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Submissions
Electricity Authority
Wellington

By e-mail: appropriations@ea.govt.nz

2024/25 levy-funded appropriations consultation – priority should be given to promotion of stronger, thriving competition

2degrees, Electric Kiwi, Flick Electric and Pulse Energy (the independent retailers) would like to see a scaling up of the Authority’s policy ambition with a willingness to go further and faster in reforming the electricity market. We want to help the Authority succeed in its strategic ambitions. If the Authority successfully promotes thriving competition, and enhances protections for consumers, independent retailers are more likely to be successful.

We welcome the Authority’s “acknowledge[ment] that we have more work to do to give confidence in the market and the level of competition.”¹ This will require a substantial levelling of the playing field between independent and incumbent suppliers, and a much more strongly competitive electricity market.

The Authority’s wholesale market review provided clear and robust evidence of substantive competition problems and sustained excessive pricing – despite the Authority shying away from reaching firm conclusions in its decision paper – and the MDAG renewables project highlighted how competition issues could get worse as reliance on renewables increases. We highlight evidence of the problems in the wholesale and retail markets in our submission which the Authority could draw on to support budget uplift and work prioritisation.

The independent retailers support additional funding (and/or re-prioritisation within the Authority’s fiscal envelope) for projects which have a clear and direct focus on addressing competition problems in the wholesale and retail markets. We also support additional funding (and/or re-prioritisation of existing funding) for the Authority’s monitoring and compliance function.

A thriving and highly competitive market should be at the heart of the Authority’s “vision and intended outcomes” [Q.5]

We agree with MDAG “Retail market competition must be effective to ensure end-use consumers fully benefit from the opportunities available in the future electricity system.”²

The independent retailers similarly welcome the Authority’s commentary that “Market competition is a key enabler to deliver a better energy future”³ and even “a small improvement in retail

¹ Electricity Authority, Annual Report 2022/23.

² MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023.

³ https://www.ea.govt.nz/documents/3053/Summary_of_Submissions_202324.pdf

competition ... is likely to have material benefits to consumers.”⁴ We support the Authority’s desire for “reduced barriers to competition”.⁵

We don’t get a sense of focus or urgency on electricity retail and wholesale competition issues from the appropriations paper or the Authority’s “vision and outcomes”, and other related documents including the October 2023 Business Case for additional funding. While the consultation paper has a heavy focus on the energy transition, from our perspective ‘all roads lead to Rome’. The MDAG and Energy Hardship Expert Panel work highlight that resolving competition issues is a key element for ensuring a smooth and successful energy transition while ensuring electricity is affordable, including for domestic and small consumers.

In our view, the “vision and outcomes” the Authority is seeking should include thriving competition in which: (i) barriers to competition (both entry and growth) are removed or substantially reduced; (ii) “no party has the means and incentive to exercise significant market power”;⁶ and (iii) all consumers benefit from competition, including vulnerable consumers and consumers in hardship. Significant or substantial market power should not be accepted as an enduring feature of the market.

The importance of prioritising and addressing competition issues is emphasised by the Commerce Commission’s decision not to open a section 36 investigation, “at this time”, “in light of the availability of alternative regulatory pathways to examine and, where appropriate, take action in relation to the issues raised in the complaints”.⁷

The Commission’s position, following conversations with the Authority, was that the Authority has “regulatory responsibilities” and “the expertise to explore and understand the issues in and underlying the complaints, and have powers to design and implement measures to address issues affecting the functioning of the relevant markets.”⁸ The Commission position pragmatically recognises it can be better to prevent abuse of market power through policy reform rather than relying on lengthy and uncertain ex post litigation.

Wholesale competition problems will continue to put upward pressure on retail tariffs and energy affordability

The competition problems in the wholesale market have unsurprisingly spilled over into an increasingly fragile electricity retail market. Based on reasonable and objective metrics, the strength of competition in the electricity retail market has gone backwards; particularly over the last couple of years.⁹

For example, independent retailer market growth has essentially stalled.

⁴ Electricity Authority, Improving retail market monitoring: clause 2.16 information notice, Consultation paper, 5 December 2023.

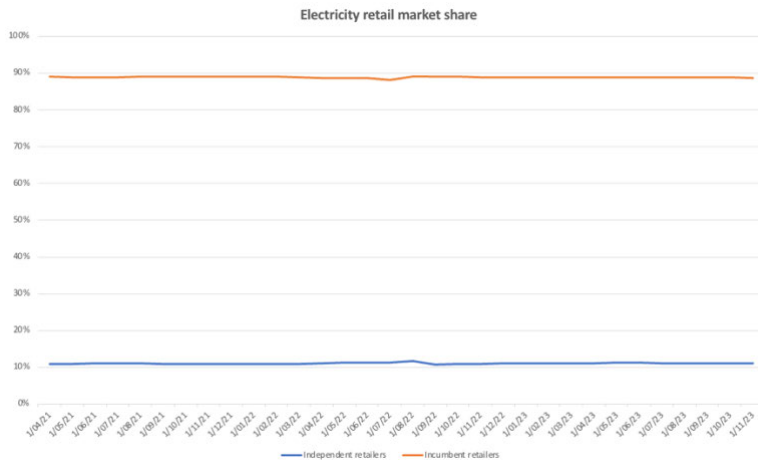
⁵ Electricity Authority, Statement of Intent 1 July 2021 – 30 June 2025, various versions.

⁶ MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023.

⁷ Commerce Commission, Commerce Act 1986 complaint re electricity gentailers – no further action, 19 December 2023.

⁸ Commerce Commission, Commerce Act 1986 complaint re electricity gentailers – no further action, 19 December 2023.

⁹ We have detailed these concerns extensively in submissions to the Authority and, most recently, provided updated evidence of the problems in submission to MBIE in response to the Energy Transition omnibus. We have provided the Authority with a copy of our MBIE Energy Transition submission: “Stronger competition is key to affordable electricity and a successful energy transition”, 3 November 2023.



While there has been some easing of wholesale pricing pressures they remain at historically high levels and will continue to put upward pressure on retail tariffs for Kiwi households and businesses. High wholesale market prices can take time to manifest through to end-consumer power bills, particularly as the incumbent gentailers are, and have been, willing and able to trade-off retail profitability for record wholesale profits.

We welcome the Energy Hardship Expert Panel’s recognition incumbent gentailers’ dominance is helping consign 300,000 people to energy hardship. The Panel’s observations highlight that promoting stronger competition is important for both the long-term benefit of consumers and consumer protection limbs of the Authority’s statutory objective.

We agree with the Energy Hardship Expert Panel that “The Electricity Authority, Commerce Commission and MBIE should focus on affordability outcomes by continuing work to improve competition and remove barriers to entry and operation for independent and social retailers.” We also agree with the Energy Hardship Panel that “affordability should become of much greater focus for the EA”, and that:¹⁰

A competitive and healthy electricity market that consumers trust is going to become even more important as we transition to a higher proportion of renewable energy. A well-functioning market is fundamental to ensuring electricity prices are as low as possible, not just for alleviating energy hardship, but to ensure people will be able to switch away from carbon-intensive energy sources, for heating, eating, and driving and other activities.

