



**MINISTRY OF BUSINESS,  
INNOVATION & EMPLOYMENT**  
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# Regulatory Charter

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Energy markets regulatory system

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# 1 Context

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## What is in a regulatory charter?

A regulatory charter:

- sets clear expectations for what the regulatory system is intended to achieve
- outlines the key principles underlying the design of the regulatory system, and
- describes the respective roles and functions of agencies in various parts of the regulatory system.

## Why have a regulatory charter?

A regulatory system comprises the rules, institutions and practices which combine to achieve a given set of behaviours or outcomes. A charter is a tool designed to help manage oversight of a regulatory system.

Promoting good regulatory stewardship is a key element of the Government’s regulatory approach, with government entities monitoring the performance and maintaining the quality of the regulatory systems they oversee.

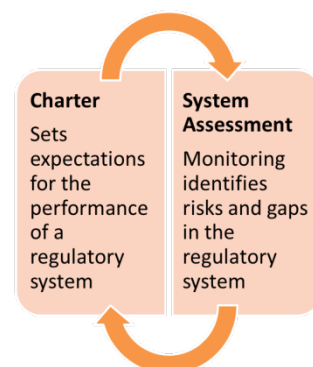
MBIE has stewardship obligations under the State Sector Act 1988 to monitor the performance of the regulatory systems it oversees, including the energy markets regulatory system.

## Objective of the regulatory charter

The charter is a management tool designed to support a living regulatory system<sup>1</sup> (see **Figure 1**). The objective of this charter is to promote active management of the energy markets regulatory system, which it does by:

- reinforcing shared ownership for the system among those government entities with policy and regulatory functions
- recording an understanding between the core agencies about their respective roles and functions, and how the system is intended to perform, and
- setting out how agencies will work together to address the gaps, overlaps and uncertainties which inevitably arise in complex systems.

**Figure 1 Charters and System Assessments complement each other**



<sup>1</sup> A living system is one which is continuously monitored and improved, rather than set and forgotten. A living system incorporates mechanisms to enable the regulators in the system to identify, assess and evaluate the system and make adjustments where appropriate to meet evolving opportunities and risks. In a living system, the system’s owners have shared expectations of how the system is supposed to perform and can assess how that system is performing against those expectations.

Relevant agencies will continue to work collaboratively and collectively across their respective roles and functions to actively manage the energy markets regulatory system.

## Charter ownership

This charter is owned by the Ministry of Business, Innovation and Employment (MBIE) as steward of the energy markets regulatory system, and was developed with input from the Commerce Commission (CC), the Electricity Authority (EA), the Gas Industry Company (GIC) and the Energy Efficiency and Conservation Authority (EECA).

The parts of the charter addressing the electricity and gas markets have been endorsed by the Council of Energy Regulators (CER), on which MBIE, EA, GIC, and CC are represented.

## Charter functionality

This charter describes the current energy markets regulatory system and how it operates. It sets out the purpose of the system and the roles and functions of different agencies, and describes known gaps and overlaps. It does not seek to anticipate future work programmes.

## Charter review and management

Responsibility for maintaining and reviewing this charter document sits with MBIE. Review of this document should occur at least every five years. The electricity and gas market components of the charter will also be considered on a regular basis as part of the operation of the CER.

Reviewing the charter will include assessments of whether:

- system objectives, policy or context have changed over time
- the charter document should be updated to reflect these changes, and
- as a result of system assessments, progress has been made in addressing identified risks and closing gaps.

This reflects the living systems approach to charter management, where adjustments are made as and when necessary to meet evolving circumstances. For the avoidance of doubt, a charter does not impose an additional obligation on core agencies to carry out system assessment. Core agencies expect that existing accountability processes and proactive self-assessments are sufficient (this is explained further in the section titled 'Monitoring and evaluation').

## 2 Background: regulating the energy markets system

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### What is the energy markets regulatory system?

The energy markets regulatory system comprises the institutions and markets involved in the production, supply and consumption of energy and related services. It includes regulatory and non-regulatory measures supporting policy objectives including: reliability and security, competition, efficiency, access and affordability.

The energy markets regulatory system includes the legislation, policy, rules and regulations for:

- **Electricity:** generation, storage, transmission, distribution and retailing.
- **Gas:** production, storage, transmission, distribution and retailing of natural gas and LPG.
- **Energy efficiency:** provision of energy efficiency product standards and information for energy consumers.
- **Liquid fuel markets:** importation, production, storage, distribution and retailing of refined oil products and other liquid fuels<sup>2</sup>.

### Why is the energy markets system important?

Access to safe, reliable and efficiently priced energy services plays a vital role in supporting the New Zealand economy. For households, the energy markets system provides access to services such as space heating, hot water, lighting, refrigeration, and personal transport. For businesses, the energy markets system also powers information and communication systems, process heat and cooling, freight, and many other services.

### Why regulate the energy markets system?

While New Zealand generally operates a free market economy, some sector-specific regulation of the energy markets system is warranted as it has particular characteristics that give rise to market failure (see **Table 1** for examples). The overarching aim of the energy markets regulatory system is to promote the long-term interests of consumers and ensure well-functioning markets.

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<sup>2</sup> We have excluded solid fuels from the energy markets regulatory system. Coal for example is regulated through the Crown Minerals Act 1991 (part of the petroleum and minerals regulatory system). In the case of wood fuel, although some market facilitation is underway by EECA, the market failures associated with other energy markets are not currently present in the wood fuel market (thereby not warranting inclusion in this Charter).

