

Summary of submissions on the Pricing Process Improvement Project Consultation Paper

Prepared by the Electricity Commission

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Introduction

1. On 18 November 2009, the Electricity Commission (Commission) released a consultation paper entitled “Issues and Indicative Options for the Spot Market Pricing Process and UTS Provisions” (the Consultation Paper). The Commission received ten submissions on the Consultation Paper.
2. This paper provides a brief summary of the key points raised in submissions and indicates whether, and how, the Commission intends to progress each of the initiatives.
3. A table with submitters’ responses to each of the questions in the Consultation Paper is attached to this paper. Note that, in some cases, the submission table includes subsequent clarifications provided by submitters to the Commission.

The conceptual framework

4. Most submitters agreed with the conceptual framework overall but had differing views about the most important attributes. Of those who commented on the conceptual framework:
 - Transpower maintains the key issue is the trade off between price certainty and price accuracy. Transpower also notes that different parties will assume more or less risk depending on where the emphasis is placed within the framework;
 - Contact considers the most important attributes to be robustness and authoritativeness;
 - Meridian believes accuracy is the most important attribute;
 - Genesis agrees that robustness and authoritativeness are key attributes, but considers timeliness, accuracy, simplicity and transparency to also be important; and
 - Mighty River Power believes predictability and accuracy are the most important attributes.
5. Submitters’ views on the most important attributes are summarised below:

	Certainty		Accuracy	Robustness	Simplicity	Transparency
	T ¹	P ²	A ³			
Contact		x		x		
Meridian			x			
Genesis	x	x	x	x	x	x
Mighty River		x	x			
Transpower	Trade off between certainty and accuracy					

¹ Timeliness

² Predictability

³ Authoritativeness

The Commission considers the conceptual framework incorporates the key attributes of an efficient pricing process. While there are differing views between submitters on the most important attributes, the Commission believes the framework provides a useful basis for assessing initiatives affecting the pricing process.

Settlement on five minute prices

6. There were widely differing views on settlement on five minute prices.
 - Genesis and M-co supported settlement on next day five minute prices;
 - MEUG supported settlement on ex-post five minute prices;
 - Simply Energy supported settlement on ex ante five minute prices; and
 - Meridian, Transpower Todd and Mighty River did not support settlement on five minute prices.
7. Most submitters noted the practical difficulties associated with moving to settlement on five minute prices. Key hurdles and costs included:
 - Improving the accuracy of SCADA-based demand estimates;
 - Addressing differences between forecasting and pricing methodologies;
 - Resolving infeasibilities;
 - Upgrading meters (both generator and oftake);
 - Upgrading generator software (for example, database changes, application changes, billing and settlement changes);
 - Changes to contracts (for example, financial contracts); and
 - Effects on constrained-on and constrained-off payments.
8. Some submitters considered that the benefits of settlement on 5 minute process were unlikely to exceed the costs.

Due to the Commission focussing on other priorities and the technical hurdles noted above, it is unlikely that further work on settlement on five minute prices will be undertaken within the next 12 months. Once work on this initiative does resume, however, the next stage will be for the Commission to undertake a full cost-benefit analysis.

Interim pricing period

9. All submitters supported the introduction of an interim pricing period.
10. Submitters had varying views on whether there should be a clear cut rule for deciding which types of errors should be corrected in final prices, or whether the Commission should have some discretion in the process. Some submitters supported a combination of both these options.
11. The preferred duration of the interim pricing period ranged from 5 hours (if only a high level description of the potential pricing error was required) up to between 1-3

days. Submitters generally supported the view that the period should be as short as possible to avoid affecting the settlement process.

The Commission intends to develop a proposal for an interim pricing period, including full cost-benefit analysis and draft rules. The details of the proposal, in terms of which errors should be corrected and the duration of the interim period, will be developed with further input from interested parties.

Aligning the pricing process with the dispatch process

12. The majority of submitters supported the inputs into the pricing process being based on initial conditions (Todd, Transpower, Meridian, MRP, M-co) with only Genesis supporting the inputs being based on the first feasible dispatch solution.

