



## **SUBMISSION**

by

**EMPLOYERS AND  
MANUFACTURERS' ASSOCIATION  
(N) INC.**

**To the Ministry of Economic Development  
On  
“Improving Electricity Market  
Performance”**

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Peter Atkinson  
Private Bag 92066  
Auckland  
Phone: 09-367-0913  
Fax: 09-367-0914  
Email: [peter.atkinson@ema.co.nz](mailto:peter.atkinson@ema.co.nz)

## **1. INTRODUCTION**

EMA (N) welcomes the opportunity to comment on the discussion paper entitled 'Improving Electricity Market Performance' dated August 2009 ('the discussion paper'). This is the first substantive review of the market since 2001.

EMA (N) is an organisation with 118 years of representation experience in the Auckland Region, having been formed in 1996 following a merger of the Auckland Employers Association and the Auckland Manufacturers Association. Both organisations were established over 100 years ago.

EMA (N) represents approximately 8400 member businesses from the Far North to Bay of Plenty, employing some 300,000 staff. EMA is the largest member of Business New Zealand which was formed from the New Zealand Employers Federation and New Zealand Manufacturers Federation during May 2001. Business NZ represents 76,000 businesses throughout New Zealand.

## **2. WHY THIS IS IMPORTANT**

- 2.1 EMA (N) is very concerned about the scale and extent of power price increases over the last 5 years and about the effect that these rises are having on the competitiveness of NZ business. A modern economy needs an efficient electricity system. It is vital for a competitive, growing economy. Electricity is a key input into the production and use of many types of goods and services, and the electricity demands of the productive sector need to be satisfied in a manner which is at least cost to the economy.

Consequently we welcome any moves to bring about a more competitive market and thereby exert downward pressure on prices. This discussion paper is a step in that direction.

In addition, EMA (N) contributed to, and fully supports the recommendations made in the submission from Business New Zealand to the discussion paper.

- 2.2 EMA (N) agrees with the objective stated in paragraph ten of the discussion paper:

"A well-functioning market should provide a reliable supply of electricity at efficient or competitive prices, that is, prices which are as low as possible consistent with ensuring reliable supply over the long term"

- 2.3 Although the discussion paper is not specific about what this market might look like, we concur with Business New Zealand's analysis in that it should be:

- a) a market-based framework where generators and retailers of any size are competing vigorously over a robust transmission network, and businesses and residential consumers are trading in a way that enables them to manage their risks at efficient prices;
- b) a focused, stable regulatory and governance framework delivering an investment climate where local and international firms feel comfortable enough to risk their capital to invest in the right generation technology at the right cost at the right time;
- c) a market where the participants are confident to use the electricity market, rather than the political process, to resolve their energy pricing and security of supply issues, and where politicians in their turn are willing to set policy but then leave the market to deliver the outcomes; and
- d) Where transparency of information about the industry's state of health is regularly delivered in a form that facilitates understanding and debate about the sector's performance

### 3. SECURITY OF SUPPLY

- 3.1. *The discussion paper recommends that consumers receive compensation if public conservation campaigns are activated, and that in addition there is a floor put under the spot price during such campaigns.*

EMA (N) agrees with both of these proposals. We don't believe that generators should have the option to under invest in generation capacity and then have a free "get out of jail" card in the form of a public conservation campaign should there be a shortage. We believe that any public conservation campaign should have a built in price signal for generators, and this could well be in the form of a payment to consumers who make savings. Such a payment would also greatly incentivise the market to make savings. Public conservation should be a commercial option, not a social, uncompensated option.

We agree in principle regarding the spot price floor, but would like to see more detail on how it might work before endorsing this idea.

- 3.2 *The discussion paper recommends that roles and responsibilities around security of supply be clarified.*

Once again we agree in principle but would need to see more detail about how this would work before commenting further. We refer you to the comments on this topic in the Business New Zealand submission.

