

04 September 2023

To: Transpower New Zealand Limited
PO Box 1021
WELLINGTON

Attention: Alison Andrew

Notice to supply information to the Commerce Commission under section 53ZD of the Commerce Act 1986 – RCP4 forecast opex

Purpose of this notice

1. The Commerce Commission (**Commission**) requires Transpower New Zealand Limited (**Transpower**) to provide it with the information specified at **Attachment A** to this notice, which forms part of this notice, issued under section 53ZD(1)(d) and (f) of the Commerce Act 1986 (the **Act**).
2. We need this information for the purpose of carrying out our functions and exercising our powers under Part 4 of the Act. Specifically, this information is required for the purpose of setting Transpower's operating expenditure (**opex**) allowance for the pricing years of the regulatory period from 1 April 2025 to 31 March 2030 (**RCP4**).
3. For the purposes of this notice, we have referred to certain opex portfolios in RCP4 as 'identified programmes', which is consistent with how this term is defined in respect of base capex in the *Transpower Capital Expenditure Input Methodology Determination* [2012] NZCC 2 (as amended) (**Capex IM**). The criteria for determining the identified programmes for RCP4, including for the relevant opex portfolios, were specified by us to Transpower on 8 March 2023.¹
4. Under sections 52P(3) and 53M(5) of the Act, in 2024 the Commission will determine the regulatory period that will apply for RCP4. However, for forecast information required by this notice, Transpower must present the forecast information based on an assumed five-year regulatory period for RCP4 and, where applicable, a subsequent assumed five-year regulatory period (**RCP5**).

¹ Email from [redacted] on 8 March 2023, titles 'Form and content of regulatory programmes and the criteria used to define identified programmes for RCP4'.

5. The forecast information required by this notice must be calculated and presented based on Transpower's information disclosure years ending 30 June.

Responding to this notice

Date of response

6. Transpower must supply the information required by this notice to us by a secure file sharing method eg, ECHO, directed to the email address: infrastructure.regulation@comcom.govt.nz by 5 pm on **1 December 2023**.
7. Please direct any correspondence to the attention of Project Manager, Transpower and Gas and include "Transpower IPP 2025 – RCP4 forecast opex" in the subject line of your email.

Information format

8. Please supply the information required by this notice in an electronic 'unlocked' MS Excel or MS Word format, as appropriate, with formulas intact, so that we can easily transfer information (ie, the information is able to be 'copied and pasted').

Supporting information

Information in the public domain

9. The requirements of this notice to supply information may be satisfied by reference to relevant information that is already publicly available if the information is readily accessible and is clearly referenced in Transpower's base capex proposal or opex proposal for RCP4.

Offences under section 103 of the Act

10. We note that section 103 of the Act provides that no person shall:
 - 10.1 without reasonable excuse, refuse or fail to comply with a notice under section 53ZD of the Act; or
 - 10.2 in purported compliance with such a notice, furnish information, or produce a document, or give evidence, knowing it to be false or misleading; or
 - 10.3 attempt to deceive or knowingly mislead the Commission in relation to any matter before it.
11. It is an offence to contravene section 103 of the Act and any person who does so is liable on summary conviction to a fine not exceeding \$100,000 in the case of an individual or \$300,000 in the case of a body corporate.

Publication of supplied information and confidentiality

12. We may publish the information provided by Transpower, in the context of our functions under Part 4 of the Commerce Act 1986, for the purpose of determining the IPP for RCP4.

13. If Transpower considers that there are good reasons that the Commission should not publish or publicly refer to any particular parts of its response, Transpower should:
 - 13.1 specify the relevant information when providing the response to the Commission;
 - 13.2 supply both public and confidential versions of the information; and
 - 13.3 give clear reasons why Transpower considers the information is confidential.
14. If Transpower indicates that we should not publish or publicly refer to part of its response, we will discuss this with Transpower before making any disclosure.
15. Any data or information provided to us in response to this notice that Transpower considers is confidential and should not be published, must be provided in an appendix or separate electronic file that is clearly marked as confidential. The responsibility for ensuring that confidential information is not included in a public version of information supplied to us rests entirely with Transpower.
16. Note that all responses we receive, including parts that we decide not to publish, can be requested under the Official Information Act 1982. This means we would be required to release material (whether published or not) unless good reason existed under the Official Information Act 1982 to withhold it. We would normally consult before releasing any material that Transpower requests not to be published.

