

# Ministerial Briefing: Electricity Authority appropriations for 2018/19

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<b>Date:</b>	13/02/2018	<b>Priority:</b>	High
<b>Security Level:</b>	In confidence – budget sensitive	<b>File Number:</b>	1085583

## Key Action Sought

Minister of Energy and Resources	<p><b>Note</b> the Electricity Authority has completed consultation on its proposed appropriations for 2018/19 in accordance with s129 of the Electricity Industry Act 2010 (the Act).</p> <p><b>Note</b> no changes have been made to the proposed 2018/19 appropriations as a result of consultation.</p> <p><b>Agree</b> to submit the proposed Electricity Authority appropriations and new initiative bid for Budget 2018.</p> <p><b>Agree</b> to the publication of this report after Budget day.</p> <p><b>Note</b> that the Authority will publish the <i>summary of submissions and Authority responses</i> along with this report.</p>
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## Contact for Telephone Discussions

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## Executive summary

The Crown funds the Electricity Authority (Authority) through appropriations of public money. The Crown recovers the cost of this funding, up to the level of actual expenditure incurred, through a levy on industry participants. The appropriations therefore have a neutral impact on the Government's operating balance and net debt. Also, any amount of the levy that is not spent is returned to levy payers after the end of each financial year.

Levies are charged to industry participants in accordance with the Electricity Industry (Levy of Industry Participants) Regulations 2010. These regulations are made on the recommendation of the Minister and are administered by MBIE.

During November and December 2017 we consulted on the Authority's 2018/19 levy-funded appropriations and work programme focus areas. This briefing contains a report on the outcome of that consultation and our 2018/19 appropriations request, in fulfilment of our obligations to you under section 129(2) of the Act.

The Authority's recommended appropriations for 2018/19 are summarised in the table below.

### Appropriations proposed after consultation

Electricity Authority	\$ million	
	Appropriation 2017/18	Proposed appropriation 2018/19
<b>Operational appropriation</b>		
Electricity industry governance and market operations	73.937	74.270
<b>Contingent appropriations</b>		
Managing the security of New Zealand's electricity supply (1 July 2017 to 30 June 2022)	6.000 over five years	
Electricity litigation fund	1.000	1.000

### Electricity industry governance and market operations

Following consideration of feedback received from the consultation process, the Authority recommends the appropriation level as consulted on of \$74.270 million.

This level of funding is sufficient to meet the Authority's obligations in respect of the long-term contracts with the service providers who operate the electricity system and markets. These services comprise over 70 per cent of the costs within this appropriation, and for 2018/19 are budgeted as follows:

- System operator (\$43.460 million)
- Clearing manager (\$2.382 million)
- Wholesale information and trading system manager (\$1.702 million)
- Pricing manager (\$0.764 million)
- Reconciliation manager (\$0.936 million)
- Registry manager (\$0.654 million)
- FTR (financial transmission rights) manager (\$0.963 million)
- Extended reserves manager (not yet contracted, but budgeted at \$0.350 million)

- System amortisation, depreciation, and IT costs that underpin the service provider functions (\$1.880 million).

The recommended appropriation is set at a level that continues to hold constant (in nominal terms) the funding for the Authority's own operating costs. This funding has been at \$18.7 million since 2012/13 and from that time has declined by five per cent in real terms. The \$18.7 million will enable the delivery of a challenging and comprehensive work programme in 2018/19, and we consider such a programme appropriate in the context of an electricity industry that is responding to technological advancements, changing consumer expectations and increasing uncertainty.

As occurs every year, there was mixed support for the proposed appropriation—including clear support from some parties, such as consumer agency Major Electricity Users' Group (MEUG). The mixed support across the sector is not surprising as the Authority's focus is on seeking better outcomes for consumers.

The feedback received on our proposed work programme focus areas will be considered during the course of the detailed development of the 2018/19 work programme. It is important to note that the Authority's work programme is developed for the long-term benefit of consumers, which does not always align with the preferences indicated in consultation feedback.

### **Real-time pricing**

In addition to the 2018/19 appropriation levels, we also consulted on the appropriation increases from 2021/22 that are required to enable the Authority's Board to make a decision to implement real-time pricing (RTP) in the wholesale electricity spot market. RTP will help 'future proof' the electricity system, unlocking opportunities for new technologies and business models. RTP would therefore play an important role in enabling the investments in distributed generation, battery storage, and demand response technologies required to transition New Zealand to a 100% renewable electricity system.