13. Arguments in support of basing pricing inputs on initial conditions included:

- The concept that pricing is based on ‘contractual’ conditions at the start of the trading period is a good one. It means that issues that arise intra trading period due to unforeseen circumstances can be likened to an FM event and the relief available under that contract (Todd);
- The ‘initial conditions’ is the market design and the basis for the willing buyer/willing seller contract (Transpower);
- Delays in the dispatch schedule process (which may increase under MSP) provide too much uncertainty (Meridian);
- Any action by the SO (e.g. for security) will result in sub-economic dispatch and an overall increase in cost to the market. Basing pricing inputs on a dispatch schedule is only feasible if ancillary services are also optimised in SPD (MRP); and
- The pricing process was designed to provide a ‘natural audit’ of the dispatch process as opposed to it replicating dispatch (M-co).

14. Arguments in support of basing pricing inputs on a dispatch schedule included:

- This would not reduce authoritativeness or heighten the need for system operator oversight. After all, the system operator already uses the dispatch schedule to dispatch generation (Genesis).

Based on support from the majority of submitters, the Commission intends to develop a proposal to base the inputs into the pricing process on the initial conditions of the trading period. The proposal will include a full cost-benefit analysis of all the options and draft rules for the preferred option.

Accuracy of metering information

Metering situation trigger

15. Most submitters (Contact, Genesis, Meridian, MRP) considered that the level of data estimation currently allowed to flow through into final prices is too high. Only M-co considered the current level of data estimation to be appropriate.
16. There was general support for the Commission to do further work to quantify the current level of data estimation that flows through into final pricing and the impact this has on price.
17. There was also general support for the Commission to investigate further options for reducing the amount of estimated data flowing through into final prices. Submitters generally supported a review of the metering situation trigger and publishing the annual consumption list monthly, but some submitters suggested additional options be considered first (some felt the proposed options were too timid).
18. Several submitters also suggested the Commission address the cause of the problem – accuracy of metering data.

The Commission has asked the Pricing Manager to monitor the current level of data estimation that flows through into final pricing, and to quantify the impact this has on price. Depending on the outcome of that analysis, the Commission will then investigate further options for reducing the amount of estimated data flowing through into final prices.

Data estimation

19. All submitters supported incorporating some flexibility into the definition of initial estimate to account for situations where the initial estimates are likely to be particularly inaccurate.
20. All submitters also supported a rule change to require an initial estimate to be provided when data is identified as being incorrect, rather than just when data is not available.
21. Several submitters raised concerns about how data would be identified as being incorrect, and by whom, and whether there would be any impact on existing timelines.

The next step is for the Commission to develop detailed rule change proposals for these initiatives, including full cost-benefit analyses, and seek further feedback through the consultation process.

Obligations for providing metering information

22. All submitters supported removing the requirement for generators to provide metering information directly to the pricing manager.

The next step is for the Commission to develop a detailed rule change proposal for this initiative, and seek further feedback through the consultation process. This initiative would likely be progressed as a minor rule change and would, therefore, not require a full cost benefit assessment.

Intermittent generator offers

23. All submitters supported using metered data from intermittent generation as an offer in the calculation of final prices.

The next step is for the Commission to develop a detailed rule change proposal for this initiative, including full cost-benefit analysis, and seek further feedback through the consultation process.

Clarity of the pricing process

Information on infeasibility and high spring washer price situation resolution

24. All submitting parties agreed that a document explaining the system operator's process for resolving infeasibilities and high spring washer situations should be published on the Commission's website. The only reservations were that the system operator's intellectual property is not infringed and that the costs remain low.

The system operator is currently finalizing the document explaining the system operator's process for resolving infeasibilities and high spring washer situations. The Commission will publish the document on its website by 30 June 2009.

Information on pricing inputs

25. All submitting parties agree that links to information on pricing inputs should be published on the Commission's website. Several parties requested that specific directions to the data within each site also be provided.
26. Transpower does not want to see the data itself published as this may impinge commercial sensitivity.

The Commission intends to include further detail in the table with specific links to information on pricing inputs, and then publish this on its website.

