2 December 2019

Mary Ann Mitchell
By email
[redacted]

Dear Mary Ann

RE: Follow-up on discussion at 14 November Board meeting

I would like to thank Flick and the other non-integrated retailers (Ecotricity, Vocus, Electric Kiwi, EnergyClubNZ and Pulse Energy) (the non-integrated retailers) for taking the time to engage with the Authority's Board and staff over the past several weeks. I refer in particular to the meeting and presentation to members of my executive team on 8 November, your meeting and presentation to the Authority's Board on 14 November, and your letter dated 15 November.

Independent retailers are a critical part of a well-functioning market, and your ongoing constructive and proactive engagement with the Authority is welcome and helpful.

Ongoing engagement is critical, as I note that the issues you most recently raised and interventions you proposed had evolved in some respects from those presented to the EPR panel. Ongoing and open discussion is an important way the Authority can continue to understand all participants' perspectives as it strives to promote the long-term benefit of electricity consumers.

The Authority has met with the four largest generator retailers and expects progress this calendar year

After meeting with you, the Authority Board met with each of the current market makers individually and, among other things, indicated to them the immediate changes to market making services the Authority seeks. The changes the Board are seeking reflect the kinds of measures the non-integrated retailers indicated are needed to ensure an immediate improvement to market confidence. In particular, the Authority Board is expecting the four largest generator-retailers to implement the following changes to market making services:

- bid-ask spreads are reduced to no higher than 3%;
- offered volume of contracts is raised to 3MW across all contracts with market making.

The letter from the Authority outlining these expectations is available on our website. For these changes to be fully effective however, they will need active participation in hedge markets from all segments of the wholesale electricity market. As your various submissions underline, there is a very large public good element in the provision of a robust and transparent forward electricity price curve. All participants benefit from this and it is best achieved by commited involvement by all parties in price formation. No participants should expect to be able to rely totally on others. The information each participant contributes to the market through its participation contributes to the robustness of the outcome. The Authority will be monitoring activity to see whether its interventions are being actively used in the market to manage risk and is seeking better information from participants to achieve this.

As a first step, the Authority is seeking de-anonymised trading data from the four largest generator-retailers. This will allow the Authority to track market maker performance directly, with a view to regular reporting of their performance. Such data will provide us with better information to test and analyse some of the claims made about the market's performance, and will enable the Authority to identify who is placing bids, and at what volumes, into the market. This will allow us to gain a better understanding of the behaviour of all participants – including non-integrated retailers – beyond just their actual trades. I note the Authority considers passively observing the market is not a strong position from which to suggest improvements to it.

As you will see in the letter to the generator-retailers, the Authority is working to develop a standard means of reporting this information on transfer pricing and profit by segment.

The Authority has a long history of designing the market to support new entrant retailers

The independent retailers' letter dated 15 November states a '*general dissatisfaction with the demonstrable lack of recognition pure retailers get from the Authority in [your] role in this market*'.

I would like to take this opportunity to point out the succession of developments the Authority has introduced to enable the development of competition and accessibility of business opportunities for independent and new entrant retailers, as well as independent generators. Examples include:

- Hedge market development – developing the market as a key financial risk management tool for non-integrated electricity industry participants, including developments relevant to both ASX and over-the-counter markets.
- What's My Number Campaign – introducing and developing the campaign which specifically delivers benefits to new retailers and is active in encouraging consumers to shop around and be open to new firms offering services.
- Switching and registry management – introducing efficiencies.
- Retailer default programme – these arrangements are largely for the benefit of independent retailers. Established generator retailers face the substantive risk in the event of defaulting new entrants.
- Prudential reform – the current settings, which impose significantly lower financial requirements than the Authority inherited, strike a balance between certainty for new entrants and exposure to market conditions.
- Official Conservation Campaigns – the Code contains allowances specific to the interests of non-integrated retailers. For example, they can negotiate alternative conditions with customers and spot exposed customers bear the risk of OCCs, not their retailer.

