Transmission Pricing Review – 2019 Issues Paper

Submission to the Electricity Authority – Public Version

Introduction

1. Vocus welcomes the opportunity to submit in relation to the Electricity Authority's 2019 TPM Issues Paper.
2. If you would like any further information about the topics in our submissions or have any queries about this submission, please contact:

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Summary of Vocus' views on TPM reform

3. As the Authority is aware, Vocus does not consider the Authority should be progressing its TPM review and proposals while other, more important, projects which could help better promote competition are stalled or taking far longer than they should.
4. We are particularly concerned about the way the wholesale electricity and hedge markets have been functioning, and related gentailer conduct. Given the serious and growing problems in the wholesale and hedge markets, we do not consider the Authority has its priorities right.
5. We find it somewhat incongruent that the Authority has put much more important projects, such as the two-tier retail market/saves and win-backs, on hold pending the outcome of the Electricity Price Review, but has not done the same for the TPM review, particularly given the Review Panel's evident scepticism about the Authority's proposals.
6. Vocus does not support radical change to the TPM or the Authority's TPM proposals, including removal of peak-usage pricing. Given the Authority has decided to continue with the TPM review, it should consider pragmatic transmission pricing options, which have been proven internationally, in order to bring the review to a close.
7. Our clear view is that the predominant impact of reviewing the TPM would be the re-allocation of sunk and fixed costs amongst transmission customers, rather than improvement in efficiency or creating a more competitive market. This is illustrated by the review focus on treatment of existing transmission investments such as HVDC and NIGU.
8. In the joint submission from Ecotricity, Electric Kiwi, energyclubnz, Flick Electric, Pulse and Vocus in response to the Electricity Price Review Options Paper we stated, in relation to transmission pricing, *"The Independent Retailers do not support wealth transfers from consumers to generators such as Meridian and Contact"*.
9. Vocus considers that the Authority should take into account both efficiency and pricing impacts (wealth transfers). Failure to do so would result in a bias against initiatives to promote competition. We would not support any TPM proposals, or element of TPM proposals, including in relation to HVDC, that would result in negative wealth transfers from consumers to electricity generators.
10. We note the Authority plans to determine how the cost of historic investments such as NIGU are allocated between consumers and generators, based on 2014-18 data. We consider this

should be tested against more up-to-date 2018-19 data, given the step changes to the wholesale electricity market over this period. We would expect this to result in a substantially higher allocation to generators, reflecting the higher economic rents they have extracted from the market during this time.

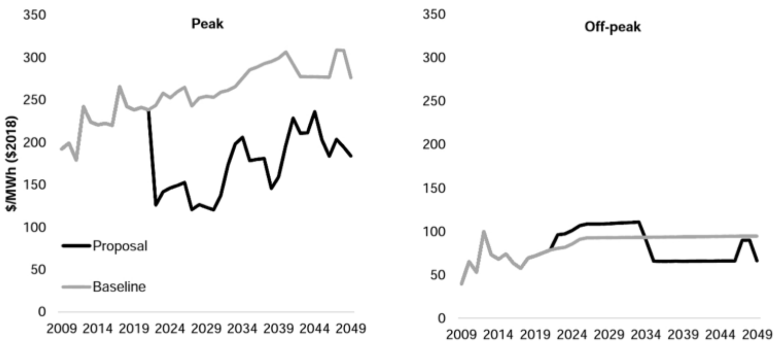
The Authority’s focus should be on urgent outstanding competition issues

11. Vocus does not consider the TPM review warrants the prioritisation the Electricity Authority has been giving it. In our 4 June 2019 submission on deferral of the Default Distributor Agreement (DDA) consultation, we advocated that the Authority should also defer other projects, such as the TPM review, to enable the Authority to refocus its immediate term work programme on resolving outstanding wholesale and retail competition issues.
12. Vocus does not consider the Authority should be progressing its TPM review and proposals while other, more important, projects are stalled. For example, the Authority had undertaken, in meetings with the independent retailers in March, that review of longer-term hedge market reform would be progressed by the end of the year this has not happened. The first consultation now won’t occur until October with the possibility of final decisions, at best, delayed until sometime toward the end of the 2019/20 financial year.
13. Vocus reiterates, from our DDA submission, that we consider the Authority’s priorities should be hedge market development, saves and win-backs/the two-tier market issue, strengthening wholesale disclosure rules (including financial separation, and internal transfer disclosure) and addressing spot market trading conduct issues. Each of these has the potential to promote a substantially more competitive and healthy electricity market, and deliver better long-term outcomes for consumers.
14. Given there has been a two and a half year gap since the last TPM consultation it isn’t obvious why there is a sudden urgency to progress the TPM review. During this time, there has been a notable deterioration in the outcomes from the operation of the wholesale and hedge markets.

Vocus considers that removal of peak-usage charges would result in higher spot prices and increased carbon emissions

15. The Authority’s analysis, and nearly all the benefits in the CBA, appear to be based on the premise that if transmission peak-usage charges (RCPD) are removed it would result in a dramatic reduction in peak and off-peak prices inclusive of interconnection charges (as depicted in the Authority graphic below).

