

General comments on the default price-quality path compliance statements submitted by electricity distribution businesses for the 2016 assessment period

May 2017

Introduction

1. Non-exempt electricity distribution businesses (EDBs) are required to submit annual default price-quality path (DPP) compliance statements. The compliance statements submitted for the 2016 assessment period have been produced under the Electricity Distribution Services Default Price-Quality Determination 2015 (Determination).^{1,2}
2. In their compliance statements, EDBs are required to assess their own compliance against the Determination and state whether or not they are compliant with the price path and quality standards set by the Determination.

Purpose

3. This document sets out findings from our review of the compliance statements submitted by EDBs for the 2016 assessment period, it provides guidance on two specific topics and makes suggestions of areas for improvement in future compliance statements. We are issuing these comments to provide feedback to EDBs on the compliance statements that have been submitted, and to clarify our expectations in a few of the areas given the changes resulting from the Determination.
4. This paper covers the following items:
 - 4.1 guidance on the operation of the Pass-through balance mechanism;
 - 4.2 normalisation of SAIDI and SAIFI Unplanned Boundary Values; and
 - 4.3 areas for improvements in future compliance statements:
 - 4.3.1 clause 11.4(d) – portion of price attributed to Distribution Price and Pass-through Price;
 - 4.3.2 clause 11.4(e) – methodology used to calculate Distribution Price and Pass-through Price;
 - 4.3.3 clause 11.4(h) – amount of charge relating to new investment contract; and

¹ Electricity Distribution Services Default Price-Quality Path Determination 2015, effective 1 April 2015 to 31 March 2020.

² The exception is Orion who follows a customised price-quality path, Orion New Zealand Limited Customised Price-Quality Path Determination 2013, effective 1 April 2014 to 31 March 2019.

4.3.4 clause 11.1(b) – price-quantity schedules in electronic format.

4.4 some general comments on compliance statements.

Guidance on the operation of the Pass-through balance mechanism

5. Through our review of the 2016 compliance statements it has come to our attention that some EDBs may be unsure how to apply the Pass-through balance mechanism correctly. We therefore consider it appropriate to provide guidance to allow for compliant treatment in future assessment periods.
6. As compliance with the price path is now demonstrated using two components, the Distribution Price and the Pass-through balance, EDBs should ensure that the apportionment of price to Distribution Price and Pass-through Price is accurate – ie, amounts not related to Pass-through costs or Recoverable costs should not be included in the Pass-through Price and vice versa. This was highlighted in the Compliance requirements paper at paragraph 3.12³

The amount of each price apportioned as a pass-through price will affect the allocation of distribution prices which in turn impacts the assessment of compliance under the weighted average distribution price cap.

7. In terms of clause 8.6(b) of the Determination EDBs are required to include a demonstrably reasonable forecast of Pass-through costs and Recoverable costs in the Pass-through Price. For the avoidance of doubt, the amount included as a demonstrably reasonable forecast may not be an amount less than the reasonable forecast. If an EDB wishes to limit price increases to consumers, this short-fall should come from the Distribution Price, not the Pass-through Price. The Pass-through Price should always include the full demonstrably reasonable forecast of Pass-through costs and Recoverable costs.
8. Where an EDB decides to limit its Pass-through Price, it effectively distorts the operation of the weighted average price cap on the distribution portion of prices. This reduction in price should have been applied to the Distribution Price, which would not be able to be carried forward into future periods. It was noted at paragraph 3.36 of the Compliance requirements paper that the revenue differential term does not allow for an under-recovery of notional revenue (using the Distribution Price) in a year to be recovered in future periods

“The revenue differential term does not allow a previous under-recovery of notional revenue to be recovered in future assessment periods.”

³ Default price-quality paths for electricity distributors from 1 April 2015 to 31 March 2020, Compliance requirements, 28 November 2014. This document can be found at <http://comcom.govt.nz/dmsdocument/12770>

9. For this reason, EDBs should ensure that the apportionment of price between Distribution Price and Pass-through Price is accurate, and that the Pass-through Price includes the full demonstrably reasonable estimate of Pass-through costs and Recoverable costs. We note that Pass-through Prices for the assessment period ending 31 March 2018 may include a component of the 31 March 2016 Pass-through balance (the under- or over-recovered Pass-through and Recoverable costs for the 2016 assessment period).
10. The Compliance requirements paper, at paragraph 3.23, indicated that the recovery of Pass-through and Recoverable costs would be an area of compliance focus. Given the incorrect interpretation and application by the two EDBs as discussed above this is likely to continue to be an area of particular focus for our compliance testing over the coming assessment periods.
11. We are aware of two EDBs who did not apply the full amount of their reasonable forecast of Pass-through and Recoverable costs when determining their Pass-through Prices. These EDBs were able to charge a higher Distribution Price relative to EDBs who priced in their full reasonable forecast of Pass-through and Recoverable costs. These EDBs have therefore been able to carry forward a Pass-through balance which they would be able to include in Pass-through Prices in future.⁴

