

Draft Electricity Distribution Input Methodology Amendments Determination 2014

Draft input methodologies made under s52X and s 52V(2) of the Commerce Act 1986 to input methodologies applicable to electricity distribution businesses contained in Decision [2012] NZCC 26.

Date of draft determination: 20 October 2014

THIS DRAFT DETERMINATION IS FOR CONSULTATION PURPOSES ONLY

Regulation Branch, Commerce Commission

Wellington, NEW ZEALAND

20 October 2014

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Electricity Distribution Input Methodology Amendments 2014

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

1. DETERMINATION AMENDED

This determination amends the *Electricity Distribution Services Input Methodologies Determination 2012* [2012] NZCC 26 (the **EDB IM Determination**).

2. COMMENCEMENT

This determination comes into force on the date on which notice of the determination is given in the New Zealand Gazette under section 52X of the Commerce Act 1986.

3. INTERPRETATION

3.1 Terms in bold type have the meaning given to those terms in the applicable Determination. Terms in bold type used in this determination that are defined in the Act, but not this determination, have the same meaning as in the Act.

3.2 Nothing in this determination limits the **Commission's** authority to amend any Determination in accordance with the Act.

4. EDB IM AMENDMENTS

4.1 In the **EDB IM Determination** amend clause 1.1.4(2) as follows:

- (a) replace the reference to "clause 4.3.3(6)" in the definition of 'amortisation of revaluations' with "clause 4.3.3(5)";
- (b) delete paragraph (b) of the definition of 'initial differences in asset values' and renumber paragraph (c) accordingly;
- (c) amend the definition of 'base year' as follows:

"base year means the disclosure year selected by the Commission, as specified in a DPP determination"

- (d) insert the following new definitions in alphabetical order:

"2013-15 NPV wash-up allowance means the amount specified in the **DPP determination** for the **regulatory period** commencing 1 April 2015 for Alpine Energy Limited, Centralines Limited, and Top Energy Limited reflecting the impact of the capped alternative rate of change for those suppliers in the *Electricity Distribution Services Default Price-Quality Path Determination 2012* [2012] NZCC 35;

“**capex wash-up amount** means the amount that is the present value of the difference in building block revenues for a **DPP regulatory period** resulting from adopting actual values of **commissioned** assets for a prior **regulatory period** instead of the forecast **commissioned** assets applied by the **Commission** when setting prices, and is calculated in accordance with clause 3.1.3(8);

“**catastrophic event allowance** means the amount determined by the **Commission** for–

- “(a) additional net costs (over and above those provided for in a **DPP determination** or **CPP determination**) prudently incurred by an **EDB** in responding to a **catastrophic event**, other than costs that are foregone revenue;
- “(b) **recoverable costs** and **pass-through costs** the **EDB** was permitted to recover under the applicable **DPP determination** or **CPP determination** through **prices**, but did not recover due to a **catastrophic event**; and
- “(c) the impact of a **catastrophic event** on any **quality incentive adjustment**,

“incurred in or relating to the period between a **catastrophic event** and the effective date of an amendment to the **DPP** or **CPP** following reconsideration of the **price-quality path** under clause [reference to be confirmed]¹ or clause 5.6.4(2)(a);

“**distributed generation allowance** means any positive allowance for costs incurred and amounts payable, or negative allowance for amounts receivable, in relation to avoided transmission charges arising from distributed generation, including embedded or notionally embedded generation, made in accordance with–

- “(a) Schedule 6.4 of Part 6 of the Electricity Industry Participation Code; or
- “(b) the Electricity Industry Act 2010;

“**distribution prices** means **prices**, other than **pass-through prices**;

“**energy efficiency and demand incentive allowance** means an allowance for foregone revenue attributable to ~~an~~ energy efficiency ~~and or~~ demand side management initiatives, projects, or activities ~~ies~~ as ~~specified~~ approved by the **Commission** in accordance with a **DPP determination** or **CPP determination**;

