



4 November 2020

Submissions
Market Development Advisory Group
Level 7, ASB Bank Tower
2 Hunter Street
Wellington

By email: mdag@ea.govt.nz

Trustpower Limited
Head Office
108 Durham Street
Tauranga
Postal Address:
Private Bag 12023
Tauranga Mail Centre
Tauranga 3143
F 0800 32 93 02
Offices in
Auckland
Wellington
Christchurch
Oamaru
Freephone
0800 87 87 87
trustpower.co.nz

TRUSTPOWER SUBMISSION: REVIEW OF THE TRADING CONDUCT PROVISIONS: SUPPLEMENTARY CONSULTATION PAPER

1. Initial Remarks

1.1. MDAG proposal

- 1.1.1 Trustpower Limited (**Trustpower**) welcomes the opportunity to provide a submission to the Market Development Advisory Group (**MDAG**) on its *Review of the trading conduct provisions: Supplementary consultation paper (the Consultation Paper)*.
- 1.1.2 The MDAG proposes to replace the current high standard of trading conduct (**HSOTC**) provisions (clauses 13.5A and 13.5B) with new trading conduct provisions centred around a No Significant Market Power (**NSMP**) standard for generator and ancillary service offers into the spot and reserves markets.
- 1.1.3 The MDAG believes its new provisions will improve the efficiency of wholesale electricity spot prices in circumstances where competition is weak.

1.2. Problem definition

- 1.2.1 We remain disappointed that the MDAG have focussed on improving drafting clarity rather than first identifying the extent to which the wholesale market suffers problematic levels of competitiveness.
- 1.2.2 This leaves us still asking the following fundamental questions around the proposed reforms:
 - (a) Is the MDAG looking for a solution to a situation where the MDAG believes there is currently no competition, some competition, workable competition for the most part, or rarely any competition?
 - (b) Does the MDAG consider that the state of competition matters in each half hour at every node or in regions over time?
 - (c) Is a regulatory solution preferable to a market one (such as increased demand response or market entry to compete away any excess returns)?
- 1.2.3 All regulatory change embodies risk for the regulated market participants. It follows that all reform needs to be founded on robust analysis, which both clarifies and quantifies the problem.

1.2.4 Regulated parties, in particular, need to know if the proposed solution (especially one which removes safe harbours and applies to all traders in every trading period irrespective of whether they are net pivotal or not) is proportionate to the identified problem.

1.3. Scope of preferred solution

1.3.1 We note that the MDAG proposal refers to generator offers and those of ancillary service agents. We think it is important that any market obligations are symmetrical and, thus, we consider that the conduct obligations should apply to the demand side as well (to the extent practicable).

1.3.2 This aligns with the MDAG's prior views on technology neutrality.

1.3.3 We also question whether there should be an exclusion from "good conduct" for participants in the financial transmission rights (**FTR**) market.

2. MDAG process

2.1. Case study testing of the trading conduct provisions

2.1.1 During the previous consultation, Trustpower submitted that further work needed to be done (through the development of case studies, for example) to demonstrate how the proposed new provisions might apply "at the trading desk" to see if, in fact, these rules will provide a "clearer standard".

2.1.2 Other submitters made similar suggestions.

2.1.3 We were very pleased that the MDAG convened two panels of considerable experience to test its initial proposal.

2.1.4 We consider this to be a very useful process and believe it should be utilised again in the future as it yielded a number of important insights.

2.1.5 We also appreciated the opportunity to have two meetings with the MDAG Chair to discuss the proposed changes. This was of great assistance to our understanding of the drivers behind the proposal.

2.2. Cost benefit analysis

2.2.1 Notwithstanding the above, we would still like to see a more comprehensive cost benefit analysis (**CBA**) from either the MDAG or the Authority as part of its Code change proposal.

2.2.2 This CBA needs to consider the extent to which market power is currently a problem (and hence the size of the expected benefits of this reform).

2.2.3 It also needs to robustly assess the costs and risks of the proposal, including those associated with:

- (a) removing market participants' ability to use their offer prices to hedge transmission risks,
- (b) recovering a margin for operating at times of transmission congestion;
- (c) creating incentives for set and forget offers; and
- (d) the additional compliance costs, which some parties have suggested could be considerable).

3. Trustpower's responses to consultation paper questions

3.1. Do you agree that the proposed 'rule' [clause 2] is better than the existing provision requirement for "conduct in relation to offers and reserve offers is consistent with a high standard of trading conduct"?

3.1.1 In short, possibly.

3.1.2 The current HSOTC rules do not stand on their own, they are accompanied by safe harbour clauses and a requirement that a generator be net pivotal. Taken as a whole, these provisions have, as we have indicated in prior submissions, given us comfort around the behaviour that is, and is not, permitted.

3.1.3 We appreciate that may not be true for all market participants, particularly those who are often net pivotal. For these participants, the new test may provide more clarity.

3.1.4 However, for our business, this proposal means we are moving away from a clear rule to a new standard with an associated compliance and interpretation risk.

3.2. Do you agree that the economic efficiency framework underpinning the proposed 'rule' is better than the existing HSOTC framework?

3.2.1 The economic framework is useful provided there is clarity around both the market definition and the behaviour which could be seen to be an abuse of market power.

3.2.2 As noted earlier, we do not believe we have this clarity currently as the process appears to have skipped an important step; that of clarification and quantification of the problem that is sought to be addressed.

3.3. Do you agree that the new preamble [clause 1] is effective in conveying succinctly the intended framework and purpose of the 'rule' [clause 2]?

3.3.1 We prefer the revised drafting (new preamble) to the previous purpose clause.

3.3.2 This is because we thought there was a high risk that the references to costs in the previous purpose clause could result in an application of the clause by the Rulings Panel and/or High Court in a manner similar to the cost-based regulation of monopolies.

3.3.3 This is inappropriate where the other benefits of monopoly regulation, such as financial capital maintenance, do not apply.

3.3.4 We still have concerns that the new test could lead to a proliferation of complaints until interpretations were settled.

3.4. Do you agree with clause 3(a), which states when market power becomes significant?

3.4.1 We are not sure if clause 3 (a) answers the primary question for us which is, "How much and for how long", and in which market?

3.4.2 The preamble may be read as meaning that a single trading period in a single location is a separate market. If so, there will be formidable compliance costs associated with this change.

3.4.3 Is it the MDAG's intent to rule out all forms of price discovery? Or is it comfortable with market participants testing out perceptions of value through the offer process?

3.4.4 This needs to be explored before the Authority can be comfortable that this change is in the long-term interests of consumers.

3.5. Overall, do you support the revised proposed code change in preference to the existing HSOTC provisions?

- 3.5.1 We support the new provisions over the MDAG's previous version however Trustpower, as an organisation, is not yet clear about the harm that is being addressed given the paucity of cases to date.
- 3.5.2 We note that there are other changes underway, including the Authority's investigation into transfer prices and profitability of the retailer activities, which will also provide constraints on the activities of market participants.

For any questions relating to the material in this submission, please contact me directly via email:
peter.calderwood@trustpower.co.nz

Regards,

A handwritten signature in blue ink, appearing to read "Peter Calderwood".

PETER CALDERWOOD
GENERAL MANAGER, STRATEGY & GROWTH