The Authority’s market participant survey results highlight major competition problems

The Authority’s observations about the results from its market participant surveys illustrate the growing competition problems in the electricity market: “only 24% of participants surveyed agreed that new entrant retailers and generators can compete on a level playing field with established retailers or generators. Survey respondents expressed concerns around the vertical integration of gentailers and their internal transfer prices, which they felt disadvantaged retailers who didn’t have a generation limb.”^{11,12}

There are very few competition-related survey questions where market participants – other than the incumbent gentailers – consider competition is working as well as it should:

¹⁰ Energy Hardship Expert Panel Report to the Minister, Energy Hardship: The challenges and a way forward, July 2023.

¹¹ Electricity Authority, Annual Report 2022/23.

¹² Our joint submission to MBIE in response to the Energy Transition omnibus provides extensive evidence of competition problems in the electricity market and that they are getting worse: 2degrees, Electric Kiwi, Flick Electric, and Pulse Energy, Stronger competition is key to affordable electricity and a successful energy transition, 2 November 2023.

Market survey competition measures	Gentailer net agreement ¹³	All other participants' net agreement
New entrant retailers can operate on a level playing field with established retailers	38%	-48%
New entrant generators can operate on a level playing field with established generators	38%	-16%
Competition between electricity generators ensures wholesale market prices are set at an efficient level	48%	-10%
Competition between electricity generators ensures they build the most efficient power stations	52%	-4%
Competition between retailers ensures consumer prices only rise in line with costs to the electricity companies	52%	-33%
Prices in the retail market reflect workably competitive outcomes	57%	-14%
Prices in the spot market reflect workably competitive outcomes	43%	0%
Prices in the hedge market reflect workably competitive outcomes	14%	-14%
Prices in the ancillary services markets reflect workably competitive outcomes	38%	6%
Competition between electricity retailers promotes efficiency	76%	-14%
Competition adjacent measures		
The current market settings encourage innovation in generation	19%	-25%
The electricity market ensures electricity is generated efficiently	57%	18%
The wholesale market efficiently coordinates electricity production and consumption	48%	30%
The hedge market efficiently coordinates electricity production and consumption.	33%	-21%
The wholesale market efficiently facilitates timely investment in the electricity system	38%	-32%
The hedge market efficiently facilitates timely investment in the electricity system	38%	-20%

¹³ Net agreement = Strong agreement + agreement – strong disagreement – disagreement.

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Summary of the independent retailers' views

- Our views are largely unchanged from last year.¹⁴
- We appreciated the additional information the Authority provided on the breakdown of its proposed expenditure increase, in response to our requests, though the late timing of the provision of the October 2023 Business Case (released 19 January) limited the extent to which we have been able to usefully review the content.

“Q.1 Do you support the Authority’s proposal for a permanent baseline increase ...?”

- **The independent retailers support additional funding to address competition problems/barriers to competition in the wholesale and downstream retail markets.** We would support additional funding to enable the Authority to progress these matters faster.
- **We would also specifically support extra funding for the Authority:**
 - **to ensure Powerswitch is fully levy-funded (see our submission on the last appropriations consultation);¹⁵ and**

We support ConsumerNZ’s view that the funding model should “reflect the recommendations made by the Electricity Price Review, namely; to fully fund Powerswitch operations and remove the need to rely on switching fees...”¹⁶

- **as part of the upgrade of the Authority’s monitoring and compliance enforcement.**

We support the MDAG recommendation “Monitoring and enforcement of Code (Recommendation 21) – Authority to increase resourcing for its monitoring activity, as well as making its monitoring function more independent from its rule-making function by establishing a monitoring and enforcement ‘unit’ within the Authority.”¹⁷
- Whatever the fiscal envelope the Authority has to work within, competition issues in the wholesale and retail markets should be prioritised. Resolving problems independent retailers have in accessing hedge products to manage spot price risk should be the Authority’s number one priority for resolution within the 2024 calendar year.

“Q.6 Do you have any comments on the Authority’s indicative work programme for 2024/25?”

- The independent retailers welcome that the Authority has adopted our recommendation to recommence consultation on its annual work programme in conjunction with appropriations.¹⁷

¹⁴ 2degrees, Electric Kiwi, Flick Electric, OurPower and Pulse, 2022/23 and 2023/24 levy-funded appropriations, Funding proposals should have a clear focus on “consumer centricity” and “thriving competition”, 1 November 2022.

¹⁵ 2degrees, Electric Kiwi, Flick Electric, OurPower and Pulse, 2022/23 and 2023/24 levy-funded appropriations, Funding proposals should have a clear focus on “consumer centricity” and “thriving competition”, 1 November 2022.

We are disappointed this issue wasn’t raised in the consultation. Last year the Authority acknowledged the feedback it received on the Powerswitch funding model and stated “The views will help inform the Authority’s future decisions on the funding it provides for the switching model”: https://www.ea.govt.nz/documents/3053/Summary_of_Submissions_202324.pdf#page13.

¹⁶ <https://www.ea.govt.nz/documents/3054/Consumer-NZ-202324-Levy-funded-appropriation.pdf>

¹⁷ It is not clear why the planned projects from 1 July includes projects that are already underway and should reasonably be expected to be completed by 30 June e.g. hedge disclosure obligations.

- We would like to see the Authority provide more information than simply listing the projects it intends to undertake: “We would like increased visibility of the Authority’s work programme, including project milestones/deliverables and consultation dates over the entire life of each project. We understand the Authority has this information for its own internal purposes and we would like it to be shared with stakeholders.”¹⁸
- We would also like to see the Authority engage proactively and collaboratively with stakeholders on what its ‘strategic road map’ should look like and how its work-plan should evolve and develop. This view is reinforced by the commentary in the Sapere reports. If the Authority has to make “difficult trade-offs about where to focus its efforts” it should be explicit about what these are and have conversations with stakeholders about how to best manage them.
- **We welcome and support the Authority’s announcement it is commencing a review of risk management options available to electricity retailers.** This should be the Authority’s single biggest priority for resolution this calendar year.

Problems in the hedge/contract market have held competition back for far too long and need to be resolved.

It will be important, if the review is to be successful, that the Authority is able to reach a clear problem definition, rather than that the problems are “uncertain”, matched with tangible market reforms. The Authority can limit the extent to which it ‘reinvents the wheel’ by drawing on work of other regulators including the ACCC.¹⁹

- In the context of the MDAG final report, **market-making for flexibility products (including shape and cap products) (Recommendation 24) should be treated as the Authority’s single most important priority for implementation as part of Recommendation 8 in 2024** (not a tranche 2 action, “contingent on assessing whether previous measures are sufficiently effective”).²⁰ Reliance on voluntary arrangements has been an abject failure.

