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Default price-quality paths for electricity distributors from 1 April 2015 to 31 March 2020

Compliance requirements

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1. Introduction

Purpose of this paper

- 1.1 This paper provides an overview of the compliance requirements that are set out in the Electricity Distribution Services Default Price-Quality Path Determination 2015 (the determination). It also provides guidance for distributors on how to comply with, and the reasons for, these compliance requirements.

Compliance with the default price-quality path determination

- 1.2 On 28 November 2014, we determined a price-quality path for all Non-exempt Electricity Distribution Businesses (distributors).¹ The default price-quality path specifies the maximum prices that may be charged by a distributor through a weighted average distribution price cap and demonstration of the recovery of pass-through costs and recoverable costs, as well as minimum standards for service quality. These paths will remain in force for the regulatory period 1 April 2015 – 31 March 2020.²
- 1.3 The determination is made in accordance with s52P of the Commerce Act 1986 (the Act) and also contains provisions for monitoring compliance with price-quality paths as provided for under s53N.

¹ This determination does not apply to Orion New Zealand Limited until the expiration of the *Orion New Zealand Limited Customised Price-Quality Path Determination 2013* [2013] NZCC 21, see clause 3.2 of the determination.

² The determination applies unless a distributor applies for a customised price-quality path. Orion raised a number of concerns regarding how the default price-quality path determination was to apply to future customised price-quality path determinations within Orion New Zealand Limited "Submission on the revised draft DPP determination and related documents" (31 October 2014), paragraph 5. Under section 53V(3) of the Act, a customised price-quality path for a supplier is imposed by way of an amendment to the s52P determination relating to the default/customised price-quality regulation applying to the supplier, ie, to the determination explained in this paper. Where future customised price-quality path proposals align with generally applicable rules set out in this default price-quality path determination we would amend the applicable schedules in the determination. However, the exact form and nature of the amendment will be determined on a case-by-case basis in accordance with relevant input methodologies at the time of the customised price-quality path determination. If more substantial changes are required to the generally applicable rules set out in the s52P determination, we may undertake a different approach at that time.

1.4 Suppliers are required to report compliance with the price-quality path, and for that reason we have provided an overview of the compliance requirements. The subjects covered by this paper are:

- 1.4.1 features of, and the due dates for, the annual compliance statement (Chapter 2);
- 1.4.2 information requirements that are necessary for distributors to demonstrate compliance with their default price-quality paths (Chapters 3-6);
- 1.4.3 information related to submitting an application for an energy efficiency and demand side management incentive allowance (Chapter 7);
- 1.4.4 timeframes for distributors to propose a customised price-quality path (Chapter 8); and
- 1.4.5 approval requirements contained within the determination (Chapter 9).³

Supporting policy papers

1.5 This paper has been published alongside our main policy paper and final determination for the default price-quality paths to apply to distributors from 1 April 2015.⁴

³ Approval requirements apply to the energy efficiency and demand side management incentive allowance, extended reserves allowances and where a distributor applies for assessing compliance against an alternative methodology following a transaction.

⁴ Commerce Commission “Default price-quality paths for electricity distributors from 1 April 2015” (28 November 2014); Electricity Distribution Services Default Price-Quality Path Determination 2015 [2015] NZCC 33.

- 1.6 We have also published papers that explain, and give our reasons for:
- 1.6.1 the low cost forecasting approaches we have used in setting the default price-quality paths;⁵
 - 1.6.2 the quality targets and incentives we have set;⁶
 - 1.6.3 amendments to input methodologies, which give effect to the Incremental Rolling Incentive Scheme (IRIS);⁷ and
 - 1.6.4 amendments to input methodologies, which affect the model we have used for setting starting prices based on the current and projected profitability of each distributor, and other aspects of default price-quality paths.⁸

Consultation on the proposed default price-quality paths

- 1.7 On 4 July 2014, we published a main policy paper for the default price-quality paths proposed to apply to distributors from 1 April 2015.⁹ This was followed by a draft determination and companion paper on the proposed compliance requirements, which we published on 18 July 2014.¹⁰
- 1.8 Following submissions on our draft decision, we made some changes to how the compliance requirements operated. In particular, these changes affected the requirements for price paths, including pass-through and recoverable costs, and quality standards.¹¹

⁵ Commerce Commission "Low cost forecasting approaches for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁶ Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁷ Commerce Commission "Amendments to input methodologies for electricity lines businesses subject to price-quality regulation: Incremental Rolling Incentive Scheme" (27 November 2014).

⁸ Commerce Commission "Amendments to input methodologies for electricity distribution services: First and second type" (27 November 2014).

⁹ Commerce Commission "Proposed default price-quality paths for electricity distributors from 1 April 2015" (4 July 2014).

¹⁰ Commerce Commission "Proposed Compliance Requirements for the 2015-2020 Default Price-Quality Paths for Electricity Distributors" (18 July 2014); Commerce Commission "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015" (18 July 2014).

¹¹ Refer to Chapters 3 and 4 respectively for guidance on the compliance requirements for price limits, including pass-through and recoverable costs, and quality targets and incentives.

- 1.9 These changes were reflected within the revised draft determination and associated paper we consulted on, issued 20 October 2014.¹²
- 1.10 Some minor adjustments have been made to the determination following submissions on the revised draft determination issued on 20 October 2014.
- 1.11 During both rounds of consultation, submissions were received on the compliance requirements we proposed for the default price-quality paths from 1 April 2015. We have considered, and are grateful for, all submissions received.

¹² Refer: Commerce Commission "How we propose to implement default price-quality paths for electricity distributors from 1 April 2015" (20 October 2014); and Commerce Commission "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015" (20 October 2014).

2. Annual compliance statement

Purpose of chapter

- 2.1 This chapter outlines and explains the main features of the annual compliance statement. This chapter covers the:
 - 2.1.1 contents of the annual compliance statement;
 - 2.1.2 due dates for the annual compliance statement;
 - 2.1.3 assurance requirements; and
 - 2.1.4 actions a distributor should take in the event of identifying an error in a previous compliance statement.
- 2.2 You can find a more detailed description of the information that must be included in the compliance statement for each major topic (for example quality standards or price restructuring) in the relevant chapter in this paper.

Contents of the annual compliance statement

- 2.3 Each year, distributors are required to provide us with a statement that demonstrates whether they have complied with the default price-quality path in the previous assessment period, which runs from 1 April to 31 March.¹³
- 2.4 An annual compliance statement should be clearly presented and understandable, and meet all the requirements set out in clause 11 of the determination. Amongst other things the compliance statement should include an explicit, up-front statement about whether or not the distributor has complied with the price path and quality standards.
- 2.5 Distributors may find it helpful to produce a checklist based on the requirements contained in clause 11 for the preparation of compliance statements to ensure that each clause of the determination is met.

¹³ See clause 11 of the determination.

2.6 Compliance statements must also contain information to support the distributor's statement of compliance or non-compliance:

2.6.1 with the price path;¹⁴

2.6.2 with the quality standards;¹⁵

2.6.3 with the requirements governing major transactions, amalgamations and mergers;¹⁶ and

2.6.4 with the requirements governing a restructure of prices.¹⁷

2.7 In addition, each compliance statement must be accompanied by a director's certificate, and an independent audit report covering all information contained within the compliance statement.¹⁸

Due dates for providing compliance statements

2.8 The determination prescribes the:

2.8.1 date by which distributors must submit their compliance statements to the Commission; and

2.8.2 date by which distributors must publish their compliance statement on their website.

¹⁴ See clause 11.4 of the determination.

¹⁵ See clause 11.5 of the determination.

¹⁶ See clause 11.6 of the determination.

¹⁷ See clauses 11.7 and 11.8 of the determination.

¹⁸ These are required by clause 11.3 of the determination. The requirements for the director's certificate and audit report are set out in schedules 6 and 7 of the determination, respectively.

2.9 Table 2.1 sets out the due dates for compliance statements.

Table 2.1: Due dates for compliance statements¹⁹

Assessment period	Last day for submission to the Commission
First (2016)	Monday 13 June 2016
Second (2017)	Thursday 15 June 2017
Third (2018)	Wednesday 13 June 2018
Fourth (2019)	Thursday 13 June 2019
Fifth (2020)	Monday 15 June 2020

2.10 Following submission to the Commission, the compliance statement must be published on the distributor's website within five working days.

2.11 Distributors are also required to provide the Commission with digital copies of their price-quantity schedules in a format compatible with Microsoft Excel within five working days of providing their annual compliance statement.²⁰

2.12 These schedules are required to enable the Commission to analyse the underlying data supporting a distributor's representation of price path compliance. Historically the Commission requested these schedules following submission of the annual compliance statement. By requiring this within the determination it will save additional requests being required to be made to distributors.

Assurance requirements

2.13 The determination requires that compliance statements be accompanied by an assurance report that covers the entire compliance statement. In the determination, we have updated the standard that applies to compliance statements. All assurance reports must now comply with the Standard on Assurance Engagements 3100 – Compliance Engagements (SAE 3100) and the International Standard on Assurance Engagements (New Zealand) 3000 (ISAE (NZ) 3000) or their successor standards.

¹⁹ These dates have been determined in accordance with clause 11.1 of the determination which requires the compliance statement to be submitted within 50 working days of the end of the assessment period. The dates take into account current public holidays as at the time of publishing this paper, but are subject to change if there are any changes to public holidays.

²⁰ See clause 11.1(b) of the determination.

- 2.14 Following feedback from auditors and distributors, we have moved away from prescribing a pro forma assurance report in the determination. Instead, we now specify a list of requirements that the assurance report must meet. This will give auditors greater flexibility in the form of the assurance report they provide.²¹
- 2.15 The list of assurance requirements is modelled on those used for information disclosure and Orion's customised price-quality path. Following submissions we have removed the requirement for the auditor to state whether, in his or her opinion, proper records have been kept to enable the complete and accurate compilation of the compliance statement.²²
- 2.16 We understand that this clause may have resulted in a number of distributors receiving qualified audit opinions due to the manual nature of interruption recording practices which are common for a number of distributors rather than specific concerns on a distributor's procedures for recording interruptions.

Errors in previous compliance statements

- 2.17 Where a distributor, in the process of preparing its compliance statement, discovers an error made in a previous compliance statement, we expect the distributor to:
- 2.17.1 bring the error to our attention;
 - 2.17.2 provide a thorough explanation for how the error occurred; and
 - 2.17.3 provide a thorough explanation of the steps taken to prevent such an error from occurring in future.
- 2.18 As errors within historic compliance statements may flow through to the current year through either the pass-through balance or revenue differential term the distributor may be required to include a comment in their next compliance statement. This would reflect the reason why the information is inconsistent between the annual compliance statement and the impact of the error on previously disclosed annual compliance statements.

²¹ The revised form of assurance statement is set out in schedule 7 of the determination.

²² Electricity Networks Association "Submission on the technical drafting of the Draft DPP Determination and IM amendments" (31 October 2014), paragraph 49-51; and Alpine Energy Limited "Submission to the Commerce Commission on Proposed Compliance Requirements for the 2015–2020 Default Price-Quality Paths for Electricity Distributors" (29 August 2014), paragraph 6 - 18.

3. Price path including pass-through and recoverable costs

Purpose of chapter

- 3.1 This chapter summarises the requirements for distributors to comply with the price path, including the treatment of pass-through and recoverable costs.
- 3.2 This chapter addresses the following points:
 - 3.2.1 changes to price path compliance from the 2012 default price-quality path determination;
 - 3.2.2 establishing distribution prices and pass-through prices;
 - 3.2.3 allowable notional revenue compliance;
 - 3.2.4 demonstration of recovery of pass-through costs and recoverable cost charges;
 - 3.2.5 recognition of pass-through costs and recoverable costs; and
 - 3.2.6 application of schedules 5A – 5H of the determination.

Changes to price path compliance from the 2012 default price-quality path determination

- 3.3 As outlined in our final decision - main policy paper, we have set a new approach for the treatment of pass-through and recoverable costs in the determination.²³ The approach is intended to mitigate the risk of price path breaches due to variations between forecast and actual pass-through costs and recoverable costs.
- 3.4 Compliance is assessed against the two components of the price path:
 - 3.4.1 allowable notional revenue compliance against the weighted average distribution price cap; and
 - 3.4.2 demonstration of recovery of pass-through costs and recoverable costs.
- 3.5 Compliance with the price path is assessed by separating the two portions of prices, being the portion attributable to recovery of current and past unrecovered pass-through costs and recoverable costs ('pass-through prices') and the remainder (now termed 'distribution prices').

²³ Commerce Commission "*Default price-quality paths for electricity distributors from 1 April 2015*" (28 November 2014), Chapter 5.

