

# INDIVIDUAL PRICE-QUALITY REGULATION OF TRANSPOWER

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REVISED PROCESS PAPER

26 August 2010



COMMERCE COMMISSION

Regulation Branch  
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# 1 INTRODUCTION

## 1.1 Purpose

- 1.1 The purpose of this Revised Process Paper for the Price-Quality Regulation of Transpower (Revised Process Paper) is to set out the Commerce Commission's (Commission) updated view on its process for setting an individual price-quality path (IPP) for Transpower New Zealand Limited (Transpower).
- 1.2 This Revised Process Paper sets out the following:
- a revised publication date for the s52P determination, which gives effect to the individual price-quality path for Transpower (IPP determination) – by 31 December 2010;
  - a revised date for the IPP determination to take effect – 1 April 2011; and
  - the Commission's initial views on the method for calculating Transpower's maximum allowable revenue (MAR) for the 2011/12 financial year (Transition Year).

## 1.2 Background

- 1.3 Transpower is currently regulated under Part 4 of the Commerce Act 1986 (the Act) by way of an administrative settlement<sup>1</sup> with the Commission in respect of breaches of the thresholds under Part 4A of the Act.<sup>2</sup> The settlement governs Transpower's revenues for each financial year until 30 June 2011.
- 1.4 The Commission must make a s52P determination applying price-quality regulation to Transpower before the expiry of the administrative settlement. The type of price-quality regulation to apply to Transpower is to be consistent with that specified in an Order in Council made by the Governor General following a recommendation to the Minister of Commerce from the Commission.
- 1.5 On 13 April 2010, the Commission made its recommendation to the Minister of Commerce that Transpower be subject to individual price-quality regulation.<sup>3</sup> Following acceptance of the Commission's recommendation by the Minister, the Governor General made an Order in Council specifying that Transpower be subject to individual price-quality regulation on 23 August 2010. Prior to the Order in Council, the Commission set out in its Individual Price-Quality Path (Transpower) Draft Reasons Paper (Draft Reasons Paper) that it would make the IPP determination by 30 November 2010 for the regulatory period beginning 1 July 2010.<sup>4</sup> The Draft Reasons Paper was published in advance of, but subject to, the Minister's acceptance of the

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<sup>1</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>2</sup> Although Part 4A was repealed by the Commerce Amendment Act 2008, section 54M under the new Part 4 of the Act provides that the administrative settlement continues to apply to Transpower until its expiry date.

<sup>3</sup> Commerce Commission, *Recommendation to the Minister of Commerce regarding the type of regulation to apply to Transpower*, 13 April 2010.

<sup>4</sup> Commerce Commission, *Individual Price-Quality Path (Transpower) Draft Reasons Paper*, 28 June 2010.

Commission's recommendation so that the Commission would have sufficient time to make the IPP determination by 30 November 2010.

- 1.6 The Commission now considers a revision of this timing and associated consultation steps is necessary for the reasons set out below.

## **1.2 Revised Process**

- 1.7 The Commission stated in its Draft Reasons Paper that it would make its IPP determination by 30 November 2010,<sup>5</sup> but now considers that this date should be 31 December 2010. The Commission's primary reason for deferring its decision by one month is that it is desirable to make the IPP determination in conjunction with the input methodologies (IM) determinations, which are due by 31 December 2010.
- 1.8 Although the Commission will be making separate IM determinations for Transpower, the Commission considers it beneficial to align the timing of the IPP and IM determinations that will apply to Transpower. This is advantageous as it allows the Commission to consult on all aspects of the proposed regulation of Transpower at the same time (i.e., the IMs that will apply to Transpower) helping to ensure that all of its determinations align well with each other, as well as with other IMs such as those that will apply to other electricity lines distribution businesses.

