

1 [Hearing commences at 9.04 am]

2  
3 **PRESENTATION BY CONTACT (Continued)**  
4

5 **CHAIR:** Good morning ladies and gentlemen. I apologise for being  
6 late having spent the last week chasing people along. So,  
7 apologies.

8 The programme today is Contact to continue from Friday and  
9 then around 10.30/11.00, NZWEA; 11.00-12.00, SEF, the  
10 Sustainable Forum; and 2.00-5.00, we have MEUG; and 5.00-5.30,  
11 Catherine Petrey or CC 93, probably both I guess, but Catherine  
12 is appearing for both those groups.

13 Just before asking Contact to resume, just a general  
14 comment which is not, I guess, on anything particular. Just to  
15 make the point that from time to time Commissioners do ask a  
16 range of questions and I think one or two of you might have felt  
17 occasionally that perhaps we were boring in on issues, but I  
18 think the point I really want to make is that the range of  
19 questions and the scope of them doesn't attempt to predict or  
20 state a conclusion or a position, it's really to try and flesh  
21 out what the issues are.

22 I think I said for one thing last week it was my view X,  
23 this was on the statement made rather than the position taken,  
24 so I'd just like to remind people don't be distressed or  
25 concerned if you think we're heading down paths that at the end  
26 of the day you may feel a bit inappropriate. We'll make all  
27 those decisions after the hearing is finished.

28 Having said that, back to Mr Stevenson, please.

29 **MR STEVENSON:** Thank you very much, Mr Chairman, and good morning;  
30 it's nice to be back.

31 We have the same team, David Hunt, myself, James Kilty and  
32 Tony Dellow.

33 Where we were on Friday, we had said that we would address  
34 five issues, being the potential for pro-competitive rule  
35 changes to be blocked, the quality of the decision-making under  
36 a Crown EGB or an industry EGB; the potential for over-  
37 investment or under-investment in the grid in either state of  
38 EGBness; the proposed extensions; and the fifth issue was  
39 whether the price finding in the process in the Rulebook amounts  
40 to Section 30 of the Commerce Act.

41 If you recall the last thing we did on Friday was to  
42 address the fifth of those issues, the Section 30 issue. I want  
43 to return to that point before finishing off the points Contact  
44 would like to make on the first four, in dealing with Section 30  
45 James Kilty had read a statement on the matter. I'm going to  
46 hand back over now to James and Tony Dellow to complete our  
47 submission on the subject of Section 30. Thank you.

48 **MR KILTY:** Good morning. If you recall on Friday, as Toby said,  
49 we read a statement; that statement was largely our position  
50 statement and was more of our conclusion to where we get to

1 today. Given there is time we would like to wind it back and  
2 show you why we reached that conclusion and I believe that was  
3 more in line with what the Commission was hoping to hear today,  
4 and for that reason we've got Tony here with us again, and I'll  
5 hand you over to him to lead us through the steps of analysis  
6 which led us to reach those conclusions.

7 **MR DELLOW:** Thanks, James. I do actually have a copy of what I'm  
8 going to say. So if you'd like to -- [**Pause taken and document**  
9 **circulated**].

10 The comments that I'm going to make are directed at the  
11 interpretation of Section 30 and they are really intended to  
12 address two things: The issues that are raised in the Draft  
13 Determination, and also, from looking at the transcripts, the  
14 questions that the Commission's asked and the things that you do  
15 seem to have wanted covered.

16 So, I think a good starting point is Decision 280, and  
17 there the Commission decided that the NZEM Rules that were then  
18 under consideration weren't caught by Section 30. The rationale  
19 really was threefold. It found that on the one hand the Rules  
20 were a contract between competitors, but in relation to its  
21 purpose that the Rules didn't have the purpose of fixing,  
22 controlling or maintaining prices because the purpose was to  
23 establish an efficient competitive wholesale electricity market.  
24 And then in relation to the effect aspect of Section 30, the  
25 Commission said the pricing mechanisms didn't allow generators  
26 or purchasers acting independently or collectively to  
27 predetermine prices. There, as we say there, it considered that  
28 the price would be set in response to and would vary as a result  
29 of changes in supply and demand.

30 In coming to that view, the Commission considered the case  
31 law that was current at the time and in our view decided it  
32 correctly, and that relates to the interpretation of fixing,  
33 controlling or maintaining price as it's set out in Section 30.

34 The principal case at the time was *Radio 2UE*, and in that  
35 case in the lower court, which was Lockhart J his conclusion  
36 was, and I've quoted there:

37 "It is important to distinguish between arrangements...  
38 which restrain price competition and arrangements which merely  
39 incidentally affect it or have some connection with it. Not  
40 every arrangement between competitors that has some possible  
41 impact on price is per se unlawful under the section."

42 That case went to appeal and the Full Federal Court agreed  
43 with that conclusion, and in respect of the definition of fixing  
44 the Court said:

45 "In our view the word "fixing"... Takes colour from its  
46 general context and from the words used with it - "controlling  
47 or maintaining" - and not every determination of a price,  
48 following discussion between competitors will amount to a price  
49 "fixing". There must, we believe, be an element of intention or

1 likelihood to affect price competition before "fixing" can be  
2 established."

3 These cases are acknowledged in the Draft Determination.

4 **MS BATES:** Excuse me, do you have a citation -- I assume you mean  
5 the Court -- was it a High Court decision?

6 **MR DELLOW:** The Full Federal Court. We can find that.

7 In Decision 280 itself the Commission also considered its  
8 own decision in the *Insurance Council* case and I've set out a  
9 quote there in relation to that:

10 "In all of the cases noted above, the terms "fix",  
11 "control" and "maintain" are synonymous with an interference  
12 with the settling of a price, as opposed to allowing such a  
13 price to be set in response to changes in the supply and demand  
14 for goods or services. Thus, in a technical sense any agreement  
15 by competitors in a market which has an influence on, or  
16 interferes with the setting of a price, amounts to 'price  
17 fixing'. However, following Lockhart J, for that interference  
18 to have any significance in a competition sense, the price that  
19 is fixed must not be instantaneous or merely " -- must not be ,  
20 and I think importantly for our purposes here -- "ephemeral,  
21 momentary or transitory or be the result of arrangements which  
22 merely incidentally affect it."

23 The Commission went on to say:

24 "Thus while the Agreement might have influenced the price  
25 of insurance " -- sorry my copy's different to yours, but you  
26 will see there's a reference to the Council having conceded that  
27 the price would be different -- "that this amounts to 'price  
28 fixing' in a competition sense."

29 So the *Radio 2UE* decision and the *Insurance Council*, in our  
30 submission, clearly indicate that actions that simply affect  
31 price are not caught by the relevant price fixing provision.

32 I'm going to come back to this later on, but I think it's  
33 quite important to be aware that those cases did acknowledge  
34 that you could have arrangements between competitors that would  
35 affect price without being price fixing. I think that addresses  
36 some of the questions that have been made and we'll come back to  
37 it later on.

38 The words "fixing", "controlling" and "maintaining" in the  
39 Competition Law context -- in our submission are not used in a  
40 neutral sense. This doesn't mean that Section 30 includes a  
41 substantially lessening of competition test, rather fix, control  
42 and maintain are used in the sense of restraining competition  
43 that is restraining the free movement of price to reflect supply  
44 and demand in the relevant market. We submit this remains the  
45 correct approach to the application of Section 30.

46 I now want to turn to the three cases that are referred to  
47 in the Draft Determination which the Commission has stated, I  
48 guess, or implied change the interpretation of Section 30, and  
49 in the Draft Determination the Commission said, just by way of  
50 background:

1 "These decisions make it clear that the competitive effect  
 2 of the provision is irrelevant in considering whether it falls  
 3 within Section 30. As a result any arguments as to the  
 4 competitive effects of the pricing mechanism are irrelevant,  
 5 i.e. Whether there are any pricing options available and whether  
 6 over time the prices established by the mechanisms would be  
 7 likely to track the prices established in the absence of the  
 8 mechanisms".

9 It's our submission that these cases, that is *Taylor*  
 10 *Preston*, *Caltex* and *ACCC v CC* do not alter the analysis of  
 11 whether the conduct falls within Section 30 in the way suggested  
 12 by the Commission.

13 We consider that the three cases leave the fundamental  
 14 point in both 2UE and the *Insurance Council* decision untouched,  
 15 and that is that Section 30 and its Australian equivalent catch  
 16 arrangements that are price fixing in the competition sense.  
 17 That is to say, for Section 30 to apply there needs to be a  
 18 restraint on the competitive process as the method of finding  
 19 price.

20 **MS BATES:** So what do you say about the deeming nature of the  
 21 Section 30 provision? If you are right, why have that deeming  
 22 provision there?

23 **MR DELLOW:** Because I think we're going to come to this later in  
 24 terms of the *ACCC v CC* case, but the point is that a substantial  
 25 lessening of competition is not necessary to establish a breach  
 26 of Section 30.

27 So, all we're looking at is what is the sense in which the  
 28 words controlling -- fixing, controlling and maintaining are  
 29 used? How do you colour those words? How do you interpret  
 30 those words in the context of the section? Once you've found  
 31 that you have restrained competition, once you find that the  
 32 arrangement is directed at shifting away from supply and demand  
 33 affecting price and actually -- there is actually an arrangement  
 34 between competitors that stops that from happening or limits the  
 35 way that happens, then you don't have to look at a substantial  
 36 lessening of competition test.

37 I think that, just to answer your question further, in the  
 38 Draft Determination --

39 **MS BATES:** I'm just trying to explore how you are saying that the  
 40 competitive effect ought to be taken into account in that first  
 41 part of the assessment under the section, that's what I'm really  
 42 interested in.

43 **MR DELLOW:** Perhaps it would be best to look at it in the context  
 44 of the matter that's actually before you, and there we are  
 45 talking about, sure, it's a contract between competitors but the  
 46 purpose of it is actually to facilitate competition, and I think  
 47 that's the test that you've got to look at it against, is, is it  
 48 directed at facilitating competition or is it actually a way of  
 49 restraining competition in any way? The degree isn't so  
 50 important provided it's not a de minimus, so low, but...

1 **MS BATES:** Let me get this clear. In deciding whether we're  
2 fixing, controlling or maintaining, your submission is that the  
3 Tribunal or Court is to look at the purpose of the arrangement?

4 **MR DELLOW:** To look at -- well, it's the purpose or the effect and  
5 we will come back to the effect too.

6 **MS BATES:** Do you think -- let's isolate them, do you think we  
7 should be looking at the purpose of the arrangement?

8 **MR DELLOW:** Of this arrangement, yes.

9 **MS BATES:** And do you think we should be looking at the effect.

10 **MR DELLOW:** Yes, you should be looking at the effect but you should  
11 be doing that in the light of what these cases have said, which  
12 is not just that the price might be different with or without  
13 the mechanism, or if you change the Rules that the price might  
14 change, but whether in fact the effect is to create a market  
15 which is competitive and allow the finding of price by the  
16 interaction of supply and demand or whether it has some other  
17 purpose which you would expect to be in the interests of the  
18 competitors.

19 **MS BATES:** I understand that argument. Now, take me back to the  
20 case which you say most supports that proposition.

21 **MR DELLOW:** The case that most supports the proposition is *Radio*  
22 *2UE*.

23 **MS BATES:** And your submission is that *Radio 2UE* has not been  
24 avenged by subsequent cases?

25 **MR DELLOW:** Yes, and that's what I'm going to come to now.

26 Before I do though, just to address -- and it relates to  
27 these three cases -- there is a difference in these cases and  
28 this will come out in what I'm going to say, but you've got to  
29 distinguish between the cases that look at whether or not  
30 Section 30 is actually triggered and the cases that look at the  
31 effect of triggering Section 30, and I think that is an issue  
32 that comes out in the Draft Determination.

33 **MS BATES:** I quite agree with that way of framing it and that would  
34 be quite useful in this case to look at it from that  
35 perspective.

36 **MR DELLOW:** So we go back in these -- this paper to page 3,  
37 paragraph 8. As I said, it is our submission that these cases  
38 don't alter the analysis of whether conduct falls within  
39 Section 30 in the way suggested, I think I've been through that.

40 I'll go on to paragraph 9. The *Caltex* case does, as the  
41 Commission says in the Draft Determination, establish that it's  
42 not necessary to be able to point to a fixed price or agreed  
43 discount for the future for the arrangement to be caught by  
44 Section 30. But we submit that, in any event, this point has  
45 never really been questioned before *Caltex*, and it's not  
46 relevant to the issue before the Commission in respect of the  
47 Rules.

48 The *Caltex* case wasn't a case which could be said to  
49 involve price fixing which was not price fixing in a competition  
50 sense. The Court found that, by agreeing to remove the free car

1 wash offer, the competitors had agreed to eliminate a discount  
2 and accordingly raise prices to the extent of the former  
3 discount that would have applied in the absence of the  
4 arrangement.

5 **MS BATES:** Can I just stop you there again because I think this is  
6 getting to the nub of the argument, and I'll apologise for  
7 interfering too much with the flow of it and I'll desist.

8 What I'm trying to understand here is, in the *Caltex* case  
9 are you saying that the decision was really influenced by the  
10 purpose of the arrangement? Are you saying that the purpose of  
11 the arrangement was taken into account in deciding whether there  
12 was actually a fixing?

13 **MR DELLOW:** Yes. The purpose and the effect. The effect of the  
14 arrangement was to raise prices for the end-user, and the very  
15 end of the submissions -- and at the very end of these  
16 submissions I'm going to come to the purpose of the Act very  
17 briefly.

18 **MS BATES:** I understand that, but on my reading of *Caltex* I thought  
19 the threshold question was answered in the affirmative, yes,  
20 there was a price fixing.

21 **MR DELLOW:** There was.

22 **MS BATES:** Because, not because of purpose but because the --

23 **MR DELLOW:** The effect was to raise price.

24 **MS BATES:** I can understand the argument that you are putting  
25 forward, that purpose and effect might be relevant in construing  
26 the section, but I don't -- I might have missed it, but I don't  
27 get that analysis from the *Caltex* decision.

28 **MR DELLOW:** I'm sorry, what I just said was that the competitors  
29 had agreed to eliminate a discount and accordingly raised prices  
30 to the extent -- perhaps you've misconstrued that as saying -- I  
31 thought the purpose was the important thing, but it was in fact  
32 the effect of the agreement that was or was not important, and  
33 that's what I'm saying.

34 **MS BATES:** Are you saying that the Judge came to a decision that it  
35 was a fix because of the effect?

36 **MR DELLOW:** Yes.

37 **MS BATES:** Okay. Is there anywhere in the judgment which actually  
38 supports that?

39 **MR DELLOW:** Well, once again we can come back to that. Contact  
40 have said they will provide you with our opinion on this issue,  
41 and --

42 **MS BATES:** I'm just highlighting the issue that's of concern to me  
43 in construing this case because that's what we've got to grapple  
44 with in coming to one -- one of the things we have to grapple  
45 with.

46 **MR DELLOW:** Then, just to go on, I think it's relevant to what  
47 you've just said. In *Caltex* it was clear that parties to the  
48 arrangement were restraining the free movement of price to  
49 reflect supply and demand in the relevant market.

**Contact**

1           The next case was the *Taylor Preston* case, and in that case  
2 we say that the Court proceeded on the basis that Section 30  
3 actually did apply, and I guess that's why it's not really so  
4 relevant to what you are looking at now. The question for you  
5 is whether Section 30 applies and that's not directly what that  
6 case is about.

7           The competitors had discussed maximum premiums and maximum  
8 schedule prices for livestock procurements and the proceedings  
9 were ultimately settled by way of admission as to a breach of  
10 the likely effect limb of Section 27.

11          The *Taylor Preston* case is simply, in our submission, not  
12 relevant to the question as to whether Section 30 applies to the  
13 Rules. The case is concerned with the question of whether the  
14 deeming effect of Section 30 as a matter of statutory  
15 interpretation is confined in its operation to the question of  
16 liability under Section 27, or whether the deeming effect is  
17 also relevant to the assessment and imposition of pecuniary  
18 penalties. The case is not concerned with whether prices have  
19 been fixed, controlled or maintained but instead relates to the  
20 ramifications of Section 30 in fact applying.

21          The last of the three cases is *ACCC v CC* and in that case  
22 four tenderers agreed that the successful tenderer -- this was  
23 for a major building contract, the value of which was about  
24 \$180 million -- agreed that the successful tender would pay the  
25 unsuccessful tenderers \$750,000 each; that is a total of  
26 \$2.25 million. This unsuccessful tenderer fee was built in in  
27 part to the tender prices for each of the tenderers who were  
28 party to the arrangement.

29          The Judge in the case considered the *Radio 2UE* case and  
30 quoted the same passages we quoted in our earlier discussion of  
31 that case.

32          Paragraph 122 of the Commission's Draft Determination  
33 includes an excerpt from the judgment from Lindgren J, and is  
34 characterised as establishing the proposition that an  
35 understanding could fall within the Australian equivalent of  
36 Section 30 without controlling price competition. However we  
37 submit that the passage quoted is more relevant to the question  
38 of whether the effect of the arrangement in question was de  
39 minimus.

40          We don't understand the Judge in that case as stating in  
41 the judgment that no effect on price competition is necessary  
42 for the arrangement to be caught by the Australian equivalent of  
43 Section 30. In fact, he says the opposite.

44          In paragraph 182. This is what he said:

45          "an agreement, arrangement or understanding that has the  
46 effect of fixing, maintaining or controlling price will have  
47 some effect on price competition, although not necessarily the  
48 effect of eliminating or even substantially lessening it. The  
49 effect of controlling price, even without a substantially

1 lessening of price competition, can form the foundation of a  
2 deemed contravention of S 45 of the Act."

3 In the Draft Determination the Commission seems to be  
4 contending that *ACCC v CC* is authority for the proposition that  
5 the word "controlling" in the context of section 30 is used in a  
6 neutral sense and that the effect on price competition is  
7 irrelevant.

8 In fact, we say that close examination of the judgment  
9 shows that Lindgren J was only contending that it was not  
10 necessary to show a substantial lessening of competition.

11 **MS BATES:** Was he the only Judge in that case?

12 **MR DELLOW:** Yes.

13 So it's not necessary to show a substantial lessening of  
14 competition but that controlling still retains pejorative  
15 connotations in that it refers to controlling in a competition  
16 sense.

17 This is consistent with what Lockhart J said in *Radio 2UE*.  
18 Lockhart J quoted -- Lindgren J quoted from Lockhart's judgment  
19 in *Radio 2UE* without suggesting that his own judgment differed  
20 from it. The view that "controlling" has a pejorative  
21 connotation can clearly be seen in the key passage in  
22 Lindgren J's judgment in which he says:

23 "I infer that the UTF understanding was likely to have the  
24 effect of controlling, by way of increasing, by \$2,250,000 or by  
25 a substantial part of that sum, the price that ACS would be  
26 charged for the Project."

27 So in summary, we submit that the appropriate analysis to  
28 be applied by the Commission is fundamentally the same as was  
29 applied by the Commission in Decision 280, i.e. That if the  
30 Commission finds that the Rules are simply a method of matching  
31 supply and demand, directed at achieving a competitive outcome,  
32 as it did in Decision 280 then the Commission should find that  
33 it does not have jurisdiction to consider the Rules relating to  
34 the wholesale electricity market.

35 **MS BATES:** Excuse me, can you take us back to the Lindgren  
36 decision, and the quote that's at the top of page 5.

37 I'm just trying to get it clear what your submission is  
38 based on that particular passage. He says an agreement,  
39 arrangement or understanding that has the effect of fixing or  
40 maintaining or controlling the price will have some effect on  
41 competition, and so, that sentence, are you taking that to mean  
42 that unless it has some effect on competition, that it's not  
43 caught?

44 **MR DELLOW:** That's right, and I think if you read the context of  
45 the decision as a whole, that's really what he's saying, and  
46 he's saying it in the context of just immediately before having  
47 quoted from *Radio 2UE*.

48 **MS BATES:** I'm just wanting to understand your submission based on  
49 that.



**Contact**

1 **MR DELLOW:** That is the submission. He's contrasting some effect  
2 on price competition with substantially lessening of  
3 competition, and he's saying it's not necessary to have  
4 substantially lessening of competition but, nevertheless, there  
5 still is -- there has to be this controlling in the competition  
6 sense.

7 **MS BATES:** Is it possible he could have been saying that some  
8 agreement, arrangement or understanding will necessarily have  
9 some effect on price competition?

10 **MR DELLOW:** Well, in our submission he's not saying that. If he  
11 was saying that and if he was -- as the Commission, I guess,  
12 implies in the Draft Determination -- saying that that's not a  
13 necessary element, then there would have been no need to have  
14 quoted the passages that he quoted from Lockhart J. He was  
15 following on from that, and in between the quotes from *Radio 2UE*  
16 and the bit that we've just quoted here, he has a discussion of  
17 what that actually means and saying really that's -- what he's  
18 really doing -- what Lockhart J was doing was just really  
19 interpreting what Section 30 was saying.

20 **MS BATES:** Thank you, that's helpful.

21 **MR DELLOW:** Okay. I want to turn now to something to some extent I  
22 dealt with, but it did come up on Friday, and that was the  
23 Commission has asked other parties making the submissions  
24 whether if the Rules changed the wholesale electricity price  
25 would change. We've taken the implication from that question,  
26 notwithstanding what the Chairman said this morning, that if a  
27 change to the Rules would have an effect on the wholesale  
28 electricity price then the Commission considers that the Rules  
29 must have the effect of fixing, controlling or maintaining price  
30 in terms of Section 30.

31 **MS BATES:** If I could just say, I don't think that there has been a  
32 concluded view reached on that particular question, but that is  
33 what we're really wanting to explore.

34 **MR DELLOW:** I accept that.

35 **MS BATES:** There's nothing set in concrete on this.

36 **MR DELLOW:** However it does give a good pointer to us making the  
37 submissions that you need to have submissions on.

38 In our view the Commission would be incorrect to infer from  
39 a finding that the wholesale electricity price could or even  
40 would change as a result of a change in the Rules, that means  
41 Section 30 applies to the Rules. Rather, the question that the  
42 Commission needs to answer is whether the Rules before the  
43 Commission, when applied to the electricity industry in its  
44 current form, have the effect of fixing, controlling or  
45 maintaining prices in a competition sense.

46 We submit that the appropriate test is the test used in  
47 Decision 280.

48 In other words, the Commission does not need to consider  
49 the effect of the Rules to which the current application relates  
50 in the context of changes that may take place in the electricity

**Contact**

1 industry in the future. Similarly, the Commission does not need  
2 to be concerned about the fact that the Rules might be changed  
3 in the future in a way that means that they do have the effect  
4 of fixing, controlling or maintaining prices. In both cases, in  
5 the absence of an authorisation, the Commerce Act will apply,  
6 that is if you have declined jurisdiction in relation to this  
7 application; the Commerce Act will apply and the Commission will  
8 be able to take action to address the effect of the change.

9 We submit that the issue that needs to be addressed by the  
10 Commission is the same issue that it was addressed by the  
11 Commission in Decision 280. That's really two questions: The  
12 first is whether the Rules now before the Commission are such  
13 that if they are applied in the electricity industry in its  
14 current form, this would allow generators or purchasers to  
15 predetermine prices, and the second question is whether the  
16 prices found under the Rules are set in response to or varied as  
17 a result of changes in supply and demand.

18 If the answer to the first question is "no", that is that  
19 generators and purchasers can't set prices, and the answer to  
20 the second question is "yes", then Section 30 does not apply and  
21 subject to analysis as to whether Section 27 otherwise applies,  
22 the Commission would have to conclude that it does not have  
23 jurisdiction to grant authorisation for the Rules in respect of  
24 the wholesale electricity market provisions.

25 Just finally in interpreting the legislation the Commission  
26 must have regard to the overall purpose of the Commerce Act. I  
27 have put this at the end because I think, unlike some arguments  
28 where it's your best argument, this is actually just a  
29 bolstering, I guess.

30 The purpose of the Act is, in Section 1A, to promote  
31 competition in markets for the long-term benefits of consumers  
32 in New Zealand. As we've already said, the cases decided prior  
33 to Decision 280, and the Decision 280 itself, interpreted  
34 Section 30 in a way that was consistent with that purpose, by  
35 specifically referring to Section 30 or its Australian  
36 equivalent, as referring to fixing, controlling or maintaining  
37 in a competition sense.

38 We've submitted that the subsequent cases referred to by  
39 the Commission have not changed the appropriate interpretation  
40 insofar as it's relevant to the Rules, and it would be  
41 unfortunate if the Commission now adopted an interpretation that  
42 would mean that the Rules, which we're submitting -- it's a  
43 matter of fact for you to consider -- have been formulated for  
44 the purpose and with the effect of creating a market that is as  
45 competitive as current technology and industry conditions allow.  
46 If the Commission was to find that they convened the Act as a  
47 result of what we submit is a new interpretation of Section 30,  
48 that is inconsistent with previous judicial decisions and the  
49 Commission's own previous decision.

**Contact**

1 **MR CURTIN:** Thank you very much for that, that was very clear.  
2 Could I come back to paragraph 20 where there were a number of  
3 questions, including quite a few from me last week, about this  
4 issue about whether the price would have been different without  
5 the Rules with them.

6 **MR DELLOW:** Yes, I've got your question.

7 **MR CURTIN:** The reason I asked that, I'd like to be clear about  
8 that.

9 We've had a couple of submissions from people whose  
10 reasoning, I think, went along these lines: That there is a risk  
11 that the Rules might be found to fall foul of "controlling"  
12 unless we argued that the price would have been the same without  
13 the Rules.

14 My questions were actually designed to get further  
15 clarification of that position because I think there is actually  
16 a completely respectable argument that does not require people  
17 to make that last step, that the price would have been the same  
18 absent the Rules.

19 **MR DELLOW:** Yes. Our submission is that, that that is not the  
20 correct analysis, that it doesn't have to be the same.

21 **MR CURTIN:** I accept that, and the practical case outside the  
22 legalities I was thinking of was that without an efficient  
23 wholesale market it's entirely possible that Contact or other  
24 parties will just have to scratch around to establish the best  
25 prices they could absent a market mechanism, and there's  
26 absolutely no way of telling what those prices might be; they  
27 might be multiple prices.

28 So, my question was in no sense taking a predetermined  
29 position, it was very much to elicit the point you have just  
30 made.

31 **MR SKELTON:** Can I just ask one quick question. Did you have a  
32 look at the transaction pricing methodology?

33 **MR DELLOW:** [**shakes head**]

34 **MR KILTY:** No, we decided having looked at that that there wasn't  
35 a great deal that we wanted to add to what the applicant had  
36 said, other than to say we support what the applicant has said  
37 on those issues.

38 **MS REBSTOCK:** I'd just like to come back to the remarks you made  
39 with respect to purpose, and I will paraphrase, but the  
40 application has contended that the purpose is to create a market  
41 so that the prices can be determined, and I think that's well  
42 understood.

43 But isn't it possible that, while it may create a market so  
44 that a price can be found, it may do so in a way that limits the  
45 space over which the competition that is meant to occur is  
46 somehow limited? So, it does encourage competition but it may  
47 encourage competition in a confined space.

48 My question to you really is, in that sense you could --  
49 whether you do here, I don't know -- but in theory, at least,  
50 you could have a substantial lessening at the same time at which

1 the purpose was to create competition within whatever space it's  
2 created, in whatever space you have confined your market to.

3 **MR DELLOW:** Well, the answer to your question, of course, is yes,  
4 in theory that could be the case. The issue to be considered if  
5 Section 27 is to be invoked is what is the counterfactual? So  
6 an improvement of competition through the Rules, where you can  
7 see there could be even more improvement, but --

8 **MS REBSTOCK:** No, I'm thinking purely in terms of Section 30. You  
9 could argue, it seems to me, that if you confine the space over  
10 which competition is to occur, even if your purpose is to allow  
11 competition in that space, you may nevertheless in theory breach  
12 Section 30 because you've controlled at least, to some extent,  
13 the price that can emerge.

14 **MR DELLOW:** Yes, if you've done that in a competition sense. I  
15 didn't go over them again but we gave examples on Friday, and I  
16 think it's been provided to you, the comments that James made on  
17 Friday. We had some examples of where there could be changes in  
18 the industry because I suppose our submission at the moment is  
19 that the Rules are as good as they could be, but there could be  
20 changes in the industry where, if the Rules didn't keep up with  
21 that, then you would be confining the range within which  
22 competition could happen, and demand side flexibility would be  
23 an example.

24 **MS REBSTOCK:** Leaving aside the current Rules though, I mean we'll  
25 have to form a view on the current Rules, but at least in theory  
26 you could say the purpose is to develop a market in which supply  
27 and demand can determine a price, but the market itself could be  
28 controlled in such a way that breaches Section 30, in theory.

29 **MR DELLOW:** If you are talking about theoretically, yes absolutely,  
30 no doubt about it.

31 **MS REBSTOCK:** And we can determine in this case whether that in  
32 fact happens.

33 **MR DELLOW:** And the other part of our submission about that, of  
34 course, is that if you declined jurisdiction now on the basis  
35 that you are satisfied that the Rules are as good as they are  
36 going to be, or as close that they can be to as good as they're  
37 ever going to be, then you do continue to have Section 30  
38 applying to those Rules, and if they fall out of favour, if you  
39 like, or if conditions change such that they're inappropriate,  
40 then that's something that can be looked at under the Commerce  
41 Act at any time.

42 **MR CURTIN:** I think I can see the reasoning there and certainly, I  
43 suppose what we're grappling with is the wider public policy  
44 issue, and I apologise if the EGB is being used as a kind of  
45 laboratory for organised markets everywhere, but there was  
46 obviously a concern about the applicability of Section 30 to  
47 many organised markets and auctions and similar organised  
48 arrangements.

49 Obviously, deciding on narrower broad readings of  
50 Section 30 could arguably take the Act to where it was not meant

**Contact**

1 to go in terms of purely finding a price, but as my colleague  
 2 observed there could be features of each given market, caps or  
 3 flaws on prices, strange features of bidding systems -- not in  
 4 any way suggesting that they're in the Rules, but just in theory  
 5 one could imagine the design of the market might have anti-  
 6 competitive features that could trigger Section 30.

7 **CHAIR:** Just a couple of questions, Mr Dellow, without again taking  
 8 a view on it. At paragraph 8, where you are quoting, I think,  
 9 the Australian case:

10 "... section 30 (and its Australian equivalent) catch  
 11 arrangements that are price fixing in the competition sense and  
 12 so there needs to be a constraint on the competitive process."

13 So the argument is, it's a market mechanism design to make  
 14 the market operate without restraining the competitive process;  
 15 is that the nub of what you are saying?

16 **MR DELLOW:** Yes.

17 **CHAIR:** And the *Caltex* one, similarly quoted, that it was price  
 18 fixing in a competition sense?

19 **MR DELLOW:** Yes.

20 I do have the citations that Ms Bates asked for.

21 **CHAIR:** Just hand those in, if you like.

22 **MR DELLOW:** Yeah, we can do that. That's fine.

23 **CHAIR:** Any other submissions on that particular point?

24 **MR KILTY:** No, we'll move on.

25 **CHAIR:** Thanks, Mr Dellow. Mr Stevenson.

26 **MR STEVENSON:** Thank you. Mr Dellow talked about creating a market  
 27 that is as competitive as current technology and industry  
 28 conditions allow. If I can go back to the point in my  
 29 submissions where I was on Friday. We were talking about the  
 30 two issues of the potential for pro-competitive rule changes to  
 31 be blocked, and the proposed extensions; those two points being  
 32 related.

33 Our submission was, and still is, that no pro-competitive  
 34 rule change has been blocked or is likely to be blocked under  
 35 governance structures as we know them or as proposed.

36 We allowed the possibility that something that looks like  
 37 inertia may arise as a result of Rule changes that strike  
 38 technical, physical, practical or security reasons or where  
 39 Transpower wants to assert their unique way of solving an issue.

