the share market, and that is a fair ask. Good quality, timely information will also support security of supply arrangements.

A design issue will be setting obligations in a way that imposes only reasonable burdens on smaller market participants. This seems doable.

### **D2 Introduce mandatory market-making options**

*Transpower's view:* we support this option

*Commentary:* we endorse the Panel's analysis of the importance of this problem and why mandatory market-making obligations are needed, and the Panel's discussion of how a framework can be designed that avoids undue risks and costs for market makers.

Further thought could be given to the horizon of the hedge market. The pathway to a low emissions economy in 2050 will require a lot of renewable generation investment, and longer-term hedge market arrangements will support those investment projects.

#### **D4 Monitor contract prices and generation costs more closely**

*Transpower's view:* this option would need to be progressed with care

*Commentary:* concerns around the profitability of generators in the wholesale market have been around for some time, and it would be helpful if the New Zealand public had more information and more confidence on this issue. The Panel suggests that the Electricity Authority periodically compare contract prices with new generation costs. Care will be needed to reflect the market context where prices are not cost-based, and the assessment of new generation costs at any point in time requires judgement. We don't want to create a situation where new generation is deterred, with security of supply implications.

## **E IMPROVING TRANSMISSION AND DISTRIBUTION**

### **E1 Issue a government policy statement on transmission pricing**

*Transpower's view:* we support this option.

*Commentary:* a Government Policy Statement could perform several useful functions for the energy sector right now. We highlight just two.

#### *Transition to low emissions economy*

The first is New Zealand's response to climate change, and the transition required to meet our 2050 objectives.

There is good information on what the pathway to 2050 looks like. The Productivity Commission has reported on the transition to a low emission economy. We have published our views in our Te Mauri Hiko report. A transformation in the energy sector and the economy is required. This will require co-ordination across energy policy, and government policy generally.

Any GPS should start broad, and articulate the long-term trajectory for the energy sector and how it interacts with other areas of government policy. This would provide important information for the sector about the medium-term direction of government policy and set important context for the more specific matters covered in a GPS.

#### *Transmission pricing*

The second focus area is transmission pricing, a topic highlighted by the Panel.

The Panel rightly identifies that reform of transmission pricing has taken too long, and the reasons for that are some "difficult issues" that need to be addressed "head on".

The key difficult issue is the role of the TPM and whether individualisation of charges at the asset level is appropriate. There are related choices of how to price existing assets, and the HVDC assets.

It is not Transpower's role to express a view on these issues. But these issues have divided the sector, and sent the TPM reform process around in circles for seven years, with the ever-present threat of litigation.

There are two reasons for this. First, the essence of these questions is policy and political, not regulatory. They go to the redistribution of wealth between regions in New Zealand and between groups of New Zealanders. It is not fair to ask a regulator to make them, let alone expect a regulator to achieve industry buy-in and consensus.

Second, once a regulator expresses a view on a high-level policy question, and says that a particular policy outcome is consistent with its statutory framework, it becomes very hard for the regulator to change that high-level view.

A circuit breaker is needed. These questions should be answered at the policy and political level, where they belong. Decision-makers at the policy and political level can take into account a broader range of factors, with democratic legitimacy. The answers may look like the Electricity Authority's current proposals, or they may not. Either way, we need answers in a form that will end both drawn out regulatory processes and threats of litigation.

The answers need to be conveyed to the sector in a way that allows the Electricity Authority to say the boundaries of the playing field are set, and now we can get on and referee the game.

For this reason, more than a standard GPS will be needed. A GPS is a good vehicle for informing the sector about the medium-term trajectory of government policy, and also the kinds of outcomes the government is looking for in the near term.

However, in relation to the difficult TPM issues - the role of the TPM; whether individualisation of charges at the asset level is appropriate; how to price existing assets; how to price the HVDC assets – confronting these head on includes reaching policy decisions and then conveying those answers to the Electricity Authority as boundaries within which it can develop the detail of the TPM.

In our draft indicative GPS we have suggested some guiding principles including:

- simple and implementable
- incremental change
- the importance of signalling peak usage.

