



11 October 2016

John Findley
Regulatory Accountant
Transpower New Zealand Ltd
96 The Terrace
Wellington, 6140

Dear John

**Transpower New Zealand Ltd – exemption from requirements of clause 28.1 of the
Transpower IPP determination – asset health pilot reporting measures**

1. In an email dated 13 June 2016 - titled Asset Health pilot reporting measures - you requested that Transpower New Zealand Limited (Transpower) be granted an exemption from providing information set out in clause 28.1 of the Transpower Individual Price-Quality Path Determination 2015 (IPP).

Background to your request

2. Clause 28.1 of the IPP requires Transpower to report on the asset health grid output measures using average remaining life as the unit-of-measure. Under clause 19.1 of the IPP this information must be included in Transpower's annual compliance statement which must be provided to the Commission and published on Transpower's website by 21 October 2016. Your request arises because Transpower has decided to change its asset health models and 'remaining asset life' will not be the outputs of the new models. In addition, you mention that asset health reporting in RCP2 will not provide any benefits.
3. We disagree that pilot asset health reporting in RCP2 will not provide any benefits. As set out in the IPP Reasons paper, we asked for pilot reporting in RCP2 in order to have suitable asset health grid output measures for RCP3.¹ We wanted to ensure that asset health grid output measures could be implemented as part of the quality standards in RCP3. Our position on this has not changed. However, we recognise that there may be other methods of reporting on asset health grid output measures than using average remaining life as the unit-of-measure that will still achieve our purpose while imposing lower regulatory compliance costs on Transpower.

Exemption granted

4. We have considered your request and agree to grant an exemption from the requirements of clause 28.1 for the 2015/16 disclosure year.
5. This exemption is granted on the condition that Transpower proposes an alternative method of measuring asset health grid output measures by no later than 31 March 2017.

Our expectations

6. The alternative method proposed by 31 March 2017 will be the starting point for developing an appropriate asset health grid output measure (AHGOM) which can be implemented as a quality standard in RCP3. We expect Transpower to develop the alternative AHGOM by 31 July 2017 to the level suitable for inclusion in the IPP for compliance reporting in October 2017.
7. Once we are satisfied with the alternative AHGOM, we will initiate the process to amend the relevant information disclosure clauses of the IPP for Transpower to pilot report on asset health using the alternative method.
8. As mentioned above the objective of developing and pilot testing AHGOM in RCP2 is to have an appropriate revenue linked asset health grid output measure for RCP3.
9. If you have any questions regarding the matters addressed in this letter, please contact Alison Young on 04 9243823.

Yours sincerely

Elisabeth Welson
Commissioner



i Setting Transpower's individual price-quality path for 2015-2020, 29 August 2014, paragraphs 4.32 and 4.33.3.

Alison Young

From: Joshua Wilson <Joshua.Wilson@transpower.co.nz>
Sent: Wednesday, 28 June 2017 2:04 p.m.
To: Alison Young
Cc: Ross Parry; John Findlay
Subject: RE: Commerce Commission publication of granted exemptions from Transpower ID requirements [CCNZ-iManage.FID206267]

Hi Alison

Thanks for the opportunity to provide clarification regarding the exemption letter. Please see below the content we would like to be published along with the exemption letter. Please let me know if you have any questions.

Regards

Josh

Content to include alongside the exemption letter

On 2nd June 2017, the Commerce Commission informed us of their intention to publish its exemption letters to our information disclosure requirements under the current individual price-quality path. We support this opportunity to increase transparency and provide further information to interested persons.

We would like to clarify to readers our view on asset health reporting that is expressed in the exemption letter dated 11 October 2016. In the letter, the Commission states the following in response to our request for an exemption to report on the pilot asset health grid output measures:

Your request arises because Transpower has decided to change its asset health models and 'remaining asset life' will not be the outputs of the new models. In addition, you mention that asset health reporting in RCP2 will not provide any benefits.

We would like to clarify that we support the use of asset health for reporting purposes in *general* as well as the inclusion of asset health output measures within the incentive regime. Asset health reporting provides our stakeholders, including the regulator, with a view of the state of our assets and highlights potential work required to manage the condition of the grid.

Our concerns arose from the *specific* pilot measures that were included in clause 28.1 in the current IPP:

- A target based on average remaining life does not reflect how we model for asset health. We have developed our asset health framework during RCP2 which has led to more mature asset health models. These models express asset health as an index rather than as estimated remaining life. This is a more meaningful measure of the condition of our assets.
- We do not think the current asset health output target would be suitable to include in the incentive regime for RCP3. An incentive regime needs to avoid perverse outcomes. An incentive linked directly to average remaining life target would not be appropriate because asset health isn't the only factor in determining when to invest in an asset. A fixed target would also not account for developments in our asset health models which may change our view of the condition of the asset and thus the appropriate time to invest. At worst, an incentive regime could distort our analysis of asset health.

We have been engaging with the Commerce Commission on the development of alternative asset health output measures that we can report on for the remainder of RCP2. We intend that these measures will be used for the basis of revenue linked output measures in RCP3. These alternative measures better reflect how we use asset health information in our asset planning decisions, and are designed to minimise the risk of unintended consequences.