- 3.3 *The discussion paper recommends that the reserve energy scheme be phased out and that the Whirinaki plant be sold or reassigned to an SOE.*

We agree with this recommendation. The present reserve energy scheme blunts price signals to investors and discourages participants from hedging

risk. We would prefer the sale to be to a private sector entity rather than to an SOE.

- 3.4 *The discussion paper recommends that SOE generators should be required to disclose their risk positions and other relevant information in the same way as private sector companies listed on the stock exchange, to improve the quality of information available on risk and to sharpen risk management incentives.*

We agree. Some standardised form of disclosure for these entities is appropriate.

- 3.5 *The discussion paper also recommended that government investigate developing terms and conditions for accessing 'reserve water' in lakes during dry year emergencies, the application of which would cap benefits to generators and in addition provide for compensation to affected communities and mitigate or avoid environmental effects.*

We think that this is a good idea in principle but needs serious thought as to the details of how it might work. We are a little concerned about the possibility of "perverse outcomes" consequent upon the crown stepping in to interfere with the market process. There may, for instance, be property right consequences for those who hold consents for alternative uses such as irrigation etc. The whole question needs to be carefully thought through.

#### **4. RESTRAINING THE COSTS OF GENERATION**

- 4.1 *The discussion paper also recommended that government ensure, when making decisions on climate change policy that full weight is given to the importance of providing certainty for investors including, to the extent possible, providing for stability and predictability on the future cost of carbon and other emissions.*

We agree. There has been a lamentable trend in recent years for governments to use energy policy as a proxy tool for achieving their climate change goals. In EMA (N)'s view this is a totally inappropriate use of energy policy. Energy policy needs to deliver security of supply at lowest possible cost for the good of the economy and all the New Zealand public. Instead we have had misguided and ill informed measures, such as the thermal ban, which contribute negatively towards energy policy goals and are there simply to achieve the aims of climate policy. In our opinion the goals of energy policy need to come first, for the good of NZ Inc. and if climate goals are able to be supported well and good, but let us not put the cart before the horse. In like manner although energy policy is not a proxy for climate policy, the impact of climate policy, both direct and indirect on the energy sector needs to be carefully considered. As the cost of carbon is going to impact quite significantly on energy pricing, and thereby on the productive sector, some certainty around this price is needed. In this respect the announcements of 14 September 2009 on changes to the ETS are welcome and are a step in the right direction.

- 4.2 *The discussion paper also recommended that government ensure that the current reviews of the Resource Management Act and water allocation consider a number of matters in relation to call-ins, fast tracking of consents, providing water for geothermal rights, and other matters.*

We have no specific comment in this area but support the views of Business New Zealand as expressed in their submission.

- 4.3 *The discussion paper also recommended that government ensure that the current petroleum resources review takes full account of the importance of gas to electricity generation using existing or new assets*

We agree. We want to see a policy of active encouragement of exploration for oil and gas on NZ's continental shelf. Our continental shelf is a huge area and will contain petroleum and gas resources of major significance, and yet to date only 8% of it has been explored. Gas, often discovered as a by product of petroleum exploration, is the fuel of choice for thermal base load stations and so ongoing exploration should be a key plank in our energy policy.

- 4.4 *The discussion paper also recommended that government consolidate responsibility for the promotion of energy efficiency in EECA, and removes it as a responsibility of the electricity regulator.*

We agree. The whole area of responsibility for energy efficiency has been divided and confused. Clarity over who is responsible, together with adequate funding for the role should fix that problem.

## 5. **IMPROVING PROCEDURES FOR UPGRADING TRANSMISSION SERVICES**

The discussion paper made two recommendations on improving procedures for upgrading transmission services. These were:

*Amend the Grid Investment Test (GIT) to make it clearer, simpler and less prescriptive, and to take into account wider competition benefits*

We would agree that the GIT could do with a bit of "fine tuning". However we think that in many respects the GIT in its present form has done good service for NZ, delivering us transmission projects at prices considerably below those first proposed by Transpower. The GIT has in fact done the job it was intended to do albeit in some cases rather too slowly and with too much duplication of effort. So we support some changes, but would like to see more detail about what is proposed.

