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Submissions
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SUBMISSION ON TPM WORKING PAPER - CBA

1 Orion New Zealand Limited (**Orion**) welcomes the opportunity to comment on the "Transmission pricing methodology: CBA" working paper (the **paper**) released by the Electricity Authority (Authority) in September 2013.

Introduction

2 The paper indicates that the Authority will release a new issues and proposals document in the future, and we will reserve our position on that until we have the full picture. In addition a number of other working papers are in preparation by the Authority. As such, our submission on this current paper is quite brief.

3 The paper is mainly directed at the way the Authority will carry out its cost benefit analyses (CBAs) in relation to TPM options. However, it also canvasses some of the wider matters raised in the original issues and proposals paper, submissions on it and discussion at the May 2013 conference. Our submission discusses these general points first before discussing the CBA framework.

General comments

4 *Presumption of inefficiency of current TPM*: para 2.2 of the paper states that "The Authority considers that the current TPM can be improved…". The weight of submissions so far is that the Authority has not made a compelling case that there is anything very wrong with the current TPM, or that the alternative would be superior. Moreover, whether there is a superior TPM is the question we are trying to answer by analysing alternatives. There can and should be no

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presumption that there is indeed a superior TPM available, be it a variant of the Authority's original proposal, or something else altogether.

5 *Decision-making and economic framework:* para 2.9 notes that the Authority will continue to be guided by the framework. We would judge that the framework has provided little useful guidance so far, and that there is no reason to believe that the situation will improve.

6 *Overview of submissions:* MC4 (page 7): we believe submissions were more that transmission *efficiency* effects, rather than *pricing* effects, are limited to timing and location of major investments. Has the Authority published the "initial analysis" referred to?

CBA Analysis framework

7 Overall the paper is proposing a more comprehensive approach to CBA than what was included in the 2012 proposal. This is certainly a welcome development.

8 However, there are a number of areas where we do not consider that the Authority's emerging thinking reflects or addresses the weight of submissions made so far:

- *The top-down approach was not specifically linked to the proposal*: As a number of submitters pointed out, the benefits were effectively just assumed, and what is more they could be assumed to flow from pretty much any proposal, not just the one put forward. We note in response to MC3 (page 7) that the paper agrees that benefits should not just be assumed, and in response proposes that benefits will "where possible…be quantified". We submit that quantifying and assuming are different things, and that the problem with the original proposal was that the method of quantification *was* assumption. We think the message from submitters was to avoid spurious quantification.

- *Static efficiency gains from changed use of the existing grid*: It is certainly conceivable that a different TPM could change the relative contribution of different generation sources. However, it is quite another thing to demonstrate that this is more efficient. The SRMC of transmission is already captured via nodal prices which reflect transmission losses and constraints. The changes that an alternative TPM might achieve would be generated by 'enhancing' those price signals, but to the extent that this drives a wedge between prices and costs it seems most likely that the outcome will be **less** efficient than the status quo. The way the paper is written it rather appears that any changes in the use of the grid will be seen as efficiency enhancing, which is circular.

- *Dynamic efficiency gains require a link to the investment decision-making process*: The paper very clearly (para 6.12) maintains the position that Transpower's price control / new investment decision-making, as administered by the Commerce Commission, is off limits in terms of the Authority's proposals. We are still unsure why the Authority is taking this stance, but given the weight of submissions suggesting that the Authority's original proposal was at best hopeful with respect to influencing future investment decisions, we believe that the Authority's new proposal will have to be very clear about *how* this will be improved when the Commission's process is not changing. Case studies based on recent significant investment decisions would be useful.

- *Dynamic efficiency benefits need to reflect an appropriate time-scale*: Even if a proposal gets over the previous hurdle, any benefits from improved investment decision-making need to be appropriately discounted to reflect that they will only arise from the date of the investment decision. As a number of submitters noted there are few significant transmission investments currently in the pipeline, and therefore few opportunities for the new TPM to deliver better investments in the short term.

9 These points can be summarised as a caution that the Authority must be very clear *conceptually* how it expects material benefits to arise from a proposed new TPM before it seeks to quantify those benefits.

10 We expect much of this will be further discussed in the Authority's working paper on sunk costs. We note in this regard that this is not just a question with respect to transmission assets: a significant proportion of the investment in New Zealand's generation capacity is largely sunk.

Concluding remarks

11 Thank you for the opportunity to make this submission. Orion does not consider that any part of this submission is confidential. If you have any questions please contact Bruce Rogers (Pricing Manager), DDI 03 363 9870, email bruce.rogers@oriongroup.co.nz.

Yours sincerely

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