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TRANSPOWER

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Submissions
Wholesale Advisory Group Chair
c/o Electricity Authority
Wellington 6143

By email: wag@ea.govt.nz

Dear John

Instantaneous Reserve Cost Allocation and Event Charge

We welcome the opportunity to provide feedback to the Wholesale Advisory Group (WAG) discussion paper released 11th October 2016.

We appreciate the thoroughness of the paper in describing the development process (both for instantaneous reserves and the event charge), and the analysis of the likely efficiency and distributional effects of changing the cost allocation. We also consider the decision by the Authority to refer back to the WAG was sensible after issues raised by submitters on the Authority's consultation in August.

Our submission focusses on two main aspects:

- The analysis to support the event charge conclusion
- A preference for incremental and proportionate change for cost allocation.

Make event charge analysis transparent

We support the WAG consideration of whether the event charge is still necessary given the presence of commercial and regulatory drivers for asset reliability. We agree too with the recognition of the costs associated with the event causer determination process, including legal challenge. However, the WAG has drawn a strong conclusion on there being no need to continue with the event charge from relying on analysis that is not fully developed in the consultation paper.

From the perspective of system operations, we consider the event charge makes a positive contribution to system reliability. To alleviate our concern for potential reliability risk from the charge removal we suggest the analysis relied on by WAG needs to be made public. This will assist confidence in the 'remove' conclusion. In addition, the other advisory group, the Security and Reliability Council, could also be asked for its view on event charge removal.

Prefer predictable allocation of instantaneous reserves cost

We agree with the WAG conclusion to not recommend a change to cost-allocation to the ‘runway’ approach. We also agree with the WAG observation that the dual nature of the HVDC as causer and provider of Instantaneous Reserve, plus the role of the TPM, makes the design of the marginal signal challenging (maybe impossible!). Our preference would be for incremental change to the current cost allocation approach that takes into account the new capability of the HVDC for IR reserves sharing. This is Option C in the Authority’s recent consultation. Fundamentally, the current pro-rata allocation arrived at by negotiation would seem to be a better fit with a hierarchy that puts market-like solutions above any administered approach.

We note the difference in views of the WAG and the Authority on the complexity of cost allocation approaches. The Authority had not preferred its ‘Option C’ (taking into account HVDC sharing) because *option C would be considerably more costly than the proposal to implement*[1]. In contrast the WAG indicates that *in terms of complexity, none of the options are considered to be excessively complex or costly to implement*[2]. Our view is that the further variants presented by WAG – indicated as ‘Cost-to-island-causers’ and ‘Cost-to-HVDC-then-to-AC-island-causers’ – would be more complicated for predicting (ex-ante) cost allocation, although we defer to generator’s expertise on that point.

Please contact me if you have any questions about this submission.

Yours sincerely

Micky Cave

Senior Regulatory Analyst

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1 EA consultation paper Proposal to alter the way availability costs are allocated available at http://www.ea.govt.nz/development/work-programme/risk-management/national-instantaneous-reserves-market/consultations/

2 WAG consultation paper page 46

Appendix A – response to questions

Question	Response
Q.1. Do you agree with our identification of the problems with current arrangements?	Yes.
Q.2. Do you agree with these basic principles for allocating IR costs?	We support causer pays as the underlying principle and the current, negotiated, pro-rata approach as preferable under the DME framework.
Q.3. 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?	Probably only in the short term.
Q.4. What are your views on the merits of moving to a runway methodology (or its sub-options)?	Agree with WAG conclusion to not recommend a change (back) to the runway approach.
Q.5. Do you agree that a de minimis should continue and, if so, at what level?	It depends if the grounds for the current approach still hold.
Q.6. Are there other cost allocation options that you think should be considered?	No.
Q.7. 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?	Our preference is for the third approach to factor in the HVDC sharing to the island allocation; this seems to be a proportionate incremental approach to the current state.
Q.8. 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?	Yes.
Q.9. 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?	We agree with the conundrum identified by WAG on the dual nature of HVDC in IR cost creation and the nature of our cost recovery from HVDC payers. We prefer incremental and proportionate change to cost allocation.

Q.10. 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?	No comment.
Q.11. If yes, which options are likely to give rise to such outcomes, and could you provide worked examples demonstrating such effects?	No comment.
Q.12. 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?	Yes, under the pro-rata approach. The Code obligation on capacity means HVDC owner has no ability to manage greater cost exposure of the runway approach.
Q.13. 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?	Continue as is.
Q.14. 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?	Yes.
Q.15. What cost-allocation approach do you think should apply for plant with under-frequency and voltage-fault-ride-through dispensations?	No comment.
Q.16. 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?	No comment.
Q.17. Do you think the event charge should be retained, and if so, on what basis?	Unsure. We consider the analysis relied on by WAG (via footnote 38 in the paper) should be made public to improve confidence in the 'remove' conclusion.