

Energy Competition Task Force

Level Playing Field Measures Q&A

1. What exactly is being proposed?

We are proposing a progressive approach to non-discrimination obligations supported by increased monitoring of gentailers' responses and consumer outcomes. If the first step proves insufficient, the Electricity Authority could then escalate to more prescriptive ways of levelling the playing field to ensure all New Zealanders can benefit from critical flexible generation.

The three proposed steps are:

Step 1: Principles-based non-discrimination requirements.

Step 2: Non-discrimination requirements set out in detail.

Step 3: All gentailer-supplied hedge contracts must be traded through a regulated market, on equal terms for all buyers.

The options paper also reconsiders the potential role of another Task Force initiative – virtual disaggregation. The Authority is also interested in hearing from stakeholders about this option.

2. Why does the Task Force want to level the playing field?

More competition in generation and retail will expand electricity supply and push prices down. We cannot achieve that outcome if the owners of flexible generation (who are also retailers) can tilt the playing field in favour of their own retail divisions. Competition will be stronger if rivals of the gentailers get a fair chance to compete on a level playing field.

3. What will the impact on consumers be?

Consumers would benefit from increased competition in the retail electricity market, and an increased supply of wholesale electricity. More electricity supply and more competition will lead to consumers having more choices and downward pressure on power prices over the longer term.

4. How long before we see these benefits?

The first step of the changes we are proposing could be in place this year (subject to feedback). We expect that independent generators and retailers would take immediate confidence from such a change. We expect that confidence to flow through to innovation in the marketplace.

5. Why are you doing this now?

This proposal follows reviews the Authority undertook in 2024 in response to increasing wholesale market volatility, increasing intermittent generation and competition concerns raised by independent retailers. Our reviews identified competition concerns and today's announcement responds to those concerns.

6. What is flexible generation?

Flexible generation is electricity generation that can quickly ramp up or down production on demand, enabling it to respond to changing needs for power at any given time. Examples include hydro and thermal (eg, gas) fuelled power. Battery storage systems are also flexible. Flexible generation helps to manage fluctuations in electricity supply due to variable renewable sources like wind and solar or sudden increases in demand.

7. What is an electricity hedge contract?

A hedge contract allows a party to reduce exposure to risk in a market, in this case to volatile electricity spot prices. To do this, the buyer and seller enter into a contract that guarantees them electricity at a certain price, instead of the spot price, during a future period. For example, an independent retailer or large industrial electricity consumer might buy a hedge contract from a generator.

8. Why do hedge contracts matter?

Hedge contracts matter because they support the financial viability of new independent retailers and generators in the electricity sector. For retailers, hedges provide insurance against very high spot prices. For new generators, hedges better enable them to enter into power purchase agreements (PPAs) with large users, which secures them a long-term revenue stream, opening up access to construction finance for new electricity generation projects.

Hedges are critical to enabling competition, which will get more power into the system, provide more choice to consumers and put downward pressure on electricity prices. The gentailers control the flexible generation that backs these hedges.

9. Who are the ‘independent’ electricity generators and retailers?

The independent, or non-integrated, retailers and generators focus on operating in one part of the electricity market, eg, they are primarily retailers, or primarily generators. An example is Flick Electric, which is focused on the retail market.

10. Why propose non-discrimination obligations?

We looked at other level playing measures and our current view is that non-discrimination obligations, combined with the new standardised flexibility product that started trading last month, are the most appropriate response to the competition risks we are observing.

Non-discrimination obligations can substantially level the playing field between the gentailers and independent generators and retailers in a matter of months rather than years.

They promote a level playing field by giving independent retailers and generators access to key products (hedge contracts) on substantially the same terms as gentailers supply themselves internally while maintaining investment incentives and security of supply.

11. What's the problem that you're trying to fix?

We want to improve competition in the electricity market. We believe this will provide better outcomes for consumers and market participants alike. Limited competition may be arising from gentailers both owning and accessing the vast majority of flexible power generation – such as hydro and thermal (eg, gas fuelled) - that is a key input into the supply of electricity hedges. This means the gentailers can influence the cost and supply of hedges to the independent generators and retailers who need them.

A lack of liquidity, high pricing and a lack of transparency for a key type of hedge contract (backed by that flexible generation) are three key indicators that the combination of gentailer vertical integration and their control of flexible generation may be hindering competition and investment in new electricity generation

12. How will non-discrimination obligations work?

Step 1: Introduce principles-based requirements that mean the gentailers would no longer be able to price in a way that favours their own retail arms or refuse to supply new hedges to independent retailers because supply is tight (while still supplying new hedges to their own retail arms). But in some cases, there would likely be more than one valid way that gentailers could comply.

Step 2: The Authority would impose more restrictive requirements, that prescribe non-discrimination requirements for gentailers in greater detail, for example the approach by which gentailers must determine their internal transfer prices.

