

Final decision

Customised price-quality paths for Wellington Electricity and Powerco

28 March 2018
Dr Stephen Gale



Headline results

Overall we are convinced both networks face challenges, and the investment plans put forward are prudent solutions in the long-term interests of consumers

Powerco

- \$1.27b of expenditure - 96% of what Powerco proposed
- Powerco can move forward with its plans to invest to address issues with safety and reliability; and capacity and supply security concerns

Wellington

- \$31.2m of resilience expenditure - 100% of what Wellington Electricity proposed
- Wellington can bring in spares and undertake strengthening work to improve its network's ability to withstand and respond to a major earthquake

Powerco's customised price-quality path



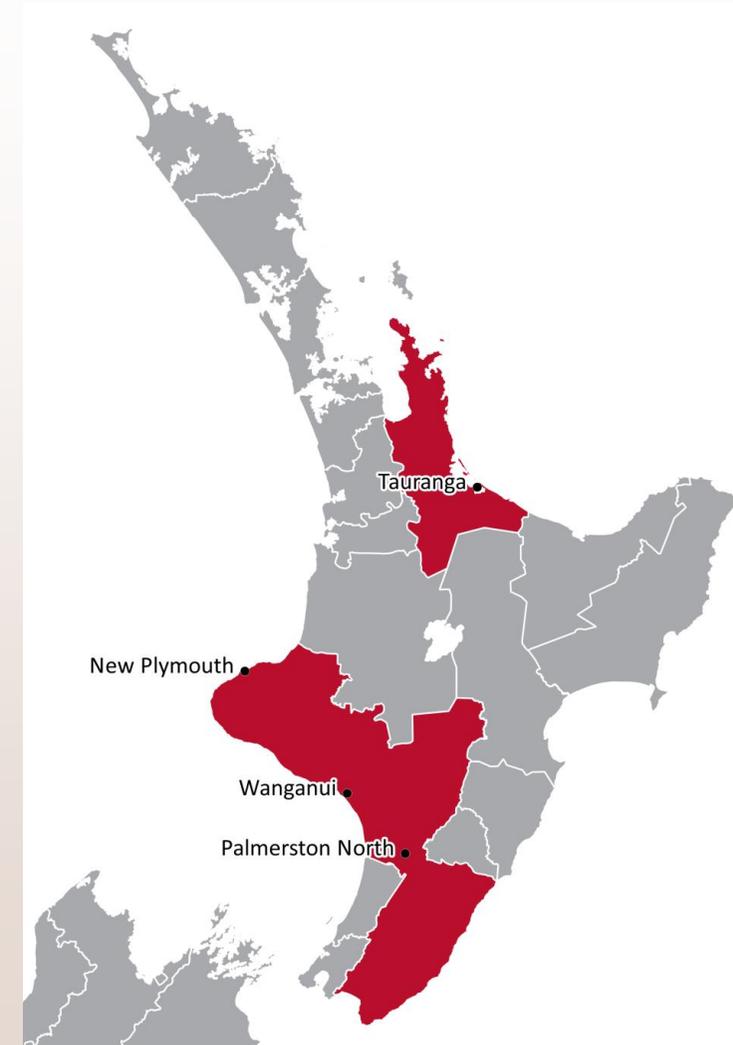
Overview

Context

- Powerco's proposal
- Our assessment process

Our decision

- Expenditure amounts & allowed revenues
- Quality standards
- Monitoring programme
- Feedback from submitters
- Consumer outcomes



Powerco's proposal

Applied for a customised price-quality path in June 2017

Proposal

- \$1.32 billion expenditure over next 5 years, about \$390m more than previous 5 years
- Argued uplift necessary to maintain current reliability levels and meet growing demand

