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Level Playing Field Measures Options Paper

Introduction

Genesis appreciates the opportunity to provide feedback on the Energy Competition Task Force's (**Task Force**) working paper "*Level Playing Field Measures Options Paper*" dated 27 February 2025 (**Options Paper**). As a vertically integrated generator-retailer, we have direct experience of the benefits that this business model brings to New Zealand's electricity system and, ultimately, to consumers.

We disagree with the Task Force's characterisation of competition issues in the New Zealand electricity market and its proposed roadmap of interventions. In our view, the Task Force's proposed measures represent a misdiagnosis of market challenges and would harm competition, investment and, ultimately, consumers.

Our responses to the consultation questions in the Options Paper are set out in the Schedule and the economic analysis of the Task Force's proposed measures by Sapere Research Group (**Sapere Report**).[1] They demonstrate that vertical integration is not the cause of reduced liquidity in hedge markets – rather, fuel and capacity scarcity are the fundamental drivers and the issues requiring attention.

The real problem: Fuel and capacity scarcity, not vertical integration

The Task Force sees current liquidity and pricing concerns in flexibility contracts as giving rise to competition risks and blames vertical integration within the New Zealand electricity market.

However, this assessment is not supported by quantitative or qualitative analysis to demonstrate that vertical integration is the root cause. The attribution of liquidity constraints to vertical integration also appears to contradict the Electricity Authority's previously cited evidence which points to fuel and capacity scarcity:

[1] Stevenson, T. & Murray K., *Economic Analysis of the Electricity Authority's Proposed Level Playing Field Measures*. Sapere Research Group (2025).

"*The evidence points to fuel or capacity scarcity often being the driver behind the current thin and illiquid market for shaped hedge cover*" (Electricity Authority's Risk Management Review Options Paper).

The view that fuel and flexible capacity scarcity is the root cause is also supported by expert analysis:

(a) Modelling by KPMG and Concept Consulting shows that flexible generation is declining relative to demand, with residential consumption increasing significantly compared to non-intermittent generation since 2020. Even in a highly renewable future (98% renewable scenario), New Zealand will require approximately 1,000 GWh of flexible generation on average, ranging from 200 GWh in wet years to 2,700 GWh in dry years. Without thermal generation from the Rankine units at Huntly, wholesale electricity prices would likely be 60% higher in the short-term and 11% higher in the long-term.[2]

(b) Sapere's analysis shows that the availability of flexible generation to underpin flexibility contracts has declined to the point of discernible fuel or capacity scarcity and will continue to decline relative to demand.[3]

This physical constraint - not vertical integration - is the fundamental issue facing the market. Yet, the Task Force's proposed measures do not address this physical scarcity and instead seek to fundamentally restructure a well-established means of managing risk (which has supported existing generation and the investment in new flexible capacity) when alternative risk management mechanisms are undeveloped and costly.

While hedge market liquidity is a legitimate area of focus for the regulator, the solutions to its challenges do not lie in non-discrimination provisions and virtual disaggregation measures. The Task Force's proposal to require proportional allocation of existing flexible resources would not increase their overall availability. No rule requiring proportional allocation of a scarce resource will make that resource more abundant. To the extent that there are perceived market inefficiencies, the Task Force should seek to be address this by consulting on a careful and evidence-based problem definition.

Evidence supports current market structure

The Task Force glosses over the importance and delivered benefits of vertical integration. These have been considered over the years, and confirmed by recent analysis showing the importance of the role that vertical integration plays, and the benefits that it provides, to the New Zealand electricity market:

(a) 2019 research and modelling by Professor Andy Philpott of the University of Auckland and others showed that vertical integration serves as an effective risk

[2] See https://assets.kpmg.com/content/dam/kpmg/nz/pdf/2025/02/the-need-for-energy-storage-kpmg-and-concept-consulting-february-2025.pdf
[3] Sapere Report, section 2.