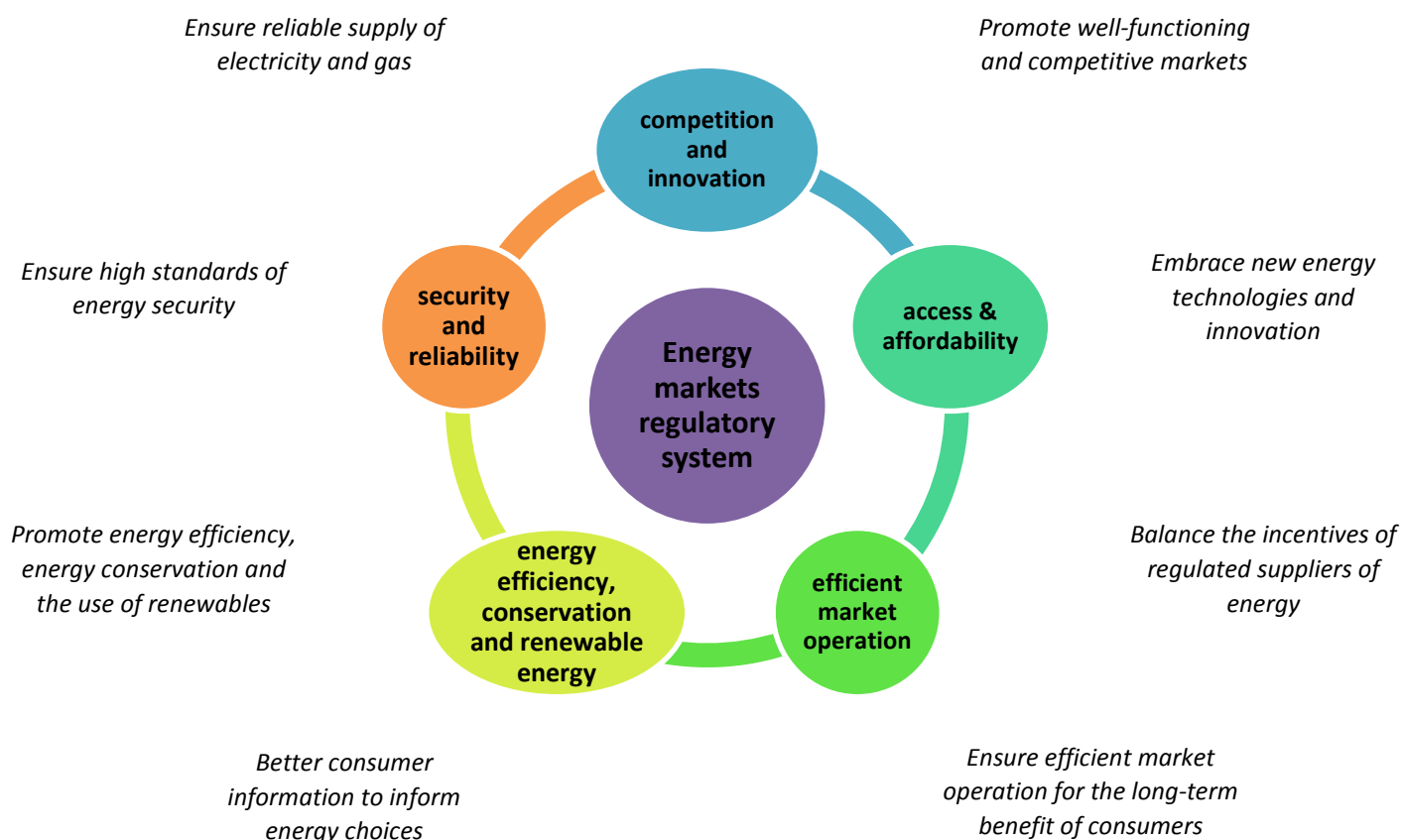
**Table 1: examples of why the energy markets system requires regulation**

|                                      |   |
|--------------------------------------|---|
| Natural monopolies                   | Economic regulation of electricity and natural gas network services with natural monopoly characteristics is warranted to prevent excessive prices and inefficiencies. Economic regulation seeks outcomes consistent with those in competitive markets, by promoting efficient allocation of costs and setting prices at a level that limits excessive profits but encourages efficiency improvements and appropriate investment. |
| Fuel quality                         | The chemical composition and performance of petrol is standardised and regulated for the protection of consumers and the environment. A consumer cannot determine the quality of the fuel before purchase (and in many cases, even after purchase), so Government regulation serves both to ensure the fitness of the fuel and to provide a signal of that fitness to consumers.  |
| Gas emergency response               | Arrangements to maintain safe pressures in gas transmission pipelines following an unexpected disruption (e.g. a leaking pipe) are regulated because prompt centralised decision-making is required to avoid free-riding and hold-out behaviour.  |
| Common quality of electricity supply | Services that determine the voltage, frequency, and reliability attributes of electricity supply are a necessary part of the electricity system (i.e. are a public good that needs to be paid for). These services require regulation to ensure the services are provided, and to prevent free-riding or hold-out behaviour by market participants.   |
| Information                          | Competition is strengthened when consumers have access to trusted information and tools to help them make informed decisions. Regulation can be used to reduce information barriers, and re-balance any information asymmetry between suppliers and consumers.  |

## Objectives of the energy markets regulatory system

The Government aims to have well-functioning energy markets that support sustainable economic growth and social well-being. The energy markets regulatory system therefore has the following core objectives<sup>3</sup>:

**Figure 2: Core objectives of the energy markets regulatory system**



## Scope of this Charter

The energy markets regulatory system consists of any legislation, entity, activity or policy objective<sup>4</sup> that is used to prescribe rules or influence conduct, calibrate incentives or change preferences<sup>5</sup> in relation to energy products and services.

<sup>3</sup> These objectives reflect primary legislation within the energy markets regulatory system, and guiding policy documents such as the New Zealand Energy Strategy 2011-2021, see <https://www.mbie.govt.nz/info-services/sectors-industries/energy/documents-image-library/nz-energy-strategy-lr.pdf>, and the New Zealand Energy Efficiency and Conservation Strategy 2017-2022 (NZECS), see <http://www.mbie.govt.nz/info-services/sectors-industries/energy/documents-image-library/NZECS-2017-2022.pdf>.

