



5 November 2020

Submissions  
Market Development Advisory Group  
Electricity Authority

By email: [MDAG@ea.govt.nz](mailto:MDAG@ea.govt.nz)

### **Supplementary Consultation: High Standards of Trading Conduct (HSOTC)**

Contact welcomes the updated proposal. The revised proposal has addressed concerns identified by submitters with the earlier proposed clause and purpose statement and is consistent with subsequent analysis undertaken by the independent evaluation panels.

#### **Operative Clause**

Contact agrees that the proposed updated rule is sound and is clearer than the existing HSOTC rule in the Code.

We also support the proposed drafting amendments to the operative clause. In particular, we support making clear that the test is based on an objective view based on the generator acting in an economically rational way – *the generator, acting rationally, would have made*.

#### **Purpose Clause**

Contact agrees with the panels' view that the proposed purpose clause creates ambiguity, and is overly complex and long. We agree with MDAG's subsequent view that the purpose clause risked being an overly simplistic comparison between prices and costs to determine whether the operative clause had been breached.

We support the recommendation to delete the purpose clause, and replace this with a simplified preamble clause. Clause (1) of the preamble provides useful guidance:

- Recognition that **normally / ordinarily** competitive discipline means that no party will have significant market power – clause (1)(a);
- Recognition that at **some locations** or for **some periods**, weakened competition may result in one or more generators may have significant market power – clause (1)(b).

This clause correctly recognises the predominance of competition and resulting competitive discipline that occurs in the New Zealand spot market.

We also support the addition of clause (3). Clause (3)(a) clarifies that market power becomes significant based on a net adverse impact on economic efficiency. The clause also ensures that any impact is assessed across both static (productive and allocative) and dynamic efficiencies. This correctly recognises that generators should be able to recover long run marginal costs over time, and incentives for future efficient investment in generation for the long-term benefit of New Zealanders.

Finally, we strongly endorse MDAG's observation that:



*In New Zealand's energy-only, hydro-dominated system, opportunity costs of hydro fuel (water) and scarcity rents are relatively significant and highly variable. In economic efficiency terms, it is important that both are fully reflected in wholesale prices.*

### **Market Uncertainty**

Contact supports the revised proposal being finalised and provided to the Electricity Authority for its consideration.

However, changes to the High Standards rule in the Code may introduce additional uncertainty in the wholesale market for the following reasons:

- With any new test, clarity with how the proposal specifically operates will take time, as the Authority considers any allegations of breach, the wording and its application, and subsequent precedents that are set.
- The new standard covers any spot market offer, with the Authority having to objectively apply the *Significant Market Power* test in each instance. In contrast, the safe harbour provision under the existing HSOTC provisions applied where a generator was not pivotal – rightly or wrongly reducing the number of trading periods where the HSOTC test might be applied.
- Responding to investigations into HSOTC allegations is time-consuming, expensive and can have reputational impacts – irrespective of the ultimate outcome of such investigations. These impacts do not fall evenly between complainants and respondents to an allegation. As a result, the risk of multiple and vexatious allegations remains.

To address these risks, Contact recommends that:

1. the Authority directly consult with the market on the MDAG recommendation if it intends to progress these changes;
2. the Authority review its resourcing to efficiently manage future HSOTC allegations, and consider active market monitoring; and
3. the Authority make early assessments of HSOTC allegations, potential materiality and whether there are sufficient grounds to progress, or alternatively close, an investigation.

Your sincerely,

A handwritten signature in blue ink, appearing to read "Chris Abbott".

Chris Abbott  
**GM Regulatory Affairs & Government Relations**