



COMMERCE COMMISSION

**Information Disclosure  
Discussion Paper**

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Network Performance Branch

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**TABLE OF CONTENTS**

**LIST OF TERMS, ABBREVIATIONS AND DEFINITIONS**

**EXECUTIVE SUMMARY ..... I**

**INTRODUCTION ..... 1**

- 1.1 Purpose of this Paper ..... 1
- 1.2 Background ..... 1
- 1.3 Structure of Paper ..... 2
- 1.4 Next Steps ..... 4
- 1.5 Consultation on this Discussion Paper ..... 6

**CHAPTER 2: STATUTORY FRAMEWORK AND REGULATORY**

**FRAMEWORK PRINCIPLES ..... 9**

- 2.1 Introduction ..... 9
- 2.2 Information Disclosure Purpose ..... 9
- 2.3 Information Disclosure Framework ..... 12
- 2.4 Principles of Information Disclosure ..... 14
- 2.5 Information Disclosure Process ..... 18
- 2.6 Relationship with Input Methodologies ..... 19

**CHAPTER 3: MONITORING PERFORMANCE ..... 21**

- 3.1 Introduction ..... 21
- 3.2 Monitoring Performance and the Regulatory Objectives ..... 22
- 3.3 Innovation and Investment ..... 23
- 3.4 Quality ..... 27
- 3.5 Profits ..... 28
- 3.6 Prices ..... 29
- 3.7 Efficiency ..... 30
- 3.8 Summary of Preliminary Views ..... 33

**CHAPTER 4: RETURN ON INVESTMENT (ROI) ..... 35**

- 4.1 Introduction ..... 35
- 4.2 Key Matters for Consideration ..... 36
- 4.3 The Proposed ROI Formula ..... 43
- 4.4 Summary of Preliminary Views ..... 44

**CHAPTER 5: FINANCIAL INFORMATION ..... 48**

- 5.1 Introduction ..... 48
- 5.2 Purpose of Financial Disclosures ..... 48
- 5.3 Key Matters For Consideration ..... 48
- 5.4 Financial Disclosures ..... 57
- 5.5 Summary of Disclosures ..... 60

**CHAPTER 6: REGULATORY ASSET BASE (RAB) DISCLOSURES.62**

6.1 Introduction ..... 62  
6.2 Purpose of Regulatory Asset Base (RAB) Disclosures..... 63  
6.3 Key Matters For Consideration ..... 63  
6.4 Regulatory Asset Base (RAB) Disclosures ..... 69  
6.5 Summary of Disclosures ..... 72

**CHAPTER 7: QUALITY DISCLOSURE AND STATISTICS.....74**

7.1 Introduction ..... 74  
7.2 Purpose of Quality Disclosures ..... 74  
7.3 Key Matters For Consideration ..... 75  
7.4 Aspects of Quality ..... 80  
7.5 Statistics ..... 84  
7.6 Summary of Disclosures ..... 86

**CHAPTER 8: ASSET MANAGEMENT PLANS .....88**

8.1 Introduction ..... 88  
8.2 Purpose of Asset Management Plans ..... 89  
8.3 Key Matters For Consideration ..... 90  
8.4 Components of Asset Management Plans ..... 94  
8.1 Summary of Disclosures ..... 102

**CHAPTER 9: PRICING AND OTHER DISCLOSURE PROVISIONS105**

9.1 Introduction ..... 105  
9.2 Pricing Disclosures..... 105  
9.3 Assumptions, Policies and Methodologies Disclosures..... 108  
9.4 Summary of Disclosures ..... 109

**CHAPTER 10: PUBLICATION, RETENTION, CERTIFICATION, STATUTORY DECLARATION AND AUDIT .....112**

10.1 Introduction ..... 112  
10.2 Publication and Retention of Information ..... 112  
10.3 Certification, Statutory Declaration and Audit ..... 116  
10.4 Summary of Preliminary Views ..... 122

**CHAPTER 11: ELECTRICITY DISTRIBUTION LINES SERVICES123**

11.1 Introduction ..... 123  
11.2 Unique Characteristics of EDBs ..... 123  
11.3 Application of Information Disclosure to EDBs..... 126  
11.4 Scope of Disclosures Summary..... 137

**CHAPTER 12: TRANSPOWER.....141**

12.1 Introduction ..... 141  
12.2 Unique Characteristics of Transpower Services ..... 141  
12.3 Application of Information Disclosure to Transpower ..... 146  
12.4 Scope of Disclosures Summary..... 152

**CHAPTER 13: GAS PIPELINE SERVICES .....157**  
13.1 Introduction ..... 157  
13.2 Unique Characteristics of Gas Pipeline Services ..... 157  
13.3 Application of Information Disclosure Regulation to Gas Pipeline Services 159  
13.4 Scope of Disclosures Summary..... 170

**CHAPTER 14: SPECIFIED AIRPORT SERVICES .....175**  
14.1 Introduction ..... 175  
14.2 Unique Characteristics of Specified Airport Services..... 175  
14.3 Application of Information Disclosure Regulation to Specified Airport  
Services ..... 179  
14.4 Scope of Disclosures Summary..... 192

**APPENDIX A: INDEX OF QUESTIONS .....197**

**APPENDIX B: STATUTORY PROVISIONS .....212**

## LIST OF TERMS, ABBREVIATIONS AND DEFINITIONS

Term/Abbreviation	Definition
AAA	Airport Authorities Act 1966
ACCC	Australian Competition and Consumer Commission
ACI ASQ	Airport Council International Airport Service Quality
AIAL	Auckland International Airport Limited
Airport Companies	AIAL, WIAL and CIAL
AMP	Asset Management Plan
Annual Disclosure	Performance indicators, financial, asset valuation, quality, statistics and asset management forecast information
BARNZ	Board of Airline Representatives New Zealand Incorporated
CAA	Commerce Amendment Act 2008
CAIDI	Customer Average Interruption Duration Index
CIAL	Christchurch International Airport Limited
Commission	Commerce Commission
CPI	Consumer Price Index
EBIT	Earnings Before Interest and Tax
EDB	Electricity Distribution Business
EGR	Electricity Governance Rules
ELB	Electricity Lines Business
EV	Economic Value
FCM	Financial Capital Maintenance
FDC	Finance During Construction
GAAP	Generally Accepted Accounting Practice
Gas Authorisation	Authorisation for the control of supply of natural gas distribution services by Powerco Limited and Vector Limited.
GIDRs	Gas (Information Disclosure) Regulations 1997
GPS	Government Policy Statement
GXP	Grid Exit Point
HVAC	High Voltage Alternating Current
HVDC	High Voltage Direct Current
IATA	International Air Transport Association
ICP	Installation Control Point
IRR	Internal Rate of Return
IT	Information and Technology
MDL	Maui Development Limited
MED	Ministry of Economic Development

<b>Term/Abbreviation</b>	<b>Definition</b>
MEUG	Major Electricity Users Group
NGC	Natural Gas Corporation
NPV	Net Present Value
NZ	New Zealand
NZ IAS	New Zealand Equivalent to International Accounting Standard
ODV	Optimised Deprival Valuation
Part 4	New Part 4 of the Commerce Act (1986), inserted by the Commerce Amendment Act (2008). Replaces Part 4A.
Part 4A	Commerce Act (1986) Part 4A
Provisions Paper	The Commerce Commission's Regulatory Provisions of the Commerce Act 1986 Discussion Paper
RAB	Regulatory Asset Base
RIV	Regulatory Investment Value
ROI	Return on Investment
SAIDI	System Average Interruption Duration Index
SAIFI	System Average Interruption Frequency Index
Services	Goods and Services
SFA	System Fixed Asset
TBA	To Be Announced
The Act	Commerce Act 1986
The April 2008 GPS	The Government's Policy Statement on Gas Governance provided to the Commission in April 2008
The May 2009 GPS	The Government's Policy Statement on Electricity Governance transmitted to the Commission in May 2009
The 2006 GPS	The Government's Policy Statement: Incentives of Regulated Businesses to Invest in Infrastructure provided to the Commission in August 2006
TPM	Transmission Pricing Methodology
UFG	Unaccounted for Gas
WACC	Weighted Average Cost of Capital
WIAL	Wellington International Airport Limited

## EXECUTIVE SUMMARY

- X1 This paper sets out the Commerce Commission's (Commission's) preliminary views on its approach to information disclosure regulation under Part 4 of the Commerce Act 1986 (the Act). The paper includes specific discussion of the application of information disclosure regulation to the suppliers of regulated electricity lines, gas pipelines and specified airport services. The purpose of the paper is to seek the views of interested parties on the development of information disclosure determinations (hereafter "disclosure requirements") for those suppliers.
- X2 The central purpose of Part 4 of the Act is to promote the long term benefit of consumers in markets where there is little or no competition and little or no likelihood of a substantial increase in competition. To achieve this, the Commission must promote outcomes in regulated markets consistent with those produced in competitive markets, such that regulated suppliers have incentives to improve efficiency and provide services with the long-term benefit of consumers in mind.
- X3 Information disclosure is the most light-handed regulatory instrument available to the Commission under Part 4. Its purpose, as stated in s 53A of the Act, is to ensure that sufficient information is readily available to interested persons to assess whether the purpose of Part 4 is being met. The disclosure of information, and the Commission's summary and analysis of that information, provide the means by which the purpose of information disclosure is to be achieved.
- X4 This Discussion Paper is the first significant consultation paper being released by the Commission as part of the process to determine disclosure requirements for suppliers regulated under Part 4. It sets out the Commission's preliminary views in relation to information disclosure regulation for regulated electricity lines, gas pipelines and specified airport services.

## PRINCIPLES OF INFORMATION DISCLOSURE

- X5 In undertaking its functions under Part 4 of the Act, the Commission considers that there are three key economic principles which stem from the three dimensions of economic efficiency. These are that decisions should:
- promote **allocative efficiency**, subject to the opportunity for regulated businesses to earn normal returns;
  - promote realistic and achievable gains in **productive efficiency**; and
  - promote **dynamic efficiency** by providing incentives for efficient investment and innovation.
- X6 The Commission has also identified four implementation principles, which are that regulatory decisions should be made with the following principles in mind:
- Consistency;
  - Transparency;
  - Cost-effectiveness; and

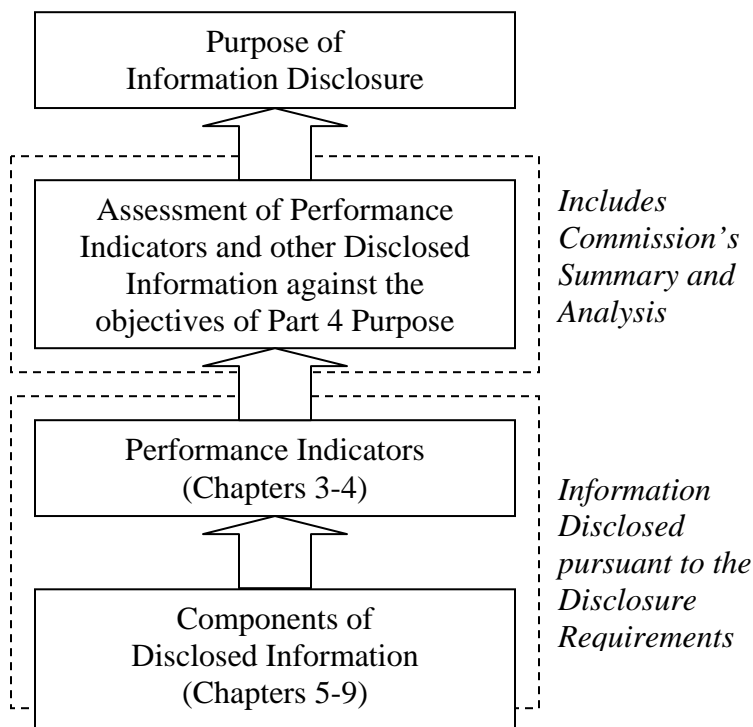


- Flexibility.
- X7 The Commission is aware that all regulatory instruments, including information disclosure, impose compliance costs upon regulated suppliers. The Commission is therefore mindful of the need to implement a least-cost regime that sufficiently informs interested persons whether the purpose of Part 4 is being met. It is noted, however, that the purpose of information disclosure regulation, requires that some information must be disclosed which unavoidably entails costs.
- X8 The Commission, throughout this paper, has identified where information should be readily available and where information may be required to be developed. This is intended to facilitate a discussion on the cost effectiveness of the various disclosures proposed.

### INFORMATION DISCLOSURE FRAMEWORK

- X9 The disclosure of information, and the Commission's summary and analysis of that information, provide the means by which the purpose of information disclosure regulation is to be achieved. In the first instance, this requires that the components of disclosed information (e.g., revenues and costs), be combined to produce a number of performance indicators (e.g., profitability). The Commission's summary and analysis supplements these indicators by providing greater narrative to explain the overall performance of regulated suppliers relative to each other and over time. Figure A below outlines the relationship between the constituent parts of the proposed information disclosure framework:

**Figure A: Information Disclosure Framework**



- X10 Where information disclosed does not readily indicate the performance of regulated

entities (such as information disclosed through an Asset Management Plan (AMP)), the consolidation and interpretation exercise undertaken by the Commission through the summary and analysis will more easily allow interested persons to assess regulated suppliers' performance. For example, the Commission proposes developing and publishing a prescribed AMP performance indicator that includes ratings on such things as investment and innovation.

### MONITORING PERFORMANCE

- X11 The Commission considers that it would be appropriate to require regulated suppliers to disclose performance indicators and supporting information relevant to each of the key performance areas outlined in the Act. The Commission considers that the annual disclosure of a limited number of relatively easily understood performance indicators would, when taken together, provide a rounded picture of the performance of regulated suppliers.
- X12 Summary Table A below outlines the key performance areas referred to in the Part 4 purpose statement, the proposed performance indicators related to those performance areas, and the components of disclosed information that support each performance indicator.

**Table A: Annual Performance Indicators**

<b>Part of Purpose</b>	<b>Key Performance Areas</b>	<b>Performance Indicator</b>	<b>Component of Disclosed Information</b>
52A(1)(a)	Innovation and investment	AMP Review Rating – Innovation and Investment	AMP
		Capital Expenditure Ratios	Financial, Asset Valuation and Statistics
52A(1)(b)	Efficiency	Operational Expenditure Ratios	Financial, Asset Valuation and Statistics
		Capacity Utilisation	Statistics
		Consumer Group Price or Average Revenue Information	Financial and Statistics
	Quality	AMP Review Rating - Quality	AMP and Quality Measures
		Service Specific Measures	Quality Disclosures

Part of Purpose	Key Performance Areas	Performance Indicator	Component of Disclosed Information
52A(1)(c)	Prices	ROI	Financial and Asset Valuation
		Consumer Group or Activity Price Information	Financial and Statistics
52A(1)(d)	Profits	ROI	Financial and Asset Valuation

X13 The Commission's preliminary view is that an ROI indicator should be the key measure of profitability under information disclosure regulation. The basic ROI formula proposed by the Commission is:

$$\text{Return On Investment} = \frac{\text{Regulatory Profit}}{\text{Asset Base}}$$

#### COMPONENTS OF DISCLOSED INFORMATION

X14 The Commission's preliminary view is that the components of disclosed information discussed below are required to support the performance indicators identified above and to assist in the analysis of those performance indicators.

##### *Financial Information*

X15 The primary purpose of financial information disclosure is to establish the basis of financial performance indicators, such as the ROI, that are used to monitor the performance of the regulated suppliers. The proposed line items of the regulatory financial statements would be structured so that they transparently link with other proposed disclosures and the financial information that is used in the performance indicators.

X16 The Commission's preliminary view is to consider GAAP as the starting point for the disclosure of financial information, but modify the disclosure requirements where necessary to meet the purposes of information disclosure under Part 4. Regulatory reporting is likely to be different from GAAP where the purposes of the regulatory regime require more prescriptive definitions and additional information than is required under GAAP. Conversely, there are certain disclosures required under GAAP that may not be relevant to the regulatory regime in that they are not required to meet the purpose of that regime.

##### *Regulatory Asset Base (RAB)*

X17 The regulatory asset base (RAB) value is the key term in the denominator in the ROI performance indicator calculation, and in some of the operational and capital

expenditure performance indicators. Asset base information is also useful to interested persons in understanding the make-up of the asset base and the accuracy of the information contained within it. It also provides information on where investment has occurred and is occurring. This is useful as it relates to the extent to which suppliers have incentives to invest (s 52A(1)(a)).

### ***Quality***

- X18 Disclosure of quality performance indicators both highlights the ability of, and promotes incentives for, regulated service providers to deliver services reflective of consumer demands (s 52A(1)(b)). Information disclosure regulation may assist in preventing deterioration of quality standards and may also assist interested persons to assess whether the quality performance exceeds that demanded by consumers.
- X19 The Commission intends designing requirements that assess regulated suppliers' quality on the aspects of reliability, supply quality, and customer service. It is the Commission's preliminary view that disclosure of safety measures is not required.

### ***Statistics***

- X20 Statistics disclosures, among other things, provide context and scale to the performance indicators so that more meaningful comparisons can be made between regulated suppliers in each sector. In the Commission's preliminary view, statistics fall into the categories of asset information, demand, capacity and pricing.

### ***Asset Management Plans (AMPs)***

- X21 In the Commission's view, sound asset management planning and the disclosure of those plans is integral to ensuring that, over the long term, interested persons can monitor whether or not regulated suppliers face appropriate incentives to improve efficiency and innovate, as well as provide services at a price and quality that reflects consumer demands.
- X22 The Commission's preliminary view is that a requirement to publicly disclose an AMP should be applied to all regulated suppliers.

### ***Pricing***

- X23 Pricing disclosures include prices, pricing methodologies, and the terms and conditions of prices. It is the Commission's preliminary view that all regulated suppliers should disclose and publish this information so that interested persons can make an assessment of relative pricing at the consumer level.

### ***Other Disclosures***

- X24 Other disclosures include assumptions, methodologies and policies. In the Commission's view, assumptions and methodologies provide further transparency to disclosures. Disclosure of specified policies including credit, delegated authority and profit distribution (among others), enable an assessment of risks that could materially impact on the profitability or viability of the regulated business.

### ***Certification, Audit, Statutory Declaration, Publication and Retention Requirements***

- X25 It is the Commission's preliminary view that performance indicators, financial,

asset valuation, quality, statistics and asset management forecast information should be disclosed as a package no later than five months after the end of the respective regulatory year. The Commission proposes that these disclosures should also be certified and audited. AMP, pricing methodologies, prices and contracts disclosures have different proposed reporting dates and different certification and auditing requirements, due to the nature of the information they contain.

### **MATTERS SPECIFIC TO REGULATED SERVICES**

- X26 The specification and calculation of information disclosure performance indicators and the components of disclosed information may vary for each regulated service due to each service's unique characteristics. The components of disclosed information that are unique for all regulated services include capital expenditure, operational expenditure, statistics, quality and regulated asset categories. In addition, each sector has other unique characteristics that affect the application of information disclosure. Outlined below is a summary of the Commission's preliminary views on how the information disclosure regime should be customised for each of the regulated services, in addition to the areas identified above.
- X27 The key Commission preliminary views on how the information disclosure regime for Electricity Distribution Businesses (EDBs) should be customised are as follows:
- Sufficient information should be provided so that interested persons can understand the impact of the differences between EDBs on performance of the EDBs, to the extent practicable;
  - Returns provided to consumer-owned EDBs, such as rebates, discounts, line charge holidays and dividends, should be treated consistently by all EDBs for regulatory reporting purposes; and
  - Separate disclosure of quality and statistics information for different networks should be required where an EDB has non-contiguous networks or is controlled by consumers of one part of the overall network.
- X28 The key Commission preliminary views on how the information disclosure regime for Transpower should be customised are as follows:
- AMP, pricing methodology and prices disclosures should be consistent with the Electricity Commission disclosure requirements;
  - An assessment of Transpower's AMPs is not required due to the Electricity Commission's procedures; and
  - Separate financial information should be disclosed for the HVDC, HVAC system operator and new investment business activities.
- X29 The key Commission preliminary views on how the information disclosure regime for gas pipeline businesses should be customised are as follows:
- Sufficient information should be provided so that interested persons can understand the impact of the differences between gas pipeline businesses on performance of the gas pipeline businesses, to the extent practicable;

- Separate disclosure of Transmission and Distribution business activities; and
  - Separate disclosure of quality and statistics information where a gas pipeline business has non-contiguous networks.
- X30 The key Commission preliminary views on how the information disclosure regime for specified airport services should be customised are as follows:
- Separate disclosure of financial information for airfield, aircraft and freight and specified terminal activities; and
  - There should be a greater focus on customer perception as a means of assessing quality.

#### NEXT STEPS

- X31 The determinations for each type of regulated service will be separate work streams (except for this discussion paper) following a common set of phases. The Commission's approach to issuing the determinations is as follows:
- Phase I: Discussion Paper
  - Phase II: Draft Determinations
  - Phase III: Final Determinations
- X32 The release of this Discussion Paper marks the start of Phase I. Phase II will consist of the preparation of draft determinations and a supporting companion paper that will provide background information to the draft determinations. Final Determinations will be made in Phase III.
- X33 The Commission welcomes submissions on all matters relevant to information disclosure. Submissions on this Discussion Paper are due by **5pm on Friday, 4 September 2009**.
- X34 Other papers already released that are relevant to regulation under Part 4 of the Act include:
- Input Methodologies Discussion Paper;
  - Reset of Default Price-Quality Paths for Electricity Distribution Businesses Discussion Paper;
  - Transpower Process and Recommendation Discussion Paper; and
  - Revised Draft Cost of Capital Guidelines.

## INTRODUCTION

### 1.1 PURPOSE OF THIS PAPER

- 1 This paper sets out the Commerce Commission's (Commission's) preliminary views on its approach to information disclosure regulation under Part 4 of the Commerce Act 1986 (the Act).
- 2 This paper outlines the Commission's preliminary views on how the purpose of information disclosure regulation as set out in section 53A of the Act is to be achieved and what information should be disclosed by regulated suppliers to assist in achieving that purpose. The paper also includes specific discussion on the application of information disclosure regulation to the suppliers of regulated electricity lines (including transmission), gas pipelines and specified airport services.
- 3 The paper covers all services regulated under Part 4 of the Act (Part 4) so that discussion on the fundamentals of information disclosure regulation can be held with all interested parties. The purpose of the paper is to seek the views of interested parties on the development of information disclosure determinations for regulated electricity lines, gas pipeline and specified airport services (hereafter "disclosure requirements").
- 4 The paper also briefly outlines how the information disclosed under the proposed disclosure requirements will assist the Commission in meeting its summary and analysis obligations.

### 1.2 BACKGROUND

- 5 The Commerce Amendment Act 2008 (CAA), which received Royal assent on 16 September 2008, has introduced significant changes to those provisions in Parts 4, 4A, 5 and 6 of the Act that relate to the economic regulation of goods and services (hereafter "services") in New Zealand.
- 6 Among other things, the amendments introduced by the CAA directly affect the scope and role of the Commission in regulating electricity and gas distribution/transmission services. They also extend the Commission's responsibilities to include the regulation of specified airport services at New Zealand's three largest international airports.
- 7 The suppliers of the following services are subject to information disclosure regulation under Part 4:
  - Electricity lines services (transmission and distribution);
  - Gas pipeline services (transmission and distribution); and
  - Specified airport services (Auckland, Christchurch and Wellington International Airports).
- 8 A regulated supplier may supply one or more types of regulated services, and may also supply unregulated services. For the purposes of this paper, we have used the

term 'business unit' to refer to that part of a regulated supplier that supplies a single type of regulated or unregulated service, whether or not the regulated supplier actually organises its operations into business units in this manner. Information disclosure regulation relates to the supply of regulated goods and services, and therefore disclosures must be disaggregated down to the regulated business unit level in order to be effective.

- 9 With the exception of the majority of regulatory provisions relating to electricity lines services, which came into force on 1 April 2009, most of the provisions in the CAA came into force from 14 October 2008.
- 10 On 19 December 2008, the Commission published the Regulatory Provisions of the Commerce Act 1986 Discussion Paper (Provisions Paper), which set out the Commission's preliminary views on the new regulatory provisions that were introduced through the CAA, including a brief discussion on the information disclosure provisions.<sup>1</sup>
- 11 On 19 June 2009, the Commission published the Input Methodologies Discussion Paper, the purpose of which was to consult on the Commission's preliminary views in relation to matters that may be determined as input methodologies under Part 4 of the Act.<sup>2</sup> This Paper has been prepared in conjunction with the Input Methodologies Discussion Paper and sets out the Commission's preliminary views on how the proposed input methodologies should be applied to information disclosure.

### 1.3 STRUCTURE OF PAPER

- 12 The structure of this paper is reflective of the information disclosure framework as outlined in paragraphs 58 to 66 below.

**Table 1: Structure of Paper**

Section	Chapter	Title
Framework	1	Introduction
	2	Statutory Framework and Regulatory Framework Principles
Performance Indicators	3	Monitoring Performance
	4	Return on Investment

<sup>1</sup> Commerce Commission, *Regulatory Provisions of the Commerce Act 1986 Discussion Paper*, 19 December 2008.

<sup>2</sup> Commerce Commission, *Input Methodologies Discussion Paper*, 19 June 2009.



Section	Chapter	Title
Components of Disclosed Information	5	Financial Information
	6	Regulatory Asset Base
	7	Quality and Statistics
	8	Asset Management Plans (AMPs)
	9	Pricing and Other Disclosures
	10	Certification, Statutory Declarations, Audit, Retention and Publication
Matters Specific to the Regulated Services	11	Electricity Distribution Services
	12	Transpower
	13	Gas Pipeline Services
	14	Specified Airport Services

- 13 Chapters 1 and 2 outline the framework for information disclosure, including discussion on the purpose of information disclosure, the purpose of Part 4 and the relevant statutory provisions.
- 14 The Commission's preliminary views of what key performance indicators should be specified in the disclosure requirements, how they relate to the purpose of information disclosure regulation and a brief outline of what information should be required to support them are presented in Chapters 3 and 4.
- 15 Chapters 5 to 9 outline the Commission's preliminary views on the types of information to be disclosed, how they relate to the performance indicators and how they should be utilised in meeting the purpose of information disclosure in addition to supporting the performance indicators.
- 16 Chapter 10 outlines the Commission's preliminary views on the requirements for certification, statutory declaration and audit of the disclosed information. This chapter also outlines the Commission's preliminary views on publication and retention of information.
- 17 Chapters 11 to 14 outline the unique characteristics of each type of regulated service that may have implications for the information disclosure regime and how the Commission proposes applying the information disclosure regime to each type of regulated service in light of those unique characteristics.

#### 1.4 NEXT STEPS

- 18 In addressing information disclosure for each of the regulated services the Commission intends taking a two step approach so that parts of the information disclosure requirements that require significant development work can be deferred beyond an initial determination (hereafter ‘determination’). Paragraphs 20 to 26 outline the Commission’s proposed next steps for making the determination. Further detail on the possibility of subsequent determinations is outlined in paragraphs 27 to 29 below.
- 19 The determinations for each type of regulated service will be separate work streams following a common set of phases, including this discussion paper which covers all services. The Commission’s approach to issuing the determinations is as follows:
- Phase I: Discussion Paper
  - Phase II: Draft Determination
  - Phase III: Determination
- 20 Table 2 below sets out the key project deliverables for each of the regulated services.

**Table 2: Overview of project deliverables**

Phase	Key Deliverable	Airports	EDBs	Transpower	Gas
Phase I	Discussion Paper	29 July 2009			
	Submissions due on Discussion Paper	4 September 2009			
	Workshops (if required)	Q4 2009			
Phase II	Consultation on specific topics	Q4 2009	TBA	TBA	TBA
	Draft Determination	Q1 2010	TBA	TBA	TBA
	Submissions due on Draft Determination	Q1 2010	TBA	TBA	TBA
	Cross-submissions due on Draft Determination	Q1 2010	TBA	TBA	TBA
	Workshops on Draft Determination (if required)	Q2 2010	TBA	TBA	TBA

Phase	Key Deliverable	Airports	EDBs	Transpower	Gas
Phase III	Release final Draft Determination	Q2 2010	TBA	TBA	TBA
	Submissions due on Technical Drafting of Determination	Q2 2010	TBA	TBA	TBA
	Final Determination comes into force	1 July 2010	TBA	TBA	TBA

- 21 The release of this Discussion Paper marks the start of Phase I. The Commission may hold one or more workshops for interested parties in relation to regulated services subject to information disclosure after submissions on this Discussion Paper have been received. The Commission will determine the necessity for, and scope of, these workshops on the basis of submissions received.
- 22 Phase II will consist of the preparation of draft determinations and a supporting companion paper, providing background information to the draft determination.
- 23 Phase II may also include workshops on the application of statistics, quality measures and definitions being applied in the draft determinations. A similar workshop was used for the drafting of the Electricity Distribution (Information Disclosure) Requirements 2008.
- 24 Phase III will be to make the determinations. This is to include a final draft determination that will be provided to the relevant regulated suppliers for technical review. A technical review is a short process where regulated suppliers are able to review the final draft determination and provide feedback on any technical drafting concerns.
- 25 The final deliverables of Phase III will be the information disclosure determination (including relevant Handbooks and other guidance material) and a supporting companion paper for each type of regulated service.
- 26 Section 53C(1) specifies the required content of these determinations, but section 53C(2) leaves the Commission some discretion as to the type of information that may be required to be disclosed.

#### *Subsequent Determinations*

- 27 As mentioned above, the Commission is mindful of the development work required to implement an effective information disclosure regime and therefore may defer the implementation or development of certain information disclosure components beyond the date of the initial determination. The decision as to which, if any, components will be deferred will be made in the course of developing the disclosure determinations. Section 52P(4) states that it is not necessary for a single determination to address all matters relating to particular regulated goods or services, or a supplier of regulated goods or services.

- 28 Any subsequent determination or material amendment can only occur after the Commission has consulted with interested parties (s 52Q).
- 29 To meet its statutory obligations, the Commission must make information disclosure determinations and those determinations must specify the input methodologies that apply. Therefore, the information disclosure determinations must include the components of disclosed information that take into account input methodologies.

#### ***1.4.1 Specified Airport Services Initial Determination***

- 30 The Commission has a statutory obligation under section 56E to make the initial information disclosure determination for specified airport services by 1 July 2010 (or, if the deadline for determining input methodologies is extended under section 52U(2), no later than the day after the date to which that deadline is extended). The Commission has outlined the next steps in meeting this requirement in Table 2 above.

#### ***1.4.2 Electricity Lines and Gas Pipelines Determinations***

- 31 Section 54I(1) and 55E(1) state that the section 52P determinations that specify how information disclosure regulation applies to each supplier of electricity lines and gas pipeline services must be made as soon as practicable after the applicable subpart comes into force.<sup>3</sup>
- 32 Under section 55J, the Gas (Information Disclosure) Regulations 1997 (GIDRs) continue to apply to each supplier of gas pipeline services until the Commission makes new information disclosure determinations under Part 4.
- 33 Under section 54W, any information disclosure requirements published by the Commission under Part 4A before 1 April 2009 continue to apply to each supplier of electricity lines services until a determination is made under Part 4.
- 34 The Commission plans outlining the proposed timeframe for making initial information disclosure determinations for electricity lines and gas pipelines services following review of submissions on this discussion paper.

Q.1) In your view, should the Commission's next steps in making information disclosure determinations for the regulated services be as outlined above? Please provide the reasons for your views.

### **1.5 CONSULTATION ON THIS DISCUSSION PAPER**

#### ***1.5.1 Submissions***

- 35 Submissions are invited on this discussion paper from all interested parties. Submissions should be received by the Commission no later than **5pm Friday, 4 September 2009** ('due-date'). All submissions should be supported by documentation and evidence, where appropriate. To assist interested parties in

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<sup>3</sup> 14 October 2008 for gas pipeline services and 1 April 2009 for electricity lines services.

making submissions, the Commission has identified a number of questions throughout this paper on which it invites comment. These questions are collated in Appendix A for ease of reference.

- 36 In order to meet the time frames prescribed in the Act, the Commission relies on submissions being provided by the due-date. The Commission will only allow extensions beyond the due-date if the submitter provides good reasons in writing prior to the deadline. Unless an extension has been granted, the Commission may not be in a position to adequately consider submissions for the next stages of the project if received after the due-date.
- 37 To foster an informed and transparent process the Commission intends to publish all submissions received on its website ([www.comcom.govt.nz](http://www.comcom.govt.nz)). Accordingly, the Commission requests an electronic copy of each submission and requests that hard copies of submissions not be provided (unless an electronic copy is not possible). Submissions should be sent to:

[NPB@comcom.govt.nz](mailto:NPB@comcom.govt.nz)

or

John Hamill  
Manager  
Network Performance Branch  
Commerce Commission  
P.O. Box 2351  
Wellington

### **1.5.2 Confidentiality**

- 38 The Commission discourages requests for non-disclosure of submissions, in whole or in part, as it is desirable to test all information in a fully public way. It is unlikely to agree to any requests that submissions in their entirety remain confidential. The Commission recognises, however, that there will be cases where interested parties making submissions may wish to provide confidential information to the Commission.
- 39 If it is necessary to include such material in a submission the information should be clearly marked and preferably included in an appendix to the submission. Interested parties should provide the Commission with both confidential and public versions of their submissions. The responsibility for ensuring that confidential information is not included in a public version of a submission rests entirely with the party making the submission.
- 40 Parties can request that the Commission makes orders under section 100 of the Act in respect of information that should not be made public. Any request for a section 100 order must be made when the relevant information is supplied to the Commission and must identify the reasons why the relevant information should not be made public. The Commission will provide further information on section 100

orders if requested by parties, including the principles that are applied when considering requests for such orders. A key benefit of such orders is to enable confidential information to be shared with specified parties on a restricted basis for the purpose of making submissions. Any section 100 order will apply for a limited time only as specified in the order. Once an order expires, the Commission will follow its usual process in response to any request for information under the Official Information Act 1982.

### ***1.5.3 Workshops***

- 41 The Commission considers that workshops could form a useful part of the consultation process for information disclosure. The purpose of holding workshops is to allow the Commission to get input from technical industry specialists in developing and/or evaluating its detailed proposals for information disclosure. The Commission notes the support for workshops in the submissions on the Provisions Paper.

## CHAPTER 2: STATUTORY FRAMEWORK AND REGULATORY FRAMEWORK PRINCIPLES

### 2.1 INTRODUCTION

- 42 This Chapter describes the purpose of information disclosure regulation and briefly outlines the purpose of Part 4, which is referenced in the purpose of information disclosure.
- 43 The Commission also summarises its preliminary views on the principles derived from the purpose statements, which the Commission has sets out in the Input Methodologies Discussion Paper.<sup>4</sup> In that paper, the Commission also set out its preliminary views on the relevant implementation principles. In conjunction with the relevant statutory provisions, these regulatory framework principles will guide how the Commission implements the information disclosure regime to achieve the purpose of information disclosure, which will in turn assist in achieving the purpose of Part 4.

### 2.2 INFORMATION DISCLOSURE PURPOSE

#### 2.2.1 *Relevant Purpose Provisions*

- 44 Section 53A provides that the purpose of information disclosure regulation is:
- to ensure that sufficient information is readily available to interested persons to assess whether the purpose of this Part [as set out in section 52A] is being met.*
- 45 The Part 4 overall purpose statement, for regulating the price and quality of goods or services is set out in s 52A and provides that the purpose of Part 4 is:
- to promote the long-term benefit of consumers in markets referred to in section 52 by promoting outcomes that are consistent with outcomes produced in competitive markets such that suppliers of regulated goods or services -*
- (a) *have incentives to innovate and to invest, including in replacement, upgraded, and new assets; and*
  - (b) *have incentives to improve efficiency and provide services at a quality that reflects consumer demands; and*
  - (c) *share with consumers the benefits of efficiency gains in the supply of the regulated goods or services, including through lower prices; and*
  - (d) *are limited in their ability to extract excessive profits.*
- 46 The standard of competition that underpins the concept of competitive markets referred to in s 52A and Part 4 is that of ‘workable or effective competition’ (hereafter ‘workable’ competition).<sup>5</sup>

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<sup>4</sup> Supra n 2, paragraphs 2.25-2.82.

<sup>5</sup> The Commission’s views on the standard of workable competition are set out in the Input Methodologies Discussion Paper (Ibid., paragraphs 2.30-2.37).

- 47 Section 53B(2)(b) outlines the Commission's summary and analysis obligations and the purpose of that summary and analysis. It specifies that the Commission:
- must, as soon as practicable after any information is publicly disclosed, publish a summary and analysis of that information for the purpose of promoting greater understanding of the performance of individual regulated suppliers, their relative performance, and the changes in performance over time.*
- 48 Apart from assisting interested persons to assess whether the purpose of Part 4 is being met - by helping to reflect the extent to which the regulatory framework principles are being promoted - information disclosure regulation, by its very nature, influences the performance of regulated suppliers. In this respect, information disclosure regulation not only contributes to its specific purpose in s 53A; it can also indirectly promote the s 52A purpose by improving the distribution of existing information between regulated suppliers and interested persons, as well as in some cases expanding the information available to regulated suppliers themselves.
- 49 Placing information and analysis about the regulated suppliers into the public domain can provide some of the incentives found in competitive markets - for example, by providing:
- better information to consumers and other interested persons, including on the extent to which efficiency gains have been shared with consumers through lower prices or other means (consistent with s 52A(1)(c)). Doing so is likely to enhance consumers' countervailing market power, thereby assisting in limiting excessive profits (consistent with s 52A(1)(d)), as well as in facilitating consumer engagement with regulated suppliers about the desired level of service quality (consistent with s 52A(1)(b));
  - better information to the owners of regulated suppliers in some cases, for example where information disclosure allows comparisons with suppliers in other areas, facilitating more effective governance and helping them identify opportunities for value-enhancing trade in assets used to supply regulated services (e.g., consolidation of businesses), management contracting and so on, thereby promoting incentives for improved efficiency (including efficient investment) and innovation (consistent with s 52A(1)(a) and (b)); and
  - potentially increased incentives for the management of regulated suppliers to improve relative and absolute performance, both through the ability of interested persons to make comparisons and the public nature of the performance measures, similarly promoting incentives for improved efficiency (including efficient investment) and innovation.
- 50 In addition, the data and information that this type of regulation provides - where it has already been provided consistent with those purposes - can be utilised by the Commission in making determinations in respect of the other regulatory instruments. Doing so will improve the cost-effectiveness of implementing the Part 4 regulatory regime, and may reduce the need for the Commission to rely on its other information gathering powers under s 53ZD and s 98.



### 2.2.2 *Definition of Interested Persons*

- 51 Given that the purpose of information disclosure regulation is to ensure that sufficient information is readily available to interested persons to assess whether the purpose of Part 4 is being met, it is important to have clarity as to who are 'interested persons'.
- 52 Wellington International Airport Limited (WIAL) suggested in its submission on the Provisions Paper that the term 'interested persons' does not include the Commission.<sup>6</sup>
- 53 The term 'interested persons' is not defined in the Act. It is the Commission's preliminary view that the term is, therefore, broad in its application and includes all persons that are interested in the activities of a regulated supplier. This may include, but is not limited to, consumers, suppliers and owners of the regulated supplier, regulatory bodies (including the Commission) and any other stakeholder of the regulated supplier. The Commission is an 'interested person' because it uses disclosed information in meeting its summary and analysis obligations as outlined in paragraph 47 above, and because it uses this information to inform the development of default price-quality paths.

Q.2) Do you agree that the term 'interested persons' is broad in its application and includes all persons that are interested in the activities of a regulated supplier? If not, please provide the reasons for your view, an alternative interpretation and why you consider this to be more appropriate.

### 2.2.3 *Other Mandatory Considerations*

- 54 Appendix B outlines the statutory provisions in Part 4 of the Act relating to information disclosure regulation other than the purpose provisions discussed above. The first part of the appendix discusses the provisions that are common to all services that are subject to information disclosure regulation. The second part discusses the provisions that apply to particular types of regulated services.
- 55 In addition to the provisions in Part 4, section 26 of the Act provides that the Commission, when exercising its powers under the Act, shall have regard to the Government's economic policies transmitted in writing from time to time to the Commission by the relevant Minister. The Government has transmitted three statements of economic policy to the Commission pursuant to s 26 of the Act that are relevant to the exercise of the Commission's powers under Part 4 and are currently in effect, being:
- the Government's Policy Statement on Electricity Governance, transmitted to the Commission in May 2009 (the May 2009 GPS);<sup>7</sup>

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<sup>6</sup> Wellington International Airport Limited, *Submission to the Commerce Commission on the Commerce Act 1986*, 20 February 2009, page 78.

<sup>7</sup> New Zealand Government, *Government Policy Statement on Electricity Governance*, (New Zealand

- the Government's Policy Statement on Gas Governance, provided to the Commission in April 2008 (the April 2008 GPS);<sup>8</sup> and
- the Government's Policy Statement: Incentives of Regulated Businesses to Invest in Infrastructure, provided to the Commission in August 2006 (the 2006 GPS).<sup>9</sup>

56 The 2006 GPS states that the Government's economic policy objective is for regulated businesses to have incentives to invest in replacement, upgraded and new infrastructure and in related businesses for the long-term benefit of consumers. This objective will be achieved by: (a) regulatory stability, transparency and certainty giving businesses the confidence to make long-life investments; (b) regulated rates of return being commercially realistic and taking full account of the long-term risks to consumers of under-investment in basic infrastructure; and (c) regulated businesses being confident they will not be disadvantaged in their regulated businesses if they invest in other infrastructure and services.

57 The 2006 GPS also states that it is important regulatory control ensures that: (a) the consumers of regulated businesses are not disadvantaged by the investments of regulated businesses in other infrastructure and services; (b) regulated businesses are held accountable for making investments in that business where those investments have been provided for in regulated revenues and prices; and (c) regulated businesses provide infrastructure at the quality required by consumers at an efficient price.

### 2.3 INFORMATION DISCLOSURE FRAMEWORK

58 In response to submissions on the Provisions Paper requesting a clear link from information required under the disclosure requirements to the purpose of information disclosure regulation, the Commission sets out below an information disclosure framework which outlines how the information disclosure requirements will be linked to the purpose of information disclosure.

59 As outlined above, the purpose of information disclosure requires that sufficient information is readily available to interested persons to assess whether the purpose of Part 4 is being met.

60 Part 4 is concerned with objectives related to specific activities and the assessment of whether the objectives of Part 4 are being met. Interested persons require information regarding those specific activities. Accordingly, it is unavoidable that

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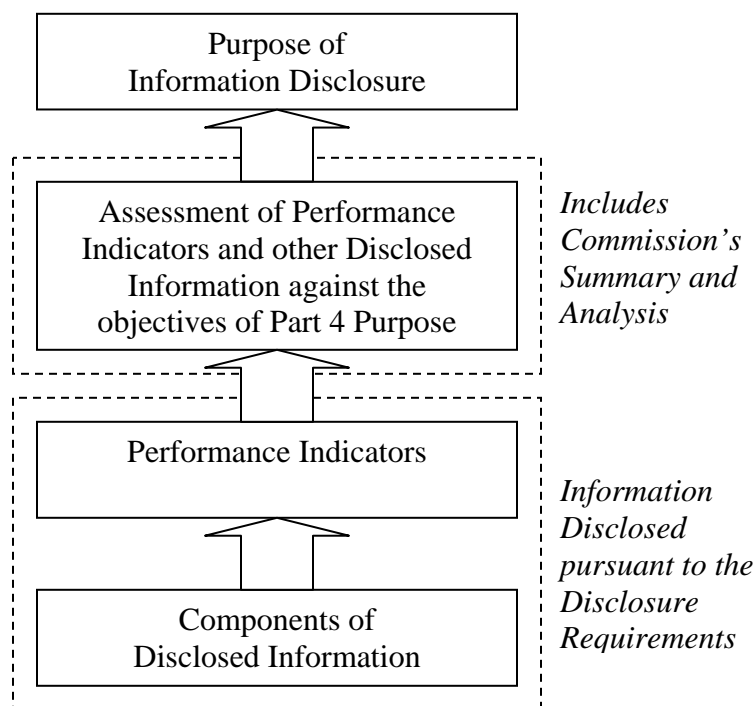
Government May 2009 GPS) May 2009.

<sup>8</sup> New Zealand Government, Government Policy Statement on Gas Governance, (New Zealand Government April 2008 GPS), April 2008.

<sup>9</sup> New Zealand Government, Statement to the Commerce Commission of economic policy of the Government: Incentives of regulated businesses to invest in infrastructure, (New Zealand Government 2006 GPS) 7 August 2006. Although this GPS will need updating to reflect the passage of the CAA, the principles still apply in the meantime.

the firms or other entities which are engaged in those activities will be required to report on those activities separate from any other activities that the same firms may engage in. Thus it is unavoidable that such firms will be required to produce information that is specific to the activities covered by Part 4 with this information in most cases being additional to the information required by other disclosure requirements such as those relating to listed companies.

- 61 The information disclosed regarding activities covered by Part 4 will be available for interested persons to analyse in the ways they find are most useful for assessing the extent to which the performance of the activities is in accordance with the objectives which Part 4 seeks to promote.
- 62 The Commission's preliminary view is that requiring disclosure of certain pre-prescribed performance indicators will assist interested persons in the assessment as to whether the purpose of Part 4 is being met. The intention of the proposed performance indicators, as outlined in Chapter 3, is to indicate whether the objectives of Part 4 as outlined in s 52A(1)(a)-(d) are being met. The Commission recognises that the assessment will not be limited to these indicators.
- 63 Components of disclosed information (Chapters 5 to 9), which should be sufficiently detailed to allow for the computation of the required performance indicators, allow a adequate assessment of the purpose of Part 4. The Commission notes that a performance indicator indicating whether the purpose of Part 4 is being met may not be objectively determinable by regulated entities in some instances. In these instances sufficient information should be disclosed so that the Commission can publish a summary and analysis of that information.
- 64 As outlined in s 53B(2)(b), the purpose of the summary and analysis is to promote greater understanding of the performance of individual regulated suppliers, their relative performance, and the changes in performance over time. The Commission envisages that this will be achieved by publishing the above mentioned performance indicators of each regulated supplier in a combined report (being a summary of individual regulated suppliers performance) and analysing these indicators as well as other relevant information.
- 65 As discussed further in paragraphs 106 and 107, the analysis of those performance indicators is required to make a rounded assessment of overall performance, as a definitive assessment of performance is not possible from the performance indicators alone.
- 66 The summary and analysis will also play a key role in making information more understandable by consolidating information where indicators of performance are not able to be objectively determined by the regulated entities. As an example, paragraphs 119 to 121 outline in further detail how the Commission proposes reviewing Asset Management Plan (AMP) information and publishing ratings as performance indicators on such things as investments and innovation.

**Figure 1: Information Disclosure Framework**

Q.3) Do you agree that pre-prescribed performance indicators will assist interested persons in the assessment as to whether the purpose of Part 4 is being met? If not, please provide the reasons for your view, an alternative approach and why you consider this to be more appropriate.

## 2.4 PRINCIPLES OF INFORMATION DISCLOSURE

67 In the Input Methodologies Discussion Paper, the Commission identified a number of principles that it considers relevant to the implementation of Part 4. These principles are intended to assist the Commission to meet the four objectives specified in s 52A(1)(a) to (d) of the Part 4 purpose statement and, ultimately, to promote outcomes consistent with those in competitive markets, for the long-term benefit of consumers. This section summarises the Commission's preliminary views on the way the economic and implementation principles are relevant for guiding decisions relating to information disclosure regulation in particular.

### 2.4.1 Economic Principles

68 As outlined in the Input Methodologies Discussion Paper, in undertaking its functions under Part 4 of the Act, the Commission considers that there are three key economic principles which stem from the three dimensions of economic efficiency. These are that decisions should:

- promote allocative efficiency, subject to the opportunity for regulated businesses to earn normal returns;

- promote realistic and achievable gains in productive efficiency; and
  - promote dynamic efficiency by providing incentives for efficient investment and innovation.<sup>10</sup>
- 69 While these economic principles are very important to price-quality regulation, they are only indirectly relevant to information disclosure regulation. This is because the economic principles are generally used to weigh up and consider the various ways that appropriate incentives could be directly provided. As noted above, the incentives provided under information disclosure regulation are indirect. Information disclosure indicators must instead be predicated on the extent to which they allow interested persons to assess whether the purpose of Part 4 is being met.
- 70 The three dimensions of efficiency are relevant to the extent that they are helpful in framing the assessment around whether or not outcomes are improving for consumers over time. In particular, whether or not the supply of regulated services is becoming more efficient, and thus whether the purpose of Part 4 and the associated objectives in s 52A(1)(a) to (d), are being met over time.

#### *Normal Returns and Financial Capital Maintenance*

- 71 In the context of price-quality regulation, it is possible to guide decision-making by relying on the concept that regulated suppliers should expect to earn a normal rate of return over time. As noted in the Input Methodologies Discussion Paper, this is a concept that is consistent with the three economic principles.<sup>11</sup>
- 72 In the context of information disclosure, the concept of a normal return is only relevant in so far as it helps interested persons to assess whether or not the purpose of Part 4 is being met. For example, it informs how the value of the regulatory asset base (RAB) should be rolled forward, and how changes in asset value should be included in the measurement of returns. In this respect, the concept is important when making assessment of financial performance measures relating to profitability, such as Return on Investment (ROI). The ROI assists interested persons in monitoring, on an ex-post basis, the extent to which financial capital is being maintained, through comparison to an appropriate cost of capital. Note that due to the similarity between the concept of normal returns and the related concept of Financial Capital Maintenance (FCM), the two terms are often used interchangeably.

#### **2.4.2 Implementation Principles**

- 73 In the Input Methodologies Discussion Paper, the Commission also identified four implementation principles, which are that regulatory decisions should be made with the following principles in mind:
- Consistency;

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<sup>10</sup> Supra n 2, paragraph 2.29-2.59.

<sup>11</sup> Ibid., paragraph 4.12.

- Transparency;
- Cost-effectiveness; and
- Flexibility.

74 A key concern for information disclosure regulation is that the information disclosed is useful to interested persons. It must therefore be understandable, relevant, reliable and comparable across suppliers provided comparability can be achieved without imposing undue cost. The application of the implementation principles to information disclosure is intended to ensure this is achieved, as discussed below.

#### *Consistency*

- 75 Information will be of most use to interested persons if it allows comparisons to be drawn between suppliers and over time (i.e., that it is ‘comparable’), which requires that disclosures are made on a consistent basis. This is particularly the case where suppliers within the same sector may have different characteristics, and it is important to be able to ensure consistency in the analysis wherever possible.
- 76 Comparability and consistency are required to the extent necessary to allow interested persons to assess whether the purpose of Part 4 is being met, which is informed by the Commission’s analysis of relative supplier performance and of supplier performance over time.
- 77 Comparability will be assisted by ensuring that information disclosure determinations are prescribed in sufficient detail to result in a basis for comparison. Higher level determinations would give greater scope for differences in application.
- 78 In applying the consistency principle the Commission also intends having consideration to materiality and disclosures made under previous regimes. Materiality is closely related to the cost-effective principle (as outlined below). If consistency can be achieved with disclosures made under previous regimes the data set from those disclosures can be used in future assessments.
- 79 There were varying views expressed in submissions as to how prescriptive information disclosure should be. The Board of Airline Representatives (BARNZ) in its submission on the Provisions Paper noted that it considers a detailed level of prescription and specified presentation requirements will make it easier for the Commission and users to assess the disclosed information and will facilitate inter-firm comparisons.<sup>12</sup> Whereas Christchurch International Airport Limited (CIAL) noted that information disclosure requirements should be held at a minimum level in terms of prescription and detail.<sup>13</sup>

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<sup>12</sup> BARNZ, *Submission on Discussion Paper by Commerce Commission on Regulatory Provisions of the Commerce Act 1986*, 16 February 2009, page 29.

<sup>13</sup> Christchurch International Airport Limited, *Response to Commerce Commission Discussion Paper*, 19 December 2008, page 28.

- 80 The Commission's preliminary view is that consistency is an important principle to ensure that suppliers in similar circumstances are treated the same way over time. Consistency will also allow comparable disclosures between regulated business units and over time, which implies that as far as possible, the requirements should be consistent with previous requirements set by the Commission. In addition, prescriptive requirements may be needed to ensure consistent disclosure. The Commission notes that consistency is only desirable in so far as it is achieved in a cost-effective manner.

