

21 February 2019

Keston Ruxton
Manager, Price-Quality Regulation
Commerce Commission
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Wellington 6011

via e-mail: marketstudies.submissions@comcom.govt.nz

Dear Keston

Submission on the market study into the retail fuel sector

The BusinessNZ Energy Council (the 'BEC') is pleased to have the opportunity to provide a submission to the Commerce Commission on its preliminary issues paper entitled 'Retail fuel market study – Preliminary issues, published on 31 January 2019.¹

Introduction

The purpose of the study is to consider and evaluate whether competition in the retail fuel market is promoting outcomes that benefit New Zealand consumers over the long-term. Providing this submission gives us the opportunity to outline some initial thoughts and comments we would like the Commerce Commission to consider going forward.

Before providing any comments, we would like to express our disappointment at the short timeframe for responses. This has made it difficult for participants to respond in a meaningful and useful way.

Comments

The BEC suggests the consideration of the following to improve the process and outcome of the market study:

- it is important that the Commerce Commission learn from its earlier, similar studies, especially its five year, multi-million-dollar study of the electricity industry by Professor Frank Wolak, an electricity markets expert from Stanford University, and a report based on Wolak's findings by the Commission itself, which made a NZ 4.3 billion calculation of excess profits explicit. Both reports found evidence that electricity generators had been able to exercise market power, but a subsequent Ministerial Review found Wolak used the wrong benchmarks for calculating impacts. Citing widespread criticisms of Wolak's

¹ Background information on the BusinessNZ Energy Council is attached in Appendix One.

methodology, a Ministerial Panel found that there is “no clear evidence of the sustained or long-term exercise of market power” in the New Zealand wholesale electricity market. These are not easy studies to undertake and caution needs to be applied by the Commerce Commission in its work;

- in a similar vein, how the Commerce Commission undertakes this market study is as important as what issues it addresses. We especially have in mind here the precedent effect of this, the Commerce Commission’s first market review under its new legislative power. BusinessNZ has previously expressed considerable concern about the then proposed power and the risks it entail. In addition to creating a widespread risk that the desire to invest is dampened due to the ex post risk of returns being expropriated by regulatory fiat. It noted the inbuilt bias towards intervening:

“Any government agency tasked with conducting a market study will invariably be tempted to include some form of recommended regulatory change, given the inconsistent and often haphazard way in which regulation has been developed in New Zealand over time.”²

A survey of experienced OECD regulators shows the regulatory or policy change is an expected study outcome.³ The implication being that regulators and businesses have an expectation that market studies will lead to regulatory/policy change and, therefore, they should only be undertaken in markets where there has been a long-term pattern of concerning outcomes or behaviour;

- the scope of the review. Paragraph 23 on page 6 of the issue paper outlines that:

“We also note that retail fuel prices are affected by several factors including international crude oil prices, movements in the value of the NZ dollar against other currencies (especially the US dollar), and the level of taxes and levies on fuel. We do not intend to focus on these factors directly.”

It is important to consider the bigger picture when considering local market pricing. Fuel prices reflect broader global and industry trends that local providers have no control over, including increases in global product prices and exchange rate fluctuation. Some of the New Zealand’s fuel provider are operating internationally. The BEC therefore suggests to include the effect of internal supply chains on the fuel retail price in New Zealand into the scope of work;

- factors that need to be considered. Paragraph 52 on page 15 outlines that:

² BusinessNZ submission to the Transport & Infrastructure Committee on the Commerce Amendment Bill, paragraph 2.5, dated 15 June 2018.

³ [https://one.oecd.org/document/DAF/COMP/GF\(2016\)4/en/pdf](https://one.oecd.org/document/DAF/COMP/GF(2016)4/en/pdf) paragraph 27

“The 2017 Fuel Study attempted to assess whether the higher prices and margins meant firms were earning excessive profits. It sought to analyse the level of returns that the fuel firms were earning on their assets, known as “return on average capital employed” (ROACE). The 2017 Fuel Study was limited in its ability to obtain the necessary information to conduct the analysis. However, it observed that where retail ROACEs had been provided, these ROACEs had increased significantly over the period under review and in some cases had increased by over 100% through the period 2012 to 2017.”

Previous fuel market studies have identified challenges around sourcing information and accounting treatments in a consistent form across companies that can be used to understand business performance and investment. This is an important factor that needs to be considered if meaningful conclusions are to be made;

- the extent to which (and how) the Commerce Commission balances the forward- or backward-looking nature of the study. Our work shows that the energy sector of today is vastly more complex than that of as little as five years ago and that the future is set to be more complex and faster moving still. This suggests that the Commerce Commission applies caution in looking backwards to determine its forward-looking interventions. Indeed, we think that there is little point to setting future policy changes by looking in the rear vision mirror then extrapolating forward. It is, of course, important to understand why we are where we are today, but to do more than that to understand the outcomes that are being achieved would not be a useful way to utilise resources. Instead we suggest the Commerce Commission focuses on the observed outcomes and the extent to which there is a gap, if one is present, between the observed outcomes and the long-term interests of consumers in a rapidly changing context; and
- the Commerce Commission needs to be mindful that this isn't a costless exercise for industry.

Summary

We urge the Commerce Commission to engage deeply and often with the market participants to ensure that the issues we have raised in this submission are appropriately managed. We look to the Commerce Commission running an exemplary process that can be held up as a model for future market inquires and we look forward to engaging with the Commerce Commission as this study unfolds.

Yours sincerely



John A Carnegie
Executive Director
BusinessNZ Energy Council

APPENDIX ONE: ABOUT THE BUSINESSNZ ENERGY COUNCIL

The BusinessNZ Energy Council (BEC) is a group of New Zealand's peak energy sector organisations taking a leading role in creating a sustainable energy future. BEC is a division of BusinessNZ, New Zealand's largest business advocacy group. BEC is a member of the World Energy Council (WEC). BEC members are a cross-section of leading energy sector businesses, government and research organisations. Together with its members BEC is shaping the energy agenda for New Zealand.

Our vision is to support New Zealand's economic wellbeing through the active promotion of the sustainable development and use of energy, domestically and globally. With that goal in mind, BEC is shaping the debate through leadership, influence and advocacy.

BusinessNZ is New Zealand's largest business advocacy body, representing:

- Regional business groups [EMA](#), [Business Central](#), [Canterbury Employers' Chamber of Commerce](#), and [Employers Otago Southland](#)
- [Major Companies Group](#) of New Zealand's largest businesses
- [Gold Group](#) of medium sized businesses
- [Affiliated Industries Group](#) of national industry associations
- [ExportNZ](#) representing New Zealand exporting enterprises
- [ManufacturingNZ](#) representing New Zealand manufacturing enterprises
- [Sustainable Business Council](#) of enterprises leading sustainable business practice
- [Buy NZ Made](#) representing producers, retailers and consumers of New Zealand-made goods

BusinessNZ is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

In addition to advocacy and services for enterprise, BusinessNZ contributes to Government, tripartite working parties and international bodies including the International Labour Organisation ([ILO](#)), the International Organisation of Employers ([IOE](#)) and the Business and Industry Advisory Council ([BIAC](#)) to the Organisation for Economic Cooperation and Development ([OECD](#)).



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