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## **SUBMISSION ON THE DRAFT DPP DETERMINATION AND RELATED DOCUMENTS**

- 1 Orion New Zealand Limited (**Orion**) welcomes the opportunity to provide a submission on the Commerce Commission's (**Commission**) "Electricity Distribution Services Default Price-Quality Path Draft Determination 2015" (the determination) issued by the Commission in July 2014.
- 2 In the interests of efficiency, this submission also comments on related proposed changes, for example to the applicable IMs and the proposed DPP compliance framework.
- 3 The Electricity Networks Association has also submitted on these matters. Orion endorses the ENA submission.

### **General comments**

- 4 With respect to the determination we find the inclusion of the term "CPP Regulatory Period" confusing and unhelpful. We are not sure why this approach has been taken. For example:
  - 4.1 The definition of "CPP Regulatory Period" includes a reference to Schedule 1, but Schedule 1 is a table of starting prices under the DPP. Orion, which is on a CPP, is not mentioned?
  - 4.2 Clause 5.1 links CPP Regulatory Period compliance to clauses 8 and 9, but it is quite possible that neither will apply to an EDB during a CPP Regulatory Period, and certainly neither applies to Orion under our current CPP. Regarding schedule 3 which is referenced in clause 9, we acknowledge the signal as to

how the Commission may establish SAIDI and SAIFI targets for Orion for the 2019/2020 year, but we do not think it is necessary to do so at this stage, and nor is it appropriate to set these targets in the absence of the method by which prices will be set for that year.

- 4.3 Clause 5.3 would appear to be unnecessarily stating the obvious: that a CPP applies in a CPP regulatory period. We do not see this clause adds anything.
- 4.4 We think a preferable method here is to acknowledge that a CPP may vary a number of terms that apply under a DPP, but do the varying under the CPP determination and otherwise make no reference to the CPP within the DPP determination.

### **Comments on wording**

- 5 We suggest using the existing defined term “Compliance Statement” rather than introducing the new term “Annual Compliance Statement”. The only reference to it in schedule 6 should then be amended by deleting the word “Annual”.
- 6 “Assessment Date” is defined as the date by which compliance must be demonstrated. This is incorrect. Compliance must be demonstrated in a Compliance Statement within 50 working days after the end of each Assessment Period. Regardless, the term “Assessment Date” is not used, so it should be deleted
- 7 “Major Event Day” is defined as any day where either the SAIDI or SAIFI boundary value is exceeded, and clause 11.5 is the only clause referencing this term (requiring an explanation of the cause of each Major Event Day). This is inconsistent with the calculation of SAIDI/SAIFI assessed values in schedule 3, which do not reference this term, and only consider SAIFI as a trigger for a major event day. These should be aligned (and below we submit that either SAIDI or SAIFI should trigger a Major Event Day).
- 8 Schedule 5 has the heading “Approval of avoided transmission and new investment costs” but it then goes on to talk about non-transmission recoverable costs.
- 9 Tables 5.4 to 5.6: are these amounts really \$000? This means the amount for Powerco is \$5 per year.

### **Determining pass through and recoverable costs**

- 10 Schedule 5, clause 1(d) requires that the pass through costs (K) and non-transmission recoverable costs (V) used to calculate allowable notional revenue must have been incurred in, or apply to, the two most recent Assessment Periods. This is incorrect.

For allowable notional revenue, costs from the preceding three assessment periods (limited to being within the regulatory period) must be included.

- 11 More importantly, the amounts used for K and V in the calculation of allowable notional revenue (other than for the first assessment period) must be equal to the amounts used for K and V in the previous year's determination of notional revenue. There should be no provision to correct the number as this would create perverse outcomes. For example, if an EDB found that a pass through cost included in the calculation of notional revenue last year was actually greater than the amount disclosed, then the prior year's assessment would have been adversely affected, requiring lower prices to satisfy the price path in that prior year. Then, if the correct amount is substituted in the current year's assessment for the calculation of allowable notional revenue, the allowable price path will be further lowered by the amount of the error, doubling the penalty for not claiming the full pass through cost.
- 12 To correct this, and provide a sound basis for assessment, we suggest the following changes to Schedule 5:
  - "1. The amount of each Pass-through Cost or Non Transmission Recoverable Cost that is used to calculate ~~allowable notional revenue or~~ notional revenue for an Assessment Period, ~~and Transmission Recoverable Cost or Indirect Transmission Charges passed through to Prices during an Assessment Period,~~ must:"And insert a clause before clause 2 that reads:
  - "2. The amount of each Pass-through Cost or Non Transmission Recoverable Cost that is used to calculate allowable notional revenue for an Assessment Period must be equal to the corresponding amounts used in the calculation of Notional Revenue in the previous Assessment Period as disclosed in the Compliance Statement for that previous Assessment Period."
- 13 Note that the removal of the reference to Transmission charges is covered below.
- 14 The requirement for pass-through and non-transmission recoverable costs to be ascertainable largely resolves existing problems with compliance risk due to inevitable differences between costs forecast made when prices are set and what those costs actually turn out to be. However, it does need to be acknowledged that this creates a *two year* delay before such costs can be recovered, because the actual costs for year t are not known until prices are set for year t+2. The consequent effects on disclosed profitability in any year might not be that obvious to an interested party. While the amounts are subject to a time value adjustment, it may be that associated changes to information disclosure are needed to avoid understatement of profitability – about a - 0.3% lower return in Orion's case for the first two years.

