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Project Reference Code: ERC0169

**Submission on Proposed Rule Changes: Expanding Competition
in Metering and Related Services**

Introduction

1. Vector Limited ("Vector") welcomes the opportunity to make this submission on the Australian Energy Market Commission's ("AEMC") consultation paper, dated 17 April 2014, on proposed amendments to the National Electricity Rules ("NER") through the:
 - National Electricity Amendment (Expanding Competition in Metering and Related Services) Rule 2014; and
 - National Energy Retail Amendment (Expanding Competition in Metering and Related Services) Rule 2014.
2. The AEMC's consultation paper seeks comments on the model proposed by the Standing Council for Energy and Resources ("SCER") to expand competition in metering and related services for residential and small business consumers, and the supporting changes required to enable competitive arrangements.
3. We also appreciate the AEMC's engagement with Vector managers in Sydney on 23 May 2014 to discuss the matters raised in the consultation paper.
4. No part of this submission is confidential and Vector is happy for it to be made publicly available.
5. Vector's contact person for this submission is:

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Support for greater market competition

6. Vector supports the objective of the SCER Rule Change Request of expanding competition in the metering market. It is consistent with the Government's market-led approach to achieving its efficiency and competition objectives for the electricity sector. It also supports the Government's policy of promoting consumer choice and demand side participation ("DSP") in the sector.
7. As a leading smart meter provider in New Zealand, the views expressed in this and previous submissions reflect our experience in the competitive New Zealand metering market. The New Zealand experience, following a market-led model and retailer-led rollout of smart meters, has shown that while challenging, it is possible to achieve consumer acceptance, positive business cases and a smooth transition all at the same time.
8. In this submission, we suggest some proposals we believe would enable the realisation of these outcomes.

Exit fees

9. There are currently some issues and proposals in the consultation paper that are likely to hinder the emergence of a competitive metering market in Australia. The key issue is **exit fees** for the displacement of legacy meters by smart meters.
10. Vector does not consider that exit fees promote the objective of the Rule Change Request to expand competition in the metering market. Exit fees create a significant barrier to entry that would most likely prevent the emergence of a competitive smart metering market. New and potential entrants should not face exit fees, particularly when the introduction of competition in similar markets have been achieved without resorting to exit fees.
11. While we do not consider exit fees to be desirable, and prefer their removal altogether, we recognise that distributors should be able to recover the costs of their efficient regulated investments. We note that the National Electricity Rules ("NER") do not necessarily mandate the use of exit fees but provide that distributors be reasonably compensated (Rule 7.3A(g)).
12. We believe that regulatory decisions regarding the recovery of these costs should aim to meet key economic and consumer protection principles. Any cost recovery mechanism should 1) minimise market inefficiencies and distortions, 2) provide the right incentives for efficient investment and market entry, and 3) avoid detriment to consumers. Exit fees do not rate well against these principles.
13. The transition to a new technology is not costless but is in the long-term interest of consumers. The transition to smart metering is a complex issue and it would be

challenging to achieve an outcome that simultaneously meets the expectations and needs of all stakeholders. There are, however, precedents for exit fees not being charged. These include the introduction of competition in the electricity retail market and the transition to competitive smart metering for large customers.

14. There are a range of other cost recovery options that the AEMC, AER and stakeholders can consider against regulatory principles. Our preferred approach is a combination of an appropriate unbundled legacy metering charge with the residual cost remaining as part of the standard control service over a considerable period of time. We propose various cost recovery approaches in our response to Questions 16 and 17 in the Appendix. Our proposals remove the need for exit fees and would not involve consumers paying more for their smart meter.

Use of principles and guidelines rather than technical specifications

15. We support the setting of minimum service levels to ensure consistency of minimum service quality delivered to consumers across jurisdictions. However, we do not support proposals that mandate minimum technical specifications. We prefer the development of principles and guidelines rather than technical specifications. As market competition emerges, the need for greater prescription should diminish.
16. In a fully competitive market, minimum service levels may not even be necessary. The discipline of market competition incentivises service providers to win the favour of consumers by providing improved services at highly competitive prices.
17. We are concerned with the proposed minimum technical functionalities for metering. This does not appear to be aligned with the AEMC's recent decision following its review on a *Framework for open access and communication standards* ("Open Access and Communication Standards Review"), which recommended the use of a services-based common market protocol (while allowing other market protocols to co-exist) instead of mandating technical standards.
18. As discussed in our submission to the AEMC on that review, mandating technical standards or specifications would:
 - limit market competition;
 - dampen investment incentives;
 - stifle technological and service innovation;
 - compromise technology neutrality;
 - shift upfront risks from investors to consumers; and
 - increase implementation and compliance costs.¹

¹ <http://www.aemc.gov.au/getattachment/16c3f7c3-6a1c-463a-8b79-9615cfbcd42/Vector.aspx>

19. We discuss our view further in our responses to Questions 21, 22 and 23 in the Appendix.

Responses to specific questions in the consultation paper

20. We set out our responses to the specific questions in the consultation paper in the **APPENDIX**. These responses support the overall view we express above.

