6 December 2018

James Stevenson-Wallace
Chief Executive
Electricity Authority
By e-mail: submissions@ea.govt.nz

Dear James,

Joint submission from independent retailers – indicative work programme for 2019/20

Electric Kiwi, Flick Electric, Pulse Energy and Switch Utilities (Vocus) appreciate the opportunity to submit on the indicative work programme for 2019/20.

We share common ground on what is needed to fix the electricity market and deliver better outcomes for consumers. There are two primary elements of the work programme we would like prioritised:

- the need for action on distribution pricing reform; and
- addressing retail market problems caused by the large, vertically-integrated, incumbent retailers.

Our views on the work programme mirror our joint submission to the Electricity Price Review.[1,2]

Summary of our concerns and key recommendations

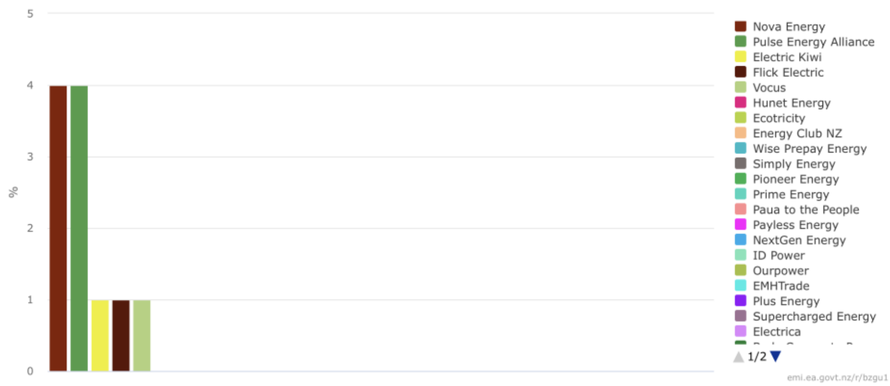
- We are concerned the indicative work programme won't help the Electricity Authority meet its commitment to deliver projects faster and set "more ambitious targets for our top priority projects, with associated changes to budget and resource allocations per project".[3]
- The proposed KPIs allow projects to continue to take too long to progress and complete.
- It should not have taken 7-years to produce the last two consultation papers on distribution pricing. This is far too long. The Electricity Authority is expecting electricity distributors to move faster on distribution pricing than it has been capable of itself, and is yet to confirm the pricing principles which should be applied.
- We **recommend** the Electricity Authority set, and then ensure compliance with, a fixed deadline for distribution pricing reform.
- Each of the proposed KPIs for the two-tier retail market (saves and winbacks), hedge market development, and spot market trading conduct projects should be met within the current financial year, not by the end of 2019/20. We would welcome consultation on the hedge market and spot market trading early (first quarter) in 2019.
- We **recommend** the Electricity Authority fast-track the two-tier retail market (saves and winbacks), hedge market development, and spot market trading conduct projects.
- We **recommend** the Electricity Authority expand the KPIs for each of its projects to include major project milestones, such as each consultation step, and target completion dates.

[1] https://www.mbie.govt.nz/info-services/sectors-industries/energy/electricity-price-review/submissions/submissions-received-epr/electric-kiwi-flick-electric-pulse-energy-and-vocus-submission-electricity-price-review.pdf
[2] We have included our recommendations to the Electricity Price Review in the Appendix to this submission as many of the recommendations are within the purview of the Electricity Authority.
[3] https://www.ea.govt.nz/dmsdocument/23836-market-brief-24-july-2018#mctoc1