Interpretation

17. In this notice, unless the context otherwise requires, bolded terms have their meaning as set out below or as defined in the **Capex IM**:

actual opex has the meaning defined in the **Transpower IM**;

base capex category has the same meaning as set out in the **Capex IM**, which include the categories used to define **identified programmes** for RCP4 that have been specified or agreed between us and **Transpower** under clause 2.2.1(2) of the **Capex IM**;

base-step-trend is a recurring approach to forecasting expenditure where a historic base year that is representative of recurring expenditure is selected and adjusted for significant, non-recurring items. This base year expenditure is then projected forward, adjusted for step changes and trends due to ongoing drivers;

Capex IM means the *Transpower Capital Expenditure Input Methodology Determination [2012] NZCC 2 (as amended)*;²

² The Commission is currently reviewing the Capex IM and Transpower IMs under section 52Y of the Act and will make its final decisions in December 2023. For further information, see our website:

forecast MAR has the meaning as defined in the **Transpower IM**;

forecast opex has the meaning as defined in **Transpower IM**;

identified programme means **base capex categories** or **opex** portfolios for which expenditure is forecast to be undertaken during **RCP4** and which are consistent with the criteria specified by the **Commission to Transpower** on 8 March 2023;³

obligation means a legally enforceable duty owed by **Transpower**, whether arising under legislation, in tort or in contract;

operating expenditure allowance or **opex allowance** means the monetary amount of **opex** specified by the **Commission** in an **IPP determination**;

opex means **operating expenditure**;

opex incentive amount has the meaning as defined in the **Transpower IM**;

pricing year means a 12 month period ending on 31 March for which a **forecast MAR** is determined;

RCP2 means the regulatory period that commenced on 1 April 2015 and ended on 31 March 2020;

RCP3 means the regulatory period that commenced on 1 April 2020 and ends on 31 March 2025;

RCP4 means the regulatory period following **RCP3** commencing on 1 April 2025 and assumed to end on 31 March 2030;

RCP5 means the regulatory period following **RCP4** which is assumed to commence on 1 April 2030 and end on 31 March 2035;

Transpower IM and **Transpower IM Determination** means the *Commerce Act (Transpower Input Methodologies) Determination 2010* [2012] NZCC 17 (as amended).

<https://comcom.govt.nz/regulated-industries/input-methodologies/input-methodologies-for-electricity-gas-and-airports/input-methodologies-projects/2023-input-methodologies-review>.

³ Refer to footnote 1 above.

If you have any queries in relation to this notice, please send them to the attention of Project Manager, Regulation Branch at: infrastructure.regulation@comcom.govt.nz.

Yours sincerely,



Dr Derek Johnston
Commissioner
Dated at Wellington

Attachment A: information required

1. Under section 53ZD(1)(d) and (f) of the Act, the **Commission** requires **Transpower** to provide the information specified below.

General information

2. A summary document that shows where we can find the information provided by **Transpower** in response to the requirements set out in this notice.

Company structure and nature of regulated services

3. A summary of **Transpower's** company structure and its regulated services, including:
 - 3.1 a current group structure map, including all companies and subsidiaries, as well as a high-level description of the main functions of each and their relationship with **Transpower**, and any proposed material changes planned to be made to the group structure for or in **RCP4**;
 - 3.2 a current organisation chart, including a description of operating units, the main organisational functions and their relationships, and staff numbers;
 - 3.3 any already-confirmed material changes planned to be made to the organisation structure for or in **RCP3** that would alter current **operating expenditure** patterns for **RCP4**; and
 - 3.4 a description of any proposed material changes to the provision of regulated services or grid outputs by **Transpower** in **RCP3** and which are planned to be made for or in **RCP4**.

RCP3 opex

4. The following information concerning **RCP3 opex**:
 - 4.1 a description of the key drivers of **opex** in **RCP3**;
 - 4.2 the actual and estimated efficiency savings achieved for each **opex** category, including forecast amounts until the end of **RCP3**;
 - 4.3 a description and the amount spent on innovation initiatives in **RCP3**, including how customers will benefit in the long term from those initiatives; and
 - 4.4 evidence demonstrating if, and how, **Transpower** has:
 - 4.4.1 pursued and is pursuing **opex** process improvements, including those identified in **Transpower's RCP3 opex proposal**;
 - 4.4.2 ensured and is seeking to ensure appropriate least-whole-of-life cost and efficient interventions;

- 4.4.3 pursued and is pursuing cost reduction strategies, with relevant examples provided from its **opex** categories; and
- 4.4.4 ensured and is seeking to ensure that both internal and external suppliers of goods and services have incentives to perform well and identify cost savings.

