ERANZ CROSS-SUBMISSION TO THE COMMERCE COMMISSION ON INPUT METHODOLOGIES FOR EMERGING TECHNOLOGY

18 AUGUST 2016

Electricity Retailers' Association of New Zealand
PO Box 25596, Featherston Street, Wellington, 6146

Contents

Executive Summary

The Commerce Commission (the Commission) has received 35 submissions responding to its input methodologies review (IM Review) draft decisions papers. We focus on submissions commenting on the Commission's IM Review Paper on the Future Impact of Emerging Technologies in the Energy Sector. These submissions have provided a useful range of views about the regulatory treatment of emerging technologies.

This cross-submission considers the key arguments put forward by other stakeholders in their submissions, and provides context and evidence in relation to these arguments, to assist the Commission with its consideration of the different viewpoints.

In particular, we would like to clear some apparent misunderstandings with respect to the approaches being taken in overseas jurisdictions and the 'calibrated regulation' proposed in work commissioned by the Electricity Networks Association in Australia. In particular, the ERANZ proposal is consistent with the approaches being taken by regulators in the United States, Europe, and Australia, where various safeguards are used to ensure competition. These regulators have also been motivated by the very same concerns that ERANZ expressed in its 4 August submission.

In response to specific comments, we provide further evidence that in order to support the long-term interests of consumers:

- Investment in storage assets should not be included in the Regulatory Asset Bases
- The argument for accelerated depreciation is ill-founded
- Approaches that allow for Electricity Distribution Businesses (EDBs) to competitively procure emerging technologies should be encouraged.

We note that references to economies of scope in many submissions are made at a high level, without an attempt to explain how they are derived or how they can be lost. In response, we provide a breakdown of economies of scope to EDBs into components and consider whether each component would be available under arrangements proposed in our 4 August submission.

Consistent with proportional regulatory responses, we suggest that regulatory arrangements should allow for different business models so long as they compete on a level-playing field.

Introduction

The Electricity Retailers Association of New Zealand (ERANZ) welcomes the opportunity to provide this cross-submission on submission on the Commerce Commission's (the Commission) Draft Decision Paper on the Future Impact of Emerging Technologies in the Energy Sector.[1]

ERANZ's 4 August submission emphasised that the Input Methodologies (IMs) need to include safeguards to ensure that emerging technologies develop in a competitive market, consistent with the long-term interests of consumers.

This cross-submission addresses key arguments made by other stakeholders in relation to the future impacts of emerging technologies in the energy sector. We provide further evidence in relation to these arguments, so that they can be considered by the Commission in light of this additional evidence or context. We are encouraged by the involvement of different stakeholders on this issue as it is important that various viewpoints are understood. Our submission is intended to provide additional context to these viewpoints and provide evidence as a basis for the Commission's assessment of different arguments put forward.

We have arranged this evidence under the following key themes:

- ERANZ's proposed approach is consistent with other jurisdictions internationally (addressing concerns raised by Vector)
- ERANZ's proposed approach is consistent with 'calibrated regulation' (addressing Vector's interpretation of the work of Synergies Economic Consulting and Yarrow for the Energy Networks Association in Australia)
- Any proposed changes must support the long-term interests of consumers (addressing different suggestions made by PowerCo, Alpine Energy, The Electricity Networks Association (ENA), PwC, and Vector)
- Regulatory risk is best addressed by a level playing field (addressing points made by certain Electricity Distribution Businesses (EDBs)).

Our Appendix provides further information on the Australian Energy Regulator's (AER's) Draft Ring-fencing Guidelines.

[1] Available at: http://www.comcom.govt.nz/regulated-industries/input-methodologies-2/input-methodologies-review/emerging-technology/

ERANZ's approach is consistent with international jurisdictions

ERANZ wishes to first respond to Vector's submission that "very few jurisdictions" are presuming network involvement in emerging technologies will obstruct the development of a contestable market.[2] This comment is made as part of a point about jurisdictions recommending evidence based regulation.

Vector is wrong both in fact and its interpretation of the approaches taken in other jurisdictions. In fact, the world's most advanced economies have all one way or another sought to ring-fence the competitive provision of emerging storage services from the risk of monopolisation by distribution and transmission network owners. Depending on the nature of the regulatory regime, this may take different forms.

