

22 March 2019

## The TPM Group

We are group which formed in 2016 because we were concerned about the Electricity Authority's (EA) proposed changes to the transmission pricing methodology (TPM) guidelines.

We comprise organisations from right across the electricity sector including large consumers, energy consumer trusts, stakeholder groups, electricity network companies, and electricity generators and retailers. Active members of the TPM group since formation are:

- Counties Power
- EMA Northern
- Federated Farmers (Auckland and Northland)
- Horizon Networks
- Norske Skog Tasman Ltd
- Northpower
- Oji Fibre Solutions
- Top Energy
- Trustpower
- Entrust
- Vector

The TPM Group meets regularly, face to face and via teleconference.

Various TPM Group publications and events have also been directly supported by:

- The Northland Mayoral Forum
- Northland Inc
- The Mayor of the Far North District Council
- The Mayor of Kawerau District Council
- EA Networks (Ashburton)
- New Zealand Federated Farmers
- Auckland Chamber of Commerce
- Counties Power Consumer Trust
- Auckland Airport

The TPM Group has been and remains concerned about both the poor processes the EA ran to come up with a proposed new TPM, timing issues and the ongoing impact of its proposed reform, particularly on end users including vulnerable consumers.

At a meeting the TPM Group asked for and held with the EA's chief executive and senior managers on 8 February this year, we were told that the EA intends to press ahead with TPM guideline changes that "*will be very similar to (that proposed by the EA in) 2016,*" and will include a new cost-benefit analysis on that preferred option. The EA Board, we were told, "*is not mindful to do a cost-benefit analysis on any other option.*" We are concerned by the EA's repeated tendency to pre-determination outcomes, despite an acknowledgement at that same meeting that the TPM Group had "*made a fair point about the lack of (EA) feedback*" on multiple expert submissions received on the EA's 2016 and earlier proposals for change

(summarised in a paper we commissioned from COVEC and published in 2017 – conclusions attached in Appendix Two).

On that note, we do want to record our disappointment that the Panel made no recommendations on improvements to the EA's processes, despite finding in its First Report that the EA's process had been deeply problematic. The EA has promised a "*better process*" in the next/final round of its TPM proposals, but the EA's position is clearly unchanged, so providing more time for "*consultation*" and "*regional technical fora*" seems a complete waste of time as they already have the solution.

## **Addressing the EPR Options Paper**

*The below submission is made on behalf of all active TPM group members, except for Vector and Entrust who are submitting separately.*

### Section E: Improving transmission and distribution

Option E1: The TPM Group strongly supports the Panel's proposal for the Government to issue a Government Policy Statement (GPS) for transmission networks that sets out its policy objectives for transmission pricing.

The Panel's terms of reference require it to consider how regulatory frameworks can be improved to facilitate the delivery of fair and efficient prices as technology evolves and New Zealand transitions to a lower emissions future. We think a GPS will do this by providing the EA with a clear direction on how the Government thinks efficiency/equity trade-offs should be resolved in the context of transmission pricing.

The Panel has requested comment on Transpower's draft GPS. We note Transpower's GPS goes beyond network pricing and includes suggestions about how regulatory frameworks could be advanced to facilitate a transition to a low emissions future. Those topics are outside the remit of the TPM Group.

We therefore attach an alternative GPS (and accompanying explanatory diagram) for the Panel's consideration in Appendix One. This GPS was drafted independently by consulting firm Law+Policy, commissioned by Trustpower. It includes relevant material from the Transpower GPS.

The TPM Group would favour a mandatory GPS, where the EA would be required to "*give effect to*" the GPS, rather than the weaker requirement to "*have regard to*" the GPS (as provided for under the Electricity Industry Act 2010). However, for the reasons noted in Appendix 1, we think a GPS issued under existing legislation is a useful intermediate step.

Option E2: There is growing support amongst the TPM Group for a GPS for distribution pricing.

