22 December 2021

James Stevenson-Wallace
Chief Executive
Electricity Authority
By email to reviewconsultation2021@ea.govt.nz

Dear James

Consultation Paper: Inefficient price discrimination in the wholesale market – Issues and options

1. This is a submission from the Major Electricity Users' Group (MEUG) on the Electricity Authority (EA) discussion paper "Inefficient Price Discrimination in the Wholesale Electricity Market – Issues and Options, an initial response to the Wholesale Market Review" published 27th October 2021 along with related materials including expert reports and models.[1]
2. Attached and to be read as part of this submission is an independent report by Mike Hensen, Senior Economist NZIER, titled "Meridian Tiwai electricity contract – Comment on Electricity Authority market review" 22nd December 2021.
3. MEUG members have been consulted in the preparation of this submission. This submission is not confidential. Members may lodge separate submissions.

MEUG does not agree with the EA decision to initially focus on the purported inefficient price discrimination issue

4. MEUG has separately submitted on the EA information paper "Market Monitoring Review of Structure, Conduct and Performance in the Wholesale Electricity Market, since the Pohokura outage in 2018." That submission notes MEUG does not agree the review work to date justifies prioritising the initial issue of focus on the purported inefficient price discrimination. MEUG suggests the EA focus on the unexplained increase in spot prices of up to $38/MWh, in parallel to commence work on options to urgently address systemic market power if that is identified as a material component of the $38/MWh, and to progress how the new trading conduct rules will be implemented and monitored.

[1] Document https://www.ea.govt.nz/assets/dms-assets/29/Inefficient-Price-Discrimination-in-the-Wholesale-Electricity-Market-Issues-and-Options-Discussion-Paper.pdf at https://www.ea.govt.nz/monitoring/enquiries-reviews-and-investigations/2021/wholesale-market-competition-review-2/

NZIER Key Points on the Issues and Options paper

5. Below is a snapshot from the NZIER report of the Key points:

Key points

Problem definition needs clarification

The Electricity Authority (EA) has defined the potential for inefficient price discrimination by generators as a market outcome that it needs to prevent. However, it is not clear if the EA wants to prevent a replication of the Meridian Tiwai contract at the end of its current term or if it expects a proliferation of smaller inefficient price discrimination contracts.

The EA notes the Meridian Tiwai contract *has several relatively unique attributes, including the large size of the supply and its impact on prices, such that all generators' revenues are expected to increase from the contract*. This suggests a proliferation of smaller inefficient price discrimination contracts is unlikely.

EA is equivocal about the efficiency of the Meridian Tiwai pricing contract

The Electricity Authority (EA) has identified a contract between NZAS and Meridian for the supply of electricity over 2021 to 2024 as a potential example of inefficient price discrimination and noted that it was rational for Meridian to make this agreement because of the scale of Meridian's generation capacity compared to other generators nationally and in the South Island. The EA but does not explicitly either describe the agreement as inefficient an exercise of market power. This issue is analysed in detail by the EA in its initial response to the wholesale market review[1]. The EA presents two very different estimates of the materiality of the impact of the agreement:

- Additional costs to spot market purchasers of $1.6 billion to $2.6 billion over three years based on the movement in forward prices after the contract was announced.
- An efficiency cost to the New Zealand economy of $57 million to $117 million.

Proposed options for EA intervention are not consistently assessed

Five of the eight options proposed by the EA are administrative solutions - rule changes designed to prevent discriminatory pricing. The success of these measures relies on setting effective rules and efficient processes for monitoring and on the regulator being able to identify and prove they have identified a better combination of trades than the market. This is likely to be difficult for the task of deciding when discriminatory pricing reflects different product and service attributes as opposed to an attempt to subsidise some customers at the expense of others.

Two of the options are to improve competition in hedging markets but these require deep and active markets to be successful.

The EA has suggested a set of evaluation criteria for the proposed options, but the consultation questions focus on pros and cons and do not apply the evaluation criteria.

Yours sincerely

Ralph Matthes
Executive Director