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By email: submissions@ea.govt.nz

Dear Fraser

Proposed Code amendments relating to the system operator and alignment with the statutory objective

We welcome the opportunity to comment on the Authority's consultation *Proposed Code amendments relating to the System Operator and alignment with the Statutory Objective*, published 8th December 2015 and as amended by corrigendum published 12th January 2016.

Transpower is committed to delivering an efficient system operator service that promotes reliable supply, competition and efficient operation and we support the direction of the changes proposed. In our submission we detail our response to all of the proposed Code changes but we wish to highlight the following two areas:

- the application of the reasonable and prudent system operator (RPO) standard
- market operation service provider (MOSP) alignment with the Authority's Statutory Objective (promoting competition, reliability and efficiency, referred to as 'CRE').

In both cases we are concerned about the potential for a significant increase in participant Code breach allegations against the system operator and therefore increased costs. The risk of speculative Code breach allegations is increased by the asymmetric costs that are low to an initiator and relatively high to the respondent and the Authority. We do not share the Authority's view that the proposed RPO and CRE changes will not create significant additional costs.

In the two appendices we answer the questions (Appendix A) and we provide comment and drafting suggestions against the proposed Code (Appendix B). Appendix B is submitted as a separate document to show the marked-up commentary.

Application of the reasonable and prudent system operator (RPO) standard

The Authority has proposed changing the application of the RPO standard from the specific system operator obligations in the Code to a general obligation across the entire system operator role. We accept and support the Authority's rationale that the benefit is to assure industry that system operator services are expected to be delivered to an accepted standard.

However, we consider that the use of the undefined term “role” in proposed clause 7.1A (1) creates the risk that the system operator will be exposed to allegations that it has breached the RPO standard for obligations that are contained only in the system operator service provider agreement (SOSPA). That would be contrary to the intent of the SOSPA parties because the system operator’s obligations and duties under the SOSPA are owed solely to the Authority.¹

To remove this risk we suggest the RPO standard described at clause 7.1A(1) applies only to the system operator obligations specified in the Code i.e. *the system operator must carry out its obligations under this Code ~~role~~ with skill, diligence, prudence, foresight, good economic management, and in accordance with recognised international good practice....*

We have proposed this drafting in Appendix B.

Alignment with the Authority’s statutory objective (CRE)

We consider the general drafting of proposed clause 3.2A is unclear and creates risk and could be improved to:

- accommodate the different ways and timetables for each MOSP to assist the Authority to give effect to CRE
- reduce the risk of speculative breach allegations against MOSPs, including for breach of the MOSPs’ obligations that appear only in their service provider agreements.

We consider that it is better and more logical for each MOSP to have specific and tailored CRE obligations in its service provider agreement, as already modelled in the new SOSPA. The Code would still oblige MOSPs to be aligned with CRE (as the Authority intends) but achieve it by cross-referencing service provider agreements for the details.

The Authority appears to have implicitly adopted this approach in paragraph 4.2.4 of the consultation paper where the word “progressively” in proposed clause 3.2A(2) is described to mean that “*the system operator will be progressively updating its policies and procedures...in a manner that provided [sic] for consistency with the Authority’s statutory objective.*” That understanding of “progressively” arose from the new SOSPA, which includes setting a process for specific system operator policies and procedures to be reviewed each year. However, the Authority’s suggested interpretation of the general CRE obligation it is proposing may not necessarily be shared by participants or the Rulings Panel. The system operator and other MOSPs could find themselves in the position of doing everything they are required (and paid) to do under their MOSPs for CRE but still be in breach, or at least alleged to be in breach, of the general CRE obligation in the Code.

In Appendix B we have proposed alternative drafting for clause 3.2A to refer to individual MOSP service provider agreements. We consider this change will better promote the statutory objective, specifically efficient operation, by reducing the risk of any unnecessary costs arising from speculative breach allegations and by using contract discussion processes to identify the effective means by which CRE assistance for each MOSP is progressively met.

