Submission on Proposed Quality Targets, Incentives and Compliance for Default Price-Quality Paths from 1 April 2015

Introduction

The Lines Company Limited (TLC) appreciates the opportunity to provide feedback to the Commerce Commission (the Commission) on the 2015 DPP Quality Incentives Paper.

Our initial comments on the proposals were included in our 15 August submission on the DPP Main Policy Paper.

TLC has expressed much of its views through the Electricity Networks Association submission. Outlined below are points of particular note for TLC. They should be read in conjunction with items we have raised in our Main Policy Paper submission.

Overview

- In preparing our submissions, TLC has tried to gain a sense of whether the DPP "works" or not given our circumstances. We manage an ageing network in a rural environment with minimal growth, a small customer base of low socio-economic areas and a high proportion of vacant/intermittent occupancy properties.

- The Commission will acknowledge that we have introduced different and innovative approaches to gain the optimal outcome for the Company and our customers. Most notable of these is our capacity/demand based pricing methodology and comprehensive AMP.

- The structure and complexity of DPP makes application of innovative approaches difficult. All of the methodologies, including the proposed incentive schemes work if you have a network enjoying reasonable growth, scale and urbanisation.

- However, it is our view that many of these methodologies are not well enough defined in terms of value and structure, or exercised in terms of application and testing outcomes, for them to be introduced.

- We acknowledge that the incentive schemes and DPP structural changes will align with the purpose statements outlined in the Act, and that the Commission is acting in accordance with those statements.

- However, the state of development of the schemes is such that it gives the impression of being rushed, an opening position that will be developed over time. This is not good legislative practice and not aligned with a low cost regulatory environment.

- Indeed the value to be derived from the application of the proposed incentive schemes, the cap on capital funding etc., is far outweighed by the expenditure needs of the TLC network in order to maintain compliance.

TLC recommends the Commission takes a longer term view to the development and introduction of schemes that introduce further complexity (and cost) without well-defined value.

Quality of Supply Incentive Scheme

- TLC has significant concern with the intent and structure of the Quality of Supply Incentive Scheme (QoSI).
- We take issue with the Commission's position that there is an inherent need to have a regulatory incentive scheme in order for EDBs to respond.
- To draw conclusions that EDBs "game" the system just to meet SAIDI and SAIFI targets at the expense of customers is nonsensical and without evidence.
- Indeed, to make statements that imply deliberate slow reactions to customers without power is demeaning to the staff involved. All personnel take pride from working in the electricity industry and doing their utmost especially in storm events.
- We expressed in our previous submission the inappropriateness of a SAIFI trigger in a rural network. In this situation, duration is more significant than the number of times a tripping occurs. For example, a customer 2 hours drive from the nearest township has more concern for being without supply for 8 hours than having a number of short interruptions.
- Network topography severely influences travel time, access, construction technique, materials etc. These drive the duration of the outage and are of more concern than how many times they experience a loss of supply.
- A rural network is further influenced by long lines of few customers, who can experience extended duration outages because of the factors described above.
- TLC understands and supports the intent of the QoSI however we do not see it as credible in its current form.

TLC recommends the QoSI scheme be omitted from the proposal until such time as it is fully researched and the implications understood.
Failing that, as a minimum, the proposal to have a SAIFI trigger on SAIDI MEDs should be omitted.

Influence of H&S Legislation

- The introduction of new Health & Safety legislation during the next regulatory period introduces a further significant influence.
- There is already strong industry evidence that Commerce Commission pressure, through QoSI and downward pressure on SAIDI & SAIFI targets, will influence fieldwork safety decision-making, particularly on planned works.

- The extent of the "bubble" around H&S legislation, and how far it reaches into the influence imposed by the QoSI, will no doubt be tested when the first prosecution is heard.
- Legislation aside, the ethical issues around safety are significant and anything that could be construed as having an influence on negative workplace decisions should be amended until all doubt can be extinguished.

TLC recommends that planned outages are discounted from the QoSI completely, rather than just a 50% weighting.

Value Equation

- Throughout the proposals for all of these schemes there is no evidence of a compelling value equation. The same can be said of applying a cap to capital and opex forecasts.
- In the case of the capital forecast, there is the ability for some value recovery. By exceeding the cap, expenditure can be established in the RAB but at the loss of depreciation and return on the asset during the 2015-20 period. There is at least the opportunity to recover in the following regulatory period.
- Our AMP preparation, supported by recent Replacement Capex evaluation against industry trends by an external party (Repex Modelling), confirms the need to increase spend in order to maintain standards.
- We refer the Commission to our discussion on capital caps and alternative X-position in our 15 August submission.
- Not spending the capital increases the risk of breaching quality and possibly health and safety standards. In any single year, a poor quality target performance puts Directors in contravention of the Commerce Act with limited ability to respond. This exposes Directors to an unreasonable position and particularly so if the threshold test becomes annualised rather than 2-out-of-3.

The proposals as a whole therefore provide no compelling case for delivering improvements in performance against either quality standards or customer costs.

Alternatively, the Commission needs to utilise its economic modelling strengths aligned with technical expertise to develop fully tested forecasting models, which are supported by the industry, before introducing structures that are unproven but with potentially serious impacts.

Incremental Rolling Incentive Scheme (IRIS)/Incentives

- The intent of low-cost regulatory structures is more akin to being rules-based than pre-approval based. The application of clear rules should negate the need for the Commission to sit in judgement of individual cases. That is not the case with the current proposals.
- The proposals for pre-approval introduce uncertainty as to the outcome.
- There is no confidence in the application of the schemes due to the arbitrary nature of the forecasts.
- As demonstrated in TLC's Asset Management Planning, the intent is to spend more on the network, not less. However the amount available gets capped as an efficiency incentive.
- Some opex is not controllable, emergency works for example. It can vary significantly from year to year.
- As with our statement related to the QoSI, we understand and support the intent of incentives, however we see the IRIS as being even less credible in the manner of its structure and justification.

TLC does not support the introduction of the IRIS. Implementation would mean we don't have a choice despite it not suiting a rural network – we need to focus on getting things done, not on a theoretical incentive scheme model.

Compliance

- TLC notes the extent of proposed changes and the scale of submission having to be prepared in response.
- As such, we draw the Commission's attention to the increase in cost to non-exempt EDBs that will inevitably be necessary to achieve compliance.

Commission Response

- We fully expect the Commission response to be one of "if your circumstances are such that they are outside the bounds of DPP, then seek a CPP".
- This again defeats the purpose of low cost regulation.
- Our circumstances are no different to many of the other smaller EDBs, and even some segments of the larger ones. DPP needs to be structured such that it is cognisant of the conditions at large. We do not feel that the proposals acknowledge this fact.

- The application of a CPP gives us no more confidence of a suitable outcome. The cost, resources, complexity and uncertainty lead to feelings of too much risk.
- Indeed, the cumbersome nature of the process exhibited through the Orion application is too much to contemplate for a small entity.
- The potential socio-economic impact of the outcome (price shock) is another deterrent.

If the Commission is determined to use the CPP process as the alternative route to DPP, the process needs to be streamlined and provide sufficient levels of confidence that a balanced, pragmatic outcome will be achieved.