

MINUTES

Meeting number: 2

Venue: Electricity Authority, Meeting Room 1, Level 7, ASB Bank Tower, 2 Hunter Street, Wellington

Time and date: 9:30am to 5:05pm, Thursday, 8 February 2018

Attendees

- James Moulder (Chair)
- James Flannery
- James Flexman
- Darren Gilchrist [items 1, 2 and 3]
- Rebecca Osborne
- Bruce Rogers
- Matt Rowe
- James Tipping

Apologies

- Stu Innes

In attendance

- Tim Street (Manager Wholesale Markets, Electricity Authority)
- Alistair Dixon (Principal Adviser Market Design, Electricity Authority)
- Elly Kappatos (Personal Assistant to Market Design, Electricity Authority)

- John Stephenson (Partner, Sense Partners) [item 2]
- Jean-Pierre de Raad (Partner, Sense Partners) [item 2]

The meeting opened at 9:29am

1 Meeting Administration

1A Apologies

Apologies were received from Stu Innes.

1B Interests register

The Chair:

- tabled the MDAG interests register
- asked the members if they needed to update their disclosures of interest
- noted some members disclosed additional interests and/or updated existing interests
- reviewed the interests disclosed/updated, and gave all group members permission to act.

1C Minutes of previous meetings

The Chair tabled minutes of the previous meeting on Tuesday 28 November 2017, confirmed by the group over email, for the record.

The group noted a member's email addressing timeframes for progressing the *Saves and win-backs* project.

The group decided the minutes should not include a summary of the projects the MDAG chose not to recommend to add to its work plan. The secretariat noted members will have the opportunity to suggest projects for the Authority's 2018/19 work programme and the MDAG's 2018/19 work plan.

James Flexman proposed re-confirmation of the minutes, which Matt Rowe seconded.

1D Matters arising

There were no matters arising.

1E Action list

The Chair noted all actions from the previous meeting were completed.

1F Correspondence

The Chair tabled correspondence sent and received for the group to note, namely:

- three letters from the Authority's Chief Executive to the MDAG Chair:
 - requesting the MDAG add the *Review of spot market trading conduct provisions* project to its work plan
 - requesting the MDAG add the *Saves and win-backs* project to its work plan
 - inviting the MDAG to lunch with the Authority Board on 3 May 2018
- a letter from the MDAG Chair to the Authority's Chief Executive, agreeing to the work plan requests.

The Chair confirmed he would continue to progress any MDAG correspondence with the secretariat unless he wished to consult first with members.

1G MDAG meeting dates calendar

The MDAG noted the calendar setting out its agreed meeting dates, and the Chair noted upcoming apologies from members.

1H Operating procedures

The Chair tabled the operating procedures agreed at the previous meeting for the record.

1I Observer from the system operator

The group discussed and agreed to invite an observer from the system operator to attend MDAG meetings where relevant. The Chair noted he would remind the system operator that any observer would not be an MDAG member, but would be encouraged to participate in group discussions.

The Chair indicated he would draft an invitation letter.

- | **Action – 2.1:** Chair to send a letter to the system operator, inviting them to nominate an observer to attend MDAG meetings by **next MDAG meeting**

3 Review of spot market trading conduct provisions

The Chair moved this item forward on the agenda ahead of its scheduled order

The secretariat presented the context of the review, and outlined various hypothetical scenarios for later discussion by the MDAG.

The MDAG decided to halt its discussion at this point and continue this agenda item later

2 Saves and win-backs

The secretariat briefly explained the landing ground between the *Saves and win-backs* project's two fundamental questions:

- Are retailers just winning customers?
- Or is competition being undermined at any stage within the realm of saves versus win-backs?

The secretariat then asked the group to consider:

- concerns regarding informational advantage for incumbents, and whether this could discourage market entry and therefore undermine competition
- whether informational advantage was considered to be an acquired asset, and whether this could promote innovation
- both the immediate and longer-term financial benefits of retailer actions.

