Entrust
Majority shareholder of Vector

10 December 2018

# The Electricity Authority needs to operate smarter and make better progress on its work programme

Entrust isn't persuaded the Electricity Authority has justified its proposed 2019/20 appropriation of $74.936 million. It should be possible for the Electricity Authority to work within a lower overall fiscal envelope. Many of our comments in relation to the 2019/20 appropriations and work programme mirror the comments we made last year, reflecting how little has changed in the subsequent 12 months.

There is ample scope for the Electricity Authority to operate smarter, and progress its work programme more quickly and effectively.

The Electricity Authority needs to avoid being distracted by matters that benefit particular vested interests, such as the wealth transfers from consumers to Meridian and Tiwai under the transmission pricing methodology (TPM) proposals, and avoid lengthy intervals between consultations.

The length of time it is taking to progress and complete the TPM review may be the most extreme example of Electricity Authority's work programme management problems, but it is far from the only one. Projects cannot continue to be allowed to drift, sometimes for three or more years, without outward progress or stakeholder engagement and consultation.

Last year, we observed personnel expenditure had risen substantially. We didn't believe the increased staff resourcing had resulted in improved progress on the work programme or lower reliance on external consultants. The Network Pricing Manager role is presently filled by a consultant and the Electricity Authority has continued to use consultants for drafting consultation papers, a function which should be a core part of any regulator's competencies.

## Summary of Entrust's views

- *The Electricity Authority should prioritise addressing retail and wholesale market competition issues:* The growing size of the gap between the tiers in the retail market, the deterioration of hedge market liquidity and ongoing issues with spot market trading conduct are three issues which aren't being addressed in a timely manner.

- We recognise some of the Electricity Authority's work programme may be displaced by the Electricity Price Review. The Electricity Authority will need to consider the implications of the final review report for its work programme.

- *The Electricity Authority needs to be upfront and open about what it is doing:* For example, the Electricity Authority didn't notify stakeholders about its trip to the United States to investigate application of beneficiary-pays for transmission pricing until well after the trip took place, and has provided no information about the trip findings.

- *Inertia and poor project management remains a systemic problem:* There continues to be a lack of progress in the work programme, including projects which have been ranked as high priority. There shouldn't be gaps of three or more years between consultations.

- *The Electricity Authority performance is poor compared to the Commerce Commission:* The new regulatory framework for fibre legislation, reflects the Government has confidence the Commerce Commission can establish an entire new regulatory regime in little more than three years. This includes establishing input methodologies, information disclosure requirements and price setting. The Electricity Authority has not shown any sign it is capable of meeting strict deadlines like this. The difference between the two regulators' project management couldn't be starker.

- *The project performance targets are inappropriate and far too soft:* Instead of addressing the problems with ongoing project delays, and failure to meet targets in the work programme, the Electricity Authority has set itself soft performance targets. It is difficult to see how some of the targets couldn't be achieved. All the Electricity Authority has to do to meet its performance target for the hedge market enhancements project is evaluate options, within the next 20 months. The Electricity Authority doesn't even need to consult.

- *There is a lack of project budget transparency:* Despite repeated requests, the Electricity Authority continues to be unwilling to provide a breakdown of its budget and expenditure by individual projects, including standard project management information. The high-level breakdown of external consultancy budget into five generalised categories is wholly inadequate.

**Entrust is disappointed by the Electricity Authority's attempts to dismiss genuine stakeholder concerns on the basis of vested interests**

In the Ministerial Briefing on the 2018/19 Appropriations,[1] the Electricity Authority repeatedly claimed "mixed support" for its proposed budget reflected "the Authority's focus is on seeking better outcomes for consumers" and "vested interests implicit in individual submissions". This seems to be the Electricity Authority's stock response when stakeholders raise concerns about its work or proposals.

Entrust rejects the Electricity Authority's claims.

