ISSN 1178–2560
Decision Series
Project no. 11.04/PRJ0045326

Public version

Determination

Mercury NZ Limited and Trustpower Limited's retail business [2021] NZCC 16

The Commission:	Sue Begg Dr John Small Tristan Gilbertson
Summary of application:	An application from Mercury NZ Limited seeking clearance to acquire Trustpower Limited's retail business
Determination:	Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission gives clearance to the proposed acquisition
Date of determination:	27 September 2021

Contents

The proposed acquisition

1. On 3 August 2021, we registered an application from Mercury NZ Limited (Mercury or the Applicant) seeking clearance to acquire Trustpower Limited's (Trustpower) retail business[1] (the Proposed Acquisition).

2. With the Proposed Acquisition, Mercury would enter into a 10-year wholesale electricity hedge arrangement with Trustpower (the Mercury/Trustpower Hedge). The Proposed Acquisition and the Mercury/Trustpower Hedge have been structured in a way that means that the Mercury/Trustpower Hedge would inevitably follow from the Proposed Acquisition. Given this, we considered the Mercury/Trustpower Hedge as part of our assessment of the Proposed Acquisition. However, any clearance given is for the acquisition of the Trustpower's retail business only.[2]

Our decision

3. We give clearance to Mercury for it to acquire Trustpower's retail business as we are satisfied that the Proposed Acquisition is unlikely to substantially lessen competition in any New Zealand market.

4. Trustpower is selling its retail business as part of a competitive sales process. It is keeping its electricity generation business, which is not included in the Proposed Acquisition. Contemporaneously with the sale of Trustpower's retail business, the Tauranga Electricity Consumer Trust (TECT) is proposing to change the rebate scheme that Trustpower's Tauranga customers receive.

5. Mercury and Trustpower's retail business compete to supply electricity to residential and small and medium-sized enterprise (SME) retail customers throughout New Zealand, and it was this competition that was the focus of our investigation.

6. In relation to electricity, on a conservative basis we assessed the Proposed Acquisition by reference to regional markets. Prices offered by retailers vary by region. The number of retailers in each region varies and the relative size of each retailer, in each region, also varies. Switching data also indicates there is regional variation in the degree to which customers switch between the different retailers. We identified the TECT rebate as being an additional factor differentiating Tauranga from other parts of the Bay of Plenty.

7. In relation to gas, we assessed the Proposed Acquisition by reference to a North Island market for the retail supply of natural gas to mass market customers. Unlike for electricity, gas retailers do not set natural gas prices on a regional basis.

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1 Comprising the retailing of electricity, gas and telecommunications services to residential and small and medium-sized enterprise customers, 'Trustpower' branding and the necessary IT systems and employees to service these customers. Application at [9].

2 Under s 66(1) of the Commerce Act 1986, a person who proposes to acquire assets or shares may give the Commission a notice seeking clearance for the acquisition. Any clearance given by the Commission under s 66(3)(a) of the Commerce Act 1986 is only in relation to the proposed acquisition of assets or shares described in the notice seeking clearance.

8. Several parties raised concerns about competition in the retail supply of electricity in Tauranga due to the effect of the TECT rebate. In particular, concerns were raised that the rebate makes it difficult for retailers to win customers from Trustpower, and that the Proposed Acquisition would exacerbate this situation. Our investigation did reveal that competition was less intense in Tauranga, as evidenced by Trustpower's existing market share, low switching rates over time and the generally higher prices charged by Trustpower compared to other existing retailers in the region.

9. However, we are satisfied that the Proposed Acquisition would not substantially lessen competition in any Tauranga regional market despite the effect of the TECT rebate. The constraint that Mercury currently imposes is not significant, and the merged entity will face a degree of constraint from competitors. Further, our analysis indicates that the merged entity's incentive and ability to raise prices in the Tauranga region is limited to a small subset of Tauranga customers and the potential price rise is also small. So any lessening of competition is unlikely to be substantial.

10. Overall our investigation found there are no regional markets in New Zealand where Mercury and Trustpower are each other's closest competitors. In addition, we found that the merged entity would face competition from other electricity and gas retailers, including both large generators and retailers (gentailers) and smaller retailers. Given this, we are satisfied that the Proposed Acquisition is unlikely to have a significant detrimental effect on competition in any market when compared with what would likely happen if the Proposed Acquisition did not proceed.

Our framework

11. Our approach to analysing the competition effects of the merger is based on the principles set out in our Mergers and Acquisitions Guidelines (our guidelines).[3]

The substantial lessening of competition test

12. As required by the Commerce Act 1986, we assess mergers using the substantial lessening of competition test.

13. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).[4]

14. A lessening of competition is generally the same as an increase in market power. Market power is the ability to raise price above the price that would exist in a competitive market (the 'competitive price'),[5] or reduce non-price factors such as quality or service below competitive levels. [6]

[3] Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2019).
[4] *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].
[5] Or below competitive levels in a merger between buyers.
[6] *Mergers and Acquisitions Guidelines* above n1 at [2.21].

When a lessening of competition is substantial

15. Only a lessening of competition that is substantial is prohibited. A lessening of competition will be substantial if it is real, of substance, or more than nominal.[7] Some courts have used the word 'material' to describe a lessening of competition that is substantial.[8]

16. As set out in our guidelines, there is no bright line that separates a lessening of competition that is substantial from one which is not. What is substantial is a matter of judgement and depends on the facts of each case.[9] Ultimately, we assess whether competition will be substantially lessened by asking whether, and if so what proportion of, consumers in the relevant market(s) are likely to be adversely affected in a material way.

When a substantial lessening of competition is likely

17. A substantial lessening of competition is 'likely' if there is a real and substantial risk, or a real chance, that it will occur. This requires that a substantial lessening of competition is more than a possibility but does not mean that the effect needs to be more likely than not to occur.[10]

The clearance test

18. We must clear a merger if we are satisfied that the merger would not be likely to substantially lessen competition in any market.[11] If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.

The parties

Mercury

19. Mercury is an electricity generator and energy retailer. It is one of five major gentailers in New Zealand. Mercury's primary activities include:[12]

    19.1 generating electricity from geothermal and hydro stations;

    19.2 wholesaling the electricity it generates; and

    19.3 retailing electricity and natural gas to residential and SME customers that it acquires via wholesale spot markets.

20. Mercury primarily supplies its retail products under the Mercury brand but it also supplies prepaid retail electricity via its Globug brand. In addition to supplying retail electricity and gas, Mercury also supplies telecommunications services to approximately 20,000 retail customers through its 49% shareholding in NOW New Zealand Limited.

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7 *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].
8 *Woolworths & Ors v Commerce Commission* (HC) above n7 at [129].
9 *Mergers and Acquisitions Guidelines* above n1 at [2.23].
10 *Woolworths & Ors v Commerce Commission* (HC) above n7 at [111].
11 Section 66(3)(a) of the Commerce Act 1986.
12 Application at [1].

Trustpower

21. Like Mercury, Trustpower is an electricity generator and energy retailer and is also one of five major gentailers in New Zealand. Trustpower's primary activities include:[13]

21.1 generating electricity from hydropower stations across New Zealand;

21.2 wholesaling the electricity it generates; and

21.3 retailing utilities to residential and SME customers including electricity, natural gas and telecommunications services. It also sells bottled LPG gas.

The Proposed Acquisition

22. The Proposed Acquisition would see Mercury acquire Trustpower's retail business, which comprises the retailing of electricity, natural gas and telecommunications services to residential and SME customers, 'Trustpower' branding and the necessary IT systems and employees to service these customers.[14] At the time Mercury filed its application Trustpower's retail business consisted of approximately 234,000 customer contracts covering approximately:[15]

22.1 249,000 electricity installation control points (ICPs);[16]

22.2 43,000 gas connections (35,500 of these are connected to the North Island natural gas network); and

22.3 109,000 telecommunications customers (covering broadband, fixed wireless, voice and mobile retail offerings).

23. The Proposed Acquisition does not include any of Trustpower's generation assets and so Trustpower will continue to wholesale electricity to other parties, as well as continuing to supply certain commercial and industrial electricity customers.[17] Post-acquisition, the new Trustpower entity would be called Manawa Energy.[18]

24. With the Proposed Acquisition, Mercury would enter into the Mercury/Trustpower Hedge to provide it financial risk cover for supply to the retail customers that Mercury would acquire from Trustpower.[19]

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13 Application at [6].

14 Application at [9]

15 As the number of customer contracts is subject to customer switching, the specific number of contracts to be acquired will be determined on the execution date.

16 ICP is a unique number given to the connection point between your site and the network company's line. https://comcom.govt.nz/.

17 [ ] Application at [FT1].

18 Trustpower announcement of new generation business name (11 August 2021).

19 Application at [12].

Industry overview

25. In this section, we outline background on:

    25.1 the structure of the electricity industry;

    25.2 how retailers acquire wholesale electricity;

    25.3 consumer trusts and the TECT; and

    25.4 the supply of natural gas.

The structure of the electricity industry

26. Mercury and Trustpower are two of the largest players in the retail and wholesale energy industry in New Zealand. The electricity industry has, essentially, four main components: generation, transmission, distribution, and retail.[20]

    26.1 Generation: the vast majority of electricity is generated by the five gentailers being Genesis Energy Limited (Genesis), Meridian Energy Limited (Meridian), Contact Energy Limited (Contact), Mercury and Trustpower. All electricity generators, apart from small scale plants, are required to supply their electricity into the same 'gross pool'. Retailers then purchase the electricity they require from this wholesale pool.[21]

    26.2 Transmission: Transpower owns and operates the national electricity transmission system (or the national grid) which transmits high voltage electricity from power stations to distribution (lines) companies and a few major industrial customers.