Normalisation of SAIDI and SAIFI Unplanned Boundary Values

12. Review of the 2016 compliance statements received from EDBs has indicated that EDBs may be determining when to apply the SAIDI Unplanned Boundary Value or SAIFI Unplanned Boundary value incorrectly. This is of concern because it is not in line with the definitions contained within the Determination. In accordance with the Determination, SAIDI values that span multiple calendar days accrue to the day on which the Interruption began, and SAIFI values are to be recorded against the day when the Interruption first arose.
13. Interruptions which occur on subsequent days but an EDB considers relate to the same event (ie, a major storm) should not all be grouped and accrued to the first day on which interruptions initially began.
14. We recognise that some major events can continue for several days and some major events may require increased levels of interruptions or system resource to rectify damage despite the major event having concluded. We consider that this application of grouping similar or related interruptions is inconsistent with both the definitions contained within the Determination and the approach undertaken in determining the SAIDI and SAIFI limits, which took the raw Interruption data as provided by EDBs

⁴ We are engaged in a compliance process with these EDBs to resolve this matter.

under responses to a s53ZD notice at the time the Commission set the 2015 Determination⁵.

15. Where an EDB is unsure of the correct interpretation to take, we would recommend that a careful review of the requirements of the Determination be undertaken. If the EDB is unable to resolve the matter, please contact us.

Areas for improvements in future compliance statements

16. We have identified a few items that EDBs should consider in the preparation of future compliance statements. While we do not consider that these items warrant enforcement action at this time, we may reconsider this position if the same issues continue to occur in the future. Therefore please consider the following:
 - 16.1 clause 11.4(d) of the Determination requires EDBs to display clearly each Price as well as the portion of the price that can be attributed as Distribution Price and the portion that is the Pass-through Price. Some EDBs had the Distribution Price in one table and the Pass-through Price in another table. Other EDBs provided one table which contained the Price, Distribution Price and Pass-through Price. This single table approach is considered more user-friendly and we believe other EDBs should consider following a similar approach;
 - 16.2 clause 11.4(e) of the Determination requires EDBs to explain the methodology used to calculate the Distribution and Pass-through Prices. Some EDBs did not provide an explanation of the methodology in their compliance statements but rather simply referred to their Pricing Methodology document. Where an EDB would have provided a reference to its Pricing Methodology we would expect that the relevant section from the Pricing Methodology is either included in the compliance statement body, or included as an attachment to the compliance statement. In such situations EDBs should ensure that the explanation written for the Pricing Methodology is adequate for the purposes of the compliance statement as the Pricing Methodology document is written for a separate purpose; and
 - 16.3 clause 11.4(h) of the Determination requires EDBs to state the amount of charge relating to any new investment contract entered into in the assessment period. Some EDBs have not clearly commented on whether there were any new investment contracts entered into during the 2016 assessment period. In addition, some 2015 compliance statements did not include disaggregated Recoverable cost information and it is hard to gauge if the new investment contract amount used in the Recoverable costs for the

⁵ We are currently engaged with an EDB where we have identified this approach has been applied.

2016 assessment period is in fact for a new charge or a carryover from prior year's contracts.

17. Clause 11.1(b) of the Determination requires EDBs to provide Excel copies of the price-quantity schedules to the Commission within five working days of providing their compliance statement. EDBs are reminded of this requirement because for the 2016 assessment period there were some EDBs who did not provide these Excel copies and we had to follow up with requests for them.

General Comments

Compliance statements submitted are of a generally high standard

18. The quality of DPP compliance statements submitted by EDBs has improved over the last few years. The 2016 compliance statements were generally of a high standard across all EDBs. We appreciate the significant time and effort that goes into the preparation of compliance statements.
19. Some EDBs provided a helpful checklist alongside their compliance statements to indicate that each clause of the Determination has been met and the corresponding page numbers/sections.

Use of templates and precedents

20. Where EDBs are using templates or precedents to prepare their compliance statements, they should ensure that the template and content is appropriately updated for the relevant year.
21. This is also relevant to those EDBs that prepare reporting on behalf of multiple entities and may use the same template for the preparation of the compliance statements and director's certificates.⁶

In the event of non-compliance

22. Where an EDB reports or anticipates non-compliance with the price or quality requirements, the Determination requires the EDB to provide relevant information as required by clause 11.4 for price path non-compliance, and clause 11.5 for quality standard non-compliance.

In the event of an error

23. Where an EDB, in the process of preparing its compliance statement, discovers an error made in a previous compliance statement, we expect the EDB to:
 - 23.1 bring the error to our attention;

⁶ We noted an instance where the directors of an EDB signed off a director's certificate which contained conflicting EDB names.

- 23.2 provide a thorough explanation for how the error occurred; and
 - 23.3 provide a thorough explanation of the steps taken to prevent such an error from occurring in future.
24. The Compliance requirements paper also includes guidance for EDBs on our expectations for instances when an error in a previous compliance statement is discovered.⁷

Concluding remarks

25. We acknowledge that EDBs put in substantial time and effort in completing their 2016 compliance statements. The compliance statements were generally of a high standard and we hope that this feedback will help to further clarify our expectations in relation to compliance statements for future assessment periods.

⁷ Also see paragraph 2.18 of the Compliance requirements paper.