¹ We note that the RPO standard is not irrelevant to SOSPA-only obligations. Both the current SOSPA and the new one under negotiation state expressly that the system operator must perform its SOSPA-only obligations to the RPO standard. However, breach of that obligation is a private contractual matter between Transpower and the Authority.

If the Authority decides to continue with proposed clause 3.2A as drafted then to remove the risk (removal of which we consider will better promote the statutory objective) we suggest the following.

- Replace the word “role” with “obligations under this Code” so that so that service provider agreement-only obligations are not captured.
- Apply proposed clause 3.2A (2) to all MOSPs as it is unlikely that any of them can immediately comply with proposed 3.2A (1).
- Add that proposed clause 3.2A (4) also applies to the Electricity Industry Act 2010 and all regulations made under it.

Other comment on Code amendments

We do not believe that there is any benefit of the Authority’s proposal to remove the definitions of “reasonable and prudent system operator” and “frequency time error” from Part 1 and relocate them into Part 7. Relocating the definition of RPO will require consequential changes to the policy statement, ancillary services procurement plan and SOSPA, among other things, which creates unnecessary cost. We suggest that all definitions should remain in Part 1 as there appears to be no ‘efficient operation’ benefit in having some definitions distributed across the Code when the majority of others are able to be easily located in one place.

Finally, we have noticed a number of clause cross-references that may require consequential changes depending on the decision for the final Code changes. We have indicated one of those, (in clause 8.11(3)) in Appendix B. There are others in clauses 8.3, 8.18, 8.20 and 8.31 and clause 5(4) of Technical Code A.

We would be happy to meet to discuss this submission further, please do not hesitate to contact me.

Yours sincerely

A handwritten signature in black ink, appearing to be 'JC' followed by a long horizontal stroke and a small flourish at the end.

Jeremy Cain

Regulatory Affairs & Pricing Manager

Appendix A – Questions and answers

	Question	Response
1.	<p>Do you agree that the proposed Code amendments relating to the system operator would better give effect to the requirements of section 8(3) of the Act?</p> <p>If not, please explain why not.</p>	<p>As the Authority has presented no ‘status quo’ assessment of the nature of Code provisions (in relation to functions, transparency and performance) it is difficult to conclude that the proposed Code amendments relating to the system operator would ‘give better effect to’ section 8 (3) of the Act.</p> <p>This point aside, Transpower supports the direction of change, and is committed to delivering a system operator service that promotes reliable supply, competition and efficient operation.</p>
2.	<p>What improvements, if any, should the Authority make to the proposed Code amendments relating to the system operator to better give effect to the requirements of section 8(3) of the Act?</p>	<p>We have made drafting suggestions and comment at Appendix B of this submission, to the following</p> <ul style="list-style-type: none"> • Definitions • Clauses 3.1, 3.2A • Clauses 7.1A, 7.2A, 7.2B, 7.2D, 7.2E, 7.3, 7.11 • Clauses 8.11, 8.14, 8.60, 8.61 • Clause 13.102
3.	<p>Do you have any comments or suggested drafting improvements regarding the proposed Code amendments relating to the system operator? Please provide comments and suggested drafting improvements with reference to the clauses set out in Appendix A.</p>	<p>We suggest the RPO standard described at clause 7.1A(1) applies only to the system operator obligations specified in the Code i.e. <i>the system operator must carry out its obligations under this Code role with skill, diligence, prudence, foresight, good economic management, and in accordance with recognised international good practice....</i></p> <p>We would prefer this RPO definition to remain under Part 1; relocating it will require consequential changes to the policy statement, ancillary services procurement plan and SOSPA, among other things, which creates unnecessary cost.</p>
4.	<p>What improvements, if any, should the Authority make to the proposed statutory objective alignment requirement to better promote the statutory objective.</p>	<p>In Appendix B we have proposed alternative drafting for clause 3.2A to refer to individual MOSP agreements. We consider this change will better promote the statutory objective, specifically efficient operation, by reducing the risk of any unnecessary costs arising from speculative breach allegations and by</p>

