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Submission to the MDAG, Price discovery in a renewables-based electricity system, Options Paper

Electra Limited (Electra) owns and operates the electricity lines and assets in the Kapiti and Horowhenua districts. We welcome the opportunity to submit to the Market Development Advisory Group (MDAG) *Price discovery in a renewables-based electricity system Options Paper* (the MDAG Options Paper). Nothing in this submission is confidential.

The focus of this submission is on our support for MDAG's proposed measures to strengthen competition. A summary of MDAG's proposed measures is in Table 1.

Table 1: MDAG's Proposed measures to strengthen competition¹

	Option Name	Rationale
D1	Develop dashboard of competition indicators for flexibility segment of wholesale market	Better assess how competition for flexibility products is changing
D2	Greater transparency of hedge info (esp. non-base load) covering offers, bids + agreed prices	Make it easier for participants to compare prices, especially for non-baseload contracts. Also get better info for regulator
D3	Develop flexibility access code (non-price elements)	Promotes reasonable access to 'flexibility contracts'
D4	Extend trading conduct rules to hedge market	Deters participants from exercise of significant market power
D5	Market-making for shaped contract products	Creates better forward price discovery and market liquidity for a shaped contract
D6	Physical disaggregation of flexible generation base	Risk of river chain coordination inefficiencies and hard to physically reallocate storage
D7	Virtual disaggregation of flexible generation base	Addresses market power at source via structural change
D8	Price caps applied in the electricity spot market	Significant risk of chilling investment

¹ The MDAG Options Paper, Table 4 on page 26.

Conduct measures are a worthy first step to strengthening competition

MDAG's proposed measures to strengthen competition present pragmatic solutions that have the potential to address the concerns outlined in our submission to the Electricity Authority's *Promoting competition in the wholesale electricity market in the transition towards 100% renewable electricity*, Issues Paper, 12 October 2022 (the Authority's Issues Paper).

'Four New Zealand wholesale electricity market generators also operate as energy retailers (Contact, genesis, Meridian, and Mercury), commonly referred to as 'gentailers'. Gentailers supply over 80% of the generation into the wholesale electricity market. The problem with this concentrated structure is that a small number of market participants have disproportionate market power. Meaning there is an oligopoly present in the New Zealand wholesale electricity market.

The problem with allowing an oligopoly to exist in a competitive market is that they dominate and can maximise their profits while minimising competition via non-price competition and product differentiation. Profit maximising behaviour by the oligopoly makes it difficult for other market participants to make a market offering in direct competition with the oligopoly. A situation comparable to monopolies, only gentailers are not regulated under Part 4 of the Commerce Act 1986.'²

MDAG considers that its range of options to strengthen competition for the provision of flexibility services falls into two broad categories—

- (a) Conduct measures — deter or mitigate the exercise of market power; and
- (b) Structural measures — address undue market power at its source.³

Structural measures represent the best enabler for flexibility services to enter and operate in the New Zealand electricity market. Of MDAG's proposed measures, D6—physical disaggregation of flexible generation base would have the greatest impact in addressing the disproportionate power of the oligopolies over the long term. However, we accept MDAG's finding that structural measures—

'...are generally more costly and difficult to implement, have greater risk of unintended consequences and can create significant disruption at a time when the sector is needing stability to support investment decisions in long life assets.'⁴

MDAG's preference is to focus on conduct-based measures in the first instance⁵ and has stated its preference for Options D1 to D4. These measures represent a mix of options:

- (i) measure competition and increase contract transparency (options D1 and D2)
- (ii) constrain anti-competitive conduct (options D3 and D4).⁶

Given that vertical separation of the gentailers is not within the Authority's powers and would require a legislative change to the Electricity Industry Act 2011, we are of the view that implementing these four preferred options first—along with Option D5, introducing market-making for a shaped product, such as a cap—and then assessing whether the desired impact has been realised is a workable and sensible approach to take. This 'first

² Electra, Submission to the Wholesale Market Competition Review, 14 December 2022

³ The MDAG Options Paper, paragraph 10.17.

⁴ The MDAG Options Paper, paragraph 10.17(b).

⁵ The MDAG Options Paper, paragraph 10.18.

⁶ Supra n5.

step' could be premised on its overall effectiveness over time. We agree with MDAG's statement that—

'It is possible that conduct-based measures may prove insufficient from a competition perspective. In that event, structural measures would be required.'⁷

If conduct-based measures prove ineffective, then structural measures should be taken. And as stated by MDAG, 'put in with the least possible delay'⁸.

Closing comments

The wholesale market is an important part of the electricity supply chain, and decarbonisation will disrupt it as New Zealand embarks on its Carbon Zero journey. The solutions in the MDAG Options Paper have been developed by industry representatives, each an expert in their field. No one part of the supply chain has been over or underrepresented. The result is a considered Options Paper with pragmatic solutions that the Authority must have regard to.

Yours sincerely



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⁷ The MDAG Options Paper, paragraph 10.20.

⁸ The MDAG Options Paper, paragraph 10.25.