Redrafting pricing rules

27. Most submitters do not support a review of the pricing rules at this time and consider the costs and unintended consequences of such a review would far exceed the benefits.
28. Genesis suggests that publishing a clear set of pricing process flow charts would be more beneficial and incur lower costs

29. Of those who do support a review at this time:

- Transpower believes part G should be re-drafted in its entirety, especially in light of further proposed market design changes;
- Contact considers redrafting the pricing rules would result in less interpretation time for end users; and
- M-co believes any review of the pricing rules should be confined to removing inconsistencies. It does not support a significant redraft as it believes the current pricing rules work well and are understood by those who need to use them on a regular basis.

The Commission does not intend to undertake a review of the pricing rules at this time, but a review of the pricing rules will remain on the wholesale work plan, with a low priority.

The Commission has published the pricing process flow charts on its website, to assist participants to understand these rules. The flow charts are available at [insert hyperlink].

UTS

Appropriateness of criteria for determining a UTS as set out in regulation 55(1)

30. Submitters generally believe the UTS criteria are appropriate, and that other mechanisms exist (or should exist) within the Rules to address participants' concerns about pricing.

The Commission does not intend to propose any changes to regulation 55(1).

A UTS constitutes a rule breach with an extra element

31. Submitters are divided on whether, in order to be classified a UTS, a rule breach would normally have an extra element to it, such as an attempt at market manipulation or misleading or deceptive behaviour.

- Contact, Transpower and TrustPower agree with the Commission's assessment that a UTS would normally have an extra element to it; and
- Genesis, Meridian, Todd and MRP do not consider an extra element, such as market manipulation, is required.

32. Submitters are also divided on whether regulation 55(2)(d) (a UTS includes...material breach of any law) should be revoked, retained or amended.

- Contact believes regulation 55(2)(d) should be revoked so that it does not limit the intent of the UTS provision under the Regulations;
- Genesis, MRP and TrustPower believe regulation 55(2)(d) should be retained in its entirety; and

- Meridian and Transpower believe regulation 55(2)(d) should be amended to state that a UTS includes a “material breach of any law, other than a breach of the rules or regulations”.

Due to the wide disparity of views on the interpretation of the UTS regulations, the Commission considers that these regulations should be clarified, to ensure that all participants and service providers have a common understanding. The Commission intends to develop a proposal to clarify the meaning of the UTS regulations.

Changes to the way the Commission investigates UTS claims

33. The majority of submitters do not think there need to be any changes to the Commission’s process for investigating UTS claims.
34. Two submitters MRP and Meridian would like to see improvements to the timeliness of the investigation process. MRP suggested introducing a timeframe of five business days for resolution.

The Commission is aware of the need to resolve UTS claims as quickly as possible, however, it may be impractical to impose a firm timeframe for completing this process. While the Commission does not intend to make any changes to the process for investigation UTS claims at this time, it will strive to improve the timeliness with which UTS claims are resolved.

UTS remedies

35. All submitters believe the UTS remedies are appropriate and, in the event of a UTS, the Commission should have wide reaching powers to resolve the UTS.
36. Submitters generally felt that the Rules should be amended to ensure that, if a UTS has been declared and in order to resolve the UTS the Commission directs participants or service providers to act in a manner that is inconsistent with the Rules or Regulations, this wouldn’t be considered a breach.

The Commission intends to develop a proposal to ensure that, when a UTS has been declared, participants are not in breach of the Rules or Regulations if they follow the Commission’s instructions to act in a manner that is inconsistent with the Rules or Regulations.

Closing out at a specified price

37. Four submitters (Genesis, M-co, Meridian and Transpower) believe that the Rules should be amended to clearly state that the Board may close out at a specified price if a UTS has occurred.
38. Meridian suggested deleting the last sentence of rule 3.27, replacing it with:

"However, the Board may order the pricing manager to republish the final price or final reserve price where the Board has found that an undesirable trading situation exists and the Board has amended that final price or final

reserve price under regulation 56(2)(c) of the Electricity Governance Regulations."

39. Three submitters (TrustPower, Contact and MRP) consider that final prices, once published as such, should stay final. TrustPower raised a concern around possible disputes regarding hedge settlements if final prices were able to be republished.

The Commission will seek further clarification from submitters on the issues that have been raised, and will test ideas with all parties before developing a more detailed proposal.