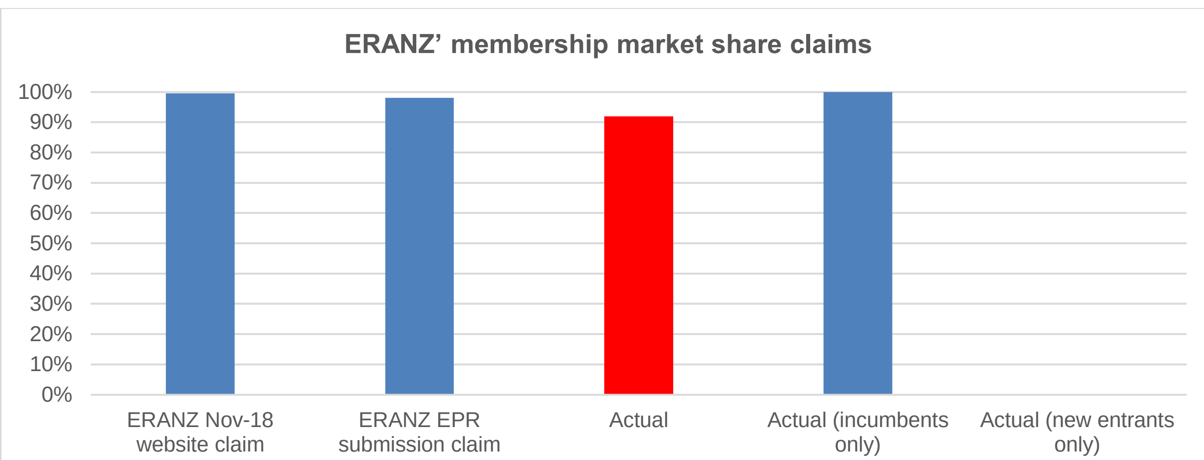
We are the four largest retailers outside of the incumbents

Collectively, Electric Kiwi, Flick Electric, Pulse Energy and Vocus represent nearly 150,000 retail customers (6.93% market share). This corresponds to 58% of the electricity retail market outside the 5 largest incumbents, or 85% of the market supplied by entrant (independent) retailers only.[4]

The following diagram shows the market shares of retailers other than the 5 largest incumbents, as at 31 October 2018.[5]



We note this contradicts ERANZ' claims about the market share its membership represents. ERANZ has simultaneously and incorrectly claimed its membership represents 98% (Electricity Price Review submission) and 99.5% (ERANZ' website) of the retail market. Both are wrong. The actual share ERANZ represents is 91.89%.[6] ERANZ membership corresponds to the incumbent retailers' market share.



If ERANZ is successful in its purported role "to promote and enhance a sustainable and competitive retail electricity market that delivers value to New Zealand electricity customers" the market share of its membership will decline over-time.

[4] Nova and, previously. King Country Energy are small incumbent retailers.

[5] https://www.emi.ea.govt.nz/Retail/Reports/R_MSS_C?Percent=Y&seriesFilter=BCPL,TAOM,ECOS,ECOT,ELKI,ENEL,EMHT,CLUB,ETRN,FLCK,HNET,IDPL,KEAE,LITE,NEXG,SKOG,TODD,ORSL,OURP,GIVE,PLEL,PION,PLUS,ORBS,PRME,PUNZ,SIMP,STAK,SUPE,SWCH,WISE,YESP&_si=tg|market-structure,v|3

[6] The inaccuracy of ERANZ' claims were first pointed out in comment on the Energy News article "New ERANZ chief executive named" 25 September 2018. While Energy News corrected the market share figure, ERANZ has continued to persevere with its claims.

The Commerce Commission implementation of the new fibre regulatory framework provides useful benchmark

The Commerce Commission's proposals for implementing the new fibre regulatory framework, which includes establishment of fibre Input Methodologies, an Information Disclosure regime and price determinations for Chorus' fibre services[7] provide useful benchmark for project management and policy development.