- 15 There would also be a reasonably substantial step change down (other things equal) in distribution prices in year 1, and a subsequent step up in year 3. For Orion this would be about +/- 2%.
- 16 Given these outcomes, we would prefer to have the option to include the majority of a non-ascertainable pass-through or recoverable cost (maybe 80%) and just carry forward the balance.

### Transmission assessment

- 17 Clause 8.5 incorrectly refers to cause 8.7, it should be 8.6.
- 18 Schedule 5 clause 1 includes a reference to Transmission Recoverable Costs and Indirect Transmission Charges that is not appropriate in part (d) because charges can (and should) be included in the year in which they accrue. This negates the need for part (b) of the same clause, part (a) excludes them and part (b) is not relevant, so the two references should be removed.
- 19 The carry forward formula in clause 8.6 for the Transmission Balance has an error. The highlighted term should be “plus” not “minus”, so that (for example) successive over-recoveries accumulate (rather than offset).

$$TB_t = \sum_i TP_{i,t} Q_{i,t} - T_t - TB_{t-1}(1+r)$$

- 20 Assessing this formula requires final chargeable quantities to be known within less than 50 Business Days after the end of an Assessment Period, which, at least in Orion’s case, is not possible without bringing forward significantly the analysis that we carry out for information disclosure purposes. We submit that this places undue and unnecessary pressure on the preparation of the compliance statement. It also introduces a new audit requirement into that process. Both the calculations (which might change due to subsequent wash-ups) and the audit would then need to be repeated for information disclosure.
- 21 We consider that t-1 (prior year) quantities are reasonably available at the point that a compliance statement is prepared, and we suggest that this can be incorporated within the process by assessing an opening Transmission Balance (instead of a closing balance). Effectively  $TB_t$  would be defined as the Transmission Balance at the start of Assessment Period t.

Then for 2016, define:

$$TB_{2016} = \text{nil}$$

And for all other assessment periods:

$$TB_t = \sum_i TP_{i,t-1} Q_{i,t-1} - T_{t-1} + TB_{t-2} (1+r)$$

- 22 The requirement for the Transmission Balance to be less than zero in the final year of a regulatory period is not acceptable, as it pretty much guarantees that we will significantly under-recover this cost. This is because we would need to allow for any variation in the cost (which is usually quite small) and in chargeable quantities (which can be much larger). Further, prices are set well before the start of the final year, so we would need to allow for variation in quantities in both years. We estimate that to provide any confidence of avoiding a breach, we would need to aim to under recover by 4%. If these same variable factors turn against us, the result could be an under recovery of 8% or more than \$5m in Orion's case.
- 23 The approach will need to be changed so that the balance can be carried forward to future regulatory periods (much as many other aspects of the regulatory regime carry forward). An alternative compliance test will then be required, and we suggest that a suitable test on the opening Transmission Balance (described above) is that it must be either nil or negative in the current Assessment Period or one (or both) of the preceding two Assessment Periods. This approach provides flexibility with an incentive to keep the Transmission Balance as small as possible. In the first regulatory period this test would first be appropriate in the fourth compliance statement, but could then be applied in every assessment period of subsequent regulatory periods (that is, there would be no initial "nil" setting in subsequent regulatory periods). It may also be possible to design some time value incentives around minimising the transmission balance.

### **Restructuring of prices**

- 24 Clause 8.7 is accurate, but fails to recognise that the calculation of allowable notional revenue for an Assessment Period following the Assessment Period in which a restructure occurs *is* affected by the restructuring. No guidance is then given on how allowable notional revenue might be calculated in this situation where t-1 prices do not align with t-2 quantities. This is a significant complication.
- 25 Clause 8.8 similarly fails to recognise that the notional revenue in an Assessment Period following the Assessment Period in which a restructure occurs also needs special consideration, essentially leaving no basis for assessment.