    26.3 Distribution: 29 Electricity distribution businesses (EDBs) connect to the national grid and distribute the electricity to consumers through their local networks[22] Each EDB sets the terms on which retailers can access their networks to enable them to supply electricity to consumers.[23]

    26.4 Retail: retailers provide a 'bundled' service for most consumers by buying electricity at wholesale (spot) prices from generators, and transmission and distribution services from EDBs. As such, retailers' charges to consumers will include the cost of the electricity supplied as well as charges for transmission and distribution. Retailers acquire nearly all of their electricity from the same gross pool that generators supply electricity into.

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20 MBIE Energy Generation and Markets - Electricity industry. https://www.mbie.govt.nz/.

21 For example, see [ ].

22 Electricity Networks Association. Electricity Network Association https://www.ena.org.nz/ and also Commerce Commission - Electricity distributor map https://comcom.govt.nz/regulated-industries/electricity-lines/electricity-distributor-map.

23 For example, see Application at [202.]

27. The Electricity Authority (EA) is the primary entity responsible for regulating the electricity industry.[24] In addition, the transmission and distribution components of the electricity industry are subject to specific regulation because they are natural monopolies. As such, as traditional gentailers, Mercury and Trustpower compete at two levels of the electricity industry: with other generators to produce electricity, and with all retailers (both gentailers and independent retailers) to supply electricity to end consumers.

How retailers acquire wholesale electricity

28. The Proposed Acquisition primarily relates to the retail component of the electricity industry as it involves aggregation of electricity customer contracts.

29. To supply electricity to end consumers, all retailers need to acquire electricity from the wholesale pool. The supply and demand for electricity from this pool sets the wholesale 'spot price' for electricity.[25]

30. As pricing on the wholesale spot market varies for each trading period, retailers generally seek to manage their exposure to changes in the spot price. This is typically achieved by entering into supplementary contracts and/or financial hedging arrangements at the wholesale level.

31. An electricity hedge arrangement is essentially an agreement that guarantees a particular price for a given volume of electricity (or certain price differential from the spot price), at a certain location over a certain time. There are three main arrangements that allow retailers to hedge their risk although the extent to which each retailer uses each type of arrangement varies. These arrangements are:

    31.1 electricity futures on the Australian Stock Exchange;

    31.2 Financial Transmission Rights, which are administered by the EA; and/or

    31.3 an Over the Counter bilateral arrangement between a generator and retailer, such as the Mercury/Trustpower Hedge.

Consumer trusts and the TECT

32. The TECT is a consumer trust that was established in the 1990s to hold shares in Trustpower for the benefit of the Tauranga region. The TECT distributes money directly to electricity customers in a defined area of Tauranga and the Western Bay of Plenty (collectively, the Tauranga region) via a rebate. To be eligible for the TECT rebate, electricity customers in the region must be a customer of Trustpower (as opposed to another retailer).[26]

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24 The EA is an independent Crown Entity established on 1 November 2010 with a statutory objective to promote competition in, reliable supply by, and the efficient operation of, the electricity industry for the long-term benefit of consumers. https://www.ea.govt.nz/.

25 Retailers buy their electricity from the spot market which operates at over 200 locations on the grid (nodes), reprice it (including adding transmission and distribution charges) and sell it to end consumers.

26 For more information on the TECT, see its website. https://www.tect.org.nz/. In addition to the TECT rebate, the TECT also runs a grants programme for funding community organisations and initiatives.

33. In some other regions in New Zealand, electricity customers also receive consumer trust rebates, but these rebates are provided to customers of all electricity retailers within the area of an EDB's network. The TECT rebate is unique and there is no other region in New Zealand where electricity customers receive a consumer trust rebate for being a customer of only one electricity retailer.

34. Currently, the TECT pays out a rebate twice a year, with customers in the Tauranga region being eligible to receive the rebate as long as they have had an active power account with Trustpower for a six-month eligibility period prior to the payment of the rebate. Under the current terms of the TECT, if a customer switches from Trustpower to another retailer, then they cease being eligible for the TECT rebate unless they switch back to Trustpower, and then are only eligible once they have been back with Trustpower for a full six-month eligibility period.

35. The level of the TECT rebate has varied year on year historically. It has comprised a fixed minimum amount plus a variable amount based on a customer's spend with Trustpower during a six-month eligibility period. However, for the latest financial year, the TECT rebate has been set at a fixed flat amount, with no variable component. Table 1 below lists the amount of the most recent TECT rebates (which have tended to be around $500 per annum (except in one year).

Table 1: The amount of the TECT rebate in recent years

Year	Rebate amount
Year to 31 March 2019	The average rebate was $505. Total rebates paid of $28m.
Year to 31 March 2020	Total $440 fixed, plus variable amount based on spend + one-off distribution of $295. Total rebates paid of $46.8m.
Year to 31 March 2021	Total $440 fixed, plus variable amount based on spend. Total rebates paid of $30.9m
Year to 31 March 2022	$500 fixed amount, half of which was paid in July (second payment due in November)

Source: TECT website and TECT annual reports.

36. Changes have been proposed to the structure of the TECT that will mean, in terms of retail customers:

36.1 that only customers of Trustpower as at 28 January 2021 (within the Tauranga region to which the rebate applies) will be eligible for the TECT rebate in the future;

36.2 customers that have joined Trustpower from 29 January 2021 will not be eligible for the TECT rebate;

36.3 Mercury customers will not be eligible for the TECT rebate post-acquisition;

36.4 where someone has moved into to the Tauranga region from 29 January 2021, they will not be eligible for the TECT rebate even if they were already a Trustpower customer or where the previous occupant of the property they move into received the TECT rebate;

36.5 where a Trustpower customer moves out of Tauranga, they are no longer eligible for the TECT rebate, even if they stay with Trustpower and later move back to Tauranga; and

36.6 any customers in Tauranga that switch away from Trustpower in the future will not be able to get the TECT rebate again if they were to switch back to Trustpower or Mercury post-acquisition.

37. In addition to changes around the customers that would be eligible to receive the TECT rebate, the TECT is proposing changes be made to the levels of the TECT rebate. While historically, the level of the TECT rebate has varied year on year, the TECT proposes to fix upfront the level of the rebate for the next 30 years. The proposal is that the TECT rebate would be $500 a year for the first ten years, would increase to $600 in 2030 and increase further to $700 in 2040, to take account of inflation. The TECT rebate would cease to be paid after 30 years.[27]

38. Both with and without the Proposed Acquisition, the TECT is intending to make these changes to restructure the TECT.[28] The proposed changes to the TECT are a condition precedent to the Proposed Acquisition.[29]

The supply of natural gas

39. In addition to retailing electricity, both Mercury and Trustpower retail natural gas that is supplied to end consumers via the North Island's reticulated gas network.

40. Similar to the electricity industry, the reticulated retail gas network has four main components: exploration and production; transmission; local distribution; and retail.[30] In respect of natural gas, neither Mercury nor Trustpower produce any natural gas so the Proposed Acquisition only involves aggregation of customer contracts at the retail level. Retailers wishing to retail natural gas on the North Island's reticulated gas network tend to acquire the necessary natural gas directly from producers or via the gas trading market (called emsTradepoint).[31]

Market definition

41. We define markets in the way that we consider best isolates the key competition issues that arise from a merger. In many cases this may not require us to precisely define the boundaries of a market. What matters is that we consider all relevant competitive constraints and the extent of those constraints, and that any market definition serves the purpose of illuminating the competition issues under consideration. For that reason, we also consider products and services that fall outside the market, but which still impose some degree of competitive constraint on the merged entity.

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27 Letter from TECT to Commerce Commission (1 September 2021).
28 Letter from TECT to Commerce Commission (1 September 2021).
29 Mercury announcement of Proposed Acquisition (21 June 2021).
30 Gas transmission and local distribution do not face direct competition for their services and are regulated under Part 4 of the Act through price-quality path regulation.
31 Application at [220].

42. This section outlines our approach to defining the relevant markets. In this case, we consider the best way to assess the overlap as a result of the Proposed Acquisition is to assess the following markets:

    42.1 a national market for the wholesale supply of electricity;

    42.2 regional markets for the retail supply of electricity to residential and SME (mass market) customers; and

    42.3 a North Island market for the retail supply of natural gas to mass market customers.

Wholesale market

43. Mercury and Trustpower compete with one another, and with other generators, to supply electricity at the wholesale level.

44. Mercury submitted that there would be no aggregation in any wholesale electricity market because Trustpower's generation assets are excluded from the Proposed Acquisition.[32] However, as part of the Proposed Acquisition the Mercury/Trustpower Hedge would be entered into.

45. Accordingly, we considered it appropriate to assess whether the Proposed Acquisition and/or the Mercury/Trustpower Hedge would affect competition in any potential national market for the wholesale supply of electricity.

Retail markets

46. Mercury and Trustpower both supply electricity and gas to residential and SME customers.

47. Mercury submitted that residential and SME customers can be assessed together as part of the same customer group (together, mass market customers). [33]

48. Consistent with Mercury's submission, we found that there is no material difference between the requirements of, and competitive alternatives available to, residential customers compared to SME customers for both electricity and natural gas.[34] We did not define separate markets for residential and SME customers.

49. In this matter, the key issue the Commission considered was the relevant geographic dimension for each of the retail supply of electricity, and the retail supply of natural gas, to mass market customers.

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32 Application at [145]-[146].
33 Application at [145]-[146].
34 For example, see
[
]

Geographic scope of the retail electricity markets

50. Mercury submitted there is a national market for the retail supply of electricity to mass market customers because:[35]

 50.1 the vast majority of electricity consumed by mass market customers comes from electricity generated and supplied to the national grid; and

 50.2 all retailers can serve all mass market customers across the entire country.

51. The above said, Mercury submitted that its views on the impact of the Proposed Acquisition would not change if the Commission considered narrower geographic retail electricity markets.[36]

52. We considered it appropriate to assess the competitive effects of the Proposed Acquisition on the retail supply of electricity to mass market customers by undertaking analysis for separate regional markets.[37]

<u>Why regional markets are appropriate</u>

53. In contrast to Mercury's submission, publicly available data, such as that published by Consumer NZ's Powerswitch website , the EA and the Ministry of Business Innovation and Employment (MBIE), as well as information provided by various industry participants, strongly indicates that competition for the retail supply of electricity should be assessed by looking at separate regional markets.