These are just some of the market initiatives the Authority has undertaken to improve the market settings in a way that encourages new entrants and independent retailers and generators. In addition to these sorts of active measures, the Authority also avoids changes that would act against greater diversity of participants in the market. For instance, the Authority has avoided introducing specific mechanisms, which are standard in other jurisdictions, such as a licencing regime, setting minimum capitalisation rules, imposing retail tariff conditions or having a fit and proper person test on participants dealing with the public.

The Authority has taken these decisions due to its position that such mechanisms are associated with reduced sector innovation and have a tendency to reward or advantage incumbents and major players. Such a move runs counter to the Authority's commitment to a market that provides efficient prices through competition for the long-term benefits of consumers.

I acknowledge other correspondence received

The core of our recent discussions have dealt with the issues noted above – namely market making and your new requests to urgently intervene in the market. I also want to take the time to note other correspondence received from non-integrated retailers recently:

- A letter from Luke Blincoe dated 10 October *Electric Kiwi urges winback ban before Christmas*
- A letter from non-integrated retailers dated 10 October *Re: Request for urgent Code amendment to mandate market making on the ASX*
- A letter from non-integrated retailers dated 30 October *Re: regulatory priorities*
- A letter from non-integrated retailers dated 30 October *Re: Win-backs*.

Those letters make various requests to reprioritise the Authority's work programme. Regarding the existing priorities in our work programme I note that receipt of the Government's response to the EPR Panel's recommendations is inevitably causing the Authority to re-prioritise its work programme. Some of that will already be evident from releases by the Authority over the last few weeks (the hedge market enhancements discussion paper, the saves and win-backs proposal, and the ACCES project quick wins consultation). The Authority expects to release a comprehensive view of its priorities for the remainder of the 2019/20 financial year after our Board meets on 18 December.

In response to some of the specific requests in your letters, I note that the Authority:

- is currently consulting on the saves and win-backs Code amendments. Whether we can make a decision by Christmas depends on the nature and volume of submissions we receive by 3 December – the deadline for submissions;
- does not agree with putting the TPM project on hold for the reasons set out in our 2019 issues paper. After receiving submissions on that paper we remain of the view that:
  - the case for changing the TPM is very clear
  - there is a need to conclude the debate: the risks to consumers and other market participants increase the longer the debate goes on
  - we are confident that changing the TPM guidelines will result in significant benefits to consumers, given the inefficient incentives for consumption and investment created by the current RCPD charge
- understands your view that further disclosure and analysis of generator-retailer transfer pricing and retail profitability is important and urgent.

Next steps

The Authority expects material progress to be made in respect of both market making services and generator-retailers and non-integrated retailers this calendar year. The Authority's Board is meeting on 18 December and will consider against the public benefit test whether to make urgent code amendment that will impose mandatory conditions on existing market makers should they fail to implement or maintain new services, including a 3% spread and an increase to 3MW of volume each across all contracts with market making.

The Authority considers these measures will improve market conditions, and with the involvement of all participants, act to improve depth and liquidity in the exchange-traded hedge markets. They will also complement the consultation on hedge market arrangements the Authority current has underway to determine what, if any, longer term changes would be in the long term interests of consumers. Urgent Code amendments last only 9 months allowing the Authority to take action when it is in the public interest for it to do so, while it considers longer-term options.

Copies of our recent correspondence will be published on the Authority's website. I want to thank all of the non-integrated retailers again for engaging with the Authority on these important matters.

Yours sincerely

James Stevenson-Wallace
Chief Executive

cc: Al Yates, Ecotricity
Luke Blincoe, Electric Kiwi
David Goadby, energyclubnz
Steve O'Connor, Flick Electric
Gary Holden, Pulse Energy
Emily Acland, Vocus Group
Dr Megan Woods, Minister of Energy and Resources
Gareth Wilson, Principal Advisor MBIE