Our position on fast-tracking extension of mandatory market-making is supported by the risks the Authority has raised in terms of ensuring the electricity system is able to meet peak electricity/winter demand and avoid 9 August 2021 type outages. The Authority has recognised the importance of flexibility products for allowing flexible supply and demand “to participants in the forward price discovery process and obtain more certain revenues while supporting the management of peak demand.”²¹

- **We would like to acknowledge the important contribution MDAG has made by laying out problems and issues for the Authority to address** in its work-plan.²² We are largely supportive of the Authority progressing the MDAG recommendations in its work-programme, subject to the comments above about bringing forward Recommendation 8 in 2024, and also that the

¹⁸ <https://www.ea.govt.nz/documents/1936/independent-retailers-submission-202122-Levy-funded-appropriation.pdf>

¹⁹ ACCC, Inquiry into the National Electricity Market, November 2022, available at: <https://www.accc.gov.au/system/files/Inquiry%20into%20the%20National%20Electricity%20Market%20-%20November%202022%20report.pdf>.

²⁰ MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023.

²¹ Electricity Authority, Potential solutions for peak electricity capacity issues, 12 January 2024.

²² This does not mean that all of MDAG’s recommendations should be adopted. As discussed above, we consider the MDAG proposal to narrow the scope of the UTS provisions to be unsound (recommendation 26), and there are other recommendations we consider should be given higher priority (particularly recommendation 24 and also recommendation 29).

Authority should remove the regulated price floor preventing negative spot prices (recommendation 29) sooner than MDAG envisage.^{23,24}

- **The main blind-spot in the otherwise good work MDAG has done is its proposal to narrow the scope of the UTS provisions (recommendation 26). We consider recommendation 26 and the associated reasoning to be unsound** and poorly thought through. The best thing would be for the Authority to confirm at the earliest stage practicable it will not be pursuing this recommendation.²⁵
- **Internal transfer payment and segmented profitability reporting should be enhanced:** The Authority should fully implement the Electricity Price Review retail-wholesale financial separation recommendation. The incumbent gentailer financial statements provide prima facie evidence they are using sustained high wholesale prices and their electricity wholesale businesses to cross-subsidise their electricity retail businesses but there are no incumbent gentailer financial separation/disclosure requirements to provide more definitive information on the extent of this.

More importantly, the Authority should require gentailers to disclose the ITPs they use for retail price setting purposes, and not just the ITPs they use for accounting purposes.

- **The Authority should reinstate its planned review of the interpretation of its statutory objective.** A pure focus on efficiency will not deliver long-term benefits for consumers. The interpretation is now particularly out-of-date given the addition of a consumer protection objective. As far as we are aware, the Authority never announced or explained why this work was put on hold.

Advisory and working groups can be useful if well run with good governance

- While the Authority has not announced what will happen with MDAG beyond the 100RE project, we would like to see MDAG and the MDAG Chair continue to assist with substantive electricity industry policy matters,²⁶ potentially including some of the work that will come out of its recommendations paper.
- There is potential for the use of working groups, particularly on technical matters, to support aspects of the Authority's work-programme. Whether they will be successful depends on how they are set up. The Authority can't just take a laissez-faire approach.

We agree with MDAG that "Success in the TCF multilateral process relied (among other things) on wide participation of market participants, a rigorous analytical framework, and a shared commitment to a disciplined process in which all participants understood that a co-designed common-good solution would better than the regulated alternative."

²³ We are fully supportive of the propositions MDAG has made about the wholesale market design (including, for example, that the "Contract market must provide clearer and more timely signals about investment needs", "Participants need better tools to manage risks associated with increased spot price volatility" and "Proactive measures [are] needed to safeguard competition – especially for flexible supply".

MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023, see 5 "Implications for wholesale market design".

²⁴ We agree with MDAG that "Artificially suppressing or elevating spot prices would mean suppliers and consumers do not face accurate signals about the true value of energy." [emphasis added] We also welcome Transpower's comments that this option should be further investigated.

²⁵ We comprehensively detailed the problems with MDAG's justification for the recommendation in our submissions to MDAG.

²⁶ As the Authority is aware, we have substantial reservations about the EAAG or using the EAAG in place of MDAG.

Broad industry representation is critical. The “sector forum” the Authority established to develop alternative, voluntary, hedge market arrangements was made up entirely of vertically-integrated suppliers and its recommendations reflected the dominant incumbent gentailer self-interest on the matter.²⁷

MDAG also allude to the discipline of a “regulated alternative”. The initial experience with the TCF is informative. In its early days, the TCF set up a working group to develop a Co-location Code for cellular sites. This was the first Code the TCF submitted to the Commerce Commission for approval. The Code the TCF proposed reflected incumbent mobile operators’ domination of the working group and was consequently rejected by the Commission. This was an important learning for the TCF and its members. The Commerce Commission decision highlighted that the TCF and its members could not simply propose Codes serving their own commercial interests and needed to ensure they were to the long-term benefit of end-users. The Commerce Commission was subsequently able to approve a substantially improved proposed Code.²⁸

²⁷ The sector forum prepared and presented a voluntary incentive-based proposal to the Electricity Authority's Board: <https://www.ea.govt.nz/projects/all/cmm/>.

²⁸ <https://comcom.govt.nz/news-and-media/media-releases/archive/commission-approves-industry-co-location-code>

It could be helpful to clarify the Authority’s strategic direction [Q.5]

The Authority has variously acknowledged “The benefits of clean and less expensive electricity can only be realised with the enabler of regulatory change”, “transformational changes [are] needed to support particularly the transition to a net zero emissions economy by 2050”²⁹ and “Existing regulation needs to keep up with a system that is fundamentally changing” [emphasis added].³⁰

The Authority also considers it “has historically been resourced for incremental change as opposed to the structural changes and major regulatory reform that are needed now, and in the future” [emphasis added],³¹ and “Acting now is a priority, as the transition is here.”³² In the most recent Annual Report, the Authority similarly commented “We recognise that existing regulation needs to keep up with a system that is fundamentally changing and we no longer have the benefit of time or a steady environment in which to develop and implement incremental reform.”³³

We welcome this commentary. One of the Authority’s guiding principles should be that regulatory change needs to be proportionate to the problems and challenges the Authority is dealing with, including in relation to the energy transition.³⁴

A difficulty we have is marrying the Authority’s acknowledgement of the need for transformational and structural changes with its underlying strategic philosophy that regulatory stability and incrementalism are prerequisites for providing certainty for investors.

The Authority has stated it considers “markets require regulatory certainty” and “Incremental and consistent regulatory change will support reliable and affordable electricity over the long term.”³⁵ The Authority describes “intervention” as a “risk” rather than an opportunity to deliver better consumer outcomes.³⁶

The Authority needs to be clear whether it believes they “no longer have the benefit of time or a steady environment in which to develop and implement incremental reform”³⁷ or “Incremental and consistent regulatory change will support reliable and affordable electricity over the long term”.³⁸ Both statements cannot be correct.

