

8 August 2017

Submissions
Electricity Authority
PO Box 10 041
Wellington

By email: submissions@ea.govt.nz

Dear Carl,

**Re: Draft decision on Application for exemption from arm's-length rules:
Top Energy Limited**

Pioneer Energy (Pioneer) welcomes the opportunity to make comments on the draft decision by the Electricity Authority (Authority) on Top Energy's application for an exemption from arm's-length rules relating to its subsidiary Ngawha Generation Limited's (NGL) investment in the Ngawha geothermal generating plant which NGL plan to expand to 65MW.

In our first submission on this exemption application Pioneer noted three specific competition concerns the Authority might consider while developing its exemption decision, namely:

- At a principles level, we are concerned about the degree to which Top Energy's (Top) total generation investments will exceed the 50MW legislative threshold. This threshold is based on carefully considered public policy and was subject to consultation and the scrutiny of Parliament.
- The costs avoided by Top (of \$1.0m – \$1.3m per annum¹) if an exemption is granted place Top's generation business at a competitive advantage relative to a third party that might consider investing in that distribution network.
- The issue of competitive neutrality is becoming more important with the increasing availability of new technologies or business models that can provide network support services.

Our understanding is the decision to grant an exemption to Top Energy for their Ngawha expansion project, at up to 65MW nameplate capacity, is on the basis that the Authority considers that:

- cost savings achieved through sharing of management services between regulated networks and unregulated generators, to achieve economies of scope or scale, is not a competitive energy markets issue.

¹ Source: paragraph 5.9 of Authority's draft decision paper <https://www.ea.govt.nz/dmsdocument/22314>

- Ngawha’s generation profile under the Authority’s factual and counterfactual tests will not materially influence network support services or national wholesale spot market prices, such that Top can be exempted from the policy thresholds.
- related management incentives and local retail competition may be competition issues, and that;
 - Part 6 of the Code and DGPP rules have adequate provisions ensuring competitive neutrality for connection and pricing terms and conditions with competing local generators
 - Part 4 of the Commerce Act has adequate accounting separation provisions to ensure appropriate allocation of costs between network and generation businesses.
- a 10 year exemption term is appropriate to ensure investment certainty for Top, whilst also acknowledging market changes are likely over the medium term.

Pioneer appreciates the supporting commentary provided in your draft decision paper. We acknowledge and note the different levels of legislative protection afforded Pioneer and other competing generators as outlined in the draft decision report.

We are, however, concerned that the draft decision paper does not address the underlying principles of the legislation that has a 50MW local generation and 250MW grid connected generation threshold. We believe there are also inconsistencies between this draft decision and recent Authority decisions on rule changes applying to local generation. We elaborate on these points of principle below:

- The Electricity Industry Act has 50MW and 250MW “line in the sand” thresholds for broader reasons than the impacts on wholesale market prices the Authority tested. These are two quite separate threshold tests and so should be treated as such. We believe the purpose of the current thresholds was to ensure confidence for the generation sector when investing that the levels of costs, risks and returns are consistent across all different owners of generation assets. These important principles have not yet been addressed by the Authority in its decision making.
- The Authority, in its December 2016 DGPP decision, stated that the avoidance of transmission costs (i.e. costs for transmission services not used by DG) created an unfair competitive advantage to DG providers. This contradicts the Authority’s approach in this draft decision that avoiding \$1.0m - \$1.3m per annum in costs through sharing overheads with a regulated business is deemed to be not relevant².
- The DGPP decision also signaled the Authority’s intention to revisit in the next 2 - 3 years the competitive neutrality and level playing field questions as well as the allocation of network costs. This has created significant investment uncertainty

² Ibid. See paragraph 7.64

“7.64 Cost efficiencies through shared management are available to any business in the industry of sufficient size, and not related to the specific relationship of Top as a distributor and NGL as a generator. Therefore, the Authority does not consider these efficiencies to be within the scope of the assessment criteria.”

for all existing DG investors³. This is in stark contrast to the Authority's draft decision to grant Top a 10 year exemption term on the basis that

"7.88 The Authority considers 10 years is appropriate to provide a level of certainty to Top and NGL for their investment, while accounting for the high possibility of major changes in the electricity industry that could impact the relevant markets."

Pioneer questions how the Authority can, on the one hand, provide 10 years of investment certainty to a distribution company building DG but, on the other hand, decide to remove any level of investment certainty from all other DG investors and their competitors. The Authority has stated on a number of occasions throughout its DGPP consultation process that it is ...not required to consider wealth transfers and investment certainty for rule changes – so why now consider these criteria for a rule exemption decision?

- We believe new provisions will be required in Part 6 of the Code and in Part 4 of the Commerce Act to ensure competitive neutrality between distribution and generation businesses for network support services. We therefore question how the Authority can even consider the second Top Energy exemption application, for 26MW of network support generation when the DGPP Code remains unresolved for all other DG investors until at least 2020? The draft decision also concludes that the Ngawha expansion will not be capable of providing network support services. We therefore expect Top will not be paying NGL any avoided cost of distribution (ACOD).

Pioneer has no issue with Top Energy and any other distribution company building local or national generation provided that all generation investors are operating on the same terms and within the current market rules. If the rules no longer apply then they should be changed by consideration of the collective costs and benefits across all players, not changed through individual case exemptions that confer competitive or pricing advantage on individual players.

The competition issues we have highlighted are much broader than the analysis undertaken by the Authority. In our view, these wider competition issues should be addressed at the big P policy level before exemptions from the current rules are granted. We have, on many occasions, requested that the Authority, Commerce Commission and MBIE, together with industry, establish a Cross-Agency working group with the express purpose of aligning government policy, regulations and rule changes that reflect the changing environment for both existing and new investors in DG and other emerging network connected technologies.

We request again that these broader policy and Code principles be addressed before any exemptions are granted. In our view, there is no urgency to make a decision about this exemption application as Top has said they will progress the expansion with or without an exemption. Therefore Top can continue to plan and construct the Ngawha expansion, due to be commissioned in 2020, while the appropriate policy debate is undertaken and decisions reached (probably late 2018). If an exemption is still the right mechanism then the Authority can make its decision at that stage.

³ IEGA commissioned PwC to estimate the enterprise value impact of the Authority's May 2016 DGPP proposals. The 27 July 2016 DGPP submission includes this report. PwC estimated \$0.5bn to \$1.5bn could be wiped off the value of DG investment if the proposals were implemented.

We would be happy to meet with the Authority to discuss these points in further detail.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Fraser Jonker'. The signature is stylized with a large 'F' and 'J'.

Fraser Jonker
Chief Executive