California expects competitive procurement to drive energy storage investment

California is interesting because it is one jurisdiction where utilities have been explicitly mandated to provide a specified amount of electricity storage at the transmission, distribution, and behind-the-meter level. The California power market is built around vertically integrated utilities, and the regulator has allowed these utilities to own up 50 percent of all storage across each grid domain. However, all storage must be procured competitively. The goal of the 50 percent ownership limit and procurement requirements is to ensure viable market options are not pre-empted. Moreover, the California Public Utilities Commission noted:

> *"Although we allow utility ownership of energy storage systems, we believe that the primary means for procuring energy storage systems should be through competitive solicitations. Thus, an IOU* [Investor-Owned Utility] *proposing utility-owned storage in any grid domain shall pursue a competitive process … Applications for approval of utility-owned energy storage systems procured outside of the RFO* [Request For Offer] *process shall be evaluated on a case-by-case basis. In the application the IOU must make a showing that holding a competitive RFO is infeasible"*[3]

New York also believes utility participation needs to be closely managed

In New York, the State Government is undertaking an ambitious redesign of its approach to electricity regulation known as Reforming the Energy Vision (REV). The New York Public Service commission has noted:

> *"As a general rule, utility ownership of DER* [Distributed Energy Resources, which includes storage] *will not be allowed unless markets have had an opportunity to provide a service and have failed to do so in a cost-effective manner."*[4]

And critically:

> *"We are persuaded that unrestricted utility participation in DER markets presents a risk of undermining markets more than a potential for accelerating market growth. … A basic tenet underlying REV is to use competitive markets and risk based capital as opposed to ratepayer funding as the source of asset development. On an ex ante basis, utility ownership of DER conflicts with this objective and for that reason alone is problematic.*

[2] See paragraph 84 of Vector's Submission.

[3] Public Utilities Commission of the State of California, Decision 13-10-040 October 17, 2013 "Decision Adopting Energy Storage Framework and Design Program", pages 51-52.

[4] State of New York Public Service Commission, Case 14-M-0101 "Proceeding on Motion of the Commission in Regard to Reforming the Energy Vision, Order Adopting Regulatory Policy Framework and Implementation Plan" (issued February 26, 2015), page 68.

Our concerns are compounded by the observation made by Staff and others that, because of their incumbent advantages, even the potential for utility ownership risks discouraging potential investment from competitive providers. Markets will thrive best where there is both the perception and the reality of a level playing field, and that is best accomplished by restricting the ability of utilities to participate. Finally, REV provides utilities the opportunity to be both the "wires" company and the platform that enables a market for DER resources."[5]

However, there are four exceptions to the Public Service Commission's general rule:

"1) procurement of DER has been solicited to meet a system need, and a utility has demonstrated that competitive alternatives proposed by nonutility parties are clearly inadequate or more costly than a traditional utility infrastructure alternative;

2) a project consists of energy storage integrated into distribution system architecture;

3) a project will enable low or moderate income residential customers to benefit from DER where markets are not likely to satisfy the need; or

4) a project is being sponsored for demonstration purposes."[6]

In granting these four exceptions, the regulator has noted that it anticipates utility ownership of DER to be the exception rather than the rule. Where assets are included in the Regulatory Asset Base (RAB), cost-recovery would be limited to actual cost: the utility will not be allowed to earn additional market revenue from the services provided by the assets. Procurement would also be subject to information disclosure, to enable competitive service providers to challenge the exceptions under which a procurement may be undertaken. The Public Services Commission also stated a willingness to review its ruling on utility ownership if there were market changes. Finally, the regulator also acknowledges that ownership through appropriately ring-fenced affiliates does not present the same concerns as direct utility ownership.[7]

European regulators expect unbundling requirements to extend to storage technologies

Article 26 of European Union (EU) Directive 2009/72/EC requires unbundling of distribution networks across the EU. Unbundling at the distribution level means legal, accounting, and functional unbundling to guarantee the operational independence of distribution services from other activities in the system.[8]

The application of the 2009 EU Directive to storage technologies lacks clarity. EU member states have generally regarded storage as a generation system. This interpretation effectively excludes ownership of storage at the transmission level, but not necessarily at the distribution level.[9] This ambiguity has prompted the Council of European Energy Regulators (CEER) to

