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WAG Chair
c/- Electricity Authority
2 Hunter Street
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By email: submissions@ea.govt.nz

Dear John

Instantaneous Reserve Event Charge and Cost Allocation

Genesis Energy Limited welcomes the opportunity to provide a submission to the Wholesale Advisory Group (“the WAG”) on the Discussion paper “Instantaneous Reserve Event Charge and Cost Allocation” dated 11 October 2016.

Considering costs and benefits beyond the IR regime

Genesis Energy supports the WAG’s principled review of the instantaneous reserve regime, and appreciates the WAG’s willingness to engage with sector participants to develop a balanced understanding of the current IR market. We also agree that a change to the IR cost allocation methodology is needed to promote causer-pay principles under the new national market for instantaneous reserves (NMIR).

Whilst we appreciate the impact of any proposed changes to the IR regime will be difficult to predict, we believe consideration of changes to the IR regime in isolation, without carefully considering the cost to efficiency in other markets, will not promote efficient operation of the electricity market *for the long term benefit of consumers*. We do not support the pursuit of efficiency gains in the IR regime where these efficiency gains will not be realised in a net reduction in the energy price. The impact on the end consumer must remain a key consideration for any proposed change/s.

Our preference is for the WAG to pursue a simple, timely solution, which is targeted to the existing problem. A complicated cost allocation method is likely to result in greater uncertainty for participants, be costly to implement, and simply add another layer of unnecessary complexity to the electricity market for little or no benefit to the end consumer.

If you would like to discuss any of these matters further, please contact me on 04 830 0015.

Yours sincerely



Victoria Parker
Regulatory Advisor

Appendix A: Responses to Consultation Questions

QUESTION	COMMENT
<p>Q1: Do you agree with our identification of the problems with current arrangements?</p>	<p>Yes, however in regards to the question “what aspects of the IR cost allocation arrangements may be resulting in inefficiencies?” - the question suggests treating reserves in isolation. Gaining efficiencies in IR cost allocation but incurring (potentially greater) inefficiencies in the energy market will be missing the mark of achieving the Authority’s statutory objective - competition in, and reliable supply by, the efficient operation of the electricity industry <u>for the long-term benefit of consumers</u>.</p>
<p>Q2: Do you agree with these basic principles for allocating IR costs?</p>	<p>Agree.</p>
<p>Q3: Do you agree that continuing with island-based cost allocation after the introduction of the NMIR is unlikely to create perverse incentives on parties to inefficiently withhold energy or IR capacity?</p>	<p>Agree.</p> <p>However, the end goal of NMIR should be a well-functioning and efficient national reserves market that delivers a better (least overall cost) outcome for the consumer.</p> <p>We believe there should be greater urgency to move towards a cost allocation regime that is fair and straightforward in a timely manner, rather than continue with island-based cost allocation just because it creates no perverse outcome.</p>

QUESTION	COMMENT
<p>Q4: What are your views on the merits of moving to a runway methodology (or its sub-options)?</p>	<p>We do not agree moving to a runway methodology or its sub-option will be viable.</p> <p>Moving to a run-way method for existing plants will result in the largest thermal unit(s) being offered at lower levels at the times of highest reserves (and energy) prices. Out of the various options, the grand-father approach will at least address this concern.</p> <p>However, we feel this point raised is not related to achieving a solution for National Allocation of Reserves, rather a fundamental reserve market design question.</p>
<p>Q5: Do you agree that a de minimis should continue and, if so, at what level?</p>	<p>If we are to move to a run-way method, the de minimis should be reduced (OMW). If not, the causers will be doubly penalised. On top of getting its 'fair' share of IR costs, the smaller generators are also completely exempted.</p>
<p>Q6: Are there other cost allocation options that you think should be considered?</p>	<p>No.</p>
<p>Q7: Which option do you think sends price signals to underlying causers of the need for, and location of, IR to be procured in a manner which best meets the cost allocation principles of section 5?</p>	<p>The options that had been indicated to be 'better' (cost-to-island-causer) and 'best' (cost-to-HVDC-then-to-AC-island-causers) are difficult to understand. We fail to see how increasingly complicated solutions, which are not easily explicable for participants of the WAG with in-depth market experience, will send price signals to the underlying causers; particularly when they may not be well understood by the traders who will be making decisions on plants.</p> <p>Option 3 "C" is our preferred option.</p>

QUESTION	COMMENT
<p>Q8: Do you think the choice of general cost allocation approach (i.e. pro-rata versus runway) has a bearing on which option for cost allocation under the NMIR would be most appropriate?</p>	<p>There will be supporters for each general cost allocation approach, and there will be (potentially different) supporters for each cost allocation option.</p> <p>To simplify things, these should be kept separate and not impede the implementation for an efficient national cost allocation solution.</p>
<p>Q9: To what extent do you think the choice of best option is affected by the effectiveness of how costs allocated to the HVDC are passed-on to 'underlying causers' of the level of energy transfer across the HVDC?</p>	<p>We believe this should be considered to a large extent if we are to pursue a 'causer pay' approach.</p>
<p>Q10: Do you believe that some IR cost allocation options could materially impact on participants' incentives to offer energy and IR to a degree that could have material outcomes on these markets?</p>	<p>Different IR cost allocation options will likely lead to different outcomes that could be material. It will be hard to predict what each participant will do, so demonstrating such effects will be very difficult.</p> <p>On this basis, we believe a simple, cost reflective solution which broadly and fairly allocates costs is most likely to achieve the desired outcome and align with the Authority's statutory objective.</p>
<p>Q11: If yes, which options are likely to give rise to such outcomes, and could you provide worked examples demonstrating such effects?</p>	<p>See Q10.</p>
<p>Q12: Do you agree that HVDC-related IR costs should continue to be allocated to the HVDC owner and passed-on to market participants via the TPM, and do you have any observations about the interim allocation of IR costs under the NMIR?</p>	<p>Key decisions are yet to be made in regards to TPM which will affect the degree to which this approach will reflect the 'causer pay' principle. Ultimately it will leave the allocation to the TPM, which may not follow the same principles set up under the NMIR.</p>

QUESTION	COMMENT
<p>Q13: Do you think cost-allocation for commissioning plant should: a) continue as is; b) change to be quantity-and-price-runway-based without application of a de minimis; or c) change to be quantity-runway-based without application of a de minimis?</p>	<p>Option a, continue as is. Commissioning of large thermal plant is extremely unlikely in the near future.</p>
<p>Q14: Do you think a change to allocating costs to commissioning plant on a runway basis should only occur if general cost allocation were to move to a runway basis?</p>	<p>As above; we do not believe there is sufficient premise to support further investigation and changes to cost allocation for commissioning plant.</p>
<p>Q15: What cost-allocation approach do you think should apply for plant with under-frequency and voltage-fault-ride-through dispensations?</p>	<p>We support the existing arrangements.</p>
<p>Q16: What measures do you think should be implemented to address small generation plant that are currently excluded from the need to comply with frequency-related AOPOs?</p>	<p>Our preference is Option 3 or 2 (to cover 10MW onwards or even less). The implementation cost should not be high as these options will be extending an existing methodology.</p>
<p>Q17: Do you think the event charge should be retained, and if so, on what basis?</p>	<p>We do not support retention if there is no compelling case to keep it, particularly if the number of events has been very low.</p>