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Andy Burgess
GM – Infrastructure Regulation Branch
Commerce Commission
Wellington 6011
By email: im.review@comcom.govt.nz

Dear Andy

Vector feedback on Transpower's capital expenditure input methodologies workshop

1. This is Vector's feedback on the Commerce Commission's (Commission) *workshop on Transpower's capital expenditure (capex) Input Methodologies (IM) Review* which took place on Friday 11 November 2022. None of this submission is confidential. We have structured our response following the same topics addressed in the workshop: investment test and evaluation criteria, resilience planning and climate change effects.

2. Whilst we welcomed the opportunity to attend online, the workshop demonstrated that a direct, in person workshop was advantageous to Transpower. The Commission was able to hear first-hand the issues raised by them in their response to the Process and Issues Paper (PIP), and Transpower was able to provide more detail and answer any questions posed by the Commission.

3. We struggle to see how the Commission could not facilitate the same levels of engagement with Electricity Distribution Businesses (EDBs) on certain topics of the IM review. For example, the Electricity Networks Association (ENA) could represent EDBs in a workshop to keep numbers low enough to hold an in-person meeting with the Commission.

4. We believe the workshop could have focused on the underlying issues such as what has changed since the last IM review, why has it changed and the impact on customers via prices and security of supply. Instead, it appeared to be a forum which addressed Transpower's issues with the regulatory process and how can it be changed to accommodate them.

5. From an EDB's perspective there appears to be a greater focus from the Commission on Transpower's issues, which was also demonstrated through a whole section devoted to Transpower in their PIP.

6. Transpower's RCP4 proposal will result in a significant increase in prices to its customers compared to RCP3.

7. We note the EDB IMs apply a 10% limit on annual increases in prices that is inclusive of pass-through and recoverable costs (including transmission charges). This means increased transmission charges could have a material impact on the ability of EDBs to recover their own costs.

8. We encourage the Commission to remain cognisant of the impact transmission charge increases could have on EDB cost recovery and ways to mitigate this. In our view, the EDB IMs should be amended to exclude transmission costs from EDBs' annual limit.

Investment test and evaluation criteria

Unquantified costs and benefits

9. In the workshop, Transpower argued that the Capex IM should not include arbitrary constraints such as the limitation that unquantified benefits are capped at "10% or less of the aggregates project costs". The Commission listened to the notion that the percentage should be considered on a case by case basis. It is our understanding that the process of calculating these benefits would be left to Transpower to demonstrate and for the Commission to sign them off.

10. Our view is that only through independent verification could this process be just and transparent. Both assumptions and methodology should be evidenced, and verification should happen early so customers and stakeholders can consider the proposals.

Forecasts and scenarios

11. We acknowledge the transition to net zero will likely require significant increases in expenditure for both Transpower and EDBs. However, the specific drivers underpinning Transpower's proposed RCP4 expenditure increase are not clear from their RCP4 consultation.

12. We would welcome more clarity on the following:

    - More granular information is needed on what investment is driven by demand growth and what is driven by the need to replace assets;
    - It is also not clear whether the proposed investment is based on a forecast that assumes high uptake of managed distribution energy resources (DER) or whether it assumes load is managed, either directly via smart algorithm or indirectly via behavioural signals (including pricing);
    - Some of the expenditure allowed for Transpower is the result of deferrals from the current regulatory period; it would be useful for EDBs to understand the risks those deferrals may have on distribution networks so they can be considered accordingly;
    - We would like clarity on the planning philosophy behind the expenditure increase (for e.g., maintaining N-1, or provision for transmission lines to connect PV in the north);
    - We would also like to understand in more detail both the location and timing of their investment requirements.

13. Specifically on scenarios, Transpower explained in the workshop that the prescriptive requirements for demand and generation scenario modelling, including the requirement to

model "all" the scenarios published by MBIE and "reasonable variation" have given rise to practical issues and would result in a modelling an excessive amount of scenarios and sensitivities.