Recent submissions on the EA's proposals for reform of distribution pricing show that the EA appear to be at odds with the rest of the industry on how the Low Fixed Charge Regulations are impacting distributors' ability to reform tariff structures and the need for distributors to engage with stakeholders, take into account practical considerations and manage transitions when implementing reform. As a consequence, the group thinks the GPS needs to provide guidance in the area of distribution pricing as well. The GPS in Appendix One addresses this as well.

## Section F: Improving the regulatory system

Option F2: The TPM Group does not support the Panel's view that a transfer of the EA's network rule-making functions to the Commerce Commission is not required.

All the evidence, including all the process and evidential issues detailed in the COVEC report, through to our recent meeting with the EA, strongly suggests that preserving the status quo will simply result in the continuation of the current set of problems.

Option F1: It follows that the TPM Group does not support the EA being given clearer, more flexible powers to regulate network access for distributed energy resources, as we think these powers should reside with the Commerce Commission.

Setting aside transmission and distribution pricing reform, we think having two different regulators address distributors' revenue requirements (including investment expenditure), quality and service performance and risks does not make sense.

Option F3: The TPM Group has significant concerns around fairness and consumer protection but consider they are best addressed by Government through a GPS clarifying how the EA should apply its current statutory objectives for the long-term interests of consumers, and other proposals such as the Consumer Advisory Council proposed in option A1, rather than through changes to the EA's statutory objectives. Adding further statutory objectives, as the Panel notes, simply creates internal conflict for the EA, and forces a small unelected Board to make tradeoff decisions for which they face limited accountability.

Option F4: The TPM Group supports merits review of regulatory decisions.

We do not understand why there should be a separate treatment for Commerce Commission IM decisions (where merits appeals are allowed) and the EA's regulatory decisions (which can only be appealed on the notoriously uncertain judicial review grounds). Both regulators have the power to make regulatory decision which have a significant impact on the sector.

Our view is that the prospect of a merits appeal of a poorly justified decision is likely to significantly reduce the prospects of that decision occurring in the first place. This will be of benefit to all stakeholders. Certainly the TPM Group's experience throughout the TPM process to date is testament to the fact that merits review of decisions is required.

Yours sincerely



**Brett O'Riley**  
Chief Executive  
EMA Northern



**Ajay Anand**  
Chief Executive  
Horizon Networks

**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



**Judy Nicholl**  
Chief Executive  
Counties Power

**Appendix 1 (see attachment)**

**Draft Government Policy Statement for transmission and distribution and explanatory diagram**

## Appendix 2

*Extract from “Expert Review of Expert Reviews of Transmission Pricing Methodology Reform Proposals” published 23 February 2017 by COVEC Ltd (available on request).*

*Chapter 6, ‘Conclusions’ (whole chapter, paras 294-305)*

*(We have added bolded the text for emphasis)*

### 6 Conclusions

294. The source materials for this review show that the EA has consistently sought to do three things: abandon the current separate charge for the HVDC link; create new transmission charge based on the benefits of individual transmission investments; and extend this beneficiaries-pay charge to existing grid assets approved since 2004. These goals have also been consistently linked together: the EA has always proposed that the costs of the HVDC link be included in its asset-based beneficiaries-pay charge.

295. **These three consistent goals did not emerge from a disciplined policy development process.** This is most apparent from reading the first issues paper (October 2012) in which the EA did not separate its review of the existing TPM Guidelines from its proposals for change. The first issues paper described the problem the EA was addressing as the absence of the solution it preferred. This approach left readers unclear as to whether a review had actually been undertaken. Moreover, **it was not until September 2014, after a further seven working papers had been issued for consultation, that the EA explicitly consulted on its problem definition.**

296. While the problem definition was sharpened somewhat as the review progressed, substantial criticisms remained. Over time, expert arguments against the (evolving) problem definition focused more heavily on the EA’s description of the interconnection charge problems and the durability problems, and on the EA’s estimates of the scale and materiality of problems.

