11 Chews Lane
PO Box 10568
The Terrace
Wellington 6143
New Zealand

Genesis Power Limited
trading as Genesis Energy

Fax: 04 495 6363

27 September 2010

Bruce Smith

Electricity Commission

2 Hunter Street

WELLINGTON

By email: submissions@electricitycommission.govt.nz

Dear Bruce

Transmission Pricing Review: Stage 2 Options

Genesis Power Limited, trading as Genesis Energy, welcomes the opportunity to provide a submission to the Electricity Commission ("the Commission") on the consultation paper "Transmission Pricing Review: Stage 2 Options" dated July 2010.

Genesis Energy has not responded to the consultation questions directly, but provides its views below on the matters raised in the consultation paper.

Genesis Energy believes that the Commission's analysis confirms there is no compelling reason to prioritise work on reviewing the transmission pricing methodology. The gross features of the existing methodology appear sound and there are not any alternatives likely to present sufficient benefits to justify the wealth transfers, transition costs and disruption to regulatory stability that a change would entail.

The Commission should note that Genesis Energy's position on transmission pricing is based on the perspective of a national generator and retailer. In particular, Genesis Energy:

- will be exposed to the high-voltage direct current (HVDC) charge when it acquires the Tekapo A and B power stations;

- has several generation development prospects in the South Island (including the Slopedown wind farm development) that will face an HVDC charge if developed; and

- has a large North Island retail base and an expanding South Island retail base.

Timing

Genesis Energy is concerned that the Commission is targeting the 2012 pricing year for implementing any changes to the transmission pricing methodology. This requires decisions to be taken early next year when the "new matters" in the Electricity Industry Act 2010 should remain far higher priorities.

It is possible that implementing a locational price risk management (LPRM) tool will have implications for transmission pricing. However, this is best addressed by progressing the Commission's LPRM work as a priority. As LPRM decisions are made, the Electricity Authority (the Authority) can review whether any unavoidable need to alter the transmission pricing methodology arises. This approach would:

- allow the Authority to focus its resources on higher priority work (particularly conservation campaign pricing, curtailment and rolling outage pricing, LPRM, distribution pricing and distribution contracting);

- mean fewer elements of market design would be under review and hence there would be less uncertainty for market participants;[1] and

- send a signal that the Electricity Authority will not change the transmission pricing methodology without clear benefits.

Competition Benefits and Option Value

Genesis Energy notes that the consultation paper's discussion on theoretically optimum transmission investment is silent on the benefits of transmission capacity in supporting good competitive outcomes and on the "option value" provided by a robust grid. These omissions are likely to bias the Commission towards overrating the benefits of delaying and discouraging transmission investment or encouraging transmission alternatives.

[1] The Authority's task of analysing the costs and benefits of the new matters would also be slightly simpler.

HVDC Charge

As a soon-to-be South Island generator, Genesis Energy is comfortable with the "beneficiary pays" rationale for recovering the costs of the HVDC link from South Island generators. There is an enduring south to north power flow in New Zealand and South Island generators undoubtedly benefit from the higher prices that access to the larger and faster growing North Island market provides.

The Commission's analysis indicates that the locational signal provided by the HVDC charge has negligible effects on expected future system costs. It also indicates that an additional submarine HVDC cable is not likely to be required in the foreseeable future. Genesis Energy is comfortable that this analysis, coupled with regulatory stability concerns, is enough to discount further work on a tilted postage stamp methodology at this time given the Authority's other priorities. However, this analysis does not support an argument for bundling the HVDC charge into the interconnection charge.

The Commission's generation expansion model (GEM) and its statement of opportunity (SoO) scenarios provide only a crude forecast of a limited range of likely future states of the power system. Given the natural resources available in the South Island, there are any number of plausible scenarios in which net export capacity could increase sufficiently to justify further HVDC expansion. Similarly, there are plausible scenarios where the locational signalling effect of the HVDC link favours North Island generation sufficiently to reduce overall system costs. In any of these scenarios, the beneficiary pays rationale remains valid and the locational signalling value of the HVDC charge is, at worst, negligible.

Historical Anytime Maximum Injection (HAMI)

Genesis Energy is not convinced there are compelling reasons to move away from HAMI as the basis for allocating HVDC charges. Any allocation methodology will have some effect on behaviour and, in this case, the main effects appear to be a very slight deterrent to investment in South Island peaking capacity and some variance in the marginal HVDC charge on generation investments depending on the size of the investor's existing South Island generation portfolio. Neither of these distortions appear to be materially detrimental.

Genesis Energy considers that a "distortion free" allocation approach would detract from the beneficiary pays rationale of the HVDC charge and would eliminate any locational signalling benefits. All South Island generators, existing and future, benefit from the higher prices that the HVDC link produces by providing access to the North Island market.

A per-MWh allocation does not appear to provide a material benefit over the status quo and would depart from the logical link between generation capacity and transmission capacity.

Deferring or Avoiding Reliability Transmission Investments

Genesis Energy doubts that flow tracing or bespoke postage stamp options would provide sufficient benefits to warrant implementation. Similarly, Genesis Energy considers that a radical re-design of the transmission alternatives framework is not required.

Generally, an over-emphasis on deferring or avoiding reliability transmission investments is likely to be misplaced given the detrimental impact of grid constraints on competition and given the option value provided by a robust grid.

Genesis Energy considers that the operation of the transmission alternatives framework could potentially be improved without altering the framework itself. As such, this is a matter for the Commerce Commission to consider through its upcoming input methodology work in the first instance.

Reactive Power

Genesis Energy considers that there would be value in the Authority carrying out further work on reactive power, but that this is best pursued as a separate project that has a broader common quality, ancillary services and network regulation perspective. In any event, this work should be a lower priority than the new matters.

If you would like to discuss any of these matters further, please contact me on 04 495 3348.

Yours sincerely

RWParry

Ross Parry
Regulatory Affairs Manager

genesis ENERGY