#### *Flexibility*

- 81 The development of prescriptive disclosure requirements to allow for comparability also needs to be balanced with providing for sufficient flexibility to allow regulated entities to disclose a fair reflection of their performance. This is a factor that should inform the design of appropriate indicators. The Commission intends to consult with interested parties to identify where the proposed requirements may hinder the disclosure of actual outcomes.

#### *Transparency*

- 82 Transparency is a key principle for information disclosure regulation. It is an essential part of allowing interested persons to make an assessment as to whether the purpose of Part 4 is being met. There are two main reasons for this. First, the rationale for including certain indicators must be clearly explained. Second, the information must be disclosed in a way that is easy for interested persons to understand. The Commission's summary and analysis is an important part of this.

#### *Cost-Effectiveness*

- 83 Various submissions on the Provisions Paper noted that the Commission should have regard to the cost of compliance when developing the information disclosure regime. Vector considered that information should be disclosed only where the costs of compliance are clearly outweighed by the benefits of disclosure.<sup>14</sup>
- 84 The Commission agrees, subject to compliance with the Act. The Commission notes that in some instances the purpose of information disclosure regulation requires that information be disclosed despite such information imposing additional costs. For example, Part 4 regulates the business unit as opposed to the entity. Therefore information on the regulated business unit is required to be extracted from the entity's financial information. If this were not done, it would be almost impossible for interested persons to assess whether the purpose of Part 4 is being met.
- 85 On the other hand, the Commission appreciates that information disclosure regulation is intended to be a relatively light-handed and cost-effective type of regulation. Therefore, the cost of compliance is an important consideration when

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<sup>14</sup> Vector Limited, *Regulatory Provisions of the Commerce Act 1986: Response to Discussion Paper*, 16 February 2009, paragraph 98.

establishing the disclosure requirements. The Commission, throughout this paper, has indicated where information should be readily available (either from financial records or other means) versus where information may be required to be developed.

- 86 The Commission also notes that it is difficult to perform a meaningful quantitative cost-benefit analysis in most instances due to actual costs and benefits being difficult to determine and the Commission's access to information regarding costs. In these instances the Commission welcomes submissions on the costs and benefits of disclosures, with the use of approximations where required.
- 87 Throughout this paper, the Commission has identified indicators that it believes would be readily available to suppliers that are operating in an efficient manner. However, there are some instances in which the disclosure of certain information would imply additional costs, even for efficient suppliers. In these cases, requirements have only been proposed to the extent that they are considered to be required to allow interested persons to assess whether the purpose of Part 4 is being met.

Q.4) Do you agree that these principles are consistent with the purpose of information disclosure which is to ensure that sufficient information is readily available to interested persons to assess whether the purpose of Part 4 is being met? If not, please provide the reasons for your view, alternative principles and why you consider these are better aligned to the purpose of information disclosure.

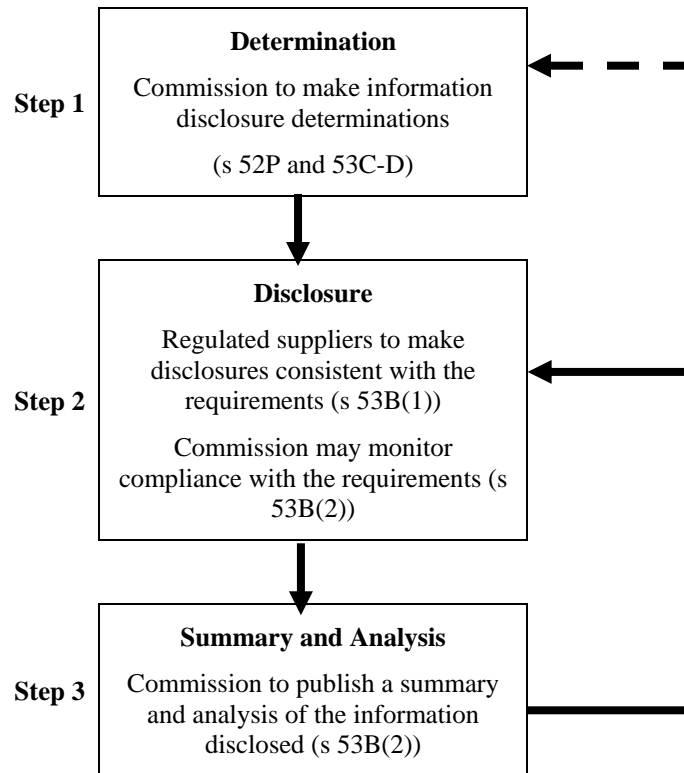
## **2.5 INFORMATION DISCLOSURE PROCESS**

- 88 Sections 54I(1), 55E(1) and 56E require the Commission to make s 52P determinations that specify how information disclosure regulation applies to each supplier of regulated services.
- 89 Section 53B(1) requires the regulated suppliers that are subject to information disclosure to publicly disclose information in accordance with the information disclosure requirements and supply the Commission with a copy. Section 53B(2)(a) provides the Commission with the ability to monitor and analyse information disclosed.
- 90 Section 53B(2)(b) requires the Commission to publish a summary and analysis of the information that is publicly disclosed. As mentioned above, the purpose of the summary and analysis is to promote greater understanding of the performance of individual regulated suppliers, their relative performance, and the changes in performance over time.



91 Figure 2 below outlines the information disclosure regime under Part 4:

**Figure 2: Information Disclosure Process**



92 The information disclosure process is a cycle, whereby each year information is disclosed and a summary and analysis is published. From time to time the Commission may choose to revisit the determination, based on things learnt through the disclosure or summary and analysis process. This allows information disclosure to continue to be relevant to the changing environment.

## 2.6 RELATIONSHIP WITH INPUT METHODOLOGIES

93 Input methodology determinations are published in accordance with s 52W of the Act. They will contain the relevant methodologies, processes, rules and matters applicable to the particular sector, according to the type of regulation. Initially, input methodology determinations are required to be made only for those services already subject to regulation under Part 4. Section 52U provides that the Commission must determine these input methodologies no later than 30 June 2010, although there is provision for an extension of up to six months to be provided by the Minister of Commerce.

94 Among other things, s 52S specifies that the Commission, in deciding or determining how regulation under Part 4 should apply to regulated services, must apply every relevant input methodology (that has already been published for the relevant regulated services in accordance with s 52W). In addition, s 52S requires regulated suppliers to apply every relevant input methodology in accordance with the relevant s 52P determination.

- 95 Table 3 identifies those input methodologies that are applicable to information disclosure determinations. Chapters 5 and 6 provide further details on the input methodologies that are applicable to information disclosure regulation.

**Table 3: Summary of Input Methodologies Applicable to Information Disclosure Determinations**

	<b>Information Disclosure</b>
<b>Cost of capital</b>	<b>x</b>
<b>Valuation of assets</b>	<b>✓</b>
<b>Allocation of common costs</b>	<b>✓</b>
<b>Treatment of taxation</b>	<b>✓</b>
<b>Pricing methodologies</b>	<b>x</b>
<b>Processes and rules</b>	<b>✓</b>
<b>Proposals for customised price-quality paths</b>	<b>x</b>

## CHAPTER 3: MONITORING PERFORMANCE

### 3.1 INTRODUCTION

- 96 The disclosure of information and the Commission's summary and analysis of that information provide the means by which the purpose of information disclosure regulation is to be achieved. In the first instance, this requires that the components of disclosed information (e.g., revenues and costs), be combined to produce a number of performance indicators (e.g., profitability). The Commission's summary and analysis supplements these indicators by providing greater narrative to explain the overall performance of regulated suppliers relative to each other and over time. This chapter provides an overview of the Commission's preliminary views on the assessment of performance.
- 97 Financial and non-financial 'performance measures' are an important part of the disclosure requirements, as provided for in s 53C(2)(f). However, the Commission notes that the term 'performance measures' is not particularly helpful, as it implies that a definitive assessment of performance is possible. The Commission's preliminary view is that this is not the case, owing to a myriad of factors other than those within the control of the regulated supplier that may affect performance.
- 98 Consequently, the Commission uses the term "performance indicator(s)" in recognition of this observation, to highlight that these are simply an indicator of performance and that further analysis is required to make a rounded assessment of overall performance. As with any analysis of the performance of regulated suppliers, the limitations associated with using 'snapshot' performance indicators must therefore be considered by interested persons when assessing whether the purpose of Part 4 is being met.
- 99 The Commission intends developing through consultation a number of key performance indicators to assist interested persons to assess whether the purpose of Part 4 is being met. Performance indicators provide a focus on those aspects of suppliers' performance that are most relevant to the purpose of Part 4, though they necessarily provide only summary information of a complex picture.
- 100 A larger range of indicators, in addition to those specified in this chapter, could be used to indicate performance. However, the Commission sees advantage in requiring the disclosure of a limited number of relatively easily understood and determined measures as a summary of performance.
- 101 Nevertheless, more complex performance indicators may be prepared by the Commission from the components of disclosed information during the summary and analysis phase, or by interested persons during their own analysis.

#### *3.1.1 Relationship with Commission's Summary and Analysis*

- 102 As soon as practicable after any information is publicly disclosed, the Commission must publish a summary and analysis of that information. This summary and analysis should not be considered to provide a complete evaluation of any individual supplier's performance. Rather, it is intended to promote greater

understanding of the performance of individual regulated suppliers, their relative performance, and the changes in performance over time.

- 103 In some sectors, summary and analysis will initially be confined to comparing performance indicators against certain benchmarks. For example, the Commission may use input methodologies for the cost of capital and pricing methodologies to monitor and analyse information. These metrics allow high level assessment to be made and more meaningful conclusions to be drawn. Indeed, though suppliers that are only subject to information disclosure regulation do not have to apply these two input methodologies, they may still be required to disclose information about the methodologies they use in their place. This is important, as summary and analysis should take a more rounded view, by trying to provide explanation for the trends that emerge.
- 104 Some elements of the summary and analysis will be possible only as more data becomes available, normalised where necessary (i.e., statistical error minimised) and once baselines have been set. This will allow the Commission to expand and deepen its analysis over time. It is very important to have consistent, good quality and reliable time-series data with statistical error minimised – for example, to undertake robust regression analysis to compare suppliers in different circumstances. This serves to reinforce the need to identify appropriate statistics and indicators from the outset.

### **3.2 MONITORING PERFORMANCE AND THE REGULATORY OBJECTIVES**

- 105 If the regulatory objectives in s 52A(1)(a) to (d) are being achieved, then it is reasonable to conclude that outcomes consistent with those realised in competitive markets will result. Therefore, in the Commission's view, these regulatory objectives provide guidance on the aspects or areas of performance that performance indicators and other information disclosed under information disclosure regulation should cover. These areas of performance are:
- innovation and investment (s 52A(1)(a));
  - quality (s 52A(1)(b));
  - prices (s 52A(1)(c));
  - profits (s 52A(1)(d)); and
  - efficiency (s 52A(1)(b)), comprising the three dimensions of allocative, productive and dynamic efficiency (refer to paragraphs 68 to 70).
- 106 The Commission considers that it would be appropriate to require regulated suppliers to disclose performance indicators and supporting information relevant to each of these areas of performance, to the extent that doing so will assist interested persons in assessing whether the Part 4 purpose is being met. Importantly, no single indicator disclosed in a particular year will be sufficient to assess whether one or more of the regulatory objectives in (a) to (d) is being achieved. Indeed, in most cases, individual indicators may not be particularly meaningful on their own, as many are interrelated. For example, profits greater than normal returns may be

consistent with the long-term benefit of consumers for a regulated supplier that is highly efficient and innovative. On the other hand, the same level of profits might be deemed excessive for a comparatively inefficient regulated supplier that rarely innovates.

- 107 The regulatory objectives under s 52A(1)(a) to (d) also indicate how each of these performance areas are expected to change compared to present levels, in order to promote the benefit of consumers in the long term. For instance, over time, the changes required include quality that reflects consumer demands and for efficiency gains to be shared with consumers, including through lower prices. Given that performance indicators are likely to be disclosed by regulated suppliers on an annual basis, the Commission's summary and analysis will play an important role in assisting in the interpretation of those indicators over time. For example, a decrease in price might not be desirable if the trade-off is to provide the relevant service at a quality less than that which consumers' demand. It is therefore only by taking a more rounded view of the performance of regulated suppliers over time that interested persons will be able to make assessments of whether the regulatory objectives in s 52A(1)(a) to (d) are being achieved and whether the Part 4 purpose is being met.
- 108 The following sub-sections discuss the Commission's preliminary views on the indicators that are likely to be required to assess performance across the areas identified above.
- 109 The Commission has had experience with information disclosure regulation for electricity lines services under Part 4 of the Act. The performance indicators and components of disclosed information proposed for the purpose of Part 4 are based on this experience.

Q.5) What other areas of performance, if any, do you think the Commission should consider when assessing whether the purpose of Part 4 is being met? Please provide the reasons for your view.

### 3.3 INNOVATION AND INVESTMENT

- 110 Indicators relating to investment will be required to allow interested persons to assess whether regulated suppliers are undertaking an appropriate level of investment in replacement, upgraded and new assets. The Commission's preliminary view is that an indicator relating to capital expenditure relative to the size of the business is therefore appropriate.
- 111 An obvious ratio to use would be that of capital expenditure compared to the regulated asset base value:

$$\text{Capital Expenditure Ratio} = \frac{\text{Capital Expenditure}}{\text{Asset Base}}$$

112 In analysing this indicator, however, consideration should be given to other drivers of capital expenditure such as trade-offs with operational expenditure, asset age and demand, as changes in capital expenditure ratios can result from other influences.

Q.6) Do you agree that an indicator relating to investment is required? If not, please provide the reasons for your view.

Q.7) Do you believe that a capital expenditure ratio is an appropriate indicator? If not, please provide the reasons for your view, an alternative and explain why you consider this to be preferable.

113 The Commission's preliminary view is that there is advantage to further assessing capital expenditure on a renewal basis and a capital expenditure growth basis. The assessment of capital expenditure on this basis is similar to that which has been applied in the Electricity Distribution Businesses (EDBs) information disclosure regime.

$$\text{Renewal Ratio} = \frac{\text{Renewal Expenditure}}{\text{Depreciation}}$$

114 The renewal ratio would compare capital expenditure on renewal initiatives to depreciation. Depreciation is an accounting assessment of the value of the assets that have been utilised in supplying a service. Therefore an assessment of renewal expenditure to depreciation indicates whether the RAB is being replaced, from a value perspective, relative to its use. Where depreciation is greater than capital expenditure, this would imply that the capital stock is being depleted. Conversely, where capital expenditure exceeds depreciation, the capital stock is more likely to be increasing.

115 The regulated supplier may rightly choose to replace assets at a rate that is inconsistent with depreciation. Therefore any assessment of renewal expenditure needs to consider other factors such as asset age and condition, changes in quality performance and the suitability of the regulatory depreciation schedule as a measure of the amount of capital that is "used up" in each period.

$$\text{Capital Expenditure Growth Ratio} = \frac{\text{Capital Expenditure on Growth Initiatives}}{\text{Capacity Increases}}$$

116 An additional indicator that the Commission sees merit in is a comparison of capital expenditure on growth initiatives to capacity increases. The Commission understands that in each of the regulated services there may be a number of means to determine capacity and it intends selecting a single measure in each of the

regulated services to provide a single measurement of capital expenditure growth across suppliers. However, this will not preclude interested persons or the Commission during the summary and analysis phase using other ratios to assess capital growth expenditure where required.

- 117 Total capital expenditure is readily available information, in so far that it is information prepared for statutory financial reporting purposes. The separation of total capital expenditure into renewal, growth initiatives and other capital expenditure may require development. The disclosure of this information, however, is considered to be appropriate because it facilitates an assessment of the investment that is being undertaken. The assessment of total capital expenditure provides interested persons with only a limited understanding of regulated suppliers' investment initiatives and the ability to assess growth and renewal initiatives allows interested persons to determine whether regulated suppliers are making adequate investment in the appropriate areas. This is consistent with s 52A(1)(a), which specifically identifies replacement, upgrade and new assets as areas where regulated suppliers should have incentives to innovate and invest.
- 118 Capital expenditure ratios can be determined based on many different denominators and no one denominator is always ideal. The use of a ratio, and any particular denominator, is intended to provide a simple way of standardising for different factors. Thus, in some cases the size of the regulated business unit will be most appropriate, but this could be measured in a variety of ways, such as the size of the asset base or number of consumers. Therefore, the Commission's preliminary view is that other capital expenditure ratios such as capital expenditure per consumer, units supplied, maximum demand, capacity and other statistics should also be made available to interested persons, although not as key performance indicators. This is because these indicators are likely to be highly correlated with each other (since they are all intended to correct for business unit size) and therefore a high level assessment need only look at a smaller number of these indicators to get a high – level understanding of performance.

Q.8) Do you have any views on the Commission's proposed treatment of capital expenditure ratios under information disclosure? If so, please provide the reasons for your views.

- 119 Indicators are also required to assess whether the timing of investment is appropriate, though this is a particularly problematic undertaking. In most markets, competitive forces put pressure on firms to undertake investments at the socially optimal time. This relates to the concept of dynamic efficiency, which tends to be the most important but least well-defined dimension of efficiency. While this is difficult to assess accurately, indicators relating to the way in which suppliers plan their investments, and the timing of their investments, would be helpful to interested persons.
- 120 A key reason that AMPs should be disclosed is to allow regulated suppliers to demonstrate their approach to making investment decisions and to innovating. This is discussed in greater detail in Chapter 8. However, the Commission is mindful

that not all interested persons have the ability or the resources to assess from the AMP disclosures whether a regulated supplier is planning in a way that would suggest that it is investing efficiently and innovating. Therefore the Commission's preliminary view is that the Commission should undertake annually, as it has in previous years for EDBs, a review of the AMPs and publicly disclose the results of those reviews.

- 121 The AMP review performance indicator would be calculated by the Commission, on the basis of the quality of the investment planning contained within the AMP disclosed by the supplier. It is the Commission's preliminary view that the AMP review results would be made publicly available by the Commission through its summary and analysis report.
- 122 For EDBs, for which the specification in s 54Q on energy efficiency, demand-side management and loss reduction is applicable, the Commission's preliminary view is that each supplier should also disclose in their AMPs information on the initiatives it is taking to encourage energy efficiency, demand side management and loss reduction in the supply and demand of regulated services (refer paragraphs 438 and 439). It is the Commission's preliminary view that the Commission's AMP review should include a review of the initiatives for energy efficiency, demand-side management and loss reduction that the supplier has included in their disclosed AMP. Any results from such a review could be included in the Commission's summary and analysis as part of the key performance indicators.
- 123 The information that the Commission is proposing for disclosure in AMPs (refer Chapter 8) is information that should be readily available from the regulated suppliers' normal planning procedures. Therefore the cost of complying with the AMP disclosure requirements should be limited to the production of the information in a form consistent with the disclosure requirements. It is conceivable, however, that some regulated suppliers may be required to improve their planning procedures so that information is available for disclosure. The development of asset planning procedures would be consistent with the purpose of Part 4, in that regulated suppliers would be provided with incentives to improve efficiency, including to innovate and invest.

Q.9) Do you agree that the disclosure of an AMP is an appropriate means of demonstrating innovation and investment? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

- 124 Dynamic efficiency is, however, about much more than just incentivising efficient investment. It is also about the discovery, use and transmission of ideas and new information. In competitive markets, innovations that raise productivity above that previously possible are rewarded by greater than normal returns (at least in the short run). Suppliers of regulated services should also expect to earn a return on such innovations. It is very difficult, however, to replicate this sort of reward structure in a regulated market, due in part to the problems associated with identifying such innovations.



- 125 The Commission is not aware of any suitable quantifiable indicators for innovation. However, the Commission will be investigating this further and invites submissions on this issue, particularly suggestions for indicators that would be capable of demonstrating whether a supplier has a track record of innovation.

Q.10) Do you have any views on appropriate indicators for measuring innovation? If so, please provide the reasons for your views.

### 3.4 QUALITY

- 126 Quality indicators are required as an indicator of performance as interested persons must be able to assess whether regulated services are provided at a quality that reflects consumer demands. This is difficult to assess. While it is relatively straightforward to develop indicators to measure variations in service quality between suppliers and across time, it is more problematic to determine whether quality is in line with consumer preferences.
- 127 The Commission's preliminary view is that indicators are required for service quality disaggregated down to the individual service level, and that suppliers should demonstrate that they have taken consumer demand for service quality into account when formulating AMPs. This should be demonstrated to the extent practicable. For example, it may only be possible to involve the largest consumers in the planning for major investments.
- 128 The Commission considers that the assessment of quality demanded by consumers (hereafter 'requisite quality') to actual quality should be performed by the regulated business unit and disclosed as part of the AMP disclosures (refer paragraphs 373 to 375). However, as noted above, there is difficulty in ascertaining an objective performance indicator from regulated suppliers when the information is being collected by the regulated supplier in question. This is because assessing consumer preferences is a fairly complex undertaking, and is not easily observable. Therefore, the Commission's preliminary view is that in the initial stages the key quality performance indicator need only indicate actual quality. The Commission would then use the summary and analysis report, on the basis of information disclosed in the AMP, to assess whether adequate attempts have been made to try to take consumer preferences into account during investment planning.
- 129 The Commission's preliminary view is that the definition and assessment of quality is likely to be different for each of the different types of regulated services. This is because the dimensions of quality demanded by consumers will differ according to differences in the types of service being provided (e.g., airport services versus gas pipeline services). Thus the types of indicator are also likely to differ. For example, interruption statistics are likely to be a key focus for electricity lines services and gas pipeline services while survey data is more likely to be a good indicator of service quality for specified airport services. Therefore the Commission's preliminary view is that although quality indicators should be specified for all regulated services, the definition of quality and how it is assessed is likely to be different.

- 130 Paragraphs 381 to 401 outline in more detail the aspects of quality that may be relevant for the regulated services, while Chapters 11 to 14 discuss in more detail those aspects that are relevant to each of the regulated services and how they should be measured.

Q.11) Do you have any views on appropriate indicators for measuring quality? If so, please provide the reasons for your views.

### 3.5 PROFITS

- 131 In regulated markets, it is important that suppliers have the opportunity to earn a normal rate of return. Thus, the Commission's preliminary view is that an indicator that provides a measure of the profitability of regulated suppliers is necessary to allow interested persons to assess whether a supplier's behaviour is consistent with the purpose of Part 4.
- 132 The Commission's preliminary view is that a Return on Investment (ROI) performance indicator should be used as the basis to assess profits. The equation for calculating the ROI is:

$$\text{Return On Investment} = \frac{\text{Regulatory Profit}}{\text{Asset Base}}$$

- 133 Chapter 4 outlines in detail the Commission's preliminary view on how the ROI should be calculated in order to accurately assess whether suppliers are earning a return broadly in line with their Weighted Average Cost of Capital (i.e., their WACC) over time. This allows interested persons to assess whether the profitability of suppliers is broadly in line with a normal rate of return.
- 134 As is discussed in the Input Methodologies Discussion Paper, just because a firm is earning more than a normal return in the short term does not necessarily mean that those higher returns are all so-called 'functionless' monopoly rents (i.e., profits that are not associated with promoting efficiency).<sup>15</sup> As the High Court has observed, supra-normal profits that arise from cost savings or innovation are not considered functionless.<sup>16</sup> Greater profit levels may actually reflect temporarily superior performance in terms of productive and/or dynamic efficiency improvements. However, in a competitive market such profits would be only temporary, because other firms will improve performance and curtail the competitive advantage enjoyed by market leaders.

<sup>15</sup> Supra n 2, paragraphs 2.34-2.35.

<sup>16</sup> *Telecom Corporation of New Zealand Ltd v Commerce Commission* [1992] NZAR 193 (HC). Referenced in Commerce Commission, *Input Methodologies Discussion Paper*, 19 June 2009, paragraph 2.34.

- 135 This indicator can also reveal where a regulated business unit is not earning a sufficient return, and may therefore be discouraged from investing. Care is required when making any such assessment as a low ROI may result from a number of factors and these all need to be considered (e.g., economic conditions or supplier performance). One of those factors may be annual fluctuations due to changes in inputs in the calculation such as operational expenditure.
- 136 In addition, there are annual fluctuations in the ROI due to changes in inputs in the calculation such as operational expenditure.
- 137 Where possible, the information used in calculating the ROI is based on information that is developed for statutory financial reporting purposes, albeit that it relates only to the regulated business unit and not the entity (as discussed in paragraph 84). Also, the calculation of regulatory profit and the RAB, for the purposes the ROI, includes various adjustments so that the ROI is aligned with the specification of the WACC. The calculation of the ROI is discussed in detail in Chapter 4.

Q.12) Do you have any views on appropriate indicators for measuring profits? If so, please provide the reasons for your views.

### 3.6 PRICES

- 138 A key feature of competitive markets is that they tend to allocate resources to their most valuable uses within the economy. Since prices provide the information that conveys the relative value of various goods and services throughout society, allocative efficiency is therefore usually associated with “pricing efficiency”.
- 139 As is discussed in the Input Methodologies Discussion Paper, allocative efficiency is more dependent on individual price levels and structure than on overall revenue - consumers respond to the prices that they face, rather than to the revenues that firms make.<sup>17</sup> Interested persons should therefore be able to assess whether suppliers are setting efficient relative prices for different consumer groups, individual services or price components. This assessment must also consider whether the service being supplied reflects the service quality that consumers demand.
- 140 As far as practicable, the consumers that bear costs should be the same as those that cause them, or - where costs cannot be directly attributed - they should be paid for by those that are most willing to do so.<sup>18</sup> The Commission’s preliminary view is therefore that performance indicators should be required to assess the efficiency of the prices charged by suppliers for particular services, consumer classes and across geographic areas.
- 141 For interested persons to assess if there is efficient pricing across different consumer groups, ideally an understanding of the prices and costs across consumer groups and products/services would be assessed. Practically this can be difficult

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<sup>17</sup> Supra n 2, paragraph 2.42.

<sup>18</sup> Ibid., paragraph 2.43.

where cost or price information per consumer group or service is not readily available. Therefore analysts may use only price information or even an estimation of price so as to get an indicator of pricing efficiency across consumer groups. Importantly, at some point the cost of collecting information outweighs the benefit of making the information available.

- 142 The Commission is mindful that the assessment of pricing efficiency between all consumer groups is difficult to consolidate into a single measure. Therefore the Commission's preliminary view is that the most effective measure of pricing efficiency for each regulated service should be presented as the key indicator, and that information be made available so that interested persons can assess other consumer groups as required.
- 143 The Commission's preliminary view is that the relative price index measurement used to assess the price variance between consumer groups in the Part 4A EDB information disclosure regime is an effective means of assessing relative pricing. This is because it provides an indication of the range of price differentiation, and should be used where an assessment of allocative efficiency between customer groups is performed.
- 144 The Commission's preliminary view of what information should be made available for the assessment of prices for EDBs, Transpower, gas pipeline services and specified airport services is outlined in further detail in Chapters 11 to 14.

Q.13) Do you have any views on appropriate indicators for measuring pricing efficiency? If so, please provide the reasons for your views.

### 3.7 EFFICIENCY

- 145 The Commission considers that efficiency relates to the economic principles outlined in paragraphs 68 to 70. As such, all proposed performance indicators are relevant to one or more dimensions of efficiency (e.g. profitability relates to allocative and dynamic efficiency). However, there are some issues that relate to broader efficiency considerations than simply prices, quality, profitability and innovation.
- 146 For example, suppliers should be expected to minimise their costs in an efficient manner, while maintaining a level of quality commensurate with that demanded by consumers. The Commission therefore considers that a number of cost-based indicators will be required to allow interested persons to assess whether regulated suppliers have taken action to minimise their costs, for a given level of quality (i.e., cost minimisation should not simply be to the detriment of the quality demanded by consumers).

Q.14) Do you have any views on the appropriate cost based indicators to assess whether regulated suppliers have taken action to minimise costs? If so, please provide the reasons for your views.

- 147 As with capital expenditure, it is important to assess whether operating expenditure levels are efficient. For this reason, the Commission's preliminary view is that an

indicator relating to operating expenditure is required, and should be expressed relative to the value of the RAB to allow comparisons to be made across suppliers of different sizes and across time as the size of an individual supplier changes.

$$\text{Operational Expenditure Ratio} = \frac{\text{Operational Expenditure}}{\text{Asset Base}}$$

- 148 Operational expenditure ratios can be an indicator that a regulated supplier is reducing its operating costs compared to its outputs or other statistics. Productive efficiencies are unlikely to be the sole driver of operational expenditure ratio changes, therefore consideration of other factors affecting the ratio, such as changes in input costs, should be considered when utilising an operational expenditure ratio in assessing operating expenditure efficiency over time.
- 149 The Commission's preliminary view is that, in the first instance, more detail could be provided to interested persons by disaggregating the components of operating expenditure down further (e.g., into overhead and maintenance expenditure). These could then be compared to the RAB value to allow comparisons to be made.

$$\text{Overhead Operational Expenditure Ratio} = \frac{\text{Overhead Operational Expenditure}}{\text{Asset Base}}$$

$$\text{Maintenance Operational Expenditure Ratio} = \frac{\text{Maintenance Operational Expenditure}}{\text{Asset Base}}$$

- 150 The key performance indicators should include an indicator of aggregate operational expenditure and assessments of overhead and maintenance operational expenditure. The assessment of overhead expenditure, separately from total operational expenditure, allows interested persons to assess the operating costs of managing the businesses separate from the assessment of maintenance expenditure, which is more appropriately considered alongside the capital expenditure ratios (owing to the relationship between the expenditure streams).
- 151 The proposed operational expenditure ratio is not the sole measure of efficiency of operating expenditure and any analysis should also take into account other indicators. This would include consideration of the capital expenditure ratio (refer paragraphs 110 to 112) and other capital and operational expenditure ratios.

Therefore the Commission's preliminary view is that other operational expenditure ratios such as operational expenditure per customer, units supplied, maximum demand, capacity and other statistics should be made available to interested persons, although not necessarily as a key performance indicator.

- 152 As with capital expenditure, total operational expenditure is readily available information, in so far that it is information prepared for statutory financial reporting purposes. The separation of total operational expenditure into overhead, maintenance and other operational expenditure categories may, however, require development. The Commission acknowledges that the development of this information may imply additional costs for suppliers. However, the Commission considers that the information is required for interested persons to gain a more complete understanding of the categories of expenditure in which regulated suppliers behave efficiently (or inefficiently as the case may be). This is an important step towards assessing whether the purpose of Part 4 is being met.

Q.15) Do you have any views on the Commission's proposed treatment of operational expenditure ratios under information disclosure? If so, please provide the reasons for your views.

- 153 An additional efficiency consideration for interested persons relates to the extent to which capacity is being appropriately installed and utilised by suppliers. This is because it is important that suppliers do not over- or under-invest in spare capacity. For example, excess capacity that is not necessary would be inefficient, as would under-investment and the possibility of reductions in quality. It may be inappropriate to assess capacity utilisation across regulated suppliers due to specific characteristics of each of the regulated suppliers. Nevertheless, an assessment of capacity utilisation over time can be an indicator of efficiency over the longer term.
- 154 In assessing capacity utilisation, consideration should be given not only to the total volume flowing through the system but also the
- peak demand at any given point in time; and
  - potentially the non-coincident sum of maximum demand.
- 155 An example of where non-coincident sum of maximum demand is used is for EDBs. Non-coincident system sum of maximum demand means the sum of anytime demands (that is, the diversified demands) of a group of assets or connection points which may be determined by adding directly measured system metered demands and connection point metered demands at different times. The use of non-coincident sum of maximum demand may not be relevant for specified airport services as demand on the various parts of airport assets is not non-coincident.
- 156 The use of capacity utilisation ratios for the purposes of assessing productive efficiency needs also to consider factors that are outside the control of the regulated supplier such as fluctuations in demand that were not foreseeable within the

investment timeframe, which the Commission may consider during the summary and analysis phase.

- 157 The information required to determine capacity utilisation should be readily available to regulated suppliers that are acting efficiently, as it is required to ensure that capital expenditure is undertaken at the appropriate time. Additional cost, however, may be incurred when capacity utilisation calculations are required in a form that is not consistent with a regulated business unit's normal internal capacity utilisation calculation.<sup>19</sup>

Q.16) Do you have any views on the Commission's proposed treatment of capacity utilisation ratios under information disclosure? If so, please provide the reasons for your views.

### 3.8 SUMMARY OF PRELIMINARY VIEWS

- 158 The Commission's preliminary list of key performance indicators to be disclosed by regulated suppliers annually in respect of each type of regulated service that they supply is outlined in Table 4 below. It is the Commission's preliminary view that the performance indicators should be disclosed as a distinct part of a regulated supplier's disclosures, to highlight the indicators to interested persons.
- 159 Table 4 also outlines the key areas of performance referred to in the Part 4 purpose statement and the dimensions of efficiency to which the performance indicators relate, as well as the components of disclosed information that make up the performance indicator. It is noted that other components of disclosed information (such as statistics, pricing disclosures, pricing methodologies and contracts) will inform an assessment of whether the purpose of Part 4 is being met. However, these have not been included in the table as they are not part of the performance indicator.
- 160 As noted above, these indicators are intended to provide a rounded picture of the performance of regulated suppliers, when taken together as a package.

**Table 4: Annual Performance Indicators**

Part of Purpose	Key Performance Areas	Performance Indicator	Component of Disclosed Information
52A(1)(a)	Innovation and investment	AMP Review Rating – Innovation and Investment	AMP
		Capital Expenditure Ratios	Financial, Asset Valuation and Statistics

<sup>19</sup> The disclosure of capacity utilisation in a form different to that of the regulated businesses' internal calculation of capacity utilisation may be required to enhance transparency and comparability over time and between regulated suppliers.

<b>Part of Purpose</b>	<b>Key Performance Areas</b>	<b>Performance Indicator</b>	<b>Component of Disclosed Information</b>
52A(1)(b)	Efficiency	Operational Expenditure Ratios	Financial, Asset Valuation and Statistics
		Capacity Utilisation	Statistics
		Consumer Group Price or Average Revenue Information	Financial and Statistics
	Quality	AMP Review Rating - Quality	AMP and Quality Measures
		Service Specific Measures	Quality Disclosures
52A(1)(c)	Prices	ROI	Financial and Asset Valuation
		Consumer Group or Activity Price Information	Financial and Statistics
52A(1)(d)	Profits	ROI	Financial and Asset Valuation



## CHAPTER 4: RETURN ON INVESTMENT (ROI)

### 4.1 INTRODUCTION

- 161 Various measures of financial performance have been considered, and while they all have their merits and limitations, the advantage of using the ROI is that it is the annual measure that is most comparable to the regulatory cost of capital, being the WACC.<sup>20</sup> This allows interested persons to assess whether profits are broadly in line with a normal economic return over time (i.e., it facilitates a relatively straightforward and transparent way to assess whether financial capital is being maintained). In addition, since it is comparable to the WACC, the ROI measure is consistent with the approach taken across regulatory instruments. For example, performance relative to a price-quality path can be more easily evaluated, since that price-quality path would be initially determined with reference to the WACC.
- 162 The basic ROI formula introduced in paragraph 132 is as follows:

$$\text{Return On Investment} = \frac{\text{Regulatory Profit}}{\text{Asset Base}}$$

- 163 The proposed ROI calculation for information disclosure as outlined in paragraphs 204 and 205 is an adaptation of the basic formula which, alongside the definition of Regulatory Profit and the total RAB, accommodates the key matters for consideration as outlined in this chapter, starting at paragraph 167.
- 164 As discussed in the Input Methodologies Discussion Paper, it is important to note that any annual estimate of returns such as that above can only ever be an approximation to proper measures of the economic returns of an investment over time, such as the internal rate of return (IRR).<sup>21</sup> A key pre-condition for accounting-based measures of profit to be approximated to the IRR is that, unlike under GAAP, all changes in asset value (including revaluation gains and losses) must flow through the profit and loss account.<sup>22</sup>
- 165 Any analysis of the profitability of regulated suppliers will almost inevitably be over a shorter time period than the economic lifetimes of the assets involved, and will have to primarily rely on accounting-based rather than economic-based data (particularly in respect of asset values).<sup>23</sup> As a result, the differences between

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<sup>20</sup> Supra n 2, paragraph 8.20.

<sup>21</sup> Ibid., paragraphs 4.56.

<sup>22</sup> J. Edwards, J. Kay and C. Mayer, *The Economic Analysis of Accounting Profitability*, Clarendon Press, Oxford, 1987, pp. 12-31.

<sup>23</sup> Internal Rate of Return (IRR) calculations are more correctly performed on a lifetime and cash-flow basis. Accounting-based measures are typically not cash-based. For example, accounting tax expense may differ significantly from actual tax paid, and more generally, many accounting

accounting-based measures of profitability and the economic IRR will differ markedly depending on the degree of fluctuations in the underlying asset values during the period of assessment – especially if that period is only a single year.

- 166 Consequently, by being able to take a longer term view, the Commission's published summary and analysis of disclosed information will play an important role. The Commission will be able to analyse the changes in disclosed ROIs over time, in light of changes in relevant disclosures relating to efficiency, in order to assist interested persons in assessing whether excessive profits are being limited, and whether financial capital is being maintained.

Q.17) Do you agree that profitability should be measured using an ROI measure? If not, please detail the measure that is appropriate and explain how that measure would better meet the purpose of information disclosure?

## 4.2 KEY MATTERS FOR CONSIDERATION

- 167 This section presents the Commission's preliminary views on how the ROI should be calculated. These preliminary views are consistent with the preliminary views in the Input Methodologies Discussion Paper; therefore if those views change following consultation, then there may be a corresponding change to the views expressed in this paper.

### 4.2.1 *Specification of ROI in a way that is comparable to the WACC*

- 168 The ROI must allow interested persons to assess whether suppliers of regulated services are earning a normal economic return over time. The ROI should therefore be specified in such a way that is comparable to the WACC. This requires that aspects of the RAB roll-forward methodology are incorporated into the definition of the ROI measure, so that profitability can be assessed appropriately. In particular:
- All non-financing income and expenditure (to the extent that it is efficient) needs to be accounted for, either through the definition of Regulatory Profit, or through movements in the RAB; and
  - Any non-cash items (including depreciation and revaluation gains/losses) must be accounted for, both in Regulatory Profit, and through movements in the RAB - that is, there must be full articulation for these items between the income and RAB statements.
- 169 Thus, changes in the value of the RAB must be reflected in the regulatory profit as income (if positive) or an expense (if negative), irrespective of whether the change is due to depreciation or revaluation. Including the movements in the asset values on the same basis in both the Regulatory Profit, and in the RAB, ensures that these movements are NPV neutral. This is required as it is important that the ROI indicator accurately reflects all returns earned by the supplier of regulated services, including those caused by changes in asset values.

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measures are accruals-based.

*Revaluations*

- 170 This treatment of revaluations for information disclosure is intended to ensure that the ROI more accurately reflects the overall return *on* capital that suppliers of regulated services are earning, which facilitates comparisons with the regulatory cost of capital. This is particularly important as the Commission's preliminary view, as outlined in the Input Methodologies Discussion Paper, is that for the majority of suppliers of regulated services (with the exception of Transpower), the initial RAB value should be rolled forward using CPI-indexation. For Transpower, an unindexed treatment is proposed.<sup>24</sup>
- 171 Unison submitted that the inclusion of revaluation gains in profit measures is confusing as it has no influence on prices, and disclosure of a commonly used measure of profit is better able to measure the ability to extract excessive profits.<sup>25</sup> As is discussed in more detail in the Input Methodologies Discussion Paper, the Commission acknowledges that revaluations cause difficulties for assessing annual ROI indicators and considers that the appropriate response is to provide high quality summary and analysis of disclosures.<sup>26</sup>
- 172 To use a measure of profitability that does not reflect asset revaluations would present a misleading picture of performance to interested persons. This is because the ROI would consequently not capture the entirety of returns earned by the supplier of the regulated service over time and not produce a profitability indicator that is comparable with the WACC.

*Depreciation*

- 173 The depreciation charge in the Regulatory Profit should also be the same value as that which is used in rolling forward the RAB value. This ensures that the return of capital is stripped out and a comparison can be made between the ROI (i.e., the actual rate of return *on* capital) and the WACC (i.e., the required rate of return *on* capital).
- 174 Depreciation write-offs of the value of assets decommissioned are a form of accelerated depreciation, which recognises a charge that in effect recovers the final unrecovered regulatory value of the asset. This is treated like depreciation, in that the same charge is applied against the RAB value and against income in the Regulatory Profit Statement.
- 175 The Commission's preliminary views on how depreciation should be determined are outlined in the Input Methodologies Discussion Paper.<sup>27</sup>

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<sup>24</sup> Supra n 2, paragraph 6.184.

<sup>25</sup> Unison Networks Ltd., *Submission on Regulatory Provisions of the Commerce Act Discussion Paper*, 16 February 2009, p.37.

<sup>26</sup> Supra n 2, paragraphs 4.53-4.58.

<sup>27</sup> *Ibid.*, paragraph 6.192 – 6.194.

*Capital Contributions and Vested Assets*

- 176 Capital contributions are contributions received from a customer or other third party for the purpose of constructing or enhancing a regulatory asset.
- 177 Vested assets are those assets which are constructed by a third party, and are then transferred to the regulated business who then takes ownership and responsibility for those assets. These may be transferred for no consideration or for partial consideration.
- 178 The Commission's preliminary view is that the value of capital contributions and vested assets (net of any consideration) should be recognised as income in the ROI. This allows appropriate comparisons to be drawn between the ROI and the WACC, as all the relevant returns earned by the supplier of the regulated service are captured.

*Regulatory Tax*

- 179 As outlined in the Input Methodologies Discussion Paper, the Commission's preliminary view is that a "tax payable" approach is the most appropriate for calculating regulatory tax.<sup>28</sup> The "tax payable" approach takes account of permanent and temporary differences and also of tax losses relating to the regulated business. The Commission's approach is intended to be a close proxy for the tax actually payable by the regulated business in the year in question. This means that no further adjustment for tax is required to allow sensible comparisons to be made between the ROI and the WACC. In other words, since it accounts for tax payable as an expense for that year, no corresponding "deferred tax balance" or other adjustments are required to the denominator of the ROI calculation.

*Lost and Found Assets*

- 180 An exception to reflecting changes in the RAB roll forward as income in the ROI, is for certain net increases (or decreases) due to changes in the asset register. In particular, "found" assets are deemed always to have been in existence, and conversely "lost" assets are deemed never to have existed. In other words, assets added to the RAB in this way are not treated as income (since suppliers should expect to earn a greater return over time as a result of an asset being "found"); likewise, assets removed are not treated as a loss. Therefore no offsetting adjustment is required to be made to the Regulatory Profit of the business, which ensures consistency with the specification of the WACC.

Q.18) Do you agree that revaluations and depreciation in the Regulatory Profit should be the same value as that which is used in rolling forward the RAB value? If not, please detail how depreciation and revaluations should be treated and how this treatment is consistent with the FCM concept.

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<sup>28</sup> Ibid., paragraph 7.58.

Q.19) Do you agree that the value of capital contributions and vested assets (net of any consideration) should be recognised as income in the ROI? If not, please explain how the value of the returns earned from vested assets and capital contributions should be treated and why you consider this to be preferable.

Q.20) Do you agree that lost and found assets should not be treated as income and expense? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

#### **4.2.2 Other ROI specification issues relating to the specification of the WACC**

- 181 It is also important to ensure that the ROI is specified in a way that is consistent with the WACC that is being used to assess profitability, notably with respect to the treatment of inflation and taxation.
- 182 If ROI is measured against a post-tax WACC, an adjustment is required for the tax effect of the interest, whereas a ‘vanilla’ WACC does not require an adjustment for the interest tax shield.<sup>29</sup>
- 183 The Commission notes that regulators in a number of overseas jurisdictions use a vanilla WACC, so comparing ROI against a vanilla WACC may more readily allow comparisons with overseas data. On the other hand, interested persons in New Zealand are more likely to be familiar with a post-tax WACC, and therefore it may also be useful for ROI to be disclosed under information disclosure in a manner consistent with that WACC formulation.
- 184 The Commission’s preliminary view is therefore that a vanilla WACC and a post-tax WACC should be published to enable both assessments of return to be calculated.
- 185 If the ROI is compared to a post-tax WACC, the Regulatory Profit is adjusted to deduct the interest tax shield.<sup>30</sup> This is the tax benefit on the deductible interest. The interest tax shield should be calculated using the same standard tax rate, interest rate and notional industry wide leverage assumption used in the post-tax WACC calculation so that the ROI is comparable to the post-tax nominal WACC.
- 186 The rationale for the basis of calculation of Regulatory Profit is to provide consistency between companies who have differing ownership, capital structures, and asset bases.

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<sup>29</sup> Ibid., paragraph 7.76.

<sup>30</sup> The Regulatory Profit / Loss (as defined in chapter 5) is net of levered tax payable (i.e., tax payable after deducting interest). However, if a post-tax WACC is used, the cost of debt term specified in the WACC is adjusted by the interest tax shield (1-Tc). To be able to directly compare the ROI with this WACC, it needs to be adjusted by the same amount. The interest tax shield adjustment is therefore essentially a technical adjustment, which is achieved by deducting the interest tax shield from the regulatory profit in the numerator of the ROI.

187 Regarding inflation, whether a real or nominal WACC is appropriate generally depends on the valuation approach of the RAB. If the RAB value is uplifted by an inflation index, the most obvious corresponding approach for the cost of capital would be to use a real WACC.<sup>31</sup> An alternative approach is to apply a nominal WACC but treat revaluation gains due to inflation as income. The approach that will be adopted will be determined through consultation on the input methodology for the regulatory cost of capital.

Q.21) Do you agree that a ROI comparable to a vanilla WACC and a post-tax WACC should be disclosed? If not, please provide the reasons for your view.

#### 4.2.3 Calculation of Asset Value

188 It is the Commission's preliminary view that the asset value used in the denominator of the ROI calculation should be the Regulatory Investment Value (RIV) as disclosed in the Regulatory Asset Statement. The composition of the RIV is discussed in paragraphs 189 to 198. The opening value of the RAB is discussed in paragraphs 298 to 300.

##### *Treatment of Cash and Non-cash Items*

189 Cash items, such as investments in the RAB (both additions and disposals) are considered to occur throughout the year. Therefore, by adding only half of the investments in the year, a return on that investment is required for only half of that first year (on average) for the purpose of the ROI assessment. The value of merger and acquisition assets is allocated for the proportion of the year that they are available for earning a return on that investment.

190 Depreciation, revaluations and other non-cash adjustments to the RAB for the current year are not included in the denominator of the ROI calculation as they are considered to be year end adjustments. To include them in the ROI calculation would make the ROI less comparable with the WACC.<sup>32</sup> It is noted that depreciation and revaluations from one regulatory year are included in the ROI calculation of the following year by virtue of being included in the opening RAB value for that year.

191 A more simplified approach to the RIV would be to use an average of the opening and closing balance of the RAB, effectively ignoring the effects of the exact timing

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<sup>31</sup> Supra n 2, paragraph 8.25.

<sup>32</sup> The determination of the ROI is a simplification, as it assumes that operating expenditure, cash taxes and revenue are all incurred at the end of the period. In reality revenues and operating expenditure will occur on a continuous basis, while cash taxes will be paid approximately three times a year. Making the same end of period assumption for depreciation and revaluations has the effect of matching the timing of depreciation and revaluations with the treatment of revenue, operating expenditure and taxes. It is noted that the return calculated with end of period cash flows will be too high, if cash outflow occurs throughout the year, as the cash outflows will be "over discounted". Conversely, if a cash inflow occurs throughout the year, then the return calculated with end of period cash flows will be too low.

of merger and acquisition activity and assuming that depreciation and revaluation occur evenly during the year. The Commission's preliminary view is that the timing of merger and acquisition activity should not be ignored due to its potential materiality and that depreciation and revaluations should be treated as year end adjustments as noted above.

#### *Works Under Construction*

192 The Commission's preliminary views on how works under construction should be treated are outlined in the Input Methodologies Discussion Paper.<sup>33</sup> As outlined in that paper, in competitive markets, assets that have not been commissioned do not normally earn a return on the capital expended. In principle, in a regulatory context a similar "competitive market" approach would provide appropriate incentives to complete capital works in a timely manner. It is the Commission's preliminary view, therefore, to provide for the finance cost at the time of commissioning. The provision of finance costs is discussed further in paragraphs 315 to 322.

#### *Net Assets Commissioned During the Year*

193 An intra-year timing issue is the time lag from commissioning of works until the works are accounted for in the disclosed RAB value. It is the Commission's preliminary view that, for the purpose of the return calculation, half the value of the net new capital investment should be reflected in the RAB. This is based on the assumption that capital works are commissioned or decommissioned evenly over the year; hence the average lag is six months.

194 Net assets commissioned during the year should exclude assets acquired from or sold to another regulated supplier. The treatment of assets acquired from or sold to another regulated supplier is discussed below.

#### *Assets Acquired from or Sold to Another Regulated Supplier*

195 Assets acquired from or sold to another regulated supplier are generally the result of merger and acquisition activity. Therefore, to ensure interested persons can appropriately assess the profitability of suppliers of regulated services, the value of assets acquired from or sold to another regulated supplier is included in the RAB only to the extent that the profit relating to those assets is recognised in the regulated supplier's regulatory profit. The  $p$  factor as outlined in paragraph 205 is the vehicle by which the value is proportioned.

196 By defining this adjustment to the RIV as regulatory value of assets acquired from or sold to another regulated supplier there is the possibility that single asset acquisitions/sales between regulated business units may be captured. In such instances it may be more appropriate to include these as part of net assets commissioned during the year as there may be no identifiably specific revenue that relates to these assets. The Commission's preliminary view, however, is that these assets should be included in this adjustment for simplicity.

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<sup>33</sup> Supra n 2, paragraphs 6.220-6.222.

197 It is the preliminary view of the Commission that assets acquired from or sold to another regulated supplier are to be transferred at their rolled-forward RAB value. Regulated businesses bear upside or downside risks in relation to the amounts actually paid for regulatory assets (in terms of disclosed ROIs and RAB values).

#### *Working Capital*

198 The Commission's preliminary view is that an adjustment to RIV for working capital is not necessary due to its materiality in relation to the RIV calculation.

Q.22) Do you agree that half the value of the net new capital investment should be reflected in the RIV value? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

Q.23) Do you agree that assets acquired from or sold to another regulated supplier or business unit should be included in the RIV to the extent that the profit relating to those assets is recognised in the regulated supplier's regulatory profit? If not, please detail how asset acquired from or sold to another regulated supplier or business unit should be treated and why you consider this to be preferable.

Q.24) Do you agree that it is appropriate to treat assets acquired from or sold to another regulated supplier that doesn't relate to merger or acquisition activity as above? If not, please explain how these should be treated and why you consider this to be preferable.

Q.25) Do you agree that an adjustment to RIV for working capital is not necessary given its likely materiality? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

#### **4.2.4 Shared Assets Costs**

199 Consideration needs to be given to the value of assets shared between business units given the possibility that this may require an adjustment to either the Regulatory Profit or the RAB and consequently will affect the ROI calculation. This would need to consider the situation where assets are used to provide more than one regulated service, and also when there are unregulated services provided.

200 The Input Methodologies Discussion Paper outlines the four main ways that sharing of assets costs between regulated and unregulated services or activities occurs, being:

- The use of unregulated assets to provide regulated services (or activities);
- The use of non-system fixed assets to provide services to both regulated and unregulated services;
- The allocation of shared capital costs; and
- The use of regulated fixed assets to provide unregulated services.<sup>34</sup>

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<sup>34</sup> Supra n 2, paragraph 5.186.



- 201 The Input Methodologies Discussion Paper goes on to note that considerable complexity can arise in determining how the capital costs associated with the use of regulated assets to provide regulated and unregulated services should be attributed. It is suggested that an alternative may be to regard the whole asset cost as a regulated asset cost, but recognise the benefit it confers on the unregulated services by allocating to it a share of the unregulated revenue, which could be considered an imputed rental value.<sup>35</sup>
- 202 If the capital costs associated with the use of network assets to provide regulated and unregulated services were to be attributed, it is the Commission's preliminary view that there would be an adjustment made to the final RAB value, and the associated depreciation and revaluations. This adjustment would reflect the value of the portion of assets that provide unregulated services. By adjusting the final RAB, the complexities of having partial assets included in the RAB and the associated accounting difficulties regarding the degree of attribution would be mitigated. The disclosure of such an adjustment is discussed further in paragraph 309.
- 203 Alternatively, if the regulated asset base was not adjusted, then the financial benefits conferred by the unregulated assets would need to be recognised as part of the regulatory profit calculation. This is discussed further in paragraph 228.