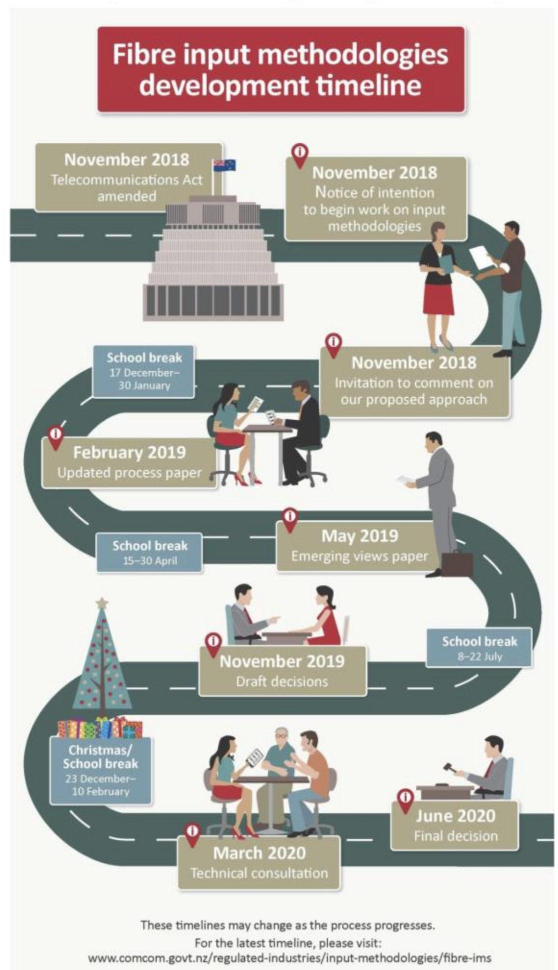
The Commerce Commission proposes to give itself 20 months to develop the Input Methodologies and, in parallel, two and half years for the first price determination (see Figure 4.1 below). The Electricity Authority typically takes much longer than this, sometimes to just produce a single consultation paper, even on much smaller projects.

The Commerce Commission has also clearly outlined the project milestones, including each consultation step and project completion date, needed for the successful development of fibre Input Methodologies (see figure 4.2 below).

Figure 4.1: Indicative timelines for implementing our new fibre regime

Note: Draft and final in this table refers to both determinations and reasons papers.

Figure 4.2: Timelines for implementing our new fibre regime



We **recommend** the Electricity Authority expand the KPIs for each of its projects to include major project milestones, such as each consultation step, and target completion dates.

[7] Commerce Commission, New regulatory framework for fibre Invitation to comment on our proposed approach, 9 November 2018.

The lack of progress on the spot market trading conduct highlights the problems with project inertia

The “Review of spot market trading conduct provisions” project is a good example of the problems with lack of progress on important projects.

The Electricity Authority determined Meridian had used its net pivotal position (market power) to raise spot prices, and breached the Electricity Industry Participation Code, on 2 June 2016.[8]

It wasn’t until November 2017 that the Electricity Authority Board requested the Market Development Advisory Group (MDAG) include a review of spot market trading conduct provisions in its workplan.[9]

The 30 June 2018 Work Programme for 1 July 2018 - June 2019” included the KPI “MDAG **publish** discussion paper, if any”. The Electricity Authority is now proposing to set a KPI to “**Initiate** development of consultation paper on MDAG recommendations” for 2019/20.

No commitment has been made as to when a first consultation paper will be published or what will happen afterwards. The proposed KPI would mean the first consultation isn’t required until over 30 months after the project was initiated, and over 4 years after the incident that gave rise to the project.

The Electricity Authority should be acting with greater urgency, particularly where it identifies abuses of market power, which raise prices and harm competition.

We want the Electricity Authority to “deliver … projects faster, so that the benefits for consumers are realised sooner”

It isn’t clear from the 2018/19 KPIs, or the proposed 2019/20 KPIs, that the Electricity Authority is “setting more ambitious targets for our top priority projects” e.g.:

- **Distribution pricing – Monitoring distributors’ adoption of more efficient prices:** The proposed KPI simply requires the Electricity Authority to “**Complete** first round of monitoring”. There is no commitment for when distribution pricing reform can be expected, despite the net benefits of this projecte purportedly being greater than $1 billion. If the Electricity Authority figures are correct, each year of delay is costing consumers over $50 million.[10]

  We **recommend** the Electricity Authority set, and then ensure compliance with, a fixed deadline for distribution pricing reform.

- **Two-tier retail market (saves and winbacks):** The KPI is to “If necessary, **amend** the Code” in 2019/20. There is no reason this project, if run efficiently, couldn’t be prioritised and completed within 2018/19.
- **Review of spot market trading conduct provisions:** The proposed KPI is to “**Initiate** development of consultation paper on MDAG recommendations”. All the Electricity Authority has to do to meet its Spot Market Trading Conduct KPI is start drafting a consultation paper in the next 20 months. This is too long and the KPI is too weak. There is no reason consultation couldn’t be undertaken in the current financial year.
- **Hedge market enhancements:** The KPI for this project is equally weak. All the Electricity Authority has to do is (internally) “**Evaluate** options to enhance hedge market”. The Electricity Authority wouldn’t even need to consult within 2019/20 to meet this KPI.