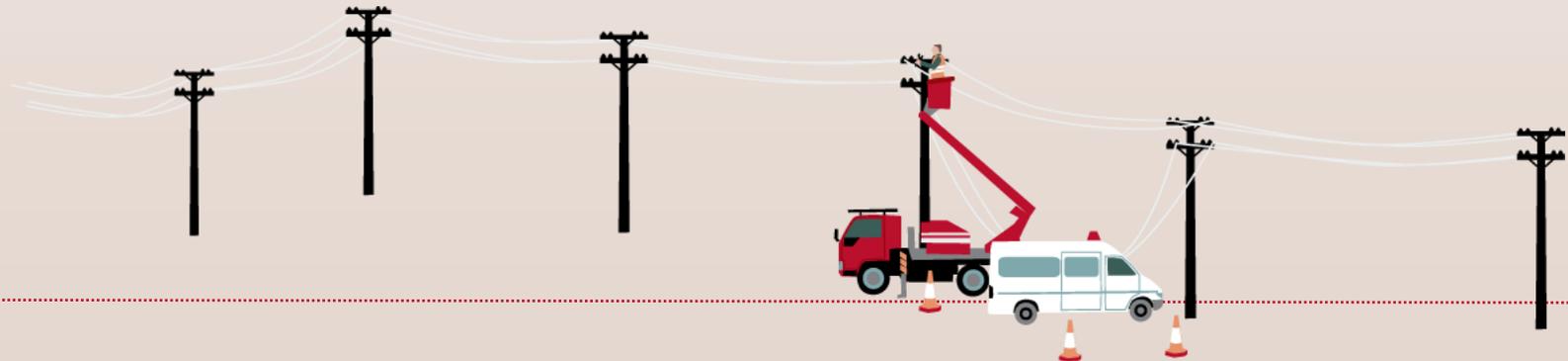
Impact (as estimated by Powerco)

- Initial 5.7% increase in revenues plus annual CPI adjustment
- Price increase of \$3-4 on a typical residential consumer's monthly bill

Assessment process

Powerco was required to consult with its consumers and have its proposal independently verified

- Consulted with consumers in early 2017 on a \$1.4b proposal
- Proposal then subjected to a robust review by independent Verifier (Farrier Swier Consulting)
- Powerco revised proposal to \$1.32b following initial feedback from Verifier
- Verifier concluded 91% of the proposed \$1.32b was reasonable



Our review

Ensures decision is in the long-term benefit of consumers

- Tested the findings of the Verifier including review by a second consultant (Strata Energy Consulting)
- Used Verifier's findings to target our review, proportionate to scale of investment/level of concern
- Sought further information from Powerco and conducted site visits across their network
- Used specialist engineering advice
- Sought views from interested parties in Issues Paper
- Released and sought views on draft decision in November 2017

Our decision

Satisfied investment needed now to deliver a safe and reliable network for the long-term benefit of consumers



Expenditure

Opex and capex included in the price path

- \$1.27 billion of expenditure over 5 years

	Powerco proposal	Our decision
Opex	\$455m	\$447m
Capex	\$873m	\$825m
Total expenditure	\$1.32b	\$1.27b

- Allows a slightly higher amount than the Verifier based on our subsequent review (96% v 91%)
- \$55 million rejected as not meeting the expenditure objective
- \$1.5 million more than the draft decision

Revenues

Annual maximum allowable revenue (MAR) that Powerco must comply with

- Initial 4.5% increase plus an annual adjustment for CPI



Quality standards

Annual reliability limits Powerco must comply with

Unplanned interruptions

- An improvement by the end of the CPP period (5% for SAIFI and 10% for SAIDI)
- Powerco had proposed using historical performance

Planned interruptions

- Annual limits based on Powerco's own forecasts, with a margin added for flexibility
- Five year limit to manage a year exceeding annual limit under 2 out of 3 compliance scheme
- Powerco had proposed no standard for planned outages

Reporting against delivery

Powerco is required to report on how it is tracking against its proposal to provide transparency around performance

- Publish an annual CPP Delivery Report
- Hold annual stakeholder events to explain its progress
- Attend annual technical meetings with Commission to discuss issues
- Key feature will be how Powerco improves its asset management practices over course of CPP



Feedback from submitters

Four key topic areas from submissions on our draft decision

- **Price-quality trade-off** – whether we should reduce expenditure and set reliability limits at current levels
- **Use of cost-benefit analysis** – whether we should use a cost-benefit analysis to underpin our decision
- **Consideration of alternative solutions** – whether Powerco has sufficiently considered non-traditional market based solutions
- **Network evolution expenditure** – whether the proposed network evolution initiatives sufficiently benefits consumers