## **1.3 Date from which the IPP will apply**

- 1.9 The Commission stated in its Draft Reasons Paper that the IPP determination would apply price-quality regulation to Transpower from the expiry of the administrative settlement, thereby taking effect 1 July 2011.<sup>6</sup> This date was considered appropriate given that it aligned with Transpower's financial year and coincided with the expiry of the administrative settlement.<sup>7</sup>
- 1.10 The Commission now considers that the IPP determination should take effect on 1 April 2011. The reason for this is that the settlement only governs the setting of Transpower's revenue requirements up to, and including those which apply to Transpower's 2010/11 pricing year, which ends on 31 March 2011. The settlement does not apply to the setting of revenues for the 2011/12 financial year (which apply to the 2011/12 pricing year). If IPP regulation was only to apply from 1 July 2011, there would be a 3 month gap during which Transpower's revenue was not regulated.
- 1.11 Section 53M(7) sets out that a s52P determination does not apply to a supplier until the date specified in the determination, which must be a date at least four months after a summary of the determination is published in the Gazette. That section applies to an IPP determination pursuant to section 53ZC(2)(a). The Commission considers, however, that it is a necessary modification, as allowed under section 53ZC(2), to reduce the notification period, in this instance, to three months, for the reasons set out in paragraph 1.8 above.

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<sup>5</sup> Supra n 4, page 2.

<sup>6</sup> Supra n 4, page 1.

<sup>7</sup> Note that, while the settlement effectively expires on 30 June 2011 as that is the end date of the final financial year against which Transpower reports under the settlement, technically, the deed of settlement does not expire until the Commission has completed its assessment of Transpower's final compliance statement under the settlement, which is submitted to the Commission in September 2011.

- 1.12 In considering whether or not it is appropriate to modify the notification period, the Commission considered the impact of this decision. The Commission found that the revised timing of the publication of the IPP determination will have no detrimental impact on either Transpower or other interested parties. It will have no detrimental effect on Transpower because, whether the IPP determination is made in November or December 2010, Transpower will need to calculate its proposed MAR for the Transition Year on the basis of information requirements issued under s 53ZD of the Act in advance of the IPP determination being made. It will have no detrimental effect on interested parties because, regardless of the date on which the IPP determination is made, the Transition Year MAR will be recalculated at year-end as part of the annual wash-up. This wash-up will be calculated based upon the Commission's final determinations, resulting in any under or over-recovery being offset by an adjustment to Transpower's customer economic value account (either HVAC or HVDC as the case may be).
- 1.13 It follows from the above that two regulatory instruments will be in force at the same time during the period between 1 April 2011 and 1 July 2011. However, the Commission considers that there is no need to revoke the administrative settlement early because there is no overlap in the relevant pricing years and hence there will be no duplication of obligations for Transpower in that sense. The Commission further considers that it is not desirable to revoke the settlement early as Transpower has a reporting obligation as at 30 September 2011 (in relation to the pricing year ending 31 March 2011 and the financial year ending 30 June 2011). To address the period during which both instruments are in force, the Commission proposes to include a transitional provision in its IPP determination.

#### **1.4 Approach to setting the Transition year MAR**

- 1.14 In June 2010, the Commission set out in its Draft Reasons Paper that Transpower would be required to calculate its MAR for the Transition Year consistent with the Commission's specified building blocks, using the Commission-approved amounts for operating and capital expenditure specified in accordance with the process set out in the Draft Reasons Paper, the applicable input methodologies and any other requirements specified by the Commission's IPP determination, and submit this to the Commission by 10 September 2010.<sup>8</sup>
- 1.15 The Commission has considered Transpower's submission on this issue<sup>9</sup> and the implementation aspects of Transpower's MAR. The Commission is now of the view that, due to timing issues, it should require Transpower to calculate its MAR for the Transition Year based predominantly on the terms of the administrative settlement. Limited modifications will be required to ensure that the most material features of the draft IM determination and framework rules in the Input Methodologies (Transpower) Draft Reasons Paper (IM Reasons Paper) are taken into account.<sup>10</sup> The Commission intends to issue its detailed requirements to Transpower by written notice under section 53ZD of the Act in September 2010.

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<sup>8</sup> Supra n 4, page19.