21. We would be happy to further discuss any aspect of this submission with AEMC officials and staff.

Yours sincerely



Bruce Girdwood

Group Manager Regulatory Affairs

APPENDIX: Vector's responses to specific questions in the consultation paper

Question 1: Are there any additional criteria that should be considered in assessing this rule change request?

1. Vector agrees in principle with the AEMC's proposed assessment framework, which considers the SCER Rule Change Request ("the Rule Change Request") in relation to the following criteria: 1) facilitating competition, 2) transparency and predictability, 3) administrative burden and transaction costs, and 4) consumer protection. We agree with these criteria, in principle. We believe they will promote the Government's competition and efficiency objectives in the metering market and the wider electricity sector, and the long-term interest of consumers.
2. In addition, it is paramount that the imposition of exit fees be assessed against the key regulatory and consumer protection principles identified in the letter above, namely: 1) minimisation of market inefficiencies and distortions, 2) promotion of efficient investment and market entry, and 3) avoidance of harm to consumers.
3. We emphasise the need for the AEMC to rethink the use of exit fees, given its potential adverse impact on investment and market entry incentives. This could frustrate the Rule Change Request's objective of expanding competition in the metering market. We **recommend** that the AEMC seriously consider and further develop the alternative cost recovery options we present in our response to Questions 16 and 17 below, which avoid the need for exit fees altogether.

Question 2: What are the benefits for competition by allowing any registered and accredited party to take on the Metering Coordinator role?

Question 3: Are there alternatives that are preferable to creating a separate Metering Coordinator role? For example, would it be appropriate to combine the proposed Metering Coordinator responsibilities with the existing Metering Provider role? If so, what advantages would this alternative deliver?

4. Making the role of Metering Coordinator contestable would ensure that the best party capable of providing the service will, in fact, end up providing it. Limiting it to specific parties creates a barrier to entry for those who could potentially provide better and more competitive services to consumers. An independent Metering Coordinator has financial and commercial incentives to provide additional services to third parties and consumers outside the base services provided by a distributor, as it seeks a greater financial return on its existing assets.
5. We have no issue with the roles of Metering Coordinator, Metering Provider and Metering Data Provider being distinctly defined. However, where it would be efficient for a willing provider to assume two of the roles or all three roles, such arrangement

should not be prevented. In a competitive market, market discipline and dynamics facilitate parties coming into various forms of commercial agreements to reduce costs and improve service delivery for consumers. It is not unreasonable to expect that a single entity could fulfil all three roles. Greater efficiencies through combined roles lower operational costs and have a positive knock-on effect on consumers.

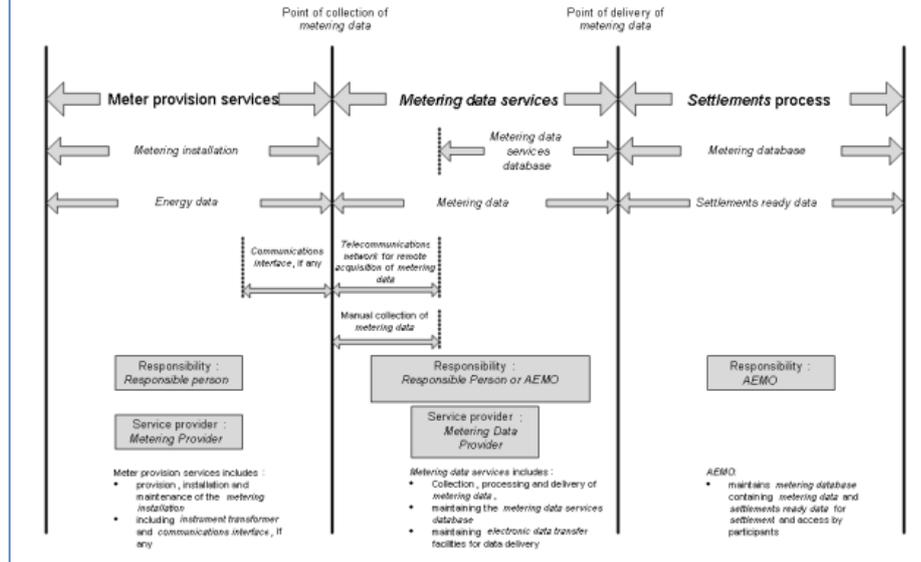
6. Given the existing roles in the marketplace, the simplest change seems to be to reallocate the Responsible Person's role to the Metering Coordinator and retain the three roles. The definition of the roles should reflect the outcome of the AEMC's Open Access and Communications Standards Review. The Review recommended that a common meter protocol is not required to support open access communication directly with the meter. Instead, a shared market protocol is proposed to allow open access to services from the "gatekeeper" to authorised parties. To make this work, we propose that:

- the Metering Provider role be expanded to include responsibility for the provision, installation and maintenance of remote two-way communication to the metering installation;
- the Metering Provider fulfil the role of gatekeeper and implement the shared market protocol;
- the Metering Data Provider role be clarified, making it clear that for smart meters, the Metering Data Provider does not require remote access direct to the meter to collect energy data, but instead collects the energy data via the remote interface (shared market protocol) provided by the gatekeeper; and
- the Metering Coordinator maintains the responsibility to ensure the required services are provided by the Metering Provider and Metering Data Provider.