Figure 1: Effective electricity prices (wholesale prices plus interconnection charges)



16. We consider this to be both counter-intuitive and implausible.
17. If Transpower were to remove its peak-usage pricing signal peak-demand would increase, as the Authority has indicated. This would result in an increase in investment in firm peaking generation to meet demand and would drive up spot prices, not reduce them. It would also require increased distribution network capacity which needs to be taken into account in the

CBA. If the Authority is wrong on this point then the positive net benefit it has derived from its CBA would be negative.

The Authority should take into account wealth transfers between suppliers and consumers

18. Vocus is unclear why the Authority has adopted a different interpretation to its statutory objective to that of the Commerce Commission under the Commerce and Telecommunications Acts, given they come down to promoting long-term benefit of consumers or end-users.

19. If the Commerce Commission had adopted a similar approach, and ignored wealth transfers, it would have had substantial negative repercussions for consumers e.g. the main benefit from the Commerce Commission decision to reduce Part 4 WACC percentile from 75th to 67th was from lower prices (wealth transfers from regulated suppliers to consumers).

20. Vocus considers that the Authority should take into account both efficiency and pricing impacts (wealth transfers). Failure to do so would result in a bias against initiatives to promote competition given that lower prices is one of the main benefits from greater competition, particularly in markets where the goods and services are largely homogeneous. This was clear from the MDAG saves and win-backs review which basically ignored the principle negative impact of saves and win-backs (over-charging sticky customers with “loyalty taxes”). This was despite the Authority’s own figures indicating the cost to consumers was in excess of $370m per annum, and the indications from the Electricity Price Review that $500+m per annum was closer to an accurate estimate of the size of the “loyalty taxes”.

21. We would not support any TPM proposals, or element of TPM proposals, including in relation to HVDC, that would result in negative wealth transfers from consumers to electricity generators. Vocus considers that South Island generators should pay for the cost of transporting electricity from the South Island to the North Island. The HVDC is essentially a connection asset required because of the supply-demand imbalance due to generation investment in the South Island

22. Based on what we have observed from the TPM review, the Authority’s focus on efficiency only has resulted in the Authority advocating changes, notably in relation to HVDC, where the negative wealth transfers are substantially higher than the claimed efficiency benefits. This impact is less transparent in the latest consultation as the Authority has not estimated the efficiency impact of removal of HVDC charges.

23. Regardless of how the Authority interprets its statutory objective, we consider it would be beneficial to be transparent about the efficiency and price impacts (wealth transfers) of the Authority’s proposals. This would be consistent not only with Commerce Commission precedent, and also the approach the Authority adopted in relation to its review of distributed generation pricing principles (see table below).

Table 1: Expected economic benefits and gross benefits resulting from the proposal, relative to the current DGPPs

	Expected economic benefits, in $million present value terms	Gross benefit to consumers, in $million present value terms
Current TPM	2.0 – 21.7	232 – 325
Current TPM for two years from April 2017, then area-of-benefit-based TPM	0.5 – 4.2	46 – 64 plus effect after 2019 (not quantified)

Problems with the impact of the price cap

24. Our concern about adverse price impacts is heightened by the problems with the Authority’s price cap. Why, for example, does Meridian get 96.77% of the benefit from its transmission

charge reduction in the first year, while Counties Power gets -45.39%? It appears that Counties Power and others pay more in the first year so that Meridian can receive virtually all of its transmission charge reductions straight away. The price cap should be designed to protect consumers not increase their prices.

25. Aspects of the price cap we consider are problematic and should be revisited include:

    (i) The cap is a cap on estimated retail prices rather than actual transmission charges.

    (ii) The cap only applies to certain components of transmission charges.

    (iii) The cap results in higher transmission charges for some transmission customers than if there was no cap.

    (iv) The cap results in very uneven changes to different transmission customers, with the cap having a much bigger impact for some customers than others which is not related to the size of the price increases they face.

What TPM reform should look like

26. If the current TPM is to be changed or reformed, Vocus' view is that:

    (i) The Authority should consider pragmatic transmission pricing options for any new TPM Guidelines, which have been proven internationally, in order to bring the review to a close. This would help avoid need for substantial continued TPM review resourcing during the development and approval stages for any new TPM so the Authority could focus on more important priorities.

    (ii) Peak-usage charges should be retained. It appears from submissions that there is an openness to considering reform of the current RCPD charges to make them more cost-reflective and better targeted.

    (iii) The reviews of electricity distribution and transmission pricing should be undertaken in a co-ordinated and complementary manner. While the Authority has claimed its position on distribution and transmission pricing is consistent, it is advocating distributors adopt peak-usage and time-of-use pricing at the same time as proposing removal of RCPD and precluding replacement with any form of permanent peak-usage pricing.

    (iv) The Authority should ensure any wealth transfers between suppliers and consumers are to the benefit of consumers. This would preclude any options which would require consumers to pay for HVDC.

    (v) The Authority should also ensure any TPM reforms avoid or mitigate price shocks to consumers, and allow businesses and industry to adjust to any rise in their cost base.

Vocus Group

1 October 2019