

31 July 2018

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By email to regulation.branch@comcom.govt.nz

Dear Matthew

Feedback on recent customised price-quality path processes

1. Orion welcomes the opportunity to have input on the Commission's request for feedback on recent customised price-quality path processes.
2. The Commission wishes to improve confidence in the customised price-quality path process.
3. In achieving this goal we encourage the Commission to take a proportionate approach when considering CPPs so that EDBs are not deterred from application, in appropriate circumstances, and the absolute and relative cost of applying is not prohibitive.
4. Our feedback is provided in the attached table which addresses each topic area and the relevant questions posed by the Commission.

Concluding remarks

5. Thank you for the opportunity to provide this feedback. We do not consider that any part of this feedback is confidential. If you have any questions please contact Dayle Parris (Regulatory Manager), DDI 03 363 9874, email dayle.parris@oriongroup.co.nz.

Yours sincerely



Dayle Parris
Regulatory Manager



Table A: Consideration of alternatives	
1.0 Whether we should require market testing of major investments, and if supported then:	<p>We do not support market testing, as opposed to consultation, of major projects being a requirement of the CPP application process.</p> <p>Much of the commentary makes comparison of EDB's CPP process to Transpower's IPP process. EDBs are somewhat different than Transpower in that we have vastly different project numbers, many more direct customers and comparatively greater financial resources. EDBs' networks are highly interconnected which makes isolation of customer benefits more difficult. In any one year Orion, for instance, processes in the order of 2,600 capex work orders individually covering expenditure between a few hundred dollars to \$2.7m. To apply market testing prior to CPP application to even a percentage of these could be disproportionate and costly.</p> <p>The consultation processes already required in the Input Methodologies, with further precedent being established on what effective consultation is as more CPP applications are processed (as well as examples from other jurisdictions), is sufficient and appropriate to allow input from interested parties. In addition consultation undertaken by EDBs is already overlaid by review of proposals by the Commission and verifier (and supporting consultants) as part of the formal CPP process conducted by the Commission.</p> <p>Consultation and market testing are two different processes. Market testing begins to reach into tendering and procurement processes ahead of EDB design processes. This could be viewed as a 'cart before horse' scenario. Alternatives should be assessed at a timing that is appropriately close to the implementation timing requirement. Market testing requires assessment of non-price as well as price factors, and appropriate prequalification of providers. We consider a CPP application requirement for market testing with third parties to be an onerous additional obligation. It is important that we do not go down the path of taking EDB business decisions away from the business.</p>
1.1. What is an appropriate threshold to require market testing (e.g., minimum dollar value of a project before it is required to be market tested);	No comment (see commentary above)
1.2 What information and processes should be required for market testing; and	No comment (see commentary above)
1.3 When the market test should be conducted, with reference to the CPP application date.	No comment (see commentary above)

Table B: Use of cost-benefit analysis	
<p>We would like to hear your views. In particular, we are interested in:</p> <p>1.0 Areas of potential customised price-quality path proposals that could be the focus of further work to understand how benefits can be quantified (e.g., health and safety);</p>	<p>We agree that cost-benefit analysis is one tool in a proposal assessment that could be used to quantify benefits as part of a broader assessment of an investment. We note, however, that this usually only addresses quantitative aspects. It is also important to consider qualitative aspects along with having the ability to exercise appropriate judgement. Cost-benefit analysis is not always appropriate depending on the problem trying to be solved, the business context, and the wider environment. A broader business case may be more appropriate.</p> <p>Other areas that could be the focus of further work are VOLL, VOI and resilience.</p> <p>However, VOLL (Value of lost load) and VOI (Value of interruption) can be problematic and customer surveys to evaluate positioning may be carried out on different bases (for example willingness to pay or willingness to accept), and customer responses will be dependent on local conditions at the time. It is difficult to know what approach is best, how to have a consistent quantification over time and across projects, and what would more readily reflect customer preferences.</p> <p>Resilience is another area that can be difficult to quantify however attention and expenditure in this area is fundamental for EDBs to deliver their obligations under the Civil Defence Emergency Management Act and more broadly to customers. Unlike reliability investment the benefits of resilience investment are often only demonstrated in the long term when a significant low probability, high consequence event actually eventuates and validates the original investment decision.</p>
<p>2.0 how an asset criticality framework could help support identifying expected benefits of additional expenditure; and</p>	<p>Orion currently uses condition based risk management models to quantify risk and to build up risk based work programmes for large volume, high expenditure assets as part of asset lifecycle management. Asset criticality forms part of the 'building block' in quantifying the risk. This is a type of cost benefit analysis when different work programme scenarios are compared with the goal of maintaining overall asset class health and reliability performance to meet customer expectations.</p> <p>An asset criticality framework could help support identifying benefits of additional expenditure and to provide some consistency of approach across EDBs however flexibility in the framework would be required to ensure calibration to local circumstances e.g. differing customer density, construction configurations, service provider costs etc.</p>
<p>3.0 potential changes to the customised price-quality path requirements that could help support the use of cost benefit analysis as a tool to inform customised price-quality path proposals.</p>	<p>A common view on the definition of benefits and how benefits can be consistently quantified could be beneficial. We submit that use of one tool over another should not be prescribed though.</p>