management mechanism, allowing companies to hedge against price and volume risks better than through contracts alone. This reduces spot market volatility impacts on retailers who can balance generation and retail positions internally. The model enhances market competition, as gentailers aligning generation and retail operations have less incentive to inflate prices since high wholesale prices would hurt their retail margins. This internal balancing creates more stable consumer prices and a more resilient electricity market.[4]

(b) A 2021 report by Dr Richard Meade concluded that vertical integration reduces transaction costs, improves risk management, and enhances retail competition by allowing gentailers to offer competitive prices while maintaining balanced generation portfolios. He concluded consumers benefit because vertical integration provides protection against wholesale price risks, insulating them from price volatility while helping gentailers finance investments. A further advantage was the elimination of double marginalization, resulting in lower retail prices than would occur under separation.[5]

The 2025 Sapere Report commissioned by Genesis confirms that vertical integration is the prevailing organisational form in competitive electricity markets globally. In Singapore, seven largest vertically integrated generator retailers produce around 90% of total electricity generation. In Australia, the three largest vertically integrated firms supply approximately 74% of residential customers in NSW, 72% in Queensland, and 73% in South Australia. Similarly, analysis of the Australian National Electricity Market by Frontier Economics for example found that:

> "*vertically integrated generators in fact behave more competitively on average than when they were operating as stand-alone generators.... This statistically significant, robust and striking result is contrary to claims that vertically integrated generators will bid at higher prices than stand-alone generators.*"

These markets function competitively without the interventions proposed by the Task Force.

Sapere also analysed each of the local and international examples cited by the Task Force in the Options Paper and found that all were addressing different problems and are inappropriate analogies. None – including the Telecom and ECNZ separations – were seeking to address the shaped liquidity problem currently facing New Zealand.[6]

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[4] Professor Andy Philpott et al.*'The New Zealand electricity market: challenges of a renewable system'*(2019) at https://www.epoc.org.nz/papers/IEEEMagazineArticlev2.pdf.

[5] Dr Richard Meade, '*Review of the economics literature on the pros and cons of vertical integration and vertical separation in electricity sectors'* (2021) at https://www.cognitus.co.nz/_files/ugd/022795_90a6a69bdaca4de9b752db7798bf2a2d.pdf commissioned for the ERANZ.

[6] Sapere Report, sections 4, 5 and 6.

Flawed competition analysis

The Task Force appears to conflate protection of competitors with protection of competition.

As the Sapere Report explains:

(a) The OECD Competitive Neutrality Toolkit emphasises, government intervention should not distort markets in favour of particular participants. The Task Force's proposals would do precisely this—providing a "leg up" to certain business models rather than allowing firms to compete on their merits;

(b) The Task Force seeks to create a level playing field by requiring gentailers to offer products like peak hedge contracts to external parties on the same terms they supply internally. This approach misconstrues competitive dynamics, contradicts established principles for competitive level playing fields, and would lead to less efficient allocation of scarce resources. Vertical integration is an efficient method for managing risks associated with investing in and maintaining long-lived flexible generation assets. However, the Taskforce's analysis appears to undervalue (or ignore outright) these factors, with the result that non-discrimination rules are favoured that would in fact incentivise business models that avoid investing in and maintaining long-lived assets. This bias would not be in the long-term interests of consumers.

(c) Competition is a process of rivalry. Effective competition is entirely consistent with the entry and exit of individual competitors. There are several reasons that may explain why independent retailers have not increased market share. Detailed analysis of the market dynamics that may drive entry and exit of firms should be carried out before considering tilting the playing field in favour of particular entities or business models.

Further, for vertical integration to harm competition through "raising rivals' costs" (foreclosure), two critical conditions must be met:

(a) the integrated supplier must have sufficient market power to unilaterally deny rivals access to an essential input or materially raise its price above competitive levels;

(b) the entity must reasonably expect to recoup the losses from denying profitable sales to a rival through higher sales resulting from the rival exiting the market.