RCP4 opex

- 5. The following **forecast opex** information in **Transpower's RCP4 opex proposal**:
 - 5.1 a description of **Transpower's** objectives for its **opex** and representative examples from its **opex** categories that demonstrate the ways in which the **opex proposal** is consistent with an expenditure outcome which represents the efficient costs of a prudent supplier, having regard to Good Electricity Industry Practice (GEIP) as the appropriate planning and performance standard for a prudent supplier;⁴
 - 5.2 a high-level explanation of material deviations between the **RCP4 opex proposal** and the **integrated transmission plan** submitted as part of Transpower's **RCP4 opex proposal**;
 - 5.3 the source documents substantiating, or relied upon to prepare, the high-level explanations at paragraph 5.2 of this attachment.
 - 5.4 an overview that gives context to, and explains:
 - 5.4.1 linkages between **Transpower's** historical **opex**, quality performance and **capex**, and **Transpower's forecast opex**, proposed quality standards and **grid outputs** and **capex** for **RCP4**, including an explanation of how the **capex** programme during **RCP2** and **RCP3** has impacted on the **forecast opex** for **RCP4**; and
 - 5.4.2 any factors driving a material change in levels of **opex** for each of the **opex** categories forecast for **RCP3** and those forecast for **RCP4**;
 - 5.5 an overview of the methods used to develop the **opex** forecast for each **opex** category and for **opex** in aggregate, which must include:

⁴ 'Good electricity industry practice' is defined in Part 1 of the Electricity Industry Participation Code 2010 as:
good electricity industry practice in relation to transmission, means the exercise of that degree of skill, diligence, prudence, foresight and economic management, as determined by reference to good international practice, which would reasonably be expected from a skilled and experienced **asset** owner engaged in the management of a transmission network under conditions comparable to those applicable to the **grid** consistent with applicable law, safety and environmental protection. The determination is to take into account factors such as the relative size, duty, age and technological status of the relevant transmission network and the applicable law [bold terms in original].

- 5.5.1 details of the forecasting approach used for each **opex** category, eg, bottom up, **base-step-trend**, benchmarking analysis;
- 5.5.2 an explanation on why the forecasting approach used is considered appropriate;
- 5.5.3 if a **base-step-trend** forecasting approach is used, an explanation on why the expenditure in the selected historic base year is representative of recurring expenditure, including information on non-recurring expenditure that has been removed from the base year expenditure;
- 5.5.4 if a **base-step-trend** forecasting approach is used, an explanation on how any included forecast step changes and trend assumptions reflect efficient costs;
- 5.5.5 details of how the effects of uncertainties are incorporated in forecasts;
- 5.5.6 details of how synergies between **opex** portfolios and between **opex** and **capex** are taken into account;
- 5.5.7 details of the challenge and approval process employed for sign-off of **opex** forecasts; and
- 5.5.8 details of the differences, if any, and improvements in the forecasting approach used to develop forecasts compared to that used for the **RCP3 opex proposal**;
- 5.6 a description of **Transpower's** approach to treating forecast efficiencies in its **RCP4 opex proposal**;
- 5.7 a description and quantification of any contingency amounts that are included in the **RCP4 opex proposal**, the methodology for calculating those contingency amounts, and how the contingency amounts apply to specific **identified programmes**, where relevant;
- 5.8 an explanation of the deliverability of proposed levels of **opex**;
- 5.9 identification of key risks associated with resourcing and delivering proposed levels of **opex**;
- 5.10 a description of the rationale for forecast expenditure of each **opex** category that is not an **identified programme**; and
- 5.11 an operational copy of the model used to generate outputs required for the **RCP4 opex proposal** (eg, **forecast opex** for each of the **opex** categories for all **disclosure years** in **RCP4**).

RCP4 identified programmes – opex

6. The following information for each of **Transpower’s identified programmes** in the **RCP4 opex proposal**:
 - 6.1 a description of the **identified programme**, including its aims, objectives and benefits;
 - 6.2 an explanation as to deliverability, including factors likely to specifically affect that **identified programme**;
 - 6.3 a description of the methodology used to generate the forecast of the **opex** for that **identified programme**, where relevant this should include:
 - 6.3.1 key assumptions and how they were applied (and how they relate to Transpower’s **policies** and reflect GEIP);
 - 6.3.2 any cost benchmarking undertaken by or for **Transpower**; and
 - 6.3.3 any information available on internal historical cost trends;
 - 6.4 where relevant an explanation of the extent to which forecast non-network **opex** for that **identified programme** implements the key assumptions, recommendations from relevant consultants’ reports, and **policies** relating to the other aims and objectives of **Transpower**;
 - 6.5 an explanation of all material departures from any:
 - 6.5.1 relevant **policies**;
 - 6.5.2 planning standards; or
 - 6.5.3 conclusions and substantive recommendations contained in consultants’ reports;
 - 6.6 an assessment of the impact of the **identified programme** on **base capex**, **major capex**, assets and quality, including a description of any significant trade-offs between **opex**, **base capex**, **major capex** and quality that **Transpower** considered in the development of the **identified programme**;
 - 6.7 a description of relevant regulatory **obligations** that have a material effect on the **identified programme**;
 - 6.8 an explanation of any material step change from historical costs in any cost component for the same or a similar type of **programme**, and an explanation of the effect of the step change on **forecast opex** for the **identified programme**; and
 - 6.9 a schedule of key models used, accompanied by explanations of the models and how they were relied upon for the **identified programme**.

