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Commerce Commission
PO Box 2351
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Review of the Commerce Commission's funding for the regulation of electricity and gas networks under Part 4 of the Commerce Act 1986

Dear Commerce Commission and Ministry of Business Innovation and Employment

Unison appreciates the opportunity to submit on the Commission's consultation on its levy funding out to 2025/26. The Commission's budget for Part 4 regulation of electricity and gas was last reviewed in 2013. We agree it is timely that the Commission's budget is reviewed particularly with the extent of the decarbonisation challenge now starkly laid out in the Climate Change Commission's report. We expect profound changes in the energy sector and significant challenges with supporting our communities to adapt. Part 4 regulation will need to enable EDBs to adapt to the demands and expectations of consumers and other stakeholders.

Unison is in a position to comment on the context within which the Commission must regulate, but we are not in a position to provide an opinion on the extent of the proposed increase. Some increase is clearly required as we observe the Commission is struggling for resources in some areas and timeliness of responses seems slow. Whether the full extent of the proposed increases is warranted is beyond our ability to make informed comment. We would encourage MBIE to carefully scrutinize the substance behind the Commission's budget bid to ensure it represents value-for-money for the ultimate payers – electricity consumers.

Specifically, we have observed that:

1. The Commission's enforcement function has been unable to keep up with providing timely enforcement decisions on quality breaches. In part, this may be because the Commission draws on a limited market for independent engineering expertise;

2. A promised enforcement guideline is still yet to appear, despite being on the Commission's work agenda for an extended period and repeated pleas from the ENA for the guideline to be made available as a matter of importance;

3. Commission Staff appear thinly stretched across activities and there seems to be a lack of continuity in Staff working on Part 4 matters. This hampers responsiveness to questions on matters of interpretation or original policy intents;

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4. The Commission has limited network engineering and operations knowledge sufficient for it to assess technical issues, which appears to have led to provider capture from an external consultant;

5. On occasion, analysis is not comprehensive in relation to the importance of the issue; and

6. There is limited substantive "Summary and Analysis" output.

With the increase in funding, the Commission states that it expects to achieve:

1. An increased level of effort and attention to performance monitoring and reporting, with a particular focus on network reliability and resilience;

2. Enhanced capability to set and enforce price paths;

3. Improve proactivity in compliance work;

4. Increase engagement with stakeholders, especially consumers and consumer groups; and

5. Reviewing rules to ensure fitness-for-purpose.

In the remainder of this submission we address the Commission's implied workplan and costings under the Commission's favored "bridging the gap" proposal.

Philosophy under-pinning the proposal

We are largely in agreement with the Commission's description of the changing energy landscape and the growing expectations on distributors to manage a more complex energy market environment, with improved engagement with consumers. How this environment translates into the Commission's work programme is the key issue at hand. There is limited detail on *how* the Commission intends to address these issues from a regulatory perspective.

The Commission's obligations are established in Part 4 and there are various "set-pieces" such as IM reviews, DPP resets, "summary and analysis" which the Commission needs to be resourced to meet, but there is an important issue to address in how the Commission goes about meeting those obligations, including its collaboration with other regulators especially in its outreach programme. Incentive regulation (and especially DPP regulation) was developed to avoid the situation of regulators having to develop detailed knowledge of the operations of regulated businesses, but instead creating a system of rewards/penalties for good/poor performance. How this factors into the Commission's approach is unclear.

The Commission rightly identifies that EDBs provide important infrastructure. The long-term interests of consumers are met when EDBs are providing resilient networks, are well-engaged with consumers and other stakeholders on meeting requirements of a more dynamic energy landscape, and are enabled by regulation to achieve this. The Commission must be a well-informed regulator and assist in creating the framework by which EDBs meet the interests of consumers and other stakeholders, but it is unclear from

the Commission's consultation paper on how far it intends on delving into the operational performance of EDBs to discharge its statutory obligations. Given the extent of the proposed budget increase, the implication is that EDBs may be expected to provide significantly more information about business operations and asset capabilities, which the Commission would then use to fulfill its Part 4 responsibilities.

If that is what is intended, then we would query whether that is in the intended spirit of the Part 4 regime, which is intended to be a relatively low cost regime. It needs to be recognised that if the Commission is intending to resource a much more detailed scrutiny of EDBs operations then it will not just be the additional costs of resourcing the Commission that is at stake, but the consequential impact on EDBs of responding to the Commission's requests for more information. We note that the Commission's recent DPP3 reset denied all non-exempt EDBs requests for additional expenditure allowances to manage a more complex business and legislative environment. If the Commission intends that more information is to be provided by EDBs in a form and level of robustness to meet a disclosure standard (generally requiring governance sign-off), then there will be a mis-match between what the Commission is funded to do and what the Commission has provided for in DPP allowances.

