



Economic Regulation Authority

The Effectiveness of the Synergy Regulatory Scheme

2016 Report to the Minister for Energy

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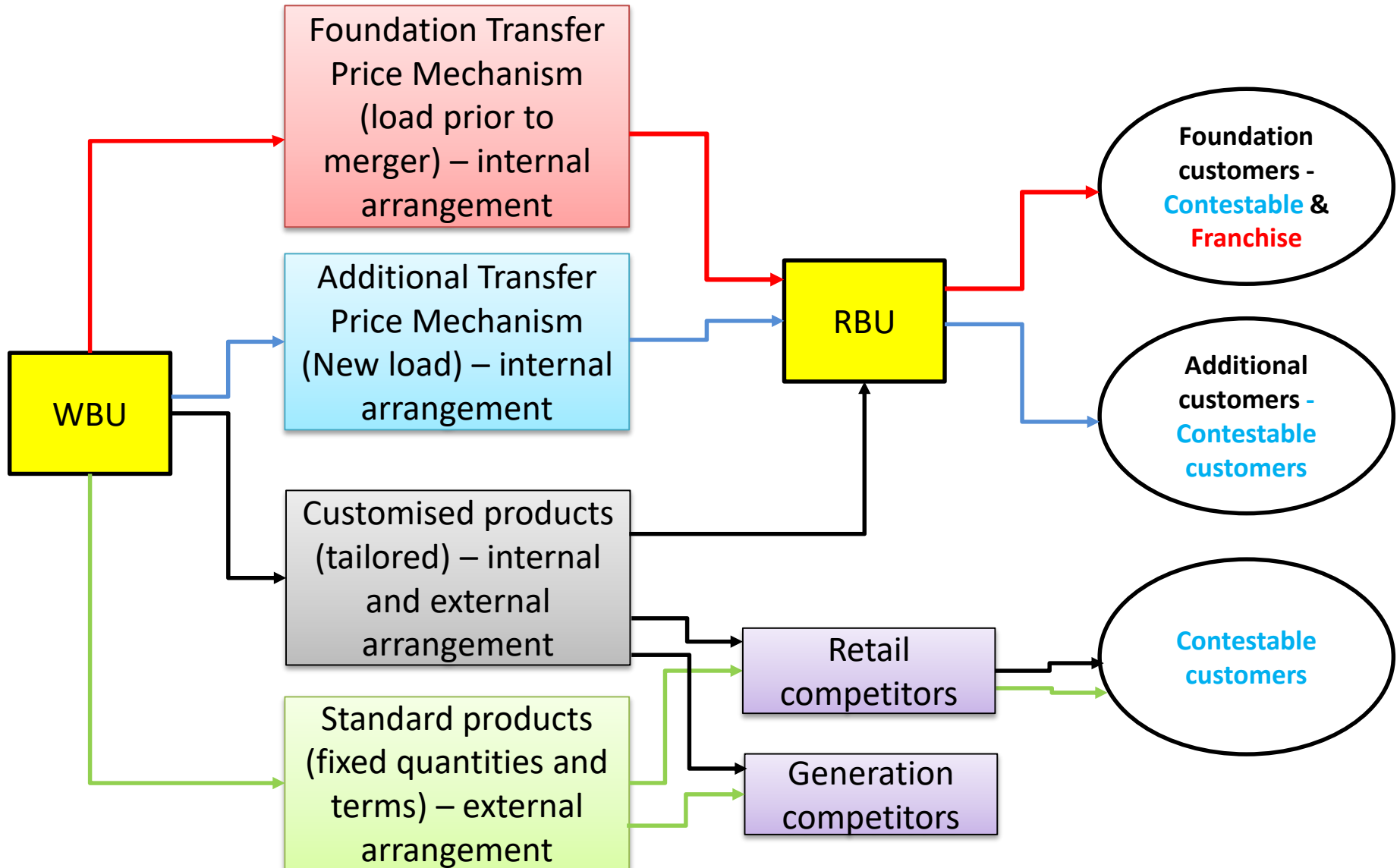
The Synergy (EGRC) Regulatory Scheme

- 1 January 2014, merger of Verve Energy and Synergy.
- Scheme requirements:
 - Segmentation;
 - Internal transfer pricing;
 - Standard products;
 - Non-discrimination
 - Audit and review; and
 - ERA reviews effectiveness of scheme annually.

The main contractual arrangements under the scheme

Bilateral wholesale supply arrangements

Retail customers





2016 Retail and Wholesale Competition

- Substantial increase in energy market price volatility;
- Synergy sets energy prices 84% of time.
- Demand for customised products but only one standard product sold;
- Competition in contestable retail market between six main participants, with generation assets to self hedge;
- Small retailers exposed to energy market volatility;
- Synergy dominant (owns or controls 74%).