In Entrust's 2017 appropriations submission, we noted our submissions "are unabashedly beneficiary and consumer focussed".[2] Entrust was clear the Electricity Authority's work programme should be "consumer-centric and focused on ensuring more competitive pricing and improved service quality".[3]

As Pioneer Generation has noted "Entrust is in a unique position – not being a retailer with vested interests but a stakeholder with a pure focus on electricity consumers".[4]

Entrust's interest is in what is best for consumers. Consumer interests are not vested interests.

Entrust wants the Electricity Authority's work programme and expenditure to represent consumers' best interests, including the over 331,000 households and businesses in Auckland, Manukau and parts of Papakura and eastern Franklin that are beneficiaries of Entrust. As we noted in last year's appropriations submission: "We don't want to see the Electricity Authority's focus diverted away from consumers to the vested interests of individual market participants. Consumers come first, second and third in the Electricity Authority's statutory objective".[5]

[1] https://www.ea.govt.nz/dmsdocument/23835
[2] https://www.entrustnz.co.nz/media/65037/ea-appropriations-submission-18-dec-17-final.pdf
[3] https://www.entrustnz.co.nz/media/65037/ea-appropriations-submission-18-dec-17-final.pdf
[4] https://www.ea.govt.nz/dmsdocument/23934
[5] https://www.entrustnz.co.nz/media/65037/ea-appropriations-submission-18-dec-17-final.pdf

**Need for a shift in gear to focus on competition problems in the retail and wholesale markets**

The Electricity Authority is operating in somewhat of a vacuum. The Electricity Price Review covers a wide range of matters within the Electricity Authority's purview, and/or work programme.

By the time the 2019/20 financial year starts, the Expert Advisory Panel should have completed the Electricity Price Review and made recommendations to the Minister of Energy. These recommendations could impact on the Electricity Authority's work programme and priorities.

What is clear from the Electricity Price Review's initial consultation on problems in the electricity market is much greater attention is needed for problems in the competitive parts of the electricity market.

Structurally, there are problems with market concentration and retail-generation vertical-integration.

It is also clear there are problems with the deteriorating health of the hedge market, the two-tier retail market (saves and winbacks), and spot market trading conduct. The Electricity Authority should be prioritising resolution of these issues.

Electric Kiwi, Flick, Pulse, and Vocus, who combined represent 86% of the market supplied by independent retailers,[6] and Vector have also laid a complaint with the Electricity Authority about an Undesirable Trading Situation (UTS) which began on 15 September 2018 and was continuing as at 8 November 2018.[7]

The UTS complaint relates to several factors affecting the wholesale electricity market, including failure to meet market-making obligations in the hedge market, and use of market power to raise spot prices. The Electricity Authority will need to be clear about the extent spot prices rose because of genuine market conditions, and scarcity issues, or use of market power.

Regardless of whether the Electricity Authority deems this situation meets its subjective UTS tests, the matters raised in the complaint reflect problems with the state of competition in the wholesale market, particularly during periods of shortages, and inadequate regulatory settings for the hedge market.

**Examples of project inertia**

The Electricity Authority is continuing to make slow progress on its work programme and priorities. The reduction in the number of projects in the work programme may help, but the remaining projects need to be properly managed with clear project milestones, including targets for project completion.

The following two examples highlight the ongoing problems with project inertia:

- *Distribution pricing reform:* The Electricity Authority consulted on criteria for assessing distribution pricing in September 2011, then on a decision-making and economic framework (DMEF) for distribution pricing in January 2012. The DMEF hasn't been mentioned again apart from the Electricity Authority confirming it will apply an identical framework for distribution and transmission in May 2012.

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[6] Electric Kiwi, Flick, Pulse, and Vocus, Joint submission from independent retailers – delivering real competition for Kiwis, 23 October 2016: https://www.mbie.govt.nz/info-services/sectors-industries/energy/electricity-price-review/submissions/copy_of_submissions-received-epr/electricity-price-review-submissions-007.pdf

[7] Fonterra subsequently has asked to join the UTS.