Following consideration of consultation feedback, which was generally supportive of implementing RTP, we intend to submit a new initiative bid in Budget 2018 for the appropriation increase (recovered from industry participants) required to implement RTP.

### **Managing the security of New Zealand's electricity supply**

This appropriation is intended to achieve enhanced security of supply in the electricity system during periods of emerging or actual security situations. We expect these situations to be rare and this appropriation is considered contingent in nature.

Following consideration of feedback, which was supportive of the proposed appropriation, no changes to the existing \$6.0 million appropriation are requested.

### **Electricity litigation fund**

This appropriation, which is also contingent, ensures the Authority is able to participate in litigation effectively and without delay. Our functions under this appropriation include defending cases against the Authority, and taking enforcement action under our enforcing compliance function.

## Summary of litigation against the Authority

Calendar year proceedings instigated	Instigating party	Type of proceeding	Result
2011	Genesis Power, Contact Energy, Todd Energy, Bay of Plenty Energy	Appeal to the High Court	Appeal dismissed by the High Court
2012	Genesis Power	Appeal to the Court of Appeal	Appeal abandoned
2014	Vector	Application to the High Court for a declaratory judgment	Application dismissed by the High Court
2015	Vector	Appeal to the Court of Appeal	Appeal abandoned
2015	Vector	Appeal to the High Court	Appeal abandoned
2016	Trustpower	Application to the High Court for judicial review	Application declined by the High Court
2016	Vector and Entrust	Application to the High Court for a declaratory judgment	Application declined by the High Court
2017	Vector and Entrust	Appeal to the Court of Appeal	Fixture date in April 2018 to be confirmed
2017	City Financial	Appeal to the High Court	Fixture allocated on 5-8 June 2018

The above table outlines the history of litigation against the Authority. A review of the submissions shows that many of those opposed to the proposed \$1m litigation fund have a history of entering into litigation against the Authority. None of them have succeeded.

Following consideration of consultation feedback we have not changed the recommended appropriation level from that consulted on.

An appropriation level of \$1.0 million will help ensure the Authority is well placed to deal with any additional litigation that may arise, and thereby continue to act effectively for the interests of consumers. As noted earlier, the levy will only recover up to the level of actual expenditure incurred.

# 1 Introduction

- 1.1 Section 129 of the Act requires the Authority to consult on proposed appropriations for the coming year before seeking appropriations from the Minister.
- 1.2 This paper sets out the results of the consultation on our proposed appropriations and work programme focus areas for 2018/19. It includes the recommended appropriations for submission into the Budget 2018 process.

# 2 Consultation

- 2.1 Consultation on the proposed appropriations took place from 21 November 2017 to 19 December 2017. The submissions were published on the Authority's website on 13 February 2018.<sup>1</sup>
- 2.2 The consultation paper also sought feedback on the focus areas of the Authority's work programme.
- 2.3 There are approximately 89 levy paying entities; we received 13 submissions from the following respondents:
  - (a) Nine from levy payers and their owners: Aurora Energy Limited (Aurora), Contact Energy Limited, Cumulus Asset Management, Entrust (majority shareholder of Vector), Mercury NZ Limited (Mercury), Meridian Energy Limited (Meridian), Transpower New Zealand Limited (Transpower), Trustpower Limited (Trustpower), and Vector Limited (Vector).
  - (b) Four from representative bodies: the Employers and Manufacturers Association (EMA), Consumer NZ, the Electricity Retailers Association of New Zealand (ERANZ), the Major Electricity Users Group (MEUG)
- 2.4 *A summary of submissions and Authority responses* is included in Appendix A, and the appropriations consultation paper is provided in Appendix B.
- 2.5 These submissions will inform the development of our 2018/19 Statement of Performance Expectations (SPE) and 2018/19 work programme.
- 2.6 The draft SPE for 2018/19 will be provided to you by 1 May 2018 and published in June 2018. The 2018/19 work programme is expected to be published in July 2018.

# 3 Appropriations—background information

- 3.1 The Crown funds the Authority through appropriations of public money. The Crown recovers the cost of this funding, up to the level of actual expenditure incurred, through a levy on industry participants. Any amount of levy that is recovered, but is not spent, is returned to levy payers after the end of each financial year. The appropriations therefore have a neutral impact on the Government's operating balance and net debt.
- 3.2 Levies are charged to industry participants in accordance with the Electricity Industry (Levy of Industry Participants) Regulations 2010. These regulations are made on the recommendation of the Minister and are administered by MBIE.
- 3.3 The Authority currently has one main operational appropriation, and two smaller contingent appropriations that are only used if certain events or situations arise.

