1 July 2021

Antonia Horrocks
General Manager Competition
Commerce Commission
Wellington

James Stevenson-Wallace
Chief Executive Officer
Electricity Authority

Dear Antonia and James,

Unlocking electricity competition in Tauranga/western Bay of Plenty

Electric Kiwi welcomes Trustpower's move to vertically-separate its retail and generation businesses.

While the acquisition by Mercury, if approved, will reduce the number of competitors in the electricity retail market, and increase already high levels of market concentration, we consider the reduction in retail-generation vertical-integration will result in a more competitive electricity retail market in the longer-term.

However, we remain strongly of the view that the Tauranga Energy Consumer Trust (TECT) dividend arrangements (selective distribution only to Trustpower customers) remain a significant barrier to competition in Tauranga/western Bay of Plenty, and are anti-competitive. The changes TECT has indicated it will need to make to its deed/dividend arrangements provide a window of opportunity for the most substantive barrier to retail competition in Tauranga/western Bay of Plenty to be addressed and to allow nascent competition to develop.

This is an issue of common interest to both the Authority and the Commission

This is an issue where the Commerce Commission and Electricity Authority "share common interests in relation to their respective statutory functions with regards to the electricity industry".[1] We are concerned this issue may 'slip through the cracks' between the responsibilities of the Commerce Commission as competition regulator, and its role in determining whether to approve the Mercury acquisition of Trustpower's retail business and brand, and the Electricity Authority's role to promote competition as electricity industry regulator.

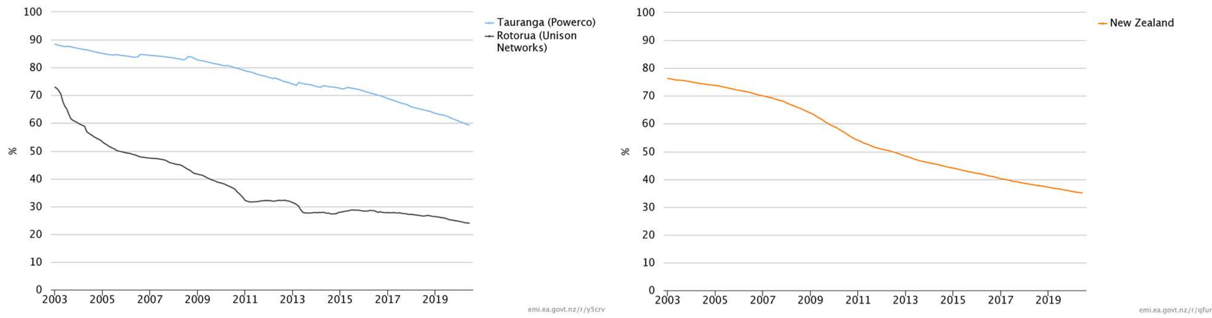
Tauranga/western Bay of Plenty is the worst performing/least competitive electricity retail market in New Zealand

The performance of competition in the electricity retail markets is blighted by Tauranga which has an HHI of 3,950. This is substantially higher than any other regional electricity retail market in New Zealand, even compared to King Country and Waitaki, and is highly concentrated under standard measures of market concentration used in New Zealand and internationally. The Tauranga residential HHI is even worse at 4,045. The story is similar when looked at in relation to Concentration Ratios. Tauranga has the highest CR1 ratio of 60.6%, with the second largest retailer in Tauranga standing at 12.9% market share.

[1] Memorandum of Understanding between the Electricity Authority and the Commerce Commission, December 2010.

The poor state of retail competition in Tauranga can be seen vividly by comparison with neighbouring Rotorua. Trustpower is the incumbent retailer in both markets but the competitive market outcomes could not be more different with Rotorua having the lowest HHI in NZ of 1,430. The trajectory for the Concentration Ratio in Rotorua has mirrored the rest of New Zealand (albeit dropping more rapidly, initially) while Tauranga remains at a stubbornly high uncompetitive level.