Regulatory reform needs to be proportionate to the problems the Authority is addressing

We reiterate from our last appropriations submission care is needed to ensure stability doesn’t mean a status quo bias and is not a roadblock against needed regulatory reforms or the promotion of competition (including “thriving competition”) for the long-term benefit of consumers.³⁹

Inaction doesn’t provide regulatory stability in the long-term.

²⁹ Electricity Authority, consultation paper, 2022/23 and 2023/24 Levy-funded Appropriations, 4 October 2022.

³⁰ <https://www.ea.govt.nz/news/general-news/message-from-our-chair-anna-kominik/>

³¹ Electricity Authority, consultation paper, 2022/23 and 2023/24 Levy-funded Appropriations, 4 October 2022.

³² <https://www.ea.govt.nz/news/general-news/message-from-our-chair-anna-kominik/>

³³ Electricity Authority, Annual Report, 2022/23.

³⁴ Including for the Code Amendment Principles.

³⁵ Electricity Authority, Statement of Intent 1 July 2021 – 30 June 2025, various versions.

³⁶ Electricity Authority, Statement of Intent 1 July 2021 – 30 June 2025, various versions.

³⁷ Electricity Authority, Annual Report, 2022/23.

³⁸ Electricity Authority, consultation paper, 2022/23 and 2023/24 Levy-funded Appropriations, 4 October 2022/Electricity Authority, Statement of Intent 1 July 2021 – 30 June 2025, various versions.

³⁹ https://www.ea.govt.nz/documents/3057/independent_retailers-202324-Levy-funded-appropriation.pdf

Regulatory stability does not, for example, provide a “steady environment for investment” if underlying market failures are not addressed and/or the regulatory environment favours or entrenches incumbent operators at the expense of investment by new entrant or independent operators.^{40,41}

In our submission to MBIE in response to the Energy Transition omnibus we noted the emphasis on the “risk of unintended consequences” trope by incumbent vested interests to argue against major or transformative reforms. This thinking needs to be turned on its head. There is substantial risk of unintended consequences from regulatory inertia and incrementalism if issues that could jeopardise a successful energy transition, competition and affordable electricity are not adequately addressed.

We agree with MBIE “... the electricity sector in New Zealand will need to adapt rapidly if it is going to maintain its social license to operate. If people lose trust in the market and market participants ... then the political process may explore alternatives to the current market. Such alternatives exist and are being used in other jurisdictions.”⁴² If underlying problems are not addressed, it could result in the need for more substantial regulation further down the line.

There are plenty of examples of ‘stable’ regulatory regimes which have been subsequently displaced because they did not deliver the outcomes they should. The conservative and incrementalist approach the Authority has generally adhered to⁴³ mirrors the approach the initial Telecommunications Commissioner adopted before the Government stepped in and radically overhauled the Telecommunications Act, introducing substantially more heavy-handed (but robust) legislation which over-rode earlier Commerce Commission decisions e.g. recommending against regulation of Local Loop Unbundling access.⁴⁴

The grocery sector review also provides a salient example.

The Commerce Commission was subject to criticism its recommended grocery reforms were inadequate for addressing the problems it had identified. The result was the Government had to step in and develop reforms beyond the Commerce Commission recommendations. Further regulatory changes are likely in light of the National-NZ First coalition agreement.

⁴⁰ https://www.ea.govt.nz/documents/3057/independent_retailers-202324-Levy-funded-appropriation.pdf

⁴¹ Refer, for example, to: Electric Kiwi, Flick Electric, Pulse and Vocus, The Authority has provided robust evidence of fundamental, structural problems in the wholesale market, 17 December 2021, “Regulatory incrementalism won’t resolve fundamental structural problems or deliver a high performing market” at: https://www.ea.govt.nz/documents/2178/independent-retailers-submission_6WBeKy6.pdf.

⁴² MBIE, Investigation into electricity supply interruptions of 9 August 2021, 2021: <https://www.mbie.govt.nz/dmsdocument/17988investigation-into-electricity-supply-interruptions-of-9-august-2021>

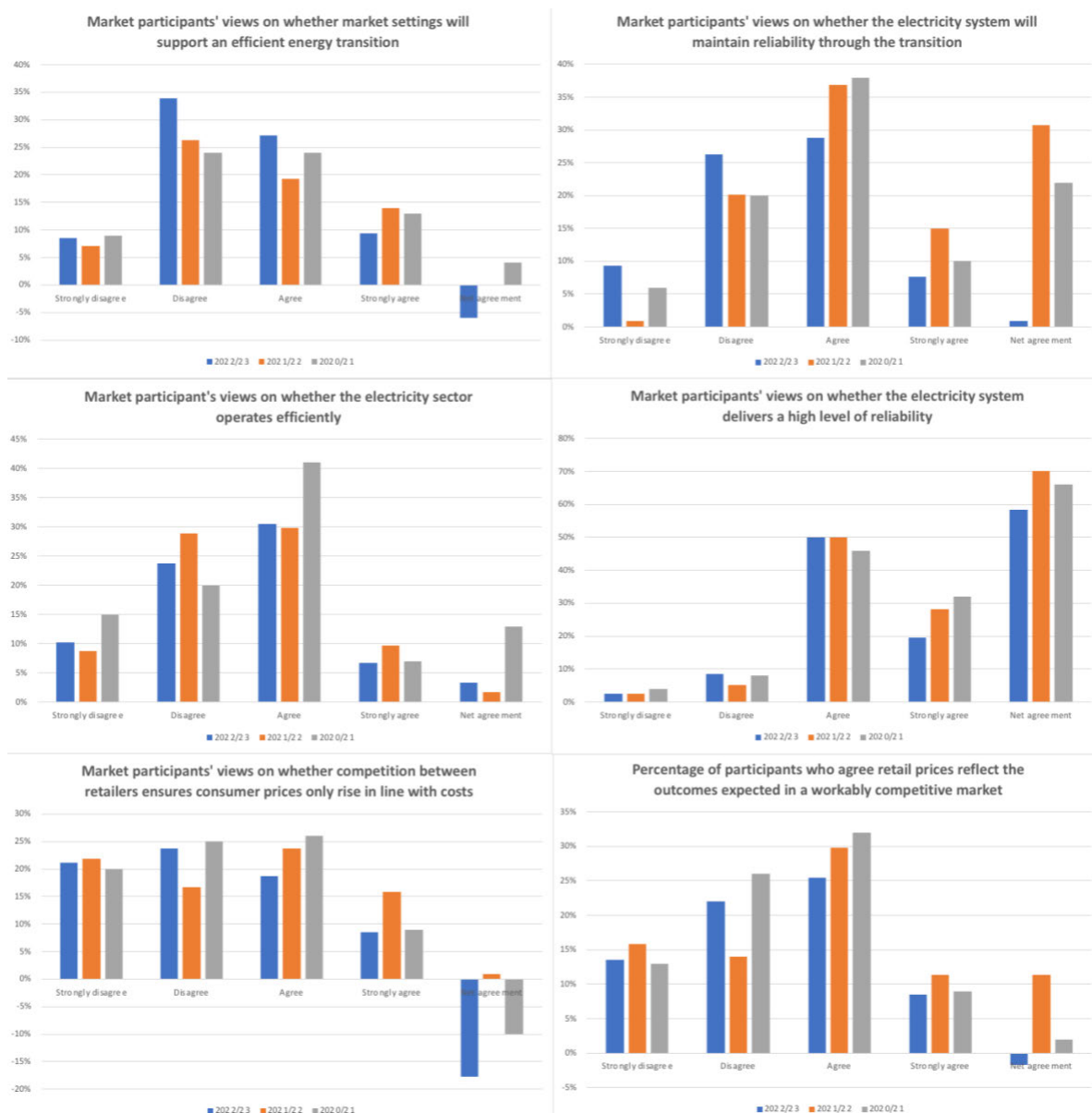
⁴³ Transmission pricing being a notable outlier.

