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Submissions
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SUPPLEMENTARY CONSULTATION PAPER - TRANSMISSION PRICING REVIEW

Network Waitaki welcomes the opportunity to comment on the 2019 Transmission Pricing Methodology (TPM) Supplementary Consultation Paper dated 11 February 2020.

Our comments relate to questions 1, 4, 5 and 6 in the consultation paper regarding the annual benefit-based charge recovery, revised proposals on the residual charge allocation as well as the prudent discount proposal. This submission is in addition to the points we made in our submission dated 1 October 2019.

Q1. Should the annual benefit-based charges that recover the costs of post-2019 investments be set using DHC, IHC or some other approach?

An Indexed Historical Cost (IHC) is preferable considering the long-term nature of the transmission business. The benefit from an asset does not diminish with age of the asset when properly maintained, indicating that the depreciated value of the asset less accurately predicts the value of the asset and the benefit to consumers compared to the Depreciated Historical Cost (DHC) approach.

Under the DHC approach there is the possibility of price shocks when fully depreciated existing assets are replaced even though one could argue that beneficiaries have benefited from the previous lower depreciated asset values. DHC could have a place for some investments, e.g. in the scenario where a big upgrade is done for a large high-risk project. However, in our opinion price stability will generally be sacrificed if DHC is used.

Q4. Should the guidelines stipulate for regular updates to the residual charge allocation?

Yes, this is necessary because individual customer usage of the transmission grid will change over time and so costs need to be able to reflect changing usage patterns which may arise from growth, decline, or the application of new technology. This is especially relevant when considering decarbonisation.

Q5. If so, is the revised proposal an appropriate way to provide for such updates?

We support a change in the residual charge allocation to cater for changes in growth rates and changing demand profiles. However, we do not agree that the use of customers' gross annual energy usage (MWh) is an effective mechanism to achieve this. The initial allocation of costs is proposed to be based on Anytime Maximum Demand (AMD) which is MW base as this was seen to be 'hard to avoid' compared to the current Regional Coincident Peak Demand (RCPD) allocation method. We still believe that a co-incident demand-based allocation

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method is more appropriate and will send the correct signals around usage at peak demand periods. Both AMD and RCPD charges (MW based) are more cost reflective (share of assets utilised) if allocated correctly than energy volumes (MWh based).

Using energy volumes as the mechanism for adjustment would go against the Electricity Authority principle of moving away from volumetric pricing and would incentivise for example direct-connected industrial customers to reduce current energy consumption (or deferring decarbonisation initiatives) by investing in other technologies to lower their portion of the residual charge, leaving the remining users to carry the burden.

We acknowledge that the intention of the residual charge is not to provide any signal but rather be similar to a tax and that the expectation is that the residual charge would reduce over time with an increasing share of transmission charge being recovered via the benefit-based charge.

However, we contend that the impact could be severe, especially in initial years when this residual charge is a significant component of the overall charge as there will be absolutely no incentive for customers to manage peak demand, creating the potential need for premature investment in both networks and generation to meet peak demand or security constraints. As previously submitted, we believe there is an over reliance on nodal pricing to drive peak demand behaviours in the proposed TPM, and the residual charge cost allocation method should be based on a co-incident peak demand measure not energy volumes.

Furthermore, the proposed four to 7-year delay could be problematic for customers with irregular loads, rapid growth or decline, or those wanting to implement new technologies to smooth load profiles or reduce overall demand. For example, a short-term manufacturing operation in an Electricity Distributor's supply area could close down within the seven-year window, leaving other customers to carry the increased residual charge. The proposed four to 7-year delay between demand and pricing impact is an example of a measure that might look innocent enough on average but could have a big impact for specific users at certain times in history. Such measures should not be encouraged for use in pricing of services based on long life assets, where pricing miscalculations will be difficult to recover from.

We are strongly of the opinion that our earlier recommendation of a three year (or five year) moving average of a contributing measure such as Coincident Maximum Demand measured in peak and shoulder periods, for example, as a proxy of size, provides a predictable adjustment of contributions to mirror ever changing conditions. By increasing the number of measurement periods (from 100, say to 1000) will make it harder to avoid and achieving the Authority's desired outcomes.

Q6. Should a load customer be eligible for a prudent discount if it can establish that its transmission charges exceed the efficient greenfield standalone cost of supply?

We support and agree that a standalone cost is an objective measure to determine whether a customer is being overcharged. Although transmission, as a long-term fixed business, should not involve price shocks to any customers as there is enough time to recover the cost of assets from users this proposal is an important sanity check to ensure transmission prices are efficient.

Network Waitaki considers itself a case in point where the proposed TPM prices along with urgently required Transmission investment (increase in capacity on non-core interconnected assets in the Waitaki valley) will push Transmission charges well above standalone cost where bypass is a viable alternative.

We are however concerned about the practicality, cost and complexity that will be involved in preparing a prudent discount application as:

- Clause 6.18 refers to the high hurdle that applications will be subjected to which with no further clarification around the detail that will be required to overcome such a high hurdle;

- Clause 6.19 refers to the cost and effort that customers would face in preparing applications without further clarification of what this mean; and
- Clause 6.20 refers to the method to be included in the new TPM to determine stand alone cost without at least a broad outline of what the method might include.

We are thus supportive of the Prudent Discount Proposal concept but request that more clarity be provided on the detail to be included in a hypothetical case. For example, would a hypothetical case include equivalent provision of the current level of supply, or will current Transmission constraints and fixes that have been applied by the customer to overcome constraints and security issues be considered as well.

We have significant concern that the cost, effort, complexity and resourcing envisaged in preparing an application for a Prudent Discount would be unreasonable for a smaller customer (who is most affected by large movements in transmission pricing) to undertake. We see similarities with the process for applying for a customised price-quality path under Part 4 of the Commerce Act – the legislation provides a mechanism, however the work involved presents a very high hurdle and as such very few companies have actually benefitted from it.

For any questions or clarifications please contact Cornel van Basten, our Regulatory and Network Support Manager on cornelb@networkwaitaki.co.nz.

Yours Sincerely

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