

13 December 2022

Submissions  
Electricity Authority  
Via email: [reviewconsultation2022@ea.govt.nz](mailto:reviewconsultation2022@ea.govt.nz)

To whom it may concern,

**Promoting competition in the wholesale electricity market in the transition toward 100% renewable electricity — Octopus Energy Submission**

Thank you for the opportunity to comment on the issue paper ‘Promoting competition in the wholesale electricity market in the transition toward 100% renewable electricity’.

The electricity industry’s performance through the transition will have a significant impact on the productivity and well being of New Zealand energy consumers, so it is timely to consider if industry arrangements are fit for purpose now and in the future.

Octopus Energy is an entrant retailer to the New Zealand electricity market.

We bring significant operational experience and innovative technology and believe retailers have an important role to play in enabling a low carbon, affordable energy transition.

We are however concerned that the New Zealand market does not have the basic regulatory framework to ensure a level playing field and that new technologies and entrants to the market succeed based on capability and efficiency.

This letter outlines general comments on the regulatory change we believe is necessary to deliver the best outcomes for New Zealand’s electricity consumers. We also endeavour to provide answers to the consultation questions.

***Market power will deter or frustrate investment in new generation, it needs addressing with ex ante regulation***

Market power is a problem in the New Zealand electricity industry, and we agree it will worsen as the market transitions to more intermittent renewables.

In the absence of structural reform it will be important for the EA to ensure there are sufficient safeguards in place to protect consumers from unreasonably high prices.

The EA and Commerce Commission analysis of the sector over many years has identified that market power is often exercised. Relying on ex-post detection of these events (e.g

reliance on trading conduct provisions) is generally considered inadequate protection for consumers.

We strongly suggest considering ex ante measures to prevent harm (such as ‘automating’ a pricing adjustment whenever a generator is considered strategic to ensure consumers aren’t gouged, and regulated contract market auctions)<sup>1</sup>.

Poor competition dynamics will have a direct bearing on the rate at which new electricity generation comes to market.

Dominant incumbents will seek to maximise value over their existing portfolio so it is in their interests to delay such investment to maintain tight supply conditions with elevated prices.

Their inherent (and increasing market power) has the potential to increase costs and obstruct new investment. Unfortunately new entrants to the generation market rely on contracting with dominant incumbents because of the New Zealand market’s limited size.

The EA needs to consider implementing further protections to ensure entrant independent generators can access fairly priced risk management products.

Additionally, implementing regulation of dominant vertically integrated players: that requires arms length trading arrangements, no cross subsidies and no discrimination, would provide independent generators and retailers with more confidence in their ability to strike fair terms with the retail side of vertically integrated players, stimulate better risk management practices and market liquidity.

### ***Contract market failure needs immediate attention***

The EA needs to address major problems with the contracts market.

The current lack of access to a futures market is a major market failure that is not given the consideration it warrants in this report. An effective contracts market is a fundamental ingredient in an effective, efficient and investment friendly market.

The failure of this market impacts independent players more than those who are vertically integrated, not addressing the market failure increases the stronghold of dominant incumbent players.

### ***Realising optimal demand response requires addressing the incentives of vertically integrated players***

The EA has highlighted the potential for the demand side to become a more active participant in the wholesale market, and that this responsiveness will play an important role in affordability and balancing the system.

---

<sup>1</sup> Market Power Mitigation Mechanisms for Wholesale Electricity Markets: Status Quo and Challenges  
Christoph Graf\* Emilio La Pera† Frank A. Wolak§ June 20, 2021

There is significant potential to shift load (hot water, EV's, heating / cooling) to times of the day when there is more system capacity. The technology is available to do this today!

Independent retailers have a strong incentive to activate load shifting, and you can already see this at play in the pricing structures and technology (HH settlement and billing capability, automation of load) they bring to the market.

However, the market as a whole is unlikely to realise these benefits without regulatory changes because the market is dominated by integrated businesses who are typically long in generation. As a result they do not face the same enduring incentives to shift load and minimise costs, indeed they may have perverse incentives to the opposite. They've also been allowed to rely on discounted internal transfer prices rather than building capability to compete in the retail market.

