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Dear Keston

Transpower Capex IM Review: Cross-Submission

Introduction

Thank you for the opportunity to participate in the Commerce Commission's (**Commission**) cross-submission process as part of the Transpower Capex Input Methodology Review.

Contact supports regulatory settings which promote the long term interests of consumers. We are therefore of the strong view that achieving a level playing field for non-transmission solutions will result in optimal outcomes for consumers of regulated transmission services. Accordingly we encourage the Commission to take a proactive approach in developing regulatory settings which facilitate such an outcome.

Contract duration is essential for non-transmission alternatives

We support comments made by IEGA, Pioneer and Trustpower (in respective order below) on the importance of contract duration to achieving a level playing field for non-transmission alternatives.

"Once signed up as an alternative to investing in transmission infrastructure, the cost of this alternative must be recovered in the same way as Transpower's transmission assets and for the life of the investment. The alternative forms part of the integrated transmission grid. The value of the alternative is not eliminated when the next tranche of transmission assets are installed even if that tranche of investment results in excess capacity."¹

"A third party trying to contract a transmission alternative solution to Transpower is very likely to have a higher WACC than Transpower. The third party is therefore at a disadvantage to Transpower's own investment – unless the contract with Transpower can provide a level of assurance for the third party"²

"The Commission should also consider the duration of the contracts Transpower is able to strike with the providers of transmission alternatives, and what types of projects are likely to be surfaced and supported with contracts of different lengths. For example, if Transpower is only able to offer the provider of a non-transmission a contract of (say) five years (until its next reset), this may not provide the certainty required by an investor in a new long-lived, capital-intensive asset such as a new power station."³

¹ <http://www.comcom.govt.nz/dmsdocument/15538> page 3.

² <http://www.comcom.govt.nz/dmsdocument/15535> page 3.

³ <http://www.comcom.govt.nz/dmsdocument/15533> page 2.

Transpower WACC impacts the competitiveness of non-transmission alternatives

Further to the comments we made in our submission, we support MEUG's position on the impact Transpower's cost of capital has on achieving a level playing field for non-transmission alternatives.

*"The largest incentive affecting Transpower's decision making for capex and opex is the uplift over the expected WACC, i.e. the difference between the mid-point WACC and the 67th percentile WACC... An investigation should be undertaken to consider if there are distortionary effect."*⁴

Wholesale spot market is not a substitute for network investment signals

We agree with the concerns raised by the IEGA on the Authority's view of the spot market's role in incentivising demand response at times of network peak demand.

*"The Authority assumed that distributed generators will still be incentivised to generate during periods of peak demand because that is when the spot price is high... More importantly, there is no proven correlation between high spot price and high demand"*⁵

In addition to the lack of correlation between spot prices and network peaks, we believe both networks and providers of network services (and certainly at this formative stage of the market's development) require a higher level of certainty than would be achieved through relying on a spot market or other market-based price signals to incentivise demand response. Reliance on a spot price is unlikely to:

- Provide networks firm, reliable capacity (especially with illiquid network services markets)
- Provide stable, long-term value to the provider of the non-transmission alternative, as value may be eliminated when the next tranche of transmission assets are installed

Transpower is currently incentivising providers of non-transmission alternatives through Grid Support Contracts and the Demand Response programme. Whilst we support these tools, we believe clarification from the Commission, the Electricity Authority and Transpower on the current and future role and objectives of these tools, as well as the wholesale spot market, would be beneficial for providers of non-transmission solutions.

Capex investment tests can ensure the most efficient transmission investments are made, including the use of non-transmission alternatives

Our submission⁶ advocated for the regulatory investment test to cover greater than approximately 20% of Transpower's capex (based on the current \$20m major capex threshold). We believe consumers would benefit from a more rigorous and transparent decision making process for a larger proportion of Transpower's capex spend, to ensure that lowest cost solutions are deployed for consumers. Further to our previous comments, we believe the Commission should carefully consider the costs and benefits of introducing greater transparency, and implement investment tests that are administratively suitable depending on the level of capex spend involved. As an example:

- For capex spend > \$20m - the current investment test could continue to be utilised;

⁴ <http://www.comcom.govt.nz/dmsdocument/15540> page 5.

⁵ Above n 1 page 2.

⁶ <http://www.comcom.govt.nz/dmsdocument/15539>.

- For capex between a mid-threshold and \$20m - a shortened form of the investment test could be utilised; and
- For capex between a low-threshold and mid-threshold - information could be provided on the Transpower website, including the technical characteristics that a non-network solution would be required to deliver, including the location, size, and profile of load reduction or additional supply.

Information asymmetry is required to support non-transmission alternatives

We support the comments made by Pioneer on the importance of achieving equal access to network information between Transpower and network service providers. We encourage the Commission to review tools which are being developed in other jurisdictions to achieve this objective, and to engage with Transpower and other stakeholders on the development and implementation of tools to support Transpower's use of non-transmission alternatives.

A proactive regulatory approach is required

The Commission should carefully review whether the approach to regulatory development advocated for by the ENA is in the best long term interests of consumers.

*"We therefore support the Commission aligning its approach to that used for the 2016 IM reviews, where changes to IMs would only be contemplated if there is clear evidence that the IM needed to be changed."*⁷

We believe this approach, which risks preserving the status quo and waiting for market failure before acting in the best interests of consumers, is at odds with the forward-looking approach being taken by regulators in other jurisdictions globally, including the AEMC and AER. We encourage the Commission to engage proactively with stakeholders towards developing market settings which drive efficient investment by creating a level playing field between networks and providers of network services. We believe a proactive approach is essential to ensuring the long-term interests of consumers of regulated network services are protected.

Projects Are Within Budget and On Time

We support comments made by Mercury⁸ and Meridian⁹ on the effectiveness of capex IM incentives - that there ought to be an incentive placed on Transpower to deliver projects within budget and on time. Timing has a large impact on demand growth and/ or generation build, and on the final cost of energy, which provides benefits to the end consumer.

⁷ <http://www.comcom.govt.nz/dmsdocument/15543>.

⁸ <http://www.comcom.govt.nz/dmsdocument/15537>.

⁹ <http://www.comcom.govt.nz/dmsdocument/15536>.

We look forward to continuing to engage with the Commission.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Louise Griffin', with a stylized flourish at the end.

Louise Griffin
Head of Regulatory Affairs & Government Relations