<sup>9</sup> Transpower, Part 1 - Submission to the Commission on Input Methodologies Transpower and Individual Price-Quality Path Transpower, August 2010, p.40.

<sup>10</sup> Commerce Commission, *Input Methodologies Transpower Draft Reasons Paper*, 25 June 2010.

- 1.16 Given that Transpower must announce prices in December each year,<sup>11</sup> Transpower's MAR must be calculated and set by the Commission sufficiently in advance of December such that Transpower has time to calculate and announce prices. The Commission has concluded that Transpower is unlikely to have sufficient time to calculate its MAR for the Transition Year in a way that fully implements the Commission's draft IM and IPP determinations.
- 1.17 The Commission notes also that those draft determinations are still subject to consultation, and, therefore, may change. In these circumstances, the Commission considers it appropriate to require Transpower (under its s 53ZD notice) to undertake this calculation in accordance with a combination of the existing principles of the administrative settlement, the framework set out in the Draft Reasons Paper and the material aspects of the draft IM determination in the timeframe available. As noted above, any differences in the calculation between the draft determinations and the final can be taken account of at the wash-up at the end of the Transition Year.
- 1.18 A key reason for requiring Transpower to implement the material aspects of the Commission's draft determinations when calculating its MAR for the Transition Year is to minimise the magnitude of the year-end wash-up following the Transition Year.
- 1.19 It should also be noted that the wash-up at year-end for the Transition Year will be undertaken on the basis of the Commission's final IPP and IM determinations. The net impact of this decision is, therefore, minimal.

### 1.3 Summary of Revised Key Steps and Indicative Dates

- 1.20 Table 1 below sets out the key steps and indicative timing of the Commission's work in relation to Transpower.

**Table 1: Revised Key Steps and Indicative Dates for the IPP for Transpower**

Phase	Task	Indicative date
Commission Individual Price-Quality Path Framework Development	Cross submissions on Draft Reasons Paper.	25 August 2010
	Submissions on Individual price-quality (Transpower) Revised Process Paper.	3 September 2010
	Individual price-quality (Transpower) Consultation Update Paper	November 2010
	Individual price-quality (Transpower) Draft Determination (consultation on technical drafting).	November 2010
	Submissions on Updated Draft Reasons and Draft Determination papers.	November 2010
	Individual price-quality (Transpower) Final Reasons.	December 2010
	Individual price-quality (Transpower) Final Determination.	December 2010
	Summary of final s 52P determination published in the Gazette.	Late December 2010
Input methodologies	Input methodologies (Transpower) Consultation Update Paper, and Input methodologies (Transpower) Revised Draft Determination (consultation on technical drafting).	November 2010
	Submissions on Consultation Update Paper.	November 2010
	Input methodologies (Transpower) Final Determination.	December 2010

<sup>11</sup> As required under the Electricity Governance Rules.

## 2 SUBMISSIONS

- 1.21 Submissions are invited on both the Commission's revised process and its view on the approach for setting Transpower's MAR for the Transitional Year as set out in this paper. Submissions on this paper should be received by the Commission no later than **5pm Friday 3 September 2010** (due date). All submissions should be supported by documentation and evidence, where appropriate.
- 1.22 In order to meet the requirements 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. If submissions are received after the due date and an extension has not been granted, the Commission may not be in a position to adequately consider submissions for the next stages of the project.
- 1.23 To foster an informed and transparent process, the Commission intends to publish all submissions on its website. 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 available). Submissions should be sent to:

[Regulation.Branch@comcom.govt.nz](mailto:Regulation.Branch@comcom.govt.nz); or  
Alex Sim  
Regulation Branch  
Commerce Commission  
P.O. Box 2351  
Wellington

### *Confidentiality*

- 1.24 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. However, the Commission recognises there will be cases where interested parties making submissions may wish to provide confidential information to the Commission.
- 1.25 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.
- 1.26 Parties can also request that the Commission makes orders under s 100 of the Act in respect of information that should not be made public. Any request for a s 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 s 100 orders if requested by parties, including the principles that are applied when considering requests for such orders. Any s 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.