Along with the need to balance intermittent generation with system demand, the carbon reduction and financial benefits of load shifting are clear.

The regulatory environment should ensure all retailers are deploying this capability and acting in the best interests of consumers to keep prices down. Vertical integration undermines this.

To address this perverse incentive we recommend arms length trading arrangements are introduced so that the retail arms of the vertically integrated gentailers are encouraged to respond to market signals to benefit consumers .

If you have any questions about this submission please contact me,

Yours sincerely

**Margaret Cooney**

Chief Customer Officer

[margaret.cooney@octoenergy.com](mailto:margaret.cooney@octoenergy.com)

[Octopusenergy.nz](http://Octopusenergy.nz)

+64 22 0441186

## **Consultation Questions**

### **Chapter 2**

*1. Do you agree that a key competition in the transition toward 100% renewable electricity is that it weakens competition during extended times when intermittent generation cannot run?*

**Yes, we agree. We have identified concerns in our introductory comments.**

*2. Do you have any comments on the contents of this chapter?*

**We have identified concerns in our introductory comments.**

### **Chapter 4**

*3 Do you have any comments on the impediments to generation investment?*

**Yes, in our view market power in itself is a major impediment to new generation investment.**

*4. Do you agree that the lag in investment is not due to anti-competitive behaviour to slow down investment and discourage entry, or can you provide instances or other evidence to the contrary?*

**We disagree with this, the investment environment is more nuanced.**

**We agree that uncertainty around Tiwai and government policy may have reduced the incentive to invest. However, the existing market structure with dominant incumbent players would on the face of it explain the slow rate of investment. These firms rationally optimise investment decisions taking into account the price impact on their whole portfolio, delaying investment has been highly profitable and is a predictable outcome of the existing market structure.**

*5. Do you have any comments on the role and impact of carbon pricing on investment and wholesale market competition or the other contents of this chapter?*

**Generation investment proposals appear to be largely focused on renewable projects so the market clearly understands the need for/value of these investments. We think this focus will remain almost regardless of carbon pricing, that said carbon pricing signals have an important role to play in investment decisions through the transition.**

## Chapter 5

*6. Do you agree with the Authority's overall conclusion that it currently considers that continued reliance on the current conduct-based measures to mitigate the exercise of market power remains broadly appropriate in the transition toward 100% renewable electricity?*

**No. We strongly disagree with the EA's conclusion and approach.**

**As highlighted in our introductory comments, conduct based tests are inadequate given the potential harm and track record of market power being exercised in the New Zealand electricity market. Internationally ex ante measures for preventing market power are preferred and we believe there is a strong case for implementing these in New Zealand.**

**We're supportive of the measures identified but in and of themselves they are inadequate at constraining the exercise of market power. We also note that the MDAG's recent work has suggested measures including an access code which we also support.**

*7. Do you agree with the objective and evaluation criteria set out in this chapter?*

**Yes.**

*8. Do you have any comments on the contents of this chapter?*

## Chapter 6

*9. Are there any other options that would promote wholesale electricity market competition in the transition that you consider would be more effective and efficient?*

**Higher than necessary prices are a drag on the economy and wellbeing of consumers.**

**Given the far-reaching implications for the New Zealand economy of deadweight loss from exploitation of electricity market power, a thorough consideration of options to address market power is necessary.**

**The EA should consider ex ante regulatory measures, such as automated price adjustments used in US electricity markets, that can be deployed to address market power.**

**We agree with the observation that intervention in price is a balancing act. However, leaving known market power problems unchecked always benefits dominant incumbent generators profiting from market power over consumers who pay for that.**

**The EA should also consider the merits of operational separation measures<sup>2</sup>. These would be relatively easy to implement to support more effective competition in both the retail and generation markets and stimulate contract market liquidity.**

**The EA should consider a mandatory auction of risk management products from dominant generation firms. This would mean that at a regular interval dominant parties are required to make available risk management products of a regulated volume, the price would be determined at auction which has the advantage of the price being determined in a competitive environment but the firm(s) can't exercise market power as they typically can.**

