

Electricity Authority Board Members

c/- Submissions

Electricity Authority

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Submission on the DGPP and TPM proposal

Dear Board Members

A.D. Harwood Ltd is a family farming company based at Upper Takaka in Golden Bay. We farm sheep, beef, deer and dairy. We are in the final stages of installing a 420kW hydroelectric scheme.

The scheme was started in 2008 when we went through the consent process; this took nearly 4 years and included an irrigation project. In 2012 we installed a 100kW turbine on the end of our irrigation pipeline as well as installing 3 km of underground power cable and fibre to control the various parts of the scheme.

From September to December 2015 we installed 2.3 km of 1000mm GRP pipe from the intake to the station. In June 2016 we took delivery of 2 x 160 kW Francis machines and generators. This will take our max output from 100kW to 420 kW depending on machine performance.

The total cost of the scheme is approximately \$1.8 million. This includes consents (\$58k and lines, \$175k). The long term budgeted income was 8.3 cents per kW on 1.85 Gwh of output annually. We expected to receive about \$30k in ACOT payments annually making roughly a 10% return on investment. This investment decision was not taken lightly and was based on advice that the electricity industry is a long term low margin, but stable business. From 2008 to 2014 there was no suggestion to us that ACOT was being considered for removal, or worse that a 'charge' was being considered for Distributed Generators (DG) for common costs.

This submission will deal with the proposal as it directly affects us. AD Harwood Ltd supports the IEGA submission and we confirm that the PWC market impact review undertaken by the IEGA reflects the financial impacts on our generation project. We do not support the Electricity Authority's (EA) proposals for both DGPP and TPM for the following reasons:

Common Costs

Of all of the EA's proposals, this is the proposal that, if implemented by network companies will send us broke. By this we mean the investment will not cover its interest costs. It has been difficult to get a firm figure on the amount proposed to be charged, but information received gives a range of 2-4.0 cents/kW. The lowest figure represents 24% of our budgeted per kW income. This level of increased costs is completely unsustainable for our company. In fact few companies could sustain this sort of cost increase. The EA could not operate if they incurred 24% more costs in their operations without

increased income. Yet, this is exactly what they are proposing to do to us (with a 15 % cut in income with the removal of ACOT).

We believe the proposal is grossly unfair and anti-competitive. The EA argues that DG gets a free ride for distribution by not having to pay for the ability to generate into local lines. How is this different from the Grid Connected Generators (GCG)? The consumer pays nearly all costs associated with distribution but if this proposal proceeds, only DG will be charged for network access and not the GCG. This is despite GCG providing the vast majority of the electricity consumed in an area. If we take the Tasman area for example, the maximum demand is approximately 150mW. DG is approximately 35mW total, so the GCG will supply more than two thirds of maximum demand at up to a 25% price advantage compared to DG. This gives the GCG with their scale and retail operations a hefty competitive advantage. Why are we expected to pay common costs if the GCG get a free ride on the local distribution system? This is not a level playing field and it is disappointing to see the EA (which is charged with providing fairness and competition), promoting a change like has been proposed.

The common cost charge will especially disadvantage DG like us because 'run of the river' schemes like ours have high generation for short periods of the year based on river flow. In our case, less than 20% of the time at full output. This proposal would cause us to throttle back our total output by half so that total generation more closely matched what the river provides on average. Otherwise, we will be paying costs based on 420 kW peak output but supplying less than 50% of this for six months of the year.

ACOT

The EA seems to have a fundamentalist view to removing ACOT. We believe this view is not being applied consistently. For example, the EA supports network companies using load management tools to lower their peak demand from Transpower, but seeks to inhibit DG's ability to benefit from the same regulations. We acknowledge that the ACOT payments have lifted to a higher level than previously but this is due to the cyclical nature of transmission investments. This means that for many years ACOT prices were also on the low side of this cycle.

It should be acknowledged that this is normal for large infrastructures, due to the way the regulations are structured, and this approach has served the country well when managing large infrastructure systems like electricity and roading. ACOT could be regulated numerous ways without the need to remove it. For example, smoothed out over a 10 year period. This would ensure ACOT payments are paid based on a long run average, linked to the actual investment.

Transpower as gate keeper of ACOT

Giving Transpower the power to decide who gets ACOT is completely inappropriate without significant safe guards and appeal mechanisms for the smaller parties involved in the process. Transpower is a large monopoly that does not normally deal with DG. If there is not an incentive, regulated or otherwise for them to fairly assess when ACOT must be paid, then the default position is that it will not be paid. A proposal that will significantly remove such a large component of the smaller party's revenue needs a fairer and transparent system than what is proposed and this is actually why the DGPP were put in place in 2007.

We do not believe that Transpower has clear incentives to deal with small generators like us. Further, Transpower is not currently set up for its role in assessing whether ACOT payments should be made. Furthermore, if the EA proposes to shift the DGPP payment mechanism to Transpower, then it would also be appropriate to ensure the potential costs of ACOT payments are included in their revenue price path. Therefore if this part of the proposal is to proceed, it should not happen until Transpower is fully set up, with Commerce Commission approved revenue budgets, and resourced to correctly assess each individual DG fairly. This should include modelling of the new system to prove beneficial outcomes.

Conclusion

The common costs proposal of the DGPP will send our investment broke. We cannot afford to operate within the proposed costs. Had we known what was being proposed we would not have invested in our hydro project. These proposals unfairly favour the GCG at DG's expense. We are concerned with the EA consultation process when such a drastic and high impact change as this can be thrown into the proposal at the last stage, and without any supporting evidence in the cost-benefit analysis?

The proposal risks economically inefficient behaviours in that DG could be forced into local distribution and system bypass in order to return to profitability. The proposal is short on credible analysis and modelling of what the outcomes of the proposal will cause for the industry as a whole. The proposal shows a lack of understanding of DG benefits. The proposal requires monopolies like Transpower and the Network companies to engage with DG without any incentive to act fairly, or have a robust appeal system. A proposal for change of this magnitude should have a lot more evidence of surety before it is implemented. The proposal is especially unfair on 'run of the river' DG and those of us who have made recent investments in the industry. We believe the EA has gone into this proposal process with an end game in mind and have reverse engineered their desired outcome.

Regards

Nigel Harwood
Manager
AD Harwood Ltd

Other information

Our project:

\$1.8 million borrowed at 6.5% is \$117k per year interest

Annual generation projected 1.850 gW hours

Budgeted kW price .083 cents (budgeted 5 yearly average, somewhat less this year)

Total income without ACOT \$153k

Total income with 2 cents kW charged for Common Costs \$116k

Small hydro earns 8-10%. ACOT removal returns us to a break even position, the Common Costs proposal will kill us off.