Electricity Authority
By email: **FTRConsultation@ea.govt.nz**

23 September 2020

Submission on Revocation of Schedule 14.3

Mercury welcomes the opportunity to provide a submission on the consultation paper on "Revocation of Schedule 14.3" and specifically the removal of the requirement for the Financial Transmission Rights (FTR) manager to calculate the amount of loss and constraint excess (LCE) to be applied to FTRs.

Our responses to the consultation questions are included in Appendix A. These should be read in conjunction with our cover letter below.

Mercury supports the proposal, but recommends an amendment

Mercury supports the proposal to revoke schedule 14.3 from the Code and agrees there will likely be a small net benefit from the change in the form of:

- reduced costs of system upgrades for the FTR manager; and
- downward pressure on monthly FTR service provider fees.

We also accept the Authority's analysis which shows that there is enough historical evidence to demonstrate allocating all LCE to FTR settlements will have no adverse impact on market outcomes.

Mercury does recommend making an additional amendment to the current settlement procedure. As the Authority knows LCE/FTRs are settled on a monthly basis. This monthly settlement can mean there is a risk of scaling in the FTR market and while this revenue inadequacy is rare, there is no guarantee of it remaining so. The Authority encourages use of hedge markets for managing risk and a core feature of efficiency in the FTR market for participants would be full and accurate settlement of FTR positions. Mercury recommends holding LCE on a three-month rolling basis to ensure FTR revenue adequacy.

Authority to also progress LCE Code change

On 1 April 2019 Mercury submitted a Code change request to the Authority to ensure the economically efficient return of excess LCE to retailers. This excess LCE is currently returned to transmission customers, and where those customers are distributors, they may retain some or all of this LCE despite having no bearing on the underlying cause of that LCE (i.e. the electricity consumed by end users). Retailers and their customers have little to no visibility on how this windfall gain is currently being treated by distributors.

At the time we made the change request Mercury also mentioned that an independent cost benefit analysis indicated a net benefit of at least $45 million in favour of the Code change. This figure is much larger than the expected net benefit of the current proposal and indicates a clear efficiency enhancing change the Authority could make for the long-term benefit of consumers.

We welcome progress on this Code change from the Authority as soon as possible, particularly given the relative benefits of it vis-à-vis the Schedule 14.3 revocation. The Authority has previously indicated this Code change request may be dependent on the development of the new Transmission Pricing Methodology but we see no reason this cannot be advanced independently.

Nothing in this submission is confidential. If you have any queries please contact me at john.bright@mercury.co.nz

Kind Regards,

John Bright
Regulatory Strategist

Appendix A. Response to consultation questions

#	Question	Mercury's response
1	Do you agree the issue identified by the Authority is worthy of attention?	Yes, it is worthy of attention but as this is not a material issue for the industry at present we recommend it is dealt with in an expedient manner. With respect to Mercury's suggested amendment in our cover letter, we do not think this would add much complexity to the changes proposed and could also be progressed now.
2	Do you agree with the objectives of the proposed amendment? If not, why not?	Yes.
3	Do you agree the benefits of the proposed amendment outweigh its costs?	Yes, we have not validated the assumptions used by the Authority but the modest net benefit seems reasonable.
4	Do you agree the proposed amendment is preferable to the other options? If you disagree, please explain your preferred option in terms consistent with the Authority's statutory objective in section 15 of the Electricity Industry Act 2010.	Mercury agrees the Authority has identified the best option, however in addition to this option we also recommend holding LCE on a three-month rolling basis (as discussed in the cover letter). We do not expect this would add any material costs and the main benefit would be ensuring revenue adequacy and confidence in the FTR market.
5	Do you agree the Authority's proposed amendment complies with section 32(1) of the Act?	Yes, however the proposal we have outlined above is likely to enhance this even further with minimal cost.
6	Do you have any comments on the drafting of the proposed amendment?	No comments.