*10. Do you have any comments on the contents of this chapter?*

**The EA needs to consider the interplay between retail competition and wholesale market competition.**

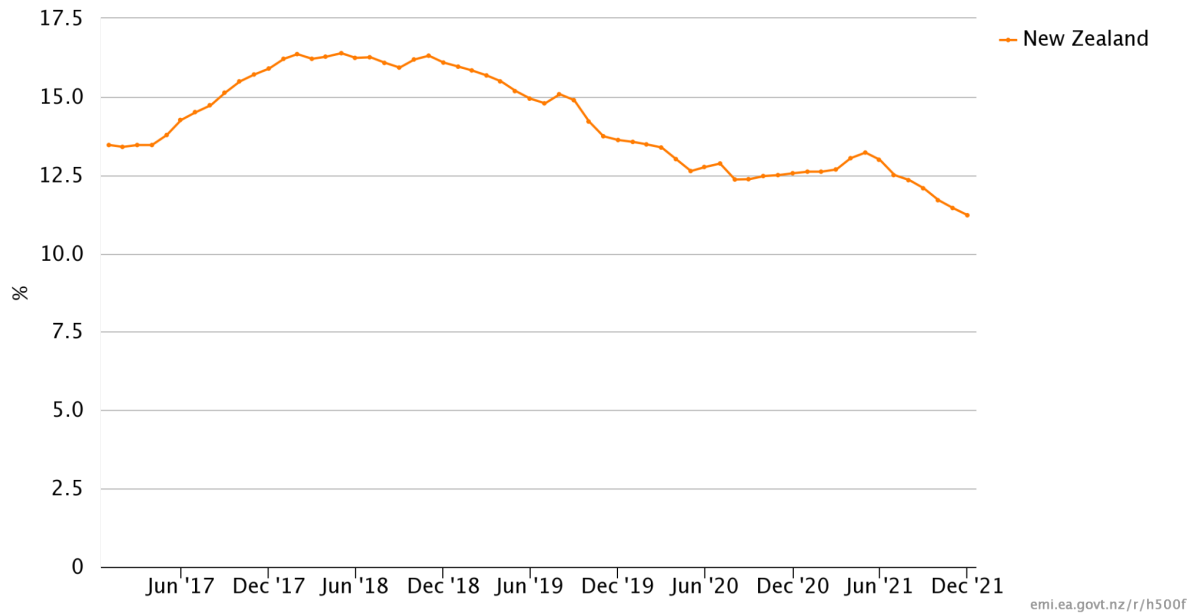
**An effective retail market is dependent on a well functioning wholesale market, and importantly, as we transition to more renewables, the retail market (as the facilitators of the demand side) will have a more central role to play in the wholesale market.**

**There is a persistent margin squeeze in the retail market impeding the ability of independent retailers to grow sustainably<sup>3</sup>. During the period of review there has been a retrenching of independent retailer customer acquisition as this margin squeeze persists. Retail competition has weakened as illustrated by the downward trend in trader switch volumes.**

---

<sup>2</sup> We've previously highlighted the UK's licensing requirements on vertically integrated firms as an example.

<sup>3</sup> Refer comments in Contact Energy's 2022 Full Year Results <https://www.youtube.com/watch?v=a7XB0qGH9Ho> disconnect between the market and retail prices commented on. In this respect it's important to note that Contact Energy has the benefit of an incumbent low churn base and a low internal transfer price v the cost of purchasing on the market.



**The decline in growth of independent retail should be of concern because these players have typically brought innovation and price competition to the market.**

**Failing to shore up retail competition will mean the benefits of new technology and competitive prices are not realised by consumers.**

**We believe that there is an immediate need to implement level playing field measures in the form of arms length trading arrangements for vertically integrated players, including a prohibition on cross subsidies and preferential contracting.**

## Chapter 7

*11. Are there any other options that would better facilitate efficient investment in renewable generation to promote wholesale electricity market competition in the transition?*

*12. Do you have any comments on the contents of this chapter?*