- 3.6 Allowable notional revenue compliance is assessed by comparing the notional revenue that the distribution prices have generated compared against allowable notional revenue.²⁴
- 3.7 Where a distributor's notional revenue exceeds its allowable notional revenue it will be non-compliant with the allowable notional revenue compliance requirement, and will therefore be non-compliant with (ie, contravened) the price-quality path. Further detail on the allowable notional revenue compliance requirements are provided under the section 'notional revenue compliance' below.
- 3.8 Each distributor is also required to report annually on the running balance of its recovery of pass-through and recoverable costs. This balance is referred to as the pass-through balance.
- 3.9 The 'pass-through balance' represents the unrecovered (or not paid back) balance of the cumulative differences between forecast and actual pass-through costs and recoverable costs for prior years (adjusted for the cost of debt).
- 3.10 A pass-through balance may be positive or negative in an assessment period. There is no requirement that a distributor must recover or repay all or part of the pass-through balance in the assessment period following that in which it had been calculated.
- 3.11 The pass-through prices used in calculating the pass-through balance comprise:²⁵
- 3.11.1 a demonstrably reasonable allowance for forecast pass-through costs and recoverable costs relating to the current year; and
 - 3.11.2 any recovery (or pay-back) of all, part of, or none of, the most recent 'pass-through balance' (ie, the pass-through balance at the end of the assessment period prior to that in which prices are set for the coming assessment period).²⁶
- 3.12 The amount of each price apportioned as a pass-through price will affect the allocation to distribution prices which in turn impacts the assessment of compliance under the weighted average distribution price cap.

²⁴ See clause 8.3 – 8.6 of the determination.

²⁵ See clause 8.6 (b) of the determination.

²⁶ For example, when setting prices for the assessment period beginning 1 April 2017 the distributor is to use the pass-through balance as at the end of the 2015/16 assessment period.

- 3.13 Where amounts are incorrectly allocated to pass-through prices which do not relate to forecast pass-through costs and recoverable costs, or recovery (or pay-back) of all or part of the most recent pass-through balance, the Commission could require an annual compliance statement to be re-calculated with revised calculations. The revised calculations would be required to reflect distribution price and pass-through price allocations in accordance with the requirements.
- 3.14 Further detail on the recovery of pass-through costs and recoverable cost requirements are provided below.

Establishing distribution prices and pass-through prices

- 3.15 The price path calculations use distribution prices and pass-through prices for the purpose of assessing compliance:
- 3.15.1 Distribution Price means the portion of prices excluding pass-through prices;²⁷ and
 - 3.15.2 Pass-Through Price means the portion of prices attributable to pass-through costs and recoverable costs.²⁸
- 3.16 Distribution prices and pass-through prices, taking into account changes in the pass-through balance, should be reconcilable to the posted prices published on a distributor's tariff schedule.²⁹
- 3.17 The distribution prices and the pass-through prices are portions of the price published on a tariff schedule but are themselves not currently required to be posted separately on a distributor's tariff schedule.
- 3.18 A distributor is required to allocate their posted prices to the distribution price and pass-through price portions in accordance with their respective definitions.
- 3.19 Accordingly when a distributor allocates portions of its prices to the pass-through price this must be only to recover pass-through costs and recoverable costs forecast for that assessment period, or related to prior years' over or under-recovered costs as represented by all, part, or none of the most recent pass-through balance.³⁰

²⁷ Electricity Distribution Input methodology Amendments Determination 2014 [2014] NZCC 31, clause 1.1 4(2).

²⁸ Electricity Distribution Input methodology Amendments Determination 2014 [2014] NZCC 31, clause 1.1 4(2).

²⁹ Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26, clause 3.1.1 (4).

³⁰ See clause 8.6 (b) of the determination.

- 3.20 A distributor may allocate a portion of price to the pass-through price based on a direct allocation of the anticipated pass-through costs and recoverable costs which relate to a consumer group or an indirect allocation where a distributor could use a proxy allocation methodology.
- 3.21 We acknowledge that there may be variances between what a distributor attempts to recover through pass-through prices and the actual amount of pass-through and recoverable costs incurred. This arises from volatility in the actual amount of costs incurred to what was forecast at the time prices were set, and the impact of having to forecast quantities for the year when setting prices in order to recover the pass-through and recoverable costs.
- 3.22 We have required distributors to provide within their annual compliance statement the methodology used to calculate distribution prices and pass-through prices. We also require them to identify that component of pass-through prices that relates to the recovery of forecast pass-through costs and recoverable costs, and that component which relates to the recovery or pay-back of all or part of the most recent pass-through balance.³¹
- 3.23 As the establishment of the recovery of pass-through costs and recoverable costs is a new mechanism this will be an area of compliance focus. Apportioning decisions will affect the allocation to distribution prices which in turn impacts the assessment of compliance under the weighted average distribution price cap.
- 3.24 The Information Disclosure requirements do not currently require separate disclosure of distribution prices or pass-through prices within published tariff schedules.³² We have noted a number of submissions representing concerns that the prices used for calculating compliance with the price path and information disclosure requirements for presentation on published tariff schedules are now different.³³ We will take these submissions into account when considering the scope of potential future rounds of amendments to the Information Disclosure Determination.

³¹ See clause 11.4 (e) of the determination.

³² Electricity Distribution Information Disclosure Determination 2012, clause 2.4.18.

³³ Orion New Zealand Limited "Submission on the revised draft DPP determination and related documents" (31 October 2014), paragraph 7; Electricity Networks Association "Submission on the technical drafting of the Draft DPP Determination and IM amendments" (31 October 2014), paragraph 12-13; and Vector "Submission on the draft Default Price-Quality Path determination 2015" (31 October 2014), paragraph 13.

Where prices change during an assessment period

- 3.25 The term $DP_{i,t}$ within clause 8.5 of the determination means the *ith* Distribution Price during any part of the Assessment Period *t*.³⁴
- 3.26 The term $PTP_{i,t}$ within clause 8.6 of the determination means the *ith* Pass-through Price during any part of the Assessment Period *t*.
- 3.27 This is applied such that if a distributor's prices change during the assessment period then:
- 3.27.1 notional revenue is calculated using the lagged quantity that corresponds to the distribution price, applied on a weighted average basis. Where a price is changed during the assessment period a distributor will need to determine the proportion of quantity that corresponds to each distribution price. For the avoidance of doubt a distributor does not use the closing price as if it applied for the entire assessment period;³⁵ and
- 3.27.2 pass-through balance is calculated using the corresponding quantity during the assessment period that corresponds to the pass-through price. Where a price is changed during the assessment period a distributor will need to determine the proportion of quantity that corresponds to each pass-through price. For the avoidance of doubt a distributor does not use the closing price as if it applied for the entire assessment period.

Notional revenue compliance

- 3.28 Rather than assessing compliance based on a distributor's actual revenue, we assess compliance on the basis of 'notional' revenue. The revenue is 'notional' because it is based on quantities that are lagged by two years, rather than the quantities for the year in question. This approach ensures that all the values can be calculated at the time the distributor sets its prices.
- 3.29 Two types of notional revenue figures are calculated:
- 3.29.1 'allowable notional revenue', which is the amount that the distributor's distribution prices are allowed to generate on a notional basis; and
- 3.29.2 'notional revenue', which is the amount that the distributor's distribution prices did generate on a notional basis.

³⁴ See Clause 8.5 of the determination which defines *i* - denotes each Distribution Price; *t* - is the year in which the Assessment Period ends.

³⁵ Were a change in prices to have occurred in the prior assessment period, the allowable notional revenue would need to also be calculated on a weighted average basis rather than using the closing price.

- 3.30 We require the notional revenue of a distributor in an assessment period to not exceed the allowable notional revenue for the assessment period.³⁶ The distributor will be compliant with this requirement if notional revenue is less than or equal to allowable notional revenue in total for the full assessment period.
- 3.31 We note that the compliance test does not apply an “at any time” requirement. Accordingly we only require information to be represented and calculations to be provided which represent compliance assessed for the full assessment period.
- 3.32 The allowable notional revenue for the first assessment period is calculated in accordance with Schedule 3A, for all assessment periods other than the first assessment period it is calculated in accordance with the formula at Schedule 3B.

The revenue differential term

- 3.33 The formula for allowable notional revenue in Schedule 3B of the determination includes the term $(ANR_{t-1} - NR_{t-1})$. This is the difference between the allowable notional revenue and notional revenue for the assessment period prior to the assessment period. We refer to this term as the revenue differential term.
- 3.34 The revenue differential term only applies to the weighted average price cap on the distribution portion of prices. It is designed to ensure that a distributor’s distribution pricing decisions in one assessment period do not impact the notional revenue which they are allowed to recover in following assessment periods.
- 3.35 The revenue differential term prevents an over-recovery (ie, a situation where notional revenue is greater than allowable notional revenue) in one assessment period, which would result in non-compliance with the price-quality path, from increasing allowable notional revenue in the next assessment period. It also prevents an under-recovery (ie, a situation where notional revenue is less than allowable notional revenue) in one assessment period from lowering allowable notional revenue in the next assessment period.
- 3.36 The revenue differential term does not allow a previous under-recovery of notional revenue to be recovered in future assessment periods. This is consistent with the price path acting as a weighted average price cap on the distribution portion of prices.

³⁶ See clause 8.3 of the determination.

Treatment of quantity wash-ups

- 3.37 The term $Q_{i,t-2}$ within clause 8.5 of the determination means the quantity for the assessment period ending two years prior to year t corresponding to the i th distribution price.
- 3.38 Distributors have previously raised questions about what quantities should be used for reporting compliance where the distributor had set its prices based on the latest available information at the time it set its prices, but then a retailer has notified the distributor of a wash-up of quantities prior to the distributor reporting compliance.³⁷
- 3.39 The earlier set of quantities that a distributor has used to calculate allowable notional revenue when setting prices, should be used again for calculating notional revenue and hence determining compliance with the price path. We consider that this approach is more consistent with the concept of a weighted average price path than using the later set of quantities for the compliance test.

Treatment of prompt payment discounts

- 3.40 The price used for the annual compliance statement must include a posted discount if a discount is taken up by consumers.³⁸
- 3.41 Accordingly where a distributor provides a prompt payment discount and some consumers have taken up the discount and other consumers have not, there are two different distribution prices and quantities used for calculating allowable notional revenue compliance.³⁹
- 3.42 One set of distribution prices takes into account the posted discount, and there are quantities associated with those who took up the posted discount.
- 3.43 A second set of distribution prices does not take into account the posted discount, and there are quantities associated with those who did not take up the posted discount.
- 3.44 Any prompt payment discount applied will only be reflected in the distribution price and not the pass-through price portion.

³⁷ Powerco "Submission on Default price-quality paths from 1 April 2015 for 17 electricity distributors: Process and Issues paper" (30 April 2014), paragraphs 110-111.

³⁸ Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26, clause 3.1.1 (4).

³⁹ The appropriate treatment of posted discounts is specified in the relevant input methodologies. See clause 3.1.1(4) of the Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26.

Disclosure within the annual compliance statement

- 3.45 A distributor is required to report on their compliance or non-compliance with the requirements within the annual compliance statement by providing the information requested at clause 11.4 of the determination.

Demonstration of recovery of pass-through costs and recoverable costs

- 3.46 Some costs that distributors face may be passed through directly to their consumers. These costs have been defined as pass-through costs and recoverable costs in the Input Methodologies.
- 3.47 As discussed in our final decision - main policy paper, distributors should have the opportunity to recover pass-through and recoverable costs in full.⁴⁰
- 3.48 Discussion on what comprises and how to calculate pass-through costs and recoverable costs is contained under the section 'Recognition of pass-through costs and recoverable costs'.

Proposed compliance requirements for pass-through and recoverable costs

- 3.49 Distributors are required to calculate their pass-through balance at the end of each assessment period.⁴¹ The balance must be provided as part of the annual compliance statement.
- 3.50 At the end of the first year of the regulatory period, the pass-through balance is the difference between the pass-through price, which is that portion of the price set to recover forecast pass-through costs and recoverable costs multiplied by actual quantities, less the amount of actual pass-through and recoverable costs incurred.
- 3.51 Actual quantities that correspond to the pass-through price for that assessment period are used rather than lagged quantities. This allows distributors to fully recover their pass-through costs and recoverable costs, rather than being impacted by potential differences between lagged and actual quantities.

⁴⁰ Commerce Commission "*Default price-quality paths for electricity distributors from 1 April 2015*" (28 November 2014), Chapter five.

⁴¹ See clause 8.6 of the determination.

- 3.52 In each subsequent year of the regulatory period, the pass-through balance is recalculated, and is:
- 3.52.1 the difference between the pass-through price multiplied by actual quantities, less the amount of pass-through and recoverable costs incurred; less
 - 3.52.2 the pass-through balance for the previous year (adjusted for the cost of debt).
- 3.53 Because pass-through prices comprise allowances for forecast pass-through costs and recoverable costs incurred for the assessment period, as well as recovery or pay-back of all or part of the most recent pass-through balance, each assessment period the pass-through balance is updated for:
- 3.53.1 differences between forecast and actual pass-through costs and recoverable costs in the assessment period;
 - 3.53.2 any recovery or pay-back in the assessment period of the most recent pass-through balance at the time prices are set;
 - 3.53.3 the cost of debt on the pass-through balance at the beginning of the assessment period; and
 - 3.53.4 any change due to updated information about quantities (discussed in paragraphs 3.54 to 3.60 below).

Quantity used for calculating the Pass-through balance

- 3.54 The term $Q_{i,t}$ means the Quantity for the Assessment Period (t) corresponding to a Pass-through Price.⁴²
- 3.55 As the $Q_{i,t}$ values used for calculating the pass-through balance (PTB) will include information up to and including 31 March of the assessment period there may be revisions to quantity amounts arising from quantity reconciliations during the time in which distributors are preparing their compliance statements.

⁴² See clause 8.6 of the Determination.