40 Otherwise we submitted that pro-competitive rule changes  
 41 have enjoyed 100% support and we expect that they will continue  
 42 to do so.

43 And if I could borrow some language from paragraph 153 of  
 44 the Decision 280:

45 "To date, Contact has seen no evidence that prices  
 46 established by the NZEM price discovery mechanism diverge  
 47 significantly on average from prices that might be established  
 48 without the price discovery mechanism."

49 **CHAIR:** Excuse me, are you able to do that, on what basis, making -  
 50 - how can you make an estimate of the price that might be

1 established in the absence of the mechanism? Have you run  
2 separate modelling or what have you done?

3 **MR STEVENSON:** No, I've said -- I should have prefaced that with  
4 "based on our experience" we have seen no evidence the  
5 limitation on the pro-competitive rule changes has been  
6 technical, physical, practical and security reasons and/or  
7 discussions about the way mechanisms should rightly be solved.  
8 That is not on the basis of modelling, it is an opinion based on  
9 our experience.

10 **CHAIR:** Thank you.

11 **MR STEVENSON:** We also submitted that the tension between the  
12 proposed governing structure and the Government via the  
13 mechanisms of the Government Policy Statement and the Auditor  
14 General review would ensure that this remains so; add to this  
15 the overlying tension created by the possibility of any future  
16 Minister of Energy being able to regulate at any time.

17 I discussed some advances in rule development which have  
18 benefitted from that tension over the last 18 months, the  
19 development of a hedge index; the release of bids and offers  
20 after one month; Spill Rules; free-to-air prices and consumer  
21 participation were some that I discussed.

22 I referred to Rule changes that have stumbled for  
23 technical, physical and security reasons such as, real time  
24 pricing, demand side participation, ex anti versus ex-post price  
25 discovery and, of course, financial transmission rights.

26 Notwithstanding all of the above, the applicant has reacted  
27 promptly to the Commission's concerns over the possibility of  
28 blocking pro-competitive rule changes by offering proposed  
29 condition 1; it's divided into two parts, neither of which are  
30 necessary in Contact's opinion. However, if the Commission  
31 wants to adopt part or all of those proposed conditions it can  
32 take a belt and braces approach and adopt them.

33 We do not consider there's any practical strengths to the  
34 parts raised by the major electricity users in Transpower in  
35 their response to the conditions and extension, those parties  
36 appear to see these practical measures adopted by the industry  
37 as a bargaining tool which it seems they will attempt to use to  
38 hold the industry and this process to ransom.

39 I repeat, with respect to the conditions, we, Contact, do  
40 not believe that the proposed conditions are necessary.  
41 However, if the Commission forms the view that one or more of  
42 them should -- if the Commission forms the view that one or more  
43 of the conditions should be applied in order for the application  
44 for authorised, i.e. For the net benefits to outweigh the public  
45 benefits, then we support those conditions but only to the  
46 extent necessary to shift the balance in favour of the net  
47 benefits.

48 And, with that, I'll turn to the other two outstanding  
49 issues.

1 **MS REBSTOCK:** Can I just stop you on those points and ask you a few  
2 questions.

3 I understand you to be saying that you would only support  
4 the use of those conditions if it was necessary to shift the  
5 balance. Is it your view that that is the only circumstances  
6 under which the Commission could impose conditions?

7 **MR KILTY:** No, that's not our view. In line with what the  
8 applicant said, I think on Thursday, we believe the Commission's  
9 power to impose conditions is very broad and you're entitled to  
10 impose the conditions you wish to impose. It's simply our  
11 submission that we don't think these conditions are necessary,  
12 as we've said we think the tensions are there to ensure in the  
13 existing model which is now reflected in the Rulebook, to ensure  
14 that pro-competitive rule changes do go through and we think  
15 history has shown they have.

16 As Toby mentioned, the only block to those changes are  
17 technical, security and physical reasons, and championed often  
18 by the system operator.

19 **MS REBSTOCK:** The other question I wanted to ask you, and I believe  
20 I put this to the applicant as well, is of course there's the  
21 possibility that if conditions could be something other than  
22 what has been proposed by the applicant, what's your submission  
23 with respect to a circumstance -- and it's purely theoretical --  
24 where the conditions could be something different than what has  
25 been proposed by the applicant? Do you still form the view that  
26 we could impose them and what's your view with respect to  
27 further consultation on that?

28 **MR STEVENSON:** The proposed amendments, I suppose the applicant  
29 could have arrived at a different mechanism to address the issue  
30 raised in the Draft Determination, but the proposed amendments  
31 benefitted from the consideration by the EGEC and the use of the  
32 Governance Working Group, which is a fully representative body,  
33 and so it's a typical example of a governance structure arriving  
34 at something that has enjoyed substantial agreement between the  
35 parties.

36 If there is another solution that they considered and  
37 rejected or didn't consider, then another time, perhaps, they  
38 would do that, but if a condition is to be applied we would  
39 accept, favour this one because it has gone through that  
40 process.

41 I'm not sure that directly answers your question. [pause].  
42 David Hunt pointed out that the representation on the Governance  
43 Working Group does include consumer representation.

44 **MS REBSTOCK:** There were more than one option -- I mean, I've  
45 looked at the material that was at least put on the website and  
46 my understanding is there was four options that were considered.  
47 Is that -- do you think that's possible to ask, if it's not  
48 appropriate, please tell me?

1 **MR STEVENSON:** I don't have them in front of me. I do recall that  
2 there were more than two but I can't remember the specifics of  
3 them.

4 **MS REBSTOCK:** And your submission is, is that there was broad  
5 agreement to the condition that was put forward?

6 **MR STEVENSON:** There was substantial agreement, I think is the term  
7 that we use for the Working Groups. I think David's point is  
8 that there were some people who argued for another complete  
9 approach to the pro-competitive rule changes, and those people  
10 will make their submissions in due course. But I think some of  
11 those approaches may have involved a complete dismantling of  
12 parts of governance structure and a re-assembling in a  
13 completely different way.

14 My point to you is that the proposals enjoy substantial  
15 support through the mechanism and they represent a continuum of  
16 Rule development as we know it, and on that basis, if the  
17 Commission -- we don't think they're necessary, but our point is  
18 that if the Commission needs them, the belts and the braces,  
19 this is a natural continuum of what exists.

20 **MR CURTIN:** Just following up here. I understand the extent to  
21 which you sort of are prepared to get in behind the late changes  
22 to the Rules of the late conditions. You argued that they're  
23 not necessary and you point to, they're in the tradition only to  
24 the extent necessary to get the thing past the finishing line, I  
25 understand those qualifications. But you're leaving a little  
26 bit open, I think, your view on the merits of the conditions  
27 absent those points.

28 I take it that -- would I be reading you correctly that you  
29 as a company do not support the condition other than in the  
30 context in which they were offered?

31 **MR STEVENSON:** Right. We don't think they're necessary because we  
32 think that the tensions that will support pro-competitive rule  
33 changes being advanced already exist. We think that the  
34 proposed code draws on the strengths and experience of the  
35 existing codes, but the governance structure is advanced because  
36 it is comprehensive and independent, and we think that add to  
37 that the tensions that we've talked about, the Rules as  
38 submitted will not require the added pieces to ensure that pro-  
39 competitive rule changes continue to enjoy advancement,  
40 notwithstanding technological limitation as they have.

41 That's the position. The mechanisms that have been  
42 proposed, we don't -- well, perhaps I could put it this way. We  
43 don't, that they would be caught -- we cannot imagine a Rule  
44 change for which they will be called on because of the  
45 experience and the tensions that exist. So that's why we think  
46 that they are unnecessary, but we would support their  
47 introduction because we don't think they will be utilised.

48 **MS BATES:** This is just a follow-up question to Ms Rebstock's line  
49 of questioning specifically about the possibility of the  
50 Commission perhaps imposing conditions which are different to



1 the ones suggested, and the question is, if the Commission was  
2 minded to do that, is it your view that the Commission should  
3 refer those back for consultation or not?

4 **MR STEVENSON:** Of course. I mean, my experience and our submission  
5 is based on agreement in Working Groups, and over the years on  
6 the Working Groups and committees that we have been on we have  
7 had a number of wins and losses, and we live by them all, and I  
8 would be concerned if a mechanism was introduced that hadn't  
9 been put to that scrutiny.

10 **MS BATES:** Thank you.

11 **CHAIR:** Are you going to come -- I'm just looking at the subsequent  
12 submission, or looking at question 9, and you've covered the  
13 penultimate paragraph in relation to systems security issues.  
14 The next one relates to the Crown EGB; are you going to cover  
15 that again today or shall I ask you a question on it now?

16 **MR STEVENSON:** Ask a question on it now.

17 **CHAIR:** Because the two to some degree are linked.

18 One of the issues that was made, I think by Mr Hansen for  
19 the applicant, was this question of security and related issues,  
20 balanced or traded off against innovation and further  
21 development.

22 What you seem to be saying -- and if I'm putting words in  
23 your mouth I'm sure you will tell me -- in both of those  
24 paragraphs the system operator, A, directly in relation to his  
25 laying pro-competitive developments, you are talking about CCGT  
26 technology and, secondly, whether it's a separate argument or  
27 the same point. You seem to be saying that the EGB will take a  
28 deferential approach to the system operator, again, is that  
29 based on an argument about systems security which is mentioned  
30 there, or are you looking at something wider?

31 Behind that I think is an issue, of course, the  
32 Commission's got to make a judgment on, but have you got any  
33 views on where both those statements are leading, and indeed  
34 what evidence have you?

35 **MR STEVENSON:** Thank you. I will cover the point by going to the  
36 last part of the presentation. If I don't cover it totally, and  
37 I have some examples -- if I don't cover it totally can we  
38 return to it, please?

39 **CHAIR:** Absolutely, yes.

40 **MR STEVENSON:** The other two points of the five that we were to  
41 make are the quality of decision-making under a Crown EGB and an  
42 industry EGB and the potential for over-investment in the grid  
43 under a Crown EGB and under-investment in the grid under an  
44 industry EGB.

45 We have some examples which David is going to distribute,  
46 but by way of preamble, in terms of the quality of decision-  
47 making there's a number of features that have been raised;  
48 Transpower has raised the issue of Working Group capture by  
49 participants, and we've just seen an example of the Working  
50 Group mechanism at play with the pro-competitive amendments. We

1 reiterate that an industry EGB will be an independent body with  
2 executive power to appoint and dissolve Working Groups as it  
3 sees fit. You have obviously picked up on the fact that the  
4 most guilty party when it comes to Working Group capture is in  
5 fact Transpower.

6 **CHAIR:** Can you give me evidence of that? I mean, have you got  
7 specific examples of where you can demonstrate that; that's a  
8 fairly strong statement?

9 **MR STEVENSON:** My pleasure.

10 The real time pricing would take us from solving every 30  
11 minutes to solving every five minutes in running the model and  
12 solving every five minutes instead of every 30 minutes. I  
13 introduced a rule change in May 1999 that we should move to  
14 ex anti real time pricing, and one of the precursors was to be  
15 the real time dispatch, the solving for dispatch purposes which  
16 would subsequently be used for solving for pricing purposes by  
17 running the model every five minutes.

18 When Transpower introduced the real time dispatch they did  
19 so with remarkably little consultation, and as you have already  
20 heard from another operator of a large thermal power station, I  
21 can confirm, as this operator of a large thermal power station,  
22 the mechanism was very disruptive. All we asked of Transpower  
23 was that they work with us in introducing a mechanism that both  
24 arrived at five minute solving a real time dispatch, but also  
25 meant that we would run our machinery and compete free and  
26 unfettered.

27 That request to participate in the process of design and  
28 implementation was seen as blocking. The CEO of Transpower  
29 stated in a submission to the Select Committee that I was  
30 blocking real time pricing, when in fact all I and the industry  
31 were doing was wanting to participate in a good formulation of a  
32 mechanism that satisfied both the physical requirements of the  
33 grid -- of generation, and the requirements for unfettered price  
34 discovery.

35 Another example. When we were doing the real time pricing  
36 work last year the Project Manager and the Market Pricing  
37 Working Group resolved that they wanted to move to ex anti, that  
38 is covering of price five minutes before real time which would  
39 hold as opposed to ex-post, which is using data immediately  
40 after real time to solve.

41 Transpower made it very clear that they would not entertain  
42 an ex anti mechanism. We had a choice to proceed with ex-post  
43 or nothing, and as I indicated the other day, we are now  
44 proceeding with ex-post five minute pricing.

45 Is that enough examples?

46 **CHAIR:** Yes, thank you.

47 **MR STEVENSON:** Thank you. We've talked about the quality of  
48 decision makings and Working Group capture, just covered. I  
49 think that Transpower genuinely believe that they have a  
50 perspective; I think that that is important for the technical

**Contact**

1 solving of these issues. I think they also believe, based on  
 2 Hogan's testimony, that the industry solely acts in self-  
 3 industry and we need Transpower to save us from ourselves. We  
 4 believe that the decisions under the independent EGB will be  
 5 superior to the counterfactual precisely because the Minister  
 6 himself comes from a point of self-interest and is in fact more  
 7 susceptible to lobbying. In our view, the independent EGB will  
 8 be independent unless susceptible to lobbying, a point I think I  
 9 made quite clearly on Friday in another context.

10 In their own word Transpower considers that lobbying will  
 11 be common to both the Crown EGB and the industry EGB but will be  
 12 more transparent apparently under the Crown EGB, the implication  
 13 that that is a good thing. Whilst I respect Transpower's  
 14 opinion on this because they are in my view the experts on  
 15 lobbying, I disagree with their conclusions. We don't need them  
 16 to save us from ourselves.

17 We consider that the proposed arrangements give rise to  
 18 benefit relative to the counterfactual.

19 With respect to specifically under-investment versus over-  
 20 investment, the assessment of balancing transmission investment  
 21 is by its nature a very technical and difficult subject, but the  
 22 point that we would make is that under-investment is very  
 23 visible, the lights go out, it's far more difficult to see where  
 24 there is over-investment because it can be hidden.

25 The technical nature of the issue and problems with seeing  
 26 over-investment mean that the only people that can be trusted  
 27 with making decisions on such investments are those that are  
 28 appropriately skilled and have a stake in the outcome, and the  
 29 industry meets both these characteristics. The industry feels  
 30 the cost of both over-investment and under-investment and the  
 31 Minister under the counterfactual would only feel the cost of  
 32 under-investment, thus the bias, which is our conclusion.

33 **MS REBSTOCK:** Do you think consumers have an interest in the  
 34 outcome?

35 **MR STEVENSON:** Of course.

36 **MS REBSTOCK:** A stake in it?

37 **MR STEVENSON:** Of course. When I refer to stakeholders I include  
 38 most definitely consumers.

39 **MS REBSTOCK:** And what's their influence going to be on these  
 40 decisions?

41 **MR STEVENSON:** Well, there's the voting -- they have the voting  
 42 rights that are in Part A in terms of forming the EGB.

43 **MR HUNT:** Perhaps to go back, in terms of the overall governance  
 44 arrangements, a third of the votes are awarded to consumers, a  
 45 third to transporters, Transpower and network companies, and a  
 46 third to generator/retailers. Consumers would also have voting  
 47 rights in the common quality chapter and in the transport  
 48 chapter; and, to the extent that consumers participate in the  
 49 wholesale market, they'll also have votes, not chapter, dealing  
 50 with Rules relating to the wholesale market as well.

1 **MS REBSTOCK:** And where do they not have votes?

2 **MR HUNT:** My recollection is, there are no votes particularly in  
3 relation to reconciliation, settlement.

4 **MR KILTY:** Perhaps it might be helpful to refer to a table in the  
5 Rulebook in Part A, governance, page 141. There's a table there  
6 that sets out the voting arrangements. David was basically  
7 reciting that, and you will be able to see from there where the  
8 votes do lie. So, that might be helpful.

9 **CHAIR:** Yes, I think we'll obviously have another close look at  
10 that as we consider all this because voting obviously is an  
11 issue. But just shorthanded you are saying that apart from  
12 reconciliation and settlement there are consumer votes generally  
13 there?

14 **MS REBSTOCK:** I just want to pursue this a little bit further.  
15 Transpower's part of this industry and has a particular interest  
16 and a particular expertise, and yet, I almost hear you saying  
17 that others in the industry are better placed to make these  
18 decisions than Transpower. Is that a fair summary of what you  
19 are saying?

20 **MR STEVENSON:** Yes it is, and the first example I'm going to use is  
21 an example of exactly how that incentive -- how that balance  
22 works.

23 If you turn to the examples showing demand forecast versus  
24 actual, and I can take you through the basis of the example that  
25 is an illustration of it.

26 A Treasury study carried out in 1985 reviewed electricity  
27 planning and electricity generation costs during the period of  
28 direct governance stewardship. The investigation reveals a less  
29 than satisfactory situation in this area of stake investment as  
30 regarding the adequacy of advice presented to Ministers by the  
31 investigation, choice, and management of projects, basic  
32 precepts of power planning and the efficient administration of  
33 state resources. The economic cost of mismanaging of just three  
34 projects was estimated in the order of hundreds of millions of  
35 dollars. Projects were not undertaken on the cheapest first  
36 basis. Future demand for electricity was consistently over-  
37 estimated; indeed demand has not obtained the levels that were  
38 forecast by the Government in 1974.

39 If you look at the chart you will see the shorter bars for  
40 each year are the actual total nationwide demand, and you will  
41 see that the forecast from 10 years earlier is the right-hand  
42 bar, and if you look at 1984 -- in 1974 they estimated that  
43 demand would be 39,000 gigawatt hours, and in 1984 demand was  
44 actually 26,000 gigawatt hours. If I might point out that  
45 demand in 2001 was still only 36,000 gigawatt hours. So in 1974  
46 they were estimating that demand would be at a level in 1984  
47 that has still not been achieved in 2001. The implication being  
48 that the decisions that are made, that what would result from  
49 that decision-making would be over-investment and, as I've

1 pointed out, over-investment is far less conspicuous than under-  
2 investment.

3 **MS REBSTOCK:** This is about generation, right? What does this tell  
4 us about Transpower's incentives to invest in transmission  
5 investments?

6 **MR HUNT:** I think it's always difficult to find examples that are  
7 exactly replicating the question we're trying to answer today.  
8 Where we see the parallels though are that, this was a -- it's  
9 the same sector, it's New Zealand, it's a little while ago  
10 admittedly, but nonetheless there are some common features. In  
11 fact, it's describing a state of the world where Ministers made  
12 the final decisions.

13 **MS REBSTOCK:** The reason I ask is, you're suggesting to us that  
14 generators in particular, presumably, are well placed to make  
15 investment decisions.

16 This was about a generation investment. You are in the  
17 same industry as Transpower, so are the incentives on you the  
18 same or are they different and why?

19 You have put forward an example about the generation side  
20 making investments -- I understand of course in this period that  
21 it was all pretty much one outfit, but I just -- you know, on  
22 the one hand you tell me it's one industry and generally things  
23 apply across it; on the other hand you are telling me that the  
24 generation side here can make more reasonable investment  
25 decisions than Transpower.

26 So, I'm just having a little trouble understanding the  
27 relevance of this evidence to the issue that you are putting to  
28 us. So, if you can help me with that.

29 **MR HUNT:** Okay. The relevance is the location of the decision and  
30 the incentives on the decision maker. Were generation to be  
31 returned to political control direct decision-making by  
32 Ministers, it would be our contention that there would be an  
33 inherent bias toward over-investment, because Ministers feel the  
34 cost of outages much more keenly and worry about that more than  
35 the cost of over-investment.

36 **MS REBSTOCK:** How much generation is now owned by the Crown?

37 **MR HUNT:** The bulk of the generation sector is still Crown owned,  
38 but the decisions are not made by Ministers. The decisions as  
39 to whether those generators invest are made by boards.

40 **MS REBSTOCK:** And if the Crown were so influenced by its political  
41 risk, it could take that decision any time, couldn't it, as  
42 owner?

43 **MR HUNT:** It could take that decision, that's correct.

44 **MS REBSTOCK:** It has not?

45 **MR HUNT:** Well, I don't know.

46 **MS REBSTOCK:** Well, presumably it could do so under the current  
47 situation, the counterfactual or under the proposal, if it  
48 wished to, over-investment, because of political risk, it has  
49 the ability to do it under each and every scenario?

1 **MR HUNT:** It certainly has the ability to influence decisions by  
2 companies that it owns, we don't dispute that fact.

3 I think our issue is more, who feels responsible for the  
4 decision and does that party feel the cost of poor decisions?

5 **MS REBSTOCK:** I'm just trying to get at, how much worse would it  
6 be?

7 **MR HUNT:** We're not arguing that, you will see this level of over-  
8 investment per se. The point that we're trying to illustrate is  
9 the difference between a party who has a balanced set of  
10 incentives -- and you know, frankly, none of these arrangements  
11 are perfect; we're not arguing that one is perfect and one is  
12 not. It's, which situation delivers the better outcome?

13 Perhaps we should just go on and deal with the other two  
14 examples and perhaps come back to the generic issue that you are  
15 raising.

16 **MS REBSTOCK:** Clearly in the draft we accepted some, that there was  
17 a potential issue here. The question for us is to quantify the  
18 extent of it, and so that's why I'm trying to encourage you to  
19 explain to me what yields this result. Others have challenged  
20 it.

21 **MR STEVENSON:** Can I approach it in another way. We're advocating  
22 the Rules as proposed, we're supporting the Rules as proposed  
23 and in it is a Part F governed by an independent governance  
24 board. We think that in that Part F there will be tensions that  
25 will produce good investments in terms of transmission and that  
26 the governance will keep it independent, the right people will  
27 be making the right decisions with the right incentives.

28 Our submission is that if the same Rules, or specifically  
29 if that mechanism were taken in under a Crown governed EGB, the  
30 balance that we see with the independent EGB structure would be  
31 disturbed, and we are submitting that it would lead to over-  
32 investment. That's our opinion based on our experience.

33 **MS REBSTOCK:** Can I just ask you one question on that. Would you  
34 accept that this is the -- potentially the area of highest risk  
35 in the proposal, in terms of public interest? If there was  
36 under-investment as a result of the proposal, the risks -- the  
37 potential risks could be quite high?

38 Would you accept that this is where -- when we look at this  
39 proposal, if there are risks in it this is where they are likely  
40 to be?

41 **MR STEVENSON:** I can't assess the greatest risk. I can assess the  
42 level of frustration that we have with under-investment with the  
43 grid at it stands. And it's our view that Part F will finally  
44 free up some investment decisions.

45 We see it as a significant step forward for some of the  
46 concerns that we have. At the moment I buy about 6,000 gigawatt  
47 hours a year at 150 different points across the country. I sell  
48 about eight and a half thousand gigawatt hours a year to 10  
49 other different points. We're moving a lot of juice around the  
50 grid and we see evidence of under-investment in the grid around

1 and Part F will be an advance in terms of solving that, so too  
 2 will the introduction of FTRs; those two and combined make the  
 3 movement of the juice around the grid much more efficient.

4 As to whether Part F is the greatest risk in the Rules, I  
 5 can't assess that. I can only assess that it is an advancement  
 6 in a frustrating -- of a frustrating situation.

7 **CHAIR:** Can I come back to Mr Hunt's point. In looking at this  
 8 graph and leaving aside when it took place and the situations,  
 9 because I think from memory there have been quite extensive  
 10 over-estimates of demand for electricity, possibly even after  
 11 these projections were published, all things being equal, I  
 12 think you said you've got a number of State Owned Enterprises  
 13 plus yourselves. Why would the incentives on the system  
 14 operator that's also a State Owned Enterprise, and in theory  
 15 should be working to the same principals as the other SOEs,  
 16 namely I think the only Government intervention is through their  
 17 SCI but otherwise decisions need to be commercially based,  
 18 intrinsically why should the incentives on that SOE be any  
 19 different from the SOE generators who were contemporaneous with  
 20 yourselves?

21 **MR HUNT:** I think the difference comes about because at the moment  
 22 Transpower will not invest unless it's assured of receiving a  
 23 return on its investment, or I shouldn't speak for Transpower --  
 24 that's how it appears to us, at least.

25 Under the proposed grown EGB arrangements, as we perceive  
 26 them, what they will do is shift that decision-making focus to a  
 27 point where Transpower is likely as system operator because we  
 28 think it will have the ear of the Government, as will the  
 29 industry and other stakeholders, but we believe that the ear  
 30 will be somewhat closer to the system operators' mouth than  
 31 ours. But also because the Minister, the party who's making the  
 32 ultimate decision, and bear in mind that the EGB is somewhat of  
 33 a veil in this in our view; the Crown EGB will be constituted  
 34 but parties are appointed by the Minister, can be dismissed at  
 35 any time by the Minister. The wording is in fact quite unusual  
 36 in our recollection as to the powers of dismissal. The  
 37 Minister's required to consult with the EGB but in turn the EGB  
 38 is required to consult with the Minister before giving a  
 39 recommendation.

40 So there is every chance the Minister is going to hear what  
 41 he or she wants to hear and for that reason we think the  
 42 Minister is going to be much more concerned about the prospect  
 43 of lights going out than that everybody pays another few  
 44 percentage on their power bills, because that's not going to be  
 45 so visible.

46 **CHAIR:** I don't want to get into the operations in detail of what  
 47 might or might not be a Crown structure, it could differ. From  
 48 the point of view of principle, and it might be better if the  
 49 question was asked, I guess, of a state generator, which I may  
 50 well do, do you think all things being equal, the fact that a

1 generator is state owned and the system operator is state owned,  
2 the system operator will have the lead on lobbying or influence  
3 as another major State Owned Enterprise, namely a generator, of  
4 which there are three?

5 **MR HUNT:** I think the issue revolves more around -- as a Minister  
6 what are you most concerned about and what are you most visibly  
7 accountable for? In our view that gives a natural bias towards  
8 taking the safest approach, even if it has higher cost, than  
9 what the parties who are supposedly benefitting and will pay for  
10 it are going to see.

11 I guess what it comes down to is, in our view, under the  
12 alternative of a stakeholder EGB there is a balance, there is  
13 more of a tension, there is more of a dynamic, the issues are  
14 more exposed to debate. We're not saying Transpower's going to  
15 be wrong and the generators are going to be right, I'm sure it  
16 will vary from time to time. There is the prospect of all of  
17 those issues being debated and resolved.

18 **CHAIR:** Thank you.

19 **MR HUNT:** Can I make one further point? The other thing that  
20 concerns us is that we see a higher likelihood of Crown EGB  
21 processes being less transparent. Now, again, we can't know  
22 because we don't know what the processes will be, but at the end  
23 of the day when the Minister has a meeting with the EGB it's not  
24 clear to us that that process will be out in the public gaze.  
25 It's different under these Rules. These Rules are very much  
26 designed around transparency.

27 **CHAIR:** Thank you.

28 **MR STRONG:** You talk a lot about the incentives on the system  
29 operator and the bias towards over-investment. A number of  
30 submitters have raised the point that the ODV process put some  
31 constraints on Transpower and how it can recover the costs of  
32 those investments. I just wonder whether that constraint might  
33 be sufficient to allay fears that there could be over-  
34 investment?

35 **MR HUNT:** I guess from our perspective it's somewhat uncertain as  
36 to how that's going to work going forward, given the changes  
37 that have been made to the regulatory environment that have not  
38 yet settled.

39 That's one issue. I think, standing back from it, it would  
40 seem to us at least arguable that if Transpower is compelled it  
41 make investments by a Minister or because it would be paid for  
42 under some voluntary arrangement by an industry, it's hard to  
43 see why that -- put it this way, Transpower would have a good  
44 argument for saying that the ODV should not be attacked,  
45 particularly if it's compelled by a Minister. So I'm not sure  
46 that that is much of a safety net. I think it's more a case,  
47 from our perspective, having users having a direct say, the  
48 people who are actually going to pay for it.

49 **MS REBSTOCK:** I have trouble with this notion that -- and I want to  
50 give you the chance to tell me what your thinking is on this.



**Contact**

1 If Transpower is so able to lobby and is -- and part of the  
 2 reason for that is around the political risk around the lights  
 3 going out; why do we see under-investment in the grid going on  
 4 for such long periods?

5 This is very hard to connect, why we see that and why you  
 6 project the Crown EGB would lead to an over-investment, because  
 7 presumably Transpower has all that ability now to influence the  
 8 Crown and yet the Crown has not shown any predisposition to  
 9 allowing over-investment over many years.

10 So, I would just like you to explain to me that -- what it  
 11 is that changes that suddenly makes over-investment the likely  
 12 result when presumably all of those political realities around  
 13 the risk of the lights going out exist now and have existed for  
 14 some time?

15 **MR HUNT:** Put very simply, Transpower does not have access to other  
 16 people's cheque books at the moment. That's what it comes down  
 17 to.

18 Under a Crown EGB the Minister can force people to pay for  
 19 investments.

20 **MS REBSTOCK:** But the Crown presumably, having had long periods  
 21 where -- and I've heard this for many years, that there's been  
 22 under-investment and that there's been serious risks in parts of  
 23 the grid, and even after the experience of, say, what happened  
 24 in Auckland, you'd think there'd be heightened concern about the  
 25 costs of a major failure -- the Crown any time could have  
 26 stepped in and provided a means for which that under-investment  
 27 was fixed, but it hasn't done so.

28 So they could have stepped in any time, in fact. If you  
 29 look at the legislation we're looking at at this Conference,  
 30 they have still indicated a reluctance to come to the fore in  
 31 this.

32 So, what is it that suddenly is going to change the Crown's  
 33 attitude towards this?

34 **MR STEVENSON:** It's not the Crown's attitude that's going to  
 35 change. What will change under the independent EGB is that  
 36 there will be a mechanism by which the decisions can be made and  
 37 the reliability for payment can be made.

38 **MS REBSTOCK:** Sure, I understand that, but you have under a Crown  
 39 EGB too; but what you are saying, that under a Crown EGB not  
 40 only would you get the investment you need but that you'd get an  
 41 over-investment?

42 **MR HUNT:** I think that there's an inherent bias.

43 **MS REBSTOCK:** And it's that leap to the over-investment side that I  
 44 have difficulty with because what it seems you are saying is  
 45 that it would support that over-investment, the dynamics for  
 46 that already exist.

47 **MR HUNT:** I think the difference is that the incentive exists at  
 48 the moment but there is no means of translating that incentive  
 49 into action as things stand.

**Contact**

1 **MS REBSTOCK:** The Crown has unlimited ability to translate its  
2 concerns into an outcome, it must have.

3 **MR HUNT:** Okay. Obviously as sovereign it has control, but put it  
4 this way, it has no easy means at the moment.

5 **MS REBSTOCK:** It not only could legislate but it could do it,  
6 couldn't it, through its ownership of a large part of the  
7 system?

8 **MR HUNT:** That's right, but were it to do that it would have to do  
9 that in a very visible and transparent way. It would to -- for  
10 example, make explicit subsidy to pay investments to Transpower.  
11 It wouldn't have to do that under this arrangement. It can  
12 simply decide that this piece of grid needs to be enforced and  
13 these customers will pay. The way it does that -- and the  
14 effect of it will be wrapped up in the much bigger picture and  
15 very hard to see as an element by itself.

16 So you are quite right, it has the ability now but were it  
17 to do that, it can't do it by stealth, and I think that's really  
18 the issue that we're highlighting. I think it's worth just  
19 covering these last two examples.

20 **MS REBSTOCK:** Okay, thanks.

21 **MR STEVENSON:** The second example is an example of power prices for  
22 commercial customers, and the chart that you have entitled  
23 "electricity price differential commercial versus all classes",  
24 there is an example. Until the early 90s power distribution was  
25 generally carried out by organisations that were overseen by  
26 boards comprised of locally elected representatives that change  
27 with reforms first mooted in 1989 and finally legislated in  
28 1992, and the chart shows the price differential between  
29 commercial versus all other classes dating first of all in the  
30 beginning from 1979 through to 2000.