However, the boundary of the energy markets regulatory system with other regulatory systems is not always clear. To clarify some particular boundary uncertainties for the purpose of this charter, the energy markets regulatory system:

- includes legislation, entities, activities and policies for:
  - the economic regulation of monopoly electricity lines and gas pipeline businesses
  - promoting competition, efficiency and reliability in the supply of energy
  - promoting energy efficiency and conservation in homes and businesses and encouraging the uptake of renewable energy
  - ensuring the quality of petrol and diesel at retail outlets<sup>6</sup>, and
  - managing or facilitating the emergency response to major energy supply disruptions.
- and excludes:
  - health and safety aspects, including the regulation of the safety of energy appliances, fittings, works and high hazard facilities
  - regulation of electrical workers and gas fitters
  - general consumer protections
  - activities relating to energy suppliers as lifeline utilities within civil defence and emergency management operations
  - transport policy, and
  - the upstream exploration and production of petroleum and gas.

The primary agencies are:

- MBIE – steward of the energy markets regulatory system.
- CC – promotes competition in New Zealand markets and responsible for the economic regulation of natural monopolies (including electricity and gas transmission and distribution).
- EA – promotes competition in, reliable supply by, and the efficient operation of the electricity industry and responsible for the Electricity Industry Participation Code.
- GIC – ensures that gas is delivered to customers in a safe, efficient, reliable, fair and environmentally sustainable manner.
- EECA – responsible for improving the energy efficiency of New Zealand homes, vehicle fleets and businesses, and encouraging the uptake of renewable energy.

Further details on the different roles and responsibilities of these agencies are included in the section ‘Agency roles in the energy markets regulatory system’.

## Linkages with other regulatory systems

The previously mentioned exclusions are included in other regulatory systems (some of which also have regulatory charters that this charter sits alongside).

As an example of the linkage with the workplace health and safety regulatory system, changes in workplace safety regulation have the potential to affect practices such as ‘live line’ work by electrical workers, with consequential impacts on costs and reliability.

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<sup>4</sup> The Treasury, Best Practice Regulation: Principles and Assessments (February 2015) (online). <http://www.treasury.govt.nz/regulation/bpr>.

<sup>5</sup> Orbach, B. (2012) What Is Regulation? 30 Yale Journal on Regulation Online 1.

<sup>6</sup> Noting that the monitoring and enforcement of petrol and diesel quality standards are included in the consumer and commercial regulatory system.



For the purposes of this charter, the general protections in place for consumers (the Fair Trading Act 1986, the Consumer Guarantees Act 1993 etc.) are covered by the consumer and commercial regulatory system and are not included here.

The upstream elements of the energy markets system – the exploration and extraction of oil and gas – are not covered in this charter as they are included in the petroleum and minerals regulatory system.

There is significant cross-over with the competition system regulatory charter, which is also owned by MBIE. The Commerce Act 1986 forms the backbone of the competition regulatory system, providing the core competition policy framework. Part 4 of the Commerce Act provides for economic regulation of markets with little or no competition (and currently applies to electricity lines services, gas pipeline services, and specified airport services). This energy markets regulatory charter includes Part 4 regulation as it is an integral part of the wider energy markets regulatory system, noting that it is also (along with the general competition regime) covered in the competition system regulatory charter.

# 3 Approach to regulation of energy markets in NZ

## Overview of the regulation of the energy markets system

New Zealand’s overall energy policy framework has been relatively stable for the last 25 years<sup>7</sup>. There has been an ongoing focus on liberalised and competitive markets, where possible using a reliance on market prices to balance supply and demand and drive investment and consumption decisions. Where competition is not efficient, economic regulation of the natural monopoly infrastructure (electricity lines and gas pipelines) is in place.

## Energy markets legislation

**Table 2** below sets out the intention and function of the primary legislation for the energy markets regulatory system. It also identifies the organisation tasked with each function and its associated responsibilities.

**Table 2: Primary legislation in the energy markets regulatory system**

| Relevant statutes   | Roles and functions within the energy markets regulatory system   |
|---|---|
| <p><i>Electricity Act 1992</i></p> <p>Provides for the regulation, supply, and use of electricity in New Zealand.<sup>8</sup></p> | <p>Minister of Energy and Resources<sup>9</sup>:</p> <ul style="list-style-type: none"> <li>administers electricity operator status.</li> </ul>   |
| <p><i>Electricity Industry Act 2010</i></p> <p>Provides a framework for the regulation of the electricity industry.</p>           | <p>Minister of Energy and Resources:</p> <ul style="list-style-type: none"> <li>recommends members of the EA Board and Rulings Panel</li> <li>can recommend that regulations be made about tariffs and other consumer issues, following consultation with the Minister of Commerce and Consumer Affairs and the EA.</li> </ul> <p>Minister of Commerce and Consumer Affairs (with advice from MBIE):</p> <ul style="list-style-type: none"> <li>approves the electricity consumer complaints scheme.</li> </ul> |

<sup>7</sup> <http://www.mbie.govt.nz/info-services/sectors-industries/energy/electricity-market/electricity-industry/chronology-of-new-zealand-electricity-reform/chronology-of-nz-electricity-reform.pdf>.

<sup>8</sup> Also has purpose relevant to health and safety, prevention of property damage, regulation of fittings and electrical appliances, and the regulation of electrical workers.

