

Tuesday, 28 October 2014

Electricity Authority
P O Box 10041
Wellington

By email: submissions@ea.govt.nz

Dear Sir / Madam

Re: Working Paper – Transmission pricing methodology: Problem definition

Pioneer Generation (Pioneer) welcomes the opportunity to make submissions on this working paper that describes in more detail the problems with the current transmission pricing methodology from the Electricity Authority (Authority) perspective.

Pioneer does not support the revised transmission pricing methodology (TPM) proposed by the Authority in its October 2012 first issues paper. The subsequent working papers have been a time consuming and expensive process where the industry has provided the Authority with more information but has no more sense now than after the May 2013 conference of what the Authority might propose in its second issues paper.

Despite our position on the Authority's overall review, Pioneer does support the Authority's decision to publish an options paper which is due to discuss options for the combination of charges (including residual) that could be proposed in the second issues paper. It is important the industry gains an understanding of the likely direction the Authority is taking after the extensive working paper process. We submit the Authority should ensure it has sufficient time to fully take into account the submissions on the options paper before finalising the second issues paper (the current timeline has only one month between the end of the time allocated for the options paper and the start of the time allocated for the second issues paper).

However, Pioneer suggests there are two factors that could eliminate the need for the Authority's major review of the TPM, namely

1. the Authority should initiate a change to the transmission investment approval process; and
2. Transpower is undertaking an operational review the structure of its charges within the current Transmission Pricing Methodology guidelines.

1. Change the transmission investment approval process

The Authority states efficient investment focuses on the lowest cost development of the industry over time and efficient use of the grid focuses on charging the efficient marginal costs of production. The Authority has dedicated a significant portion of the working paper to discussing efficient investment and its view that the current process for identifying and approving transmission investments leads to inefficient transmission investment. As a consequence the Authority claims that more signals are required to ensure efficient transmission investment by using the transmission pricing methodology for allocating transmission costs. Further, the Authority seems to have the view that the limited expertise available to review / scrutinise transmission investment proposals means that inefficient investment in transmission is likely to continue.

The working paper includes what the Authority considers to be strong evidence that the current investment approval regime results in inefficient transmission investments.

Pioneer has no view about whether the transmission investment is efficient or not and has not engaged in the investment approval process. However leaving that aside, we wonder if the Authority had more confidence in the investment approval process would it be proposing such a complex TPM?

A complex TPM to encourage more efficient transmission investment appears to be a second order solution. We suggest the Authority should be trying to improve the investment approval process – either via a review of the capital expenditure input methodologies managed by the Commerce Commission or mounting a case for change to the regime with the Minister.

2. Transpower's operational review

Transpower is undertaking an operational review of its TPM within the constraints of the existing Guidelines for Transpower: Transmission Pricing Methodology. The purpose of Transpower's review is to determine whether there are problems with the TPM that could be addressed within the constraints of the existing Guidelines.

As you are aware, this operational review is looking at pricing regions, the value of N within the interconnection charge and the use of HAMI to allocated HVDC charges. This analysis overlaps with the Authority's consideration of whether the current interconnection and HVDC charges result in inefficient behavior by generators and the demand-side.

Pioneer supports Transpower's operational review. We expect Transpower to robustly quantify the efficiency gains of any changes it proposes. The efficiency gains from amending the current TPM within the constraints of the existing Guidelines may exceed the efficiency gains from the Authority's proposal especially when implementation costs are taken into account. Pioneer strongly submits that the Authority must be prepared to consider the option of not proceeding with its major review once it has had the opportunity to analyse the results of Transpower's operational review.

At a minimum, the overlap in topics being reviewed means the Authority must take into account the analysis and submissions made on Transpower's operational review when developing its options paper and second issues paper.

Submission by the Independent Generators Association

Pioneer supports the report commissioned and submitted by the Independent Generators' Association and prepared by ASEC, which addresses the entire working paper. In particular, we agree:

- that the Authority's proposal has little support and will not be durable (section 5);
- with the analysis regarding the impact of the interconnection charge on net load reduction, including embedded generation (section 6);
- the use of HAMI to allocate HVDC charges impacts generators that are not connected to the grid as well as grid connected generators (section 7);
- a volatile and unpredictable transmission charging regime will be economically inefficient (page 19); and
- it is not economically efficient to levy interconnection charges on generators (page 20)

Pioneer's comments on the working paper

Pioneer is motivated to comment specifically on Question 18.

With respect to the other questions raised in section 10 of the working paper, the analysis justifying the Authority's position on the interconnection charge and HVDC charge often, in our view:

- is based on spurious assumptions – for example, basing analysis on assumptions that can't be confirmed resulting in a conclusion where it is uncertain "which of the four scenarios most accurately describes reality";
- includes NPV estimates of efficiency losses for numerous situations where it is not clear whether there is double counting; and
- implies the Authority continues to be fixated with a complex solution – for example the use of Ramsey pricing to calculate the deadweight loss of variabilised transmission charges.

Question 18: Do you agree that the interconnection charge and ACOT payments may oversignal the value of embedded generation? Please explain your answer.

We note that the working paper states that

"The Authority is yet to complete its consideration of submissions on the ACOT working paper so has yet to reach a final position on the efficiency or otherwise of the ACOT arrangements. The matter will be addresses in the second issues paper." (page vii)

and

"At this point, the Authority has not formed a final view on the extent to which the interconnection charge appropriately signals the value of embedded generation." (paragraph 11.88)

and

"At this point, the Authority has not formed a final view on the overall efficiency of ACOT payments." (paragraph 11.95)

Having made these statements Pioneer finds it contradictory and disappointing that Question 18 then asks if submitters agree with the Authority's view that "... ACOT payments may over-signal the value of embedded generation?"

Pioneer, and others, made significant submissions on the ACOT working paper. The Authority's summary of submissions clearly shows that the majority of submitters disagree with the Authority's views.

We note the short analysis in the problem definition working paper:

- uses the same numbers as in the ACOT working paper – many submitters provided feedback about the Authority's numerical analysis that should be used by the Authority in forming any views;
- now claims that the interconnection charge over-signals the value of embedded generation when the ACOT working paper concluded that ACOT arrangements result in little effective locational signaling for distributed generation or transmission investment; and
- in the ACOT working paper the Authority argued that the availability of the underlying renewable resource influences the location of distributed generation to a far greater extent than access to ACOT payments (and therefore interconnection charge).

As stated previously Pioneer does not agree with the Authority's views with respect to embedded generation. We refer to our submission on the ACOT working paper.

In summary, Pioneer Generation is concerned to ensure market arrangements promote competition, reduce barriers to entry and achieve the efficient end to end delivery of electricity for the long term benefit of consumers. In our view, the Authority should be focused on simplifying the industry as the current complexity creates confusion and distrust from consumers and represents a significant barrier to new entrants and innovation.

Yours Faithfully,



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