14. For Vector it is not even clear what demand growth scenarios have been modelled and what sensitivity analysis has been undertaken (for example, different uptake of DER and whether these are orchestrated to minimise system costs) and which of these scenarios have been adopted.

Stakeholder consultation

15. Whilst we recognise that Transpower has held a webinar and requested written submissions on both their RCP4 proposals including service measures, Vector would welcome more direct engagement including Transpower's understanding of the impact of their proposals on the Auckland region.

Resilience planning

16. In the workshop Transpower proposed that the IMs should be flexible enough for the Commission to consider uncertainty mechanisms for the funding of 'proactive' resilience projects. Resilience is not solely an issue for Transpower. Vector and other EDBs have raised the expected increase in expenditure to address climate change adaption and the need to ensure networks are able to resist the effects of weather events of increasing severity.

17. Vector raised this in our PIP response in the context of Regulatory Asset Base (RAB) indexation. We stated that the IMs must be amended to ensure regulated businesses have sufficient cashflow to undertake efficient expenditure for the long-term benefit of consumers. In the current context, where significant upfront expenditure is required for the transformation of the energy sector and climate change adaptation, the existing IM risks jeopardising the delivery of the needed energy transformation.

Climate change effects

18. We agree with Transpower that a move towards a low-carbon energy system benefits consumers when you look at the whole system energy cost to New Zealanders. We believe that by supporting digitalisation and data transformation and other key enablers of decarbonisation, we are encouraging the long-term interests of "energy wallet" savings for customers.

19. Vector has long been advocating that achieving an efficient energy transition at least cost to consumers requires consideration of costs across the whole supply chain. A narrow focus on the cost impact on only one part of the supply chain (e.g. just distribution or just transmission) will not provide the true picture of the costs and benefits of a particular investment.

20. It is also important to bear in mind that the benefits of electrification extend beyond benefits to consumers in their capacity as consumers of the regulated service. Accordingly, we encourage the Commission to remain cognisant of costs across the energy system. Otherwise there is a

risk the real impact that potential IM changes (and resulting investment behaviour) would have on consumers in practice is not considered.

21. We encourage Transpower to pay close attention to how it can best utilise grid support technologies to manage peak demand. We recommend Transpower contract with distributors, DER owners, and aggregators of DER portfolios to provide services that assist Transpower avoid transmission investment. This could lead to significant cost savings over time.

22. Transpower believes that a strict market benefit test may not be flexible enough to consider wider NZ Inc. benefits such as Government climate change policy and CO_2 emissions, even if these benefits align with the long-term benefit of consumers. The Commission seems to be focussed on Transpower's ability to deliver these benefits when EDBs are clearly delivering them too.

23. In their final decision for the IM review decision-making framework[1], the Commission has noted the permissive considerations in section 5ZN of the Climate Change Response Act 2002, it has given itself considerable leeway to disregard those considerations if the Commission feels that they conflict with the Part 4 purpose.

24. Vector believes there is scope in the IM review and DPP reset to give consumers a greater voice through greater engagement with their willingness to address wider societal issues. Transpower cited these as consumer value propositions in their response to the PIP, a term adopted from Ofgem defined as "the ways in which their [regulated business'] plan goes beyond the minimum requirements and beyond the functions typically undertaken by an energy network company as business as usual and how this will lead to benefits for consumers[2]".

25. We are interested in the new mechanisms proposed by Transpower such as the use of 'use it or lose it' allowances for decarbonisation and sustainability projects and/ or programmes which respond to consumer value propositions. Vector and others have suggested the Commission consider the use of similar mechanisms or an enhanced innovation funding mechanism in the distribution sectors.

Yours sincerely

[redacted]

Richard Sharp

GM Economic Regulation and Pricing

[1] https://comcom.govt.nz/__data/assets/pdf_file/0034/294793/Input-methodologies-2023-Decision-Making-Framework-paper-12-October-2022.pdf
[2] https://www.ofgem.gov.uk/sites/default/files/docs/2021/02/ed2_business_plan_guidance_-_published_1_february_2021.pdf