 53.1 The number of retailers in each region varies and the relative size of each retailer, in each region, also varies. For example, EA data on mass market ICP counts shows that, when compared to the national average, a retailers' share of customers can vary significantly by region.[38]

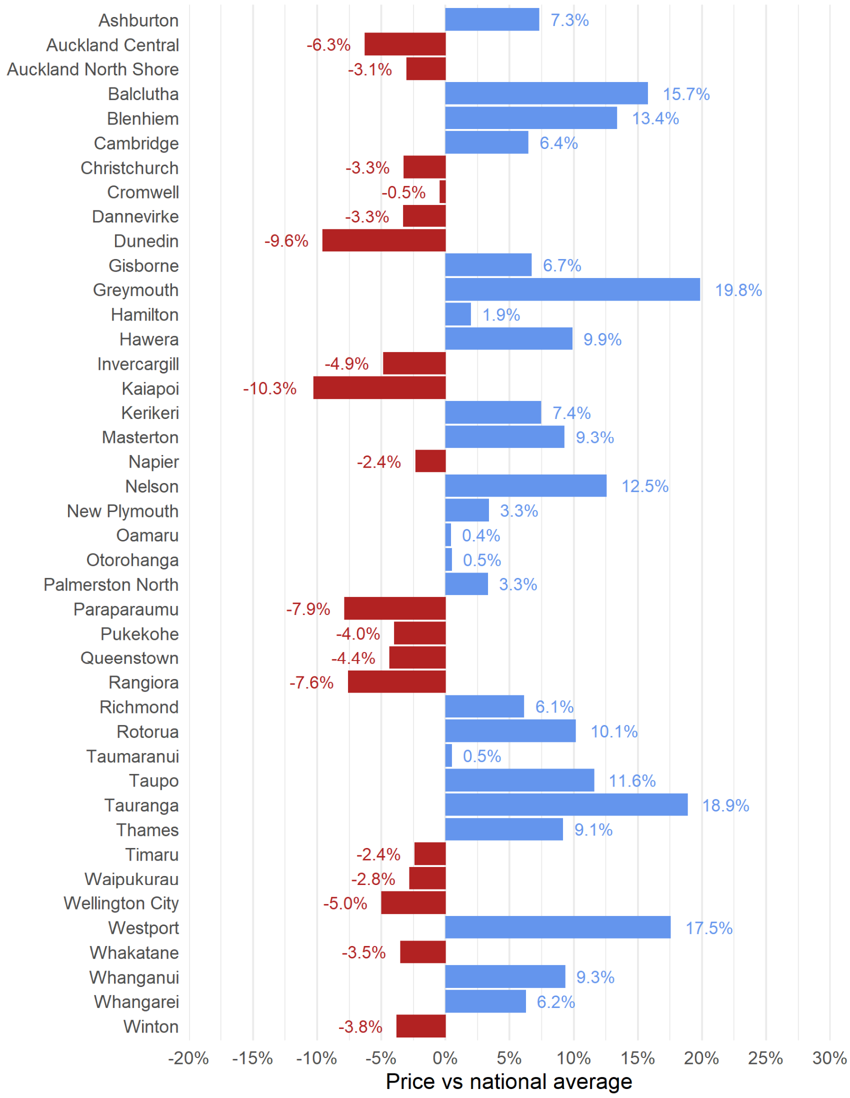
 53.2 The equivalent switching data also indicates there is regional variation in the degree to which customers switch at all, and also regional variation between the different retailers in terms of the extent of switching. For example, mass market ICP churn rates for the year ended 30 June 2021 ranged from 14% to 27% across regional markets, and that the identity of the retailer that wins most ICPs depends on the regional market considered, often in line with regional market shares. Switching data indicates that gentailers generally have lower levels of churn compared to other retailers.[39]

 53.3 Prices offered by retailers vary by region. For example, Figure 1 shows MBIE's estimates for retail pricing across different regions of New Zealand in August 2021 (after subtracting the component of the price that is determined by

35 Application at [145]-[146].
36 Application at [147].
37 If there is no substantial lessening of competition in any regional market there can be no substantial lessening of competition in an hypothetical national market.
38 Regional and national market shares, calculated using this EA data, can be found in Table 2 below.
39 Regional churn rates were calculated as the number of ICPs that switched retailers over the period divided by the total number of ICPs at the start of the period.

each area's EDB).[40] As can be seen, the data shows significant price variation across different geographic areas. The data also indicates significant variation when each area is compared to a national average. For example, Greymouth, Tauranga and Westport were, respectively, 19.8%, 18.9% and 17.5% above the national average, while Kaiapoi, Dunedin and Paraparaumu sat 10.3%, 9.6% and 7.9% below the national average. Figure 1 indicates that Tauranga has some of the highest pricing.

Figure 1: August 2021 differences between local average and national average for household electricity prices (generation + retail components only)



Source: MBIE data.

53.4 The cost to supply mass market customers varies by region. Retailers advised that, in addition to different regions having different network charges (charged by different EDBs), their costs to service customers in different regions vary due to factors such as the wholesale acquisition costs, proximity

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[40] MBIE data from its quarterly survey of domestic electricity prices (QSDEP) is available on its website at https://www.mbie.govt.nz/building-and-energy/energy-and-natural-resources/energy-statistics-and-modelling/energy-statistics/energy-prices/electricity-cost-and-price-monitoring/.

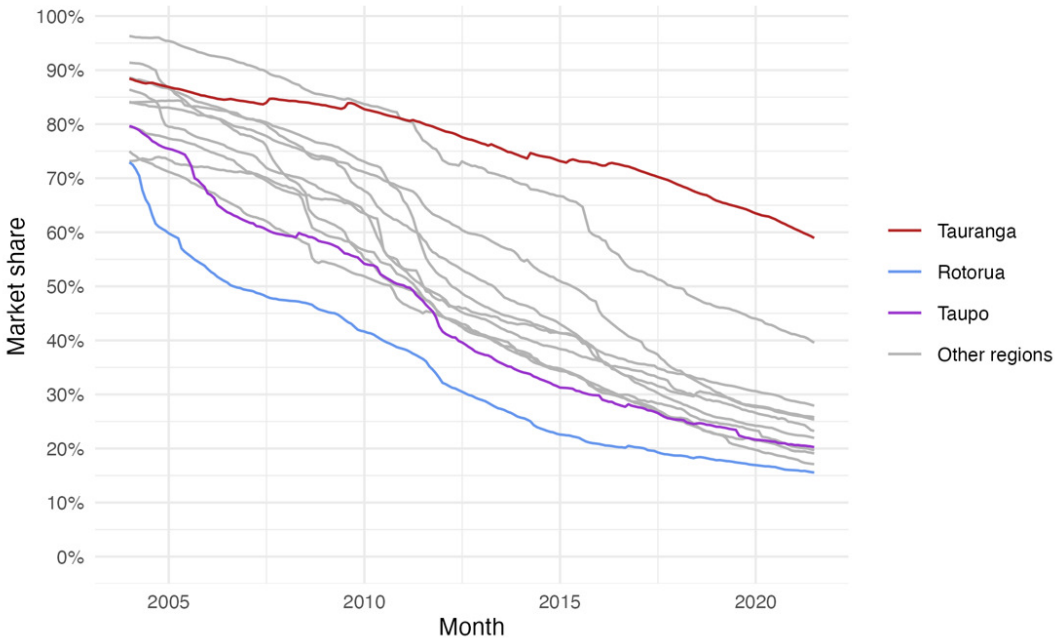
of customer base to generation assets and the usage profile of a retailer's customer base in a particular regional market.[41]

Why a more narrowly defined Tauranga market is appropriate

54. Almost all competitors advised that, unlike in other regions, Trustpower's customers in the Tauranga region tend to be very sticky and that they observe low levels of switching in the Tauranga region, and considered that this is because of the TECT rebate.[42]

55. Figure 2 compares the trend in Trustpower's market share in the Tauranga region compared to other regional markets or local areas in which Trustpower had more than 50% market share in January 2004. This shows a significantly slower decline in Trustpower's market share in the Tauranga region than in other regional markets, and particularly in comparison with neighbouring areas of Rotorua and Taupo.

Figure 2: Trend in Trustpower's market share in Tauranga compared to other areas[43]



Source: EA data.

56. Switching data for the year ended 30 June 2021 indicates that switching rates across all retailers in the Tauranga region were relatively low at 17%. However, the data also indicates that, over that same period, Trustpower lost a substantially smaller percentage of its customers in the Tauranga region than its competitors.

41 See for example, [ ].

42 See for example, [ ] and submission from Vocus to the Commerce Commission (31 August 2021).

43 Figure 2 (and Figure 4 further below) are both based on segmented time series ICP count data from the EA that goes back to January 2004. The entire time-series of data is segmented by customer type using the definitions of customer segments adopted by the EA in 2013, but we do not consider that these definitions being applied retrospectively is likely to affect the accuracy of our outputs.