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<sup>1</sup> The submissions are available at <https://www.ea.govt.nz/about-us/corporate-projects/201819-planning-and-reporting/consultations/#c16902>

- 3.4 The *Electricity industry governance and market operations* appropriation is the operational appropriation<sup>2</sup>. Over 70 per cent of this appropriation is used to fund the service providers that operate the electricity system and markets, with the remainder funding the Authority's own operating costs.
- 3.5 The Authority places significant importance on ensuring the costs of operating the electricity system and markets continue to represent value-for-money. Accordingly, over the last several years we have renegotiated the contractual agreement with Transpower for system operator services, and undertaken competitive procurements for five of the six existing market operation service provider roles.
- 3.6 The renegotiated agreement with the system operator includes increased transparency over service and performance, greater commercial discipline over costs, and requirements for more engagement with stakeholders. As a result of the competitive procurements, contracts that enable the continued use and maintenance of existing market systems have been entered into with service providers, and this has led to significant decreases in annual amortisation expenses. The appropriation components for system and market operations have reduced by \$1.9 million; from a peak of \$55.0 million in 2015/16 down to \$53.1 million in 2018/19.
- 3.7 Within the operational appropriations, the Authority's own operating expenses budget has continued to be held flat at \$18.7 million since 2012/13, and has therefore declined by five per cent in real terms.

## 4 Alignment with Annual Letter of Expectations for 2018/19

- 4.1 In the draft letter of expectations you advised that, as Minister, your objective for the Energy and Resources portfolio over the next three years is to ensure secure, affordable and sustainable energy that supports the transition to a low emissions economy. The alignment between the Authority's work and your specific expectations is outlined below.

### Transition to a low emissions economy

- 4.2 We will support the work of agencies, including MBIE, the Interim Climate Change Committee and when established, the Climate Change Commission, to achieve the Government's commitment to transition New Zealand to 100% renewable electricity generation (in a normal hydrological year) by 2035.
- 4.3 Many of our market development initiatives will facilitate the transition if implemented. These include:
- (a) introducing hedge market cap products to provide more robust and transparent price signals about long-term supply risks and to stabilise income for generation and demand-response that support security of supply during dry years. Both factors (better long-term pricing and greater income stability) are important because an increasing share of renewables is likely to significantly increase the volatility of spot market prices
  - (b) revising provisions in the Electricity Industry Participation Code 2010 (Code) to allow wind generators to have more flexibility in the way they are able to offer their output to the spot market. This will facilitate greater investment in wind generation

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<sup>2</sup> Up to 30 April 2014 the Authority also had a separate operational appropriation for *Promoting and facilitating customer switching*.

- (c) reviewing the Code to ensure there are no unnecessary barriers to new storage technology participating in the wholesale market, further supporting increased forms of intermittent generation, particularly wind and solar generation
- (d) making a final decision on whether to introduce real time pricing in the spot market to provide better short-term price signals to new and more responsive generation technologies and demand response resources, which supports increased levels of renewable generation
- (e) considering whether to broaden the availability of the current dispatchable demand facility in the spot market to reduce barriers to the involvement of aggregators in the electricity market. Aggregators facilitate the participation of smaller scale generation and demand response in the market. Much of the smaller scale generation is expected to be renewable, such as small scale solar
- (f) producing regulatory principles for efficient forms of demand response, which supports increased levels of renewable generation by assisting investors to find the lowest cost ways of supporting high value electricity demand during periods when renewable generation is not operating at expected levels (for example, calm or cloudy days).