Policies, processes and consultants' reports

7. A schedule listing and describing key **policies**, processes and consultants' reports applicable to:
 - 7.1 **opex identified programmes;**
 - 7.2 business planning;
 - 7.3 insurance (including self-insurance);
 - 7.4 procurement related to **opex;**
 - 7.5 monitoring and reporting on forecast versus actual performance (including efficiency gains) achieved for **opex** categories;
 - 7.6 programs and initiatives that have been the subject of **Transpower's** internal approval system;
 - 7.7 the demarcation between **capex** and **opex**, the trade-off between **capex** and **opex** and the decision processes for investing in **capex** or **opex**; and
 - 7.8 any other **policies** that materially shape the **RCP4 opex proposal**;

Procurement

8. A description of the procurement processes that **Transpower** will use to help deliver **identified programmes** in the **RCP4 opex proposal**.
9. Identify and explain any key risks associated with procurement with the potential to affect the delivery of an **identified programme** in the **RCP4 opex proposal**.

Escalation factors and foreign exchange assumptions

10. The following information in respect of each escalation factor relied on to account for changes in input prices used in the **RCP4 base capex proposal** and **opex proposal** in responding to this notice:
 - 10.1 a description of each escalation factor and the rationale for its use;
 - 10.2 the methodology underlying the calculation of the escalation factor's quantum, by reference to inputs and assumptions;
 - 10.3 the weighting given to the escalation factor and description of how that weighting was determined, including any assumptions relied upon; and
 - 10.4 for escalation factors that relate to labour or material inputs, an explanation of whether additional contingency factors were applied and, if so, a description of the uncertainties that the contingency factors account for and how the contingency factors were calculated.

11. In respect of the foreign exchange assumptions used in responding to this notice, the following information:
 - 11.1 a list of the foreign exchange rates, and the source of those rates, used to prepare the **opex proposal**; and
 - 11.2 an estimate of the forecast exposure to foreign exchange movements for each foreign currency for each year of **RCP4** and a description of how these estimates were produced.

Instantaneous reserve event charges

12. An estimate of instantaneous reserve event charges for each year of **RCP4**, and a description of the methodology used to develop the estimates.

Insurance

13. The following information in relation to any proposed self-insurance allowance:
 - 13.1 an explanation of the method used to forecast the self-insurance allowance; and
 - 13.2 a description of the methodology used to calculate the self-insurance risk premium for any material new insured risks (ie, step changes in the proposed self-insurance allowance attributable to increases in the scope of insured risks); and
 - 13.3 a report from an actuary, who is qualified to provide such advice, on:
 - 13.3.1 the reasonableness of any 'step' in the self-insurance calculation attributable to changes in market trends in insurance premiums; and
 - 13.3.2 the methodology used to quantify the effect of any material new insured risks.

Cost allocation

14. The following information in relation to the allocation of **Transpower's** costs:
 - 14.1 relevant policy documents that describe the cost allocation methodology, consistent with clause 2.1.1 of the **Transpower IM determination**, used by **Transpower** for allocating **opex** between **electricity transmission services**, other regulated services and unregulated services;
 - 14.2 a description of all material changes between the cost allocation methodology used for **Transpower's RCP3 opex proposal** and the methodology used in the **opex** forecasts for **RCP4**, and the reasons for those changes; and

- 14.3 the variance, if any, between the **opex** values that would have been allocated for **RCP4** using the methodology used in the **RCP3 opex proposal** and the **opex** values allocated in the **opex** forecasts for **RCP4**.

Quantitative information

15. The following quantitative information:
- 15.1 a mapping of the cost categories used for **opex** as part of **Transpower's RCP3 opex** proposal onto the **RCP4 opex** categories and a list of all **opex** categories that are **identified programmes**;
 - 15.2 a comparison of **actual opex** and the **opex allowances** for each of the **opex** categories for each **disclosure year** of **RCP3**, where **actual opex** values are available;
 - 15.3 **forecast opex** and **opex allowances** for each **opex** category for each **disclosure year** of **RCP3** where **actual opex** is not available;
 - 15.4 **forecast opex** for each **opex** category for each **disclosure year** of **RCP4**;
 - 15.5 the total **forecast opex** values for each **disclosure year** of **RCP4**, excluding operating lease payments capitalised in accordance with the **Transpower IM**, which will be used for the **RCP4** calculations of the **forecast MAR**; and
 - 15.6 the total **forecast opex**, values for each **disclosure year** of **RCP4**, including operating lease payments capitalised in accordance with the **Transpower IM**, which will be used for the **RCP4** calculations of the **opex incentive amount**.