

Rio Tinto Alcan New Zealand
Level 16, 2 Hunter Street
Wellington 6011
New Zealand
Postal Address:
GPO Box 1665
Wellington 6140
New Zealand
T +64 (0) 4 471 1527
F +64 (0) 4 472 8041

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Lisa White
Electricity Group
Energy & Communications Branch
Ministry of Economic Development

By email to electricity@med.govt.nz

Dear Lisa

SUBMISSION ON DRAFT GOVERNMENT POLICY STATEMENT ON ELECTRICITY GOVERNANCE

Introduction

1. This submission is made by Rio Tinto Alcan New Zealand Limited (RTANZ), on behalf of RTA Power (N.Z.) Limited and New Zealand Aluminium Smelters Limited (NZAS). It is made in response to the Minister of Energy's draft Government Policy Statement (GPS) on Electricity Governance of February 2009. Nothing in this submission is confidential.
2. RTANZ supports the changes in the draft Policy Statement, with the exception of two. RTANZ does not support the inclusion of paragraphs 87 and 88 on investment in minor transmission works in a GPS and for similar reasons, does not support the related amendments to paragraph 95.
3. To RTANZ' knowledge, no problem has been publicly disclosed that requires the sort of solution proposed in these paragraphs. Regardless, even if there is a real problem, trying to create a quick-fix with ad-hoc tinkering to the GPS is a very poor regulatory approach and only exacerbates concerns around the quality of governance in the sector.

Conflict with the Electricity Governance Rules

4. At a fundamental level RTANZ believes the GPS is the wrong vehicle for such a direction to the Commission. These two paragraphs appear to attempt to divide the Grid Investment Test (GIT) into two limbs along the lines of:
 - for investments with a total cost above the threshold (\$20m is proposed) use Test A;
 - but, for investments with a total cost below the threshold, use Test B.
5. This clearly suggests that it is the Electricity Governance Rules (EGRs) that relate to the GIT that should be amended and not the GPS.
6. In fact, these proposed amendments to the GPS set up another conflict between the GPS and the laws that the Commission must follow in the EGRs. It is RTANZ' view that the Commission should follow the law and thus the requirements of the EGRs have primacy over directions in the GPS.
7. However, Section 172O(j) of the Electricity Act 1992 requires the Commission to 'give effect to GPS objectives and outcomes'. It is this section of the Act that sets up the conflict between the GPS and the EGRs if they do not match-up exactly.
8. It is RTANZ' view that if the Commission follows the proposed amendments in the draft GPS, to the way the GIT is to be applied, then it will expose itself to judicial review for not following the GIT as set out in the EGRs. RTANZ has no doubt that the existing conflicts already significantly contribute to the complexity of the decisions that the Commission is being asked to make around approving transmission investments.

Role of the GPS

9. It is RTANZ' view that the GPS should be just that – a statement of Government policy. However, the GPS on Electricity Governance is much more than that – it is a detailed set of instructions that direct the Commission's actions, investigations and analysis. In particular, the GPS is becoming increasingly prescriptive over what the Commission must consider when evaluating transmission investment proposals. The proposed amendments to the GPS extend this prescription even further. Such prescription is not a role for a GPS – it is a role for legislation administered by the regulators of the electricity sector.
10. RTANZ has a growing concern about the repetitive amendments to the GPS. Such an approach undermines the credibility of the regulatory regime, increases uncertainty and ultimately reduces

investment. The recent LECG report¹ for Business New Zealand has some very relevant comment that is worth repeating here:

The policy shift required for successful regulation of market activities is to refocus regulatory tasks away from determining market outcomes and towards facilitating effective market processes. At the risk of over-simplification, effective regulation of markets should become less executive and more judicial, more legislative and more contractual in nature.

Against this backdrop, the former Ministers' of Energy conclusion that the GPS needed to be revised and expanded in 2002, 2003 (draft), 2004, 2005 (draft), 2006 and 2008 is illuminating; it suggests a much more fundamental problem than the particular symptoms addressed by each change.

11. The proposed insertion of paragraphs 87 and 88 into the GPS appear very much like an attempt to treat the symptoms of a problem that has yet to be publicly specified. RTANZ' view is that it is not appropriate to implement another ad-hoc intervention through yet another amendment to the GPS. As previously indicated, we doubt the effectiveness of this amendment to the GPS as it is in conflict with the rules and will therefore be problematic for the Commission to implement.

Roles of the Electricity and Commerce Commissions

12. It is important to note that the Electricity Commission's review of Grid Upgrade Plans was introduced to give Transpower revenue certainty. The trade-off was that major capital expenditure projects would be subject to technical and economic review under the GIT.
13. The Commerce Commission price regulation under the May 2008 Settlement Agreement with Transpower also provides revenue certainty for Transpower. However, in contrast with the EGRs, their review of replacement, refurbishment and enhancement capital expenditure looks at policy, processes and procedure and, if it is comfortable with these, accepts the outputs so long as the process for setting Transpower's business plan have been complied with. If the Commerce Commission is not satisfied that the policies, processes and procedures deliver least cost outcomes an adjustment can be applied which means that if Transpower spends more than the threshold value (currently \$1.5m) it cannot put those assets into the regulatory asset base and get paid for them.
14. The proposals in the draft GPS are in effect extending the approach taken by the Commerce Commission and applying it to the smaller grid upgrade projects. The objective for doing this is to streamline

¹ Page 10 of 'Determining outcomes or facilitating effective market processes: a review of regulation and governance of the electricity sector', 4 February 2009.

the decision making processes. It appears more logical for such an approach to fall under the Commerce Commission's jurisdiction rather than the Electricity Commission. Doing this would leave the Electricity Commission to undertake full and detailed reviews of the big picture and the big ticket grid expansion projects.

15. The approach described above still requires a solution for setting the threshold above which projects are to be submitted to the Electricity Commission for a full review using the GIT. One possible solution may be to use a logical decision tree rather than a specified dollar value. Our understanding is that currently Transpower categorises which regulatory regime a project falls under by applying criteria set out in a decision flow chart. Such a flow chart could be set out by the Commerce Commission and form part of the threshold compliance regime.

Recommended Actions

16. Firstly, and most critically, the problem that is being addressed needs to be clearly and publicly specified so that there is a wide understanding that a problem actually exists and that it needs solving.
17. Possible solutions to the problem then need to be developed and consulted upon. These are likely to cover the jurisdictions of both the Commerce and Electricity Commissions.
18. However, jumping to amend the GPS, as an easy quick-fix, is not an appropriate solution. It is likely to be much less effective than the Government thinks. But much worse is the negative signal it sends about regulatory stability and certainty.

General

19. We would be happy to discuss any questions or comments you may have in relation to the points made above. If you would like to discuss our comments further, please contact me.

Yours sincerely



Ray Deacon
Manager Regulatory and Government Affairs