Consultation on FTR settlement in event of a delay to final prices

Consultation Paper

Submissions close: 5pm 10 February 2014

10 December 2013

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Executive summary

On 18 July 2013, the Authority made an urgent amendment to the Electricity Industry Participation Code 2010 (Code) to provide for increased flexibility regarding the timing of invoicing of the wholesale electricity market in the event of a delay in the publication of final prices.

Because the amendment was made under urgency, it will expire on 19 April 2014, 9 months after the date it came into force.

The Authority expects that a delay to final pricing that would affect clearing manager invoicing would be a very rare event, but should it occur, the issuing of clearing manager invoices and subsequent payments would need to be delayed as, until the urgent Code amendment was made, there was no provision under the Code for late settlement or revisions of FTR clearing manager settlements. For these reasons the Authority considers that the changes made by the urgent Code amendment should be made permanent.

The purpose of this consultation paper is to obtain participants' views on changes to clauses 14.36 and 14.73 of the Code that:

(a) allow flexibility for invoicing timeframes if the publication of final prices is delayed

(b) ensure that invoicing does not proceed in the absence of information without the Authority's direction

(c) allow invoicing to be delayed, removing the possibility of the clearing manager or FTR manager breaching the Code if final prices are delayed

(d) enables the clearing manager, if it receives revised reconciliation information after issuing invoices, to either prepare revised invoices, or seek direction from the Authority, depending on the timing of receiving the revised reconciliation information

(e) requires the Authority, when the clearing manager seeks direction (as referred to in paragraph (d) above) to direct the clearing manager as to when the clearing manager must issue the invoice.

Submitters should note that the proposed amendment could require industry participants to modify their financial arrangements to respond to invoicing or settlement being, at worst case and in rare events, several days later than expected. This delay could cause some participants inconvenience, if these clauses are ever required to be used.

Glossary of abbreviations and terms

Act	Electricity Industry Act 2010
Authority	Electricity Authority
Code	Electricity Industry Participation Code 2010

Contents

2. Introduction and purpose of this paper

2.1 Introduction

2.1.1 On 3 July 2013, the Electricity Authority Board approved an urgent Code amendment to provide for increased flexibility regarding the timing of invoicing of the wholesale electricity market in the event of a delay in the publication of final prices.

2.1.2 The Authority expects that a delay to final pricing that would affect clearing manager invoicing would be a very rare event, but should it occur, the issuing of clearing manager invoices and subsequent payments would need to be delayed as, until the urgent Code amendment was made, there was no provision under the Code for late settlement or revisions of the clearing manager's FTR settlements.

2.1.3 The Code amendment was required urgently so that the FTR market was covered against the risk of any delay in the publication of final prices from August 2013, which was the first month in which FTRs were to be settled.

2.1.4 Section 40 of the Electricity Industry Act 2010 (Act) allows the Authority to make an urgent Code amendment if:

(a) the Authority considers it is necessary or desirable in the public interest that the proposed amendment be made urgently

(b) along with the notice of the amendment that is published in the Gazette, the Authority publishes a statement of the reasons why the urgent amendment is needed.

2.1.5 If a Code amendment is made urgently under section 40, the Authority is not required to comply with the requirements to publicise a draft of the proposed amendment; prepare and publicise a regulatory statement; and consult on the proposed amendment and the regulatory statement before making the Code amendment.

2.1.6 However, a Code amendment made under section 40 of the Act expires 9 months after the date on which it comes into force. If the Code amendment is required for longer than that period, the Authority must follow the process set out in sections 38 and 39 of the Act for amending the Code.

2.2 Purpose of this paper

2.2.1 The Authority considers that the changes made by the urgent amendment should be made permanent by a further Code amendment, when the urgent Code amendment expires in April 2014. The purpose of this paper is to consult on an amendment to clauses 14.36 and 14.73 of the Code.

