

22 March 2018

Hon Dr Megan Woods  
Minister of Energy and Resources  
Private Bag 18041  
Parliament Buildings  
Wellington 6160

Dear Minister

### **ANNUAL LETTER OF EXPECTATIONS 2018/19**

Thank you for your letter dated 1 March 2018 setting out your strategic and performance expectations for the Electricity Authority in relation to 2018/19.

As per your request, we set out below our response to the expectations in your letter. This approach has been discussed and agreed with MBIE.

#### **Review of electricity pricing**

The Authority will support MBIE on aspects of the electricity price review that are identified as sitting most appropriately with the Authority.

In your letter you indicate that you expect the work programme of the Authority to complement, not duplicate aspects of the electricity price review. We understand that the finalised terms of reference of the review will be available to us shortly, at which point we will have more certainty about potential duplication.

At this stage there appears to be potential duplication with respect to one project we are yet to commence, called *Review of the distribution sector*, which focuses on the ability of distributors to respond to emerging technology. We have developed the scope and methodology for this work (attached) and we were intending to consult interested parties about that before beginning the project proper. We will discuss the timing for this with MBIE in the context of the electricity price review.

#### **Energy resilience**

The Authority supports the resilience of New Zealand's electricity system through its focus on reliability—this delivers on our statutory objective.

As technologies continue to evolve, a wider diversity of services and businesses will become available in the market. While this creates opportunities for innovation, it can also affect future supply risks by affecting decision making about asset operation, investment and market entry. Also, the entry of new types of electricity businesses may erode some aspects of our current security of supply regime and increasing levels of renewable generation will require market arrangements to evolve to deliver efficient levels of security of supply.

We appreciate the expectation in your letter that our work programme reflect these developments, and we confirm that has been the case in recent years and will remain the case over the next few years.

In particular, our current work programme includes a suite of projects on risk management and promoting a flexible and resilient electricity market and electricity systems. It includes a very significant initiative on real-time pricing in the spot electricity market and other initiatives aimed at providing greater income stability for providers of last-resort plant and demand response, better price signals about future supply risks, and more options for addressing those risks.

For example, we are currently facilitating the listing of exchange-traded cap products to improve investment signals for generators and demand-side response resources, while providing retailers with additional tools for effectively managing wholesale spot price volatility. Our work programme also includes an initiative aimed at more effective and efficient management of the hosting capacity available on electricity networks, which is important for the reliability of electricity networks.

### **Work with a range of agencies**

The Authority has effective working relationships with a range of existing agencies that affect the electricity sector. These include MBIE, the Council of Energy Regulators, the Ministry for the Environment (MfE), Environment Canterbury, the New Zealand Transport Agency (NZTA), Treasury, the Commerce Commission, the Productivity Commission, the Gas Industry Company (GIC), the Energy Efficiency and Conservation Authority (EECA) and Utilities Disputes Limited.

For example, last year the Authority, the Commerce Commission and MBIE created an interface working group. The objective is to improve the coordination between agencies to ensure, among other things, that industry arrangements promote the efficient uptake of new technologies. The Commerce Commission also has an observer sitting on our Innovation and Participation Advisory Group (IPAG) to assist IPAG to understand the potential interactions between the work IPAG is undertaking with the Equal access project and the way the Commission regulates electricity network businesses.

We are also looking forward to collaborating with the Interim Climate Change Committee, and when established, the Climate Change Commission.

### **General expectation and good governance**

#### *High performing Board*

Our vision for the Authority is to be a world class electricity regulator for the long term benefit of consumers and New Zealand. We are not able to achieve this vision if we as a Board are not focused on our own performance. The Board has an annual discussion on its own performance as do the respective Board sub-committees. We also have a comprehensive governance manual and a thorough induction process for new Board members.

We will strengthen our review processes as per your general expectations and report the results of our self-assessment to you and MBIE by 30 September 2018. As requested, this report will include information about steps the Board is taking to respond to the findings of the self-review.

We will continue our dialogue with MBIE on the skills required to maintain a strong Board. In particular, we will continue our practice of advising MBIE on succession planning and forthcoming appointments.