### **Advance notification of price restructuring**

- 26 We do not understand the obligation in clause 8.10 to provide advance notice of a price restructuring together with derived prior quantities and forecast future quantities.

This serves no purpose as the Commerce Commission cannot take any action in relation to the information. We also consider that any derivation of prior quantities will be unduly influenced (and information may not even be available) if it is required to be prepared more than 16 months in advance of the preparation of the relevant compliance statement. Quite separately, it creates a second reporting requirement that is unnecessary, and we submit that all information should be disclosed within the normal annual compliance statement. Clause 8.10 should be removed.

### **Approval mechanisms**

- 27 The documents propose approval mechanisms for a number of recoverable costs. In most cases we do not agree that approval is appropriate. All that should be required is that the distributor can establish that the cost was incurred.

### **Change to recovery of avoided transmission charges**

- 28 The current ID determination definition for Transmission charge includes avoided transmission charges as follows:

“Transmission charge means any payment made in respect of the use of the transmission system. For the avoidance of doubt, this includes avoided transmission charges”

- 29 Consistent with this, we have included avoided transmission charges when determining our transmission prices. However, the revised IM determination excludes avoided transmission charges with:

“Transmission charge means any payment made in respect of a Transmission Recoverable Cost”, and

“Transmission Recoverable Cost means a recoverable cost specified in clause 3.1.3(1)(b), (c), (d), or (f).”

As avoided transmission charges are in part (e), they are not included.

- 30 We agree with this change, and we will need to reduce our transmission prices and apply a corresponding increase in distribution prices to implement it. We submit that the ID Determination should be amended to remove the conflict between the two.

### **Change to definition of distributed generation payments as recoverable cost**

- 31 We agree that the existing definition needs to be amended as it is not meaningful. However, the draft sets out a new definition that links the allowance to the regulated avoided transmission charge, which is problematic.
- 32 For most of our generating customers we agree an alternative basis for credits, where we provide certainty over when to generate in exchange for a lower credit price. It would be almost impossible for a customer to know when to run their generator in order to coincide with the 12 half-hours of regional peak demand, and any that tried might find themselves operating for hundreds of hours for no reward. Orion is in a much better position to co-ordinate this activity, with direct access to all regional loads and participation in a regional load management arrangement. We effectively eliminate the risk for customers of when to generate, but we need to be able to claim the actual payments made as a recoverable cost in order to take this approach.
- 33 If the proposed definition is implemented we will be forced to adjust our export credit approach and we will probably need to abandon our separate generation credit arrangement. We think our arrangements work well and that the Commission should be wary of making changes to what are long-standing arrangements.

### **Definition of Interruption**

- 34 We are occasionally required to interrupt supply (in an unplanned way) by the System Operator under its AUFLS and AUVLS schemes, or we could be required to interrupt supply (in a planned or unplanned way) by the System Operator under its Rolling Outage scheme. These interruptions can originate on equipment that is embedded within our network, including on equipment that we own. However, these types of outages, and any others required by regulation, are outside our control, and should not contribute to reliability limits or assessed values.
- 35 We suggest that the definition of interruption be amended to exclude these outages with the following additional exclusion:
- “e) as a result of an automatic under voltage, under frequency or rolling outage scheme (or similar) required as part of the System Operator Services or other instruction from an appropriately authorised regulator.”
- 36 As a separate issue, we note that the definition of unplanned interruption is one in which no notice or less than 24 hours' notice is given. We believe the majority of EDBs operate to a previous Electricity and Gas Complaints Commission Scheme requirement to provide 4 working days' notice, which is much more meaningful in terms of allowing consumers to prepare. We submit that the quality requirements

should be amended to reflect this. While the disclosure requirements should also be similarly amended, a temporary discrepancy is of little consequence as we simply don't issue advance notice of less than 4 working days.

- 37 We otherwise support the definition of Class B Interruption, Class C Interruption, Interruption, Planned Interruption and Prescribed Voltage Electric Line.

**Concluding remarks**

- 38 Thank you for the opportunity to make this submission. Orion does not consider that any part of this cross submission is confidential. If you have any questions please contact David Freeman-Greene (GM Commercial), DDI 03 363 9848, email david.freeman-greene@oriongroup.co.nz.

Yours sincerely



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