“**extended reserves allowance** means an amount determined by the **Commission** as a positive allowance for costs incurred and amounts payable, or a negative allowance

¹ This catastrophic event re-opener clause will be inserted when the High Court issues its orders on the appeals on the input methodologies. We expect this to be prior to our final decision due in November 2014. Clauses 4.5.1 to 4.5.3 currently cover the reconsideration of a default price-quality path.

for amounts receivable, in accordance with any extended reserves regulations made under the Electricity Industry Act 2010;

~~“incentive rate means the financial reward or penalty attributable to a non-exempt EDB’s performance against the quality standards specified in a DPP or CPP, as specified in a DPP determination or CPP determination;~~

“pass-through prices means prices attributable to pass-through costs and recoverable costs;

“quality incentive adjustment means an amount that provides incentives for a non-exempt EDB to maintain or improve its quality of supply in accordance with s 53M(2) of the Act, ~~and is a function of—~~

~~“(a) a non-exempt EDB’s performance above or below the quality targets, up to the caps or collars specified in relation to the quality targets;~~

~~“(b) revenue at risk; and~~

~~“(c) incentive rate;~~

“calculated in accordance with the method specified in a DPP determination or CPP determination;

“reconsideration event allowance means the positive or negative amount determined by the Commission—

“(a) for additional net costs (over and above those provided for in a DPP or CPP) prudently incurred by an EDB as a result of a change event in the period between the change event and the effective date of an amendment to the DPP determination or CPP determination under clause [to be confirmed] or clause 5.6.4(2)(c);

“(b) to mitigate the effect of an error or provision of false or misleading information on the relevant DPP determination or CPP determination under clauses [to be confirmed], [to be confirmed], 5.6.4(2)(b) or 5.6.4(4); and

“(c) for the impact of a change event, error, or provision of false or misleading information under clause [to be confirmed] or 5.6.4(4), on any quality incentive adjustment;

~~“revenue at risk means the maximum financial reward or penalty attributable to a non-exempt EDB’s performance against the quality standards as specified in a DPP determination or CPP Determination;~~

“transmission asset wash-up adjustment means an amount equal to the present value of revenues allowed in a DPP or CPP for additional capital expenditure and additional operating expenditure associated with a transmission asset forecast to be

purchased in **disclosure years** preceding the **regulatory period** but were not completed, as specified in a **DPP determination** or **CPP determination**.”.

4.2 In the **EDB IM Determination** amend clause 2.3.4(2) as follows:

“(2) For the purpose of subclause (1), 'notional deductible interest' means the amount determined in accordance with the formula—

$$((\text{regulatory investment value} \times \text{leverage} \times \text{cost of debt}) + \text{term credit spread differential allowance})$$

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$$\sqrt{1 + \text{cost of debt}}.$$
”.

4.3 In the **EDB IM Determination** amend clause 3.1.1(2) as follows:

“(2) Allowable notional revenue means, in respect of a 12 month period, a function of—

“(a) relevant **CPIs**;

“(b) the X factor applicable to the **EDB**; and

“(c) **distribution prices** in the preceding 12 month period multiplied by quantities.”.

4.4 In the **EDB IM Determination** amend clause 3.1.1(3) as follows:

“(3) Notional revenue means, in respect of a 12 month period, **distribution prices** in that period multiplied by quantities.”.

4.5 In the **EDB IM Determination** amend clause 3.1.3(1) as follows:

“(1) A recoverable cost is a cost that is—

“(a) any positive net balance determined in accordance with clause 3.3.2(2), provided that any requirements pursuant to an **ID determination** regarding **auditor** certification of any value determined in accordance with Subpart 3 have been met;

“(b) a charge payable to **Transpower** for **electricity lines services** provided to a **non-exempt EDB** in respect of the transmission system in accordance with the transmission pricing methodology **Transpower** uses to determine the prices it charges for its services, as specified in the Electricity Industry Participation Code, including any such charges on-charged at cost by an **EDB** to a **non-exempt EDB** that does not have a transmission agreement with **Transpower**;

