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Submissions
Electricity Authority
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by email: submissions@ea.govt.nz

To Whom It May Concern

RE: TPM OPTIONS: TREATMENT OF LOSS AND CONSTRAINT EXCESS

On 16 June 2015 the Electricity Authority (Authority) released the *Transmission Pricing Methodology Review: TPM options working paper* (the "TPM Options Paper").[1] This is the latest of a series of working papers in the Transmission Pricing Methodology (TPM) review process.

The TPM Options Paper includes a proposal on the treatment of the Loss and Constraints Excess (LCE or transmission rentals). The Authority proposes to credit LCE against transmission charges as follows:[2]

(a) LCE attributable to an individual connection asset or deeper connection asset would be credited against the charges of customers that pay for that asset

(b) LCE not attributable to connection or deeper connection assets would be credited in bulk against Transpower's remaining MAR [(Maximum Allowable Revenue)].

The Authority has previously consulted on the treatment of the LCE.[3] In response to that consultation, Andrew Shelley Economic Consulting Ltd (ASEC) submitted that the LCE should continue to be allocated on a link-by-link basis, and thereby to the parties that pay for the asset.[4] The Authority's current proposal in respect of the LCE credit attributable to individual connection or deeper connection assets is therefore supported.

However, ASEC does not support the proposal to credit the remaining LCE in bulk against Transpower's remaining MAR. A key component of the proposed TPM Options is the Area of Benefit charge. A party paying for the Area of Benefit charge should also receive an LCE credit for those assets. The logic for this is essentially the same as the logic as to why those who pay for connection and deep connection assets should receive a benefit: if beneficiaries did actually

1 Electricity Authority, *Transmission Pricing Methodology Review: TPM options*, Working paper, 16 June 2015.

2 TPM Options Paper, p. 115, para B.8.

3 Electricity Authority, *Transmission pricing methodology: Use of LCE to offset transmission charges*, Working paper, 21 January 2014.

4 Andrew Shelley, "Re: Use of the Loss & Constraints Excess to Offset Transmission Charges", Andrew Shelley Economic Consulting Ltd, 3 March 2014.

club together to contract for an Area of Benefit asset, the option would exist for them to collectively own that asset and thereby receive the LCE that arises on the asset.

Note also that the larger the pool of beneficiaries paying for an asset, the less that the LCE credit could be said to distort the marginal price signal received by any given user of the asset. In any given half hour there is likely to be a significant difference between the beneficiaries assumed by the TPM and the actual users of an asset. Crediting the LCE generated on the transmission asset will ensure that the overall price levels for individual assets are correct over time, but will not alter the market price signals in a given half hour.

If the proposed TPM were to be implemented, this extension of the LCE credit to Area of Benefit assets would mean that Auckland and Northland would receive a the LCE for the central North Island and NAaN upgrades, and the relevant identified beneficiaries would receive the LCE credit for the HVDC.

Finally, the Authority has not identified a material problem with the current allocation methodology for the LCE, and there is no need to change it. Under the proposed TPM Options, this would mean that the LCE that arises on Connection, Deeper Connection, and Area of Benefit assets should be allocated to the parties that pay for those assets. The remaining LCE can be credited against the Residual charge.

Please do not hesitate to contact me if you have any questions about this submission.

Yours faithfully

Andrew Shelley
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