⁴⁴ https://www.ea.govt.nz/documents/3057/independent_retailers-202324-Levy-funded-appropriation.pdf

Market participants are becoming increasingly concerned about the the electricity market

The Electricity Authority’s market participant surveys are useful for highlighting where the Authority and the industry is doing well, and areas that warrant focus and priority in the work programme.

It is clear that over the first three surveys market participants’ confidence has gone backwards in relation to whether market settings will support an efficient energy transition, the electricity sector operates efficiently and provides reliable electricity supply, and how well retail competition is working. While market participant views on how well the electricity system delivers reliability remains high (albeit lower than 2 years ago), the views about how well the the system will maintain reliability during the transition has plummeted dramatically.

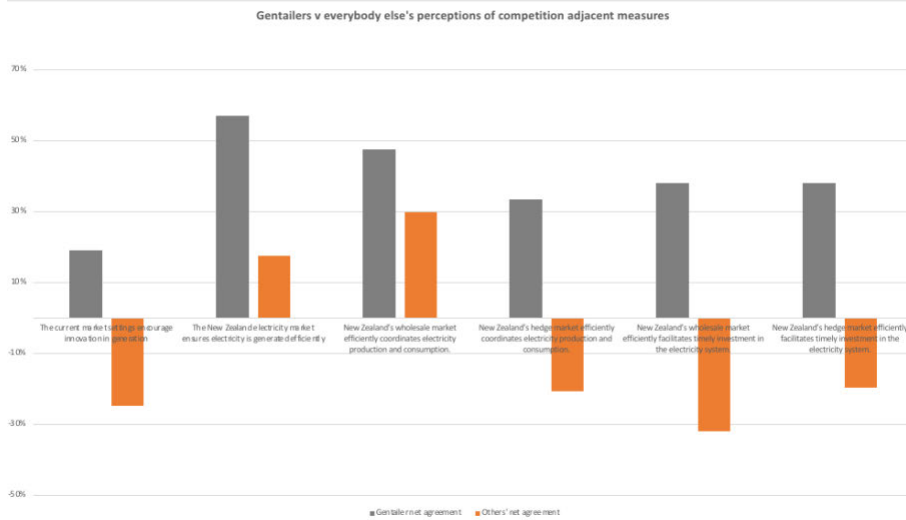


There is a clear message that market participants are becoming increasingly concerned about competition, reliability of electricity supply, the efficient operation of the electricity market and consumer outcomes, and these outcomes could get worse during the transition. These adverse survey results all go directly to the Authority’s statutory objective.

Market participants lack confidence in electricity market competition

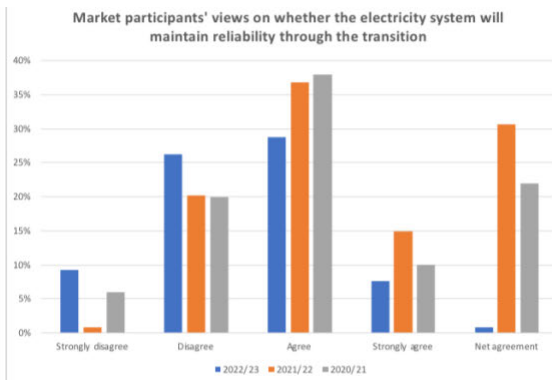
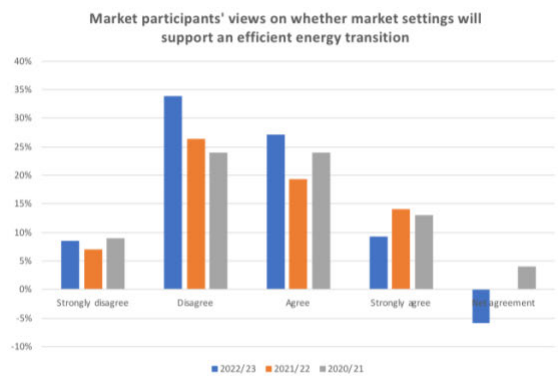
A clear and unambiguous message from the Electricity Authority's surveys is that all market participants, except gentailers, consider that competition isn't working well, and we are not seeing workably competitive market outcomes in the hedge, wholesale and retail markets.





These results are also clear from market participant views that the hedge market is not delivering efficient outcomes, and the wholesale market doesn't efficiently facilitate timely investment. They may also explain why confidence market settings will support an efficient energy transition, and the electricity system will maintain reliability through the transition has substantially deteriorated over the 3 years the Authority has been conducting the surveys.

The results should be of particular concern in the context of electrification and the energy transition, both of which hinge on substantial increase in investment in renewables.



There is clear evidence of competition problems

The independent retailers consider that the Authority's identification of problems in the wholesale market review was sound – the Authority didn't give itself or its staff the credit they deserved – and provides a good starting point for exploring competition issues. A mistake that was made though was to treat problems in the wholesale market as stand-alone and not to consider how these issues manifest in the downstream retail market. The siloed approach meant the Authority did not consider all the harm caused by problems in the wholesale market.

The competition problems in the wholesale market have spilled over into an increasingly fragile electricity retail market.

There are clear and worrying outcomes which are far removed from outcomes in a workably competitive market, including but not limited to:

- independent retailers deliberately curbing customer growth in the absence of access to adequate hedge cover;
- Electric Kiwi and Flick Electric withdrawing from Powerswitch for periods of time;
- Flick Electric not accepting new customers for a period of time;
- the 'soft-launch' into the electricity market by Octopus Energy despite it being well-resourced and its success in other jurisdictions; and
- 2degrees limiting its new electricity retail customers to customers that aren't already 2degrees customers and that take up bundled electricity plus broadband packages.