[5] "Proceeding on Motion of the Commission in Regard to Reforming the Energy Vision", page 67. Note – in reaching this decision, the regulator gave weight to the number of existing participants in DER markets, which is currently not the case in New Zealand.
[6] Ibid, page 70.
[7] Ibid, pages 66-67, 70-71.
[8] Giorgio Castagneto Gissey, Paul E. Dodds, Jonathan Radcliffe "Regulatory barriers to energy storage deployment: the UK perspective", page 5.
[9] Directorate General for Internal Policies, European Parliament "Energy Storage: Which Market Designs and Regulatory Incentives Are Needed?" (October 2015), page 30.

examine the future regulatory treatment of electricity storage. The Council, which represents 27 regulators, has concluded the following:

> *"We propose to use a regulatory toolbox for NRAs* [National Regulatory Authority] *to address a number of non-core activities, or "grey areas", where DSOs* [Distribution System Operators] *may participate in activities but where there are concerns. These grey areas include energy efficiency advice, the extent of involvement in flexibility and storage, and engagement with end consumers.* ***The more that DSOs are involved in non-core activities, the greater the need for regulatory control or unbundling***[10]

And:

> *In the changing energy sector with new markets and services, the consultation document stated that there might be a need for further regulatory and legal requirements on DSOs with a vertically integrated undertaking (VIU) in addition to the current unbundling rules****. If the DSO takes on new roles, sufficient controls and structural prerequisites will be required to ensure that DSOs do not use access to data to gain commercial advantage or create market distortion.***
>
> *In our consultation paper, full ownership unbundling is considered to be the strongest model for the independence of the DSO. But other models can also ensure transparent and independent decision making and equal treatment of all DSO stakeholders, as long as sufficient ring-fencing, regulatory monitoring and oversight are in place."*[11]

In a parallel consultation, the Agency for Cooperation of Energy Regulators has also found that:

> "*New services will appear which will enable consumers to engage more fully and effectively in the energy market. These services may relate to demand-side energy management or to other energy services, and may be coupled with non-energy services.* ***These new markets should not be foreclosed by existing energy players, and in particular by the activities undertaken by incumbent monopoly DSOs. In this regard, unbundling rules must be respected.*** *DSOs may use smart grid solutions, including flexibility services, to optimise the efficient operation of the network ultimately to the benefit of consumers. The regulatory framework should enable the introduction of new services and efficient cooperation among market players including DSOs and should facilitate the development of efficient network solutions, including smart grids."*
>
> …
>
> *"CEER will develop a "toolbox approach" for the regulation of DSOs, to be adopted flexibly according to nationally prevailing conditions, including a set of consistent options to ensure an adequate level of business separation of core DSO functions from potentially competitive activities."*[12]

These reports illustrate both the importance placed by European regulators on preserving efficient and competitive markets. They recognise the wide variety of potential storage technologies that are available, and that there should be competitive neutrality between all forms of storage and all participants in storage markets.

---

[10] Council of European Regulators "The Future Role of DSOs: A CEER Conclusions Paper" (13 July 2015), page 6.
[11] Ibid, page 14.
[12] Agency for the Cooperation of Energy Regulators "Energy Regulation: A Bridge to 2025 - Conclusions Paper" (19 September 2014), page 22.

Consistent with the calibrated approach advocated both by ERANZ and the Synergies Economic Consulting and Professor Yarrow report (discussed below), European regulators are moving towards an approach which seeks to manage network participation by separating potentially competitive activities from core monopoly services.

We note, each country has its own slight variation on the interpretation of the EU rules but all honour the separation imbedded in the EU rules:

- **Belgium**

  Belgium permits network ownership of storage assets, but only as a last resort. Under Article 9(1) of the Belgian Electricity Act, the conditions for network ownership of storage are:

  (i) *"the electricity is generated for balancing purposes only, with an explicit prohibition for commercial purposes;*
  (ii) *the stored electricity is called upon as a last resource;*
  (iii) *under the form of negotiated drawing rights;*
  (iv) *to the limit of the power needed for ancillary services;*
  (v) *upon the prior approval of the regulator;*
  (vi) *after having completed all relevant procedures for calling upon the market."*[13]

- **United Kingdom (UK)**

  In the UK, there are restrictions on network ownership of storage due to unbundling rules. Storage is treated like generation, which effectively blocks distributor ownership and operation of storage systems, subject to *de minimis* rules.

