

Energy sector cross-submission to the Commerce Commission

8 August 2023

Sector participants are committed to collective action to enable Aotearoa's energy transition

The energy sector stands ready to support Aotearoa New Zealand's transition to a low-carbon economy. As part of this support, in 2022 a group of sector participants commissioned an independent whole-of-sector view articulating the best route to transition to a low-carbon energy system¹.

We recognise collective action will be critical to delivering this whole-of-sector change, and have been progressing discussions to enable this future with wide sector representation.

Participants in these discussions are developing a united sector view on the key priority topics critical to setting up Aotearoa New Zealand for a successful decarbonisation transition. One of the first actions identified by the group is to:

Drive a unified voice on the importance of improving investment incentives and funding to networks via Commerce Commission regulatory settings, recognising that without scaled network investment, there is a risk of a bottleneck in achieving electrification goals.

The focus of this letter to the Commerce Commission (the Commission) is to reiterate some of the key points of alignment between industry participants² in relation to network investment and funding, as a first step towards driving this unified voice.

The electricity sector will deliver significant, long-term benefits to consumers through the transition

There is widespread recognition that the scale of the investment challenge facing the electricity sector over the coming decades is unprecedented – in particular investment in transmission and distribution network infrastructure.

In the modelling undertaken for sector participants in 2022, BCG and Concept estimated that in the 2020s alone, \$42bn of new investment will be required, of which \$22bn is expenditure on distribution network infrastructure, and \$8bn in transmission networks. Over the three decades to 2050, total investment in distribution networks is estimated to be \$71 bn.

The benefits to consumers of increasing electricity consumption and reducing use of fossil fuels will be significant. Electricity Networks Aotearoa recently commissioned Sapere to examine the impact of electrification on the overall consumer 'energy wallet'³. Their analysis showed that even

¹ BCG (2022). *The Future Is Electric: A Decarbonisation Roadmap for New Zealand's Electricity Sector*. Available online at <https://www.bcg.com/publications/2022/climate-change-in-new-zealand>

² Industry participants that have been progressing sector-wide discussions and that express support for this letter include Contact Energy, Electricity Retailers' Association New Zealand, Mercury, Top Energy, Transpower, Vector, Nova Energy, Unison Networks, Manawa Energy, Orion, PowerCo, Lodestone Energy, Wellington Electricity, Electricity Networks Aotearoa, Independent Electricity Generators Association, Flick Electric, Far North Solar Farm, Helios Energy, Hiringa and First Gas.

³ Sapere (2022). *Total Household Energy Costs NZ*. Available online at <https://www.poweringup.org.nz/updates/total-household-energy-costs-will-reduce-with-electrification/>

with the increased investment in electricity infrastructure, supporting increased consumer expenditure on electricity consumption, consumers are likely to save hundreds of dollars per year on their bills across all energy consumption (including gas and transport fuels).

By 2050, BCG estimates the electricity sector would be delivering over 25m tonnes of emissions reductions, per year, compared with current levels.

The real prize for the sector, and consumers, is two-fold:

- ensuring that the future electricity system is operated in as 'smart' a way as possible (BCG's assessment was that the 'smart system' would deliver the greatest benefits to consumers, by minimising the quantity of new infrastructure required); and
- ensuring that this quantity of infrastructure is delivered as efficiently as possible, at least cost to consumers.

Funding and financeability must be a core focus of any regulator's decision-making

Clearly, the Input Methodologies (IMs), along with the electricity Code, have a huge role to play in delivering these outcomes for consumers.

Within this context, and the huge size of the prize, this IMs review comes at a crucial time for the sector. The 2020s are the critical decade.

The costs for under-investing, for both capacity and resilience, will be very high. The required investment must be delivered on time at the very latest, but network owners often have little visibility of consumers' plans and can be required to develop connections, or upgrade their networks, at short notice. The regime must ensure it is not placing undue constraints on parties' ability to make such investments.

As illustrated above, the scale of the investment challenge is unprecedented. Critical to networks' ability to meet their customers' evolving needs is their capacity and ability to fund this investment. This investment will only be made if it is attractive to shareholders, and financeable. With close to \$100 bn of investment in transmission and distribution networks required over the next three decades, any constraints on funding, and/or minor increases in the cost of that funding, will end up increasing the burden on consumers materially.

Section 53P (8) (a) of the Commerce Act provides for the Commission to consider both the impact on consumers of significant price shocks, and the ability of networks to fund investment. Both are of critical importance at a time when investment is scaling up right across the sector, and the Commission (and other Government agencies) must ensure the appropriate balance is struck.

As much as monitoring consumers' ability and willingness to pay is important, the challenge of attracting this much capital to the sector cannot be underestimated. The financeability of investment must be a core consideration of any regulatory regime. Therefore, the Commission must ensure that this is explicitly accounted for in its decision-making – just as it should be for any decisions made by the Electricity Authority that impact long-term investment incentives for other long-lived infrastructure, such as generation.

A relatively straightforward solution would be for the Commission to add a financeability test to the IMs, ensuring the cashflows of the regulated entity are sufficient to support the investment required and enabling the appropriate balance between affordability and investment funding to

be struck. The UK regulator, Ofgem, provides a useful precedent, and is transparent about the financial ratios it monitors.

Relatedly, the importance of the regime ensuring investment is efficient and costs to consumers are minimised is equally relevant to connection costs. As the Commission notes, new and upgraded connections to networks are a critical part of electrifying the economy. Network companies should continue to be encouraged and incentivised to explore alternative arrangements with consumers who are willing to opt into, and accommodate, “non-standard”, lower-cost connections. These could come through (for example) the consumer flexibly managing their demand in concert with the network company, as we are seeing emerging with electrified transport charging, or providing their own alternative (non-network) form of resilience.

Such approaches are particularly relevant for the cases referred to above in which a network company may have little notice of a consumer’s intention and must respond as quickly as they can. Allowing for flexibility in connection approaches provides an enabler for timely response.

The parties supporting this letter would be very happy to discuss these points with you.