Q.26) In your view, how should the capital costs associated with the use of regulated assets to provide regulated and unregulated services be attributed? Please provide the reasons for your view.

### 4.3 THE PROPOSED ROI FORMULA

- 204 The proposed formula for calculating ROI and assessing it against the Post-Tax WACC is :

$$ROI = \frac{\text{Regulatory Profit} - \text{Interest Tax Shield}}{\text{Regulatory Investment Value}}$$

- 205 The proposed formula for calculating ROI and assessing it against the Vanilla WACC does not require an adjustment for the interest tax shield and is as follows:

$$ROI = \frac{\text{Regulatory Profit}}{\text{Regulatory Investment Value}}$$

<i>Regulatory Profit</i>	=	Regulatory Profit / (Loss)
<i>Interest Tax Shield</i>	=	an adjustment required to make the ROI comparable with a post-tax WACC (which

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<sup>35</sup> Ibid., paragraph 5.191.

	includes the interest tax deduction in the specification of the WACC formula);
<i>Regulatory Investment Value</i>	= $RAB_0 + 0.5 \times \text{Net Assets Commissioned} + pA$
$RAB_0$	= the Total Regulatory Asset Base Value as at the beginning of the year, uplifted by any FDC allowance;
<i>Net Assets Commissioned</i>	= net assets commissioned during the year;
$A$	= regulatory value of assets acquired from or sold to another regulated supplier during the year;
$p$	= denotes the proportion of the year following the acquisition/sale of assets.

#### 4.4 SUMMARY OF PRELIMINARY VIEWS

206 The following table provides a summary of the Commission's preliminary views on the ROI performance indicator.

**Table 5: Summary of Commission's Preliminary Views on the ROI**

Topic	Commission's Preliminary View
Profitability Indicator	The Commission's preliminary view is that the ROI calculation is the appropriate measure of assessing profitability at the business level, which helps assess whether prices in aggregate are efficient.

Topic	Commission's Preliminary View
Specification of ROI in a way that is consistent with the WACC	<p data-bbox="581 281 755 312"><u>Revaluations</u></p> <p data-bbox="581 331 1328 474">The Commission's preliminary view is that the regulatory profit used in the ROI calculation is adjusted for revaluations irrespective of the method of calculating the revaluation.</p> <p data-bbox="581 495 755 527"><u>Depreciation</u></p> <p data-bbox="581 546 1328 653">The Commission's preliminary view on how depreciation should be calculated is outlined in the Input Methodologies Discussion Paper.<sup>36</sup></p> <p data-bbox="581 674 1105 705"><u>Capital Contributions and Vested Assets</u></p> <p data-bbox="581 724 1328 831">The Commission's preliminary view is that the value of capital contributions and net value of vested assets should be recognised as income in the ROI.</p> <p data-bbox="581 852 786 884"><u>Regulatory Tax</u></p> <p data-bbox="581 903 1338 1010">The Commission's preliminary view on how tax should be calculated is outlined in the Input Methodologies Discussion Paper.<sup>37</sup></p> <p data-bbox="581 1031 878 1062"><u>Lost and Found Assets</u></p> <p data-bbox="581 1081 1338 1146">The Commission's preliminary view is that assets added to the RAB in this way are not treated as income.</p>

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<sup>36</sup> Ibid., paragraph 6.213.

<sup>37</sup> Ibid., paragraph 7.115.

Topic	Commission's Preliminary View
Other ROI specification issues related to the specification of the WACC	The Commission's preliminary view is that a ROI comparable to a 'vanilla' WACC and a ROI comparable to a post-tax WACC should be published to enable both assessments of return to be assessed.
Calculation of Asset Value	<p>The Commission's preliminary view is that the asset value used in the ROI calculation should be the opening RAB value (adjusted for an allowance for Finance During Construction (FDC) if appropriate); half the value of asset commissioned during the year; and a proportionate adjustment for assets acquired from or sold to another regulated business during the year (RIV value).</p> <p><i>Treatment of Cash and Non-cash Items</i></p> <p>The Commission's preliminary view is that cash items, such as asset additions and disposals occur throughout the year and therefore should be reflected in the RIV by adding half the value to the asset base to reflect the fact that on average the asset has only been earning a return for half of the year.</p> <p>Non-cash items such as depreciation, revaluations should be excluded from the RIV on the basis they are year-end adjustments.</p> <p><i>Works Under Construction</i></p> <p>As outlined in the Input Methodologies Discussion Paper, the Commission's preliminary view is that compensation for finance cost should be provided at the time of commissioning.<sup>38</sup></p> <p><i>Working Capital</i></p> <p>The Commission's preliminary view is that an adjustment to RIV for working capital is not likely to be necessary due to its small size in relation to the RIV calculation.</p>

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<sup>38</sup> Ibid., paragraph 6.222.

<b>Topic</b>	<b>Commission's Preliminary View</b>
Shared Assets Costs	<p>If the capital costs associated with the use of network assets to provide regulated and unregulated services were to be attributed, it is the Commission's preliminary view that there would be an adjustment made to the final RAB value, and the associated depreciation and revaluations. This adjustment would reflect the value of the portion of assets that provide unregulated services.</p> <p>Alternatively, if the regulated asset base was not adjusted, then the financial benefits conferred by the unregulated assets would need to be recognised as part of the regulatory profit.</p>

## **CHAPTER 5: FINANCIAL INFORMATION**

### **5.1 INTRODUCTION**

- 207 This chapter provides an overview of the Commission's preliminary view on the requirement to disclose specified regulatory financial statements, including the rationale for the components of financial disclosures.
- 208 The relevant regulatory provisions of the Act supporting disclosure of financial information are s 53C(2) and s 53D. These provisions are discussed in Appendix B and, in summary, note that the information required to be disclosed may include financial statements, including projected financial statements, related party transactions and consolidated information.

### **5.2 PURPOSE OF FINANCIAL DISCLOSURES**

- 209 The primary purpose of financial information disclosure is to establish the basis of financial performance indicators that may be used to monitor the performance of the regulated suppliers. Financial performance indicators assist interested persons to assess whether the purpose of Part 4 is being met. In particular, they provide information that can be used to assess prices, profits and efficiency (consistent with s 52A(1)(b), (c) and (d)).
- 210 Chapter 4 outlines the Commission's preliminary views on the determination of the ROI performance indicator. As noted in this chapter, the determination of Regulatory Profit and the RAB are key components of the ROI measure, and including movements in the asset values on the same basis in both the Regulatory Profit and in the RAB ensures that these movements are NPV neutral.
- 211 The proposed regulatory financial statements are structured and line items defined, so that they transparently link with other proposed disclosure reports and the financial information that is used in the performance indicators.
- 212 An assessment of financial viability also assists in meeting the purpose of information disclosure as it is considered an integral part of the assessment as to whether there are incentives to innovate and to invest. Regulated suppliers may be discouraged or unable to invest if their financial viability is at risk, which would not be consistent with s 52A(1)(a) (which specifies that regulated suppliers have incentives to innovate and invest). An inability to invest is also contrary to the purpose of promoting the long term benefit of consumers.

### **5.3 KEY MATTERS FOR CONSIDERATION**

- 213 This section outlines the key financial matters for consideration when making an information disclosure determination and covers aspects of the regulatory financial statements that are specific to the requirements of regulatory reporting, and also includes matters that are subject to input methodology determinations.
- 214 It is noted that some of the matters covered in the Chapter 4 are relevant to the determination of regulatory profit but are not covered in this section. Those matters include:

- Capital contributions and vested assets;
- Depreciation and revaluations; and
- Taxation methodology.

### **5.3.1 *Input Methodologies***

215 Amongst other things, s 52T(1) requires that the input methodologies relating to a particular good or service must include, to the extent applicable to the type of regulation under consideration, methodologies for evaluating or determining the following matters in respect of the supply of the goods or service:

- allocation of common costs, including between activities, businesses, consumer classes, and geographic areas; and
- treatment of taxation.

216 The Commission is required to apply the relevant input methodologies upon which s 52P determinations are based. The Commission's preliminary views on the allocation of common costs and treatment of taxation input methodologies are outlined in Chapters 5 and 7, respectively, of the Input Methodologies Discussion Paper.

### **5.3.2 *Application of Generally Accepted Accounting Practice (GAAP)***

217 For the purposes of this paper, the term "statutory financial statements" refers to those financial statements prepared for the purposes of meeting the Companies Act 1993 requirements. Generally accepted accounting practice (GAAP) is a term used to refer to the widely accepted rules, conventions and standards for the preparation of statutory financial statements.

218 Aurora Energy Ltd submitted that GAAP should be the basis for financial information disclosures and is concerned with the extent to which regulatory disclosures (e.g., depreciation and taxation) can differ from accounting disclosures. For specific regulatory reporting, the Commission's preliminary view is to consider GAAP as the starting point, but modify the disclosures where required to meet the purposes of information disclosure under the regulatory regime. This approach is considered to minimise compliance costs as GAAP reporting is derived from existing reporting and accounting systems.

219 Regulatory reporting is likely to be different from GAAP where the purposes of the regulatory regime require more prescriptive definitions and additional information than is required under GAAP. More prescriptive definitions and additional information may be necessary to enable meaningful assessment of the regulated business unit. It may also be useful for consistency of reported information to facilitate comparisons between regulated businesses.

220 Conversely, there are certain disclosures required under GAAP that may not be relevant to the regulatory regime in that they are not required to meet the purpose of the Act. Also in some cases the information would be useful, but allocating the regulatory component from the information may be more costly to produce than any

actual or perceived benefit from making the information available. The Commission's preliminary view on what could be excluded for regulatory purposes includes:

- Equity information;
- Financing information;
- Working capital information; and
- Cashflow information.

- 221 Equity information is not required because the assessment of the ROI is at the business level (prior to financing costs), rather than on the return to the shareholders. Assessing a return to the shareholder would require full disclosure of financial information; however this is considered to be outside the scope of the Act.
- 222 It is the Commission's preliminary view that financing information, including working capital information should not be required for information disclosure purposes as discussed in paragraph 244 below.
- 223 Cashflow information has limited value in assisting interested persons to assess whether the purpose of Part 4 is being met. Therefore, given the cost, it is the Commission's preliminary view that cashflow information should not be required for regulatory reporting purposes.

Q.27) Do you agree that the Commission should consider GAAP as the starting point, but modify the disclosures where required to meet the purposes of information disclosure under the regulatory regime? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **5.3.3 Cost Allocation and Sharing of Assets Costs**

- 224 A regulated supplier under Part 4 is not defined according to legal entity structures. Rather it is defined in terms of the type or types of regulated services that it supplies. Consequently, input methodologies for cost allocation between business units supplying regulated and/or unregulated services may require costs to be allocated within and between legal entities to determine what is appropriately attributable to different services provided by a regulated supplier.
- 225 Many of the suppliers of services regulated under Part 4 of the Act have multiple business units. In some cases, all of the supplier's business units are regulated, but in others only some are regulated.
- 226 In order to determine the financial contribution of a regulated business unit, it is necessary to have transparency around the allocation of costs and assets between the regulated and unregulated activities and across regulated entities. Also where the regulated business has more than one regulated activity, transparency will be required for each component.



- 227 The Input Methodologies Discussion Paper discusses the Commission's preliminary views on cost allocation for regulated suppliers.<sup>39</sup> In this discussion the Commission suggests the use of a cost allocation handbook to assist with applying the input methodology and to provide transparency as to how costs are allocated.<sup>40</sup>
- 228 The Input Methodologies Discussion Paper also discusses the matter of shared assets.<sup>41</sup> The Commission considers there are two means for addressing the sharing of asset costs, being:
- adjusting the final RAB value to reflect the proportion of the regulated assets that have been made available for non-regulated purposes; or
  - recognising the benefit shared assets confers on the unregulated services by allocating to the regulated business a share of the unregulated revenue, which could be considered an imputed rental value.
- 229 The Commission outlines further details on how the above methods could be implemented in paragraphs 199 to 203 and paragraphs 308 to 310.

#### **5.3.4 Gains/Losses on Sale of Assets**

- 230 Gains or losses on sale of assets generally represent the over or under recovery of depreciation. Depreciation is an estimation of the useful life of assets used in supplying a service.
- 231 The sale of an asset for a value that is more or less than the regulatory value, as adjusted for depreciation, occurs when the estimation of the useful life of the assets was proven to be inaccurate, or alternatively if the sale price is not reflective of the underlying value of the asset. It is the Commission's preliminary view that where the sale of the asset is made to an unregulated entity or business unit, then the regulatory profit should be adjusted to reflect the difference in actual versus estimated depreciation, being the residual gain or loss on sale.
- 232 As outlined in paragraphs 195 to 197, the Commission's preliminary view is that assets acquired, sold or merged with another regulated supplier should be transferred at the RAB value. On this basis there is no requirement to account for a gain or loss on sale.
- 233 Paragraph 313 also discusses the depreciation clawback issue, and the associated tax implications that arise when assets are transferred between regulated suppliers.

Q.28) Do you agree that where the sale of the asset is made to an unregulated entity or business unit, then the regulatory profit should be adjusted for gains or losses on sale? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

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<sup>39</sup> Ibid., Chapter 5.

<sup>40</sup> Ibid., paragraph 5.204.

<sup>41</sup> Ibid., paragraphs 5.186–5.192.

### 5.3.5 *Pass-Through Revenue*

- 234 Pass-through revenue is revenue that is received on the basis that it is to be distributed to consumers or other third parties.
- 235 It is the Commission's preliminary view that pass-through revenue and the associated distribution should be transparently disclosed in the regulatory profit statement.
- 236 Separate disclosure of pass-through revenue received and passed on, provides transparency around any timing differences that may otherwise lead to short term distortion of Regulatory Profit which would impact on performance indicators. It is noted that AC Loss Rental Rebates for electricity lines businesses is the only known pass-through revenue for the Part 4 regulated suppliers.

Q.29) Do you agree that pass-through revenue and the associated distribution should be transparently disclosed in the regulatory profit statement? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### 5.3.6 *Pass-Through Costs*

- 237 In regard to information disclosure, the Commission's preliminary view as outlined in the Input Methodologies discussion paper, is that the criteria for a cost to be eligible for inclusion as a pass-through cost requires costs to be:
- outside the control of a regulated business;
  - unforeseen (i.e., amount unable to be accurately forecast);
  - defined and approved as a pass-through cost before information disclosure requirements are set.<sup>42</sup>
- 238 Given that the corresponding recovery of pass-through costs is often not able to be unbundled in the regulatory revenue, the preliminary view of the Commission is to have separate disclosure of the pass-through costs. This will enable analysis of the impact of increases in pass-through costs to be made and allow interested persons to assess whether operating costs are distorted by movements in pass-through costs.

Q.30) Do you agree that pass-through costs should be separately disclosed? If not please provide a detailed explanation as to why it shouldn't be separately disclosed.

### 5.3.7 *Insurance*

- 239 The Commission has previously sought feedback, during the review of the information disclosure requirements for EDBs under Part 4A, on the treatment of insurance costs and on practical ways to achieve comparability between regulated suppliers that self-insure compared to regulated suppliers that contract with an insurer.

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<sup>42</sup> Ibid., paragraph 10.118.

240 The feedback received demonstrated a mixed response, with some submitters arguing that insurance was not material enough to warrant separate disclosure of premiums, whilst others argued for the benefits of separate disclosure. Based on the evidence of insurance expenses provided, the Commission's view was that this was not a particularly material issue. It is therefore the Commission's preliminary view that insurance expenses should be included in the calculation of Regulatory Profit only where these are paid to an insurance entity.

Q.31) Do you agree that insurance expenses should be included in the calculation of Regulatory Profit only where these are paid to an insurance entity? If not please, provide a detailed explanation as to why insurance should or shouldn't be disclosed, including a reference to the materiality of the insurance costs.

### **5.3.8 Merger and Acquisition Costs**

241 The Commission's preliminary view is that merger and acquisition expenses should be included in Regulatory Profit. Merger and acquisition expenses are likely to be lumpy; therefore, the Commission's preliminary view is that they should be separately disclosed so that interested parties can understand the effect these expenses have had on the ROI.

Q.32) Do you agree that merger and acquisition expenses should be included in Regulatory Profit? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **5.3.9 Financing Information and the Assessment of Financial Viability**

- 242 As discussed in paragraph 212 the Commission considers the assessment of financial viability as important. The Commission, however, also notes the difficulty in assessing financial viability for a specific business unit given the difficulty in allocating equity and debt to individual business units where activities are financed on a whole entity or group basis, as is normal business practice.
- 243 One means of assessing financial viability would be to assess the financial viability of the whole entity through using publicly available information on the entity's financial structure. The Commission, however, also notes that such information may not always be available in the public arena. The Commission may, therefore, also look to identify issues related to the financial viability of businesses through assessment of consolidated information (including both regulated and unregulated aspects of the business) as may be required under s 53D, and to make public its findings through the summary and analysis.
- 244 It is the Commission's preliminary view that financing information for regulated business units would not be required for information disclosure purposes due to the difficulty in meaningfully allocating the portion that relates to the regulated business unit(s).

245 Financing assumptions are also used in the calculation of deductible interest in the regulatory tax calculation<sup>43</sup> and the calculation of the interest tax shield used in determining an ROI that is comparable to the post-tax WACC.<sup>44</sup> The Commission's preliminary view is that regulated suppliers should use the leverage assumption and cost of financing assumptions outlined in the cost of capital input methodology in preparing these disclosures. It is noted that suppliers that are subject only to information disclosure regulation do not have to apply a cost of capital input methodology.<sup>45</sup> This is discussed further in paragraph 788 and 789.

Q.33) Do you agree that financing information should not be required due to the difficulty in meaningfully allocating the portion that relates to the regulated business? If not, please provide details on how information on financing can be meaningfully allocated to regulated business units.

Q.34) Are there any additional means for which an assessment of financial viability could be made? If so, in light of the regulatory provisions, please provide details of how the assessment can be made.

Q.35) Do you agree that regulated suppliers should use the leverage assumption and cost of financing assumptions outlined in the cost of capital input methodology in preparing the deductible interest and interest tax shield calculation? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### **5.3.10 Segmentation of Financial Information**

246 The segmentation of financial information into different consumer groups or business activities is beneficial in the assessment of efficiency at the customer or business activity level.<sup>46</sup> However, the Commission is mindful that the cost of preparing segmented information at these levels may outweigh the benefit of being able to make such an assessment.

247 The Commission outlines its preliminary views on where segmented financial information should be disclosed in Chapters 11-14.

### **5.3.11 Related Party Transactions**

248 The Commission's preliminary view is that the disclosure of related party transactions would be at least consistent with GAAP, in particular the New Zealand equivalent to International Accounting Standard 24 (NZ IAS 24).

<sup>43</sup> Supra n 2, paragraphs 7.62-7.63.

<sup>44</sup> Ibid, paragraphs 7.77-7.79.

<sup>45</sup> See section 53F(1)(b) of the Act.

<sup>46</sup> Business activity is defined in this context as a regulated business activity, of which there may be more than one with a regulated supplier.

- 249 The objective of NZ IAS 24 is to ensure that an entity's financial statements contain the disclosures necessary to draw attention to the possibility that the financial position and profit or loss may have been affected by the existence of related parties and by transactions with such parties.
- 250 A related party transaction is defined in NZ IAS 24 as a transfer of resources, services or obligations between related parties, regardless of whether a price is charged.
- 251 This definition which includes obligations between related parties extends the requirement to the disclosure of the mere existence of a related party relationship, given that this may be sufficient to affect the transactions of the entity.
- 252 In considering each possible related party relationship, attention is directed to the substance of the relationship and not merely the legal form.
- 253 Related party is defined in clause 9 of NZ IAS 24 as being a party related to an entity if :
- (a) *directly, or indirectly through one or more intermediaries, the party :*
    - (i) *controls, is controlled by, or is under common control with, the entity (this includes parents, subsidiaries and fellow subsidiaries);*
    - (ii) *has an interest in the entity that gives it significant influence over the entity; or*
    - (iii) *has joint control over the entity;*
  - (b) *the party is an associate (as defined in NZ IAS 28 Investments in Associates) of the entity;*
  - (c) *the party is a joint venture in which the entity is a venturer (see IAS31 Interests in Joint Ventures);*
  - (d) *the party is a member of the key management personnel of the entity or its parent;*
  - (e) *the party is a close family member of the family or any individual referred to in (a) or (d);*
  - (f) *the party is an entity that is controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or*
  - (g) *the party is a post-employment benefit plan for the benefit of employees of the entity, or of any entity that is a related party of the entity.*
- 254 In addition to disclosures required under GAAP, it is the preliminary view of the Commission that disclosure will also be required for transactions between regulated and unregulated business units of the regulated supplier. This is consistent with the s 53D(3)(a) of the Act which provides that the Commission may require any other information referred to in section 53C for the purpose of monitoring compliance with the information disclosure regulations. Section 53C(2)(e) includes transactions with related parties. GAAP reporting, specifically NZ IAS 24, does not contemplate the disclosure of transactions between business units as it deals with disclosure requirements for the whole entity.
- 255 The Commission notes that GAAP reporting would not necessarily assist with identifying whether monopoly rents are being shifted to unregulated business units. In requesting disclosure of transactions, including transfer pricing, with unregulated

business units, the Commission is mindful that some entities may be uncomfortable disclosing this information which may necessarily result in transparency of commercially sensitive unregulated activities. Also, the disclosure of related party transactions, including transfer pricing information, could be costly.

- 256 The Commission, however, sees value in disclosing related party information for monitoring purposes and proposes that these transactions be disclosed as part of the consolidation and reconciliation provisions as discussed below in paragraphs 257-260.

Q.36) Do you agree that disclosure of related party transactions should at least be consistent with GAAP and also include transactions between business units? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.37) Do you agree that transactions with related parties, including transfer pricing information, should be disclosed? If so, please provide details of how this information should be disclosed. If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### ***5.3.12 Consolidation and Reconciliation Provisions***

- 257 For regulated suppliers that supply both regulated and unregulated goods and services, the primary requirement will be to report on the assets and activities of the regulated services. However, under section 53D of the Act, the Commission may require consolidated information for the purpose of monitoring compliance with information disclosure regulation. This may include reporting on all entities within a group, and also on unregulated goods and services provided by the reporting entity.
- 258 It is the preliminary view of the Commission that reconciliation between consolidated statutory reporting and regulatory reporting should be required for the purpose of monitoring compliance. It is likely the Consolidation Statement will include items such as revenue, operational expenditure, depreciation, revaluations, tax, profit, and the RAB so as to provide the Commission with adequate information to monitor compliance with information disclosure regulation.
- 259 Generally the Commission would consider that information disclosure and more specifically, consolidation and reconciliation information should be made publicly available. There might be certain circumstances, however, where consolidation and reconciliation information (including related party transactions) should only be disclosed to the Commission due to the confidential nature of the information.
- 260 The Commission acknowledges that consolidation and reconciliation information may not be readily available and therefore costly to disclose. The Commission, however, considers that this information is necessary and appropriate for monitoring purposes.

Q.38) Do you agree that reconciliation between consolidated statutory reporting and regulatory reporting should be required for the purpose of monitoring compliance? If not, please provide that reasons for your view, an alternative to monitoring compliance and why you consider this to be preferable.

Q.39) In your view, what form should the consolidation and reconciliation disclosures take? Please provide the reasons for your view.

#### **5.4 FINANCIAL DISCLOSURES**

261 This section covers the Commission's preliminary view of the structure of the regulatory financial statements, being the Regulatory Profit Statement and notes, Regulatory Asset Statement, Regulatory Tax Calculation, Forecast Statement and Consolidation Statement.

##### **5.4.1 Regulatory Profit Statement**

262 The Commission's preliminary view is that the Regulatory Profit Statement should be based on the regulatory components of earnings before interest and tax (EBIT). The EBIT would then be adjusted with a deduction for the regulatory tax calculations, and an adjustment for asset revaluations to arrive at a Regulatory Profit.

263 The regulatory components of EBIT would be based on aspects of income and expenditure that specifically relate to the regulated businesses, with some specific adjustments to align the reporting with the FCM concept as discussed in paragraphs 167 to 180. There may also be a requirement to include adjustments for the treatment of shared assets costs depending on what is determined to be the most appropriate accounting treatment, as discussed in paragraphs 199 to 203.

264 The Commission's preliminary view is that income should comprise the gross revenue of regulated activities, an adjustment for capital contributions, the value of vested assets (net of any consideration made towards the acquisition) and net pass-through revenue. In addition there may also be an adjustment to reflect unregulated revenue earned from regulatory assets depending on the accounting treatment of shared assets, as discussed in paragraphs 202 and 203.

265 The Commission's preliminary view is that expenses should comprise the operational expenditure related to regulated service, and depreciation, including write-downs of regulatory assets. The possible approaches to calculating regulatory depreciation are covered in the Input Methodologies Discussion Paper.<sup>47</sup>

266 Operational expenditure relating to regulated services forms the basis of the operational expenditure ratio, one of the performance indicators to measure productive efficiency. To provide meaningful analysis of operating costs it will be necessary to disclose separately the costs of managing the business from the asset maintenance expenditure, given that the efficiency of asset maintenance

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<sup>47</sup> Supra n 2, pages 172-179, paragraphs 6.186 – 6.214.

expenditure is more appropriately assessed alongside the capital expenditure ratios. This is discussed further in paragraphs 147 to 152.

- 267 The Input Methodologies Discussion Paper covers the approach to asset revaluations,<sup>48</sup> and the calculation of regulatory tax.<sup>49</sup>
- 268 The notes to the regulatory profit statement are primarily intended to provide further detail and explanation of the information disclosed in the regulatory profit statement and may include information regarding merger and acquisition expenses, details of material operating expenditure (being items that are greater than 10% of the operational expenditure line item), reclassifications of operating expenditure, related party transactions and reconciliation of regulatory profit information with other disclosures.

#### **5.4.2 Regulatory Asset Statement**

- 269 The Regulatory Asset Statement is limited to reporting financial position information that is relevant to regulatory performance assessments and will comprise disclosure of information regarding the asset base, a breakdown of capital expenditure, and details of capital works under construction.
- 270 The line items are defined so that they transparently link with other disclosure and performance indicators including the RIV calculation, which is the denominator of the Return on Investment (ROI) performance indicator, as specified in paragraph 188.
- 271 The valuation of the RAB is covered in the Input Methodologies Discussion Paper,<sup>50</sup> and is discussed further in Chapter 6 of this paper.
- 272 The Regulatory Asset Statement will provide transparency to the RIV. The preliminary view of the Commission is that the RIV will comprise the RAB value at the beginning of the year adjusted for half the value of asset additions and disposals in the current year and a proportionate adjustment for assets acquired from or sold to another regulated supplier during the year. In addition, an adjustment may be required for the capitalised value of finance during construction as discussed in paragraphs 318 to 322. It is, however, the preliminary view of the Commission to capitalise the actual cost of finance in line with GAAP. On this basis there would be no requirement to make a separate adjustment for the cost of finance during construction.
- 273 It is the preliminary view of the Commission that capital expenditure should be broken down into categories which are consistent with the AMP disclosure requirements. These categories should include capital expenditure relating to such things as growth and replacement. Disclosure requirements for AMPs are discussed

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<sup>48</sup> Ibid., paragraphs 6.146-6.152.

<sup>49</sup> Ibid., paragraph 7.58.

<sup>50</sup> Ibid., paragraph 6.1.



further in paragraphs 464 to 469 in regard to reconciling forecast within AMPs with actual capital expenditure.

- 274 It is recognised that in any given year there will not be exact alignment between capital expenditure incurred and the capitalisation of newly commissioned works. It is the value of commissioned works that is required to be disclosed as part of the RAB in the RIV calculation. Therefore, in order to provide a transparent linkage from one year to the next, and between the disclosure of expenditure and the roll forward of the RAB, a capital works roll-forward calculation is required as part of the Regulatory Asset Statement.

#### **5.4.3 Regulatory Tax Calculation**

- 275 The purpose of the Regulatory Tax Calculation disclosure is to make transparent the calculation of regulatory tax. The Input Methodologies Discussion Paper outlines the Commission's preliminary views on the treatment of taxation.<sup>51</sup>
- 276 Under the proposed tax payable approach the calculation of regulatory tax requires adjustments to the regulatory EBIT, to take account of the difference between regulatory and tax depreciation, and also any other differences in the calculation of permanent and temporary differences which arise as a result of the differences between regulatory and taxable profits.
- 277 As outlined in the Input Methodologies Discussion Paper, 'levered' tax costs should be estimated on the basis that it removes the need to carry out complicated reconciliations and ensures that the tax estimates are more transparent. Disclosure of such estimation is likely to be required.<sup>52</sup>
- 278 Also outlined in the Input Methodologies Discussion Paper the regulatory treatment of tax losses needs to be considered.<sup>53</sup> If it is determined that tax losses should be included, disclosure would be required in the regulatory tax calculation.

#### **5.4.4 Forecast Statement**

- 279 As discussed in paragraph 467, it is the Commission's preliminary view that AMPs should include, amongst other things, the disclosure of forecasts of capital and operational expenditure relating to assets. The Commission sees value in disclosing this information alongside historic information as it allows interested persons to review trends of historic information in light of forecasts and vice versa.
- 280 The disclosure of forecast information in the Annual Disclosure means that it can be audited at the same time as the historical information and removes the need to have separate audit provisions relating to this information.

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<sup>51</sup> Ibid., paragraphs 7.115 – 7.117.

<sup>52</sup> Ibid., paragraph 7.117.

<sup>53</sup> Ibid., paragraphs 7.64 - 7.70.

#### 5.4.5 Consolidation Statement

- 281 The purpose of disclosing a Consolidation Statement is to enable the Commission to monitor compliance with information disclosure regulations. This is covered under section 53D of the Act and also discussed in paragraph 257 of this chapter.
- 282 It is the Commission's preliminary view that a consolidation would include separate disclosure of each regulated business within a statutory reporting entity plus disclosure of the unregulated businesses in aggregate. The consolidation, being the sum of these disclosures, should then be reconciled to the statutory financial statements. The nature and amounts of reconciling items, such as the differences in accounting treatment between statutory financial reporting and regulatory reporting, would also need to be disclosed.
- 283 As discussed in paragraph 254 above, notes to the Consolidation Statement may also require disclosure of related party transactions between business units of a regulated supplier.

Q.40) Do you agree that financial information should be disclosed by way of a Regulatory Profit Statement, Regulatory Asset Statement, Regulatory Tax Calculation, Forecast Statement and Consolidation Statement? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

#### 5.5 SUMMARY OF DISCLOSURES

- 284 The following table provides a summary of the proposed financial disclosures and their purpose.

**Table 6: Summary of Proposed Financial Disclosures**

Component	Purpose	Description
Regulatory Profit Statement	Provides essential financial data that feeds into performance indicators.	Statement will be based on regulatory components of EBIT, adjusted for income tax and asset revaluations. Includes aspects of income and expenditure that specifically relate to the regulated business unit with adjustments to align reporting with the FCM concept.
Regulatory Asset Statement	Provides transparency to the RIV calculation and other financial position information.	Focuses on financial position information relevant to regulatory performance. Comprises disclosure of asset base information, a breakdown of capital expenditure, a capital works roll-forward calculation and details of capital works under construction.

Component	Purpose	Description
Regulatory Tax Calculation	Provides the calculation of regulatory tax.	Calculation of notional tax payable on the regulatory aspects of the business. Adjustments required for differences between regulatory and taxable profit, including an adjustment for interest. Interest expense based on notional industry-wide leverage assumptions.
Forecast Statement	To analyse trends and compare historic performance with forecast information.	Forecast of capital and operating expenditure is consistent with suppliers' AMPs.
Consolidation Statement	To monitor compliance with information disclosure regulations.	Consolidated reporting of business units. Items disclosed likely to include revenue, operating expenditure, depreciation, revaluations, tax, profit, and the asset base. Notes may also require disclosure of related party transactions.

## CHAPTER 6: REGULATORY ASSET BASE (RAB) DISCLOSURES

### 6.1 INTRODUCTION

- 285 This chapter discusses the disclosure of information relating to the RAB. It does this by outlining the matters discussed in Chapter 6<sup>54</sup> of the Input Methodologies Discussion Paper that relate to the establishment of the initial RAB value and roll forward of the RAB value, before linking these preliminary views to the assessment of performance under information disclosure.
- 286 As outlined in Chapter 4, the RAB is a key component of many of the performance indicators, including the ROI performance indicator. The basic ROI formula is shown below. The relevant part of the ROI formula is emphasised.

$$\text{Return On Investment} = \frac{\text{Regulatory Profit}}{\text{Asset Base}}$$

- 287 In paragraph 272 the Commission outlines its preliminary view on the composition of the asset base to be used in the ROI calculation.
- 288 Amongst other things, Part 4 of the Act requires that the input methodologies relating to a particular type of service must include, to the extent applicable to the type of regulation under consideration, “the valuation of assets, including depreciation and treatment of revaluations” (s 52T(1)(a)(ii)). The Commission is required to state the relevant input methodologies upon which section 52P determinations are based. The Commission’s preliminary views on the asset valuation input methodology are outlined in Chapter 6 of the Input Methodologies Discussion Paper.<sup>55</sup>
- 289 As outlined in the Input Methodologies Discussion Paper, the Commission explained that the key decisions that it needs to make in respect of the valuation of assets can be thought of in two parts, namely:
- establishing the ‘initial’ value of the RAB; and
  - ‘rolling forward’ the initial RAB.<sup>56</sup>
- 290 This chapter distinguishes between the two key decisions by referring to the ‘initial’ RAB value and the ‘rolled forward’ RAB.

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<sup>54</sup> Ibid., paragraph 6.1.

<sup>55</sup> Ibid., paragraph 6.293.

<sup>56</sup> Ibid., paragraph 6.2.

- 291 It is intended that the precise content of each disclosure will ultimately be outlined in sector specific disclosures, as these will necessarily require customisation to reflect the industry specific factors as outlined in Chapters 11-14 relating to the respective valuation information. A generic description of the categories within each of the reports is provided in paragraphs 330 to 340.
- 292 The Commission is mindful that different approaches to asset valuation may require different disclosures. This Chapter has been prepared on the basis of the Commission's preliminary views on Asset Valuation as outlined in the Input Methodologies Discussion Paper.<sup>57</sup> Paragraphs 296 to 323 briefly outline some of the factors in the disclosure requirements that may need to be considered.

## **6.2 PURPOSE OF REGULATORY ASSET BASE (RAB) DISCLOSURES.**

- 293 As outlined in Chapter 3, the RAB value will assist in contributing to the purpose of information disclosure regulation by being the denominator in the ROI performance indicator calculation and also in some of the operational and capital expenditure performance indicators. Importantly, a regulatory valuation of the asset base is necessary to allow interested persons to assess whether suppliers that are subject to information disclosure are earning excessive profits, as outlined in s 52A(1)(d). Asset base information is therefore useful to interested persons in understanding the make-up of the asset base and the accuracy of the information contained within it.
- 294 It also provides information on where investment has occurred and is occurring. This is useful as it relates to the extent to which suppliers have incentives to invest (s 52A(1)(a)). An understanding of the RAB and the investments included in it will therefore assist with the analysis of performance indicators. RAB disclosures should also be sufficiently detailed to allow transparency of the RAB calculation.

## **6.3 KEY MATTERS FOR CONSIDERATION**

- 295 This section outlines the key matters for consideration in developing RAB disclosure requirements. It is noted that some of the matters covered in chapter 4 are relevant to the roll forward and disclosure of the RAB. These matters include:
- Capital contributions and vested assets (refer paragraphs 176 to 178);
  - Revaluations (refer paragraphs 170 to 172);
  - Depreciation method, excluding asset lives considerations (refer paragraphs 173 to 175); and
  - Working Capital (refer paragraph 198).

### **6.3.1 Initial RAB Value**

- 296 The Commission's preliminary views on the determination of the initial RAB for regulated suppliers are outlined in the Input Methodologies Discussion Paper.<sup>58</sup>

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<sup>57</sup> Ibid., paragraph 6.293.

<sup>58</sup> Ibid., paragraphs 6.102-6.112.

While the means of deriving the initial RAB value may differ between regulated services, there is consistency in the approach in instances in which the initial RAB value is derived by updating a base valuation. In these cases, the updating process will include adjustments to reflect such items as capital additions, disposals, revaluations (to the extent that they have been taken into account in pricing) and depreciation.

- 297 It is the Commission's preliminary view that if the initial RAB value is established by updating a base valuation, then supporting disclosure of the methodology and assumptions would be required for transparency.

Q.41) Do you agree that if the initial RAB value is established by updating a base valuation, then supporting disclosure of the methodology and assumptions will be required for transparency? If not, please provide the reasons for your view.

### 6.3.2 Roll Forward of the Initial RAB

- 298 Chapter 6 of the Input Methodologies Discussion Paper, indicated that the typical formula to roll forward the value of the RAB is as follows:

$$\begin{aligned} \text{RAB value (end of year)} = & \text{RAB value (beginning of year)} - \text{Depreciation} \\ & + \text{Revaluations} + \text{Capital Expenditure} + \text{Acquisitions} \\ & - \text{Disposals}^{59} \end{aligned}$$

- 299 The Input Methodologies Paper also outlines the Commission's preliminary views on rolling forward the initial RAB value, including that:
- the initial RAB value should be rolled forward using CPI indexation, unless there are specific circumstances that are likely to merit an un-indexed approach. The Commission considers that land could possibly continue to be valued at opportunity cost, or indexed to an appropriate land value index, provided associated revaluation gains and losses are appropriately taken into account;<sup>60</sup>
  - the RAB value should be reduced if a non-specialised asset such as land is removed from the asset base, using the relevant opportunity cost (market value) at the time of removal;<sup>61</sup> and
  - the primary form of regulatory depreciation that should be applied by suppliers under Part 4 is straight-line depreciation calculated using the physical life of the asset.<sup>62</sup>
- 300 It is the Commission's preliminary view that disclosures relating to the roll forward of the RAB should be sufficiently transparent so as to show the above calculation.

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<sup>59</sup> Ibid., paragraph 6.113.

<sup>60</sup> Ibid., paragraph 6.293.

<sup>61</sup> Ibid., paragraph 6.185.

<sup>62</sup> Ibid., paragraph 6.213.

Q.42) Do you agree that disclosures relating to the roll forward of the RAB should be sufficiently transparent so as to show the roll-forward calculation? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### **6.3.3 Capital expenditure reviews**

- 301 The role of capital expenditure reviews in seeking to ensure only efficient investment is reflected in the RAB of regulated business units has been discussed in the Input Methodologies Discussion Paper.<sup>63</sup>
- 302 In summary, where information disclosure is the only regulatory instrument, a regulator does not generally make any *direct* adjustments in respect of capital expenditure efficiency and prudence. If a supplier was also subject to an alternative regulatory instrument however, then direct adjustments may be made to the value of the RAB on the basis of efficiency or prudence.
- 303 Therefore, the roll forward of the RAB will need to allow for adjustments to the RAB where adjustment is required as a result of expenditure efficiency and prudence review under another regulatory instrument, such as customised price-quality regulation or individual price-quality regulation.

### **6.3.4 Types of Regulated Assets**

- 304 The Input Methodologies Discussion Paper outlines the Commission's preliminary views on what types of assets should be included in the RAB.<sup>64</sup> It is noted that the Commission has requested through the Input Methodologies Discussion Paper feedback on this preliminary view. It is the Commission's preliminary view that the types of assets to be included in the RAB for information disclosure should be aligned to those that are described in the Input Methodologies Discussion Paper.

### **6.3.5 Classification of Assets**

- 305 The RAB commonly distinguishes between system fixed assets and non-system fixed assets for reporting and analysis purposes. The Commission's preliminary view is that the distinction between system fixed assets and non-system fixed assets under an indexed or un-indexed historic cost roll-forward approach is not required for the on-going purpose of information disclosure. However, this may be required for the disclosure of the initial RAB value. It is considered that specifying asset classes within the total RAB, rather than seeking to distinguish between system and non-system fixed assets is more appropriate for information disclosure. Chapters 11 to 14 provide the Commission's preliminary views on what asset categories should be used for each type of regulated service.

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<sup>63</sup> Ibid., paragraph 6.241.

<sup>64</sup> Ibid., paragraphs 6.9-6.15.

Q.43) Do you agree that the distinction between system fixed assets and non-system fixed assets under an indexed or un-indexed historic cost roll-forward approach is not required for the on-going purpose of information disclosure? If not, please provide the reasons for your view.

### **6.3.6 Determination of Assets Lives**

- 306 Asset lives are a key component in determining the allowable depreciation charge in the ROI, with the other significant component being the depreciation method. The Commission's preliminary view, as outlined in the Input Methodologies Discussion Paper, is that regulated suppliers should apply straight-line depreciation using the physical life of the asset. As with prescribing the depreciation method, establishing asset lives should not affect whether or not the supplier earns a normal return on their investments over time. However it can affect cash flows and also the calculation of ROI during the life time of the asset.
- 307 The Commission sees value in specifying lives for the main types of regulated assets with asset lives revisited periodically so that they continue to reflect the useful economic lives of significant regulatory assets or asset classes.

### **6.3.7 Shared Asset Costs**

- 308 Paragraph 202 notes that a possible way of treating costs associated with shared assets would be to make an adjustment to the final RAB value, depreciation and revaluations, which would be representative of the capital cost attributed to the portion of the RAB that is not earning regulated revenue. This section discusses those adjustments.
- 309 To remove parts of assets from the RAB would be challenging especially when the proportion of the assets varies from year to year. Therefore, the Commission's preliminary view is that an adjustment should be made to the RAB subsequent to the RAB being rolled forward. The adjustment to the RAB would represent the value of the RAB that is attributed to another activity. However, to exclude all effects of that attributed asset, depreciation and revaluations would also be required to be adjusted.
- 310 It is the Commission's preliminary view that disclosure of the basis of the calculation of the attribution would be required, given the impact that adjustments to the asset base have on performance measures, such as return on investment, that are used by interested persons to assess efficiencies.

Q.44) Do you agree that if shared asset costs were to be excluded from the RAB this should be done by way of an adjustment to the final RAB value, depreciation and revaluations? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **6.3.8 Leased and Owned Assets**

- 311 It is standard business practice for businesses to utilise lease arrangements to manage financing and other business risks. In the context of the information



disclosure regime, it is the Commission's preliminary view that businesses should manage these arrangements as they see fit. The use of lease arrangements can, however, distort the indicators of performance by increasing operating costs (lease costs) and reducing depreciation costs and the value of the RAB. This might compromise the comparability of measures, between regulated suppliers. It is noted that the transfer of value out of the RAB and the increase in operating costs will not affect the ROI measure as long as the adjustments are implemented in a way that ensures that suppliers are able to earn a normal return on their efficient investments.

- 312 The Commission is mindful that the treatment of lease arrangements is a complex issue and for this reason it is the Commission's preliminary view that the treatment of leases consistent with GAAP would be the most cost-effective approach.

Q.45) Do you agree that the treatment of leases consistent with GAAP is the appropriate approach under information disclosure? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **6.3.9 Asset Transactions with Other Regulated Suppliers**

- 313 As discussed in paragraph 197 it is the preliminary view of the Commission that assets acquired from or sold to another regulated supplier are to be transferred at their rolled-forward RAB value. In addition, in the Input Methodologies Discussion Paper the Commission outlines its preliminary view that regulated suppliers should be compensated for the appropriate portion of any tax depreciation clawback, paid as part of the acquisition price, resulting from any such transaction.<sup>65</sup> The Commission's preliminary view is that the value of the assets transferred would be adjusted by an appropriate depreciation clawback amount prior to being included in the acquiring regulated supplier's RAB.

- 314 The disclosure of information relating to assets acquired from or sold to another regulated supplier is important to ensure transparency of any such transaction. The Commission's preliminary view is that the level of prescription of information disclosed should be consistent with that disclosed in the initial RAB and be sufficiently detailed to provide transparency.

Q.46) Do you agree that the level of prescription of information disclosed for assets acquired from or sold to another regulated supplier or business unit should be consistent with the information disclosed in the initial RAB and be sufficiently detailed to provide transparency? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **6.3.10 Finance during Construction Allowance**

- 315 As outlined in paragraph 192, the Commission's preliminary view is that compensation for finance costs occurring during construction should be provided for at the time of commissioning.

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<sup>65</sup> Ibid., paragraph 7.98.

- 316 The Commission notes that, under the existing information disclosure requirements for ELBs, allowances for finance during construction (FDC) have historically been provided for in one of two ways, being:
- including in the ODV values, used to determine the ODV valuation, an FDC allowance that represented the average financing costs associated with commissioning the individual assets (Transpower information disclosure regime); or
  - where the FDC was not inherent in the replacement costs used in the ODV values (as discussed above), an FDC allowance was applied to the total RAB value as a separate line item (EDB information disclosure regime).
- 317 Different practices may have occurred in other sectors. Therefore, in some instances, the valuations used to determine the initial RAB values may already include allowances for finance during construction, while others will not. The Commission notes, however, that finance during construction is only one of a number of factors associated with establishing an initial RAB value at an appropriate level. It is therefore the preliminary view of the Commission that the historic treatment of finance during construction is not material to the initial value of the RAB.
- 318 Under GAAP, specifically NZ IAS 23 'Borrowing Costs', the financing costs that are directly attributable to the acquisition, construction or production of a qualifying asset, are eligible for capitalisation. The financing costs are those costs that would have been avoided if the expenditure on the qualifying asset had not been made.
- 319 The eligibility to capitalise finance costs under GAAP depends on the way in which assets are funded (either debt or equity), which may result in different values being capitalised for similar assets, depending on the financing approach of the regulated supplier. This may disadvantage those regulated suppliers who choose not to use specific debt finance to fund capital projects as there will be no eligible finance costs to capitalise.
- 320 An alternative approach of compensating for finance occurring during construction, as has been applied in the past and outlined in paragraph 316, would be to apply a multiplier to the asset base which reflects the average cost of financing capital projects. This FDC allowance approach allows for all regulated suppliers to be compensated for finance during construction, irrespective of whether interest is eligible to be capitalised under GAAP.
- 321 The disadvantage of an FDC allowance approach is that the RAB value of assets would need to exclude any interest capitalised in accordance with GAAP, for the purpose of regulatory reporting. This would be necessary as otherwise those regulated suppliers that are entitled to capitalise interest would effectively get the benefit of the finance cost twice. However this adjustment to exclude capitalised interest would create an inconsistency with asset values used for financial reporting purposes and has the potential to increase compliance costs.

322 The Commission considers that financial and regulatory reporting of assets should be aligned where feasible. It is therefore the Commission's preliminary view that going forward, the actual cost of finance during construction should be capitalised in line with GAAP and that the inconsistency that results from this approach (as discussed in paragraph 319) would not materially affect consistency.

Q.47) What do you consider to be the implications of the two approaches for recognising the cost of finance during construction, being either application of an FDC allowance, or application of GAAP? Which approach do you prefer, and why?

### **6.3.11 Roll-Forward Handbook**

323 As outlined in the Input Methodologies Discussion Paper, in order for a business to implement whichever roll-forward methodology is determined through the input methodologies, the Commission will need to set the rules by which that methodology should be applied.<sup>66</sup> The Input Methodologies Discussion Paper addresses the need for a handbook, and matters that may be involved in preparing it (e.g., likely content).<sup>67</sup>

### **6.3.12 Consolidation and Reconciliation Provisions**

324 The Commission notes that under section 53D of the Act, it has the ability to require various reconciliations between the information of regulated and unregulated business units, and the consolidated position of the regulated supplier. Where more than one kind of regulated good or service is supplied, the Commission may also require the supplier to provide reconciliation between the regulated activities.

325 It is the preliminary view of the Commission that reconciliation between consolidated statutory financial reporting and regulatory reporting will be required. As is discussed in paragraph 258, it is the Commission's preliminary view that the Consolidation Statement would include a consolidation and reconciliation of the RAB value.

## **6.4 REGULATORY ASSET BASE (RAB) DISCLOSURES**

326 This section covers the Commission's preliminary views on the structure of the RAB disclosures. It is the intention of the Commission to structure the RAB disclosures so as to provide a transparent link with other disclosures of information including those of financial information, asset management information and relevant performance indicators.

327 The Commission's preliminary view is that the specified regulatory financial statements relating to the RAB should comprise :

- Regulatory Valuation Roll-Forward Report;

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<sup>66</sup> Ibid., paragraph 6.256.

<sup>67</sup> Ibid., paragraphs 6.256-6.260.

- Annual Roll forward by Asset Class Report;
- Asset Transactions with Other Regulated Suppliers Disclosure; and
- The Initial RAB Report (only required for the first disclosure).

#### **6.4.1 Regulatory Valuation Roll-Forward Report**

328 The Regulatory Valuation Roll-Forward Report would disclose the RAB value at the start of the year and the movements which roll forward that initial RAB value during the year. As noted above, the Commission's preliminary views on how the initial RAB value should be established and how this would be rolled forward are outlined in the Input Methodologies Discussion Paper.

329 This report is intended to be a transparent representation of how the RAB value has been rolled forward. The Commission's preliminary view is that the report should disclose each of the components that make up the following roll-forward amounts:

- Asset additions;
- Asset disposals;
- Revaluations, including the calculation of revaluations;
- Depreciation;
- Net acquisitions from (sales to) another regulated business unit;
- Net increases (decrease) due to changes in asset register information; and
- Any adjustments due to capital expenditure reviews (where relevant).

330 The Commission's preliminary views on what should make up each of the above items are outlined in the following paragraphs.

331 The asset additions will include the cost of assets acquired, the value of self-constructed assets at the time they are commissioned and the gross value of vested assets. Asset additions will exclude those assets that have been acquired from another regulated supplier. The value of vested assets will be added to the RAB consistent with their treatment as income in calculating Regulatory Profit.

332 The revaluation adjustment to the RAB will be consistent with the asset valuation input methodology. If the RAB is indexed for inflation, it is likely that disclosure of the revaluation calculation will be required for transparency and to ensure compliance with the revaluation requirements. The indexed revaluation must align with the revaluation figure in the Regulatory Profit calculation, as described in paragraph 168.

333 The depreciation charge is to be calculated as outlined in the asset valuation input methodology. The depreciation charge must also align with the figure used in calculating Regulatory Profit as discussed in paragraph 168.

334 Depreciation write-offs of the value of assets decommissioned are a form of accelerated depreciation, which recognises a charge that in effect recovers the final unrecovered regulatory value of the asset. This is treated like depreciation, in that

the same charge is applied against the RAB value and against income in the Regulatory Profit Statement.

- 335 The preliminary view of the Commission is that assets acquired from or sold to another regulated business are to be transferred at their rolled-forward RAB value as discussed in paragraphs 313 to 314.
- 336 As outlined in paragraph 180, an exception to reflecting changes in the RAB roll forward as income in the ROI, is the treatment of the net increase (or decrease) due to changes in the asset register. Separate disclosure of this amount is required for transparency.
- 337 Paragraph 302 notes that adjustments to the RAB will be required where the results of an expenditure efficiency and prudence review under another instrument require adjustment.
- 338 The roll forward of the RAB will need to allow for adjustments to the RAB where adjustment is required as a result of an expenditure efficiency and prudence review under another regulatory instrument. The “adjustment due to capital expenditure reviews” component has been proposed for this reason.
- 339 As outlined above, the rolled-forward RAB value may also need to be adjusted for the FDC allowance (where appropriate) and for shared asset costs (where adjustment to the RAB is confirmed as the appropriate means by which to reflect the deduction to the RAB for shared assets costs). These adjustments should be transparently disclosed in this report.
- 340 The disclosure of more than one year allows interested persons to obtain a greater appreciation of movements in the RAB value. Therefore the Commission’s preliminary view is that this should be provided for in this report.

#### **6.4.2 Valuation Roll Forward by Asset Class**

- 341 The Valuation Roll forward by Asset Class Report would disclose a summary roll forward of the RAB value by asset class. The disclosure of asset values by asset class should provide interested persons with an understanding of the types of assets regulated business units have invested in over the past. The disclosure of roll-forward information by asset class allows interested persons to understand what classes of assets have been invested in or divested over the current period.

#### **6.4.3 Asset Transactions with Other Regulated Suppliers Report**

- 342 It is proposed this report be required only when asset transactions occur between regulated suppliers or where assets are transferred between regulated business units. Its purpose is to disclose the RAB values by which the other reports are adjusted as a result of the transaction. This assists in ensuring consistency between the consequent RAB value changes for the different regulated suppliers or business units.