Wholesale Arrangements

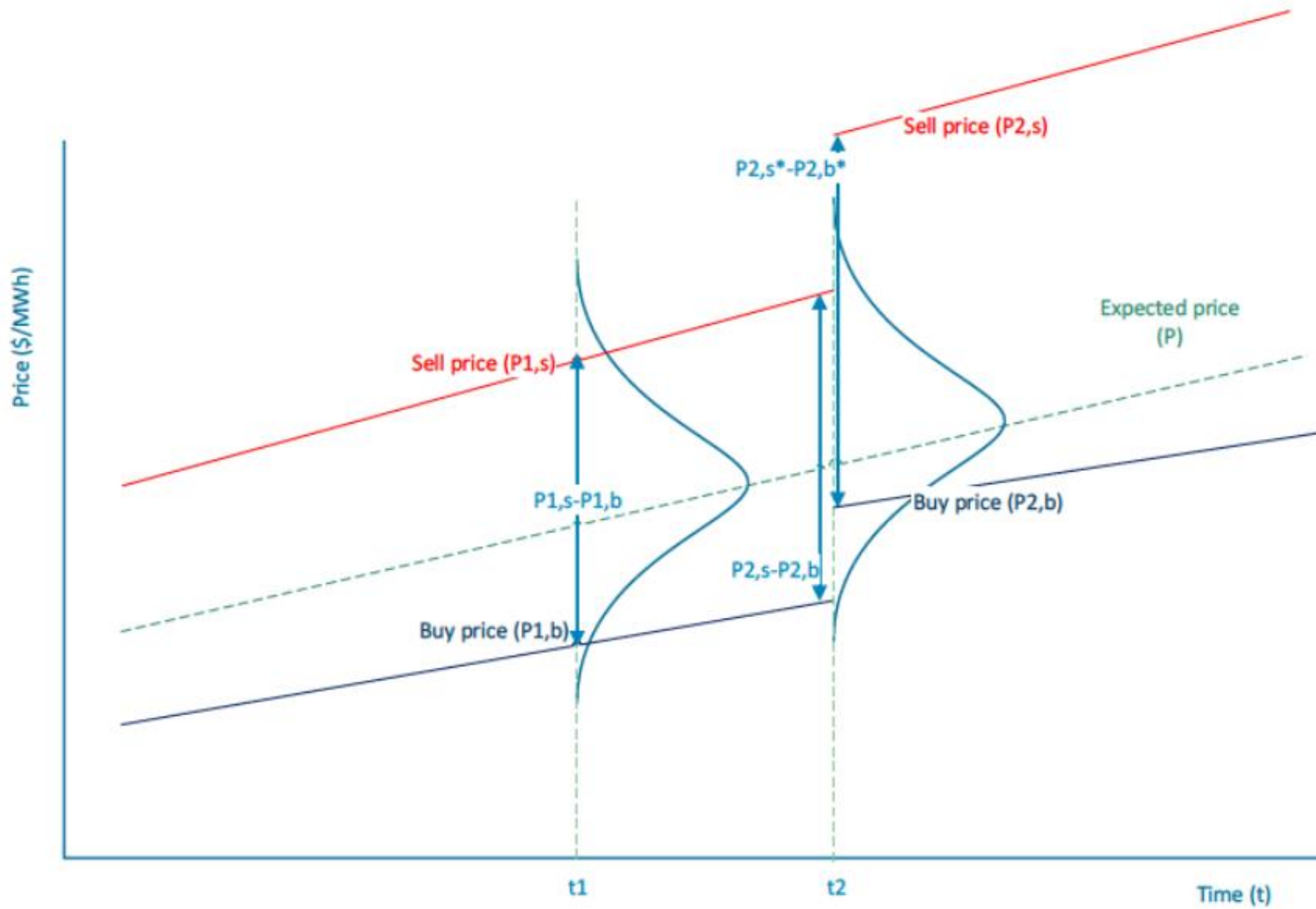
- Previously, transfer pricing based on past contracts and budgets.
- Revisit transfer pricing every 3 years.
- From 1 July 2017 an energy forward curve (Synergy's forecast of future energy market prices) used to calculate foundation and additional transfer prices.
- Also underlies calculation of standard product prices.
- Must also underlie customised products.



Efficient pricing in the WEM depends on

- Pricing at short run marginal cost in energy markets;
 - Reliable and efficient forecasting of future energy market prices by Synergy;
 - The buy/sell spread – which constrains Synergy’s pricing of bilateral contracts.
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- **set a narrower spread of 10 percent between buy and sell price to ensure that pricing discipline is placed on Synergy.**

Figure 2. Buy–sell spread and relationship to expected price*





RBU Involvement in Setting Forward Energy Curve

- RBU involvement in setting contract prices may confound the ring fencing requirements;
- Stakeholders may not be aware of the replacement transfer pricing method.
- There is no requirement for Synergy to inform the ERA to allow for regulatory scrutiny
- **Synergy publishes its foundation transfer price and the method it uses for calculating this price.**



Standard Product Arrangements

- Credit requirements burdensome and intrusive;
 - Specifications too rigid; and
 - Asymmetric force majeure provisions.
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- **Relax credit requirements so they are proportionate to Synergy's exposure to risk of counterparty default;**
 - **Review and amend standard product specifications and force majeure clauses**



Segment Financial Reporting

- No requirement to separate gas and electricity or contestable and non-contestable financial results.
- **Synergy to produce consolidated segmental financial reports. Information to be treated as ‘commercial in confidence.’**



Questions / comments?