



MAJOR ELECTRICITY USERS' GROUP

19 February 2009

Bronwyn Christie
Electricity Commission
By email to submissions@electricitycommission.govt.nz

Dear Bronwyn

Submission on Report on Review of 2008 Winter and the period leading into winter

1. This is a submission by the Major Electricity Users' Group (MEUG) on the report prepared for the Electricity Commission titled *Review of 2008 Winter and the period leading into winter*¹ (the "Winter Review"). MEUG members agree with the key conclusion of the Winter Review that under the current security of supply policy settings some generators can pass their costs and risks off to others, including competing suppliers and customers. The report goes on to say²

"This can weaken the incentive to take good security decisions. In our view, a 'better' market approach would see these risks and rewards internalised."

2. We also agree with the proposed course of action in the Winter Review and the Commission's assessment that the focus should now be on implementation. Detailed comments on each recommendation as requested by the Commission are provided in the appendix.
3. From the analysis in the report and our own initial assessment, we see no difficulty in implementing the recommendations of the Winter Review as soon as possible ahead of any of the possible changes to the market that might arise from existing Commission work streams such as the Market Design Review or the Commerce Commission Part 2 investigation. Implementing the Winter Review recommendations will only deal with security of supply issues. More effort and lateral thinking to improve the market as a whole is urgently needed.
4. Implementing the key recommendations may not be completed before this winter and hence suppliers have the same incentives as last year to shift risk to others. Some interim measures should be considered. For example generators could pay for reserve energy acquired (fixed and variable costs) by the Commission in proportion to shortage of dry-year generation they cause. This would immediately internalise one of the largest security of supply costs that is currently shifted to other parties.
5. The Winter Review is not an investigation into the behaviour of suppliers pursuant to Part 2 of the Commerce Act. Separately MEUG is likely to raise with the Commerce Commission some concerns we have about certain behaviour observed last winter.

Yours sincerely

Ralph Matthes
Executive Director

¹ Refer <http://www.electricitycommission.govt.nz/pdfs/opdev/secsupply/pdfsconsultation/Winter-Review-Report.pdf>

² Winter Review p47

MEUG comments on recommendations in Winter Review³

Winter Review recommendation	MEUG comments
<p>1. To reduce or remove the scope for participants to externalise the cost of their risk management decisions, we recommend that:</p> <ul style="list-style-type: none"> ▪ The market rules be changed to ensure decision-makers face the cost to consumers of any forced demand curtailment, and then that the present reserve energy scheme be discontinued or modified to ensure costs are targeted as closely as possible to those parties who benefit from its use (preferred option); or ▪ A compulsory dry year insurance regime be adopted (alternative option) 	<p><u>Merit: 1st = priority.</u> This is the most important recommendation of the Winter Review.</p> <p><u>Implementation:</u> Urgent implementation is needed, ie better define the preferred option and then conduct a detailed cost-benefit-analysis. Assuming the analysis confirms the conclusion of the Winter Review report; then start process to change relevant legislation, regulation or rules.</p> <p>If the implementation timeline will not lead to changes in time for this winter, then other interim measures to ensure suppliers face the consequences of being unable to meet energy demand in dry-years should be considered, eg Whirinaki levy costs being paid for by suppliers in proportion to the dry-year risk they shift to other parties.</p>
<p>2. Analysis be undertaken to determine whether the three 52 MW units at Whirinaki could make a greater and/or more cost-effective contribution to New Zealand electricity supply at a different location or with a different fuel capability; and</p> <p>If the analysis indicates that location or fuel modification is desirable, the units be offered for transfer out of the reserve energy scheme to facilitate such reconfiguration</p>	<p><u>Merit: None. This recommendation is not supported.</u></p> <p><u>Implementation:</u> In undertaking a full cost-benefit-analysis on recommendation 1, the option set out in recommendation 2 should be one of the alternatives considered (along with the compulsory dry year insurance option). We believe that the full cost-benefit-analysis will validate the Winter Review preferred option recommendation 1 and therefore more detailed work on recommendation 2 by the EC will be unnecessary. Prospective buyers of Whirinaki power station of course are likely to consider re-location and different fuel options.</p>
<p>3. Triggers and plans for any emergency measures be pre-defined as far as practicable, and that they should be published.</p>	<p><u>Merit: 5th priority.</u> Will help. This should have been in place in 2008.</p> <p><u>Implementation:</u> Should be part of BAU continuous improvement by EC.</p> <p>There is also a question as to whether retailers adequately informed their customers of potential rolling black-outs in order that end consumers could develop appropriate contingency plans.</p>
<p>4. The 'informal' improvements to information provision adopted for winter 2008 be examined to determine whether any should be codified into existing arrangements or contingency</p>	<p><u>Merit: 6th priority.</u> Will help.</p> <p><u>Implementation:</u> Most of this should be in place for this winter.</p>

