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**DRAFT DECISION REGARDING AN ALLEGED UTS ON 26 MARCH 2011 – TRUSTPOWER CROSS-SUBMISSION**

Reference:

- A. <http://www.ea.govt.nz/our-work/consultations/uts/26Mar11/>

Thank you for the opportunity to provide a cross-submission on the submissions and consultation document at Reference A.

As the Authority will be aware, TrustPower did not submit a UTS claim in response to the events of the 26<sup>th</sup> of March.

Having read other parties' submissions on the Authority's draft decision, TrustPower notes that there is a clear divergence of views between those that support the decision but generally believe the remedial offer price caps to be too high, and those that do not support the decision. In general, those that do not support the decision feel that the Authority's actions are setting a significant precedent for the future of market-based pricing. Those that believe the decision is correct feel that if the UTS claims are not upheld, the actions of particular generators on the 26<sup>th</sup> of March set a significant precedent for the future of market-based pricing. Whatever the final decision made by the Authority, market behaviour (and price-setting) is unlikely to continue as it has done in the past.

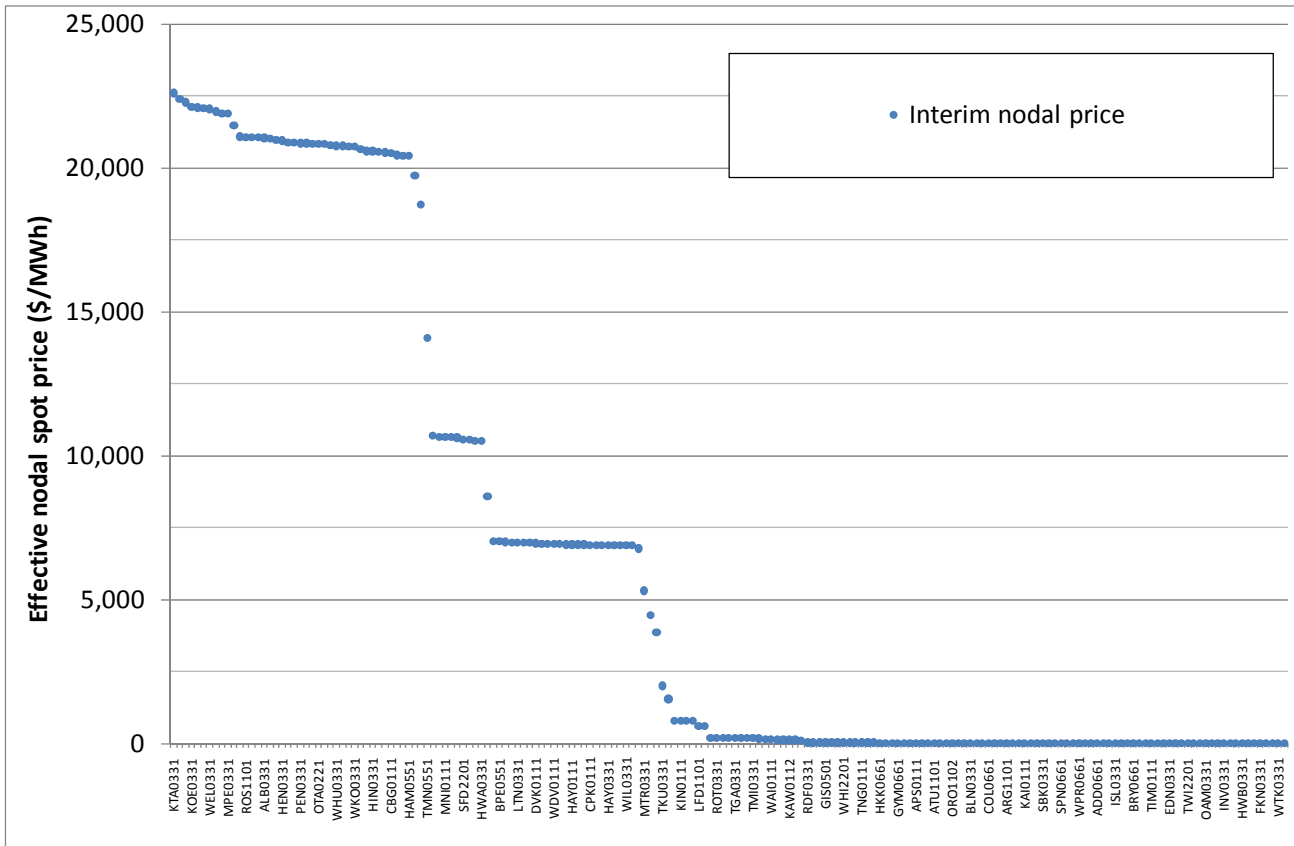
As TrustPower noted in its original submission, in principle it does not support changes to pricing model outcomes *after the event*. TrustPower also noted that a similar event in the past (albeit one that led to prices of only around \$5000/MWh) did not lead to UTS claims, hence must have been acceptable to market participants. Over the past few weeks TrustPower has therefore been considering other ways in which this particular situation could be remedied, without requiring any adjustment to the market-based pricing outcomes themselves. We have attempted to find a solution that not only leaves interim prices intact, thereby not altering the market outcome or penalising those parties that did act in response to the high-priced signals they saw, but also goes some way to dampening the financial impact on loads exposed to those prices.