<sup>9</sup> Noting that MBIE advises both the Minister of Energy and Resources and the Minister of Commerce and Consumer Affairs.

|   |   |
|---|---|
|   | <p>EA:</p> <ul style="list-style-type: none"> <li>• undertakes market facilitation measures</li> <li>• makes and administers the Electricity Industry Participation Code (the Code)</li> <li>• investigates and enforces compliance</li> <li>• undertakes market reviews and studies</li> <li>• contracts for market operation services.</li> </ul> <p>Electricity Rulings Panel:</p> <ul style="list-style-type: none"> <li>• assists in enforcing the Code by determining complaints and disputes, and determining appeals against certain decisions.</li> </ul>  |
| <p><i>Gas Act 1992</i></p> <p>Provides for the regulation, supply, and use of gas in New Zealand, and for the regulation of the gas industry in New Zealand.<sup>10</sup></p> | <p>Minister of Energy and Resources:</p> <ul style="list-style-type: none"> <li>• recommends gas governance body (GIC) and may recommend replacing that body with an Energy Commission</li> <li>• makes/recommends gas governance rules and regulations</li> <li>• appoints members of Gas Rulings Panel</li> <li>• approves the gas consumer complaints scheme.</li> </ul> <p>GIC:</p> <ul style="list-style-type: none"> <li>• undertakes market facilitation measures</li> <li>• contracts for market operation services</li> <li>• investigates and enforces compliance</li> <li>• develops and recommends gas governance rules and regulations to the Minister.</li> </ul> <p>Gas Rulings Panel:</p> <ul style="list-style-type: none"> <li>• assists in enforcement by determining complaints, disputes and appeals against certain decisions.</li> </ul> |
| <p><i>Commerce Act 1986 (Part 4)</i></p> <p>Promotes competition in markets for the long-term benefit of consumers within New Zealand.</p>                                    | <p>Minister of Commerce and Consumer Affairs:</p> <ul style="list-style-type: none"> <li>• recommends members of the CC Board</li> <li>• may recommend Orders in Council specifying whether particular gas pipelines are exempt from or subject to regulation.</li> </ul> <p>CC:</p> <ul style="list-style-type: none"> <li>• determines input methodologies</li> <li>• makes and administers information disclosure requirements</li> <li>• determines and administers price-quality paths</li> <li>• recommends whether particular gas pipelines are exempt from or subject to regulation</li> <li>• enforces compliance.</li> </ul>  |

<sup>10</sup> Also has purpose relevant to health and safety and the prevention of property damage.

|  |  |
|--|--|
|  | <p>High Court:</p> <ul style="list-style-type: none"> <li>determines merits appeals on input methodologies and customised price-quality paths.</li> </ul>  |
| <p><i>Energy Efficiency and Conservation Act 2000</i></p> <p>Promotes, in New Zealand, energy efficiency, energy conservation, and the use of renewable sources of energy.</p> | <p>Minister of Energy and Resources:</p> <ul style="list-style-type: none"> <li>appoints members of EECA Board</li> <li>determines and reviews energy efficiency and conservation strategy</li> <li>makes minimum energy performance standards (MEPS) and mandatory energy performance labelling (MEPL) regulations.</li> </ul> <p>EECA:</p> <ul style="list-style-type: none"> <li>develops and recommends MEPS and MEPL regulations</li> <li>administers programmes and measures giving effect to energy efficiency and renewable energy policy objectives.</li> </ul> |

In addition to the specific functions outlined in the table above, portfolio ministers can propose legislative changes to Cabinet (with policy support from MBIE) where required. They also have general ownership responsibilities for their departments and crown entities, including administering relevant appropriations and overseeing agency performance.

The High Court can generally hear and determine appeals on points of law and applications for judicial review of any regulatory decisions, but also more specifically merit appeals on input methodologies and customised price-quality paths (as noted in the table).

## Electricity and gas markets

The regulatory frameworks for the electricity and gas markets include mechanisms to provide some separation between agencies and Government. These mechanisms include:

- The EA and CC are independent crown entities with broad statutory rule-making powers. This means they cannot be directed by ministers, whose key formal levers are recommending Board members and budgets. However the EA and CC must have regard to relevant statements of government policy issued by the Minister of Energy and Resources (under section 17 of the Electricity Industry Act) and the Minister of Commerce and Consumer Affairs (under s26 of the Commerce Act), respectively.
- The GIC is an industry-owned company that acts in a co-regulatory capacity within the gas market. The GIC must take account of (rather than give effect to) government policy on gas governance. Ministers do not appoint any members of the GIC's Board. The costs of the GIC's activities are recovered by industry levies, which are prescribed annually in regulations recommended by the Minister of Energy and Resources.
- The Minister of Energy and Resources makes gas governance rules and regulations, but some can only be made on the GIC's recommendation, and others only after the GIC has had a reasonable opportunity to make recommendations.
- MBIE acts as policy advisor and administrator for the Ministers of Energy and Resources, and Commerce and Consumer Affairs.

Transpower is also a contracted service provider to the EA, in its role as System Operator (SO). The SO has the role of coordinating the real-time transmission of electricity (as set out in the Electricity Industry Act 1992). The Code (administered by the EA) puts certain requirements on the SO to maintain grid reliability standards and security of supply. SO services are also subject to economic regulation by the CC under Part 4.

Further details on the roles and responsibilities of agencies can be found under 'Agency roles in the energy markets regulatory system'.

## Monopoly services

The natural monopoly services of transmission and distribution in the supply of electricity and natural gas are regulated by the CC under Part 4 of the Commerce Act. There are several forms of economic regulation that these services are subject to:

- Electricity lines businesses and gas pipeline businesses are subject to information disclosure, under which they must annually disclose specified financial and non-financial performance measures and asset management plans.
- Transpower is subject to an individual price-quality path, under which maximum revenue and minimum service quality are set for a five year period, and significant expenditure must be evaluated by the CC before it can be fully recovered.
- Five gas pipeline businesses (GPBs) and 17 of the 29 electricity distribution businesses (EDBs) (those not consumer owned<sup>11</sup>) are subject to default price-quality paths (DPP), under which maximum average price and minimum service quality are set. Default price-quality paths (DPPs) are set for four to five years in a relatively low cost way, typically by applying generic approaches using business-specific parameters.
- EDBs can propose that a customised price-quality path (CPP) be applied to its business instead of a DPP. CPPs are set for three to five years, are more tailored to business-specific circumstances than DPPs, and involve more detailed scrutiny of business-specific parameters. Orion (Christchurch's EDB), Powerco (EDB for Taranaki, Wanganui, Rangitikei, Manawatu, Wairarapa, and eastern and southern Waikato), and Wellington Electricity are each subject to a CPP. The CC makes determinations on CPP proposals.
- Regulatory processes and parameters for the price-quality paths are specified in the form of input methodologies (IMs)<sup>12</sup>, which are periodically reviewed by the CC at intervals no less than seven years, and are subject to merits appeal in the High Court.

