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**Submission to the Commerce Commission
on the Initial Reset of the Default Price-
Quality Path for Electricity Distribution
Businesses
Draft Decisions Paper**

Submitted by

Wellington Electricity Lines Limited

12 October 2009

1. Introduction

- 1.1 Wellington Electricity Lines Limited (“Wellington Electricity”) welcomes the opportunity to provide feedback to the Commerce Commission (“CC”) on its Draft Decisions Paper on the Initial Reset of the Default Price-Quality Path for Electricity Distribution Businesses (“Draft Decisions Paper”).
- 1.2 We acknowledge the effort the CC has put into developing the Draft Decisions Paper and as set out in this submission are supportive of many of the decisions the CC has made in regard to the Default Price-Quality Path (“DPP”) for Electricity Distribution Businesses (“EDBs”).
- 1.3 Wellington Electricity recommends that the CC gives particular regard to the submission from the Electricity Networks Association (“ENA”). A submission which Wellington Electricity has reviewed and supports.
- 1.4 Wellington Electricity’s comments follow in table form.
- 1.5 For any questions related to this submission, please contact:

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3.49	The Commission's draft decision is to adopt the provisions for re-openers as set out in the relevant input methodology, following its publication. No interim provisions for re-openers will be included in the Initial Reset Determination.	<p>As set out in Wellington Electricity's submission on the Discussion Paper¹, Wellington Electricity is strongly of the view that the Initial Reset Determination requires flexibility to deal with significant unforeseen circumstances that may impact on an individual or multiple EDBs. The 29 September 2009 earthquake and tsunamis in the Pacific (for which much of the New Zealand was put on alert) is a recent and tragic example of such circumstances that would likely require a re-opener.</p> <p>Wellington Electricity considers that it would be more pragmatic and flexible to include provisions for re-openers in the Determination rather than be required to amend a Determination and develop provisions under potentially difficult circumstances.</p>
3.65	The Commission's draft decision is to structure the Reset DPP to include separately assessed price and quality paths.	Wellington Electricity supports separate quality price and quality paths. Wellington Electricity also supports the CC's continued work in this area including the development of the S-factor which we believe will drive an improved regulatory regime.
3.66	The Commission's draft decision is to not include the customer communication criterion as part of the Reset DPP. The Commission proposes that the information disclosure work stream will seek to develop an equivalent mechanism.	Wellington Electricity supports the CC's decision.
4.12	The Commission's draft decision is that the price-path under the Reset DPP should be indexed using a CPI-X mechanism.	<p>Wellington Electricity supports the continued use of a CPI-X mechanism, however, we do not support that the proposed price path formula which is different from the existing specification.</p> <p>The proposed price path specification has the effect of resetting Allowable Notional Revenue each year based on the previous year's actual prices. This has a number of implications discussed below.</p>

¹ Wellington Electricity Submission to the Commerce Commission on its Discussion Paper on a Reset of Default Price-Quality Path for Electricity Distribution Businesses, 17 July 2009, q. 14, p. 10.

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		<p>Pass through costs such as Electricity Commission Levies and Local Body Rates are not known at the time of setting prices and therefore a degree of estimation is required. In addition whilst typically transmission costs are fixed for the upcoming pricing year and known there can be unforeseen changes such as changes to assets employed at connection points that can change the charge for the pricing year.</p> <p>As a result EDBs may conservatively price below the Allowable Notional Revenue cap due to the significant ramifications of a breach.</p> <p>The proposed price path specification will result in:</p> <ul style="list-style-type: none"> • The level of headroom will be lost in the subsequent year • The EDB will need to include a level of headroom in the subsequent year • The amount of foregone headroom from previous years is compounded by inflation compared with the position had the EDB not taken a conservative approach. <p>Wellington Electricity, consistent with the ENA submission on the Draft Decisions Paper, proposes that price path specification must not reset Allowable Notional Revenue based on the prior year actual prices and should be adjusted based on the maximum Allowable Notional Revenue of the prior year unaffected by actual pricing decisions of the EDB. We support the adjustment to the specification as proposed in the ENA's submission.</p>
4.31	The Commission's draft decision is that a definition of price based on that set out in the Thresholds Notice is appropriate under the Reset DPP.	Wellington Electricity supports the CC's decision, however, we do not support the application of actual prices used in the derivation of Allowable Notional Revenue as set out above.
4.43	The Commission's draft decision is that it is appropriate to annually update base quantities in the notional revenue formula under a DPP, dispensing with the use of a fixed reference year. Furthermore, the Commission's draft decision is that the t-1 approach is appropriate.	<p>Wellington Electricity supports the t-2 approach to defining quantities for the price path. The proposed t-1 approach introduces unnecessary estimation and uncertainty into the price path.</p> <p>There is a potential for material variances between actual and estimated quantities under the t-1 approach simply due to abnormal weather and movements associated with wash ups that occur during the year.</p> <p>The costs associated with estimation, audit difficulties, additional reporting and analysis (for</p>