7. To reinforce the proposed rules, the AEMC should consider the following:

- In Figure 4.1 of the NSMP MFS Version 1.3 (as attached to the Rule Change Request), the scope of Smart Metering Infrastructure ("SMI") is defined. We propose that the Metering Provider be responsible for the provision, installation and maintenance for the full scope of the SMI. The MDP should not have any responsibility for any SMI.
- In Schedule 7.1 of the NER, Chapter 7 (see figure below), we **recommend** that the responsibility for "Telecommunications network for remote acquisition of metering data" be reallocated from the Metering Data Provider to the Metering Provider and amended to "Telecommunications network for remote acquisition of energy data".

Schedule 7.1 Responsibility for metering installation and metering data



8. We support the proposal giving the retailer the right to appoint the Metering Coordinator, by default, should the consumer not appoint a Metering Coordinator.

Question 4: If established, should the new Metering Coordinator role be classified as Registered Participant under the NER or should other arrangements be put in place? If so, what accreditations may be required?

9. We agree that the new Metering Coordinator role should be classified as a Registered Participant in the NER.
10. We would prefer accreditation requirements to be based generally on requirements that are widely accepted and well known to market participants. This would ensure a smooth transition that would not impose onerous costs on those seeking accreditation.
11. The accreditation of a Metering Coordinator should include validating the applicant's:
- ability to meet previous Responsible Person obligations or similar obligations;
 - appropriate handling of customer protection processes, e.g. obligations related to consent and notification; and
 - appropriate handling of notifications to market participants.

Question 5: Are there specific arrangements required in the event that a Metering Coordinator fails?

Question 6: Should there be any specific changes to the ROLR arrangements regarding metering?

12. If a Metering Coordinator is also the Financially Responsible Market Participant ("FRMP") or is elected by the FRMP, it would be sufficient to place an obligation on the FRMP to ensure a Metering Coordinator is appointed for each metering installation. The FRMP (e.g. retailer) should be able to appoint another Metering Coordinator if the current one faces financial failure.
13. The situation is more complicated where the customer elects a party other than the FRMP or distributor to be the Metering Coordinator, and the Metering Coordinator fails. It is possible and more likely that multiple FRMPs will be affected by a Metering Coordinator failing, and it may be appropriate for the Australian Energy Market Operator ("AEMO") to coordinate an industry-wide response to the event. Escrow arrangements may not be sufficient to ensure continuity of metering services. The most likely response is for another Metering Coordinator to negotiate a commercial arrangement to take over the failed business
14. We envisage the insolvency of a Metering Coordinator to be a rare event. As competition emerges, we can expect the development of efficient market processes that enable retailers to win customers and receive metering data services from the failing Metering Coordinator or its service providers (Metering Provider, Metering Data Provider). We expect the standard churn/switching procedures to be able to support a retailer-of-last-resort ("ROLR") event.
15. We **recommend** that the AEMC, or a working group established to consider transitional options, review existing arrangements to determine whether existing market arrangements and/or general insolvency legislation are sufficient to address a Metering Coordinator's failure. If it is determined that "residual risks" still exist (i.e. there is still a market failure or there are remaining inefficiencies), the working group could provide advice on:
 - what new arrangements could be established or existing ones could be expanded to the Metering Coordinator role to ensure the efficient transfer of consumers to another Metering Coordinator;
 - the least disruptive process for the expeditious restoration of normal market processes;
 - what specific arrangements should be put in place to ensure supply to any consumer is not interrupted, ensuring that consumer confidence is not undermined;

- the cost allocation mechanism that would ensure inefficient costs are avoided, i.e. ensure that only the 'causer pays' and costs are not socialised to other industry participants;
- which party would be responsible for communicating the failure of a Metering Coordinator to relevant industry participants (should this be required) to ensure it is done in an expeditious and cost-effective manner; and
- the potential impact of any residual risks on other industry participants and how this would be addressed.

Question 7: How would the proposed jurisdictional arrangements impact on the proposed approach for competitive provision of metering and related services?

Question 8: Should SCER's proposal for prescribing Metering Coordinator exclusivity be limited [to] certain metering types? If yes, what are the metering types that should be considered?

16. As a transitional measure, we have no issue with allowing a class of Metering Coordinators exclusivity in coordinating metering services for "basic metering services" (i.e. services not subject to competition such as Type 6 meters or street lighting where there is no apparent benefit of opening the service to competition). We assume the eventual widespread displacement of Type 6 meters would effectively end the Metering Coordinators' exclusivity in that market or the end of that market itself in the relevant areas.
17. In relation to (non-regulated) smart meters, Metering Coordinators should be allowed to coordinate all types of meters. Market participants make commercial decisions based on their portfolio of services and the optimal mix of services they could deliver to their customers. This is influenced by the efficiencies obtained from the inter-linkages and interdependencies of the various services they offer. Limiting the types of meters the Metering Coordinator can consider would mean opportunities to achieve such efficiencies would be missed and would not be passed on to consumers.

Question 9: What information and consent requirements would be appropriate under the competitive model for provision of metering and related services?