Step 3: This would require the gentailers and others to trade all hedges through a regulated market in a manner prescribed by the Authority. There would be no more internal trading by the gentailers.

13. What are the escalation points?

Step 1 to 2:

Regulating the standardised flexibility product: low offer or trading volumes

Introducing more detailed non-discrimination requirements: even-handed treatment not demonstrated by evidence (non-compliance with non-discrimination principles, eg, internal transfer prices are not the same as external prices offered, and there is no efficiency-based reason for the difference).

Step 2 to 3:

Evidence that the existing non-discrimination obligations are failing in eliminating discrimination.

14. Why not do structural separation?

Structural separation would require gentailers' retail and generation arms to be fully separated into different companies, with different ownership.

Primary legislation would be required to implement structural separation. It would also take substantially longer to implement, and be more disruptive to critical investment and development, than our proposed non-discrimination remedy. This is discussed in more detail on page 45 of the options paper.

15. What are the benefits of a graduated change?

Because it's the quickest way to deliver the benefits to consumers:

It starts the change process faster – principles-based non-discrimination is the quickest level playing field option to implement (it could be in place this year, depending on feedback)

It gives gentailers an opportunity to embrace the change and make it work, while providing for a timely escalation pathway if they choose not to

It would improve the potential future implementation of mandatory trading of gentailer hedges (the most severe intervention) – by allowing time to gather further data and to design the intervention more effectively.

Overall, it best balances promoting competition (through increased hedge market liquidity and addressing discrimination concerns) with the risks to consumers and the economy that come with direct market intervention.

16. What is the evidence that there's a risk to competition?

The Authority's risk management review last year identified concerns about competition risks over the pricing and availability of certain hedge contracts, specifically those that cover 'super peak' periods – mornings and evenings when consumer demand is highest.

Despite having access to relevant information, those who disagreed with our competition concerns in their feedback did not present any specific evidence to support their views.

We expect the proposed level playing field measures if implemented, together with the new standardised flexibility product, would have a material, positive impact on retailers' and generators' ability to fairly access hedge contracts, particularly for morning and evening periods when consumer demand is highest.

17. How will the proposal increase competition?

Ensuring hedge contracts are traded on even-handed terms promotes competition by creating a level playing field for generators and retailers to compete in. Our proposal requires gentailers to offer independent retailers and generators access to products (such as hedge contracts) on substantially the same terms as gentailers give to their internal retail arms, while maintaining investment incentives and security of supply. This means that gentailers would not be able to favour themselves by, for example, giving their retail arms access to flexible generation/hedge contracts on better terms than they offer to third parties.

18. Will the proposal increase retail prices in the short term?

If the proposal is implemented, our current view is that it will ultimately put downwards pressure on retail prices. We can't predict short-term gentailer reactions, but in our view the proposal does not justify them increasing prices. In the short term there are a number of factors that could drive retail price changes, including the Commerce Commission's decisions last year about Transpower's and local electricity distributors' revenue limits, which will flow through to consumer prices on 1 April 2025.

19. How will you mandate the proposed non-discrimination obligations?

If the proposals are implemented this will be done by amending the Electricity Industry Participation Code which market participants must abide by. The maximum penalty for a breach of the Code is \$2m.

20. How long will it take for the Code amendment to be in place?

The length of time to develop a Code amendment is dependent on the feedback we receive. If, following review of feedback, the Authority decides to progress this proposal to introduce principles-based non-discrimination obligations the Code amendment would be in place this year.

21. What are you doing about internal transfer prices?

Concerns have been raised about gentailers using their generation profits to cross-subsidise their retail businesses, making it harder for independent retailers to compete.

The proposal addresses those concerns by putting requirements in place regarding the gentailers internal transfer prices (ITPs) – what gentailers “charge” their own retail arms for electricity. Step 1 of the proposal includes a principle that requires gentailers to establish economically meaningful ITPs.

It will provide the Authority and the sector with more useful data to assess whether any discrimination is occurring.

22. What are you doing about virtual disaggregation as proposed by the Market Development Advisory Group?

We are still considering virtual disaggregation. However, our thinking, and the evidence and circumstances we are responding to, has developed since August. We still conceptually agree with the Market Development Advisory Group’s 2023 framework that led to a very targeted virtual disaggregation approach, but our proposal is not the standalone option put forward by MDAG.

Instead, our proposed approach to implementing non-discrimination obligations seeks to address both the issue that underlies MDAG’s recommendation and broader level playing field concerns. We expect this coherent approach will ultimately deliver greater value for consumers.

Key elements of virtual disaggregation remain in the Authority’s progressive approach, particularly in Mandatory Trading of Genterailer Hedges (Step 3).

Virtual disaggregation remains a potentially powerful tool and we welcome stakeholder feedback and suggestions further on it.