### **Address barriers to innovation and exploit new technology benefits**

- 4.4 The Authority has a comprehensive programme of work focused on identifying and removing unwarranted barriers to evolving technologies and business models across the supply chain. New technologies—for instance battery storage, electric vehicles, smart devices for managing demand and new ways of doing business have the potential to benefit all consumers and to assist with the transition to 100% renewable electricity generation.
- 4.5 There are potential barriers for any new technology that changes the way electricity is generated, transported, stored and consumed. Reducing barriers to the use of batteries and electric vehicles is of long term benefit to consumers as it exerts downward pressure on prices without imposing investment risk on consumers. For example, in the case of electric vehicles the Authority:
- (a) has worked with the New Zealand Transport Agency (NZTA), the Energy Efficiency & Conservation Authority (EECA) and the industry to ensure that infrastructure can be seamlessly adopted in the electricity market
  - (b) is encouraging electricity distributors to alter how they charge for using their network so that consumers charge their vehicles at times that do not adversely impact on the operation of their networks or require inefficient increases to network capacity
  - (c) is facilitating the development and voluntary roll out of smart meters in New Zealand that can provide information that supports the reforms to network pricing mentioned in (b) above.
- 4.6 The Authority's work in this area is also supported by the recently established Innovation and Participation Advisory Group (IPAG). The IPAG consists of an independent chairperson and members who represent a broad array of expertise in areas such as software platforms, transmission and distribution networks, energy management, retailing, household consumers and telecommunications.
- 4.7 The IPAG independently advises the Authority on:
- (a) initiatives to improve the efficient development and use of evolving technologies and business models across the supply chain, including reducing inefficient barriers to:

- (i) any consumers purchasing directly from the wholesale electricity market or directly from local generators
  - (ii) mass-market demand response, and aggregators of mass-market demand response
  - (iii) mass-market distributed energy resources, and aggregators of these resources, including distributed generation, batteries, micro-grids and 'prosumer' situations
- (b) initiatives to efficiently promote consumer participation through the whole supply chain, including:
- (i) improving consumer awareness, understanding, motivation and action by mass-market consumers
  - (ii) increasing choices available to mass-market consumers by further enhancing competition.

4.8 The IPAG is currently considering whether electricity distributors provide equal opportunities for everyone that wants to access their networks to provide new energy services to consumers. The IPAG will provide recommendations to the Authority on how to best address any problems identified. The key objective of this project is to ensure that new and existing businesses are confident that access to the network is on a level playing field and to ensure continuing innovating to increase competition and consumer choice.

### Energy resilience

4.9 The Authority supports the resilience of New Zealand's electricity system through our focus on reliability—this delivers on our statutory objective.

4.10 As technologies continue to evolve, a wider diversity of services and businesses will become available in the market. While this creates opportunities for innovation, it can also affect future supply risks by affecting decision making about asset operation, investment and market entry. More efficient and effective risk management by both lines businesses and generators will promote the adoption of rapidly evolving technologies, by avoiding ad hoc barriers arising to protect their assets when unexpected events occur.

4.11 The Authority is implementing a strategy focused on promoting flexible and resilient electricity market and electricity systems, including an initiative aimed at efficient management of the hosting capacity available on electricity networks. The Authority is also pursuing initiatives aimed at providing greater income stability for investors, better price signals about future supply risks, and more options for addressing those risks. For example, we are currently facilitating the listing of exchange-traded cap products to improve investment signals for generators and demand-side response resources, while providing retailers with additional tools for effectively managing wholesale spot price volatility.

### Work with a range of agencies

4.12 The Authority has effective working relationships with a range of existing agencies that affect the electricity sector. These include MBIE, the Ministry for the Environment (MfE), Environment Canterbury, NZTA, Treasury, the Commerce Commission, the Productivity Commission, the Gas Industry Company (GIC), EECA, and Utilities Disputes Limited.

4.13 For example, last year the Authority, the Commission and MBIE created an interface working group. The objective is to improve the coordination between agencies to ensure, among other things, that industry arrangements promote the efficient uptake of new technologies. The Commerce Commission also has an observer sitting on IPAG given the

potential interactions between the work IPAG is undertaking with the Equal Access project and the way the Commission regulates electricity network businesses.

- 4.14 We are also looking forward to collaborating with the Interim Climate Change Committee, and when established, the Climate Change Commission.

### Review of retail electricity pricing

- 4.15 The Authority will support MBIE on aspects of the review that have been identified as sitting most appropriately with the Authority.

## 5 Summary of proposed 2018/19 appropriations after consultation

- 5.1 The recommended appropriations are set out in table 1.

