

**Submission on the
Initial Reset of the DPP for Electricity Distribution
Businesses**

Draft Determination Consultation Update Paper

Technical Consultation

From the Electricity Networks Association

20 November 2009

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1. Introduction

1. This submission, from the Electricity Networks Association (ENA), is in response to the Commerce Commission's (the Commission) Consultation Update Paper (for technical consultation) on the draft determination on the Initial Reset of the DPP for Electricity Distribution Business (Consultation Update Paper).
2. The Consultation Update Paper has been issued following consultation on the Draft Decisions Paper and the Draft Determination which set out the Commission's initial decisions and first draft of the Determination in respect of the Reset DPP to apply from 1 April 2010.
3. As requested, the scope of this submission is limited to comments on the technical drafting of the Initial Reset Determination (provided as Appendix D to the Consultation Update Paper). We have presented our comments on each of the clauses in the Initial Reset Determination in turn, consistent with the format of the determination included in Appendix D.
4. The ENA's contact person for this submission is:

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2. Application and Interpretation

Electricity Lines Services

5. The Consultation Update Paper indicates that the previous references to Electricity Distribution Services are to be replaced with references to the Section 54C definition of Electricity Lines Service. The ENA supports this amendment. Our previous submission that this definition must be supplemented by provision for Excluded Services for the purpose of the DPP has however not been accepted. The Consultation Update Paper indicates that the Commission agrees with submissions that some of the services excluded under the Thresholds continue to be excluded under Part 4 by virtue of the electricity lines services definition. (Appendix A, Row 3).
6. It is not clear what services the Commission is referring to and we suggest that the Commission clarifies its position in the Final DPP Decisions Paper in particular in respect of the services it believes are now included under the DPP which were previously excluded under the Thresholds.

Transmission Charges

7. We acknowledge the changes made to the definition of transmission charges. The edits however fail to accommodate the issue we raised in our previous submission regarding the provision of transmission services that are sold by one EDB to another. At least one EDB currently provides another with transmission services (effectively a pass through of Transpower charges) as not all EDBs have direct access to the transmission grid. Accordingly the definition of transmission charges needs to be changed to refer to the Transmission System rather than Transpower. If this change is not made, those EDBs without direct access to the grid will not be able to include any transmission charges in their pass through costs.

Transmission Charge means any amount in respect of:

- (a) Electricity Lines Services provided to a Non-exempt EDB ~~by Transpower~~ in respect of the Transmission Grid in accordance with the Transmission Pricing Methodology; and
- (b) the provision of System Operator Services; and
- (c) new investment contracts, as defined in Schedule F5 of section IV of Part F of the Electricity Governance Rules 2003, ~~between Transpower and a non-exempt EDB~~; and

(d) Avoided Transmission Charges.

Avoided Transmission

8. The Consultation Update Paper indicates that the Commission has decided that the definition of Avoided Transmission Charges will not be amended. This is contrary to our previous submission on the topic and there is no explanation as to how the Commission has reached this conclusion. The definition included in the Determination has introduced a change to the avoided transmission provisions which were included in the Thresholds, as indicated in our earlier submission. To the best of our knowledge there has been no discussion or consultation about this change and no opportunity for interested parties to consider the potential impact of this. The Draft Determination now removes the mechanism in the price path for accommodating changes in the distribution and transmission boundary. This introduces a disincentive for Non-exempt EDBs considering the purchase of assets, such as spur lines, from Transpower. Accordingly, the definition of Avoided Transmission must be amended, as follows, to avoid such disincentive, which was previously accommodated in Clause 5(4) of the Thresholds.

Avoided Transmission Charge means:

(a) any expense (including the cost of capital) of a Non-exempt EDB that arises during the Assessment Period from any activity which substitutes for the use of the Transmission System; and

(b) where Electricity Lines Services are transferred between Transpower and a Non-exempt EDB includes the value of the Transmission Charges avoided from the date of the transfer

Pass Through Costs

9. The revised definition of Pass Through Costs introduces unnecessary complexity to the compliance process for Annual Compliance Statements. The inclusion of the requirement to demonstrate “*to the satisfaction of the Commission*” is unworkable as Auditors are unable to assess whether this requirement is met when auditing Compliance Statements and EDBs are unable to assess this standard when preparing their Annual Compliance Statements.
10. We also submit that this requirement is excessive, as it is a standard which is not used throughout the Determination, and nor should it be. In compiling an Annual Compliance Statement a Non-exempt EDB must provide sufficient evidence to support its entire statement to the satisfaction of the auditor. Where amounts have been omitted from Pass-Through Costs due to the transparent pass

through to consumers/retailers, the Non-exempt EDB will need to provide sufficient evidence of the pass through to satisfy their auditor. This is reasonable and sufficient. The Determination therefore requires the following amendment:

Pass-Through Costs means:

(a) the Transmission Charges, Rates, Electricity Commission Levies, and Commerce Act levies paid or payable by a Non-exempt EDB during an Assessment Period;

but does not include:

(b) any amounts described in paragraph (a) if the Non-exempt EDB demonstrates ~~to the satisfaction of the Commission~~ that those amounts were passed on transparently to its Consumers and/or electricity retailers.

11. If the Commission does not accept this amendment, then the Determination must as a minimum include the equivalent of Clause 7(2) from the existing thresholds Gazette Notice which absolves the Non-exempt EDB or the auditor from stating whether the “to the Commission’s satisfaction” standard has been met, as follows:

The Annual Compliance Statement and Auditors report need not state whether the Commission is satisfied as to the matters referred to in ...