- 3.56 Accordingly in order to prepare the annual compliance statement a distributor may choose a date after the end of the assessment period to use as the cut-off for determining the $Q_{i,t}$ values for the assessment period. This date should be chosen to allow the most accurate information for $Q_{i,t}$ values for the assessment period to be used in the annual compliance statement while ensuring the distributor has sufficient time to complete their annual compliance statement within 50 working days.
- 3.57 Due to the potential inaccuracies in $Q_{i,t}$ values used for the calculation of the assessment periods pass-through balance we have required the PTB_{t-1} to be re-calculated using any additional information available at the end of the current assessment period.⁴³
- 3.58 When re-calculating the PTB_{t-1} a distributor is required to establish what the quantities were for the prior assessment period using information available as at 31 March of the current assessment period. The PTB_{t-1} must be calculated using these values. This may therefore differ from the value calculated as the pass-through balance in the prior assessment period.
- 3.59 We note Vector's submission that this requirement should be removed due to the increased cost of both audit and management costs in establishing what the $Q_{i,t}$ values used to determine PTB_{t-1} should be.⁴⁴
- 3.60 We acknowledge the increased compliance burden involved in re-calculating the PTB_{t-1} rather than using the values as calculated for the prior assessment period. However we believe requiring the PTB_{t-1} to be re-calculated will provide more accurate calculations and be more consistent with allowing distributors' full recovery of their pass-through costs and recoverable costs.

⁴³ See clause 8.6 (a) of the determination.

⁴⁴ Vector "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015: Mark-ups by Vector Limited for submission purposes" (31 October 2014), clause 8.6.

Carry-over of the pass-through balance

- 3.61 Our draft decision in July included a restriction on carrying over balances to the next regulatory period.⁴⁵ We received a number of submissions against that proposed provision, expressing concern that the conservative setting of pass-through prices that this would require would lead, if the pass-through balance were to be not allowed to be carried over, to some pass-through and recoverable costs being never recovered.⁴⁶
- 3.62 We have not at this stage imposed a requirement that the pass-through balance must be negative or within prescribed boundaries after each assessment period or at the end of a regulatory period. For this regulatory period distributors may pay-back or recover all, part or none of the pass-through balance in their pass-through prices for each assessment period. They may not pay-back or recover more, however, than the total amount of the most recent pass-through balance at the time prices are set (ie, at the end of the assessment period prior to the period during which distributors set prices for the current assessment period—namely, the balance at the end of the $t - 2$ period).⁴⁷

Time value of money for the pass-through balance and for recoverable costs

- 3.63 A time value of money calculation applies via three separate mechanisms for the pass-through balance and for some recoverable costs. The two mechanisms are:
- 3.63.1 the factor $(1 + r)$ in the formula for the pass-through balance in clause 8.6 of the determination;
 - 3.63.2 the adjustment for the time value of money to the amount approved referred to in clause 4 of Schedule 5A and clause 4 of Schedule 5H; and
 - 3.63.3 the adjustment for the time value of money as calculated by a distributor under Schedule 5B.
- 3.64 The $(1 + r)$ factor referred to in paragraph 3.63 above applies a debt rate adjustment for the one year in which the pass-through balance is PTB_{t-1} .

⁴⁵ We note that the consultation in July was on the previously proposed 'Demonstration of recovery of transmission charges' approach. However we consider a similar concern may have arisen with the Demonstration of recovery of pass-through costs and recoverable costs within the determination.

⁴⁶ Aurora Energy Limited "Proposed Compliance Requirements for the 2015-2020 Default Price-Quality Paths for Electricity Distributors" (29 August 2014), p.5; and Wellington Electricity "Submission on Draft Determination for 2015-2020 Default Price-Quality Path and Compliance Matters" (29 August 2014), p.5.

⁴⁷ See clause 8.6 (b) of the determination.

- 3.65 The adjustments referred to in paragraph 3.63 above will provide an adjustment at the cost of debt for the recoverable costs for which an ex ante approval is required. This approval process will result in a delay from the assessment period in which the recoverable cost is incurred to the assessment period in which it is recognised as a recoverable cost.
- 3.66 Distributors are required to calculate a quality incentive adjustment following the expiration of the assessment period and adjust for the time value of money using the cost of debt. As the recoverable cost will lag the quality outcomes by two years the time value of money adjustment should reflect the cost of debt for two years ie, the quality incentive adjustment must be multiplied by $(1+\text{cost of debt})^2$.

Disclosure within the annual compliance statement

- 3.67 We also require distributors to provide information which shows how:
- 3.67.1 notional revenue, allowable notional revenue and pass-through balance have been calculated including the price-quantity schedules used to calculate these values.⁴⁸
 - 3.67.2 the allocation of distribution price and pass-through prices has been determined and the amounts of pass-through price which is attributable to recovery of costs for the current assessment and what amount relates to recovery or repayment of a prior pass-through balance.⁴⁹
 - 3.67.3 the pass-through balance has been updated and calculated.⁵⁰ This will include the amounts attributable to factors identified at paragraph 3.53.
- 3.68 We expect distributors to provide sufficient commentary to explain significant variances, which may include outlining the assumptions on which the relevant forecast was made. In explaining variances, distributors may find it useful to provide prior year values.

Recognition of pass-through costs and recoverable costs

- 3.69 In calculating the pass-through balance distributors must establish:
- 3.69.1 K_t – the sum of all Pass-through Costs for the Assessment Period t ; and
 - 3.69.2 V_t – the sum of all Recoverable Costs for the Assessment Period t .

⁴⁸ See clauses 11.4 (c) and 11.4 (f) of the determination.

⁴⁹ See clauses 11.4 (d) and 11.4 (e) of the determination.

⁵⁰ See clauses 11.4 (g),(i),(j) and (k) of the determination.

- 3.70 Pass-through Costs has the meaning given in clause 1.1.4 (2) of the Input Methodologies Determination, and applies to an Assessment Period in accordance with Schedule 5.⁵¹
- 3.71 Recoverable Costs has the meaning given in clause 1.1.4 (2) of the Input Methodologies Determination, and applies to an Assessment Period in accordance with Schedule 5.⁵²
- 3.72 Distributors may only recognise as a pass-through cost or recoverable cost those costs that meet the relevant definition contained within the Input Methodologies. Where a cost can be recognised per the Input Methodologies, Schedule 5 provides information on the amount and timing of when costs are to be recognised.
- 3.73 In accordance with Schedule 5, clause 1:

Any amounts attributable to Pass-through Costs or Recoverable Costs during an Assessment Period, must:

not have already been recovered in a previous Assessment Period;

not otherwise be or intended to be recovered other than through Prices; and

not be attributable to Pass-through Costs or Recoverable Costs that relate to an Assessment Period prior to 1 April 2015, except for the amount of any levies payable under regulations made under the Electricity Industry Act 2010 for the Assessment Period ending 31 March 2015 that were not recovered in that Assessment Period.

- 3.74 These requirements apply for all recoverable costs and pass-through costs.
- 3.75 We note that these requirements do not use “incurred” or other accounting accrual concepts which may in some circumstances require recognising and recording a recoverable cost (positive or negative) for amounts which have not yet been approved or which could not be reasonably forecast when a distributor was setting prices.
- 3.76 As calculations are required or approvals are needed for certain recoverable costs we do not have a recognition timing criteria which applies consistently to all costs. We have specifically addressed within Schedules 5A to 5G when some costs should be recognised, where the timing of a cost is not specifically addressed it should be recorded in the assessment period to which it relates. The approval process for recoverable costs requiring the Commission’s approval is contained within chapter 9 of this paper.

⁵¹ See clause 1.4 of the determination.

⁵² Ibid.

- 3.77 An example of this is the quality incentive adjustment. The timing of recognition of this is stated within Schedule 5B. A quality incentive adjustment must be calculated following the expiration of the assessment period and is recognised as a recoverable cost in the assessment period following that in which it was calculated.
- 3.78 Recoverable costs and pass-through costs that relate to the prior regulatory period have already been recognised under the 2012 Default Price-Quality Path Determination and are excluded from being recognised under clause 1 of Schedule 5. Accordingly these are not allowed to be recognised in this regulatory period.
- 3.79 An exception to this is the unrecovered Electricity Authority (EA) Levy for the 2014/15 assessment period.
- 3.80 We were advised that expected EA levies for distributors for the period 1 July 2014 to 30 June 2015 were likely to be higher than the amount forecast when distributors set their prices for the pricing year which commenced 1 April 2014. This followed a change to the way in which EA levies are allocated.
- 3.81 A number of distributors submitted in response to the revised draft determination that they considered it appropriate that the Commission include a mechanism within the determination to allow recovery of the increase in the EA levy which had not been reflected in the distributors' price setting.⁵³
- 3.82 Vector and the Electricity Networks Association (ENA) both suggested approaches by which the revised draft determination could be amended to allow the recovery of these costs in the 2015 – 2020 regulatory period. Although we have not adopted the mechanisms as proposed by Vector or the ENA we have drafted the determination to provide for recovery of the increase in the EA levy in the 2015 – 2020 regulatory period.
- 3.83 The recovery of the additional EA levies which relate to the assessment period 2014/15 is an exception to the recognition criteria for recoverable costs or pass-through costs in the determination which restricts the inclusion of pass-through costs or recoverable costs which relate to the prior regulatory period.

⁵³ Vector "Submission on the draft Default Price-Quality Path determination 2015" (31 October 2014), paragraph 18-19; Powerco "Submission on technical and additional consultation on the electricity distribution default price-quality path from 1 April 2015" (31 October 2014), paragraph 21 – 23; and Electricity Networks Association "Submission on the technical drafting of the Draft DPP Determination and IM amendments" (31 October 2014), paragraph 44 – 48.

- 3.84 We have allowed this exception for recovery of unrecovered EA levies which relate to the prior regulatory period as the circumstances of this case are quite specific and unusual. Further, consideration of these levies is a mandatory consideration in our determination of the DPP under section 54V (4)(e) of the Commerce Act 1986, and in this occasion there is a very clear and identifiable mid-period change, well documented, from the draft to final levies determination of the EA.

Application of Schedule 5A – 5H of the determination

- 3.85 The table below indicates where additional information is contained within the determination in order to assist in calculation of recoverable costs.

Table 3.1: Schedules within DPP Determination to assist in determining recognisable recoverable cost

IM reference – 3.1.3 (1)	Type of Recoverable Cost	Schedule within the Determination
(a)	Incremental Rolling Incentive Scheme balance	Schedule 5G
(b)	Transpower electricity lines service charges	
(c)	Transpower new investment charges ¹	
(d)	System operator charges	
(e)	Avoided cost of transmission arising from purchases of Transpower assets	Schedule 5E
(f)	Distributed generation allowance	
(g)	S54K(3) and 53ZB(3) claw-back	Schedule 5C
(h)	CPP proposal application fee	
(i)	Commission assessment of CPP proposal fee	
(j)	Fee payable to verifier (CPP)	
(k)	Auditor's cost (CPP)	
(l)	Engineer's fees (CPP)	
(m)	Energy efficiency or demand incentive allowance	Schedule 5A
(n)	Catastrophic event allowance	
(o)	Extended reserves allowance	Schedule 5H
(p)	Quality incentive adjustment	Schedule 5B
(q)	Capex wash-up amount	
(r)	Transmission asset wash-up adjustment	Schedule 5F
(s)	2013-15 NPV Wash-up allowance	Schedule 5D
(t)	Reconsideration event allowance	

¹ No separate Schedule applies but evidence of the amount of charge related to New Investment Contracts is required to be provided under clause 11.4 (f)

Schedule 5A: Approval of energy efficiency and demand side management incentive allowances

- 3.86 Schedule 5A outlines the requirements for approval of an energy efficiency or demand side management incentive allowance.
- 3.87 Further information regarding the energy efficiency or demand side management incentive allowance is contained within Chapter 7 of the main policy paper.⁵⁴ Information on the contents of an application and principles for estimating foregone revenue are contained within Chapter 7 of this paper and the approval process is addressed in Chapter 9.
- 3.88 The amount approved by the Commission as an energy efficiency or demand side management incentive allowance is recognised as a recoverable cost in the assessment period following its approval and will be adjusted for the time value of money using the cost of debt.