57. Mercury and Trustpower internal documents
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].[44]

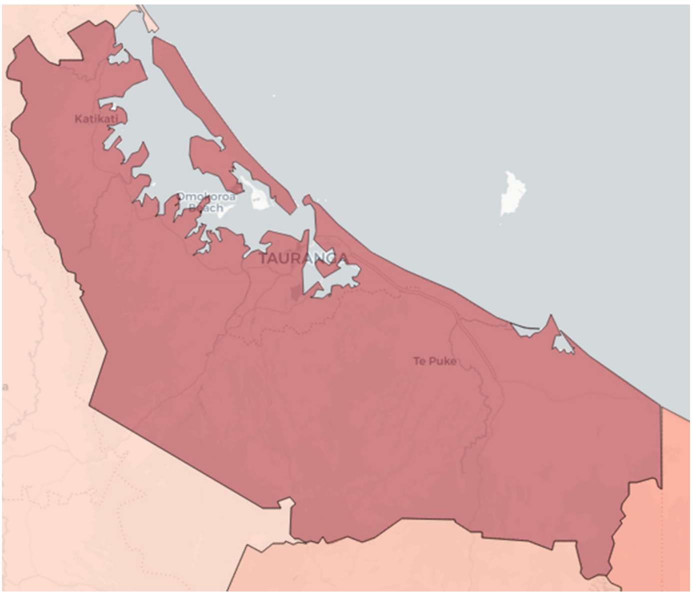
58. The boundaries of the regional markets we have defined are largely in line with the networks of the different EDBs,[45] with one exception. In relation to Powerco's network, we considered it appropriate to split this into two separate geographic markets.

59. The data and evidence above, along with Table 2 and Figure 4 later, show significant differences between the Tauranga region and other areas of Powerco's network in terms of retail pricing, customer switching behaviour and retailer market shares.

60. The split also recognises the fact that the TECT rebate is available to customers in only part of the Powerco's network.

61. Other than Mercury and Trustpower, all market participants (including the EA), submitted that it is appropriate to assess the parts of Tauranga and the Western Bay of Plenty to which the TECT rebate applies separately from the rest of Powerco's network.[46] Figure 3 shows the geographic boundary of this Tauranga regional market.[47]

Figure 3 Tauranga regional market



Source: EA.

[44] [ ]

[45] Commerce Commission - Electricity distributor map https://comcom.govt.nz/regulated-industries/electricity-lines/electricity-distributor-map.

[46] Commerce Commission meeting with EA (20 August 2021),
[ ] submission from David Riley to Commerce Commission (30 August 2021), submission from Electric Kiwi to Commerce Commission (31 August 2021) and submission from Vocus to Commerce Commission (31 August 2021).

[47] https://www.emi.ea.govt.nz/Wholesale/Datasets/MappingsAndGeospatial/NetworkRegionShapefiles. This closely approximates the TECT area, see https://www.tect.org.nz/district-map/.

62. This resulted in us assessing separately 30 regional markets for the retail supply of electricity to mass market customers.[48]

63. The Commission has considered the geographic scope of retail electricity markets in previous merger decisions.[49] We have defined national markets previously, however some time has passed since we last did so, and we look at acquisitions on a case by case basis (as noted at [41]). Market definition provides a framework for analysis, and we define markets in such a way as to expose any relevant competition law issues with a merger.[50] Previous decisions are instructive, but not determinative. For the reasons noted above, information received in this investigation strongly suggests defining regional markets, including a Tauranga regional market.

Geographic scope of the retail natural gas market

64. Mercury submitted that there is a North Island market for the retail supply of natural gas to mass market customers because:[51]

    64.1 all natural gas customers are supplied with natural gas that is transported to them on the North Island's reticulated network; and

    64.2 all natural gas retailers are able to supply customers on the reticulated network by entering into the relevant distribution and metering agreements.

65. Our market enquiries supported Mercury's above submissions. In addition, gas retailers advised that, unlike for electricity, they do not set prices on a regional basis. Rather, they set uniform pricing across the North Island's reticulated network.[52]

With and without scenarios

66. Assessing whether a substantial lessening of competition is likely requires us to compare the likely state of competition if the Proposed Acquisition proceeds (the scenario with the merger, often referred to as the factual) with the likely state of competition if it does not (the scenario without the merger, often referred to as the counterfactual) and to determine whether competition is likely to be substantially lessened by comparing those scenarios.

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48 We note that there is the potential to define more than 30 regional markets because some EDBs have non-contiguous networks in different areas of New Zealand. For example, Powerco's network covers the Bay of Plenty and Coromandel, plus much of Taranaki, Manawatu, Whanganui and the Wairarapa. Powerco has different electricity distribution prices for different areas within its network (https://www.powerco.co.nz/publications/pricing-schedules/), which will be reflected in differences in retail prices. However, defining the boundaries of the regional markets even more narrowly would not have changed our competition analysis in this case.

49 For example, see Contact Energy/Enerco (Commerce Commission Decision 333, 18 December 1998) and Genesis Power/Energy Online (Commerce Commission Decision 476, 10 October 2002).

50 *NZME Limited v Fairfax Limited* [2017] NZHC 3186 at [42].

51 Application at [275]-[276].

52 For example, see
[ ]

67. With the Proposed Acquisition, Mercury would acquire Trustpower's mass market retail business and Trustpower would no longer be an independent retail competitor to Mercury for mass market customers (including SMEs).

68. We consider the factual scenario is best assessed against a status quo counterfactual scenario, with that counterfactual reflecting Trustpower retaining its mass market retail business.[53] As noted earlier, in both the factual and the counterfactual, changes are proposed to restructure the TECT.

How the acquisition could substantially lessen competition

69. We have considered whether the Proposed Acquisition would be likely to substantially lessen competition by assessing the potential unilateral, coordinated and conglomerate effects of the Proposed Acquisition.

    69.1 Unilateral effects can occur when a firm merges with a competitor that would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that the merged firm can profitably increase price above the level that would prevail without a merger without the profitability of that increase being thwarted by rival firms' competitive responses.

    69.2 Coordinated effects can occur when a merger or acquisition makes it significantly more likely that the remaining firms can collectively exercise market power to increase prices, restrict output or reduce quality.

    69.3 Conglomerate effects can occur where a merger gives the merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively.

Unilateral effects in the wholesale supply of electricity

70. We consider that neither the Proposed Acquisition nor the Mercury/Trustpower Hedge is likely to impact on any market for the wholesale supply of electricity because they are unlikely to change other retailers' ability to acquire wholesale electricity on competitive terms. This is primarily because:

    70.1 the purpose of the Mercury/Trustpower Hedge is to provide Mercury with financial risk cover for supply to the retail customers that Mercury would acquire from Trustpower with the Proposed Acquisition. In our assessment, it reflects the internal arrangements that Trustpower would have in place to supply the same customers in the counterfactual scenario; [54] and

    70.2 Trustpower is not 'long' on generation and so has tended not to offer electricity hedges to other retailers.[55] As such, retailers have not been reliant

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53 Application at [25].

54 [ ]

55 For instance, when a gentailer cannot generate sufficient electricity to supply all its existing customers, it is considered to the "short" on electricity and it will be acquiring additional wholesale electricity in order to supply its customers. When the reverse is the case, the generator is considered to be "long".

on Trustpower offering them electricity hedges to enable them to supply electricity in any retail market. Manawa Energy (as an independent generator with the Proposed Acquisition) could offer retailers hedges in the future.

71. The Mercury/Trustpower Hedge is unlikely to result in a material reduction in the amount of hedge cover (and therefore a material increase in the price of such cover) available to retailers. If Manawa Energy offered retailers hedges in the future this would likely assist wholesale market competition.

Unilateral effects in regional markets for the retail supply of electricity

72. We do not consider that the Proposed Acquisition is likely to result in a substantial lessening of competition due to unilateral effects in any regional market in New Zealand for the retail supply of electricity to mass market customers. The following section sets out our reasoning.

73. In summary, we found differences in the level of competitive intensity, and in retail prices being offered to mass market customers, in different regional markets. However, our investigation found there are no regional markets in New Zealand where Mercury and Trustpower are each other's closest competitors. In many regional markets, the aggregation with the Proposed Acquisition would be relatively low. We also found that the merged entity is likely to face competition from other electricity retailers, including both large gentailers and smaller retailers.

Mercury's submissions

74. Mercury submitted that, in any relevant retail electricity geographic market, the Proposed Acquisition would only result in a marginal increase in Mercury's scale and it would not give Mercury any greater influence over its competitors such that it could increase electricity retail prices.[56] This is because:

    74.1 Mercury and Trustpower are not each other's closest competitors in any region for any electricity retail product or service;[57]

    74.2 existing electricity retailers would individually and collectively act as a significant constraint on the merged entity, primarily because there are no constraints on retailers expanding;[58] and

    74.3 there are limited barriers to mass market customers switching retailers.[59]

75. Various internal documents supplied by Mercury, and separately by Trustpower, tended to support Mercury's submissions on retail competition and the view that the merged entity would face constraint from a range of different competitors.[60]

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56 Application at [180].
57 Application at [163.2]
58 Application at [198].
59 Application at [187].
60 [ ]

Assessment of regional retail electricity markets

76. In assessing the potential unilateral effects of the Proposed Acquisition in the retail supply of electricity to mass market customers, we considered, in each regional market:

76.1 market shares and concentration including the magnitude of any increase in concentration with the Proposed Acquisition;

76.2 the competition between Mercury and Trustpower that would be lost with the Proposed Acquisition;

76.3 the constraint provided by existing retail competitors; and

76.4 the barriers to expansion/entry by competitors including the ability and incentive for customers to switch retailers.

Market shares and concentration assessment

77. For each regional market, we assessed market share and concentration data provided by the EA, which was based on ICP counts in July 2021.[61] This data is set out in Table 2 on the next page. We also examined trends in market shares over time, as shown in Figure 4 (which appears on the page after Table 2). Our assessment of this data is that:

77.1 concentration varies widely across each regional market and while ‘incumbent’ retailers have been historically dominant in each regional market, their market share has declined over time, albeit at differing rates;

77.2 Mercury and Trustpower each have high market shares in some regional markets although these areas do not tend to overlap;

77.3 there are many regional markets in which aggregation in market shares with the Proposed Acquisition is relatively low (less than 5%) and which are unlikely to raise competition concerns;

77.4 based on it, we could rule out likely competition concerns in many other regional markets (including the regional markets that have the greatest aggregation with the Proposed Acquisition) due to the market shares of other competitors relative to the merged entity; and

77.5 Tauranga is the one regional market of potential concern with the Proposed Acquisition in which the incumbent’s share (Trustpower) has eroded the least and the area where the merged entity’s market share would be the highest.