  The UK's largest owner of distribution networks, UK Power Networks, has commissioned a study into the regulation of storage in the UK. To be consistent with the strong focus on contestability within the regulatory framework, the study recommends competitive procurement and ring fencing of storage services:

  > *"Promote contestability in provision of storage*
  >
  > *Where distribution businesses identify the potential for storage (or other non-conventional solutions) to deliver network services, the licensee should be encouraged to source solutions through competitive means in the first instance, with DNO* [Distribution Network Operator] *provision a fall-back option in the event that appropriate third party provision is not forthcoming.*
  >
  > *Ensure non-distortion of competition*
  >
  > *Pending the potential future evolution of the distribution business role to encompass DSO activities, trading activity for storage assets with DNO involvement needs to be handled via a third party. However, there appears to be no reason why an affiliate of the distribution licence holder cannot be the third party under the approach where storage is a distinct licensed activity"*[14]

[13] stoRE Project "European Regulatory and Market Framework for Electricity Storage Infrastructure Analysis and recommendations for improvements based on a stakeholder consultation" (June 2013), p 28.
[14] Simon Bradbury, John Hayling, Panagiotis Papadopoulos and Nick Heyward "Smarter Network Storage Electricity Storage in GB: SNS 4.7 Recommendations for regulatory and legal framework (SDRC 9.5" (September 2015), section [4.3].

…

"In cases where competitive provision is not forthcoming or solutions are offered that do not meet the distribution business's needs, then the DNO itself has the ability to progress provision of storage assets to meet its requirements. This means that the DNO takes on a 'provider of last resort' role."[15]

In addition, available examples of network procurement of emerging storage technologies in the UK and Ireland all appear to be on a market-orientated basis. For example, similar to Transpower's Demand Response Programme, EirGrid, is developing a programme, due to start in 2017, that will allow energy storage companies to provide grid services via a system of competitive bids. In Scotland, one distributor purchases the services of a grid-scale battery through a congestion management contract. In 2014, the UK National Grid held its first capacity market auction, which was also open for energy storage facilities.[16]

- **Italy**

  In the context of urgent grid constraints, Italy has allowed distribution and transmission to own and operate batteries, subject to regulatory oversight. However, investment must be justified through a cost-benefit analysis showing that the storage system is most cost-effective than a lines upgrade, and reviewed by the regulator. The network is not permitted to receive remuneration higher for the storage system than the (measurable) cost of alternative solutions.[17] Moreover, storage systems are also classified as generation and are therefore subject to metering and dispatch requirements.

The Australian Energy Regulator has recognised that cross-subsidies and discrimination justify ring-fencing of contestable services

Our 4 August Submission emphasised the decision of the Australian Energy Markets Commission (AEMC) to require ring-fenced ownership of behind-the-meter storage. The Australian Energy Regulator (AER) has now also released a draft decision on emerging technologies, which proposes ring-fencing of contestable services from monopoly services.

The AER's explanatory document outlines similar concerns to those expressed by ERANZ in our 4 August submission. Preventing cross-subsidies and discrimination in favour of monopoly affiliates are key rationales for the current separation between contestable and monopoly services in the electricity market. It is therefore critical that regulatory frameworks and instruments should continue to be guided by these concerns in evolving circumstances. Just as the AER has applied this reasoning to updating ring-fencing guidelines in Australia, we believe the Commission should do the same for the IMs in New Zealand.

In particular, the AER has noted that:

Ring-fencing protects the long term interests of consumers by avoiding cross-subsidies that could undermine the efficient costs of regulated services provided by DNSPs [Distribution Network Service Provider]*. This aligns with the National Electricity Objective (NEO). Ring-fencing also limits the ability of a DNSP to discriminate in favour of its own affiliates (related bodies corporate and other service providers). Ring-fencing therefore*

[15] "Smarter Network Storage Electricity Storage in GB", page 38.

[16] Directorate General for Internal Policies, European Parliament "Energy Storage", page 31.

[17] European Commission Directorate-General for Energy "The future role and challenges of Energy Storage", page 30.

protects the long term interests of consumers more broadly by promoting competition in competitive markets. For example, a DNSP may be able to provide non-regulated services and possibly gain an advantage over other service providers through its provision of regulated services. Ring-fencing aims to prevent this. Ring-fencing levels the playing field in competitive markets by seeking to eliminate the advantage a DNSP or its affiliates may otherwise have in providing services.[18]

Overall, ERANZ's proposals are therefore entirely consistent with emerging international practice

The views expressed by experienced regulators indicate that Vector is wrong in interpreting the evolving thinking in international jurisdictions. Regulators are not waiting for the emergence of the market to decide what to do and have recognised that waiting without setting clear rules risks waiting until it is too late.

