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Network Tasman submission on the Electricity Authority's Consultation Paper – Transmission pricing methodology: 2019 Issues Paper, Supplementary consultation

28 February, 2020

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Dear Jean-Pierre,

This letter constitutes Network Tasman's submission on the Authority's TPM supplementary consultation paper.[1]

The focus of our submission is on the methodology proposed by the Authority's proposal to regularly update the residual charge allocation.

Authority recognizes that Transpower should have the ability to adjust the allocation of residual/benefits-based charges to account for a substantial change to demand due to factors over which they have no control.

For example, in the issues paper the Authority stated that to charge a distributor high charges, based on a high level of demand, when that level of demand no longer exists would be perceived as unfair (and so would undermine the proposed TPM's durability).

The Authority reinforces this view in the supplementary consultation, stating that consumer decision-making would be distorted and the durability of the TPM undermined if a region (served by a distributor) ends up making a disproportionally large contribution to the residual charge.

Network Tasman endorses this view. It is neither fair, efficient nor durable for the TPM to be specified in a way that enables a transmission customer incurring disproportionately large transmission charges.

Based on the Authority's current TPM proposal, a misalignment between the (historical) data that is used to calculate a distributor's residual charge, and that same distributor's actual circumstances, when they incur their transmission charges can occur in two ways.

1. Incrementally over time as a result of regular small but material changes in demand each year.
2. As the result of a single disconnection of significant demand; or

The Authority has sought to address both of these issues in the TPM, but Network Tasman submits there are gaps and inconsistencies in how they have been addressed.

[1] Electricity Authority, *Transmission pricing methodology: 2019 Issues paper – Supplementary consultation*, 11 February 2020.

Incremental change over time

The Authority didn't prescribe a regular adjustment process for the residual charge in the Issues Paper. Instead, it proposed that Transpower could update the residual allocator from time to time through an operational review of the TPM, using gross AMD lagged by ten years.

Having considered submissions on the Issues Paper, the Authority now proposes that the initial allocation of the residual charge is to be adjusted annually based on charges in the four-year rolling average gross annual energy use, lagged by seven years.

The driver of this change is the same as for adjusting the residual charge following a substantial change in an individual transmission customer's demand – to ensure that customers don't end up making a disproportionately large contribution to the residual charge.

As the electricity industry continues to evolve there will naturally be misalignment between a transmission customer's four-year rolling average gross annual energy usage, lagged by seven years, and their current average gross annual energy usage. What is not clear is the level of misalignment that occurs as a result of using a lag of seven years. The Authority states that based on recent patterns of growth in MWh, the absolute distributional impacts are small.

The implication of this statement is that the seven year lag does not pose a problem because the effect of it is small. If the distributional impact of the proposed methodology increases over time, it is not clear whether the Authority would consider this a problem, and if it did, how that problem should be addressed.

Network Tasman submits that the Authority should be explicit about what it considers the threshold under which the distributional effect is considered to be small, whether a distributional effect that exceeds this boundary is a problem and if so how that problem should be addressed.

Large one-off change

In the Issues Paper, the Authority identified that the TPM needs to be flexible enough to deal with circumstances where a distributor has experienced a significant reduction in load.

> Transpower should adjust the allocation where a customer has experienced a substantial change to demand due to factors over which they have no control. This principle is intended to allow, for example, a downward adjustment to the AMD of a distributor where a large industrial customer that was previously connected to the distribution network has closed down. An example is the exit of the Holcim cement plant, which reduced demand on Buller Electricity's distribution network. In our view, to charge such a distributor high charges based on a high level of demand, when the industrial customer that caused that level of demand has since closed down, would be perceived as unfair (and so would undermine the proposed TPM's durability).

The Authority drafted Section 41 of the TPM guidelines to address this issue where it relates to the residual charge. Section 41 is reproduced below.

> 41. The **TPM** must provide that, in initially allocating the **residual charge** under clause 40, Transpower may adjust the allocation where necessary to accommodate circumstances in which a designated transmission customer has experienced a substantial change in demand due to factors beyond their control or influence. For the purposes of this clause, a substantial change in demand is to be assessed relative to the designated transmission customer's remaining demand.

The reference to "initially allocating the residual charge" means that Transpower can only make an adjustment to how the residual charge is allocated if one of its customers experiences a substantial change to demand before the initial allocation is made. Once the allocation is made, there is no mechanism for adjustment.

This appears to be an oversight.

The inability to review the residual charge after its initial allocation is inconsistent with how the benefit-based charge is administered. Section 26(a) of the proposed guidelines states that Transpower may review the allocation of future annual benefit-based charges if it considers there has been, or expects there will be, a substantial and sustained change in grid use affecting one or more customers. Transpower's ability to review the benefits-based charge has no time limitations.

There is no reason Section 41 should be limited to the initial allocation of the residual charge. The Authority's reasons for allowing adjustments to how the residual charge is allocated become no less valid after the initial allocation has been set. Transpower should be able to apply an adjustment any time a customer experiences a substantial change in demand due to factors beyond their control or influence.

Network Tasman submits that Section 41 of the proposed TPM guidelines be amended so that Transpower's ability to amend the allocation of the residual charge is not subject to an arbitrary time limitation.

Network Tasman proposes Section 41 of the TPM Guidelines be amended as below:

> 41. The **TPM** must provide that~~, in initially allocating the~~ ~~**residual charge**~~ ~~under clause 40,~~ Transpower may adjust the allocation of the **residual charge** where necessary to accommodate circumstances in which a designated transmission customer has experienced a substantial change in demand due to factors beyond their control or influence. For the purposes of this clause, a substantial change in demand is to be assessed relative to the designated transmission customer's remaining demand.

Kind regards,

Daniel Vincent

Regulatory and Commercial Manager