Each of the proposed KPIs for the two-tier retail market (saves and winbacks), hedge market development, and spot market trading conduct projects should be meet within the current financial year,

[8] Letter from Brent Layton (Chair, Electricity Authority) to Mark Binns (Chief Executive, Meridian), Meridian’s trading conduct on 2 June 2016, 8 May 2017.
[9] https://www.ea.govt.nz/dmsdocument/23078-letter-to-mdag-2017-18-work-plan-trading-conduct
[10] Assuming an interest rate of 7% and the NPV was calculated over a 20-year period.

not by the end of 2019/20. We would welcome consultation on the hedge market and spot market trading early (first quarter) in 2019.

We **recommend** the Electricity Authority fast-track the two-tier retail market (saves and winbacks), hedge market development, and spot market trading conduct projects.

Submissions to the Electricity Price Review send a clear message retail competition issues need to be addressed as a priority

We are heartened by stakeholder submissions to the Electricity Price Review.

There was a wide range of submissions on retail competition issues and the remedies that are needed. These submissions support our **recommendation** the Electricity Authority fast-track the two-tier retail market (saves and winbacks), hedge market development, and spot market trading conduct projects.

Some examples of stakeholder comments on retail competition problems include:[11]

- **Questions about whether price rises are justified** (Consumer NZ): "Both retail and distribution charges have contributed to the significant increase in power prices that consumers have experienced over the past decades. Despite flat demand in the past few years, there has been no reduction in domestic prices. … there has been insufficient scrutiny of price increases and whether they're justified.
- **Large industrial users facing similar issues to independent retailers** (Winston's Pulp): "… there are problems with some generators having short-term market power; and with the depth and liquidity of the hedge contract market. These issues directly impact on our ability to manage our electricity costs and the associated risks."
- **Retail competition isn't working well:** Paua to the People -"Competition is not working to deliver low prices for all households. In fact, prices remain high for many households and the market dominance of generator/retailers continues unabated despite the plethora of new entrant retailers." energyclubnz: - "energyclubnz believes that the NZ electricity market is on the verge of being 'broken' and is weighted in the favour of the Gentailers and not consumers."
- **The retail market isn't a level playing field** (ENA): "ENA suggests there are a number of factors which supports the view that new entrants to retailing don't face a level playing field. These barriers to entry contribute to slow growth in market share of new entrant retailers."
- **The retail market is concentrated** (Entrust): "Retail and generation remain oligopolistic and highly concentrated … 72% of regional electricity retail markets in New Zealand are concentrated, based on the Commerce Commission definition. … Applying UK tests, 74.3% of the regional electricity retail markets in New Zealand are highly concentrated, and 25.6% concentrated."
- **Vertical-integrated retail-generators' related party transactions lack transparency** (Ecotricity): "it should be noted that 90% of the customers are supplied by vertically integrated retailers, therefore internal transfer prices are masking the real margins gentailers are making or subsidized using their generation assets."
- **The hedge market is illiquid and poorly functioning** (Vector): "New Zealand stands out among international electricity markets as having some of the lowest levels of contract market liquidity and highest levels of vertical integration between generation and retail. … A poorly functioning hedge market creates a significant barrier to entry and expansion of independent retailers." (ENA): "… improving the depth and resilience of the contract market should be given higher priority."
- **There are problems with spot market trading conduct** (Ecotricity): "Generators are absolutely rigging the Spot market. … Similar to the generation sector, the retail sector is structured in favor of gentailers."

