20 December 2024

Electricity Authority
P O Box 10-041
Wellington

By email: rmr@ea.govt.nz

Dear team

Re: Reviewing risk management options for electricity retailers - Issues Paper

Flick welcomes the opportunity to make this submission on the Electricity Authority's (Authority) Issues Paper relating to the review of risk management options for electricity retailers.

Flick is a signatory to the joint submission by the Independent Electricity Retailers (IER) group. Our own submission focuses on our concern about the disconnect between the evidence / outcomes / analysis the Authority has included in the Issues Paper and what the Authority has indicated might be next steps.

The Authority's two conclusions from this review appear to be that:

- OTC super-peak hedge contract prices are not competitive as they trade at a substantial unquantified premium over ASX baseload prices adjusted for shape[1]
- evidence suggests that a deeper and more liquid OTC market would benefit consumers particularly for those hedges that can be combined with baseload hedges to create effective portfolios[2]

The Authority then proposes "key criteria that might be required for any policy intervention in the risk management space, flowing from the evidence and analysis in this review".[3]

Flick submits the "key criteria" would be completely ineffectual in ensuring a deeper and more liquid OTC market. Further, the evidence included in the review is wide ranging and reveals that gentailers use a range of ways to refuse to supply OTC contracts to independent retailers.

Appendix A overleaf is direct extracts from the Issues Paper on the evidence the Authority collected from its information requests of independent retailers and gentailers.

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[1] Page 2
[2] Paragraph 5.1 Chapter 8
[3] Paragraph 5.2 Chapter 8

The Authority's statutory objective includes to promote competition. In our view, the evidence reveals there is no competition if, for example:

- only one gentailer can be relied on to respond to all RFPs
- [only] around half the time [this could be less than 50% of the time] super peak requests received at least one conforming offer [that is, only one but maybe more than one offer - how many times did a super peak request receive 2 or more offers?]
- over a third of all OTC trades made by non-integrated retailers were from non-conforming offers [that is, in order to secure a hedge non-integrated retailers accepted a non-conforming offer a third of the time]

Flick agrees with the Authority that "there is a risk the Authority should respond to: "*there is also a plausible driver that has competition implications, eg, refusing to supply products on appropriate terms to counterparties who are downstream competitors, indicating that some level of market power could have been in play*".

In Flick's view the only solution to ensure a workably competitive wholesale market is for the Authority to regulate an equal access regime that ensures there is no price discrimination by generators - all generators compete to sell all their electricity to any retailer on the spot or hedge markets (exchange traded and OTC) ensuring there is no cross subsidisation of any 'related' retail business. Details of this solution have already been provided in the IER urgent Code change request.

A workably competitive wholesale market is critical to a workably competitive electricity retail market. Our view continues to be that gentailer activity (pricing and supply) in the wholesale market, including the OTC market that is the focus of this review, constitutes a margin squeeze and refusal to supply competitors that the Authority has concluded bring benefits to consumers.

No part of this submission is confidential.

Yours Sincerely

James Leslie

FLICK

APPENDIX A

The following are direct extracts from the Issues Paper where the Authority has stated information (evidence) or conclusions based on its analysis of the information. These extracts (found from numerous parts of the Issues Paper with the location provided in brackets) are grouped under headings.

Availability of hedges

- One gentailer (Mercury) priced responses for the vast majority of RFPs. Mercury states that it will "endeavour to price all requests from credible sources", and appears to do so (FN 8 page 10 Ch 7)

- This was a different approach to the other gentailers (point (b) para 5.4 page 6 Ch 7)

    - In some cases, Meridian chose not to respond [to RFPs] from gentailers or speculators "because there was limited commercial interest in the proposal, ie, the contract did not suit our portfolio at the time". Meridian said that it always endeavours to respond to at least some aspect of each request from non-integrated retailers (FN 6 page 6 Ch 7) Meridian … may choose not to respond to some aspects of a request if "the contract did not suit our portfolio at the time" (FN 8 page 10 Ch 7)

    - Some gentailers unilaterally decide that they would be unlikely to offer a competitive price, and therefore did not price the RFP/test the market (FN 6 page 6 Ch 7)