The Electricity Authority subsequently consulted on the impact of evolving technology in November 2015, nearly four years later. It has taken the Electricity Authority over three years to produce the Distribution Pricing Principles consultation paper, and we are still waiting for its release.

- *Transmission Pricing Methodology review:* The Electricity Authority first consulted on the TPM in February 2011 and the review has dragged on for nearly eight years. The Electricity Authority has now released 15 consultation papers. The last consultation was two years ago, in December 2016.

  Based on the 2019/20 indicative work programme it could take the Electricity Authority nearly a decade to make decisions on amendment of the 19 TPM Guidelines. The more substantive task of developing and implementing a new TPM would then commence.

Both of these examples relate to network regulation which is the area where the Electricity Authority appears to have had the most problems. This is notable given the number of submissions to the Electricity Price Review recommending responsibility for all aspects of network regulation be transferred to the Commerce Commission.

### The Electricity Authority is setting itself soft performance targets

The ongoing and lengthy project delays resulted in the Electricity Authority failing to meet its 2017/18 target that 80% of top-priority market development projects meet all of their milestones.[8]

| DESIRED RESULT | TARGET | RESULT FOR 2017/18 |
| --- | --- | --- |
| Top-priority market development projects, as listed in the Electricity Authority Work Programme, achieve planned deliverables for the year.* | 80% of top-priority market development projects meet all of their milestones. | **Not achieved:** Six (75%) of our eight top-priority market development projects met their milestones for 2017/18. Further details are available in the 2017/18 work programme report.* |

The Electricity Authority's previous Chief Executive claimed earlier this year that the Authority "is progressing well on its comprehensive work programme, with significant work being done to reduce barriers to innovation" and "halfway through the current financial year ... we are tracking extremely well against the targets set".[9] It appears these claims were made off the back of soft targets in the Electricity Authority's work programme. The Electricity Authority set itself targets such as "Complete an analysis of the submissions on the issues paper", and "Start investigation".

Nearly a third of the Electricity Authority's targets for 2018/19 were simply to decide next steps. These don't require the Electricity Authority to deliver anything or make outward progress, as is evidenced by the notional "achievement" for the TPM review. The last consultation on the TPM was in 2016, and the next consultation won't be until sometime in 2019, yet the Authority claims to be "on track".

The situation is little different for the Electricity Authority's proposed 2019/20 key performance indicators (KPIs). Nearly a third are simply to start a project, start developing a consultation paper, or to evaluate options. None of these should require 20 months to achieve.

[8] Electricity Authority, 2017/18 Annual Report.
[9] https://www.ea.govt.nz/about-us/media-and-publications/market-commentary/outlook/authority-tracking-well-on-work-programme/

We want to see clearer signs from the 2019/20 KPIs that the Electricity Authority's is "setting more ambitious targets for our top priority projects".[10]

If the Electricity Authority is going to provide stakeholders with surety and confidence it will manage its work programme better, and projects will be completed in a timely manner, it needs to start issuing project workplans, which detail each of the project deliverables and milestones, including each of the planned consultation steps, and a project completion target.

Where a project isn't scheduled to be completed within the current or next financial year, there should be both intermediate progress KPIs and a set KPI for when the project will be completed.

**The Electricity Authority needs to be more upfront and open about what it is doing**

There is a lack of transparency about some of the work the Electricity Authority is doing.

It is unclear why the Electricity Authority didn't announce its intention to visit several United States' electricity system operators, the New York regulator and Professor Hogan, before the trip took place. The Electricity Authority has provided no information to stakeholders about the findings from the trip.

Another example is the study into lines company adaption to new technology. We understand this is being undertaken under the auspices of the Review of Distribution Sector project, which sat dormant on the Electricity Authority's work programme for seven years.

The only information provided about this study has been a letter to line company Chief Executives, and a reference to an "EDB survey" in the 22 November version of the Consultation Calendar.