2.2.2 Section 39(1)(c) of the Act requires the Authority to consult on any proposed amendment to the Code and the regulatory statement. Section 39(2) provides that the regulatory statement must include a statement of the objectives of the proposed amendment, an evaluation of the costs and benefits of the proposed amendment, and an evaluation of alternative means of achieving the objectives of the proposed amendment. The regulatory statement is set out in part 3 of this paper.

2.2.3 The proposed amendment is attached as Appendix C.

2.2.4 The Authority invites submissions on the regulatory statement and the proposed amendment, including drafting comments.

2.3 Submissions

The Authority's preference is to receive submissions in electronic format (Microsoft Word). It is not necessary to send hard copies of submissions to the Authority, unless it is not possible to do so electronically. Submissions in electronic form should be emailed to submissions@ea.govt.nz with Consultation Paper—Consultation on FTR settlement in event of a delay to final prices in the subject line.

If submitters do not wish to send their submission electronically, they should post one hard copy of their submission to either of the addresses provided below.

Submissions
Electricity Authority
PO Box 10041
Wellington 6143

Submissions
Electricity Authority
Level 7, ASB Bank Tower
2 Hunter Street
Wellington

Tel: 0-4-460 8860

Fax: 0-4-460 8879

2.3.1 Submissions should be received by 5pm on 10 February 2014. Please note that late submissions are unlikely to be considered.

2.3.2 The Authority will acknowledge receipt of all submissions electronically. Please contact the Submissions' Administrator if you do not receive electronic acknowledgement of your submission within two business days.

2.3.3 If possible, submissions should be provided in the format shown in Appendix A. Your submission is likely to be made available to the general public on the Authority's website. Submitters should indicate any documents attached, in support of the submission, in a covering letter and clearly indicate any information that is provided to the Authority on a confidential basis. However, all information provided to the Authority is subject to the Official Information Act 1982.

3. Background

3.1 Current clearing manager invoice process

3.1.1 The clearing manager is required to issue invoices once per month. The invoice includes wholesale market settlements, ancillary service costs, constrained-on compensation, and FTRs.

3.1.2 The clearing manager invoice cycle is currently:

(a) the clearing manager must issue an invoice two business days after receiving reconciliation information from the reconciliation manager (clause 14.36). The reconciliation manager is required to provide this information by the 7th business day of each reconciliation period (clause 28 of schedule 15.4)

(b) the clearing manager must use final prices in the calculation of invoice amounts (clauses 14.40, and 14.45), including constrained on amounts

(c) the FTR manager must use information from the final price schedule (clause 9 of schedule 14.6) to calculate the amount of loss and constraint excess that must be retained by the clearing manager and paid into the FTR account no later than 1600 hours on the 7th business day of the month following the relevant billing period (clause 14.73)

(d) if the clearing manager does not issue an invoice within two business days of receiving reconciliation information or the invoice is delayed for any other reason, a payer may delay payment by the same period of time (clause 14.37(1)). However, in the absence of the urgent Code amendment or the proposed Code amendment, the clearing manager would have breached clause 14.36.

3.1.3 Provided that the clearing manager has received all information by the time it receives the reconciliation information, there will be no problem with issuing invoices. However, in the absence of the urgent and proposed Code amendments, if the publication of final prices is delayed later than the 7th business day of a month, invoicing and settlement may be delayed and:

(a) if the clearing manager delays invoicing, having received reconciliation information, the clearing manager would breach clause 14.36 as there would be no provision in the Code for invoicing to be delayed if other information is delayed

(b) if a payer exercises its right under clause 14.37(1) to delay payment because an invoice is delayed, this would affect the clearing manager's payments to payees. In this instance scaling would occur to payee payments for FTRs (clause 14.48C) and for payments to generators (clause 14.49). On receipt of a delayed payment, the clearing manager would be required to distribute an allocation to payees until all payer payments are received (clause 14.51).

3.1.4 Although any errors in wholesale settlements or constrained-on payments can be washed-up in subsequent invoice months, FTRs cannot. There is no provision for correcting FTR payments in subsequent invoice months.

