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To: IM.Review@comcom.govt.nz

A FlexForum perspective on the draft input methodologies

The FlexForum is an association of people and organisations¹ from across the electricity eco-system that want to take practical action to accelerate progress to ensure consumer and distributed energy resources (CDER) and flexibility are available to:

- support affordable and reliable operation of the electricity market and power system
- enable accelerated electrification by households and businesses as part of the transition to a zero emissions economy.

Flexibility is our focus because it is central to electrification and decarbonisation. Encouraging the supply and use of flexibility provides households, businesses, communities and the electricity supply chain with more capability and options to accelerate electrification and decarbonisation.

Our touchstone is the [Flexibility Plan 1.0](#) which we produced in August 2022 to provide a checklist of the practical steps needed to establish the frameworks and capabilities required to ensure flexibility is available to maintain and improve reliability and affordability of supply.

The input methodologies are critical to setting the pace for uptake of flexibility and electrification

The input methodologies (IMs) applying to electricity distribution and transmission network operators (collectively, network operators) have a critical role in the uptake of flexibility and the pace of electrification by providing incentives for network operators to efficiently deliver distribution and transmission services.

The existing IMs and incentives were designed for a different operating environment in which network planning, forecasting and operating decisions were based on the quite predictable usage patterns of household and business power consumption. Distribution and transmission network operators now face material changes to patterns and types of use of their networks, and particularly the low voltage network, for a range of reasons, including increases in solar, electric vehicle charging, electrification of home, commercial

¹ The FlexForum is open to people and firms that want to support practical action to achieve its objective and purpose. FlexForum Members currently include (in alphabetical order): Ara Ake, ANU Battery Storage and Grid Integration Program, Cortexo, ecotricity, Electricity Engineers Association (EEA), evnex, influx, Manawa Energy, Mercury, Meridian, Orion, Our Energy, Overlay, Powerco, revolve energy, Robinson Bowmaker Paul, SEANZ, The Energy Collective, Transpower, University of Auckland Energy Centre, Vector, Vector Metering, Wellington Electricity, and two individuals (consumers).

heating, and process heat. These changing circumstances require the Commerce Commission to ensure network operators can develop new capabilities and to adapt their operational and investment practices, and ensure regulation is responsive to external drivers of change, including consumer needs and preferences.

Flexibility is a feature of these changing circumstances because it is part and parcel of electrification. Consumer and distributed resources – the EV chargers, distributed generation, smart and inverter-based devices being connected to the power system every day – can be operated flexibly to provide network operators an extra tool to manage power quality and network congestion if the right frameworks and capabilities are in place.

Right now, the frameworks and capabilities needed to use flexibility are not in place. All network operators, and the wider electricity ecosystem, including flexibility suppliers, must invest in learning-by-doing to understand and develop the capability required to use flexibility and to become confident the tool will work. This learning-by-doing will only occur at the pace required to achieve decarbonisation goals if the Commerce Commission provides network operators suitable financial incentives to test and use non-network solutions (ie, flexibility). The IMs and their implementation in the 2025 default price-quality path (DPP) reset are critical to this outcome because distributors have a critical role to play to assist and enable flexibility suppliers and others across the electricity ecosystem to develop the capability to deliver flexibility to manage power quality and network congestion.

Several distributors are not price-regulated and not subject to the incentives provided through the IMs. Maximising the value of CDER and flexibility requires all distributors to coordinate to ensure alignment of capabilities and processes, eg, procurement and deployment processes. The Commission should ensure that there are effective tools and incentives in place to encourage all distributors to take a coordinated approach to investing in the common capabilities and processes which are needed to maximise the value of flexibility. Electrification in general, and flexibility specifically, will be delayed unless the Commission does what it can, whether through the IMs or through other regulatory tools, to avoid a patchwork of approaches which raises barriers to entry and increases transactions costs.

