

13 May 2022

s9(2)(a)

Dear s9(2)(a),

Thank you for your request, received on 20 April 2022, for the following information under the Official Information Act 1982 (the Act):

- “Summary of Submissions on the Authority’s Wholesale Market Review, as supplied to Minister Hon Dr Megan Woods on 25 March, 2022.”

The Authority has identified one document within scope of your request. This is attached to this letter. Some information is being withheld under the Act for the below reasons:

- Section 9(2)(a) – to protect the privacy of natural persons.
- Section 9(2)(g)(i) - the free and frank expression of opinions by or between or to Ministers of the Crown or members of an organisation or officers and employees of any public service agency or organisation in the course of their duty.

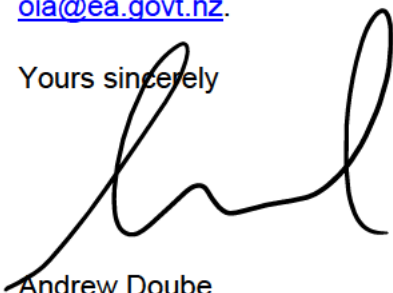
I am satisfied, in terms of section 9(1) of the Act, that the need to withhold the information referred to above is not outweighed by other considerations that render it desirable, in the public interest, to make the information available.

You have the right to seek an investigation and review by the Ombudsman of this decision. Information about how to make a complaint is available at www.ombudsman.parliament.nz or freephone 0800 802 602.

This request and its response will be published on the Electricity Authority website.

If you wish to discuss this decision with us, please feel free to contact us by emailing oi@ea.govt.nz.

Yours sincerely



Andrew Doube
GM Market Policy

MINISTERIAL BRIEFING

Summary of submissions on the Authority's Wholesale Market Review

Date:	Fri, 25 March 2022	Priority:	Medium
Security classification:	In Confidence	Electricity Authority reference number:	BR-22-0017

Action sought – Noting		
	Action	Deadline
Hon Dr Megan Woods Minister of Energy and Resources	note the Authority's summary of submissions and next steps	N/A
Appendices included	Yes	

Contact for telephone discussion (if required)				
Name	Position	Telephone		1st Contact
Andrew Doube	General Manager, Market Policy	-	s9(2)(a)	✓
Imogen Turner	Policy Analyst	-	s9(2)(a)	

Drafter	Imogen Turner	Position	Policy Analyst
----------------	---------------	-----------------	----------------

Authorisation for publication on Authority website	<input type="checkbox"/> Approved	<input type="checkbox"/> Declined
---	-----------------------------------	-----------------------------------

The following departments/agencies have been consulted
The Authority has discussed submissions with the Ministry of Business, Innovation and Employment (MBIE)

- Minister's office to complete:**
- | | |
|---|--|
| <input type="checkbox"/> Approved | <input type="checkbox"/> Declined |
| <input type="checkbox"/> Noted | <input type="checkbox"/> Needs change |
| <input type="checkbox"/> Seen | <input type="checkbox"/> Overtaken by Events |
| <input type="checkbox"/> See Minister's Notes | <input type="checkbox"/> Withdrawn |

Comments

Purpose

As noted in the Authority's briefing to you on 12 October 2021 (BR-21-0045), we undertook to provide a summary of submissions and next steps following consultation on the Authority's recent consultation papers:

- Market Monitoring Review of structure, conduct and performance in the wholesale market (Wholesale market review paper); and
- Inefficient price discrimination in the wholesale market – Issues and options (Inefficient price discrimination paper), which is the Authority's initial response to the Review.

