TRANSPOWER
Keeping the energy flowing

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4th March 2014
John Rampton
Electricity Authority
PO Box 10041
Wellington, 6143

By email: submissions@ea.govt.nz

Dear John

Working Paper – Loss and Constraint Excess

We appreciate the opportunity to comment on the working paper *Loss and Constraint Excess (LCE)* published by the Electricity Authority (The Authority) on 21st January 2014. Our interest in this consultation is as Grid Owner and administrator of the TPM.

Use of Loss and Constraint Excess

In our submission to the October 2012 TPM issues and proposals consultation we did not support the proposal that LCE should be offset against specific assets. That was because we considered a direct asset-by-asset rebate would affect generator pricing decisions and compromise the integrity of the nodal price signal.

We are pleased to see that the Authority has, in the LCE working paper, recognised this concern and has accounted for it in its analysis of the three options it presents. We agree, conceptually, that the LCE should be thought of as a revenue stream, albeit a decreasing one over time[1], to recover some of the economic cost of providing transmission services. It follows that is should be a component of the maximum allowable revenue (MAR). On balance we support option 1 which is non-distortionary and likely to be the most administratively efficient and direct way to return the surplus to consumers.

However we consider that option 2, preferred by the Authority given its concern with wealth transfers between customers, would be acceptable although we note operational policy choices would be needed with this option. For example:

- the rules need to accommodate that since some connection rentals are negative then some connection parties will pay us LCE
- a decision is needed about how to treat LCE returns to connection asset customers if there are insufficient funds. Should connection rentals be paid in full and the MAR contribution reduced, or would the connection rentals be scaled to match the funds available (as occurs in the FTR market)?

[1] The available LCE is expected to decrease as the recent grid investment programme has eased constraints and because the LCE is the funding source for the expanding FTR market.

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Interaction with Commerce Act regulation

It should be recognised that the Commerce Act economic regulation applicable to Transpower is cognisant of the current TPM. For example, the IPP[2] recognises that we have two customer classes and corresponding revenue streams. Those are HVAC customers, who provide HVAC revenue through connection and interconnection charges, and HVDC customers, who provide revenue through HVDC charges. We are required to demonstrate compliance with our price path by showing that our forecast revenue does not in aggregate exceed our forecast MAR for the disclosure year. We do this by showing the revenue to be collected from the two customer classes.

All of the options proposed consider the LCE should contribute to the MAR in some way which means that whatever option is progressed will likely require consequential changes to the IPP to recognise the LCE as a revenue stream.

At this stage we have not scoped the changes required or discussed the issue with the Commerce Commission. The implications for Commerce Act regulation, which may also be triggered by other changes to the TPM, should be considered explicitly as part of any options assessment and factored into the cost benefit analysis.

Please contact me if you would like to discuss any of the points made in this submission. You can reach me on 04 590 7544 or jeremy.cain@transpower.co.nz.

Yours sincerely

Jeremy Cain
Chief Regulatory Advisor

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[2] Under the *Individual Price-Quality Path* regulation applying to Transpower.