- 343 If adjustment to the value of regulatory assets is required to compensate regulated suppliers for depreciation claw-back costs as outlined in paragraph 313,,it is the Commission's preliminary view that this adjustment would be made in this report.
- 344 The report should provide sufficient detail so that there is a transparent link between information disclosed in each of the transacting parties' disclosures.

#### **6.4.4 Initial RAB Report**

- 345 The Initial RAB Report is intended to be a 'one-off' report for the purpose of making transparent the calculation of the initial RAB. The initial RAB report would only be required in the first disclosure under the new regime as in subsequent years, interested persons will be able to understand how the RAB has been determined from the RAB roll-forward report.
- 346 As discussed in the Input Methodologies Paper, the proposed basis for establishing the initial RAB value is to update a base valuation to become the initial RAB value.<sup>68</sup> It is proposed this report will commence as at the date of the base valuation and roll forward changes in the RAB value (similar to the Annual Valuation Update Report) up until the commencement of the initial RAB value.

Q.48) Do you agree that RAB information should be disclosed by way of a Regulatory Valuation Roll-Forward Report, Annual Valuation Roll- Forward by Asset Class Report, Asset Transactions with Other Regulated Suppliers Report and Initial RAB Report? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **6.5 SUMMARY OF DISCLOSURES**

- 347 The following table provides a summary of the proposed RAB disclosures and their purpose:

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<sup>68</sup> Ibid., paragraphs 6.105-6.112.

**Table 7: Summary of Proposed RAB Disclosures**

<b>Component</b>	<b>Purpose</b>	<b>Description</b>
Regulatory Valuation Roll-Forward Report	<p>Transparent disclosure of the RAB roll forward pursuant to the relevant roll-forward methodology.</p> <p>Links adjustments to the RAB value to the corresponding Regulatory Profit amounts.</p> <p>Discloses the RAB value used in the Performance Indicators.</p>	<p>Discloses the RAB value at the start of each year and the movements which roll forward this valuation. Report likely to disclose asset additions and disposals, revaluations, indexed or otherwise, depreciation; net acquisitions from or sales to another regulated supplier; and net increases (decreases) due to changes in asset register information.</p>
Annual Valuation Roll forward by Asset Class Report	Provides asset value information by asset classes.	Report contains a summary of the roll-forward components as disclosed in the Regulatory Valuation Roll-Forward Report but disaggregated to the asset class level and only for the current year.
Asset Transactions with Other Regulated Suppliers Report	Transparent disclosure of asset values transferred between regulated business units.	<p>Disclosure of RAB values by which the other reports are adjusted as a result of a transaction.</p> <p>Proposed that this Report be required only when asset transactions occur between regulated suppliers or business units.</p>
Initial RAB Report	Transparent disclosure of the initial RAB value.	This Report will commence at the date of the base valuation and reflect movements consistent with the appropriate Input Methodology for establishing the initial RAB value.

## **CHAPTER 7: QUALITY DISCLOSURE AND STATISTICS**

### **7.1 INTRODUCTION**

- 348 Section 53C(2)(i) of the Act specifies that the Commission may require suppliers of regulated goods or services to disclose information regarding quality performance measures and statistics. As discussed in paragraphs 97 - 98, the Commission prefers to use the term “indicators” rather than “measures”.
- 349 The Commission views quality indicators as a key factor in promoting the long-term interests of consumers and the efficient operation of regulated services. Along with financial and other performance data, they serve the purpose of information disclosure by providing information that assists evaluation of regulated suppliers’ performance in terms of s 52A(1)(b) of the purpose statement.
- 350 This chapter outlines the Commission’s preliminary views on the categories of quality information that would require disclosure, and how this contributes to meeting the purpose of information disclosure regulation. Key matters for consideration are discussed.
- 351 Statistics disclosures are used in conjunction with other performance indicators (including quality) to provide context and scale so that interested persons can make valid comparisons between suppliers of regulated services. The chapter also outlines statistics that may be disclosed by regulated suppliers in support of the quality and other performance indicators.

### **7.2 PURPOSE OF QUALITY DISCLOSURES**

- 352 Disclosure of quality performance indicators both highlights the ability of, and promotes incentives for, regulated suppliers to deliver services reflective of consumer demands, in accordance with s 52A(1)(b).
- 353 In markets in which competition is limited, in the absence of quality standards a regulated supplier may seek to increase profits through reductions in quality. This raises the potential for a deterioration of quality standards below a level that reflects consumer demand.
- 354 Information disclosure regulation may assist in preventing deterioration of quality standards and may also assist interested persons to assess whether the quality performance exceeds that demanded by consumers.
- 355 Section 52A(1)(b) requires that suppliers of regulated services have incentives to improve efficiency and provide services at a quality that reflects consumer demands. Disclosure of quality indicators and statistics, and the Commission’s summary and analysis of such information, should assist interested persons to assess whether the price-quality trade-off is targeted correctly.
- 356 Suppliers are also expected to provide services at a quality that reflects consumer demands, at the same time as they attempt to minimise their costs. Quality information, when analysed alongside cost based performance indicators, assists



interested persons to assess whether regulated suppliers are adequately minimising costs in respect of the quality provided.

- 357 Quality disclosures can also indicate the degree of a supplier's dynamic efficiency where investment in replacement, upgraded and growth related assets are aimed at improving service quality to consumers. Together with other disclosures of a supplier's approach to investment planning and timing (in particular, the AMP), quality measures are relevant to s 52A(1)(a) of the Part 4 purpose statement by helping to indicate whether appropriate investments occur at socially optimal times.
- 358 Where competition is limited, a regulated supplier may lack sufficient incentives to innovate (discover and use new information) in order to meet requisite quality expectations of consumers. In the Commission's view, quality disclosures encourage regulated suppliers to consider consumers' expectations of quality when making investment decisions.
- 359 A regulatory objective in section 52A is to promote outcomes such that suppliers of regulated services share with consumers the benefits of efficiency gains in the supply of regulated services, including through lower prices.<sup>69</sup> A gain in efficiency involves a change in cost and/or a change in performance. In the Commission's view, the disclosure of quality performance indicators enables interested persons to assess the degree to which the benefits of efficiency gains in regard to quality, and not just price, are being shared with consumers over time.

### **7.3 KEY MATTERS FOR CONSIDERATION**

- 360 The Commission's preliminary view is that regulated suppliers should be required to disclose a core set of standard quality indicators for each regulated service to allow consistency, transparency, and to more easily facilitate the comparison of regulated suppliers' quality performance. Further investigation is needed to both set the quality standards that apply to each regulated service and determine the most appropriate means of evaluating the performance of regulated suppliers against those standards.
- 361 The remainder of this section outlines the Commission's preliminary views on specifying standard quality measures and evaluating quality performance.

#### **7.3.1 *Measurement of Quality***

- 362 Table 8 below summarises the Commission's preliminary view of the concepts of quality that would most effectively allow the specification of quality indicators to serve the Part 4 purpose statement. The Commission considers that there is a clear distinction between the concepts of requisite, target and actual quality, and that this should affect the ways in which they are determined and measured. These concepts are further explained in the table below.

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<sup>69</sup> See Section 52A(1)(c) of the Act.

**Table 8: Concepts of Quality**

<b>Quality Concept</b>	<b>Description</b>	<b>Disclosure</b>
Requisite Quality	Representation of quality demanded by consumers.	AMPs
Quality Targets	Quality performance goals specified by regulated suppliers in alignment with requisite quality. Disclosed on the same basis as actual quality.	Quality and statistics disclosures AMPs
Actual Quality	Quality performance level(s) achieved by the regulated supplier. Measured using standardised quality performance measures.	Quality and statistics disclosures AMPs

*Requisite Quality*

- 363 In contrast to actual quality, requisite quality comprises the quality demanded by consumers. It is the Commission's preliminary view that under information disclosure regulation, requisite quality (in the first instance) is best determined by regulated suppliers themselves in consultation with their consumers. Refer to paragraphs 368 - 372 for discussion of how requisite quality is determined.
- 364 To the extent possible, disclosures of requisite quality should enable a comparison with actual quality. As requisite quality is determined by a supplier's consumers, the Commission's preliminary view is that it is best disclosed as part of AMP disclosures, alongside the consumer engagement requirement. This is discussed further in paragraphs 437 and 448 - 452.

*Quality Targets*

- 365 The purpose of quality targets is to disclose the target against which the regulated supplier will be assessed in terms of actual quality levels. The Commission's preliminary view is that quality targets should be specified by regulated suppliers from requisite quality, in alignment with actual quality measures.
- 366 It is the Commission's preliminary view that suppliers of regulated services should be required to disclose quality targets on an annual basis. In terms of the purpose statement (specifically s 52A(1)(a)), target quality data informs interested persons whether a regulated supplier is demonstrating an appropriate approach to investment planning. The Commission's preliminary view is that target quality should be disclosed through quality and statistics disclosures in addition to AMPs.

### *Actual Quality*

367 As distinct from requisite quality, actual quality is the quality performance level(s) achieved by the regulated supplier. Actual quality is determined from the analysis of actual performance data gathered using the core standard quality measures. The Commission's preliminary view is that actual quality should be disclosed through quality and statistics disclosures in addition to AMPs.

Q.49) Do you agree that the requisite quality, quality targets and actual quality are appropriate measurements of quality for the purposes of information disclosure? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **7.3.2 Determining Requisite Quality**

#### *Identifying Consumer Demands*

- 368 The measurement of requisite quality is complicated by diverse consumer groups potentially having a variety of service requirements. In practice, levels of quality (requisite and actual) vary between different consumer groups.
- 369 It is the Commission's preliminary view that, for requisite quality, the most pragmatic solution is for suppliers of regulated services to have the option to choose the best way to establish and disclose the requisite level of quality, provided a robust rationale (or methodology) is provided for the value that is established. The Commission would then be able to assess whether each supplier is developing and incorporating these benchmarks into their planning in an appropriate and consistent manner. The Commission should subsequently be in a better position to assess whether each supplier is delivering services at a quality that reflects consumer demands.
- 370 If regulated suppliers choose to use a different method for measuring requisite quality than those specified for the measurement of actual quality, care will need to be taken to ensure they can be reconciled to the measurement of actual quality. Refer to paragraph 437 of the AMP Chapter for discussion of the Commission's preliminary view on how regulated suppliers should be required to reconcile actual and requisite quality. The Commission considers that it would be appropriate for regulated suppliers to meet certain minimum standards when determining requisite quality, in accordance with the approach discussed in paragraph 449.
- 371 The Commission also notes that the methods of acquiring requisite quality data may differ between consumer groups within each regulated sector. For example, it may be more appropriate to collect information from large industrial customers through industry specific workshops while, residential requisite quality data may be more effectively gathered through quality focused surveys.
- 372 The Commission's preliminary view is that, for simplicity, an average of all consumers' quality results should be used in the disclosure of performance

indicators for actual quality.<sup>70</sup> This reinforces the comparability and transparency principles mentioned above.

Q.50) Do you agree that requisite quality should be disclosed by suppliers of regulated services through the AMP so that they can choose the best way to establish and disclose the requisite level of quality? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### ***7.3.3 Requisite and Target Quality, Asset Management Plans and Consumer Engagement***

- 373 As noted above, it is the Commission's preliminary view that, under information disclosure regulation, regulated suppliers are in the best position to determine requisite quality and to determine quality targets, subject to an appropriate level of engagement with consumers.
- 374 It is the Commission's preliminary view that the service quality measures, the process used to establish those measures and the progress made in achieving them should be disclosed through the AMP. The Commission can then use the summary and analysis process (specifically the AMP review process) to assess how regulated suppliers have performed.
- 375 In assessing how a regulated supplier has performed against requisite quality standards the Commission's preliminary intention is to consider:
- the process by which suppliers engage with their consumers to assess requisite quality;
  - how target quality has been determined based on requisite quality information; and
  - how the supplier has performed against target quality.

#### *Consumer Engagement*

- 376 Section 52A(1)(b) requires that suppliers of regulated services have incentives to provide services at a quality that reflects consumer demands. It is the Commission's preliminary view that to deliver services that reflect consumer demands, suppliers of regulated services should engage with consumers so as to understand consumer demands. The Commission acknowledges that this may be a costly process.
- 377 In accordance with the Part 4 purpose statement, the Commission considers that regulated suppliers should be able to demonstrate:
- how they engage or plan to engage with consumers, directly or indirectly, to explain the tradeoffs between quality and price, and to assess consumers' willingness to pay for different quality levels;

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<sup>70</sup> Except where noted in the gas pipeline and electricity distribution lines services chapters.

- what service offers or commitments they make to consumers, directly or indirectly, in response to information obtained during these engagements;
- how they make decisions about requisite quality standards;
- what types of contractual or other arrangements, if any, they enter into in relation to quality; and
- how they plan to deliver requisite quality in terms of medium-term service delivery.

378 While a specific consumer engagement criterion existed within the quality thresholds for EDBs under Part 4A of the Act, the Commission has previously indicated that the aims of the consumer engagement provisions should be served within the information disclosure requirements.<sup>71</sup> This proposal was supported by a number of EDBs in their submissions to the Commission following the release of the Provisions Paper.<sup>72</sup>

379 The Commission's preliminary view is, therefore, that provisions similar to the consumer engagement criterion for EDBs should be included in AMP disclosures for regulated suppliers of all three regulated services, consistent with the view that regulated suppliers are best placed to provide requisite quality information through their AMPs as described in paragraph 374 above. This is discussed further in paragraphs 437 and 448 - 452.

Q.51) Do you agree that the Commission should assess the process by which suppliers engage with their consumers to assess requisite quality, how target quality has been determined based on requisite quality information and how the supplier has performed against target quality? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

Q.52) Do you agree that suppliers of regulated services should be required to engage with their consumers and disclose how they engage or plan to engage with consumers, what service offers or commitments they make to consumers, how they make decisions about requisite quality standards, what types of contractual or other arrangements, if any, they enter into in relation to quality and how they plan to deliver requisite quality in terms of medium-term service delivery? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

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<sup>71</sup> Commerce Commission, *Regulation of Electricity lines Businesses, Targeted Control Regime, Threshold Reset 2009 Discussion Paper*, 19 December 2007, page v.

<sup>72</sup> Vector, for example, supports the Commission's view that the consumer engagement criterion should be transferred from the thresholds regime to the information disclosure requirements. See Vector Ltd, *Regulatory Provisions of the Commerce Act 1986, Response to Discussion Paper*, 16 February 2009, Appendix A, paragraph 130.

### 7.3.4 Audit of Disclosed Quality Information

380 It is the Commission's preliminary view that the disclosures of quality information should be audited. Quality is difficult to quantify, and thus more scope exists for error. The Commission's preliminary view is that an independent audit requirement for quality would increase incentives for suppliers to monitor, deliver, and disclose, service quality accurately. The Commission acknowledges the difficulties in auditing some of the quality measures, such as interruptions, and intends to set standards for the auditing of quality information where necessary. The audit requirement is discussed in further detail in chapter 10.

Q.53) Do you agree that quality information should be audited? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

## 7.4 ASPECTS OF QUALITY

- 381 Quality can be perceived and measured in different ways, therefore, the Commission sees value in outlining its preliminary view on the aspects of quality that are relevant to the information disclosure regime. Discussion on the measurement of quality for specific regulated services is covered in more detail in the service specific chapters.
- 382 This section outlines the Commission's preliminary views on the aspects of quality that are important because they assist in promoting the purpose of information disclosure regulation and how they might be best measured.
- 383 There are various ways of assessing quality performance. This can be done by measuring inputs, outputs or customer perceptions of quality.<sup>73</sup> The most appropriate method is dependent on the aspect of quality and the availability of information. Where an aspect of quality is difficult to measure, it may be more appropriate to use consumer perception as the means of measurement. However, comparability may be compromised where consumer perceptions are used. Therefore, when an aspect of quality is quantifiable it may be more appropriate to use a measurement of outputs. The Commission is also of the preliminary view that certain minimum standards should be met in terms of quantifiable outputs.
- 384 The measurement of inputs can be advantageous where the quality of service is directly related to a measurable input such as the condition of assets. The measurement of inputs can also provide insight into why service quality is poor and be an indicator of how performance may improve in the future.
- 385 Table 9 below summarises each aspect of quality that the Commission considers relevant to information disclosure regulation. These aspects of quality are discussed in greater detail below.

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<sup>73</sup> For a discussion in greater depth on the assessment of quality in terms of inputs, outputs and customer perception, see ACCC, *Guidelines for Quality of Service Monitoring at Airports (Revised March 2004)*.

**Table 9: Aspects of Quality**

<b>Aspect of Quality</b>	<b>Commission's Preliminary View</b>	<b>Proposed Measurement Basis</b>
Reliability	Key aspect of quality for electricity lines and gas pipeline services. Different in nature for specified airport services.	Output
Safety	In most instances safety is monitored by other agencies (where there is a minimum safety quality standard), therefore the cost of disclosing for information disclosure purposes, in most cases, is likely to outweigh the benefit.	Input or Output
Supply Quality - Other	Should only be used to measure actual quality where quantifiable and appropriate. Otherwise should be considered by regulated suppliers in the assessment of requisite quality.	Input, Output or Customer Perception
Customer Service	Aspect of quality that is possibly most relevant to consumers of airport services. Helpful in determining quality of service for electricity lines and gas pipeline service that is not directly related to the network assets.	Output or Customer Perception

#### 7.4.1 Reliability

386 Reliability is one of the most easily perceived aspects of quality by the consumers of electricity lines and gas pipeline services. There has been wide agreement among interested parties that reliability is a core element of a quality definition applied to electricity lines services. For example, in its submission on the Commission's Process Paper for Default Price-Quality Paths, Vector stated that reliability of supply "is the 'component' of quality of service that is generally most important to our customers".<sup>74</sup>

<sup>74</sup> Vector Ltd., *Submission on Reset of Default Price-quality Path for Electricity Distribution Businesses, Process and Issues Paper*, 15 April 2009, paragraph 25.

- 387 Reliability in electricity lines and gas pipeline services is currently measured using measures of supply interruption duration (SAIDI) and frequency (SAIFI). The Customer Average Interruption Duration Index (CAIDI) is another measure of reliability that quantifies the average outage duration that any given customer experiences. The Commission's preliminary view is that reliability of supply is the characteristic of quality that is most relevant to electricity lines and gas pipeline performance. Its application to the respective information disclosure regimes for EDBs and gas pipeline businesses is detailed in Chapters 11 and 13 respectively.
- 388 Reliability may be measured in a different way for the airports sector, as the indices above may not be as relevant for non-network infrastructure sectors. Consumers of airport services, in the Commission's preliminary view, may also not view supply interruptions as highly as other measures of quality. This is discussed further in Chapter 14.

#### **7.4.2 Safety**

- 389 Although regulated suppliers' safety performance is an essential, and in instances a readily identifiable aspect of requisite quality, safety issues are seen as a minimum mandatory requirement which is already monitored to a high degree of specificity by other industry-specific regulatory organisations.<sup>75</sup> The Commission's preliminary view is that the additional benefit gained in terms of regulatory oversight by the inclusion of a safety quality aspect within the information disclosure regime would not outweigh the costs involved in developing it. In addition, regulated suppliers typically incur certification and evaluation costs in meeting minimum safety requirements. Disclosure of safety measures through information disclosure may unnecessarily duplicate these costs.
- 390 It is therefore proposed that safety not be an explicit aspect of actual quality performance indicators. As noted in paragraph 449 however, the Commission's preliminary view is that safety should be disclosed in the service levels section of an AMP.

#### **7.4.3 Supply Quality – Other**

- 391 The Commission has proposed the 'supply quality – other' aspect of quality in order to address aspects of supply quality other than reliability and safety, including capacity and qualitative passenger terminal services for specified airport services,<sup>76</sup> voltage stability for electricity lines services and pipeline pressure for gas pipeline services.

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<sup>75</sup> An example is the Energy Safety Service a branch of the Ministry of Economic Development which monitors and enforces safety within energy industries.

<sup>76</sup> For example, those related to direct customer experience, such as check-in waiting times. Refer to Chapter 14 (Specified Airport Service) for further information.



- 392 Consistent with its view expressed in the October 2008 Information Disclosure Companion Paper, the Commission considers that a measurement of supply quality, other than reliability, should comprise part of the quality disclosures for EDBs.<sup>77</sup>
- 393 Measures of supply quality are largely dependent upon the type of regulated service and the requisite quality expectations of individual consumers and consumer groups. For example, technical measurements such as voltage stability and pipeline pressure are clearly specific to electricity lines and gas pipeline sectors respectively. The Commission, alongside regulated suppliers, intends learning from the disclosures made through AMPs to ascertain the most appropriate means of measuring supply quality.
- 394 The Commission notes that certain definitions of quality of supply may, in some instances, be beyond the direct control of regulated suppliers. For example, voltage stability for EDBs is often a function of conditions at transmission level, rather than electricity distribution. In the Commission's view this is relevant when designing disclosure requirements to accurately measure supply quality that is within the influence of regulated suppliers.
- 395 In light of this, it is the Commission's preliminary view that supply quality may best be addressed as part of the AMP disclosures on requisite quality, and that the scope for including supply quality as a performance indicator or even a measure of actual quality may be limited in some instances.
- 396 Just as this aspect of quality varies between regulated suppliers in different sectors, the process for collecting and measuring supply quality may similarly vary. Where aspects of supply quality are quantifiable, such as voltage, it may be more appropriate to measure the output. Where a supply quality is not quantifiable, such as cleanliness, it may be more appropriate to measure consumer perception.

#### **7.4.4 Customer Service**

- 397 Customer service relates to how a regulated supplier interacts with consumers. It can include such aspects as the speed with which a regulated supplier responds to emergencies, answers the telephone or responds to consumer requests.
- 398 The Commission sees this as an important aspect of quality and its preliminary view is that all regulated suppliers should disclose information on their performance in relation to customer service, where relevant. This is consistent with earlier consultation on the Part 4A EDB Information Disclosure Requirements, where the Commission outlined its view that disclosure of information on the quality of customer service should be covered.<sup>78</sup>

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<sup>77</sup> Commerce Commission, *Companion Paper to the Revised Information Disclosure Requirements*, 31 October 2008, paragraph 410.

<sup>78</sup> Commerce Commission, *Regulation of Electricity Lines Businesses, Review of the Information Disclosure Regime Decision Paper*, 13 October 2005, paragraph 419.

- 399 While the Commission remains of the view that customer service is a significant measure of quality for EDBs, it believes that it could be even more important for other regulated services. For example, consumers of specified airport services may place customer service higher than other aspects of quality in determining requisite quality. In its submission to the Commission on the Provisions Paper, the International Air Transport Association (ITIA) notes that service levels and customer satisfaction as key areas of information relevant to the development of information disclosure requirements for regulated airport companies.<sup>79</sup> Consumers of specified airport services may also have a wider variety of customer service expectations than those of other regulated services. This complicates the development of customer service quality measures.
- 400 Another issue concerning the development of a customer service quality measure is that of compliance costs. Submissions on this aspect of quality in response to earlier consultation have questioned whether the cost of disclosing customer service information outweighs its value.<sup>80</sup> It is the Commission's view that the disclosure of suppliers' efforts at engaging with their consumers is essential for the development of a meaningful quality performance indicator. As stated in paragraphs 448 - 452, in the Commission's view quality data (including customer service information) should be gathered as a consequence of preparing AMP disclosures. Duplication of compliance costs should therefore be minimised.
- 401 The Commission's preliminary view is that service quality is a key aspect of quality disclosures and should be included in the disclosure requirements for all regulated suppliers to varying degrees, depending on its relevance. Customer service for each regulated service is discussed in greater detail in Chapters 11 to 14 below.

Q.54) Do you agree that the aspects of quality most relevant to suppliers of regulated services should include reliability, supply quality-other and customer service? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

## 7.5 STATISTICS

### 7.5.1 Purpose of Statistics Disclosures

- 402 Statistics disclosures are a necessary component of information disclosure regulation as they support and inform the analysis of other performance indicators. The disclosure of statistical information assists the purpose of information disclosure regulation by providing further information to allow interested persons to assess a regulated supplier's performance in the context of the Part 4 purpose statement. By providing context and scale to the disclosed information, statistics

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<sup>79</sup> International Air Transport Association, *Submission to the New Zealand Commerce Commission on Regulatory Provisions of the Commerce Act 1986 Discussion Paper*, page 21.

<sup>80</sup> *Supra* n 77, paragraph 412.

can assist in allowing a more meaningful comparison by interested persons of a supplier's performance against other suppliers within each regulated service.

### ***7.5.2 Components of Statistics Disclosures***

403 In the Commission's view, the meaningful assessment of a regulated supplier's performance indicators requires the disclosure of statistics in data categories that are identifiable with specific regulated services, and which may assist in standardising assessments for differences in the circumstances of particular regulated suppliers. The specific aspects within each category will necessarily vary between the regulated sectors. This is discussed in more detail in Chapters 11 to 14. In general terms the data required of regulated suppliers may fall into the categories described below.

#### *Asset information*

404 This category would include data related to asset age, size (including length where relevant), and where the asset is located, such as geographical terrain. Asset related statistical information is likely to be used in the assessment of several of the performance indicators, including the capital expenditure and operating expenditure ratios.

#### *Demand*

405 Demand data feeds into a number of the performance indicators, including capacity utilisation and capital expenditure growth ratio.

406 The Commission considers that information relating to both annual and peak demand should be disclosed. Such information feeds into the calculation of the capacity utilisation ratio, which can be an indicator of productive efficiency over the longer term.<sup>81</sup> Disclosure of both annual and peak demand information is intended to allow consideration of factors outside the control of the regulated supplier - such as unforeseen fluctuations in demand within the investment timeframe. The Commission would consider such unforeseen factors during the summary and analysis phase.

#### *Capacity*

407 Disclosure of statistical capacity information in relation to assets is related particularly (but not exclusively) to the assessment of capacity utilisation, and the capacity utilisation performance indicator. Capacity statistics may be a measure of quality, as with the specified airport services. This is discussed above in paragraph 391, and Chapters 11 to 14.

#### *Pricing Statistics*

408 Allocatively efficient pricing dictates that prices should reflect the cost of providing the service, at the requisite quality, for each customer class or group. By requiring

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<sup>81</sup> See paragraphs 153 to 157 for further discussion of capacity utilisation in this context.

the disclosure of pricing information by customer, interested persons can assess the relative pricing performance demonstrated by regulated suppliers at the customer level.

- 409 The Commission considers that, where appropriate, suppliers should be required to disclose pricing statistics across a variety of services, consumer classes and/or geographic areas. Unit price statistics for each category should be derived by dividing the gross income for each customer group by the total units for each group. The units for each sector would need to be specified and will depend on the drivers for generating revenue. In some sectors, it may be appropriate to have multiple units especially where a diverse range of services is provided.
- 410 From the calculated unit price, it would then be possible where appropriate to calculate a price index which is relative to each customer grouping. This enables a comparison across the specified customer categories for monitoring purposes.
- 411 The Commission acknowledges that the preparation of pricing statistics can be costly where revenue and consumption data for the consumer groups is not readily available. It is the Commission's preliminary view, however, that this information is necessary to allow interested persons to assess the regulated entities' pricing performance. The disclosure of pricing statistics for each of the regulated services is discussed further in Chapters 11 - 14.

Q.55) Do you agree that statistics information should include asset information, demand and capacity information? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

## 7.6 SUMMARY OF DISCLOSURES

- 412 The following table provides a summary of the proposed quality and statistics disclosures:

**Table 10: Summary of Proposed Quality and Statistics Disclosures**

Component	Purpose	Description
Target and Actual Quality Disclosures	To disclose suppliers' performances in meeting target quality.	Determined from actual performance data using standardised quality performance measures. Disclosed both within annual disclosures and AMPs.
AMP Quality Disclosures	To disclose suppliers' performances in providing services at a quality that reflects consumer demands.	Disclosure of requisite, target and actual quality, with a description of how requisite quality has been determined and how this compares to actual and target quality.

Component	Purpose	Description
Asset Statistics	Assists in standardising assessments for differences in the circumstances of particular regulated suppliers.	Includes information such as asset age, size, and location, (e.g. geographical terrain).
Demand Statistics	Used in the calculation of performance indicators, including the capital expenditure, operational expenditure, and capacity utilisation ratios.	Includes annual and peak demand information.
Capacity Statistics	Used in the calculation of capacity utilisation ratio. May also be a measure of quality in regard to specified airport services.	Exact units of measurement are sector specific.
Pricing Statistics	Allows assessment of pricing at the consumer level.	Disclosures of prices across a variety of services, consumer classes and/or customer groups. Unit price statistics are sector specific, based on specific revenue drivers.

## CHAPTER 8: ASSET MANAGEMENT PLANS

### 8.1 INTRODUCTION

- 413 Section 53C(2)(h) of the Act specifies that the Commission may require suppliers of regulated services to disclose AMPs.
- 414 This chapter outlines the Commission's definition of asset management as a discipline, and the purpose of disclosing an AMP. The chapter also discusses a number of key issues that arise in respect of an AMP disclosure requirement. Finally, it discusses each of the categories of information that may be contained in an AMP that the Commission considers to be relevant for the purpose of information disclosure. This includes a discussion of the role of each category of information in the context of promoting the purpose of the regulatory regime.
- 415 It is the Commission's preliminary view that a requirement to publicly disclose an AMP should be applied to all sectors regulated under the Act, with the exception of Transpower (as long as comparable provisions for Transpower are in place outside the Act).<sup>82</sup>
- 416 The Commission has previously defined asset management, in a broad sense, as the development and implementation of plans and processes, encompassing management, financial, consumer, engineering, information technology and other business inputs to:
- assess and record the nature, location, condition and performance of assets;
  - develop and implement plans for the acquisition, creation, maintenance, operation, refurbishment, repair and disposal of its assets;
  - ensure that the level of service provided to consumers through the use of its assets meets the supplier's internal targets, including those for requisite quality, and its regulatory and statutory obligations;
  - minimise the risks associated with the failure or reduced performance of assets; and
  - develop, test or simulate and implement contingency plans to deal with events which have a low probability of occurring, but are realistic and would have a substantial impact on consumers,
- in a way which minimises cost to consumers over the expected life cycle of assets.<sup>83</sup>

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<sup>82</sup> It is noted that Transpower's major asset-related expenditure is regulated by the Electricity Commission under Part F of the Electricity Governance Rules 2003. Transpower is excluded as it is already required to submit investment related planning information to the Electricity Commission for approval. See paragraph 680 for further discussion.

<sup>83</sup> Commerce Commission, *Regulation of Electricity Lines Businesses Asset Management Plans: Revised Information Disclosure Requirements and Handbook Decision Paper*, 31 March 2006, paragraph 10.

## 8.2 PURPOSE OF ASSET MANAGEMENT PLANS

- 417 The requirement to disclose an AMP serves to fulfil the statutory purpose of the information disclosure regime, by contributing to the provision of sufficient information to allow interested persons to assess if the purpose of Part 4 is being met.<sup>84</sup> Disclosure of an AMP more directly serves s 52A(1)(a) and (b) of the purpose statement in Part 4 of the Act (the purpose statement) by requiring disclosure of regulated suppliers' asset management practices and the incentives they follow in the management of, and investments in, their assets.
- 418 In the Commission's view, sound asset management planning is an integral part of ensuring that, over the long term, interested persons can monitor whether or not regulated suppliers face appropriate incentives to innovate, improve efficiency and provide services at a price and quality that reflects the demands of consumers. Although preparing and putting into practice an effective AMP is not a costless exercise, the Commission considers that suppliers of infrastructural services subject to competitive market pressures would make the preparation and implementation of such a plan a priority, as part of good asset management practice.
- 419 In the absence of workable competition, a business may lack sufficient incentives to improve its processes and procedures, and ultimately the goods and/or services it supplies to meet the needs of its consumers. An AMP disclosure requirement helps to:
- increase the amount of information available to consumers of the business' goods and services, and to the market more generally, thereby promoting the s 53 A purpose of information disclosure;
  - promote the engagement of suppliers of regulated services with consumers so that consumers' quality and service expectations can be more readily understood and incorporated into asset management planning; and
  - encourage a regulated supplier to assess its own asset management related activities, with a view to the investment incentives being followed and the outcomes promoted by the purpose statement.
- 420 By requiring disclosure of forecast capital and maintenance expenditure, interested persons can determine (often in combination with other information disclosure components) if a regulated supplier controls its asset-related costs by using inputs efficiently (consistent with s 52A(1)(b)). By requiring the disclosure of quality information, an AMP disclosure requirement can assist in an assessment of the way a business allocates resources to provide services at the quality expected by its consumers, over time. This is also consistent with s 52A(1)(b).
- 421 The publication of the results of the Commission's summary and analysis of AMP disclosures may either support the regulated suppliers' capital expenditure decisions, or raise concerns that the purpose of Part 4 is not being met. In this way,

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<sup>84</sup> See Section 53A of the Act.

the effectiveness of suppliers' decision-making may be increased by virtue of indirect incentives. These indirect incentives are also consistent with promoting the long-term benefit of consumers (i.e., with the purpose of Part 4) and may include:

- reputational effects – boards and management may react to avoid the public perception that their AMPs (and by implication, their asset management practices) are of poor quality;
- strategic responses by suppliers to possible future initiatives arising from analysis of the information (e.g., a supplier could seek to improve the efficiency of capital expenditure to mitigate the 'threat of regulation');
- incentives for a regulated supplier to engage with its consumers (e.g., better informed users may be better able to communicate their preferences to the regulated supplier); and
- for those suppliers that are also subject to price-quality regulation, the possibility that imprudent investments may be written down ex post under a different regulatory instrument (e.g., regulated suppliers submitting customised price-quality proposals may be subject to a prudency review of past investments).

422 The Input Methodologies Discussion Paper also notes that in regard to the purpose of information disclosure regulation, an important characteristic is that it does not involve direct intervention by the regulator in setting prices or enforcing performance standards. Where information disclosure is the only regulatory instrument, the Commission would not make any direct adjustments in respect of capital expenditure efficiency and prudency, which might otherwise result in amendments being made to proposed additions to the RAB. Information disclosure regulation can encourage, but not ensure, that only prudent and efficient capital expenditure is added to the RAB, and thus whether they have appropriate incentives to invest and improve efficiency.<sup>85</sup>

423 For these reasons, the Commission's preliminary view, as stated in the Input Methodologies Discussion Paper, is that certified AMPs should be produced by all regulated suppliers, with the exception of Transpower. This will help ensure that interested persons are able to assess whether suppliers are adding appropriate assets to the RAB, and thus whether they have appropriate incentives to invest and improve efficiency.<sup>86</sup>

### **8.3 KEY MATTERS FOR CONSIDERATION**

#### ***8.3.1 Best Practice Asset Management***

424 The Commission considers that requiring the disclosure of an AMP may promote best practice asset management within regulated sectors. The Commission

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<sup>85</sup> Supra n 2, paragraph 6.225.

<sup>86</sup> Ibid., paragraph 6.241.



anticipates that regulated suppliers would apply best practice asset management principles in the preparation of their AMPs.

- 425 The Commission is interested in exploring options for incorporating recognised AMP standards into the AMP requirements. One such set of standards is PAS 55 - a publicly available specification published by the British Standards Institution that gives guidance and good practice on asset management in regulated industries. Certification against PAS 55 is gaining support with regulators and businesses in a growing number of industries, including energy and water infrastructure industries in the UK.<sup>87</sup> While the Commission has no immediate plans to apply the standard under the information disclosure requirements, the standard may have relevance to information disclosure for regulated infrastructure industries, including gas, electricity and airports infrastructure. In the Commission's view the standard may be a useful tool for organisations seeking to demonstrate professionalism in managing their physical assets. The Commission therefore suggests that regulated suppliers may wish to apply PAS 55 principles in the preparation of their AMPs.

Q.56) Do you agree that suppliers of regulated services should apply a recognised AMP standard? If so, what is the appropriate standard that should be applied? Please provide the reasons why you consider it to be preferable?

### **8.3.2 Timing of Asset Management Plans and Forecast Period Covered**

- 426 The Commission's view is that AMPs should be required to cover at least a ten-year forecast period, to allow a sufficient window for assessing expected network and/or asset developments and trends, and to be consistent across all AMPs.<sup>88</sup> Regulated suppliers should be able to disclose for a longer planning period if they wish. The Commission recognises there is greater accuracy in short to medium term planning, and therefore holds the view that detailed forecasts should only be required for the first five years of the planning period.
- 427 The Commission is also of the view that an AMP should be disclosed prior to the beginning of each financial year. This is with the understanding that the respective financial years of the Electricity, Gas and Airports sectors begin at different times throughout a calendar year. In the Commission's view, disclosure after the beginning of the financial year from which the AMP forecast period is measured reduces the extent to which an AMP can be used as a key internal planning document for the forecast period.

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<sup>87</sup> For further information see [www.ofgem.gov.uk](http://www.ofgem.gov.uk); [www.ofwat.gov.uk](http://www.ofwat.gov.uk), and the website of the British Standards Institute, [www.bsi-global.com](http://www.bsi-global.com).

<sup>88</sup> This is supported by Parson Brinckerhoff Associates in their paper *Electricity Distribution Businesses Asset Management Plans and Consumer Engagement: Best Practice Recommendations*, April 2005, paragraph 5.2.2.3.

Q.57) Do you agree that AMPs should cover at least a ten-year forecast period? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### 8.3.3 Certification of AMPs

- 428 Certification of EDB AMPs is currently required in the form of a statutory declaration, under which a Director of a regulated supplier declares that the AMP is a true copy of information made available to the public; and also in the form of a Directors' certificate, in which two Directors of the supplier certify that an AMP complies with the information disclosure requirements.
- 429 As discussed in paragraph 544 and Table 14, the Commission's preliminary view is that this dual certification should apply to AMPs for all regulated services. This is to both incentivise oversight of asset management planning at the governance level within regulated suppliers, and to encourage the regular reporting of asset management outcomes at the Board level.
- 430 The Commission's preliminary view is that certification by Directors for AMPs should be enhanced to certify that an AMP describes actual processes and practices implemented by the business.<sup>89</sup> In the Commission's view this would strengthen incentives for developing good quality AMPs generally, and would provide interested persons with greater assurance that the contents of an AMP reflect the suppliers' actual decisions.
- 431 A secondary benefit of AMP disclosures is to instil and disseminate good asset management practice among regulated suppliers over time, and thereby to promote the management of assets with the long-term benefit of consumers in mind (in promotion of the purpose statement). The Commission considers that certification by directors that AMPs describe implemented processes and practices would strengthen this incentive.

Q.58) Do you agree that the AMPs should be certified by Directors that they are compliant with the requirements and that the AMP describes actual process and practices implemented by the business? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### 8.3.4 Asset Management Plan Reviews

- 432 As noted in paragraph 119, the Commission considers that performance indicators relating to the way in which suppliers plan their investments, and the timing of those investments, will be required to allow interested persons to assess the efficiency of regulated suppliers investments, in terms of the purpose statement (s 52A(1)(a) and (b)).

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<sup>89</sup> Current certification requirements for directors of EDBs introduced in 2008 require directors to certify that the AMP complies with the disclosure requirements, not that the AMP describes the processes and practices actually used by the EDB. For further discussion, see *Supra* n 2, paragraph 6.240.

433 The Commission is also of the preliminary view that enhancements to the AMP review process, when applied across all sectors regulated under the Act, will increase the value of AMP disclosures for regulated suppliers and interested persons alike.

434 Under the information disclosure requirements currently applicable to asset management reviews for EDBs, the Commission undertakes (assisted by external experts) and publicly discloses an annual review of AMPs as part of its summary and analysis obligations under the Act.<sup>90</sup> This assists interested persons as not all interested persons will have the ability or resources to assess regulated suppliers' levels of innovation and efficient investment from the AMP disclosures.

435 As stated in paragraph 433 above, the Commission intends to develop the AMP review to facilitate further the assessment of regulated suppliers. The Commission's preliminary view is that consideration of the following as part of the AMP review process would further the section 53A purpose of information disclosure:

- Investment and Innovation;
- Quality; and
- Energy Efficiency, Demand Side Management and Energy Losses (EDBs only).

436 A key rationale behind the preparation and public disclosure of AMPs is to allow interested persons to assess whether suppliers of regulated services have incentives to innovate and invest, in accordance s 52A(1)(a). The Commission's preliminary view is that a specific investment and innovation review should be a key criterion that informs an AMP rating performance indicator in regard to innovation and timely investment.

437 A quality criterion may include assessments of the:

- suitability of service level targets chosen by the regulated supplier, including a review of the process for setting service level targets within the business;
- actions undertaken by a supplier to self-assess its current level of service against the requisite quality, including to seek input and feedback from its consumers on its level of service and the determination of requisite quality; and
- current level of service against the requisite quality.

Service quality is discussed in detail in paragraphs 448 - 452.

438 In regard to energy efficiency, s 54Q of the Act requires that the Commission:

*"...must promote incentives, and must avoid imposing disincentives, for suppliers of electricity lines services to invest in energy efficiency and demand side management and to reduce energy losses, when applying this part in relation to electricity lines*

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<sup>90</sup> Section 53(B)(2) of the Act.

services”.

- 439 The Commission notes that the scope of this requirement is limited to suppliers of electricity lines services. The Commission’s preliminary view is to require EDBs to disclose an assessment of their investments from an energy efficiency perspective, within their AMPs. This is discussed further in paragraphs 611 and 612.
- 440 The process of carrying out an AMP review will be undertaken by the Commission, once it receives suppliers’ AMP disclosures. Therefore, it is the Commission’s preliminary view that the AMP review results would not be required to be disclosed by regulated suppliers as a key performance indicator, but would instead be made publicly available through the Commission’s Summary and Analysis Report.
- 441 In order to help interested persons assess whether the purpose of Part 4 is being achieved, it is the Commission’s preliminary intention to rate AMP disclosures on a sector-specific basis as part of the AMP review.

Q.59) Do you agree that the Commission should review investment and innovation, quality and energy efficiency, demand side management and loss reductions as part of the AMP review process for Electricity Distribution Lines Businesses? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.

### **8.3.5 Asset Management Plans in relation to Airports and Consume -Owned Electricity Distribution Businesses**

- 442 As the Commission outlined in the Input Methodologies Discussion Paper, in a light-handed regulatory environment with no ex ante approval of investments, there is a need for transparency and accountability to ensure that interested persons are able to assess whether regulated suppliers are making effective decisions about ongoing investment.<sup>91</sup> This is particularly true of sectors for which information disclosure is the only form of regulation that will apply, such as Airports and consumer-owned EDBs.
- 443 In these circumstances, it is the Commission’s view that the value of AMP disclosures is increased as information disclosure is the only means by which interested persons can assess a regulated supplier’s financial and service quality performance in light of internal processes and investment-related decisions. AMP disclosures in these conditions would greatly assist interested persons in monitoring the appropriateness of a regulated supplier’s investment and asset – related decisions.

## **8.4 COMPONENTS OF ASSET MANAGEMENT PLANS**

- 444 The Commission’s preliminary view is that the AMP information categories included below would form the core of an AMP disclosure requirement as applied to suppliers of regulated services under the Act. The Commission also notes that

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<sup>91</sup> Supra n 2, paragraph 237.

this information either represents, or at least relates to, the types of commercially relevant information that a firm should be gathering and analysing about its own business to meet the purpose of Part 4. In this respect, the Commission considers it unlikely that the requirement to disclose an AMP will have a material impact on business costs.

#### **8.4.1 Background and Objectives**

445 It is the Commission's preliminary view that an AMP should include details of the background and overall approach to, and objectives of, a regulated supplier's asset management and planning processes. This should:

- allow interested persons to compare regulated suppliers in their approach to identifying stakeholder interests;
- allow interested persons to assess how suppliers' investments are likely to be treated, and whether investments occur with the long-term benefit of consumers in mind; and
- encourage a supplier to focus upon quality of service and what investment is appropriate to provide their services at the requisite quality.

446 More specifically, the Commission's preliminary view is that this section of an AMP should include:

- The purpose of the plan – a statement declaring the intention of the supplier in preparing the AMP, and the objectives of the asset management and planning processes. These should be consistent with the supplier's vision and mission statements, and show recognition of stakeholder interests.
- A description of the interaction and relationship between the plan's purpose and other corporate goals, business planning processes, and plans;
- The period covered by the plan, and the date the plan was approved by the Board of Directors;
- A description of stakeholder interests (owners, consumers etc). AMPs should identify important stakeholders and indicate what their interests are. It should also indicate how those interests are identified, accommodated in asset management practices, and how conflicting interests are managed;
- A description of the accountabilities and responsibilities for asset management within the business at all levels (governance, executive and field operations);
- Details of asset management systems and processes, including asset management systems/software and information flows. This would include a description of the key systems used to hold asset data, the data held in each system and what it is used for; and
- A description of key asset management processes used for:
  - managing routine asset inspections and maintenance;
  - planning and implementation of development projects; and

- measuring asset performance for disclosure purposes.

Q.60) Do you agree that an AMP should include details of the background and overall approach to, and objectives of, a regulated supplier's asset management and planning processes? If not, please provide reasons for your view.

#### 8.4.2 *Assets Covered*

447 The Commission's preliminary view is that an AMP should include details of the assets covered by the plan. In general terms, this should include:

- A high-level description of the geographical area covered by the assets and the degree to which these are interlinked. The description should identify consumers that have a significant impact on operations or asset management priorities, and indicate peak capacity and/or levels of demand reached in the previous year;
- A description of how the various assets are configured and/or interlinked;
- A description of the assets by category, including an assessment of their age, value, and condition; and
- The justification for retaining or maintaining the assets. The basic justification for a supplier's asset base is that it is the minimum required to provide sufficient capacity and reliability to all consumers, accommodating reasonable growth forecasts. This allows some assessment as to whether assets are potentially over-specified.

Q.61) Do you agree that an AMP should include details of the assets covered by the plan? If not, please provide reasons for your view.

#### 8.4.3 *Service Levels*

448 It is the Commission's preliminary view that asset management planning should be demand driven, rather than supply driven. Consumers should thus play a key role in the formulation of investment planning. The focus of this AMP information category is upon service quality, with a view to the management of assets to meet the requisite quality expectations of customers.

449 Once requisite quality has been established, regulated suppliers can then establish quality targets. This setting of targets and their relationship with requisite quality is discussed in paragraphs 363 - 366. The Commission considers that disclosed AMPs should include details of the proposed levels of service across several categories including:

- Consumer oriented performance targets. This would typically include measures of safety and reliability performance including the reliability performance measures as used for gas pipeline business;<sup>92</sup>

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<sup>92</sup> This includes measures of frequency and duration of interruptions to service delivery such as SAIDI, SAIFI and CAIDI. For further discussion refer to Chapter 7, paragraph 387.

- Targets relating to asset performance, asset efficiency and effectiveness, and the efficiency of the business activity; including technical and financial performance indicators related to the efficiency of asset utilisation and operation; and
- Justification for target levels of service based on consumer, legislative, regulatory, stakeholder, and other considerations. This includes the way in which the target level for each performance indicator was determined. Targets should take account of stakeholder requirements and reflect what is practically achievable.

450 Responsiveness to consumers is an important element of service quality. When explaining target service levels, it is the Commission's view that a regulated supplier should be able to demonstrate how stakeholder needs were ascertained and translated into service level targets. For example, this may include the way in which a supplier engaged, via surveys or other means, with its consumers on service issues related to asset management.

451 Under the previous Part 4A regime the Commission included a specific customer engagement criterion in the thresholds regime for EDBs.<sup>93</sup> Reflecting on possible changes to the consumer engagement criterion under the Default Price Path (DPP) workstream, the Commission considers that this may be better placed within information disclosure regulation. This is because (due to the subjective nature of the consumer engagement criterion) the results of suppliers' various consumer engagement initiatives would effectively contribute to the s 53A purpose of information disclosure. Placing consumer engagement under information disclosure is also likely to allow regulated suppliers the flexibility to develop their own effective consultation programs without the threat of breaching a quality path.

452 For these reasons it is the Commission's preliminary view that a specific customer engagement requirement should be included in AMPs across all sectors regulated under the Act.

#### **8.4.4 Development Planning**

453 This information component requires regulated suppliers to disclose their plans for asset growth, and their methods for reaching asset related growth decisions. Information disclosed under this section, when analysed together with data from other components (such as capital expenditure information), will assist interested persons in assessing if suppliers of regulated services:

- have appropriate incentives in relation to their investment decisions;
- are being innovative in their investments, in order to provide services at a quality and cost demanded by consumers; and

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<sup>93</sup> Commerce Act, *Electricity Distribution Thresholds Notice 2004*, as published in the New Zealand Gazette 31 March 2004, Clause 6(c).

- are investing in an efficient way that will likely lead to lower costs over the planning period.
- 454 Disclosed AMPs would include a detailed description of development plans, including:
- A description of the planning criteria and assumptions. The AMP should describe the criteria used for determining the capacity of new equipment for different types of assets or different parts of the asset base;
  - Process and criteria for prioritising asset development projects. These should be aligned with the overall corporate goals and vision;
  - Demand forecasts, including the basis on which they are derived, and where constraints are expected due to forecast load increases and/or equipment constraints;
  - Policies on non-asset solutions - a description of economically feasible and practical alternatives to conventional asset growth policies. For example, approaches that would reduce demand or improve asset utilisation;
  - Analysis of the development options available and details of the decisions made to satisfy and meet target levels of service; and
  - Description and identification of the asset development programme actions to be taken, including associated expenditure projections. This would include details of projects planned for the period covered by the AMP, including details of capital budgets where available and appropriate, and separate identification of major planned works and investments.

Q.62) Do you agree that an AMP should include details of the regulated suppliers' plans for asset growth and their methods for reaching asset - related growth decisions? If not, please provide reasons for your view.

#### **8.4.5 Lifecycle Asset Management Planning (Maintenance and Renewal)**

- 455 The focus of this section is upon the businesses plan for maintenance and renewal of assets over the planning period. As for the Development Planning information category above, it provides information that assists in determining, in accordance with the purpose statement, whether suppliers of regulated services:
- have appropriate incentives in their investment decisions relating to maintenance and renewal practices; and
  - are being innovative in doing so, in order to provide services at least cost to consumers of regulated services.
- 456 In addition, information disclosed under this section, when analysed together with the performance indicators such as operating and capital expenditure information, will allow interested persons to assess whether the supplier is maintaining and/or renewing its asset base in a productively efficient way that will minimise costs to consumers of goods and services supplied over the planning period.



- 457 In this section disclosed AMPs would include a detailed description of lifecycle asset management plans, including:
- *Description of the key drivers behind maintenance planning;*
  - *Description and identification of maintenance policies* including routine and preventative inspection and maintenance, inspection types, programmes, condition monitoring and actions to be taken for each asset category, including associated expenditure projections;
  - *Separate descriptions of asset renewal and refurbishment policies and programmes*, including programmes or actions to be taken for each asset category. The supplier would outline the process for deciding whether and when assets should be replaced or refurbished, and include the factors upon which it bases these decisions;<sup>94</sup> and
  - *Asset replacement and renewal expenditure.*

Q.63) Do you agree that an AMP should include details of the regulated suppliers plans for maintenance and renewal of assets over the planning period? If not, please provide reasons for your view.

#### **8.4.6 Risk Management**

- 458 In accordance with good practice, a well designed and efficient risk management process will be implemented in a cost-effective manner. Risk management disclosures will therefore inform interested persons as to this aspect of a supplier's level of productive efficiency. They also assist interested persons in determining if a supplier can provide a reliable service (in the face of risks) in terms of the requisite quality that consumers demand.
- 459 This section focuses on the risks to assets and to maintaining service levels by requiring the supplier to demonstrate their level of preparedness, in terms of how it identifies and assesses asset related risks. It includes details of risk policies, assessment, analysis and mitigation methods, and details of emergency response and contingency plans.
- 460 In addition to indicating a supplier's preparedness for dealing with risks to assets and/or the wider business, disclosure of risk management practices provides information that interested persons may wish to consider when assessing a supplier's wider approach to asset related planning in general.

Q.64) Do you agree that an AMP should include details of risk policies, assessment, analysis and mitigation methods, and details of emergency response and contingency plans? If not, please provide the reasons for your view.

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<sup>94</sup> In common with the development planning section above, this would include details of renewal and refurbishment projects planned for the period covered by the AMP, including budgeting details, and a separate identification of major planned works and investments.

#### **8.4.7 Evaluation of Performance**

461 This section of an AMP is a regulated supplier's assessment of its performance against its own financial and service level targets as they relate to asset management planning. It includes details of performance measurement, evaluation, and actions to be taken for improvement.