**Table 1: appropriations proposal after consultation**

Electricity Authority	\$ million	
	Appropriation 2017/18	Proposed appropriation 2018/19
<b>Operational appropriation</b>		
Electricity industry governance and market operations	73.937	74.270
<b>Contingent appropriations</b>		
Managing the security of New Zealand's electricity supply (1 July 2017 to 30 June 2022)	6.000 over five years	
Electricity litigation fund	1.000	up to 1.000

## 6 Electricity industry governance and market operations appropriation

- 6.1 We consulted on an appropriation level of \$74.270 million for 2018/19.
- 6.2 In the consultation we also sought specific feedback on the continuation of the *What's My Number* advertising campaign; the campaign's purpose is to motivate consumers to check if they are getting the best deal on their electricity. If this activity were ceased it would allow the 2018/19 appropriation to be reduced by approximately \$1.0 million.

### Submissions on the proposed appropriation

- 6.3 There were 10 respondents that provided comments on the proposed *Electricity industry governance and market operations* appropriation for 2018/19. As occurs every year, there was mixed support for the proposed appropriation, although clear support from consumer agencies. Further details are available in the *summary of submissions and Authority responses* in Appendix A.

### Recommended appropriation

- 6.4 The Authority has considered the overall feedback received on the proposed *Electricity industry governance and market operations* appropriation for 2018/19, and is recommending the appropriation level of \$74.270 million as consulted on.
- 6.5 This level of funding is sufficient to meet the Authority's obligations in respect of the long-term contracts with the service providers, who operate the electricity system and markets—the cost of these services comprise over 70% of this appropriation. Table 2 at the end of this section provides a breakdown of the appropriation components.

- 6.6 As noted in the consultation, there remains some uncertainty around the costs of the new extended reserves regime—as the contractual arrangements have not yet been finalised.
- 6.7 The remainder of this appropriation is used to fund the Authority’s own operating expenses, including the costs of the Authority’s work programme and work specifically targeted at facilitating consumer participation.
- 6.8 The electricity industry is responding to technological advancements, changing consumer expectations and increasing uncertainty. Within this context of increasing change and opportunity, a significant commitment to market development will be beneficial for consumers and for the on-going transition to a more renewable electricity system. Hence, we are recommending the Authority’s operational funding be held at a level that enables the delivery of a challenging and comprehensive work programme in 2018/19.
- 6.9 The feedback we received from the consultation on our proposed work programme focus areas will be considered during the course of its development. It is important to acknowledge that as the Authority’s work programme is developed to promote the long-term interests of consumers, the work programme will not always align with the preferences indicated in consultation feedback and the vested interests implicit in individual submissions.
- 6.10 In relation to the specific feedback on the continuation of the *What’s My Number* advertising campaign, the Authority will undertake research on how the campaign could be repurposed to assist consumers to more easily compare and switch between traditional and emerging innovation services and products, and between suppliers of these products.
- 6.11 This research is not expected to be completed until the end of the 2018. We are planning to run the current campaign until any new repurposed campaign is developed.

**Table 2: Breakdown of proposed 2018/19 electricity industry governance and market operations appropriation**

Operational appropriation - Electricity Authority	\$ million	
	Appropriation 2017/18	Proposed appropriation 2018/19
System operator - operating expenses	26.396	26.396
System operator - capital-related expenses	16.731	17.064
<b>System operator expenses</b>	<b>43.127</b>	<b>43.460</b>
Service provider - clearing manager	2.312	2.382
Service provider - wholesale information and trading system (WITS)	1.797	1.702
Service provider - pricing manager	0.750	0.764
Service provider - reconciliation manager	0.909	0.936
Service provider - registry	0.636	0.654
Service provider - FTR manager	0.935	0.963
Service provider - depreciation and amortisation*	1.797	1.785
Service provider - IT costs	0.095	0.095
Service provider - Extended reserve manager*	0.350	0.350
<b>Other service provider expenses</b>	<b>9.581</b>	<b>9.631</b>
<b>Facilitating consumer participation expenses</b>	<b>2.500</b>	<b>2.450</b>
<b>Authority operating expenses</b>	<b>18.729</b>	<b>18.729</b>
<b>Total appropriation</b>	<b>73.937</b>	<b>74.270</b>

\* The contractual arrangements for the extended reserve manager role have not yet been finalised; this means there is some uncertainty for both the extended reserve manager fees and the amortisation expenses associated with the systems that underpin the role.

