



MAJOR ELECTRICITY USERS' GROUP

5 October 2009

Kate Hudson
Electricity Commission

By email to submissions@electricitycommission.govt.nz

Dear Kate

Submission on Interim Pricing Period rule change proposal

1. This is a submission by the Major Electricity Users' Group (MEUG) on the Electricity Commission *Consultation Paper: Interim Pricing Period*, dated 4th September 2009¹ (the "consultation paper").

Benefits versus costs

2. The consultation paper notes²
"The interim pricing period proposal would improve both the accuracy and predictability of prices, but may reduce the timeliness and certainty of prices. Overall, the Commission believes the benefits of the proposal would exceed the costs."
3. We agree the interim period proposal will improve accuracy and predictability. However the risk of final prices being based on data or process errors to date has been very low and the value impacts to date have been relatively modest³. Assuming the past is a good indicator of the future; then the likely benefit of the proposal is very small.
4. The consultation paper suggests the proposal will lower the risk to suppliers and hence lower their cost of capital. MEUG disagrees. We find it hard to believe this rule change proposal will be sufficiently material that:
 - a) The equity and debt markets will change the cost of capital used for assessing the value and risk of electricity suppliers relative to all other sectors of the economy; and
 - b) The electricity companies themselves will change their internal target rate of return for projects to reflect any change in risk.
5. The Commission could verify with the equity and debt markets and companies themselves as to whether the cost of capital will change as a result of this proposal.
6. We agree there is a cost of adopting the interim period proposal because final prices will, when the proposal is triggered, be later than the status quo. Because the frequency of errors to be

¹ Refer <http://www.electricitycommission.govt.nz/consultation/interim-pricing/view>

² Refer consultation paper, Executive Summary, page A

³ Ibid, paragraph 1.1.3 notes 2 events since 1st March 2004. First, Bay of Plenty event on 24th April 2004 with \$389,000 cost to participants. Second, Wilton T8 event on 28th April 2006 with \$225,000 cost to participants.

covered by the proposal have in the past been very low and are expected to be very rare events in the future, the reduced timeliness and price certainty associated with the proposal will also be small.

7. The consultation paper uses an estimate that the cost of software changes will be less than \$1m⁴. No further accuracy is needed because the cost of capital benefits is assumed in the consultation paper to be several times greater than \$1m. However if our analysis above is correct and the cost of capital benefits are not material, then whether the implementation costs are closer to \$1m or \$50,000 become important, eg:
 - a) At the lower end of costs the proposal should proceed because there is an obvious flaw in the rules (ie known data and process errors lead to final prices without any remedy) and a modest cost of \$50,000 would be within the margin of error of estimating the benefit of improving the rules.
 - b) At the higher range of costs it is not clear the benefits would exceed the relatively high implementation costs. In this case the Commission may have to consider other options such as deferring modifications to software and processes until other changes to the pricing processes or Part G of the rules are implemented to gain economies of scope.

Objection to claims for an interim price being restricted to market participants

8. MEUG is very concerned the proposal will limit parties that can lodge claims to trigger an interim price only to participants⁵.
9. This is a significant change in the philosophy of the rules that have endeavoured to include all affected parties not just those directly affected. For example:
 - a) The ability to request a public conference after a notice of intention to approve a Grid Upgrade Plan is not restricted to parties that directly pay transmission charges⁶.
 - b) The rules provide for broad consultation on System Operator Common Quality Policy Statements and Ancillary Services Procurement Plans not just with parties that directly pay those charges.
 - c) Any party can claim an Undesirable Trading Situation⁷.
10. We see no downside risk to allowing any affected party to lodge a claim to trigger an interim price. Only valid claims will lead to the interim price rules being triggered. Possibly the Commission was concerned there may be excessive non-valid claims from non-participants requiring additional Pricing Manager resources. That is unlikely to be an ongoing problem because precedents would quickly be established and frequent repetitive non-valid claims quickly identified and dismissed. On the other hand, restricting access to non-participants will erode public confidence in now transparent the market is and reinforce the view this is a suppliers market.
11. MEUG recommends the Commission allow any affected party, not just participants, to lodge a claim to trigger an interim price.

Yours sincerely



Ralph Matthes
Executive Director

⁴Ibid, paragraph 3.4.14

⁵ Ibid, paragraph 3.2.6

⁶ Electricity Governance Rules, Part F, Section III, rule 15.2

⁷ Refer EC report, Undesirable Trading Situations Guidelines for Participants, version 2.0, from 1 December 2004, opening paragraph to section 3.1 states (<http://www.electricitycommission.govt.nz/pdfs/rulesandregs/uts/utspdfs/utsv2.pdf>) :

"There is no limit on who may register a complaint to the Board about a UTS or potential UTS. Refer Regulation 65(1) which reflects the principle that complaints are filtered with reference to substance rather than form."