In our submission to MBIE on the Energy Transition, we noted that on any reasonable or objective metric, the strength of retail competition has gone backwards; particularly over the last couple of years e.g.:⁴⁵

- Twenty-three electricity retailers have exited the market in the last five or so years.
- Independent retailer market share has stalled around 11% since May 2021.
- HHI for the overall NZ electricity retail market is about the same as it was in December 2019.
- CR1 is about the same as January 2021.
- CR2 is about the same as August 2021.
- CR3 is about the same as October 2018.
- CR4 is about the same as November 2017.

⁴⁵ Our joint submission to MBIE in response to the Energy Transition consultation, "Stronger competition is key to affordable electricity and a successful energy transition", 3 November 2023, goes into more detail about the evidence of competition problems. See the "Appendix: There is clear evidence of competition problems in the electricity retail market", in particular.

- All national market concentration statistics have deteriorated over the last two years e.g. HHI was 2,085 at the end of September 2021 and increased to 2,265 at the end of September 2023.
- Market concentration has also worsened at the regional level. The HHI has increased in 82% (32 out of 39) of the regional electricity markets in the last two years. CR4 (CR3) has increased in 97% (87%) of regional markets.⁴⁶
- Switching rates have been declining since 2018 and are now back at 2000s levels.

While industry regulators shouldn't necessarily be concerned about the plight of individual competitors, the ability to survive or meaningfully grow market share can be symptomatic of wider industry and competition problems. We agree with the ACCC that: "It is expected that businesses will enter and exit well-functioning markets. For example, businesses operating based on higher risk strategies or whose innovations fail will be prone to exiting the market at any time, particularly when disruptions occur. However, large numbers of retailers exiting the market (or becoming inactive) may negatively impact competition." [emphasis added]⁴⁷

⁴⁶ At the residential level, the HHI has increased in 85% (33 out of 39) of the regional electricity markets in the last two years. The CR4 (CR3) has increased in 100% (87%) of the RESIDENTIAL regional electricity markets in the last two years.

⁴⁷ ACCC, Inquiry into the National Electricity Market, November 2022, available at: <https://www.accc.gov.au/system/files/Inquiry%20into%20the%20National%20Electricity%20Market%20-%20November%202022%20report.pdf>.

Hedge market issues should be prioritised [Q.6]

We welcome the Authority has announced a review of risk management options available to electricity retailers. It will be critical to the Authority and the electricity market’s success that tangible reforms come out of this work. This work should be fast-tracked for resolution within the 2024 calendar year. This fast track is analogous – albeit a lot more straight-forward/less demanding on the Authority’s resources – to the Authority requiring Transpower to develop a new TPM and then implement it, within 12 months respectively.

The clear priority for the Authority, if it wants to achieve its strategic ambitions, is to introduce regulation of the hedge market which opens market access. This includes ensuring access to long-term hedging and retail shape products that enable independent retailers to compete against the incumbent gentailers on a more level playing field.

We agree with the advice provided by Ben Hamlin to the Energy Hardship Expert Panel that “One of the barriers to entry into electricity retailing is obtaining electricity on the wholesale market. Independent and social retailers can purchase electricity on the spot market, but they find it difficult to obtain longer term arrangements that protect them from price spikes. Existing large retailers are vertically integrated and do not face this barrier.”⁴⁸

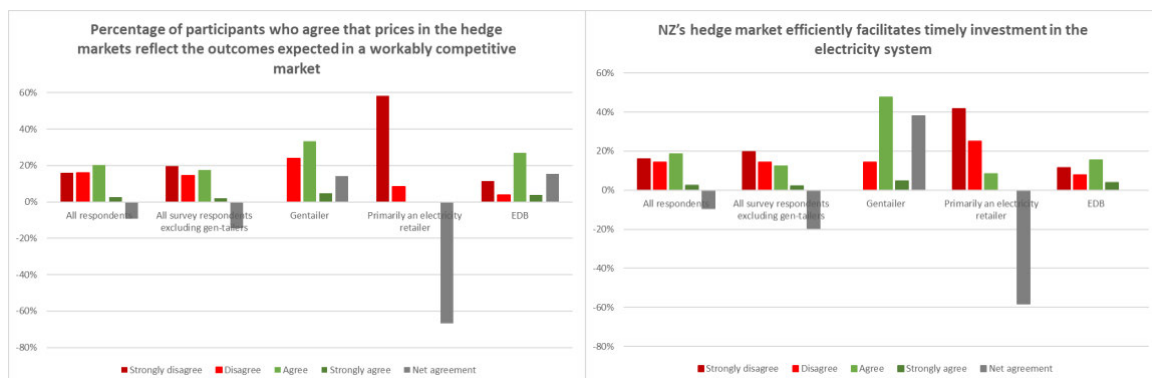
The MDAG final report makes very clear that one of the key pillars, which needs to be “beefed up”, for a well-functioning wholesale market is that “market participants need tools to efficiently manage their risks. These tools can be physical options (e.g. an ability to increase supply or reduce demand) or financial arrangements where parties contract with others who can manage the underlying risk at a lower cost.” MDAG was very clear the issue of access to flexibility products (including shape and cap products) “could tear at the fabric of the broader market” and “undermine competition in the retail and new investment market”.⁴⁹

We agree with MDAG that:

“The importance of flexibility contracts to the electricity system is expected to increase even further in future as the proportion of supply from intermittent sources rises. Indeed, we think flexibility contracts will become the market’s ‘secret sauce’ – enabling a range of wholesale market processes to function effectively.”

“... the contract market must be strengthened so it can do more of the heavy lifting in future. In particular, the market for ‘flexibility contracts’ needs to develop significantly.”

There is very low confidence amongst market participants (other than gentailers) about how well the hedge market is working.