The 30 June 2018 version of the work programme for 2018/19 vaguely stated "We want to assess, and better understand the factors which influence, the readiness and capability of EDBs to respond to technological change", and the Board would "decide on response to the review".

There have also been issues with lengthy delays between when the Electricity Authority receives submissions and when it publishes them. The submissions on equal access weren't published until 15 October 2018, seven months after the submission due date.[11] It wasn't until they were published that Entrust became aware our submission had been omitted and therefore wasn't available for the Innovation and Participation Advisory Group (IPAG) to consider. In Entrust's view, the omission of our submission is a clear breach of expected regulatory practice and we are concerned the views of IPAG could be irretrievably biased.

The Electricity Authority should proactively keep stakeholders up-to-date with initiatives it plans to undertake, or is undertaking, and publish all stakeholder correspondence.

**There is opportunity to provide better information, so stakeholders can fully scrutinise the Authority's appropriation proposals**

Information about cost and performance delivery is useful for helping determine whether the Electricity Authority is delivering value for money for consumers. There is opportunity for the Electricity Authority to improve transparency about its performance, and how effectively and efficiently it is operating.

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[10] https://www.ea.govt.nz/dmsdocument/23836-market-brief-24-july-2018#mctoc1

[11] Our letter to Chief Executive of the Electricity Authority "Omission of Entrust submission to IPAG on equal access", 3 December 2018, is attached.

The Electricity Authority has stated that it has changed budget and resource allocations in order to focus more on priority work, and deliver projects faster.[12] There is no visibility or transparency about these changes.

The Electricity Authority provided no breakdown of how it plans to allocate operating expenditure ($21.179 million) amongst each of the projects in the work programme.

All that was provided is a high-level apportionment of the $6.050 million budget for external work programme support costs between five groupings of the work programme, and "business-as-usual" activities.

We reiterate our request for the type of information the Electricity Authority provided for potential appropriation increases from 2021/22 for real time pricing (RTP), and to the Commerce Committee on budget versus actual expenditure for some projects,[13] to be provided for all projects, or at least all major projects, as part of the proposed appropriations. A number of other stakeholders have made similar requests to the Electricity Authority.

Information the Electricity Authority should have readily at hand, which we would like provided as part of the appropriations consultation and project management procedures, includes for example:[14]

- A breakdown of budgeted and actual costs for each project on an annual basis, and over the course of the project. This has only been provided on an ad hoc basis to the Select Committee on some projects in the past;
- The target completion date for each project. There is a lack of transparency about how long the Electricity Authority expects each project to take which makes it difficult to ascertain whether projects have actually been delayed and by how long;
- The length of any delays and not just whether a project has been delayed in a particular financial year; and
- Details of projects that have been delayed too offset cost overruns in other projects (if applicable).

**Concluding remarks**

Looking back at the concerns we raised last year about the Electricity Authority's work programme and appropriations, most of the concerns we raised remain:

- Entrust was unclear about what the Electricity Authority's priorities were, as we doubted all the projects listed as first priority had equal priority. The Electricity Authority has now replaced the priority categories with indicative net benefits. We assume this is intended to reflect the Electricity Authority's priorities.
- Entrust remains concerned about the lack of progress on many projects and priorities.
- Entrust remains concerned about the lack of transparency about how the Electricity Authority spends its budget on individual projects.
- Entrust considers a tighter, more focussed work programme should save money, but this isn't reflected in the Electricity Authority's proposed budget for 2019/20.

[12] https://www.ea.govt.nz/dmsdocument/23836-market-brief-24-july-2018#mctoc1
[13] Commerce Committee 2015/16 annual review questions 1 – 102 to the Electricity Authority, 15 November 2016, question 8.
[14] Entrust has also proposed the Electricity Authority provide this information in our submissions on the Authority's 2018/19 appropriations, and its Multiple Trading Relationships consultation.