The MDAG began by noting:

- differential pricing and “cherry picking” are characteristics of competition in other industries
- on-boarding costs and their impact on small retailers
- loss-leading customers, the use of private information by retailers to target particular customers, and whether engaged versus passive consumers are a wider social, rather than an industry, issue

- retailers had their own individual strategies regarding the customer acquisition costs they are prepared to incur.

Members discussed the approach to saves and win-backs in the telecommunications industry, and noted that in electricity retailing:

- there are generally no required notice periods for switching (unlike in telecommunications)
- the reason losing retailers are still allowed to contact any customers under contract is to avoid poor outcomes for those consumers.

The group then discussed:

- the implications of targeting educated consumers (the main switchers) and whether the short-term wins for retailers from acquiring these consumers could be maintained on an ongoing basis
- while some consumers may benefit in the short-term from acquisition activity such as saves and win-backs, there is potential for them to suffer in the long-term if this reduces competition; this in turn could affect the sustainability of the market and have adverse effects on equity
- the different situations of vertically integrated gentailers compared with small retailers
- the difficulty retailers faced in billing customers they served for only a short period of time eg, five days
- whether there would be benefit in a 30-day moratorium on win-backs
- the unique nature of transfer requests in electricity, where a retailer received a warning or notice of a customer switching
- that a retailer with a switching strategy could have higher acquisition costs than a retailer with a holding strategy, so by necessity new entrant retailers must have a switching strategy
- whether it is unfair that incumbent retailers have the ability to win-back customers they have lost to competitors
- correspondence to the Authority following its 2014 consultation on the saves protection scheme, particularly whether interested parties now hold differing positions.

The MDAG agreed it would be beneficial to invite some interested parties, particularly small retailers who had recently written to the Authority, to present their perspective on saves and win-backs at the next MDAG meeting in the format of a round table discussion.

The group also asked the secretariat to:

- investigate survey material, particularly of consumers, by the Authority or other parties in relation to saves and win-backs
- provide the group with any non-confidential correspondence the Authority received on saves and win-backs.

| **Action – 2.2:** Secretariat to invite small retailers to 15 March MDAG meeting by next MDAG meeting

| **Action – 2.3:** Secretariat to investigate survey material, particularly of consumers, by the Authority or other parties by next MDAG meeting

Action – 2.4: Secretariat to provide non-confidential correspondence on saves and win-backs by next MDAG meeting

The MDAG then emphasised the importance of ensuring that the saves and win-backs issues paper incorporated a consumer perspective. In particular, the group discussed:

- the notion of very high tariffs for disengaged consumers
- the extent to which retailers conduct value analysis, specifically competitive activity not shown through switching
- consumer perceptions about the value provided by particular retailer innovations
- whether raising competition would actually decrease prices, especially for the marginal consumer
- the Office of Gas and Electricity Markets (OFGEM) papers regarding electricity retailing competition in the United Kingdom
- negative consequences in standardising tariffs
- the ability of a consumer to distinguish between a save and a win-back
- whether there could be an effective switch withdrawal process, demarcated by an ‘error correction’ as opposed to a reversal; however, members agreed this was an undesirable option as it would sanction aggressive win-back targeting
- inviting a Consumer New Zealand representative to attend the April 2018 MDAG meeting.

The secretariat indicated it would prepare a draft issues paper, incorporating member discussion at this meeting, for the MDAG to consider at its next meeting.

Action – 2.5: Secretariat to prepare draft *Saves and win-backs* issues paper by next MDAG meeting

3 Review of spot market trading conduct provisions

The group resumed its discussion of this agenda item

The group began discussing the hypothetical scenarios presented earlier by the secretariat.

1. Raising an offer price to avoid a constraint price difference

The MDAG discussed:

- the implications of a volatile HVDC flow, specifically where a generator has inadequate risk management strategies
- the use of transitory market power to manage constraints, whether this ability constituted a “property right”, and whether there should be limits on this behaviour
- how time was a critical yardstick, ie, while 24 hours is a perfectly adequate notice period to adjust, two hours is questionable
- where prudent risk management includes any spot market exposure, and when it becomes too late to hedge
- mitigating loss by forcing others into loss

- a party deciding to stop offering hedges in the North Island, and the resulting fundamental change in the party's management of transmission risks
- whether there should be a change to gate closure
- whether parties should be required to buy FTRs to manage locational price risk; however, members noted questions regarding the liquidity and availability of FTRs.

