Proposed Scarcity pricing Code amendments

Summary of submissions

Contents

1 This paper summarises submitters' views on the consultation paper

1.1 On 26 April 2016, the Authority published the consultation paper *Proposed Scarcity pricing Code amendments* (consultation paper).[1]

1.2 The consultation paper proposed six amendments to the Electricity Industry Participation Code 2010 (Code) to resolve six corresponding operational issues with the Code's current scarcity pricing regime:

(a) Issue 1: the regime is unclear regarding which trading periods the system operator should specify in a notice relating to an event or an island-wide instruction to disconnect demand

(b) Issue 2: the regime does not allow the pricing manager enough time to publish notice of and resolve an infeasibility or metering situation that, by coincidence, exists at the same time as a shortage situation, before subsequently giving notice of the shortage situation

(c) Issue 3: the regime does not allow for any delays (which can occur due to reasons outside the pricing manager's control) in the pricing manager resolving provisional price situations

(d) Issue 4: if interim prices change after the pricing manager publishes them, the regime does not require the pricing manager to recalculate and republish interim prices using the scarcity pricing methodology in Schedule 13.3A of the Code

(e) Issue 5: the regime's deadline for the pricing manager to calculate and publish interim prices using the scarcity pricing methodology under Schedule 13.3A is too tight

(f) Issue 6: there is a typographical error in the Code's formula for calculating island GWAP.

1.3 The consultation paper put forward the Authority's view that the proposed Code amendments would correct and clarify these aspects of the scarcity pricing regime, and prevent unintended consequences in operating it. This would ensure that the regime operated correctly and efficiently, which, consistent with the Authority's statutory objective, would promote an efficient level of reliable supply in the electricity industry for the long-term benefit of consumers.

1.4 This paper summarises the views submitters expressed on the consultation paper. The paper first outlines submitters' responses to the specific questions the Authority asked in the consultation paper, and then summarises other general comments included in the submissions. The consultation paper itself sets out each of the amendments that submitters have responded to, in more detail.[2]

[1] A copy of the consultation paper can be found on the Authority's website at: https://www.ea.govt.nz/development/work-programme/operational-efficiencies/review-of-scarcity-pricing/consultations/#c15960.

[2] Ibid.

2 Eight parties made submissions on the consultation paper

2.1 The Authority received a submission from each of the following parties:

(a) Contact Energy Limited (Contact)

(b) Genesis Energy Limited

(c) Major Electricity Users' Group (MEUG)

(d) Meridian Energy Limited (Meridian)

(e) Mercury Energy Limited (Mercury)

(f) Transpower New Zealand Limited

(g) Pioneer Energy Limited (Pioneer)

(h) NZX Limited (NZX).

2.2 This summary does not contain the full text of the submissions. However, the Authority has published all submissions in full on its website.[3]

3 Submitters responded to the questions in the consultation paper

Most submitters considered that the proposed Code amendments address issues with the scarcity pricing regime that should be resolved (questions 1 and 2)

3.1 Most submitters considered that the proposed Code amendments would address issues with the scarcity pricing regime that the Authority should resolve. However, two submitters raised concerns and suggestions in relation to several of the proposed amendments:

(a) the proposed amendment for Issue 1 would require the system operator to specify the start and end time of the situation to which the notice under clause 5 of Technical Code B of Schedule 8.3 applied, rather than the trading periods. Pioneer submitted that, as the end time of the relevant situation (under clause 5(1) or 5(1A) of Technical Code B) might not be immediately clear, including the end time in the first notice should be optional. Pioneer considered that once the end time of the relevant situation became apparent, the system operator could issue a further notice providing this information

(b) NZX raised two concerns with the proposed amendment for Issue 2:

(i) the proposed amendment should require the pricing manager to resolve *all* types of provisional price situations (including high spring washer price situations) in a trading period before the pricing manager determines whether a scarcity pricing situation exists in that trading period

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[3] Submissions on the consultation paper are available at: https://www.ea.govt.nz/development/work-programme/operational-efficiencies/review-of-scarcity-pricing/consultations/.

(ii) the proposed amendment requires the pricing manager to delay publishing a shortage situation notice for a trading period until it has resolved all infeasibility, metering and SCADA situations in that trading period. NZX considered that this delay could cause unnecessary confusion for participants in the context of a serious event

(c) NZX put forward an alternative to the proposed amendment for Issue 2 that NZX considered would address its two concerns

(d) Pioneer submitted that the time constraints described in Issue 2 only arise because clause 13.144 requires the pricing manager to publish notice of a shortage situation after receiving notice of the shortage situation from the system operator under clause 5(1A) of Technical Code B. Pioneer suggested that it would be more appropriate for the system operator (rather than the pricing manager) to publish notice of the shortage situation under clause 13.144, leaving the pricing manager to calculate scarcity prices

(e) regarding the proposed amendment for Issue 3, NZX suggested that it would be preferable to allow the pricing manager to calculate the average island GWAP under clause 13.135C using provisional prices, and to publish the resulting scarcity prices as provisional. NZX considered that participants would rather see some form of pricing information in a shortage situation (even if it is provisional) rather than none at all

(f) Pioneer also queried whether the proposed Code amendment for Issue 5 (to extend the deadline for publishing interim prices under clause 13.135B(b)(ii)) was consistent with the Authority's focus on publishing 'actionable prices' and the trend toward real-time pricing (RTP).[4]

Two submitters raised additional issues with the scarcity pricing regime that the proposed amendments did not address (question 3)

3.2 NZX noted that the pricing manager's system and the wholesale information trading system are currently configured to publish prices once a day for the entire trading day. NZX submitted that the deadline for publishing interim prices under clause 13.135B(b)(ii) does not accommodate any other provisional price situations that occur on the same trading day but *after* the trading period in which a scarcity pricing situation occurs. NZX proposed an amendment to the wording of clause 13.135B(b)(ii), which NZX considered would resolve this additional operational issue.