Table C: Long term pricing impact	
Please provide us with your feedback on whether: 1.0 an applicant should be required to consult on the long term price impact of its proposal;	We agree that consultation on the long term impact of proposals as a whole is beneficial for customers. It should be noted that recognising that the longer term impact, beyond the 5 year period, is more uncertain and would only be indicative.
2.0 the option of making an input methodology amendment is appropriate; and	A consistent method for quantifying next regulatory impact would be useful.
3.0 there are other options available that will encourage applicants to consult on the long term pricing impact.	No comment

Table D: Calculating revenue and pricing changes Attachment B	
Please provide us with your feedback on: 1.0 whether there are any issues in using a standard approach to calculating revenue and price changes consistently for consumer consultation purposes as well as in our customised price-quality path decisions;	We support having a standard approach to calculating revenue and price changes consistently for consumer consultation.
2.0 whether our proposed approach to calculating these changes and the assumptions we make as outlined in Attachment B are appropriate;	<p>We broadly support the proposed approach provided in Attachment B.</p> <p>We note that the approach assumes an even distribution of price changes although at times a change may only apply to certain affected customers.</p> <p>MBIE data is not the “cheapest” of all retailer plans, it uses the lowest published price for each retailer for a representative pricing plan and then takes the ICP weighted average of these. Therefore data may include small businesses i.e. not just residential as noted in Attachment B point 22.</p> <p>We presume that the supplier provided DPP estimate for the counterfactual is verified?</p>
3.0 whether focusing the analysis on the ‘typical consumer’ as outlined in Attachment B is appropriate; and	We agree
4.0 whether there are any other relevant consumer types that should be included in this analysis and, if included, where the necessary information could be sourced from.	No comment

Table E: Delivery and accountability of CPP commitments	
Please provide us with your feedback on whether: 1.0 there needs to be improved transparency that demonstrates a customised price-quality path applicant is delivering the commitments for which it has been funded in a transparent and easily understandable way;	We agree in principle
2.0 an applicant should be required to provide a stakeholder facing delivery report that sets out how it is delivering the major projects and wider commitments it has been funded for under a customised price-quality path; and	We agree delivery of commitments is important. However there should be flexibility for discussion and pragmatism that recognises that in a forecast situation circumstances can change and other favourable solution options can come along that weren't available when the CPP decision was made. In addition alternative solutions initially discounted can become more favourable over time. Any obligation to report should allow flexibility for delivery of a different solution to that initially proposed to meet the commitment provided that the expenditure impact does not escalate and the new solution is in the interests of customers.
3.0 it is appropriate to require customised price-quality path applicants to propose additional quality measures that are closely linked with the key drivers of its proposal to establish greater accountability for increased revenue, and whether these should be linked with revenue.	Yes