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[11] https://www.mbie.govt.nz/info-services/sectors-industries/energy/electricity-price-review/submissions

- **Spot trading conduct may not be up to Financial Markets Authority standards** (Axiom): "… the EA determined that it was acceptable for Meridian to engage in trading behaviour that, in effect, took advantage of its pivotal position to create a shortage in one location to cover its retail exposure in another. In our opinion, it is questionable whether such conduct would be permitted in, say, the context of a financial market. We note for example that, in a recent presentation to the EA's Market Development Advisory Group (MDAG), Mr Colin Magee of the Financial Markets Authority explained that: … 'Trading which created a shortage in one market in order to affect prices in another market would be considered to have an illegitimate purpose, as would trading to push a price up in one market being used to offset losses in another market.'"
- **The application of UTS provisions encourages abuse of market power in the spot market** (Axiom): "… the way the EA has historically interpreted and enforced the Undesirable Trading Situation (UTS) provisions risks exacerbating the problems associated with the exercise of short-term pricing power."
- **There is evidence of exercise of market power and anti-competitive conduct** (Waitaki Power Trust): "The exercise of market power to sharply raise prices on the wholesale spot market, by the five big generator/retailers, even in the short term when supply is tight, is distinctly anticompetitive, as are risky selling strategies associated with hedge priced contracts with large volumes of base load electricity attached, signed between the generator and industrial users such as Comalco and pulp and paper processors."
- **There is a two-tier retail market** (energyclubnz): "Loyal 'non-switching/disengaged' incumbent customers are being 'priced up' by their existing retailers which is driving up the overall savings available. This could result in pricing that is up to 20% higher than their current incumbent retailers best market details."
- **The size of the gap between the tiers is increasing** (Counties Power Consumer Trust): "As a consumer representative trust, CPCT is concerned about the size of retailers' margins and the upward trend in most of these (The Report's Figure 17). We believe that this should be a central focus of the next phase of the Review.
- **Potential for saves and winbacks to foreclose the market** (Commerce Commission): "A competition concern could arise where the use of win-back discounts result in customer foreclosure and raising rivals' costs - increasing the costs of customer acquisition and making it more difficult to achieve minimum efficient scale. This, in turn, means there is potentially less competitive pressure on incumbent retailers and higher prices in the future. In addition, discounts may be targeted at the high value customers, so that challenger retailers end up with disproportionately low value customers."

Submissions to the Electricity Price Review bolster support for our concerns about the two-tier retail market (saves and winbacks)

A number of stakeholders raised concerns about the saves and winbacks issue that had not engaged with the Electricity Authority/MDAG process, including the Commerce Commission, energyclubnz, ENA, Northpower, Top Energy, and Vector. For example, ENA has acknowledged "concerns that 'saves' and 'win-backs' are an impediment to full and effective retail competition and consumer switching", while Northpower and Top Energy advocate restricting winbacks for 60 days after a residential consumer switches retailer.

The stakeholder submissions included concerns, consistent with our own, about the dominance of large incumbent retailers on MDAG. Vector noted that "Although we welcome the EA's investigation of the impact of win-backs, we are concerned that on this and other issues, they are unduly influenced by the large incumbent players. We note that there are currently no independent retailers represented on the MDAG, which has been tasked with investigating win-backs". ENA made similar comments.

The Electricity Price Review submissions highlight the incumbent retailer defense of the two-tier retail market (saves and winbacks) is becoming increasingly isolated. The only submission supporting the incumbent retailers' views was from Sapare. While the Sapare report was submitted by Business NZ, it was funded by the gentailers (Sapare is one of Meridian's main consultants), and was not representative of members of the Business Energy Council.

Concluding remarks

We want to see distribution businesses adopt tariff reform which supports innovative retail tariff offerings and want a more competitive electricity market.

The Electricity Authority has acknowledged: “The competitive “fringe” is extremely important to discipline the larger incumbent players. … The impact of Uber on the taxi industry is a good example of how a new innovative competitor can materially impact on well-established business models”.[12]

It is independent retailers that are driving better competitive outcomes for consumers. If the retail market is fixed to ensure a level playing field there is no reason we should remain a “fringe”.

There is still a long way for the electricity market to transform from an oligopoly, dominated by 5-large incumbents, to a fully competitive market. Sorting out issues with the two-tier retail market (saves and winbacks), hedge market liquidity, and spot market trading conduct are important steps for enabling independent retailers to deliver better competitive outcomes (promotion of competition) for the long-term benefit of consumers.