Schedule 5B: How to calculate the quality incentive adjustment

- 3.89 The quality incentive adjustment is to be calculated by a distributor within 50 working days following the expiration of the assessment period and is recognised as a recoverable cost in the assessment period following its calculation.
- 3.90 Further information regarding the quality incentive adjustment is included within the quality targets and incentives paper.⁵⁵

Schedule 5C: Claw-back

- 3.91 Those distributors who are entitled to a claw-back under clause 3.1.3 (1)(g) of the Input Methodologies are required to apply Table 5C.1.
- 3.92 Further information regarding claw-back is contained within Chapter 5 of the main policy paper.⁵⁶

⁵⁴ Commerce Commission "Default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁵⁵ See Chapter 2 of Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁵⁶ Commerce Commission "Default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

Schedule 5D: NPV wash-up allowances

- 3.93 Those distributors who are entitled to a NPV wash-up allowance under clause 3.1.3 (1)(s) of the Input Methodologies are required to apply Table 5D.1.
- 3.94 Further information regarding the NPV Wash-up allowance is contained within Chapter 13 of the IM Amendments paper.⁵⁷

Schedule 5E: Avoided transmission charges

- 3.95 Different rules apply for calculating avoided transmission charges allowed under clause 3.1.3 (1) (e) of the Input Methodologies for a purchase of system fixed assets from Transpower before 1 April 2015 and purchases made after this date.
- 3.96 Further information regarding avoided transmission charges is contained within Attachment D of the main policy paper.⁵⁸

Schedule 5F: Transmission asset wash-up adjustment

- 3.97 We have introduced a transmission asset wash-up due to the significant materiality of transmission asset purchases forecast for 2014/15 for Eastland Network Limited and Network Tasman Limited.
- 3.98 The adjustment amount to be included as a recoverable cost can be calculated by these distributors by taking the amount stated as a transmission asset wash-up adjustment and applying this to the formula contained within the Input Methodologies at clause 3.1.3 (1) (r).
- 3.99 Further detail on this adjustment is contained within chapter 8 of the Input Methodologies amendments paper.⁵⁹

Schedule 5G: Specified amounts for the incremental rolling incentive scheme

- 3.100 Further detail on the incremental rolling incentive scheme is addressed within the Incremental Rolling Incentive Scheme (IRIS) paper.⁶⁰
- 3.101 This is not a recoverable cost in the regulatory period 1 April 2015 – 31 March 2020.

⁵⁷ Commerce Commission "Input methodology amendments affecting the default price-quality paths for electricity distributors" (27 November 2014).

⁵⁸ Commerce Commission "Default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁵⁹ Commerce Commission "Input methodology amendments affecting the default price-quality paths for electricity distributors" (27 November 2014).

⁶⁰ Commerce Commission "Amendments to input methodologies for electricity lines businesses subject to price-quality regulation: Incremental Rolling Incentive Scheme" (27 November 2014).

Schedule 5H: Approval of extended reserves allowance

- 3.102 Schedule 5H specifies the application requirements which a distributor must submit for an extended reserves allowance if any amounts were incurred or received in relation to any extended reserves regulation made under the Electricity Industry Act 2010.
- 3.103 Further detail on this adjustment is contained within chapter 11 of the Input Methodologies amendments paper.⁶¹
- 3.104 The amount approved by the Commission as an extended reserves allowance is recognised as either a positive or negative recoverable cost in the assessment period following its approval and will be adjusted for the time value of money using the cost of debt.
- 3.105 Further detail on the approval process related to this allowance is addressed within chapter 9 of this paper.

⁶¹ Commerce Commission "Input methodology amendments affecting the default price-quality paths for electricity distributors" (27 November 2014).

4. Quality standards

Purpose of this chapter

- 4.1 This chapter outlines and explains:
 - 4.1.1 the quality standards and how they are assessed;
 - 4.1.2 the application of normalisation to SAIDI and SAIFI;
 - 4.1.3 the information that distributors must provide to demonstrate compliance with the quality standards; and
 - 4.1.4 the relationship between the quality standards and the revenue-linked quality incentive scheme.
- 4.2 The chapter explains the compliance requirements for the quality standards and the quality incentive scheme, which together constitute the package of quality incentives for the price-quality path.

The quality standards and how they are assessed

- 4.3 Section 53M of the Commerce Act 1986 requires default price-quality paths to specify the quality standards that must be met by the regulated suppliers. This requirement has been met by setting quality standards for each distributor as explained below.

The quality standards

- 4.4 The quality standards are contained within clause 9.1 and 9.2 of the determination, as shown in Box 4.1.

Box 4.1: Quality standards⁶²

9.1 A Non-exempt EDB must, in respect of each Assessment Period, either:

(a) comply with the annual reliability assessment specified in clause 9.2 for that Assessment Period; or

(b) have complied with any annual reliability assessments in each of the two preceding Assessment Periods.

9.2 For the purpose of subclause 9.1(a), to comply with the annual reliability assessment—

(a) a Non-exempt EDB's SAIDI Assessed Value for the Assessment Period must not exceed the SAIDI Limit specified in Schedule 4A; and

(b) a Non-exempt EDB's SAIFI Assessed Value for the Assessment Period must not exceed the SAIFI Limit specified in Schedule 4A.

- 4.5 Distributors can be assessed as being non-compliant in the first assessment period in the regulatory period. For this, assessment of the previous two years (2014 and 2015) uses the limits and calculations applicable to that regulatory period.
- 4.6 Although the calculation of the quality measures have changed from the 2012 default price-quality path determination, it is important to refer to the two years prior to the 2015 - 2020 regulatory period. This allows the first two assessment periods of the regulatory period to be assessed with the multi-year assessment. If the previous years were not considered, then the first two assessment periods of the regulatory period would contribute less to the probability of non-compliance.

⁶² Commerce Commission, *Electricity Distribution Services Default Price-Quality Path Determination 2015* [2015] NZCC 33, clauses 9.1 and 9.2.

- 4.7 The application of the quality standards is illustrated in Table 4.1, which shows whether a distributor would be compliant with the quality standards in a range of different scenarios.

Table 4.1 Illustration of quality compliance assessment

Year	Measure	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5	Scenario 6
2013/14	SAIDI	Within	Within	Exceed	Within	Exceed	Within
	SAIFI	Within	Within	Exceed	Within	Exceed	Within
2014/15	SAIDI	Exceed	Exceed	Within	Within	Within	Within
	SAIFI	Exceed	Exceed	Within	Within	Within	Within
2015/16	SAIDI	Exceed	Exceed	Within	Exceed	Exceed	Exceed
	SAIFI	Exceed	Exceed	Within	Within	Within	Within
2016/17	SAIDI	Within	Exceed	Exceed	Within	Within	Within
	SAIFI	Within	Exceed	Exceed	Within	Within	Exceed
2017/18	SAIDI	Within	Within	Within	Exceed	Within	Within
	SAIFI	Within	Within	Within	Within	Within	Within
Non-compliance		2015/16	2015/16 2016/17	None	2017/18	2015/16	2016/17

Reliability limits (SAIDI and SAIFI)

- 4.8 The reliability limits for the quality standards are set by the Commission in the determination. A limit is set for each distributor, which applies to each assessment period of the 2015-2020 regulatory period, unless a mid-period re-calculation is undertaken for an amalgamation, merger, major transaction or transmission asset purchase or sale.
- 4.9 The SAIDI and SAIFI reliability limits are calculated for each distributor as one standard deviation above the historical SAIDI and SAIFI average. The method used to calculate the SAIDI and SAIFI average and limits is more fully explained in the accompanying quality paper.⁶³

⁶³ Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014), Chapters 5 and 7.

- 4.10 The method for re-calculating the reliability limits for the quality standards following an amalgamation, merger, major transaction or transmission asset purchase or sale is the same as for re-calculating the parameters of the revenue-linked quality incentive scheme.⁶⁴ This method is specified in Schedule 4B of the determination and is explained in the accompanying quality paper.⁶⁵

Establishing SAIDI and SAIFI assessed values

- 4.11 For the purposes of assessing compliance with the quality standards and calculating the quality incentive scheme adjustment, distributors are required to calculate and report their SAIDI and SAIFI assessed values in the annual compliance statement.⁶⁶ The annual compliance statement should also include the data and calculations used to calculate the SAIDI and SAIFI assessed values.
- 4.12 The method for calculating SAIDI and SAIFI assessed values is provided in Schedule 4A of the determination.
- 4.13 Planned interruptions and unplanned interruptions are treated differently in calculating the SAIDI and SAIFI assessed values as prescribed within Schedule 4A. Due to their generally lower impact on consumers, planned interruptions are de-weighted by 50% while unplanned interruptions are given a full 100% weighting.

Normalisation

- 4.14 A normalisation methodology is applied to SAIDI and SAIFI data for the assessment of quality standards and the revenue-linked quality incentive scheme. This includes our normalisation of historic reference data for calculation of the SAIDI and SAIFI reliability limits and distributors' normalisation of assessed SAIDI and SAIFI values during the regulatory period for comparison against the limits.
- 4.15 The full explanation and rationale for SAIDI and SAIFI data normalisation is provided in the quality targets and incentives paper.⁶⁷

⁶⁴ Mergers and Amalgamations also require recalculation of an EDB's quality standards. This is discussed in 3.27 – 3.33 of Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁶⁵ Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁶⁶ See clause 11.5 of the determination.

⁶⁷ Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014), Chapter 3.

- 4.16 The normalisation approach is applied to reduce the effect of one-off extreme events to enable the observation of the underlying general level of reliability. Days with particularly high unplanned interruption SAIDI or SAIFI values (usually due to one-off extreme events) are known as major event days. The term 'major event day' is also defined in the determination.⁶⁸
- 4.17 The normalisation approach is applied to the SAIDI and SAIFI data separately. A day can be classified as a major event day for SAIDI but not for SAIFI and vice versa. For these days, the SAIDI or SAIFI value is replaced with a boundary value (explained in paragraph 4.22) to limit the effect of the unusually high SAIDI or SAIFI.
- 4.18 The normalisation approach is only applied to unplanned interruptions.
- 4.19 We have set the following normalisation parameters that must be used by distributors to calculate their assessed SAIDI and SAIFI values:
- 4.19.1 triggers for major event days; and
 - 4.19.2 boundary values for major event days.
- 4.20 We have used the same normalisation method and parameters to set the reliability limits, as described in the accompanying quality paper.⁶⁹

Triggers for major event days

- 4.21 The trigger for SAIDI and SAIFI major event days is when a distributor reaches the boundary value on any given day. This limits the amount of SAIDI and SAIFI that can be accrued by a distributor in any one day. The detail and rationale of this is provided in the accompanying quality paper.

Boundary values for major event days

- 4.22 The boundary values for major event days have been set for each distributor as the 23rd highest daily SAIDI and SAIFI event over the ten year reference period. The boundary values are only applied to unplanned interruptions. Further detail and rationale regarding boundary values is provided in the accompanying quality paper.⁷⁰
- 4.23 Boundary values are only applied to daily unplanned SAIDI and SAIFI values. This is because the normalisation for major event days is done to remove the effect of

⁶⁸ See clause 4.2 of the determination.

⁶⁹ Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014), paragraphs 3.17-3.43.

⁷⁰ Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014), Chapter 4.

extreme events outside the control of the distributors, whereas planned interruptions are generally within the control of the distributors.

- 4.24 The SAIDI effects of an interruption accrue only to the day in which the interruption began, regardless of whether the interruption continues into other days.⁷¹ This means that for a single large interruption the boundary value will only be applied once, which supports the aim of reducing the effect of extreme events outside the control of the distributors.

Information required to support statement about compliance

- 4.25 Along with stating whether or not they are compliant with the quality standards, distributors must provide certain information to support that statement, as explained below. The required information is set out in clause 11 of the determination.⁷²

Confirmation of compliance

- 4.26 The information required under 11.5(c), (d), (e), and (f) of the determination is required to assist us in confirming distributors' assessment of compliance. The information will help us understand the assessed SAIDI and SAIFI values reported..
- 4.27 Clause 11.5 (e) of the determination requires distributors to provide a description of policies and procedures used for recording SAIDI and SAIFI statistics.
- 4.28 This is the same requirement as existed in the Electricity Distribution Services Default Price-Quality Path Determination 2012. In undertaking previous compliance reviews we have noted inconsistencies between distributors in the level of detail provided in response to this requirement.⁷³
- 4.29 We expect that sufficient detail will be provided to clearly demonstrate the policies and procedures used for recording SAIDI and SAIFI. Distributors may find process diagrams that indicate the controls and checks performed useful in this regard. Where internal policy documents that are not publicly available are referred to a summary of the relevant content of these policies should be provided.
- 4.30 It is likely that distributors' practices for recording interruptions may be a focus of our attention in the future.

⁷¹ See 'SAIDI Value' definition within clause 4.2 of the determination.

⁷² See clause 11.5 of the determination.

⁷³ Commerce Commission "General comments on the default price-quality path compliance statements submitted by electricity distribution business for the 2011, 2012 and 2013 assessment periods" (17 December 2013).

- 4.31 Explanations for any major event days should clearly describe the cause(s) of the high SAIDI or SAIFI values for that day.

Understanding non-compliance

- 4.32 In addition to the information above, the following information is required because it will help us understand why a distributor has been non-compliant:

4.32.1 reasons for exceeding the SAIDI or SAIFI limit in the assessment period; and

4.32.2 what actions the distributor has taken to mitigate any non-compliance and to prevent similar non-compliance in the future.⁷⁴

- 4.33 The requirement applies where the SAIDI or SAIFI limit has been exceeded in the assessment period to enable timely receipt of information and because distributors will have the information more readily available. Were it to apply only in the instance of quality standards non-compliance (ie, failing the two out of three year rule) a distributor would need to revisit previous assessment periods to explain quality standard non-compliance.

- 4.34 Some distributors have previously submitted separate confidential documents to the Commission explaining in further detail the reasons for exceeding the SAIDI and / or SAIFI limits. This provides useful information to the Commission and assists in informing whether any further investigation is required.

Relationship between the quality standards and the quality incentive scheme

- 4.35 The revenue-linked quality incentive scheme can impose revenue gains or losses upon distributors depending on their assessed values of SAIDI and SAIFI. This operates separately from compliance with the quality standards.
- 4.36 A description of the revenue-linked quality incentive scheme is provided in the accompanying paper on quality.⁷⁵ This paper also provides more detail on the calculation of the SAIDI and SAIFI caps and limits, which are used in the assessment of compliance against the quality standards and for the calculation of the quality incentive adjustment.