**Allocation of the loss and constraint excess**

Based on the interim SPD results of the 26<sup>th</sup> of March, a total loss and constraint excess (LCE) of approximately \$95 million was generated across the 48 trading periods. This is the difference between what purchasers will pay for their electricity, and what generators will be paid. In contrast, the LCE for the 25<sup>th</sup> of March, a relatively "normal" day, was around \$160,000.

Approximately \$21 million of the total LCE is attributable to rentals across the HVDC link, determined by the price difference between Benmore and Haywards. Those rentals are paid directly to the South Island generators, as the parties that fund the link. The vast majority of the remaining \$74 million rentals would have been generated over the North Island AC transmission system.

Using trading period 28 on the 26<sup>th</sup> of March as an example, Figure 1 below shows the spread of interim prices across the country, sorted from highest price to lowest price.

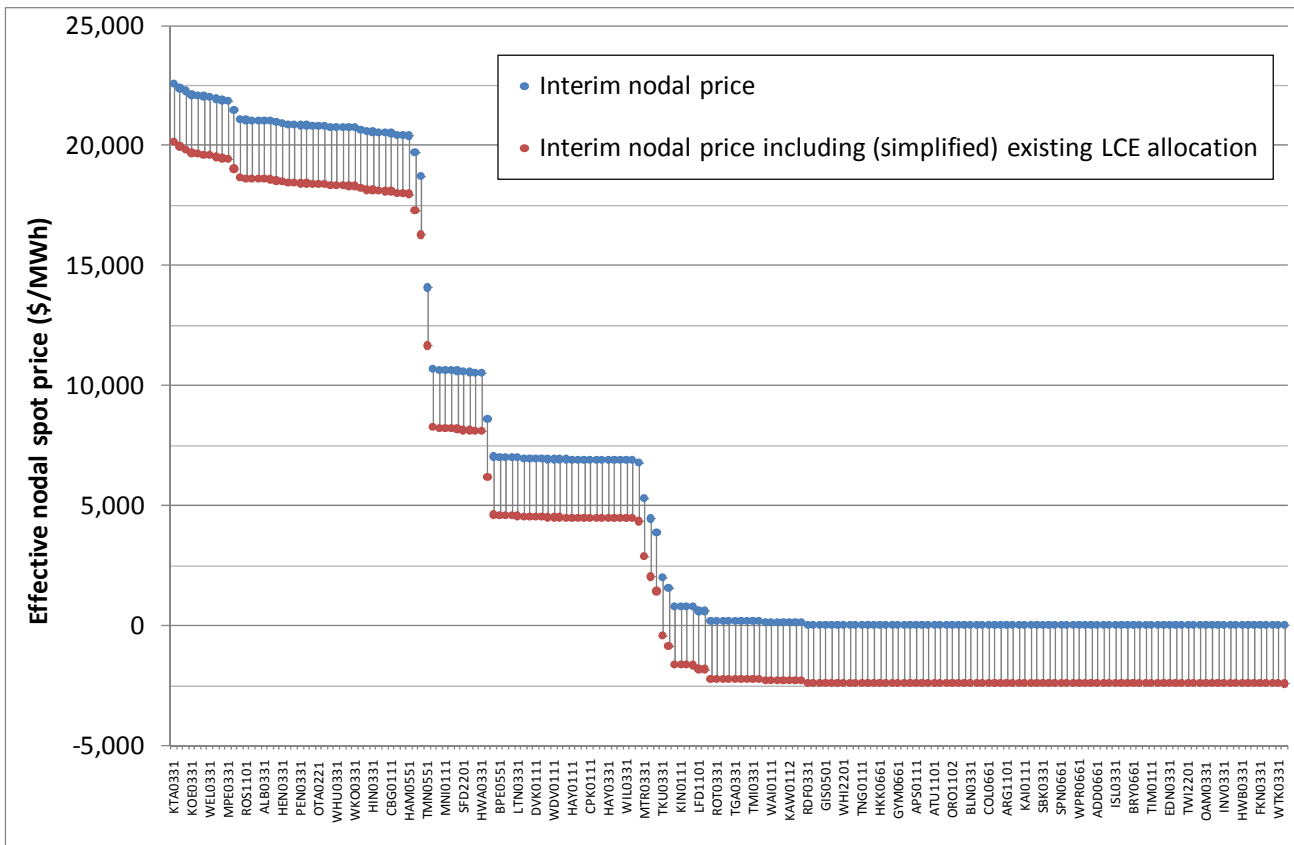