We are conscious that submissions on the Panel's Options Paper may include several different but similar proposals for the content of a GPS (putting aside the "difficult issues" referred to above). As a process suggestion, it might be helpful if, after submissions are made, interested parties share their submissions and meet to establish as broad a consensus as possible. Transpower is confident sector participants can work together to produce a draft GPS that can play a significant role in providing direction and certainty to regulators, investors and consumers.

## **E2 Issue a government policy statement on distribution pricing**

*Transpower's view:* we support this option

*Commentary:* reform of distribution pricing will need to be done well if the sector is to encourage innovation, the take up of new technology, and the consumption of new services. This is an important part of the transition to a low emissions economy. We

agree with the Panel there is a role to play for a government policy statement that informs sector participants about the outcomes the government is looking for.

We are not experts in distribution pricing; we are aware the issues to be worked through are hard; and that the distribution sector has been applying a lot of time and resources to this task. In response to the Panel's request for guiding principles, from our perspective we suggest consistency with the approach to transmission pricing unless the distribution context suggests something different. In the transmission context we have suggested guiding principles in our response to E1.

#### **E4 Limit price shocks from distribution price increases**

*Transpower's view:* we support this option, and agree both transmission and distribution network pricing should be cognisant of the need to limit price shocks for consumers.

#### **E5 Phase out low fixed charge tariff regulations**

*Transpower's view:* we support this option, and we note that both distributors and retailers agree low fixed charged tariff regulations should be phased out.

#### **E6 Ensure access to smart meter data on reasonable terms**

*Transpower's view:* we support this option and a balanced solution.

*Commentary:* we agree with the Panel that this is an important issue, and cut through is needed. If consumption data is captured, shared and used well, this will facilitate improvements in network management and investment, the development of new services, the entry of new service providers, and management by consumers of their consumption and their budgets. It will also have benefits further up the value chain, including improving the forecasting by the system operator, which links to wholesale market competition and security of supply.

Retailers and distributors both have a perspective on the current stand-off, but the stand-off is unhelpful and if anyone should have control of the data and how it is used it should really be the consumer.

A balanced solution must be possible: one that recognises it is important to capture this information in a usable way, that we can address any competition and privacy concerns without holding up the development of this opportunity, and that consumers must retain control of how their information is used.

#### **E7 Strengthen the Commerce Commission's power to regulate distributors' performance**

*Transpower's view:* we support giving the Commerce Commission greater powers to better regulate electricity distribution businesses' (EDBs) performance. We also support the Commerce Commission making greater use of its existing powers.

*Commentary:* Good EDB performance will be a key enabler to meet our 2050 goals and the transfer to a low emission economy. It will also be crucial in ensuring New Zealanders only pay for the efficient costs of being connected to the electricity network.

The Options paper raises three themes when discussing whether to strengthen the powers of the Commerce Commission: greater supervision of trust-owned EDBs, a more forward-looking supervision of asset management, and more intrusive regulation and penalties for EDBs currently subject to regulation.

We endorse the need for greater supervision of consumer trust-owned EDBs. The distribution sector as a whole must meet the challenges of new technology and the path to

a low emissions economy. This will be part of retaining the confidence of all New Zealanders as we work through the many changes ahead.

We also see the value in exploring how the Commission and EDBs might work together on a more forward-focused framework for asset management. This will obviously need to be collaborative, to ensure it improves asset management outcomes and doesn't shift responsibility for asset management to the regulator.

However, we are cautious about the options of forcing an EDB onto a CPP, and higher maximum penalties for breaching price-quality regulations.

The proposal that the Commission be empowered to move an EDB from a DPP to a CPP is a significant change to the DPP / CPP framework, and one not well canvassed with the sector to date. It would be helpful to understand more about the problem being addressed, and have time to consider the possible consequences of this regulatory change.

In relation to penalties, we believe the current \$5 million penalty per contravention has a strong deterrent effect on EDBs, including the larger distributors. Recent penalties and settlements have imposed substantial financial impost on EDBs. We are concerned that simply increasing the size of the potential penalty may not be without risk. We support regulatory approaches that are forward-focused and collaborative. Network operators and regulators are in a long-term relationship. We encourage development of a framework that will ensure enough flexibility for EDBs to work with the Commission to respond appropriately as events happen. Network management challenges can arise and evolve within a five-year regulatory period. Actions having a price impact in one regulatory period may not necessarily be visible in quality until a later regulatory period. A flexible framework will still need to ensure everybody respects the price-quality standards, but should ensure that both EDBs and the Commission can look ahead.