Calculation of the Quality Incentive Adjustment

- 4.37 Schedule 5B of the determination describes how distributors are to calculate the quality incentive adjustment. The quality incentive adjustment is the recoverable cost consisting of the financial gain or loss that is attributable to the distributor's

⁷⁴ See clause 11.5 (a) and (b) of the determination.

⁷⁵ Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

reliability through the revenue-linked quality incentive scheme. The adjustment must be calculated within 50 working days following the end of the assessment period, and is then applied as a recoverable cost in the following assessment period (ie, there is a two-year lag).

- 4.38 Due to the one year lag on reporting and two-year lag on recovering the adjustment, no data and calculation towards a quality incentive adjustment will be required in the annual compliance statement in the first assessment period of the 2015 - 2020 regulatory period.
- 4.39 The parameters of the scheme are already set in the determination, but can be adjusted under Schedule 4B of the determination due to a major transaction, transmission asset purchase or sale, amalgamation or merger. In this case, a distributor would need to provide us with a clear and thorough explanation (through data and calculations) of the re-calculation of quality incentive scheme parameters in the annual compliance statement. The data and calculations should be sufficient for us to be able to carry out the re-calculation of the parameters for compliance checking.
- 4.40 Distributors are also required to provide a similar level of data and calculations used for their calculation of the quality incentive adjustment recoverable cost.
- 4.41 If the parameters of the incentive scheme (targets, caps and collars) are not changed for the assessment period using Schedule 4B of the determination, then the SAIDI and SAIFI incentive rates will remain as stated in the determination. If the parameters are changed due to a mid-period major transaction, transmission asset purchase or sale, amalgamation or merger the incentive rates will need to be re-calculated using Schedule 5B, in which case the calculations will need to be provided in the annual compliance statement.
- 4.42 The assessed values for SAIDI and SAIFI used for the calculation of the quality incentive scheme adjustment must be the same as the assessed values presented for the purposes of the quality standard. These values are discussed further in paragraphs 4.11 to 4.13.

5. Transactions

Purpose of this chapter

- 5.1 This chapter provides guidance to distributors on the compliance requirements relating to transactions.

There are four types of transactions

- 5.2 There are four types of transactions dealt with under the heading of “transactions” in the determination.⁷⁶ These are:
- 5.2.1 Amalgamations, which covers situations where two Non-Exempt EDBs amalgamate under Part 13 of the Companies Act 1993 (Companies Act);⁷⁷
 - 5.2.2 Mergers, which covers situations where one Non-exempt EDB takes over another Non-exempt EDB by any means other than a Part 13 Companies Act amalgamation;⁷⁸
 - 5.2.3 Major Transactions, which covers situations which result in consumers being served by a different distributor but which are not a Merger or Amalgamation between Non-exempt EDBs;⁷⁹ and
 - 5.2.4 Purchases of transmission assets from Transpower, or sale of system fixed assets to Transpower.
- 5.3 The definitions of the four types of transactions listed above are intended to be mutually exclusive.
- 5.4 The remainder of this chapter describes the compliance requirements relating to each of the types of large transaction listed above.

⁷⁶ See section 10 of the determination. “Transactions” is not itself a defined term, but rather a grouping of like clauses.

⁷⁷ For the complete definition, see clause 4.2 of the determination, which defines “Amalgamation” by reference to clause 1.1.4(2) of the Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26.

⁷⁸ For the complete definition, see clause 4.2 of the determination.

⁷⁹ A transaction between a Non-exempt and an Exempt EDB that would, but for the fact that it involves an Exempt EDB, be a Merger, will therefore be a Major Transaction. Likewise, a transaction between a Non-exempt and an Exempt EDB that would, but for the fact that it involves an Exempt EDB, be an Amalgamation, will be a Major Transaction.

Compliance requirements for Amalgamations and Mergers

5.5 The compliance requirements for amalgamations and mergers are the same.

Requirement to notify the Commission of an agreement for amalgamation or merger

5.6 Each Non-exempt EDB that has entered into an agreement for a Merger or Amalgamation must notify the Commission in writing within 30 Working Days of entering into the agreement if the transaction meets either of the size thresholds set out at clause 10.1 of the determination.⁸⁰

Treatment of the price-quality path following a Merger or Amalgamation

5.7 Where a Non-exempt EDB completes a Merger or Amalgamation with another Non-exempt EDB, clause 10.3 of the determination address how the price-quality paths⁸¹ of the Non-exempt EDBs involved in the Merger or Amalgamation are determined following the Merger or Amalgamation.⁸² In this situation, amalgamations and mergers are effectively treated the same. In the case of amalgamations, clause 10.3 of the determination requires that clause 3.2.1 of the Input Methodologies relating to amalgamations applies, or the case of mergers, that clause 3.2.1 of the Input Methodologies applies as if the Merger was an Amalgamation.

5.8 In addition, the resulting Non-exempt EDB must aggregate its quality path. How this is to be performed is contained within Schedule 4B.

Reporting of Amalgamations and Mergers in the annual compliance statement

5.9 Every Non-exempt EDB's compliance statement must state whether or not an amalgamation or merger has occurred in the assessment period.⁸³

⁸⁰ It could be the case that for one distributor involved in the Merger or Amalgamation, the notification threshold in clause 10.1 is met, while for the other distributor involved, the threshold is not met. In this case, only the distributor for which the threshold is met is required to notify the Commission of the Merger or Amalgamation.

⁸¹ Mergers and Amalgamations also require recalculation of a distributor's quality standards. This is discussed at paragraphs 3.27-3.33 in Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁸² See clause 10.3 of the determination. Note that these requirements apply to all Mergers and Amalgamations, irrespective of whether the transaction meets the prior notification threshold.

⁸³ See clause 11.2(d)(iii) of the determination. Whether a major transaction has 'occurred' during the period is defined within clause 10.5 of the determination.

- 5.10 If a Non-exempt EDB has entered into an agreement for a Merger or Amalgamation in the assessment period, that Non-exempt EDB must in its compliance statement:
- 5.10.1 state whether it has complied with the notification requirement in clause 10.1 of the determination;⁸⁴ and
 - 5.10.2 include information or calculations demonstrating that clause 10.1 notification requirement was met (ie, by demonstrating that the transaction met/did not meet the notification threshold and so notification was given/not given).⁸⁵
- 5.11 If a Non-exempt EDB has completed a Merger or Amalgamation in the assessment period, it must in its compliance statement:
- 5.11.1 state whether or not it has complied with clause 10.3 of the determination by applying clause 3.2.1 of the IMs;⁸⁶ and
 - 5.11.2 include any information or calculations required to be made in applying clause 3.2.1 of the IMs (ie, showing how its price-quality path was determined following the Merger or Amalgamation).⁸⁷

Compliance requirements for Major Transactions

- 5.12 Some of the compliance requirements that apply to Mergers and Amalgamations also apply to major transactions. However, there are some requirements that differ.

Requirement to notify the Commission of an agreement for a Major Transaction

- 5.13 As is the case for Mergers and Amalgamations, each Non-exempt EDB that has entered into an agreement for a major transaction must notify the Commission in writing within 30 Working Days of entering into the agreement, if the transaction meets either of the size thresholds set out at clause 10.1 of the determination.⁸⁸
- 5.14 A notice to the Commission of a Major Transaction must include the information set out at clause 10.2 of the determination to the extent the information is practically available.

⁸⁴ See clause 11.6(a) of the determination.

⁸⁵ See clause 11.6(b) of the determination.

⁸⁶ See clause 11.6(a) of the determination.

⁸⁷ See clause 11.6(b) of the determination.

⁸⁸ Note that it could be the case that for one distributor involved in the Major Transaction, the notification threshold in clause 10.1 is met, while for the other distributor involved, the threshold is not met. In this case, only the distributor for which the threshold is met is required to notify the Commission of the Major Transaction.

- 5.15 We adopted the standard of practically available because we recognise that not all of the requested information will be available within 30 Working Days of entering the agreement for a major transaction.⁸⁹ Where requested information is not provided on the grounds that it is not practically available, we expect the notice to explain why the information was not practically available. We also require that the information not initially provided will be provided as soon as it becomes available.

Re-calculation requirements upon completing a Major Transaction

- 5.16 The major transactions provisions of the determination set out how distributors are to calculate its allowable notional revenue, notional revenue, pass-through balance and quality measures following the transaction.⁹⁰
- 5.17 The purpose of the re-calculation requirements set out below is to maintain the price-quality paths that apply during a regulatory period and to ensure consumers supplied by either electricity distribution business are not, in aggregate for either electricity distribution business worse off as a result of the transaction.
- 5.18 In the period in which a major transaction occurs, each Non-exempt EDB that was involved must:⁹¹
- 5.18.1 adjust its allowable notional revenue in accordance with Schedule 3C of the determination;⁹²
 - 5.18.2 adjust the Pass-through Balance in accordance with Schedule 3C of the determination; and
 - 5.18.3 recalculate the quality measures that apply to the distributor, which is discussed further in the quality targets and incentives paper.⁹³

⁸⁹ See Electricity Networks Association "Submission on the detailed drafting of the Draft DPP Determination and IM amendments" paragraph 181.

⁹⁰ Major Transactions also require recalculation of a distributor's quality standards. This is discussed in Chapter 3 of Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

⁹¹ See clause 10.4 of the determination. Note that these requirements apply to all Major Transactions, irrespective of whether the transaction meets the prior notification threshold.

⁹² See clause 10.4(a) of the determination.

⁹³ See clause 10.4(c) of the determination and Chapter 3 of Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

- 5.19 We have revised our approach from the revised draft determination which required distributors to establish the pass-through costs and recoverable costs attributable to the major transaction.⁹⁴ We consider that these costs will be appropriately recognised by the distributor who incurs the cost based on the recognition criteria within Schedule 5 and there is no need for additional allocation rules.
- 5.20 Our revised draft determination did not explicitly require a change in the pass-through balance following a major transaction. We have revised this approach and now require an adjustment to the Pass-through balance to also be recognised. We believe this is more consistent with the purpose of the re-calculation requirements as stated at paragraph 5.17 and indicated previously.⁹⁵

Further detail on the re-calculation requirements in Schedule 3C of the determination

- 5.21 Our focus is on ensuring the weighted average distribution prices are maintained at an equivalent level, and therefore providing no disincentive for parties to maintain prices for consumers at a similar level to the level that would have occurred absent the transaction.
- 5.22 Schedule 3C provides two sets of re-calculation requirements:⁹⁶
- 5.22.1 one applies where the counterparty to the Major Transaction is another Non-exempt EDB; and
 - 5.22.2 the other applies where the counterparty to the major transaction is an Exempt EDB.

⁹⁴ See Commerce Commission "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015" (20 October 2014), clause 10.2 (c).

⁹⁵ Commerce Commission "How we propose to implement default price-quality paths for electricity distributors from 1 April 2015" (20 October 2014), paragraph 4.44; and Commerce Commission "Proposed Compliance Requirements for the 2015-2020 Default Price-Quality Paths for Electricity Distributors" (18 July 2014), paragraph 5.7.2.

⁹⁶ Where Schedule 3C does not specify an adjustment to an input to the price path that input is to be determined in accordance with the normal price path formula in clause 8 of the determination. For example, notional revenue is calculated in accordance with the normal clause 8 formula because the inputs to notional revenue are unaffected by the Major Transaction. Whereas, Schedule 3C requires that allowable notional revenue transfers because there is no lagged price.

- 5.23 When both parties to the transaction are non-exempt distributors, the parties themselves must determine the allocation of allowable notional revenue and pass-through balance attributable to the ICPs transferred as a result of the transaction.⁹⁷ The allocation of these amounts agreed by the parties must reasonably relate to the ICPs transferred.⁹⁸
- 5.24 However, where a Non-exempt EDB completes a major transaction with an Exempt EDB, there will be no price path amounts for the exempt EDB. In these circumstances, the non-exempt EDB calculates the changes required to allowable notional revenue and pass-through balance using a formula-based approach.
- 5.25 For transactions between a non-exempt EDB and an exempt EDB, a ratio referred to as the 'transaction factor' is calculated by dividing:
- 5.25.1 the sum of the seller's prices multiplied by quantities for the assets being sold; by
 - 5.25.2 the sum of the seller's prices multiplied by quantities for all of the seller's network.
- 5.26 This 'transaction factor' is then used as an allocator to determine the amount attributable to the transaction for some of the components of the price path calculations.
- 5.27 The 'transaction factor' is used to represent a measure of the size of the transaction rather than requiring the exact allocation of all cost and quantity components to be determined.
- 5.28 The values used in this calculation are 'prices' (as opposed to separate distribution and pass-through prices). This is because, for an exempt distributor, only a total 'price' will be available (ie, it will not necessarily have separate distribution and pass-through prices).

⁹⁷ See Schedule 3C, paragraph 2, of the determination.

⁹⁸ Previously the Commerce Commission "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015" (20 October 2014), Schedule 3C clause 1 required a distributor to 'demonstrate to the reasonable satisfaction of the Commission' which applied across all clauses within this schedule. This requirement has been removed and Schedule 3 clause 2 has been adjusted to reflect that the allocations agreed between the distributors must be demonstrably reasonable.

