Waikoukou
22 Boulcott Street
PO Box 1021
Wellington 6140
New Zealand
P 64 4 495 7000
F 64 4 495 6968
www.transpower.co.nz

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Tim Sparks
Principal Advisor
Electricity Authority
2 Hunter Street
Wellington 6011

Tenā koe Tim

Status of existing prudent discount agreements and notional embedding contract under new TPM

As the Authority is aware, Transpower is currently party to:

- a Notional Embedding Contract with Network Waitaki and Meridian, dated April 2006 and expiring on 31 March 2026 (**Blackpoint NEC**);
- a Prudent Discount Agreement with Aurora Energy and Trustpower, dated December 2013 and expiring on 23 October 2023 (**Waipori PDA**); and
- a Prudent Discount Agreement with Horizon Energy, Southern Generation and Trustpower, dated April 2014 and expiring on 31 March 2029 (**Aniwhenua/Matahina PDA**).

The status of these agreements under the new TPM, and specifically whether they should come to an end on the effective date of the new TPM or continue, is an unresolved issue.

Our current view (not yet shared with the counterparties) is:

- the Waipori PDA and Aniwhenua/Matahina PDA must cease to apply on the effective date of the new TPM (i.e. at the start of the first pricing year to which the new TPM applies); and
- the Blackpoint NEC will continue to apply after the effective date of the new TPM, possibly with some amendments arrived at through the regulatory change process in the terms of the Blackpoint NEC.

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In the proposed TPM, "prudent discount" is defined as an "inefficient bypass prudent discount" or "stand-alone cost prudent discount". Those terms are defined as follows (emphasis added):

> **inefficient bypass prudent discount** means a discount of a **customer's transmission charges** *provided under this* ***transmission pricing methodology*** for the purpose in clause 129
>
> **stand-alone cost prudent discount** means a discount of a **customer's transmission charges** *provided under this* ***transmission pricing methodology*** for the purpose in clause 135

None of the discounts under the existing agreements are provided under the new TPM; the Waipori PDA and Aniwhenua/Matahina PDA discounts were provided under the current TPM and the Blackpoint NEC discounts were provided pre-TPM. Therefore, none of the discounts are prudent discounts, and clause 116(1) of the proposed TPM (which makes transmission charges subject to prudent discount agreements) would not apply to them.

Accordingly, we would breach clause 12.95(1) of the Code if we were to give effect to either the Waipori PDA or Aniwhenua/Matahina PDA under the new TPM:

> **12.95 Charges to comply with approved transmission methodology**
>
> (1) Except for the **input connection contracts**, **new investment agreement contracts**, and **notional embedding contracts**, **Transpower** must charge for those transmission services affected only in accordance with the approved **transmission pricing methodology**.

Outside of the types of contract referred to in clause 12.95(1) and the TPM itself, we cannot contract out of the TPM (and nor would we want the discretion to do so). Further, if we were to contract out of the TPM in breach of 12.95(1), the recoverability of all customers' transmission charges would be compromised (clause 12.102(2)(b) of the Code).

One of the contract types referred to in clause 12.95(1) is "notional embedding contracts", which the Blackpoint NEC fits the definition of having been entered into before 1 April 2008. Accordingly, the Code permits transmission charges under the new TPM to be modified by the Blackpoint NEC.

In principle, we do not consider any of the existing agreements should continue under the new TPM. The basis for transmission charging is changing fundamentally, making it far from obvious the alternative projects underlying the current discounts would be commercially

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viable. We think it likely the alternative projects would not be commercially viable under the new TPM because embedded generation does not reduce a load customer's residual charge allocation (all of the existing agreements involve notionally embedded generation).

However, because of the special status notional embedding contracts have under clause 12.95(1), we consider we are bound to continue to give effect to the Blackpoint NEC for its remaining term, rather than treating it the same as the Waipori PDA and Aniwhenua/Matahina PDA. This different treatment is based only on the date on which the different agreements were entered into.

We have not yet fully considered how the Blackpoint NEC would impact transmission charges under the new TPM. Our preliminary view is the Blackpoint NEC would at least (until 31 March 2026):

- reduce Network Waitaki's connection charges at Blackpoint to zero (those connection charges going to residual revenue instead) and result in Network Waitaki's allocations for post-2019 benefit-based investments being calculated based on notional net offtake at Blackpoint; and
- result in Meridian's allocations for post-2019 benefit-based investments in the HVDC link being calculated based on notional net injection at Waitaki.

In our view, the existing agreements should be treated consistently. For the reason above, we consider all of them should cease to apply on the effective date of the new TPM. The next best option would be to allow all of them to continue for their remaining terms, or at least for some period after the effective date of the new TPM that provides enough time for the counterparties to reapply for a prudent discount if they wish to do so. Either of these outcomes could be achieved through an appropriate amendment of clause 12.95(1) of the Code.

We would like to discuss this issue with the Authority. Please let me know when would be convenient to do that.

Nāku noa, nā

Rebecca Osborne
Head of Grid Pricing