31 In 1992 the Energy Companies Act gave distribution  
32 companies clear business objectives and provided for the  
33 appointment of commercial directors to oversee the enterprises.

34 You see there that the differential between commercial  
35 versus all classes has fallen from some 85% to virtually  
36 negligible now.

37 **CHAIR:** Was that legislated for or was it a general exultation to  
38 the industry? I mean, it was pretty -- Mr Dellow may recall  
39 anyway, but it was acknowledged that there was, as you said,  
40 consumer subsidy of quite some magnitude because of the way  
41 power boards were elected. But was it legislatively required to  
42 remove those subsidies or was it general exultation?

43 **MR DELLOW:** I think it was more that deregulation of the industry  
44 in the sense that the companies faced competition at the edges  
45 of their -- and from new retailers coming in which was possible  
46 before then, if that answers the question as I understand it.

47 **CHAIR:** It wasn't legislated before apart from the setting up of  
48 the electricity companies, that was all?

**Contact**

1 **MR DELLOW:** And removing the need for licences under the old  
2 Electricity Act so that other retailers could come in and  
3 compete.

4 **MR HUNT:** Could I add, I think there were two important effects;  
5 one was competition, as Tony mentions, and the other way -- and  
6 we can't prove this but I think it's a hypothesis that's hard to  
7 dismiss -- and that as it's an elected board the parties running  
8 the distribution companies prior to the reforms were more  
9 concerned about looking after those people who elected them i.e.  
10 The numerous residential customers, at the expense of the not so  
11 numerous commercials. And as an evidence of that these prices  
12 are delivered prices, they are the energy component which there  
13 was competition for, and the network component which there  
14 wasn't competition for and you have seen the differential move  
15 down to virtually nil for both. So, it's not just competition.  
16 It would appear that something else is happening as well.

17 **CHAIR:** Okay, thank you.

18 **MR STEVENSON:** The last example I want to refer to, in terms of the  
19 Crown's influence, was the South Island differential.

20 Prior to the establishment of the wholesale market under a  
21 single central structure a differential was applied in favour of  
22 South Island consumers, it was generally held to reflect the  
23 relative abundance of lower cost electricity from higher  
24 degeneration in that island. The differential that was  
25 maintained between the North Island prices and South Island  
26 prices was to the order of 20%, depending on how it's measured.

27 At the time of the establishment of the wholesale market  
28 there was a high degree of concern by a number of politicians  
29 that this differential might shrink or disappear -- I should  
30 say, a high degree of concern by a number of South Island  
31 politicians especially that this differential might shrink or  
32 disappear, and I understand that this was one of the most  
33 difficult issues to receive political reconciliation at the time  
34 that the wholesale market was being -- it was being agreed that  
35 a wholesale market could emerge.

36 There were some transitional arrangements put in place to  
37 provide a top-up to the differential in the event that the  
38 market prices between the islands did not meet the desired  
39 political threshold. What we've seen under the wholesale market  
40 in fact over the last two or three years, the differential  
41 between North Island and South Island prices on average, 1999  
42 was 8%, 7% in 2000 and, in fact, last year there was only half  
43 of 1% difference between the North Island and South Island. So  
44 that 20% differential did not reflect what has been discovered  
45 under a wholesale pricing regime -- unfettered price discovery.

46 **CHAIR:** So you are saying that the wholesale market in essence  
47 levelled that out in relation to how the market operated?

48 **MR STEVENSON:** Yes, and so, the South Island differential that had  
49 been maintained, circumstances may have been different, but  
50 we're arguing that that was purely politically held, and it's

1 another example of Crown interference in the way a market would  
2 naturally discover prices.

3 **MR HUNT:** Could I just make one concluding comment on this. I  
4 think, although they don't directly relate to the decisions that  
5 you face, they all have one thread in common and that is that,  
6 when Ministers -- elected people are forced to be the decision  
7 maker you get a different outcome from one where that elected  
8 person can get someone else to make the decision.

9 I guess what we're arguing here is that, under a  
10 stakeholder EGB the Minister has the ability to intervene but is  
11 not obliged to, whereas under a Crown EGB the Minister must make  
12 the decisions, they must therefore take the accountability for  
13 it. It's our view that the Ministers and Parliament has, in  
14 effect, said our preference is that you tie our hands to the  
15 mast; in as much as the detail of this, we would rather  
16 stakeholders work out, we would prefer to set overall direction.

17 **CHAIR:** You make the point. Thank you.

18 **MR STEVENSON:** At the risk of being repetitive, I have a couple of  
19 concluding remarks. They should all have been covered, but just  
20 in case I missed one.

21 We think the Commission should consider the following. The  
22 Government doesn't want to regulate, in fact it seems at pains  
23 to avoid it. They state in the Government Policy Statement "to  
24 meet the Government's policy it favours industry solutions where  
25 possible". It continues "the Government wishes to see further  
26 revolution of Self Regulatory arrangements". So, we would argue  
27 the Government does not want a Crown EGB specifically and we  
28 would also argue the only realistic option is an industry EGB as  
29 is the subject of the application.

30 In Contact's view the proposed EGB enjoys the benefit of  
31 what has been learnt to date as well as the benefits of being  
32 comprehensive and independent.

33 The granting of the authorisation if applied for does not  
34 stop anti-competitive conduct being before the Commission in  
35 future, nor does it stop the Crown regulating it, it does not  
36 consider that the industry EGB is meeting the Government Policy  
37 Statements. Why wouldn't you give it a chance to succeed?

38 **CHAIR:** Thank you very much, and for coming back this morning after  
39 we broke on Friday.

40 Well look, just going back --

41 **MR STRONG:** Could I ask a few questions? I think the Commission's  
42 found it very useful, you've gone through a number of examples  
43 this morning and no doubt we'll hear some counter-examples from  
44 those parties that are opposed.

45 I don't want to pre-empt other people, but Transpower in  
46 its submission notes that there are some, what they consider  
47 existing anti-competitive rules, and one example they cite is  
48 with respect to transitional dispensations. If I can quote  
49 them:

1 "Transitional dispensations effectively exempt incumbent  
2 asset owners from certain security obligations on an ongoing  
3 basis and provide that those individual incumbents will not be  
4 allocated the cost of ancillary services required as a result of  
5 the dispensation given to them.

6 Under the counterfactual of a Crown EGB it is likely that  
7 dispensations will be equally applied to incumbents and new  
8 entrants, i.e. Any quantifiable cost that arises from a  
9 dispensation will be allocated to the individual asset owner  
10 that receives the benefit of that dispensation."

11 And they suggest that transitional dispensations are a  
12 futation of the assumption that industry members will create  
13 efficient rules for industry based on cost/benefit trade-offs by  
14 industry participants.

15 So I wonder if you could perhaps work through that as an  
16 example that they consider is an anti-competitive rule.

17 **MR KILTY:** What you are referring to is what's commonly known as a  
18 grandfathering provision which is simply, we would submit, a  
19 reflection of the practical implications of introducing new  
20 standards to a plant that has been around for a long, long time.

21 We would also point out that grandfathering provisions are  
22 common in legislation where there's an update in standards, or  
23 conditions. An example that Tony and I discussed a couple of  
24 days ago, and I might throw this one to Tony, was under the  
25 Electricity Act, is that right, Tony?

26 **MR DELLOW:** Yeah, well there are examples, of course, of the --  
27 they're called grandparenting provisions. The example you're  
28 talking about is the provisions in the Electricity Act, also in  
29 the Telecommunications Gas Act, that protect existing works at  
30 the time of deregulation that are on land from merging with the  
31 land when the legislation that they have been put thereunder is  
32 repealed. So protecting the existing works protects the access  
33 of the owners to them across the land.

34 **MR KILTY:** The point I'm trying to make here is that those  
35 dispensations are for practical reasons and so we would refute  
36 any implication that it's otherwise than that. Whether it's  
37 anti-competitive at all, it's simply a fact that the plant is  
38 old; that's all.

39 **MR HUNT:** Can I just add one other thing, and I'm not entirely sure  
40 about, that I can't swear to it, but my recollection, at least,  
41 is that under the proposed Rules the dispensations would in fact  
42 be granted by the system operator and it's our understanding  
43 that the process they would follow is a very transparent one,  
44 and all dispensations granted will be notified publicly. So,  
45 there's not, in our view, really much scope for mischief, so  
46 we're rather surprised that that should be raised as an example.

47 **MR STRONG:** Transpower also raises this example of a failure to  
48 develop this pro-competitive Rule with respect to FTRs, and I  
49 note your comments the other day that you consider that the time  
50 for FTRs has come.

**Contact**

1 I suggest that generator/retailers have sought to control  
2 the loss and constraint rentals and that Transpower wishes to  
3 use those -- the monies resulting from those constraints as a  
4 means of funding FTRs and suggest that, by trying to control the  
5 rentals the further development of FTRs would be hindered.

6 I wondered if you could point to that as well.

7 **MR STEVENSON:** I thought I was going to get away without having to  
8 discuss this. Here we go.

9 The misinformation around this subject is vast. There  
10 should have been FTRs in 1997 within a year of the market. A  
11 great deal of efficiency in terms of investments and trading has  
12 been lost in the absence of them and I welcome Transpower's  
13 attention to the financial transmission right issue now. I said  
14 to the leader of the Financial Transmission Project as late  
15 as December 2000 -- I demonstrate I have indicated Contact's  
16 support for financial transmission rights then and we continue  
17 to support financial transmission rights, but I appealed to them  
18 then to make sure they include the industry in the  
19 considerations of the design of FTRs, the distribution -- the  
20 allocation of loss and constraint rentals and the governance  
21 over the regime.

22 It is mischievous for Transpower to turn around now and say  
23 that the industry is blocking FTRs when all the industry has  
24 asked is that they participate in a process. Transpower's view  
25 has been we don't understand and they don't have time to get us  
26 to understand; they have to get on and introduce the product.

27 So, they interpret our wanting to participate in the  
28 development of FTRs as blocking; I reject that.

29 The issue of loss and constraint rentals is borne partly  
30 out of the frustration that Transpower won't satisfactorily deal  
31 with the industry. The Rule changes that were proposed in the  
32 latter part of last year were not designed to block FTRs at all.  
33 That is quite wrong and misleading. The Rule changes that were  
34 proposed were that the status quo allocation of loss and  
35 constraint rentals be institutionalised in the Rules so that the  
36 introduction of FTRs would also be done under the umbrella of  
37 the Rules. It was not intended to block FTRs at all.

38 **CHAIR:** Thank you, we can obviously ask Transpower as well when  
39 they give evidence.

40 **MR HUNT:** Can I just give one final comment on that and that is, I  
41 think if you talk to major users they have the same concerns as  
42 generator/retailers over the process that's been followed for  
43 the initial design of FTRs and they have very similar concerns  
44 to generator/retailers.

45 **CHAIR:** Well, the major users are submitting this afternoon and  
46 they may wish to raise it, thanks very much.

47 All right, well I'll thank you again for coming back this  
48 morning and for answering a range of questions and giving us  
49 your views.

**Contact**

1           The New Zealand Wind Energy Association is timed next,  
2 initially we thought it was 10.30. Perhaps we should make that  
3 11.00 and Sustainable Energy Forum following, if that's okay,  
4 Molly. All right, we'll break for quarter of an hour. Thank  
5 you.

6  
7  
8                   **Adjournment taken from 10.44 am to 11.03 am**

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11   **\*\*\***  
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**NZ Wind Energy Association****PRESENTATION BY NEW ZEALAND WIND ENERGY ASSOCIATION**

1  
2  
3 **CHAIR:** It's now 11 o'clock and I thank the New Zealand Wind  
4 Energy Association for agreeing to delay their presentation.  
5 So, Mr Wilson, please.

6 **MR WILSON:** Thank you. I'm going to speak to our submission  
7 dated 22 February, the letter, and add a few points of  
8 clarification and be reasonable succinct, if that's possible,  
9 and answer any questions.

10 We, as you are probably aware, are a non-profit  
11 organisation. My name is Alistair Wilson. I'm the elected  
12 Chairman of the New Zealand Wind Energy Association, so I'm  
13 speaking on behalf of our membership.

14 As a non-profit organisation you might appreciate that  
15 our resources are reasonably limited so we've taken a high  
16 level approach; so will endeavour to assist to the extent of  
17 our capability.

18 We have a number of organisations who are members of our  
19 Association; that includes everything from large generators in  
20 the New Zealand system to small individual remote area power  
21 supply type people, farmers who have a small 1-2 kilowatt wind  
22 turbine which they use to support their own power needs.

23 The Wind Association has serious concern with respect to  
24 the EGB governance structure in its current form. We do not  
25 believe it's representative of the role of renewable and  
26 distributed generation, sustainable development or  
27 environmental integrity or responsibility and, therefore,  
28 fails the test of public benefit.

29 This has been a keenly debated position inside our  
30 Association as you might expect, given the membership, hence  
31 the outcome is for four principle reasons, which I guess I'll  
32 elaborate on.

33 We do have some significant concerns inside our  
34 Association that the industry is not co-ordinated, it is quite  
35 fragmented. We have some further concerns that such a  
36 fragmented industry is capable of having a self-governance  
37 mechanism that will be able to solve for all.

38 We have some further concerns that there is a strong  
39 desire and driver to protect the existing asset base of the  
40 incumbents, potentially at the expense of the entrance of new  
41 technology, whether that's new generation or demand side  
42 management or other site things; we've looked at some length  
43 for some way through which new technology. Wind, as you may  
44 be aware, is in fact the fastest growing generation technology  
45 in the world, unfortunately not here in New Zealand but it is  
46 elsewhere in the globe.

47 We have concerns that new technology is not going to be  
48 able to find its way into or have a seat at the table.

49 We did not, nor were we granted the opportunity to,  
50 participate, nor are we on any of the Working Groups. We're



*NZ Wind Energy Association*

1 definitely a new start-up industry, if I can use the  
2 colloquialism, "outside the tent". That's fine --

3 **MS REBSTOCK:** Did you seek to be on the Working Group?

4 **MR WILSON:** We have sought, and to be fair we did manage to bend  
5 the ear of the Chairman, that was the only ear we managed to  
6 bend, and we found that quite useful, but we have not managed  
7 to be able to put forward in forceful context the idea that  
8 new technologies should be factored into the thinking of the  
9 design of the Rules.

10 So we've concentrated our comments on the governance  
11 structure. We did ask the Chairman of the Working Group that  
12 perhaps he may wish to provide us with a legal opinion from a  
13 reputable firm that the rewrite of the principles did in fact  
14 reflect the Government Policy Statement. He didn't think that  
15 was such a good idea, so we still have concerns at the fact  
16 that the Government Policy Statement is in fact reflected  
17 appropriately in the governing principles as proposed by the  
18 industry EGB. We think there's a serious disjoint between the  
19 two.

20 We still continue to have some concerns that the  
21 environment as a concept, encapsulated within sustainable  
22 development is a key part of Government policy, is still  
23 omitted from the overall structure.

24 Hence, on balance, we find ourselves favouring a Crown  
25 or alternate solution to be able to take into account those  
26 types of more public good/public benefit type issues.

27 That's really all we wanted to say, other than answer  
28 any questions, if I can.

29 **CHAIR:** Thank you very much. I might start off, if that's okay.

30 In sub-para 1 of the submission of 22 May that you  
31 referred to in relation to new technologies in particular; I  
32 think the applicant, and I want to come back to it when they  
33 sum up at the end of the hearing, but were making the point  
34 that the way in which the Rules were being developed under the  
35 EGB were in essence not to inhibit new technology, and you  
36 would put wind generation outside that definition or  
37 statement?

38 **MR WILSON:** Historically wind generation has been a new  
39 technology and has struggled to penetrate the existing system  
40 due to a number of barriers to entry. I won't --

41 **CHAIR:** I mean, has it been cost?

42 **MR WILSON:** Cost is part of the equation because -- the cost gap  
43 is publicly disclosed at about a cent a kilowatt hour. That  
44 cost gap is in fact closing quite rapidly, and, for example,  
45 the Tararua project of which I do have some detailed  
46 knowledge, is in fact competitive with current generation.  
47 That's due to its location to load and wind resource. So, the  
48 gap is shrinking, but you still run into trouble.

49 Of the Rules, for example, connecting generation systems  
50 were not drawn up with intermittency of wind, for example, in

**NZ Wind Energy Association**

1 mind, because wind wasn't on the radar screen when the Rules  
2 were done. So what you do is, you faced a barrier to get the  
3 Tararua project up at the time, about being able to connect  
4 what was a utility scale wind farm still only 31.68 megawatts  
5 because the Rules had not contemplated the idea of a utility  
6 scale wind farm, therefore, intermittent generation.

7 That's an example of what we're trying to provide for  
8 here by saying, "Okay, there's going to be some new Rules",  
9 where we can we'd like to provide for new technology, whether  
10 that's wind or PV or the other -- even biomass and the other  
11 renewable technologies, provide for their ease of entry rather  
12 than having Rules which are controlled and drawn up by  
13 incumbents and protect existing assets.

14 **CHAIR:** But presumably -- I'm not sure who owns the Tararua wind  
15 farm now --

16 **MR WILSON:** It's owned by TrustPower now; it was joined by  
17 Central Power.

18 **CHAIR:** What about the one in Masterton?

19 **MR WILSON:** The one in Masterton is owned by Genesis and it's  
20 actually at the moment -- you may choose to ask Genesis --  
21 it's in the public arena; that's being targeted for expansion  
22 and it is having some difficulties expanding because of  
23 barriers to entry.

24 **CHAIR:** The point that follows, I guess, if Genesis own that one  
25 and Transpower own the other, both of which have more  
26 traditional generation facilities, presumably it's not a long  
27 stretch to see those companies being able to influence the  
28 Rules in time so that, when power can be incorporated into a  
29 space system.

30 **MR WILSON:** You may direct that question to them. I think they  
31 consider themselves to be a minority.

32 **CHAIR:** Okay, I just ask the question, that's all.

33 **MR WILSON:** That, of course, ignores the large number of 2-3  
34 kilowatt, remote area power supply type farmers who have 3  
35 phase power supply at their wool shed and, because of the  
36 flaky nature of the rural line, they have their own turbine.

37 **CHAIR:** But is it practical? I mean, I'm not a Rules expert, but  
38 presumably it's the utility size wind farm, like Masterton or  
39 the Tararua one, that the Rules are likely to have to  
40 accommodate rather than you or me in a farm out the back of  
41 nowhere with a supplementary generator driven by wind?

42 **MR WILSON:** We'd ideally like them to accommodate them all. We  
43 don't see why the farmers should be disadvantaged or not able  
44 to improve his power supply situation because the Rules are  
45 not drawn up to contemplate it.

46 **CHAIR:** Without being too technical, if you are a farmer you,  
47 presumably, are having electricity for yourself; how would the  
48 Rules affect that?

49 **MR WILSON:** You're still going to be connected to the network and  
50 to connect any generating asset, regardless how small it is --

*NZ Wind Energy Association*

1 even a PV cell on your roof -- you will still find there's a  
2 code and technical requirements.

3 **MR CURTIN:** You have a point about distributed generation here,  
4 and I think the flavour of some of the submissions was that  
5 distributed generation and transmission investment are in a  
6 sense substitutes for each other, and that kind of leads me to  
7 believe that in some circumstances presumably Transpower would  
8 be in your corner, if I could put it that way --

9 **MR WILSON:** That would be a new experience.

10 **MR CURTIN:** Okay. Maybe I've got the wrong end of the stick here  
11 because it seems to me that you're propping up power in  
12 particular spots might actually relieve them of the obligation  
13 to make investments in other spots.

14 Maybe you could just explain what's actually going on  
15 here.

16 **MR WILSON:** That's very logically true and example in point is,  
17 that's why the Government waived the distribution companies,  
18 they are now allowed to invest up to 5% in renewable energy to  
19 get this nice balance or a little bit of positive competition  
20 between further investment, but this is at the distribution  
21 level. Invariably the frustration between what's stopping it  
22 is the way Transpower sets the charges for a distribution  
23 company is, it works against intermittent generators, because  
24 you have to pay for the full amount of your peak demand.

25 In the middle of the winter the worst thing that can  
26 happen to a wind farm is you get a long windy really cold  
27 winter day; peak demand, and you pay for that peak. So what  
28 you find is, the wind farm is not able to extract the -- or  
29 get any share of the embedded benefits.

30 To contrast that with Australia where the ACCC just  
31 announced a decision that basically said you, the distributor,  
32 will pass through to us charges to renewable generators;  
33 beginning and end of debate. That is the edict.

34 Hence what you now have is five to \$10 of megawatt hour  
35 passed through by compulsion from the distributor to the  
36 embedded generator as a contribution to the avoided capital  
37 expenditure costs of further investment in transmission.

38 **CHAIR:** If the same principal applied, for example, to Contact's  
39 plant in Auckland, are they having to pay something toward the  
40 wider grid costs as against --

41 **MR WILSON:** This is Otahuhu B?

42 **CHAIR:** Yes, the design side.

43 **MR WILSON:** You'd need to address that to them, but I believe  
44 that's connected to the main network. The cost of the  
45 connection to the transmission system, no doubt, would have  
46 been the subject of extensive negotiation depending on its  
47 proximity and augmentation and...

48 **CHAIR:** But the same principle could apply -- obviously we'll --

49 **MR WILSON:** Generally, closer to load, you should have cheaper  
50 transmission costs, potentially even a contribution if you can

**NZ Wind Energy Association**

1 avoid a major transmission upgrade. The first thing that  
2 people will say about wind is, wind is an intermittent, as an  
3 example, works again it in trying to be a fully absolving a  
4 CapEx investment on transmission, so you get into a  
5 combination of energy storage which is why wind's natural  
6 alignment with small hydro systems for storage is.

7 **CHAIR:** It's more relevant, yes.

8 **MR CURTIN:** Could I just follow up. You mentioned the Rulebook  
9 as it is and the current Rules of the industry in your view  
10 don't help new technologies like wind. What would a Rulebook  
11 that did accommodate your concerns look like?

12 **MR WILSON:** Very good question. Well, it's hard to provide for  
13 every outcome, I guess.

14 After some extensive debate the Wind Association has  
15 gone with trying to get the guiding principles right; let's  
16 get the high level right and, if you can get the high level  
17 right that contemplates -- whatever arrangement's in place,  
18 it's hoped to have some longevity about it and will have some  
19 degree of revolution; so, will obviously evolve and change  
20 over time.

21 So just trying to provide for the fact that renewable  
22 distributed generation is provided for and is not precluded  
23 for at the high level in the guiding principles; hence there's  
24 been a strong drive from us and other associations to hang our  
25 hat on the Government's Policy Statement, which is very strong  
26 on this as a concept, looking potentially into  
27 intergenerational if you wish.

28 So we would be keen -- rather than saying, well, we  
29 support Part F or we don't support Part I -- I couldn't really  
30 tell you what's in those parts, we haven't really gone into  
31 that; we've just gone with, "Hey, if we can get the guiding  
32 principles right and get the high level governance structure  
33 conducive to participation, not just of wind, but of any  
34 renewable or distributed generation in the future", well then,  
35 that's the best we can hope for.

36 **MR CURTIN:** Just one final question, and that is, you mentioned  
37 in passing barriers to entry for you, some of which perhaps  
38 are just technical or engineering related to current  
39 production technologies.

40 But, did you have any other institutional or man-made ,  
41 if you like, barriers to entry in mind when you were  
42 considering them?

43 **MR WILSON:** I mean, it's in the public arena, the Association --  
44 in its website -- has barriers to entry, it lists 12. They  
45 range from -- you're quite right -- technical requirements  
46 about voltage drop and how long you have to stay on-line  
47 which, to be fair, were drawn up so many years ago for large  
48 generators. So that, for example, a large steam based type  
49 generator can hang in there if there's a big voltage drop.

**NZ Wind Energy Association**

1           Whereas, a wind turbine, is actually -- and as is a lot  
2 of the new renewable technology -- sensitive to fluctuation in  
3 the grid, it will actually shut itself off to avoid trying to  
4 do any damage. So, it tends to go off-line a lot quicker so,  
5 therefore, you have trouble about being able to hang in there  
6 with historical technical requirements.

7           So, there's one level of barriers that fall into that  
8 category; then you just have the pure negotiation barrier of  
9 trying to extract some form of embedded to bridge that  
10 financial gap that we were talking about before.

11           Now, that financial gap, in our view, is narrowing and  
12 may in fact be bridged in the foreseeable future for wind, not  
13 probably by the value of potentially carbon on a world scale,  
14 not necessarily here in New Zealand. The Government has  
15 already set a cap, as you are probably aware, at \$25 a tonne  
16 from 2008 out where, as soon as you try and give a price  
17 signal for carbon, that one cent a kilowatt hour gap for wind  
18 starts to become quite achievable, and the technology is  
19 coming down in cost.

20 **CHAIR:** Some of the early North America plants were subsidised,  
21 weren't they, and in California those initial wind farms there  
22 were subsidised, I think?

23 **MR WILSON:** You're correct. Unfortunately, that give wind a very  
24 bad name because what happened was, there was a tax write-off  
25 for 100% in one year, so a lot of these things went up which  
26 didn't have longevity about them, so they then went -- were  
27 left to rack and ruin after only two or three years. So, that  
28 has given wind a bad name.

29           In Europe, where it's been a longer term perspective, I  
30 mean these are a real asset. The nature of wind is, it's very  
31 similar to a hydro, you sink a lot capital in at the front and  
32 you have very low O & M costs on an ongoing basis.

33           That's another thing about wind in the New Zealand  
34 context; it's not susceptible to fuel price risk, i.e. Gas.  
35 So when you put a wind farm in, not only does it diversify the  
36 supply from whether it rains or doesn't rain, it also doesn't  
37 have fuel price risk over time. You have put your asset in,  
38 you have sunk your money, all you've got do is recover the  
39 cost of the your asset.

40           Your operational and maintenance costs for three or four  
41 guys to climb turbines and change oil is equivalent to a small  
42 hydro O & M costs. So your effect on the system -- and there  
43 are some studies in Australia on this -- the effect on the  
44 system is to actually have quite a smoothing effect because  
45 wind is a spot price taker generally; bids in at very low and  
46 always gets dispatched like hydro.

47 **CHAIR:** And you can't store it, can you?

48 **MR WILSON:** No, you can't store it.

**NZ Wind Energy Association**

1 **MS BATES:** You've talked about what you consider to be a serious  
2 disconnect between Government policy and the guiding  
3 principles.

4 I just want to bring you to the Rules that are actually  
5 proposed in this application and ask you if you can tell us,  
6 in broad terms, what sort of changes you would make to them to  
7 meet the concerns of your association?

8 **MR WILSON:** One example, when we first managed to bend the ear of  
9 the Chairman of the Working Group, we were looking for the  
10 words "sustainable development", we couldn't find them  
11 anywhere in the first draft of the industry. So, as a  
12 concept, just at a very high level we said, "Hang on, that as  
13 a concept is core to Government Policy. Where's that in the  
14 industry guidelines?", and couldn't find it anywhere.

15 And the point was made that, had you reflected that as a  
16 concept in practical terms into -- and that that is true, but  
17 I guess, just because you can't reflect it in practical terms  
18 doesn't mean you should sacrifice the concept; the concept is  
19 pretty fundamental.

20 **MS BATES:** No, but once you have got the concept in there it does  
21 have to have some mechanism, doesn't it?

22 **MR WILSON:** Yep. We couldn't even find the concept first time  
23 round.

24 **MS BATES:** So, have you given any thought to mechanism?

25 **MR WILSON:** No. We have, and we have made submissions to  
26 Government on mechanism, but as you would expect the mechanism  
27 is very much tied up with -- you are now jumping across EGB,  
28 climate change, the National Energy Efficiency and  
29 Conservation Strategy as to mechanism, although they all come  
30 quite inter-lined. The logical place for the mechanism is out  
31 of the National Energy Efficiency and Conservation Strategy.

32 **CHAIR:** This is the one EECA has run, is it?

33 **MR WILSON:** Correct.

34 **MS BATES:** I might have lost you a bit there, but do you think  
35 the Rules could be altered to meet your concerns or not?

36 **MR WILSON:** Yes.

37 **MS BATES:** Can I just ask you again, how would you do that?

38 **MR WILSON:** We would rewrite the concepts to be more orientated  
39 toward sustainable development on an intergenerational basis,  
40 and bring in mechanisms such as contemplated in the National  
41 Energy Efficiency and Conservation Strategy, and we would seek  
42 total compliance with the Government's Policy Statement.

43 **MS BATES:** Let me just turn to the counterfactual.

44 **MR WILSON:** The Crown EGB -- yes.

45 **MS BATES:** Yes, the Crown EGB, and I want to ask you why you  
46 think that would necessarily be any better given that you  
47 could have a Minister who didn't share your concerns or the  
48 priority which you wish them to be given?

49 **MR WILSON:** Yes. I guess the answer there is -- it's a  
50 fundamental view on whether the Minister is going to be

***NZ Wind Energy Association***

1 aligned with sustainable development in intergenerational  
 2 equity. I can't answer that. I can only assume that the  
 3 democratic system is likely to solve for some degree of  
 4 responsibility or accountability on that count. Hence, it's  
 5 more attractive to have a concept or a solution that provides  
 6 for that than as an industry, we will make the decisions.

7 **MS BATES:** I suppose, would it be true to say that you are basing  
 8 the view on Government Policy as stated here and now?

9 **MR WILSON:** Yes.

10 **MR CURTIN:** One thought occurred to me that, one of the quality  
 11 control systems, if you like, in the proposed EGB is oversight  
 12 by the Parliamentary Commissioner for the Environment.

13 **MR WILSON:** The two ticks and you're out, yeah.

14 **MR CURTIN:** Exactly, the two ticks and you're out mechanism.

15 Would you see that as addressing some or any of the  
 16 concerns you've raised today?

17 **MR WILSON:** That's ambulance at the bottom of the cliff stuff. I  
 18 shouldn't have said "two ticks", I should have said "two  
 19 crosses". That was a concession secured at Select Committee  
 20 which we also presented to try and bring the environment into  
 21 the picture. But it's really, as I understand it, two crosses  
 22 and you're the out, i.e. The industry run EGB fails to be  
 23 cognizant of the audit by the Parliamentary Commissioner,  
 24 there will be a Crown EGB, but that's after the environmental  
 25 damage has already been done, which is, if you pull back and  
 26 look at it from a public benefit point of view or an  
 27 intergenerational point of view, I say, "Whoa, that's after  
 28 it's already happened".

29 **CHAIR:** But the Parliamentary Commissioner for the Environment  
 30 has not been renowned for being backward in coming forward,  
 31 and one assumes the Select Committee at least saw that measure  
 32 as at least some solution to the sustainability issue.

33 **MR WILSON:** You need to direct that to -- I think David Cunliffe  
 34 was the Chair.

35 **CHAIR:** Yes, we will review the report obviously, but one assumes  
 36 that it was seen --

37 **MR WILSON:** I think it was a last minute addition to the Select  
 38 Committee run out of a deal between -- my understanding, I  
 39 wouldn't swear on it -- was, it was a deal run between Greens  
 40 and Labour to get Greens support.

41 **CHAIR:** I'm not sure of the background of it, but the point is,  
 42 it's there, and certainly the current and the previous  
 43 Parliamentary Commissioner for the Environment will stand up  
 44 and be counted if they think they need to be.

45 **MR WILSON:** Well, if that's the case; example: There are three  
 46 gas combined cycles going through environmental permitting in  
 47 various stages in New Zealand at the moment, they will totally  
 48 change the amount of greenhouse gases omitted in New Zealand  
 49 in the foreseeable future; change the percentage of the

**NZ Wind Energy Association**

1 electricity sector significantly, change it from being 62%  
2 hydro or renewable to less than 50.

3 There is not one submission as those plants went through  
4 permitting from any Government agency on greenhouse gas  
5 omissions.

