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Submissions  
Electricity Authority  
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## **ERANZ SUBMISSION ON REWARDING INDUSTRIAL DEMAND FLEXIBILITY**

The Electricity Retailers' Association of New Zealand ('ERANZ') welcomes the opportunity to provide feedback on the Electricity Authority's issues and options paper 'Rewarding industrial demand flexibility' from May 2025.

ERANZ is the industry association representing companies that sell electricity to Kiwi households and businesses. Collectively, our members supply almost 90 per cent of New Zealand's electricity. We work for a competitive, fair, and sustainable electricity market that benefits consumers.

### **Objectives of industrial demand flexibility**

ERANZ strongly supports the goal of unlocking industrial demand flexibility as a tool for enhancing market efficiency, enabling the integration of renewable generation, and improving price outcomes for consumers. However, we are concerned that the issues and options paper's proposed focus risks diverting the initiative away from this objective.

Taskforce initiative 2D is seeking to unlock the value that industrial demand response ('DR') can bring to the electricity system by enabling more efficient participation by large industrial users in responding to short-term supply and demand conditions. This includes enabling industrials to contribute to:

- Smoothing intra-day price volatility,
- Deferring peak demand investment,
- Supporting system balance as intermittent renewables increase, and
- Improving overall market efficiency.

Unfortunately, the issues paper focuses heavily on the development of an Emergency Reserve Scheme ('ERS') as an out-of-market, last-resort mechanism aimed solely at system security. While ERS may have merit in extreme scarcity events, it is not a mechanism that meaningfully unlocks the value of industrial DR. Instead, it reflects a traditional capacity procurement model, with limited scope to support innovation or flexible behaviour in normal operating conditions.

We are concerned that by prioritising ERS, the Authority risks:

- Missing the opportunity to develop price-responsive, dispatchable flexibility services that operate within the market;
- Distorting incentives by rewarding rare, emergency interventions over continuous, proactive flexibility; and
- Crowding out commercial and bilateral flexibility arrangements between industrials, aggregators, and retailers.

ERANZ submits that the Authority's focus should return to the core purpose of Taskforce 2D: unlocking short-term (particularly intra-day) flexibility from industrial electricity users via market-based signals, mechanisms, and products.

ERANZ recommends the Authority prioritise enhancements to existing market mechanisms, including real-time pricing, hedge market depth, and third-party access in order to improve incentives for demand-side response. ERANZ supports the development of a standardised flexibility hedging product, as long as it remains voluntary, competitively neutral, and does not rely on regulatory underwriting.

ERANZ does not believe in creating new schemes to replicate capacity markets, because this risks undermining the integrity of New Zealand's energy-only market and long-term investment signals for new generation.

Unlocking industrial demand flexibility is not just about paying consumers to reduce demand in extreme events, it is about enabling them to participate in the electricity market in ways that deliver continuous value, reduce costs, and improve reliability through efficient, market-based engagement.

### **Payments beyond market price signals**

ERANZ supports the efficient integration of industrial demand flexibility into the electricity market. However, we are concerned by the proposal to introduce payments to industrial participants that go beyond avoided energy costs and price exposure. This represents a departure from the current market-based approach and risks distorting both price formation and competition.

The issues paper suggests that industrial demand flexibility providers could be compensated through additional payments over and above spot market price avoidance where this is deemed to offer a "net benefit" to consumers:<sup>1</sup>

*"This could involve payments to industrial demand flexibility providers, additional to avoided energy costs – if there is a clear benefit for consumers."*

While we recognise the Authority's intent to unlock underutilised demand-side capability, we caution against the use of non-market, administratively determined payments to do so.

Payments for demand response outside of the market:

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<sup>1</sup> Electricity Authority, 'Rewarding industrial demand flexibility: issues and options paper', page 3.

- Undermine price-based incentives, which are the cornerstone of efficient operation in an energy-only market.
- Create a risk of “over-compensating” demand response providers relative to their opportunity cost, distorting investment and dispatch decisions.
- Introduce complexity, subjectivity, and risk of rent-seeking, particularly if benefits are difficult to quantify or payments are based on counterfactual demand estimates.
- May result in unequal treatment across consumer types, especially if some participants receive regulated payments while others rely on market signals.

The Authority’s previous position that consumers should respond to prices, not be paid not to consume, remains valid. Where demand flexibility is efficient, price signals should be sufficient to incentivise participation. If they are not, the solution should lie in improving price signals (e.g., through scarcity pricing, better hedge products, or dynamic tariffs), not layering on subsidies.

Moreover, introducing payments beyond price avoidance risks setting a precedent for out-of-market interventions that may be difficult to reverse and could dampen long-term investment signals for generation, storage, and true flexible capacity.

ERANZ recommends that the Authority recommit to market-based incentives for demand response, ensuring that demand flexibility is rewarded through energy and hedge market signals. We consider that the Authority should avoid introducing administered payments or subsidies that are not grounded in real-time price signals or open competition.

If additional payments are considered, the Authority should develop clear, transparent, and time-bound criteria to ensure they are used only as a transitional mechanism, and are explicitly reviewed for cost-effectiveness and distortionary effects. Unlocking demand-side flexibility should reinforce the integrity of the electricity market, not introduce parallel mechanisms that fragment it.

### **Standardised demand flexibility hedge product**

ERANZ supports initiatives that enhance risk management tools in the wholesale market, especially as the system transitions to higher levels of intermittent generation. We acknowledge the potential value of a standardised demand flexibility hedge product in helping to unlock industrial demand response and improve access to flexibility services for a wider range of market participants.

We welcome the Authority’s intent to explore this idea through an industry-led co-design process, building on the approach used for the development of the super-peak hedge contract. A standardised product may reduce transaction costs, foster innovation, and increase liquidity, particularly for smaller retailers or aggregators who may otherwise find it difficult to negotiate bespoke bilateral arrangements.

At the same time, we encourage the Authority and the co-design group to carefully consider important design features as this work progresses. Firstly, any standardised product should remain voluntary, without becoming de facto mandatory or creating expectations that participants must use it to demonstrate prudent risk management.

The product should be grounded in clear commercial value, with demand and uptake driven by participants' own needs, not by regulatory pressure or incentives. ERANZ would be cautious about any proposal where the Authority or system operator acts as a counterparty or provides financial backing. Products should succeed or fail based on their own market merit.

The Authority should consider wider applications of the product and be open to a range of flexibility sources, including aggregators, distributed resources, and smaller commercial loads—not just large, industrial users. Care must be taken to ensure that the introduction of this product does not undermine the operation of existing hedge products or unintentionally shift risk between parties in a non-transparent way.

In summary, ERANZ is open to the exploration of a standardised demand flexibility hedge product, provided its development is guided by market principles, remains optional, and enhances rather than displaces the competitive dynamics of the electricity market.

## **Conclusion**

ERANZ would like to thank the Authority for considering our submission.

Yours sincerely,

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