*Transfer approval of major grid upgrades to the Commerce Commission to ensure integrated consideration of transmission expenditure, performance and prices, subject to rules on service and reliability standards, pricing methodologies and the grid investment test set by the electricity regulator.*

This seems to be a good suggestion. We support the views of Business New Zealand as expressed in their submission.

**6. IMPROVING WHOLESALE AND RETAIL COMPETITION**

- 6.1 The discussion paper gave three options for restructuring SOE generator-retailer assets:

*Option One: Create a new SOE generator-retailer comprising the Huntly and Manapouri power stations, and, additionally, transfer Tekapo A and B to Genesis and Whirinaki to Meridian.*

*Option Two: Transfer the Huntly power station to Solid Energy, the Manapouri station to Genesis and the Whirinaki station to Meridian.*

*Option Three: Transfer the e3p and P40 power stations from Genesis to Meridian and the Manapouri power station from Meridian to Genesis.*

We think that there is merit in the idea of an asset swap but that this is not an action that should occur in advance of other recommendations in the discussion paper. We believe that before any decisions are made about the detail of an asset swap there is a need for further work on principles and practice around how such asset and retail share reallocations might best be done. This work should be done sooner rather than later.

- 6.2 *The discussion paper recommended allowing lines companies to provide electricity retailing services in their local areas.*

The reason given is that such a move “may help provide more retail competition”. We disagree. We think that vertical integration of this type could be equally likely to result in monopolies, particularly in regional areas serviced by the smaller trust owned lines companies which would be at a competitive advantage with respect to other retailers.

A better idea would be to allow lines companies to enter the generation market as competition at the generation level is more likely to lead to downward pressure on retail prices.

- 6.3 *The discussion paper recommended a number of measures to facilitate consumer switching and recommended a funding provision to fund these activities.*

We acknowledge the fact that switching levels are not as high as they could be but we are opposed in principle to spending taxpayer money on helping achieve the financial goals of private commercial entities. Less than optimal switching levels is not a market failure of significance that justifies this sort of

intervention. We would have thought that it would be better for each generator-retailer to market the benefits of its own commercial offerings at their own cost in the normal way and then leave the market mechanisms to operate. Perhaps a more appropriate role for government to encourage switching could be to establish some rules around switching so that customers can switch quickly and reliably (say within 3 days). A policy of this type should not require the expenditure of huge amounts of taxpayer money.

## **7. IMPROVING GOVERNANCE OF THE ELECTRICITY SECTOR**

7.1 *The discussion paper recommended that the Electricity Commission be replaced with an Electricity Market Authority. The Electricity Market Authority's objective would be to ensure the efficiency of the electricity market, including reliability, for the long-term benefit of consumers. The functions of the Electricity Market Authority would be:*

- *Developing and approving market rules (including guidelines and model contracts).*
- *Monitoring compliance with rules and, through a Rulings Panel, penalising breaches.*

*The Electricity Market Authority would not have a role in approving major Grid upgrades. This role would be transferred to the Commerce Commission. The Electricity Market Authority would also not have a role in Energy Efficiency promotion. This role would be transferred to EECA.*

EMA (N) agrees that the issues of energy efficiency and affordability should be removed from the role of the regulator. We agree that it makes sense to transfer the approval of major grid upgrades to the Commerce Commission. EMA (N) also agrees that a new regulator is required to replace the Electricity Commission, but we question whether the establishment of an Electricity Market Authority is the best answer. In some ways, with the reduction in scope of the regulators activities, this is like using a sledgehammer to crack a walnut. We concur with Business New Zealand in thinking that greater effort and thought needs to be put into other possible options. We are not convinced that a Crown Entity type structure is necessary.

We endorse the arguments on this topic put forward in section 8 of Business New Zealand's submission.

**We do not wish to be heard in support of our submission**