Question 10: Should opt-in / opt-out provisions apply where a party seeks to upgrade a consumer's metering installation to achieve business operational efficiencies that may lead to reduced costs for consumers?

18. We believe section 6.1.1 in the consultation paper ("Consent arrangements") is misguided. It proposes to require retailers to seek consumer consent before changing

the services available from their metering installation and to give the consumer the right of opt out. If implemented, this would mean a need to consult with each consumer as part of the smart meter rollout and then provide each consumer a bespoke metering product that contained only the services they wanted.

19. There may be circumstances where the retailer would choose to deploy metering that is 'cost neutral' to the consumer and has little or no impact on the consumer other than the installation process. This would have no impact on the consumer whatsoever (in the short term) but could, in fact, result in reduced costs for the same consumer (in the long term).
20. The requirement to inform the consumer of all changes that would have no impact on the charges they face and services delivered to them would be excessively costly. It is also unnecessary as there is nothing stopping a meter being installed that is *capable* of delivering services X, Y and Z, but the consumer agreeing with their retailer that they only wanted service X. It is often the case that the smart meter would have multiple services available; the cost of canvassing each customer on the services they want to opt out of would be prohibitively costly.
21. It is not unreasonable to assume that many consumers would not want to be bothered with any information that would have no impact on their charges or the services they receive.
22. Further, if a meter was to contain a service of benefit to the network (e.g. notification of a voltage drop) then we do not see any reason why consumer consent is necessary.
23. We **recommend** that the AEMC rethink the cost implications of the above proposal, or make it voluntary, not compulsory.

Question 11: Should retailers be required to inform consumers of their metering services charges? If so, what is an appropriate means for retailers to fulfil this obligation?

24. This proposal could be onerous on retailers, particularly during the transition period. It should be left to retailers to determine the most appropriate means of informing their customers of their charges. It is retailers who know the most efficient and cost-effective way of communicating with their customers, and what their customers (or various groups of customers) need or prefer. This proposal should be voluntary, not compulsory.
25. Mandating a single way of informing consumers would severely limit service providers' ability and the use of new and emerging technologies, such as more timely and interactive apps. It may stifle innovation and improvements in retailers'

engagement with their existing and potential customers and in how they keep raising the bar to win their customers' loyalty.

26. Our experience in the competitive New Zealand metering market is that market competition provides strong incentives for service providers to advertise their service offerings (including charges) through the most effective communications media available. The AEMC should focus on enabling greater competition in the metering market, rather than mandating how consumer information should be delivered. In a competitive market, consumers have the benefit of being able to choose their retailer, pricing plans and services or service bundles that would best suit their preferences.
27. While price is a key determinant in many consumer decisions, there are other factors that influence consumer choice. This includes how the service is bundled with other services and their impact on the total price and consumer experience. For example, Trustpower in New Zealand now provides a 'triple-play' offering of electricity, gas and broadband services. Service providers should be allowed to determine how they could best convey what they charge (as standalone services or a package) their customers. This would enable customised information to be provided to consumers.
28. What the AEMC can do to promote consumer awareness (including what they pay for electricity retail services) is to encourage various jurisdictions to enable efficient consumer access to information on what's available in the market. For example, the New Zealand Electricity Authority's "What's My Number?" campaign enables consumers to easily compare and switch retailers. This has increased consumers' propensity to switch to retailers that provide better deals.²

Question 12: Should the relationship between the retailer and the Metering Coordinator be based on a commercial arrangement? If not, what alternatives should be considered? What are considered the costs and benefits of a standard contract for this relationship?

29. Yes. Commercial arrangements between the retailer and Metering Coordinator (rather than regulated arrangements) should be promoted as market competition emerges. Unlike in a retailer-small consumer supply arrangement, both parties in this case are of significant size and would have the wherewithal to negotiate contract terms that would suit their preferences.
30. The development of standard contracts is unnecessary in an increasingly competitive market. It would stifle contracting innovation that could benefit consumers. In some circumstances, it may be one of the parties that would request special terms to better meet its unique requirements or those of its customers.

² <http://www.ea.govt.nz/about-us/media-and-publications/media-releases/2013/september/>

31. We believe the development of contracting guidelines (rather than a standard contract) would be more appropriate. A commercial, rather than a regulated, approach to contracting would be consistent with the Government's market-led approach for the metering sector.
32. On page 44 of the consultation paper (last bullet), the focus on meter functionality seems misplaced:

SCER recognises that a competitive framework...should seek to [*ensure*] that functions/services provided by the meter should be the same irrespective of the retailer.
33. This misses the point around competitive markets – that retailers should be able to compete on the basis that they can offer different services from another retailer. As emphasised above, greater prescription should become unnecessary as market competition emerges.
34. The consultation paper appears to take the view that meter churn is inefficient (page 45). Our experience in the competitive New Zealand metering market demonstrates this has not been a big issue. Meter churn is effectively dealt with by market participants through their wholesale agreements.
35. We do not consider meter churn, or even metering provider churn, to be a necessarily harmful outcome depending on who bears the cost. It could be a reflection that inefficient meters or metering providers are being displaced from the market. The sooner efficiencies are recognised by market participants, the less it would cost them to rectify those inefficiencies or exit the market.