Table F: Link between price and quality	
<p>We want to better understand how an asset criticality framework could be adopted to support customised price-quality path proposals. In particular:</p> <p>1.0 What is the current practice within the sector for making decisions on investment trade-offs, and communicating trade-off decisions?</p>	<p>Increasing EDB maturity in asset management practices by way of industry guidelines is important but at this level should not be prescribed in the CPP IMs.</p> <p>Orion currently applies condition based risk management (CBRM) models to quantify risk and to build up risk based work programmes for large volume, high expenditure assets as part of asset lifecycle management. Asset criticality forms part of the ‘building block’ in quantifying the risk. This is a type of cost benefit analysis when different work programme scenarios are compared with the goal of maintaining overall asset class health and reliability performance to meet customer expectations communicated to us through our engagement programme. These scenarios, incorporating asset criticality, undergo internal challenge from experienced operational/technical personnel before coming to a preferred work programme for a particular asset class in the context of our business risk appetite informed by our customer engagement.</p> <p>Investment decisions we make are subject to documented asset management reports and business cases which includes, as appropriate, relevant alternatives. Approval of recommendations is sought from management and board as appropriate.</p> <p>Our engagement programme with customers continues to develop, and we have engaged with customers on trade-offs in both our customer workshops and in our Customer Advisory Panel.</p> <p>See our response to question 4 below for further detail.</p>
<p>2.0 What are the potential compliance costs of implementing an asset criticality framework?</p>	<p>Time to determine data requirements, and processes to collect data and input to models. Building models requires significant investment. Building expertise in interpretation of outputs.</p>
<p>3.0 What is preventing asset criticality being implemented across the sector?</p>	<p>Orion introduced the CBRM approach in 2010 and (subject to delays in its development as a result of the Canterbury earthquakes) we have continued to evolve and improve its use and application. A CBRM approach that incorporates asset criticality requires accurate asset data, experienced people to calibrate models and time to evolve understanding with use to embed the intellectual property across the business. The calibration process requires comprehensive data on reliability performance at asset level, construction cost at asset level, and local knowledge of the physical environment assets reside in. The process can be resource heavy, due to the dynamic environment in which our assets operate and ongoing learnings from this, which requires recalibration of the model at periodic intervals.</p> <p>An EDB may make the business decision not to implement a CBRM including asset criticality due to consideration of their size, and the number of assets and the function of a particular asset class. That is, an increasing volume of assets and data places a greater emphasis on more sophisticated ways of assessing asset health, criticality and priority for work programmes than where a network of assets is of lower volume and</p>

	<p>more easily assessed through intrinsic network knowledge. There is a significant investment required to develop CBRM models.</p> <p>The EEA is currently collaborating with EDBs to develop an asset criticality framework. Collaborating in this way delivers cost efficiency.</p>
<p>4.0 How do price and quality trade-offs get communicated to consumers so they can more meaningfully engage?</p>	<p>It is critical for us to continue to understand the needs of customers and the community to ensure we are providing them with the services they want, not just now but also in the future. We sought our customers' views in a variety of forums:</p> <ul style="list-style-type: none"> • we held "Powerful Conversations" workshops with customers exploring their views on network investment decisions that affect reliability, resilience and safety; and sought their opinions on future technology options. In particular, in these conversations we sought to educate our customers on the types of and elements of trade-offs we make to encourage an open two way conversation that allowed customers to share their thought process around trade-offs and provide us with their own positioning on the trade-off continuum. • surveyed more than 800 residential and business customers to verify what we had heard at our workshops • established the Orion Customer Advisory Panel where we host lively and informative discussions quarterly on a range of topics • conducted a series of Focus Groups seeking customers' views on pricing options and our customer communications • conducted our annual Residential Customer Perceptions survey to measure satisfaction with our performance and communications • held two Major Customer Seminars on key matters of relevance to people who operate intensive power dependent businesses <p>We were reassured to find customers are generally satisfied with our approach to safety, the reliability of our network and our level of investment in resilience. Customers encouraged us to look pro-actively to the future to make sure we are ready to enable them to take advantage of new technology.</p> <p>We are taking what we learned in these conversations into our future planning. One area customers told us they'd like better service was communication around power outages. We took this feedback on board in our approach to an eight hour outage proposed for a major project to upgrade the power supply to Lyttelton.</p> <p>We briefed the local Community Board, held face to face conversations with local businesses and letterbox dropped around 1,600 affected households. Considering feedback on the impact an eight hour power cut would have on the community, we made the decision to put in two large generators so the power could remain on in Lyttelton throughout the day.</p>

