

31 August 2023

Tēnā koutou

External reviews of electricity distribution businesses' 2023 asset management plans and of efficiency and productivity

Purpose of this letter

The purpose of this letter is to advise you of the scope of two reviews of information disclosed by electricity distribution businesses (EDBs), with which we intend to engage external consultancies to assist us. These reviews are:

- 2023 asset management plan (AMP) review; and
- EDB efficiency and productivity review.

This letter describes the scope and timing of the reviews of disclosed information that we are undertaking. It is not intended as a formal notification for consultation, but to introduce the reviews, their approach and, where relevant, the consultants that have been engaged.

Background and Context: Ensuring our regulation under Part 4 remains fit for purpose

We recognise the energy sector is in a period of change and uncertainty, and that the pace of change may accelerate. Where and when investment may be required by EDBs will depend on a number of factors, including how government policy, consumer demand, and market responses evolve. At the same time as electricity demand is expected to increase, there are new technologies and alternative solutions for accommodating growth on electricity networks.

Given that context, we consider:

- understanding EDBs' asset management practices and the robustness of their demand and expenditure forecasts will benefit our programme of performance analysis and the DPP4 reset (the default price-quality path which applies to non-exempt EDBs from 1 April 2025).
- it is timely to review whether our information disclosure requirements for EDB AMPs are fit for purpose.
- there is heightened interest in understanding EDBs' efficiency and productivity, given the likely significant investments in networks and new technologies, including non-network solutions, that EDBs will need to undertake and deploy in next few years.

The reviews will be carried out as part of our function under s53B(2)(b) of the Commerce Act 1986 to publish a summary and analysis of disclosed information for the purpose of promoting greater understanding of the performance of individual regulated suppliers.

2023 Asset Management Plan review

A key part of our regulation of EDBs is the requirement for the public disclosure of AMPs. These provide a forward-looking view of how EDBs intend to invest in, maintain and operate their networks for current and future consumers. AMPs serve as a useful tool for people to assess the performance of individual EDBs. Expenditure forecasts in AMPs are also key sources of information when setting price-quality paths for 'non-exempt' EDBs.

The Commission periodically reviews AMPs to identify good industry practice and to promote continuous improvement in asset management practices.

We have engaged IAEngg (Innovative Assets Engineering) to undertake the 2023 AMP review. They will publish findings in two stages:

- 1) Stage 1: Forecasting and planning analysis contained in EDBs' 2023 AMPs; and
- 2) Stage 2: Review of the current AMP disclosure requirements¹ and a separate resilience planning assessment.

The scope of these reviews is outlined in Attachment A.

The reviews are not intended as an audit of EDB quantitative information, a physical inspection of assets, or a review of the state of an EDB's network.

Stage 1: Assessment of forecasting and planning contained in EDBs 2023 AMPs

The review of 2023 AMPs holds particular significance as some AMPs signal proposed step changes in expenditure in response to decarbonisation through electrification and in adapting to climate change (e.g. extreme weather events and managed retreat), as well as reflecting other areas of increased risk (e.g. natural hazards, supply chain, cyber security).

In the review, we expect IAEngg to identify and analyse key drivers of change, uncertainties, and variables in financial and demand forecasts and provide an opinion on the reasonableness of the variations. As part of this, we expect IAEngg will need to engage with some EDBs to request additional information beyond that contained within the 2023 AMP.

We would appreciate your constructive engagement with IAEngg and prompt responses to any questions in order to achieve the delivery dates.

¹ AMP disclosure requirements are contained within Attachment A of the Electricity Distribution Information Disclosure Determination 2012

We do not intend to publicly disclose the responses provided to IAEngg. However, information provided may be referred to within IAEngg's report. We will consider any confidentiality requirements before publishing the final report.

We expect this engagement will occur from 8 September 2023 through to mid-October 2023. Engagements will be a mixture of written questions, video conferences, and face-to-face meetings. Given the interaction with DPP4, we expect initial engagement will be with those EDBs subject to price quality regulation, with engagement with exempt EDBs occurring in the later stages.

We are planning to complete the process late in 2023 and make the report from IAEngg publicly available early in 2024.

Given the proposed timing of release of the report, we would not anticipate EDBs will be able to take into account all parts of the report for the 2024 AMP.