## Contestable services

Contestable electricity and gas services<sup>13</sup> are subject to pro-competitive trading rules and non-regulatory measures developed and administered by the sector-specific regulators. This promotes competition between suppliers – ensuring suppliers have incentives to maintain the reliability and quality demanded by consumers and putting downward pressure on prices – and ensures consumers have access to information and tools to actively participate in energy markets.

The EA makes and monitors rules in the Electricity Industry Participation Code (the Code), guided by objectives set out in statute.

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<sup>11</sup> For further information on the treatment of consumer owned EDBs, see <http://www.comcom.govt.nz/regulated-industries/electricity/electricity-archive/electricity-default-price-quality-path-archive/treatment-of-consumer-owned-electricity-distribution-businesses/>

<sup>12</sup> IMs are the upfront rules, processes, requirements and evaluation criteria for services that are regulated under Part 4 of the Commerce Act. This includes, for example, methodologies for determining the cost of capital, valuation of assets and treatment of taxation. Once set, IMs feed into price-quality paths and disclosure regulation.

<sup>13</sup> Such as generation, wholesaling, and retailing of electricity, and processing, wholesaling and retailing of gas.

The GIC develops and recommends gas governance rules and regulations to the Minister of Energy and Resources, guided by objectives in statute and in the Government Policy Statement on Gas Governance<sup>14</sup> (GPS).

There is a strong focus on the use of non-regulatory measures with the EA, for example, seeking to use voluntary market facilitation measures (including best practice guidelines) rather than Code amendments. These measures have been used to set expectations for managing security of supply, for retailers operating in the spot market and for contracting (among other things).

## Consumers

Energy market participants are subject to general consumer protection law (not covered in this charter), but there are also specific consumer-facing aspects of the energy markets regulatory system.

Electricity retailers are subject to consumer obligations that they must follow, as well as voluntary guidelines. Some of these obligations are set out in the Code, for example requiring retailers to compensate customers in the event of an official conservation campaign. The EA also sets and monitors compliance with guidelines, such as those for managing medically dependent and vulnerable consumers, terms and conditions for retail contracts, and communication of price changes to consumers.

Gas retailers are subject to consumer obligations set within certain rules and regulations developed and administered by the GIC. For example, the Gas (Switching Arrangements) Rules 2008 enable consumers to choose and efficiently switch between competing gas retailers by prescribing a switching process. The Retail Gas Contracts Oversight Scheme also provides a non-regulated process for reviewing retailers' supply contracts with small consumers.

The Utilities Disputes Limited (UDL) provides free and independent dispute resolution for consumers with electricity and gas complaints. It is the approved dispute resolution scheme under the Electricity Industry Act 2010 and the Gas Act 1992. These Acts set out who is able to make a complaint, how the UDL can resolve complaints and the types of remedies available.

## Energy efficiency

Energy efficiency and renewable energy are promoted with limited use of regulatory instruments. Other related environmental outcomes are achieved through market instruments (notably the Emissions Trading Scheme (ETS), which puts a price on greenhouse gas (GHG) emissions) and cross-sectoral regulation to manage local environmental effects and resource allocation.

Policy measures promoting energy efficiency have traditionally been justified by market failures such as:

- unpriced environmental externalities associated with energy supply or consumption (e.g. impaired amenity resulting from wind farms or damming rivers, GHG emissions and other pollutants from combustion of fossil fuels)
- inefficient pricing, especially at times of scarcity or network congestion, and
- energy insecurity or exposure to macro-economic shocks resulting from cartel manipulation of oil prices.

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<sup>14</sup> This sets out the objectives and outcomes the government wants the GIC to pursue. It is made pursuant to s43Z0 of the Gas Act 1992 as amended by the Gas Amendment Act 2004. The GIC is required to have regard to the objectives and outcomes in this statement when making recommendations for rules or regulations.

However, the intervention logic for energy efficiency is increasingly focusing on information and behavioural barriers, split incentives and lack of expertise. For example, those investing in energy efficiency measures are not always the ones receiving the direct benefit; the landlord supplies insulation and appliances, whereas the tenant pays the energy bills.

EECA provides information and raises awareness of energy efficiency benefits through a combination of direct intervention (such as funding for home insulation) and influence (such as marketing, behaviour change and expert advice).

Regulation is focused on minimum energy performance standards and labelling for products and appliances such as fridges, washing machines, dryers and computer equipment (for example, EECA provides the Energy Rating Label for 24 products and appliances).

The New Zealand Energy Efficiency and Conservation Strategy 2017 – 2022 (NZECS)<sup>15</sup> sets the overarching policy direction for government support and intervention for energy efficiency, energy conservation and the use of renewable sources of energy. It sets out policies, objectives and targets and how these will be achieved. EECA's work programme is guided by the NZECS (as well as EECA's letter of expectation from the Minister of Energy and Resources).

EECA is a crown agent, which means the Minister of Energy and Resources may give certain directions to the entity.

## Liquid fuel markets

New Zealand has a largely de-regulated downstream liquid fuel market, with price control and licensing removed in 1998. Only the quality of petrol and diesel sold at retail outlets is regulated.