3.2 Introduction of FTRs

3.2.1 The introduction of FTRs has added a further situation in which invoicing correctly depends on the publication of final prices. Under clause 14.73 the FTR manager is required to calculate the FTR portion of the loss and constraint excess (LCE) and to provide that information to the clearing manager. However, the clearing manager is not required to wait for the LCE information before issuing an invoice. The LCE (less any amount applied to fund FTRs) is required to be paid to the grid owner (clause 14.73(4)).

3.2.2 The potential for delays in the publication of final prices to disrupt invoicing is not new, and has always existed in the Code. Authority and service provider staff try to ensure that all information is available in time to avoid the issue arising.

3.2.3 The last interim price error claim that almost caused a disruption to invoicing related to pricing information for 24 April 2013. If such an event occurs, and the Code does not provide a solution, settlement of the affected trading periods would not be able to proceed.

3.2.4 If this issue is not able to be resolved by the 7th business day of a reconciliation period, participants owed FTR payments would not receive them, and their financial arrangements and confidence in FTRs as a hedging tool would be undermined.

4. Regulatory Statement

4.1 Authority's proposal

4.1.1 The Authority proposes amendments to clauses 14.36 and 14.73 of the Code as described below.

4.1.2 There are two known possible causes of a delay in the publication of final prices beyond the 7th business day of the settlement month. Both are rare events. They are:

(a) a pricing error claim could occur in the final days of the billing period. This could cause a delay of several days which, depending on the complexity of the error, could mean that final prices may not be available by the 7th business day of the reconciliation period

(b) an undesirable trading situation (UTS) could cause a delay of up to several months before final prices are resolved.

4.1.3 The proposed Code amendment:

(a) addresses problems with the shorter term delay that would be caused by a pricing error claim. The proposed Code amendment could also address a longer delay (for example, due to a UTS), but in either case leaves it for the Authority to determine what actions are appropriate in those cases depending on the circumstances at the time

(b) could affect industry participants as they may need to modify their financial arrangements to allow for an extended due date payment under rare circumstances to respond to invoicing or settlement being, at worst case, several days later than expected. This could inconvenience some participants, if these clauses are ever required to be used.

4.1.4 Specifically, the proposed amendment to clause 14.36:

(a) provides for the clearing manager to delay the issue of an invoice if it has not received all information to issue the invoice (for example, reconciliation, hedge settlement agreement, constrained-on, final price, or FTR information)

(b) provides for the clearing manager to issue a delayed invoice no less than two business days before settlement day (20th day of a month)

(c) if the clearing manager receives the necessary information later than two business days before settlement day, requires the clearing manager to refer the matter to the Authority

(d) requires the Authority, on receiving that advice, to direct the clearing manager as to the time by which the clearing manager must issue the invoice. For example, the Authority may direct the clearing manager to:

(i) delay invoicing if information would become available within the next two business days; or

(ii) continue to invoice for the periods for which final prices have been published, possibly omitting ancillary services or constrained-on amounts where prices are not available and to correct this on a subsequent wash-up invoice, or

(iii) deal with FTR invoicing as appropriate at the time

(e) requires the clearing manager, if it has already issued invoices but then receives revised reconciliation information, to either:

(i) use the revised information to issue revised invoices (if it receives the revised information more than 2 business days before settlement day); or

(ii) refer the matter to the Authority if it receives the revised information later than 2 business days after settlement day.

4.1.5 The proposed amendment to clause 14.73:

(a) would require the FTR manager to advise the clearing manager of the amount of LCE to be paid into the FTR account one business day after final prices are received if any final price is published after 1600 hours on the 6th business day of the month following the relevant billing period

(b) means that the FTR manager is not automatically in breach of 14.73 if final prices are not available by the time that the FTR manager is normally required to deliver the information.

4.1.6 Longer delays to final prices are only expected to occur if there is an alleged UTS. In that situation, the Authority would need to consider the specific set of circumstances and direct relevant market operation service providers accordingly.

4.1.7 The draft Code amendment is provided in Appendix C.

Q1.	**Do you agree or disagree with the proposed amendment? Please give reasons.**

4.2 Statement of the objectives of the proposed amendment

4.2.1 The objectives of the proposed amendment are to provide flexibility within the invoice time frame when invoicing information is delayed, making the best use of the available time.