Table G: Consumer consultation	
<p>In particular, we are seeking your views on: 1.0 whether a process is required to align expectations between the Commission and applicant prior to consultation being undertaken;</p>	<p>We agree a process may be useful to align expectations between the Commission and applicant prior to consultation being undertaken for a CPP (in the context of a specific CPP e.g. post catastrophe). Currently, there is a risk of customer consultation not satisfying a threshold the Commission expects in any particular consultation process. This could be as simple as an EDB sharing its engagement programme and objectives.</p>
<p>2.0 the role of specific tools such as consumer panels;</p>	<p>We support a forum that allows EDBs to share information and build knowledge within a group of customers over time on its business and investment decisions and solutions.</p> <p>Established in 2018, Orion’s Customer Advisory Panel is a forum for us to engage with leaders of community groups and non-government organisations that represent the interests of a broad cross-section of our customers. With a customer advocacy focus, the Panel helps us understand customer needs, issues and service requirements.</p> <p>Panel members represent a cross section of the community and reflect the diverse perspectives of our customers.</p> <p>Our customer advisory panel fulfills an important role in our decision making and has helped us to refresh our understanding of customer expectations and the linkage to our asset management practices. See Table F(4) for more detail on other elements to our engagement programme. This is a maturing model and we continue to follow other jurisdictions to understand how we can develop this practice.</p>
<p>3.0 scope for specifying the existing requirements to provide further clarity; and</p>	<p>The application of the proportionate scrutiny principle is also important for consumer consultation. Scoping of the types of activities that the Commission would endorse as appropriate consultation would provide further clarity.</p> <p>There are some frameworks used in Australia such as IAP2 (International Association for Public Participation). A review of existing frameworks in other jurisdictions may be useful so that the Commission can provide an indicative list of endorsed frameworks that represent good practice.</p> <p>However we do not believe that consumer consultation requirements should be prescribed. This will limit the ability of EDBs to tailor their approach based on the circumstances, material they plan to consult on and the audience with whom they are consulting. A principles based approach is preferable.</p>
<p>4.0 the role of incentives at improving consumer engagement to get better long-term outcomes for consumers.</p>	<p>Consumer engagement is specifically required as part of a CPP application which should provide implicit motivation for quality engagement as part of an applicant’s proposal. We do not believe that specific incentives are appropriate or necessary.</p>

Table H: Verification	
We would like to hear your views on the following: 1.0 whether the present verifier flexibility is sufficient and if the verifier should be required to signal early in the verification process the projects and programmes that they intended to verify;	No comment
2.0 should we be more prescriptive about the extent of the material required for the verified projects and programmes, keeping in mind that the Commission may also request additional material during its own assessment of the proposal;	No comment
3.0 whether we need to formalise the applicant information provision requirements to ensure information is provided to the verifier in a timely manner;	No comment
4.0 whether a verifier emerging views paper or preliminary report has merit;	No comment
5.0 whether the boundary between the audit and verification processes is sufficiently clear and if not, how can it be improved;	No comment
6.0 Have the changes to the verification process, made during the last input methodologies review, improved the verification and Commission customised price path assessment processes.	No comment

Table I: Defining and applying proportionate scrutiny	Proportionate scrutiny: The level of scrutiny applied should be commensurate with the price and quality impact on consumers of the tailoring being sought.
Please provide us with your feedback on: 1.0 your view regarding the current definition of proportionate scrutiny and whether you consider this is sufficient and provides enough clarity to potential customised price-quality path applicants;	See our comments under Table G(3)
2.0 whether you believe there is a need for the Commission to better define the principle of proportionate scrutiny and the circumstances when it may be applied in practice; and	Any additional guidance is welcome
3.0 any further steps you think could be taken by the Commission to provide more certainty to all industry participants and stakeholders about how customised price-quality path applications will be assessed?	No comment