Question 13: Should residential and small business consumers be able to exercise a right to appoint their own Metering Coordinator? If so, what arrangements would need to be put in place to govern that relationship?

Question 14: Are any additional consumer protections required to support a direct relationship between a consumer and a Metering Coordinator?

36. We agree that residential and small business consumers should be allowed to appoint their own Metering Coordinator. We do not, however, expect this to become the predominant practice, as their main interest is the reliable supply of electricity at a price they can afford or find acceptable. Having them deal with the retailer and metering provider separately could only increase consumer costs (e.g. time costs and inconvenience).
37. We therefore support having the retailer appoint the Metering Coordinator as a default arrangement should the residential or small business consumer not make that choice.

38. We agree that consumers should be able to engage directly with a Metering Coordinator. The AEMC should assess whether existing consumer protection in relation to consumer-retailer relationship could be adopted or expanded to new Metering Coordinator-consumer relationships, particularly whether it would provide appropriate and sufficient protection for small consumers.
39. All Metering Coordinators should be bound by the same standards of accreditation and service standards to ensure that long-term consumer experience is not adversely impacted, and to avoid inefficient meter churn.

Question 15: Do the NER require any changes to facilitate unbundling of metering charges from distribution use of system charges? If so, what factors should be considered?

40. We **recommend** that the NER clearly provide that a customer should not pay more than once for metering services. A customer should only pay metering service fees to the party who is bearing the cost of providing that service.
41. Question 15 needs to be considered in the context of exit fees and how distribution businesses can recover the costs of efficient regulated investments without significant distortions to investment and market entry incentives, and harm to consumers. Whether changes to the NER are required should be a matter of consequence.
42. We explain in detail our view on unbundling charges and exit fees in our response to Questions 16 and 17 below.

Question 16: Should the AER have a role in determining exit fees for accumulation and manually read interval meters?

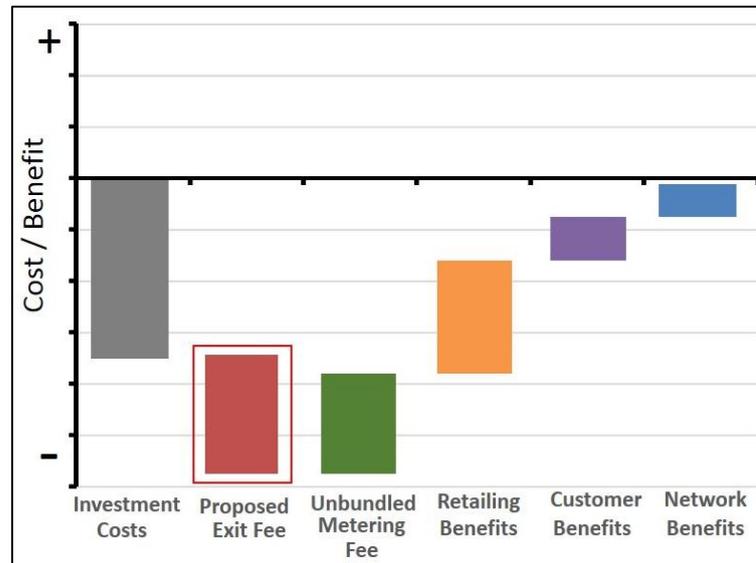
Question 17: If so, are SCER's proposed criteria for determining exit fees appropriate, and should a cap on fees be considered?

43. The AEMC's consultation paper (page 51) calls for the exit fee to be equal to the average depreciated value of a distributor's asset base plus any operational costs associated with processing the exit fee. We understand this could lead to an exit fee of \$67-\$197 in NSW. The key cost driver is the historical level of investment in higher-cost Type 5 metering. We understand these costs include administration fees for meter displacement at ~\$50 per meter, which we consider to be excessive.
44. Vector does not consider that exit fees (for accumulation and manually read interval meters) would promote the objective of the Rule Change Request of expanding competition in the metering market. Exit fees are a significant hurdle for potential

investors, particularly for a first-mover investor (which subsequent investors may not have to face).

45. The adverse impact of exit fees on investment and entry decisions is illustrated in Figure 1 below.

Figure 1. Exit fees as a significant cost barrier to market entry



46. The higher the exit fee, the greater the cost barrier that must be overcome by any potential entrant in making a competitive business case. In our view, exit fees are likely to prevent (at best, significantly delay) the emergence of a competitive smart metering market for residential and small business consumers until such time that the fees are reduced. Should investment in smart metering be stifled or delayed, there is a risk that the temptation to impose a regulated rollout would emerge. We would not want a regulated rollout of smart meters replicated in other jurisdictions, as was undertaken in Victoria, which resulted in cost blowouts to consumers.
47. While we do not consider exit fees to be desirable (and would prefer them to be removed altogether), we recognise that distributors can reasonably expect to recover investment costs in legacy metering technologies where those costs were approved by regulators. The transition to a new technology is not costless; however, we believe the recovery of these costs should be undertaken in a way that creates the lowest distortionary effect on investment and market entry incentives, and in a manner that would not harm consumers. Exit fees do not meet these tests.
48. In particular, new investment decisions should not have to take sunk (investment) costs into account. Sunk costs are unavoidable and including them in decision making leads to sub-optimal investment or a decision not to invest. This could occur despite the incremental benefits being greater than the incremental costs on a purely

economic basis. Efficient investment only considers the incremental costs and benefits involved.

