

Our process for setting Transpower's expenditure allowances, quality standards and individual price-quality path for 2015 to 2020

15 November 2013

- 1 This paper sets out the process we intend to follow in setting Transpower's expenditure allowances, quality standards and individual price-quality path for 2015 to 2020.

Transpower will propose expenditure allowances and quality standards

- 2 By 2 December 2013, Transpower's is required to submit a proposal for the operating and base capital expenditure allowances and quality standards to apply for the regulatory period from 1 April 2015 to 31 March 2020. These allowances and quality standards are important determinants of the individual price-quality path (IPP) that will apply to Transpower over this period.
- 3 Transpower's proposal is required by the Capital Expenditure Input Methodology Determination (Capex IM determination)¹ and an information gathering notice we issued in accordance with s 53ZD of the Commerce Act 1986 (the Act).²
- 4 When received, Transpower's proposal will be published on our website.³
- 5 Two types of expenditure allowances will be proposed by Transpower; base capital expenditure (base capex) and operating expenditure (opex). Major capital expenditure (major capex) is approved on a project by project basis.
- 6 The proposal will also include the proposed standards for quality of supply to apply for the period. Some of the proposed quality measures will be revenue-linked so that Transpower has financial incentives to improve quality performance.

¹ Commerce Commission, *Re Transpower Capital Expenditure Input Methodology* [2012] NZCC 2. link to the 53ZD notice and an explanation that it includes Opex information.

² This information gathering notice primarily contains information requirements for operating expenditure and can be found at the link below.

³ <http://www.comcom.govt.nz/regulated-industries/electricity/electricity-transmission/transpower-individual-price-quality-regulation/transpowers-price-quality-path-from-2015-to-2020/>

We will evaluate Transpower's proposal

- 7 We will evaluate the expenditure allowances and quality standards Transpower proposes. Our evaluation approach will be consistent with the Capex IM determination and will promote the purpose of Part 4 of the Act⁴
- 8 The purpose of Part 4 is to promote the long-term benefit of consumers, by promoting outcomes that are consistent with outcomes produced in competitive markets, such that Transpower:
- 8.1 has incentives to innovate and invest, including in replacement, upgrades and new assets,
 - 8.2 has incentives to improve efficiency and provide services at a quality that reflects consumer demands,
 - 8.3 has incentives to share with consumers the benefits of efficiency gains, including through lower prices, and
 - 8.4 is limited in its ability to extract excessive profits.

We will then set Transpower's individual price-quality path

- 9 Transpower's opex and capex allowances are important determinants of Transpower's Individual Price-Quality Path (IPP) for the regulatory period.
- 10 Under Part 4 of the Commerce Act 1986, we are responsible for determining an IPP for electricity lines services supplied by Transpower.⁵ Electricity lines services include both transmission services and system operator services.
- 11 Transpower's system operator services, however, are not currently subject to IPP regulation due to the existence of a contract between Transpower and the Electricity Authority for these services. It is our view that this contract results in outcomes consistent with those that would be observed in a workably competitive market.
- 12 We first set an IPP for Transpower for the regulatory period for 1 April 2011 to 31 March 2015. We will now set Transpower's IPP for the next regulatory period, from 2015 to 2020.
- 13 The IPP determines Transpower's maximum allowable revenues and quality standards. Transpower revenues are determined using a 'building blocks' approach.⁶

⁴ S 52A(1) of the Commerce Act 1986.

⁵ S 53ZC(1) of the Commerce Act 1986.

⁶ Commerce Commission, *Commerce Act (Transpower Individual Price-Quality Path) Determination 2010*, Decision No. 714.

This approach aggregates the individual components of Transpower’s forecast costs, such as the return of and on capital, opex, and tax to construct Transpower’s maximum allowable revenues.

- 14 We are required to reach a final decision on the IPP to apply for the next regulatory period by 30 November 2014. We aim, however, to publish the final determination by 31 October 2014.

How you can have your say

- 15 We will be consulting at various points in our process, beginning with the consultation on Transpower’s published proposal.

Timeline

- 16 The table below sets out our proposed process steps and indicative dates:

Table 1: Process steps and indicative dates

Indicative date	Process step
2 December 2013	Publish Transpower's proposal
10 February 2014	Date by which we publish an issues paper inviting you to have your say on Transpower's proposal
3 March 2014	Submissions due on our issues paper
10 March 2014	Cross submissions due on our issues paper
16 May 2014	Publish our draft decision on expenditure allowances and quality standards, our draft decision on compliance obligations and the form of the IPP, and our draft IPP determination
27 June 2014	Submissions due on our draft decisions and our draft IPP determination
11 July 2014	Cross-submissions due on our draft decisions and our draft IPP determination
29 August 2014	Publish our final decision on expenditure allowances and quality standards
29 August 2014	Issue information request to Transpower to calculate revenue
31 October 2014	Publish decision on compliance obligations and form of the IPP
31 October 2014	Publish IPP determination

- 17 Our process and indicative dates may change. Any changes to these dates will be posted on our website. For example, we may decide to hold workshops on particular aspects of Transpower’s proposal.

Our next step

- 18 We intend to publish an issues paper in February 2014 inviting submissions on:

- 18.1 Our proposed approach to evaluating Transpower’s proposal, and

18.2 Any specific matters on which we seek your view in relation to Transpower's proposal.

Please contact us with any questions in relation to our process

19 Please contact Paolo Ryan, RCP2 Project Manager, if you have any questions.

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