Interaction with DPP4

For the most recent DPP reset (DPP3, for the regulatory period 1 April 2020-31 March 2025), we used a base-step-trend approach to setting operating expenditure forecasts, and largely used EDBs' own capital expenditure forecasts, except where spend exceeded thresholds for increases compared to the previous DPP period.

We are considering our approach to setting forecast expenditure for the forthcoming DPP reset (DPP4), but it is likely that supplier forecasts will be a key source of information.

An intended outcome of the 2023 AMP review is that IAEngg provides an independent opinion on the reasonableness of the expenditure forecasts contained in the AMPs. Accordingly, we anticipate findings from this review will be considered and inform our DPP4 expenditure forecasting programme of work.

The DPP is intended to be a relatively low-cost regulatory tool, so we do not expect that the extent of analysis or level of assurance which will be provided by IAEngg will be at a similar level to 'customised price-quality path' proposals, which are supported by independent verification.

As part of the DPP4 issues paper which we intend to publish in October 2023, you will have an opportunity to provide feedback on our proposed approach to forecasting expenditure which will include the potential use of the 2023 AMP review. You will also have further opportunities to engage on the use of the 2023 AMP review during other consultation processes and workshops occurring as part of the DPP4 reset process.

Stage 2: AMP information disclosure requirements and resilience planning

Understanding environmental risks and assessment of high impact low probability events is a focus of many EDBs and regulators, given the impact of extreme weather events that have

affected New Zealand infrastructure. We want to understand the approach and level of assessment that has been undertaken within current asset management plans.

Stage 2 of the review, which will also be conducted by IAEngg, is a consideration of the information disclosed within EDBs' AMPs and the current AMP information disclosure requirements, as well as an assessment of resilience planning undertaken.

The review should provide the Commission and other stakeholders a better understanding of EDBs' AMP reporting, including a targeted focus on resilience planning practices. The review will mean we are better informed as to whether our information disclosure requirements are fit for purpose.

We do not anticipate any engagement being required by EDBs for stage 2. Following receipt of these reports, we will consider whether amendments are required to our information disclosure regime and will consult as part of that process.

Some EDBs have indicated that 2024 AMPs may have refined approaches to resilience practices, given the impact of significant events late in the 2023 disclosure year. We consider the 2023 AMP is appropriate to use for this review as an EDB's approach to resilience should be documented within the AMP. While recent events may have changed risks and parameters, it will not necessarily have changed an EDB's approach to resilience. The 2024 AMP is an *update* and so may not contain the same extent of disclosures as provided within the 2023 full AMP. This review is separate to the DPP4 reset which will consider updated information provided within the 2024 AMPs.

Efficiency and productivity review

Separate from the review set out above, we are also undertaking a review of the efficiency and productivity of EDBs. This will be an ongoing project with the intention of embedding periodic assessments and publications on EDBs' efficiency/productivity within the Commission's performance and analysis function.

The efficiency of EDBs is relevant to the promotion of the Part 4 purpose (section 52A) of the Commerce Act. We have an obligation (under s53B(2)(b)) to publish a summary and analysis of disclosed information for the purpose of understanding the changes in EDB performance over time, and the relative performance of EDBs, which includes their efficiency and productivity.

The efficiency and productivity review will be undertaken in three phases:

Phase 1 – Total factor and partial productivity analysis of the EDB sector

An assessment of the total factor productivity (TFP) and partial factor productivity (PFP) for all EDBs in aggregate.

Phase 2 – Proof of concept for EDB comparative efficiency study

Developing and testing appropriate analytical technique(s)/methodology(ies) for assessing EDBs' relative productivity and efficiency, including incorporating engineering expertise.

Phase 3 – Apply analytical technique(s) and methodology(ies) to produce EDB comparative efficiency analysis and performance assessment

Selecting and applying the chosen analytical technique(s)/methodology(ies) to EDBs to obtain draft comparative EDB efficiency/productivity analysis(es).

Shortly, we will seek a consultant to undertake the first phase of this review.

We may use the first phase findings on total factor and 'opex' partial factor productivity as context for the draft decision on the DPP4 reset.