6 **CHAIR:** Again, it's more anecdotal, but I understood that the  
7 Contact combined cycle plant, they had to produce some --  
8 either plant, forest or whatever to mitigate some of the  
9 greenhouse effects there, or back-off New Plymouth or  
10 something like that?

11 **MR WILSON:** Otahuhu B which was called in by Simon Upton was the  
12 subject of particular economists to do that.

13 Otahuhu C, which is the one they were putting through  
14 permitting, was under appeal by the Environmental Defence  
15 Society and the New Zealand Wind Energy Association went to  
16 the Environment Court for some means to avoid, mitigate or  
17 remedy the greenhouse gas emissions.

18 **CHAIR:** And what happened?

19 **MR WILSON:** That project has been suspended, as I understand it.

20 **MS REBSTOCK:** I just want to ask you: You talked about barriers  
21 to entry with respect to the structure of the EGB, the Rules,  
22 but you also remarked on the voting structure itself. I  
23 wondered if you could tell us in what sense you see the voting  
24 structure as a barrier to entry?

25 You may have been here for the presentation from Contact  
26 who suggested that sufficient players had voting rights to  
27 ensure people with an interest were represented. You seemed  
28 to not accept that, at least from your perspective.

29 **MR WILSON:** Yeah, I mean our perspective is, we're outside the  
30 tent looking in and we're looking at an existing club, to use  
31 a colloquialism again, and it's probably fine for the existing  
32 club but any potential new member of the club has probably got  
33 a different perspective on whether the voting rights are a)  
34 going to be practical to get consensus decision-making. There  
35 seems to be a lot of positioning for a vested interest; if you  
36 are in the distribution sector you have one view on life; if  
37 you are in the transmission sector you have another view on  
38 life; if you are a generator/retailer, well then, you will  
39 have a different view on life. I guess, if you are a potential  
40 new small generator you have even another.

41 We're struggling with the view that the industry will be  
42 able to self-govern, given a lot of the entrenched self-  
43 interest positions and, as you might expect, that has been  
44 expensively debated and there's not consensus on that, but I  
45 think there is some concern that the industry will be able to  
46 bury the hatchet, if you like, and make -- because there are  
47 certain powers of vetoes hidden away in the voting rights  
48 which could lead to some non-decisions which could lead to  
49 some undesirable outcomes.



**NZ Wind Energy Association**

1 **MS REBSTOCK:** Tell me a little bit about these hidden veto  
2 rights.

3 **MR WILSON:** Obviously the generators and the retailers are  
4 joined; they will have significant voting power, those with  
5 the large customer bases and those with large generation base,  
6 and they will outweigh the smaller generators/retailers.

7 Then you will have Transpower sitting there with its  
8 veto rights through certain parts of the code and, as an  
9 outsider looking in, they seem to have trouble agreeing with a  
10 lot of things.

11 **MS REBSTOCK:** If I listen to some of your concerns, I wonder if  
12 you have given thought to conditions because -- and I don't  
13 want to oversimplify what you are saying -- but it does seem,  
14 to me, that a condition that aligned the guiding principles  
15 with the Government Policy Statement, married with a condition  
16 that gives the independent EGB board executive powers, would  
17 address your concerns; is that...?

18 **MR WILSON:** That's a very fair statement but in floating that,  
19 it's not that we hadn't made any progress.

20 **MS REBSTOCK:** So you have floated those ideas?

21 **MR WILSON:** They were the subject of some ear bending, yes.

22 **MS REBSTOCK:** I don't want to put words in your mouth, but does  
23 it meet your concerns then, those two conditions?

24 **MR WILSON:** If I can be so bold, any outcome is a series of  
25 compromises. We may not get all of our concerns met -- but I  
26 come back to our earlier comment; if we can get the higher  
27 level governance and principals in place to allow new  
28 technology and sustainable development to be provided for in  
29 the future, in all honesty -- personal opinion -- we should be  
30 happy.

31 **MS REBSTOCK:** And you think that would achieve that?

32 **MR WILSON:** Will it achieve it or allow the platform for -- as  
33 things evolve, for it to be provided for? It's potentially a  
34 realistic outcome.

35 **MS REBSTOCK:** Thank you.

36 **CHAIR:** All right. Well, thanks very much, Mr Wilson. Thanks  
37 indeed.

38 The next presenter is Sustainable Energy Forum; Molly  
39 Melhuish, please.  
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*Sustainable Energy Forum***PRESENTATION BY SUSTAINABLE ENERGY FORUM**

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**MS MELHUIISH:** Just introducing myself: I am on the Executive of the Sustainable Energy Forum which is a collection of about 120 members whose interest is to promote debate regarding sustainable energy. It takes a long -- it's executive is recently confirmed that it has an increasing concern that economic necessity resource depletion, climate change and pollution is moving New Zealand ever more efficiently towards an unsustainable energy future. So, we are at the moment fairly pessimistic.

Yesterday I put in a second submission which is based on what I have heard in the three days to date. This urges the Commission, and all of us, to reflect more carefully on the real world in which electricity decisions are made.

Essentially what happens to electricity depends on whether you flick the switch or not. That is, it's the end consumers who are making the decisions to which the whole supply industry must accommodate.

Therefore, pricing efficiency, allocative efficiency, is meaningful only by comparing the marginal price to that consumer who flicks the switch, with the marginal cost of supplying that user. In that sense I believe the retail market and the prices and the costs going as far as the end consumer are the only basis on which your benefit/detriment can rationally be based.

For new investments, it is the real world in which people make investments that you must consider, and investments in hot water cylinders and insulating building envelopes and steam pipes save electricity just as new power stations generate it.

My overwhelming impression during these three fascinating days is of having a group of people inhabiting a world of their own, almost like a club. Their world is complex, has great professional challenges and each of the people you heard from has met those challenges successfully.

They seem, to me, to be urging Commissioners to understand their world better so that they can accept the compelling logic of the application.

So, the Rulebook has an inherent coherence which I think has helped it insulate -- be insulated from the real world that this little ecosystem of theirs inhabits. Indeed, links to the real world are openly rejected by the applicant's benefit/detriment assessment.

Now, I give two cases of that; let's see if I can find them. The first is contained in the economic assessment dated 5th of December by LECG. It addresses the constraints which would happen with a Crown EGB. They see the Government as wishing to promote non-economic objectives at the expense of long-term efficiency gains.

**Sustainable Energy Forum**

1           Now, I believe that the economic objectives, the broader  
2 economic objectives, are within what must be put in an  
3 assessment of benefits and detriments and not outside it.

4 **MS BATES:** Could you just repeat that last sentence, please?

5 **MS MELHUISH:** I'll try. The Crown EGB is criticised in the  
6 5th December paper as wishing to promote non-economic  
7 objectives at the expense of long-term efficiency gains and  
8 they feel that this would be economically inefficient. I say  
9 that the so-called non-economic objectives are actually within  
10 economics and need to be incorporated within the Commission's  
11 assessment of benefit and detriment.

12           The second is this fascinating thing about the guiding  
13 principles themselves. In the applicant's original  
14 authorisation application, Section 12 guiding principle, they  
15 say the Rulebook contains 10 guiding principles -- this is  
16 12A. They are intended to provide a guide for Rule changes  
17 and to be a touchstone for the evolution of Rules. They are  
18 not meant to -- they are meant to guide the Rules but not be  
19 essentially consistent with them.

20           So the guiding principles, they see as a translation of  
21 the Government Policy Statement into things which can have  
22 legal meaning in the contractual environment.

23           Interestingly, the guiding principles as chosen by the  
24 applicant do not mention managing risks. All the guiding  
25 principles that I remember during my involvement with this  
26 process since about 1991 always said risks should be placed  
27 with the party's best set up to manage those risks. I'd  
28 always felt, that's great, because here's the big generator --  
29 at that stage it was just ECNZ, and in the early stages it was  
30 ECNZ/Transpower -- they above all are able to manage risk  
31 because they have a great deal of diversity. Let's let them  
32 manage some of the risks that otherwise consumers would have  
33 to manage.

34           Now, I looked carefully through the guiding principles  
35 and it does not mention "risk" whereas the latest Government  
36 Policy Statement still says "risks relating to the security of  
37 supply, in particular the risks of dry years and inadequate  
38 transmission and distribution security, are properly and  
39 efficiently managed". There is no reflection of that that I  
40 can find in the guiding principles themselves.

41           An interesting thing about the applicant's presentation  
42 on the first day, I noted that the presentation of the  
43 applicant didn't mention the retail market. Now, I argued for  
44 SEF's submission that the retail market is critical, and yet  
45 that wasn't even addressed in the response to submissions by  
46 the applicant; which, it was quite happy to quote other bits  
47 of SEF's submission when it suited them.

48           My second submission which you received late yesterday;  
49 first thing, it is not a draft, I'm sorry it was not out for

*Sustainable Energy Forum*

1 consultation as was the other one, so please delete "draft"  
2 from this, and it's been substantially modified accordingly.

3 **CHAIR:** Has it been given to the other parties to this hearing as  
4 well?

5 **MS MELHUISH:** Yes, it's been given to the Consumer Institute, and  
6 I tried to get it to MEUG, but I got a virus yesterday.

7 **CHAIR:** We'll probably circulate it to them all, if that's okay.

8 **MS MELHUISH:** It's already been circulated. It was in time to  
9 make it before 5 o'clock, and it's been fully circulated.

10 **CHAIR:** All right. Thank you.

11 **MS MELHUISH:** But, during the consultation phase I actually  
12 consulted with people on our side.

13 This second submission invites the Commission to take a  
14 macro view of benefits and detriments. It focuses entirely on  
15 benefits and detriments rather than being an outline of what  
16 our preferred electricity market might be like or anything  
17 like that. It compares what I believe is likely to happen  
18 under the applicant's proposal, which I call AP, and under the  
19 counterfactual.

20 So far as all the quantification done in all the  
21 economic analyses and in the separate submissions, say, by  
22 Transpower and the others, and MEUG, in fact, all that  
23 quantification is taken from within the system, the little  
24 ecosystem which is all about the Rules, but the Rules only  
25 cover the wholesale market; there is no retail link.

26 The quantification so far is very detailed, it's  
27 disaggregated by three types of efficiency and by a dozen  
28 different -- or in the order of a dozen different issues, and  
29 there's numbers attached to all sorts of these things.

30 We prefer a simpler way of looking at the benefits and  
31 detriments of the application. So, most of my second  
32 submission is describing why I believe the applicant, if  
33 accepted, would move in one direction and most particularly  
34 the counterfactual would move rather more rapidly in a  
35 different direction.

36 Now, you will have read my second submission, was that  
37 possible? That's good, so I won't really go through it at  
38 all.

39 **MS REBSTOCK:** Sorry to interrupt you, but in your second  
40 submission you develop a very detailed scenario for the  
41 counterfactual, and it seems to me -- well, generally we don't  
42 do that.

43 **MS MELHUISH:** Indeed.

44 **MS REBSTOCK:** Because it is very hard to look out 11 years and  
45 try to make assumptions about what might happen in a  
46 counterfactual, but you seem to be suggesting that is in fact  
47 what we should do.

48 **MS MELHUISH:** No. I myself have put a scenario which, of course,  
49 is only that; it's one of a million different futures, but the  
50 thing which needs to -- it's the text on the first two pages

*Sustainable Energy Forum*

1 which is defining, but if you want to put numbers on there is  
 2 going to be implicitly something not very different from what  
 3 I did.

4 Any time you say there are \$12 million worse in MPV if  
 5 the Crown makes certain uneconomic decisions; they're things  
 6 behind the numbers which are not very different from the  
 7 details of years up to year 11. So the intention of that was  
 8 to make transparent if somebody -- and I would like somebody  
 9 actually to be paid to put a true quantification, because I  
 10 think that would help the Commission focus its mind on the  
 11 real differences. To do that I chose to be transparent, but  
 12 I'm not asking you to believe that scenario or any other  
 13 scenario whatsoever.

14 **MS REBSTOCK:** I guess my question is, really, given how many  
 15 variations on this scenario there may be.

16 **MS MELHUIHSH:** Oh, millions.

17 **MS REBSTOCK:** And the further you go out in time, the more  
 18 significant it is; it becomes very difficult then to -- almost  
 19 impossible for the Commission to do that type of analysis.

20 **MS MELHUIHSH:** I didn't intend you to believe that, I intended you  
 21 to focus on what I said on the first page, which was, if you  
 22 want to say even which direction the Rulebook would evolve  
 23 under either of the proposal in the CF, you need to  
 24 characterise it at present.

25 Now, you will see that I characterise it substantially  
 26 differently from what, for example, Professor Hogan  
 27 characterised it. He said it was quite close to industry best  
 28 practice. I have said that it deviates from that through  
 29 having no ex anti market, and according to Contact Energy this  
 30 morning, as I heard them, if I heard them right, no intention  
 31 of getting there if Transpower has anything to say.

32 Now, that is very characteristic of the -- one end of  
 33 the polar extreme that I described in all my submissions, the  
 34 end that says, "Here's a physical system. Here are the costs  
 35 of the system. You pay for them." which is not actually a  
 36 market, it's essentially administrative pricing.

37 **MS REBSTOCK:** Can I just pursue that a little bit. Is this issue  
 38 about the demand side basically not coming into play something  
 39 to do with the Rules as they have developed in the wholesale  
 40 market as they have developed in New Zealand, or is it simply  
 41 a reflection of the nature of this market?

42 In other words, we probably have fairly --

43 **MS MELHUIHSH:** You mean, of any market?

44 **MS REBSTOCK:** No, the market of electricity. If we have  
 45 inelastic demand, many, many consumers, is it surprising that  
 46 the supply side in fact dominates the market?

47 **MS MELHUIHSH:** No, it is a reflection of New Zealand's particular  
 48 market and is not a general case about electricity markets or  
 49 about inelasticity of consumer demand.

*Sustainable Energy Forum*

1           Consumer demand could become far more elastic if  
2 consumers were able to manage their risks with help from both  
3 technology and from cost responsive pricing systems when they  
4 wish to choose it. They will not choose that unless they can  
5 manage their risks unless the final price is lower.

6 **MS REBSTOCK:** Is there a strong case --

7 **MS MELHUISH:** It is this market.

8 **MS REBSTOCK:** -- is there a strong case that the cost of doing  
9 that would be warranted?

10 **MS MELHUISH:** No.

11 **MS REBSTOCK:** Given the cost of electricity?

12 **MS MELHUISH:** There is a very strong case that that consumer side  
13 management is warranted and my best example of that is the  
14 vision statement that I appended at the end of the new  
15 submission, which is the vision of the very -- FERC, the  
16 Federal -- what is it? Federal Energy Regulatory Commission  
17 in the US, which believes that as soon as five or 10 years  
18 from now it is possible to believe that a market may come in  
19 which prices actually do reflect cost right at the retail end  
20 in which --

21 **MS REBSTOCK:** The fact that they say "in five to 10 years"  
22 suggests that conditions aren't met now.

23 **MS MELHUISH:** Oh, that's true, and Professor Hogan said the same.  
24 He said that FERC has suddenly realised that it matters to  
25 have a vision and to move towards it. I believe he  
26 misdescribed the vision because I believe FERC -- part of the  
27 implementing thing which lies in the same document, but after  
28 what I printed, includes an ex anti market for both  
29 transmission and energy.

30           Now, when you asked, is the reason consumers can't  
31 participate to do with market rules or fundamental elasticity  
32 of demand my answer was clear; it is to do with market rules.  
33 One of the biggest issues is a lack of ex anti market.

34           Consumers cannot adjust their demand unless they see,  
35 before they flick the switch, what it might cost them. And ex  
36 anti markets have been developed and many, possibly the  
37 majority, of implementations worldwide, of new electricity  
38 markets.

39 **MS REBSTOCK:** Do they tend to be in markets that have much higher  
40 overall costs of providing electricity?

41 **MS MELHUISH:** No. Let's look at Australia. Their ex anti  
42 markets in both New South Wales and Victoria, they have very  
43 low costs.

44 **MS REBSTOCK:** And the evidence here supports that being  
45 economical in the New Zealand environment, to do that now?

46 **MS MELHUISH:** Yes.

47 **MS BATES:** Could you just tell me, do you know in Australia, with  
48 the introduction of the ex anti market, what evidence there  
49 was of consumer response to that?

*Sustainable Energy Forum*

1 **MS MELHUIISH:** The consumer response hasn't happened yet. It is  
2 still essentially a supply market, and I can't remember  
3 whether the ex anti is voluntary or compulsory, and different  
4 implementations around the world, some are voluntary, some are  
5 compulsory. But how New Zealand's ex anti market differed was  
6 that it was a commitment market, whereas some of them just  
7 say, "Here is what I think I will do", and I believe there are  
8 some ex anti commitment markets; but I didn't print off the  
9 reference that I found on that.

10 New Zealand's ex anti commitment market was not  
11 supported as Transpower -- sorry, as the applicant correctly  
12 noted in commenting on our submission. But, it wasn't  
13 supported because it's a very big ask for a commitment market  
14 to happen in an environment when there is absolutely no  
15 ability to manage transmission congestion. One cannot expect  
16 a commitment market until you can manage your risks.

17 One of -- probably the biggest debate, almost certainly  
18 the biggest debate in the different restructuring of  
19 restructurings, has been how to manage transmission risks and  
20 transmission congestion.

21 So, those are the market details which need to be fully  
22 implemented as a first but not an only pre-requisite to active  
23 consumer demand management.

24 My scenario, for all its appalling detail, does contain  
25 my belief of the other primary need, which is to inform  
26 consumers and empower them with financial mechanisms -- loans,  
27 not subsidies -- and to do the kind of advertisement,  
28 community consultation, discussion which is needed for the  
29 cultural revolution which I believe will happen -- will be  
30 needed before active demand side participation moves beyond  
31 the major electricity users.

32 This will be a culture shock. I didn't even see it as  
33 beginning except at a pilot stage until at least year five,  
34 and still only pilot. I wouldn't see really strong demand  
35 side participation until year eight or nine, and the scenario  
36 you see was a vehicle for you to read how I'm thinking, not  
37 for you to use as a cost/benefit calculation.

38 **MR CURTIN:** Just to get myself clear here. I think in your  
39 original submission at paragraph 25 you considered it unlikely  
40 that a Crown EGB would be the result.

41 **MS MELHUIISH:** Yes, correct.

42 **MR CURTIN:** And then in this latest submission, if I'm reading  
43 you correctly, you're saying "yes", and what's more, you could  
44 imagine it evolving in a sort of competitive pro-consumer  
45 demand side management kind of way. So...

46 **MS MELHUIISH:** That was partly trying to follow what I believe are  
47 your Rules, because I'm trying to get you to have a different  
48 way of thinking about the benefit/detriment. You are required  
49 to consider a Crown counterfactual and that is not -- and I  
50 have said at the beginning, this few pages is not what SEF

*Sustainable Energy Forum*

1 prefers but it is addressed to the particular challenge you  
2 have about doing a cost/benefit.

3 **MR CURTIN:** Okay, so essentially you are saying that you are  
4 inviting us really to think about a Crown EGB as a  
5 counterfactual, but --

6 **MS MELHUISE:** Well, you have said you must. I believe you have  
7 said you must.

8 **CHAIR:** We have said "it's likely".

9 **MS MELHUISE:** You must take the most likely?

10 **CHAIR:** We attempt to take, based on what's been argued and our  
11 own judgment, what was likely; fair point.

12 **MR CURTIN:** If everybody came here and said, "No, no, you've got  
13 it wrong, the most likely thing is this, that or the other"  
14 then we'd have to think about that; but that's where we are at  
15 the moment.

16 **MS MELHUISE:** Now, but it's also true that I wrote this before I  
17 heard the pages of discussion and before I'd read too many of  
18 the second lot of the submissions, and it does seem to me more  
19 likely than I would have judged earlier, when I wrote number  
20 one, that a Crown counterfactual might actually happen.

21 That's partly -- again from Professor Hogan's  
22 comments -- that any Crown counterfactual may well involve,  
23 what I thought was essential, was an independent regulatory  
24 oversight. It did seem that there is quite a bit of support  
25 for independent regulatory oversight, which I believe would be  
26 very difficult with the application, but would be feasible and  
27 likely with the other.

28 Again, one of the main points of that oversight is to  
29 focus the debate on the coherence of the model. Do we really  
30 want the pure model at one end of the axis which is supported  
31 by Hogan and the Harvard project, or do we want an incremental  
32 move towards more liquid markets, more contestability of  
33 supply, contestability of supply by both demand and by  
34 distributed generation?

35 I believe we want it, I believe FERC wants it, and has -  
36 - that's why I appended the vision statement. I believe that  
37 that will lead to lower overall costs to the economy as a  
38 whole.

39 As I say, I'm urging you to get away from the very  
40 detailed benefit/cost benefit/detriment assessment which is  
41 done entirely within the ecosystem; it's a tiny ecosystem. I  
42 want you to think of benefits and detriments in the real world  
43 in which consumers flick the switch, and it's the costs to  
44 them that determine allocative efficiency.

45 **MS BATES:** They have got to flick the switch to something else?

46 **MS MELHUISE:** No, no, they could just turn it off.

47 **MS BATES:** Say you are a business, if you wanted to, you can't  
48 just opt out often, okay, you've got to do it?

49 **MS MELHUISE:** But the business may well have an uninterruptible  
50 power supply, a UPS, and they need to invest in that if they



*Sustainable Energy Forum*

1 judge that the reliability of their CBD is at risk, their  
2 Central Business District is at risk.

3 **MS BATES:** So you would favour a move towards consumers taking on  
4 their own risk?

5 **MS MELHUIISH:** Yes. But in order to invest in such things they  
6 need to benefit from the lower overall costs from the  
7 wholesale electricity market and transmission market.

8 They can't afford to invest in their often reasonably  
9 costly things if people are building another DC link and, you  
10 know, everything else to make damn sure the lights stay on.  
11 And, of course, the lights won't stay on; you always have --  
12 in many cases people are safer and meeting their minimum  
13 supply through their own security devices.

14 But, having said that, there are a number -- and again  
15 the scenarios were a vehicle for me to highlight to you some  
16 of the technologies. Now, one technology is smart controls of  
17 appliances; everything from hot water to fridges to any  
18 substantial energy using. The appliance itself sees the  
19 problem and turns itself off; totally distributed.

20 Now, if a lot of people on a poorer quality transmission  
21 area had -- and here I'm thinking of that magic year 2013 --  
22 if you have a community which is threatened to be cut off when  
23 the Electricity Act allows the lines company to cut them off,  
24 if they put a bunch of smart switches on their appliances and  
25 have just a little bit of hydro, maybe supplemented by  
26 photovoltaic would be characteristic in these areas of  
27 generation, then transmission line goes down, they don't get  
28 stuck; they actually have the power on to keep the essential  
29 services on.

30 **CHAIR:** It's the same point that was made by Mr Wilson, I think,  
31 from the Wind Association, and again whether the Rules will  
32 evolve to be able to take account of those changes in  
33 situations I think is obviously a moot point.

34 **MS MELHUIISH:** To me that is the defining difference between the  
35 AP and the counterfactual. Which way the Rules evolve I see  
36 as a simple -- and I'm taking as my model that polarisation  
37 picture, which is not widely discussed, because I believe the  
38 people within this ecosystem really see their world; they  
39 don't see a different world, and the power of an ex anti  
40 market of friendly rather than unfriendly transmission  
41 pricing, because transmission is -- and of good risk  
42 management, the power of that to change the world is enormous  
43 and again that's why I wrote a scenario which you will find is  
44 not very different and implementation of FERC's vision  
45 statement. It's one of a million implementations.

46 **MS REBSTOCK:** We've heard from a number of players that the  
47 proposal allows significant input from consumers so that they  
48 can affect the direction that the Rules take, and I wondered  
49 if you could give us your perspective on that.

*Sustainable Energy Forum*

1 **MS MELHUIH:** I see the input from consumers in working parties  
 2 as being relatively ineffective. I would say consumers need  
 3 to have a very full, if not very deep, understanding of the  
 4 way electricity markets work, and of where the technical  
 5 effects about electricity dominate what actually happens and  
 6 make that supply/demand intersection go differently from --  
 7 often different to what's intuitively obvious.

8 Now, I did a course at New South Wales, a three day  
 9 course, called the "short course on electricity markets" in  
 10 which the grimy details of this were gone through, not as a --  
 11 not to be able to run a system but to be able to understand  
 12 quite fully the constraints that happen.

13 Until you have gone through that or an equivalent  
 14 course, you are unlikely to be able to participate actively in  
 15 debates about market rules, and I don't believe the other  
 16 consumer representatives have. It may be the major  
 17 electricity users have; it may not be. I don't know.

18 **MS REBSTOCK:** Isn't that very much the same issue under a Crown  
 19 EGB? Consumers still have to pass that threshold in order  
 20 to --

21 **MS MELHUIH:** Yes.

22 **MS REBSTOCK:** So in terms of the difference between the proposal  
 23 and the counterfactual, with respect to the consumer input,  
 24 why is there a difference?

25 I mean, under the counterfactual and under the proposal  
 26 the Crown itself tries to represent the public's interest  
 27 through the Government Policy Statement and through ex-post-  
 28 monitoring, so what is the difference between the two?

29 **MS MELHUIH:** Well, I believed that -- I have said, now this goes  
 30 more to what I prefer than to what I believe is likely, but I  
 31 think I could afford to say that I believe it is more likely  
 32 that consumers would be offered sufficient funding and to get  
 33 expertise of their choice and sufficient opportunity to find  
 34 representatives who are prepared to get up to speed and be  
 35 able to argue the details of the Rules. I believe that's more  
 36 likely than what happened in the applicant's proposal simply  
 37 because the applicant has vested interests in not having this  
 38 happen, and the Crown has a Government Policy Statement which  
 39 contains a lot of fine words and no way, so far, to implement  
 40 them.

41 I think the Crown would recognise reasonably soon that  
 42 there is a need to implement, to empower consumers through  
 43 information, through expert advice and in the fullness of time  
 44 through financial loan type mechanisms, to actually  
 45 participate in the demand market.

46 **MS REBSTOCK:** We've heard from a number of parties that in their  
 47 view there is a coincidence of interest, the long-term  
 48 business interests, with the interests of consumers in the  
 49 long run, and you seem to be implicitly rejecting that notion  
 50 and I would welcome your direct comments on that, and

*Sustainable Energy Forum*

1 specifically any examples that you can give us where you think  
2 there's evidence that that coincidence of interest holds.

3 **MS MELHUISH:** Well, I'll choose as an example my long-term  
4 monitoring of this idea that risks are to be managed where  
5 they are best managed and that the Rules must encourage that.

6 Now, as I said, I welcomed that at the outset because I  
7 believed that ECNZ had always said, "Here's the costs of  
8 generating electricity; you pay it." and I'd felt that if  
9 there was enough insulation of hot water cylinders, all these  
10 things, electricity demand would drop and the expensive new  
11 power stations wouldn't be necessary.

12 Now, I'm suddenly going from risks to costs -- and I  
13 have to try to think on my feet because I've answered a  
14 slightly different question. Let me pursue the costs.

15 My picture was, at one of many seminars that I attended,  
16 at which ECNZ was talking about their new vesting contracts  
17 which are -- that is, when Contact was separated, I believe it  
18 was then that vesting contracts were set up to balance the  
19 risk of generators so that they see things more from the  
20 consumer's point of view -- do you see how that relates? Do  
21 you see the connection between vesting contracts?

22 With vesting contracts the Crown owned generators were  
23 required to sell their generation ahead, maybe 85% of it at  
24 the start, then it rolled back to maybe 60 or maybe 30 or 40%  
25 in the third year, and that meant that the generators  
26 themselves had a risk profile much more like the consumers.

27 As those vesting contracts died away the purchasers of  
28 electricity suddenly faced much more risks than if they went  
29 out on the market and said, "I want some more hedging  
30 contracts", and the generator says, "Okay, what are you  
31 prepared to pay for them?" in the end NGC didn't buy the  
32 forward contracts that they needed.

33 Now, I felt that the big generators have -- as soon as  
34 the Crown's Rule ran out, that you must accept a more consumer  
35 like, a purchaser like risk profile, they said, "No, this  
36 doesn't suit us."

37 So there's an example -- is that in partial answer to  
38 your question?

39 **MS REBSTOCK:** Thanks, yep.

40 Have I taken you right away from your presentation?  
41 Take the opportunity to go back to it if you like.

42 **MS MELHUISH:** Let's see what happens if I just -- of course, I  
43 will have covered quite a lot of it.

44 I have noted under "4" I was convinced -- and I think  
45 this is -- the bit on page 2, the application of my  
46 perspective of two directions of evolution of market design.  
47 The application of that to the AP and the CF is in the middle  
48 of page 2, that I see that the AP would further suppress  
49 smaller market players and retail participants. In  
50 suppressing that, several of the references that I read

*Sustainable Energy Forum*

1 recently emphasise that if you have effective demand side  
2 participation, when you have spot prices which have been  
3 pushed up by gaming behaviour the demand side can come up and  
4 make a killing.

5 So, I believe it's the FERC -- one of the two or three  
6 FERC documents that I have read recently says specifically  
7 that demand side participation is the way that they mentioned,  
8 the particular way to mitigate market power. So, in the AP I  
9 see market power and, therefore, higher prices to consumers,  
10 and I believe that that ought to be your conclusion in setting  
11 up my macro view of a benefit/detriment analysis.

12 **MS REBSTOCK:** We can only get there, can't we, if we can make the  
13 assumption that the counterfactual will see the development of  
14 the demand side at a --

15 **MS MELHUIISH:** Yes, or moving in that direction.

16 **MS REBSTOCK:** -- at a faster pace than the proposal?

17 **MS MELHUIISH:** Yes, and in support of saying this is likely to  
18 happen I note the difference between what the applicant has  
19 chosen to include within its guiding principles and what  
20 I believe a Crown EGB will be asked to do; which is get that  
21 consumer Rulebook written. As soon as they get that written  
22 they will be forced to consider the retail side, which the  
23 applicant doesn't have within its ecosystem.

24 **MS BATES:** The Minister does have the power to require an  
25 industry EGB to do that very thing.

26 **MS MELHUIISH:** To do so, yes. But it hasn't so far. He has said,  
27 "I would like to see a consumer book, but he hasn't said that  
28 that book will literally write the retail market into it.

29 You see, an obstacle to getting the retail market in --  
30 I mean, the retailer/generators are considered to be  
31 absolutely competitive. You know, they say consumer choice  
32 will solve everything and, therefore, we don't have to  
33 regulate retail at all.

34 I believe that with a Crown -- and they don't want to  
35 regulate retail -- I believe with a Crown EGB or with the  
36 status quo -- remember my first submission said that I  
37 expected most likely that we would stick with the status quo  
38 for a period and consumers would get in there and really work  
39 with industry to get a better status quo -- the essential  
40 factor is how, if our objective is meaningful, that is  
41 marginal price equal marginal costs, and as I say that's only  
42 meaningful if those prices apply to people who flick the  
43 switch -- that scenario, the question is whether it's more  
44 likely under a Crown EGB or an industry EGB, and whether it is  
45 actually a Crown EGB or what I said in my first scenario, I  
46 think it is more likely if the applicant gets its proposal  
47 that it will retreat to inside its ecosystem and continue to  
48 wish away the retail world.

49 They have to have a pretty strong push if they want to  
50 open themselves up to the retail world and for a very good

*Sustainable Energy Forum*

1 reason, because Professor Hogan said the industry is doing  
2 that, not just because they are lazy, but because it suits  
3 their shareholders better. So, these industry people each  
4 have their own commercial objectives, and no commercial person  
5 wants to openly face an uncertain world in which the demand  
6 side is empowered to contest their business.

7 **CHAIR:** That was Professor Hogan's view, wasn't it?

8 **MS MELHUISH:** I believe so. I share that. I actually share most  
9 of his ideas on governance, while disagreeing with most of his  
10 ideas on detailed market design. That's possible.