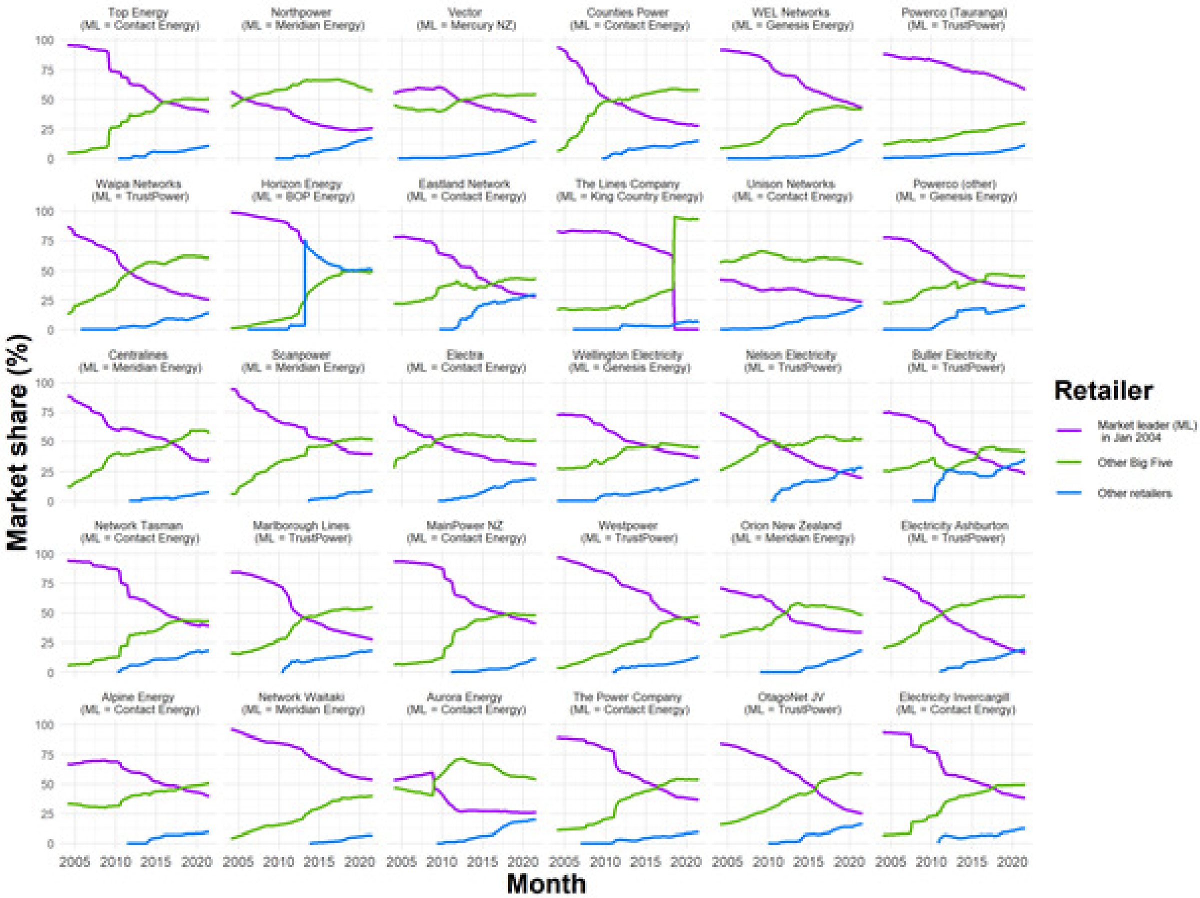
[61] The EA publishes data on market shares and switching in retail electricity at https://www.emi.ea.govt.nz/. Our analysis of market shares, concentration and switching relies on more detailed data provided to us by the EA the period January 2004 to July 2021 segmented by customer type.

Table 2: Summary table of retail electricity concentration measures, sorted highest to lowest based on merged entity market share

	Merging retailer market shares (%)			Other retailer market shares (%)							3-firm concentration ratio (%)	
Regional market	Mercury	Trustpower	Merged	Genesis	Contact	Meridian	Nova	Pulse Energy	Electric Kiwi	Other	CR3 before	CR3 after
Powerco (Tauranga)	6.9	58.3	65.2	12.0	4.7	7.2	3.3	1.8	3.2	2.6	77.5	84.4
The Lines Company	3.8	51.4	55.2	21.1	5.8	11.1	1.5	2.4	1.2	1.6	83.6	87.4
Westpower	7.1	39.6	46.6	7.9	17.4	14.4	2.1	8.4	0.7	2.5	71.4	78.5
Vector	31.3	7.1	38.5	18.1	18.7	10.4	2.1	2.5	4.0	5.6	68.2	75.3
Waipa Networks	12.0	25.2	37.2	25.6	11.9	11.4	5.4	2.8	2.8	2.8	62.9	74.7
Marlborough Lines	9.0	27.3	36.3	9.9	14.2	21.6	2.8	10.4	2.3	2.5	63.1	72.1
OtagoNet JV	6.2	25.0	31.2	13.8	16.4	22.6	4.2	7.9	1.0	2.9	63.9	70.2
Top Energy	16.3	10.2	26.5	14.3	39.2	9.8	1.1	4.3	1.3	3.4	69.8	80.0
Electricity Invercargill	5.1	20.3	25.4	9.1	38.3	15.1	3.5	4.7	1.3	2.6	73.7	78.8
Nelson Electricity	5.6	19.7	25.3	8.8	18.0	19.8	4.3	14.4	3.9	5.4	57.5	63.1
Buller Electricity	1.6	23.2	24.8	8.2	19.7	12.3	1.6	30.8	0.6	1.9	73.7	75.4
Counties Power	19.2	5.3	24.5	20.9	27.5	12.6	5.1	3.6	2.7	3.1	67.6	72.9
Aurora Energy	8.7	13.0	21.8	14.6	26.3	17.4	1.1	8.9	5.7	4.1	58.3	65.5
Powerco (excluding Tauranga)	12.8	8.9	21.7	34.5	11.2	12.6	11.0	3.7	2.3	3.0	59.9	68.8
WEL Networks	8.3	13.3	21.6	43.0	11.5	8.9	3.8	1.8	2.8	6.5	67.8	76.1
Horizon Energy	14.6	5.7	20.4	17.1	5.0	6.6	37.6	7.6	3.0	2.6	69.4	75.1
Unison Networks	9.0	11.3	20.3	28.0	23.6	8.1	6.0	6.2	3.9	3.9	62.8	71.9
Electricity Ashburton	3.6	16.4	20.0	9.2	8.7	42.6	3.1	11.3	1.4	3.6	70.4	74.0
Network Tasman	4.9	14.9	19.8	7.3	38.7	15.9	2.2	9.5	2.9	3.6	69.6	74.5
The Power Company	7.2	12.5	19.7	8.8	36.9	25.3	1.9	4.4	0.9	2.1	74.7	81.8
Northpower	17.4	2.1	19.4	24.4	13.5	25.7	4.8	4.2	4.2	3.8	67.5	69.6
Alpine Energy	6.9	11.1	17.9	15.5	39.5	17.6	2.1	4.4	1.4	1.6	72.6	75.1
Eastland Network	6.6	10.9	17.5	18.3	27.9	7.2	10.0	13.1	1.2	4.8	59.3	63.7
Wellington Electricity	7.6	8.4	16.0	36.8	14.7	15.0	5.9	1.2	5.1	5.2	66.6	67.9
Network Waitaki	4.7	9.4	14.1	10.1	15.8	53.5	0.9	3.0	0.9	1.7	79.3	83.3
MainPower NZ	2.7	9.6	12.3	13.7	41.0	21.6	1.7	5.0	2.1	2.5	76.3	76.3
Scanpower	8.6	2.8	11.4	23.1	17.0	39.7	5.0	1.4	0.5	1.9	79.8	79.8
Orion New Zealand	6.6	4.6	11.2	15.7	21.4	33.7	2.9	1.8	6.4	7.0	70.8	70.8
Electra	5.1	5.7	10.8	30.4	30.6	10.2	4.6	8.5	2.1	2.9	71.1	71.7
Centralines	4.4	3.5	7.9	29.2	19.7	35.9	1.8	1.5	2.4	1.6	84.8	84.8
New Zealand	**15.1**	**11.7**	**26.9**	**22.1**	**19.2**	**15.4**	**4.5**	**3.9**	**3.6**	**4.5**	**56.6**	**68.1**

Source: July 2021 ICP data from the EA. Residential and SME customers only.

Figure 4: Trend in market shares of retailer groups over time in each regional market



Source: EA data.

78. In the rest of this section we set out our competition assessment for the 29 regional markets other than Tauranga, considering:

78.1 existing competition between Mercury and Trustpower;

78.2 the constraint on the merged entity from competitors; and

78.3 barriers to entry and expansion.

79. We discuss the Tauranga regional market separately in a subsequent section.

Existing competition between Mercury and Trustpower

80. For the 29 regional markets other than Tauranga we identified, switching data provided by the EA and our interviews with industry participants was consistent with Mercury's submission that Mercury and Trustpower are not each other's closest competitors.

80.1 There are multiple competitors to whom Mercury and Trustpower lose more mass market customers than Mercury and Trustpower lose to each other. [

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80.2 There is no regional market in which Trustpower loses mass market customers most often to Mercury.

80.3 In almost all regional markets, Mercury most often loses customers to retailers other than Trustpower. [ ].[62]

The constraint on the merged entity from competitors

81. For the 29 regional markets other than Tauranga we identified, we consider that the merged entity is likely to be constrained by competing retailers. Moreover, we consider that there would be no significant change in the level of constraint imposed by these competitors.