The detailed timelines for the review have not yet been developed. However, our engagement expectations are as follows:

- For **phase 1**, we expect stakeholders will have an opportunity to comment on the aggregate TFP and PFP draft results around the time we release the DPP4 reset draft decision, if not before.
- For **phase 2**, we expect to engage with stakeholders on potential approaches and model specifications for our relative performance analysis. However, we do not expect to initiate this phase of the study until the second half of the 2024 calendar year at the earliest, with most of the engagement more likely to occur after the November 2024 DPP4 reset decision.
- For **phase 3**, we also expect to engage with stakeholders on understanding the potential insights from the relative performance analysis.

In undertaking this review, we are mindful of the restriction under s53P of the Commerce Act 1986 that we may not use comparative benchmarking on efficiency in order to set starting prices, rates of change, quality standards, or incentives to improve quality of supply.

Other related programmes

We plan to publish the DPP4 Issues paper in October 2023. It will discuss further how the 2023 AMP review may be considered within the DPP4 reset. Information about the DPP4 project is available [here](#).

We will separately engage with stakeholders on potential changes to information disclosure requirements as part of our Targeted Information Disclosure review (TIDR) and the efficiency and productivity review at an appropriate time in the process.

We are also considering a separate and smaller project for a consultant to report on EDBs' responses to one or more of the new information disclosure requirements, such as the requirement relating to new connection practices.

If you have any queries on this letter please contact
Hristina Dantcheva, Head of Performance and Understanding at
infrastructure.regulation@comcom.govt.nz
Including '2023 AMP and efficiency reviews' in the subject line of your email.

Ngā mihi nui



Andy Burgess
General Manager,
Infrastructure Regulation

Attachment A: 2023 AMP review scope

Forecasting and planning assessment

The forecasting and planning assessment review will include:

- a) review of Asset Management Plans (AMPs) with a focus on 10-year forecasts,
- b) identify and analyse key drivers of change, uncertainties, and variables in financial and demand forecasts. For all Electricity Distribution Business (EDB), assessment of,
 - i. reasonableness and accuracy of key inputs / drivers used in forecasting expenditure
 - ii. reasonableness of underlying drivers where EDBs are forecasting a potential significant step change in expenditure requirements compared to previous levels
 - iii. identification of trigger points where increased certainty on level of spend required may be obtained
 - iv. key dependencies or risks which may impact forecast scenarios
 - v. sensitivity of the expenditure plan to out-turn differences in requirements (such as incremental demand growth, resilience, decarbonisation, and connection growth)
 - vi. reasonableness of EDB forecasts accounting for availability of materials and skilled staff to deliver programmes of work if there are significant increases in expenditure forecasted
 - vii. identification of good electricity industry practice, and
 - viii. comparison to scenarios and key drivers identified by Transpower or other published scenarios.
- c) providing an opinion on the reasonableness of the variations, both the certainty and uncertainty, for example:
 - i. for capex, specifically identifying projects or programmes of work where there is significant uncertainty about either the need for, or timing of, investment requirements for the 2025 - 2030 regulatory period, and what the particular drivers of uncertainty are, and
 - ii. for opex, identifying categories of cost where variances to historical levels are not well supported, or where there are significant assumptions applied in the forecasted values for the period 2025 - 2030.
- d) identify key forecast assumptions, uncertainties, and risks.

AMP information disclosure requirements

The review is to be undertaken across all 29 EDBs AMPs and will include:

- a) gap analysis between ISO 55001 and Commerce Commission determination disclosure requirements
- b) asset management performance metrics being utilised by EBDs
- c) review the AMPs structure and requirements, and the role of a strategic asset management plan
- d) review the effectiveness of AMMAT (Schedule 14)
- e) identify and review AMP performance metrics
- f) asset planning risk and criticality assessments
- g) reviewing how the needs and expectations of stakeholders is included in asset planning
- h) recommendations on areas to improve Commerce Commission information disclosures
- i) development roadmap for improving and analysis of AMPs, with the aim to improve the level of assurance from AMPs, and
- j) spotlighting EDBs with good electricity industry practice.

Resilience planning

Assessment will include all 29 EDBs approach. The review focus is to provide an opinion and identify good industry practice on:

- a) initiatives raised to improve resilience
- b) assessment of natural disaster risk to networks
- c) resilience assessment and evaluation, and
- d) analysis of expenditure on resilience.