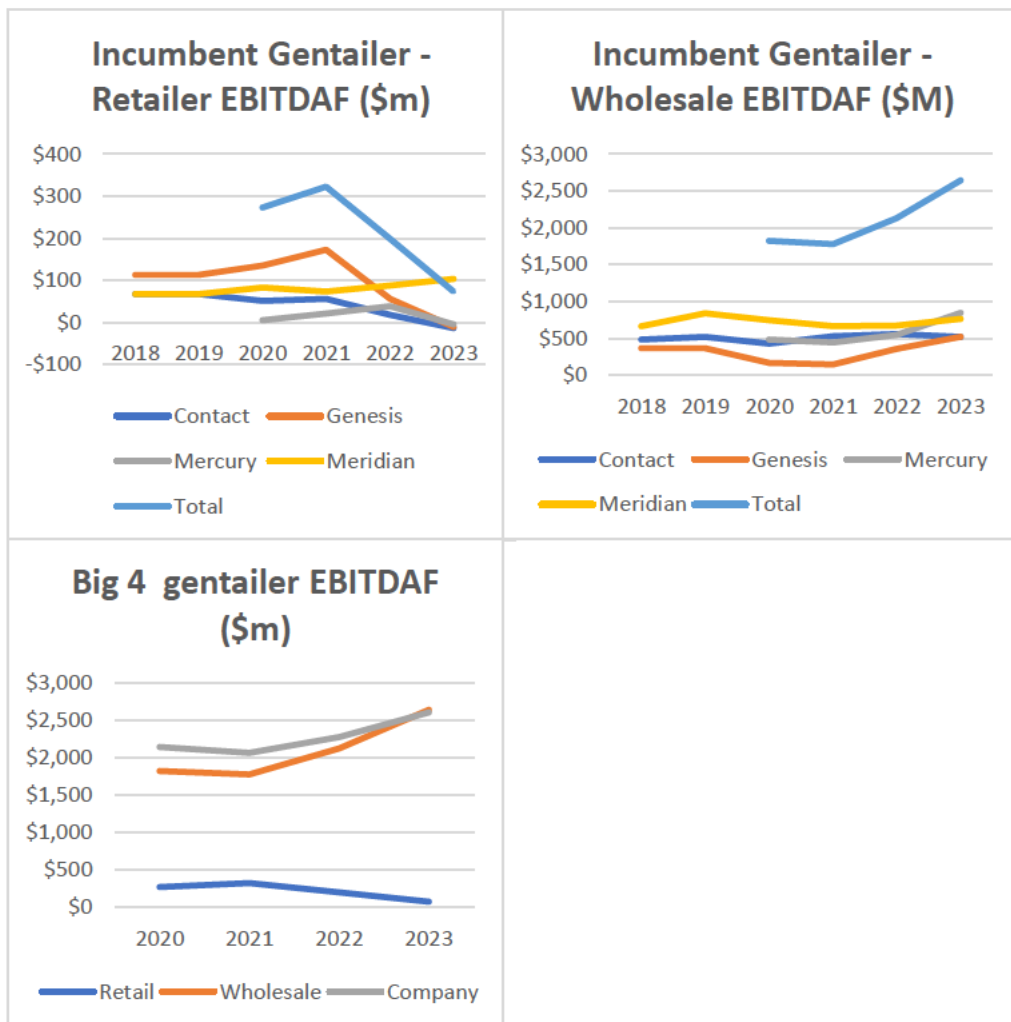


⁴⁸ Ben Hamlin, Barrister, Advise to Energy Hardship Expert Panel, 16 June 2023.

⁴⁹ MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023.

ITP and segmented profitability reporting should be enhanced [Q.6]

The Authority should fully implement the Electricity Price Review retail-wholesale financial separation recommendation. The incumbent gentailer financial statements provide prima facie evidence that their electricity wholesale businesses are cross-subsidising their electricity retail businesses but there is no incumbent gentailer financial separation disclosure requirements to provide more definitive information.



Relatedly, the Authority should reform the gentailer ITP disclosure requirements to include disclosure of the ITPs they use for retail price setting purposes, and not just the ITPs they use for accounting purposes i.e. the cost of purchasing electricity for on-sale at retail prices.

The Authority has correctly explained the disclosure ITPs are “primarily an accounting concept for allocating costs across two business units and has limited application in commercial decision making, such as pricing new business” and “The Authority was advised by generator-retailers that they do not rely heavily on the ITP in a period to price new retail customers. Pricing is more dependent upon the opportunity cost of the electricity at the time a customer is signed up, eg current futures prices for the expected term of the contract, subject to some discretion reflecting perceptions of customer profitability, competitive conditions, and the entity’s business strategy.”⁵⁰ This highlights the limits of the current disclosure requirements for determining discriminatory or anti-competitive behaviour.

⁵⁰ Electricity Authority, Internal transfer prices and segmented profitability reporting, Consultation paper, 8 April 2021.

The MDAG final report is a useful input into the Authority’s work programme and priorities

We would like to acknowledge the important contribution MDAG has made by laying out problems and issues for the Authority to address as part of the energy transition/reliance on greater renewable generation.⁵¹

Market-making for flexibility products (including shape and cap products) (Recommendation 24) should be treated as the Authority’s single most important priority for implementation as part of Recommendation 8 in 2024 (not a tranche 2 action, “contingent on assessing whether previous measures are sufficiently effective”).⁵²

We are largely supportive of the Authority progressing the MDAG recommendations in its work-programme, subject to the comments above about bringing forward Recommendation 8 in 2024, and also that the Authority should remove the regulated price floor preventing negative spot prices (recommendation 29) sooner than MDAG envisage.^{53,54}

Our position on fast-tracking extension of mandatory market-making is supported by the risks the Authority has raised in terms of ensuring the electricity system is able to meet peak electricity/winter demand and avoid 9 August 2021 type outages. The Authority has recognised the importance of flexibility products for allowing flexible supply and demand “to participants in the forward price discovery process and obtain more certain revenues while supporting the management of peak demand.”⁵⁵

We note MDAG’s principal objection to vertical-separation of the gentailers’ wholesale and retail businesses is that this does not address gentailer wholesale market power. We accept in principle that it would be preferable to address the underlying wholesale market power – vertical-integration isn’t a problem where suppliers do not have market power. Where the MDAG reasoning falls down is that its recommendations would have limited impact on wholesale market power.

The main blind-spot though in the otherwise good work MDAG has done is its proposal to weaken the UTS provisions (recommendation 26). With respect, we consider recommendation 26 and the associated reasoning to be unsound and poorly thought through. The best thing would be for the Authority to confirm at the earliest stage practicable it will not be pursuing this recommendation.⁵⁶

MDAG’s description of the UTS provisions as “martial law” scores well for hyperbole but is off the mark and wildly inaccurate. The terminology unhelpfully depicts the UTS provisions as a far bigger intervention than it actually is or has been in practice.

⁵¹ This does not mean that all of MDAG’s recommendations should be adopted. As discussed below, we consider the MDAG proposal to narrow the scope of the UTS provisions to be unsound (recommendation 26), and there are other recommendations we consider should be given higher priority (particularly recommendation 24 and also recommendation 29).

⁵² MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023.

⁵³ We are fully supportive of the propositions MDAG has made about the wholesale market design including, for example, that the “Contract market must provide clearer and more timely signals about investment needs”, “Participants need better tools to manage risks associated with increased spot price volatility” and “Proactive measures [are] needed to safeguard competition – especially for flexible supply”.

MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023, see 5 “Implications for wholesale market design”.

⁵⁴ We agree with MDAG that “Artificially suppressing or elevating spot prices would mean suppliers and consumers do not face accurate signals about the true value of energy.” [emphasis added]

⁵⁵ Electricity Authority, Potential solutions for peak electricity capacity issues, 12 January 2024.

⁵⁶ We comprehensively detailed the problems with MDAG’s justification for the recommendation in our submissions to MDAG.