### *Effective monitoring of Agency performance*

We constantly work towards achieving our vision of being a world class electricity regulator. To guide this work, we conducted an organisational Performance Improvement Framework self-review in 2014/15,<sup>1</sup> and a follow-up self-review in September 2017. This work helped us define the areas of focus for our organisational development programme. We monitor progress against our work programme and report on those achievements in our four-monthly reports to you and in our annual reports.

### *Strategy and performance information*

Our planning process includes strong elements of stakeholder consultation and strategic prioritisation so that resources are applied appropriately to our business-as-usual and market development work. We are transparent about our work programme, consulting during its development, publishing the work programme itself, and publishing regular progress reports.

The draft 2018/19 Statement of Performance Expectations will be provided to you in mid-April 2018, which provides specific performance metrics which we report against in our annual reports.

### *Risks, opportunities and no surprises*

We will operate a “no surprises” policy with your office that meets the requirements of the General expectations set out in Annex 1 of your letter.

We will also provide notification to your office when we receive substantive media queries.

Yours sincerely



Brent Layton  
**Chair**

cc: James Stevenson-Wallace  
GM Energy and Resource Markets  
MBIE

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<sup>1</sup> State Services Commission organisational improvement model see: [www.ssc.govt.nz/pif](http://www.ssc.govt.nz/pif).

# Appendix A Scope for the review of the distribution sector

## Electricity Authority

### Scope of the Review of the electricity distribution sector

#### 1 About us

1. The Electricity Authority (Authority) was established as an independent Crown entity on 1 November 2010 by the Electricity Industry Act 2010 (Act).
2. The Authority's Statutory Objective is to promote competition in, reliable supply by, and the efficient operation of, the New Zealand electricity industry for the long-term benefit of consumers. We provide independent regulation and governance of the electricity industry and oversee the operation of the New Zealand electricity system and markets. We interpret our statutory objective as requiring us to exercise our functions in ways that:
  - facilitate or encourage increased competition in the markets for electricity and electricity-related services
  - encourage industry participants to develop and operate the electricity system efficiently to manage security and reliability
  - increase the efficiency of the electricity industry.
3. The Authority's [Statement of Intent 2017-2021](#) was published in June 2017. It outlines the strategic direction and framework of the Authority.

#### Background

4. There are large changes ahead for the electricity distribution sector (distributors), which are being driven by emerging technologies. The outcome of how these technologies are adopted has the potential to lead to efficiency gains and lower costs for consumers. However, these gains are far from certain and could ultimately depend on how well distributors are placed to adapt to the changing environment.
5. Accordingly, the Authority is interested in indicators of distributor's capability to react to the impending technological disruption in ways that benefit consumers.

#### Objectives

6. The research question we will use for the review is: *What indicators would tell us whether the distributors are well-placed to adapt to the impending technology change in ways that benefit consumers, and what are the options to track the progress of distributors?*

#### Approach

7. In carrying out this review, it will be important to understand and assess the beliefs and myths retailers and other stakeholders have about the capability of distributors to adapt. We expect to use a combination of surveys and interviews for this phase.
8. Interactions with distributors will initially consist of a set of questions based on a scan of good industry practice which will be used to gain insights into distributor innovation and new technology. Ideally this is a voice interview process by informed interviewers so that respondent comments can be explored to uncover greater insights on to their capabilities and practices.
9. Analysis of the insights from this initial interaction will provide the basis for two further streams of work:
  - a. An in-depth survey sent to all distributors

- b. More detailed interviews or workshops, or both, with selected distributors

### **Scope of the review**

- Literature search of technological uptake and how this might relate to distributors
- Review of past technological changes and how distributors responded
- Survey and other qualitative measures of technology uptake and incentives
- Indicators of ability to host new technology
- Review case-studies of how comparable sectors have successfully adapted to changing circumstances
- Details of ongoing monitoring

### **Deliverables**

10. The deliverable for the review is a report including the underlying data such as survey results and interview notes.
11. We expect that other Authority projects and regulatory agencies will draw upon insights from this review.

### **Timing**

12. The indicative timeframe for delivering this research is completion during the 2018/19 year.