The Government also has a policy of promoting electric vehicles and other low emission vehicles. The Ministry of Transport (MOT) leads the regulatory and non-regulatory measures promoting this objective, with EECA and MBIE in supporting roles. For example, EECA administers the vehicle fuel economy labelling programme<sup>16</sup>.

The relationships between fuel quality and vehicle tailpipe emissions require some coordination in the development of fuel quality regulations (administered by MBIE) and vehicle emission regulations (administered by MOT).

## Factors affecting energy market investment and performance

While the overall regulatory framework has been largely stable during the last two decades, we are beginning to see a number of different factors that will potentially affect energy market investment, and may require regulatory change.

The investment environment and regulatory settings going forward are influenced by both significant market-related uncertainties, and current government work programmes, such as:

- changing costs and performance of emerging technologies such as electric vehicles, solar photovoltaic (PV) generation and battery storage
- the government-initiated review into electricity pricing
- long-running reviews of electricity transmission pricing
- ongoing reviews of the regulation of fresh water quality and allocation mechanisms (which have the potential to impact the amount of water available for hydro generation)

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<sup>15</sup> <http://www.mbie.govt.nz/info-services/sectors-industries/energy/documents-image-library/NZECS-2017-2022.pdf>.

<sup>16</sup> Requires the display of mandatory fuel economy labels on new and used vehicles for sale (except for private sellers) and fuel economy information on websites selling vehicles.

- uncertainty over the commercial viability of the Tiwai Point aluminium smelter and other large industrial electricity consumers
- the depletion of gas fields and changing gas reserves
- exploration of pathways to achieve 100 per cent renewable electricity generation by 2035 (and the wider global transition to a low emissions economy)
- the introduction and removal or revision of subsidies or policies, such as the ETS.

## Regulatory principles

This section describes the high level principles that underpin the design and operation of the energy markets regulatory system.

The left hand column of **Table 3** describes the general intent of each principle<sup>17</sup>. The right hand column explains how each principle is given effect in the energy markets regulatory system, with illustrative examples where relevant.

The EA has also adopted further regulatory strategy principles to guide its approach to regulation through the Code and other market facilitation measures, for example avoiding a ‘one size fits all’ approach<sup>18</sup>.

**Table 3: Regulatory principles for the energy market regulatory system**

| Principles   | Description of the design or operational approach   |
|--|---|
| <b>Growth compatible:</b> economic objectives are given an appropriate weighting relative to other specified objectives, including other factors contributing to higher living standards | Legislation governing the energy markets regulatory system has the primary objective of promoting the long-term interests of consumers. Emphasis is given to promoting competition, achieving outcomes consistent with workably competitive markets, efficient operation of markets, reliability, and incentives to invest. This is in recognition of energy as an essential input to all sectors underpinning our economy.   |
| <b>Proportional:</b> the burden of rules and their enforcement should be proportional to the benefits that are expected to result  | <p>The economic regulation of monopoly electricity and gas pipeline businesses strives to balance the costs and benefits of such regulation by combining lower cost default price-quality regulation with provision for ‘customised’ regulation where necessary. In addition, of the 29 electricity lines businesses in New Zealand, 12 firms are subject only to information disclosure regulation on the grounds that their ownership and governance limits the potential benefits of price-quality regulation.</p> <p>Other elements of the electricity and gas regulatory systems give priority to non-regulatory measures, such as model contracts, principles, guidelines and other ‘market facilitation’ measures.</p> |

<sup>17</sup> These principles are taken from the Treasury’s principles for best practice regulation.

<sup>18</sup> See Electricity Authority, *Strategic directions for market development*, p 20, <http://www.ea.govt.nz/about-us/corporate-projects/2013-2016-planning-and-reporting/development/strategic-directions-for-market-development>



| Principles   | Description of the design or operational approach   |
|--|---|
| <p><b>Certain and predictable:</b> regulated entities have certainty as to their legal obligations, and the regulatory regime provides predictability over time</p>  | <p>‘Input methodologies’ (IMs) are a key input to the price-quality regulation of electricity lines and gas pipeline businesses under Part 4 of the Commerce Act. The purpose of IMs is to provide certainty to regulated suppliers and consumers about the rules, requirements and processes applying to Part 4 regulation. IMs are reviewed at least every seven years. This regime therefore promotes stability and predictability by providing suppliers and investors in regulated firms the confidence to invest in the long-lived infrastructure underpinning these services.</p>  |
| <p><b>Flexible and durable:</b> regulated entities have scope to adopt least cost and innovative approaches to meeting legal obligations. The regulatory system has the capacity to evolve in response to changing circumstances</p> | <p>The EA and CC have discretion to develop and evolve their regulatory measures over time in response to changing circumstances, subject to following rigorous statutory process and guided by high level objectives. For example, the EA has complete discretion regarding the Code and the CC has the ability to review and change IMs.</p> <p>The GIC has more limited regulatory tools available, but flexibility is afforded by the ability to regulate via tertiary rules, made by the Minister of Energy and Resources on the GIC’s recommendation.</p>   |
| <p><b>Transparent and accountable:</b> rules development, implementation and enforcement should be transparent</p>   | <p>Rules and regulations applying to the electricity and gas sectors are only introduced after comprehensive consultation and evaluation of the costs and benefits. Minimum energy performance standards and labelling regulations are developed in conjunction with relevant Australian agencies, and are subject to New Zealand’s regulatory impact assessment conventions. All agencies in the energy markets regulatory system undergo significant consultations with stakeholders as part of their decision making processes.</p> <p>Accountability regarding economic regulation is promoted by provision for merits appeal of input methodologies in the High Court.</p> |
| <p><b>Capable regulators:</b> the regulator has the people and systems necessary to operate an efficient and effective regulatory regime</p>   | <p>Capacity assessments are undertaken at regular intervals and subject to independent input and review.</p>  |
| <p><b>Understanding behavioural responses:</b> regulatory requirements are designed with the likely behavioural responses of market participants in mind</p>   | <p>EECA’s energy efficiency programmes are designed and reviewed with information from market research about the behaviour of individuals, households, businesses and suppliers.</p> <p>The EA’s market facilitation measures, especially those seeking to inform and empower consumers, are equally informed by market research to enhance their effectiveness.</p>  |