Consumer outcomes

Network performance

- Safe, secure and reliable network which meets the long term needs of Powerco's consumers
- Improvement in frequency and duration of power outages
- Greater transparency on Powerco's performance

Cost

- We estimate an increase of about \$2.70 to the typical residential consumer's monthly bill of \$210
- Estimated additional increase of around \$6 in five years if investment forecasts eventuate

Questions



Wellington Electricity's customised price-quality path



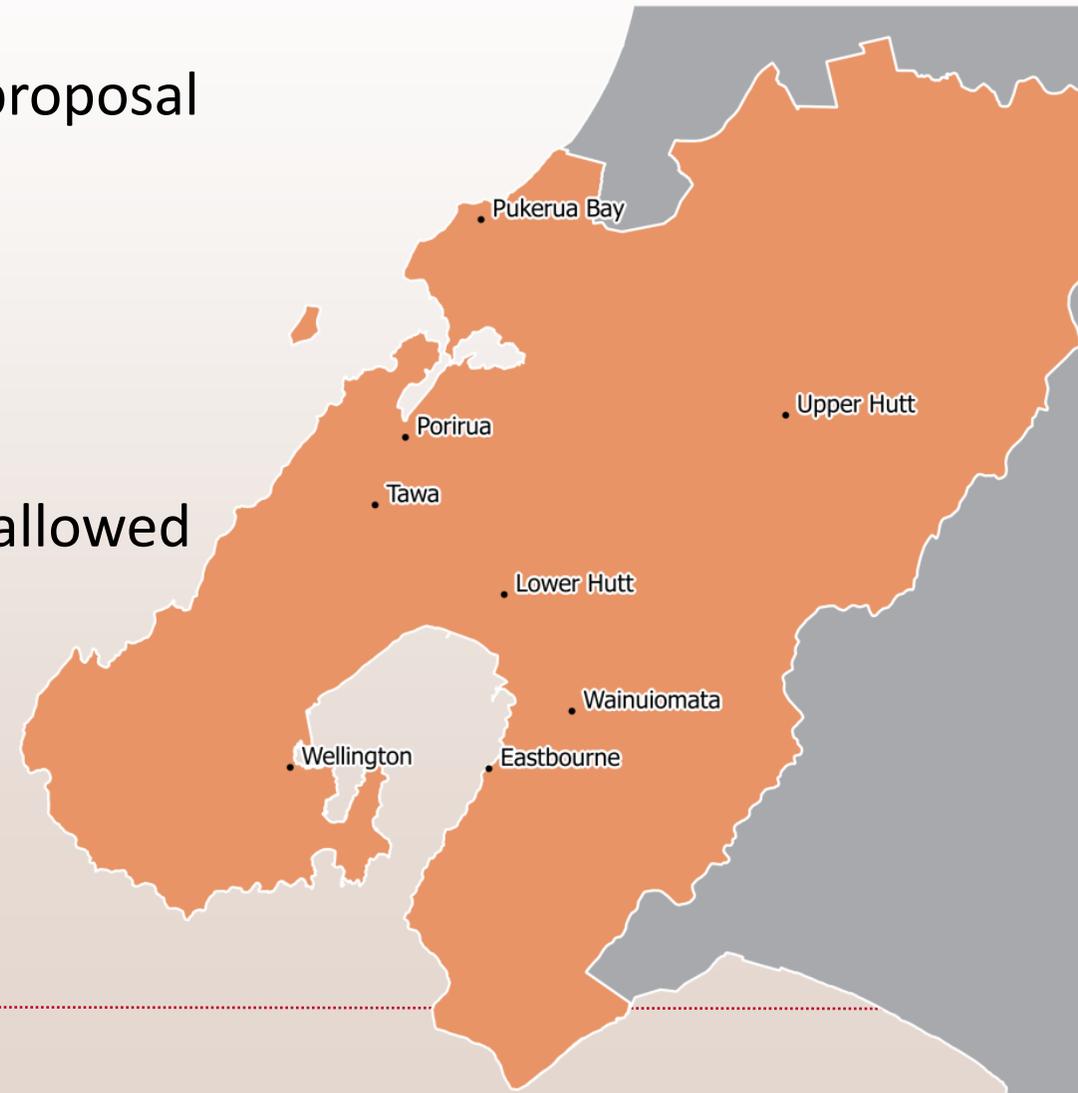
Overview

Context

- Wellington Electricity and its proposal
- Our assessment process

Our decision

- Final expenditure amounts & allowed revenues
- Quality standards
- Feedback from submitters
- Consumer outcomes