## 7 Managing the security of New Zealand's electricity supply appropriation

- 7.1 This appropriation is intended to achieve enhanced security of supply in the electricity system during periods of emerging or actual security situations. We expect these situations to be rare.
- 7.2 The appropriation is limited to the system operator (Transpower) managing actual or emerging emergency events relating to the security of New Zealand's electricity supply. The system operator can request funding from this appropriation to:
- increase monitoring and management responsibilities in the event of an emerging or actual security situation
  - plan and run an official conservation campaign.
- 7.3 A new security management multi-year appropriation was established in Budget 2017, with the same scope and budget (\$6 million over five years) as the previous appropriation that expired on 30 June 2017. For 2018/19 we did not propose any changes to this appropriation.
- 7.4 The security management appropriation is contingent in nature and will only result in a charge to levy payers to the extent that actual costs are incurred.

## Submissions on the proposed appropriation

- 7.5 Five respondents provided comments on the proposed *Managing the security of New Zealand's electricity supply* appropriation for 2018/19. All respondents supported the proposal. Further details are available in the summary of submissions in Appendix A.

## Recommended appropriation

- 7.6 The Authority has considered the overall feedback that has been provided on the proposed *Managing the security of New Zealand's electricity supply* appropriation, and will proceed with recommending no change to the current appropriation level of \$6.000 million as consulted on.

## 8 Electricity litigation fund appropriation

- 8.1 This appropriation is intended to ensure that the Authority is able to participate in litigation effectively and without delay. Our functions under this appropriation include defending cases against the Authority, and taking enforcement action under our enforcing compliance function.
- 8.2 The *Electricity litigation fund* appropriation is contingent in nature and will only result in a charge to levy payers to the extent that litigation costs are actually incurred.
- 8.3 For 2018/19 an appropriation level of up to \$1.0 million was consulted on—the same amount as in 2017/18.

## Submissions on the proposed appropriation

- 8.4 Six respondents provided comments on the proposed *Electricity litigation fund* for 2018/19. Two of these respondents (Mercury and MEUG) supported the proposal, while four were opposed (EMA, Entrust, Transpower, and Trustpower).

## Recommended appropriation

- 8.5 Following consideration of submissions on the appropriation we are requesting that it remains unchanged.
- 8.6 The table below details the history of litigation against the Authority. A review of the submissions shows that many of those opposed to the proposed \$1m litigation fund have a history of entering into litigation against the Authority.

**Table 3: Details of litigation against the Authority**

Calendar year proceedings instigated	Instigating party	Type of proceeding	Result
2011	Genesis Power, Contact Energy, Todd Energy, Bay of Plenty Energy	An appeal to the High Court against the Authority's decision that an undesirable trading situation (UTS) developed on 26 March 2011	Appeal dismissed by the High Court
2012	Genesis Power	An appeal to the Court of Appeal against High Court decision the Authority was correct that a UTS developed on 26 March 2011	Appeal abandoned
2014	Vector	An application to the High Court for a declaratory judgment regarding whether components of the NAaN project were 'connection' assets or 'interconnection' assets	Application dismissed by the High Court
2015	Vector	An appeal to the Court of Appeal against the High Court's decision not to grant Vector's application for a declaratory judgment	Appeal abandoned
2015	Vector	An appeal to the High Court against the Authority's decision to decline Vector's application for an exemption from the transmission pricing methodology in respect of components of the NAaN project	Appeal abandoned
2016	Trustpower	An application to the High Court for judicial review of the Authority's process decisions relating to the TPM and DGPP reviews	Application declined by the High Court
2016	Vector and Entrust	An application to the High Court for a declaratory judgment that the Authority does not have jurisdiction to introduce a default distribution agreement	Application declined by the High Court
2017	Vector and Entrust	An appeal to the Court of Appeal against the High Court's decision not to grant Vector and Entrust's application for a declaratory judgment that the Authority does not have jurisdiction to introduce a default distribution agreement	Fixture date in April 2018 to be confirmed
2017	City Financial	An appeal to the High Court against the Authority's decisions not to pursue complaints that Transpower had breached the Code; and applications for judicial review of the same decisions, and of Transpower's conduct that gave rise to the decisions.	Fixture allocated on 5-8 June 2018

- 8.7 During 2018/19 the Authority will continue to advance market development initiatives that have the potential to have net benefits of hundreds of millions of dollars for consumers over the next decade. These initiatives are contentious as they may have adverse financial impacts on some parties; these parties are generally large and well-funded and the Authority has noted a rise in litigation activity.
- 8.8 An appropriation level of \$1.0 million will help ensure the Authority is well placed to deal with any additional litigation that may arise, and thereby continue to act effectively for the interests of consumers.
- 8.9 The Authority's existing baseline appropriation for the *Electricity litigation fund* in 2018/19 is currently \$0.444 million. We consider that some litigation risks are likely to shift from 2017/18 to 2018/19, and we therefore consider it prudent to recommend that up to \$0.556 million of 2017/18 appropriation funding is transferred, through the March 2018 baseline update process, to 2018/19.
- 8.10 This transfer would be fiscally neutral across the two years, and as with the Authority's other appropriations, the *Electricity litigation fund* has a neutral impact on the Government's operating balance and net debt.