None of the Authority's investigations have concluded that any of the gentailers have sufficient market power to foreclose a rival and as the Sapere Report shows neither of these conditions are met in the New Zealand electricity market.

Finally, we note that while some participants have left the market, others have entered, including Lodestone Energy which appears to have had little difficulty

investing in a material volume of new renewable generation, competes for customers, and has recently chosen to operate an integrated model.

Individual businesses are free to choose whether to invest capital in generation assets in New Zealand and, in doing so, to access the resulting benefits in economic risk management. It is not the role of regulators to intervene to transfer those benefits from those that have invested to those who have chosen not to.

Evidence shows vertical integration delivers substantial benefits

In addition to those discussed earlier, vertical integration delivers the following quantifiable benefits:

Shielding consumers from price volatility

Vertically integrated businesses play a key role in protecting consumers from market volatility. Their ability to manage risk efficiently acts as a buffer between consumers and the often volatile wholesale electricity market, providing price stability for consumers in challenging market conditions. This benefit is reflected in the Authority's Review of Winter 2024, which found that residential customers were shielded from high spot prices due to effective hedging.[7]

Investment in Generation and Flexible Capacity

Vertical integration creates revenue stability and risk management capacity essential for long-term investment. This is reflected in the substantial investment in existing and new generation by vertically integrated firms over the past three decades.

Our Gen35 strategy demonstrates this and recognises the dual need for renewable expansion and system security. We are:

(a) committed to deliver approximately 5 TWh of renewable energy by FY2028;

(b) developing more than 1,300 MW of flexible capacity (coal, gas, biomass, BESS) to secure against market volatility in a highly renewables based grid;

(c) progressing several renewable projects including Lauriston Solar Farm (63 MWp), Edgecumbe Solar (127 MWp), Leeston Solar (67 MWp), and Foxton Solar (200 MWp); and

(d) investing in a 100 MW Battery Energy Storage System (BESS) at Huntly.

Significant Risks with the Task Force's Proposed Approach

The Task Force's proposed three-step roadmap carries significant risks:

[7] Electricity Authority, April 2025, 'Review of Winter 2024', https://www.ea.govt.nz/documents/7069/Review_of_winter_2024.pdf

Creating Regulatory Uncertainty and Undermining Investment

The Task Force's proposals threaten the investment framework that has delivered existing and new generation capacity. Interfering with the benefits of vertical integration without addressing the underlying issue of capacity scarcity, risks undermining investment incentives at precisely the time when New Zealand needs more investment in flexible generation.

The New Zealand electricity market is emerging from a period of heightened investment uncertainty compounded by prolonged policy and regulatory uncertainty. The sources of these uncertainties included:

(a) the proposed New Zealand Battery Project and the prospect of the Government entering into the market to provide firming capacity, undermining incentives for peak supporting plant;

(b) the offshore gas exploration ban and temporary halt to onshore exploration permits, reducing incentives for gas production against a backdrop of declining gas production from New Zealand's major gas fields; and

(c) Rio Tinto's intentions to close the Tiwai aluminium smelter raising the prospect of significant demand reduction reducing wholesale prices, and undermining the business case for new firm capacity.

The Task Force's three-step approach, with escalating interventions, creates more uncertainty. This uncertainty is particularly damaging in a sector characterised by long-lived assets and substantial capital requirements.

We note that the uncertainty does not just impede investment in new generation capacity and alternative fuels - it undermines the economic case for maintaining existing flexible generation assets that provide critical security of supply.

The KPMG/Concept Consulting study clearly demonstrates that Huntly's Rankine units represent the most cost-effective form of hydro firming available to New Zealand. Despite this, Genesis faces the difficult decision to retire the third Rankine unit in February without securing long-term Huntly Firming Option (HFO) contracts.

The fundamental challenge is that as new renewables enter the market, flexible generation runs less frequently, requiring higher prices for a period of time to achieve economic returns. When these higher price levels are considered unacceptable by market participants and regulators without due regard to the underlying drivers, this results in an unsustainable economic model for maintaining crucial firming capacity.