462 A key aim of an AMP disclosure is to identify significant asset performance gaps that need to be addressed, or to highlight the need for adjustments to service level and asset performance targets that may be, for example, required to meet consumer demands as intended under the purpose of Part 4. The self-evaluation of performance against financial and service quality related targets is intended to:

- encourage suppliers to set realistically achievable goals, and to focus the attention of the supplier and interested persons upon the efficiency of its target-setting process;
- assist in identifying (in concert with other information disclosure components) whether the business has consistently met the needs of its consumers at the optimal time through its quality and financial performance;
- serve the purpose statement by, in part, focussing a regulated supplier's attention upon the tenets of good asset management practice and encourage the following of proper investment incentives (i.e. with the demands of consumers in mind); and
- serve the intent of the 2006 GPS referred to in paragraphs 55 - 57 above, in which a stated purpose of regulatory control is to hold regulated suppliers accountable for their investments. While information disclosure cannot 'control' investment behaviour, it is intended to enable interested persons (such as consumers) to do so.

463 Key criteria of this information category are:

- a review of progress against plan, both physical and financial, including explanations for any significant differences between forecast and actual performance, in both growth and maintenance related expenditure categories;
- an evaluation and comparison of actual performance against targeted performance objectives; service level and asset performance measurement should be carried out for all the targets discussed under the Service Levels section of the AMP; and
- gap analysis and identification of improvement initiatives, including a description of any initiatives taken to address gaps between targeted and actual performance.

#### **8.4.8 Expenditure Forecast and Reconciliation**

464 The disclosure of expenditure against forecasts is intended to encourage regulated suppliers to justify their investments in light of expenditure provided for in regulated revenues and prices.

- 465 In common with the AMP requirement to self-evaluate performance (see paragraphs 461 - 463 above) the Commission believes that it is important that, where practicable, the businesses are accountable for making those investments.<sup>95</sup> This ensures that the interests of consumers are protected against “gaming” by the regulated business when regulated revenues are set based on forecasts of efficient capital expenditures. Where actual capital expenditure over the control period falls below the amounts forecast, such differences should be due to efficiency gains, rather than to the regulated business reducing service quality below levels that consumers demand.
- 466 Under the information disclosure requirements for AMPs currently in place for EDBs, suppliers of regulated services must disclose:
- forecasts of capital and operating expenditure for the minimum ten year asset management planning period; and
  - reconciliations of actual expenditure against forecasts for the most recent financial year for which data is available.
- 467 The Commission’s preliminary view is that capital and operational expenditure forecasts should be disclosed, in accordance with historical disclosure requirements, in the AMPs of all suppliers regulated under the Act. Disclosure of this information draws attention, over time, to a supplier’s success at minimising its operating and maintenance related costs.
- 468 The Commission considers it to be of value to readers of AMPs to be able to compare previous forecasts with reported actual expenditure. Enabling interested persons to review variances from forecast expenditure allows them to review the incentives followed by suppliers in their investment behaviour.<sup>96</sup> It also imposes a forecasting discipline on regulated suppliers to disclose forecasts that are rigorous and realistic. It also helps maintain consistency year-on-year in the categorisation of expenditure, assisting in maintaining a high standard of information disclosure integrity over time.
- 469 The comparison between forecast and actual expenditure will also assist in informing both the regulated supplier and interested persons of the degree to which the supplier is anticipating and allowing for growth (or decline) in the demands made by the consumers of its services, in its investments. This serves the aim of information disclosure, and of the wider purpose of Part 4 (s 52A(1)(b) in particular).

Q.65) Do you agree that an AMP should include a regulated supplier’s assessment of its performance against its own financial and service level targets as they relate to asset management planning? If not, please provide the reasons for your view.

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<sup>95</sup> This is consistent with s 8(b) of the 2006 GPS.

<sup>96</sup> This helps to fulfil s 52A(1)(b) of the Part 4 purpose statement in particular.

## 8.1 SUMMARY OF DISCLOSURES

470 The following table provides a summary of the proposed AMP disclosures and their purpose:

**Table 11: Summary of Proposed Asset Management Plan Disclosures**

Key AMP Category	Purpose	Brief Description
Background and Objectives	Allows comparison of regulated suppliers': <ul style="list-style-type: none"> <li>▪ approach to identifying stakeholder interests;</li> <li>▪ investment incentives; and</li> <li>▪ encourages regulated suppliers to focus on quality aspects of their own operation.</li> </ul>	High-level view of regulated suppliers' approaches to investment behaviour and efficiency. Includes details of the suppliers' approaches to asset management and planning processes.
Assets Covered	Provides readers with an understanding of the assets addressed in the AMP.	Description of assets by category, geographical area covered by the assets, and how they are interlinked. Includes a justification for the assets.
Service Levels	Allows assessment of degree to which asset management meets the requisite quality expectations of consumers.	Details of proposed service levels and targets including: consumer oriented performance, asset performance, asset efficiency and effectiveness, and efficiency targets.  Also includes justification for target service levels, through the assessment of requisite quality.

Key AMP Category	Purpose	Brief Description
Development Planning	<p>Allows the assessment and evaluation of a business unit's plans for growth, its degree of innovation in doing so, and the incentives for its investment behaviour. Informs the assessment of investments' contribution to lowered costs.</p>	<p>Disclosure of plans for asset growth, and their methods for reaching asset related growth decisions. Would include descriptions of development plans, planning criteria, priorities, forecasts, non-asset solutions (if any), analysis of the development options and decisions, and descriptions of asset development programme actions to be taken.</p>
Lifecycle Asset Management Planning	<p>Assists assessment of whether suppliers:</p> <ul style="list-style-type: none"> <li>▪ are following appropriate incentives in their investment decisions relating to maintenance and renewal practices; and</li> <li>▪ are innovating to provide services at cost and quality demanded by consumers.</li> </ul>	<p>Includes descriptions of lifecycle asset management planning, including: key drivers behind maintenance planning; identification of maintenance policies and projections; asset renewal and refurbishment policies; and replacement and renewal expenditure.</p>
Risk Management	<p>Allows assessment of cost - effectiveness of suppliers' risk management procedures, potentially of wider approach to asset related planning, and whether they could fulfil requisite quality (in terms of reliability) in the face of perceived risks to supply.</p>	<p>Demonstrates suppliers' risk preparedness in terms of how they identify and assess asset related risks. Includes details of risk policies, assessment, analysis and mitigation methods.</p>

Key AMP Category	Purpose	Brief Description
Evaluation of Performance	<ul style="list-style-type: none"> <li>▪ Encourages the setting of realistic performance targets;</li> <li>▪ Assists with the assessment of a supplier's ability to meet customer needs prudently; and</li> <li>▪ Encourages good asset management practice.</li> </ul>	Key criteria include a review of progress against plan; evaluation and comparison of actual performance against targeted performance objectives; and gap analysis and improvement initiatives.
Expenditure Forecasts and Reconciliation	Informs the assessment of productive efficiency, and investment and innovation. Imposes forecasting discipline on regulated suppliers. Encourages forecasting consistency.	Includes forecasts of capital and operating expenditure for the minimum ten year asset management planning period; and reconciliations of actual expenditure against forecasts for the most recent financial year.

## **CHAPTER 9: PRICING AND OTHER DISCLOSURE PROVISIONS**

### **9.1 INTRODUCTION**

- 471 This chapter provides an overview and the Commission's preliminary views of information disclosure requirements regarding prices, terms and conditions and pricing methodologies (s 53C(2)(c)), contracts (s 53C(d)), and assumptions, policies and other methodologies used or applied (s 53C(2)(j)).
- 472 The first section discusses the disclosure of pricing and related disclosures (being pricing methodologies, prices, terms and conditions of prices, pricing statistics and contract disclosures). The second section discusses the proposed disclosures for assumptions, policies and other methodologies disclosure requirements.

### **9.2 PRICING DISCLOSURES**

#### **9.2.1 Purpose of Pricing Disclosures**

- 473 One of the objectives of Part 4, as outlined in section 52A(1)(c), is to promote outcomes that are consistent with outcomes produced in competitive markets such that suppliers of regulated goods or services share with consumers the benefits of efficiency gains in the supply of the regulated goods or services, including through lower prices.
- 474 Requiring regulated suppliers to disclose pricing information (including pricing methodologies, prices and pricing statistics) provides information to assist interested persons to assess whether regulated suppliers are pricing efficiently, or at least applying efficient pricing principles to the extent practicable, based on the service quality demanded by consumers.
- 475 The assessment of efficient pricing requires an understanding of the terms and conditions associated with prices. Typically, suppliers in monopolistic positions not only have the power to control prices but also the terms and conditions of supply, such as payment terms. Unduly onerous terms allow for a transfer of wealth through means other than price. The disclosure of the terms and conditions of prices and contracts allows an assessment of the true price to be made.
- 476 Efficient pricing would be expected to result in profitability that achieves a normal return for the business, thereby limiting suppliers in their ability to extract excessive profits (i.e., consistent with s 52A(1)(d)). A normal return would also suggest that suppliers were sharing the benefits of efficiency gains with consumers (consistent with s 52A(1)(c)). The ROI calculation, as discussed and specified in Chapter 4 (paragraphs 204 and 205), is an assessment of whether prices, in aggregate, are generating a normal economic return for the business.
- 477 However, an assessment of allocative efficiency also requires the consideration of pricing components of different consumer groups and products and services (i.e., to monitor whether s 52A(1)(b) is being achieved). For interested persons to assess if there is pricing efficiency *between* different consumer groups ideally an

understanding of the price and costs across consumer groups and products and services would be assessed. Practically this can be difficult where cost or price information per consumer group or services is not readily available. Therefore analysts may use only price information or even an estimation of price so as to get an indicator of allocative efficiency between consumer groups.

478 Disclosure of pricing statistics provides a means of comparing (between regulated suppliers and consumer groupings) revenue earned from consumer groupings, which assists interested persons assessing pricing efficiency as outlined in paragraph 477. Details of pricing statistics disclosures are discussed in paragraphs 408 to 411.

479 Disclosure of contractual terms and conditions relating to price provides information regarding obligations around pricing such as frequency and notification of increases. It therefore provides the basis for interested persons to make an assessment of “true” pricing between the regulated supplier and the counterparty.

### **9.2.2 Pricing Methodology Disclosure**

480 Under s 53F, suppliers that are subject only to information disclosure regulation do not have to apply pricing methodologies that are set by the Commission.<sup>97</sup> However, under s 53C(2)(c) the Commission may still require the disclosure of pricing methodologies. The transparent disclosure of pricing methodologies is important as it assists interested persons to assess whether the principles for allocatively efficient pricing (as outlined in the Input Methodologies Discussion Paper) are applied in the methodology.<sup>98</sup>

481 The regulatory approach to the establishment of pricing methodologies is discussed in the Input Methodologies Discussion Paper. This outlines various options for pricing methodologies and discusses the disclosure of pricing methodologies in regard to the requirement to provide sufficient information for interested persons to assess if the purpose of Part 4 is being met.<sup>99</sup>

482 It is the Commission’s preliminary view that all regulated suppliers, including consumer-owned EDBs and suppliers of specified airport services (who are exempt from applying pricing methodologies), should disclose and publish their pricing methodology. This preliminary view is irrespective of the regulatory approach to the input methodology for pricing methodologies. It is consistent with s 53F(2)(b) of the Act, which provides that suppliers who are only subject to information disclosure regulation may still be required to disclose information about the pricing methodologies that they use.

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<sup>97</sup> Regulated suppliers that are also subject to price-quality regulation are required to comply with pricing methodologies specified in input methodologies.

<sup>98</sup> *Supra* n 2, paragraph 9.19.

<sup>99</sup> *Ibid.*, paragraphs 9.46 – 9.54.



- 483 The information required for the pricing methodology disclosure should be readily available from regulated suppliers that are operating in an efficient manner. Therefore the cost of complying with the pricing methodology disclosure requirements should be limited to the production of the information in a form consistent with the disclosure requirements. It is conceivable, however, that some regulated suppliers may be required to improve their pricing methodology procedures so that information is available for disclosure. The development of pricing methodology procedures would be consistent with the purpose of Part 4, in that regulated suppliers would be provided with incentives to improve efficiency.
- 484 The level of disclosure may need to be tailored for each industry sector, but it is the preliminary view of the Commission that the minimum disclosure should include:
- a description of the methodology used and how the methodology links to any applicable pricing principles;<sup>100</sup>
  - the rationale for customer groupings and the method for determining the allocation of customers to the customer groupings;
  - quantification of key components of regulated revenue and costs;
  - description of the methodology and quantification of allocation of revenues and costs to the customer groupings; and
  - customer and volume statistics.

Q.66) Do you agree that all regulated suppliers should disclose and publish their pricing methodologies? Please provide the reasons for your view.

### **9.2.3 Prices Disclosures**

- 485 Prices disclosure discloses the actual prices charged for the services provided. The prices should be determined based on the pricing methodology as discussed above. The level of disclosure of prices should be such that interested persons, including individual consumers, can identify the prices that are of interest to them.
- 486 This is different to the pricing statistics disclosure paragraph 478, which provides a means of comparing (between regulated suppliers and across consumer groups) revenue earned from consumer groups. Prices disclosures may not always allow for this comparison especially when actual charges are based on different pricing methodologies.

Q.67) Do you agree that regulated suppliers should disclose prices? If not, please provide the reasons for your view.

### **9.2.4 Terms and Conditions of Prices and Contract Disclosures**

- 487 As discussed above, disclosure of terms and conditions of supply is a means of assessing the potential of regulated businesses to exercise monopoly power.

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<sup>100</sup> Ibid., paragraphs 9.65.

- 488 The Commission's preliminary view is that the scope of contracts disclosure is limited initially to the terms and conditions for the supply of regulated services. These regulated services may be carried out by the regulated supplier or an entity employed by the regulated supplier to carry out regulated services on an outsourced basis. As knowledge of the supply of regulated services is developed, the Commission may reconsider the scope of contracts disclosure at a later date if it is determined additional disclosure would assist in meeting the purposes of the Act.
- 489 The level of disclosure may need to be tailored for each industry sector. However, the Commission's preliminary view is that contracts should be publicly disclosed within one month of taking effect, and should include :
- description of goods or services;
  - quantity or method of determining quantity;
  - price;
  - timing of payment;
  - security of payment; and
  - modifications of terms and conditions.
- 490 The Commission is mindful that disclosure of terms and conditions of supply should not compromise commercial confidentiality in respect of any single customer.
- 491 It is also noted that s 53C(4) provides that a s 52P determination may not require a supplier to publicly disclose any provision of an existing contract that, immediately before the goods or services became subject to information disclosure regulation, was not required by or under Part 4A (being Part 4A of the Act as in force immediately before its repeal by the Commerce Amendment Act 2008) or any other enactment, to be publicly disclosed.

Q.68) Do you agree that regulated suppliers should be required to disclose the terms and conditions of supply and that the scope of disclosures should be limited to terms and conditions for the supply of regulated services? If not, please provide the reasons for your view.

### **9.3 ASSUMPTIONS, POLICIES AND METHODOLOGIES DISCLOSURES**

- 492 This section discusses the assumptions, policies and methodology disclosure requirements that the Commission may require disclosure of under s 53C(2)(j).

#### ***9.3.1 Assumptions and Methodologies***

- 493 Disclosure of assumptions and methodologies, which are integral in supporting information disclosures, are required to provide transparency to disclosures.
- 494 The Commission's preliminary view is that assumptions and methodologies that support disclosed information should be included with the relevant disclosures. Where appropriate, the assumptions should be included in the disclosure templates.

### 9.3.2 Policies

- 495 Disclosure of specified policies is to enable an assessment of risks that could materially impact on the profitability or viability of the regulated business.
- 496 It is the Commission's preliminary view that, in addition to AMP policies (as discussed in chapter 8) there should be disclosure of the following policies which have the potential to affect the profitability or financial viability of a regulated business:
- Credit policy;
  - Delegated authority policy;
  - Profit distribution policy;
  - Sponsorship policy; and
  - Insurance policy.
- 497 The purpose of disclosing the credit policy would be to allow interested persons to understand if there is appropriate protection of debtor balances and that prudential requirements are fair and reasonable in regards to the risk exposure.
- 498 The purpose of disclosing the delegated authority policy would be to assess that there are appropriate levels of accountability regarding entering the company into commitments with financial implications.
- 499 The purpose of disclosing the profit distribution policy would be to assess the returns that are made to stakeholders, which may include but are not limited to consumers, employees and shareholders. Disclosure could include all profit distributions including consumer rebates and discounts, employee bonuses, and shareholder dividends.
- 500 The purpose of disclosing the sponsorship policy is to assess whether community support is distributed in a manner which provides benefits to consumers. This would be assessed by reviewing the policy to determine the selection criteria and process for awarding sponsorship.
- 501 The purpose of disclosing the insurance policy is to evaluate the level of self-insurance and associated risk exposure.

Q.69) Do you agree that that disclosure of policies will assist in achieving the stated purposes? If not, why not, and what information do you suggest would provide meaningful information?

### 9.4 SUMMARY OF DISCLOSURES

- 502 The following table provides a summary of the proposed pricing methodology, prices, pricing statistics, contracts, assumptions, methodologies and policies disclosures and their purpose:

**Table 12: Summary of Proposed Pricing and Other Disclosures**

<b>Disclosure</b>	<b>Purpose</b>	<b>Description of Disclosure</b>
Pricing Methodology	To assess whether the methodology applied to setting prices is consistent with efficient pricing principles.	Description of the methodology including rationale for customer groupings, quantification of key components of revenue and expense including the allocation to customer groupings.
Prices	Transparent disclosure of actual prices.	Disclosure of current prices and prices immediately preceding current prices at a level that interested persons, including individual customers can identify the prices that are of interest to them.
Pricing Statistics	Provides a means of comparing (between regulated entities and consumer groups) revenue earned from consumer groups.	A calculation to determine a price per unit for specified consumer groups, including a comparison with a relative unit price.
Contracts	Provides a means of assessing the potential of regulated businesses to exploit market power on non-price terms.	For the supply of regulated, and also related services. Includes a description of goods and services supplied, the method of determining quantity, timing and security of payment, and modifications to terms and conditions.
Assumptions	Assists with providing a better understanding of disclosures.	Details of assumptions.
Methodologies (other than pricing)	Assists with providing a better understanding of disclosures.	Description and quantification of any methodology used for disclosure of required information.

<b>Disclosure</b>	<b>Purpose</b>	<b>Description of Disclosure</b>
Policies	To determine the exposure to business practices that could materially impact the profitability or viability of regulated businesses.	Disclosure of policies covering credit, delegated authority, profit distribution, sponsorship and insurance.

## CHAPTER 10: PUBLICATION, RETENTION, CERTIFICATION, STATUTORY DECLARATION AND AUDIT

### 10.1 INTRODUCTION

503 This chapter discusses the Commission's preliminary views on the requirements for director certification, statutory declarations, independent audits, and publication and retention of information. The relevant provisions of the Act are outlined below.

504 Section 53B(1) outlines the effect of being subject to information disclosure regulation and stipulates that:

*Every supplier of goods or services that are subject to information disclosure regulation must-*

- (a) *publicly disclose information in accordance with the information disclosure requirements set out in the relevant section 52P determination; and*
- (b) *supply to the Commission a copy of all information disclosed in accordance with the section 52P determination, within 5 days after the information is first made publicly available; and*
- (c) *supply to the Commission, in accordance with a written notice by the Commission, any further statements, reports, agreements, particulars or other information required for the purpose of monitoring the supplier's compliance with the section 52P determination.*

Section 53C(1) specifies that a section 52P determination relating to goods or services that are subject to information disclosure regulation must:

...

- (d) *specify the manner in which the information is to be disclosed; and*
- (e) *specify the form of disclosure; and*
- (f) *specify when, and for how long, information must be disclosed; ...*

505 Section 53C(3) of the Act, amongst other things, states:

*The section 52P determination may do all or any of the following:*

- (a) *require disclosed information, or information from which disclosed information is derived (in whole or in part), to be verified by statutory declaration;*
- (b) *require independent audits of disclosed information;*
- (c) *require the retention of data on which disclosed information is based, and associated documentation:...*
- (f) *impose any other requirements that the Commission considers necessary or desirable to promote the purpose of information disclosure regulation.*

### 10.2 PUBLICATION AND RETENTION OF INFORMATION

506 This section outlines the Commission's preliminary views on the manner in which information would be disclosed, the form of the disclosures, the timing of disclosures and the retention of information supporting disclosures.

507 It is the Commission's preliminary view that performance indicators, financial, asset valuation, quality, statistics and asset management forecast information should be disclosed as an annual disclosure package (Annual Disclosure). The nature of

the AMP, pricing methodologies, prices and contracts disclosures, their disclosure dates and the different certification and auditing requirements (as outlined below) dictate that these should be disclosed separately.

### 10.2.1 Publication of Disclosures

508 Section 53B(1), as noted above, requires every supplier of regulated services that are subject to information disclosure to:

- publicly disclose information in accordance with the information disclosure requirements; and
- supply to the Commission a copy of all information disclosed within 5 days after information is first made publicly available.

509 Section 52C includes definitions of the two types of disclosure noted in s 53B(1), being:

*publicly available, in relation to making a document or information available, means that-*

- (a) *the document or information is available for inspection, free of charge, on an Internet site that is publicly accessible at all reasonable times; and*
- (b) *a copy of the document or information is available for inspection at all reasonable times, free of charge, at the head office of the person that is required to make it publicly available or, if the person is the Minister, at the head office of the department responsible for the administration of this Act; and*
- (c) *copies of the document may be purchased by any person at a reasonable price*

*publicly disclose, in relation to information required to be disclosed under information disclosure regulation, means to disclose information to the public in the manner required by a section 52P determination*

510 Under s53B(1)(b), all disclosed information must be made publicly available. However, under s53B(1)(a), the Commission may determine how information is to be "publicly disclosed" in the relevant s52P determination. This suggests that the Commission's definition of "publicly disclose" should incorporate the statutory definition of "publicly available", but may also include other requirements, such as an obligation to disclose information in the *Gazette* so that interested persons are made aware that the information has been disclosed.

511 The Commission's preliminary view is that publicly disclose should require a notice in the *Gazette* of that disclosure. The *Gazette* notice should identify the Internet site where the information disclosed can be found and where hard copies of the information disclosed can be inspected or obtained.

512 This proposed definition of 'publicly disclose' is consistent with the definition of 'publish' as included in the current EDB information disclosure requirements<sup>101</sup>.

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<sup>101</sup> Refer to Commerce Commission, *Electricity Distribution (Information Disclosure Requirements) issued 31 March 2004, consolidating all amendments to 31 October 2008, clause 2.*

- 513 The Commission's preliminary view is that the Annual, AMP and pricing methodology disclosures should be publicly disclosed so that interested persons are made aware when the disclosures are made. While prices and contract disclosures should not require notification in the Gazette, therefore, they should only be required to be made publicly available. Prices disclosures, however, should also be notified to each consumer by whom the charge is payable.
- 514 To allow for ease of comparison and analysis, the Commission's preliminary view is that where information is required to be disclosed in a standardised form, regulated suppliers should make disclosures consistent with standardised templates. It is noted, however, that it may not be practical in all instances for disclosures to be made consistent with standard templates.
- 515 Where standard templates can be used, the Commission's preliminary view is that disclosures should also be made available to the Commission in Excel format so as to better ensure that disclosures are internally consistent. The provision of Excel format disclosures will also assist the Commission in meeting its summary and analysis obligations by facilitating comparison of the relative performance of the various regulated suppliers.
- 516 For the current information disclosure requirements for EDBs, the Commission has made available an Excel template with formulae that are consistent with those requirements. The purpose of the Excel template has been to provide ease of disclosure for EDBs and a level of comfort to the Commission that disclosures are internally consistent. The Commission's preliminary view is that Excel templates are of assistance and therefore should be provided. The Commission proposes that disclosures made available to the Commission in Excel format should be required to have relevant formulae in place.

Q.70) Do you agree that publicly disclose should require a notice in the Gazette of that disclosure? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.71) Do you agree that the Annual, AMP and pricing methodology disclosures should be publicly disclosed? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.72) Do you agree that prices disclosures should also be notified to each consumer by whom the charge is payable? If not, please provide the reasons for your view.

Q.73) Do you agree that templates should be used where appropriate and that disclosures should be made available to the Commission in Excel format with relevant formulae in place? If not, please provide the reasons for your view.

### ***10.2.2 Timing of Disclosures and Regulatory Year End***

- 517 The Commission's preliminary view is that Annual Disclosure should be made no later than five months after the regulatory year end. This should leave suppliers sufficient time to prepare their disclosures while still ensuring that disclosures are timely. It is also consistent with the time allowed for preparing financial reporting



by the Companies Act 1993, which is also 5 months, and so will not require earlier preparation of financial results for regulatory purposes.<sup>102</sup>

- 518 Based on the Commission's previous experience with other information disclosure regimes, the Commission considers that AMP disclosures should be made prior to the beginning of the forecast period so as to provide timely information. The pricing methodologies in place at the beginning of the regulatory year should be disclosed at the beginning of the regulatory year and within 1 month of a change or the adoption of a different methodology. Disclosure of required contracts is to occur no later than 1 month after entering into the contract. The Commission's preliminary view is that prices disclosures should be made at least 20 working days before introducing a new charge.
- 519 The Commission's preliminary view is that the regulatory year should end on the following dates, so that where possible they are aligned to commonly used financial year ends for the appropriate regulatory service:
- |                                     |          |
|-------------------------------------|----------|
| ▪ Specified airport services        | 31 March |
| ▪ Gas pipeline services             | 30 June  |
| ▪ Electricity distribution services | 31 March |
| ▪ Transpower                        | 30 June  |
- 520 The Commission notes that the proposed regulatory year ends are aligned to the year ends used by the regulated suppliers under their current respective disclosure requirements, except Maui Pipeline Limited (MDL). It is the Commission's preliminary view that MDLs regulatory year end should not be required to align to the 30 June year end that is used by other regulated gas pipeline suppliers, as any benefit for comparability in respect of gas transmission services would likely be minimal.

Q.74) Do you agree with the proposed timing for disclosures? If not, please provide the reasons for your view.

Q.75) Do you agree with the proposed regulatory year end dates? If not, please provide the reasons for your view.

### ***10.2.3 Retention of Information***

- 521 The Commission's preliminary view is that regulated suppliers should continue to disclose information and retain disclosed information and information supporting the disclosed information for a period of at least seven years. This is consistent with retention requirements for statutory financial records.

<sup>102</sup> The Commission notes that suppliers that are listed companies subject to Stock Exchange Disclosure Rules must provide annual reports within three months of their financial year end.

Q.76) Do you agree that regulated suppliers should continue to disclose information and retain disclosed information and information supporting the disclosed information for a period of at least seven years? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### **10.3 CERTIFICATION, STATUTORY DECLARATION AND AUDIT**

522 This section outlines the Commission's preliminary views on director certification, statutory declaration and audit requirements. As noted above, the Commission has specified powers to require statutory declarations and audit reports (s 53C(3)(a) and (b)). Section 53C(3)(f) also provides the Commission with powers to require other requirements that the Commission considers necessary, such as the provision of Directors' certificates.

523 Table 15 below outlines the Commission's preliminary views on when Director certifications, statutory declarations and audits should be required.

#### ***10.3.1 Director Certification***

524 The purpose of Director certification is for Directors to certify that, having made all reasonable enquiry, to the best of their knowledge, the information being disclosed complies with the relevant requirements. The Commission's preliminary view is the Director certification should be signed by two directors and attached to the disclosures when disclosure is made, including publication on the internet.

525 The Commission's preliminary view is that Director certification should be required for the Annual, AMP and pricing methodology disclosures to certify that the information being disclosed complies with the relevant requirements. The AMP and pricing methodology Director certifications (respectively) should also certify that the:

- AMP describes actual processes and practices implemented by the business; and
- pricing methodology has been used to set disclosed prices.

526 It is the Commission's preliminary view that Director certification would not be required for prices and contract disclosures as the proposed requirements only require the disclosure of the information and do not include specific requirements about how the information is to be prepared.

527 As noted in the Input Methodologies Discussion Paper, the Commission considers that certification by Directors that the AMPs describe actual processes and practices implemented by the business would provide stronger incentives for developing good plans to reflect good, or improve bad, practice.<sup>103</sup> The Commission considers that a weakness of the current information disclosure requirements for EDBs is that the certification requirements for Directors introduced in the Electricity Distribution

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<sup>103</sup> Supra n 2, paragraph 6.240.

(Information Disclosure) Requirements 2008 require Directors to only certify that the AMP complies with the disclosure requirements, not that the AMP describes the process and practices actually used by the EDB.

Q.77) Do you agree that Director certification should be required for the Annual, AMP and pricing methodology disclosures to certify that the information being disclosed complies with the relevant requirements? If not, please provide the reasons for your view.

### **10.3.2 Audit Report**

- 528 The purpose of audit reports is to provide independent assurance that information being disclosed complies with the relevant requirements. It is the Commission's preliminary view that audit reports should be required for Annual Disclosures but not AMP, pricing methodology, prices or contract disclosures.
- 529 It is noted, however, that summary capital expenditure and operating expenditure forecasts from the AMP disclosures are also disclosed in the Annual Disclosure. It is the Commission's preliminary view that this forecast information should be audited to the extent that assurance is provided that the forecasts have been properly compiled from assumptions made or adopted in the AMP. The expected standard of assurance is outlined in Table 13 below.
- 530 The Commission's preliminary view is that the audit of prices and charges disclosure should not be required for the reason that Director certification is also not required, as discussed in paragraph 526.
- 531 To avoid any potential conflicts between disclosure requirements and mandatory professional auditing standards, the Commission's preliminary view is that the form of audit reports should be flexible enough to allow for any changes in the New Zealand Auditing Standards (issued by the New Zealand Institute of Chartered Accountants) without requiring an amendment to the requirements.
- 532 The Commission considers that, rather than providing a prescriptive template for auditors' reports, the disclosure requirements should include a number of provisions setting out the Commission's expectations in respect of the scope and content of the report, and the standard of assurance for the audit report.
- 533 Given that the audit reports need to address compliance with the requirements it is the Commission's preliminary view that the reports should include a statement as to whether the disclosures comply with the requirements and include explanations of any material non-compliance.
- 534 It is the Commission's preliminary view that different auditing requirements should apply to historical financial information, historical non-financial information, prospective (i.e. forecast) financial information and prospective non-financial information.
- 535 The Commission considers that this is necessary to recognise the difficulty in making judgments about the robustness and accuracy of forecast information.

- 536 The Commission's preliminary view is that the auditing requirements for prospective financial and non-financial information should be similar to the standard of assurance required by the Securities Regulations 1983 in respect of prospectus information for equity securities, being:

*If the registered prospectus contains prospective financial information, the auditor's report must contain a statement in the following form:*

*"In our opinion, the prospective financial information, so far as the accounting policies and calculations are concerned, has been properly compiled on the footing of the assumptions made or adopted by the issuer set out at pp.... of this prospectus and is presented on a basis consistent with the accounting policies normally adopted by the company (group)."*<sup>104</sup>

- 537 The standard of assurance required for non-financial information should recognise that the auditor is reliant on technical experts for the interpretation of technical data and so can give only limited assurance.

**Table 13: Expected Standard of Assurance**

Type of Information	Expected Standard of Assurance
Historical financial information	The information is prepared in all material respects in accordance with the requirements.
Historical non-financial information	The information is prepared in all material respects in accordance with the requirements and, where relevant, applicable industry standards.
Prospective financial information	The prospective financial information, so far as the accounting policies and calculations are concerned, has been properly compiled on the basis of the assumptions made or adopted by the company set out in the AMP and is presented on a basis consistent with the accounting policies normally adopted by the company (group).
Prospective non-financial information	The prospective non-financial information, so far as the technical measurement standards, specifications and calculations are concerned, has been properly compiled on the footing of the assumptions made or adopted by the company set out in the AMP and is presented on a basis consistent with the technical standards and practices normally adopted by the company (group).

The indicated standard of assurance is to assist consultation and is not intended to present the final wording of the audit opinions themselves, which may differ according to context.

<sup>104</sup> Securities Regulations 1983, Schedule 1, Clause 42 (2).

- 538 The Commission's preliminary view is that audit reports should be attached to the disclosures when disclosure is made, including disclosure on the internet.
- 539 It is the Commission's preliminary view that audit reports should be addressed to interested persons so as to align with the purpose of information disclosure. It is also the Commission's preliminary view that the audit report should contain a statement that acknowledges the auditor's duty of care to the Commission.

#### *Independent Auditor*

- 540 The New Zealand Institute of Chartered Accountants (NZICA) has published standards and guidance regarding auditor independence for assurance engagements (specifically CODE OF ETHICS: Independence in Assurance Engagements).<sup>105</sup>
- 541 It is the Commission's preliminary view that, in addition to adhering to these standards and guidance, auditors engaged to audit information disclosed under the information disclosure requirements should:
- be qualified for appointment as auditor of a company under the Companies Act 1993 or, where the regulated supplier is a public entity (as defined in section 4 of the Public Audit Act 2001), is the Auditor-General;
  - have no relationship with, or interest in, the regulated supplier that is likely to involve the auditor in a conflict of interest;
  - not have assisted with the compilation of the information or provided advice or opinions (other than in relation to the audit reports) on the methodologies or processes used in compiling the information; and
  - neither be associated with, nor directed by, any person who has provided any such assistance, advice or opinions.

Q.78) Do you agree that audit reports should be required for Annual Disclosures? If not, please provide the reasons for your view, an alternative to obtaining independent assurance and why you consider this to be preferable.

Q.79) Do you agree that audit reports should not be required for AMP, pricing methodology, prices or contract disclosures? If not, please provide the reasons for your view.

Q.80) Do you agree that the form of audit reports should be flexible enough to allow for any changes in the New Zealand Auditing Standards without requiring an amendment to the requirements? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.81) Do you agree that audit reports should include a statement as to whether the disclosures comply with the requirements and include explanations of any material

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<sup>105</sup> New Zealand Institute of Chartered Accountants, *CODE OF ETHICS: Independence in Assurance Engagements*, August 2003.

non-compliance? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.82) Do you consider it appropriate for there to be different assurance requirements for different types of information and what do you think they should be? Please provide the reasons for your view.

Q.83) Do you agree that audit reports should be addressed to interested persons and contain a statement that acknowledges the auditor's duty of care to the Commission? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.84) What do you consider to be an appropriate level of independence for auditors? Please provide the reasons for your view.

### ***10.3.3 Statutory Declarations***

542 The purpose of the statutory declaration is to have a Director verify that the information provided to the Commission is a true copy of the information made available to the public. It is the Commission's preliminary view that statutory declarations should be attached to all information made available to the Commission under any disclosure requirement.

#### *Consumer-owned Statutory Declaration*

543 The Commission's preliminary view is that consumer-owned EDBs should also provide to the Commission on an annual basis a statutory declaration declaring that they meet the definition of consumer-owned in s 54D of the Act. This is discussed further in paragraphs 613 and 614.

Q.85) Do you agree a statutory declaration should be attached to all information made available to the Commission under any disclosure requirement? If not, please provide the reasons for your view.

### ***10.3.4 Summary of Director Certification, Audit Report and Statutory Declaration***

544 Table 14 summarises the Commission's preliminary views on Director certification, audit reports and statutory declarations.

**Table 14: Proposed Director Certification, Audit Reports  
and Statutory Declarations**

<b>Component</b>	<b>Purpose</b>	<b>Commission's Preliminary View</b>
Director Certification (s 53C(3)(f))	To certify that information being disclosed complies with the relevant requirements.	Director certification should be signed by two Directors and attached to the disclosures when disclosure is made.  AMP certification should require additional certification that an AMP describes actual processes and practices implemented by the business.  Pricing methodology disclosures should require additional certification that they have been used to set disclosed prices.
Audit Reports (s 53C(1)(b))	To provide independent assurance that information being disclosed complies with the relevant requirements.	Only required for Annual Disclosure (not AMP or other) and should be flexible enough to accommodate changes in NZ Auditing Standards.
Statutory Declarations (s 53C(1)(a))	To verify that the information provided to the Commission is a true copy of information available to the public.	A statutory declaration should be attached to all information made available to the Commission under the disclosure requirements.  Consumer-owned EDBs should make a statutory declaration declaring that they meet the definition of consumer-owned in s 54D of the Act.

#### 10.4 SUMMARY OF PRELIMINARY VIEWS

**Table 15: Proposed Publication, Retention, Certification, Statutory Declaration and Audit Requirements**

Required Information	Proposed Package	Method of Disclosure	Timing of Disclosure	Certification Requirements
Performance indicators	Annual Disclosure	Publicly Disclose	No later than five months after regulatory year end	Certification, Audit <sup>(1)</sup> and Statutory Declaration
Financial				
Asset valuation				
Quality				
Statistics				
Asset management forecasts				
Asset Management Plans	AMP Disclosure	Publicly Disclose	Before start of forecast period	Certification and Statutory Declaration
Pricing Methodologies	Pricing Methodology Disclosure	Publicly Available	(2)	Statutory Declaration
Prices	Prices Disclosure	(3)	(4)	Statutory Declaration
Contracts	Contracts Disclosure	Publicly Available	(5)	Statutory Declaration

- (1) Some information disclosed in the annual report is likely to require different audit sign off. Refer paragraphs 534 to 537 above.
- (2) At the beginning of the regulatory year, or within 1 month of a change or the adoption of a different methodology.
- (3) Publicly available and notified in writing to each consumer by whom the price is payable.
- (4) At least 20 working days before introducing a new charge.
- (5) Not later than 1 month after entering into a contract.



## **CHAPTER 11: ELECTRICITY DISTRIBUTION LINES SERVICES**

### **11.1 INTRODUCTION**

- 545 This chapter provides an overview of the information disclosure matters unique to electricity distribution lines services and therefore covers regulated suppliers of electricity lines services other than Transpower. The first section provides an overview of the key characteristics of electricity distribution lines services that are both unique and relevant to the information disclosure regime. The second section of this chapter outlines the Commission's preliminary views on how components of the information disclosure regime should be customised for electricity distribution lines services.
- 546 Electricity lines services are regulated under subpart 9 of Part 4. The definition of electricity lines services in s 54C(1) captures both Transpower and EDBs. However, the regulatory provisions that apply to Transpower and EDBs are quite different, therefore this chapter discusses EDBs only. Transpower is considered separately in Chapter 12.

### **11.2 UNIQUE CHARACTERISTICS OF EDBS**

#### ***11.2.1 Application of Regulatory Instruments***

- 547 Section 54F provides that all electricity lines services are subject to information disclosure regulation. Section 54G(2) provides that consumer-owned suppliers of electricity lines services are exempt from default/customised price-quality regulation.
- 548 Submissions have suggested that information disclosure requirements for suppliers that are exempt from price quality regulation (on the basis that they are consumer owned) should be distinguished from those suppliers that are not exempt.<sup>106</sup>
- 549 Irrespective of whether other regulatory instruments apply to a supplier in addition to information disclosure regulation, the Commission's preliminary view is that a similar scope, detail, prescription and consistency of disclosed information would need to apply to all regulated suppliers of the same type of regulated service. This approach is considered appropriate in order to determine whether the Part 4 purpose is being met, and in order for the Commission to promote a greater understanding of the relative performance of all suppliers of the same regulated service, and their performance over time.

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<sup>106</sup> For example, PriceWaterhouseCoopers, *Submission to the Commerce Commission on the Regulatory Provisions of the Commerce Act 1986 Discussion Paper, Made on Behalf of 20 Electricity Distribution Businesses*, 16 February 2009, page 20 and 21.

### ***11.2.2 Information Disclosure for EDBs to Date***

- 550 EDBs were originally subject to information disclosure under the now revoked Electricity (Information Disclosure) Regulations 1999 administered by the Ministry of Economic Development (MED), pursuant to the Electricity Act 1992. Subsequent to this, the Commerce Act 1986, which came into effect on 8 August 2001, provided for a regulatory regime for large electricity lines businesses to be implemented by the Commerce Commission. The Commission issued an initial set of information disclosure requirements pursuant to subpart 3 of Part 4A.<sup>107</sup> These requirements have been subject to review and amendment.
- 551 The fact that EDBs have established systems and processes to comply with information disclosure regulation means that to the extent which the current disclosure requirements are consistent with the relevant provisions of Part 4, significant compliance costs should not be involved.

### ***11.2.3 Variances in EDBs Operating Environments***

- 552 The Commission is cognisant of the fact that there are many variables that impact on the performance of EDBs and which create practical difficulties for making comparisons between EDBs when reporting on their relative performance. These variables may relate to geography, consumer density, legacy pricing and cross subsidisation, network design and capacity utilisation, age of system assets, and network amalgamations, among others.
- 553 As outlined in Chapter 3, it is the view of the Commission that information disclosures should not be assessed in isolation, but should be viewed as contributing to building an overall view of EDB performance.
- 554 When assessing performance of EDBs, interested persons and the Commission through the summary and analysis process should consider these variables. The information disclosure regime should therefore provide sufficient information for interested persons to understand the variances between EDBs. Also the summary and analysis should be used to identify the relevant variables that may be affecting performance.

### ***11.2.4 Ownership Structures of EDBs***

- 555 EDBs comprise a mix of ownership structures including but not limited to public listings, shareholder cooperatives, community trusts and local body ownership, with the majority of EDBs being wholly or at least partially owned by trusts. The ownership structure of the EDB has implications for how an EDB is regulated under the Act. Under s 54F information disclosure will apply to all EDBs, however those EDBs that are not ‘consumer-owned’ are also automatically subject to default/customised price-quality regulation (s 54G). The definition of consumer-owned is outlined in s 54D of the Act.

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<sup>107</sup> Commerce Commission, *Electricity Information Disclosure Requirements 2004*.

556 A table outlining the ownership of the 29 EDBs is in Appendix B of the Input Methodologies Discussion Paper.<sup>108</sup>

*Ownership of an EDB Operating in More than One Network*

557 The ownership of an EDB operating in more than one network area can be held by consumers who are primarily resident in only one of the component networks.<sup>109</sup> Examples of this are Unison's Hawkes Bay and Rotorua / Taupo networks, and also Vector's Auckland and Northern networks. In these scenarios, the Commission considers it important that certain performance indicators for each component network are disclosed. Separate disclosure of network statistics, price statistics and quality information allows an assessment of relative performance to be made for each network area and is a requirement in the current disclosure requirements for EDBs.

*Consumer-owned EDBs Mechanisms for Returning Profits*

558 Consumer-owned EDBs frequently provide returns to consumer-owners through rebates, discounts, line charge holidays or through dividends. Generally they are distributed by way of a credit on the consumer's electricity account. EDBs disclose these distributions in different ways for statutory financial reporting depending on the method of distribution. It is the preliminary view of the Commission that for regulatory reporting purposes, the disclosure of the distribution be treated consistently across all EDBs. This is discussed in paragraphs 566 to 568.

**11.2.5 Role of the Electricity Commission**

- 559 The Government sets the objectives and outcomes that it expects of the Electricity Commission by way of a Government Policy Statements (GPS) on electricity governance. The 2009 GPS on Electricity Governance sets out the Government's expectations regarding the interrelationship between the Commerce Commission and the Electricity Commission, and continues to give the Electricity Commission, among other things, responsibility for developing model approaches to distribution pricing. The Electricity Commission is able to recommend regulations, if required, to ensure compliance with the model distribution pricing.
- 560 Both the Electricity Act 1992 and the 2009 Government Policy Statement indicate a preference for a voluntary approach to electricity distribution pricing in the first instance. Such a voluntary approach could include published pricing principles, guidelines, or a model distribution pricing methodology.
- 561 The Electricity Commission is proposing to develop a model distribution pricing methodology with the expectation that distributors will seek to align their pricing

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<sup>108</sup> Supra n 2, Appendix B, Table B1.

<sup>109</sup> EDBs, who are owned by trusts or customer cooperatives as defined in s 54D(2) and are operating in more than one network area, that do not distribute income to at least 90% of the persons who are consumers of that supplier do not meet the definition of 'consumer-owned'. See s54D(1)(d) of the Act.

methodologies to the model over time. The Electricity Commission acknowledges that it would be impractical to develop a mandatory approach, given the complexities of distribution pricing and variations between EDBs reflecting individual network design, capacity utilisation, geographical differences, historical pricing and cross subsidisation. For monitoring purposes, it is the expectation of the Electricity Commission that EDBs will report on variations from the proposed model.<sup>110</sup>

- 562 The Electricity Commission is also developing a model Use of System Agreement (UOSA) which includes a provision that the distributor will publish its final pricing methodology, prices and reasons for its decisions.<sup>111</sup> While this model agreement will be optional, the Electricity Commission will monitor the uptake and it is possible that the Electricity Commission may recommend regulation changes to the Minister of Energy.
- 563 The Commission's preliminary view is that the Electricity Commission's model distribution pricing methodology could be used as a basis from which EDBs disclose where their pricing methodologies are not aligned with the Electricity Commission's methodology and provide justification for any departures.

Q.86) Are there any additional characteristics of EDBs that would affect how the information disclosure regime for EDBs should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.

### 11.3 APPLICATION OF INFORMATION DISCLOSURE TO EDBS

- 564 This section outlines the Commission's preliminary views on how components of disclosed information should be customised to EDBs. The Commission's preliminary view is that the components of disclosed information should be as outlined in Chapters 5-10 where no customisation is proposed.

#### 11.3.1 Performance Indicators

- 565 The table below outlines the Commission's preliminary views on what performance indicators are relevant to EDBs. Chapter 3 provides further details on the objectives of each of the performance indicators and how the Commission's summary and analysis would utilise these indicators in achieving the purpose of information disclosure regulation.

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<sup>110</sup> Electricity Commission, *Distribution Pricing Methodology, Consultation Paper on a Model Approach*, 5 June 2009, page 10.

<sup>111</sup> Electricity Commission, *Model Use of Systems Agreement (Interposed)*, Consultation Draft, April 2008, clause 9.2 (d).

**Table 16: Proposed EDB Performance Indicators**

<b>Key Performance Area</b>	<b>Performance Indicator</b>	<b>Method of Calculating</b>
Innovation and investment	AMP review rating – innovation and Investment	Rating determined by Commission as part of the summary and analysis
	Capital expenditure ratio	$\frac{\text{Capital Expenditure}}{\text{Asset Base}}$
	Renewal ratio	$\frac{\text{Renewal expenditure}}{\text{Depreciation}}$
	Capital expenditure growth ratio	$\frac{\text{Growth expenditure}}{\text{Change in Transformer Capacity}}$
Efficiency	Operational expenditure ratio	$\frac{\text{Operational expenditure}}{\text{Asset base}}$
	Overhead operational expenditure ratio	$\frac{\text{Overhead expenditure}}{\text{Asset base}}$
	Maintenance expenditure ratio	$\frac{\text{Maintenance expenditure}}{\text{Asset base}}$
	Capacity	$\frac{\text{Maximum Demand}}{\text{Transformer Capacity}}$
	Relative Unit Price Index	(1)
Quality	SAIDI and SAIFI	Based on annual values adjusted for extreme events
	AMP review rating - quality	Rating determined by Commission as part of the summary and analysis
	Customer Perception	(2)
Prices and Profits	ROI	$\frac{\text{Regulatory profit}}{\text{Asset base}}$

Key Performance Area	Performance Indicator	Method of Calculating
Energy Efficiency, Demand Side Management and Loss Reductions (s 54Q)	AMP review rating – energy efficiency, demand side management and loss reductions.	Rating determined by Commission as part of the summary and analysis

- (1) *The calculation for the relative unit price index is included in the Electricity Distribution (Information Disclosure) Requirements 2008.*
- (2) *The method for assessing customer perceptions is yet to be determined. The Commission is to consider submissions on this performance indicator prior to publicising its draft determination. The Commission intends publishing its draft determination in the next round of consultation.*

Q.87) Do you agree that the performance indicators outlined in Table 16 are sufficient for the purpose of information disclosure under Part 4 for electricity distribution lines services? If not, please provide detailed examples of what performance indicators would better serve the purpose of information disclosure for electricity distribution lines services.

Q.88) What do you consider to be the appropriate method for calculating the customer perception performance indicator? Please provide the reasons for your view.

### **11.3.2 Network Rebates, Network Holidays, Discounts, Dividends**

- 566 Profit distributions to consumers are discussed at paragraph 558. It is the preliminary view of the Commission that, for the purposes of determining regulatory income, the discretionary rebates, discounts and line holidays should be treated as being equivalent to dividends, as that they are effectively a distribution of profit. This means that the distribution should not affect the disclosed regulatory profit given that the regulatory profit is prior to distributions. On this basis revenues should be disclosed on a gross basis and should not be net of any distributions. Equally distributions should not be disclosed as an operating expense. This would be irrespective of the way these payments are treated for accounting and tax purposes.
- 567 The exception to this is where a discount is included in the ‘posted’ price which is the published price. It is therefore not discretionary, given that it is the published price that the consumer responds to, and should therefore form the basis of performance measures. In this case the revenue which forms part of the regulatory profit should be disclosed net of the posted discount.
- 568 The preliminary view of the Commission is that the disclosed distributions should be the pre-tax amounts. Any tax effects which arise because the Inland Revenue Department (IRD) recognises rebates as a tax deductible expense, will be considered as part of the specification of regulatory tax payable.

Q.89) Do you agree that, for the purposes of determining regulatory income, the discretionary rebates, discounts and line holidays should be treated as being equivalent to dividends? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### ***11.3.3 Disclosures by Non-Contiguous Networks***

- 569 Non-contiguous networks are those networks which are controlled by a single EDB but which are geographically separate. Examples of EDBs that have sufficiently non-contiguous networks (where events occurring in one area have either very little or no impact on the other) are Aurora (Dunedin and Central Otago) and Powerco (East and West). Due to the types and locations of these networks, performance in one is not necessarily equivalent to the other. For example, Aurora's Dunedin urban network is unlikely to have similar performance levels as the predominantly rural Central Otago network. If they were considered as a single area it would mask their respective performance and prevent an accurate assessment of either area.
- 570 It is the Commission's preliminary view that separate disclosure of quality and statistics for each of the non-contiguous networks (that meets the criteria outlined in s 54C) controlled by an EDB should be required. On this basis, small networks that do not meet the criteria would not be required to make separate disclosures. All other disclosures, including financial and performance measures would be provided on the basis of the combined regulated business unit of the EDB.

Q.90) Do you agree that separate disclosure of quality and statistics for each of the non-contiguous networks controlled by an EDB should be required? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### ***11.3.4 Pass-through Revenue***

- 571 Pass-through revenue, as discussed in paragraphs 234 to 236 is intended to net to zero, therefore, any discrepancies should be purely of a timing nature.
- 572 It is the Commission's preliminary view that where an EDB receives transmission revenue from another EDB that this should be disclosed as pass-through revenue.<sup>112</sup>
- 573 It is the Commission's preliminary view that AC Loss Rental rebates received and then passed on should be disclosed separately. This provides transparency around any timing differences that may otherwise lead to short term distortion of Regulatory Profit which would impact on performance indicators.

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<sup>112</sup> Transmission revenue can be received from another EDB when electricity is provided to that EDB rather than that EDB receiving the electricity directly from the transmission network. It is not a common occurrence for EDBs to receive transmission revenue from another EDB.

Q.91) Do you agree that transmission revenue received from another EDB and AC Loss Rental rebates received and passed on should be separately disclosed? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### ***11.3.5 Operational Expenditure Categories***

- 574 The preliminary view of the Commission is that Operating expenditure for EDBs should be broken down into the following seven categories :
- General management administration and overheads;
  - System management and operations;
  - Routine and preventive maintenance;
  - Refurbishment and renewal maintenance;
  - Fault and emergency maintenance;
  - Pass-through costs; and
  - Other.
- 575 The category for General Management, Administration and Overheads would be for disclosure of “corporate” expenditure, which is not directly related to the management and operations of the network. This would include expenditure on items such as corporate management and reporting, board expenditure, accounting, non-system information technology, procurement, property, legal, regulatory, health and safety, insurance and statutory expenses.
- 576 System Management and Operations would cover all expenditure associated with the management and operation of the network, but which is not directly incurred in maintaining the network. This would include the operation of system control centres as well as asset management in its widest sense, involving planning studies, design, record-keeping, contract management, and maintenance of various operational and maintenance-related standards and procedures.
- 577 There are three proposed asset management-related expenditure categories, covering Routine and Preventative, Refurbishment and Renewal, and Fault and Emergency maintenance, respectively. This disaggregation distinguishes proactive from responsive maintenance and, under the “Refurbishment and Renewal” category, distinguishes the more significant project-based work which in many cases is designed to extend asset lives.
- 578 Transmission charges payable to Transpower are separately disclosed to enable assessment of movements on the corresponding recovered revenue. Although the transmission charges are passed through and form part of the line charge revenue, the recovered revenue is not necessarily transparent where it is incorporated into the pricing for lines charges.