Wellington Electricity's proposal



Applied for a customised price-quality path December 2017

Proposal

- Spend \$31.2 million to better prepare its network for an earthquake
- Includes bringing emergency hardware, mobile substations and switchboards, critical emergency spares, and enhanced communication systems into the region, as well as strengthening of substations

Impact (as estimated by Wellington Electricity)

- Price increase of \$1.50 to \$1.90 on a typical residential consumer's monthly bill

Streamlined CPP overview

Context

- 2016 Kaikoura earthquake highlighted region's vulnerability
- Government Policy Statement outlined expectations we should consider options for WELL to recover resilience expenditure

Three year CPP (2018-2021)

- Move from price cap to revenue cap to reflect IM changes
- Used existing DPP allowances plus allowable revenue for additional resilience expenditure for first two years
- Final year calculated using BAU forecast expenditure (using the tailored DPP building blocks approach) plus allowable revenue for additional resilience expenditure

Our assessment approach

- Detailed scrutiny of additional resilience expenditure proposed by WELL
- Scrutiny of BAU expenditure allowances to ensure the resilience expenditure has not already been provided for (ie, no “double-dipping”)
- Modified verification and audit requirements consistent with the streamlined CPP process
- Sought feedback on our draft decision in February 2018

Our decision

Satisfied investment needed and appropriately costed so
Wellington Electricity is better prepared to withstand and
respond to a major earthquake



Expenditure

Opex and capex included in the price path

- Allows for existing BAU expenditure in first two years consistent with the DPP allowance
- Allows for forecast BAU expenditure consistent with Wellington Electricity 's proposal in third year
- Allows for full \$31.2 million of resilience expenditure over the three years

Revenues

Annual maximum allowable revenue (MAR) that Wellington Electricity must comply with

- Initial 5.1% increase compared to allowable revenues under its current DPP, plus annual CPI adjustment
- \$6m change from draft decision to clarify the existing DPP base revenue allowance in first two years



Quality standards

Annual reliability limits WELL must comply with

- WELL will be subject to a reliability quality standard and incentives consistent with the DPP set in 2014

Annual resilience standard WELL must comply with

- Additional quality standard and incentive for WELL to meet the objectives of additional resilience expenditure
- If WELL fails to meet a minimum resilience level it will breach its quality path and we may take enforcement action
- Introduced a revenue linked incentive, if WELL does not deliver the resilience improvements, as outlined in proposal, its revenue will be reduced in the next regulatory period

Feedback from submitters

Three key topic areas from submissions on our draft decision

- **Streamlined process** – precedent implications and appropriateness to WELL’s situation
- **Cost-benefit analysis** – was the CBA used by WELL appropriate for Commission decision making
- **Resilience standard** – should this apply for each year of the CPP given the urgent nature of the work

Consumer outcomes

Network performance

- More resilient network that is less susceptible to earthquake damage
- Reduced risk of prolonged interruptions following earthquake

Cost

- We estimate an increase of about \$1.70 to typical residential consumer's monthly bill of \$185
- Estimate an additional increase of a similar amount in next period

Feedback on CPP processes

CPP regime should improve with each application

- We have received valuable feedback from submissions
- We intend to debrief with each applicant and capture our own reflections on the process
- We intend to publish an open letter/emerging views paper for feedback later this year to establish what the next steps are for improvements to the CPP regime



Questions

Information on both decisions and processes is available at:
<http://comcom.govt.nz/regulated-industries/electricity/cpp/cpp-proposals-and-decisions/>