3.3 Contact noted that in the case of emergency load shedding situations, its preference was that scarcity prices be based on a fixed figure rather than a range of figures. Contact did not believe that basing scarcity prices on the cost of last-resort generation (rather than the value of lost load) was consistent with the assumption that load shedding must occur to trigger scarcity pricing.

3.4 Contact also considered that enabling generators to reduce offer prices within the two hour gate closure window would:

(a) provide a better indication of the true balance between demand and supply

4 See the Authority's 12 April 2016 information paper *Assessment of real-time pricing options* available at: http://www.ea.govt.nz/dmsdocument/20599.

(b) avoid artificially limiting available generation when the market unexpectedly becomes stressed.

Most submitters considered that the benefits of the proposed amendments outweigh the costs, and that there were no existing alternatives for achieving the objective of the proposed amendments (questions 4 and 5)

3.5 Most submitters agreed with the position put forward in the consultation paper that:

(a) there were no alternatives for achieving the objective of the proposed amendments

(b) by correcting and clarifying aspects of the scarcity pricing regime, the proposed amendments would support the delivery of the positive net benefits identified in the cost-benefit analysis for the Code amendment that introduced the regime.[5]

3.6 Meridian agreed with the position in the consultation paper as outlined above, but recommended the Authority also assess the proposed amendments against the Authority's spot market refinements and RTP projects.[6]

3.7 NZX submitted that adjusting the proposed amendments to provide for the suggestions in NZX's submission would ensure the scarcity pricing regime functioned as intended. NZX considered that in the context of a scarcity pricing situation, this would mitigate or eliminate the risks the pricing manager might face from participants challenging its pricing process though a pricing error claim.

3.8 In terms of alternatives for achieving the objective of the proposed amendments:

(a) NZX submitted that its proposal for addressing Issue 3 could offer greater benefit to the market

(b) MEUG considered that Issues 4 and 5 would not arise if the Authority adopted certain of the options under consideration in the RTP project. MEUG noted that an alternative therefore would be to wait for one of the relevant RTP options to be implemented to address those issues. However, MEUG preferred the proposed amendments over this alternative, because MEUG considered RTP would take at least three years to implement and a scarcity pricing event could occur in the interim.

The proposed amendments comply with section 32(1) of the Act (question 6)

3.9 All submitters that responded to question 6 in the consultation paper considered that the proposed amendments complied with section 32(1) of the Act.

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[5] The cost-benefit analysis for the Code amendment that introduced the scarcity pricing regime in June 2013 is set out at Appendix E of the consultation paper for this amendment, which is available at: http://www.ea.govt.nz/about-us/what-we-do/our-history/archive/dev-archive/work-programmes/market-wholesale-and-retail-work/scarcity-pricing/consultations/#c13855.

[6] See above at n4.

One submitter commented on the drafting of the proposed amendments (question 7)

3.10 NZX recommended two changes to the proposed drafting for clause 13.135B:

(a) change subclause (2) to address the situation where an interim price is changed in the previous 336 trading periods

(b) change subclause (2)(b) to better align its wording with the purpose of clause 13.135B.

3.11 NZX also submitted that the proposed new clause 13.144(1A) made no sense for metering situations because metered quantities refer to the sum of energy over a trading period. NZX therefore recommended that subclause (1A) only apply to notices under subclause (1) that relate to shortage situations.

4 Submitters made other general comments on the consultation paper

One submitter considered the scarcity pricing regime to be too complex

4.1 Mercury supported the intent of the proposed amendments to correct and clarify aspects of the scarcity pricing regime, but expressed concern that the mechanics of the regime remained complex and opaque—particularly for new-entrant industry participants and other stakeholders. Mercury considered the factors and process that gave rise to scarcity pricing to be particularly complex, including the fact that the pricing manager determined scarcity pricing ex-post.

One submitter encouraged the Authority to simplify regulatory arrangements for the industry

4.2 Pioneer encouraged the Authority to focus on simplifying the regulatory arrangements for the industry. Pioneer considered that complexity in the industry creates confusion and distrust from consumers and represents a significant barrier to new entrants and innovation in the industry.

Appendix A Consultation questions – proposed Scarcity pricing Code amendments consultation paper

Consultation questions
Q1: Do you agree that the Authority should address the six identified issues with the scarcity pricing regime? If not, why not?
Q2: Do you agree that the Authority's proposed amendments address these issues with the scarcity pricing regime? If not, why not?
Q3: Do you consider that there are other issues with the scarcity pricing regime that the proposed amendments do not address? If so, please provide details of these other issues and any suggestions you have for resolving them.
Q4: Do you agree the benefits of the proposed amendments outweigh their costs?
Q5: Do you agree with the Authority's assessment of alternatives for achieving the objective of the proposed amendments? If you disagree with the Authority's assessment, please explain your preferred alternative in terms consistent with the Authority's statutory objective under section 15 of the Act.
Q6: Do you agree the Authority's proposed amendments comply with section 32(1) of the Act?
Q7: Do you have any comments on the drafting of the proposed amendments?