We are advancing negotiations with industry participants to maintain the third Huntly Rankine Unit, supported by long-dated Huntly Firming Options (**HFOs**) and discussions for a jointly-funded coal reserve for national energy security. Without these arrangements, the economic case for maintaining this capacity will not exist. While HFOs will be offered to the broader market (as occurred last year), market

participants must be willing to contribute to the costs and risks if they wish to benefit from this capacity.

The difficulty in justifying investment in existing firming plant demonstrates the even greater challenge in developing new firming capacity and fuels - precisely when the system needs more flexibility to support increasing intermittent renewable generation. The uncertainty created by the Task Force's proposals exacerbates these challenges.

Misallocating Scarce Resources

The Task Force proposes a fundamental change in how the market allocates scarce flexible generation resources by requiring flexible generation suppliers to shift from allocating available hedge capacity based on price to allocating it based on quantity.

The Sapere Report notes:

> "*A move by the Authority to favour a quantity allocation method of a scarce resource is perplexing. The policy shift runs counter to established literature on the design of efficient markets. The Authority appears not to have turned its mind to the distortions to the efficient operation of the market (one of its statutory objectives) that would be introduced by its proposed rule. This apparent lack of analysis is surprising, as a matter of economic analysis, and because the Authority is required by the Government Policy Statement 2024 to have regard to "the benefits that accurate price signals and decentralised risk management provide in promoting efficient reliability and security of supply."*

Efficient price discovery is essential for the optimal allocation of scarce resources. By departing from this fundamental principle, the Task Force's proposal risks creating inefficiencies that will ultimately harm consumers through higher prices and reduced security of supply.

Conclusion and Recommendation

Sapere caution that:

> *"The Authority seems intent to embark on a roadmap toward removing an established means of managing risk—a means which in practice has been necessary to support investment in flexible generation—when alternative mechanisms of risk management are under-developed or costly. Such an action cannot be reconciled with the long-term interests of consumers".*[8]

New Zealand's electricity market faces genuine challenges requiring thoughtful policy responses. Misdiagnosing vertical integration as the problem while ignoring physical capacity constraints will exacerbate those challenges.

[8] Sapere Report, at page 21.

For the reasons set out in this submission and the Sapere Report, Genesis urges the Task Force to:

(a) reconsider its problem definition and focus on the real constraint – physical scarcity of flexible generation resources;

(b) recognise the benefits of vertical integration and avoid interventions that would compromise these benefits without clear evidence of harm to consumers;

(c) adopt a "first do no harm" approach that recognises the high costs of regulatory error in a sector characterised by long-lived assets and substantial capital requirements;

(d) focus on developing measures that would address the real constraint:

  (i) support for investment in new flexible generation capacity and alternative flexibility resources;

  (ii) market settings that provide price signals for flexibility services; and

  (iii) continued development of standardised flexibility products.

Yours sincerely

Matt Ritchie
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SCHEDULE

Question	Comment
Q1. What are the benefits of vertical integration between generation and retail? Do you have any evidence to better specify and quantify these benefits? In particular, we are interested in benefits that would be realised by New Zealand's electricity consumers.	As a vertically integrated generator-retailer, we have direct experience of the benefits that this business model brings to New Zealand's electricity system and, ultimately, to consumers. As discussed in this submission and the Sapere Report, vertical integration delivers clear, quantifiable benefits to New Zealand electricity consumers.
Q2. Do you agree with our description of the competition concerns that can arise from the combination of Gentailer vertical integration and market power? Why/why not? Do you have any evidence to better specify and quantify the competition risks of vertical integration?	Genesis Energy does not agree with the Task Force's characterisation of competition concerns arising from vertical integration nor its proposed non-discrimination obligations. As discussed above and in the Sapere Report: 1. The Task Force has fundamentally mischaracterised the nature of competition in vertically integrated markets by failing to apply the proper economic framework for assessing foreclosure concerns. 2. The primary drivers of concerns about hedge market liquidity and pricing concerns are fuel and flexible generation capacity, not vertical integration. 3. Vertical integration delivers substantial benefits to the New Zealand electricity market, including enhanced investment incentives, revenue stability, more competitive wholesale pricing, and better management of residual volume risk.