## 9 New initiative bid for Budget 2018: Real-time pricing

- 9.1 In addition to the *Electricity industry governance and market operations* appropriation level for 2018/19, we also consulted on the appropriation increases (\$3.221 million in 2021/22 and \$3.061 million in 2022/23 and out-years) that are required to enable the Authority's Board to make a decision to implement real-time pricing (RTP) in the wholesale electricity spot market.
- 9.2 The Authority's RTP proposal is a significant development for New Zealand's electricity market and is the result of a detailed programme of work over four years. In August 2017 we consulted<sup>3</sup> on a detailed design for the preferred RTP option. There was good consultation engagement from stakeholders, and submissions were broadly supportive of the proposed RTP design. The implications for levy payers of implementing RTP were outlined in the subsequent appropriations consultation; and feedback was generally supportive.
- 9.3 RTP will reduce barriers to new business models and new technologies entering the electricity sector, such as distributed renewable generation, battery storage, and smart devices for better enabling demand response. RTP would deliver significant benefits to consumers, and help enable the investments required to transition New Zealand to 100% renewable electricity generation.
- 9.4 Currently, prices in New Zealand's wholesale electricity spot market are not known with certainty until at least two days after the fact. Final prices are calculated using different inputs, and may be subject to extensive manual intervention—they can therefore differ markedly from the limited indicators available in real-time, especially when the power system is under stress. Consumers and market participants may in turn come to regret the decisions they make in real-time. New Zealand is the only wholesale electricity spot market

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<sup>3</sup> The Authority's RTP proposal, as consulted on with electricity industry participants and stakeholders between August and October 2017, contains comprehensive information on this initiative, including a cost-benefit analysis and regulatory statement. It is available on the Authority website at <http://www.ea.govt.nz/development/work-programme/pricing-cost-allocation/spot-market-settlement-on-real-time-pricing/consultations/#c16609>

still using such an ex-post approach to pricing; the Authority's proposed RTP design, and variations to it, are common practice internationally.

- 9.5 Implementing RTP would provide much better price certainty: electricity spot prices would be produced by the same process used to run the power system at the time; they would be more reliable, more accurate, and easier to understand. RTP would then make spot prices more 'actionable' and more efficient, unlocking opportunities for innovation through new technologies and new business models. Battery storage and smart devices for demand response, for example, require reliable and accurate prices to enable investment and to realise the benefits of those investments.
- 9.6 The Authority expects RTP to produce net benefits to electricity consumers of approximately \$53 million in the base case, with upper and lower case estimates of \$114 million and \$19 million.
- 9.7 After consideration of consultation feedback, we consider that it is appropriate to submit a new initiative bid for RTP, and we are working with MBIE to complete the required documentation for the RTP initiative to be considered in the Budget 2018 process.

## 10 Feedback on the focus of the Authority's work programme

- 10.1 The work programme framework includes six distinct programmes (A to F), each linked to delivering one or more of our key strategies (refer section 2.17 of Appendix B). We consult on the focus of our programmes each year before finalising our SPE and annual work programme to ensure we remain responsive to changes in our operating environment.
- 10.2 We plan to engage further with participants and consumers as we continue to develop the detail of our 2018/19 work programme.

### Comments on the proposed work programme focus areas

- 10.3 In total, 12 respondents submitted comments on the proposed focus areas for the 2018/19 work programme. There were divergent views among the respondents about the specific focus areas. Further details are available in the summary of submissions in Appendix A.

## 11 Communications plan

- 11.1 In the interests of transparency, the Authority recommends that you agree to this briefing paper being published after Budget day. The Authority will also publish the attached *summary of submissions and Authority responses* along with this report.

## 12 Conclusions

- 12.1 The Authority has consulted levy payers on its proposed appropriations as required by the Act.
- 12.2 The Authority has considered consultation feedback, and reached the conclusion that the appropriation levels as consulted on are appropriate to ensure the Authority can continue to perform its statutory functions effectively and operate in a financially sustainable manner.