- 579 The Commission's preliminary view is that avoided transmission charges, being payments to parties other than Transpower, which substitute for the use of the transmission system, should be disclosed separately as a transmission cost.
- 580 Levies imposed by regulatory bodies, such as the Electricity Commission and the MED should be disclosed as pass-through costs.
- 581 A category for other expenses is also proposed to ensure that expenditure that cannot be readily categorised elsewhere is disclosed, rather than effectively requiring such expenditure to be allocated arbitrarily to a specific category.
- 582 In all cases, the expenditure to be disclosed should be that which relates to electricity lines business activity. Where required, common costs will be allocated (between the line business activity and any other businesses or other activities) according to the cost allocation methodology which will be prescribed through the input methodologies, and any associated cost allocation handbook.
- 583 Where an EDB manages multiple networks for which separate disclosures are required, an allocation of network management and operational expenses will also be required.
- 584 The Commission considers that the management and administration overheads should be disclosed separately, rather than being allocated across business unit activities. The Commission considers that this approach is transparent and aids comparability between distribution businesses given the possible variations in allocating costs. This tends to mask genuine resource differences and therefore reduces the usefulness of the disclosed information.
- 585 The Commission intends to provide further guidance where necessary to assist with consistent expenditure classification across EDBs. This is because the Commission recognises that in practice, judgements are often involved in deciding the appropriate classification of expenses.

Q.92) Are there any additional operating expenditure categories that would assist in meeting the purpose of information disclosure for electricity distribution lines services? If so, please provide details of how the proposed operating expenditure categories would assist the purpose of information disclosure.

### ***11.3.6 Capital Expenditure Categories***

- 586 It is the preliminary view of the Commission that capital expenditure on EDB system fixed assets be disclosed in six categories, consistent with the current disclosure requirements, which are as follows:
- Customer connection;
  - System growth;
  - Reliability;
  - Safety and environment;
  - Asset replacement and renewal; and

- Asset relocations.
- 587 The proposed categories are based on the drivers for such expenditure. Capital expenditure on customer connections is directly driven by growth in customer numbers, while system growth-related capital expenditure is a function of the combination of growth in customer numbers and growth in the intensity of use. Growth-related capital expenditure may also result from localised growth in peak demand, which may result from factors such as increased use of irrigation or air conditioning in particular regions within a distribution network. This category includes expenditure required to maintain the security of supply, since in system planning terms this is intertwined with capacity and demand.
- 588 Expenditure that is driven by reliability, safety and environmental requirements is essentially independent of growth. This expenditure may be to bring parts of the network up to required standards, and may be to meet more onerous standards than existed when that part of the network was first constructed.
- 589 Asset Replacement and Renewal expenditure is expenditure that is primarily driven by the need for the replacement or renewal of assets which are at the end of their economic or functional lives.
- 590 Asset Relocation expenditure is capital expenditure primarily driven by the need to move assets. This normally results from local authority or Transit road-widening projects. Accordingly this category of expenditure is to be used where the cost of moving assets is other than for reasons of routine maintenance, refurbishment and renewal maintenance or fault and emergency maintenance.

Q.93) Are there any additional capital expenditure categories that would assist in meeting the purpose of information disclosure for electricity distribution lines services? If so, please provide details of how the proposed capital expenditure categories would assist the purpose of information disclosure.

### ***11.3.7 Asset Categorisation and Asset Lives***

- 591 The Commission's preliminary view is that asset categories for EDBs for system fixed assets should remain the same as existing disclosures in report AV2- 'Regulatory Valuation Disclosure by Asset Class'. It is considered that the current disclosures provide sufficient information for interested persons to understand what investment has occurred. The existing categories of assets are as follows:
- Subtransmission;
  - Zone substations;
  - Distribution and LV Lines;
  - Distribution and LV Cables;
  - Distribution substations and transformers;

- Distribution switchgear; and
- Other system fixed assets.<sup>113</sup>

592 As outlined in the Input Methodologies Discussion Paper, in the first instance the standard asset lives set out in the Commission's 2004 ODV Handbook may be appropriate for inclusion in a Historic Cost Handbook for EDBs.<sup>114</sup>

Q.94) Are there any additional asset categories that would assist in meeting the purpose of information disclosure for electricity distribution lines businesses? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.

### ***11.3.8 Statistics and Capacity Utilisation***

593 A purpose of disclosing statistics is to enable meaningful assessment of performance indicators and provide a basis for comparisons between EDBs. The Commission's preliminary view is that information disclosure of relevant statistical information for EDBs should include: assets; demand; capacity; and pricing statistics. Where it is considered that existing disclosures continue to meet or assist with meeting the purposes of regulation, then it is the Commission's preliminary view that the disclosures should remain unchanged.

#### *Assets*

594 The existing disclosures include circuit length by voltage with separate disclosure of overhead and underground; circuit length by terrain allocated into urban, rural, remote and rugged; transformer capacity (discussed further in paragraphs 598 to 600), average age and expected life of system fixed assets. The Commission's preliminary view is that these disclosures should remain unchanged.

#### *Demand*

595 Given that demand for energy fluctuates significantly throughout the day, and throughout the year, it is the Commission's preliminary view that demand should be measured at several levels.

596 The maximum coincident demand reflects the fact that the peak demand for different groups of consumers can occur at different times of the day. It is determined by measuring the actual demand at different times, and represents the maximum peak demand. The maximum non-coincident demand reflects the total demand if all consumers simultaneously demanded their peak requirement.

597 Subsets of demand data are captured at the maximum coincident demand point given that this reflects the realistic situation where different customer groups have their maximum demand at different times of the day. This is consistent with the

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<sup>113</sup> Commerce Commission, *Electricity Distribution (Information Disclosure) Requirements 2008*, Appendix A, Report AV2.

<sup>114</sup> *Supra* n 2, paragraph 11.94.

current EDB disclosure requirements. It is the Commission's preliminary view that the information disclosure should remain the same as the existing requirements.

### *Capacity*

- 598 Distribution transformer capacity gives a measure of the maximum capacity of the system which can then be compared to the maximum demand on the network. The Commission appreciates that capacity requirements are location specific, but it is the Commission's preliminary view that it is valid to measure and track capacity at the network level. Total capacity in the network should also require an estimate of the capacity of non-EDB owned transformers.
- 599 Separate disclosure of zone substation transformer capacity provides greater understanding of the levels of transformation in each network.
- 600 It is the Commission's preliminary view that existing capacity disclosures should remain unchanged.

### *Pricing Statistics*

- 601 The preliminary view of the Commission is that pricing statistics should continue to be reported for EDBs who charge on an installation control point (ICP) basis, in four categories, being small connections (up to 25kVA), medium connections (25 – 69 kVA), large connections (greater than 69 kVA), and the largest 5 connections.
- 602 The Electricity Commission is currently working on developing appropriate categories for the model pricing methodology work. It is the Commission's intention to align pricing statistics disclosure with these categories.
- 603 For each category, the unit price, being cents per kWh, can be calculated by dividing the gross line charge income for the category by the energy supplied to that category.
- 604 For EDBs that charge on a GXP basis, as opposed to an ICP basis, the categories have been tailored to their specific situations or alternative disclosure arrangements have been made. The Commission intends reviewing the disclosure of pricing statistics for EDBs once the Electricity Commission has completed its work on the model pricing methodology.

Q.95) Do you agree that relevant statistical information for electricity distribution lines services should include asset information, demand, and pricing statistics? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.96) Do you agree that pricing statistics, as currently required, should continue to be disclosed? If not please provide the reasons for your view, an alternative means for making comparisons between regulated suppliers on price and why you consider this to be preferable.

### 11.3.9 Quality

605 As discussed in paragraph 385, the Commission's preliminary view is that there are four aspects of quality that could be measured, being:

- reliability of service;
- supply quality;
- customer service; and
- safety.

This section discusses the four aspects of quality and the Commission's preliminary views on their applicability for EDBs. The Commission's preliminary views on the disclosure of quality in the AMPs are outlined in paragraphs 373-379, while the disclosure of actual and target quality is discussed in paragraphs 365-367.

606 It is considered that safety is an essential component of quality, however as outlined in paragraphs 389 to 390, it is the Commission's preliminary view that disclosure of safety measures is not required.

607 In order to measure quality, there is a requirement to establish the consumer's expectations of quality in terms of the nature and level of customer service. Given the diverse range of EDB consumers, from individual households through to large corporates, it is likely that different service quality levels will be demanded by different consumer groups.

608 Disclosure of reliability of supply for EDBs refers to the ability of a power system to provide a secure supply of electrical energy at any point in time. Implicit to this is the continuity of supply, as characterised by the number and duration of supply interruptions. The measures currently disclosed comprise interruption statistics including industry measures of outage duration (SAIDI), outage frequency (SAIFI) and average interruption duration (CAIDI). The Commission's preliminary view is that these disclosures need to be reviewed in order to provide more meaningful information for interested persons. Current information is limited in its usefulness because it is based on annual averages and includes extreme events which distort normal reliability performance. It is considered that the information would be more meaningful if it was based on normalised daily data, which would require an adjustment for extreme events. To the extent daily data is used to remove extreme events from the data of non-exempt EDBs under the Default Price Path regulation, exempt EDBs might be disadvantaged if they did not disclose such information.

609 Supply quality – other is referred to as technical quality for electricity distribution lines services and generally relates to the technical characteristics of supply voltage, concerning magnitude, frequency, waveform and symmetry of the phases. Technical quality is largely out of direct EDB control, and is not currently disclosed. It is the Commission's preliminary view that monitoring may be considered in the future.

610 Customer service quality is directly associated with the transactions between utilities and customers. There are varying service responsibilities between retailers and EDBs. The Commission seeks the views of interested parties on this dimension of service quality.

Q.97) Do you agree that the key aspects of service quality for electricity distribution lines services should include reliability, supply quality and customer service? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.98) Do you agree that reliability for electricity distribution lines services should include the disclosure of planned and unplanned interruptions, the causes of interruptions and SAIDI, SAIFI and CAIDI measures? If not, please provide the reasons for your view, alternatives and why you consider these to be better aligned to the purpose of information disclosure.

Q.99) In your view, what measures of supply quality – other (technical quality), if any, should be measured for electricity distribution lines businesses? Please provide the reasons for your view and why you consider these to be important.

Q.100) In your view how should customer service quality be measured for electricity distribution lines services? Please provide the reasons for your view.

### ***11.3.10 Energy Efficiency, Demand Side Management and Loss Reductions***

611 As discussed in paragraph 122, the specification in s 54Q on energy efficiency, demand side management and loss reduction is applicable to EDBs. The Commission's preliminary view is that each supplier should disclose in their AMPs information on the initiatives it is taking regarding energy efficiency, demand side management and loss reduction in the supply and demand of regulated services (refer paragraphs 438 and 439).

612 It is the Commission's preliminary view that the Commission's AMP review should include a review of the initiatives for energy efficiency, demand-side management and loss reduction that the supplier has included in their disclosed AMP. Any results from such a review could be included in the Commission's summary and analysis as part of the key performance indicators.

Q.101) Do you agree that the Commission's AMP review should include a review of the initiatives for energy efficiency, demand-side management and loss reduction that the supplier has included in their disclosed AMP? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### ***11.3.11 Consumer Owned Statutory Declaration***

613 As mentioned in paragraph 543, it is the Commission's preliminary view that EDBs exempt from default/customised price-quality regulation should provide to the Commission on an annual basis a statutory declaration demonstrating that the consumer-owned criteria in section 54D of the Act have been met. This information would be sought under section 53C(2).

614 This information proposed is to ensure that each EDB is subject to the appropriate regulatory instrument(s). It is proposed that statutory declarations, and any supporting information, be disclosed at the same time as price-quality path compliance information. The Commission has proposed that annual price-quality path compliance information be disclosed within 35 working days of 31 March each year.

Q.102) Do you agree that EDBs exempt from default/customised price-quality regulation provide to the Commission on an annual basis a statutory declaration demonstrating that the consumer-owned criteria in section 54D of the Act has been met? If not, please provide details of how exempt EDBs should prove to the Commission that they are exempt and therefore not subject to default/customised price-quality regulation.

#### 11.4 SCOPE OF DISCLOSURES SUMMARY

615 The following table summarises the Commission's preliminary views on the scope of the EDB disclosures and compares this to the current disclosure requirements. The table identifies where the scope of disclosure of information is similar to the current disclosure requirements. Actual content may, however, differ from those current disclosure requirements identified. The requirements will need to be consistent with the relevant Input Methodologies and any new or revised handbooks.

**Table 17: Scope of Proposed Disclosures Summary**

Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>115</sup>
Performance Indicators	As outlined in Table 16.	Proposed disclosures are generally consistent with current disclosures. The key exception is the inclusion of the AMP review ratings.

<sup>115</sup> Commerce Commission, *Electricity Distribution (Information Disclosure) Requirements 2008* and *Electricity Information Disclosure Requirements issued 31 March 2004* (where relevant).

Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>115</sup>
Financial Information	<p>The proposed financial disclosures are consistent with GAAP, where appropriate. For regulatory reporting purposes, however, there are instances where either more, or less, prescriptive information than GAAP is required.</p> <p>The proposed disclosures include:</p> <p>Regulatory Profit Statement &amp; Notes;</p> <ul style="list-style-type: none"> <li>▪ Regulatory Asset Statement;</li> <li>▪ Regulatory Tax Calculation;</li> <li>▪ Forecast Statement; and</li> <li>▪ Consolidation Statement.</li> </ul> <p>Key areas where more prescriptive information is required include:</p> <ul style="list-style-type: none"> <li>▪ Treatment of revaluations, vested assets and capital contributions; and</li> <li>▪ Disclosure of operational and capital expenditure categories.</li> </ul>	<p>Proposed disclosures are consistent with current disclosures, except for the consolidation statement which is a new disclosure. The relevant current financial disclosures include Requirements 3 and 7(5), and Schedules 2-4 and 12.</p>
Regulatory Asset Base	<p>The proposed disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Regulatory Valuation Roll-Forward Report;</li> <li>▪ Annual Valuation Roll-Forward by Asset Class Report;</li> <li>▪ Asset Transactions with Other Regulated Suppliers Report; and</li> <li>▪ Initial RAB Report (one-off report).</li> </ul>	<p>Proposed disclosures are consistent with current disclosures, except the initial RAB Report which is a new disclosure. The relevant current RAB disclosures include Requirement 4 and Schedules 5-8.</p>



Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>115</sup>
Statistics	<p>The proposed statistics information includes:</p> <ul style="list-style-type: none"> <li>▪ Asset Statistics;</li> <li>▪ Demand Statistics;</li> <li>▪ Capacity Statistics; and</li> <li>▪ Pricing Statistics.</li> </ul>	<p>Proposed disclosures are consistent with current disclosures. The relevant current disclosures include Requirement 6 and Schedule 9.</p>
Quality	<p>The proposed actual quality disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Interruptions;</li> <li>▪ Faults;</li> <li>▪ Reliability; and</li> <li>▪ Customer service.</li> </ul> <p>The disclosure of target and requisite quality are outlined in the AMP section.</p>	<p>Proposed disclosures are consistent with current disclosures, except where the Commission has proposed additional disclosures for reliability and customer service. The relevant current disclosures include Requirement 6 and Schedule 9.</p>
Asset Management Plans	<p>The proposed AMP disclosure includes:</p> <ul style="list-style-type: none"> <li>▪ Assets covered;</li> <li>▪ Service levels;</li> <li>▪ Development planning;</li> <li>▪ Lifecycle asset management planning;</li> <li>▪ Risk management; and</li> <li>▪ Evaluation of performance.</li> </ul> <p>It is proposed the AMP disclosures cover a period of no less than 10 years.</p>	<p>Proposed disclosures are consistent with current disclosures, except that it is proposed that the Directors certify that the AMP describes actual process and practices implemented.</p>

Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>115</sup>
Pricing	<p>The proposed pricing disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Pricing Methodology;</li> <li>▪ Prices;</li> <li>▪ Pricing Statistics; and</li> <li>▪ Contracts.</li> </ul>	Proposed disclosures are generally consistent with current disclosures.
Segmentation of Business Activity	Proposed requirement to disclose separate quality and statistics information for non-contiguous networks and where an EDB is controlled by consumers of one part of a network.	Proposed disclosures are consistent with current disclosures. The relevant current disclosures are in Requirement 6(1).
Other	<p>The proposed other disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Assumptions;</li> <li>▪ Methodologies; and</li> <li>▪ Policies.</li> </ul>	Proposed assumptions and methodologies disclosures are consistent with current disclosures. Some new policies disclosures are proposed.
Publication, Retention, Certification	<p>Director certification and audit requirements for Annual Disclosures.</p> <p>Director certification requirements for AMPs.</p> <p>Statutory declaration requirements for all disclosures.</p>	Similar to current requirements. The relevant requirements include Requirements 10, 11 and 13.

616 The Commission has reviewed the disclosures under the current information disclosure requirements for EDBs in light of the new purpose statements and considers that all the current types of disclosures will continue to be applicable, albeit possibly in a new form or established on different basis. The current EDB information disclosure requirements were revised recently in line with the purpose of Part 4A.

Q.103) In your view, are there any current information disclosure requirements that should not be carried forward? If so, please provide the reasons for your view.

## CHAPTER 12: TRANSPOWER

### 12.1 INTRODUCTION

617 This chapter provides an overview of the information disclosure matters unique to Transpower. The first section provides an overview of the key characteristics of Transpower that are both unique to Transpower and relevant to the information disclosure regime. The second section of this chapter outlines the Commission's preliminary views on how components of the information disclosure regime should be customised to Transpower.

### 12.2 UNIQUE CHARACTERISTICS OF TRANSPOWER SERVICES

#### 12.2.1 *Transpower's Scope of Services for Information Disclosure Purposes*

618 Transpower is the sole owner and operator of the New Zealand national electricity transmission grid. As owner and operator of the national electricity grid, the main activities undertaken by Transpower are as follows :

- transmission services, being the transmission of electricity from generators to substations where it is supplied to local EDBs or large industrial consumers;
- system operator services, being operation of the national grid to ensure electricity is delivered at the required quality standards and meets electricity demand; and
- new connection contracts for the provision of grid connection assets.

619 The Commission considers that activities which relate to quality and reliability of electricity transmission are integral to the conveyance of electricity by line.<sup>116</sup> The Commission's preliminary view is that the system operator activities provided by Transpower form part of the conveyance of electricity by line and would therefore be subject to regulation, including information disclosure, under Part 4 of the Act.

620 Transpower also provides grid connection assets required by individual customers. These services are termed 'new investment contracts' and are between the individual customers and Transpower. The Commission's preliminary view is that the services provided by new investment contracts fall under the Part 4 definition of electricity lines services because they involve the conveyance of electricity by line. They would therefore be subject to regulation, including information disclosure, under Part 4 of the Act.

621 Transpower has a number of subsidiaries including :

- Energy Market Services Limited, which provides data management, reconciliation and metering services for clients in New Zealand and Australia;

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<sup>116</sup> Supra n 2, paragraph 3.79.

- d-cyphaTrade, which operates in Australia and provides services to the electricity derivatives market; and
  - Risk Reinsurance Limited, which provides insurance services to the Transpower group of companies.
- 622 The Commission's preliminary view is that these services do not involve the conveyance of electricity and would therefore not be regulated services under Part 4 of the Act.

### ***12.2.2 Applicable Regulatory Instruments***

- 623 As a supplier of electricity lines services, Transpower is subject to information disclosure regulation under Part 4 of the Act. The Act requires that a s 52P determination, specifying how the new information disclosure regulation applies to Transpower, must be made as soon as practicable after 1 April 2009. The Commission intends to set new information disclosure requirements after the applicable input methodologies have been determined.
- 624 The information disclosure requirements that were published by the Commission under Part 4A before 1 April 2009 will continue to apply until such time as the Commission sets new information disclosure requirements under Part 4 of the Act.
- 625 Also, under subpart 9 of Part 4 of the Act, Transpower continues to be subject to the administrative settlement until it expires on 30 June 2011.<sup>117</sup>
- 626 Before Transpower's administrative settlement expires, the Commission must recommend to the Minister of Commerce that Transpower be subject to either default/customised or individual price-quality regulation.<sup>118</sup> Transpower will be subject to price-quality regulation once the Governor-General makes an Order in Council declaring which type of price-quality regulation applies to Transpower, and the Commission makes a s 52P determination applying the regulation to Transpower.
- 627 Transpower, in its submission on the Provisions Paper, questioned the value of the information provided under the 2004 Electricity Information Disclosure regulation given the substantial compliance costs associated with producing it and the difficulties associated with using the information.<sup>119</sup> Transpower suggested instead that the information provided in its annual threshold compliance report under the terms of its administrative settlement should be sufficient for the purpose of the information disclosure regime.

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<sup>117</sup> Commerce Commission, *Decision and Reasons for Not Declaring Control of Transpower New Zealand Limited & Decision to reset Transpower's Thresholds*, 13 May 2008.

<sup>118</sup> Section 54M(3) of the Act.

<sup>119</sup> Transpower New Zealand Ltd, *Submission to the Commerce Commission on Regulatory Provisions of the Commerce Act 1986: Discussion Paper*, February 2009, pages 4-5.

- 628 Irrespective of whether other regulatory instruments apply to a supplier in addition to information disclosure regulation, the Commission's preliminary view is that a similar scope, detail, prescription and consistency of disclosed information would need to apply to Transpower to that applied to other regulated services. This approach is considered appropriate in order to determine whether the Part 4 purpose is being met, and in order for the Commission to promote a greater understanding of the performance of all suppliers. Areas of the current disclosures that are not considered necessary for the purpose of information disclosure are discussed in paragraphs 681 and 683.
- 629 In the submissions on the Provisions Paper, MEUG suggested that the information disclosure requirement for transmission services should use a measure of economic profit that is based on the latest assessment of WACC rather than the assessment that was made when the settlement was agreed.<sup>120</sup> The Commission's proposed approach to measuring economic profit is outlined in paragraphs 181 to 187.

### ***12.2.3 Economic Value Account***

- 630 Transpower currently has a mechanism called the economic value (EV) account that records any over or under recovery by Transpower during a financial year. The balance of the EV account is used in the calculation of the following year's revenue requirement.
- 631 The economic gains and losses attributed to customers of the high voltage alternating current (HVAC) network and high voltage direct current (HVDC) customers are recorded in separate customer EV accounts.
- 632 It is the Commission's preliminary view that transfers from the EV account during a year should be separately disclosed in the revenue section of regulatory profit so as to allow an assessment of Transpower's net economic returns in the assessment of regulatory profits.

### ***12.2.4 HVDC and HVAC Services and Customers***

- 633 Transpower's transmission services include:
- transmission of HVAC in the North and South Islands; and
  - transmission of HVDC mostly between the South Island and North Island.
- 634 Transmission customers of HVAC and HVDC services have different service requirements. The Commission's preliminary view is that Transpower should provide separate disclosure of information regarding quality and statistics for HVAC and HVDC services.

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<sup>120</sup> Major Electricity Users Group, *Submission on Regulatory Provisions of the Commerce Act 1986 Discussion Paper*, 16 February 2009, Appendix, page 3.

### 12.2.5 Role of Electricity Commission

- 635 Transpower is subject to oversight from the Electricity Commission under the provisions of the Electricity Act 1992. Section 172O of the Electricity Act provides that the Electricity Commission is empowered to make recommendations to the Minister of Energy on regulations and rules including, but not limited to:
- investments made by Transpower in upgrading and expanding transmission grid assets (Part F Capital Expenditure);
  - quality standards for the national grid;
  - transmission agreements containing the terms and conditions for connection to the grid; and
  - the pricing methodology for recovering Transpower's overall revenue requirements.<sup>121</sup>

#### *Part F Capital Expenditure*

- 636 Under the settlement agreement, capital expenditure has been categorised as either Part F or Non-Part F. Non-Part F investments are discussed below at paragraph 647 to 649.
- 637 The Electricity Commission is responsible under Part F of the Electricity Governance Rules 2003 (EGRs) for approving or declining reliability investments and economic investments contained in grid upgrade plans if submitted by Transpower for approval. Among other things, the purpose of the grid upgrade and investment rules under Part F Section III of the EGRs are to:
- facilitate Transpower's ability to develop and implement long term plans (including timely securing of land access and resource consents) for investment in the grid;
  - assist participants to identify and evaluate investments in transmission alternatives;
  - facilitate efficient investment in generation; and
  - enable the cost of approved investments to be recovered through the transmission pricing methodology applied in transmission agreements.
- 638 Reliability investments are defined as investments by Transpower in the grid, or alternative arrangements by Transpower, the primary effect of which is, or would be, to reduce expected unserved energy.<sup>122</sup>
- 639 Economic investments are defined as investments in the grid that can be justified on the basis of a cost-benefit test. The cost-benefit test employed by the Electricity Commission is the grid investment test.<sup>123</sup>

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<sup>121</sup> Electricity Commission, *Electricity Governance Rules*, 1 April 2008, Part F, Section IV

<sup>122</sup> *Supra* n 2, paragraph 12.73.

*Quality Standards*

640 Transmission and system operator's service levels are set out in Part C of the EGRs. Transpower provides a number of performance reports to the Electricity Commission. It is the Commission's preliminary view that where appropriate, information already provided to the Electricity Commission should be used for the purpose of information disclosure.

*Transmission Agreements*

641 Part F of the EGRs requires the Electricity Commission to develop benchmark agreements for connection to the grid and for the use of the grid. Benchmark agreements apply to connection asset and information services, and interconnection information services. Benchmark agreements are set out as:

- the foundation for Transpower and its customers to negotiate transmission agreements; and
- default transmission agreements if Transpower and its customers are unable to agree on transmission agreements before a date specified by the Electricity Commission.<sup>124</sup>

642 The Electricity Commission determines the contents of the benchmark agreements, which include but are not limited to, service definitions, service levels, and service measures.

643 The Commission's preliminary view is that reporting of quality measures for Transmission agreements should, wherever possible, be consistent with the service levels and measures defined in those agreements.

*Pricing Methodology*

644 Part F of the EGRs sets out a process whereby the Electricity Commission recommends to the Minister of Energy a 'transmission pricing methodology' (TPM) proposed by Transpower.<sup>125</sup> The purpose of the TPM is to ensure that the full economic costs of Transpower's services are allocated in accordance with the principles set out in rule 2 of section IV of part F. The charges calculated in accordance with the approved pricing methodology are enforceable against designated transmission customers.

645 The Electricity Commission is currently undertaking a full review of the current TPM. A final 'issues paper' and evaluation of a preferred option for transmission pricing is planned for the end of 2010.

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<sup>123</sup> Ibid., paragraph 12.73

<sup>124</sup> Supra n 121, Part F, Schedule F2.

<sup>125</sup> Ibid., Part F, Section IV.

646 It is the Commerce Commission's preliminary view that the TPM administered by the Electricity Commission should be disclosed in the same format for the purposes of information disclosure.

### **12.2.6 Non-Part F Capital Expenditure**

647 Under the administrative settlement agreement with Transpower the Commission is required to set a threshold for non-part F capital expenditure on an annual basis. In setting the annual threshold the Commission does not undertake a full technical review of individual projects. The objective of the review is to approve a reasonable level of capital expenditure through ensuring Transpower selects projects on the basis that they are the least cost option.

648 The non-Part F investments are related to 'specified services' and are of a type in respect of which the Electricity Commission currently has no established process in place for approval under Part F of the EGRs.

649 It is the Commerce Commission's preliminary view that disclosures should distinguish Part F from Non-Part F, as discussed at paragraph 658.

Q.104) Are there any additional characteristics of Transpower that would affect how the information disclosure regime for Transpower should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.

## **12.3 APPLICATION OF INFORMATION DISCLOSURE TO TRANSPOWER**

650 This section outlines the Commission's preliminary views on how components of disclosed information should be customised to Transpower. The Commission's preliminary view is that the components of disclosed information should be as outlined in Chapters 5-10 where no customisation is proposed.

### **12.3.1 Performance Indicators**

651 The table below outlines the Commission's preliminary views on the performance indicators that are relevant to Transpower. Chapter 3 provides further details on the objectives of each of the performance indicators.

**Table 18: Transpower Performance Indicators**

<b>Key Performance Area</b>	<b>Performance Indicator</b>	<b>Method of Calculating</b>
Innovation and investment	Capital expenditure ratio	$\frac{\text{Capital Expenditure}}{\text{Asset Base}}$
	Renewal ratio	$\frac{\text{Renewal expenditure}}{\text{Depreciation}}$
	Capital expenditure growth ratio	$\frac{\text{Growth expenditure}}{\text{Change in Transformer Capacity}}$



Key Performance Area	Performance Indicator	Method of Calculating
Efficiency	Operational expenditure ratio	<u>Operational expenditure</u> Asset base
	Overhead operational expenditure ratio	<u>Overhead expenditure</u> Asset base
	Maintenance expenditure ratio	<u>Maintenance expenditure</u> Asset base
	Capacity	<u>Maximum Demand</u> Transformer Capacity
	Pricing	(1)
Quality	Interruptions	System minutes
Prices and Profits	ROI	<u>Regulatory Profit</u> Asset base

- (1) *The method for calculating a pricing performance indicator is yet to be determined. The Commission is to consider submissions prior to publishing its draft determination. The Commission intends publishing its draft determination in the next round of consultation.*

Q.105) Do you agree that the performance indicators outlined in Table 18 are sufficient for the purpose of information disclosure under Part 4 for Transpower? If not, please provide detailed examples of what performance indicators in your view would better serve the purpose of information disclosure for Transpower.

Q.106) What, if any, do you consider to be the appropriate performance indicator to demonstrate relevant performance efficiencies in supplying HVDC and HVAC, and South Island and North Island customers? Please provide the reasons for your view.

### 12.3.2 Economic Value Accounts

652 The EV accounts, as discussed above in paragraphs 630 to 632, require transparency given that any surplus or shortfall from Transpower's revenue requirement is carried forward through the EV account and factored into the following year's pricing calculation. It is the Commission's preliminary view that, as long as Transpower retains EV accounts, disclosure under the Act should show a reconciliation of the opening and closing balance, clearly showing the balance of any surplus or shortfall. The reconciliation of opening and closing balances of all EV accounts should be disclosed in the Regulatory Asset Statement and the value of any surplus or shortfall in the Regulatory Profit Statement.

Q.107) Do you agree that Transpower should be required to disclose movements in the EV account and that Regulatory Profit should be adjusted for surplus or shortfall transfers from the EV account? If not, please provide reasons for your view, an alternative and why you consider this to be preferable.

### ***12.3.3 Operational Expenditure Categories***

- 653 The Commission's preliminary view is that operating expenditure for transmission should be broken down into similar categories to those contained in the administrative settlement.
- 654 In order to calculate the performance indicators to measure efficiency, it will be necessary to have separate disclosure of overhead expenditure, maintenance expenditure, and other expenditure.
- 655 It is also considered there should be separate disclosure of expenses associated with each of the three main business activities, being transmission services, system operator services, and new investment contracts.
- 656 The Commerce Commission intends working with Transpower and the Electricity Commission to develop appropriate operating expenditure categories prior to the next round of consultation on information disclosure requirements for Transpower.

Q.108) In your view, what operating expenditure categories should be disclosed by Transpower? Please provide the reasons for your view in light of the operational expenditure ratios identified above.

### ***12.3.4 Capital Expenditure Categories***

- 657 The Commission's preliminary view is that like operational expenditure categories, the appropriate categories of capital expenditure will also be established in consultation with Transpower and the Electricity Commission. Where possible, this is to achieve consistency with existing information, but also to ensure that there is sufficient information to support the capital expenditure ratios.
- 658 It is the Commission's preliminary view that disclosure of capital expenditure should also include whether it was approved by the Electricity Commission (Part F), the Commerce Commission (Non-Part F), or internally approved by Transpower. It is considered that this information will provide a level of transparency for interested persons.
- 659 It is the Commission's preliminary view that approved capital expenditure over the regulatory period should be tracked on a rolling basis with a comparison of both actual and forecast capital expenditure against approved capital expenditure. This information is readily available and should therefore be cost-effective to disclose.

Q.109) In your view, what capital expenditure categories should be disclosed for Transpower? Please provide the reasons for your view in light of the capital expenditure ratios identified above.

Q.110) Do you agree that disclosure of capital expenditure for Transpower should specify which regulatory body, if any, provided approval? If not, please provide the reasons for your view.

### ***12.3.5 Asset Categorisation and Asset Lives***

660 The Commission's preliminary view is that asset categories for Transpower should remain the same as existing disclosures. The existing categories of assets are as follows:

- HVAC transmission lines;
- HVDC transmission lines;
- HVAC substations;
- HVDC substations and submarine cables;
- communications; and
- administration assets.

661 It is the preliminary view of the Commission that system operator assets and new investment contract assets do not require separate disclosure, and can be included in the existing categories.

662 It is also the preliminary view of the Commission that existing asset lives continue to be applied to Transpower's assets.

Q.111) Are there any additional asset categories that would assist in meeting the purpose of information disclosure for Transpower? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.

### ***12.3.6 Statistics and Capacity Utilisation***

663 As discussed in paragraph 402, one of the purposes of disclosing statistics is to support and inform the analysis of other performance indicators. Statistics should also provide a basis for assessing trends over time.

664 It is the Commission's preliminary view that the existing categories of statistical disclosures for Transpower would meet the purposes of the Act. The detail of the disclosures, however, may require additional consideration. The existing categories include performance measures and statistics relating to the following:

- Load factor;
- Loss ratio;
- Capacity utilisation;
- System length, by voltage;
- Circuit length of overhead lines, by voltage;
- Circuit length of underground electric lines;
- Transformer capacity;

- Maximum demand;
- Total electricity entering the system;
- Total electricity supplied from the system on behalf of generators and retailers; and
- Total connected customers.

665 It is the Commission's preliminary view that capacity utilisation for Transpower should be measured on the basis of the non-coincident peak demand at both the grid injection point and the grid exit point. It should also include separate disclosures for the South Island, North Island and the HVDC link. This information enables an assessment of the trend of capacity improvement over time.

Q.112) In your view, what statistical information should be disclosed for Transpower? Please provide the reasons for your view.

Q.113) Do you agree that capacity utilisation for Transpower should be measured on the basis of the non-coincident peak demand at both the grid injection point and the grid exit point for the South Island, North Island and the HVDC link? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

### 12.3.7 *Quality*

666 As discussed in paragraph 385, the Commission's preliminary view is that there are four aspects of quality that could be measured, being :

- reliability of service;
- supply quality;
- customer service; and
- safety.

This section discusses these aspects of quality and the Commission's preliminary views on their applicability for Transpower. The Commission's preliminary views on the disclosure of quality in the AMPs is outlined in paragraphs 373-379, while the disclosure of actual and target quality is discussed in paragraphs 365-367.

667 It is considered that safety is an essential component of quality, however as outlined in paragraphs 389 to 390, it is the preliminary view of the Commission that disclosure of safety measures is not required.

668 Under s 54M(6) it is stated that the only requirements that may be included in a section 52P determination in respect of the quality standards of Transpower are requirements that give effect to quality standards set by the Electricity Commission.

669 Reliability performance measures for the transmission grid are currently subject to reporting under the EGRs, as outlined at Part F, Section III, Rule 12A. This report is required to be published within six months of the date of publication of the

Statement of Opportunities, or a date agreed in consultation between the Electricity Commission and Transpower.

- 670 As such, the Commission preliminary view is that quality disclosures for information disclosure purposes should be aligned to the Electricity Commission required disclosures. It is the preliminary view of the Commerce Commission that at a minimum disclosures should include:
- Total number of unplanned interruptions;
  - Electricity customer interruptions in system minutes – planned, and unplanned;
  - Underlying electricity customer interruptions in system minutes – planned and unplanned;
  - Average supply reliability;
  - Planned interruption restoration performance; and
  - Unplanned interruption response.
- 671 The System Operator is also required to submit an annual performance review to the Electricity Commission as outlined in Part C, Section II, Rule 14. This is to be submitted by the 30 September each year, for the preceding year ended 31 August.
- 672 Transpower, under the administrative settlement, is currently subject to a quality threshold that tests three components, being number of unplanned interruptions, total interruptions and customer communication. The number of interruptions is not to exceed a five year average. Regarding customer service, Transpower is required to undertake customer communication regarding quality. This includes consulting with customers about the requisite quality of goods and services, and then adequately considering these views when making asset management decisions.
- 673 It is important for Transpower to disclose its process for consumer engagement, however if provisions are already in place for Transpower to disclose this to the Electricity Commission, then no additional requirements are likely to be necessary.
- 674 It is the preliminary view of the Commission that summarised information of existing performance measures, as specified by the Electricity Commission, be provided, and aligned with the reporting period of other information disclosures under Part 4.
- 675 It is proposed that a workshop be held with interested parties to determine the content and format of quality and statistical disclosures which will meet the purpose of information disclosure.

Q.114) In your view, are there other Transpower specific quality performance indicators that should be considered? If so, please provide the reasons for your view.

Q.115) In your view, what should the summarised performance indicators of quality for Transpower be? Please provide details of your view, including how they are aligned to the purpose of information disclosure and how they will be calculated.

### ***12.3.8 Segmentation of Regulated Business Activities***

676 As outlined in paragraph 618, Transpower undertakes three regulated business activities, including:

- Electricity Transmission;
- System Operator Services; and
- New Investment Contracts.

677 To allow the appropriate assessment of Transpower's performance, it is the preliminary view of the Commission that disclosure of information for each main business activity should include: revenue; operating expenditure; taxation; and RAB information, including depreciation and revaluation.

678 As outlined in paragraphs 633 to 634, the Commission's preliminary view is that there should also be separate disclosure of the HVDC and HVAC quality and statistics information.

Q.116) Do you agree that there should be separate disclosure of transmission services, system operator services and new investment contracts financial information? If not, please provide reasons for your view, an alternative and why you consider this to be preferable.

Q.117) Do you agree that there should be separate disclosure of the HVDC and HVAC quality and statistics information? If not, please provide reasons for your view.

### ***12.3.9 Other Disclosures by Transpower to the Electricity Commission***

679 Pricing Methodologies and disclosure of Transpower's prices is excluded from discussion on the basis that this is regulated and disclosed to the Electricity Commission. For completeness, the Commerce Commission would require a copy of the disclosures made to the Electricity Commission.

680 As discussed in paragraph 423 it is the Commission's preliminary view that Transpower should not be required to disclose AMP information which extends beyond the major asset expenditure which is subject to regulatory oversight by the Electricity Commission. For completeness, the Commerce Commission would require a copy of the disclosures made to the Electricity Commission.

Q.118) Do you agree that Transpower should be excluded from specific pricing methodology and AMP disclosure requirements under the Part 4 other than to disclose that which is already disclosed to the Electricity Commission? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

## **12.4 SCOPE OF DISCLOSURES SUMMARY**

681 The following table summarises the Commission's preliminary views on the scope of Transpower disclosures and compares this to the current disclosure requirements. The table identifies where the disclosure of information is similar to the current disclosure requirements. Actual content may, however, differ from those current

disclosure requirements identified. The requirements will need to be consistent with the relevant Input Methodologies and any new or revised handbooks.

**Table 19: Scope of Proposed Disclosures Summary**

<b>Proposed Disclosures</b>	<b>Scope of Disclosures</b>	<b>Comparison to Current Disclosure Requirements<sup>126</sup></b>
Performance Indicators	As outlined in Table 18.	Includes a number of new disclosures that are derived from the proposed disclosed information.
Financial Information	<p>The proposed financial disclosures are consistent with GAAP, where appropriate. For regulatory reporting purposes, however, there are instances where either more, or less, prescriptive information than GAAP is required.</p> <p>The proposed disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Regulatory Profit Statement &amp; Notes;</li> <li>▪ Regulatory Asset Statement;</li> <li>▪ Regulatory Tax Calculation;</li> <li>▪ Forecast Statement; and</li> <li>▪ Consolidation Statement.</li> </ul> <p>Key areas where more prescriptive information is required include:</p> <ul style="list-style-type: none"> <li>▪ Treatment of vested assets and capital contributions; and</li> <li>▪ Disclosure of operational and capital expenditure categories.</li> </ul>	Current disclosures are based on GAAP. Some operational expenditure information, however, is required.

<sup>126</sup>

Commerce Commission, *Electricity Information Disclosure Requirements issued 31 March 2004*.

<b>Proposed Disclosures</b>	<b>Scope of Disclosures</b>	<b>Comparison to Current Disclosure Requirements<sup>126</sup></b>
Regulatory Asset Base	<p>The proposed disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Regulatory Valuation Roll-Forward Report;</li> <li>▪ Annual Valuation Roll-Forward by Asset Class Report;</li> <li>▪ Asset Transactions with Other Regulated Suppliers Report; and</li> <li>▪ Initial RAB Report (one-off report).</li> </ul>	Includes disclosures additional to what has previously been required.
Statistics	<p>The proposed statistics information includes:</p> <ul style="list-style-type: none"> <li>▪ Asset Statistics;</li> <li>▪ Demand Statistics;</li> <li>▪ Capacity Statistics; and</li> <li>▪ Pricing Statistics.</li> </ul>	The proposed pricing statistics are new. Other proposed statistics may be more refined than in the current disclosures.
Quality	<p>The proposed actual quality disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Interruptions;</li> <li>▪ Reliability; and</li> <li>▪ Customer service.</li> </ul> <p>The disclosure of target and requisite quality are outlined in the AMP section.</p>	The proposed disclosures are a refinement of the current disclosure requirements, except that the proposed customer service disclosures are new. Proposed disclosure requirements are more aligned to the information on quality required for the administrative settlement for Transpower.
Asset Management Plans	Asset management information disclosed to the Electricity Commission to be disclosed to the Commerce Commission as part of the AMP disclosure requirements.	AMPs are not required under the current requirements.



Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>126</sup>
Pricing	<p>The proposed pricing disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Pricing Methodology;</li> <li>▪ Prices;</li> <li>▪ Pricing Statistics; and</li> <li>▪ Contracts.</li> </ul>	Proposed disclosures are generally consistent with current disclosures or Electricity Commission disclosure requirements, except new pricing statistics disclosures.
Other	<p>The proposed other disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Assumptions;</li> <li>▪ Methodologies; and</li> <li>▪ Policies.</li> </ul>	<p>Increased disclosure of assumptions and methodologies.</p> <p>Proposed policies disclosures are new.</p>
Segmentation of Business Activity	<p>Proposed requirement to separately disclose information on the:</p> <ul style="list-style-type: none"> <li>▪ HVDC and HVAC business activities;</li> <li>▪ System operator business activities; and</li> <li>▪ New investments business activities.</li> </ul>	HVDC, HVAC and new investment contracts revenue currently disclosed separately. No other segmentation requirements under the current requirements.
Publication, Retention, Certification	<p>Director certification and audit requirements for Annual Disclosures;</p> <p>Director certification requirements for AMPs; and</p> <p>Statutory declaration requirements for all disclosures.</p>	Similar to current regulations. The relevant requirements include Requirements 30, 31 and 36.

682 The remainder of this section outlines the information required for disclosure under the Electricity Information Disclosure Requirements 2004 that in the Commission's preliminary view should not be required under the proposed new disclosure regime for Transpower. The Electricity Information Disclosure Requirements 2004 require Transpower to prepare financial information in compliance with GAAP. As noted in paragraphs 219 and 220, the Commission's preliminary view is that some GAAP disclosure may not be appropriate or necessary for regulatory reporting purposes.

683 Paragraphs 221 to 223 outline the Commission's preliminary views on why financing and financial instruments, cash flow and equity information should not be required for disclosure under Part 4. Derivatives and their fair value adjustments should not be required for the same reasons.

Q.119) Do you agree that the above mentioned disclosures from the Electricity Information Disclosure Requirements 2004 are not required for the purposes of information disclosure for Transpower under Part 4? If not, please explain how they would assist with the purpose of information disclosure.

## CHAPTER 13: GAS PIPELINE SERVICES

### 13.1 INTRODUCTION

684 This chapter provides an overview of the information disclosure matters unique to gas pipeline services. The first section provides an overview of the key characteristics of gas pipeline services that are both particular to gas pipeline services and relevant to the information disclosure regime. The second section of this chapter outlines the Commission's preliminary views on how the information disclosure regime should be customised to gas pipeline services.

### 13.2 UNIQUE CHARACTERISTICS OF GAS PIPELINE SERVICES

#### *13.2.1 Scope of Regulated Services*

685 The Input Methodologies Discussion Paper outlines the Commission's preliminary views on the scope of regulated gas pipeline services.<sup>127</sup> The Commission considers that the definition of gas pipeline services suggests an active management of pipelines rather than merely providing and maintaining the pipelines and associated equipment. It includes ensuring that pipelines are appropriately pressurised, are safely operated and are appropriately maintained. It also includes many contractual and administrative functions necessary for the conveyance of natural gas.

686 In summary, the Commission's preliminary views, as outlined in the Input Methodologies Paper, are that the following are considered to be included in regulated gas pipeline services:

- gas pipeline services;
- supply, operation and maintenance of operational meters;<sup>128</sup> and
- administration of balancing services.

687 The Commission's preliminary view is that connection and disconnection services,<sup>129</sup> supply of metering services (excluding costs associated with the supply, operation and maintenance of operational meters), supply of balancing gas (excluding administration of balancing) and financial responsibility for losses of natural gas would be excluded from the scope of regulated services.

#### *13.2.2 Ownership of the Regulated Suppliers of Gas Pipeline Services*

688 There are four suppliers of regulated gas pipeline services being:

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<sup>127</sup> Supra n 2, paragraph 3.108.

<sup>128</sup> Operational meters are all meters other than those at consumer premises. They therefore include meters at transmission system receipt and delivery points.

<sup>129</sup> Connection and disconnection services relate to the connection and disconnection of consumer premises at the request of a retailer (not the supplier) for reasons of credit and vacant premises. See Supra n 2, paragraphs 3.109 - 3.112.

- Vector Ltd. (distribution and transmission services);
- Powerco Ltd. (distribution services);
- Maui Development Ltd. (MDL) (transmission services); and
- Wanganui Gas Ltd. (distribution services).

689 These suppliers each have their own unique ownership structures. MDL's structure may be of relevance to the application of information disclosure. MDL is a bare nominee company that acts as an agent for the three joint venture companies (Shell Petroleum, OMOVNZ and Todd Energy). MDL submitted, in response to the Provisions Paper, that it does not have financial statements that it can disclose and that any information additional to that already disclosed, "...if available, will be artificially constructed, expensive to produce and may be of limited practical value".<sup>130</sup>

690 The Commission notes that MDL is required to disclose an ROI performance measure under the GIDRs, and therefore considers that this financial information must already be readily available, even if not in the format proposed for the information disclosure requirements under the Act. Irrespective of this, it is the Commission's preliminary view that MDL should disclose financial information for the regulated business, for the reasons outlined in paragraphs 209 to 212.

### ***13.2.3 Separate Treatment of Distribution and Transmission Services***

691 Gas pipeline services as defined in s 55A include both gas distribution and transmission services, as both involve the conveyance of natural gas by pipeline. This is similar to the way that the electricity lines services are defined in s 54C to include distribution and transmission. However, unlike the electricity lines services definition which has specific provisions for transmission, the same provisions apply in respect of gas distribution and transmission services.

692 As outlined below, it is considered that some components of disclosed information regulation, such as the disclosure requirements relating to capacity utilisation and quality measurement, may need to be treated differently for distribution and transmission services.

693 It is the Commission's preliminary view that separate disclosure requirements should be determined for distribution and transmission businesses, with separate disclosures required for each type of service where a supplier provides both transmission and distribution services.

### ***13.2.4 Applicable Regulatory Instruments***

694 Gas pipeline services are subject to information disclosure regulation (s 55C) and price-quality regulation on or after 1 July 2010 (s 55D).

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<sup>130</sup> Maui Development Limited, *Response to Commerce Commission: Regulatory Provisions of the Commerce Act 1986 Discussion Paper*, 9 February 2009, page 4.

695 The information disclosure regime is a standalone regime with the purpose of ensuring that interested persons have sufficient information to determine whether s 52A is being met. Irrespective of whether other regulatory instruments apply to a supplier in addition to information disclosure regulation, the Commission's preliminary view is that a similar scope, detail, prescription and consistency of disclosed information would need to apply to all suppliers of regulated services. This is in order to determine whether the Part 4 purpose is being met, and to promote a greater understanding of the performance of those suppliers.

Q.120) Are there any additional characteristics of gas pipeline services that would affect how the information disclosure regime for gas pipeline businesses should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.

### 13.3 APPLICATION OF INFORMATION DISCLOSURE REGULATION TO GAS PIPELINE SERVICES

696 This section outlines the Commission's preliminary views on how components of the disclosed information should be customised to gas pipeline services. The Commission's preliminary view is that the components of disclosed information should be as outlined in Chapters 5-10 where no customisation is proposed.

#### 13.3.1 Performance Indicators

697 The table below outlines the Commission's preliminary views on what performance indicators are relevant to gas pipeline services. Chapter 3 provides further details on the objectives of each of the performance indicators.

**Table 20: Specified Gas Services Performance Indicators**

Key Performance Area	Performance Indicator	Method of Calculating
Innovation and Investment	AMP review rating – innovation and Investment	Rating determined by Commission as part of the summary and analysis
	Capital expenditure ratio	$\frac{\text{Capital Expenditure}}{\text{Asset Base}}$
	Renewal ratio	$\frac{\text{Renewal expenditure}}{\text{Depreciation}}$
	Capital expenditure growth ratio	$\frac{\text{Growth expenditure}}{\text{Change in Transformer Capacity}}$

Key Performance Area	Performance Indicator	Method of Calculating
Efficiency	Operational expenditure ratio	<u>Operational expenditure</u> Asset base
	Overhead operational expenditure ratio	<u>Overhead expenditure</u> Asset base
	Maintenance expenditure ratio	<u>Maintenance expenditure</u> Asset base
	Capacity Utilisation	<u>Maximum Demand</u> TBA
	Relative Unit Price Index	(1)
Quality	SAIDI and SAIFI	Based on annual values
	AMP review rating - quality	Rating determined by Commission as part of the summary and analysis
Prices and Profits	ROI	<u>Regulatory profit</u> Asset base

- (1) *The method for calculating the relative unit price performance index performance indicator is yet to be determined. The Commission is to consider submissions on this performance indicator prior to publicising its draft determination. The Commission intends publishing its draft determination in the next round of consultation.*

Q.121) Do you agree that the performance indicators outlined in Table 20 are sufficient for the purpose of information disclosure under Part 4 for gas pipeline services? If not, please provide detailed examples of what performance indicators would better serve the purpose of information disclosure for gas pipeline services.

Q.122) What do you consider to be the appropriate method for calculating the relative unit price index? Please provide reasons for your view.

### ***13.3.2 Operational Expenditure Categories***

698 The Commission's preliminary view is that operating expenditure for gas pipeline services should be required to be broken down into the following categories:

- General management, administration and overheads;
- System management and operations;
- Maintenance;
- Pass-through costs; and
- Other.

- 699 The category for general management, administration and overheads would be for disclosure of “corporate” expenditure, which is not directly related to the management and operations of the network. This would include expenditure on items such as corporate management and reporting, Board expenditure, HR, accounting, non-system IT, procurement, property, legal, regulatory, operational health and safety, insurance and statutory expenses. The general management, administration and overheads expenses category should be used to determine the overhead operational expenditure ratio outlined in paragraphs 149 and 150.
- 700 System management and operations would cover all expenditure associated with the management and operation of the network, but which is not directly incurred in maintaining the network. This would include the operation of system control centres as well as asset management in its widest sense, involving planning studies, design, record-keeping, contract management, and maintenance of various operational and maintenance-related standards and procedures.
- 701 Costs in the asset maintenance category will include costs associated with maintaining the assets of the regulated supplier. Asset maintenance costs are to be used in the maintenance operational expenditure ratio as outlined in paragraphs 149 and 150.
- 702 Regulators generally provide for a pass-through cost mechanism as a way of appropriately sharing risk from unforeseen and uncontrollable costs between suppliers and consumers of regulated services. The criteria for a pass-through cost are discussed in paragraphs 237 and 238.
- 703 The Commission’s preliminary view is that the following pass-through costs would be appropriate to include as pass-through costs under information disclosure regulation for suppliers of gas pipeline services:
- local authority rates;
  - levies payable under 53ZE of the Act;
  - levies payable under the Gas Act 1992; and
  - levy payable under Commerce (Levy for Control of Natural Gas Services) Regulations 2005.<sup>131</sup>
- 704 A category for other expenses is also proposed to ensure that expenditure that cannot be readily categorised elsewhere is disclosed, rather than effectively requiring such expenditure to be allocated arbitrarily to a specific category.
- 705 In all cases, the expenditure to be disclosed should be that which relates to the provision of gas pipeline services. Where required, common costs will be allocated (between the pipeline business activity and any other businesses or other activities) according to the cost allocation input methodology.