We do, however, acknowledge that the issue of network ownership of emerging technology is one that regulators around the world, including the Commission, are grappling with at this very time. We note that all leading regulatory jurisdictions are motivated by the desire to avoid unnecessary intervention and consider the incentives that different regulatory arrangements create and what this is likely to mean for developing competitive markets.

[18] Australian Economic Regulator "DRAFT Ring-fencing Guideline: Explanatory statement" (August 2016), page 1.

ERANZ's approach is consistent with 'calibrated regulation'

Our proposed approach is not only in line with the international trends, it is consistent with the advice commissioned by the Electricity Networks Association in Australia (ENA Australia) and the positions publicly expressed by the ENA Australia on optimal integration of emerging technology within the regulatory framework.

Synergies Economic Consulting and Professor Yarrow's Report for ENA Australia

Vector's submission narrowly reports Professor Yarrow and Synergies Economic Consulting's report.[19] In fact, that report, commissioned by ENA Australia, provides a balanced discussion of both the risks of imposing restrictions and the need to have safeguards against monopoly market power. Vector quotes only one part of the discussion. The options that report puts forward include the kinds of safeguards we have proposed, reflecting that there the need to safeguard against the exercise of monopoly market power ultimately needs to be addressed.

Professor Yarrow and Synergies Economic Consulting's report states there is a:

> *"fundamental trade-off in determining the best regulatory approach [between]…the cost of policing business conduct, including the costs that policing imposes...[and] the benefits that can be expected to derive from greater competition."*[20]

The report suggests that regulatory approaches need to 'calibrated' or proportional to the circumstances. They introduce the concept of a "differentiated rule book" stating that:

> *"The extent to which a particular set of rules supports competitive neutrality and non-discrimination might then depend upon, or be calibrated against, the extent to which a particular network business's choices raise of lower policing costs and the risks of anti-competitive behaviour."*[21]

Being well calibrated (appropriate and proportionate) is judged in relation to the:

> *"likely implications for the long-term interests of consumers, given feasible, alternative regulatory arrangements."*[22]

Professor Yarrow and Synergies Economic Consulting's report considers how calibrated regulation could operate in Australia, identifying similar potential arrangements to those that ERANZ propose:

> *"In the Australian electricity market, it might be feasible, for example, to adopt a regulatory rule-book that provided for:*
>
> - *network business that remained content to avoid participating in the competitive segments (or who limited their involvement substantially) might remain under broadly current arrangements;*
> - *distribution businesses that adopted a split structure, separating into two business units under a common ownership – a distribution network assets business and a*

[19] See paragraphs 91, 104, 105, and 114 of Vector's submission.

[20] Pages 4-5 of "Applying the Hilmer Principles on economic regulation to changing energy markets", Synergy Economic Consulting and George Yarrow for ENA Australia, April 2016. Available at: http://www.ena.asn.au/sites/default/files/hilmer_principles_in_changing_energy_markets_040416.pdf

[21] Ibid, paragraph 4 on page 7.

[22] Ibid, paragraph 5 on page 7.

distribution system operation business (such as are emerging in the US) – might operate under a regulatory model more akin to telecommunications; or

- *network businesses that decided to participate in contestable market under their current form might be offered a set of rules with a much greater emphasis on accounting separation, information disclosure and ring fencing, perhaps necessitating greater regulatory compliance costs, but with greater latitude to compete to offer services to customers."*[23]

In ENA Australia's response to the AER's Ring-fencing Guideline Preliminary Positions Paper, subsequently picked up on this need for an appropriate balance when stating "The challenge is to strike an appropriate balance so that networks do not exercise undue power. To this end, some form of ring-fencing is appropriate."[24]

[23] "Applying the Hilmer Principles", page 8.

[24] Page 3 of ENA Australia's response to the AER's Ring-fencing Guideline Preliminary Positions Paper. Available at: http://www.ena.asn.au/sites/default/files/20160530_ena_submission_on_aer_ring_fencing_preliminary_positions_paper.pdf

Any proposed changes must support the long-term interests of consumers

Submitters proposed extensions to certain proposals in the Commission's Draft Decision, and in some cases proposing different approaches. We comment on three key proposals made by submitters: what should be part of the RAB, accelerated depreciation, and the regulation of opex.