4.3 Evaluation of the costs and benefits of the proposed amendment

4.3.1 The orderly settlement of the electricity market has a significant effect on customer and participant confidence in the electricity market. Should the clearing manager not be able to invoice within the Code required time frames, or be forced by the current Code to invoice on incorrect information, participants may incur increased costs that may include:

(a) transaction costs with delayed payments

(b) potential for disputes where incomplete or inaccurate information is used

(c) recalculation of invoices

(d) breaches of the Code by market operation service providers.

4.3.2 The Authority considers that the proposed amendments:

(a) will impose only a small cost to the Authority to implement

(b) will impose no cost to participants to implement.

4.3.3 Should invoicing need to be delayed, the Authority considers that under the proposed amendments:

(a) any cost of a delay to invoicing or payments would more than offset the benefit of managing the invoicing process

(b) any potential risk to orderly settlement, in the event that all information is not available within the time period required for invoicing currently set into the Code, would be removed.

Q2. Do you agree or disagree with the assessment of costs and benefits? Please give reasons.

4.4 Evaluation of alternative means of achieving the objectives of the proposed amendment

4.4.1 The Authority considers that there is only one alternative to the proposed amendment to the Code and this is to do nothing until/if an event occurs.

4.4.2 The likelihood of a situation arising where information is delayed, and consequently invoicing is delayed, is low, and may not occur at all. Instead of making a Code amendment, the Authority could allow the urgent Code amendment to expire, and the Code to revert to the provisions that existed prior to the urgent Code amendment coming into force. If this approach was taken, the Authority and participants would need to assess an invoicing situation as it arose and quickly decide how to act depending on the options open at the time. In particular, it could make every effort to resolve pricing error claims as quickly as possible to avoid the problem, particularly if they fall at the end of a calendar month.

4.4.3 This option would save the cost and effort in putting in place a Code amendment that may never be used. Resources would only be used if a rare invoicing situation did occur. It could be expected that, if the Code amendment was not made, the Authority and service providers could informally agree a solution and all parties would be expected to act pragmatically to protect the FTR market. However, any such agreement would be restricted by the provisions of the Code.

4.4.4 However, the Authority has limited tools to use in this situation and would have limited time in which to work out a solution. While the service providers are likely to assist with a pragmatic solution, if a workaround was not covered by the Code, it would expose service providers to additional risk as well as Code breaches. If the situation does occur, the Authority's objectives in establishing FTRs could be compromised if the situation was not resolved in a timely manner. Extra resource and transaction costs would be required.

Q3. Do you consider that there are other alternatives that have not been considered and should be considered? Please provide discussion of other alternatives.

4.5 Assessment under section 32(1)

4.5.1 Section 32(1) of the Act provides that Code provisions must be consistent with the Authority's objective and be necessary or desirable to promote any or all of the following:

(a) competition in the electricity industry;

(b) the reliable supply of electricity to consumers;

(c) the efficient operation of the electricity industry;

(d) the performance by the Authority of its functions;

(e) any other matters specifically referred to in this Act as a matter for inclusion in the Code.

4.5.2 Appendix B contains a table setting out an assessment of the proposed amendment against the requirements of section 32(1) of the Act.

4.6 Assessment against the code amendment principles

4.6.1 When considering amendments to the Code, the Authority is required by its Consultation Charter to have regard to the following Code amendment principles, to the extent that the Authority considers that they are applicable.

4.6.2 *Principle 1 – Lawfulness:* The Authority and its advisory groups will only consider amendments to the Code that are lawful and that are consistent with the Act (and therefore consistent with the Authority's statutory objective and its obligations under the Act).