## 4 Agency roles in the energy markets regulatory system

|  |  |   |
|--|--|---|
| Ownership of policy and primary legislation  | <b>Minister of Energy and Resources</b><br>Responsible for <ul style="list-style-type: none"> <li>› Electricity Act</li> <li>› Gas Act and Gas GPS</li> <li>› Electricity Industry Act and 'low fixed charge' regulations</li> <li>› EECA Act</li> <li>› Approves 'gas industry body' (GIC)</li> <li>› Makes gas governance rules and regulations (some on GIC's recommendation only)</li> <li>› Recommends EA and EECA board members</li> <li>› Appoints Rulings Panel members</li> </ul> | <b>Minister of Commerce and Consumer Affairs</b><br>Responsible for <ul style="list-style-type: none"> <li>› Commerce Act (incl. regulation of monopolies under Part 4)</li> <li>› Fair Trading Act &amp; Consumer Guarantees Act</li> <li>› Recommends CC members</li> <li>› Approves electricity and gas consumer complaints schemes</li> </ul> |
|  | <b>Ministry of Business, Innovation and Employment</b> <ul style="list-style-type: none"> <li>› Leads departmental advice on competition and energy policy</li> <li>› Monitors energy policy environment</li> <li>› Provides secondary advice on GIC regulatory recommendations</li> <li>› Monitors performance of Crown entities</li> <li>› Develops and enforces compliance with petrol and diesel quality fuel standards</li> </ul>   | <b>Council of Energy Regulators</b> <ul style="list-style-type: none"> <li>› Supports MBIE's regulatory stewardship responsibilities</li> <li>› Provides a forum for high level collaboration and information sharing</li> <li>› Takes a whole-system view to consider regulatory issues and trends, risks and gaps</li> </ul>                    |
| Policy advice and system stewardship   | <b>Commerce Commission</b> <ul style="list-style-type: none"> <li>› Monitors compliance with generic competition law</li> <li>› Administers regulation of gas and electricity lines businesses</li> </ul>  | <b>Electricity Authority</b> <ul style="list-style-type: none"> <li>› Undertakes market facilitation measures</li> <li>› Makes and administers the Electricity Code</li> <li>› Procures market services</li> <li>› Monitors compliance</li> </ul>   |
|  | <b>GIC (Industry body/co-regulator)</b> <ul style="list-style-type: none"> <li>› Undertakes market facilitation measures</li> <li>› Recommends gas governance rules and regulations</li> <li>› Procures market services including GCCO)</li> <li>› Monitors compliance</li> </ul>  | <b>EECA (Crown Agent established under EECA Act)</b> <ul style="list-style-type: none"> <li>› Promotes energy efficiency and renewable energy</li> <li>› Regulates minimum energy performance standards and labelling requirements for products</li> </ul>  |
|  | <b>Utilities Disputes Ltd</b> <ul style="list-style-type: none"> <li>› Resolves 'deadlock' complaints against electricity and gas suppliers</li> </ul>   | <b>Electricity Rulings Panel</b> <ul style="list-style-type: none"> <li>› Enforces compliance with Electricity Code</li> </ul>  |
|  | <b>Gas Rulings Panel</b> <ul style="list-style-type: none"> <li>› Enforces compliance with gas governance rules and regulations</li> </ul>   | <b>High Court</b> <ul style="list-style-type: none"> <li>› Considers merit appeals against decisions under Part 4 of the Commerce Act</li> <li>› Considers appeals on points of law against EA, GIC and Rulings Panel decisions</li> </ul>  |
| Policy delivery, economic regulation, market rule administration and market facilitation |  |   |
|  |  |   |
| Dispute resolution and compliance enforcement  |  |   |
|  |  |   |

Figure 3 illustrates the key agencies (and additional statutory bodies and roles) within the energy markets regulatory system and their main functions.

Note that **Figure 3** does not include various service-provider roles that are critically important to the electricity and gas markets (for example the electricity System Operator and gas Critical Contingency Operator) but are not considered part of the regulatory system.

Despite the colour-coding in **Figure 3**, the system is not neatly divided up into these ‘vertical’ functions. Some agencies span different regulatory functions, for example:

- Regarding enforcement, the EA investigates complaints and determines settlements of breaches and disputes under the Code, while formal complaints can be referred to the Rulings Panel.
- EECA’s primary role is delivering programmes to implement Government policy on renewable energy and energy efficiency, but it also provides policy advice on these matters, including the NZEECS. EECA also develops and administers regulations for minimum energy performance standards and labelling of appliances.
- The GIC recommends rules and regulations to the Minister and MBIE provides ‘second opinion’ advice on the GIC’s recommendations. Regulatory decisions rest with the Minister (for rules) and with the Executive Council (for regulations).

‘Horizontal’ role distinction between agencies can also be unclear, or warrant careful attention. For example:

- The CC must promote incentives for electricity lines businesses to invest in energy efficiency and demand-side management when regulating those businesses. At face value this provision has the potential to overlap with EECA’s role in promoting energy efficiency, and with the EA’s role in facilitating markets for demand-side services.
- The GIC may recommend regulations prescribing terms and conditions for access to gas transmission and distribution pipelines, and for requiring certain transmission pipeline investments (including how they will be paid for). This appears to overlap with the CC’s regulatory function of determining gas transmission pricing methodologies.

The legislation governing the energy markets regulatory system endeavours to limit any jurisdictional overlap, and there are a number of statutory obligations intended to manage situations where gaps and overlaps between relevant agencies do occur. For example, there are situations where primary legislation requires an agency to take into account things that another agency does<sup>19</sup>.

