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Feedback to open letter on ensuring our energy regulation is fit for purpose

Mercury welcomes the opportunity to provide feedback to the Commerce Commission on its open letter on 'Ensuring our energy and airports regulation is fit for purpose'.

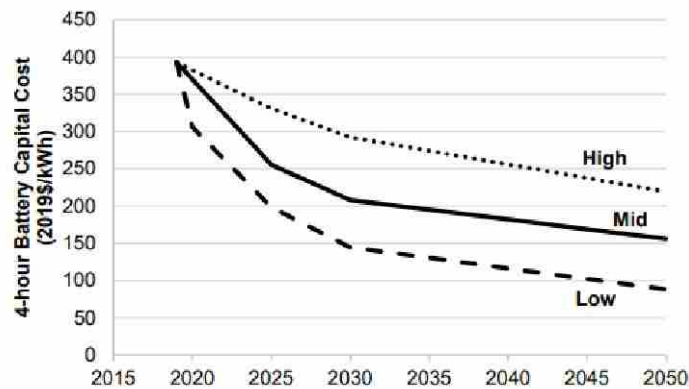
The energy sector faces a significant challenge in the next few decades to support the achievement of New Zealand's stated climate change goals and objectives. This requires the maintenance of existing supply infrastructure, as well as delivering new sources of grid and distributed scale generation, storage and integrating known and emerging innovative technologies. The industry is responding to this challenge with significant capital currently being deployed.

Ensuring regulatory frameworks remain open and flexible to new technologies will be essential to support the transition to a low carbon economy. The outlook for example for the declining costs of battery storage (see figure 1) has significant implications for distribution services both as potential alternative investments to conventional 'poles and wires' and in terms of transport electrification. Distributed storage in the form of electric vehicles for example will create new challenges for distributors who will need to work collaboratively across the supply chain to understand how best to manage and integrate this new technology to ensure the future reliability of their networks.

As a principle Mercury has long supported open, transparent and competitive markets to deliver greater flexibility into distribution systems from new technologies in a least cost manner for consumers. This is a current focus of the Electricity Authority's (EA) IPAG process. The industry has made progress to establish clear data sharing arrangements via bilateral agreements with distributors and through the EA's Default Distribution Agreement process. However, retailers do not contract for or hold all forms of data that distributors may find valuable to ensure the reliability of their networks, such as voltage or real-time outage information, which distributors must contract with Metering Equipment Providers (MEPs) to obtain.

Mercury understands that some distributors have made requests to the Commerce Commission to recover the reasonable costs of procuring these data services from MEPs but that the Commission was not inclined to allow this outcome. Mercury would be interested to understand more of the context around this issue as there are likely to be consumer benefits from allowing distributors to recover such costs both in terms of improved reliability and through enabling the provision of transparent information to the market for flexibility services within distribution networks. On the latter point Mercury is aware for example that and in some overseas jurisdictions, distributors are encouraged to provide information in the form of heat maps on where constraints are within their networks that market participants can then put forward solutions. Mercury would support a similar approach being implemented in a light-handed manner in New Zealand that balances costs to consumers noting that markets for flexibility are just emerging and will likely take some time to develop.

Figure 1. Battery projection costs for 4-hour lithium ion systems¹



Mercury supports the work the Commission has undertaken to date to evolve the distribution regulatory settings to promote a level playing field for investments in new distributed technologies and enable competition. It will be important that these settings are reviewed periodically to ensure they remain fit for purpose as the competitive market for distributed energy resources scales up.

Mercury agrees that a key focus for the distribution regulatory framework is to ensure distributors have in place robust asset management plans informed by accurate assessments of the state of current distribution infrastructure. While climate change policy is driving a focus on new technology, Mercury does not consider that the core focus of the ILMs on sound asset management to ensure consumer reliability will diminish in the coming decades. Recent experiences with Aurora’s customized price-quality path indicate that there can be material long-term disbenefits for consumers where the focus on sound asset management processes are overlooked. We support the Commission to continue its solid work to improve reporting and information in this area and enforce best-practice asset management among distributors.

The open letter also raises questions around how the regulatory framework may need to adapt for gas networks given government policy and recent draft advice from the Climate Change Commission. Gas infrastructure assets have considerable economic lives. It would be reasonable to assume that where policy sets limitations on the ability to grow new gas connections that capital holders will be concerned by the ability to earn a long-term return on the cost of capital on existing assets and seek to defer as long as possible further investment to maintain and/or grow their networks. This will likely result in reduced service and quality outcomes for consumers over time and increased costs for those remaining connected to the network.

Mercury notes the recent comment from the Energy and Resources Minister² that the government needs to balance the phase-out fossil fuels with ensuring consumers can still meet their energy requirements as gas assets could play a role in supporting decarbonisation through distributing alternative renewable fuels such as green hydrogen and biogas. This has implications for the regulatory reset process to determine how best to strike the balance between reducing costs for consumers in the short term versus maintaining incentives for continued investment in the gas network to preserve longer term decarbonisation options. Mercury agrees there is value in preserving long term options given emissions reductions will need to be delivered over a 30-year period and there is significant scope for technological advances that could deliver emissions abatement at much lower cost in the future.

Overall Mercury’s initial view is that current input methodologies are largely fit for purpose and are unlikely to provide any material or unforeseen impediments to transitioning to a low carbon economy. While there are areas where the frameworks could be enhanced to promote this outcome, ensuring robust asset management practices should continue to remain a key focus.

¹ Cole, Wesley, and A. Will Frazier. (2020). Cost Projections for Utility-Scale Battery Storage: 2020 Update. Golden, CO: National Renewable Energy Laboratory. NREL/TP-6A20-75385. <https://www.nrel.gov/docs/fy20osti/75385.pdf>

² Rood, E. (19 May 2021). Woods softens stance on gas. Energy News. <https://www.energynews.co.nz/news/gas-generation/93958/woods-softens-stance-gas>



If you have any questions on this feedback please contact me at john.bright@mercury.co.nz

Your Sincerely,

A handwritten signature in black ink, appearing to read 'John Bright', written in a cursive style.

John Bright
Regulatory Strategist