- “(c) a charge payable by an **EDB to Transpower** in respect of a new investment contract (as 'new investment contract' is defined in the Electricity Industry Participation Code) between those parties, or an equivalent type of contract;
- “(d) a charge payable by an **EDB** for the **supply** of system operator services, where 'system operator' has the same meaning as defined in s 5 of the Electricity Industry Act 2010, to the extent that the charge is not a **pass-through cost**;
- “(e) an amount of a charge described in paragraphs (b) or (c) that the **Commission** is satisfied an **EDB** has avoided liability to pay as a result of the **EDB** having purchased transmission assets from **Transpower**, subject to—
- “(i) the requirement specified in subclause (2); and
- “(ii) subclause (4);
- “(f) an amount equal to a **distributed generation allowance**;
- “(g) claw-back applied by the **Commission** under sections 54K(3) or 53ZB(3) of the **Act**;
- “(h) a standard application fee for a **CPP proposal** under 53Q(2)(c), subject to the proviso specified in subclause (5);
- “(i) a fee notified by the **Commission** as payable by the **EDB** in respect of the **Commission** assessing a **CPP proposal** and determining a **CPP** in accordance with s 53Y of the **Act**, subject to the proviso specified in subclause (5);
- “(j) a fee payable to a **verifier** subject to the requirement specified in subclause (3);
- “(k) any **auditor's** cost incurred for the purpose of meeting clauses 5.1.4 or 5.5.3, subject to the requirement specified in subclause (3);~~or~~
- “(l) a fee payable to an **engineer** for the purpose of meeting a requirement of clauses 5.4.5(c) or 5.4.12(4)(c), subject to the requirement specified in subclause (3);~~;~~
- “(m) an amount equal to an **energy efficiency and demand incentive allowance**;
- “(n) an amount equal to a **catastrophic event allowance**, as specified in a **DPP determination** or **CPP determination**;
- “(o) an amount equal to an **extended reserves allowance**, subject to the requirements specified in subclauses (2) and (7);

- “(p) an amount equal to a **quality incentive adjustment**;
- “(q) the amount calculated for a **non-exempt EDB** in accordance with the following formula for a **disclosure year** in a **DPP regulatory period** other than the first **disclosure year**–

$$\left(\frac{\text{capex wash-up amount}}{l - 1} \right) \times (1 + r)^{y+0.5}$$

where–

- l* is the number of **disclosure years** in the **DPP regulatory period**;
- r* is the **cost of debt** applying to the **DPP regulatory period**; and
- y* is the number of **disclosure years** preceding the **disclosure year** in question in the **DPP regulatory period**;
- “(r) an amount calculated for a **non-exempt EDB** if the acquisition of the transmission asset is not completed prior to the commencement of a **regulatory period** in accordance with the terms of any contract setting out the terms and condition of sale, in accordance with the following formula for a **disclosure year** in a **regulatory period** other than the first **disclosure year**–

$$\left(\frac{\text{transmission asset wash-up adjustment}}{l - 1} \right) \times (1 + r)^{y+0.5}$$

where–

- l* is the number of **disclosure years** in the **regulatory period**;
- r* is the **cost of debt** applying to the **regulatory period**; and
- y* is the number of **disclosure years** preceding the **disclosure year** in question in the **regulatory period**;
- “(s) an amount equal to the **2013-15 NPV wash-up allowance**; or”
- “(t) an amount equal to a **reconsideration event allowance**, as specified in a **DPP determination** or **CPP determination**.”.

4.6 In the **EDB IM Determination** amend clause 3.1.3(2) as follows:

The requirement of this subclause is that in respect of a particular **EDB**, the **Commission's** approval for the amount of cost must be obtained in accordance with any process relating to the type of cost in question specified in a **DPP determination** or **CPP determination**.