- 5.29 For transactions between a non-exempt distributor and an exempt distributor, we specify a 'Part-year Factor', which is the proportion of an assessment year for which the new ownership arrangements apply. This factor is then used to allocate amounts that would have otherwise applied had the transaction taken effect from the first day of the assessment period.
- 5.30 Schedule 3C also allows a Non-exempt EDB that has completed a major transaction with an Exempt EDB to propose an alternative approach for calculating allowable notional revenue and the impact on pass-through balance following a major transaction, using any reasonable alternative methodology.⁹⁹ We expect this may be used where cost and quantity components are able to be more accurately assigned than on a proportion basis.
- 5.31 Where a distributor proposes an alternative approach under Schedule 3C, we would expect the proposal to explain why the alternative approach better gives effect to the principle outlined at paragraph 5.17 above than the prescribed approach.
- 5.32 The process for approval of a proposal for an alternative approach is discussed further in the approvals section of this paper at Chapter 9.

Reporting of Major Transactions in the annual compliance statement

- 5.33 Every Non-exempt EDB's compliance statement must state whether or not a major transaction has occurred in the assessment period.¹⁰⁰

⁹⁹ See Schedule 3C, paragraph 9. We note Orion's submission that we should allow an alternative compliance approach to be used where a Non-exempt EDB completes a Major Transaction with an Non - Exempt EDB (see Orion "Submission on the revised draft DPP determination and related documents" (31 October 2014), para 14). We have limited the availability of the alternative compliance provision to Major Transactions involving an Exempt EDB because we consider that the recalculation requirements for Major Transactions between Non-Exempt EDBs are sufficiently flexible in that the parties are free to agree any reasonable allocation. Whereas, for Major Transactions involving an Exempt EDB, there is a prescriptive recalculation methodology.

¹⁰⁰ See clause 11.2(d)(iv) of the determination.

- 5.34 If a Non-exempt EDB has entered into an agreement for a major transaction in the assessment period, that Non-exempt EDB must in its compliance statement:
- 5.34.1 state whether it has complied with the notification requirement in clauses 10.1 and 10.2 of the determination;¹⁰¹
 - 5.34.2 include information or calculations showing why the clause 10.1 notification requirement was met (ie, by demonstrating that the transaction met/did not meet the notification threshold and so notification was given/not given).¹⁰² When as a result of a major transaction ICP's are being supplied by a different EDB in the assessment period, a distributor must in its compliance statement:
 - 5.34.3 state whether it has complied with the requirements of clause 10.4 by applying Schedule 3C and Schedule 4B;¹⁰³ and
 - 5.34.4 include information or calculations demonstrating that Schedule 3C and Schedule 4B were applied in re-calculating the price path and quality standards for the purposes of clause 10.4 of the determination.¹⁰⁴

Compliance requirements for transfers of transmission assets to or Transpower

- 5.35 Unlike for amalgamations, mergers and major transactions, the compliance requirements relating to the purchase of transmission assets from Transpower or sale of such assets back to Transpower, largely relate to the quality standards rather than the price path.
- 5.36 The price path is not significantly affected by the purchase of transmission assets from Transpower because the reduction in transmission charges following the purchase is essentially offset by a recoverable cost relating to the avoided transmission charges.

Compliance requirements upon completing a transfer of transmission assets

- 5.37 Once a Non-exempt EDB completes a purchase of transmission assets from Transpower that become system fixed assets of the distributor, the Non-exempt EDB must recalculate its quality standards in accordance with Schedule 4B of the determination.¹⁰⁵ This requirement also applies where a Non-exempt EDB completes

¹⁰¹ See clause 11.6(a) of the determination.

¹⁰² See clause 11.6(b) of the determination.

¹⁰³ See clause 11.6(a) of the determination.

¹⁰⁴ See clause 11.6(b) of the determination.

¹⁰⁵ See clause 10.5 of the determination.

a purchase of transmission assets from Transpower in the year 2014/15 assessment period. Including those purchases identified at Schedule 5F for Eastland Network Limited and Network Tasman Limited.

- 5.38 The adjustment to the quality standards is discussed further in the quality incentives and targets paper.¹⁰⁶

Reporting of completed purchases of transmission assets from Transpower in the annual compliance statement

- 5.39 Every Non-exempt EDB's compliance statement must state whether or not it has received system fixed assets from Transpower in the assessment period.¹⁰⁷

¹⁰⁶ See clause 10.4(c) of the determination and Chapter 3 of Commerce Commission "Quality targets and incentives for default price-quality paths for electricity distributors from 1 April 2015" (28 November 2014).

¹⁰⁷ See clause 11.2(d)(ii) of the determination.

6. Price restructuring

Purpose of this chapter

6.1 This chapter provides guidance on the compliance obligations for distributors that restructure their prices. In particular, it covers:

- 6.1.1 the rules for determining quantities following a price restructuring;¹⁰⁸ and
- 6.1.2 the reporting obligations following a price restructuring.¹⁰⁹

Purpose of the price restructuring requirements

6.2 When calculating notional revenue and allowable notional revenue, a distributor must use the quantities from two years previous ('lagged' or 'historical' quantities) that correspond to the extent practicable with each of its prices.¹¹⁰ A price restructure may make it difficult to establish lagged quantities that relate to prices. The rules set out in the determination explain which quantities should be used, and how to derive a reasonable estimate where actual lagged quantities are not available or they do not practicably correspond to a restructured price

We have updated the price restructuring requirements

6.3 We have adjusted the compliance requirements relating to price restructuring from the 2012 determination. These changes have been made as a result of concerns raised with the previous price restructure requirements as noted in some distributors compliance statements. The changes to the price restructuring requirements are focused on clarifying how the quantities corresponding to restructured prices are to be determined. In particular, we have introduced:

- 6.3.1 a definition of price restructuring;
- 6.3.2 rules for how suppliers are to determine quantities where they undertake a price restructure;
- 6.3.3 guidance for situations where lagged quantity data is available; and
- 6.3.4 guidance for situations where lagged quantity data which corresponds to price is not available or where the lagged quantity is considered to not practicably relate to the restructured price.

¹⁰⁸ These are found within clause 8 of the determination.

¹⁰⁹ These are found within clause 11 of the determination.

¹¹⁰ As per the definition of quantities set out in clause 3.1.1.(5)(a) of the Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26.

- 6.4 We consider that the new approach provides greater clarity for distributors about the treatment of pricing restructures.

Price restructuring is now defined

- 6.5 We have introduced a definition of price restructuring to make it easier for distributors to identify whether a given change to its prices needs to be treated as a restructuring.¹¹¹
- 6.6 Restructure of prices means any change in the allocation of connections to Consumer Groups, the introduction of a new Consumer Group, or any change in Prices, but excludes:
- 6.6.1 a change to the value of a Price applicable to an existing Consumer Group; and
 - 6.6.2 the movement of connections between existing Consumer Groups at the request of the Consumer or retailer.

Rules relating to price restructuring

- 6.7 A distributor may restructure its prices during an assessment period. A price restructuring will affect how it calculates notional revenue for that period because it may be difficult to identify a lagged quantity that corresponds to a current price. However, a price restructure does not impact a distributor's allowable notional revenue because allowable notional revenue is determined using prices from the prior period, which will be unaffected by the restructure and will therefore correspond to lagged quantities.

¹¹¹ Restructure of prices was not defined in the 2012 determination.

- 6.8 The distributor must use the quantities determined using the rules described below to:
- 6.8.1 in the assessment period in which the restructure took place, calculate notional revenue;¹¹² and
 - 6.8.2 in the assessment period immediately following that in which the restructure took place, calculate allowable notional revenue and notional revenue.¹¹³

Rules for determining quantities

- 6.9 When distributors calculate allowable notional revenue and notional revenue, they must:
- 6.9.1 use the same quantities in calculating both allowable notional revenue and notional revenue;¹¹⁴ and
 - 6.9.2 for every price in their pricing schedule, have a quantity (other than forecasts) that corresponds to the extent practicable to that price.¹¹⁵
- 6.10 The general principle underpinning these requirements is that quantities should follow the price to which they relate.

¹¹² See clause 8.8(a) of the determination. As identified by the ENA, allowable notional revenue is not recalculated in the year of the price restructure, but notional revenue is (see ENA “Submission on the technical drafting of the Draft DPP Determination and IM amendments” (31 October 2014), para 16). Allowable notional revenue is not recalculated, because it is based on prices from the year before the restructure, which will therefore correspond to a lagged quantity. As a result, for the year in which the restructure occurred, the lagged quantities used for notional revenue may differ from those used for allowable notional revenue. We recognise that this creates a compliance risk and will therefore have a particular focus on assessing the compliance of price restructures involving the estimation of lagged quantities. As discussed further below, we would therefore encourage distributors contemplating a pricing restructure to discuss it with the Commission well in advance of undertaking it.

¹¹³ See clause 8.8(b) of the determination.

¹¹⁴ Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26, clause 3.1.1(1)(d).

¹¹⁵ Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26, clause 3.1.1(5)(a).

Where historical quantities are available

- 6.11 In practice, using historical quantity information to work out the quantities that correspond to prices in a restructured price schedule may be straightforward. Instances of this for which we have determined specific rules are:¹¹⁶
- 6.11.1 combining consumer groups; and
 - 6.11.2 separating a consumer group.¹¹⁷
- 6.12 Where the distributor has combined existing consumer groups, the quantity corresponding to this group is the sum of the quantities corresponding to each of the previous groups.
- 6.13 Where the distributor has assigned connections in an existing group into multiple new groups, the quantities corresponding to each new consumer group must be based on the connections from the original group assigned to each new group. As such, the sum of the quantities for all of the new groups must equal the sum of the quantities for the original group.

Where historical quantities may be estimated

- 6.14 In some circumstances, it may be considered that the lagged quantity which is available does not reasonably correspond to the restructured price. In other circumstances, corresponding lagged quantities may not be available. In these circumstances a distributor must derive a demonstrably reasonable estimate of a lagged quantity which corresponds to the restructured price.¹¹⁸
- 6.15 Unison submitted that the Commission's approach to price restructures within the draft DPP Determination and revised draft determination were unlawful when considered against the mandatory requirements of section 54Q of the Commerce Act 1986.¹¹⁹

¹¹⁶ See clause 8.9 of the determination.

¹¹⁷ In our draft determination, we had a third instance for which we proposed to specify a rule. That was where the distributor creates a new 'empty' consumer group (ie, one that is to be populated only by consumers moving by their own request or the request of their retailer). In that situation, we had proposed that the quantity corresponding to that group be zero. Having considered Vector's submission that this treatment may discourage distributors from introducing innovative price structures that may be of benefit of to consumers, we have not included that provision in the final determination (see Vector "Mark-ups by Vector Limited for submission purposes" (20 October 2014), page 15, comment A11.

¹¹⁸ See clause 8.10 of the determination.

¹¹⁹ Unison Networks Limited "Submission on Proposed Compliance Requirements for the 2015-2020 DPP for Electricity Distributors" (29 August 2014); and Unison Networks Limited "Submission on DPP draft determination, IM amendments and associated companion papers" (31 October 2014).

- 6.16 The revised draft determination required distributors to use actual lagged quantities against restructured prices.
- 6.17 Unison submitted that the Commission could provide for the effects of structural changes to be accounted for in the restructuring provisions by allowing reasonable demand elasticities to be applied to relative price changes between existing tariffs and restructured tariffs or by allowing recovery as an Energy Efficiency and Demand Incentive Allowance.
- 6.18 While we do not consider the requirements proposed in the revised draft were unlawful when considered against s54Q of the Commerce Act 1986, the price restructure provisions have been adjusted between the technical and final determination. The revision allows a distributor to use an estimate of lagged quantities(t-2) where quantities are available which could be allocated against the restructured price but a distributor considers these do not reasonably correspond to the restructured price.
- 6.19 An example of where this may apply includes the introduction of time-of-use tariffs during an assessment period, which is anticipated to impact consumer behaviour and usage. The introduction of these tariffs may result in the lagged t-2 quantities not reasonably corresponding to a restructured price. Where this occurs the quantity allocated between tariff codes must be demonstrably reasonable and meet the requirements contained within clause 8.10 (a) – (d).
- 6.20 We believe there would be limited instances where an adjustment to the quantum of the lagged t-2 quantities would be appropriate. Instead the estimation would reflect the best estimate of the appropriate allocation of quantities to the restructured tariff codes.
- 6.21 The price restructure requirements allow suppliers to retain pricing flexibility to set time-of-use tariffs, eg, peak/off-peak, and seasonal prices.
- 6.22 For any price restructuring other than the types listed in paragraph 6.11, all prices in a distributor's price schedule must still have a two-year lagged quantity associated with them.

- 6.23 Where an estimate is being used, a distributor may use any reasonable methodology to calculate it, provided that it uses any relevant information – related to quantities or otherwise – available at the time.¹²⁰ However, a distributor may not estimate any quantity using any forecast quantities.¹²¹ Once the distributor has adopted the methodology for determining quantities, it must continue to use a substantially similar methodology for future assessment periods.¹²²
- 6.24 We expect that price restructuring will be a particular focus for our compliance checking over the next regulatory period, particularly where estimated quantities have been used.