82. The three other gentailers (Genesis, Contact and Meridian) each expressed the view that, overall, there would be no material change in competition with the Proposed Acquisition, and that they would provide a constraint on the merged entity in all these 29 regional markets.[63]

83. Similarly, other retailers advised us that, overall, there would be no material change in competition with the Proposed Acquisition in any of these 29 regional markets.[64] However, several retailers advised that they face challenges to expanding generally due to factors unrelated to the Proposed Acquisition. We discuss these issues below.

Barriers to entry and expansion

84. In the 29 regional markets other than Tauranga we identified, we found that the strength of competition that the merged entity would face from retailers expanding and entering is likely to vary by area. Further, we found that different retailers are likely to impose differing levels of constraint in different regions.

85. Our investigations revealed that some 'independent' retailers (who, unlike gentailers, do not own any generation assets) are currently not actively seeking new customers [ ]. This means that they may be less likely to constrain the merged entity.

86. Several independent retailers expressed concerns that the current structure of the electricity industry is affecting their ability to acquire wholesale electricity, which then impacts on their ability to expand.[65] However, we note that:

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62 [ ]

63 [ ]

64 For example, see [ ]

65 Submission from Electric Kiwi to Commerce Commission (31 August 2021), submission from Vocus to Commerce Commission (31 August 2021), [ ] In addition, we note that the

86.1 these concerns relate to an existing feature of the wholesale market that would not change with the Proposed Acquisition; and

86.2 the Mercury/Trustpower Hedge is unlikely to change the way retailers acquire wholesale electricity.

87. While there is the possibility that some independent retailers might not expand, or that they may even retrench or exit certain regions, this is not likely to occur as a direct consequence of a change associated with the Proposed Acquisition. Moreover, even if the exit of some independent retailers was to happen, mass market customers will have several alternatives to the merged entity in each regional market. Also, independent retailers that exited may be able to re-enter relatively easily if market conditions improved in the future. We note that:

87.1 Electric Kiwi and Flick Electric advised they are not currently actively seeking new customers but would return to competing for new customers once [ ];[66] and

87.2 earlier this year, Octopus Energy NZ Limited announced plans to enter New Zealand retail markets.[67] It has delayed its entry[68] [[69]]

Conclusion on regional markets other than Tauranga

88. In the 29 regional markets other than Tauranga, we conclude that the merged entity would face competition from other electricity and gas retailers, including both large generators and retailers (gentailers) and smaller retailers. In these 29 regional markets, the Proposed Acquisition is unlikely to have a significant detrimental effect on competition.

89. We consider the remaining regional market, Tauranga, next.

Assessment of the Tauranga regional market

90. This section outlines our analysis of the likely effects of the Proposed Acquisition in the Tauranga regional market.

91. The Tauranga region market was a focus for our investigation because there is evidence that competition is weaker in Tauranga and post-acquisition supply would be

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EA is reviewing competition in the wholesale market for the period 2018 to early 2021, including analysis of spot and forward prices. https://www.ea.govt.nz/monitoring/enquiries-reviews-and-investigations/2021/wholesale-market-competition-review/.

66 Flick Electric stops taking on new customers in blow to power competition, Stuff (21 July 2021), Electric Kiwi focuses on Australia after losing confidence in wholesale market, NZ Herald (14 July 2021), [ ]

67 https://octopusenergy.nz/about-us/.

68 Market concerns delay Octopus retail push, Energy News (2 September 2021).

69 [ ]

more concentrated. It was also suggested to us that the presence of the TECT rebate that only Trustpower customers receive is relevant to the state of competition in the Tauranga region and that we should consider the impact of proposed changes to the TECT.

92. In our assessment of the likely effects of the Proposed Acquisition in the Tauranga regional market, we consider three questions.

    92.1 Is Mercury a significant constraint on Trustpower now?

    92.2 Would competitors be able to expand to replace the constraint lost by the acquisition?

    92.3 Would the merged entity have an increased incentive/ability to raise prices?

Is Mercury a significant constraint on Trustpower now?

93. The Proposed Acquisition could raise concerns in the Tauranga region if it removed a significant competitive constraint in Mercury. For the reasons set out below, we do not consider that Mercury is a significant constraint in Tauranga.

94. Trustpower has a significant incumbent presence in the Tauranga region,[70] as shown in Table 2. As Figure 2 and Figure 4 show, Trustpower's incumbent share in the Tauranga region has eroded at a significantly slower rate than incumbents' in other regional markets. Trustpower currently has a 58.3% market share of mass market customers in the Tauranga region.

95. The evidence indicates that Trustpower customers in the Tauranga region are very 'sticky' and less likely to switch away than customers of other retailers in Tauranga, and electricity customers in other regional markets in New Zealand.[71] As a result of this stickiness, Trustpower has retained a relatively high share of customers in the Tauranga region over time.

96. With the Proposed Acquisition, the merged entity would have a 65.2% share and the number of competitors with at least 5% market share would reduce from four to three. In terms of the three-firm concentration ratio, this would increase from 77% to 84.4% post-acquisition (an increase of 6.9%). Post-Acquisition, the supply of retail electricity in the Tauranga region would become more concentrated.[72]

97. However, Mercury has a relatively small share of customers in the Tauranga region. The main change in Tauranga as a result of the Proposed Acquisition would be the

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70 Trustpower has been the incumbent in the Tauranga region since the reforms of the electricity sector in the late 1990s which required retailers and EDBs to be separated (Electricity Industry Reform Act 1998 – see Application starting at [45]). Trustpower chose to retain its retail business in Tauranga but sell its electricity distribution network in that region. For more information, see https://www.mbie.govt.nz/assets/2ba6419674/chronology-of-nz-electricity-reform.pdf.

71 See earlier discussion as part of geographic market definition.

72 Concentration measures assist in assessing whether an acquisition might raise competition concerns. Markets are considered concentrated where the three largest suppliers in a market have a combined market share of (the three firm concentration ratio is) 70% or more and one supplier has a market share of 40% or more. *Mergers and Acquisitions Guidelines* above n1 at [3.51].

aggregation of Mercury's existing customers with the existing Trustpower customers and the associated increase in concentration in the market.

98. Consistent with Mercury's submission, Mercury and Trustpower do not appear to be each other's closest competitors in the Tauranga region. Switching data that we analysed for the year ended 30 June 2021 indicated that both Mercury and Trustpower lose a material portion of mass market customers to competitors in the Tauranga region. The data also showed that Mercury lost proportionally more customers to Trustpower than Trustpower lost to Mercury.[73]

Would competitors be able to expand to replace the constraint lost by the acquisition?

99. The Proposed Acquisition could raise concerns in the Tauranga region if competitors could not expand to replace the competition lost with the Proposed Acquisition. For the reasons set out below, we consider that the merged entity would continue to face ongoing competition in the Tauranga region post-acquisition from other retailers.

100. In considering whether the constraint that the merged entity would face from competitors, including their ability to expand, in the Tauranga region we considered:

100.1 the market shares of competitors in Tauranga;

100.2 evidence from competitors that we interviewed, or who made submissions to us, with respect to their ability to compete and expand in Tauranga;

100.3 data on pricing in in Tauranga; and

100.4 information on the impact of the TECT rebate on competition in Tauranga, and on the proposed changes to the TECT.

<u>The market shares of competitors in Tauranga</u>

101. As Table 2 shows, Genesis is the second largest retailer in the Tauranga region, with a 12% share of ICPs as at July 2021. Meridian is the only other retailer (other than Mercury) with a market share above 5%.

102. While competitors have a small presence in the Tauranga region (compared to the incumbent share of Trustpower), Figure 4, above, nonetheless shows that competition has eroded Trustpower's incumbent share to a degree over time. As noted above, in the year ended 30 June 2021, both Mercury and Trustpower lost a material portion of customers to Genesis and Meridian. This suggests that competitors are likely to provide a degree of constraint on the merged entity.

<u>Evidence from competitors</u>

103. Almost all the competitors that we interviewed or received submissions from, raised issues with their ability to compete with Trustpower and expand in Tauranga, and pointed to the existence of the TECT rebate as being the reason why this is the case.

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73 [ ]

103.1 [ ] advised that they have made efforts in the past to increase their presence in Tauranga but have had limited success. They had tended not to specifically target attracting new customers in the Tauranga region.[74] [ ] noted that it had not tried too hard to compete on price in Tauranga because the TECT rebate makes it too difficult.[75]

103.2 [ ] advised that there is no way that it can match the TECT rebate, noting that in the retail market [ ]. It said that this was the case even though Tauranga customers are typically paying a higher-than-usual price for energy. It struggles to compete in Tauranga and would not put resources trying to win Trustpower customers in Tauranga.[76]

103.3 [ ] told us that Trustpower's Tauranga region is one of the hardest ones to break into due to the TECT rebate.[77]

103.4 [ ] said that it has found it particularly difficult to acquire customers in Tauranga due to the TECT rebate, which attract customers to Trustpower despite it charging really high prices. It has offered prices undercutting Trustpower but has not been successful.[78]

103.5 [ ] advised that it is not investing in any specific marketing in Tauranga given the TECT rebate, which it cannot meet and against which it has not been able to compete.[79]

103.6 Electric Kiwi submitted that the TECT rebate is a significant barrier to competition in the Tauranga region. It stated that [ ].[80]

104. However, competitors also generally indicated to us that the Proposed Acquisition would not necessarily make any competition issues in Tauranga any worse.

<u>Pricing in Tauranga</u>

105. In terms of pricing in the Tauranga region, pricing data on Consumer NZ's Powerswitch website[81] indicates that Trustpower's pricing to its customers in Tauranga is comparatively higher than other retailers' pricing in the region. Table 3 below sets out some price estimates generated by the Powerswitch comparison website in September 2021 for a typically household in Taranga using several different usage levels and house configurations.