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<sup>131</sup> Supra n 2, paragraph 13.132.

- 706 Where a gas pipeline business manages multiple networks for which separate disclosures are required, then an allocation of network management and operational expenses between networks will also be needed.
- 707 For consistency, all expenditure allocated to the categories other than general management, administration and overheads should be costs directly associated with those categories and should not include any “overhead” costs. “Overhead” costs should be separately disclosed as part of general management, administration and overheads rather than being built into those cost categories. The Commission considers that this approach is transparent and aids comparability between regulated suppliers. The Commission considers that there can be considerable variation in approach where such costs are allocated and incorporated within the disclosed expenditures. This tends to mask genuine resource differences and therefore reduces the usefulness of the disclosed information for comparisons between the businesses.
- 708 The Commission intends to provide further guidance where necessary to help ensure that regulated suppliers apply a consistent approach when classifying expenditure.

Q.123) Are there any additional operating expenditure categories that would assist in meeting the purpose of information disclosure for gas pipeline businesses? If so, please provide details of how the proposed operating expenditure categories would assist the purpose of information disclosure.

### ***13.3.3 Capital Expenditure Categories***

- 709 It is the Commission’s preliminary view that the following four categories be applied when disclosing capital expenditure on Gas Pipeline Businesses’ fixed assets:
- consumer connection and system growth;
  - reliability, safety and the environment;
  - asset replacement and renewal; and
  - asset relocations.
- 710 The proposed categories are based on the key drivers for capital expenditure. Capital expenditure on consumer connections is directly driven by growth in consumer numbers, while system growth-related capital expenditure is a function of the combination of growth in consumer numbers and growth in the intensity of use. Growth-related capital expenditure may also result from localised growth in peak demand. This category includes expenditure required to maintain security of supply, since in system planning terms this is intertwined with capacity and demand.
- 711 Expenditure that is driven by reliability (not including security of supply issues), safety and environmental requirements is essentially independent of growth. This expenditure may be to bring parts of the network up to required standards, and may



be to meet more onerous standards than existed when that part of the network was first constructed.

- 712 Asset replacement and renewal expenditure is primarily driven by the need for the replacement or renewal of assets which are at the end of their economic or functional lives.
- 713 Asset relocation expenditure is capital expenditure primarily driven by third party needs to move assets. This normally results from local authority or Transit roading projects. Accordingly, this category of expenditure is to be used where the cost of moving assets is for reasons other than routine maintenance, refurbishment and renewal maintenance or fault and emergency maintenance.

Q.124) Are there any additional capital expenditure categories that would assist in meeting the purpose of information disclosure for gas pipeline businesses? If so, please provide details of how the proposed capital expenditure categories would assist the purpose of information disclosure.

#### ***13.3.4 Asset Categories and Asset Lives***

714 As outlined in paragraph 305, the Commission sees advantage in categorising the value of the RAB into asset categories. The Commission's preliminary view is that asset categories for gas pipeline services should distinguish between assets with different accounting treatments and major classes of assets. Therefore, the Commission considers that the asset categories for gas pipeline services should include:

- pipelines and associated service pipelines;
- stations (including gate stations and pressure reducing stations);
- valves (underground valves - distinct from those installed at stations – and ancillary equipment);
- control Systems (e.g. SCADA hardware and software); and
- stores and spares.

715 The Commission reviewed the asset categories when determining the authorisation for the supply of controlled gas pipeline services by Powerco and Vector (Gas Authorisation)<sup>132</sup> and found these categories to be appropriate.

Q.125) Are there any additional asset categories that would assist in meeting the purpose of information disclosure for gas pipeline services? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.

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<sup>132</sup> Commerce Commission, *Authorisation for the Control of Supply of Natural Gas Distribution Services by Powerco Limited and Vector Limited, Decisions Paper*, 30 October 2008.

716 The Commission considers that, in the first instance, either the standard asset lives set out in the MED's updated (2002) draft Gas ODV Handbook, or the Commission's Valuation Methodology for the Gas Authorisation, may be appropriate for inclusion in a Historic Cost Handbook for suppliers of gas pipeline services.<sup>133</sup> The Commission notes in the Input Methodologies Discussion Paper that it may allow for deviation from standard asset lives where appropriate.<sup>134</sup>

### ***13.3.5 Statistics and Capacity Utilisation***

717 As discussed in paragraph 402, the purpose of disclosing statistics is to support and inform the analysis of performance indicators, thereby providing further information to assess the provision of services in terms of the Part 4 purpose statement. Statistics relating to assets used, capacity, demand and pricing are required for this purpose.

718 The Commission's preliminary view is that relevant statistical information for gas pipeline services should include:

- assets statistics – including system length by pipe type, operational meter capacity, age of system fixed assets and capacity of intake and offtake connection points statistics;
- demand statistics – including total annual amount of gas conveyed, maximum demand, non-coincident maximum demand and consumer connections demand;
- energy delivery efficiency statistics – including load factor and unaccounted for gas ratio; and
- pricing statistics – including average price information per unit, per consumer size grouping, calculated based on total revenue for each consumer size group compared to units supplied. This information allows the calculation of the unit price index as discussed in paragraph 410.

719 The Commission considers that requiring the disclosure of pipeline length, pipeline material and pipeline diameter will assist interested persons in their assessment of whether information disclosure regulation is promoting the purpose of Part 4 of the Act because it provides further information that will enhance the assessment of the efficiency of operational and capital expenditure.

720 The GIDRs allow estimates to be used in regard to certain capacity measures relating to metered and unmetered gas flow.<sup>135</sup> The Commission's preliminary view is that estimates should continue to be used where appropriate.

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<sup>133</sup> Supra n 2, paragraph 13.98.

<sup>134</sup> Ibid., paragraph 6.285.

<sup>135</sup> Estimates are permitted in regard to gas flows that are not metered. Refer to the Gas (Information Disclosure Regulations 1997, Schedule 1(5)(9) (Measured volumes and estimates).

- 721 As discussed in paragraphs 154 and 155, for capacity utilisation to be assessed, an understanding of annual, maximum peak and non-coincident maximum peak demand is useful. The Commission's preliminary view is that maximum peak demand should be measured. The measurement of maximum non-coincident peak demand allows for capacity utilisation to be assessed. The capacity of operational meters will need to be disclosed at the points where maximum peak demand is measured to allow this to occur.
- 722 The load factor and unaccounted for gas (UFG)<sup>136</sup> ratio provide interested persons with an indication as to the efficiency of the system, although it is noted that factors other than efficiency are likely to influence the outcomes of the load factor and UFG ratios. The Commission's preliminary view is that the load factor and UFG ratio should be calculated on the same basis as the GIDRs, as the calculations are simple, familiar to sector participants, and are readily comparable measures of system efficiency.
- 723 As outlined in paragraph 409, the Commission considers that, where appropriate, suppliers should be required to disclose prices across a variety of services, consumer classes and/or geographic areas. This is consistent with the view that efficient prices reflect requisite quality within each consumer grouping, as outlined in paragraph 408. Under the EDB disclosure requirements, the disclosure of pricing statistics is intended to facilitate comparison between regulated suppliers in terms of average prices charged to readily identifiable consumer groups. Consumers are categorised into similar groups in the gas sector, making a similar approach to gas statistics disclosure appear valid.
- 724 The Commission's preliminary view is therefore that suppliers of gas pipeline services should be required to disclose pricing statistics for consumers grouped by size, similar to the current information disclosure requirements for EDBs.<sup>137</sup> Disclosure of pricing statistics by non-contiguous network will also be required as outlined in paragraph 409.
- 725 The Commission's preliminary view is that consumer size pricing information should be separated into the following categories:
- domestic – end consumers generally with an installed meter capacity of less than 10 standard cubic meters per hour (scm/hr);
  - commercial – commercial consumers with meter capacities up to 200 scm/hr; and

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<sup>136</sup> The term UFG refers to the difference in gas volume entering the network and gas leaving the network as measured by consumers' meters. The difference may be accounted for by leakage, theft or meter inaccuracies. UFG provides an indication of network condition and the accuracy of measurement devices. However the Commission notes that due to a number of variables, exact volumes are difficult to measure in some cases.

<sup>137</sup> Commerce Commission, *Electricity Distribution (Information Disclosure) Requirements 2008*, 31 October 2008, Schedule 11.

- Industrial – end consumers with a load size great than 200 scm/hr.

Q.126) Do you agree that relevant statistical information for gas pipeline services should include asset information, demand, energy delivery efficiency and pricing statistics? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.127) Do you agree that the maximum demand and maximum non-coincident peak demand should be measured? If not, please provide details of how capacity utilisation should be measured and the reasons for your view.

Q.128) Do you agree that suppliers of gas pipeline services should be required to disclose pricing statistics for consumers grouped by size, as currently required in the EDB information disclosure requirements? If not, please provide the reasons for your view, an alternative to assessing pricing efficiency and why you consider this to be preferable.

### 13.3.6 Quality

726 As discussed in paragraphs 381 - 385, the Commission's preliminary view is that there are four aspects of quality that could be measured, being :

- reliability of service;
- supply quality (including pipeline pressure);
- customer service; and
- safety.

This section discusses the four aspects of quality and the Commission's preliminary views on their applicability for gas pipeline services. Given that the Commission recently considered appropriate indicators of service quality for gas pipeline businesses in setting terms for the Gas Authorisation, this section makes a number of references to the decisions paper for that authorisation. The Commission's preliminary views on the disclosure of quality in the AMPs is outlined in paragraphs 373-379, while the disclosure of actual and target quality is discussed in paragraphs 365-367.

727 It is considered that safety is an essential component of quality; however as outlined in paragraphs 389 and 390 it is the Commission's preliminary view that disclosure of safety measures is not required.

Q.129) Do you agree that the key aspects of service quality for gas pipeline services should include reliability, supply quality and customer service? If not, please provide details of the aspects of quality that are relevant and the reasons for your view.

#### *Reliability of Service*

728 Reliability for gas pipeline services is currently measured under the GIDRs in terms of unplanned interruptions to the gas supply experienced (and originating) at both the transmission and distribution levels. At the transmission level, this is currently

measured by unplanned outages affecting the pipeline, by cause, and in terms of the number of hours lost. At the distribution level, this is recorded as the number of interruptions experienced by consumers, and hours lost. In addition, the GIDRs require the disclosure of UFG – in terms of the ratio of the volume of UFG to total gas delivered to entry points.<sup>138</sup>

- 729 The Commission proposes to retain the focus of reliability measures using service interruptions, UFG and the current transmission/distribution segmentation of interruption origin. The Commission also proposes to augment the current requirements by requiring additional information with which interested persons can assess system reliability. In addition to the existing requirements under the GIDRs, the Commission proposes to include requirements to disclose:
- planned (as distinct from unplanned) interruptions to the gas supply;
  - interruptions that originate at the highest points (i.e. at the wellhead and/or processing level) in the gas supply chain; and
  - the cause of each interruption.
- 730 It is the Commission’s preliminary view that interruption classes and sub categories would therefore comprise the following:
- gas transmission: planned and unplanned interruptions;
  - gas distribution: planned and unplanned interruptions (not required for gas transmission disclosures); and
  - other.
- 731 The Commission also considers that quantifiable measures of reliability such as SAIDI, SAIFI and CAIDI discussed in paragraph 387 above, as currently applied to Vector and Powerco under the Gas Authorisation may usefully be applied to information disclosure for the gas pipelines sector.<sup>139</sup>
- 732 In addition to interruptions, additional incident categories the Commission considers should be disclosed include third party damage events, leaks, and public reported escapes - whether or not such events cause interruptions to service.<sup>140</sup>
- 733 The Commission considers that the additional information available through these mechanisms will serve the purpose of Part 4 by enhancing the ability of interested persons to compare suppliers in terms of reliability. The Commission acknowledges that this may increase the compliance costs of regulated suppliers and is interested to hear from interested parties as to what these costs would be.

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<sup>138</sup> Gas (Information Disclosure) Regulations 1997, Schedule 1(3)(1)(b).

<sup>139</sup> Commerce Commission, *Commerce Act (Powerco Natural Gas Service) Authorisation 2008*, Schedule 5, page 22.

<sup>140</sup> *Ibid.*, Schedule 6, page 24.

Q.130) Do you agree that reliability for gas pipeline services should include the disclosure of planned and unplanned interruptions, the causes of interruptions, third party damage events, leaks, public reported escapes and SAIDI, SAIFI and CAIDI measures? If not, please provide the reasons for your view, alternatives and why you consider these to be better aligned to the purpose of information disclosure.

### *Supply Quality*

734 As noted in paragraph 391, the supply quality category is intended to capture aspects of quality other than reliability and safety that lie within the direct control or influence of the regulated supplier. Measures of supply quality are largely dependent upon the type of regulated service. A supply quality criterion for the gas pipeline sector could include measures of system condition and integrity, such as gas pressure experienced by consumers, including poor pressure due to network causes. Other technical measures of gas quality (such as calorific value or Wobbe index measurements) may be beyond the direct control of gas distribution or transmission businesses. In such cases, the Commission's preliminary view is that they should not be included as part of information disclosure requirements applicable to gas pipeline services.

735 For this reason and because (as noted in paragraph 368) requisite quality expectations vary between different consumer groups, it is the Commission's preliminary view that the scope for including supply quality as a performance indicator or even a measure of actual quality may be limited to those aspects within the suppliers' control. The Commission is of the view that supply quality for regulated suppliers is best addressed as part of the asset management plan disclosures on requisite quality.

Q.131) What measures do you think might be appropriate for the measurement of supply quality (other than reliability) for gas pipeline services? Please provide your reasons.

### *Customer Service*

736 As noted in paragraph 398, customer service is an important measure of quality for regulated suppliers. Customer service can be measured through the assessment of consumer perceptions or outcomes of performance. The Gas Authorisation outlines three outcome-based performance measures related to customer service, being:

- responses to emergencies – proportion of emergencies responded to within a certain time period;
- answering telephone calls – call centre answering statistics, including time to connect; and
- complaints – number of complaints received.<sup>141</sup>

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<sup>141</sup> These measures are currently applicable under the Commerce Commission Authorisations for Gas

- 737 The Commission notes that there may be different points of contact for consumers (as defined above) in regard to customer service for suppliers of gas pipeline services. While suppliers typically advertise a contact number for pipeline related issues, this number is intended to be used in relation to works taking place in the vicinity of gas pipelines, and is thus related to safety (rather than consumer experience) issues. Consumers are more likely to contact their gas retailer with service issues, whether an issue is within the control of the gas service provider or not. The Commission expects to raise this point for discussion at workshops to be scheduled prior to the setting of the information disclosure requirements.
- 738 It is the Commission's preliminary view that the three measures above could be useful in assessing customer service for suppliers of gas pipeline services.

Q.132) What do you believe is the appropriate means of measuring service quality for gas pipeline businesses? Please provide the reasons for your view.

### ***13.3.7 Disaggregation and Segmentation of Information***

- 739 The Commission sees value in the assessment of performance between non-contiguous networks, due to the risk of one network potentially subsidising another network, or quality being compromised in one network in favour of another. For this reason the Commission has required EDBs to disclose separate statistics and quality information for non-contiguous networks. Interested persons can assess specific network performance by analysing pricing and quality statistics, with statistics regarding assets, demand and capacity informing the assessment.
- 740 The Commission's preliminary view is that there is value in applying a similar approach to gas pipeline services. This would require the separate disclosure of statistics and quality information for networks that are geographically separate. A strict separation of gas networks on the basis of transmission system delivery points would result in an overly segmented approach where only small rural networks are connected to the transmission system. The Commission has noted that for EDBs, those networks that are geographically separate may be considered non-contiguous, but where they meet a certain threshold of size they do not require separate disclosure. In the Commission's preliminary view, a similar approach should be taken for gas.

Q.133) Do you agree that disclosure of separate statistics and quality information for non-contiguous networks is appropriate information for the assessment of performance? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

Q.134) In your view, what thresholds or criteria should the Commission use as a means of excluding networks from the requirement to separately disclose quality and statistics information? Please provide the reasons for your view.

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Pipeline Services that apply to Powerco Ltd. (Decision 656) and Vector Ltd. (Decision 657). For reference, see *Ibid.*, Schedule 5, page 23.

### 13.4 SCOPE OF DISCLOSURES SUMMARY

741 The following table summarises the Commission's preliminary views on the scope of the gas pipeline services disclosures and compares this to the current disclosure requirements. The table identifies where the disclosure of information is similar to the current disclosure requirements. Actual content may, however, differ from those current disclosure requirements identified. The requirements will need to be consistent with the relevant Input Methodologies and any new or revised handbooks.

**Table 21: Proposed Scope of Disclosures Summary**

<b>Proposed Disclosures</b>	<b>Scope of Disclosures</b>	<b>Comparison to Current Disclosure Requirements<sup>142</sup></b>
Performance Indicators	As outlined in Table 20.	Includes a number of new disclosures that are derived from the proposed disclosed information.

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<sup>142</sup> Gas (Information Disclosure) Regulations 1997.



Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>142</sup>
Financial Information	<p>The proposed financial disclosures are consistent with GAAP, where appropriate. For regulatory reporting purposes, however, there are instances where either more, or less, prescriptive information than GAAP is required.</p> <p>The proposed disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Regulatory Profit Statement &amp; Notes;</li> <li>▪ Regulatory Asset Statement;</li> <li>▪ Regulatory Tax Calculation;</li> <li>▪ Forecast Statement; and</li> <li>▪ Consolidation Statement.</li> </ul> <p>Key areas where more prescriptive information is required include:</p> <ul style="list-style-type: none"> <li>▪ Treatment of revaluations, vested assets and capital contributions; and</li> <li>▪ Disclosure of operational and capital expenditure categories.</li> </ul>	<p>Current disclosures are based on GAAP. Some operational expenditure information, however, is required.</p>
Regulatory Asset Base	<p>The proposed disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Regulatory Valuation Roll-Forward Report;</li> <li>▪ Annual Valuation Roll-Forward by Asset Class Report;</li> <li>▪ Asset Transactions with Other Regulated Suppliers Report; and</li> <li>▪ Initial RAB Report (one-off report).</li> </ul>	<p>No mandatory asset valuation methodology or other disclosure requirements prescribed other than as per GAAP.</p>

Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>142</sup>
Statistics	<p>The proposed statistics information includes:</p> <ul style="list-style-type: none"> <li>▪ Asset Statistics;</li> <li>▪ Demand Statistics;</li> <li>▪ Capacity Statistics; and</li> <li>▪ Pricing Statistics.</li> </ul>	<p>The proposed pricing statistics are new. Other proposed statistics may be more refined than in the current disclosures.</p>
Quality	<p>The proposed actual quality disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Interruptions;</li> <li>▪ Reliability; and</li> <li>▪ Customer service.</li> </ul> <p>The disclosure of target and requisite quality are outlined in the AMP section.</p>	<p>The proposed disclosures are a refinement of the current disclosure requirements, except that the proposed customer service disclosures are new.</p> <p>Proposed disclosure requirements are more aligned to the information on quality required for the authorisation for the controlled gas pipeline services of Powerco and Vector.</p>
Asset Management Plans	<p>The proposed AMP disclosure include:</p> <ul style="list-style-type: none"> <li>▪ Assets covered;</li> <li>▪ Service levels;</li> <li>▪ Development planning;</li> <li>▪ Lifecycle asset management planning;</li> <li>▪ Risk management; and</li> <li>▪ Evaluation of performance.</li> </ul> <p>It is proposed the AMP disclosures cover a period of no less than 10 years.</p>	<p>AMPs are not required under the current requirements, however, some information proposed to be included in AMPs was previously disclosed.</p>

Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>142</sup>
Pricing	<p>The proposed pricing disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Pricing Methodology;</li> <li>▪ Prices;</li> <li>▪ Pricing Statistics; and</li> <li>▪ Contracts.</li> </ul>	Proposed disclosures are generally consistent with current disclosures, except new pricing statistics disclosures.
Other	<p>The proposed other disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Assumptions;</li> <li>▪ Methodologies; and</li> <li>▪ Policies.</li> </ul>	Increased disclosure of assumptions and methodologies. Proposed policies disclosures are new.
Segmentation of Business Activity	<p>Proposed requirement to prepare separate disclosures for Transmission and Distribution activities.</p> <p>Proposed requirement to disclose separate quality and statistics information for non-contiguous networks.</p>	The separate disclosure of Transmission and Distribution activities is consistent with the current requirements. Separate disclosure of non-contiguous networks is a new requirement.
Publication, Retention, Certification	<p>Director certification and audit requirements for Annual Disclosures.</p> <p>Director certification requirements for AMPs.</p> <p>Statutory declaration requirements for all disclosures.</p>	Similar to current regulations. The relevant requirements include Regulations 31 and 32.

742 The remainder of this section outlines the information required to be disclosed under the GIDRs that, in the Commission's preliminary view, should not be required under the proposed new disclosure regime. The GIDRs require disclosing entities to prepare financial information in compliance with GAAP. As noted in paragraph 220, the Commission's preliminary view is that some GAAP disclosures may not be appropriate or necessary for regulatory reporting purposes.

- 743 Paragraphs 220 - 223 outline the Commission's preliminary views on why financing and financial instruments, cashflow and equity information should not be required for disclosure under Part 4. Derivatives and their fair value adjustments should not be required for the same reasons. Paragraphs 222 and 244 outline why working capital disclosures are not considered necessary.
- 744 The GIDRs include the requirement to disclose detailed information regarding a regulated supplier's network capacity.<sup>143</sup> The proposed disclosure requirements include the following information which will include some of the information on network capacity from those disclosures:
- Statistics – summary capacity and demand information; and
  - AMP – detailed capacity and demand information.
- 745 The Commission seeks the views of interested parties as to whether the detailed information regarding a regulated supplier's network capacity should continue to be disclosed.
- 746 The GIDRs also include provision for the disclosure of information that only relates to the Corporation (formerly NGC), and they do not apply consistently to all regulated suppliers. It is the Commission's preliminary view that the requirements should not distinguish between regulated suppliers.

Q.135) Do you agree that the above mentioned disclosures from the GIDRs are not required for the purposes of information disclosure under Part 4? If not, please explain how they would assist with the purpose of information disclosure.

Q.136) In your view, should the detailed network capacity information currently required to be disclosed through the GIDRs continue to be required under the new information disclosure requirements? Please provide the reasons for your view.

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<sup>143</sup> Gas (Information Disclosure) Regulations 1997, Schedule 1, Part 5.

## CHAPTER 14: SPECIFIED AIRPORT SERVICES

### 14.1 INTRODUCTION

747 This chapter provides an overview of information disclosure matters that are specific to specified airports services. The first section of the chapter provides an overview of the characteristics of specified airport services that are both unique to specified airport services and relevant to the information disclosure regime. The second section outlines the Commission’s preliminary views on how, in light of the unique characteristics of specified airport services, the information disclosure regime should be customised to specified airport services.

### 14.2 UNIQUE CHARACTERISTICS OF SPECIFIED AIRPORT SERVICES

#### *14.2.1 Definition of Consumers of Specified Airport Services*

748 As discussed in Chapter 4 of the Input Methodologies Discussion Paper, the Commission considers that, in the case of airports, “consumer” refers not only to end-users such as airline passengers, but also to airlines and other users of the specified airport services such as border protection agencies and freight forwarding companies. In particular, the Commission recognises that some services, such as:

- services involved with hangar activities, might be considered to be consumed by airlines and freight forwarders, although passengers may receive an indirect benefit from this;
- the provision of flight information display screens, might be considered to be consumed by passengers, although airlines receive an indirect benefit from this; and
- the provision of passport control space, might be considered to be jointly consumed by a border protection agency and passengers.

749 In seeking to achieve the purpose of information disclosure regulation as it applies to specified airport services, the Commission will consider the extent to which the interests of the various types of “consumer” coincide or diverge.

#### *14.2.2 Ownership and Business Activities of the Regulated Airports*

750 Suppliers of regulated specified airport services provide both infrastructure (with third parties obtaining access in order to provide downstream services) and certain downstream and/or supporting services such as ground handling, rescue fire, and air traffic control services themselves. The extent of downstream services varies depending on the airport – see below. The Commission’s preliminary view is the difference in businesses activities of the regulated airports may make comparison between regulated suppliers problematic. There is therefore greater value to be obtained from ensuring transparency so that interested persons can understand the effect different business activities have on reported performance.

751 A summary of the structure and ownership, extent of business activities and the overall assets employed by Auckland International Airport Limited (AIAL), WIAL

and CIAL is contained in Table 22. As shown in the table, all three airports supply a mixture of regulated and unregulated services.

**Table 22: Regulated Airports and Key Information**

Airport Operator	Overall business activities	Overall Airport Assets <sup>144</sup>
Auckland International Airport Limited (AIAL)	<p>Provides airfield and terminal services, a rescue fire service, meteorological services, and international apron management.</p> <p>Provides food and beverage services in the international terminal with its joint venture partner, Host Marriott.</p> <p>Previously operated the quarantine waste disposal facility at the airport but has now ceased.</p>	<p>Land, runways, aprons, three terminal buildings, a substantial retail precinct, car parking, vehicles and commercial and office buildings.</p> <p>A new international pier was completed in 2008 and is capable of accommodating the new A380 aircraft.</p>
Wellington International Airport Limited (WIAL)	<p>Provides airfield, terminal and other directly related services and facilities.</p> <p>Also provides services to passengers including car parking, bus and taxi facilities, food and beverage, shops, lounges and advertising.</p> <p>Approximately 20 hectares of land is used for non-core aeronautical use including hangers, freight/cargo facilities, offices and warehousing.</p> <p>Owens an outdoor advertising company, ISite Media.</p>	<p>Land, a single runway, aprons, the terminal building, car parking, other ancillary buildings, commercial retail development, other assets held for strategic purposes.</p> <p>Has expanded and redeveloped the international lounge, constructed two safe end runways and undertaken car parking development since 2005.</p>
Christchurch International Airport Limited (CIAL)	<p>Provides airfield, terminal and other directly related services and facilities.</p> <p>Diversifies its revenue base by focusing on investments and land holdings. Also offers technical input on site, with Air New Zealand having a maintenance base at the Airport.</p> <p>Owens the waste disposal facility at the Airport, contracting the operations out to the Medical Waste Group.</p> <p>Owens and operates the Antarctic Centre.</p>	<p>Land, two runways, aprons, the terminal building, car parking, and other ancillary land and buildings.</p> <p>Has commenced the development phase for the new domestic and international integrated terminal, due for completion in 2011.</p>

Source: *Final Report - Part IV Inquiry into Airfield Activities at Auckland, Wellington and Christchurch International Airports, August 2002, Annual Reports and Disclosure Financial Statements 2000-2008 and Company websites.*

<sup>144</sup> The assets used by each of the airports to provide the specified airport services that are regulated under the Act are a subset of these total assets.

### **14.2.3 Assets Utilised in Providing Regulated Services**

- 752 Unlike gas pipeline and electricity lines businesses, whose assets are largely physically constructed network assets (i.e., system fixed assets, or ‘SFA’), land makes up a high proportion of the assets used in providing specified airport services.
- 753 The other major asset types owned by the airports are the sealed surfaces that comprise the runway, taxiway and aircraft aprons, and buildings such as passenger terminals, hangars and freight storage.
- 754 The Commission’s preliminary view is that capital expenditure, operating expenditure, asset categories and the determination of asset lives should be customised to specified airport services to reflect the different assets utilised in providing the regulated services compared to other services that are regulated under Part 4.

### **14.2.4 Regulation under the Airport Authorities Act 1966 (AAA)**

- 755 Since 1986, the three airports have been subject to the generic pro-competitive and regulatory provisions in the Act, including the threat of control under Part 4. In addition, they are also subject to the Airport Authorities Act 1966 (AAA), which requires airports to operate as commercial undertakings. The AAA and associated regulations include provisions to address competition concerns and enhance the countervailing market power of airlines.
- 756 In particular, under section 4B of the AAA, airport operators are required to consult substantial customers when setting charges, and also when undertaking major capital expenditure. Section 4A allows an airport company, after consulting with substantial customers<sup>145</sup>, to set such charges as it thinks fit for the use of the airport and its services or facilities.
- 757 The consultation requirements currently imposed on the three airport companies by the AAA serve a different purpose to that of information disclosure under the Act. In particular, disclosures made under the AAA requirements are between the respective parties to the consultation and therefore would not meet the purpose of information disclosure in that they are not made available to all interested persons.

### **14.2.5 Scope of Information Disclosure Requirements for Suppliers of Specified Airport Services**

- 758 Suppliers of specified airport services are subject to information disclosure regulation only. AIAL in its submission on the Provisions Paper suggested that the

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<sup>145</sup> The AAA defines a *substantial customer* to be a person who pays (or is liable to pay) more than 5% of an airport’s annual revenues in relation to identified airport activities. In addition, a person who is authorised in writing to represent a number of persons who in aggregate pay (or are liable to pay) more than 5% of an airport’s annual revenues in relation to identified airport activities. For example, the Board of Airline Representatives of New Zealand Inc. (BARNZ) is deemed to be a substantial customer.

information disclosure regime itself must recognise that airports are subject to information disclosure only, which Parliament intended to be light-handed with low compliance costs.<sup>146</sup> The Commission agrees that the information disclosure requirements should only require suppliers to disclose information that is necessary to achieve the purpose of information disclosure regulation.

- 759 The Commission acknowledges these submissions and highlights that the information disclosure regime is a stand-alone regime with the purpose of ensuring that interested persons have sufficient information to determine whether s 52A is being met. Irrespective of whether other regulatory instruments apply to a supplier in addition to information disclosure regulation, the Commission's preliminary view is that a similar scope, detail, prescription and consistency of disclosed information would need to apply to all suppliers of regulated services in order to determine whether the Part 4 purpose is being met, and in order to promote a greater understanding of the performance of those suppliers.

#### **14.2.6 Single-Till and Dual-Till**

- 760 There are two common approaches used internationally for presenting the regulatory accounts of airports: a 'dual-till' and a 'single till' approach. Keeping the regulated and unregulated parts of an airport separate corresponds to a dual-till approach.<sup>147</sup> The single-till terminology is used to refer to the undifferentiated treatment of regulated and unregulated costs and revenues (which removes the need to allocate common costs between business units).<sup>148</sup>
- 761 In contrast to the position for many other utilities, regulated and unregulated airport services are usually considered to be mostly complementary services. Goods or services are complementary when they are consumed together, with the price of one affecting the demand for both. While debated internationally, some regulators argue that the complementary nature of demand for airport services implies that it might be efficient for the airport to cross-subsidise the regulated service using revenues from the unregulated part, provided that the incremental benefit to the whole airport from the reduced charges for regulated services outweighs the incremental cost.<sup>149</sup>
- 762 As explained in the Input Methodologies Discussion Paper, the Commission's preliminary view is that the purpose for which the Commission may require the disclosure of consolidated information under s 53D(1) in respect of unregulated

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<sup>146</sup> Auckland Airport, *Submission to the Commerce Commission on the Regulatory Provisions of the Commerce Act 1986 Discussion Paper*, 16 February 2009, page 3.

<sup>147</sup> The term 'dual till' therefore includes situations in which regulated or unregulated accounts are disaggregated down further, into multiple business units (alternatively, such a situation may occasionally be referred to as a 'multiple till').

<sup>148</sup> *Supra* n 2, Appendix A, paragraphs A17-A18.

<sup>149</sup> Network Economics Consulting Group, *'Dual till' at Sydney Airport – A report prepared for the ACCC by NECG, May 2000, p.6.*



services implies that the Commission is restricted to taking a dual-till approach to information disclosure regulation for suppliers of specified airport services.<sup>150</sup>

#### **14.2.7 Defining Service Quality**

763 In its submission on the Provisions Paper, AIAL suggested that the Commission, when designing an appropriate regulatory regime for airports, needs to take into account how service quality is different to that of network (distribution) utilities. AIAL noted that service quality for airports involves a significant experiential dimension (e.g. customer and passenger satisfaction) that is more challenging to quantify and measure.<sup>151</sup>

764 The Commission's preliminary view is that the definition of quality should be customised for specified airport services and should contain more emphasis on customer perception than the other regulated services. How quality is defined for specified airport services is discussed further in paragraphs 790 to 809.

#### **14.2.8 Other Characteristics Proposed by Submitters**

765 In its submission to the Provisions Paper, AIAL noted that the publication of forecast information as part of information disclosures would trigger continuous disclosure obligations of a listed company such as AIAL. AIAL said that this would require immediate disclosure of relevant information to the market as it becomes available, which would be inappropriate and unworkable.<sup>152</sup> The Commission notes that listed EDB companies are able to deal with this issue under their current information disclosure requirements.

766 Given the importance of forecasts in determining if investment and innovation is occurring, the Commission's preliminary view is that forecast information, where it assists in achieving the purpose of information disclosure, should be provided by all regulated suppliers, including suppliers of specified airport services.

Q.137) Are there any additional characteristics of specified airport services that would affect how the information disclosure regime for specified airport services should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.

### **14.3 APPLICATION OF INFORMATION DISCLOSURE REGULATION TO SPECIFIED AIRPORT SERVICES**

767 This section outlines the Commission's preliminary views on how components of disclosed information should be customised to specified airport services. The Commission's preliminary view is that the components of disclosed information should be as outlined in Chapters 5-10 where no customisation is proposed.

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<sup>150</sup> Supra n 2, paragraph 10.24.

<sup>151</sup> Supra n 146, page 9.

<sup>152</sup> Ibid., paragraph 189.

768 The table below outlines the Commission's preliminary views on what performance indicators are relevant to specified airport services. Chapter 3 provides further details on the objectives of each of the performance indicators.

**Table 23: Specified Airport Services Performance Indicators**

Key Performance Area	Performance Indicator	Method of Calculating
Innovation and investment	AMP review rating – innovation and Investment	Rating determined by Commission as part of the summary and analysis
	Capital expenditure ratio	$\frac{\text{Capital Expenditure}}{\text{Asset Base}}$
	Renewal ratio	$\frac{\text{Renewal expenditure}}{\text{Depreciation}}$
	Capital expenditure growth ratio	$\frac{\text{Growth expenditure}}{(1)}$
Efficiency	Operational expenditure ratio	$\frac{\text{Operational expenditure}}{\text{Asset base}}$
	Overhead operational expenditure ratio	$\frac{\text{Overhead expenditure}}{\text{Asset base}}$
	Maintenance expenditure ratio	$\frac{\text{Maintenance expenditure}}{\text{Asset base}}$
	Average price per unit	$\frac{\text{Total revenue}}{(1)}$
Quality	AMP review rating - quality	Rating determined by Commission as part of the summary and analysis
	Capacity Utilisation	(1)
	Customer Perception	(1)
Prices and Profits	ROI	$\frac{\text{Regulatory profit}}{\text{Asset base}}$

(1) The method for calculating the capacity and customer perception performance indicators and what denominators should be used in the capital expenditure growth ratio and average price per unit performance indicators is yet to be determined. The Commission is to consider submissions on these

*performance indicators prior to publicising its draft determination. The Commission intends publishing its draft determination in the next round of consultation.*

- Q.138) Do you agree that the performance indicators outlined in Table 23 are sufficient for the purpose of information disclosure under Part 4 for specified airport services? If not, please provide detailed examples of what performance indicators would better serve the purpose of information disclosure for specified airport services and the reasons for your view.
- Q.139) What do you consider to be the appropriate denominator for the capital expenditure growth ratio? Please provide the reasons for your view.
- Q.140) What do you consider to be the appropriate denominator in the average price per unit performance indicator? Please provide the reasons for your view.
- Q.141) What do you consider to be the appropriate calculation for the capacity utilisation performance indicator? Please provide the reasons for your view.
- Q.142) What do you consider to be the appropriate method for calculating a customer perception performance indicator? Please provide reasons for your view.

#### **14.3.1 Revenue**

769 As discussed in paragraphs 750 and 751 above, the extent of downstream services provided varies according to the airport. The Commission's preliminary view is that regulated suppliers of specified airport services should be required to disclose the level of revenue they are earning from property rent and lease income which, along with the disclosures as outlined in paragraph 819 below, will assist interested persons in understanding the degree to which services are provided or not provided and hence allow greater comparability between regulated entities.

- Q.143) Do you agree that specified airport service suppliers should disclose the level of revenue they are earning from property rent and lease income and that this, along with disclosure of the extent to which downstream services are provided by the airport company or its contracted suppliers, will be sufficient for interested persons to understand the affects of the different business activities on the performance of the regulated business unit? If not, please provide examples of disclosures that will allow interested persons to gain this understanding.

#### **14.3.2 Operational Expenditure Categories**

770 The Commission's preliminary view is that operating expenditure for specified airport services should be disclosed in the following categories:

- General management, administration and overheads;
- Asset management and operations;
- Asset maintenance; and
- Other expenses.

771 The category for general management, administration and overheads would be for disclosure of "corporate" expenditure. This expenditure should not directly relate

to the management and operations of the airport assets and service activities, but would include expenditure on items such as corporate management and reporting, Board expenditure, HR, accounting, non-system IT, procurement, legal, regulatory, operational health and safety, insurance and statutory expenses. The general management, administration and overheads expenses category should be used to determine the overhead operational expenditure ratio outlined in paragraphs 149 and 150.

- 772 The asset management and operations category covers all expenditure associated with the management and operation of the airport. This should not include expenditure that is directly incurred in maintaining the assets, but would include the costs associated with the operation of specified airport services, as well as asset management (in its widest sense) involving planning studies, design, record-keeping, contract management, and maintenance of various operational and maintenance-related standards and procedures. Total operational expenditure, excluding general management, administration and overheads, is a direct cost.
- 773 Costs in the asset maintenance category will include costs associated with maintaining the assets of the regulated supplier. Asset maintenance costs are to be used in the maintenance operational expenditure ratio outlined in paragraphs 149 and 150.
- 774 The other expenses category is proposed to ensure that any expenditure that cannot be readily categorised does not get arbitrarily allocated to an inappropriate category.
- 775 As discussed in the Input Methodologies Discussion Paper, the Commission is not aware of any pass through costs, currently incurred by suppliers of specified airport services that meet the criteria for pass-through and are significantly material to warrant separate disclosure.<sup>153</sup> Therefore, it is the Commission's preliminary view that no provision for the disclosure of pass-through costs is required.
- 776 In all cases, the expenditure to be disclosed should be that which relates to the activities described in s 56A(1) of the Act. Where required, common costs will be allocated (between the specified airports services activity and any other businesses or other activities) according to the input methodology for cost allocations.
- 777 For consistency, business overhead costs should be separately disclosed as part of general management, administration and overheads rather than being built into specific cost categories as defined in paragraph 770. The Commission considers that this approach is transparent and aids comparability between regulated suppliers. The Commission considers that there can be considerable variation in approach where such costs are allocated and incorporated within the disclosed expenditures. This tends to mask genuine resource differences and therefore

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<sup>153</sup> Supra n 2, paragraphs 10.118–10.122.

reduces the usefulness of the disclosed information for comparisons between the businesses.

- 778 The Commission intends to provide further guidance where necessary to help ensure that regulated suppliers apply a consistent approach when classifying expenditure.

Q.144) Are there any additional operating expenditure categories that would assist in meeting the purpose of information disclosure for specified airport services? If so, please provide details of how the proposed operating expenditure categories would assist the purpose of information disclosure.

### ***14.3.3 Capital Expenditure Categories***

- 779 It is the Commission's preliminary view that capital expenditure should be allocated to one of the following four categories:
- capacity growth;
  - reliability, safety and environment;
  - security requirements; and
  - asset replacement and renewal.
- 780 These four categories are intended to reflect the drivers of the capital expenditure.
- 781 Capacity growth capital expenditure is directly driven by growth in demand and is used in the capital expenditure growth ratio as outlined in paragraphs 116 - 118.
- 782 Asset replacement and renewal expenditure is expenditure that is primarily driven by the need for the replacement or renewal of assets that are at the end of their economic or functional lives. Asset replacement and renewal expenditure is used in the renewal ratio as outlined in paragraphs 113 and 114.
- 783 Separating the reliability, safety and environment category and the security requirements category enables these capital costs to be excluded from the calculation of the capital expenditure growth ratio and the renewal ratio.
- 784 These categories are similar to those proposed by BARNZ in its submission to the Provisions Paper, except that it excludes asset relocations.<sup>154</sup> The asset relocation expenditure category is not considered appropriate for specified airport services as airports would not normally be required to relocate assets by an external party. This is not the case for electricity lines or gas pipeline services that can be required to relocate assets as a result of local authority or Transit road-widening projects.
- 785 The Commission is mindful that airports capital expenditure can be more 'lumpy' than some other regulated businesses and this will need to be considered when assessing airports' investment performance. The Commission's summary and analysis will assist in providing clarity on this matter. In particular, it will be

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<sup>154</sup> Supra n 12, page 31.

important to try to gauge the extent to which expansion projects are being delivered at the least cost.

Q.145) Are there any additional capital expenditure categories that would assist in meeting the purpose of information disclosure for specified airport services? If so, please provide details of how the proposed capital expenditure categories would assist the purpose of information disclosure.

#### ***14.3.4 Asset Value Categories and Asset Lives***

786 As outlined in paragraph 305, the Commission sees an advantage in categorising the value of the RAB into asset categories. The Commission's preliminary view is that asset categories for airports should distinguish between assets with different accounting treatments and major classes of assets. Having considered submissions on the Provisions Paper, the Commission's preliminary view is that the asset categories for Airports should be:

- Land;
- Sealed surfaces;
- Infrastructure;
- Buildings; and
- Vehicles, plant and equipment.

Q.146) Are there any additional asset categories that would assist in meeting the purpose of information disclosure? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.

787 As outlined in the Input Methodologies Discussion Paper, standard asset lives would need to be specified for each of the main asset types. There have been no airport standard asset lives established for regulatory purposes in the past. The Commission notes the assets of each regulated supplier may have some unique characteristics. Thus, the Commission proposes to request regulated suppliers of airport services to provide to the Commission asset life information that has been certified by an appropriately qualified valuer and directors of the regulated supplier. The Commission would then consult with other interested parties on the appropriateness of those asset lives.<sup>155</sup>

#### ***14.3.5 Financing Assumptions***

788 The Commission has expressed its preliminary view in the Input Methodologies Discussion Paper that a cost of capital input methodology will not initially be established for airports.<sup>156</sup> However, as outlined in paragraph 245, financing

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<sup>155</sup> Supra n 2, paragraph 10.79.

<sup>156</sup> Ibid., paragraph 10.8.

assumptions are required when calculating deductible interest, regulatory tax, and the interest tax shield in the post-tax ROI calculation.

- 789 For other regulated services where a cost of capital input methodology is being established, it has been proposed (paragraph 245) that the relevant assumptions in the cost of capital input methodology be used where financing assumptions are required for information disclosure. If a cost of capital input methodology is not established for airports, the Commission proposes to issue the required financing assumptions for use in information disclosure. How the Commission will make the financing assumptions available is yet to be decided.

Q.147) Do you agree that if a cost of capital input methodology has not been established for specified airport services that the Commission should issue the required financing assumptions for use in information disclosure? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.

#### ***14.3.6 Quality Performance Indicators and Utilisation Statistics***

- 790 As discussed in paragraphs 385 - 401, the Commission's preliminary view is that there are four aspects of quality that could be measured, being :

- reliability of service;
- supply quality (including capacity and utilisation);
- customer service; and
- safety.

This section discusses the four aspects of quality and the Commission's preliminary views on their applicability for specified airport services. The Commission's preliminary views on the disclosure of quality in the AMPs is outlined in paragraphs 373-379, while the disclosure of actual and target quality is discussed in paragraphs 365-367.

- 791 It is considered that safety is an essential component of quality, however as outlined in paragraphs 389 - 390, it is the preliminary view of the Commission that disclosure of safety measures is not required.
- 792 It is also noted that capacity at airports is a complex issue due to the number of potential capacity constraints and the difficulty in measuring those constraints. It is the Commission's preliminary view that capacity and utilisation would be the major component of the second category in paragraph 790. The Commission is aware that the New Zealand Airport Association (NZAA) and BARNZ are working together to identify ways to measure capacity and utilisation at the airfield, at the apron, and at a number of terminal facilities during a peak period. The Commission intends using the measures identified through this process to inform the development of capacity utilisation performance indicators for airports.
- 793 As noted above, AIAL, in its submission on the Provisions Paper, outlined the view that service quality (in contrast to the quantitative metrics of quality in a network utility sector) involves a "significant experiential dimension ...customer and

passenger satisfaction that is more challenging to quantify and measure”.<sup>157</sup> Air New Zealand, in its submission to the Provisions Paper, states that complexity should not be a reason to restrict disclosure to just the specified airport services.<sup>158</sup>

Q.148) Do you agree that the key aspects of quality for specified airport services should include customer service, reliability and capacity/utilisation? If not, please provide the reasons for view, an alternative and why you consider this to be preferable.

- 794 The Commission notes that, under the information disclosure regime, it may only require the disclosure of information related to the provision of regulated services (or consolidated information, for the purpose of monitoring compliance with the requirements that apply to regulated services). However, given that quality measures are often based on consumer perceptions, then suppliers and the Commission may be unable to restrict consumer feedback (as a result of surveys) to that only in relation to regulated services.
- 795 The complementary nature of airport services, as discussed in paragraphs 794 to 796, creates difficulty in the assessment of quality. It can be difficult for consumers to distinguish between the regulated and unregulated activities. For example, if a consumer is asked to provide their perception on the ambience of an airport, it can be difficult for them to distinguish between the ambience of the regulated (e.g. aerobridges) versus unregulated (e.g. customs) areas of the airport.
- 796 In developing the quality standards, the Commission considers there will need to be a balance between having complex and potentially costly quality indicators versus more simplistic quality indicators that may address the quality of both regulated and unregulated services.

Q.149) Do you agree that there will need to be a balance between having complex and potentially costly quality indicators versus more simplistic quality indicators that may address the quality of both regulated and unregulated services? Please provide reasons for your view.

- 797 In its submission on the Provisions Paper, Air New Zealand noted a number of operational performance measures that may have relevance for quality and statistics disclosures. These included both raw data and statistics such as revenue per passenger.<sup>159</sup> In its submission, BARNZ noted additional quality performance measures and statistics related to interruptions. BARNZ also noted that for these to be meaningful, the reasons for unavailability would need to be disclosed. BARNZ

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<sup>157</sup> Supra n 146.

<sup>158</sup> Air New Zealand Limited, *Submission to the Commerce Commission on Regulatory Provisions of the Commerce Act 1986 – Discussion Paper*, 16 February 2009, page 21.

<sup>159</sup> Ibid., page 24.



considered that, in addition to availability, performance measures were needed, in quantitative form where possible.<sup>160</sup>

798 The Commission is aware that the NZAA and BARNZ are also working collectively to identify indicators that they see as appropriate for the measurement of quality for airports.

*Perceptions of Customer Service*

799 As noted above, passenger perception has been identified as an important means of assessing quality for specified airport services. Passenger perception can often provide a direct assessment of performance against expectations. As with other regulated services, passenger perception measures are an appropriate means of assessing customer service. In the case of airport services, it can also be a helpful measure of supply quality.

800 It is standard industry practice for airports and independent researchers to collect information on customer perceptions via surveys of airline passengers. The Airport Council International Airport Service Quality (ACI ASQ) survey is one such survey that is currently in use at AIAL and CIAL. The Commission understands that the WIAL is willing to start using the ACI ASQ survey if it is implemented as a quality assessment tool for specified airport service by the Commission.

801 The Commission's preliminary view is that the following ACI ASQ measures may have relevance for the measurement of customer perception for specified airport services:

- Availability of baggage carts / trolleys;
- Ease of finding your way through airport;
- Flight information screens and signs per passenger;
- Walking distance inside the terminal;
- Ease of making connections with other flights;
- Courtesy / helpfulness of airport staff;
- Availability of washrooms / toilets;
- Cleanliness of washrooms / toilets;
- Comfort waiting / gate areas;
- Cleanliness of airport terminal; and
- Ambience of terminal.

802 It is the Commission's preliminary view that customer perception of customer service should be used as an indicator of performance and that an established survey be used to collect information, if possible. The Commission is interested in

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<sup>160</sup> Supra n 12, page 34.

understanding what surveys are available and what the benefits/shortcomings of each are.

Q.150) Do you agree that passenger perception surveys should be used to measure customer service and supply quality for specified airport services? If not, please provide the reasons for your view.

Q.151) Do you agree that the ACI ASQ survey is an appropriate survey for collecting passenger perceptions for specified airport service? If not, please provide details of why the ACI ASQ survey is not appropriate and details of why an alternative survey would be more appropriate.

Q.152) Do you agree that the identified measures are appropriate for measuring passenger perceptions of quality? Are there any additional measures that would assist in the measurement of quality for specified airport services through passenger perceptions? If so, please provide the reasons for your view.

### *Reliability of Service*

803 The Commission's preliminary view is that reliability of service is relevant measurement of quality for specified airport services.

804 Planned and unplanned interruptions to the runway, stand positions, aerobridge and baggage handling services disclosures are currently required under the current disclosure requirements for airports.<sup>161</sup> The Commission's preliminary view is that reliability of service should continue to be disclosed, with indicators enhanced as necessary to assist in identifying whether the airport or a third party caused the interruption. BARNZ, in its submission on the Provisions Paper, agreed that the cause of interruption should also be disclosed.<sup>162</sup>

805 These measurements of reliability are concerned with the output performance of the service provider (such as the availability of a service). A different or extended approach is to measure the effect of the interruptions on the consumers of the service. This is not dissimilar to what the SAIDI, SAIFI and CAIDI measures for electricity lines services seek to achieve. Such a measure could consider whether the unavailability of services provided by the airport, whether material services or not, caused an on time departure delay and the extent of that delay.

Q.153) Do you agree that reliability of services should be disclosed and that the disclosures should be enhanced to identify the cause of the disclosure? If not, please provide the reasons for your view.

Q.154) Are there any additional services that should require disclosure of interruption information? If so, please provide of the reasons why the additional categories are important to the purpose of information disclosure.

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<sup>161</sup> Airport Authorities (Airport Companies Information Disclosure) Regulations 1999, Schedule, Clause 8.

<sup>162</sup> Supra n 12, page 34.

Q.155) Do you see the disclosure of the effect of interruptions on consumers as an important measure of quality for specified airport services? If so, please provide details of how this could be measured and the reasons for your view.

*Supply Quality – Capacity and Utilisation*

806 As mentioned above (paragraph 792), capacity is considered to be a key measure of quality for specified airport services. Capacity for specified airport services could be measured at the following points:

- Airfield (international and domestic); including:
  - Parking bays; and
  - Runways; and
- Terminal (international, domestic, and combined areas), including:
  - Aerobridges;
  - Check-in desks;
  - Departure lounge (seats and space);
  - Security screening space;
  - Passport control space (inbound and outbound);
  - Biosecurity screening and inspection and customs secondary inspection space;
  - Airside circulation space;
  - Baggage system;
  - Baggage collection space;
  - Baggage trolleys;
  - Flight information display screens; and
  - Information points.

807 Car parking and retail activities have not been included as they are not specified airport services under Part 4 of the Act. The adequate provision of security screening, passport control and biosecurity screening and inspection and customs secondary inspection *space* is proposed to be considered as these services are included as specified airport services under Part 4.

808 It may not be appropriate to measure capacity by comparing peak demand and service capacity given that it may be reasonable for airports to be fully constrained during peak times.<sup>163</sup> Rather it may be more appropriate to consider the duration of capacity constraint or near-full constraint.

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<sup>163</sup> The implication of being fully constrained at an airport is that customers may be delayed. Given the

809 It is the Commission's preliminary view that capacity should be disclosed at the points identified in paragraph 806 and that measurement of utilisation should be aligned to standard industry practice. The Commission proposes liaising with NZAA, BARNZ and other interested parties to determine the appropriate means of measuring capacity and utilisation for specified airport services. This is likely to occur in workshops organised by the Commission.

Q.156) Do you agree that capacity and utilisation of capacity is a key supply quality issue for specified airport services? Please provide the reasons for your view.

Q.157) Do you agree that capacity and utilisation should be measured at the above points? If not, please provide details of where capacity and utilisation should or should not be measured and the reasons for your view.