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		EDBs and the CC) as well as the potential for the CC to revert to another methodology (including a t-2 approach as mooted) creates additional costs and uncertainty compared with implementing a t-2 approach as preferred by Wellington Electricity.
4.53	The Commission's draft decision is to implement a lagged CPI indexation of the price-path assessment formulae. The Commission's draft decision is to allow a six month lag between the most recent quarterly CPI change used in the formula and the start of the pricing year. The proposed formula for the calculation of CPI is outlined in below. A numeric example of its implementation is provided in Appendix B.	<p>The change in the CPI definition from the approach under the existing Threshold Notice to a lagged CPI introduces a disconnect between the CPI series of the existing and proposed price path specifications.</p> <p>Whilst Wellington Electricity supports the ENA submission of a principle based approach to maintaining the CPI series, Wellington Electricity acknowledges that the lagged CPI is a pragmatic solution to the estimation error.</p>
4.61	<p><i>Draft Decision on Pass-through of Local Authority Rates & Levies</i></p> <p>The Commission's draft decision is that the following rates and levies should be treated as pass-through costs under the Reset DPP:</p> <ul style="list-style-type: none"> • local authority rates; • Commerce Act levies; and • Electricity Commission levies. 	<p>Wellington Electricity supports the Decisions Paper's treatment of these as pass-through costs.</p> <p>However, as set out above, we note that Commerce Act levies, local authority rates and Electricity Commission levies are not known with certainty at the times prices are set for the coming year and therefore direct you to our response regarding the price path specification at paragraph 4.12.</p>
4.62	The Commission considers that Commerce Act levies incurred by EDBs during the Initial DPP should, in principle, be eligible for pass-through under the Reset DPP (e.g., amortised under the regulatory period).	Wellington Electricity supports the CC's decision.
4.71	<p><i>Draft Decision on Pass-through of Transmission Charges</i></p> <p>The Commission's draft decision is that transmission charges should be treated as a pass-through cost under the Reset DPP.</p>	Wellington Electricity supports the CC's decision.

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5.14	In light of these views, and having considered submissions, the Commission's draft decision is that starting price adjustments should be considered for EDBs under the Reset DPP.	As set out in our previous submission on the discussion paper ² , Wellington Electricity considers that a P_0 adjustment mid way through a regulatory period creates a high degree of uncertainty for EDBs. Therefore the determination should allow for a consultation process for P_0 adjustments following finalisation of the Input Methodologies.
5.44	The Commission's draft decision is that starting prices for the Reset DPP will be those that applied at the end of the Initial DPP and that they should be specified as the Actual Prices posted by each EDB as at 31 March 2010. The role of starting prices when assessing price-path compliance is discussed in paragraph 4.81.	Wellington Electricity supports the CC's decision.
6.138	The Commission's draft decision is to set the rate of change under the Reset DPP (i.e., the X-factor) to be 0% per annum. As the X-factor reflects the difference between industry-wide and economy-wide productivity, a zero X-factor does not imply a lack of expected productivity improvements. Rather, for an input price differential of zero, an X-factor of zero means that the EDBs are expected to improve their productivity performance by at least the same rate as the economy as a whole. The Commission considers that, once appropriate starting price adjustments are made, it is not unreasonable for EDBs to keep their prices constant in real terms over the Reset DPP period. Exceptions will, however, occur in those	Wellington Electricity supports the ENA submission (from Pacific Economic Group) with regard to this decision.

² Wellington Electricity Submission to the Commerce Commission on its Discussion Paper on a Reset of Default Price-Quality Path for Electricity Distribution Businesses, 17 July 2009, q. 9, p. 7.