49. Additionally, there is a risk that any proposed administration fee could be excessive. It is our understanding that administration fees are intended to recover the costs of removing the metering information from the distributors' systems. Even if this process is manual, it should not could cost so much. If the process could be automated, we would expect the cost to be low. In principle, if administration fees are charged, they should be no higher than the efficient and reasonable costs of a distributor and distributors should be incentivised to manage these costs as efficiently as possible.
50. We note that the NER does not mandate the use of exit fees, but provides that "the Local Network Service Provider...[be] reasonably compensated for the alteration to the *metering installation*" (Rule 7.3A(g)).
51. We also understand that competition in retail and large customer metering was introduced in Australia *without* exit fees. Imposing exit fees for the displacement of legacy meters for residential and small business consumers means these consumers are being charged to enter the competitive metering market, while larger customers paid nothing. We also understand that exit fees had been waived overseas for some environmentally friendly power generation and small generators.
52. To minimise inefficiencies and market distortions in the recovery of distributors' regulated investment costs, we **recommend** that any sunk cost recovery mechanism should meet the following principles:
 - *not distort efficient investment*, i.e. marginal prices should equal marginal costs. Residual costs should be recovered through non-distortionary methods;
 - *minimise investors' perceptions of regulatory risk*. This is promoted through consistency and stability in policy and regulatory settings and across jurisdictions; and
 - *not lead to stranded investment*. Writing off the value of regulated assets would increase investor perceptions of regulated risk. This could lead to an increase in the sector's Weighted Average Cost of Capital which would be applied over a much larger asset base.
53. We consider options for recovery of the legacy metering costs against the above principles:
 - **Option A: No sunk cost recovery**. This option would not distort efficient investment in the smart metering market as it ensures sunk costs would not

be taken into account by new entrants when making investment decisions. However, it is contrary to the principles that investors' perceptions of regulatory risk should be minimised and stranded investment should be avoided.

- **Option B: Exit fee mechanism.** This option would ensure that distributors can recover their sunk costs, so would avoid stranded investment. However, it would substantially distort investment decisions and inhibit the emergence of market-led smart metering and associated consumer and industry benefits. It is also inconsistent with the precedents mentioned above when retailing and large-customer metering became competitive.
- **Option C: Appropriate unbundled metering service fee.** This option would ensure the unbundled metering service fee (which has yet to be set) includes a portion for sunk cost recovery. This fits reasonably well with the principles above and has advantages of consumer transparency and consistency. However, the fee may need to be set at a uniform level across the networks and thus, on its own, might not be able to recover all sunk costs on all networks.
- **Option D: Enable asset value to be recovered as part of standard control service.** This option would be consistent with the principles above. However, it may lead to some concerns regarding transparency of and justification for the charges.
- **Option E: Combination of options C and D.** In our view, this option would have the ability to overcome the disadvantages with options C and D while retaining the benefits. It may be the best available option.

54. The above options remove exit fees and do not require consumers to pay more for their smart meter. We recognise that different options may be more applicable to particular distributors; hence, they may have to be considered on a case-by-case basis. We **recommend** that the AEMC provide guidance to the AER on how any of the above options could be implemented in relation to distributors' regulatory settings for the next regulatory control period.
55. Should the AEMC still pursue the imposition of exit fees, we **recommend** that a cap be placed on exit fees to avoid these fees inhibiting market entry and frustrating the policy objective of expanding competition in the metering market.
56. We believe that the AER is the appropriate regulator to determine any exit fees, given the inter-linkages between exit fees and the setting of regulatory settings for distributors for the next regulatory control period.

Question 18: Are the existing arrangements under the NER appropriate to enable a distribution network business to allow for advanced metering technology as part of a regulated DSP business case/program?

Question 19: If not, what additional arrangements might need to be put in place to allow sufficient certainty to distribution businesses to do so?

57. Any distributor should be able to propose, as part of its regulatory determination, a programme of investment in DSP. The AER can then monitor these on their merits. This could be a competitive part of the distributor's business or third party service provider's services to the distributor.
58. However, it should be recognised that it is not only distributors that could facilitate the promotion of DSP; other providers of smart metering services also contribute to the achievement of this policy objective. There should be a 'level playing field' for DSP investments, and distributors have as much right as any other party to invest in DSP.
59. The AEMC can facilitate DSP by promoting a fully competitive and dynamic smart metering market that would provide efficient incentives to all market participants and transparent pricing for consumers. Such a dynamic market would enable distributors to establish commercial relationships with third party Metering Coordinators and other service providers and encourage the competitive provision of services that facilitate DSP.

Question 20: Are changes required to the AER's ring fencing guidelines to accommodate a distribution network business seeking to take on the role of Metering Coordinator?

