MAJOR ELECTRICITY USERS' GROUP

22 November 2016

John Hancock
Chair
Wholesale Advisory Group
By email to wag@ea.govt.nz

Dear John

Review of IR Event Charge and Cost Allocation

1. This is a submission by the Major Electricity Users' Group (MEUG) on the Wholesale Advisory Group (WAG) discussion paper "Instantaneous Reserve Event Charge and Cost Allocation" 11 October 2016.[1]

2. MEUG members have been consulted in the preparation of this submission. This submission is not confidential. Some members may make separate submissions.

3. Responses to questions in the discussion paper follow. MEUG notes that the discussion paper "contains the preliminary findings from the WAG's review of these arrangements" and the paper was prepared prior to the introduction of a national market for IR (NMIR).[2] Correspondingly the MEUG responses below are preliminary and without experience gained from observing actual outcomes since NMIR began on 20 October 2016.

Question	MEUG response
1. Do you agree with our identification of the problems with current arrangements?	Yes.
2. Do you agree with these basic principles for allocating IR costs?	Yes MEUG agrees with the 2 principles: 1. Costs would be allocated to parties causing the need for IR; and 2. The cost allocation would send a marginal signal.

[1] URL http://www.ea.govt.nz/dmsdocument/21354 at http://www.ea.govt.nz/development/work-programme/pricing-cost-allocation/review-of-ir-event-charge-and-cost-allocation/consultation/#c16198.
[2] Ibid, s1.1, p9

Question	MEUG response
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?	We would like to observe market behaviour with NMIR in various situations before being able to comment.
4. What are your views on the merits of moving to a runway methodology (or its sub-options)?	Changing to a runway methodology is conceptually superior. The question should be how and when to adopt a runway methodology. We do not subscribe to a view no change is needed because it's expected no new large generation plant will be built in the future. The market design should be agnostic as to what might happen because markets are unpredictable and we should not rule out new large scale generation plant being built. MEUG has no view at this stage whether an overnight change to a runway method or a transition would be best.
5. Do you agree that a de minimis should continue and, if so, at what level?	As we prefer a runway methodology then there would, with that approach, be no de minimus. If the pro-rata allocation is retained deciding the optimal de minimus is at best complicated and at worse arbitrary. Another reason why the runway methodology is conceptually superior to the status quo.
6. Are there other cost allocation options that you think should be considered?	No; though we are open to consider options that other submitters may identify.
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?	MEUG's preliminary view is to agree with the preliminary finding in the WAG discussion paper "option 5 (allocating costs to the HVDC then AC island causers) would be the option which best sent a signal to the underlying causers of how much, and where, IR needs to be procured." As with response to Qu. 6 above we are open to views and analysis of other parties on what, as is demonstrated in the analysis on pp45 to 50, a very complex issue.
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?	-

Question	MEUG response
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?	That is a policy market design issue to be addressed in the review of TPM.
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?	-
11. If yes, which options are likely to give rise to such outcomes, and could you provide worked examples demonstrating such effects?	-
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?	See response to Qu. 9.
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?	A change to a quantity-and-price-runway approach for plant being commissioned best meets the two principles we agreed with in response to Qu. 2 above. However there are also additional costs in having the "price" leg of the approach and therefore net benefits may be maximised with just a quantity-runway based approach. The choice should be decided with a more detailed CBA.
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?	See response to Qu. 13.
15. What cost-allocation approach do you think should apply for plant with under-frequency and voltage-fault-ride-through dispensations?	-
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?	-

Question	MEUG response
17. Do you think the event charge should be retained, and if so, on what basis?	The preliminary view of MEUG is the event charge should not be retained provided a change to a runway approach is adopted. A change to the runway methodology for all procurement costs gives a time consistent better marginal cost signal to likely exacerbators than the current status quo mix of pro-rata allocation subject to a de minimus with event charges. Put another way if the current pro-rata cost allocation is retained then so too should an event charge to provide some sort of marginal cost signal. On another related topic MEUG suggests there is value in the market and the EA understanding who was the causer, the reasons for and the magnitude of all events. At the moment those statistics are collected and used for the purpose of deciding which party and how much they should pay for event charges. Ceasing collection of those statistics (except value of event charge) would be a mistake because having that information provides a useful history of actual outcomes to assess the performance of changes to the regime and if necessary further changes.

4. We look forward to WAG making a recommendation to the EA by March 2017.

Yours sincerely

Ralph Matthes
Executive Director