11 So, I did want to emphasise that the FERC standard  
12 design is not Professor Hogan's design but is one which has ex  
13 anti and transmission markets. That fact comes not from the  
14 vision that I appended but from the implementation which  
15 appears later on in the same paper; so you may wish to go  
16 through that.

17 So, in talking about the quantified benefit/detriment  
18 analysis I think you must recognise that, with market rules  
19 that fully incorporate the Government Policy Statement which,  
20 remember, the applicant said they couldn't really do and stay  
21 within the contractual situation -- as soon as they fully  
22 incorporate the much broader principles which recognise  
23 sustainability and need for disclosure of hydro spill and  
24 particularly the active demand side market, as soon as they do  
25 that you have a contesting of high supply prices and a chance  
26 for consumers to capture some of the high spot prices for  
27 their own purposes. That, we claim, is more economically  
28 efficient by all, but particularly by allocative, that is  
29 pricing efficiency, but also investment efficiency. It is  
30 essentially in my macro models much more efficient to buy  
31 insulation for hot water cylinders than to buy a new combined  
32 cycle gas turbine to generate the same electricity.

33 That brings us to another point which I have barely  
34 mentioned in my second submission but which really needs to be  
35 emphasised; that any benefit/detriment, if it is to look at  
36 the world outside the narrow rules world, must recognise that  
37 unless a new large gas field is found there will be a real  
38 squeeze on gas prices.

39 Now, it isn't your job to decide whether it's more or  
40 less likely that a new gas find arrives, but I think you must  
41 prepare for the possibility that it might not be and Shell may  
42 not get their way of having a tripling of gas wholesale  
43 prices; but I think you must give recognition to the fact that  
44 there's a good deal of market power in the gas industry, both  
45 in transmission and increasingly now in supply, with Shell now  
46 owning what Fletchers used to own, and that high gas prices  
47 are perhaps more likely than has been thought of in the recent  
48 past.

*Sustainable Energy Forum*

1           Now, this will immediately lower the hurdle for wind  
2 energy to jump, and may make wind energy more economic in the  
3 beginning.

4           I think that remark doesn't apply directly to the nature  
5 of changes in market rules, but I think it may well be --  
6 certainly in my macro view of benefit/detriment -- it may very  
7 well make quite a difference, quite an impact on the  
8 quantitative benefit/detriment that you might assign to the  
9 factual versus counterfactual.

10 **MS REBSTOCK:** I wonder about that, because if it's more  
11 economical to increase wind generated power and some of the  
12 large generators now invest in that, I'm wondering what it is  
13 that would make the result different under the counterfactual  
14 than under the proposal, because they seem to have the numbers  
15 to get Rule changes through that would allow that economical  
16 source of energy to come to fore under the industry proposal,  
17 and you seem to be suggesting that it would happen under the  
18 counterfactual?

19 **MS MELHUIISH:** More likely under the counterfactual.

20 **MS REBSTOCK:** I'm trying to understand why it would be more  
21 likely?

22 **MS MELHUIISH:** Well, I made a few notes when you were quizzing the  
23 Wind Association on that. The market rules as they stand  
24 are -- now, transmission pricing is something which is way  
25 beyond my limited understanding of how wholesale markets work.  
26 But I believe network pricing, particularly by the  
27 transmission companies, sometimes also by the distributor,  
28 there is a very wide scope of ways for transmission pricing to  
29 work. After all, they've got about 20 different things,  
30 they've got connection charges and you name it; many, many  
31 different components of pricing.

32           Transmission pricing as it is does not reward the many  
33 network benefits that even an intermittent generator may  
34 provide. So, there's a broad statement of one thing that's  
35 wrong with transmission pricing.

36           Another thing is, in its security hat, the system  
37 operator puts very strong requirements on generating  
38 companies -- yes, on small generators. Some of these  
39 requirements may be stronger than is necessary.

40           There's a good deal of debate overseas as to whether a  
41 transmission -- sorry, as to whether a small scale generator  
42 which is intermittent must -- what was it, I was reading this  
43 just yesterday --

44 **CHAIR:** I think the point that the Wind Energy Association made,  
45 I think, is the same one you are making; that the Rules in  
46 relation to access to the grid, at the moment can be seen as a  
47 block to intermittent generators. That's the point?

48 **MS MELHUIISH:** That's true, that's only part of it. Part of it is  
49 the prices that they are paid, and if the prices reflect, and  
50 if they are required to cover all of their security by some

*Sustainable Energy Forum*

1 kind of hedging contract saying, "Oh, maybe we may not be on  
2 at some peak time", then that doesn't necessarily happen, and  
3 in other places around the world it's quite different.

4 But if the core principle, which it is in New Zealand's  
5 very specific type of market, the core principle in  
6 New Zealand's market is here are all the prices in the  
7 electricity system as is, the incumbent system, here are all  
8 the costs that they face; you either -- consumers or new  
9 generators, have to meet every one of those costs. That's at  
10 one end of the pole.

11 Other implementations of markets say, here are a  
12 spectrum of existing and new generators, here is how their  
13 costs and risks can and should be met. You see how I'm  
14 talking about a coherent model which might be different?

15 **CHAIR:** Yeah, I think we'll probably also raise some of those  
16 points with Transpower if they don't raise them because  
17 Mr Wilson was basically saying the same thing, I think, and  
18 obviously it's a question that we'll be interested in hearing  
19 from Transpower on.

20 **MS MELHUIH:** One of the ways around this is so-called net  
21 metering and net metering is often discussed in terms of solar  
22 houses; a single house with a photovoltaic panel. If it were  
23 allowed to connect the panel directly up to the grid, then  
24 every time the sun was on and their appliances weren't the  
25 meter would run backwards; that's called net metering. Net  
26 metering is allowed in many countries, and sometimes people  
27 say, "Oh, this will cause terrible problems with security of  
28 supply." generally I believe that isn't borne out, it really  
29 causes a commercial risk to the retailer.

30 But net metering would be one of those market rules, but  
31 that would be to some extent a retail market rule which would  
32 favour distributed generation.

33 In general, my answer -- and I can't remember the  
34 question, but these are my notes on what would have to happen  
35 to the Rules to enable distributed generation to really work -  
36 - essentially the general point is that the incumbents find  
37 distributed generation sort of a nuisance; partly to their  
38 planning, partly to their technical management, partly to  
39 their -- they compete, you know, there's costs they're  
40 generating when the others would like to.

41 **CHAIR:** Yet I think there have been some decisions in relation to  
42 putting generators closer to load, for example, that in  
43 essence acknowledges that some of the incumbents are looking  
44 at distributed generation?

45 **MS MELHUIH:** Oh yes, so long as the incumbents can do it  
46 themselves.

47 **CHAIR:** Maybe, yeah, that's a question for later, I guess. But  
48 certainly from the Wind Energy Association point of view it  
49 would seem its conditions to access to networks rather than  
50 the network, that's the issue. In other words, I don't think

*Sustainable Energy Forum*

1           there was, from what Mr Wilson said we get the impression that  
2           people were being intrinsically stopped from connecting to the  
3           network; it was the condition rather than the fact I think.

4   **MS MELHUISH:** I don't think there's a blanket prohibition so long  
5           as the wind generator can pay the costs that Transpower can  
6           think of.

7   **CHAIR:** One assumes the distributor generator says the same  
8           thing?

9   **MS MELHUISH:** No doubt.

10   **MS BATES:** Do you think, in order to get new technology underway,  
11           that it would be necessary for the Government to subsidise  
12           them?

13   **MS MELHUISH:** The short answer is, no.

14   **MS BATES:** So, how would it be funded?

15   **MS MELHUISH:** With friendly market rules. I believe -- and this  
16           is especially true if the gas remained short, which I believe  
17           it will -- but already there are, as Alistair said, in the  
18           Tararua farm the Tararua farm would be uneconomic. In the  
19           very best areas, very high wind speed, stable sheer pattern,  
20           all the things that make wind generation work, it's economic  
21           now, it doesn't need to be subsidised.

22   **MS BATES:** Well, I thought what you were saying was that the  
23           costs that new technology would face under the proposal would  
24           actually prevent that from happening.

25   **MS MELHUISH:** Yes, because there are costs which are not true  
26           costs. There are costs from the perspective of within the  
27           ecosystem. But, you see, from the incumbent's perspective  
28           everything that gets in their way is a cost. From the  
29           perspective of the real world the incumbents have costs of  
30           their own, that they have monopoly ability to recover their  
31           costs if those costs were contested, and the best example of  
32           that is energy efficiency.

33   **MS BATES:** Can I ask you if you think -- examining that, you  
34           think the new technology providers would be charged with costs  
35           which they weren't actually incurring?

36   **MS MELHUISH:** They are incurring them from the perspective inside  
37           the Rulebook, but that is not the only perspective. Other  
38           rulebooks can be written which have a wider perspective; in  
39           particular, a perspective which includes and maybe, for  
40           heavens sakes, even starts from end consumers. From that  
41           perspective the entry of wind generation into a place such as  
42           Bearing Head is not a cost but a benefit, because it meets  
43           network requirements which are otherwise difficult to meet.  
44           Bearing Head is at the end of a long line. It has all sorts  
45           of problems in supplying high quality power to Wainuiomata.  
46           Wind would help that, but those wind generators would not be  
47           paid for the services that they provide to the system.

48   **MS BATES:** I understand what you are saying.

49   **MS MELHUISH:** "subsidy" is a pejorative word and there are cases,  
50           and I've mentioned them, in which some -- some of them -- in



*Sustainable Energy Forum*

1 which a body such as EECA, or an expanded EECA, might well be  
2 justified in paying a loan or even a grant to get some  
3 technology started.

4 I'm not against -- and even if you call it a "subsidy",  
5 I'm not necessarily against it, but I'm saying that a great  
6 deal of this, it is barriers not high costs that prevent them  
7 from entry, and that's confirmed by what the Wind Energy  
8 Association said.

9 **MS BATES:** So, to get back to your Bearing Head example, it's  
10 that, it doesn't pop into the incumbent's head as being a  
11 viable solution for that area?

12 **MS MELHUISH:** The incumbent is well aware of it, but the market  
13 Rules as they stand simply assign costs to wind generation at  
14 Bearing Head.

15 **MS BATES:** If they assigned costs to wind generation at Bearing  
16 Head, which would make it uneconomic?

17 **MS MELHUISH:** Which would almost make it uneconomic. As it  
18 happens, Bearing Head is one of the most economic of all the  
19 potential generators, and it was really local nimbi that  
20 prevented it.

21 **MS BATES:** So, you're getting to -- that the industry should  
22 provide different costing structures to allow the development  
23 of new technology?

24 **MS MELHUISH:** Yes, exactly.

25 **MS BATES:** And that's the way you see it as being funded?

26 **MS MELHUISH:** Exactly. And that those cost structures are  
27 entirely realistic, logical, economic, except from within the  
28 Rules which are at one end of the perspective of possible  
29 Rules.

30 **MS REBSTOCK:** If the argument for doing that is net public  
31 benefit, shouldn't it be the public that pays it and not other  
32 industry players? Because, in effect --

33 **MS MELHUISH:** Other public pay the industry players; it's always  
34 the public that pays it.

35 **MS REBSTOCK:** Well, it does seem like what "industry friendly  
36 rules" means is that the industry subsidises, in effect, the  
37 introduction of new generation such as wind.

38 **MS MELHUISH:** "industry friendly rules" means that wind could  
39 only be introduced if somebody out there subsidised it. Yes,  
40 under rules that favoured incumbents but suppressed new  
41 entrants, then the incumbents would have to appear to be  
42 subsidising the new entrants. But if that's an artifact of  
43 the Rules and if there are other rules structures which I  
44 maintain FERC is advocating, then it might look quite  
45 different. Perspective is a good word; it changes what you  
46 see, what you observe.

47 **CHAIR:** Okay, any other points that we need to take into account,  
48 because I think some of what you are saying is reinforcing  
49 what the Wind Energy Association said. I think there's a  
50 fairly clear picture on sustainability issues.

**Sustainable Energy Forum**

1 **MS MELHUIISH:** Well, it goes beyond sustainability issues. To me,  
2 this -- I'm not portraying the difference between proposal and  
3 counterfactual as primarily a sustainability issue. I'm  
4 portraying it as a way of assessing the cost of saying yes to  
5 the applicant and allowing them to continue to live within  
6 their own, dare I say, comfortable world; and a market rules  
7 system in which the guiding principles were incorporated  
8 inside the Rules, not kind of hanging outside, and which would  
9 evolve by some kind of track from where we are -- because,  
10 remember, we are now at a very tightly constrained ecosystem -  
11 - it would take quite a long time, quite a bit of public  
12 education, and this would need some funding, I don't think a  
13 lot of funding, but I've named in my scenario how much I felt  
14 it might take. It would take both time and money and quite a  
15 lot of consultation, much broader than the consultation we  
16 have seen so far, because I maintain the consultation with  
17 consumers has been essentially ineffective.

18 **CHAIR:** Yes, I think you've made that point pretty clear to us.

19 **MS MELHUIISH:** If that happened, I think you would have lower  
20 costs to the New Zealand economy as whole, and I think from  
21 the macro view it's self-evident. From the micro view I don't  
22 know how you calculate it.

23 **CHAIR:** Well, I think, obviously we'll have to have a hard look  
24 at what you have said to us given the different paradigm that  
25 you are looking at. I think it does fit with what Wind Energy  
26 have said to us in principle.

27 **MS MELHUIISH:** Not surprisingly.

28 **CHAIR:** Thank you very much. Thank you for answering the  
29 questions we've put to you. Thanks indeed.

30 Well, I think I'll adjourn now and at 2 o'clock we've  
31 got MEUG's presentation. So, we'll break now and reconvene at  
32 2.00. Thanks, Molly.

33

34

**Adjournment taken from 12.36 pm to 2.00 pm**

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36 **CHAIR:** All right, it's 2 o'clock so we'll resume, and the next  
37 presenter is MEUG. Mr Currie and Mr Matthes, please.

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*Major Electricity User's Group***PRESENTATION BY MAJOR ELECTRICITY USER'S GROUP**

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**MR CURRIE:** Thank you, Mr Chairman, and good afternoon Commissioners. My name is Terrence Currie. I am Chairman of the Major Electricity User's Group. My involvement in the electricity sector dates back to 1983 when I negotiated with the Department of Trade and Industry, or might have been Industry of Commerce by then, and Treasury, a major or large energy users transition scheme because the two and three part bulk supply tariff was being changed to a four part tariff.

So my experience commences with, in terms of the electricity sector, in 1983 and since that time I have been involved probably in too much of it for my own welfare in terms of the reform process.

Specifically of relevance to the Commission, I was a member, still am, a member of the Governance Working Group under the EGEC process. I'm also a member of the Grid Security Committee, although that appointment post -- is post the agreement by the Grid Security Committee to the transitional dispensation agreement. So, I was not part of the particular GSC grouping which determined the transitional dispensation agreement.

I have at various times been on the Wholesale Electricity Market Development Group, the Rural Structure Working Group and have had an involvement in most of the, as I say, the reform processes over the last 19 years.

With me is Mr Ralph Matthes, the Executive Director of MEUG. He is currently the Consumer Coalition 93 rep on EGEC; he is the consumer rep on the Winter 2002 Steering Committee; he is a consumer rep on the Outage Protocol Forum; and previously and in recent times he has been a member of the Financial Transmissions Rights Industry Consultation Working Group; the Chair of Ancillary Services Working Group, which is a subcommittee under the GSC; and a member of the Instantaneous Reserves Working Group.

The presentation this afternoon, we would like to -- although we attempted to actually address a wide range of issues that have been -- that arose from either the applicant's submission, other parties' cross-submissions or the dialogue over the last four days, it's our intention to try and actually focus on eight issues which MEUG have identified as being important to it, as well as a brief commentary on some of the material lodged by the applicant, and I think there are a couple of items which came up during the question and answer sessions which we could also add some light to.

Clearly, we place some score on the readability, hence I choose to do everything in 14 point, and hence the document you have got in front of you is a -- probably if it was at a

*Major Electricity User's Group*

1 different type size, it wouldn't be quite as bulky as it would  
2 otherwise appear.

3 **CHAIR:** Would you rather we ask questions as you go along or...

4 **MR CURRIE:** I was going to actually take you through the  
5 document. There is the occasional interpolation that I will  
6 make. It was not my intention to read every word that you  
7 have in front of you.

8 **CHAIR:** So you don't mind if we ask questions as they come up?

9 **MR CURRIE:** That's totally in order.

10 As far as key issue number 1 is concerned, the scope and  
11 basis of the application, MEUG continues to be concerned that  
12 there is no -- there is no clear picture or not an absolute  
13 finite picture of what the applicant is seeking. The  
14 application lodged on the 6th of December dealt with issues by  
15 way of characterisations. There was certainly a reformatting  
16 of the application on the 5th of February, but I don't believe  
17 that interested parties -- certainly MEUG as an interested  
18 party, I shouldn't try and speak for others -- but MEUG as an  
19 interested party does not have a clear picture of exactly what  
20 the Commission is being -- what is being sought from the  
21 Commission.

22 The applicant in its original application noted in  
23 paragraph 6.4 that:

24 "it does not consider it appropriate for the  
25 authorisation to cover a characteristic not specifically  
26 brought to the Commission's attention. Accordingly, the  
27 Applicant accepts that the authorisation should only apply to  
28 those provisions of the Arrangement which give rise to the  
29 identified characteristics."

30 And then there were the characteristics identified;  
31 comprehensive coverage of the Rulebook; price determination  
32 process; uniform standards; performance assurances;  
33 transmission service definitions and transmission investment;  
34 costs allocation and information disclosure requirements.

35 So, for clarity, the applicant specified in para 6.8  
36 three items which it designated that the authorisation did not  
37 encompass.

38 By way of the 5th of February 2002, the application was  
39 reformulated and this was done by annexures 1 through to 7 so  
40 that there was then a schedule of parts or Rules which were --  
41 which accounted or made up for the characterisation.

42 That reformatting reclassified those characteristics  
43 into primary provisions; being those provisional -- principal  
44 provisions identified in the application and secondary  
45 provisions; being those provisions that are essentially  
46 implementation and enforcement provisions that give effect to  
47 the primary provisions.

48 In general terms, just as a reformatting, an interested  
49 party can look at those annexures and identify the primary

**Major Electricity User's Group**

1 provisions and secondary provisions because they are contained  
2 in the schedule.

3 The applicant also requested that the authorisation  
4 cover, in relation to each set of provisions, any ancillary  
5 provisions which indirectly give effect to the identified  
6 provisions. The applicant further observed that:

7 "The Rulebook is integrated and giving effect to one  
8 aspect of the rules may arguably entail giving effect to the  
9 provisions for which authorisation is sought, although in an  
10 incidental manner."

11 Potential members, some of whom are MEUG direct connect  
12 members, have indicated serious concerns that they will be  
13 expected to join an arrangement; part of which may have been  
14 authorised but parts of which the status is simply unclear.

15 There are no easy answers that one can give in response  
16 to questions.

17 It clearly should not be a matter for the applicant to  
18 deem what it thinks ancillary and, therefore, authorised.  
19 Likewise we would have a concern that any form of "deem to be  
20 authorised", or a blanket authorisation for non-specified  
21 ancillary provisions. We think that just leaves the  
22 Commission somewhat exposed.

23 The applicant may have adopted this approach to avoid  
24 the need to seek fresh authorisations for amendments, but it  
25 does leave the prospective membership with the potential  
26 liability for being a party to an arrangement, which is  
27 arguably or potentially in breach of the Commerce Act 1986 and  
28 many private sector companies will feel particularly  
29 uncomfortable with this outcome.

30 A further complication is the request to extend the  
31 application for voting structures and in its response dated 22  
32 May the applicant has requested that to protect the industry  
33 against a risk of challenge, authorisation is sought for the  
34 for the voting arrangements -- I refer to paragraph 10.3,  
35 page 26. I suspect that is for the applicant's response  
36 dated -- that cross-reference is the applicant's response  
37 dated 22 May.

38 The applicant opined that in its view the voting  
39 arrangements are pro-competitive and, therefore, in the first  
40 instance authorisation was not originally believed to be  
41 necessary. Also, the applicant observed that the extension  
42 sought was of a minor nature and that the Commission had  
43 commented on the voting structure in the Draft Determination,  
44 hence its attention to that aspect.

45 In a numerical sense the minor nature extension involves  
46 26 primary provisions spanning eight parts of the Rulebook. I  
47 think the only part of the Rulebook not covered by the new  
48 annex is Part B because they are consumer matters, because  
49 that's not populated anyway.

*Major Electricity User's Group*

1           The secondary provisions involve a further four matters  
2 and an unspecified number of ancillary provisions which  
3 indirectly give effect.

4           In terms of issues within the EGEC process, and given my  
5 time on the Governance Working Group I was very well aware of  
6 this, voting structures and the allocation of votes was one of  
7 the most contentious issues. The generator/retailers saw  
8 chapter-by-chapter voting and the allocation of votes as the  
9 means by which they retained control of the decision-making  
10 processes.

11          The subject was revisited multiple times and consumer  
12 representative submissions were repeatedly overruled.

13          Just to interpolate there, the consumers were not at all  
14 or did not endorse at any stage the concept of chapter-by-  
15 chapter voting.

16 **CHAIR:** Could I just ask you a question at that stage to kick it  
17 off. Do some of the other parties to the EGB working party,  
18 do you see the generator/retailers being -- were in practise,  
19 they're the same company for marketing purposes and structure,  
20 in the market are they clearly demand side -- or purchaser  
21 class and generating class?

22 **MR CURRIE:** No, I characterise the vertical integration of the  
23 generators/retailers as "gentailers". I just have to be  
24 careful about how I pronounce it.

25 **CHAIR:** But in practise, they are seen though as two sides of the  
26 market?

27 **MR CURRIE:** No. The vertical integration is a quite -- is a  
28 significant structural defect and in terms of the behaviour of  
29 the gentailer representatives sitting around the Governance  
30 Working Group, I saw no particular sign that they were  
31 representing either the generation arm of their business or  
32 the retailing arm of their business.

33          The Governance Working Group, from memory, was made up  
34 of two consumer representatives, two line company or  
35 distributor representatives; Transpower; the balance four or  
36 five generators or gentailers, and an independent Chairman who  
37 came from -- the Chairman of the MARIA Governance Board came  
38 across to chair the Governance Working Group.

39 **MS BATES:** As this is the section in which you appear to be  
40 addressing the question of voting rights -- is that right?

41 **MR CURRIE:** No.

42 **MS BATES:** Is that later?

43 **MR CURRIE:** I deal with voting rights much -- several times,  
44 actually.

45 **MS BATES:** Is that going to be a theme throughout?

46 **MR CURRIE:** Yes. I think I actually deal with -- under key issue  
47 number 5, the involvement of the consumers in the decision-  
48 making process, and then in the commentary on the applicant's  
49 case I deal with it again.

*Major Electricity User's Group*

1 **MS BATES:** I suppose we'll pick it up then, but I suppose what  
2 I'd hoped you would cover is the extent of the voting rights  
3 and the extent to which MEUG considers them not to be  
4 adequate.

5 **MR CURRIE:** I will certainly attempt to do that during the course  
6 of this afternoon.

7 **MS BATES:** I think that's one of the things we need to  
8 understand.

9 **MR CURRIE:** Just returning to the submission to para 16. MEUG  
10 does not accept that the extension sought is of a minor nature  
11 and submits to the Commission that this matter cannot be dealt  
12 with in the timeframe of the application lodged on the 6th  
13 of December and as reformulated.

14 The fact that the Commission identified the voting  
15 arrangements as containing some competition concerns, does not  
16 in MEUG's opinion legitimise an out of time extension of the  
17 application. I will comment further on this during the course  
18 of the afternoon.

19 **MS REBSTOCK:** Are you going on to the next line?

20 **MR CURRIE:** I was going to quickly touch on paras 19 through to  
21 22, but...

22 **MS REBSTOCK:** If you don't mind, I'll ask you a few questions.  
23 If you are going to come to it anyway, that's fine, you can  
24 tell me.

25 I think it's an important issue, this issue about the  
26 scope, and we have tended to always ask for the provisions to  
27 be authorised to be quite explicitly set out.

28 As you know, in the Draft Determination we defined them  
29 in a certain way, but it does seem that other parties have  
30 picked up the point when they have said that implicitly  
31 looking at those provisions that were identified we have found  
32 it necessary to look at some of the other provisions; for  
33 instance, voting structure. And in the Draft Determination we  
34 did comment on it. It became difficult to separate the  
35 different bits of the proposal in terms of the full Rulebook  
36 and the specific provisions that an authorisation was being  
37 sought for.

38 I guess my question to you is, do you think that we can  
39 do the analysis on the bits of the -- the provisions that were  
40 originally questioned to be authorised without considering  
41 things such as the voting structure and the ancillary  
42 provisions?

43 **MR CURRIE:** I don't believe that the Commission can deal with the  
44 application in front of it without looking at the voting  
45 structures and what I believe are the non-specified ancillary  
46 provisions. The devil is always in the detail -- no, the  
47 devil can be in the detail, and it does seem to me to be an  
48 unsatisfactory aspect of the application that you do not have  
49 a complete schedule in front of you.

*Major Electricity User's Group*

1           Although it creates a problem for MEUG in some respects,  
 2 the position that we have adopted is that you actually need to  
 3 look at the Rulebook in its entirety; that was part of our  
 4 submission in response to the original lodging, and certainly  
 5 in response to the Draft Determination the MEUG position was,  
 6 you simply need to look in the Rulebook, all parts, and all  
 7 the matters that the applicant has raised with you to  
 8 determine, I think, in a complete way what parts you can  
 9 authorise.

10           If you don't accept the MEUG position, that you can't  
 11 actually authorise part; you in effect are authorising the  
 12 Rulebook as laid in front of you because of the way the  
 13 applicant has built its case or presented its case.

14 **MS REBSTOCK:** If we accepted that position, it seems to me we  
 15 would be basically saying to the applicant that we don't have  
 16 an application that we can proceed with currently, because we  
 17 have accepted the original application on the basis of the  
 18 provisions that were identified for authorisation, which did  
 19 not include some of the ancillary provisions and didn't  
 20 include the voting structure.

21           So your submission really is, they need to go back to  
 22 first base with an application?

23 **MR CURRIE:** I think that is my position. I just find that I  
 24 think that the reformatting did address part of the problems  
 25 which we found in the initial application lodged on the 6th,  
 26 but there are still too many matters which have not been  
 27 specified and yet there is -- the applicant himself or itself  
 28 concedes that the Rulebook is an integrated document.

29           So, I think the Commission does have a major problem in  
 30 the matter that we are just discussing.

31 **MS REBSTOCK:** I just pursue that one step further. If we were to  
 32 proceed on the basis of the list of provisions that were set  
 33 down, but not accept the extension to the proposed voting  
 34 arrangements on the grounds that it wasn't part of the  
 35 original application and there's a natural justice issue if we  
 36 were to accept that in hearing that now; would you see any  
 37 difficulties for us to nevertheless just consider those  
 38 provisions which they sought authorisation for, and make it  
 39 quite clear that it does not extend to the ancillary  
 40 provisions or the voting arrangements?

41           Can you see any difficulty, either in a process sense or  
 42 in a substantive sense, in us proceeding on that basis?

43 **MR CURRIE:** That clearly is an option for the Commission. Can I  
 44 perhaps reflect on it before I give you -- because it is a  
 45 material issue for MEUG, because I think you have to raise not  
 46 only the voting structure, which is by way of an extension,  
 47 there is simply no clarity as to the applicant's position in  
 48 respect of the Section 30 -- namely, the wholesale pricing  
 49 mechanism, the common allocation, the fees for non-members and  
 50 the transmission services -- I don't believe that the



*Major Electricity User's Group*

1 application in front of the Commission is totally clear in  
2 that respect, and then there is the aspect of the conditions  
3 lodged as per or in response to the invitation from the  
4 Commission.

5 So, I think there are a number of aspects about the  
6 application which are problematic in a due process or in a --  
7 just in a management sense for the Commission.

8 **MS REBSTOCK:** It seems to me, and I'm interested in your views  
9 and the views of others, that if we were to consider  
10 authorising the Rulebook as a whole, would it be your view  
11 that we in fact would be signing off on any future Rule  
12 changes that included provisions that weren't specifically  
13 covered in this authorisation, in fact would receive the  
14 protection of an authorisation?

15 **MR CURRIE:** No. No, I don't. I think that the applicant has  
16 submitted a -- almost a declaration approach to how future  
17 rule changes are going to be handled.

18 We wouldn't want to see a system whereby for every rule  
19 change the -- whatever form of EGB is finally resolved, would  
20 have to be in front of the Commission on a continuous basis.  
21 Our resources simply wouldn't permit that either. So there  
22 has to be some form of pragmatic decision in terms of future  
23 Rule changes.

24 In terms of the application in front of you, I don't  
25 believe that the Commission can authorise non-specified  
26 ancillary provisions, and our submission is that the voting  
27 structure extension cannot be dealt with in the context of  
28 this application; that clarity is required in respect of the  
29 Section 30 application, and if a breach or if Section 30 is  
30 found to infringe, then I do believe that the applicant will  
31 have to re-submit or re-lodge, because there has been no cost-  
32 benefit analysis in any quantifiable or quantitative sense of  
33 the benefits which would simply leave itself not addressing  
34 the Section 27 implications as a consequence of finding a  
35 Section 30 breach or infringement.

36 **MS REBSTOCK:** If I take your point, if it's not specified then  
37 the onus is on the Commission to identify every possible  
38 scenario that it would need to consider and factor that in; is  
39 that generally the point?

40 **MR CURRIE:** Yes.

41 **MS REBSTOCK:** And I think it's a serious issue because,  
42 generally, we don't take that approach.

43 **MR CURRIE:** I'm not aware of any precedent from the Commission  
44 where you give almost, in effect, a blind authorisation.

45 **MS REBSTOCK:** Yes. So that, if we were to accept that position  
46 then, we would be coming back to the position of looking at  
47 authorising those specific provisions that were in the  
48 application, and a question mark over the voting structure,  
49 which is an extension, but clearly identified?

50 **MR CURRIE:** I think we're pretty close together on that.

*Major Electricity User's Group*

1 **MS REBSTOCK:** All right. Thank you.

2 **CHAIR:** Could I ask one more before you carry on.

3 The suggested additional conditions which were  
4 circulated just before the hearing started, your view's pretty  
5 clear on that; you think the timing and the relationship to  
6 the total application makes it inappropriate for those to be  
7 considered, leaving aside the substance of the issue?

8 **MR CURRIE:** The timing is -- much has been made of the timing,  
9 that is -- it is the process, and I will address that also  
10 during the presentation, but in the context of where we're  
11 talking about the scope and application and the authorisation  
12 or the determination, simply the MEUG position is quite  
13 simple, that the use of conditions submitted by the applicant  
14 is unprecedented.

15 There has been one case, which we are aware of and have  
16 looked at, where the -- relating to a trade practice -- where  
17 the Commission did, in its final determination, add  
18 conditions, but I know of no precedent where there has been an  
19 invitation to parties to address competition policy shortfalls  
20 or the detriments by way of a condition. Therefore, it is the  
21 process and the substance of those conditions which MEUG is  
22 totally opposed to. The timing -- timing can be remedied but  
23 not actually, I think, the process.

24 **CHAIR:** The timing isn't a manifestation of some of the process.  
25 If the conditions, as were circulated just recently, were part  
26 of the originating application, you'd be judging them solely  
27 on the substance rather than the way in which they have been  
28 promoted; is that...?

29 **MR CURRIE:** That is. For the record, it should be noted that as  
30 a CC 93 representative on the Governance Working Group I  
31 opposed those conditions and the concept of submitting  
32 conditions to the Commission as part of the application.

33 **MS BATES:** Could you just tell us what the problem you see -- not  
34 substantive issue -- but the procedural problem or wrong that  
35 you see in that?