What should be part of RAB

PowerCo proposes that where emerging technologies are used to deliver a regulated service, they should be able to be included in the RAB.[25] However, storage assets can perform three main functions: market balancing, network optimisation, and the enhancement of renewables (that is, an energy trading function). We do not underestimate the importance of storage in network optimisation. The problem is that if network businesses are allowed to include investments in storage assets in their RAB, consumers will pay for the entire asset through the monopoly network charges as if storage assets only provide this network optimisation service. Consumers will then pay again for other services that network owners supply to the market. However, if storage services are provided competitively, consumers will pay for the value of each service, without paying multiple times. Hence, our objective is to create an environment where EDBs can take full advantage of network optimisation, but do so without distorting the market and in a way that is in the long-term interests of consumers.

Both Vector and PowerCo's submissions support the importance the Commission has assigned to ensuring that economies of scope are able to be achieved. Vector raise this in the context of ensuring that regulatory approaches are proportionate. In order to understand how different proposals may impact on the ability to realise economies of scope it is useful to unpack what we mean when using this term.

In practice, economies of scope may be derived from:

- Using the capabilities that EDBs have developed for their regulated business to deliver unregulated activities
- Ensuring that the assets that can provide multiple services are utilised fully.

ERANZ's proposal (in our 4 August submission) allows these economies of scope to be achieved. A form of ring-fencing we propose would not in any way stop EDBs from utilising their capabilities effectively. Our proposal will also ensure that emerging technologies such as battery storage are used effectively to deliver the multiple functions they can assist with. Further, there may be economies of scope that others involved in the electricity industry can bring, leveraging their own capabilities, but that they will not if they must compete with distributors that can cross-subsidise their activities in competitive markets.

The ability to leverage economies of scope under our proposal is exemplified by the recently announced partnership between the GreenSync and Victorian utility United Energy (UE). Under this partnership, GreenSync will engage and incentivise households, businesses, and community organisations on the lower Mornington Peninsula to help reduce or shift their electricity usage, including through the use of solar PV and energy storage systems. This will allow UE to delay having to build new infrastructure to meet infrequent high demand in the

[25] See paragraphs 276-281 of PowerCo's submission.

area.[26] This project is being undertaken with the ring-fenced regulatory model of the type we are advocating.

We urge the Commission to get behind the headline of "economies of scope" and to consider carefully what such economies are and how they are achieved.

In addition, we underscore our legal advice, which has concluded that that behind-the-meter storage falls outside of the definition of lines service in New Zealand legislation. For this reason alone, this type of storage technology should not be included in the RAB.

Accelerated depreciation

Alpine Energy, ENA, PwC, and Vector support the Commission's proposal of allowing EDBs to apply for shortened asset lives (or accelerated depreciation) but disagree with the proposed cap of limiting this to at most a 15 percent reduction in asset lives.[27] Some also suggest this should apply to all EDBs. In contrast, Contact, Meridian, and the Major Electricity Users' Group (MEUG) do not support the proposal to accelerate depreciation. We also note MEUG's comments:

> *"MEUG supports tightening of the [cost allocation] thresholds as a minimum and will be interested in the views of retailers that are more incentivised and therefore informed on the tension at the boundary between regulated services and workably competitive markets."*[28]

We believe that the issue of accelerated depreciation is in fact unrelated to the regulatory treatment of emerging technology.

If new technology were to lead to the early retirement of distribution assets (which is a big if), then it would do so regardless of whether new technologies are introduced competitively or by the distribution companies themselves. In fact, more efficient, unsubsidised market entry would likely leave fewer assets stranded.

It is difficult to see how allowing significant reductions in asset lives and applying this to a wider set of entities would be in the long-term interests of consumers.

Regulation of Opex

ERANZ is supportive of Vector's suggestion that opex allow for EDBs to procure services from the market.[29] If storage services are to be procured as opex, long-term contracts should be respected and EDBs should have the assurance that they would not be disallowed in future re-sets. However, for this to work, there has to be assurance of open and competitive procurement. This is not currently required and evidence provided by Asplundh suggests that this kind of competitive procurement is not observed in practice where there are options to procure internally.[30]

---

[26] See: http://www.greensync.com.au/greensync-partners-with-united-energy-for-landmark-asset-deferral-project/

[27] See paragraphs 23-27 of Alpine Energy's submission, paragraphs 3 and 39-45 of ENA's submission (the submission also calls for a provisioning that the life of all new assets not exceed 25 years), paragraph 44 of PwC's submission.