More generally, Unison submits that the Commission should not be seeking to insert itself into a senior management role by scrutinizing operational-level information, but approach at least some of its "summary and analysis" obligations from a governance level perspective. For example, if the Commission is interested in cyber-security resilience, rather than seeking specific detail on how EDBs may be managing cyber-security risks, the Commission could approach it by asking Governance type questions such as "Does the EDB have a specific Information Security Policy?", "When did the EDB last carry out an independent Information Security audit?," "Does the EDB adhere to a recognised standard for Information Security?". Such a governance-type approach would be lower cost to implement, but assist in illuminating interested stakeholders on the management effectiveness of EDBs in addressing risks and ensuring the resilience of networks. Without understanding how the Commission intends to enhance its performance monitoring and reporting, it is not possible to comment on whether the budget requirement is appropriate.

In a similar vein, we note the Commission's expressed interest in a significant expansion in its outreach activities. To a degree we support this. The Commission needs to be an informed regulator to ensure it is meeting the long-term aspirations of consumers, as well as having regard to the interests of stakeholders that are likely to have a growing interest in the services and performance of EDBs. But it will also be important that the Commission avoid "reinventing the wheel" or duplicate the engagement activities of other regulators, industry associations and the consumer engagement activities of the EDBs themselves. Leveraging existing forums and engagement processes should be encouraged, especially in collaboration with the Electricity Authority. We observe that the Commission has undertaken significant outreach activities with consumers in its deliberations on Aurora's CPP application. It will be of significant interest to all observers how the Commission's decision is affected by the feedback and views of consumers.[1] We observe that it is possible to expend substantial resources on consumer engagement, but translating that into actionable information to make better decisions is a real challenge. The

[1] We think it would be useful for the Commission to separately publish a review these outreach activities, so that stakeholders can learn from this experience. This is a growing area of practice for both distributors and regulators and is not an easy exercise to get right in terms of eliciting useful information and feedback, so any lessons will be invaluable.

consultation document does not provide the detail of how it plans to carry out its outreach activities, so this may be an area MBIE should explore with the Commission.

In summary, the Commission's consultation paper does not illuminate how it intends to use the additional resources to carry out its role, so it would be useful for MBIE to test with the Commission what overarching philosophy will apply in achieving the objectives of Part 4. In particular, we submit that MBIE should test the balance that the Commission envisages between development of incentive frameworks and mechanisms to adjust to a more dynamic energy environment, compared with expending resources on taking a more active stance in delving into businesses.

Input methodology review

The Commission has indicated its expectation is that the IM review would build on the first review and is likely to be much more focused in its approach. We agree. The rules currently in existence have been proved through a number of resets and have provided a stable, predictable environment. There are some critical, but narrow issues where the review will need to focus on, but we would be very surprised if more resources would be required compared with the previous IM review, especially in regard to the technical/economics aspects. The IMs focus on relatively technical/accounting and procedural issues, with the Commission retaining significant discretion over how those rules are applied in resetting DPPs. We think the more fertile ground for advancing regulatory arrangements for EDBs and GPBs will be in the application of the IMs in reset decisions, rather than substantial changes to the IMs themselves. We do note that the current method of determining an estimate of the cost of capital and how it is applied to determine revenues and the regulatory asset base is not seen as sustainable given the abnormalities occurring in interest rate markets. A similar budget as applied to the last IM Cost of Capital review will be required to address the cost of capital IM.

The Commission identifies that in the next IM review it would likely conduct a much more significant out-reach effort than in the previous review. We note that in the previous IM Review the Commission hosted workshops to cover issues including the changing energy landscape and a conference of experts on cost of capital matters. In our view, we are unsure of the benefits of attempting any broader outreach compared with the previous review. The workshops were attended by industry participants and technical consultants / advisors on generally technical matters. Consumers rely on the Commission as an expert regulator to make effective judgements on the matters covered by Input Methodologies and it is unclear how an expanded outreach programme will enable the Commission to make better decisions. We think MBIE could probe this area with the Commission further in settling on a budget amount for outreach during the IM process.

Concluding comments

Overall, we support an increase in the Commission's budget to ensure it can be effective in meeting its statutory duties. But how much of an increase we do not know. A well-informed regulator with capable, sufficiently resourced staff is essential in delivering good outcomes for consumers and maintaining investor confidence in the regulated providers.

We would therefore encourage MBIE to undertake a detailed scrutiny of the underlying plans to ensure that they:

- are the most efficient use of electricity consumers' money;
- use resources effectively (for example, judicious use of expert economic and technical consultants may deliver more effective outcomes); and
- represent a realistic assessment of what is required to deliver regulatory outcomes that enable EDBs to meet stakeholders' needs. The energy market environment is likely to be much more dynamic than in the past as New Zealand responds to the challenges of decarbonisation.

We also recommend that MBIE also consider its own resources to enable it to hold the Commission to account in delivering the outcomes that it suggests will be achieved with an increased budget. Setting meaningful KPIs and publicly reporting on the Commission's achievements will be useful in ensuring value for money for electricity consumers.

I hope that you find these comments helpful. I would be happy to discuss any of our comments further.

Yours sincerely

Nathan Strong
General Manager Commercial