**Figure 1: Interim nodal prices for trading period 28 on the 26<sup>th</sup> of March, 2011**

A total LCE of approximately \$6.6 million was generated in this trading period, of which \$1.4 million was generated across the HVDC link. This leaves a total HVAC surplus of approximately \$5.2 million. It would seem both sensible and fair to somehow allocate it to those customers whose nodal prices were significantly increased on the day, in order to attempt to alleviate their financial losses.

For the sake of simplicity, one can assume that under the current LCE allocation methodology, customers across the country will eventually receive a share of the total LCE approximately in proportion to their load on the day. In reality, the methodology is significantly more complicated than this, but this assumption helps to illustrate the points made in this cross-submission.

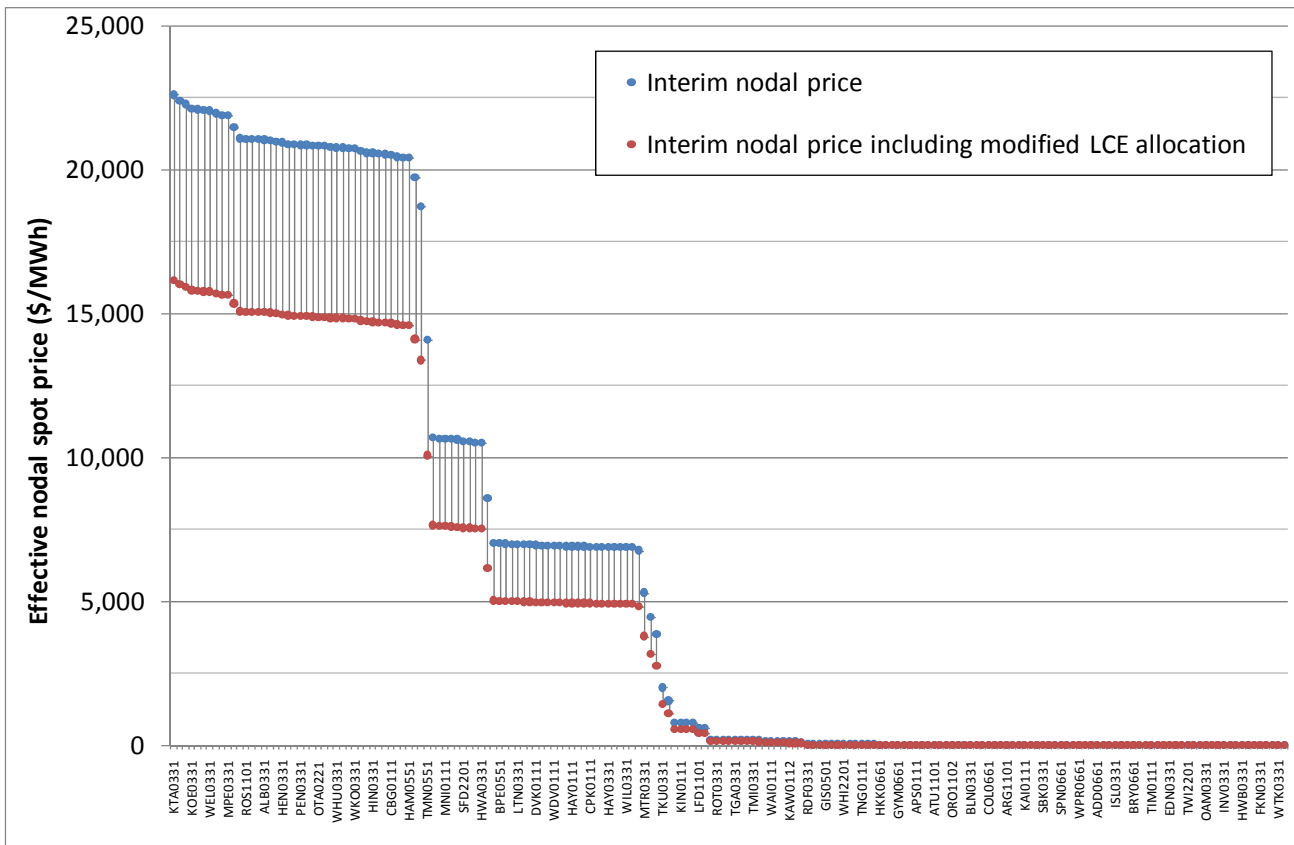
The key point about the existing methodology is that it is not targeted at those customers whose prices increase as a result of transmission constraints. Each MWh of consumption in a particular trading period receives approximately the same share of the LCE. Dividing the \$5.2 million AC excess by the 4300 MW (2150 MWh) of load during the trading period gives loads an equal share of \$2400/MWh. This leads to the effective nodal prices shown below in Figure 2.