Recommended action

Hon Dr Megan Woods, Minister of Energy and Resources

It is recommended that you:

1. Note that consultation on the Wholesale market review paper and the Inefficient price discrimination paper closed on 22 December 2021. **Noted**

Wholesale market review paper
2. Note that the Wholesale market review paper looked at competition in the wholesale market from January 2019 until early 2021 using a structure, conduct and performance framework (i.e., the right structure drives good conduct which results in a performing market). **Noted**
3. Note that submissions on the Wholesale market review paper were broadly consistent within categories of stakeholder – at a high level, generators generally considered the wholesale market is competitive and supported the status quo, whereas independent retailers and industrial users thought the market is not working and advocated for structural reform. All submissions have been published on the EA website. **Noted**
4. Note the Authority will consult again with stakeholders in June/July 2022 on the next steps in the review, s9(2)(g)(i) **Noted**

Inefficient price discrimination paper
5. Note that the Inefficient price discrimination paper was the Authority's initial response to the Wholesale market review paper and addresses the incentive generators have to enter large contracts that result in inefficient price discrimination - in effect economically withholding electricity and thereby raising prices for consumers not party to the contract. **Noted**
6. Note that submissions on the Inefficient price discrimination paper were broadly consistent within categories of stakeholder - generators generally did not consider there to be a material problem, whereas independent retailers did, and industrial users viewed the 'Tiwai contracts' as a symptom of more fundamental competition issues. **Noted**

7. Note the Authority is of the opinion that issues outlined in the inefficient price discrimination are on-going and material and intends to consult in June/July 2022 with an expectation to implement potential remedies by the close of 2022.

Noted

Departmental engagement and links to other work

8. Note the Authority is in regular contact with MBIE on both papers and is seeking to re-engage with MBIE and the Treasury at working level as the work progresses into the next phases of analysis.

Noted



Andrew Doube
General Manager
Electricity Authority

25 / 03 / 2022

Hon Dr Megan Woods
Minister of Energy and Resources

..... / /

Background

1. The Wholesale market review paper investigated competition in the wholesale market from January 2019 until early 2021. A structure, conduct and performance framework was used, which is based on the theory that market structure has a direct impact on firms' conduct in a market, which in turn affects their performance.
2. The Authority looked at different indicators to assess structure, conduct and performance during the review period. The indicators suggested some potential concerns around competition, though drawing conclusions based on a single indicator can be problematic:
 - Structure - Meridian was gross pivotal 90-95% of the time during the review period. In contrast, Meridian was gross pivotal around 77% of the time in each year before the review period from 2016 to 2018.
 - Conduct - some evidence that spot prices may not always have been determined in a competitive environment, and potential inefficiency from the 'Tiwai contracts' between Meridian Energy, Contact Energy and New Zealand Aluminium Smelters (NZAS).
 - Performance - there was a thin pipeline of investment in new generation, potentially signalling a problem with barriers to entry and investment.
3. The Inefficient price discrimination paper responded to the review paper's observation regarding the potential for inefficient price discrimination illustrated by the Tiwai contracts, and was prioritised because the inefficiencies were potentially large and with material implications for consumers and generators. The Authority viewed that Meridian and Contact had the incentive to subsidise the smelter because retaining NZAS's demand increases spot and forward prices nationally and therefore leads to higher revenues for all generators. The cost of any subsidy is potentially more than offset by the higher revenues earned from other consumers.
4. The Authority's main concern was that there may be an on-going incentive for generators to enter contracts of a Tiwai type nature given these commercial incentives. The Inefficient price discrimination paper also proposed potential regulatory interventions the Authority could advance through a Code amendment if the Authority found there is a need for a policy response.
5. The Authority sought feedback on the robustness and completeness of the methodology in the Wholesale market review paper. The Authority consulted on the completeness of the indicators used and whether any others should be considered. With respect to the Inefficient price discrimination paper, the Authority also sought feedback on the materiality of the problem and its future relevance, as well as comments on the possible regulatory interventions.

Summary of submissions

6. Submissions closed on 22 December 2021 and the Authority received submissions from 31 different stakeholders as shown in the appendix. All 31 submitters commented on the Wholesale market review paper and 23 submitters commented on the Inefficient price discrimination paper. All submissions are also available on our website.
7. The Authority received roughly equal numbers of submissions from generator retailers, industrial users and independent retailers on both papers. Other submitters represented electricity distributors, independent bodies, consultancies and interested individuals.