	4. Genesis Energy's approach to portfolio management demonstrates how vertical integration enables a balanced strategy that supports both energy security and decarbonisation. For the reasons set out in this submission and the Sapere Report, Genesis urges the Task Force to: (e) reconsider its problem definition and focus on the real constraint – physical scarcity of flexible generation resources; (f) recognise the benefits of vertical integration and avoid interventions that would compromise these benefits without clear evidence of harm to consumers; (g) adopt a "first do no harm" approach that recognises the high costs of regulatory error in a sector characterised by long-lived assets and substantial capital requirements; (h) focus on developing measures that would address the real constraint: (i) support for investment in new flexible generation capacity and alternative flexibility resources; (ii) market settings that provide price signals for flexibility services; and continued development of standardised flexibility products.
Q3. To what extent does vertical integration of smaller gentailers, such as Nova and Pulse, raise competition concerns? Should these smaller gentailers be subject to any proposed	For the reasons set out above and in the Sapere Report, the Task Force's premise is flawed and it has misdiagnosed the problem. We note Lodestone Energy's intention to vertically integrate[9] as an example of new entrant using the model to build a significant amount of new renewable generation and compete

[9] https://www.energynews.co.nz/news/solar/817170/lodestone-seeks-faster-growth-through-retailing.

Level Playing Field measures?	for customers. We do not consider that the vertical integration gives rise to the concerns raised and gentailers – irrespective of their size – should not be subject to the proposed measures.
Q4. Are there other specific areas (other than access to hedges) where Gentailer market power and vertical integration are causing competition concerns?	Please see responses above and the Sapere Report.
Q5. Do you agree with our preliminary view that the evidence indicates there may be good reasons to introduce a proportionate Level Playing Field measure to address the competition risks in relation to hedging/firming? Why/why not?	We do not agree with the Task Force's preliminary view. The Task Force provides no quantitative or qualitative analysis that vertical integration is the root cause of insufficient peak hedge contracts being made available for competing retailers and generators or pricing concerns. The principal drivers of concerns with liquidity and pricing are fuel and capacity scarcity. We ask the Task Force to reconsider its approach and focus on measures that will address the real constraint rather than introducing potentially damaging interventions. Please see further the responses above and the analysis in the Sapere Report.
Q6. Have we focused on the right Level Playing Field options? Are there other options that we should add or remove to the list in paragraph 4.1?	The Task Force has misdiagnosed the problem and as a result has not focused on the correct options. The four options identified all target vertical integration when the evidence clearly indicates that the fundamental issue is fuel and the physical scarcity of flexible generation resources. We recommend that the Task Force: 1. Remove corporate separation (Option 4) from consideration due to its high costs and uncertain benefits

	2. Refocus its efforts on options that directly address the physical scarcity of flexible generation resources, including: o Measures to support investment in flexible generation o Further development of the standardised flexibility products 3. Adopt a "first do no harm" approach that recognises the high costs of regulatory error and the critical importance of maintaining investment incentives for flexible generation Please see further the responses above and the analysis in the Sapere Report.
Q7. Are there any other important factors we should consider when identifying options (see paragraphs 4.2 to 4.5)?	Please see the responses above and the analysis in the Sapere Report.
Q8. Are there other key features, pros or cons we should consider in our description of the four Level Playing Field options?	Please see the responses above and the analysis in the Sapere Report.
Q9. Have we identified the right criteria for assessing Level Playing Field options (Figure 6)? Is there anything we should add or remove?	Please see the responses above and the analysis in the Sapere Report.