**Figure 2: Interim nodal prices for trading period 28 on the 26<sup>th</sup> of March, 2011, showing the LCE allocation under the existing methodology, which is based on load**

Therefore, the existing method, which spreads the LCE across all loads in the country equally, leads to an equal decrease in effective spot prices across the country. Loads in the South Island, in particular, end up receiving around \$2400 per MWh of consumption, despite being unaffected by the transmission constraint in the North Island. Their effective nodal prices are approximately -\$2400/MWh. However, those North Island loads affected do receive some offset to their costs, reducing their effective nodal prices too.

If the Authority has the power to do so, it would appear both fairer and more sensible to allocate the LCE to loads based on the prices they were charged on the day. A proportional allocation is shown below in Figure 3. This leads to reductions in price of nearly \$6500/MWh for Kaitaia, \$6000/MWh for Otahuhu, \$3000/MWh for Stratford and \$2000/MWh at Haywards. This is a 28% reduction in prices right across the country.



**Figure 3: Interim nodal prices for trading period 28 on the 26<sup>th</sup> of March, 2011, showing the LCE allocation under proposed methodology, proportional to spot price**

The proposed methodology could be refined further by allocating the North Island LCE to North Island loads, and the South Island LCE to South Island loads. This would leave the South Island prices virtually untouched, while sharing the vast majority of the total LCE across the North Island. Another refinement would be to pay a greater proportional share to the loads north of Huntly whose nodal prices were highest, by increasing the weighting placed on the absolute level of spot price.

TrustPower notes that the effective spot prices including the LCE allocation shown above in Figure 3 are still very high. Therefore, the Authority may not consider this allocation a complete solution. However, as noted above, this proposal does have the advantages of neither having to adjust market prices after the fact, nor penalising those parties that did act in response to the high-priced signals. If the Authority does still decide to cap Huntly's offers, it could still lessen the overall impact of the event on North Island loads by adopting the LCE allocation methodology proposed.

Please note that in this cross-submission, TrustPower is proposing this allocation method for the LCE generated on the 26<sup>th</sup> March as a possible remedy to the UTS. TrustPower's views on the suitability of the existing LCE allocation methodology going forward may be found in its submission to the Authority's recent consultation on the implementation of financial transmission rights, which closed on the 12<sup>th</sup> of May.

Please get in touch if you have any questions regarding this cross-submission.

Yours faithfully,

**Therese Thorn**  
**GENERAL MANAGER TRADING**