36 **MR CURRIE:** In terms of the process of procedural issue, the due  
37 process involves an applicant lodging a case, interested  
38 parties being invited to comment, a draft determination being  
39 issued, parties then having another opportunity of commenting  
40 and submitting, then a Conference or proceedings and then a  
41 final determination.

42 So, you're quite right to identify part of the problem  
43 we have is a procedural concern that those conditions come --  
44 interrupt that process or that procedure and they have not  
45 really been subject to the normal competition policy analysis  
46 or the cost-benefit analysis. We have not had the benefit of  
47 the Commission's preliminary -- or Draft Determination on  
48 those conditions.

49 So, I readily concede there is a process or a procedural  
50 aspect.

*Major Electricity User's Group*

1 **MS BATES:** What say the Commission -- this is theoretical,  
2 obviously -- but the Commission decided to run with those  
3 conditions and put out another draft asking for the other  
4 people's comments on them? Would your procedural objection be  
5 met then?

6 **MR CURRIE:** Yes, I would then have to address the substantive  
7 issue rather than the procedural issue. I can't have it both  
8 ways. If you follow due process, one has to then look at how  
9 those conditions fit in to the overall application, but there  
10 is -- clearly those procedural defects can be addressed and  
11 then it is over to us to argue the merit of the substantive  
12 issue.

13 **CHAIR:** Thank you.

14 **MR CURRIE:** I was, I think, through to para 19, which was that --  
15 and I think I really have mentioned in passing this issue --  
16 this confusion regarding the four pricing issues which I have  
17 dealt with.

18 Then we had a presentation by Contact on Friday  
19 afternoon and again today which still, I think, has left me  
20 somewhat confused -- but it may just be my confusion and it  
21 may not be shared by other parties -- but the position, as I  
22 took it, from Contact Energy is if the Commission found that  
23 the wholesale pricing mechanisms did not infringe Section 30  
24 then the Commission must decline jurisdiction. Therefore, it  
25 would not be entitled or not required to authorise the  
26 primary, secondary and ancillary decisions specified in annex  
27 2.

28 There appeared to be, certainly from the written  
29 document tabled by James Kilty and, I think, circulated  
30 perhaps yesterday -- no, on Monday; time starts to blur a  
31 little bit in terms of when the material is circulated -- but  
32 that's what I took from Contact Energy, and I don't think  
33 anything that was submitted today actually rebutted or varied  
34 that position.

35 On the other hand, the applicant in its original  
36 application on the 6th of December conceded that the  
37 provisions relating to non-members does breach Section 30.  
38 So, there appears to be a potential dislocation between that  
39 aspect of the Part G and their view conveyed in respect of the  
40 wholesale pricing mechanism or the price discovery mechanism.

41 I do think that MEUG would value an unambiguous  
42 statement or a clear unequivocal statement from the applicant  
43 in respect of its intentions, and it probably has to cover the  
44 two options in respect of whether it was found to be in breach  
45 of Section 30 or whether, in fact, if Section 30 cost does not  
46 apply, therefore there is no jurisdiction, what is still the  
47 residual matters relating to the non-member's part?

48 I comment simply in para 22 that if the -- if it is  
49 found that Section 30 does apply, then I do think that that is  
50 a matter which will require a pause in the proceedings,

*Major Electricity User's Group*

1 because I don't believe that a case has been made in respect  
 2 of authorisation for something which is deemed under  
 3 Section 27 to substantially lessen competition.

4 **CHAIR:** Just before you move on. Do staff have any comment on  
 5 the scope of the application piece?

6 **MR ADAM:** Not at this point.

7 **MR CURTIN:** Just on paragraph 22, I'm not sure that I understand  
 8 that, but we do have comprehensive cost/benefit assessment of  
 9 the Rulebook taken as a whole at various different line items  
 10 in there. Isn't that the cost/benefit assessment that would  
 11 be required to justify an authorisation of -- even the one  
 12 price fixing or Section 30 breach that the applicant has  
 13 conceded?

14 **MR CURRIE:** I can't recall any -- the applicant particularly  
 15 addressing in a quantitative sense the benefits and detriments  
 16 attached to those four pricing matters that have been  
 17 canvassed in front of the Commission, but I'm more than happy  
 18 to go away and refresh. I may have made a, sort of, an  
 19 incorrect assumption, but nothing stood out that there had  
 20 been a thorough analysis of those issues.

21 There had been almost a presumption that Decision 280  
 22 would carry the day and, therefore, it was not necessary to  
 23 undertake a full and comprehensive analysis of those  
 24 provisions. In fact, I think the -- without wanting to sort  
 25 of misrepresent the applicant, I understood that their  
 26 position seemed to be that the non-member matter was the only  
 27 element which they thought impinged on Section 30, that the  
 28 wholesale pricing mechanism which has come across into the  
 29 EGBL application was largely that evident in NZEM, hence had  
 30 been found by the Commission in Decision 280 not to infringe  
 31 on Section 30. It was the Commission who, I think, identified  
 32 the two or three other matters in pricing which needed to be  
 33 addressed, and my sense is that there has been no detailed  
 34 analysis, but as I say, I could be wrong; there is -- one does  
 35 start to sort of try and remember whether it's been read or  
 36 whether we've just simply ignored something sort of by choice.

37 **CHAIR:** I think, leaving aside the benefit detriment analysis,  
 38 there were some fairly detailed submissions this morning by  
 39 Contact on the wholesale pricing issue as it related to  
 40 Section 30, argued not only in relation to the NZEM decision  
 41 of whatever number it was, but also in relation to the various  
 42 cases that have been quoted in the Draft Determination; so  
 43 it's obviously been argued substantively as well as just tying  
 44 it to the earlier decision on NZEM.

45 **MR CURRIE:** We're about to actually canvass it now, the next  
 46 section deals with the application of Section 30.

47 **CHAIR:** Yes, obviously, to get your views on the same issue are  
 48 very interesting.

49 Any other comment, Dick, on the jurisdiction issue at  
 50 this point?

*Major Electricity User's Group*

1 **MR ADAM:** No.

2 **CHAIR:** All right, thank you.

3 **MR CURRIE:** Clearly the question of whether any aspect of the  
4 Rulebook infringed Section 30 has become quite a critical  
5 issue, and I think it is not surprising that the applicant in  
6 -- and a number of supporting parties, have argued that the  
7 wholesale pricing mechanism in Part G simply allows the price  
8 to be set according to the market. The market constitutes a  
9 price discovery process whereby a price is found for each  
10 trading period to meet the market forces of supply and demand.

11 I simply note in para 25 that Decision 280 in 1996,  
12 which I think MEUG was actually represented, at both the  
13 preliminary determination relating to Contact and ECNZ and the  
14 full application by EMCO, but there is clearly a strong desire  
15 by the applicant that the findings be carried across or be  
16 simply -- whereas MEUG strongly supports the position, and I  
17 accept it is a preliminary position, a la the Draft  
18 Determination, and I refer to paragraphs 106 to 148 of the  
19 Draft Determination, that if any of the Rules which surround  
20 the price discovery mechanism have the purpose or effect or  
21 the likely effect of fixing or controlling or maintaining  
22 prices the provision becomes caught by Section 30. In MEUG's  
23 opinion the pro-competitive defence is not available to the  
24 applicant.

25 It should be a matter of fact, not rhetoric, to  
26 determine whether any of the Rules interfere with the free  
27 actions of the market participants in discovering a price  
28 which simultaneously solves a supply demand curve at 247 -- I  
29 think that is the right number of nodes or off-take points --  
30 in discrete locations around the country.

31 When you look at the detail of Part G there are a number  
32 of Rules which may or may not interfere with that --  
33 discovering a price.

34 The two hour rule, the requirements that bids and offers  
35 are expected to change by more than 20 megawatts or 10% of the  
36 original bid/offer must be advised to the market  
37 administrator, the ability to block dispatch for certain  
38 generators -- and I think there has been some brief comment on  
39 block dispatch -- constrained on payments, constrained off  
40 payments are a quite unique characteristic of the New Zealand  
41 market, is my point F; the role of the clearing manager which  
42 is to act as a buyer to all sellers and a seller to all  
43 buyers -- that is almost a unique characteristic of this  
44 design -- the fact that the new Rules provide for all physical  
45 trades to be conducted through the EGB market whereas the  
46 existing NZEM can be bypassed.

47 **MS REBSTOCK:** It would be quite helpful if you could tell us -- I  
48 accept that you are saying that these warrant further  
49 consideration, but if you have in mind a way in which these  
50 specific provisions might lead us to a view on Section 30,

*Major Electricity User's Group*

1 what aspect of it do you think leads to a breach of  
2 Section 30, that would be quite helpful?

3 **MR CURRIE:** Commissioner Rebstock, I instance in para 33 one.  
4 What I'd like to do is -- but that's really the only -- just  
5 as a for instance I deal with that.

6 I observed in para 29 that this list is not exhaustive  
7 and other Rules associated with ancillary services, losses and  
8 constraints and the ability of the system operator, as per the  
9 Rules, to change the ratings in the software in the SPD model,  
10 thereby dramatically interfering with the price, could also be  
11 examined.

12 **MS REBSTOCK:** Would you accept that sometimes with provisions,  
13 you can imagine, in some markets that while they do to some  
14 extent constrain, and by definition they do because you  
15 actually create a market on which trading can occur, you get  
16 some constraint in the outcomes but sometimes the effect is  
17 simply get rid of most of the noise but nevertheless you  
18 converge on a sort of market driven outcome; do you accept in  
19 principle that may be what these rules in fact do? That it's  
20 at least possible that these provisions may have that effect  
21 rather than the effect of controlling or fixing prices?

22 **MR CURRIE:** Can I make the argument on the two hour rule and then  
23 perhaps we can re-canvass, without being -- I'm not too sure  
24 whether we're talking -- whether noise or this concept of it  
25 being brief, transitory, ephemeral, sort of the -- I'm not  
26 wanting to avoid your question --

27 **MS REBSTOCK:** Fine.

28 **MR CURRIE:** But perhaps in the context of -- when I discuss --  
29 well, let's jump to para 33 just so that I can address that  
30 issue now.

31 In the two hour rule this prevents -- and it started at  
32 four hours but now is two hours -- it prevents market  
33 participants from changing their bids or offers within two  
34 hours of the specific trading period.

35 I'm sure that the market administrator would give a much  
36 more articulate description of how that process works, but  
37 given that by 1 o'clock on one day the bids and offers start,  
38 or they have to be in by 1 o'clock, then there is an iterative  
39 process through to the gate closure; and that is two hours  
40 before the trading period, participants are prevented from  
41 changing their bids or offers after that period.

42 Now, it has been observed to the Commission that this is  
43 necessary for grid security purposes. However, from a strict  
44 interpretation or analysis point of view that operation of  
45 that Rule prevents a demand side participant from responding  
46 to a price spike. Two hours ahead of time or in real time a  
47 major consumer notes that the price has gone right through the  
48 roof, and it does; this is a volatile market, prices can move  
49 from \$50 to \$500 in the space of half an hour. So, from five

*Major Electricity User's Group*

1 cents a unit to 50 cents a unit. That is an extreme example  
2 but, nevertheless, it is quite a volatile market.

3 A demand participant, and I'm thinking of a major pulp  
4 and paper company who operates continuously, 24 hours a day,  
5 365 days a year, it decides that the price is not prepared --  
6 it is not prepared to pay that price for electricity for that  
7 half hour but unless it has given notice in that two hours  
8 prior it is in breach of the Rules.

9 However, if it responded to that price spike and reduced  
10 its demand in part, in full, then there would be an  
11 instantaneous response in the next half hour period, and all  
12 parties would benefit because that demand had meant that that  
13 lowered the point where the supply demand curve intersected.

14 Now, it does seem that there is a reasonably plausible  
15 argument that the operation of the two hour rule does maintain  
16 that price higher than it otherwise would have been if the  
17 demand side was not inhibited in its ability to respond to  
18 that price spike.

19 Now, if that is categorised as being noise, that may be  
20 appropriate, but it is --

21 **MS REBSTOCK:** Does it hold also on the supply side, if you get a  
22 price dip?

23 **MR CURRIE:** No. I wouldn't see a price dip for the supply side.

24 Well, it depends on what their bidding strategy is, but  
25 if we took Genesis literally, they don't bid into the market  
26 unless they -- they only bid into the market at a price that  
27 they are prepared to be dispatched on.

28 **MS REBSTOCK:** So, it's sort of an asymmetrical effect.

29 **MR CURRIE:** It is an asymmetrical effect.

30 **MS REBSTOCK:** Which at any point in time might cause a -- you'd  
31 only get a movement up rather than down the resulting price?

32 **MR CURRIE:** I'm not too sure whether one of our MEUG's members  
33 has a representative of Comalco here. But Comalco had a study  
34 undertaken because they had responded to price spikes by  
35 dropping off a relatively small part of their load because,  
36 you know, they represent 15 or 16% of total demand, their  
37 consumption is enormous, but they have 25 or 30 megawatts of  
38 controllable load and when prices spike they drop off that 30  
39 megawatt demand aspect of their total demand and they have had  
40 some modelling done which reflects in the quantity, or the  
41 difference between the price that it would have been versus  
42 the price that -- the new price which emerged post the demand  
43 side management that they undertook.

44 **MS REBSTOCK:** And for the purposes of Section 30, it really would  
45 be your submission that it doesn't really matter, even whether  
46 there's the opportunity to manipulate price hikes at that  
47 point. That's here nor there, just the fact that it can  
48 happen is enough to potentially catch it under Section 30?  
49 There doesn't have to be the ability to somehow --

*Major Electricity User's Group*

1 **MR CURRIE:** I was not actually instancing abuse of market power  
2 or gaining or any other -- it just simply has a -- the cause  
3 of that spike may be a constraint. It may not be anything to  
4 do -- it cannot be attributed to any action of a particular  
5 generator, so I'm not submitting that this is an orchestrated  
6 or a managed event; simply, the fact that a spike occurs and  
7 the two hour rule could be argued to maintain prices higher  
8 than they otherwise would be, and the frequency after two  
9 hours, so after four trading periods if that spike still is up  
10 there or those high prices, that constraint may still be in  
11 place, it is then a buyer -- a purchaser could adjust their  
12 load down and then be compliant with the two hour rule. But  
13 for at least that four hours, which is what, a sixth of a day  
14 or something -- no, 12th of the period, they are caught and  
15 prices are maintained higher than they otherwise could be.

16 **MS REBSTOCK:** I understand the point.

17 **MR CURRIE:** It has been argued that the two hour rule is  
18 necessary for security purposes, but equally security in a  
19 sort of a legal sense is not part of the equation determining  
20 purpose, effect or likely effect of fixing, control or  
21 maintaining prices.

22 **MR CURTIN:** I hear what you are saying and I'm picking up on the  
23 word "technical", in particular, because you could make the  
24 same point on every marketplace other than on a completely  
25 instantaneous matching of the supply and demand, and even in  
26 the huge liquid market, let's take foreign exchange or  
27 something, there's probably a two second delay between someone  
28 inputting a bid and someone else picking it up, and you could  
29 argue that technically the slowness of the system to match  
30 bids and offers would be a breach of Section 30, but that  
31 would be pushing technicality to a rather extreme point.

32 I wonder if you'd care to give us some advice on where,  
33 in looking at a market empirically, we would decide that,  
34 yes -- give us maybe some further clarity on where maintaining  
35 or controlling a price would kick in and recognition of sheer  
36 practicality would kick in?

37 **MR CURRIE:** I think it would be appropriate for us to submit --  
38 in terms of giving you an instantaneous response, Commissioner  
39 Curtin, I do think there is a significant difference between a  
40 matter of micro seconds, or that brief period in that example  
41 you gave in terms of a foreign exchange market and a two hour  
42 rule.

43 Would it be in order for me to come back to you? I'm  
44 not too sure that I can give you a most considered answer  
45 right now.

46 **MR CURTIN:** That's okay. Could I just look at point F in your  
47 paragraph 28, because I think obviously we are interested in  
48 any features that are brought to our attention that might  
49 operate in the way you suggest as not being just mere  
50 implementation of the competitive market, but the role of the



*Major Electricity User's Group*

1 clearing manager, which I think you suggested was unique to  
2 this market; could I suggest to you that a clearing house  
3 arrangement is extremely common, for example, in overseas  
4 futures markets and has actually been credited with dealing  
5 with issues of credit worthiness of counter-parties and  
6 generally assisted the liquidity and formation of prices?

7 **MR CURRIE:** Yes, we accept that the role of a clearing house is  
8 not unique, but I think this particular product, and I think  
9 perhaps my thinking was -- was coloured by, perhaps, the role  
10 that the clearing manager or NZEM currently plays as the load  
11 following generator; but that admittedly is in the NZEM  
12 market, not the new market.

13 What we have in this particular situation is clearing  
14 manager under Part G where all electricity, because you  
15 almost have to look at F and G together, all electricity that  
16 is physically traded throughout the whole of the country all  
17 go through the clearing manager and there will be no other  
18 source, with the exception, I suppose one could describe, of  
19 fully embedded generation. Excluding fully embedded  
20 generation all electricity traded will go through this one  
21 process. I think in most other markets or jurisdiction that  
22 is one can contemplate there normally is an alternative  
23 process; off-market trading, over the counter trading, there  
24 is a variety of alternatives which is available, or other  
25 methods can be found of acquiring foreign exchange cover etc.

26 So, I think there is quite a -- it is not -- it may not  
27 be totally unique but it is -- it does have some quite unique  
28 features about it.

29 **MS BATES:** Could I just ask you what effect you think that  
30 provision, the role of the clearing manager, has on Section 30  
31 in fixing, maintaining and controlling prices? In other  
32 words, what effect does that have on price?

33 **MR CURRIE:** It's not clear what effect it has but you have to  
34 simply compare it with other market model designs, such as  
35 NETA, the New Electricity Trading Arrangements in the UK,  
36 where a pool not dissimilar to the New Zealand pool was in  
37 existence, has been replaced with -- now 97% of the  
38 electricity traded in the UK is now physical bilateral trades  
39 with only 3% going through a balancing pool.

40 So, I really was instancing just areas which I think one  
41 needs to sort of take into account -- needs to have regard or  
42 consider and, perhaps, on close examination, constrained on  
43 payments or constrained off payments do not fix, control or  
44 maintain prices, but they at least warrant a closer look given  
45 that the market has changed from that contemplated in or  
46 confirmed in Decision 280 where the NZEM market could be  
47 bypassed.

48 We have moved, via the application in front of the  
49 Commission, into a mandatory wholesale market and absent an  
50 exemption which the EGB may give if an applicant can prove net

*Major Electricity User's Group*

1 public benefit, all electricity will be traded through the  
2 market.

3 **MR MATTHES:** I think there are a couple of ways that the clearing  
4 manager will impact on price. One is, one of the prudential  
5 requirements that the clearing manager sets. If the clearing  
6 manager sets them -- whatever rate the clearing manager sets  
7 those prudential requirements, that will impact on the  
8 clearing price in the market. There's no other competing  
9 commodity, electricity commodity market that people can go to  
10 if they think the prudential requirement is too high or too  
11 low.

12 The other aspect is in terms of the clearing manager's  
13 actual costs themselves. The clearing manager is a monopoly.  
14 It could have extremely high costs and the way that its costs  
15 are allocated across purchasers and sellers in the market will  
16 affect the way that the price is finalised.

17 **CHAIR:** Just again, without belabouring it at the moment, are  
18 there any other pools operating apart from NZEM? I mean,  
19 there were, I think, some years back attempts to introduce a  
20 competing market, but is that still done or not?

21 **MR CURRIE:** What you had really was a series of bilateral trades  
22 where to an extent TrustPower had its own internalised pool  
23 simply using MARIA and the dispatch functions of Transpower.  
24 Phoenix Energy ran its own pool, once again using MARIA for  
25 reconciliation and settlement, and the dispatch function of  
26 Transpower. In both those cases NZEM performed the role of  
27 the load following generator; which meant that any overs and  
28 unders under those pools got met by essentially the NZEM pool.

29 So, there was bypass and there was bypass undertaken by  
30 I think Todds, TrustPower, Phoenix Energy, there may have been  
31 other parties who may have actually used part of their -- they  
32 may have been members of the NZEM and used NZEM for parts of  
33 their business, but in other parts used the bypass  
34 arrangements to trade and sell, buy and sell electricity for  
35 their own customer base.

36 **MR MATTHES:** I think later on we will come, in terms of our  
37 commentary on the applicant's case, to the issue of whether or  
38 not the clearing manager accepts a gross or a net clearance as  
39 well. So, that's another way that prices will be affected.

40 **CHAIR:** All right, back to you then, Terrence.

41 **MR CURRIE:** I think we'd got through to about para 30. There I  
42 was going to comment that -- or am commenting that there seems  
43 to me to be a reasonable amount of common ground between the  
44 preliminary -- do I interpolate in the second line --  
45 preliminary interpretation by the Commission and the arguments  
46 advanced by the applicant. If we think in terms of the  
47 Section 30 really requiring -- having two legs, that was two  
48 or more competitors, and then the second leg was it must have  
49 the purpose, effect or likely effect of controlling and  
50 maintaining prices.

*Major Electricity User's Group*

1           The area of apparent disagreement is whether or not  
 2 having established that there is some interference or  
 3 influence on prices, the arrangements are deemed automatically  
 4 to be in breach, and that's my tentative reading of the  
 5 Commission, or some threshold of competitive intent must be  
 6 proved which is how I read the applicant and the supporting  
 7 parties' case.

8           So, MEUG has carefully examined Appendix B, the legal  
 9 issues identified by the applicant in its response dated 22  
 10 May, and I cross-reference paragraph 6.1 through to 7.3.

11          If you stand back, having read all the commentary on the  
 12 various cases from 2UE and what Lockhart meant or didn't mean,  
 13 it appears to me that if on analysis the Rules did have the  
 14 effect of interfering with a price being set according to  
 15 normal market forces of supply and demand then the applicant  
 16 would accept that a breach of Section 30 does occur.

17          It does seem to me that in a sense the Section 30  
 18 argument almost gets down to a purpose versus effect or likely  
 19 effect or outcome argument, and I will attempt to deal or find  
 20 a way through that at a later stage of the presentation.

21          At the top of page 8, about the tail end of para 33, I  
 22 advance the argument that -- just coming back to the two hour  
 23 rule that I propositioned -- the security aspects of this Rule  
 24 are not germane to the competition policy issue involved, i.e.  
 25 Security issues do not over-rule the anti-competitive effect  
 26 of this Rule.

27          Just also, almost as another observation, prices can be  
 28 controlled by the system operator in circumstances where bids  
 29 and offers cannot be varied because of designated  
 30 circumstances, and there are a number of circumstances  
 31 prescribed in the Rules whereby the system operator can issue  
 32 a security notice -- there may be a threat, potential threat,  
 33 real or otherwise, of a hiccup in the system; a security  
 34 notice is issued, and bids and offers are in a sense frozen.  
 35 So, they cannot be varied. Whatever the circumstances that a  
 36 demand side may find himself in, they are nevertheless locked  
 37 into the bids and offers which were lodged with the clearing  
 38 manager or with the system manager.

39 **MS REBSTOCK:** How often does that come into play?

40 **MR CURRIE:** Sometimes there are multiple security notices in a  
 41 single day, and other times it can be infrequent. I think  
 42 probably the party to enquire would be Transpower -- inquiry  
 43 from would be Transpower who can give you a much clearer  
 44 indication of system operator.

45          But, for example, just 10 days or so ago there was --  
 46 Transpower, as system operator, identified that there may be a  
 47 generation or an energy shortfall in the Auckland area. A  
 48 constraint was then entered into the modelling software at  
 49 Huntly and the prices north of Huntly skyrocketed. Over the  
 50 next three -- or over the next 24 hours that security notice

*Major Electricity User's Group*

1 was withdrawn and replaced with different ratings in the  
2 modelling software three times.

3 Now, that has enormous impact on the prices. It may  
4 have been done for security or -- no, essentially for security  
5 reasons, but the consequences are dramatic and at least one of  
6 the MEUG members thought that they were still totting up the  
7 cost, but we're talking of hundreds of thousands of dollars,  
8 and I thought that the aggregate consumers north of Huntly  
9 probably ended up paying \$2-3 million more for their  
10 electricity -- this is at wholesale level -- because of that  
11 introduction of a security notice and the changing of the  
12 ratings within that notice over that span of 24 hours.

13 **CHAIR:** Just while you are gathering your thoughts, in 35, which  
14 you will come to in a minute, you say that you argued back in  
15 96, I think it was -- anyway, whenever it was --

16 **MR CURRIE:** It was 96. I was starting to get confused between  
17 all the dates but, thank you, it was 96.

18 **CHAIR:** The very simple question is, if you thought the thing was  
19 in breach of Section 30 and that if price fixing was an issue,  
20 then why didn't you challenge it; because presumably with  
21 price spikes occurring, for some of the reasons you suggest,  
22 it would have been in your interest to have challenged that?

23 **MR CURRIE:** We were arguing the theory rather than the practise  
24 because the Decision 280 came out, I think on the 13th  
25 of September, and the market started on the 1st of October.  
26 We were arguing a potential situation but we were not unhappy,  
27 even though we argued that there was a breach, that the price  
28 discovery mechanism, this complicated algorithm which sets the  
29 objective function; it was not optimal from our point of view.

30 The fact that the Commission determined at that time  
31 that it did not have jurisdiction meant that at any stage, if  
32 we felt aggrieved, we could come back and challenge the price  
33 discovery mechanism.

34 That was really the -- we were always uncomfortable  
35 that -- oh no, always felt that there was some aspects;  
36 describing the price discovery mechanism as simply a pro-  
37 competitive design to find a price which met supply and demand  
38 at all the nodes, all the off-take nodes. It was the  
39 associated Rules which perhaps sullied or dirtied that  
40 particular objective, and it was the conditions attached  
41 around that which made it.

42 I think we were also, not constrained, but I think the  
43 Commission did take the view that there was no evidence at  
44 that time, because actually the market hadn't been -- hasn't  
45 really been functioning, but even internationally there was no  
46 evidence which said that a wholesale electricity market per se  
47 would force prices to diverge from what they would otherwise  
48 be, but I think the number of markets which have now gone some  
49 quite significant transformational review suggests that market  
50 design is not as neutral as we thought.

*Major Electricity User's Group*

1 **MR MATTHES:** I think also you need to -- we have been looking at  
2 ways that the market can be reviewed. There was a Ministerial  
3 Inquiry in 2000, we made a submission; there was a review of  
4 last year's winter crisis, we made a submission. A lot of  
5 those submission details were about the detailed Rules and the  
6 governance of the Rules. So, if you like, we've been trying  
7 to get a reform of this market through different forums.

8 **CHAIR:** Thank you.

9 **MS REBSTOCK:** Could I just ask you one more question on this  
10 point in paragraph 35. Do you think there's any evidence of  
11 the fact that the NZEM Rules were not protected by an  
12 authorisation, that it's somehow constrained behaviour?

13 **MR CURRIE:** Yes.

14 **MS REBSTOCK:** Can you tell me how that might have been?

15 **MR CURRIE:** It is -- and my response is intuitive rather than  
16 evidenced by empirical data -- but I believe that there has  
17 always been an awareness that the pricing -- the price  
18 discovery process was not immunised from challenge. So, it's  
19 an intuitive response rather than me being able to point to  
20 particular minuted decisions or conscious decisions that no,  
21 they would not do this or do that, because that may impact.

22 **MS REBSTOCK:** I raise it because, if we came to the view that  
23 Section 30 was breached and we authorised, then it might mean  
24 that we couldn't assume the same constraints would apply that  
25 have applied in the past, potentially.

26 **MR CURRIE:** That does create a dilemma for MEUG as well as --  
27 and, I was going to deal with it later, but we could deal with  
28 it now, because I think the position that MEUG finds itself in  
29 is that, we believe that the Rules surrounding the price  
30 discovery process -- do we end up intervening or interfering  
31 with the price mechanism, thereby infringing Section 30?

32 But then we have this dilemma that, because if  
33 Section 30 is infringed then is deemed to breach Section 27,  
34 you then have to address the question of authorisation. But  
35 if authorisation is granted, then any improvements to the  
36 price mechanism, and it evolving, are unlikely to happen  
37 because simply the process of having to make a fresh  
38 application to deal with a Rule change in respect of Part G  
39 may -- that may be difficult to achieve given the voting  
40 structures or review -- giving the dominance of the supply  
41 side to Part G Rule alterations.

42 So, this is where the dilemma really bites, it's almost  
43 like a catch 22 situation. We have a strong preference for  
44 the pricing mechanisms not to be authorised, but we also can  
45 argue, and are arguing, that they are caught by Section 30  
46 because they have the effect or likely effect of fixing and  
47 controlling, maintaining prices; so that really is a dilemma  
48 for us.

49 **MS BATES:** Could I ask you; were you here when Professor Hogan  
50 spoke?

*Major Electricity User's Group*

- 1 **MR CURRIE:** Yes.
- 2 **MS BATES:** Did you agree with his assessment of the market design  
3 in New Zealand?
- 4 **MR CURRIE:** I think I took from the professor's remarks that he  
5 thought the strongest aspect of the New Zealand market design  
6 was the full nodal pricing aspect. I'm not too sure that I  
7 heard him dive into the detail of other aspects; I may have  
8 selective hearing, but I thought that the strongest -- his --  
9 it was an overview that he gave the market design in terms of  
10 a price discovery mechanism providing for dispatch based  
11 prices on a full nodal pricing model -- he had a nice little  
12 araldite articulate sort of view of it.
- 13 **MS BATES:** Yes, he basically said it was good.
- 14 **MR CURRIE:** At that high level, yes.
- 15 **MS BATES:** His main issue seemed to be with governance, as I  
16 apprehended it?
- 17 **MR CURRIE:** He certainly raised and instanced his US and other --
- 18 **MS BATES:** The reason I'm asking you is, I'm not quite clear on  
19 the extent to which MEUG has problems with the market design  
20 and the pricing mechanism.
- 21 **MR CURRIE:** We have less problems with the -- Ralph, you can have  
22 it in two seconds -- we have not challenged the pricing  
23 mechanism in NZEM since its inception on the 1st of October.  
24 We have looked for changes from time to time to it, evolution,  
25 but we have not fundamentally challenged.
- 26 We are probably more concerned about abuse of market  
27 power or the lack of competition at the generator level and,  
28 therefore, the potential for the abuse of market power and  
29 structural defects and the consequences of vertical  
30 integration and the availability or the non-availability of  
31 realistically priced hedges. We've argued that there are a  
32 number of issues which we have identified, but concern about  
33 the design of the market, at various stages we've argued for  
34 an ex anti market, we have wanted more demand side  
35 participation, more information, there are a number of things,  
36 of improvements, but we have not challenged the market in a --  
37 the existing market in a legal sense.
- 38 That does not prevent us, in this particular application  
39 for authorisation, pointing out that in our opinion aspects of  
40 the market may be in breach of Section 30.
- 41 **MS BATES:** Yes. No, I didn't think it did. I just wanted to  
42 clarify the extent of your concern. Did you want to add  
43 anything?
- 44 **MR MATTHES:** Yep, just a small comment. The devil's in the  
45 detail with a lot of these things. I mean, it's the -- the  
46 issue, for example, of release of bids and offers, it's a  
47 detail but it is important in terms of the way that consumers  
48 participate in the market; there's still a lot of confusion  
49 about this.

*Major Electricity User's Group*

1           The NZEM have lodged an application for authorisation to  
2 have bids and offers released within two weeks but we see that  
3 the applicant, for example, still has as a detriment the  
4 release of bids and offers. I mean, it's a detail, but it is  
5 quite important in terms of the way that consumers participate  
6 in the market on the final prices, but I agree with Terrence  
7 that, overall, the structure itself is pretty sound; which  
8 isn't to say that we're not always looking for other  
9 structures, such as the NETA in the UK, to see how they  
10 perform.

