ISSN: 1178-2560
Project no. 14.11/15108

Public version

Transpower Input Methodologies Amendment Determination 2017

[2017] NZCC [17]

Amendments made under s 52X of the Commerce Act 1986 to input methodologies applicable to Transpower contained in Decision [2012] NZCC 17.

The Commission:

S Begg

Dr S Gale

E Welson

G Crombie

Date of determination: 29 June 2017

Transpower Input Methodologies Amendment Determination 2017

Pursuant to Part 4 of the Commerce Act 1986 (the Act) the Commerce Commission makes the following determination:

1. TITLE

This determination is the Transpower Input Methodologies Amendment Determination 2017.

2. DETERMINATION AMENDED

This determination amends the *Transpower Input Methodologies Determination* [2012] NZCC 17 (the Transpower IM Determination).

3. COMMENCEMENT

3.1 This determination comes into force on the date on which notice of this determination is given in the *New Zealand Gazette*.

4. AMENDMENTS TO TRANSPOWER IM DETERMINATION

4.1 Clause 3.6.4 (3) of the Transpower IM Determination is amended by replacing it with:

The 'baseline adjustment term' is calculated in accordance with the formula–

differences in penultimate year

×

$((1-(1+WACC)^{-6})/WACC)$

×

$(1+WACC)^{2}$

where–

differences in penultimate year means the amount calculated in accordance with subclause (4)

WACC means the **WACC** as determined by the **Commission** and applicable to **Transpower**'s current **regulatory period**.

4.2 Clause 3.6.4 (4) of the Transpower IM Determination is amended by replacing it with:

'Differences in penultimate year' is an amount determined by the Commission, having regard to the views of interested persons, that is the difference between forecast opex and actual opex in the penultimate year of the preceding regulatory

period, minus any amount resulting from savings that occurred in the preceding years of the regulatory period. For the purpose of this definition, savings can be both negative and positive. The amount so determined is to be notified to Transpower.

_____

Sue Begg, *Deputy Chair*
Dated at Wellington this 28th June 2017.
COMMERCE COMMISSION

EXPLANATORY NOTE

The *Transpower Input Methodologies Determination* [2012] NZCC 17 (Transpower IM Determination) assumes that any permanent savings made up to, and including, Year 4 are incorporated in Transpower's IPP forecast. However, Transpower has informed us that its initial IPP forecasts are developed in Year 3 of the previous regulatory period. Therefore, unless a specific adjustment is made, the final IPP forecast opex forecast is unlikely to incorporate Year 4 savings.

The implications of this are that if Year 4 permanent savings are not included in Transpower's final IPP forecast, then a problem arises because the IRIS mechanism will over-reward savings (and over-penalise overspends) in Year 4 of the previous IPP period.

In the absence of an adjustment, the reward for permanent savings would be almost twice the intended amount. Transpower would be rewarded through both the unadjusted IPP forecast, and again through a recoverable cost under the IRIS (the opex incentive). This situation results in a retention factor of 64% for permanent savings made in Year 4, almost double the intended 34% retention factor.[1]

To rectify this we can either identify and remove Year 4 permanent savings from the IPP forecast allowance proposed by Transpower, or adjust the definition of the baseline adjustment term in the Transpower IRIS IM. Given the potential difficulties in removing Year 4 permanent savings from Transpower's IPP forecast, our solution is to amend the Transpower IRIS IM. This option applies a more mechanistic approach, without adding significant complexity to the existing IRIS mechanism.

[1] Under the current IPP2 WACC value.