4.7 ~~In the **EDB IM Determination** add a new clause 3.1.3(7) as follows:~~

~~“(7) For the purpose of giving approval under subclause (2) in respect of an **extended reserves allowance**, the **Commission** will have regard to any policy intent stated by the Electricity Authority as to whether—~~

~~“(a) some or all compensation payments to be made by an **EDB** under the extended reserves regime would be expected to constitute negative **recoverable costs** and be passed through to **consumers** via corresponding reductions in **prices**; and~~

~~“(b) revenues that an **EDB** may receive under the extended reserves regime would be expected to be treated as unregulated income;”.~~

4.8 In the **EDB IM Determination** add new clauses 3.1.3(8) and 3.1.3(9) as follows:

“(8) For the purpose of clause 3.1.3(1)(q), the ‘capex wash-up amount’ is an amount equal to the present value of the difference in the series of building block revenues for the **DPP regulatory period** in question from adopting—

“(a) the sum of **value of commissioned assets** for each **disclosure year** that follows the **base year** in the preceding **DPP regulatory period**,

“instead of—

“(b) the **forecast aggregate value of commissioned assets** determined by the **Commission** in respect of each of those **disclosure years**,

“when determining prices in accordance with s 53P(3)(b).

“(9) For the purpose of subclause (8)—

“(a) the present value must be determined by discounting the building block revenues to the end of the preceding **DPP regulatory period** using a discount rate equal to the **WACC** applied by the **Commission** in setting prices for the **DPP regulatory period** in question;

“(b) the series of building block revenues for the **DPP regulatory period** are those used to reset starting prices based on the current and projected profitability of each **EDB** and must—

~~“(i) be calculated using the same methodology that was applied by the **Commission** in setting starting prices for the **EDB** for the **DPP**, including adopting the same **forecast operating expenditure values for all inputs to the calculation of building block revenues except for the value of commissioned assets**;~~

~~“(ii) for subparagraph (i), adopt the sum of **depreciation** calculated under Part 2 in respect of each **disclosure year** that follows the **base year** in the preceding **DPP regulatory period** for assets having a **commissioning date** in the preceding **DPP regulatory period**; and~~

~~“(iii) be expressed consistent with cash flow timing assumptions for calculating amounts in revenue date terms as applied in the relevant DPP;~~

“(c) where building block revenues from adopting the sum of **value of commissioned assets** exceed the building block revenues from using the **forecast aggregate value of commissioned assets** then the difference is a positive amount of capex wash-up; and

“(d) where building block revenues from adopting the sum of **value of commissioned assets** is less than the building block revenues from using the **forecast aggregate value of commissioned assets** then the difference is a negative amount of capex wash-up.”.

4.9 In the **EDB IM Determination** amend clause 4.3.1(4) by deleting “ – **term credit spread differential allowance**” where it appears.

4.10 In the **EDB IM Determination** amend clause 4.3.3(2) as follows:

“(2) For the purpose of subclause (1), 'notional deductible interest' means the amount determined in accordance with the formula–

$$((\textit{opening investment value} \times \textit{leverage} \times \textit{cost of debt}) + \textit{term credit spread differential allowance})$$

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$\sqrt{1 + \textit{cost of debt}}$.”.

4.11 In the **EDB IM Determination** replace clause 4.3.3(3) with the following:

“(3) For the purpose of subclause (1), 'amortisation of initial differences in asset values' is determined in accordance with Part 2 as of the **base year**”.

4.12 In the **EDB IM Determination** delete clause 4.3.3(5) and renumber clause 4.3.3(6) accordingly.

4.13 In the **EDB IM Determination** amend clause 5.3.16(2) as follows:

“(2) For the purpose of subclause (1), 'notional deductible interest' means the amount determined in accordance with the formula–

$$(((\textit{regulatory investment value} + \textit{RAB proportionate investment}) \times \textit{leverage} \times \textit{cost of debt}) + \textit{term credit spread differential allowance})$$

÷

$\sqrt{1 + \textit{cost of debt}}$.”.