11 **MR CURRIE:** One of my glaring omissions would be the fact that  
12 much has been played about the dynamic attention between  
13 supply and demand, but we have a market where supply is  
14 represented by the generators on one side of the market and  
15 the purchasers are represented by the retailing arms of those  
16 generators. That does have, I think, a -- may have a  
17 pervasive impact on that so-called tension between that price  
18 discovery process, where theoretically purchasers always are  
19 trying to reduce the cost of acquiring their product. If they  
20 are simply price takers and the generators are the price  
21 makers, then that sort of --

22 **MS BATES:** I understand.

23 **MR CURRIE:** -- that criteria. Just by way of observation, as of  
24 the 12th of September 1996 -- I got the date right this time,  
25 Mr Chairman, it is 96 -- at the time of Decision 280 there  
26 were 33 participants in the market. Today there are nine and  
27 when you look at the -- of those nine, they virtually are  
28 gentailers. With only one or two exceptions they are all in  
29 fact simply the generator and the retailing arm of the  
30 parties.

31           I commented, we are not attacking the fundamental  
32 design. I want to preserve the right to attack it in the  
33 future if I believe that it is -- there are anti-competitive  
34 aspects, but having said that I think it is appropriate that  
35 we have pointed out that there are some -- there are aspects  
36 of the market which warrant a very close look at in case they  
37 impact -- in case they infringe on Section 30.

38 **CHAIR:** Thank you.

39 **MR CURRIE:** I think I got through to about para 36. I almost got  
40 to that stage.

41 **CHAIR:** What say we try and get up to issue number 3 then we'll  
42 break.

43 **MR CURRIE:** Are you setting a target for me?

44 **CHAIR:** Let's try for number 3. Work through the rest of this  
45 section first.

46 **MR CURRIE:** Okay.

47 **CHAIR:** I'm not trying to hurry you.

48 **MR CURRIE:** No, I didn't feel hurried.

49 **CHAIR:** Thank you.

*Major Electricity User's Group*

1 **MR CURRIE:** In para 36 I simply comment again, perhaps  
2 belabouring the point but, nevertheless, the applicant has  
3 sought authorisation of Part G, Section 4 pricing as a  
4 primary. It then cites Part G, Section 1 (rule 5),  
5 Section 2, Section 3 and Section 5; so all five parts of  
6 Part G are caught up under the authorisation, and then  
7 whatever ancillary provisions, not specified. So, although  
8 the applicant itself has said we do not believe that these  
9 matters breach Section 30, the authorisation does seek to  
10 have it authorised.

11 I think I've already covered paras 38 and 39, and even I  
12 get tired of reiterating the same point multiple times.

13 In paragraph 40 we say that it would be appropriate for  
14 us to know exactly what is being requested.

15 I've already covered comment about the immunisation. I  
16 have commented in terms of NETA, and we had hoped to attach to  
17 this document some -- a number of attachments, one of which  
18 dealt with a report from NETA, but advancing our presentation  
19 from tomorrow to today we just simply ran out of time, and I  
20 think you are already suffering an overload of reading  
21 material, but the OFGEM website does give some -- and it is  
22 our intention I think -- Ralph may have negotiated with the  
23 Commission staff the ability to -- for us to lodge a couple of  
24 documents that we simply could not attach to today's  
25 presentation, but we would be circulating or lodging those  
26 knowing that they should be circulated in an immediate  
27 timeframe and to all other parties.

28 **CHAIR:** We'll certainly do that, and I think the focus will be  
29 appreciated if we still have a fair amount in front of us any  
30 way.

31 **MR CURRIE:** I think para 42 also includes a comment that we  
32 simply believe that on authorisation -- and I think we're  
33 probably saying, relative to the counterfactual, whichever  
34 counterfactual, and there is some comment we'd like to make on  
35 that -- but relative to the counterfactual indicated by the  
36 Commission, such as a Crown EGB, we would suggest that  
37 authorisation of the trading arrangements as requested and  
38 resident in an industry EGB, it is much less likely that those  
39 trading arrangements will evolve over time in any of the ways  
40 that we would see them appropriately moving.

41 **MS REBSTOCK:** Can I just ask you a question there. The Crown  
42 under the industry EGB must still set down a GBS for the  
43 industry EGB every year, and it seems reasonable to expect  
44 that to be as strategic -- or have a strategic focus and  
45 undoubtedly the need for reform of the overall market design  
46 would be something you would think, if that was generally  
47 perceived as something that should happen, the Crown, even in  
48 an industry EGB, can signal that expectation and effect  
49 change, and it does seem to me that consumers will, even under



*Major Electricity User's Group*

1 an industry EGB, be able to influence where the Crown takes  
2 its statement to the industry.

3 I'd just like you to comment on that, because I think  
4 the applicant has put a fair amount of weight on those  
5 mechanisms by which the Crown both -- in the lead-up period  
6 for each period signals to the industry what is in the  
7 interests of consumers but also monitors against it at the  
8 end.

9 Can you tell me why, those arrangements being in place  
10 with an industry EGB, you wouldn't be able to effect reviews?

11 **MR CURRIE:** I believe that the negotiation of those annual  
12 performance objectives certainly does give the Minister or the  
13 Government of the day or -- an opportunity of directing the  
14 attention of the industry EGB to improvements or changes that  
15 it believes are desirable.

16 I nevertheless believe that an industry EGB will largely  
17 deal with those matters in its own timetable, not in its own  
18 timeframe; notwithstanding the fact that it is then audited  
19 against those former objectives by two statutory  
20 organisations.

21 So, I still believe that it is possible -- it would be  
22 possible for a Crown EGB to affect more quickly, and if it was  
23 found conclusively, more dramatically than an industry EGB.  
24 If there was such overwhelming experience coming out of NETA  
25 or some of the other markets going through a reform process  
26 that we needed a substantial redesign of the market, which may  
27 commercially disadvantage some participants, I believe that it  
28 is more likely that such decisions would be made by a Crown  
29 EGB rather than an industry EGB.

30 **MS REBSTOCK:** What about the impact of the ongoing threat of  
31 switching to a Crown EGB?

32 **MR CURRIE:** Two strikes down? Well, it's at least a 24 month  
33 plus, isn't it, sort of timeframe?

34 **CHAIR:** But you'd have to give any arrangement, be it a Crown EGB  
35 or whatever, some time to see if it's going to work or not, I  
36 mean -- so, 24 months isn't necessarily too far away?

37 **MR CURRIE:** No, in terms of the timeframe that's -- I suppose I  
38 was -- a slightly knee-jerk reaction.

39 **MS REBSTOCK:** We've had it put to us that this tension in terms  
40 of the role of the Minister or the backstop legislation to  
41 switch to a heavy-handed approach would discipline -- in  
42 effect discipline the industry to progress issues such as  
43 this, and you seem to be disagreeing with that position?

44 **MR CURRIE:** I think it's probably -- the extent of the  
45 disagreement is probably perhaps not as great as I have made  
46 out.

47 I think it is my judgment that under certain conditions  
48 it is likely that a Crown EGB could move more quickly and more  
49 effectively on some issues which were directed at enhancing  
50 the welfare of consumers than an industry EGB. But I -- it

*Major Electricity User's Group*

1 probably is not as dramatic a difference as -- than I had  
2 expressed previously.

3 **MS REBSTOCK:** Mighty River used this term, "institutional  
4 inertia", and it almost sounds like a variation on that theme.

5 **MR CURRIE:** I think agenda setting, remembering that under the  
6 industry EGB it's largely process -- it is a manager of a  
7 process given that it doesn't have the executive authority to  
8 make decisions and that can be put out for a vote. The  
9 concept of multiple votes that have now been proposed -- it  
10 just...

11 **MS REBSTOCK:** The industry EGB, correct me if I am wrong, does  
12 however have the ability to set the agenda of what is to be  
13 considered and the timeframe; the independent board does with  
14 the industry EGB. That, in a sense, does at least kick off a  
15 process, and that seems quite similar to a Crown EGB, to me.

16 **MR CURRIE:** It does have the ability to set the agenda to the  
17 extent of getting the Working Groups underway.

18 So, as I say, I may have over-emphasised the difference  
19 between the timetabling and timeframes of the industry EGB  
20 versus the Crown EGB.

21 **MS REBSTOCK:** Then we'll have to make some judgment if we  
22 accepted that view that there's a timing issue in terms of,  
23 you know, how do you quantify that. You may not have had a  
24 chance to give that much thought, on how you might quantify  
25 that, but I suspect we'll come back to that when we get  
26 further into your submission.

27 **MR CURRIE:** I'm conscious of your target, Mr Chairman. In terms  
28 of paragraph 43, I really just observe that the fact that the  
29 Rules have largely been replicating NZEM Rules does not of  
30 itself mean that you -- they don't warrant a very close  
31 scrutiny.

32 **CHAIR:** Right. I had another question but I think it's probably  
33 picked up in the counterfactual because in the submission you  
34 made on our Draft Determination you are looking at a different  
35 counterfactual; the question is, do you support the different  
36 counterfactual? This we'll come back to when you get to  
37 argument 3.

38 So, thanks, Mr Currie. We'll break until about quarter  
39 to four, I think, then we'll resume. Thank you.

40 **Adjournment taken from 3.32 pm to 3.45 pm.**

41 **CHAIR:** All right, well, we'll resume. I think we might go  
42 through, Terrence, until 5.30 with your presentation. We've  
43 asked CC 93 to come in in the morning, but, of course, if you  
44 go over 5.30 you can start at 9 o'clock in the morning. I'd  
45 like to take a break at about quarter to five for 10 minutes  
46 to give our transcriber five minutes to catch her breath.

47 So let's run through now until quarter to five, then a  
48 break and at 5.30 sharp, and if you have to go over to  
49 tomorrow, we'll obviously the time is there.

50 **MR CURRIE:** Thank you.

*Major Electricity User's Group*

1 Moving to key issue number 3, the counterfactual. If  
2 you recall, MEUG argued in its initial submission that it  
3 lodged back in, I think February and also in its 22nd of May  
4 submission, that is that an alternative counterfactual was at  
5 least arguable, and the actions of the applicant since the  
6 Draft Determination was released on 26 April confirm that an  
7 alternative arrangement that enhances consumer welfare cannot  
8 be ruled out on the grounds of timing or that the industry  
9 would accept no further compromises.

10 In our opinion the counterfactual submitted by MEUG has  
11 gained further currency and warrants reconsideration by the  
12 Commission. I'll develop that argument further, but it's  
13 important to remind the applicant of the MACQS application to  
14 the Commission, although a number of the main players in the  
15 applicant's team will remember those events; an initial  
16 application was made on the 2nd of October in 98. Consumer  
17 groups, including CC 93 and MEUG, expressed strong disapproval  
18 for a number of aspects of that application which were  
19 subsequently withdrawn.

20 Further discussions and negotiations took place within  
21 what was then called the Interim Grid Security Committee and  
22 once agreement was reached a revised application was lodged on  
23 the 28th of May.

24 Most of those changes related to governance and the  
25 involvement of representation, and the revised application  
26 included nominated representatives on the Grid Security  
27 Committee from the Consumers Institute, the Major Electricity  
28 User's Group and the Chamber of Commerce. There was no  
29 consumer representation involved in the first application  
30 lodged back in October.

31 This time, or by May 1999 consumers fully supported the  
32 maximum application for authorisation, and in due course,  
33 following the due process, the MACQS application -- which  
34 largely dealt with the rule making process, the governance and  
35 the rule making process -- was authorised.

36 In para 48 I simply comment that the applicant has  
37 demonstrated that further changes to the arrangements can be  
38 made if the industry is sufficiently incentivised.  
39 Furthermore, such changes can be devised in a relatively short  
40 timeframe and MEUG hypothesises that if the applicant was  
41 faced with two options; the first to negotiate a more consumer  
42 enhancing set of arrangements which, just for example,  
43 addressed voting structures and the misaligned set of guiding  
44 principles, or a second option, being to refuse to contemplate  
45 any further changes, thereby forcing the Government to  
46 initiate a Crown EGB, it is in MEUG's opinion the applicant or  
47 the industry represented by the applicant would choose the  
48 first option.

49 **MS REBSTOCK:** I just wonder if the issue here is merely whether  
50 or not the applicant would have sufficient incentive or

*Major Electricity User's Group*

1 whether the issue is that the Crown has said, "This is your  
2 chance, and if it doesn't happen we're going to go to a Crown  
3 EGB model straight away."

4 So, my understanding of what the applicant has said is  
5 not that they wouldn't do it if they were in a MACQS type  
6 situation; what they are saying is, they are not. They have  
7 been told that this is the chance and if it doesn't happen  
8 this time then the Crown will step in and activate the  
9 backstop option.

10 You seem to be suggesting that the Crown won't step in  
11 immediately, that it will give the industry more time, and I  
12 think the argument has been that the Crown won't give that  
13 time; not that there isn't adequate incentives.

14 **MR CURRIE:** I think the applicant has run two lines. One line is  
15 that the existing arrangements represent the strongest  
16 compromise that they have been prepared to make and that a  
17 review of a -- of a forced review of the existing arrangement  
18 would unravel those compromises; that's one line.

19 The second line is that the -- they have been pressed,  
20 they have exhausted the Government's patience in terms of time  
21 already, and that the Government would not allow them any  
22 further time to re-caucus and re-submit.

23 I believe that hypothetical, if the Commission were to  
24 not authorise the application in front of it, and in making  
25 that final determination gave the applicant strong signals and  
26 directions as to what it believed needed to be remedied and  
27 the areas that needed to be addressed, it is my opinion that  
28 the EGEN process would immediately address those, and I don't  
29 believe that the political climate, given that there is a  
30 period of -- we're confronted with an element of time of  
31 political hiatus in terms of an election and a new Government  
32 settling in, that there would be no time at all to address  
33 those issues which we believe need to be addressed.

34 That is one of the reasons why CC 93 has stayed with the  
35 process rather than walked from the table, because  
36 notwithstanding the repeated veto, over-ruling, ignoring,  
37 which has driven to us a point of frustration, we have  
38 believed that it is better to stay in the tent and we have  
39 always believed that there was a number of opportunities still  
40 to improve and to achieve an improved set of arrangements.

41 **MS REBSTOCK:** When we talked about the voting structure extending  
42 the scope of the authorisation to include the voting  
43 structure, you indicated that you thought there were  
44 significant issues which would require considerable time, and  
45 I just wonder now about, and in fact in discussing whether  
46 conditions should be imposed, again the view that conditions  
47 are -- that could be contemplated as significant and would  
48 require some time to work through. That's consistent with  
49 your view in this instance on the counterfactual, that a  
50 second application could be made that would take account of

*Major Electricity User's Group*

1 any competition concerns, if that's what happened, in fairly  
2 short order.

3 **MR CURRIE:** It probably would require a pretty strong lead from -  
4 - in the final determination for the matters to be addressed  
5 expeditiously.

6 Yes, I -- there is -- MEUG acknowledges there has been  
7 this time -- this pressure on delivering a new set of  
8 arrangements which incorporate the NZEM, MARIA and MACQS  
9 processes.

10 But I don't think you can rule out that as being a  
11 plausible option. The EGEC has already advised that it is  
12 addressing the issues raised by Meridian, Transpower and  
13 Comalco. They took only a matter of weeks to address the  
14 issue of voting, indirectly by the condition they have  
15 proffered. Also, I think they have shown an ability to re-  
16 caucus and make progress, but I think a condition precedent  
17 for that would be a strong direction from the Commission, and  
18 clearly a recognition from the Government, and this is in one  
19 instance; one talks about the lobbying and providing of  
20 contestable policy advice to Governments of the day and  
21 Ministers etc, and clearly this is one instance where we would  
22 be arguing very strongly that time should be provided to  
23 enable an improved set of arrangements to emerge from a  
24 reconvened -- well actually, the EGEC process is continuing  
25 on, it didn't stop on the 12th of June, it is continuing on,  
26 there is still -- as I say, a couple of work streams.

27 So, it is a plausible scenario.

28 **MS BATES:** Can you just tell me whether MEUG would prefer, and it  
29 seems that you may, to have an industry EGB with a board  
30 making decisions provided that you have appropriate  
31 representation; would you prefer that sort of process to the  
32 Crown EGB process whereby the decision-making is in the hands  
33 of the Minister?

34 **MR CURRIE:** Our preference is for an improved arrangement with an  
35 industry EGB with the governance and decision-making defects  
36 addressed -- there are about four or five key points which I  
37 think are probably encapsulated in the CC 93 submission, and  
38 if those prerequisites were met, we have always expressed a  
39 preference for an industry EGB. As I say, we have devoted an  
40 enormous amount of resources and stuck in there when a number  
41 of us would have been tempted to walk away, because our hope  
42 was that we could end up with an industry EGB that we'll be  
43 coming along and supporting, not opposing.

44 **MS BATES:** On that model, does MEUG prefer the decision-making  
45 power to be in a board rather than within the EGB itself?

46 **MR CURRIE:** Totally and absolutely, a big tick to that. It is an  
47 anathema to have a board, a high calibre -- a board that we  
48 actually want to place, you know, has got a number of serious  
49 and major tasks to deal with, we believe there should be --  
50 that should have executive decision-making powers, but with a

*Major Electricity User's Group*

1 call-through on some issues if there is an industry reaction  
 2 if they, as under the MACQS process under the governance  
 3 arrangements, if the industry can gather as shareholders do,  
 4 if they can gather sufficient numbers of votes or proxies they  
 5 can request that the board put a matter to an industry vote  
 6 and we always saw that as a -- the backstop to a board which  
 7 had just total and absolute executive power.

8 So, our approach has been for executive making powers,  
 9 authority, but with a backstop.

10 **MS BATES:** So, would it be correct to say that under the Crown  
 11 EGB model, with the Minister making the decisions, you  
 12 wouldn't see yourselves as being in the tent?

13 **MR CURRIE:** Well, I think the Crown EGB could -- the actual model  
 14 and how it set up the infrastructure underneath that is not  
 15 clear. There's been a lot of speculation, but it is not  
 16 clear.

17 We would anticipate the Working Groups, there would  
 18 definitely be consumer representation on all Working Groups.  
 19 We would believe that the primary objective specified in the  
 20 EIEA or EEIA would be -- the acronyms start to become  
 21 confusing -- but we would see the primary objective being part  
 22 of that Crown EGB board.

23 It could be that we end up with a Crown EGB which does  
 24 not function dramatically differently from an industry EGB,  
 25 except you would not have the supply side dominating -- you  
 26 would not have a chapter-by-chapter voting process, in our  
 27 opinion, under a Crown EGB.

28 **MS BATES:** Well, there wouldn't be a voting process, would there,  
 29 because then the Minister would decide?

30 **MR CURRIE:** Yes, he would have regard -- the dialogue you had  
 31 last week in terms of the consultative process, a lot of the -  
 32 -

33 **MS BATES:** It's not clear how a Crown EGB itself would come to a  
 34 decision, but...

35 **MR CURRIE:** No. But, nevertheless, I don't think MEUG has backed  
 36 away from and changed its view. It would like an industry EGB  
 37 which met its, I think, relatively straight forward  
 38 prerequisites.

39 **CHAIR:** It may be, of course, the applicant with a sum -- when  
 40 they sum up at the end of the day, whether they have a view on  
 41 this, I don't know, and it may be interesting to see what  
 42 Transpower have to say when they submit because they have  
 43 views on the structure, as you know, in their submission.

44 I mean, what you have said is consistent with your  
 45 response to the Draft Determination, that's basically the same  
 46 point, isn't it?

47 **MR CURRIE:** Yes. I hope that we sort of -- well, we try and  
 48 remain reasonably consistent with our argument.

49 I think, just moving on, in para 49, I think the -- in a  
 50 sense the counterfactual is always looked at as a with or

*Major Electricity User's Group*

1 without and on a pragmatic assessment, as I say, given that  
2 there is sort of a little bit of a timeframe that we have as a  
3 consequence of a decision to go to the polls. I believe that  
4 the counterfactual that MEUG has submitted cannot be ruled  
5 out, and we do believe that the consequences of that could be  
6 an improved consumer welfare enhancing set of arrangements.

7 **MS REBSTOCK:** Sorry to do this to you, but can I ask you one more  
8 question on the counterfactual.

9 There seems to be some difficulty with the  
10 counterfactual, as you suggest, and let me put it to you this  
11 way: You've suggested the counterfactual could be that the  
12 industry go away in light of the Commission's indications in  
13 the draft and come up with something with an improved  
14 proposal.

15 It does seem to me it gets a bit circular. The  
16 Commission can define the counterfactual in a way that ensures  
17 virtually that by definition from our perspective it must be  
18 improved -- the counterfactual must be -- have higher net  
19 benefits than the proposal, and I just really wonder if that's  
20 the purpose of defining the counterfactual.

21 I mean, it really -- it almost by definition makes this  
22 application fail. The circularity of that seems undesirable  
23 to me on the basis for which we should make our decision.

24 I know I haven't expressed that clearly, so if you  
25 didn't understand what I'm saying, please tell me.

26 **MR CURRIE:** I understood the circularity argument. I was just  
27 putting my mind to "what do you know" sides I could see.  
28 Sometimes things do have to take a circular route to achieve  
29 the best outcome. So, I don't automatically associate failure  
30 of this application as being a downside.

31 **MS REBSTOCK:** That's not really what I'm saying. I mean, in a  
32 sense it opens up the possibility that the Commission really  
33 does design this market, it indicates clearly what it wants  
34 and compares any proposal to that. In other words, redefine  
35 what is -- rather than comparing this proposal with the most  
36 likely alternative, we actually compare it with what we think  
37 is preferable, and that seems to be -- have very undesirable  
38 characteristics and present serious problems to anyone who  
39 puts in any sort of application to us if we followed that  
40 path.

41 **MR CURRIE:** On that basis I'd have to totally agree with you. I  
42 do not want to see the Commission designing the market or the  
43 arrangements or even entering into negotiations. I do think  
44 that that's not -- I suppose in a sense when I talk to you --  
45 when I proposed earlier on that a set of directions or  
46 indications where on balance, or according to the net benefits  
47 versus detriments, you identified a number of areas that  
48 needed to be addressed, I didn't envisage the detailed design;  
49 I thought you were still staying at a relatively high level.

*Major Electricity User's Group*

1           But I have to say that I am not inviting -- I would not  
2 want to actually encourage the Commission in any way to become  
3 involved in the designing of the market, and hence the  
4 reservation that I have about the whole concept of conditions  
5 as well.

6 **MS REBSTOCK:** I didn't take what you said as encouraging us to do  
7 that. I'm putting to you, is the effect of choosing your  
8 counterfactual to be -- in effect, lead to that outcome even  
9 if it wasn't the intent; and, that seems undesirable from a  
10 general process point of view?

11 **MR CURRIE:** I would like to give that issue some further thought  
12 because the question of the counterfactual is important. I  
13 think we, in our 22nd of May submission, instance that we  
14 thought that an alternative counterfactual was arguable, but  
15 for the purposes of trying to deal with the application in  
16 front of the Commission, we did accept in terms of -- for  
17 quantifying and measuring and that quantitative analysis, we  
18 were prepared to do that on the basis of the Commission's  
19 choice of a Crown EGB.

20           So, I suppose I was wanting a bet both ways; I was  
21 concerned or indicated that it was plausible, actions of the  
22 applicant had demonstrated that it could reconsider and deal  
23 with things that gave a degree of currency to MEUG's  
24 counterfactual scenario. But you have raised an important  
25 issue in terms of to what extent and whether that leads you  
26 into a design or simply establishing a counterfactual that in  
27 essence no amount of reworking may necessarily achieve.

28           So, I will think about that, if I may, overnight and  
29 perhaps address that issue specifically. It may be -- it is  
30 likely that I will be part of the CC 93 team in which case I  
31 could potentially address it then, because it is an important  
32 issue.

33 **MS REBSTOCK:** Thank you.

34 **MR CURRIE:** If we can move on to key issue number 4. There has  
35 been considerable play for the support of self-governance, and  
36 there has been statements, quotes, citations and the whole  
37 impression conveyed is that there has been this strong support  
38 for self-governance, and I suppose by implication -- or MEUG  
39 has taken it that by implication the applicant is saying that  
40 there is the strong support for this particular set of  
41 arrangements placed in front of the Commission.

42           I think there is no question that the Minister and  
43 cabinet have indicated a preference for an industry self-  
44 governance where possible; the Crown EGB was a fall-back  
45 position. But I don't believe that any of that support or the  
46 general support conceptually or philosophically for industry  
47 self-governance can be taken to be support, per se, for the  
48 arrangements in front of the Commission, and the test of  
49 whether this set of arrangements does meet the Government's



*Major Electricity User's Group*

1 expectations will be when it is declared an EGO in terms of  
2 the EA Act.

3 **CHAIR:** I think in fairness to the applicant, they have  
4 acknowledged that there are still some issues that are in  
5 dispute. I mean, let's be frank.

6 **MR CURRIE:** I understand that, Mr Chairman. I was just really  
7 observing that there was a strong theme, an underlying theme  
8 coming through, and I think it's important from an antagonist  
9 or a protagonist point of view, whichever you like to describe  
10 it, simply to indicate that in order for the applicant to make  
11 the strongest case possible. I think there is some tests and  
12 thresholds which have to be met before that position can  
13 really be advanced much beyond the rhetoric.

14 In issue number 5 we talk about consumer involvement in  
15 decision-making, and I must point out that we have had  
16 representatives on the three Working Groups: that is, the  
17 Rationalisation Working Group, which Ralph and another CC 93  
18 rep was on; on the Governance Working Group, myself and  
19 another CC rep was on; and on the Transport Working Group  
20 there were three CC 93 representatives; and on the plenary  
21 session, that's the overall -- the head committee or council,  
22 there were two.

23 So, we have been involved in the process of developing  
24 the application. The fact that we've been outvoted on every  
25 instance is probably of no great surprise to you.

26 We sought involvement in the election of the board,  
27 that's the initial election process; we sought involvement in  
28 the referendum process, we wanted to -- we didn't want voting  
29 by chapter. We believed that the board should have that  
30 executive authority. But on Working Groups we wanted mandated  
31 consumer representation.

32 We were relatively neutral on whether the industry board  
33 and industry EGB should be completely independent or should be  
34 a mixture of industry and representatives and independents, as  
35 long as a majority were independents which reflected the GPS.

36 The critical issue which I've already commented to  
37 Commissioner Bates is this question of the executive  
38 authority, and we wanted to make -- we wanted to have an  
39 executive -- an industry board which did have executive powers  
40 to make decisions consistent with its responsibilities;  
41 accountability; mandate from the industry; performance  
42 objectives negotiated with the Government, consistent with  
43 legal requirements and consistent with the guiding principles.

44 We wanted a board which achieved a high level of  
45 consensus; so we wanted a 75% majority.

46 A detailed proposal was made by consumers to the EGEC on  
47 the 16th of July 2001, and I think we attached that to the  
48 first submission by CC 93 to the Commission on 22 February,  
49 and it may be more appropriate -- although we're quite happy  
50 to deal with any questions -- to address that with CC 93

*Major Electricity User's Group*

1 tomorrow, although if there is any questions arising we would  
2 be more than happy to deal with it now.

3 **CHAIR:** It's just a question, tomorrow morning for CC 93, will  
4 that pick up MEUG's concerns as well in that presentation or  
5 are there points of difference; that's all?

6 **MR CURRIE:** I don't think -- I'm unaware of any differences  
7 between CC 93 and MEUG in terms of the decision-making  
8 processes.

9 **CHAIR:** Perhaps it might be better to do that tomorrow morning  
10 from a question and answer perspective, if that's okay.

11 **MR CURRIE:** Okay.

12 **MS REBSTOCK:** I did have one questions that I wanted to put to  
13 you as representing the major users, and that is the --  
14 several comments have been made by industry players that, you  
15 know, if you assigned executive decision-making rights to the  
16 independent board, you are basically interfering with the  
17 running of these very significant companies who report to  
18 their own shareholders, and I just wonder how many of your own  
19 members would allow them to voluntarily put themselves in that  
20 position where they gave over control of their companies to an  
21 independent board that was not accountable to their  
22 shareholders?

23 **MR CURRIE:** Well, in a sense the application does that, it  
24 actually gives the industry control to impact on my demand  
25 side participants. So, giving the power via a chapter-by-  
26 chapter vote has -- and in particular you go to chapters of  
27 the Rulebook where consumers don't have any votes at all, or  
28 certainly a minority or they can't -- they are unlikely to be  
29 able to uninfluence the outcome. So, it is a two-sided coin  
30 in terms of approach.

31 The supply side do not want an independent board to --  
32 which can impinge or make decisions which impact on their  
33 assets. The demand side probably would prefer an independent  
34 board with executive making decisions with a primary objective  
35 of enhancing consumer welfare than having an industry board  
36 which is capable of domination by the supply side.

37 **MS BATES:** Just taking that a bit further, because it was  
38 something that I was interested in, what arrangement you  
39 preferred; you'd prefer more to be part of an industry board  
40 with voting rights that you thought were appropriate? Your  
41 answer -- I'm sorry, I don't mean to put words in your mouth,  
42 but I had the impression before that you were in favour of an  
43 industry board with appropriate voting rights rather than --

44 **MR CURRIE:** With appropriate executive authority. The votes  
45 would only come back -- would be used as a backstop mechanism,  
46 not as a primary method of decision-making.

47 **MS BATES:** I see.

48 **MR CURRIE:** There is distinction. I don't want to belabour the  
49 point, but the difference, really, is between all votes, other  
50 than on matters of trivia, being virtually put out to the

*Major Electricity User's Group*

1 industry where the industry do have control via the chapter-  
 2 by-chapter voting mechanism, versus an industry EGB where  
 3 there is executive authority resident in the board but with a  
 4 backstop of a voting through process which is not -- which I  
 5 liken to the ability of a group of shareholders to perhaps  
 6 question the decisions of a board.

7 So, I was trying -- I do see those as quite different  
 8 models.

9 **MS BATES:** Yep, that's more clear.

10 **MR CURRIE:** And the new preference is for the first model, which  
 11 is the executive authority.

12 **CHAIR:** I mean, just a related question. I think Meridian in  
 13 their submission, which they will be tabling tomorrow, make a  
 14 fairly strong statement in relation to the industry EGB  
 15 interfering with asset values and so on, which I think is the  
 16 point you made as well.

17 I think Meridian make it much more starkly, it's one or  
 18 the other I think; but, anyway, they will obviously make their  
 19 own submission.

20 **MR CURRIE:** Yes, I noted there was a very strong statement from  
 21 Meridian which was that, you know, they couldn't conceive of  
 22 something along those lines, of consumers being involved in a  
 23 process whereby their asset values could be impacted.

24 **CHAIR:** It's a fairly black and white statement, as it were, but  
 25 it leads on --

26 **MR CURRIE:** Didn't they actually -- in another part of their  
 27 submission say they preferred a Crown EGB --

28 **CHAIR:** It was an alternative, I think, but we can explore that  
 29 with Meridian tomorrow, but the question it all leads to,  
 30 though, and you made the point in relation to some of the  
 31 large companies that are members of MEUG. Under a Crown EGB  
 32 you would have, in theory anyway, a Minister and/or a Crown  
 33 EGB board taking decisions that impacted on your assets or  
 34 Meridian's assets or anybody's assets.

35 **MR CURRIE:** But that is not too unusual -- there is nothing  
 36 different in terms of an operation operating within a  
 37 regulated environment on all sorts of fronts. So, as distinct  
 38 from an industry organisation, Mr Chairman, where the  
 39 suppliers or part of the industry can dominate the decision-  
 40 making or the rule making and rule changing processes, and I  
 41 do think there is a distinction between a Crown EGB making  
 42 decisions and Ministerial decisions, that's part of the -- I  
 43 suppose, the process of doing business in New Zealand that you  
 44 accept, you know, Government ability to legislate to enact, to  
 45 regulate. As distinct from letting a self-governing,  
 46 supposedly an industry self-governing arrangement where a part  
 47 of the sector has minimal ability to impact and protect its  
 48 own interests.