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80 Submission from Electric Kiwi to the Commerce Commission (1 July 2021) and [ ]

81 Consumer NZ's Powerswitch website is available at https://www.powerswitch.org.nz/.

Table 3: Powerswitch price estimates for a Tauranga customer as of September 2021

Configuration	1	2	3	4	5	6	7	8	9	10
Total annual usage (kWh)	4000	4000	6000	6000	8000	8000	10000	10000	12000	12000
People living in home	1 to 2	1 to 2	1 to 2	1 to 2	3 to 4	3 to 4	3 to 4	3 to 4	5+	5+
Heating source	Electric heater	Heat pump	Electric heater	Heat pump	Electric heater	Heat pump	Electric heater	Heat pump	Electric heater	Heat pump
Heat pump used as summer air conditioner?	n/a	Yes	n/a	Yes	n/a	Yes	n/a	Yes	n/a	Yes
Hot water source	Electric cylinder	Heat pump	Electric cylinder	Heat pump	Electric cylinder	Heat pump	Electric cylinder	Heat pump	Electric cylinder	Heat pump
Insulation	Ceiling only	Floor, wall, ceiling	Ceiling only	Floor, wall, ceiling	Ceiling only	Floor, wall, ceiling	Ceiling only	Floor, wall, ceiling	Ceiling only	Floor, wall, ceiling
Cost of cheapest Trustpower plan ($) excluding TECT rebate	1,558	1,557	2,274	2,276	2,989	2,991	3,584	3,587	4,179	4,180
Cost of cheapest alternative plan from each retail brand ($)										
Powershop	1,173	1,164	1,701	1,690	2,229	2,213	2,637	2,617	3,038	3,014
Mercury	1,212	1,211	1,756	1,757	2,300	2,301	2,730	2,732	3,161	3,162
Pulse Energy	1,257	1,256	1,854	1,856	2,450	2,451	2,835	2,836	3,219	3,220
Contact	1,293	1,293	1,877	1,878	2,461	2,462	2,895	2,896	3,324	3,324
Comtricity	1,366	1,365	1,969	1,970	2,572	2,573	3,059	3,061	3,545	3,545
Energy Online	1,279	1,278	1,855	1,856	2,431	2,433	2,891	2,893	3,342	3,343
Meridian	1,401	1,400	2,038	2,040	2,675	2,676	3,186	3,189	3,698	3,699
Genesis	1,476	1,475	2,153	2,154	2,829	2,831	3,372	3,374	3,906	3,907
Estimated savings on alternative plans compared to Trustpower ($)										
Powershop	385	393	573	586	760	778	947	970	1,141	1,166
Mercury	346	346	518	519	689	690	854	855	1,018	1,018
Pulse Energy	301	301	420	420	539	540	749	751	960	960
Contact	265	264	397	398	528	529	689	691	855	856
Comtricity	192	192	305	306	417	418	525	526	634	635
Energy Online	279	279	419	420	558	558	693	694	837	837
Meridian	157	157	236	236	314	315	398	398	481	481
Genesis	82	82	121	122	160	160	212	213	273	273
Max savings ($)	**385**	**393**	**573**	**586**	**760**	**778**	**947**	**970**	**1,141**	**1,166**
Median savings ($)	**272**	**272**	**408**	**409**	**534**	**535**	**691**	**693**	**846**	**847**

Source: Powerswitch, as per randomly selected residential home in Fraser Street, Tauranga South, on TrustPower All inclusive – Friends plan, with fixed term discounts disabled and someone home during the day.

106. While the figures in Table 3 are estimates, they suggest that (without factoring in the TECT rebate) Trustpower was most expensive retailer as at September 2021 and that Mercury was one of the cheaper retailers (second cheapest after Meridian's Powershop brand).[82]

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82 Although we note Table 3 excludes some low-priced independent retailers that have recently taken themselves off Powerswitch.

107. When the TECT rebate is taken into account, Trustpower's prices for many customers are not the most expensive. These customers may therefore end up paying more if they were to switch away from Trustpower. However, many other customers are likely to be able to pay less for their electricity if they switched from Trustpower to another retailer, even after factoring in the TECT rebate.

108. Retailers that we spoke to as part of our investigation of the Proposed Acquisition cited price as the main reason for customers switching retailers. Because Table 3 indicates many Tauranga customers are likely to pay less for their electricity if they switched to another retailer, this pricing data is further evidence that other factors may contribute to customers not switching away from Trustpower in Tauranga. These factors may include consumer biases which may be present even absent the TECT rebate (eg, due to inherent complexity of comparing offers made by electricity retailers).

109. This aside, the data in Table 3 suggests that through its higher pricing in Tauranga, Trustpower is capturing a significant share of the TECT rebate its customers get. We received submissions from some competing retailers to this effect.[83]

The impact of TECT rebate and proposed changes to it

110. We have previously received, and made enquiries into, complaints that Trustpower customers are more 'sticky' than customers of other retailers due to the presence of the TECT and the rebate that it pays.[84] We received similar complaints during our assessment of the Proposed Acquisition, plus additional information on the TECT.

111. There is strong evidence indicating that the TECT rebate makes it more difficult for competitors to expand in the Tauranga region compared with other regions. This includes Trustpower's higher existing market share, lower switching rates over time and the generally higher prices charged by Trustpower compared to other existing retailers in the region. Through its higher electricity pricing in Tauranga, Trustpower is capturing a significant share of the TECT rebate its customers get. This benefit would flow to Mercury with the Proposed Acquisition.[85]

112. As set out at [36] to [37] above, changes are being proposed to the TECT that would mean that, over time, the number of customers in the Tauranga region eligible to receive the TECT rebate will likely reduce. This may increase opportunities for competitors to win customers.[86]

83 Submission from Vocus to the Commerce Commission (31 August 2021) and submission from Electric Kiwi to the Commerce Commission (31 August 2021).

84 [ ]

85 [ ] See Confidential Attachment A for this evidence.

86 [ ] See Confidential Attachment A.

113. However, the proposed changes to the TECT may also provide a disincentive to Trustpower customers to switch to other retailers, given once they do so they will no longer be eligible for the TECT rebate again, even if they subsequently re-join Trustpower. This change to the TECT could make it more difficult for competitors to expand, or compete for Trustpower customers that currently are eligible for the TECT rebate.

114. Some competitors submitted that the proposed changes to the TECT would make it harder for them to compete in the Tauranga region and make customers less likely to churn away from Trustpower.

114.1 [ ] commented that currently a customer can leave Trustpower to 'test the waters' with another retailer, but has the option to switch back to Trustpower and get the TECT rebate again. However, with the proposed changes to TECT, once a customer leaves Trustpower it can never get the TECT rebate again, which may result in near zero churn of Trustpower's TECT customers in the future.[87]

114.2 Electric Kiwi submitted that the proposed changes to TECT are even more harmful to competition than the existing TECT arrangements. Trustpower customers will know that if they switch away from Trustpower they will permanently lose the TECT rebate, which will foreclose over 50% of customers in Tauranga to competitors.[88]

114.3 Vocus submitted that the proposed changes to TECT are worse for competition that the current arrangements, as they lock in the TECT rebate for 30 years and the new 'use-it or lose it' entitlement criteria for the rebate will inhibit switching by Trustpower customers (who would permanently lose their entitlement to future TECT rebates). Competing retailers would need to offer prices between $500 and $700 cheaper than Trustpower to compete for TECT customers.[89]

115. As noted earlier, changes to the TECT are proposed to occur both with and without the Proposed Acquisition. While we consider that the TECT rebate does affect competition in the Tauranga regional market, it does not contribute to any lessening of competition as a result of the Proposed Acquisition. We consider that with the Proposed Acquisition, Mercury would not gain any additional ability to retain Mercury customers, as they will not be eligible for the TECT rebate. The merged entity is unlikely to have a materially greater ability to retain Trustpower customers than Trustpower does today. The Proposed Acquisition would not make the impact of the TECT rebate worse from a competition perspective.

Would the merged entity have an increased incentive/ability to raise prices?

116. The Proposed Acquisition could raise concerns in the Tauranga region if the merged entity's incentives were sufficiently different to those of Trustpower without the

87 [ ]
88 Submission from Electric Kiwi to the Commerce Commission (31 August 2021).
89 Submission from Vocus to the Commerce Commission (31 August 2021).

acquisition and meant that that the merged entity could profitably increase prices above the level that would prevail without the acquisition. In other words, if customers would be likely to face higher price rises with the Proposed Acquisition than would be the case without the acquisition. For the reasons set out below, we consider that the available evidence does not suggest that this is likely to be the case.

117. Internal documents provided by both Mercury and Trustpower contained nothing to suggest that there would be any change in their ability or incentive to raise prices with the Proposed Acquisition, compared to the scenario without the acquisition.[90]

118. We undertook some quantitative analysis to understand the effect of the Proposed Acquisition, in terms of potential price increases. This analysis included indicative gross upwards pricing pressure index (GUPPI) calculations and dual-brand analysis (DBA) around pricing.

119. The GUPPI measures the incentive of the merged entity to increase prices.[91] It takes into account recent data on the gross customer margins earned by Mercury and Trustpower and the rate at which departing customers of one retailer join the other (the diversion rate).

119.1 GUPPI calculations for Tauranga suggest that, if the merged entity retains separate pricing for Mercury and Trustpower, it would have an incentive to increase prices by 8.7% for Mercury customers and 1.4% for Trustpower customers.

119.2 However, if diversion rates fall post-acquisition, the strength of the merged entity's incentives to raise prices may also fall. The Mercury-to-Trustpower diversion rate may be especially affected by the proposed changes to the TECT, as customers switching from Mercury to Trustpower may no longer receive the TECT rebate.[92] We consider that this may partially offset any increase in incentive to raise prices for the Mercury brand post-acquisition. We estimate that if the diversion rate from Mercury to Trustpower halved,

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90 [ ] See Confidential Attachment A for this evidence.