## 13 Attachments

- 13.1 The following items are attached to this paper:
  - (a) Appendix A: Summary of submissions and Authority responses: Electricity Authority 2018/19 Appropriations and work programme focus areas.

- (b) Appendix B: 2018/19 Levy-funded appropriations and work programme focus areas—consultation paper

## 14 Recommendations

14.1 The Authority recommends that you:

- (a) **note** that the Authority has completed consultation on its proposed appropriations for 2018/19 under section 129 of the Act and has considered the submissions
- (b) **note** no changes have been made to the proposed appropriations as a result of consultation
- (c) **note** that, as the Authority is levy-funded, the appropriations have a neutral impact on the Government's operating balance and net debt
- (d) **note** the proposed Authority 2018/19 appropriations are:
- (i) \$74.270 million for *Electricity industry governance and market operations*
  - (ii) \$6.000 million over the five year period from 1 July 2017 to 30 June 2022 for *Managing the security of New Zealand's electricity supply* (this is a multi-year appropriation)
  - (iii) \$1.000 million for the *Electricity litigation fund*
- (e) **note** a new initiative bid will be put forward for consideration in Budget 2018 for an increase in the *Electricity industry governance and market operations* appropriation of \$3.221 million in 2021/22 and \$3.061 million in 2022/23 and out-years, to enable the Authority's Board to make a decision to implement RTP in the wholesale electricity spot market
- (f) **agree** to submit the proposed Electricity Authority 2018/19 appropriations and new initiative bid for Budget 2018
- (g) **agree** to publication of this report after Budget day 2018
- (h) **note** that a draft 2018/19 SPE will be provided to you for comment by 1 May 2018.

**Agreed / agreed with amendments / not agreed**



Brent Layton  
Chair  
Electricity Authority

Hon. Dr Megan Woods  
Minister of Energy and Resources

## Glossary of abbreviations and terms

<b>ACOT</b>	Avoided cost of transmission
<b>Act</b>	Electricity Industry Act 2010
<b>Authority or EA</b>	Electricity Authority
<b>ASX</b>	Australian Securities Exchange
<b>BAU</b>	Business as usual
<b>CBA</b>	Cost benefit analysis
<b>Code</b>	Electricity Industry Participation Code 2010
<b>CRE</b>	Competition, reliability and efficiency (components of the Authority's statutory objective)
<b>DDA</b>	Default distributor agreement
<b>DG</b>	Distributed generation
<b>DGPP</b>	Distributed generation pricing principles
<b>EDB</b>	Electricity distribution business
<b>EECA</b>	Energy Efficiency and Conservation Authority
<b>EDF</b>	Electronic dispatch facility
<b>EMA</b>	Employers and Manufacturers Association
<b>ENA</b>	Electricity Networks Association
<b>EIEP</b>	Electricity information exchange protocol
<b>FTR</b>	Financial transmission right
<b>GIT</b>	Grid investment test
<b>GRS</b>	Grid reliability standard
<b>HVDC</b>	High voltage direct current
<b>ICP</b>	Installation control point
<b>IPAG</b>	Innovation and Participation Advisory Group
<b>LFC Regulations</b>	Electricity (Low Fixed Charge Tariff Option for Domestic Consumers) Regulations 2004
<b>MBIE</b>	Ministry of Business, Innovation and Employment
<b>MDAG</b>	Market Development Advisory Group
<b>MEUG</b>	Major Electricity Users' Group
<b>Minister</b>	Minister of Energy and Resources
<b>MUoSA</b>	Model use-of-system agreement
<b>NPV</b>	Net present value
<b>NAaN</b>	North Auckland and Northland
<b>PV</b>	Photovoltaics
<b>RAG</b>	Retail Advisory Group
<b>SO</b>	System operator
<b>SOI</b>	Statement of Intent
<b>SOSPA</b>	System operator service provider agreement
<b>SPE</b>	Statement of Performance Expectations
<b>SME</b>	Small and medium sized enterprise
<b>TPM</b>	Transmission pricing methodology
<b>UoSA</b>	Use-of-system agreement
<b>WMN</b>	What's my number



Appendix A Summary of submissions: Electricity Authority  
2018/19 appropriations and work programme  
focus areas

Appendix B 2018/19 Levy-funded appropriations and work programme focus areas—consultation paper