Yours sincerely,

Luke Blincoe	Steve O’Connor	Gary Holden	Johnathan Eele
Chief Executive Electric Kiwi	Chief Executive Flick Electric	Chief Executive Pulse Energy	General Manager Commercial and Regulatory Vocus Group

[12] Electricity Authority, Electricity Authority Electricity Price Review submission, 19 October 2018, question 15.

Appendix: Recommended reforms for the electricity retail market submitted to the Electricity Price Review

	ISSUE	SOLUTIONS
Network pricing reform		
	Little progress has been made on distribution pricing reform	1. Require networks to offer time-of-use or peak/off peak pricing options. This would allow consumers that are price sensitive to shift discretionary consumption to lower priced periods. 2. Set and then ensure compliance with, a fixed deadline for distribution pricing reform.
Empowering consumers		
	Lack of consumer voice	3. Re-prioritise Electricity Authority funding for a 'Consumer Champion' who has a deep understanding of industry economics and can advocate for consumers and engage with consumer groups.
	It is difficult for consumers to access the benefits of the competitive market	4. Ensure all tariffs are advertised in a clear and transparent way – for example, inclusive of GST. 5. Enhance Powerswitch so it is less confusing and more accurate. It should be based on actual usage data and tariff information. This could be enabled by a centralised data model.
Wholesale market power		
	There is a high degree of market power in the wholesale electricity market, particularly in dry-years and when supply conditions are tight	6. Prevent further market concentration of generation. 7. Increase scrutiny of trading conduct in the spot, reserves and contract market. These markets require more stringent and more timely oversight and enforcement to retain (or regain?) confidence in the market. It may be appropriate for the Commerce Commission to take on this responsibility. See also the recommendations below on vertical-separation.
Retail market competition		
	There is a two-tier retail market, which results in 'loyal' consumers missing out on the benefits of retail competition and in fact, subsidising those who switch	8. Prohibit saves and winbacks, and the use of consumer data once customers have decided to leave. Currently this provides an opportunity for price discrimination and inhibits competition. By way of contrast, in the telecommunications market where outgoing retailers do not engage in save or winback activity has meant above the line price competition,

	ISSUE	SOLUTIONS
		proactive retention based on price, and a socialising of the benefits of competition. The Expert Advisory Panel should not rely on the Electricity Authority to resolve the two-tier retail market/saves and winbacks issue.
	The quality of retail competition varies across New Zealand	9. Investigate the extent to which barriers to competition are causing regional variation in the level of retail competition across New Zealand. 10. Prohibit the TECT tying dividend entitlement to being a Trustpower customer/replace with entitlement based on geographic location. See also the recommendations below on smart metering and data access.
Vertical-integration		
	Vertically-integrated incumbent retailers have incentives and ability to restrict competition in down-stream (retail) markets	11. Full vertical separation of wholesale and retail services. If full vertical separation is not adopted, then as a minimum corporate separation with arm's length rules and financial disclosure requirements should be adopted. This should include (non-discrimination) equal wholesale access obligations.
Access to data		
	Data access is a key enabler of competition	12. Adopt a centralised data model and market reconciliation similar to the NEM in Australia. This would be a centralised source of data for Network Companies and Retailers and would eliminate the need for market and network reconciliation. 13. Ensure the smart meter roll- out reaches all consumers. 14. Address issues with Meter Equipment Provider performance and data quality: We recommend standardised metering contracts be introduced. These standardised contracts should: a. Facilitate economic displacement in the best interests of end-consumers; b. Include minimum service delivery levels for both legacy and smart meter data with clawbacks for non-delivery; and c. Be subject to regular review to ensure relevance as new technology and business models emerge and the metering landscape changes.

	ISSUE	SOLUTIONS
Assisting low-income and vulnerable consumers		
	The electricity market could do better at delivering affordable outcomes for beneficiaries and low-income households	15. HNZ/MSD could utilise their scale and bargaining power, by running tender(s) for supply of beneficiaries and low-income consumers.
	"Prompt Payment Discounts" are misleading and hide excessive late payment fees	16. Mandate 'Prompt payment discounts' are called what they are - late payment fees. 17. Adopt the ACCC recommendation to require late payment fees are reflective of the cost of credit and not punitive.