Obligation to report price restructuring in the annual compliance statement

- 6.25 There are a number of reporting obligations relating to price restructuring. These are found in clause 11 of the determination and explained below.

Every distributor must state whether or not a price restructuring occurred

- 6.26 Every distributor must state in its annual compliance statement whether or not it has undertaken a price restructuring in the assessment period or the previous assessment period.¹²³

Reporting obligations where a price restructuring has taken place

- 6.27 If a distributor has undertaken a price restructure that first applied in the most recent or prior assessment period, that distributor must in its compliance statement:¹²⁴
- 6.27.1 state the nature of the price restructuring. For example, state whether new consumer groups were created, deleted, merged or split. We expect this to include an explanation of the rationale of the price restructuring; and
 - 6.27.2 identify the consumer groups affected by the restructuring.

¹²⁰ Previously the Commerce Commission "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015" (20 October 2014), 8.10 required a distributor to 'demonstrate to the reasonable satisfaction of the Commission'. This requirement has been removed and Clause 8.10 has been adjusted to reflect that the estimate of quantity used must be demonstrably reasonable.

¹²¹ See clause 8.10(a) of the determination.

¹²² See clause 8.10(d) of the determination.

¹²³ See clause 11.2(d)(i) of the determination.

¹²⁴ See clause 11.7 of the determination.

Additional reporting obligations for restructures where no lagged quantity exists

- 6.28 If a Non-exempt EDB has undertaken a price restructuring and no lagged quantity exists that corresponds to a restructured price, that distributor must provide additional information its compliance statement for the assessment period in which that restructure first applied.¹²⁵
- 6.29 For each restructured price where no lagged quantity exists, the distributor must:
- 6.29.1 explain the methodology used to determine the corresponding lagged quantity;
 - 6.29.2 provide a forecast of the corresponding quantity for the assessment period in which the restructure occurred, prepared by the distributor at the time it restructured the Price; and
 - 6.29.3 provide the corresponding actual quantity for the assessment period in which the restructure occurred.
- 6.30 The distributor must also explain any differences between the forecast and actual quantities described above at paragraphs 6.29.2 and 6.29.3. A difference between the forecast and actual quantities does not amount to non-compliance. Rather, this information provides useful context for the Commission in assessing the reasonableness of the quantities used for assessing compliance within the annual compliance statement.

We have not adopted the proposed prior notification requirement for price restructuring

- 6.31 In our draft determination, we proposed a requirement that distributors notify the Commission in advance of undertaking a price restructuring.
- 6.32 We proposed the prior notification requirement in order to mitigate the risk of distributors undertaking price restructuring and using estimates of quantities which are later considered inappropriate. We intended this requirement to be for the benefit of suppliers, but a number of objections were raised to it.¹²⁶

¹²⁵ See clause 11.8 of the determination.

¹²⁶ See for example: Orion “Submission on the revised draft DPP determination and related documents” (31 October 2014), paragraphs 8–11; and Powerco “Technical and additional consultation on the electricity distribution default price-quality path from 1 April 2015” (31 October 2014), paragraphs 12–13.

- 6.33 Given that suppliers are not precluded from approaching the Commission to discuss a contemplated price restructuring, we have removed the requirement for prior notification to the Commission. By removing this requirement, we have essentially made prior notification of a price restructure optional, should the distributor wish to seek guidance from the Commission on the contemplated restructuring.
- 6.34 We would strongly encourage distributors that are unsure about the impacts of contemplated price restructures to contact the Commission well in advance of undertaking them.

7. Compensation for demand side management initiatives

Purpose of this chapter

- 7.1 This chapter outlines and explains the information that we require in support of an application for compensation under the energy efficiency and demand side management incentive. It also describes the process for having the amounts approved.
- 7.2 Further information on the energy efficiency and demand side management incentive is contained within the main policy paper.¹²⁷

Application for compensation

- 7.3 Applications for approval of an energy efficiency and demand side management incentive allowance are to be submitted no later than 70 working days after the assessment period for which an allowance is sought.¹²⁸
- 7.4 Qualifying initiatives:¹²⁹
 - 7.4.1 include initiatives where distributors can demonstrate energy efficiency or demand side management purpose and intent; and
 - 7.4.2 exclude predominantly tariff-based measures .
- 7.5 Following assessment of the information provided, we would determine an amount of foregone revenue attributable to the energy efficiency or demand side management initiative.¹³⁰ We may also request additional information we consider necessary to establish a causal link between the foregone revenue and the initiatives undertaken by the distributor.

¹²⁷ Commerce Commission "Default price-quality paths for electricity distributors from 1 April 2015 to 31 March 2020: Main policy paper" (28 November 2014), Chapter 7.

¹²⁸ This timeframe gives us time to approve applications by the end of November in time for distributors to set the following year's prices. The timeframe also allows distributors to streamline any sign-off requirements needed for both the compliance statement and energy efficiency incentive applications.

¹²⁹ The scope of the scheme is discussed in the main policy paper: Commerce Commission "Default price-quality paths for electricity distributors from 1 April 2015 to 31 March 2020: Main policy paper" (28 November 2014), Chapter 7 and Attachment E.

¹³⁰ For the avoidance of doubt, if approved, the recoverable cost would be applied two assessment periods after the assessment period to which the foregone revenue relates.

Contents of an application

7.6 As described in the determination any application should include:¹³¹

- 7.6.1 A detailed description of the energy efficiency or demand side management initiative, program, or activity for which the EDB seeks an energy efficiency and demand side management incentive allowance;
- 7.6.2 Reasonable estimates of the actual foregone quantities arising in the Assessment Period from each energy efficiency or demand side management initiative, program, or activity, as well as the data, calculations, and assumptions used to derive the estimate;
- 7.6.3 A statement identifying other factors that may have materially contributed to the foregone quantities and reasonable estimates of their impact;
- 7.6.4 The Price(s) that applied to the foregone quantities during the Assessment Period; and
- 7.6.5 An estimate of foregone revenue directly attributable to the energy efficiency or demand side management initiative, program, or activity.

Demonstrating and verifying the link between activities and foregone revenue

- 7.7 The key aspect of the approval process will be for the Commission to obtain confidence in the link between initiatives undertaken by the distributors and the reduction in quantities claimed by the applicant, without requiring overly onerous verification procedures.
- 7.8 We have adopted a principles based approach to establishing the link between energy efficiency and foregone revenue. A credible link must be demonstrated between the activity and foregone revenue in order for the incentive to adequately promote outcomes described in s 54Q of the Commerce Act 1986.
- 7.9 However high costs of demonstrating and verifying such a link may hamper these objectives. A principles based approach that provides some discretion as to the level of scrutiny and information required offers an appropriate solution.

¹³¹ Electricity Distribution Services Default Price-Quality Path Determination 2015 [2015] NZCC 33, Schedule 5A.

- 7.10 The principles based approach was supported by submitters who realise it is a practical method for introducing the scheme, but also noted the Commission needs to be seen to be acting in “fair and reasonable” manner when applying the principles.¹³²
- 7.11 The principles that we intend to apply are shown in Table 7.1.

¹³² Electricity Networks Association "Submission on proposed compliance requirements for the 2015-2020 Default Price-Quality Paths for electricity distributors" (29 August 2014), paragraph 152; and Vector "Submission on the Default Price-Quality Paths from 1 April 2015: Main Policy Paper" (15 August 2014), paragraph 91.

Table 7.1– Principles for estimating foregone revenue

1	Foregone revenue (FR) occurs as a result of a change in quantities to which a value is attributed; the calculation should separately identify the foregone quantity estimate (FQ) and the price estimate (P).
2	The price estimate shall be those components that relate to the use of the distribution network (i.e. price components from generation, transmission and retail should be excluded)
3	The foregone quantities may include energy consumption, energy demand and/or capacity. In addition, the quantities may relate to a specific time-period such as peak, off peak, or shoulder. Estimates of foregone quantities provided should be consistent with the relevant tariff structure
4	The energy efficiency initiative should be aimed at a clearly identified target quantity reduction (such as energy demand). This may be different to the actual quantity reduction calculated after the initiative has been implemented. The target quantity reduction for the efficiency initiative should be identified as part of the EDB's design of the measure.
5	When estimating foregone revenue (<i>ex-post</i>), the actual quantities foregone should be compared with the targeted change in quantities. The estimation process should consider whether other factors (such as weather or economic conditions) may explain part or all of the reduction in demand claimed. The application, or reporting, should state why the energy efficiency initiative provides a credible explanation for foregone revenue
6	Estimates of foregone quantities may be derived with reference to a representative sample, accompanied with an explanation of how it provides a reasonable estimate of actual aggregate effects of the initiative. If the efficiency measure is implemented and managed through an energy performance contract or similar arrangement, the measurement process under the contract may meet this requirement
7	Estimates of prices to be applied to foregone quantities should be based on the appropriate tariff applying at the time the quantity was foregone. In other words, if an EDB implements an efficiency initiative in year t-1 which results in lower quantities in year t-1, then the relevant price is that tariff that would have applied to the foregone quantity in year t-1
8	If the efficiency initiative is targeted at a specific customer or project, the actual tariff applying to that customer or project should be used to estimate the foregone revenue.
9	If the efficiency initiative affects quantities associated with more than one tariff, the price can be estimated based on actual quantities or appropriate weightings. The basis for any weighting needs to be shown to be appropriate for an estimate of foregone revenue
10	The approaches used to estimate changes in quantities should be consistent with the prices used to determine foregone revenues. For example, the same approach and assumptions should be used for weighting quantities and prices
11	The Commission may request further information, independent evidence, director certificates or audit statements relating to the activities, sample or calculations used to establish the link between the initiative and foregone revenue. However, such requests shall take into account the likely cost of providing the information relative to the extent of the benefits identified."

Further information may be required

- 7.12 Principle 11 in Table 7.1 notes that further information requests may be required as part of the verification process. This is consistent with the approach recommended by Castalia to ensure the amount of information required reflects an appropriate standard of confidence in the link between energy efficiency and foregone revenue as part of the D-factor scheme established under the default price-quality path.¹³³
- 7.13 The further information steps that may be undertaken by the Commission are:
- 7.13.1 requesting further information on the activities, representative samples or the calculations made to establish the link with foregone revenues;
 - 7.13.2 requesting an independent review of foregone revenue calculations or their basis; and/or
 - 7.13.3 obtaining director certificates and/or an audit statement declaring the accuracy and veracity of the information presented.¹³⁴
- 7.14 It will be up to the Commission to determine which of these justifications, if any, will be required in each case. As noted in the draft decision reasons paper we are committed to ensuring that compliance costs are as low as practical in order to maintain the benefits of any energy efficiency initiatives.¹³⁵
- 7.15 Submissions agreed with this approach and we have further underlined this commitment by including an additional Principle 11 at the suggestion of the ENA that specifically refers to balancing these objectives.¹³⁶

¹³³ Castalia, "Providing a D-Factor Mechanism under the DPP Framework: Report to Vector", (April 2014).

¹³⁴ Depending on the timing and mode of recovery, these certifications may already accompany the distributor's annual compliance statement.

¹³⁵ Commerce Commission "Proposed default price-quality paths for electricity distributors from 1 April 2015" (4 July 2014), paragraph E19.

¹³⁶ Electricity Networks Association "Submission on proposed compliance requirements for the 2015-2020 Default Price-Quality Paths for electricity distributors" (29 August 2014), Attachment A; and Vector "Submission on Proposed Electricity DPP Compliance Requirements" (29 August 2014), paragraph 32.

Level of detail in the determination

- 7.16 A number of submissions were keen for us to provide more detail in the determination on the approvals process. In particular there were suggestions that the determination should be revised to include:¹³⁷
- 7.16.1 the principles we will apply making a decision on whether to approve an application;¹³⁸
 - 7.16.2 a timeline of the approval process; and
 - 7.16.3 a statement that we will take into account the costs of requesting and processing further information against the value of the foregone revenue being applied for.
- 7.17 The provision of principles in this paper is intended to give distributors sufficient certainty about the approach the Commission will take when assessing applications.
- 7.18 We provide further details on our approach to the approvals process of the energy efficiency and demand side management incentive in chapter 9.

¹³⁷ Electricity Networks Association "ENA submission (determination mark-ups) on revised draft DPP for EDBs from 1 April 2015" (31 October 2014), Schedule 5A, Vector "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015: Mark-ups by Vector Limited for submission purposes" (31 October 2014), Schedule 5A; and Wellington Electricity "WELL submission (determination mark-ups) on revised draft DPP for EDBs from 1 April 2015" (31 October 2014), Schedule 5A.

¹³⁸ The principles are those provided in Table 7.1.

8. Dates for proposing a customised price-quality path

Purpose of chapter

- 8.1 This chapter explains, and provides reasons for, the dates that distributors may propose customised price-quality paths during the regulatory period from 1 April 2015 to 31 March 2020.
- 8.2 This chapter covers:
- 8.2.1 the dates for proposing a customised price-quality path; and
 - 8.2.2 the length and timing of the application windows;

Dates for proposing a customised price-quality path

- 8.3 Our final decision is consistent with our draft decision for the dates that distributors may propose a customised price-quality path during the regulatory period from 1 April 2015 to 31 March 2020 (other than following a catastrophic event). These dates are set out in Table 8.1.