4.6.3 The Authority considers the proposed amendment to be lawful.

4.6.4 *Principle 2 – Clearly Identified Efficiency Gain or Market or Regulatory Failure:* Within the legal framework specified in Principle 1, the Authority and its advisory groups will only consider using the Code to regulate market activity when:

(a) it can be demonstrated that amendments to the Code will improve the efficiency of the electricity industry for the long-term benefit of consumers; [1]

(b) market failure is clearly identified, such as may arise from market power, externalities, asymmetric information and prohibitive transaction costs; or

[1] Where efficiency refers to allocative, productive and dynamic efficiency, and improvements to efficiency include, for example, a reduction in transaction costs or a reduction in the scope for disputes between industry participants.

(c) a problem is created by the existing Code, which either requires an amendment to the Code, or an amendment to the way in which the Code is applied.

4.6.5 The Authority considers that:

(a) the proposed amendment would deliver improvements to the efficiency of the electricity industry by reducing transaction costs and risk associated with potential disruption to FTR settlement if the publication of final prices was delayed

(b) the proposed amendment is desirable and would further promote efficient market operation because it would provide the clearing manager and FTR manager with clear direction as to what to do if this situation occurs.

4.6.6 *Principle 3 – Quantitative Assessment:* When considering possible amendments to the Code, the Authority and its advisory groups will ensure disclosure of key assumptions and sensitivities, and use quantitative cost-benefit analysis to assess long-term net benefits for consumers, although the Authority recognises that quantitative analysis will not always be possible. This approach means that competition and reliability are assessed solely in regard to their economic efficiency effects. Particular care will be taken to include dynamic efficiency effects in the assessment, and the assessment will include sensitivity analysis when there is uncertainty about key parameters.

4.6.7 The proposed amendment will have a qualitative net benefit of promoting confidence in FTRs as a locational price risk hedging tool among wholesale market participants, and consequently will help to promote competition in the retail electricity market for the long-term benefit of consumers.

Q4. Do you agree or disagree with the assessment against the Code amendment principles? Please give reasons.

Appendix A Format for submissions

Question No.	Question	Response
1	Do you agree or disagree with the proposed amendment? Please give reasons.	
2	Do you agree or disagree with the assessment of costs and benefits? Please give reasons.	
3	Do you consider that there are other alternatives that have not been considered and should be considered? Please provide discussion of other alternatives.	
4	Do you agree or disagree with the assessment against the Code amendment principles? Please give reasons.	

Appendix B Assessment under section 32(1) of the Act

Section 32(1) requirements:	Response
The proposed amendment is consistent with the Authority's objective under section 15 of the Act, which is as follows:	
(a) to promote competition in, reliable supply by, and the efficient operation of, the electricity industry for the long-term benefit of consumers	The proposal is to the long-term benefit of consumers, as it would improve the robustness of FTRs as a locational price risk hedging tool, which assists with promoting competition and the efficient operation of the electricity market
The proposed amendment is necessary or desirable to promote any or all of the following:	
(a) competition in the electricity industry	The proposed amendment would promote confidence in the wholesale market in relation to the use of FTRs as a locational price risk hedging tool, thereby promoting increased competition in the retail electricity market
(b) the reliable supply of electricity to consumers	The proposed amendment would have no effect on the reliable supply of electricity
(c) the efficient operation of the electricity industry	The proposed amendment would promote the efficient operation of the electricity industry by providing certainty to market operation service providers and participants if final prices are delayed
(d) the performance by the Authority of its functions	The proposed amendment would avoid the Authority and its providers needing to devise a pragmatic solution at short notice, which could occur if this proposed amendment were not in place
(e) any other matter specifically referred to in this Act as a matter for inclusion in the Code.	Not applicable

Appendix C Proposed amendment

14.36 Issue of invoices

(1) 2 **business days** after the **clearing manager** receives **reconciliation information** in respect of the prior **billing period** from the **reconciliation manager** in accordance with clause 28(c) of Schedule 15.4, the **clearing manager** must issue to each **purchaser** an invoice in respect of the **trading period** of the **billing period** to which the **reconciliation information** applies.

(2) At the same time as the **clearing manager** issues invoices under subclause (1), the **clearing manager** must issue an invoice to each person to whom **ancillary service** costs have been allocated.