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	circumstances where a CPP is warranted.	
7.26	The Commission's draft decision is that daily SAIDI and SAIFI data from the period 1 April 2004 to 31 March 2009 be used to inform quality standards under the Reset DPP.	Wellington Electricity supports the CC's decision.
7.52	The Commission's draft decision is that the Reference Dataset and the annual Assessment Datasets should be normalised to take account of extreme events. This is to be done using the process described above and set out in detail in Appendix C.	<p>Wellington Electricity supports the submission from the ENA that the SAIFI component of the quality path is independent of the SAIDI component and that Steps RT3 and AA2 as set out in Appendix C of the Decisions Paper should be reconsidered and altered to include an additional step where MEDs for SAIFI are identified using the SAIFI boundary value.</p> <p>The separation of SAIFI is important as operational best practice drives an EDB to reduce the duration of unplanned outages (and thereby minimise the SAIDI index impact) but can result in SAIFI breaches.</p> <p>The CC's MED provisions do not capture the consequences of subsequent planned and unplanned outages following a MED which is required to make temporary repairs permanent. These subsequent outages typically arise as pre-event condition and security levels are restored. The CC's proposed mechanism for extreme events does not adequately deal with this situation as one event and recovery could influence two adjacent control periods leading to a SAIDI or SAIFI breach.</p>
7.67	<p>The Commission's draft decision is that normal variability be taken into account when setting the Reliability Targets though the use of a dead-band. The size of the dead-band is to be based on the standard deviation present in the normalised Reference Dataset. Further detail on this process is set out in Appendix C. Specifically, an EDB's annual:</p> <ul style="list-style-type: none"> • SAIDI Reliability Target: will be set as the sum of the average SAIDI value in the normalised Reference Dataset and one (1) 	Wellington Electricity supports the recommendations in the ENA submission (SRA Report).

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	<p>times the standard deviation of the SAIDI data in the normalised Reference Dataset; and</p> <ul style="list-style-type: none"> SAIFI Reliability Target: will be set as the sum of the average SAIFI value in the normalised Reference Dataset and one (1) times the standard deviation of the SAIFI data in the normalised Reference Dataset. 	
7.80	<p>The Commission's draft decision is that an EDB would have complied with the quality standard during a particular assessment period if:</p> <ul style="list-style-type: none"> its SAIDI and SAIFI Assessed Values for the assessment period are both less than or equal to the respective Reliability Targets; or its SAIDI and SAIFI Assessed Values in the previous two extant assessment periods did not exceed the respective Reliability Targets. 	Wellington Electricity supports a two step test to manage normal quality variability. We refer the CC to the ENA Submission (SRA Report) for further information.
8.7	The Commission proposes to publish a single Determination to give effect to its decisions on the Reset DPP.	In its submission the ENA notes that the Decisions Paper indicates that a final draft decision will be made available in mid November, along with a draft determination. The draft determination will be subject to a one week technical drafting consultation period. Wellington Electricity supports the ENA's submission that this period is insufficient to enable interested parties to test and consider the definitions, formula and other requirements such as the form of auditors' reports and the information to be included in compliance assessments. We agree with the ENA that parties need at least two weeks for this purpose, which will assist in removing any potential errors or over sights in the final determination.
8.17	The Commission proposes, if appropriate, to include a provision in the Initial Reset Determination that states it will be amended to specify any applicable input methodologies as	Wellington Electricity supports the CC's decision.

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	soon as practicable after those methodologies are published.	
8.43	The Commission's draft decision is to require compliance related documentation to be submitted within 50 working days of each assessment date in the regulatory period (i.e., within 50 working days of 31 March).	Consistent with our previous submission ³ Wellington Electricity recommends a three month period for Annual Compliance Reporting. The CC's draft decision of 50 working days is a welcome improvement over the existing regulations, however, we consider three months provides a more reasonable timeframe for the preparation of this information given the large financial and regulatory work load for EDBs (and auditors) during this period. We also consider that a three month reporting period is unlikely to impact on the CC.

³ Wellington Electricity Submission to the Commerce Commission on its Discussion Paper on a Reset of Default Price-Quality Path for Electricity Distribution Businesses, 17 July 2009, q. 4, p. 5.