Table 8.1: Dates for proposing a customised price-quality path¹³⁹

Calendar year	February window	May window
2015		Mon 4 May—Mon 11 May
2016	Mon 8 Feb—Mon 15 Feb	Mon 2 May—Mon 9 May
2017	Mon 13 Feb—Mon 20 Feb	Mon 1 May—Mon 8 May
2018	Mon 12 Feb—Mon 19 Feb	Mon 7 May—Mon 14 May
2019	Mon 11 Feb—Mon 18 Feb	

- 8.4 We have not made any changes to the timing of the application windows that were provided as part of our draft decision.

¹³⁹ Following a catastrophic event, a customised price-quality path proposal may be made at any time during the 24 months following the event. However, no customised price-quality path proposals can be submitted in the 12 months before the end of a regulatory period.

Length and timing of the application windows

- 8.5 We limit applications to two one-week windows because the Act requires us to prioritise applications, and provides prioritisation criteria, where we receive more than four in one year.¹⁴⁰ In order to undertake this prioritisation exercise in accordance with s 53Z (3), we need set timeframes for when proposals may be submitted.
- 8.6 The first of these windows as set out in the determination is the second full week of February.¹⁴¹ This is so that the Commission can prioritise applications, complete the customised price-quality path determinations within the statutory timeframes, and have them ready to come into effect at the beginning of the next disclosure year.
- 8.7 The second window is set in the first full week of May to allow distributors a second chance each year to submit an application. Customised price-quality path proposals submitted in this window may not be evaluated in time to come into effect at the beginning of the next disclosure year.
- 8.8 There are no application windows in February 2015 or in May 2019. This is because customised price-quality paths are not permitted under the Act to be proposed within 12 months of the end of a regulatory period.¹⁴²

¹⁴⁰ Commerce Act 1986, s 53Z.

¹⁴¹ *Electricity Distribution Services Default Price-Quality Path Determination 2015* [2015] NZCC 33, clause 7.

¹⁴² Commerce Act 1986, s 53Q(3).

Submissions on our draft decision

- 8.9 We received submissions from Powerco, Aurora Energy and the ENA regarding the dates for proposing a customised price-quality path.
- 8.9.1 Powerco supported the application windows proposed in our draft decision.¹⁴³
- 8.9.2 Aurora Energy was concerned that the proposed windows were too short, and that greater flexibility should be considered.¹⁴⁴
- 8.9.3 The ENA acknowledged that the Commission needs sufficient time to evaluate a customised price-quality path proposal and make a determination, but also submitted that the February application window was “unrealistic”.¹⁴⁵
- 8.10 Having specific times of the year when customised price-quality path proposals can be submitted are important, even in years where we do not receive more than four applications. Statutory timeframes apply for the consideration of customised price-quality path proposals. Set application windows therefore provide certainty for distributors and consumers in terms of when customised price-quality paths may take effect.
- 8.11 A longer February application window (eg, two weeks or one month) could affect our ability to prioritise applications, complete the customised price-quality path determinations within the statutory timeframes, and have them ready to come into effect at the beginning of the next disclosure year.

¹⁴³ Powerco “Submission on Proposed Compliance Requirements for the 2015-2020 Default Price-Quality Paths for Electricity Distributors” (29 August 2014), paragraphs 66-67.

¹⁴⁴ Aurora Energy Limited “Submission: Proposed Compliance Requirements for the 2015-2020 Default Price-Quality Paths for Electricity Distributors” (15 August 2014), p.1 and p.11.

¹⁴⁵ ENA “Submission on proposed compliance requirements for the 2015-2020 Default Price-Quality Paths for electricity distributors” (29 August 2014), paragraph 157.

- 8.12 A longer May application window could be considered given that customised price-quality path proposals submitted in this window may not be evaluated in time to come into effect at the beginning of the next disclosure year anyway. However, we think it is more appropriate to signal our indifference as to which application window we receive customised price-quality path proposals. Given the absence of specific recommendations from submitters, we have not been persuaded that increasing the number or length of application windows in a year is appropriate or necessary.¹⁴⁶
- 8.13 We consider that the ENA's submission that the proposed February application window was "unrealistic" may reflect ENA's views on the customised price-quality path proposal process set out in the input methodologies and not reflect the proposed window itself.¹⁴⁷ The ENA's concerns may therefore be addressed more effectively when amendments to the input methodologies applying to customised price-quality paths are considered.¹⁴⁸

May application window

- 8.14 In our draft decision, we stated that the May application window would only be available in the event that the Commission did not receive four or more applications in the February window.¹⁴⁹ However, consistent with the Electricity Distribution Services Default Price-Quality Path Determination Amendment No.3 published in 2012, we consider that the May window should be available regardless of how many proposals are received in the February window.¹⁵⁰

¹⁴⁶ Aurora Energy Limited "Submission: Proposed Compliance Requirements for the 2015-2020 Default Price-Quality Paths for Electricity Distributors" (15 August 2014), p.1 and p.11; and ENA "Submission on proposed compliance requirements for the 2015-2020 Default Price-Quality Paths for electricity distributors" (29 August 2014), paragraph 157.

¹⁴⁷ ENA "Submission on proposed compliance requirements for the 2015-2020 Default Price-Quality Paths for electricity distributors" (29 August 2014), paragraphs 156-157.

¹⁴⁸ For example, the date when the cost of capital for customised price-quality paths is determined and/or the consumer consultation processes that are required.

¹⁴⁹ Commerce Commission "Proposed Compliance Requirements for the 2015-2020 Default Price-Quality Paths for Electricity Distributors" (18 July 2014), Chapter 8.

¹⁵⁰ Commerce Commission "Electricity Distribution Services Default Price-Quality Path Determination Amendment No.3 Reasons Paper" (22 March 2012), paragraphs 23-24.

- 8.15 Should we receive four or more complete proposals in the February window, we can still assess the completeness of the proposals that we receive in the May window. However, the evaluation of a proposal submitted in the May window may be deferred to a subsequent year. Prioritisation of these May proposals would be determined in accordance with the Act.¹⁵¹

¹⁵¹ Commerce Act 1986, s 53Z (3).

9. Approvals

Purpose of chapter

- 9.1 This chapter outlines the approvals process for certain recoverable costs and treatments which require the Commission's approval before they may be included in an annual compliance statement.

Outline of this chapter

- 9.2 This chapter covers the:
- 9.2.1 approvals which must be obtained before a distributor may include certain recoverable costs in a compliance statement; and
 - 9.2.2 approvals of an alternative methodology for calculating the price path or quality standard impact of transactions.

Approvals required by the Commission

- 9.3 Some new recoverable costs introduced by the amendments to the input methodologies require Commission approval.¹⁵²
- 9.4 The Commission has limited the requirement for ex ante approval of costs to those that are not independently verifiable, and which therefore require the Commission to exercise judgement in how the amounts may be derived and valued.
- 9.5 The Commission is required to approve the following recoverable costs before these may be included in the pass-through balance calculation:
- 9.5.1 energy efficiency and demand side management recoverable costs; and
 - 9.5.2 extended reserves allowance.

Approval of energy efficiency and demand side management incentive allowance

- 9.6 The rules governing our approval of foregone revenue associated with energy efficiency and demand side management initiatives are set out in Schedule 5A of the determination. This recoverable cost is discussed further in chapter 7 of this paper and in chapter 7 of the main policy paper.¹⁵³

¹⁵² Electricity Distribution Input methodology Amendments Determination 2014 [2014] NZCC 31.

¹⁵³ Commerce Commission "Default price-quality paths for electricity distributors from 1 April 2015 to 31 March 2020: Main policy paper" (28 November 2014).

- 9.7 The application for approval, the requirements of which are set out in Schedule 5A clause 2, must include a detailed description of the initiative, programme or activity and information sufficient to allow the Commission to establish the reasonableness of estimates relating to foregone quantities and revenue.
- 9.8 The Commission may request additional information to support or assess the information initially provided including requiring either director or audit certification. Such requests will take into account the likely cost of providing this information.
- 9.9 An application for approval of energy efficiency or demand side management incentive allowance is to be submitted no later than 70 working days following the end of an assessment period.
- 9.10 A number of submissions were received requesting the determination be amended to contain the process which the Commission will undertake to approve these costs and to specify when these costs must be approved by.¹⁵⁴ Timelines have not been specified in Schedule 5A as the Commission does not want to place an arbitrary restriction on the time taken to provide approval.
- 9.11 The Commission intends to provide approvals in a timely manner consistent with the timescale suggested by the ENA. However including deadlines in the determination may restrict our ability to approve applications, in instances when more information is required, but not available immediately.
- 9.12 This flexibility on the timing is likely to benefit distributors who may otherwise have their application rejected if firm deadlines could not be met. Any delay in approvals can be recovered in the following assessment period by a cost of debt adjustment.

Pre-approval of initiatives

- 9.13 We are open to working with distributors in providing a non-binding ex ante view, particularly for initial applications under the scheme. We understand that an ex ante view would be useful to distributors to provide indication of the outcomes of the approvals process.
- 9.14 We consider that this approach is consistent with a submission from Vector that the process should provide an “ex ante view, at least at an in-principle level, on the foregone revenue calculation methodology.”¹⁵⁵

¹⁵⁴ Vector "Submission on the draft Default Price-Quality Path determination 2015" (31 October 2014), paragraph 30 – 32; and Electricity Networks Association "Submission on the technical drafting of the Draft DPP Determination and IM amendments" (31 October 2014), paragraph 52 – 62.

¹⁵⁵ Vector "Submission on Proposed Electricity DPP Compliance Requirements" (29 August 2014), paragraph 31.

Repeated activities

- 9.15 We also consider that a streamlined process should take place for initiatives that have previously been approved, although we note that an estimate of the volume impact is still required on an ex-post basis for each year for which an initiative applies. However on a practical level we would expect previously approved initiatives would be subject to a less onerous approval process for subsequent assessment periods.

Consultation on the level of the incentive allowance

- 9.16 We expect to consult with interested parties if we believe the materiality of the compensation warrants further scrutiny from interested parties during the approvals process.
- 9.17 A submission by the Major Electricity Users' Group (MEUG) suggested that there should be a consultation process with interested parties in advance of any approval for any compensation under the energy efficiency and demand side management compensation scheme. MEUG suggests that this consultation should either take place by the distributor prior to the application being made or by the Commission on receipt of the application.¹⁵⁶
- 9.18 We think this request would significantly increase compliance costs which we are trying to minimise. A requirement to consult before approving any compensation does not appear workable or beneficial when compared against the potentially low value of some submissions.

Approval process for extended reserves allowance

- 9.19 The rules governing our approval of an extended reserves allowance are set out in Schedule 5H of the determination. This recoverable cost is discussed further in chapter 11 of the amendments to input methodologies paper.¹⁵⁷
- 9.20 The application for approval, must include details of all compensation payments made or received by the distributor under the regime and any other explanatory material or supporting information to allow the Commission to assess the reasonableness of the application.
- 9.21 The Commission may request additional information to support or assess the information initially provided including requiring either director or audit certification. Such requests will take into account the likely cost of providing this information.

¹⁵⁶ Major Electricity Users' Group "Proposed DPP for EDB from 1 April 2015" (15 August 2014), paragraph 15.

¹⁵⁷ Input methodology amendments affecting the default price-quality paths for electricity distributors" (27 November 2014).

- 9.22 An application for approval of an extended reserves allowance must be submitted no later than 70 working days following the end of an assessment period but does not constitute part of the annual compliance statement.
- 9.23 The Commission acknowledges submitter requests for a documented process and timelines for approval of the extended reserves allowance.¹⁵⁸
- 9.24 However due to work currently being undertaken in the area of extended reserves by the Electricity Authority and uncertainty around what the end result of that will be the Commission has not specified a process or a timeline for approval.
- 9.25 We have not included specific deadlines in the determination as this may restrict us in our ability to approve applications, in instances when more information is required, but not available immediately.
- 9.26 When the Electricity Authority has completed its work in the area it is possible the Commission will be able to provide further guidance on the approval process.

Approval of an alternative methodology following a major transaction

- 9.27 Within the determination a distributor may propose an alternative approach to determining the effect of a major transaction on the price path or quality standards than that specified in the determination.¹⁵⁹
- 9.28 The use of an alternative methodology must be approved by the Commission before it can be represented within an annual compliance statement.
- 9.29 The ability to propose an alternative approach covers a wide breadth of potential transactions including a merger between a Non-exempt EDB and an Exempt EDB through to only a small number of ICP's being transferred between a Non-exempt EDB and an Exempt EDB. It also covers a variety of potential approaches a distributor could propose as an alternative approach.
- 9.30 Accordingly we have not detailed what an application to use an alternative methodology must contain. We suggest distributors engage with the Commission early in the process if they believe they may wish to apply for this requirement.

¹⁵⁸ Vector "Submission on the draft Default Price-Quality Path determination 2015" (31 October 2014), paragraph 30 – 32, Electricity Networks Association "Submission on the technical drafting of the Draft DPP Determination and IM amendments" (31 October 2014), paragraph 58 – 62.

¹⁵⁹ See Schedule 3C clause 9 and Schedule 4B clause 13 within the determination.

- 9.31 When proposing an alternative methodology consideration should be given to the purpose of the major transaction requirements as discussed within chapter 4 of this paper.