Figure 1: Electricity retail CR1 trends



We have previously detailed how the Trustpower-TECT arrangements have restricted competition in Tauranga and adversely impacted prices and consumers in the Tauranga market.[2] The dividend arrangements are case of ‘robbing Peter to pay Paul’ with the dividends essentially matching the level of retail over-pricing. The Electricity Price Review (EPR) Panel noted Trustpower’s prices average $575 a year more than the cheapest alternative in the Tauranga area, as at May 2019.[3] This contrasts with an average TECT rebate of $505 In November 2018.

Basically, Trustpower is capturing the benefits from trust-ownership rather than consumers (the intended Trust beneficiaries) and this (monopoly) value will be transferred to Mercury if TECT goes ahead with its plan to lock payment of its dividends in with Tauranga consumers staying with the new owner of the Trustpower retail business. During the briefings with analysts following the announcement some analysts estimated the capitalised value of the retail overpricing enabled by the dividend has an implied value of circa $200m NZD.

The changes to the TECT Deed/dividend arrangements don’t need to embed existing barriers to competition or transfer Trustpower’s local monopoly to Mercury

While TECT may need to change its deed/dividend arrangements as a consequence of Trustpower selling its retail business and brand it can do so in way that is competitively neutral and does not lock in the current trust-dividend barrier to competition for the next 30 years (until 2050 under the TECT proposals).

By way of example, the TECT dividend arrangements could be changed such that payments are made to all electricity consumers in Tauranga/western Bay of Plenty, which would better serve the interests of the entire local community the TECT is serving, or grandfather payments based on pre-existing beneficiaries (as of Thursday 28 January 2021) regardless of who their subsequent retail supplier is.

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[2] Electric Kiwi and Haast, Electricity Price Review -Options Paper, 22 March 2019, Appendix 3 : Supplementary evidence of problems with The Great Wall of Tauranga, available at: https://www.mbie.govt.nz/dmsdocument/4837-electric-kiwi-and-haast-energy-submission-electricity-price-review-options-paper-pdf.

[3] Electricity Price Review, HIKOHIKO TE UIRA, FINAL REPORT, 21 May 2019.

The TECT proposals in 2018 for reforming its dividend arrangements demonstrate a way forward that would enable sale of the business and promotition of competition in Tauranga for the long-term benefit of consumers.

Concluding remarks

Trustpower's intended sale of its retail business and brand provides an opportunity to address the worst performing retail market in New Zealand. Payment of dividends to ALL consumers in the Western Bay of Plenty and Tauranga and not just to Trustpower-Mercury customers, for example, would better serve the interests of the local community and promote competition for the long-term benefit of consumers (the local community).

Electric Kiwi considers that – as part of the responsibilities for promoting competition – the Commerce Commission and Electricity Authority both have a duty of care to work together and consider how this matter can be resolved. The Authority will not achieve its strategic ambitition of "thriving comptition" if the current TECT dividend arrangements prevail for the next 30 years and/or there continue to be highly concentrated retail markets. Based on market concentration measures used by competition and industry regulators internationally any electricity market with an HHI above 1,500 should be considered to be concentrated.[4]

We recognise the retail market concentration statistics for Tauranga have improved over the last decade, but only compared to a monopoly situation where Trustpower had over 90% market share. The EPR observation that Trustpower is able to sustain prices that average $575 a year more than the cheapest alternative in the Tauranga area, as at May 2019,[5] highlight these modest improvements are not necessarily translating to better pricing and affordability outcomes for Tauranga consumers.

Yours sincerely,

Luke Blincoe
Chief Executive, Electric Kiwi Ltd
[redacted]

[4] For example, the United States Department of Justice: https://www.justice.gov/atr/herfindahl-hirschman-index.
[5] The Authority has discontinued its residential consumer savings monitoring since 2019.