However the potential for further overlap is real and must be actively managed. For example, there are a number of statutory objectives that require an agency to promote something that another agency in the system is also supposed to promote<sup>20</sup>.

## Agency interactions within the system

### Day to day interactions

Where regulatory overlaps are not managed through statutory obligations, a memorandum of understanding (MOU) provides a framework under which two agencies can identify potential boundary issues and agree how to manage them. The EA and GIC each have a MOU with the CC,

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<sup>19</sup> For example, in the Commerce Act, s54V regards the interface with decisions under the Electricity Industry Act, and s55I regards decisions under the Gas Act. In the Electricity Industry Act, s32(2) sets out the interface between the Code and what the CC is required to do under the Commerce Act.

<sup>20</sup> For example, s15 and s32(1) of the Electricity Industry Act both reference promoting competition, which is the overarching mandate of the CC. The EA and CC both promote reliability. S54Q of the Commerce Act requires the CC to promote energy efficiency, which is the primary mandate of EECA.

setting out how they will work with one another on matters of common interest. The EA and EECA also have a MOU with MBIE<sup>21</sup>.

Among other things, the inter-agency MOUs explicitly identify matters of common interest where there may be some scope for uncertainties. While the MOUs govern bilateral relationships between agencies, the Council of Energy Regulators (CER) provides an additional forum in which the same matters can be discussed and, if necessary, managed on a multi-agency basis. The CER is discussed further under the heading 'System Stewardship'.

This charter identifies some areas of common interest between regulatory agencies but does not set out how these overlaps will be managed between agencies (i.e. it does not replace or supersede the bilateral MOUs already in place).

## Agency interactions and functions in common with other regulatory systems

The roles of agencies within the energy markets regulatory system also intersect with those of agencies in other regulatory systems, in which case cross-agency engagement is general practice. For example:

- Within the Civil Defence and Emergency Management system, many energy suppliers are 'lifeline utilities' and must ensure they are able to function to the fullest possible extent, even though this may be at a reduced level, during and after an emergency. Therefore energy suppliers have further responsibilities relating to disaster risk reduction, readiness, response and recovery. These responsibilities have the potential to interact with the CC's functions in regulating the price and quality of electricity lines and gas pipeline businesses, and the EA's functions relating to electricity transmission quality standards.
- Promoting energy efficiency in buildings and homes are objectives shared with the regulatory systems for building, housing and tenancy. The adequacy of, and access to, home heating (promoted through EECA's Warm Up New Zealand programme<sup>22</sup>) are also relevant to the health and welfare systems.
- The primary regulatory tools relating to the energy performance of buildings and promoting access to warm and dry homes sit with the building regulatory system and in the housing and tenancy regulatory system. These regulatory tools are complemented by services delivered by EECA (through public information and insulation retrofit incentives) within the energy markets regulatory system.
- The regulation of engine fuel standards, fuel efficiency labelling, and the promotion of biofuels and electric vehicles intersect with vehicle emission standards, excise taxes, and road user charges administered by MOT.

## Monitoring and Evaluation

The monitoring and evaluation function is undertaken in a range of ways across the energy markets regulatory system. These include:

- MBIE has formal responsibilities for monitoring the performance of crown entities in the system against their respective Statement of Intent and Statement of Performance Expectations.

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<sup>21</sup> Copies of the inter-agency MOUs can be found at <https://www.ea.govt.nz/about-us/strategic-planning-and-reporting/mous/> and <http://www.comcom.govt.nz/the-commission/about-us/relationships-with-other-agencies/>.

<sup>22</sup> This programme makes homes warmer, drier and healthier through retrofitted insulation for low-income home owners and tenants.

- All core agencies engage with regulatory system participants when undertaking their respective work programmes, ranging from formal consultation papers to informal industry engagement.
- Formal reviews of policies and regulations are undertaken by core agencies to assess the performance of the system (where specific issues have been identified).
- MBIE collects and publishes a range of energy statistics, including supply and demand by fuel types, energy balance tables, pricing information, international comparisons and greenhouse gas emissions. These are used to monitor energy markets (e.g. identifying trends and issues) and inform related work programmes. The other core agencies also publish a range of data and market performance metrics for a similar purpose.
- The EA, CC, GIC, Utilities Disputes and the Rulings Panels all contribute to monitoring the performance of the system through dispute resolution and compliance enforcement. This is underpinned by the EA, CC and GIC's investigation functions, and complaints raised by both industry and consumers.

## System stewardship

The Council of Energy Regulators (CER) was established to support MBIE's regulatory stewardship responsibilities in the electricity and gas markets. The CER meets quarterly and is made up of the CEOs, or their substitutes, from MBIE, the EA, the CC and the GIC. The CER provides a forum for high level collaboration and information sharing to contribute towards the efficiency and effectiveness of our energy markets regulatory system. The CER takes a whole-systems view to consider regulatory issues and trends in the electricity and gas markets, and identify any overlaps or gaps. The CER also helps to facilitate a coordinated response in addressing issues for which there are overlaps or gaps.

The EA and CC also have an Interface Working Group, which MBIE participates in as an observer. Its purpose is to identify and make recommendations on ways to manage the interface between the role of the EA and the role of the CC, within the existing legal framework, in agreed focus areas. An example focus area that the group will be considering is emerging technologies.

Both of these initiatives are timely in the context of an evolving energy markets system. Emerging technologies<sup>23</sup> in the electricity system are opening up new options to consumers and industry players in how electricity is generated, transported and managed. These technologies can deliver exciting benefits but challenge our current regulatory and policy settings. Both the CER and the Interface Working Group help align the regulators and policy makers to ensure a collaborative approach going forward.

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<sup>23</sup> Including but not limited to solar photovoltaics, distributed and grid electricity storage, electric vehicles and home energy management systems.