Four outcomes of the IMs process which would benefit consumers

The FlexForum considers the IMs process will realise long-term benefits for consumers if it delivers these four outcomes:

1. Improves the understanding of, and confidence in, the IMs by flexibility suppliers, owners of flexible resource, and anyone who isn't a network operator.
2. Effective and accessible incentives for network operators to invest in innovation and non-traditional solutions (including flexibility) to support efficient electrification and decarbonisation, especially in the short-to-medium term as solutions are developed.
3. Ensures network operators have effective incentives to make the appropriate investment decisions in the long term.
4. Ensures the IMs enable agility so the Commission and network operators can respond to fast-evolving consumer needs.

Improve the understanding of, and confidence in, the IMs by flexibility suppliers

To most people outside the distributors and Transpower (grid owner), the IMs are complex, arcane and effectively a black box. Understanding whether the IMs do what it says on the box requires significant effort and expertise. Although external expertise to aid understanding of the IMs can be purchased, the cost of doing so is a barrier to many of the parties impacted by the IMs. Given this, it is difficult for flexibility suppliers (and anyone who does not work for a distributor or the Commission) to be confident that the IM's provide the incentives necessary to jump-start development and use of flexibility.

The difficulty experienced by flexibility suppliers and others across the electricity ecosystem to understand and have confidence in the IMs creates uncertainty that discourages investment needed to access the flexibility of CDER, because their investors do not have clear line of sight of a return on investment. The Commission has in the past put much stead in the positive opinion of ratings agencies of the IM and DPP framework. However, this positive opinion is not necessarily shared by the investors in the firms looking

to use networks to supply flexibility to distributors, Transpower (as grid owner and System Operator) and across the electricity supply chain.

The Commission can improve the understanding of, and confidence in, the IMs by providing practical guidance about the incentives and associated outcomes the IMs are designed to deliver, particularly for parties that may want to offer flexibility services to distributors and across the power system (and so will rely on the operational and investment choices of network operators). Providing practical guidance would be consistent with the purpose of the information disclosure regime, that is, to ensure that sufficient information is readily available to interested persons to assess whether the purpose of the IMs is being met. A potential side-effect of demystifying the IMs is more efficient decision-making by network users, and therefore, by network operators (because network operators make decisions in response to the actions of network users).

The FlexForum is happy to support this effort by convening a workshop to reality test a working version of a guide to the incentives and outcomes the IMs are designed to deliver.

Effective incentives and accessible allowances to invest in innovation and non-traditional solutions (including flexibility)

The proposed “Innovation and non-traditional solutions” allowance is welcomed to support the learning-by-doing required for flexibility to become business-as-usual network management tool.

The proposed allowance for flexibility will stimulate the development and testing of flexibility and assisting to build the capability of network operators and flexibility suppliers so that flexibility is a proven alternative when it is needed.

The practical effect of the allowance depends on the detailed implementation through the 2025 DPP determination. This dependency could create significant uncertainty for network operators and flexibility suppliers and delay efforts to test and use flexibility. Delay will increase the costs borne by consumers and slow the pace of reductions in carbon emission.

The FlexForum suggests the Commission clarify how the allowance will work in practice ahead of the 2025 DPP determination and is happy to engage with the Commission to support this. Fast-tracking development of critical aspects of the allowance mechanism ahead of the 2025 DPP determination due in November 2024 will help to avoid the costs of delay and uncertainty. Things to solve early include:

- ensuring processes for accessing the allowance are streamlined and right-sized relative to the amounts involved
- ensuring the mechanism explicitly supports the range of learning-by-doing required rather than being constrained by impractical definitions of innovation or non-traditional. The Flexibility Plan and Network Transformation Roadmap provide a useful reference point for the learning-by-doing which should be supported
- ensuring the allowance mechanism takes account of the nature, timing and allocation of risk and cost borne by distributors, flexibility suppliers and others participating in learning-by-doing. In particular, the IMs should ensure that distributors are not discouraged from using flexibility because they are not funded appropriately or are not incentivised to participate in trials, pilots or development programmes. This would have a broad chilling effect on investment in flexibility (and electrification) because distributors are a critical partner for developing flexibility.

Ensure network operators have effective incentives to make the appropriate investment decisions

The Commission needs to be sure that the IMs create realisable incentives for network operators to make appropriate investment decisions, eg, when making a choice between investing in flexibility (from new or existing sources) or more poles and wires.