³ When requesting comments the Commission specifically requested:

- "merits, or otherwise, of proceeding to more detailed work;" and
- Work that could be implemented by this winter and work for implementation by later years.

<p>5. Major sellers of electricity contracts be required to provide regular disclosures regarding their aggregate risk position;</p> <p>Major sellers of electricity contracts be required to update their disclosure if there is a material adverse change to their risk position; and</p> <p>If it is decided that no public disclosure is appropriate, this information should be disclosed to the Electricity Commission.</p>	<p><u>Merit: 4th priority.</u> MEUG support further investigation of this option. We have over the years unsuccessfully attempted to have voluntary standardised disclosures for the largest suppliers.</p> <p><u>Implementation:</u> Could be possible for this winter provided it does not divert Commission resources from implementing higher priority recommendations. Designing disclosure requirements relating to security of supply policy could also be merged with any disclosure regime designed to assist competition and or provide transparency on supplier profits. The latter might be one of the outcomes from the Commerce Commission Part 2 inquiry.</p> <p>MEUG also note that large suppliers' and end consumers could agree a voluntary disclosure regime with the fallback if agreement cannot be reached being regulation.</p>
<p>6. The Electricity Commission consider whether there are any steps it can take to provide more certainty around the terms of resource consent access to 'emergency' generation resources where consents directly or indirectly make reference to the Electricity Commission.</p>	<p><u>Merit: 7th priority.</u> Recommendation should be considered further; though MEUG is not entirely satisfied a change from the status quo where the onus is on the consent holder to obtain certainty will result in better outcomes. The current case-by-case approach overcomes the risk of rigid decision making criteria being so inflexible so that discrete circumstances cannot be effectively managed. The power system is very complex and having more prescription on how the EC should act when referred to in consents will be very challenging.</p> <p><u>Implementation:</u> Could be possible for this winter; however we suggest it isn't high priority and resources better used to implement higher priority recommendations.</p>
<p>7. The respective roles of the Minister and the Electricity Commission in the security of supply area be clarified; and</p> <p>The Electricity Commission have a greater degree of independence in the exercise of regulatory functions.</p>	<p><u>Merit: 2nd = priority.</u> This is important for both security of supply policy (ie the issue addressed by the Winter Review) and for improving the overall electricity sector governance and structure.</p> <p><u>Implementation:</u> Part of this should be possible for this winter (eg clarifying roles) but gaining more independence will require a legislative change. Implementing this recommendation should be undertaken in conjunction with recommendation 8.</p>
<p>8. The EC place priority on initiatives that will facilitate competition.</p>	<p><u>Merit: 2nd = priority.</u> This is important for both security of supply policy (ie the issue addressed by the Winter Review) and for improving the overall electricity sector governance and structure.</p> <p><u>Implementation:</u> Continue with various EC work streams including Market Design review work; at the same time MED should undertake a fundamental stock take of the market design and industry governance with the overall objective of improving competition. Implementing this recommendation should be undertaken in conjunction with recommendation 7.</p>