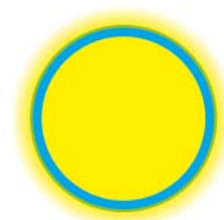


27 September 2010

Matthew Lewer  
Regulation Branch  
Commerce Commission  
PO Box 2351  
Wellington

[By email to: npb@comcom.govt.nz ]



Dear Matthew,

**Powerco Submission on 2010-2015 Electricity Distribution Default Price-Quality Path Refinements Discussion and Draft Decisions Paper**

1. Thank you for the opportunity to submit on the 2010-2015 Electricity Distribution Default Price-Quality Path (DPP) Refinements Discussion and Draft Decisions Paper (the Draft Decisions Paper). This submission should be read in conjunction with Powerco's previous submissions on the input methodology draft decisions and the DPP starting price adjustment.

**Revenue differential term**

2. The Commission has proposed that a revenue differential term is appropriate for future regulatory periods of the 2010-2015 Default Price Path (DPP). The details of the adjustment term are specified in Appendix A of the Draft Decisions Paper.
3. Powerco supports the Commission's proposal to include a revenue differential term. We agree that it ensures electricity distribution businesses (EDBs) are not rewarded for breaching the price path and that the relationship between an EDBs pricing behaviour and allowable revenue is decoupled.
4. Powerco has reviewed the new formula for allowable notional revenue in Appendix A and supports the change to incorporate the revenue differential term.

**Potential amendments to take account of input methodologies**

5. The Commission has outlined the impacts of the draft electricity input methodologies on the 2010-2015 DPP and how the initial reset determination may need to be amended. Powerco agrees with the Commission's list of matters to be included in the DPP Determination (assuming that the Commission's draft decisions remain unchanged):
  - a. the specification of price;
  - b. pass-through costs;
  - c. the specification of recoverable costs, including:
    - i. avoided transmission costs
    - ii. new investment contracts;

- iii. the net carry-forward amount of the incremental rolling incentive scheme;
  - d. the CPP application window;
  - e. the treatment of transactions between EDBs; and
  - f. the circumstances under which the price path may be reconsidered.
6. We will not repeat our recommendations on these proposals as we have already submitted extensively on a number of them in previous submissions. If the Commission continues with its current input methodology proposals, we have the following comments on how they are incorporated into the DPP Determination.

*Specifying information on recoverable costs*

- 7. In paragraph 3.14 the Commission's initial view is that all recoverable costs should be specified separately as part of the annual compliance statement to clearly identify each recoverable cost and demonstrate its effect.
- 8. Powerco recommends that the Commission provides detailed specification on the degree of information it requires. This is because information is very costly to collect. The Commission must be realistic in the degree of evidence it will expect and explicitly state what is needed.

*Information to support avoided transmission charges*

- 9. In paragraph 3.21 the Commission states that the Initial Reset Determination will be amended to require EDBs to supply supporting information concerning each individual investment contributing to an avoided transmission charge (ACOT) as part of its annual compliance statement.
- 10. Powerco recommends that EDBs should not have to publish information on ACOT invested before the input methodologies are published as it is detrimental to investor certainty as it makes retrospective decisions on previous investments.
- 11. In addition, the Commission accepts that there may be issues with supplying complete information on the impact on the total cost to supply electricity. Powerco recommends that the Commission creates a mechanism for EDBs to confirm that their ACOT meets the Commission's criteria before including it in their prices or making an investment. For example, this might just be checking that the evidence the EDB had available is to a satisfactory level.

**Potential amendment of the derivation of the CPI**

- 12. The Commission's draft decision is that the CPI value up to 31 December 2010 will be adjusted to remove the impact of the increase to the Goods and Service Tax (GST). The Commission's justification is that it expects the cost base of each supplier to be unaffected as wages are unlikely to increase and suppliers claim back their direct GST costs.
- 13. Powerco disagrees with adjusting the definition of CPI for the one-off GST change on 1 October 2010. There are many examples of how the CPI does not reflect changes in a supplier's cost base, most notably changes in input costs.<sup>1</sup> The CPI

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<sup>1</sup> An example of an index more consistent with the inputs used by suppliers is the Capital Goods Price Index. An example of how CPI differs from this index was provided in the Gas Authorisation. For example, from June 2000 and June 2005, the Capital Goods Price Index for Pipelines increased by 27 per cent whereas CPI increased 13 per cent over the period. Myrick, Indexation Issues for Gas Control, 5 July 2007, pp. 8-11.

however, has been accepted by the Commission due to its large sample, long established methodology and timely production<sup>2</sup>. At specific points in time there may be short run distortions, but, in the long run, the Commission has seen it as broadly in line with delivering financial capital maintenance (FCM).

14. The input methodologies, and consequently CPI, can only be defined once every seven years. It is opportunistic and highly inconsistent for the Commission to make a one-off adjustment for a Government policy being implemented just before the Final Determination. There may be numerous other tax and policy changes in the next seven years that will not be incorporated into the CPI. The Commission has set a point of principle which it cannot consistently apply and it should be removed.

### **Timing of potential amendments**

15. The Commission has proposed to make all amendments (accept the revenue differential term) by 1 December 2011, to come into effect on 1 April 2012. The Commission plans to publish a draft decisions paper and draft amendment by June 2011. The alternative the Commission mentioned is to make an earlier amendment by 31 March 2011 for non pricing matters.
16. Powerco supports the Commission's initial view of only having one amendment to the DPP. This allows the maximum time to fully consider issues and digest the final input methodology determination.
17. We note however, that the Act requires the DPP to be amended within nine months of the publication of the input methodologies. Therefore this one amendment would be needed before September 2010 (depending on when the input methodologies are published). The Commission's stated date of December 2011 would be too late.
18. Finally, there are a number of unknowns about how the Commission intends to operate the proposed ACOT and new investment contract rules. We would appreciate more information being released as soon as possible to address this uncertainty.
19. Thank you for considering the points raised in this submission.

Yours sincerely

Paul Goodeve  
Regulatory and Business Manager

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<sup>2</sup> Commerce Commission, Gas Authorisation Final Decisions Paper, 30 October 2008, pp 288-289.