    - We have considered whether to seek further clarification from gentailers of the basis for any refusals to price responses to RFPs for shaped hedges, but decided that this was unlikely to lead to a more definitive view than the contemporaneous documents. As set out in chapter 8, we consider that this uncertainty is better addressed going forward by clearer requirements for gentailers around offering shaped hedges. (FN 6 page 6 Ch 7)

- Almost all requests (over 99%) received <u>at least</u> one offer (para 2.3 Ch 5) [emphasis added]

- Baseload requests almost always received at least one conforming offer while peak requests had a slightly lower rate and super-peak requests the lowest rate (para 4.2 Ch 5)

- Super-peak contracts are the most commonly requested and traded, but have the lowest rate of offers (para 4.9 Ch 5)

- Around half the time super peak requests received at least one conforming offer. (para 4.2 Ch 5)

- Super-peak contract requests … received fewer offers per request (point a) para 2.3 Ch 5)
- All offers received for super-peak contract requests were from gentailers (no other participant types responded to such requests) (point c) para 2.3 Ch 5)
- We consider it likely that (usually) the maximum number of respondents to super-peak requests is three. (para 4.9 Ch 5)
- Around half of all requests resulted in a trade (point d) para 2.3 Ch 5)
- the proportion of trades differed by contract type (para 4.9 Ch 5)
- Peak requests had a slightly higher proportion which resulted in a trade, while baseload and super-peak were similar (para 4.9 Ch 5)
- Occasionally multiple offers were accepted for one request (para 4.12 Ch 5)
- the recent high wholesale prices in July and August 2024 highlight the need for other contract types (covering periods outside the super-peak trading periods) as well (para 4.2 Ch 5)

Conforming versus Non-conforming

- Around a third of all offers received were for less volume than requested (point b) para 2.3 Ch 5)
- Over a third of all OTC trades made by non-integrated retailers were from non-conforming offers (para 3.11 Ch 5)
- It is less common for requests to get more than one conforming offer (para 4.6 Ch 5)
- For a small proportion of all requests that resulted in a trade, requestors accepted a non-conforming offer over a conforming one (para 4.6 Ch 5)
- [during 2024] There was an increase in the volume of contracts traded that were from non-conforming offers (para 4.13 Ch 5)
- A high proportion of traded baseload hedges were conforming offers, and prices were often comparable to ASX prices (para 2.6 Ch 5)

Price

- there appears to be an increasing trend in super-peak prices over time (relative to ASX baseload prices). When we add a shape premium to ASX prices, super-peak prices are sometimes still substantially higher. Offer prices for super peak contracts could be consistent with a lack of competition, or simply reflect scarcity. (para 2.7 Ch 5)

- There have been some accepted prices that were substantially higher than ASX prices (plus shape premium). This could be because the contract was competitively priced, or because the buyer had no other viable alternative (point (a) para 2.7 Ch 5)
- We also compared the OTC offer prices for super-peak products to the ASX baseload prices updated incorporating our estimates for premia. The results indicate that the accepted offers are still mostly above the ASX prices, even after including the premia (para 6.12 Ch 5)
- A high proportion of traded baseload hedges were conforming offers (para 2.6 Ch 5)
- OTC baseload offer prices have been comparable to ASX baseload prices. (para 6.6 Ch 5)
- Accepted offers for baseload tend to be closer to the ASX prices compared to prices that were not accepted (para 6.6 Ch 5)
- Requests with no offers accepted often (but not always) showed the highest deviation from the ASX, with a few offers priced considerably above the ASX (para 6.6 Ch 5)
- There was a slightly increasing trend in offer prices for baseload products over the time period we have data for. (para 6.6 Ch 5)
- peak products are usually offered at higher prices relative to baseload products, as expected for a shaped product (para 6.8 Ch 5)
- Offer prices for peak contracts did not appear to be increasing over the time period we have data for (relative to ASX baseload prices) (para 6.8 Ch 5)
- For peak products: When we added our estimates for premia to the ASX baseload prices, we found that some of the accepted offers were lower than the adjusted ASX prices, while some were still higher. We note in appendix A that we have not included some risk premia that we think would be added in a competitive market (due to estimation complexities). Therefore, these ratios would be even lower if we included more risk premia (para 6.9 Ch 5)