The one area where there has been progress is in relation to the widely held concern there were too many projects in the Electricity Authority's work programme. This is a considerable and welcome shift from the Electricity Authority's position in February when it defended the large number of projects.[15]

While a tighter work programme is positive this needs to translate to faster completion of projects and more ambitious performance targets. Entrust questions the extent to which the Electricity Authority's has set "more ambitious targets" for its top priority projects. This is not apparent from review of either the revised 2018/19 work programme, issued in July, or the indicative 2019/20 work programme. Nearly a third of the KPIs in the 2019/20 work programme are simply to start a project, start developing a consultation paper, or to evaluate options.

There is also insufficient visibility or transparency about individual project budgets to verify whether the budget and resource allocation changes have been made, or whether this is reflected in the 2019/20 proposed appropriations.

**For further information, contact:**
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Kind Regards

Karen Sherry
**Chair Regulation & Strategy sub-committee**

[15] https://www.ea.govt.nz/dmsdocument/23833

Entrust
Majority shareholder of Vector

3 December 2018

James Stevenson-Wallace
Chief Executive
Electricity Authority
**Wellington**

cc John Hancock, Chair, Innovation and Participation Advisory Group

**Email:** james.stevenson-wallace@ea.govt.nz, john@hancock.co.nz

Dear James,

**Omission of Entrust submission to IPAG on equal access**

It has come to our attention that our April 2018 submission on equal access has not been published with other submissions and has been omitted from the Electricity Authority's summary of submissions. The submission was e-mailed to the Electricity Authority over 7 months ago on 5 April 2018, with receipt acknowledged the next day.

**Integrity of the Electricity Authority' process**

While we would hope the omission is an isolated case, it raises questions about the Electricity Authority's processes and the Equal Access review and consultation.

Entrust is concerned the Innovation and Participation Advisory Group (IPAG) has been deliberating on the equal access project which is a contentious issue, without the view of Entrust, an organisation that represents over 331,000 households and businesses in Auckland. This is detrimental to the review process as it means IPAG has not been able to give proper and due consideration to all submissions.

Many of our submission comments were time sensitive. Our comments on the scope of the project, including potential overlap with Commerce Commission processes, for example, were intended to help ensure IPAG started the equal access project with the right context and the review was tightly and clearly focussed.

We would like to understand how the Electricity Authority intends to remedy the omission of our submission. While the Electricity Authority can provide the omitted submission to IPAG (as well as on its website), and update the summary of submissions, this would not remedy the fact IPAG has been deliberating on equal access for the last 7 months without the benefit of all relevant information on stakeholder views. This is likely to create real difficulties in IPAG at this point giving full weight to those parts of our submissions that ought to have received timely consideration but haven't.

In Entrust's view the omission of our submission is a clear breach of expected regulatory practice and we are concerned the views of IPAG are likely to be irretrievably biased, consciously or otherwise.

## Timely publication of submissions is needed

The Electricity Authority has an established practice of publicly releasing submissions a considerable amount of time after they have been submitted. In this instance, submissions were released 7 months after the submission due date.[1]

Going forward, Entrust would like the Electricity Authority to commit to release all submissions within 1 or 2 business days of receipt. If cross-submissions were used as a standard part of the Electricity Authority's consultation processes, as they are with the Commerce Commission, the issue would also be less likely to have arisen.

## Closing remarks

Our concerns about ensuring the best outcomes for consumers has seen us increase our engagement on regulatory and policy matters in recent times, so it is very dispiriting to see our efforts seemingly wasted due to what appears to be poor Electricity Authority processes.

We look forward to your response, including how the Electricity Authority will ensure full and proper consideration will be given to our submission.

Yours sincerely,

William Cairns
**Chairman**

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[1] A similar issue arose with the submissions to the Market Development Advisory Group (MDAG). The delay in submissions being published, and an issue with date stamping on Trustpower's submission, created the impression Trustpower's submission was substantially late.