91 GUPPI does not take account of any offsetting downward pricing pressures, for example from merger efficiencies, or supply side responses. Farrell and Shapiro (2010) suggest a 10% default efficiency credit. It is therefore not a measure of likely post-merger price increases and will be positive so long as there is an overlap between the merging firms' products and the respective gross margins are positive. There is not a 'bright-line' threshold test for the value of a GUPPI that may give rise to *a priori* concerns about potential unilateral effects. See Salop S and S Moresi (2009), *Updating the Merger Guidelines: Comment*, Georgetown Law Journal 2009; Farrell J and C Shapiro (2010) *Antitrust Evaluation of Horizontal Mergers: An Economic Alternative to Market definition*, The B.E. Journal of Theoretical Economics, Vol 10, Issue 1, Article 9.

92 We note that the proposed changes to TECT (already publicly announced) could already have had impact on customer switching in the Tauranga region, if it has discouraged customers from switching to Mercury to Trustpower this year (in the knowledge that they will not be or are not eligible for the TECT rebate). This may mean that we have already seen an effect of the proposed changes to TECT in the switching data we analysed for the year ended 30 June 2021.

the GUPPI for Mercury would also halve to 4.3% (the GUPPI for Trustpower would be unchanged).

120. The DBA estimates the number of customers that Mercury and Trustpower could afford to lose (pre- and post-acquisition) before a unilateral 5% price rise became unprofitable in Tauranga. We would expect this allowance to increase for both brands post-acquisition because, by continuing to operate Mercury and Trustpower as separate brands, the merged entity would be able to recoup some of the lost margins of the portion of departing Mercury customers that join Trustpower, and vice versa. We refer to this effect as a ‘dual-brand advantage’, and it would offset some of the costs incurred by losing a customer, therefore increasing the merged entity’s incentive to take the risk of raising prices.[93]

120.1 Analysis of a dual-brand strategy for the merged entity in Tauranga suggests that, post-acquisition, the merged entity could profitably impose a 5% price increase for Trustpower customers in Tauranga as long as it does not lose more than 19.4% of Trustpower customers. Pre-acquisition, Trustpower could profitably impose a unilateral 5% price rise as long as it does not lose more than 18.4% of customers.

120.2 This reflects only a small increase in the merged entity’s incentives to raise Trustpower prices in Tauranga, and therefore the dual-brand advantage is unlikely to be sufficient to increase the likelihood of such a price increase taking place. In both scenarios, we estimate that the Trustpower brand would have to retain just over 80% of customers to profitably sustain a 5% price increase.

120.3 Our DBA indicates that Mercury could currently afford to lose 25.6% of customers while profitably imposing a 5% price increase, but post-acquisition this allowance could grow to 46.0% of customers. However, if the Mercury-to-Trustpower diversion rate halved, this allowance would only grow to 32.9% of customers.

120.4 This may reflect a moderate increase in the incentive to raise Mercury prices as a result of the dual-brand strategy. However, the size of this increase depends on the merged entity’s ability to sustain Mercury-to-Trustpower diversion rates post-acquisition, which may be weakened by the proposed changes to the TECT.[94]

121. The above findings are not predictions of price increases nor do they provide a definitive answer on whether the Proposed Acquisition would substantially lessen

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93 This is essentially a reframing of the GUPPI, as it is similarly based on the margins earned by Mercury and Trustpower and the diversion rate between the two. However, it also takes into account the prices set by Mercury and Trustpower and the effect on margins of a 5% increase in these prices. Note that the DBA is not a direct measure of whether such a price increase is likely to be imposed by either Mercury or Trustpower, pre- or post-acquisition. Rather, it measures any increase in incentives to raise prices that may arise from the merged entity’s dual-brand strategy.

94 We may have already seen an effect of the proposed changes to TECT in the switching data we analysed for the year ended 30 June 2021. See above n92.

competition in Tauranga. The findings simply provide an indication of the possible strength of incentives that the merged entity would have to increase prices post-acquisition.

122. In our view, the analysis suggests that the Proposed Acquisition would be unlikely to substantially increase the merged entity's incentive to raise Trustpower prices in Tauranga beyond their current levels (compared to the incentives that Trustpower has already to raise prices). While it also suggests that the merged entity may have an incentive to raise prices by 5-8% for its Mercury customers in Tauranga, we consider this would be unlikely to amount to a substantial loss of competition in the Tauranga regional market, since Mercury has only a 7% share in the Tauranga market. We also consider that this incentive may diminish if departing Mercury customers are less inclined to switch to Trustpower when they are not eligible for the TECT rebate, which is likely to be the case.

Conclusion on the Tauranga regional market

123. We consider the Proposed Acquisition is unlikely to result in a substantial lessening of competition in the retail supply of electricity to mass market customers in the Tauranga region. The constraint that Mercury currently imposes is not significant, and the merged entity will face a degree of constraint from competitors (both gentailers and other retailers). Further, our analysis indicates that the merged entity is unlikely to have the ability to substantially raise prices in the Tauranga region.

Unilateral effects in the retail supply of natural gas

124. We do not consider that the Proposed Acquisition is likely to result in a substantial lessening of competition due to unilateral effects in the North Island market for the retail supply of natural gas to mass market customers.

125. Mercury submitted that the Proposed Acquisition would only result in a marginal increase in Mercury's scale and it would not give Mercury any greater influence over its competitors such that it could increase natural gas retail prices.[95]

126. Our investigation indicated that there are limited barriers to electricity retailers bundling natural gas in the North Island with other services in their portfolios.

127. No industry participants submitted that Mercury and Trustpower are each other's closest competitors in this market. With no upstream gas assets, the primary reason that Mercury and Trustpower, as well as other existing retailers such as Contact and Pulse Energy, retail natural gas is to offer customers an energy bundle and this helps reduce the churn of their electricity customers.[96]

128. No-one that we consulted submitted that the merged entity would be in a better position to negotiate more favourable wholesale supply terms with a gas supplier,

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95 Application at [302].

96 For example, see
[ ]

and so the Proposed Acquisition is unlikely to have an impact on their ability to compete.

Coordinated effects in the retailing of electricity or gas

129. A merger can substantially lessen competition if it increases the potential for the merged entity and all or some of its remaining rivals to coordinate their behaviour and collectively exercise market power such that output reduces and/or prices increase across the market. Unlike unilateral effects, which can arise from the merged entity acting on its own, coordinated effects require some or all of the firms in a market to be acting in a coordinated way.

130. Given the similarities between the relevant retail electricity and gas markets, the analysis for both electricity and gas is substantively the same. Our assessment of the potential for coordination in each of these markets is set out below.

131. While some conditions of retail electricity and gas markets point to the potential for coordination (eg, transparent pricing), there are also frequent deviations from published prices (eg, where discounts are offered to win or retain a customer), making it difficult for retailers to coordinate on price.

132. We do not consider that the Proposed Acquisition is likely to result in a substantial lessening of competition due to coordinated effects in any retail electricity or gas market.

133. Mercury submitted that the Proposed Acquisition will not, and will not be likely to, increase the potential for coordinated effects to arise and we have not identified any market(s) where the Proposed Acquisition would increase the merged entity's and the remaining retailers' collective ability: [97]

    133.1 to profitably increase prices to certain retail mass market customers; and/or

    133.2 to allocate certain customers that they will supply to.

134. Our investigations supported Mercury's submissions.

135. No industry participants raised concerns about the potential for coordinated effects to arise from the Proposed Acquisition, or that the Proposed Acquisition would change the conditions in any retail electricity or gas market making them more prone to coordination. This is primarily because:

    135.1 the relevant retail markets include a range of competitors of different sizes, scale and scope. This would continue to be the case post acquisition, even though the merged entity would become closer in size and scale to Genesis;

    135.2 we have seen no evidence that the removal of Trustpower as an independent retailer with the Proposed Acquisition would remove a player that is disrupting or preventing coordination; and

[97] Application at [209] and [325].

135.3 the merged entity would continue to face constraint from competitors, who can reasonably easily expand and enter in most retail markets, making it hard to sustain coordination.

Conglomerate effects in retailing of electricity and/or gas

136. A merger between suppliers (or buyers) who are not competitors but who operate in related markets can result in a substantial lessening of competition due to vertical or conglomerate effects. This can occur where a merger gives the merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively (which we refer to as 'foreclosing rivals').

137. We do not consider that the Proposed Acquisition is likely to result in a substantial lessening of competition due to conglomerate effects in any relevant retail electricity or gas market. Market power is a precondition to a conglomerate effects theory or harm and without market power no concerns can arise.

138. Bundling is a feature of retail electricity and/or gas markets currently and it is becoming more prevalent. Many retailers bundle electricity and gas together as a dual fuel offering and many energy retailers also offer bundles that include telecommunications products.

139. Mercury submitted that that the Proposed Acquisition would not have, or be likely to have, the effect of substantially lessening competition due to conglomerate effects because Mercury's acquisition of Trustpower's retail businesses will not give it any new or greater bundling capabilities than what already exist.[98]

139.1 Other retailers offer the same or similar bundles of services as the merged entity.

139.2 Having a bundling of services is not essential to compete in any electricity or gas market.

139.3 It is relatively straightforward for electricity retailers to add 'white label' products and services to their existing retail portfolios, if they choose to.

140. Our investigations supported Mercury's submissions.

Overall conclusion – no substantial lessening of competition

141. On the basis of the evidence before us, we are satisfied that the Proposed Acquisition is unlikely to substantially lessen competition in any of the relevant markets that we have identified.

98 Application at [215] and [332].

Determination on notice of clearance

142. Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission determines to give clearance to clearance to Mercury NZ Limited to acquire Trustpower Limited's retail business, including the retail electricity (excluding commercial and industrial), reticulated and bottled gas, fixed and wireless broadband and mobile phone business operated by Trustpower, as set out in the Agreement for Sale and Purchase of Retail Business of Trustpower Limited dated 19 June 2021.

Dated this 27th day of September 2021

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Sue Begg
Deputy Chair

Confidential Attachment A