60. Yes.
61. We **recommend** that the AEMC develop ring fencing guidelines for a distributor seeking to become a Metering Coordinator. The AEMC could seek advice from the appropriate working group in developing these guidelines, and release them for stakeholder consultation.

Question 21: What do you consider are the appropriate governance arrangements for allowing for a new smart meter minimum specification in the NER?

Question 22: Is AEMO the appropriate body to develop and maintain the proposed minimum functionality specification to support competition in metering and related services, or are there alternative options that could be considered?

62. Vector does not support mandating minimum (technical) specification for smart meters. We instead support the promotion of guidelines for minimum service levels and an outcomes-based approach, which ensure consistency in the minimum quality of service that consumers across various jurisdictions experience. Low-level technical specifications will increase the risk of obsolescence and increase costs for providers and consumers, defeating the Rule Change Request's objectives of promoting competition and consumer choice.
63. Vector supports the use of international standards wherever possible. Australia has the ability to adopt and influence international standards via established processes in Standards Australia. These processes should be implemented in an efficient way should the need for technical specifications be identified.
64. The service provider, not any regulator, is the best judge of the technical specifications and mix of resources that would deliver the same, if not better, services to its customers. Some of these efficiencies could be achieved more cost effectively through other means; for example, customer supply monitoring may be done more efficiently as a back office function rather than through the meter.
65. Mandating or promulgating minimum technical specifications is not consistent with the AEMC's own decision not to impose prescriptive technical specifications/protocols (defining service levels rather than technical standards). Following its recent Open Access and Communication Standards Review, the AEMC recommended that:
- ... a shared market protocol be adopted, which would define the format of the communications between authorised service providers and the parties ("gate keepers") that manage access to a smart meter's functionality. The shared market protocol should be a services-based standard that is built on extending the business-to-business systems maintained by the...AEMO.
- ... In order not to stifle innovation, we also recommend that the use of other communication protocols should be allowed.³
66. The promotion of minimum service levels, instead of minimum technical functionalities, ensures that services delivered meet well understood business needs of market participants. The focus should be on improving service providers' delivery of the most cost-effective service outcome, as opposed to just meter functionality.
67. In addition, distributors must be required to provide open access to the legacy metering installation and access data (meter types, location, access requirements, etc) to facilitate entry to the smart metering market and the deployment of smart meters.

³ <http://www.aemc.gov.au/getattachment/4fb3d76b-9711-42ed-a65e-a1fce7d4f055/3-Information-Sheet-Final-Report.aspx>, page 1

68. We consider the AEMO to be the appropriate body to govern the setting of minimum service levels in the context of the shared market protocol. And we consider Standards Australia to be the appropriate body to govern technical specifications to ensure Australian alignment with international standards.
69. In this connection, we suggest the AEMC and AEMO promote the consideration of standards internationally, i.e. not only focusing on Australia-specific standards. A wider lens would facilitate the discovery process by market participants of what standards would be most suitable in the Australian context. This would ensure the most cost-effective standards are adopted over time, lowering costs for service providers and ultimately, consumers.
70. We also emphasise the importance of promoting the concept of displacement rights if the meter cannot meet the “market requirements”. The definition of market requirements is going to be a challenge. We would like to clarify under what basis a meter will be allowed to be replaced from a competitive point of view. From an investment perspective, if there is an arbitrary displacement risk (e.g. solar installer providing metering instead of the retailer), then the life expectancy of the meter will be far shorter, which in turn, will increase the price/cost and defeat the ‘consumer neutral’ business case.

Question 23: Should there be arrangements that allow for jurisdictions to determine their own new and replacement policies or should all new and replacements meet a common minimum functionality specification?

71. To avoid exacerbating and perpetuating exit fee issues, jurisdictions should not be required to mandate common minimal technical/functionality specifications. For example, Vector does not support the South Australian Government’s proposed policy requiring the installation of ‘smart ready’ meters by default where a new or replacement meter is required.⁴
72. As stated in our response to Questions 21 and 22, we have no issue with jurisdictions being allowed to mandate service outcomes, but not technical specifications. Policies mandating functionality/technical specifications are not necessary to facilitate the deployment of smart meters. We believe it would instead produce unintended outcomes that would not support the Government’s market-led approach for the development of a competitive metering market.
73. Mandating functionality specifications or particular technical standards effectively mandates the use of a particular type of metering technology – the technology preferred by the distributor or that is compatible with, for example, a mandated ‘smart ready’ meter. The same technology may well not be the technology of choice

⁴ Vector Limited, *Submission on the South Australian Policy for New and Replacement Electricity Meters*, submitted to the South Australian Department for Manufacturing, Innovation, Trade, Resources and Energy, 27 March 2014.

by future smart meter providers. This implies that market participants or potential investors who prefer to use alternative metering technologies could be 'locked out' of the market, creating a barrier to market entry and limiting competition.