		identifying the means by which 'progressively' can be met.
5.	Do you agree that the proposed new clause 3.2A (2) and (3) that would apply to the system operator alongside the statutory objective alignment requirement, promotes the statutory objective? If not, please explain why not	<p>In part. We agree with the need to ring-fence real-time operations from the CRE assistance obligation as expressed by new clause 3.2A (3). We also agree with the intent of the new clause 3.2A (2) that recognises that 'assistance' cannot be immediate. However, we consider our proposed drafting for clause 3.2A better promotes the Statutory Objective for reasons given at question 4.</p> <p>If the Authority decides to continue with proposed clause 3.2A as drafted then to remove the breach allegation risk (removal of which we consider will better promote the statutory objective) we suggest the following.</p> <ul style="list-style-type: none"> • Replace the word "role" with "obligations under this Code" to signal that breach allegations only apply to Code obligations. • Apply proposed clause 3.2A(2) to all MOSPs as it is unlikely that any of them can immediately comply with proposed 3.2A (1) • Add that proposed clause 3.2A (4) should also apply to the Electricity Industry Act 2010 and all regulations made under it.
6.	Do you have any comments or suggested drafting improvements regarding the proposed new clause 3.2A? Please provide comments and suggested drafting improvements with reference to specific provisions of the proposed new clause 3.2A set out in Appendix A	<p>Below, and in Code drafting comments at Appendix B of this submission.</p> <p>3.2A Market operation service providers to assist Authority to give effect to Authority's statutory objective</p> <p>(1) Each market operation service provider agreement must require the market operation service provider to perform its role in a way that assists the Authority to give effect to the Authority's statutory objective.</p> <p>(2) Each market operation service provider agreement that does not include the obligation referred to in sub clause (1) is deemed to include that obligation.</p> <p>(3) If a market operation service provider agreement includes provisions that set out specifically how the market operation service provider is required to assist the Authority to give effect the Authority's statutory objective, the obligation referred to in sub clause (1) will be fulfilled if the market operation service provider</p>

		<p>complies with those provisions.</p> <p>(4) Despite anything to the contrary in the market operation service provider agreement:</p> <p>(a) the system operator is not required to comply with the obligation referred to in sub clause (1) when exercising discretion in real time in performing its functions; and</p> <p>(b) the obligation referred to in sub clause (1) does not permit a market operation service provider to contravene the Act, any regulations made under the Act, or this Code</p>
7.	Do you agree with the objectives of the proposed Code amendments that relate to the system operator? If not, please explain why not.	In part, our Code drafting comments at Appendix B of this submission.
8.	Do you agree with the Authority's evaluation of the costs and benefits of the proposed Code amendments that relate to the system operator? If not, please explain why not.	We consider that the balance of costs and benefits of the proposed changes should result in a net benefit to consumers.
9.	Do you agree with the Authority's evaluation of alternative means of achieving the objectives of the proposed Code amendments that relate to the system operator? If not, please explain why not	Yes
10.	Do you agree with the objective of the proposed statutory objective alignment requirement? If not, please explain why not.	Yes we agree with the policy intent. In our submission we suggest an alternative means to meet the policy objective for CRE assistance, see response to Q4 and 5.
11.	Do you agree with the Authority's evaluation of the costs and benefits of the proposed statutory objective alignment requirement? If not, please explain why not	In part. While we agree with the Authority's assessment that the administrative costs of the proposed changes are negligible, the changes potentially increase compliance costs resulting from alleged breaches of this clause. Our alternative drafting for 3.2A (see Appendix B) is to mitigate this risk.
12.	Do you agree with the Authority's evaluation of alternative means of achieving the objectives of the proposed	See response to question 10.

	<p>statutory objective alignment requirement?</p> <p>If not, please explain why not.</p>	
13.	<p>Do you agree with the Authority's assessment of the proposed Code amendments against section 32(1) of the Act?</p> <p>If not, please explain why not.</p>	Yes.
14.	<p>Do you agree that the Authority's proposed Code amendments comply with the Code amendment principles? If not, please explain why not</p>	Yes.