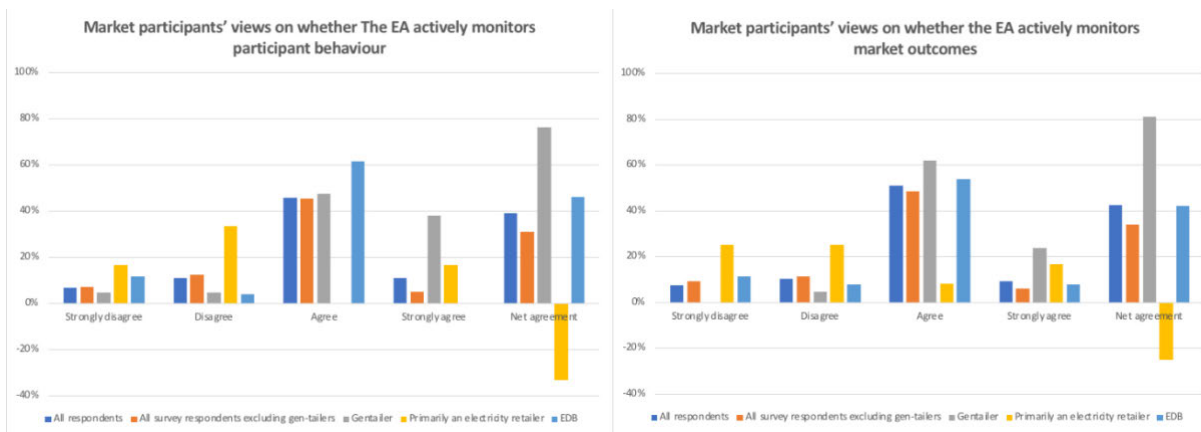
Likewise, it is inaccurate, and misunderstands the relationship between the UTS provisions and trading conduct rules, to depict the UTS provisions as a trading conduct “over-ride” or an “exception for trading conduct rules”.

Our submission to MDAG highlighted that the Authority determines whether an event is a UTS prior to determining it is a trading conduct breach, and the sound reasons for this. The MDAG suggestion “it is logical that the Authority should not be able to invoke UTS powers if an event or situation can be remedied by other Code provisions” does not reflect the practical reality of how the UTS provisions are operated, or the potential need for urgency in a UTS provision, which would be undermined by reversing the process to require determination of whether an event or situation is a trading conduct breach before determining whether it is a UTS. It is logical for the Authority to address a potential UTS and undermining of market confidence at pace and not to be side-tracked by trading conduct considerations before it can remedy the UTS.

We continue to support additional funding for monitoring and compliance enforcement

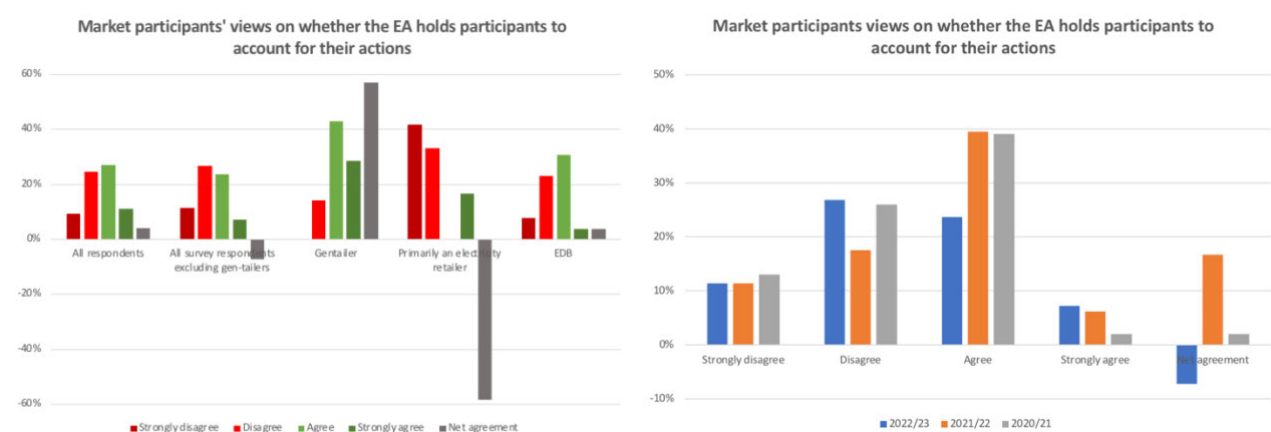
We support the MDAG recommendation “Monitoring and enforcement of Code (Recommendation 21) – Authority to increase resourcing for its monitoring activity, as well as making its monitoring function more independent from its rule-making function by establishing a monitoring and enforcement ‘unit’ within the Authority.”⁵⁷

It is apparent most market participants consider the Authority actively monitors participant behaviour and market outcomes, except for independent retailers most likely because they are the victims (along with consumers) of adverse incumbent behaviour and market outcomes.



It is also apparent market participants – other than incumbent gentailers – consider that the Authority does not hold participants to account for their actions. This highlights the merit of the Authority ramping up its resourcing and market enforcement activity.

Likewise, it is notable market participant perceptions about how well the Authority holds participants to account has dramatically fallen away in the last year.



⁵⁷ MDAG, Price discovery in a renewables-based electricity system FINAL RECOMMENDATIONS PAPER, 11 December 2023.









Concluding remarks

What the Authority sees through the lens of economic efficiency, consumers see in terms of well-being, affordability and ‘dollars in the back-pocket’, and the independent retailers presently see in terms of existential threat. We urge the Authority to prioritise its strategic ambition of “thriving competition” and put this at the centre of its “vision and outcomes” which requires the present barriers to competition and high levels of market concentration in both the wholesale and retail markets are eliminated or reduced.

We support additional funding (and/or re-prioritisation within the Authority’s fiscal envelope) for projects which have a clear and direct focus on addressing competition problems in the wholesale and retail markets. Issues with access to hedging contracts have held back competition and resulted in contraction of retail competition for far too long. The Authority can no longer rely on slow but positive, year-on-year, improvements in retail market concentration statistics. We also support additional funding (and/or re-prioritisation of existing funding) for the Authority’s monitoring and compliance function.

While the Authority has been clear it “is not concerned with the outcomes for individual competitors in the process, except to the extent that it impacts on the long-term benefit of consumers”,⁵⁸ the reality is that if the Authority succeeds in promoting thriving competition it will benefit consumers (which should be the Authority’s principal focus) and new and independent suppliers. In some circumstances, protecting the process of competition can have the effect of protecting a competitor.⁵⁹

Yours sincerely,

<p>Emma-Kate Greer Chief Corporate Affairs Officer</p>  	<p>Luke Blincoe Chief Executive</p>  
<p>Pavan Vyas Chief Executive</p>  	<p>Sharnie Warren Chief Executive</p>  

⁵⁸ Electricity Authority, Re: Flick Electric submission to the Petitions Committee on market pricing and vertical-integration in the electricity market, 27 May 2022. 2Commerce Commission v Fletcher Challenge Ltd [1989].

⁵⁹ NZLR 554 (HC) at 604; and Union Shipping NZ Ltd v Port Nelson Ltd [1990] 2 NZLR 662 at 700.