## **F IMPROVING THE REGULATORY SYSTEM**

### **F3 Give regulators environmental and fairness goals**

*Transpower's view:* we support the option to give the Electricity Authority a consumer protection function

*Commentary:* Refer to our response to B1.

### **F6 Establish an electricity and gas regulator**

*Transpower's view:* we support this option for the medium-term.

*Commentary:* To respond to the challenge of climate change, a transformation in the energy sector and the economy is required. As the response to climate change gathers pace in the years ahead, New Zealanders will demand a greater degree of co-ordination and oversight across energy policy, and regulatory decisions in the sector.

This is not just a matter of staying on track, as important as that is. Right now, there is a significant risk the transition in our energy sector puts the cost onto the New Zealanders who can least afford it, and creates risks to our security of supply. To avoid those outcomes, and maintain public commitment to the transition to a low emissions economy, we will need co-ordination of policy and regulatory decisions across the energy sector.

Gas and electricity industries have many similarities and links. A single regulator developing and enforcing regulations for both industries in a consistent and coherent way would serve the interests of consumers and reduce uncertainty for regulated businesses.

This has been done before, with a good example being in the UK, where the Office of Gas and Electricity Markets (**OFGEM**) acts as the gas and electricity regulator.

Electricity and gas sectors also have some differences that may mean there is less similarity and synergy than might be expected. While gas is a crucial input into the current electricity system, the same could be said for other energy sources, such as coal. The key difference with gas at present is the lack of transparency and observability the electricity industry has of gas availability. We strongly believe that more transparency is required of the gas market and that efforts to establish a new regulator should occur once a new regime is urgently established.

While we support moving towards the single regulator option, we note more work needs to be undertaken to develop this option. There are some immediate questions that need to be addressed (such as developing a TPM) and we do not support development of a single regulator that distracts from these more immediate priorities. We also note the Panel is not suggesting any change that removes price-quality control from the Commerce Commission's jurisdiction, and we endorse that approach.

## **G PREPARING FOR A LOW-CARBON FUTURE**

### **G2 Examine resilience of electricity supply**

*Transpower's view:* we support this option.

*Commentary:* Transpower as system operator plays a key role in maintaining security of supply, and has worked successfully with the EA and the existing Security and Reliability Council (SRC) on improving many of the building-blocks of system security and security of supply. We view resilience of electricity supply in New Zealand to be particularly important in the context of frequent earthquakes, new technologies and the unprecedented challenge of climate change. We need to navigate these challenges as we maintain appropriate levels of reliability and security. Therefore, a review of the wider security and resilience of the electricity system as it evolves to meet these challenges is timely, and we support this.

We consider the current SRC could usefully perform this role, but its functions could be enhanced by clarifying its mandate and role to address the long-term impact of new and changing technology on the security of supply. It might also be given greater independence and appropriate levels of funding, such that it can commission expert advice. An independent SRC reporting directly to the Minister would free up the Authority to focus on its core responsibilities. An option could be for a separate working group to be set up.

In addition, the system operator's role could be expanded to look further ahead into the changing landscape, well into the generation investment cycle. A more long-term systems view would enhance the timely identification of evolving system risks and provide the framework for a low-cost transition to new technologies. This would complement the grid owner and MBIE's long term scenarios and forecasting.

We are keenly aware that security of supply is an investment issue, as well as an operational one. We support a holistic approach to improving the building-blocks of system security and security of supply, bearing in mind that security of supply depends in part on generators having incentives to invest, which links back to the discussion of a just transition to a low emissions economy and managing price effects in a way that recognises consumer welfare and investment incentives.

### **G4 Improve the energy efficiency of new and existing buildings**

*Transpower's view:* we support this option



*Our commentary:* We support the Government leading the way on this option. Energy efficiency gains across our existing stock of buildings and anticipated new buildings has the potential to yield very significant and permanent savings in the sector for the direct benefit of consumers, as well as significant health and welfare benefits for New Zealanders. These gains are predictable and achievable. This is definitely a “low hanging fruit” option.