[28] See paragraph 20 of MEUG's submission.

[29] See paragraph 96 of Vector's submission.

[30] See Asplundh's submission.

We support EDBs being able to procure network innovation through opex and suggest regulatory arrangements that support this model (and provide assurances around other models) should support the long-term interests of consumers.

Regulatory risk is best addressed by a level playing field

ERANZ recognises that there may be a risk of constructing a regulatory model before the market is established and before we know how it will work. Equally, there is a risk in constructing a default regulatory model by doing nothing.

There is risk with both routes. When deciding which path to take, ERANZ believes that the Commission needs to be guided by the philosophy behind the current regulatory framework. This philosophy is that competitive markets and the separate regulation of monopoly enterprise will together maximise the long-term interests of consumers. A market is only truly competitive when there is a level playing field between all participants. Cross-subsidies, de-risking of investment and the potential for discrimination by networks are real risks and would serve to undermine any prospect of a level playing field in markets for emerging technology.

Moreover, in response to Vector, ERANZ wishes to make it clear that our proposal is not trying to second-guess the future shape of the electricity industry or create sector-specific rules. On the contrary, our proposal aims to create a regulatory framework that allows contestable markets to efficiently drive the adoption of emerging technologies. Where a market is contestable, the regulatory framework should be as neutral as possible in terms of impact.

In our view, the question is not what the market for emerging technology will look like? Rather, it is what regulatory frameworks will best ensure the efficient development of those markets? As part of that framework, the IMs have a critical role in managing incentives on monopolies to efficiently participate in contestable markets.

Furthermore, there has been suggestion that EDB participation is important for early adoption of emerging technology in New Zealand.[31] This may be true in an international context where technologies are used to meet climate change and renewables goals. However, in New Zealand our Emission Trading Scheme approach encourages the use of contestable markets to deliver the least cost reductions. This context further underscores the importance of encouraging competition in such technology markets.

Overall, ERANZ acknowledges that the EDBs have a key role in facilitating the efficient evolution and adoption of emerging technologies in New Zealand. Their networks provide the platform on which competition will take place. And, with appropriate ring fencing of assets and procurement and information disclosure rules, EDBs should be free to participate in contestable markets. These requirements form the basis of a level playing field, which will best serve the long-term interests of consumers.

[31] See Vector, ENA, and PwC's submission.

Appendix: AER's Draft Ring-fencing Guidelines – Explanatory Table

Table 1 Draft Ring–fencing Guideline—summary of obligations

Harm affecting customers and markets	Ring-fencing obligation	
Cross-subsidies	Legal separation of DNSP from other entities	A DNSP cannot provide any non-Network Services (Subject to a materiality threshold) (Network services are distribution services and/or transmission services)
	Account separation / Cost allocation	Accounts – DNSP must establish and maintain accounts (in relation to Direct Control Services plus regulated Transmission Services). Costs – DNSP must not allocate / attribute to Distribution Services costs that properly relate to non-Distribution Services.
Non-discrimination	Not discriminate	A general obligation on the DNSP that it will not discriminate (either directly or indirectly) in favour of a related body corporate or its customers.
	No cross-promotion	A DNSP will not advertise or promote the services provided by its affiliate.
	Functional separation	Physical separation – DNSP must operate independent and separate offices to a related body corporate or an affiliated service provider that provides non-network energy-related services Staff sharing – DNSP must ensure that staff directly involved in the provision or marketing of a Direct Control Service or a regulated Transmission Service are not also involved in the provision or marketing of non-network energy-related services
	Information access and disclosure	Protection – DNSP must protect information provided by a customer, prospective customer for Direct Control Services and / or regulated Transmission Services, and ensure its use is only for the purpose for which that information was provided. Similarly, a DNSP must protect information it acquires in the normal course of business.
		Sharing – Where a DNSP acquires information in providing Direct Control Services and/or regulated Transmission Services, and shares this information with a related entity, it must provide access to others on the same price, quality and terms and conditions. Disclosure – DNSP must not disclose information (acquired in providing Direct Control Services and/or regulated Transmission Services) to any party without the informed approval of the relevant customer or prospective customer to whom the information relates.