74. Mandating technical specifications may also stifle technological and service innovation. It is unlikely to provide meter providers with the right incentives to introduce more efficient and innovative equipment and services to the market. Under such circumstances, there is a risk they could become more regulator-focused instead of delivering innovative and competitive services and better anticipating their customers' needs and expectations.
75. Prescribing technical specifications are also likely to raise exit fees as the cost of deploying 'smart ready' meters would need to be recovered should these meters be displaced through competition. This would create another barrier to market entry in the form of increased legacy metering costs that distributors will seek to recover. And would further delay the deployment of smart meters, depriving consumers the benefits from an early uptake of smart metering services.
76. Importantly, upgrading meters to be 'smart ready' would not significantly reduce the cost of any future smart meter rollout as it is just as cost-effective to displace the entire meter as it is to install a communications pack.
77. One way to minimise transition costs is to allow distributors to deploy low-cost legacy meters (not 'smart ready' meters) until such time that competition emerges in the metering market. This will keep the costs of the metering assets that distributors need to recover at a lower level than if the distributor were to upgrade their meters to be 'smart ready'. The meters that distributors should install should be 'fit for purpose', i.e. they match the services required by stakeholders at that metering point.

Question 24: Is it appropriate that the Victorian distribution network businesses would become the Metering Coordinator for the smart meters they have deployed?

78. Victorian distribution businesses should be required to align their metering services with the obligations of the equivalent Authorised Parties and Service Providers in the National Electricity Market, once the rules for competitive metering are in place. As such, it is appropriate for Victorian distribution businesses to assume the role of Metering Coordinator and to fulfil their obligations as Metering Provider and Metering Data Provider.

Question 25: Should an exclusivity arrangement be put in place to allow Victorian distribution network businesses to continue in the Metering Coordinator role for a specified period of time? If so, should this be determined by the Victorian Government or defined in the NER?

Question 26: Should Victoria's local distribution network business be required to take on the Metering Coordinator role as a ring fenced entity after the exclusivity period has ended?

79. We do not object to the proposal granting Victorian distributors exclusivity arrangement to continue in the Metering Coordinator role for a specified period of time. Exclusivity arrangements, however, should be phased out as soon as possible.
80. In the long term, the new role of Metering Coordinator should be open to any party that wishes to assume it, including Victorian distributors on their own natural monopoly networks, retailers, metering providers or end consumers. This would promote competition and ensure that the party best able to deploy smart meters and provide the required services does so, which is to the benefit of Victoria's electricity consumers.
81. Where the smart metering provider is a vertically integrated business (both a distributor and smart meter provider on the same network), ring-fencing arrangements should be put in place. This is regardless of whether it is part of a transition to a competitive arrangement or in an already workably competitive market.
82. We believe the Victorian Government itself is best placed to determine the transition path it should take towards a competitive metering market, rather than following rules defined in the NER. It would provide the Victorian Government and participants in the state's electricity sector greater flexibility in responding to changing technologies and market dynamics as competitive pressures start to take effect.

Question 27: Is it appropriate that as part of the transitional arrangements, the local distribution network business would become the initial Metering Coordinator for existing meters for which it is the Responsible Person?

Question 28: If so, should the local distribution network business be required to take on this role as a ring fenced entity? And by what stage of the transition would the ring fenced entity need to be established?

83. The new role of Metering Coordinator should be open to any party that wishes to assume it. This will ensure that the party best able to provide the required services does so, benefitting consumers in the long term. Metering contestability, reversion policies and minimum service levels will create a healthy competitive market moving forward.
84. Where the local distributor or retailer becomes the initial Metering Coordinator for existing meters they are responsible for, it is appropriate to impose ring-fencing

arrangements for a defined period. This should not, however, prevent other parties that could make a better business case from providing the service in the near future.

85. Ring fencing is most appropriate if the distributor's metering business is continuing to compete in the competitive market for smart meters. It may be more efficient and cost effective for all parties to have Type 5-7 metering businesses remain with the distributors as they wind down and the meters are gradually replaced.

Question 29: Is it appropriate that as part of the transitional arrangements, retailers would become the initial Metering Coordinator for existing meters for which it is the Responsible Person?

86. It is appropriate that a retailer become the Metering Coordinator for installations where it is currently the Responsible Person. This is likely to only significantly impact Type 4 installations which are already competitive.

Question 30: Are there any other systems, procedures or guidelines that might need to be amended to support competition in metering and related services?

Split incentives

87. In our view, it is also important to consider the issue of split incentives. Split incentives can arise when different stakeholders are exposed to only a portion of the overall costs and benefits, i.e. the party making the investment cannot capture the full benefits, many of which accrue to other parties that may seek to 'free ride' on the investment. In such circumstances, levels of investment will tend to be less than is socially optimal.
88. In the case of smart metering, split incentives arise among the various parties due to the allocation of costs relative to the allocation of benefits. Neither the network, nor the retailer or third party metering service provider can efficiently capture the benefits of all the other parties, while the investor must bear virtually all of the upfront costs.
89. Bilateral negotiation of the value of network benefits on a network-by-network basis should, in theory, address this problem. However, this approach has relatively high transaction costs, which may explain the lack of any negotiated payments from networks to date, after more than five years of the smart metering technology becoming generally available to the market.
90. Addressing the split incentives issue in smart metering is warranted even in the case where sunk costs are excluded from the exit price in order to maximise economic efficiency.

91. We **recommend** that the AEMC ensure that any proposed measure minimise, if not avoid altogether, the presence of split incentives.