297. **Alongside these concerns about the problem definition, experts have been very critical of the EA’s proposed beneficiaries-pay charges, including the core features of asset-level benefit charging, and the inclusion of pre-existing assets, which have remained in place since the first issues paper in October 2012. Carefully drafted expert reports have examined in detail the way these proposals are likely to affect the conduct of grid users, and concluded that there are serious problems with the EA’s analysis.**

298. The EA has modified its proposals over this period but remained firmly in favour of highly detailed asset-level estimation and allocation of benefits, and firmly in favour of extending beneficiaries pay charges to pre-existing assets approved since 2004.

299. I have been left with the impression that the EA has not been heavily influenced by the criticism these experts have made of its proposals. **While there have been many consultation papers since October 2012, and the proposals have changed over that time, the EA remains firmly committed to the original two underlying goals.** Indicators for this conclusion include:

a. NZIER, which has been much less critical of the EA's proposals than many experts, noting in response to the second issues paper the curious fact that *"the application of the same set of 'decision-making and economic framework' in TPM1 and TPM2 principles has led to a markedly different allocation of costs between EDBs and direct connect industrials"*.

**b. Despite years of work to refine and explain the proposals, the expert reports are unanimous (12 – 0) in disagreeing with the proposition that *"the EA has established that an AoB charge will send desirable price signals"*.**

**c. By far the most rejected proposition I have assessed, is the most fundamental of all of the propositions, that *"the AoB charge is superior to the alternatives"*. My review found unanimous (32 – 0) disagreement on this point in the expert reports.**

300. As an independent regulator, the EA is expected to stand-up to vested interests when that is necessary to fulfil its statutory obligations. So the *volume* of criticism identified in this review should not necessarily be determinative. Instead, the EA is obliged to dispassionately weigh up the evidence in reaching its determinations. Often this weighing up process is reflected in a regulator's consultation papers, including with citations to submissions making the arguments that are being weighed up.<sup>21</sup>

**301. For the most part, the EA's style throughout this process has been to avoid citing particular critics. Instead it has tended to refer to "submissions" in the aggregate, without identifying particular arguments made by individual experts, claim they have been considered and then reiterate the EA's view. This style is unfortunate in the current context, where there is a substantial weight of expert opinion that opposes the EA's desires: it suggests that the EA is not actually engaging with the submissions.**

302. To illustrate this point, consider the question of whether AoB charging should apply to new assets only (Application B) or to all assets installed since 2004. I choose this topic because it is one of the few on which the EA has engaged substantively with expert submissions. Prior to the second issues paper, expert opinion on this question was unanimously (15 – 0) against including pre-existing assets. Those fifteen expert reports argued (see section 5.1 above) that there were no clear dynamic efficiency benefits from such backdating on a beneficiaries-pay basis, but clear static efficiency losses. The EA's second issues paper responded (at ¶5.97 – 5.98):

*"the dynamic efficiency gains from applying such pricing to historical assets are restricted to future modifications of those assets, and so are much weaker than implied in paragraphs 5.91 to 5.96 above. Arguably, therefore, in these circumstances a stronger emphasis should be placed on allocative efficiency, and so a greater focus on approximations to 'lump sum' charges for recovering the cost of those investments. Nevertheless, the Authority is of the view that there are good reasons to apply service-based and cost-reflective pricing approaches to recent major historical investments as well as future investments"*

<sup>21</sup> See, generally, the consultation papers issued by the Commerce Commission during its development of Input Methodologies. These papers frequently referred to specific submissions, despite being produced under onerous timelines dictated by legislation.

303. Despite the EA's attempt to justify this position, a (5 – 2) majority of experts commenting on the second issues paper remained unconvinced. I have explained above (¶274) why I agree with the majority.

**304. A second and rather stark example concerns the EA's arguments over the durability of the TPM. Throughout the period under review, the EA has consistently argued that its**

preferred TPM Guidelines would be more durable than the status quo because there will be less arguing and lower costs of disputes. The experts disagree by a margin of eight to two. This is one topic on which the number of submissions seems particularly relevant. Most of the people currently arguing with the EA disagree with the EA that there will be less arguing if the EA pushes this proposal through.

305. Based on the above review and analysis I consider that the vast majority of expert opinion has disagreed with the EA throughout this review, and that the EA has not attempted to explain why it disagrees with these experts.”

END OF CHAPTER.