Q10. Do you agree with our application of the assessment criteria (Table 5)? Are changes needed to the colour coding or reasoning?	Please see the responses above and the analysis in the Sapere Report.
Q11. Are there any other material benefits or risks that should be considered (but are currently not) in our assessment of options?	Please see the responses above and the analysis in the Sapere Report.
Q12. Do you agree with our selection of non-discrimination obligations as our preferred Level Playing Field measure? Why/why not?	Please see the responses above and the analysis in the Sapere Report.
Q13. What are your views on our proposed roadmap for the implementation of non-discrimination obligations?	Please see the responses above and the analysis in the Sapere Report.
Q14. Which products should any non-discrimination obligations apply to? Should all hedge contracts be captured, or should the rules be focused on super-peak hedges only? Are there are other interactions between Gentailers and their	Please see the responses above and the analysis in the Sapere Report.

competitors which would benefit from non-discrimination rules?	
Q15. Do you have any feedback on the indicative draft non-discrimination principles (and guidance) set out in Appendix B? Without limiting your feedback, we would be particularly interested in your views on the following questions: a. Have we got the level of detail/prescription right? For example, do you consider that the principles and guidance will lead to economically meaningful Gentailer ITPs being put in place? What would be the costs and benefits of instead applying a more prescriptive ITP methodology? b. How far should the allowance in the principles for different treatment where there is a "cost-based, objectively justifiable reason" extend? Do you agree with the guidance that this allowance should not be extended to volume (at paragraph 13 of Appendix B)?	Please see the responses above and the analysis in the Sapere Report.

Q16. Do you agree that escalation options are needed if principles-based non-discrimination obligations are implemented initially? Why/why not?	Please see the responses above and the analysis in the Sapere Report.
Q17. Are prescribed non-discrimination requirements and mandatory trading of Gentailer hedges via a common platform suitable escalations given the liquidity, competitive pricing and even-handedness outcomes we are seeking? Why/why not? What alternatives would you suggest (if any)?	Please see the responses above and the analysis in the Sapere Report.
Q18. What costs and benefits are likely to be involved in setting more prescriptive regulatory accounting rules which detail how ITPs should be calculated? What would be appropriate triggers for introducing more prescriptive requirements for ITPs?	Please see the responses above and the analysis in the Sapere Report.

Q19. Do you have any views on how the non-discrimination requirements should best be implemented to ensure that Gentailers are no longer able to allocate uncontracted hedge volumes to their own retail function in preference to third parties? What are the key issues and trade-offs?	Please see the responses above and the analysis in the Sapere Report.
Q20. Do you have any views on the triggers for implementing the stronger regulation proposed in our roadmap	Please see the responses above and the analysis in the Sapere Report.
Q21. Does our proposed approach to implementing non-discrimination obligations (as set out in the roadmap in Figure 7) sufficiently address the underlying issue that originally led to MDAG recommending virtual disaggregation?	The Task Force's proposed non-discrimination obligations fail to address the fundamental issue of physical scarcity of flexible resources that led to MDAG's recommendation for virtual disaggregation. Instead of targeting vertical integration, which provides important risk management benefits and supports investment, the Task Force should focus on policy settings that will increase the supply of flexible resources to support New Zealand's transition to a highly renewable electricity system. Please see further the responses above and the analysis in the Sapere Report.
Q22. Do you have any views on whether virtual disaggregation provides a useful response to the competition risks we have identified	Virtual disaggregation is not an appropriate or useful response to the Task Force's alleged competition risks. It would be a high-risk approach that addresses the wrong problem, potentially undermining security of supply while failing to address the fundamental challenges facing New Zealand's electricity system. The fundamental challenge is ensuring energy system stability and security in a market with

(relative to the proposed roadmap) and, if it does, how it should be best applied?	increasing intermittent generation and declining thermal capacity. Virtual disaggregation incorrectly assumes that market power, rather than physical constraints, is the primary barrier to hedge liquidity. Please see further the responses above and the analysis in the Sapere Report.