12. A similar clause is required to accommodate the proposed wording in clause 10.3 regarding the alternative approach to the merger and acquisition evidence and the requirement to demonstrate this also “to the Commission’s satisfaction”.

Multi Event Interruptions

13. The Update Paper has appropriately clarified that the quality limits and assessed values will be assessed on the basis that multi day events are to be attributed to the first day of the event. It also must be clarified that where an event causes ongoing interruptions, these are also ascribed to the first day of the event, as follows:

Assessment Dataset means the set of daily SAIDI Values and SAIFI Values for an Assessment Period, with Interruptions that span multiple calendar days and all Interruptions attributable to the same event accrued to the day on which the Interruption began

Reference Dataset means the set of daily SAIDI Values and SAIFI Values for the Reference Period, with Interruptions that span multiple calendar days and all Interruptions attributable to the same event accrued to the day on which the Interruption began

3. Price Path

Specification of Allowable Notional Revenue

14. The Consultation Update Paper acknowledges our previous submissions for a “revenue adjustment term” to ensure the price path reflects the intent of the CPI-X price cap form of regulation. The Consultation Update Paper (in Appendix A, Row 10) indicates that the Commission wishes to consider a number of implementation issues in this respect and therefore has not included an adjustment term in the Draft Determination. The intention is that an adjustment term will be further considered in 2010 prior to price setting at the end of 2010.
15. We are disappointed at this decision and believe it is inappropriate as EDBs have insufficient information now for price setting for the current year. The relationship between Allowable Notional Revenue and Notional Revenue for the Assessment Period commencing 1 April 2010 (for which prices are being determined currently) will directly influence the impact of the revenue adjustment term. EDBs need to know the consequences of their price setting decisions now for this purpose. Once again we submit that the revenue adjustment term should be included, as previously proposed.

$$R_t = (\sum P_{i,t-1} Q_{i,t-1} - K_{t-1} + R_{t-1} - NR_{t-1}) \times (1 + \Delta \text{CPI})(1-X)$$

16. The list of issues to be considered further by the Commission in this respect appears to include issues which should have been, and to our understanding have been considered throughout the consultation on the DPP. We do not therefore accept that the “relatively late introduction of the formula” as suggested in Appendix A means the formula cannot be included at this time.
17. In addition, the new definition of the price path in Clause 8.3, which has been amended to ensure that at no time should Notional Revenue exceed Allowable Notional Revenue during an Assessment Period, is confusing and incorrect. We submit it can be corrected as follows:

~~Allowable Notional revenue (Rt) specifies the maximum Prices that may be charged during an Assessment Period, such that the notional revenue (NRt) of a Non-exempt EDB at any time during the Assessment Period must not exceed the greater of the notional revenue at the Assessment Date and the allowable notional revenue for the Assessment Period; Notional revenue at any time during the Assessment Period (NRt) is not to exceed Allowable Notional Revenue (Rt),~~
where:

Quantities

18. We support the change of decision to move to a t-2 approach to quantities for the price path. We note Chapter 4 of the Consultation Update Paper (Row 4) suggests this will allow known audited quantities to be used in the price path. It is important to clarify that although the quantities will be known, they will not have been audited. The audit of the quantities will form part of the Annual Compliance Statement audit.

Price Restructure

19. Clause 8.5 includes provisions for evidence to be included when a Non-exempt EDB restructures its prices. We support the recent amendments made to these provisions. We note however that the move to a t-2 approach to quantities potentially makes compliance with Clause 8.5 more difficult, especially if prices have been restructured in the past two years and the relevant quantity evidence required for DPP purposes may not exist. The information requirements relevant to Clause 8.5 are included in Clause 11.1(iii). We suggest that a similar provision as that introduced for mergers (Clause 10.3) and that included in the previous Threshold Notice (Clause 5(5)) is included in Clause 11.1 (iii) to allow for such circumstances, as follows:

(b) Despite the other provisions of this clause, because of lack of information, it is not practicable to comply with subclause(a) the Non-exempt EDB will be regarded as having complied with this clause by demonstrating compliance by use of an alternative approach that has the equivalent effect

4. Auditors Report

20. We note that the form of the auditors report has now changed from that included in the Draft Determination. The audit report is now more appropriate for the DPP than the previous draft. The requirements however in respect of auditor independence are excessive and unnecessary and contrary to those recently consulted upon and implemented in respect of the Information Disclosure Requirements. We also anticipate they will be difficult to meet in practice for most auditors. The requirements in respect of auditor independence are also inconsistent with the definition of auditor included in Clause 4 in respect of independence. We therefore submit that the following amendment to the Schedule 4 Form of Auditor's Report is required:

~~Other than in my/our capacity as auditor~~ I/we have no relationship with, or interests in *[insert name of Non-exempt EDB]* other than *[insert relationship and/or interests including a statement verifying that no conflict of interest exists]*.

21. This is consistent with the guidance on independence issued by the Institute of Chartered Accountants in New Zealand which most appropriately addresses the matter. It is also consistent with the definition of auditor included in Clause 4 of the Determination, specifically:

(b) has no relationship with, or interest in, the Non-exempt EDB that is likely to involve the Person in a conflict of interest; and

(c) has not assisted with the preparation of the Annual Compliance Statement or provided advice or opinions (other than in relation to audit reports) on the methodologies or processes used in preparing the Annual Compliance Statement