We are not convinced the proposed IMs do this because they do not provide an enduring financial incentive for distributors to choose a more efficient flexibility solution (operating expenditure - opex) to defer a poles and wires network solution (capital expenditure - capex).

We understand the challenge is that the Incremental Rolling Incentive Scheme (IRIS) mechanism does not allow opex and capex substitution across regulatory periods and that this discourages distributors from choosing flexibility solutions (ie, using opex over capex options). The Commission's response to this issue is to provide allowances for purchasing flexibility so distributors do not have to rely on the IRIS to substitute for capex for opex allowances for funding. This is a reasonable stop-gap and we support this a short-term solution. However, this is not an enduring solution because the inherent uncertainty in opex forecasts will undermine confidence in the resulting opex allowances and distributor revenues. The concern is that best endeavours forecasts are not allowed or are materially reduced by the Commission when making the 2025 DPP determination, which would reduce the funds available for testing and paying for flexibility.

The FlexForum suggests the Commission commit to solving this issue after finalising this IM change process, and ideally as part of the 2025 DPP determination process.

Ensures the IMs enable agility so the Commission and network operators can respond to fast-evolving consumer needs

The IMs need to provide network operators and the Commission with the ability to be more agile and adaptable to fast-evolving consumer preferences, and the associated implications for network operations and investment.

The draft IMs provide two pathways for network operators to respond to unforeseen events and the impact of known and unknown unknowns on forecasts:

- a reopener mechanism
- applying for a customised quality-price path.

The Commission has discounted including a regulatory sandpit in the IMs. This is reasonable given sandpits are more suited to testing new market settings, and new products and services. However, **the FlexForum suggests the Commission ensure the IMs encourage the involvement of network operators in projects testing new market settings, products and services.**

The FlexForum understands applying for a CPP requires a massive effort and is an extended process. On this basis, we do not see a CPP as a tool enabling network operators to be agile and adaptable.

The reopener mechanism is presented as a tool for managing unforeseen events and material variations to forecasts. However, the proposed approach will not provide the agility or adaptability which will be needed. As proposed, the mechanism creates a very high hurdle which will delay or prevent network operators from delivering (unforeseen) customer preferences, thereby delaying electrification. Cumbersome process requirements will lead to an inefficient diversion of resources by network operators and the Commission.

- at a minimum, the Commission should commit to resourcing the mechanism to ensure it is used and usable based on the timeframes and expectations of customers, rather than those of the regulator. Streamlining the process, including having fit-for-purpose criteria for using the process, will help network operators and the Commission make efficient use of scarce resources. The specifics of the process should be outside the IMs – but the IMs should specify expected timelines and outcomes. The process timeframes should be based on matching (or improving on) customer expectations, with a starting point being the timelines for existing connection processes, eg, for DG.
- The criteria for reopener mechanisms should be equivalent for all distributors given they all are facing the same challenges and circumstances, eg, the expectations of a solar developer connecting in Tauranga or Christchurch are equivalent (and the customer may be the same party).

The FlexForum is happy to assist the Commission to identify fit-for-purpose criteria and timeframes for the reopener mechanism to include in the IMs, and to subsequently assist the Commission to fast-track the detailed design of a streamlined process.

Concluding points

The IMs have a critical role in the uptake of flexibility and the pace of electrification by providing incentives for network operators to efficiently deliver distribution and transmission services.

The most important thing the Commission can do to ensure the IMs enable households, businesses, communities and the electricity supply chain to maximise the value of consumer and distributed resources and flexibility is to provide network operators, and the wider electricity ecosystem, with the flexibility to adapt to fast-evolving consumer needs and preferences, and the ability and incentive to take advantage of new ways to provide consumers with affordable and reliable and sustainable electricity services.

You can contact us at info@flexforum.nz with any questions and to arrange any further discussion of the FlexForum perspective on the role the IMs have in maximising the value of flexibility and consumer and distributed resources, and accelerating electrification and decarbonisation.

Kind regards

The FlexForum

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