Themes arising in submissions on the Wholesale market review paper

Opinions on methodology and scope

8. In terms of the methodology deployed, some submitters advocated for broadening or changing the analysis in the Wholesale market review paper, including:
 - investigating over a longer time period;
 - using alternative frameworks with which to compare market outcomes (e.g., assessing outcomes against perfect or workable competition using simulations, assessing outcomes against the levelized cost of electricity instead of to short-run marginal costs); and
 - expanding the scope to include the impacts on retail markets and the environment.
9. Some generators and industrial users discussed the need for an energy strategy and joined up approach between the Authority, GIC and other government departments during the transition.

Opinions on whether the wholesale market is competitive and suggested implications

10. In terms of the functioning of the wholesale market:
 - Generators consider the market is competitive and are broadly supportive of the status quo.
 - Independent retailers and industrial users consider the market is not working and advocate for structural reform.
11. Generators, independent retailers, and industrial users suggested a range of potential interventions or areas for further investigation if the Authority decides to make changes based on the observations in the review. Given the diversity of views on the extent of competition problems amongst market participants, it is not surprising that a wide range of possible interventions were proposed:
 - greater information disclosure around gas,
 - increased monitoring of the new trading conduct rules with greater penalties,
 - deeper investigation into barriers to investment,
 - proposals to reform market design e.g., various options on how electricity should be priced, options for dealing with intertemporal constraints,
 - more (or improved) financial risk products, including calls for the Authority to support the development of a market platform for power purchase agreements, and
 - structural reform e.g., splitting up of generators or vertical separation

Intention to consult on next steps

12. s9(2)(g)(i) [REDACTED]
13. The Authority intends to consult on the next steps in the review in June/July 2022. s9(2)(g)(i) [REDACTED]

Themes arising in submissions on the Inefficient price discrimination paper

Generator retailers support the status quo

14. Generator retailers generally did not consider the Tiwai contracts were indicative of an on-going problem – they viewed the Tiwai contracts as resulting from a unique set of circumstances. Most generator retailers, especially Meridian and Contact, criticised the Authority's efficiency analysis and did not consider the Tiwai contracts were inefficient. Generator retailers generally did not think a case had been made for intervention.
15. Some generator retailers questioned whether the some of the proposed policy options were within the Authority's mandate. They raised concerns that some of the proposed options may result in unintended consequences and create additional uncertainty at a time when significant investment is needed to transition to 100% renewables. As a consequence, generator retailers argued that in the event the Authority intervened, the intervention should be of a less intrusive nature to some of the proposed policy options e.g., greater transparency, limits to use it or lose it clauses and extending the trading conduct rules from the spot market to the hedge market.
16. In particular, some generator retailers raised concerns about the Authority pre-approving large contracts. They argued the Authority is not well placed to assess the efficiency of contracts and would create delays and uncertainty, as well as creating an undesirable precedent of the Authority interfering with commercial arrangements. In coming to this view, it is possible that generator retailers thought that pre-approval would apply to a large number of contracts, whereas this option, if implemented, would in practice only apply to perhaps a few contracts each decade.
17. It is also noticeable that generator retailers' submissions focused on the specific case of the Tiwai contracts rather than the existence of and incentives to subsidise large demand to maintain national price levels.

Independent retailers support intervention to address inefficient and wider price discrimination

18. Independent retailers were generally supportive of the Authority's findings and supported intervention to address inefficient price discrimination. Independent retailers considered intervention would support investment during the transition and give greater confidence in the market to participants.
19. Some independent retailers argued for the widening of the scope of the Authority's investigation into inefficient price discrimination to include other areas such as: access and pricing of hedges in the Over the Counter (OTC) market and prohibiting cross subsidies within generator retailers to prevent margin squeezing. s9(2)(g)(i)
[REDACTED]
20. Most independent retailers supported intervention to prevent inefficient price discrimination in future, so long as this did not result in the Authority deprioritising addressing the more fundamental competition issues they argue exist in the wholesale market.