Compensation

40. Most submitters do not support giving the Rulings panel the power to award compensation in excess of the current penalty limits.
- Meridian and Genesis support this view, provided the Commission is able to close out at a specified price if a UTS has occurred. Meridian also noted that there are penalties and remedies in other laws, for example the Commerce Act, which may be invoked;
 - M-co also disagrees with an increase in the compensation levels because of the inherent difficulties in determining such levels;
 - Transpower raised concerns about the potential impact on service providers, who, unlike other industry participants, are subject to fixed fee arrangements; and
 - Todd Energy believes that parties adversely affected by a rule breach should receive some form of compensation but recognises that a breach by a service provider may be problematic in that it would advantage some parties while disadvantaging others. Todd consider further difficulties arise as parties are not able to insure against loss arising from third parties' actions that may, through rule breaches, affect wholesale market prices. Todd also notes that an interim pricing period provides an opportunity for parties to challenge prices prior to final publication and this could largely allow for resolution of material pricing errors resulting from a breach of the Rules.
41. Contact does believe the Rulings panel should be given the power to award compensation in excess of the current penalty limits. Contact believes that if a service provider or participant breach impacts financially on the market, that service provider or participant should be financially exposed to the impact of the breach.

The Commission does not intend to amend the compensation provisions at this time.

Next steps

42. Submitters generally agree with the next steps outlined in the consultation paper. Several submitters consider the interim pricing period initiative to be the most important initiative and suggest that this be developed first.

Summary table

43. The following table provides a summary of the discussion above.

Initiative	Priority	Next steps	Timeframe
Settlement on five minute prices	Low	Undertake full cost-benefit analysis.	Unlikely to be undertaken within the next 12 months.
Interim pricing period	High	Work with interested parties to develop a detailed rule change proposal, including full cost-benefit analysis, for an interim pricing period.	Consultation paper to be released by 30 June 2009.
Aligning the pricing process with the dispatch process	Medium	Develop a detailed rule change proposal, including full cost benefit analysis, to base the inputs into the pricing process on the initial conditions of the trading period.	Commencing July 2009.
Accuracy of metering information	High	<i>Metering situation trigger</i> – undertake analysis to monitor the current level of data estimation flowing into final pricing and its effect on price.	To be completed by 30 June 2009.
	Medium	<i>Data estimation</i> – develop detailed rule change proposal, including full cost benefit analysis, to incorporate flexibility in the definition of initial estimate and to clarify when an initial estimate is required.	Commencing July 2009.
	Medium	<i>Obligations for providing metering information</i> – develop a detailed rule change proposal (minor) to remove the requirement for generators to provide metering information directly to the pricing manager.	Commencing July 2009.
	Medium	<i>Intermittent generator offers</i> – develop a detailed rule change proposal, including full cost-benefit analysis, to use metered data from intermittent generation as an offer in the calculation of final prices.	Commencing July 2009.
Clarity of the pricing process	Medium	<i>Information on infeasibility and high spring washer price situation resolution</i> – finalise document and publish on Commission’s website.	To be completed by 30 June 2009.
	Medium	<i>Information on pricing inputs</i> – include further detail in table, including specific links to information on pricing inputs and publish on Commission’s website.	To be completed by 30 May 2009.

Initiative	Priority	Next steps	Timeframe
	Low	<i>Redrafting pricing rules</i> – retain on wholesale work plan.	Unlikely to commence work within the next 12 months.
UTS	-	<i>Appropriateness of criteria for determining a UTS as set out in regulation 55(1)</i> – no changes required.	-
	High	<i>A UTS constitutes a rule breach with an extra element</i> – develop a proposal to clarify the meaning of regulation 55(2)(d).	Commencing May 2009.
	High	<i>Changes to the way the Commission investigates UTS claims</i> – strive to improve the timeliness with which UTS claims are resolved.	Commencing May 2009.
	High	<i>UTS remedies</i> – develop a proposal to ensure that, when a UTS has been declared, participants are not in breach of the Rules or Regulations if they follow the Commission’s instructions to act in a manner that is inconsistent with the Rules or Regulations.	Commencing May 2009.
	High	<i>Closing out at a specific price</i> – seek further clarification from submitters on the issues that have been raised and test ideas with all parties before developing a more detailed proposal.	Commencing May 2009.
		<i>Compensation</i> – no changes required.	-