(3) At the same time as the **clearing manager** issues invoices under subclause (1), the **clearing manager** must issue an invoice in respect of any amount due in respect of an **FTR**.

(3A) Despite subclauses (1) to (3), the **clearing manager** may issue an invoice at any time on or before the day that is 2 **business days** before the 20th calendar day of the month following the relevant **billing period** if the **clearing manager**—

- (a) has not received all information necessary to issue the invoice in respect of every **trading period** in the **billing period** by the time specified in subclause (1); and
- (b) receives all necessary information in time to issue the invoice before the day that is 2 **business days** before the 20th calendar day of the month.

(3B) However, if the **clearing manager** receives the information later than 2 **business days** before the 20th calendar day of the month, the **clearing manager** must refer the matter to the **Authority** and the **Authority** must direct the **clearing manager** as to the time by which the **clearing manager** must issue the invoice.

(3C) If subclause (3B) applies, the **clearing manager** must issue the invoice by the time determined by the **Authority**.

(4) Despite anything in this clause, if the **clearing manager** receives revised **reconciliation information** from the **reconciliation manager**~~, the **clearing manager** must use that revised **reconciliation information** in preparing the next invoices to **purchasers**.~~ relating to a **billing period** after the **clearing manager** has issued invoices for that **billing period** and—

- (a) the **clearing manager** receives the revised **reconciliation information** before the day that is 2 **business days** before the 20th calendar day of the month following the relevant **billing period**, the **clearing manager** must use the revised **reconciliation information** to prepare revised invoices for **purchasers**; or
- (b) the **clearing manager** receives the revised **reconciliation information** after the day that is 2 **business days** before the 20th calendar day of the month—
  - (i) the **clearing manager** must refer the matter to the **Authority**; and
  - (ii) the **Authority** must direct the **clearing manager** as to the time by which the **clearing manager** must issue the invoice; and
  - (iii) the **clearing manager** must issue the invoice by the time determined by the **Authority**.

14.73 Payment of loss and constraint excess

(1) On the final day for payment under clause 14.37, and when the **clearing manager** has received notification from its **bank** that the **generators** and **purchasers** have deposited **cleared funds** in the **operating account**, the **clearing manager** must, subject to clause 14.47, pay the appropriate **loss and constraint excess** and **residual loss and constraint excess** to each **grid owner** in accordance with subclause (3) and

subclause (4).

(2) A **loss and constraint excess** accrues for a **billing period** when the total amounts to be paid by the **clearing manager** to the **generators** for that **billing period** for the contracts formed in accordance with clause 14.30 differ from the total amounts to be paid to the **clearing manager** by the **purchasers** for that **billing period** for the contracts formed in accordance with clause 14.33.

(2A) The **FTR manager** must—

(a) determine the amount of **loss and constraint excess** that must be retained by the **clearing manager** and paid into the **FTR account** in accordance with Schedule 14.6; and

(b) advise the **clearing manager** of that amount no later than—

(i) 1600 hours on the 7th **business day** of the month following the relevant **billing period**; or

(ii) if **publication** of **final prices** is delayed for any **trading period** in the relevant **billing period** so that **final prices** for a **trading period** in the **billing period** are **published** later than 1600 hours on the 6th **business day** of the month following the relevant **billing period**, 1 **business day** after all **final prices** for the **billing period** are **published**.

(2B) Each **grid owner** and the **pricing manager** must provide information to the **FTR manager** in accordance with Schedule 14.6.

(2C) The **clearing manager** must retain the amount advised under subclause (2A) and pay the amount into the **FTR account**.

(2D) If the amount that the **FTR manager** advises the **clearing manager** under subclause (2A) exceeds the amount of the **loss and constraint excess** for the **billing period**, the **clearing manager** must retain all of the **loss and constraint excess** and pay all of the **loss and constraint excess** into the **FTR account**.

(3) The **Authority** must advise the **clearing manager** of the proportion of the **loss and constraint excess** and **residual loss and constraint excess** each **grid owner** is to be paid.