49 **CHAIR:** Although the point was made in a submission this morning,  
 50 quite strongly, that the system operator would indeed be a

*Major Electricity User's Group*

1 strong protagonist for the Crown EGB. Obviously, the system  
 2 operator may have a different view when they submit to us, but  
 3 if you follow that one through logically then you could have  
 4 one particular sector of the industry -- and I'm not taking a  
 5 view on it but it was argued to us -- having significant  
 6 influence over the Crown EGB which in essence has influence  
 7 over people's assets.

8 So, all I'm saying is, is the Crown EGB process and, as  
 9 I think you have said and others, one doesn't know what form  
 10 it will take or how it will be structured. From submissions  
 11 made by some parties it would appear that there is a  
 12 possibility that one or other interest group could capture  
 13 that Crown EGB and have similar impact on asset values or  
 14 whatever.

15 So I guess what I'm driving at is, at the end of the day  
 16 is that a risk in relation to the application as it is  
 17 currently framed -- and you made some suggestions as to what  
 18 might be alternatives -- and/or the EGB when we see it  
 19 develop, both having a strong influence on people's assets.

20 I mean, a formal Regulator, which has sort of been  
 21 sculling around the edges of this debate as you know, would  
 22 presumably, in developing a regulatory regime for the  
 23 industry, go through a fairly extensive process of  
 24 consultation and debate; I mean, we're doing the same thing  
 25 with thresholds on lines companies as you know.

26 **MR CURRIE:** And ODV.

27 **CHAIR:** That's right.

28 **MR CURRIE:** A number of new roles have been imposed or allocated  
 29 to the Commission to -- as a defacto -- well, not even as a  
 30 defacto; a Regulator.

31 **CHAIR:** The point I'm trying to get at, coming back to this one,  
 32 is that in the absolute, whether you can bullet proof either  
 33 an industry EGB or a Crown EGB from influence at some point  
 34 that reflects either a minority or a majority -- I won't say  
 35 abrogating, but influencing the value of assets of other  
 36 parties. That's all I'm saying.

37 **MR CURRIE:** I agree, Mr Belgrave. I don't think there are no  
 38 absolutes and not -- I think there would be concerns about a  
 39 Crown EGB, and that is not our first choice.

40 **CHAIR:** No, looking at your counterfactual, I wouldn't assume it  
 41 is looking at that.

42 **MR CURRIE:** So, there are risks. I think we're trying to ensure  
 43 that those risks are minimised.

44 **CHAIR:** I think, you know -- the debate we're having, I think, is  
 45 really teasing it out, and that's what it's all about.

46 **MS BATES:** Can I come back to your preferred option because I'm  
 47 still not sure that I've got it absolutely clear.

48 You prefer an industry EGB. Now, the membership of that  
 49 EGB, would it be independent members but sort of non-  
 50 representative as is contemplated at the moment?

*Major Electricity User's Group*

1 **MR CURRIE:** [pause]. I'm reflecting, just trying to avoid  
2 misleading you, Commissioner Bates.

3 **MS BATES:** I'm sure you are not intentionally misleading me.  
4 It's just that I want to be clear what you want.

5 **MR CURRIE:** At one stage of the process I think we argued for a  
6 MACQS type of governance or of representation, and I think we  
7 were looking for a nine person board with five -- a majority  
8 of five who were non-industry people, and we would have  
9 thought they could have been representative.

10 In one of the many compromises that we made, I think we  
11 did accept a board of seven independents. So, as long as the  
12 consumer sector could participate in the election process, and  
13 I think at that particular time we struck a, not a bargain,  
14 but we were looking for 50% of the votes on the election of  
15 the board in return for accepting seven person independents.  
16 Now, that little sort of bit of history still translates to,  
17 we would be happy with a seven independent strong board and  
18 have a strong preference for 50% of the votes in that election  
19 process.

20 **MS BATES:** That's clear now, but let's come to the decision-  
21 making ability of that board and how it ties back with what  
22 you call the backstop of -- I think you said a backstop, you  
23 may not have -- the voting rights. It wasn't quite clear how  
24 that would actually operate.

25 **MR CURRIE:** The seven person board would have executive decision-  
26 making authority. We would like to see that board achieve a  
27 high level of consensus in exercising those decisions, and we  
28 proposed a 75% majority. I think on a seven person board that  
29 means probably six out of seven have to agree to that  
30 particular decision.

31 However, as occurs in the MACQS and other governance  
32 structures that we looked at, there should be a call-through  
33 so that if the participants in the market -- the members of  
34 the arrangement -- sufficient numbers of those participants in  
35 the market in the arrangements were unhappy with a board  
36 decision they could call for a vote on a particular decision.  
37 So you would set a threshold; it may be 5% or 25% of  
38 participants in the market could seek a vote.

39 Now, this would be an all up vote, not a voting by  
40 chapter. That whole chapter-by-chapter voting would be  
41 euthanised, done away with.

42 **MS BATES:** Okay, I understand.

43 **MR CURRIE:** I hope I'm not belabouring the point.

44 **MS BATES:** No, I just wanted to make sure I was clear as to what  
45 you wanted.

46 **MR CURRIE:** Can I just -- in terms of efficiency of resources,  
47 why don't I pass over key issue number 6 to Mr Matthes.

48 I haven't given him any warning, so that's come as a bit  
49 of a surprise.

50 **MR MATTHES:** Thank you, Terrence.

*Major Electricity User's Group*

1           This section 6, basically I look at the claimed benefits  
2 and the estimated detriments, and then the summary of the net  
3 benefits and detriments.

4           Just to sort of background it. As you know, well, you  
5 are probably well aware, this whole issue of trying to  
6 quantify benefits and detriments is as much an art as science,  
7 and I certainly don't claim that the numbers in here that MEUG  
8 suggest have had any sort of robust calculations behind them  
9 at all. Rather, what we have tried to do is signal, perhaps,  
10 a couple of detriments that the Commission has -- might want  
11 to consider, and also aspects where we think maybe the order  
12 of magnitude might be in the wrong direction.

13           Let me go straight into paragraph 70. You will see the  
14 format here is exactly the same for all of the claimed  
15 benefits and detriments. What I've done is just worked out or  
16 just list the original applications; net present value  
17 estimate; what the Draft Determination estimated; whether  
18 there is a revision by the applicant; and MEUG's estimate.

19           The first claimed benefit -- this was a new one by EGBL,  
20 was the risk of a strike-down by the transmission and system  
21 operator. This wasn't identified in the Draft Determination  
22 but it's been suggested by the applicant subsequent to that.

23           Paragraph 73. We suggest that there are two flaws with  
24 this claimed detriment. First of all, any benefits and/or  
25 detriments with respect to the Transmission Asset Owner's  
26 decision-making, principally around new grid investment, has  
27 already been taken into account in the other benefits and  
28 detriments.

29           In paragraph 73 b), more importantly we suggest that  
30 Transpower -- well, the evidence is that Transpower acting as  
31 the system operator has in fact been more likely to advance  
32 pro-competitive changes to market design rather than delay  
33 those changes.

34           We've listed three examples there. First of all, the  
35 FTR product; second, the original promotion of nodal pricing,  
36 which Transpower have always been an advocate of; and,  
37 thirdly, the more recent ex-post five minute real time pricing  
38 indicator.

39 **MR CURTIN:** Could I just tease that out a bit more because what  
40 you have said in sub-points i), ii) and iii) is quite contrary  
41 to what we have heard from a variety of people up till now.

42           If you are looking at your paragraph b), in general I  
43 think the thrust of the study that Murray & Hanson did of what  
44 rules got out of the Rules process, to the extent that it  
45 identified pro-competitive rules that had been knocked back, I  
46 think a clear implication -- or their view was that some of  
47 them were blocked quite explicitly by Transpower for one  
48 reason or another, so that's a general point.

49           In terms of point i), I think we heard from Contact  
50 earlier today -- and I'm just really reciting things and this

*Major Electricity User's Group*

1 isn't obviously necessarily my own view, but they said that  
2 they were actually strongly in favour of FTRs and so are a lot  
3 of other people in the industry, it's just this design of the  
4 particular scheme they had issues with.

5 Similarly, on your sub-point iii), again we had evidence  
6 from Contact that they actually wanted to go beyond ex-post  
7 and go ex anti and have real time ex anti pricing, and we're  
8 actually disappointed with the progress Transpower made of a  
9 trial of ex-post pricing.

10 So, all I'd say is that, I mean, we've had a degree of  
11 evidence which is pretty much 180 degrees; somehow you've  
12 characterised things here and maybe you'd care to square the  
13 various circles for us?

14 **MR MATTHES:** Yeah, well I guess it's -- they are different  
15 viewpoints. Perhaps if I take FTRs for a start. I am  
16 certainly not defending Transpower in terms of the way that  
17 they may have managed the process. Perhaps they could have  
18 done it better in terms of their consultation over the actual  
19 FTR product itself, but my recollection is definitely that  
20 some of the suppliers, I'm not too sure whether Contact was  
21 one of them, were akin FTRs at the outset.

22 **MR CURTIN:** And point iii)?

23 **MR MATTHES:** Yes, this debate about ex anti and ex-post. I mean,  
24 I wasn't here this morning when Contact were giving evidence,  
25 but I suppose, are Contact suggesting that Transpower use  
26 their resources to thwart an ex anti type product?

27 **MR CURTIN:** That's the gist of it.

28 **MR MATTHES:** Yeah, look, I can't really -- it's just a different  
29 view, I think, in terms of which is the best product; ex anti  
30 or ex-post. I mean, personally in this market we've got an  
31 ex-post market, it just makes sense in terms of cost to go for  
32 this ex-post five minute price indicator trial.

33 **MR CURRIE:** Can I just add a comment in terms of subclause i),  
34 regarding FTRs, because in the notes for the Conference I  
35 think a letter from MEUG is incorporated in that as evidence  
36 of the concerns about the design of the FTR and the process  
37 that Transpower was embarking on.

38 As you would expect within MEUG, as within many  
39 organisations, there's quite a wide variety of views held by  
40 members and there is an ongoing debate about the effectiveness  
41 of or the appropriateness of financial transmission rights  
42 which may create a hedge for a transmission product if the  
43 market power inherent in the energy market is -- still exist.  
44 So there's an ongoing debate and I'm not too sure that it is -  
45 - we have not settled on a single position regarding FTRs.

46 I think that Transpower does take a very conscious  
47 position in terms of security, security is paramount for it,  
48 and over the last 14 years or so or more. They always want to  
49 see a very thorough work stream and analysis done on any of

*Major Electricity User's Group*

1 the issues, but they are more pro-competitive than I think  
2 they are being given credit for.

3 **MR CURTIN:** Thank you.

4 **MR MATTHES:** Just another comment on that. I guess you have to  
5 look at the incentive of the system operator relative to the  
6 suppliers. I mean, the system operator in their Statement of  
7 Corporate Intent is required to look after the national  
8 benefit as well as be a successful company. Whereas the  
9 suppliers, you know, their objective is to maximise their  
10 shareholder wealth. You know, can you rely on the self-  
11 interest of those suppliers as opposed to the system operator  
12 who has an economic objective, I guess?

13 **CHAIR:** Yes, well in fairness to -- Transpower has to make a  
14 return on its investments, so I guess there is some commercial  
15 objective there.

16 **MR CURRIE:** Yes, it does have an EVA of shareholders of zero,  
17 don't they?

18 **CHAIR:** That's right.

19 **MR CURRIE:** And those gains in excess of their target of return  
20 are put into essentially a stakeholder account and returned by  
21 way of a reduction in fees the subsequent year. That tends  
22 not to be the case in terms of a generator.

23 **CHAIR:** SOE or not?

24 **MR CURRIE:** SOE or not.

25 **MR ADAM:** Can I just ask Mr Matthes about the question of the ex-  
26 post or the ex anti market.

27 Did I take you to say that MEUG would prefer a five  
28 minute ex-post market, not a five minute ex anti market; and  
29 that the ex-post market is inherently more competitive than  
30 the ex anti market?

31 **MR MATTHES:** No, not inherently competitive; it's just an ex anti  
32 market or trial would have cost a lot more than an ex-post  
33 trial.

34 **MR ADAM:** But you are arguing in here though that, as I  
35 understand it, Transpower tends to promote pro-competitive  
36 rules as opposed to generators who tend to block competitive  
37 Rule changes, and that action -- an example of that the --  
38 Contact's promotion of an ex anti market is anti-competitive?

39 **MR MATTHES:** No, I think it came from Commissioner Curtin who  
40 said that -- I mean, there's an opposite view expressed this  
41 morning about whether or not this is an example of Transpower  
42 acting pro-competitively or whether Transpower sometimes goes  
43 off the rails and goes the other direction.

44 **MR CURRIE:** Or blocks or delays or defers.

45 **MR ADAM:** But I don't think you used this as an example of  
46 generators acting anti-competitively?

47 **MR MATTHES:** No, definitely not. This is an example of the  
48 system operator being pro-competitive, in my view.



*Major Electricity User's Group*

1 **MR CURRIE:** I wouldn't want you to take from that, that Contact's  
2 advancing an ex anti five minute -- that they are different  
3 propositions.

4 **MR ADAM:** Or alternatives?

5 **MR CURRIE:** Well, one would view them as alternatives but I just  
6 think that they are two examples. Contact advanced this  
7 morning that they have a consistent history of promoting pro-  
8 competitive rule changes. I think they instanced -- and the  
9 work done and the analysis undertaken by LECG, there were  
10 suggestions or commentaries which to an extent bagged  
11 Transpower or indicated that Transpower delayed, deferred or  
12 blocked pro-competitive rules, or that they were a factor in  
13 the pro-competitive rules not proceeding.

14 I think MEUG has just observed, I think we phrase the  
15 beginning of the -- that it is possible to argue that  
16 Transpower -- I think you actually -- we distinguish in a  
17 sense between Transpower as set owner and Transpower as system  
18 operator; we say that Transpower as system operator is looking  
19 and has looked in a number of instances, and we cite three, at  
20 pro-competitive activities.

21 **CHAIR:** Well look, we might just break now for 10 minutes to give  
22 our transcriber time to gather her breath again and starting  
23 again at 5.00. Thank you.

24 **Adjournment taken from 4.46 pm to 5.00 pm.**

25 **CHAIR:** In the interests of keeping the most important person,  
26 our transcriber, wanting to come back again we need to finish  
27 at 5.30. So, if we have to carry on tomorrow morning with  
28 MEUG we'll just do that. So back to you, Mr Currie or  
29 Mr Matthes.

30 **MR CURRIE:** The transcribers are as important as translators in  
31 the United Nations processes, and if one the translators  
32 decide they are not going to work any longer then the whole  
33 process comes to an immediate cessation, so...

34 **CHAIR:** We don't want that.

35 **MR CURRIE:** No.

36 **CHAIR:** All right, over to you.

37 **MR MATTHES:** The second claimed benefit that I deal with is the  
38 efficiency of the decision-making and in the generation  
39 market. This, of course, used to be the primary claimed  
40 benefit by the applicant before they discovered that the  
41 system operator was going to have -- strike-down pro-  
42 competitive rules. The table there illustrates the range of  
43 numbers, and you can see that MEUG says there's no benefit for  
44 this and in paragraphs 75 to 79 we go through the reasons why  
45 we don't think there is a benefit for the applicant's proposal  
46 relative to the Crown EGB counterfactual.

47 It's primarily around -- or the applicant suggests that  
48 this benefit arises because of the information advantage that  
49 an industry EGB would have relative to a Crown EGB.

**Major Electricity User's Group**

1           In our written submission on the 22nd of May we said  
2 that the Crown EGB would be able to match the industry EGB in  
3 terms of technical expertise, but over and above that the  
4 Crown EGB would actually have processes and informational  
5 advantage compared to an industry EGB in terms of assessing  
6 the national interest.

7           In paragraph 77 we present some new observations, which  
8 was really brought home by Professor Hogan, and I'll just read  
9 this. Professor Hogan in his evidence brought this issue into  
10 focus by noting that the information disadvantage observed in  
11 overseas regulatory regimes related to instances -- related  
12 to, the standard old rate of the term regulation, in CPI-X  
13 regimes.

14           Whereas what the Crown EGB will be doing is setting the  
15 overall conditions for generators and retailers to compete in.  
16 It therefore is not an argument about bilateral information  
17 disadvantage between a central agency and each company.

18           Professor Hogan said it a lot better than what I did.

19           At paragraph 78 we just go on to say that really the  
20 informational disadvantage that the applicant says the Crown  
21 EGB will have is actually information about the self-interest  
22 of those with voting rights in each chapter. Sure, a Crown  
23 EGB will not be able to assess what that self-interest will  
24 be, but I guess does that matter in terms of the national  
25 interest?

26 **MS REBSTOCK:** Can I just ask you a question. There must be a  
27 very large number of decisions that need to be made where the  
28 self-interest or the commercial interests of the industry is  
29 precisely what's needed for the -- or the knowledge associated  
30 with that will lead to very good outcomes in terms of the  
31 electricity market?

32           I mean, I take Professor Hogan's remarks as being that  
33 there are a minority of times where the commercial interests  
34 may have perverse results, but they are the minority; the vast  
35 majority of times an industry-led process will yield  
36 reasonably positive results; do you accept that sort of  
37 description?

38 **MR MATHES:** Yes, I do. You are absolutely right in terms of the  
39 majority of times I think that the industry -- I also mean  
40 consumers ' -- self-interest will make sure, as I think  
41 Professor Hogan said, sort of, "the truth will out", and we've  
42 experienced that in the MACQS arrangement in terms of the work  
43 of the Grid Security Committee, the Ancillary Services Working  
44 Group that I chaired, the current work of the Policy of  
45 Procurement Working Group. The people sitting around the  
46 table, that is suppliers and end consumers, have the technical  
47 knowledge of knowing what's possible and what's not; where is  
48 the technology going; what makes sense from a practical point  
49 of view and let's get on with it; and unwind, for example, the

*Major Electricity User's Group*

1 system operator's black box -- you know, we've all got the  
2 same incentive to get on with that job.

3 For the majority of the work there's just that plain  
4 technical, you might say boring, but necessary work that we  
5 get on with. It's actually in the more difficult decisions  
6 where I think this is where Professor Hogan said that, can you  
7 rely on just a partial sort of or subset of the stakeholders,  
8 namely the generators, acting in their self-interest to vote  
9 for the national interest? I guess that's what we're saying,  
10 is no.

11 **MS REBSTOCK:** How would you characterise that subset where the  
12 wider public interest becomes an issue? What are the exact  
13 areas that are covered by this application where you feel that  
14 the proposal -- that there would be difficulties in ensuring  
15 the wider public interest was served?

16 **MR MATTES:** If I take your question correctly, I think it just  
17 comes back to the discussion we had about our vision of a  
18 standard company corporate model, the board makes the  
19 decisions, it's accountable to its stakeholders which happen  
20 to be industry and consumers and I think it comes back down to  
21 that, doesn't it?

22 **MS REBSTOCK:** I understand the logic of how you got there; what  
23 I'm asking you is, what are the areas where -- what sort of  
24 decisions will there be affecting which parts of the  
25 electricity network where there will be a divergence between  
26 private interests of companies and the public interest?

27 **MR CURRIE:** Can I think of an example which we have already  
28 canvassed, or which has been canvassed to a considerable  
29 extent, is this bids and offers issue. The publication, as I  
30 think Contact described, from October 01, the start of the  
31 market, the stacks have been available, but some of the stacks  
32 are in blocks so it's not easy to actually identify who are  
33 the parties.

34 Given that we, you know, there have been concerns about  
35 gaming or the use of market power, the release of the identity  
36 of bids and offers we have seen as being a necessary element  
37 to be able to trace, monitor or expose the exercising of  
38 market power, and I think the evidence from LECG did track the  
39 time lag, the conflicting reports on pro and anti-competitive  
40 nature of those; the fact that in Australia bids and offers  
41 have been available from 24 hours after the event from the  
42 start of their market over there. That was an authorised or a  
43 regulated outcome that -- to prescribe or to publish bids and  
44 offers.

45 So there is an information area where we would say there  
46 are public interest issues involved in there. I think there  
47 are a range of other issues as well, which one could imagine,  
48 where the commercial interest of a number of the parties  
49 sitting around the table where they potentially could be  
50 impacted. I think there is an unrealistic expectation that

*Major Electricity User's Group*

1 those commercial interests will be set aside for a decision  
2 made in favour of the public good.

3 **MS REBSTOCK:** What about Part F? What's your view on Part F?

4 **MR CURRIE:** Part F is probably one of the most positive outcomes  
5 of the process because I think there is a general attitude,  
6 certainly within major users, that there has been under-  
7 investment in the grid and part of the blockage to investment  
8 has been the problem that no one is going to stump up, or  
9 there is not a full proof or bullet proof way of that  
10 investment in grid upgrades being recovered from the  
11 participants.

12 So, I'd have to say that the Part F process has  
13 generally been perceived by major users as a positive outcome,  
14 one of the most positive outcomes of the process that we've  
15 been engaged in.

16 **MS REBSTOCK:** What is it in the proposal that yields the change  
17 in result of dealing with hold-out? I mean...

18 **MR CURRIE:** Well, there is the identification of a discrete set  
19 of connected parties who, having examined all the options, the  
20 cost benefits, the market implications, the transmission and  
21 removal of constraints -- so all the technical information has  
22 been placed on the party. Then there is the prospect that you  
23 have a vote of those stakeholders, and there is the backstop  
24 that at the end of the process one can go to the Commission.

25 So, there's a whole series of changed circumstances  
26 which we believe, and I think a changing attitude towards the  
27 need for a mechanism to enable investment in the grid, the  
28 necessary investment in the grid to take place.

29 **MS REBSTOCK:** What about the concern about over-investment?

30 **MR CURRIE:** I have seen no evidence --

31 **MS REBSTOCK:** In the case of a Crown EGB?

32 **MR CURRIE:** Well, at the moment you have Transpower, since its  
33 separation it has been an SOE with a Statement of Corporate  
34 Intent. Even previously as part of ECNZ, I don't think there  
35 is very many examples that one can point to where there has  
36 been over-investment in the grid under the current model.  
37 Certainly that doesn't reflect Transpower being able to  
38 capture the high ground in its dialogue with Government and  
39 the Ministers.

40 So, we are less fearful of over-investment in the grid  
41 than we have been with under-investment and the fact that  
42 constraints now, I think in a recent report from the system  
43 operator to the Grid Security Committee, they pinpointed a  
44 particular stretch of line which had now been permanently  
45 constrained for 16 or 17% of the year and the implications,  
46 the nodal price implications, of that for consumers on the  
47 other side of that constraint are enormous to the extent that  
48 one of the major pulp and paper companies in New Zealand is  
49 contemplating not investing in New Zealand in the immediate

*Major Electricity User's Group*

1 future until that whole question of constraint and reinforcing  
2 the grid and removing those constraints is addressed.

3 **CHAIR:** So that puts some pretty strong incentives on the wider  
4 industry?

5 **MR CURRIE:** Yes.

6 **CHAIR:** In relation to that.

7 Just going back a step, I don't want to hold you up too  
8 long, but the other points you make in relation to 78 about  
9 who knows best about national economy; there then I just  
10 wonder, a Crown EGB, depending of course who's on it, but  
11 whether in fact it would be much more acknowledgment of the  
12 national interest and that an EGB industry with, from time to  
13 time, the Minister issuing either guiding principles or  
14 Section 26 or whatever. I'm not sure that the wise people on  
15 the Crown EGB will in practise be any better at it.

16 **MR MATTHES:** I guess a Crown EGB, you know, would have -- like  
17 any Central Government agency or Regulator -- would be  
18 properly resourced, would be accountable. I guess one of the  
19 arguments I come back to is, so too is an industry EGB. But  
20 the industry EGB, of course, gets its monies voted by the  
21 parties to the Rulebook, so there's a potential problem there,  
22 perhaps.

23 I think there is the lag issue, you know, when the  
24 Minister gives the industry EGB some objectives or goals or  
25 outcomes that they want, how does the Minister get -- arrive  
26 at those objectives and outcomes? Probably it's asking the  
27 industry EGB in the first case what they should be or does the  
28 Minister have a whole bunch of officials duplicating the work  
29 of the industry EGB?

30 I mean, I'm not too sure.

31 **MR CURRIE:** I think the response, Mr Chairman, really goes back  
32 to paragraph 74 where MEUG's estimate is, there is nil benefit  
33 and that -- so, we actually are not alleging that either the  
34 industry or the Crown EGB is going to have any better or  
35 more -- is going to produce a quantifiable benefit in terms of  
36 decision-making, one relative to the other.

37 **CHAIR:** No, that's fine.

38 **MR MATTHES:** My estimate of "nil" is, as I said right at the  
39 outset, plus or minus -- well, a little bit.

40 **CHAIR:** There are ranges in most of these estimates, as you know.  
41 That's fine.

42 **MR CURTIN:** Just one quick one on those numbers.

43 Again, this morning you probably heard Contact giving  
44 two examples of where they thought Crown direction of the  
45 industry had got it quite badly wrong: One was in terms of  
46 systematically over-optimistic forecasts of demand; another  
47 was pricing electricity higher to commercial users than to the  
48 voters, and in their original written submission Contact  
49 pointed to the fact that the hydro dams weren't built in the  
50 order of cheapest first but to some other criteria.

*Major Electricity User's Group*

1           So we just had evidence put forward today that actually  
2 there have been some fairly large instances of a Crown EGB  
3 wandering off on some strange mission of its own, or not a  
4 Crown EGB then, but the political input into the process at  
5 the time.

6 **MR MATTHES:** Sure, I mean -- but that's -- the whole world used  
7 to be like that. We're going back a couple of decades when  
8 you are talking about those examples. The word has moved on.  
9 This is now post-1996 and we now have a full nodal price  
10 market. I mean...

11 **CHAIR:** Some of those estimates, of many years back of ECNZ,  
12 electricity demand were quite frightening if they were to be  
13 realised but, as you say, it's some years back.

14 **MR CURRIE:** Most of those -- there were a number of structures in  
15 place. There were reports, annual reports released from your  
16 once upon a time Ministry who -- sorry, the Ministry was  
17 there --

18 **CHAIR:** It wasn't mine.

19 **MR CURRIE:** You played a not unimportant role in that Ministry,  
20 but there was a structure there, but if you recall under the  
21 old Electricity Act or NZED they had a statutory obligation  
22 that they had a surplus between the then predicted supply and  
23 demand and there was certainly a political implication when  
24 NZED was responsible for generating 96 or 97% of the energy,  
25 that brown-outs were not -- or black-outs were simply  
26 politically unpalatable.

27           In respect of the question raised by -- or comment made  
28 by Mr Curtin, I apropos the table placed in front of the  
29 Commission this morning by Contact relating to the removal of  
30 the cross-subsidisation between commercial and domestic  
31 customers. That was as a consequence of heavy breathing or  
32 table thumping by the Minister who at the time threatened to  
33 regulate unless the then electricity supply authorities, as a  
34 consequence of restructuring and their corporatisation of  
35 their restructuring and deregulation of the supply  
36 authorities, that they needed to address the question of  
37 tariff rebalancing, and there was an exercise undertaken -- I  
38 think the decision made by the early 90s, decision of the  
39 annual Conference of the electricity supply authorities to  
40 undertake a five year progressive rebalancing of the tariff.  
41 So, it was the threat of regulation.

42           The suggestion that it was a consequence of competition;  
43 there was simply no competition evidenced by customer  
44 switching for five or six years after -- for many years, a  
45 number of years after the tariff rebalancing was completed,  
46 and even then it was in the order of three or 4% customer  
47 switches per year.

48           So, as we all -- it may be that my memory has become  
49 particularly selective, but as I recall the tariff  
50 rebalancing, it was an initiative, not a pro-competitive

*Major Electricity User's Group*

1 response; it was really in the threat of regulation, or as a  
2 by-product of them being obligated to function in a commercial  
3 way with commercial objectives and no longer be independent  
4 upon the domestic electricity consumer for members to be re-  
5 elected to the constituent boards.

6 **MR MATTHES:** I think, also, we used to have a control and command  
7 regime in the electricity industry. As I said, the world has  
8 moved on. If you just look at some of the policy issues which  
9 recent Governments have looked at, we've had a Ministerial  
10 Inquiry, we've had the setting of a Government Policy  
11 Statement; all of those processes were very, very transparent.  
12 We all had an opportunity to make comments. That's the way  
13 the world now works. So, I think some of those examples from  
14 Contact relate to a different era.

15 **MS BATES:** Could I just ask you this. Given that you have said  
16 that you don't see any benefit or detriment, one way or the  
17 other, between decision-making and an industry EGB and Crown  
18 EGB with the Minister making the decision, why it is that you  
19 actually prefer the industry EGB?

20 One would have thought that the decision-making  
21 advantage might have been a factor, you might have seen it as  
22 a factor in it, but I'd like you to explain it because I'm  
23 slightly mystified.

24 **MR CURRIE:** It is a relatively fine call. There is -- and within  
25 CC 93 and MEUG I think there are a number of constituents who  
26 would be just as happy with a Crown EGB as with an industry  
27 led EGB with improved arrangements. I think also you have to  
28 look at -- I mean, what these paragraphs here were doing was  
29 commenting on the applicant's claim that there were benefits  
30 of an industry EGB relative to a Crown EGB.

31 We say, we don't believe that; in fact, we think that  
32 there are significant detriments because of the risk of  
33 strike-down of pro-competitive rules. So, I mean, they sort  
34 of --

35 **MS BATES:** Well, I'm still mystified then because I thought you  
36 had expressed a clear preference for an industry EGB over a  
37 Crown EGB.

38 **MR MATTHES:** Sorry, the industry EGB that we are using here is  
39 really the applicant's industry EGB.

40 **MS BATES:** I see.

41 **MR MATTHES:** Not CC 93's industry EGB, which is a totally  
42 different governance structure.

43 **MS BATES:** I see, so your comments are really confined to this --

44 **MR MATTHES:** Particular application, correct.

45 **CHAIR:** Well look, I don't want to draw things to a close but I'm  
46 conscious of the need not to over-work our transcriber  
47 because she's been at it since 9.00 in the morning.

48 I wonder -- there are a number of headings still, Ralph,  
49 that you've got to work through -- whether we should do those  
50 in the morning.

**Major Electricity User's Group**

1           We've got CC 93 to follow and then the Market  
2           Surveillance Committee at 10.00. Having got the Chair in  
3           from -- I think he lives out the Hutt somewhere or even  
4           further out, I think we have to meet with them at 10 o'clock.

5           **MR CURRIE:** We will accommodate Sir Duncan.

6           **CHAIR:** Is that okay?

7           **MR CURRIE:** Yes, not a problem.

8           **CHAIR:** And then Comalco, I think, 1.30 to 2.30 have to go in  
9           that block. But I think we'll play it as we move along, if  
10          that's okay.

11          **MR CURRIE:** We had planned and allocated all of Thursday the 20th  
12          being here anyway, because that's when we expected to be on,  
13          so we don't have a problem just fitting in with your -- in  
14          general respects, I'm not giving you total carte blanche.

15          **CHAIR:** I wouldn't ask that anyway.

16                 Okay, well, I think what say we draw the day to a close  
17          and we'll start again at 9 o'clock sharp and thank you very  
18          much indeed.

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**Hearing adjourned at 5.25 pm  
Resuming Thursday, 20 June 2002 at 9.00 am**

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**I N D E X**

Presentation by **CONTACT (Continued)**..... 1

Presentation by **NZ WIND ENERGY ASSOCIATION**..... 32

Presentation by **SUSTAINABLE ENERGY FORUM**..... 42

Presentation by **MAJOR ELECTRICITY USER'S GROUP**..... 59

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