2. Raising an offer price to deal with expected fuel scarcity

The group discussed:

- conduct at times of pivotal scarcity and future scarcity
- whether the safe harbour provisions addressed the issues arising in this scenario
- the "time after" principle of first becoming aware of a risk in pricing for an enduring event.

3. Using engineering co-efficients to affect offer

The MDAG discussed:

- whether it would be acceptable to ramp down at a rate other than capability
- whether it is possible to solve for the ramp rate, specifically whether there are engineering factors at play, or whether ramp rate is more or less fixed at physical capacity
- that offerors' preferences should change in the offer to account for price and quantity

4. Use of reserve coefficients to affect offer

The group noted:

- sometimes plant was offered when it was not physically available
- the "inverted bathtub", illustrated on slide 13 of the presentation, and whether there could be a reason to alter an offer for any reason other than a physical one
- the issue around pricing quantities as opposed to more indirect means of signalling restrictions on plant availability.

5. Unsignalled withdrawal of capacity without physical reason

The MDAG discussed:

- whether there is a third state between having plant available and not being available (and recorded as such in POCP), ie, when plant is not offered, but not on outage
- POCP technical update times
- whether all capacity should be offered, inherently creating the two-state world
- the idea of notification

Darren Gilchrist left the meeting at 2:56pm

- the interpretation of 'as soon as it can' in Part 13.5B(3)(b) of the Electricity Industry Participation Code 2010, translating into as soon as reasonably practicable
- the importance of both the return to service and the withdrawal of plant

- withdrawal of plant near gate closure, the reasoning which prompts such an event and the reduced demand
- the increasing significance of this issue in the future with residential battery aggregation.

The group also briefly discussed the other scenarios mentioned on slide 8 of the presentation, in particular considering:

- whether the withdrawal of small distributed generation and interruptible load both individually and across multiple plant reflected a high standard of trading conduct, noting this matter required careful consideration
- comments from members that there may be an issue about whether interruptible load and dispatchable demand offered was in practice available.

The MDAG concluded by discussing the issue of constrained-on payments, specifically whether behaviour seeking to maximise these payments was covered by the trading conduct provisions.

The Chair then asked members to talk to parties in other industries about trading conduct in different contexts, including any other scenarios of potential relevance.

| **Action – 2.6:** MDAG members to discuss the concept of trading conduct with parties outside the electricity industry, including any other scenarios of potential relevance by next MDAG meeting

The group agreed to:

- target presenting the discussion paper to the Board in November / December 2018
- bring forward the milestone for presentation of the recommendations paper to the Board from December 2019 to September 2019
- invite Toby Stevenson from Sapere Research Group, consulting for Meridian Energy, to present to an upcoming MDAG meeting to provide views on a range of scenarios
- invite Phill Anderson, Genesis Energy and Meridian Energy to present at an upcoming MDAG meeting.

| **Action – 2.7:** Secretariat to invite Phill Anderson, Genesis Energy and Meridian Energy (including Toby Stevenson) to present at upcoming MDAG meetings by next MDAG meeting

The Chair also asked the secretariat to enquire about whether Sapere's upcoming paper on trading conduct could be provided to the MDAG.

| **Action – 2.8:** Secretariat to enquire about whether the Sapere paper on trading conduct could be provided to the MDAG by the next MDAG meeting

4 Publication of meeting papers

The group confirmed the meeting papers could be published on the Authority's website once the secretariat updated the papers to account for minor formatting changes agreed by members.

The meeting ended at 3:45pm

I, James Moulder (MDAG Chair), certify that the minutes recorded disclose all issues discussed at the meeting (date at the top), are recorded truthfully and without bias.

Signature:



Date: Friday 23 March 2018 (23.03.2018)