9 August 2023

Ben Woodham
Manager, Electricity Distribution
Commerce Commission
PO Box 2351
Wellington 6140
By email to infrastructure.regulation@comcom.govt.nz

Dear Ben

Electricity Networks Aotearoa (ENA) appreciates the opportunity to provide this cross-submission on the Commerce Commission's (Commission's) Input Methodologies (IMs) review draft decision.

ENA is the industry membership body that represents the 27 electricity distribution businesses (EDBs), that deliver electricity to homes and businesses across Aotearoa. ENA harnesses the collective expertise of members to promote safe, reliable and affordable power for our members' customers.

Flexibility

ENA supports Transpower's proposed use-it-or-lose-it resilience mechanism

Transpower in its submission proposed a use-it-or-lose-it mechanism to access funds for selected resilience projects. ENA supports the adoption of this mechanism and believes a similar mechanism should be established for EDBs.

The Major Electricity Users' Group's (MUEG's) concerns over the Commission's decision not to set timeframes for Default Price-quality Path (DPP) reopeners are shared by ENA. MEUG's comments are clear evidence that this simple change would be of benefit to both regulated businesses and their customers. Documenting greater clarity and consistency in DPP reopener processes and timelines within the IMs would therefore deliver greater regulatory certainty to all involved. ENA recommends the Commission act on the view of stakeholders and reverse its decision and establish clear timeframes for the consideration of reopeners.

ENA also shares MEUG's questions as to why the Commission has chosen to set different catastrophic event limits for Vector and Powerco. ENA believes a single threshold should apply to all EDBs.

ENA notes that the BusinessNZ Energy Council agrees with our position that a more flexible regime than set out in the draft decision is needed. Their statement that the Commission's proposed status quo approach "would likely result in a slower and impeded transition, making it more challenging for the country to meet its international commitments to achieve net-zero emissions within the designated timeframe" should act as a call to arms for the inclusion of greater flexibility mechanisms into the IMs.

Financeability

The independent analysis by Frontier Economics for Vector supports and reinforces ENA's call for the Commission to include financeability provisions in the IMs. The inclusion of these provisions would ensure Commission-determined revenue allowances provide all regulated businesses sufficient cashflows to achieve the credit ratings assumed in the WACC IMs.

WACC

Universal support for the use of a trailing average cost of debt

Submissions reveal universal, cross-industry support for the use of a trailing average cost of debt. Not a single submitter raised concerns about the use of the trailing average.

ENA agrees with Transpower's view that the trailing average "reflects more appropriately prudent debt management; and acts as a preventative measure against price volatility between regulatory periods."[1]

Chorus succinctly summarised how the trailing average approach delivers on the objectives of Part 4. Noting it "provides a stable and commercially realistic weighted average cost of capital (WACC), and appropriately reflects the practicalities of debt portfolio hedging in New Zealand markets."[2]

Contact Energy, in its submission, raised concerns about the price volatility between regulatory periods that is likely to occur as a result of movements in WACC. ENA suggests the simplest and most effective way to remove this volatility is to adopt the trailing average cost of debt.

ENA calls on the Commission to take heed of the collected advice of stakeholders, independent finance experts, and its own advisors and adopt the trailing average because it has been demonstrated to advance the Part 4 objectives set down in section 52A of the Act.

Percentile

ENA agrees with Transpower's view that the Commission has not presented compelling evidence to support a departure from the 67th percentile WACC estimates for price-quality path regulation. As Firstgas points out the Commission has stated "when considering proposed IM changes, we must therefore be mindful of the importance of predictability, which plays a role in providing suppliers with incentives to invest in accordance with section 52A(1)(a)"[3]. Arbitrarily changing the WACC percentile based on what is essentially the same evidence as 2016 fails to uphold this principle.

ENA supports the BusinessNZ Energy Council's view that some of the Commission's proposed changes "are retrograde steps, such as reductions to the weighted average cost of capital (WACC) percentiles for EDBs, which seem questionable given the need for investment in decarbonisation and the transition away from being less dependent on thermal generation[4]".

ENA disagrees with MEUG's submission on the WACC. The Commission has not demonstrated sufficient justification to reduce the WACC to the 65th percentile. MUEG provides no further evidence or justification for the change and once again relies on the selective use of the decision

1 Transpower, Submission on IM Review 2023 Draft Decisions, p34
2 Chorus, Submission on Part 4 input methodologies review – draft decisions, p2
3 Firstgas, Submission Part 4 Input Methodologies Review 2023, p2
4 BusinessNZ Energy Council, letter to the commerce commission on the input methodologies (IM) review regarding electricity distribution businesses, p1

made by regulators in jurisdictions with materially different regulatory regimes – decisions which have been stripped of their vital regulatory context.

Debt wash-up

ENA in its submission noted that the Commission's proposed debt wash-up mechanism is novel and untested. ENA engaged PricewaterhouseCoopers to review the mechanisms for unintended consequences on Financial Capital Maintenance (FCM) and price volatility.

ENA's view is that the proposed mechanism supports the achievement of FCM. However, in situations where actual inflation is significantly above forecast the wash-up mechanism would result in net cash flow volatility. ENA agrees with the view of CEG and Frontier that alternative mechanisms can achieve the outcomes intended by the wash-up without introducing the potential net cash flow volatility during periods when actual inflation is significantly above forecast inflation.

Revenue smoothing

ENA strongly opposes Contact Energy's suggestion that the 'revenue smoothing limit' be applied to all costs, including pass-through costs.

The purpose of the IM pass-through provisions is to ensure that EDBs are not forced to bear costs over which they have no control. EDBs have no influence over the volatility of transmission charges, and the inclusion would adversely affect the ability of EDBs to fund investments in their networks. A core function of retailers is to manage the volatility of input costs with wholesale prices varying every 30 minutes. This demonstrates that retailers are best placed to deal with risk of transmission cost volatility. Contact Energy's proposal would therefore be detrimental to the achievement of the section 52A purpose.

Yours sincerely

[redacted]

Keith Hutchinson

Regulatory Manager