Industrial users thought inefficient price discrimination was a secondary issue

21. Industrial users and their representatives generally thought Tiwai was a secondary issue, and the Authority should focus on addressing structural problems in the wholesale market. MEUG and BEC thought that some of the more far-reaching policy options identified in the inefficient price discrimination paper may create regulatory uncertainty at a time when a significant amount of investment is needed to transition to 100% renewables.

s9(2)(g)(i)

Media and communications approach

24. Our media approach will focus on providing a clear narrative which addresses the need for interventions to remain consistent with the longer-term need for investment in renewable generation. We'll work closely with specific journalists to ensure we're continuing to develop public understanding and perception of the Wholesale Market Review programme of work. This will include back pocket Q & As which address any risks noted below and provide clear key messages for both your Office and the Authority.

Risk mitigation

25. These responses to the review will come at a time when there is significant media interest around inflationary pressures and the cost of living. Electricity is a significant cost to New Zealand households, more so given historically high spot and futures prices. There is a risk that media and public opinion calls for immediate interventions to address high prices, including structural reform, which may not be consistent with incentives to invest in renewable generation, and may not prove to be in the long-term interest of consumers.

26. The Authority is mitigating this risk, s9(2)(g)(i) through undertaking a rigorous policy process coupled with regular communications activity with stakeholders, including consumer groups. These activities emphasise transparency around the Authority's processes and timelines. Our communications will also highlight the different causes of price rises i.e. due to fundamentals, such as gas uncertainty, dry year risk and global supply chain issues or, due to possible issues with the competitiveness of the wholesale market. The different causes will likely have implications for the appropriate policy interventions e.g. welfare interventions to address access and affordability versus competition and efficiency interventions to improve the long term interests of electricity consumers.

Next steps

27. The Authority intends to:

- consult on the Authority's next steps following the Wholesale market review paper in June/July 2022.
- s9(2)(g)(i)

Appendix

Table 1: Submissions by category of submitter

Category	Submitter	Submission commented on the Wholesale market review paper	Submission commented on the Inefficient price discrimination paper
Generator retailers / representatives	Meridian	Yes	Yes
	Contact	Yes	Yes
	Trustpower	Yes	Yes
	Genesis	Yes	Yes
	Mercury	Yes	Yes
	Nova	Yes	Yes
	ERANZ	Yes	Yes
Total submissions from generator retailers		7	7
Industrial users / representatives	MEUG	Yes	Yes
	Business Energy Council (BEC)	Yes	Yes
	NZAS	Yes	No
	NZ Steel	Yes	Yes
	Fonterra	Yes	Yes
	Winston Pulp	Yes	Yes
	OceanaGold	Yes	Yes
Total submissions from industrial users		7	6
Independent retailers / representatives	Electric Kiwi + Haast	Yes	Yes
	Flick Electric	Yes	Yes
	Independent retailers	Yes	Yes
	Octopus Energy	Yes	Yes
	Community Power	Yes	Yes
	Paua to the People	Yes	Yes
Sustainability Trust	Yes	Yes	
Total submissions from independent retailers		7	7
Other submitters	Electric Power Optimization Centre	Yes	No
	Community Energy Network	Yes	No
	Energy Link	Yes	No
	Entrust	Yes	Yes
	Energy Resources Aotearoa	Yes	No
	Exergi	Yes	No
	Neil Walbran	Yes	No
	Paul Maynard	Yes	Yes
	Roderick Aldridge	Yes	Yes
	Bryan Leyland	Yes	No
Total submissions from other submitters		10	3
Total submissions across all categories of submitter		31	23