Q.158) Do you agree that it may not be appropriate to measure capacity by comparing peak demand and service capacity and that it may be more appropriate to consider the duration of capacity constraint or near-full constraint? If not, please provide the reasons for your view.

#### **14.3.7 Other Statistics**

810 As discussed in paragraph 402, the purpose of disclosing statistics is to support and inform the analysis of performance indicators. The information required to meet this purpose includes information on assets used, capacity, demand and pricing. As outlined above, capacity is a key measure of quality for airports, therefore a number of statistics on capacity and utilisation will feed into those quality measures discussed above.

811 The Commission's preliminary view is that relevant statistical information for Airports should include:

- a description of the assets and the capacity of those assets;
- details on the international and domestic demand, including passengers (arriving and departing), freight tonnage and aircraft;
- details on international and domestic peak demand, including passengers (arriving and departing) and aircraft; and
- pricing statistics.

812 As outlined in paragraphs 473 to 479, the purpose of disclosing pricing statistics is to assist in the assessment of pricing performance. As outlined by BARNZ in its submission on the Provisions Paper, "each airport expresses its charges in a different way. In addition, some charges are levied on airlines and others on passengers."<sup>164</sup> Therefore, the disclosure of pricing statistics on a common basis

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delivery of service can be delayed (which is not usually the case for electricity lines and gas pipeline businesses) customers may accept some delays during peak demand rather than be required to pay for additional capacity that is rarely utilised.

<sup>164</sup> Supra n 12, page 32.

(e.g., by passengers) will allow an assessment of prices between regulated suppliers.

- 813 As outlined in paragraphs 748- 749 the definition of consumers for specified airport services refers not only to end-users such as airline passengers, but also to airlines and other users of the specified airport services such as border protection agencies and freight forwarding companies. The Commission has proposed that for regulated electricity lines and gas pipeline services, pricing information be segregated so that an assessment of prices to the different consumer groups can be made.
- 814 The Commission's preliminary view is that there would be limited value in assessing prices at a consumer level for specified airport services as non-end-users such as airlines pass on the charges to the end-users, being passengers. Therefore, it may be more appropriate to disclose pricing statistics based on total revenue generated rather than who is directly charged.
- 815 When disclosing pricing statistics the Commission has for other regulated services (regulated under information disclosure provisions) analysed total revenue compared to outputs and have attempted where possible to use outputs that are aligned to the outputs used to determine charges, such as passenger numbers. However, the method for determining charges, such as the airlines terminal charge, varies between the three regulated airports. It is the Commission's preliminary view, therefore, that commonly used outputs that are the basis for airport pricing should be used in the pricing statistics disclosure.

Q.159) Do you agree that a description of the assets and their capacity should be disclosed? If not, please provide the reasons for your view.

Q.160) Do you agree that demand disclosures for specified airport services should include disclosure of international and domestic volumes for passenger, freight and aircraft movements? If not, please provide details of what should or should not be disclosed and the reasons for your view.

Q.161) Do you agree that pricing statistics disclosures for specified airport services should compare total revenue to units handled? If not, please provide the reasons for your view.

Q.162) Do you agree that pricing statistics for specified airport services should not assess prices at a consumer level? Please provide the reasons for your view.

#### ***14.3.8 Segmentation of Business Activities***

816 As outlined in paragraph B39 of Appendix B, specified airport services include three business activities:

- Aircraft and freight activities;
- Airfield activities; and
- Specified passenger terminal activities.

- 817 The three regulated airports have in the past, under the Airport Authorities (Airport Companies Information Disclosure) Regulations 1999, segmented their disclosures by business activity. The Commission's preliminary view is that the segmented information remains appropriate for assessing performance at the business activity level.
- 818 The Commission's preliminary view is that the segmented information should include revenue, operating expenditure, taxation and RAB information, including depreciation and revaluation. In coming to this view, the Commission considers the cost of collecting the required information to be relatively low compared to the contribution it makes to the purpose of information disclosure regulation by allowing an appropriate assessment of performance.
- 819 As discussed in paragraphs 750 - 751, the extent of downstream services provided by the airport company or its contracted suppliers varies according to the airport. This may make comparisons between regulated suppliers difficult to interpret. The Commission's preliminary view is that each supplier of specified airport services should be required to disclose its level of involvement in each specified airport service to allow interpretation of comparisons between the regulated suppliers. The Commission envisages a disclosure to the level of detail of the activities identified in the definitions of specified airport services in the AAA as being appropriate.

Q.163) Do you agree that separate disclosure of segmented aircraft and freight activities, airfield activities and specified terminal activities are important to assess regulated supplier performance for specified airport services? Please provide the reasons for your view.

#### **14.4 SCOPE OF DISCLOSURES SUMMARY**

- 820 The following table summarises the Commission's preliminary views on the scope of the specified airport services disclosures and compares this to the current disclosure requirements. The table identifies where the disclosure of information is similar to the current disclosure requirements. Actual content may, however, differ from those current disclosure requirements identified. The requirements will need to be consistent with the relevant Input Methodologies and any new or revised handbooks.

**Table 24: Proposed Scope of Disclosures Summary**

<b>Proposed Disclosures</b>	<b>Scope of Disclosures</b>	<b>Comparison to Current Disclosure Requirements<sup>165</sup></b>
Performance Indicators	As outlined in Table 23.	Includes a number of new disclosures that are derived from the proposed disclosed information.
Financial Information	<p>The proposed financial disclosures are consistent with GAAP, where appropriate. For regulatory reporting purposes, however, there are instances where either more, or less, prescriptive information than GAAP is required.</p> <p>The proposed disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Regulatory Profit Statement &amp; Notes;</li> <li>▪ Regulatory Asset Statement;</li> <li>▪ Regulatory Tax Calculation;</li> <li>▪ Forecast Statement; and</li> <li>▪ Consolidation Statement.</li> </ul> <p>Key areas where more prescriptive information is required include:</p> <ul style="list-style-type: none"> <li>▪ Treatment of revaluations, vested assets and capital contributions; and</li> <li>▪ Disclosure of operational and capital expenditure categories.</li> </ul>	Current disclosures are based on GAAP.

<sup>165</sup> Airport Authorities (Airport Companies Information Disclosure) Regulations 1999.

<b>Proposed Disclosures</b>	<b>Scope of Disclosures</b>	<b>Comparison to Current Disclosure Requirements<sup>165</sup></b>
Regulatory Asset Base	<p>The proposed disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Regulatory Valuation Roll-Forward Report;</li> <li>▪ Annual Valuation Roll-Forward by Asset Class Report;</li> <li>▪ Asset Transactions with Other Regulated Suppliers Report; and</li> <li>▪ Initial RAB Report (one-off report).</li> </ul>	No mandatory asset valuation methodology or other disclosure requirements prescribed other than as per GAAP.
Statistics	<p>The proposed statistics information includes:</p> <ul style="list-style-type: none"> <li>▪ Asset Statistics;</li> <li>▪ Demand Statistics;</li> <li>▪ Capacity Statistics; and</li> <li>▪ Pricing Statistics.</li> </ul>	The proposed pricing statistics are new. Other proposed statistics may be more refined than in the current disclosures.
Quality	<p>The proposed actual quality disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Reliability;</li> <li>▪ Capacity and utilisation; and</li> <li>▪ Customer service.</li> <li>▪ The disclosure of target and requisite quality are outlined in the AMP section.</li> </ul>	The proposed disclosures are a refinement of the current disclosure requirements, except that the proposed customer service disclosures are new.



Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>165</sup>
Asset Management Plans	<p>The proposed AMP disclosure include:</p> <ul style="list-style-type: none"> <li>▪ Assets covered;</li> <li>▪ Service levels;</li> <li>▪ Development planning;</li> <li>▪ Lifecycle asset management planning;</li> <li>▪ Risk management; and</li> <li>▪ Evaluation of performance.</li> </ul> <p>It is proposed the AMP disclosures cover a period of no less than 10 years.</p>	AMPs are not required under the current requirements.
Pricing	<p>The proposed pricing disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Pricing Methodology;</li> <li>▪ Prices;</li> <li>▪ Pricing Statistics; and</li> <li>▪ Contracts.</li> </ul>	Proposed disclosures are generally consistent with information disclosed under the current requirements, except new pricing statistics disclosures.
Other	<p>The proposed other disclosures include:</p> <ul style="list-style-type: none"> <li>▪ Assumptions;</li> <li>▪ Methodologies; and</li> <li>▪ Policies.</li> </ul>	Increased disclosure of assumptions and methodologies. Proposed new policies disclosures.
Segmentation of Business Activity	Proposed requirement to disclose separate financial information for airfield, aircraft and freight and specified terminal activities.	The separate disclosure of airfield, aircraft and freight and specified terminal activities information is consistent with the current disclosure requirements.

Proposed Disclosures	Scope of Disclosures	Comparison to Current Disclosure Requirements <sup>165</sup>
Publication, Retention, Certification	Director certification and audit requirements for Annual Disclosures. Director certification requirements for AMPs. Statutory declaration requirements for all disclosures.	The proposed Director certification and audit requirements are similar to the current regulations. New statutory declaration requirements.

- 821 The remainder of this section outlines the information required for disclosure under the Airport Authorities (Airport Companies Information Disclosure) Regulations 1999 that in the Commission's preliminary view should not be required under the proposed new disclosure regime. The Airport Authorities (Airport Companies Information Disclosure) Regulations 1999 require disclosing entities to prepare financial information in compliance with GAAP. As noted in paragraphs 220, the Commission's preliminary view is that some GAAP disclosure may not be appropriate or necessary for regulatory reporting purposes.
- 822 Paragraphs 220 - 223 outline the Commission's preliminary views on why financing and financial instruments, cash flow and equity information should not be required for disclosure under Part 4. Derivatives and their fair value adjustments should not be required for the same reasons. Paragraphs 222 and 244 outline why working capital disclosures are not considered necessary.
- 823 It is proposed that WACC information also not be required in the Annual Disclosure. As outlined in paragraph B25 of Appendix B, regulated suppliers that are subject only to information disclosure do not have to apply methodologies for evaluating or determining the cost of capital, but the Commission may require regulated suppliers to disclose the methodology they have used (s 53F(2)(b)). Also, the Commission may use the input methodologies for evaluating or determining the cost of capital to monitor and analyse information as outlined in paragraphs B13 - B15 of Appendix B.
- 824 BARNZ, in its submission on the Provisions Paper suggested that the WACC used by airports should be disclosed.<sup>166</sup> It is the Commission's preliminary view that if the WACC is a material assumption in the pricing methodology then this should be disclosed as part of the pricing methodology.

Q.164) Do you agree that the above mentioned disclosures from the Airport Authorities (Airport Companies Information Disclosure) Regulations 1999 are not required for the purposes of information disclosure under Part 4? If not, please explain how they would assist with the purpose of information disclosure.

<sup>166</sup> Ibid.

**APPENDIX A: INDEX OF QUESTIONS**

Q.1)	In your view, should the Commission's next steps in making information disclosure determinations for the regulated services be as outlined above? Please provide the reasons for your views.	6
Q.2)	Do you agree that the term 'interested persons' is broad in its application and includes all persons that are interested in the activities of a regulated supplier? If not, please provide the reasons for your view, an alternative interpretation and why you consider this to be more appropriate.	11
Q.3)	Do you agree that pre-prescribed performance indicators will assist interested persons in the assessment as to whether the purpose of Part 4 is being met? If not, please provide the reasons for your view, an alternative approach and why you consider this to be more appropriate.	14
Q.4)	Do you agree that these principles are consistent with the purpose of information disclosure which is to ensure that sufficient information is readily available to interested persons to assess whether the purpose of Part 4 is being met? If not, please provide the reasons for your view, alternative principles and why you consider these are better aligned to the purpose of information disclosure.	18
Q.5)	What other areas of performance, if any, do you think the Commission should consider when assessing whether the purpose of Part 4 is being met? Please provide the reasons for your view.	23
Q.6)	Do you agree that an indicator relating to investment is required? If not, please provide the reasons for your view.	24
Q.7)	Do you believe that a capital expenditure ratio is an appropriate indicator? If not, please provide the reasons for your view, an alternative and explain why you consider this to be preferable.	24
Q.8)	Do you have any views on the Commission's proposed treatment of capital expenditure ratios under information disclosure? If so, please provide the reasons for your views.	25
Q.9)	Do you agree that the disclosure of an AMP is an appropriate means of demonstrating innovation and investment? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	26
Q.10)	Do you have any views on appropriate indicators for measuring innovation? If so, please provide the reasons for your views.	27
Q.11)	Do you have any views on appropriate indicators for measuring quality? If so, please provide the reasons for your views.	28
Q.12)	Do you have any views on appropriate indicators for measuring profits? If so, please provide the reasons for your views.	29
Q.13)	Do you have any views on appropriate indicators for measuring pricing efficiency? If so, please provide the reasons for your views.	30

Q.14)	Do you have any views on the appropriate cost based indicators to assess whether regulated suppliers have taken action to minimise costs? If so, please provide the reasons for your views.	30
Q.15)	Do you have any views on the Commission's proposed treatment of operational expenditure ratios under information disclosure? If so, please provide the reasons for your views.	32
Q.16)	Do you have any views on the Commission's proposed treatment of capacity utilisation ratios under information disclosure? If so, please provide the reasons for your views.	33
Q.17)	Do you agree that profitability should be measured using an ROI measure? If not, please detail the measure that is appropriate and explain how that measure would better meet the purpose of information disclosure?	36
Q.18)	Do you agree that revaluations and depreciation in the Regulatory Profit should be the same value as that which is used in rolling forward the RAB value? If not, please detail how depreciation and revaluations should be treated and how this treatment is consistent with the FCM concept.	38
Q.19)	Do you agree that the value of capital contributions and vested assets (net of any consideration) should be recognised as income in the ROI? If not, please explain how the value of the returns earned from vested assets and capital contributions should be treated and why you consider this to be preferable.	39
Q.20)	Do you agree that lost and found assets should not be treated as income and expense? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	39
Q.21)	Do you agree that a ROI comparable to a vanilla WACC and a post-tax WACC should be disclosed? If not, please provide the reasons for your view.	40
Q.22)	Do you agree that half the value of the net new capital investment should be reflected in the RIV value? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	42
Q.23)	Do you agree that assets acquired from or sold to another regulated supplier or business unit should be included in the RIV to the extent that the profit relating to those assets is recognised in the regulated supplier's regulatory profit? If not, please detail how asset acquired from or sold to another regulated supplier or business unit should be treated and why you consider this to be preferable.	42
Q.24)	Do you agree that it is appropriate to treat assets acquired from or sold to another regulated supplier that doesn't relate to merger or acquisition activity as above? If not, please explain how these should be treated and why you consider this to be preferable.	42
Q.25)	Do you agree that an adjustment to RIV for working capital is not necessary given its likely materiality? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	42

Q.26)	In your view, how should the capital costs associated with the use of regulated assets to provide regulated and unregulated services be attributed? Please provide the reasons for your view.	43
Q.27)	Do you agree that the Commission should consider GAAP as the starting point, but modify the disclosures where required to meet the purposes of information disclosure under the regulatory regime? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	50
Q.28)	Do you agree that where the sale of the asset is made to an unregulated entity or business unit, then the regulatory profit should be adjusted for gains or losses on sale? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	51
Q.29)	Do you agree that pass-through revenue and the associated distribution should be transparently disclosed in the regulatory profit statement? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	52
Q.30)	Do you agree that pass-through costs should be separately disclosed? If not please provide a detailed explanation as to why it shouldn't be separately disclosed.	52
Q.31)	Do you agree that insurance expenses should be included in the calculation of Regulatory Profit only where these are paid to an insurance entity? If not please, provide a detailed explanation as to why insurance should or shouldn't be disclosed, including a reference to the materiality of the insurance costs.	53
Q.32)	Do you agree that merger and acquisition expenses should be included in Regulatory Profit? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	53
Q.33)	Do you agree that financing information should not be required due to the difficulty in meaningfully allocating the portion that relates to the regulated business? If not, please provide details on how information on financing can be meaningfully allocated to regulated business units.	54
Q.34)	Are there any additional means for which an assessment of financial viability could be made? If so, in light of the regulatory provisions, please provide details of how the assessment can be made.	54
Q.35)	Do you agree that regulated suppliers should use the leverage assumption and cost of financing assumptions outlined in the cost of capital input methodology in preparing the deductible interest and interest tax shield calculation? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	54
Q.36)	Do you agree that disclosure of related party transactions should at least be consistent with GAAP and also include transactions between business units? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	56

Q.37)	Do you agree that transactions with related parties, including transfer pricing information, should be disclosed? If so, please provide details of how this information should be disclosed. If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	56
Q.38)	Do you agree that reconciliation between consolidated statutory reporting and regulatory reporting should be required for the purpose of monitoring compliance? If not, please provide that reasons for your view, an alternative to monitoring compliance and why you consider this to be preferable.	57
Q.39)	In your view, what form should the consolidation and reconciliation disclosures take? Please provide the reasons for your view.	57
Q.40)	Do you agree that financial information should be disclosed by way of a Regulatory Profit Statement, Regulatory Asset Statement, Regulatory Tax Calculation, Forecast Statement and Consolidation Statement? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	60
Q.41)	Do you agree that if the initial RAB value is established by updating a base valuation, then supporting disclosure of the methodology and assumptions will be required for transparency? If not, please provide the reasons for your view.	64
Q.42)	Do you agree that disclosures relating to the roll forward of the RAB should be sufficiently transparent so as to show the roll-forward calculation? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	65
Q.43)	Do you agree that the distinction between system fixed assets and non-system fixed assets under an indexed or un-indexed historic cost roll-forward approach is not required for the on-going purpose of information disclosure? If not, please provide the reasons for your view.	66
Q.44)	Do you agree that if shared asset costs were to be excluded from the RAB this should be done by way of an adjustment to the final RAB value, depreciation and revaluations? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	66
Q.45)	Do you agree that the treatment of leases consistent with GAAP is the appropriate approach under information disclosure? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	67
Q.46)	Do you agree that the level of prescription of information disclosed for assets acquired from or sold to another regulated supplier or business unit should be consistent with the information disclosed in the initial RAB and be sufficiently detailed to provide transparency? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	67
Q.47)	What do you consider to be the implications of the two approaches for recognising the cost of finance during construction, being either application	

	of an FDC allowance, or application of GAAP? Which approach do you prefer, and why?	69
Q.48)	Do you agree that RAB information should be disclosed by way of a Regulatory Valuation Roll-Forward Report, Annual Valuation Roll-Forward by Asset Class Report, Asset Transactions with Other Regulated Suppliers Report and Initial RAB Report? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	72
Q.49)	Do you agree that the requisite quality, quality targets and actual quality are appropriate measurements of quality for the purposes of information disclosure? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	77
Q.50)	Do you agree that requisite quality should be disclosed by suppliers of regulated services through the AMP so that they can choose the best way to establish and disclose the requisite level of quality? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	78
Q.51)	Do you agree that the Commission should assess the process by which suppliers engage with their consumers to assess requisite quality, how target quality has been determined based on requisite quality information and how the supplier has performed against target quality? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	79
Q.52)	Do you agree that suppliers of regulated services should be required to engage with their consumers and disclose how they engage or plan to engage with consumers, what service offers or commitments they make to consumers, how they make decisions about requisite quality standards, what types of contractual or other arrangements, if any, they enter into in relation to quality and how they plan to deliver requisite quality in terms of medium-term service delivery? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	79
Q.53)	Do you agree that quality information should be audited? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	80
Q.54)	Do you agree that the aspects of quality most relevant to suppliers of regulated services should include reliability, supply quality-other and customer service? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	84
Q.55)	Do you agree that statistics information should include asset information, demand and capacity information? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	86
Q.56)	Do you agree that suppliers of regulated services should apply a recognised AMP standard? If so, what is the appropriate standard that should be applied? Please provide the reasons why you consider it to be preferable?	91

Q.57)	Do you agree that AMPs should cover at least a ten-year forecast period? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	92
Q.58)	Do you agree that the AMPs should be certified by Directors that they are compliant with the requirements and that the AMP describes actual process and practices implemented by the business? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	92
Q.59)	Do you agree that the Commission should review investment and innovation, quality and energy efficiency, demand side management and loss reductions as part of the AMP review process for Electricity Distribution Lines Businesses? If not, please provide a reason for your view, an alternative and why you consider this to be preferable.	94
Q.60)	Do you agree that an AMP should include details of the background and overall approach to, and objectives of, a regulated supplier's asset management and planning processes? If not, please provide reasons for your view.	96
Q.61)	Do you agree that an AMP should include details of the assets covered by the plan? If not, please provide reasons for your view.	96
Q.62)	Do you agree that an AMP should include details of the regulated suppliers' plans for asset growth and their methods for reaching asset - related growth decisions? If not, please provide reasons for your view.	98
Q.63)	Do you agree that an AMP should include details of the regulated suppliers' plans for maintenance and renewal of assets over the planning period? If not, please provide reasons for your view.	99
Q.64)	Do you agree that an AMP should include details of risk policies, assessment, analysis and mitigation methods, and details of emergency response and contingency plans? If not, please provide the reasons for your view.	99
Q.65)	Do you agree that an AMP should include a regulated supplier's assessment of its performance against its own financial and service level targets as they relate to asset management planning? If not, please provide the reasons for your view.	101
Q.66)	Do you agree that all regulated suppliers should disclose and publish their pricing methodologies? Please provide the reasons for your view.	107
Q.67)	Do you agree that regulated suppliers should disclose prices? If not, please provide the reasons for your view.	107
Q.68)	Do you agree that regulated suppliers should be required to disclose the terms and conditions of supply and that the scope of disclosures should be limited to terms and conditions for the supply of regulated services? If not, please provide the reasons for your view.	108
Q.69)	Do you agree that that disclosure of policies will assist in achieving the stated purposes? If not, why not, and what information do you suggest would provide meaningful information?	109



Q.70)	Do you agree that publicly disclose should require a notice in the Gazette of that disclosure? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	114
Q.71)	Do you agree that the Annual, AMP and pricing methodology disclosures should be publicly disclosed? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	114
Q.72)	Do you agree that prices disclosures should also be notified to each consumer by whom the charge is payable? If not, please provide the reasons for your view.	114
Q.73)	Do you agree that templates should be used where appropriate and that disclosures should be made available to the Commission in Excel format with relevant formulae in place? If not, please provide the reasons for your view.	114
Q.74)	Do you agree with the proposed timing for disclosures? If not, please provide the reasons for your view.	115
Q.75)	Do you agree with the proposed regulatory year end dates? If not, please provide the reasons for your view.	115
Q.76)	Do you agree that regulated suppliers should continue to disclose information and retain disclosed information and information supporting the disclosed information for a period of at least seven years? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	116
Q.77)	Do you agree that Director certification should be required for the Annual, AMP and pricing methodology disclosures to certify that the information being disclosed complies with the relevant requirements? If not, please provide the reasons for your view.	117
Q.78)	Do you agree that audit reports should be required for Annual Disclosures? If not, please provide the reasons for your view, an alternative to obtaining independent assurance and why you consider this to be preferable.	119
Q.79)	Do you agree that audit reports should not be required for AMP, pricing methodology, prices or contract disclosures? If not, please provide the reasons for your view.	119
Q.80)	Do you agree that the form of audit reports should be flexible enough to allow for any changes in the New Zealand Auditing Standards without requiring an amendment to the requirements? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	119
Q.81)	Do you agree that audit reports should include a statement as to whether the disclosures comply with the requirements and include explanations of any material non-compliance? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	119

Q.82)	Do you consider it appropriate for there to be different assurance requirements for different types of information and what do you think they should be? Please provide the reasons for your view.	120
Q.83)	Do you agree that audit reports should be addressed to interested persons and contain a statement that acknowledges the auditor's duty of care to the Commission? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	120
Q.84)	What do you consider to be an appropriate level of independence for auditors? Please provide the reasons for your view.	120
Q.85)	Do you agree a statutory declaration should be attached to all information made available to the Commission under any disclosure requirement? If not, please provide the reasons for your view.	120
Q.86)	Are there any additional characteristics of EDBs that would affect how the information disclosure regime for EDBs should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.	126
Q.87)	Do you agree that the performance indicators outlined in Table 16 are sufficient for the purpose of information disclosure under Part 4 for electricity distribution lines services? If not, please provide detailed examples of what performance indicators would better serve the purpose of information disclosure for electricity distribution lines services.	128
Q.88)	What do you consider to be the appropriate method for calculating the customer perception performance indicator? Please provide the reasons for your view.	128
Q.89)	Do you agree that, for the purposes of determining regulatory income, the discretionary rebates, discounts and line holidays should be treated as being equivalent to dividends? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	129
Q.90)	Do you agree that separate disclosure of quality and statistics for each of the non-contiguous networks controlled by an EDB should be required? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	129
Q.91)	Do you agree that transmission revenue received from another EDB and AC Loss Rental rebates received and passed on should be separately disclosed? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	130
Q.92)	Are there any additional operating expenditure categories that would assist in meeting the purpose of information disclosure for electricity distribution lines services? If so, please provide details of how the proposed operating expenditure categories would assist the purpose of information disclosure.	131
Q.93)	Are there any additional capital expenditure categories that would assist in meeting the purpose of information disclosure for electricity distribution	

	lines services? If so, please provide details of how the proposed capital expenditure categories would assist the purpose of information disclosure.	132
Q.94)	Are there any additional asset categories that would assist in meeting the purpose of information disclosure for electricity distribution lines businesses? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.	133
Q.95)	Do you agree that relevant statistical information for electricity distribution lines services should include asset information, demand, and pricing statistics? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	134
Q.96)	Do you agree that pricing statistics, as currently required, should continue to be disclosed? If not please provide the reasons for your view, an alternative means for making comparisons between regulated suppliers on price and why you consider this to be preferable.	134
Q.97)	Do you agree that the key aspects of service quality for electricity distribution lines services should include reliability, supply quality and customer service? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	136
Q.98)	Do you agree that reliability for electricity distribution lines services should include the disclosure of planned and unplanned interruptions, the causes of interruptions and SAIDI, SAIFI and CAIDI measures? If not, please provide the reasons for your view, alternatives and why you consider these to be better aligned to the purpose of information disclosure.	136
Q.99)	In your view, what measures of supply quality – other (technical quality), if any, should be measured for electricity distribution lines businesses? Please provide the reasons for your view and why you consider these to be important.	136
Q.100)	In your view how should customer service quality be measured for electricity distribution lines services? Please provide the reasons for your view.	136
Q.101)	Do you agree that the Commission’s AMP review should include a review of the initiatives for energy efficiency, demand-side management and loss reduction that the supplier has included in their disclosed AMP? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	136
Q.102)	Do you agree that EDBs exempt from default/customised price-quality regulation provide to the Commission on an annual basis a statutory declaration demonstrating that the consumer-owned criteria in section 54D of the Act has been met? If not, please provide details of how exempt EDBs should prove to the Commission that they are exempt and therefore not subject to default/customised price-quality regulation.	137

Q.103)	In your view, are there any current information disclosure requirements that should not be carried forward? If so, please provide the reasons for your view.	140
Q.104)	Are there any additional characteristics of Transpower that would affect how the information disclosure regime for Transpower should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.	146
Q.105)	Do you agree that the performance indicators outlined in Table 18 are sufficient for the purpose of information disclosure under Part 4 for Transpower? If not, please provide detailed examples of what performance indicators in your view would better serve the purpose of information disclosure for Transpower.	147
Q.106)	What, if any, do you consider to be the appropriate performance indicator to demonstrate relevant performance efficiencies in supplying HVDC and HVAC, and South Island and North Island customers? Please provide the reasons for your view.	147
Q.107)	Do you agree that Transpower should be required to disclose movements in the EV account and that Regulatory Profit should be adjusted for surplus or shortfall transfers from the EV account? If not, please provide reasons for your view, an alternative and why you consider this to be preferable.	148
Q.108)	In your view, what operating expenditure categories should be disclosed by Transpower? Please provide the reasons for your view in light of the operational expenditure ratios identified above.	148
Q.109)	In your view, what capital expenditure categories should be disclosed for Transpower? Please provide the reasons for your view in light of the capital expenditure ratios identified above.	148
Q.110)	Do you agree that disclosure of capital expenditure for Transpower should specify which regulatory body, if any, provided approval? If not, please provide the reasons for your view.	149
Q.111)	Are there any additional asset categories that would assist in meeting the purpose of information disclosure for Transpower? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.	149
Q.112)	In your view, what statistical information should be disclosed for Transpower? Please provide the reasons for your view.	150
Q.113)	Do you agree that capacity utilisation for Transpower should be measured on the basis of the non-coincident peak demand at both the grid injection point and the grid exit point for the South Island, North Island and the HVDC link? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	150
Q.114)	In your view, are there other Transpower specific quality performance indicators that should be considered? If so, please provide the reasons for your view.	151

Q.115)	In your view, what should the summarised performance indicators of quality for Transpower be? Please provide details of your view, including how they are aligned to the purpose of information disclosure and how they will be calculated.	151
Q.116)	Do you agree that there should be separate disclosure of transmission services, system operator services and new investment contracts financial information? If not, please provide reasons for your view, an alternative and why you consider this to be preferable.	152
Q.117)	Do you agree that there should be separate disclosure of the HVDC and HVAC quality and statistics information? If not, please provide reasons for your view.	152
Q.118)	Do you agree that Transpower should be excluded from specific pricing methodology and AMP disclosure requirements under the Part 4 other than to disclose that which is already disclosed to the Electricity Commission? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	152
Q.119)	Do you agree that the above mentioned disclosures from the Electricity Information Disclosure Requirements 2004 are not required for the purposes of information disclosure for Transpower under Part 4? If not, please explain how they would assist with the purpose of information disclosure.	156
Q.120)	Are there any additional characteristics of gas pipeline services that would affect how the information disclosure regime for gas pipeline businesses should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.	159
Q.121)	Do you agree that the performance indicators outlined in Table 20 are sufficient for the purpose of information disclosure under Part 4 for gas pipeline services? If not, please provide detailed examples of what performance indicators would better serve the purpose of information disclosure for gas pipeline services.	160
Q.122)	What do you consider to be the appropriate method for calculating the relative unit price index? Please provide reasons for your view.	160
Q.123)	Are there any additional operating expenditure categories that would assist in meeting the purpose of information disclosure for gas pipeline businesses? If so, please provide details of how the proposed operating expenditure categories would assist the purpose of information disclosure.	162
Q.124)	Are there any additional capital expenditure categories that would assist in meeting the purpose of information disclosure for gas pipeline businesses? If so, please provide details of how the proposed capital expenditure categories would assist the purpose of information disclosure.	163

Q.125)	Are there any additional asset categories that would assist in meeting the purpose of information disclosure for gas pipeline services? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.	163
Q.126)	Do you agree that relevant statistical information for gas pipeline services should include asset information, demand, energy delivery efficiency and pricing statistics? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	166
Q.127)	Do you agree that the maximum demand and maximum non-coincident peak demand should be measured? If not, please provide details of how capacity utilisation should be measured and the reasons for your view.	166
Q.128)	Do you agree that suppliers of gas pipeline services should be required to disclose pricing statistics for consumers grouped by size, as currently required in the EDB information disclosure requirements? If not, please provide the reasons for your view, an alternative to assessing pricing efficiency and why you consider this to be preferable.	166
Q.129)	Do you agree that the key aspects of service quality for gas pipeline services should include reliability, supply quality and customer service? If not, please provide details of the aspects of quality that are relevant and the reasons for your view.	166
Q.130)	Do you agree that reliability for gas pipeline services should include the disclosure of planned and unplanned interruptions, the causes of interruptions, third party damage events, leaks, public reported escapes and SAIDI, SAIFI and CAIDI measures? If not, please provide the reasons for your view, alternatives and why you consider these to be better aligned to the purpose of information disclosure.	168
Q.131)	What measures do you think might be appropriate for the measurement of supply quality (other than reliability) for gas pipeline services? Please provide your reasons.	168
Q.132)	What do you believe is the appropriate means of measuring service quality for gas pipeline businesses? Please provide the reasons for your view.	169
Q.133)	Do you agree that disclosure of separate statistics and quality information for non-contiguous networks is appropriate information for the assessment of performance? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	169
Q.134)	In your view, what thresholds or criteria should the Commission use as a means of excluding networks from the requirement to separately disclose quality and statistics information? Please provide the reasons for your view.	169
Q.135)	Do you agree that the above mentioned disclosures from the GIDRs are not required for the purposes of information disclosure under Part 4? If not, please explain how they would assist with the purpose of information disclosure.	174

Q.136)	In your view, should the detailed network capacity information currently required to be disclosed through the GIDRs continue to be required under the new information disclosure requirements? Please provide the reasons for your view.	174
Q.137)	Are there any additional characteristics of specified airport services that would affect how the information disclosure regime for specified airport services should be applied? If so, please give examples of how components of the information disclosure regime should be customised in light of the characteristics identified.	179
Q.138)	Do you agree that the performance indicators outlined in Table 23 are sufficient for the purpose of information disclosure under Part 4 for specified airport services? If not, please provide detailed examples of what performance indicators would better serve the purpose of information disclosure for specified airport services and the reasons for your view.	181
Q.139)	What do you consider to be the appropriate denominator for the capital expenditure growth ratio? Please provide the reasons for your view.	181
Q.140)	What do you consider to be the appropriate denominator in the average price per unit performance indicator? Please provide the reasons for your view.	181
Q.141)	What do you consider to be the appropriate calculation for the capacity utilisation performance indicator? Please provide the reasons for your view.	181
Q.142)	What do you consider to be the appropriate method for calculating a customer perception performance indicator? Please provide reasons for your view.	181
Q.143)	Do you agree that specified airport service suppliers should disclose the level of revenue they are earning from property rent and lease income and that this, along with disclosure of the extent to which downstream services are provided by the airport company or its contracted suppliers, will be sufficient for interested persons to understand the affects of the different business activities on the performance of the regulated business unit? If not, please provide examples of disclosures that will allow interested persons to gain this understanding.	181
Q.144)	Are there any additional operating expenditure categories that would assist in meeting the purpose of information disclosure for specified airport services? If so, please provide details of how the proposed operating expenditure categories would assist the purpose of information disclosure.	183
Q.145)	Are there any additional capital expenditure categories that would assist in meeting the purpose of information disclosure for specified airport services? If so, please provide details of how the proposed capital expenditure categories would assist the purpose of information disclosure.	184

Q.146)	Are there any additional asset categories that would assist in meeting the purpose of information disclosure? If so, please provide details of how the proposed asset categories would assist the purpose of information disclosure.	184
Q.147)	Do you agree that if a cost of capital input methodology has not been established for specified airport services that the Commission should issue the required financing assumptions for use in information disclosure? If not, please provide the reasons for your view, an alternative and why you consider this to be preferable.	185
Q.148)	Do you agree that the key aspects of quality for specified airport services should include customer service, reliability and capacity/utilisation? If not, please provide the reasons for view, an alternative and why you consider this to be preferable.	186
Q.149)	Do you agree that there will need to be a balance between having complex and potentially costly quality indicators versus more simplistic quality indicators that may address the quality of both regulated and unregulated services? Please provide reasons for your view.	186
Q.150)	Do you agree that passenger perception surveys should be used to measure customer service and supply quality for specified airport services? If not, please provide the reasons for your view.	188
Q.151)	Do you agree that the ACI ASQ survey is an appropriate survey for collecting passenger perceptions for specified airport service? If not, please provide details of why the ACI ASQ survey is not appropriate and details of why an alternative survey would be more appropriate.	188
Q.152)	Do you agree that the identified measures are appropriate for measuring passenger perceptions of quality? Are there any additional measures that would assist in the measurement of quality for specified airport services through passenger perceptions? If so, please provide the reasons for your view.	188
Q.153)	Do you agree that reliability of services should be disclosed and that the disclosures should be enhanced to identify the cause of the disclosure? If not, please provide the reasons for your view.	188
Q.154)	Are there any additional services that should require disclosure of interruption information? If so, please provide of the reasons why the additional categories are important to the purpose of information disclosure.	188
Q.155)	Do you see the disclosure of the effect of interruptions on consumers as an important measure of quality for specified airport services? If so, please provide details of how this could be measured and the reasons for your view.	189
Q.156)	Do you agree that capacity and utilisation of capacity is a key supply quality issue for specified airport services? Please provide the reasons for your view.	190



Q.157)	Do you agree that capacity and utilisation should be measured at the above points? If not, please provide details of where capacity and utilisation should or should not be measured and the reasons for your view.	190
Q.158)	Do you agree that it may not be appropriate to measure capacity by comparing peak demand and service capacity and that it may be more appropriate to consider the duration of capacity constraint or near-full constraint? If not, please provide the reasons for your view.	190
Q.159)	Do you agree that a description of the assets and their capacity should be disclosed? If not, please provide the reasons for your view.	191
Q.160)	Do you agree that demand disclosures for specified airport services should include disclosure of international and domestic volumes for passenger, freight and aircraft movements? If not, please provide details of what should or should not be disclosed and the reasons for your view.	191
Q.161)	Do you agree that pricing statistics disclosures for specified airport services should compare total revenue to units handled? If not, please provide the reasons for your view.	191
Q.162)	Do you agree that pricing statistics for specified airport services should not assess prices at a consumer level? Please provide the reasons for your view.	191
Q.163)	Do you agree that separate disclosure of segmented aircraft and freight activities, airfield activities and specified terminal activities are important to assess regulated supplier performance for specified airport services? Please provide the reasons for your view.	192
Q.164)	Do you agree that the above mentioned disclosures from the Airport Authorities (Airport Companies Information Disclosure) Regulations 1999 are not required for the purposes of information disclosure under Part 4? If not, please explain how they would assist with the purpose of information disclosure.	196

## APPENDIX B: STATUTORY PROVISIONS

### INTRODUCTION

B1 This appendix outlines the information disclosure provisions of the Commerce Act 1986 (Act). The first part of the appendix discusses the provisions that are common to all services that are subject to information disclosure regulation. The second part discusses the provisions that apply to particular types of regulated services.

### PROVISIONS COMMON TO ALL REGULATED SERVICES

#### *Information Disclosure Determinations*

- B2 Under the Act, the Commission must make s 52P determinations specifying how information disclosure regulation applies to suppliers of regulated services, in accordance with sections 54I (for electricity lines services), 55E (for gas pipeline services), and 56E (for specified airport services).
- B3 Section 52P(4) provides that it is not necessary for a single determination to address all matters relating to particular regulated goods and services and different parts of any determination may come into effect at different times.
- B4 Under s 52P(7), as soon as practicable after making a determination, the Commission must give a copy of the determination to each supplier to whom the determination relates, publish a summary in the Gazette, and make the whole determination publicly available.
- B5 Section 53C(1) provides that information disclosure determinations must specify the services and the suppliers to which they apply; the information to be disclosed; the manner in which information is to be disclosed; when, and for how long information must be disclosed; the input methodologies that apply; and any other methodologies that apply.
- B6 Under s 53C(2), the information required to be disclosed may include financial statements (including projected financial statements); asset values and valuation reports; prices, terms and conditions relating to prices, and pricing methodologies; contracts; transactions with related parties; financial and non-financial performance measures; plans and forecasts, including (without limitation) plans and forecasts about demand, investments, prices, revenues, quality and service levels, capacity and spare capacity, and efficiency improvements; asset management plans; quality performance measures and statistics; assumptions, policies, and methodologies used or applied in these or other areas; and consolidated information that includes information about unregulated goods or services.
- B7 Section 53C(3) allows for further specifications to be made in a determination, including requiring verification of disclosed information, transitional provisions and possible exemptions from information disclosure requirements.
- B8 Section 53C(4) provides that a determination may not require a supplier to publicly disclose any provision of an existing contract that, immediately before the services became subject to information disclosure regulation, was not required by or under

Part 4A or any other enactment to be publicly disclosed.

B9 Part 4 of the Act sets out regulatory provisions relating to consolidated information. Section 53D states:

- (1) The purpose of this section is to enable the Commission to monitor compliance with information disclosure regulation applying to regulated goods or services.
- (2) A section 52P determination may require information referred to in subsection (3) to be disclosed only to the extent required to enable the purpose in subsection (1) to be met.
- (3) If a regulated supplier provides goods or services that are not subject to regulation under this Part (unregulated goods or services), the supplier may be required to disclose
  - (a) consolidated financial statements, and any other information referred to in section 53C, for all businesses (including those related to the supply or unregulated goods or services) undertaken by that supplier; and
  - (b) consolidated financial statements, and any other information referred to in section 53C, for the supply of all unregulated goods or services in aggregate; and
  - (c) reconciliation between information provided under paragraphs (a) and (b) with information disclosed in accordance with information disclosure requirements applying to the regulated goods or services.
- (4) If a supplier supplies more than 1 kind of regulated goods or services, the Commission may require the supplier to provide consolidated information and performance measures relating to all, or any combination of, the regulated goods or services.

### ***Input Methodologies***

B10 Section 52U provides that the Commission must determine input methodologies for the services regulated under subparts 9 to 11 of Part 4 no later than 30 June 2010. This deadline may be extended by the Minister by up to 6 months.

B11 Given that s 53C(1)(g) requires information disclosure determinations to “specify the input methodologies that apply”, the Commission intends to make new information disclosure determinations after the applicable input methodologies have been determined.

B12 Under s 53F, if information disclosure regulation is the only type of regulation that applies (as is the case for suppliers of specified airport services and suppliers of electricity lines services that are consumer-owned):

- suppliers do not have to apply input methodologies in respect of pricing methodologies or methodologies for evaluating or determining the cost of capital; however,

- the Commission may still use these input methodologies to monitor and analyse information, and may require suppliers to disclose information about the pricing and cost of capital methodologies that they do in fact use.

### *Summary and Analysis*

- B13 Section 53B(2) sets out the Commission's powers and obligations for monitoring and analysing disclosed information. The Commission may monitor and analyse disclosed information. It must publish a summary and analysis of disclosed information as soon as practicable after it is publicly disclosed.
- B14 As explained in further detail below, the Act provides that existing information disclosure regulations continue to apply until the Commission makes new information disclosure determinations under Part 4. The Commission is not obliged to publish a summary and analysis of information disclosed under regulation set under other Acts that remains in force during the transition to the new regime.
- B15 For electricity lines services, the Commission will continue to publish a summary and analysis of disclosures as it was required to do under the previous regime. For gas pipeline services, the Commission is not required to publish a summary and analysis until it receives disclosures pursuant to a determination under the Act (refer paragraph B37). For specified airport services, the Commission may (but is not required to) monitor and analyse information disclosed under the existing airports regulations (refer paragraph B45).

## **PROVISIONS THAT APPLY TO PARTICULAR REGULATED SERVICES**

### *Electricity Lines Services*

- B16 Section 54F provides that all electricity lines services (as defined in the Act) are subject to information disclosure regulation.
- B17 Part 4 of the Act sets out regulatory provisions relating to electricity lines services in subpart 9. Section 54C(1) provides that:
- (1) In this subpart, unless the context otherwise requires, electricity lines services means the conveyance of electricity by line in New Zealand.
- B18 A number of exclusions are provided for in subsection 2.

However, none of the following are electricity lines services:

- (a) conveying electricity solely for the supplier's own consumption or for the consumption of the supplier's associates:
- (b) conveying electricity only from a generator to the national grid or from the national grid to a generator:
- (c) conveying electricity (other than via the national grid) only from a generator to a local distribution network or from a local distribution network to a generator:
- (d) conveying electricity by lines that are not connected, directly or indirectly, to the national grid:

- (e) conveying electricity only by a line or lines that are mostly in competition with a line or lines operated by another supplier of electricity lines services that is not an associate of the person, provided that the competition is actual competition and not potential competition:
  - (f) conveying electricity if the total circuit length of all of the prescribed voltage electric lines provided by the supplier (or over which electricity is conveyed by the supplier, as the case may be) is less than 25 kilometres:
  - (g) conveying electricity if the total amount of electricity conveyed to consumers by the supplier is less than 20 gigawatt hours per annum:
  - (h) conveying electricity if the total number of consumers to whom the supplier conveys electricity is less than 500.
- B19 Under s 54M, Transpower remains subject to an administrative settlement with the Commission until June 2011. This is in addition to being subject to information disclosure regulation.
- B20 Section 54G provides for certain electricity lines services to also be subject to default/customised price-quality regulation (other than Transpower) unless they are a supplier that is exempt because the supplier is consumer-owned as defined in s 54D.
- B21 Under s 54I, the Commission must make a s 52P determination setting out how information disclosure regulation applies to each supplier of electricity lines services “as soon as practicable” after 1 April 2009.
- B22 As noted above, given that s 53C(1)(g) requires such determinations to “specify the input methodologies that apply”, the Commission intends to set new information disclosure requirements after the applicable input methodologies have been determined.
- B23 Section 54Q requires the Commission to promote incentives, and avoid imposing disincentives, for suppliers of electricity lines services to invest in energy efficiency and demand side management, and to reduce energy losses, when applying Part 4 of the Act in relation to electricity lines services.
- B24 Section 54V outlines the respective obligations of the Electricity Commission and the Commerce Commission in performing their obligations under the Electricity Act 1992 and the Commerce Act 1986 respectively as they impact upon Part 4.
- B25 Consumer-owned suppliers are subject only to information disclosure regulation. Section 53F provides that suppliers that are subject only to information disclosure regulation need not apply any input methodologies that relate to pricing methodologies, or methodologies for evaluating or determining the cost of capital.
- B26 Notwithstanding this limited exception to the obligation to apply input methodologies, the Commission may use those input methodologies to monitor and analyse information, and consumer-owned suppliers may still be required to disclose information about the pricing methodologies or methodologies for evaluating and determining the cost of capital that they do use (s 53F(2)).

B27 In contrast, as non-consumer-owned suppliers are also subject to default/customised price-quality regulation, there is no exception available to them in relation to the obligation to apply any input methodologies that relate to information disclosure requirements for pricing methodologies, or methodologies for evaluating or determining the cost of capital.

B28 Any information disclosure requirements that are determined by the Commission under Part 4A of the Act (prior to its repeal on 1 April 2009) continue to apply until such time as the Commission makes new requirements under the new legislative provisions.<sup>167</sup> Section 54W provides that:

*Any information disclosure requirements published by the Commission under subpart 3 of Part 4A before 1 April 2009 continue to apply to each supplier of electricity lines services in respect of every financial year that precedes the first financial year to which a determination made by the Commission under section 54I(1) applies to that supplier.*

B29 The information disclosure requirements currently applicable to suppliers of electricity lines services consist of:

- Electricity Distribution (Information Disclosure) Requirements 2008;
- Electricity Information Disclosure Requirements 2004 (consolidating all amendments to 31 October 2008);
- Electricity Information Disclosure Handbook; and
- Handbook for Optimised Deprival Valuation of System Fixed Assets.

B30 The Commission's obligations with respect to summary and analysis for suppliers of electricity lines services under Part 4 are included in s 53B(2) as outlined above. The Commission's previous summary and analysis obligations under s 57T of Part 4A were similar to those under the new Part 4. Therefore, the Commission's obligations with regard to summary and analysis for electricity lines businesses will continue during the period prior to a determination being made.

### ***Gas Pipeline Services***

B31 Section 55C provides that gas pipeline services (as defined in the Act) are subject to information disclosure regulation.

B32 Subpart 10 sets out regulatory provisions relating to gas pipeline services.<sup>168</sup> The meaning of 'gas pipeline services' is defined in s 55A(1), as:

In this subpart, unless the context otherwise requires, gas pipeline services means the conveyance of natural gas by pipeline, including the assumption of responsibility for losses of natural gas.

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<sup>167</sup> Note that the Commission has recently set new *Electricity Information Disclosure Amendment Requirements (No. 3) 2008* and *Electricity Distribution (Information Disclosure) Requirements 2008* (available on the Commission's website: [www.comcom.govt.nz](http://www.comcom.govt.nz)).

<sup>168</sup> Subpart 10 of Part 4 came into force on 14 October 2008.

B33 Section 55A(2) provides a number of exemptions from regulation under this subpart:

However, none of the following are gas pipeline services:

- (a) conveying natural gas to a gas processing facility:
- (b) conveying natural gas if the total amount of gas conveyed to consumers by the supplier is less than 75 000 gigajoules per annum:
- (c) conveying natural gas by a pipeline that is listed in the second column of Schedule 6.

B34 Gas pipeline services are subject to information disclosure regulation (s55C) and default / customised price-quality regulation (s55D). Under s 55E, the Commission must make a determination setting out how information disclosure regulation applies to each supplier of gas pipeline services “as soon as practicable” after 14 October 2008.

B35 As noted above, given that s 53C(1)(g) requires such determinations to “specify the input methodologies that apply”, the Commission intends to set information disclosure requirements after the applicable input methodologies have been determined.

B36 The existing information disclosure requirements made under the Gas Act 1992 continue to apply until such time as the Commission determines new requirements under the Act. Section 55J provides that:

- (1) The Gas (Information Disclosure) Regulations 1997 continue to apply to each supplier of gas pipeline services in respect of every financial year that precedes the first financial year to which a determination made by the Commission referred to in section 55E(1) applies to that supplier.
- (2) After that, no regulations made under section 55 of the Gas Act 1992 apply to the supplier of gas pipeline services.

B37 The Commission is not required to publicly disclose a summary and analysis of information disclosed under the GIDRs, but will be required to do so under Part 4 once it issues an information disclosure determination for gas pipeline services.

### ***Specified Airport Services***

B38 Specified airport services are subject to information disclosure regulation under the Act (s 56C). No other form of regulation applies to suppliers of specified airport services under Part 4 of the Act.

B39 Section 56A defines specified airport services as all of the services supplied by Auckland International Airport, Wellington International Airport and Christchurch International Airport in markets directly related (whether for international and domestic flights) to aircraft and freight activities; airfield activities; specified passenger terminal activities; and any other services that are determined by the Governor-General, by Order in Council, to be specified airport services. The Input Methodologies Discussion Paper provides further detail of what each of the

activities mentioned above includes, with reference to the definitions contained in the Airport Authorities Act 1966.<sup>169</sup>

- B40 Section 56E provides that the Commission must make a determination setting out how information disclosure regulation applies to the airport companies no later than 1 July 2010 (or, if the deadline for determining input methodologies is extended under s 52U(2), no later than the day after the date to which that deadline is extended).
- B41 As noted above, given that s 53C(1)(g) requires such determinations to “specify the input methodologies that apply”, the Commission intends to set new information disclosure requirements after the applicable input methodologies have been determined.
- B42 However, as the statutory deadline for such a determination (1 July 2010) is one day after the statutory deadline for the determination of input methodologies (30 June 2010), consultation on the information disclosure determination for regulated airport services will necessarily take place in parallel with consultation on applicable input methodologies.
- B43 Given the need for a parallel process to determine input methodologies and information disclosure requirements, the Commission expects to align the consultation on draft determinations for input methodologies in February 2010 with the draft determinations for information disclosure for the regulated airports services.
- B44 Section 53F provides that suppliers that are subject only to information disclosure regulation need not apply any input methodologies that relate to pricing methodologies, or methodologies for evaluating or determining the cost of capital. Notwithstanding this limited exception to the obligation to apply input methodologies, the Commission may use those input methodologies to monitor and analyse information, and suppliers may still be required to disclose information about the pricing methodologies or methodologies for evaluating and determining the cost of capital that they do use (s 53F(2)).
- B45 The existing information disclosure requirements made under the Airport Authorities Act 1996 continue to apply until such time as the Commission determines new requirements under the Act. Suppliers of specified airport services are required to supply to the Commission a copy of any information disclosed and the Commission may monitor and analyse that information. Section 56F provides that:
- (1) The Airport Authorities (Airport Companies Information Disclosure) Regulations 1999 continue to apply to each supplier of specified airport services in respect of every financial year that precedes the first financial year to which a determination made by the Commission under section 56E applies

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<sup>169</sup> Supra n 2, paragraphs 3.26 - 3.31.



to that supplier.

- (2) After that, no regulations made under section 9A of the Airport Authorities Act 1996 apply to that supplier.
- (3) Each supplier of specified airport services must supply to the Commission a copy of any information disclosed under those regulations, as soon as practicable after so disclosing.
- (4) The Commission may monitor and analyse any information supplied to it under this section.

B46 The Commission must review the information disclosure requirements that are in place under the Act from 2010 as soon as practicable after suppliers set any new price for a specified airport service in 2012 (s 56G). This review must be carried out regardless of whether or not any new price for a specified airport service is actually set before 2012. The Commission must consult (without necessarily holding an inquiry) with interested parties and report to the Ministers of Commerce and Transport as to how effectively information disclosure regulation is promoting the purpose in s 52A in respect of the specified airport services.