2020–2025 price-quality paths for EDBs and Transpower

Final decisions: Presentation to Stakeholders

27 November 2019

Sue Begg, Deputy Chair

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COMMERCE COMMISSION NEW ZEALAND
Te Komihana Tauhokohoko

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Outline of presentation

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Highlights

- Key revenue figures
- The WACC effect
- Consumer Impact
- Changing Environment

Electricity Distributors DPP (DPP3)

- Background
- Revenue
- Capex & Opex
- Quality
- Incentives
- Reopeners

Transpower IPP (RCP3)

- Revenue
- Expenditure

Final Decisions: Highlights

Overall allowed revenues in year one (2020/21)

Electricity distributors

$1.011b

Down $72m (6.7%) from 2019/20

Transpower

$788m

Down $142m (15.2%) from 2019/20

These reductions in revenues are largely due to a reduced cost of capital (WACC) offset by increases in network size and opex

Note
- EDB figures do not include pass-through and recoverable costs
- Powerco and Wellington Electricity are not included in the electricity distribution figure as they are subject to customised price-quality paths (CPPs)

Impact from the change in WACC

- The final decision uses a WACC estimate of 4.57%. This is a change from 7.19% in DPP2 for EDBs and RCP2 for Transpower
- Savings due to lower economy-wide interest rates passed on to consumers
- The WACC effect alone has reduced nominal revenue requirements in 2020/21 for:
  - EDBs by $225m
  - Transpower by $140m
- We used the WACC formula specified in the IMs

Overall consumer impact

- Distribution costs are around a third and transmission around a tenth of the total residential electricity bill
- The average change across all affected EDBs is a reduction of $6 per month
    - Prices will increase for Aurora customers ($1 per month)
    - Prices will decrease for average customer on all other networks
- The actual change consumers receive will depend on various factors, including the network the consumer is on

Note: Estimates are based on the average residential consumer on a Low Fixed Charge Tariff based on MBIE QSDEP data.
They include the effect of incentive schemes and the change in transmission charges.

Distributors face changing environment

- The Government’s response to Electricity Price Review has included a focus on innovation and decarbonisation
- Within constraints of low-cost approach, the DPP reset aligns to this context through:
    - A new recoverable cost for innovation projects
    - Alignment of incentives for operating and capital expenditure
    - Revenue cap facilitates distribution pricing reform
    - A re-opener for large unforeseen consumer driven connections and system growth capex

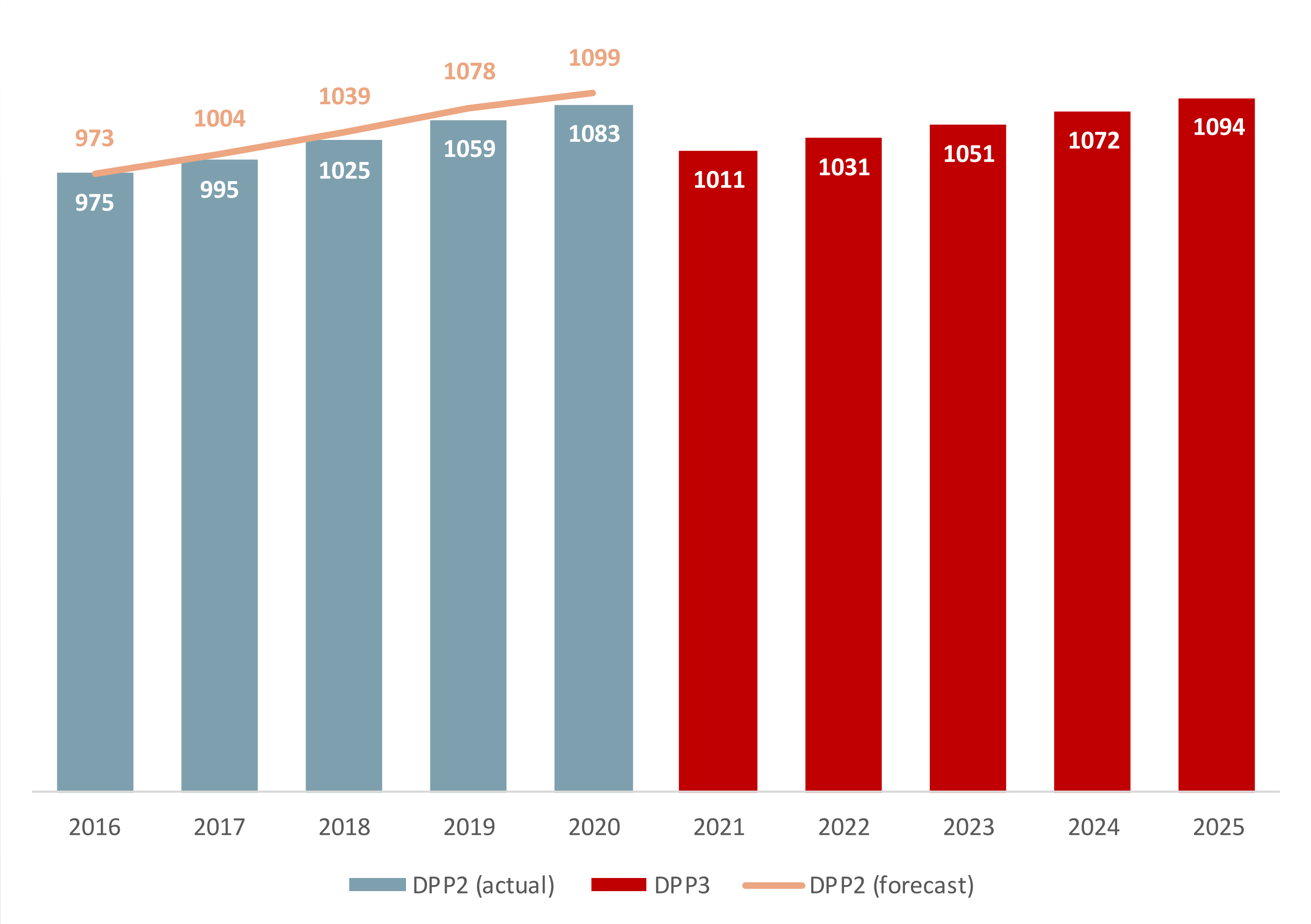
EDB DPP3 Final Decision: In Detail

Background to EDB DPP3 Decision

- The DPP is intended to be relatively low-cost and may not cater for every eventuality, uncertainty or specific need of an EDB
- Same core components as the current DPP2 price-quality framework
- Refinements to improve outcomes for consumers, certainty for businesses and incentives for innovation and technology
- Applies to 15 price-quality regulated EDBs or around 1.2m consumers

Nominal Regulated EDB Revenue over DPP3

Total revenue allowances for DPP2 and DPP3 periods ($m nominal)



- Initial 6.7% decrease as revenue realigned to match forecast costs
- Growth over the DPP3 period generally at CPI
- Total allowed revenue 2.4% higher in DDP3 v DDP2

Note

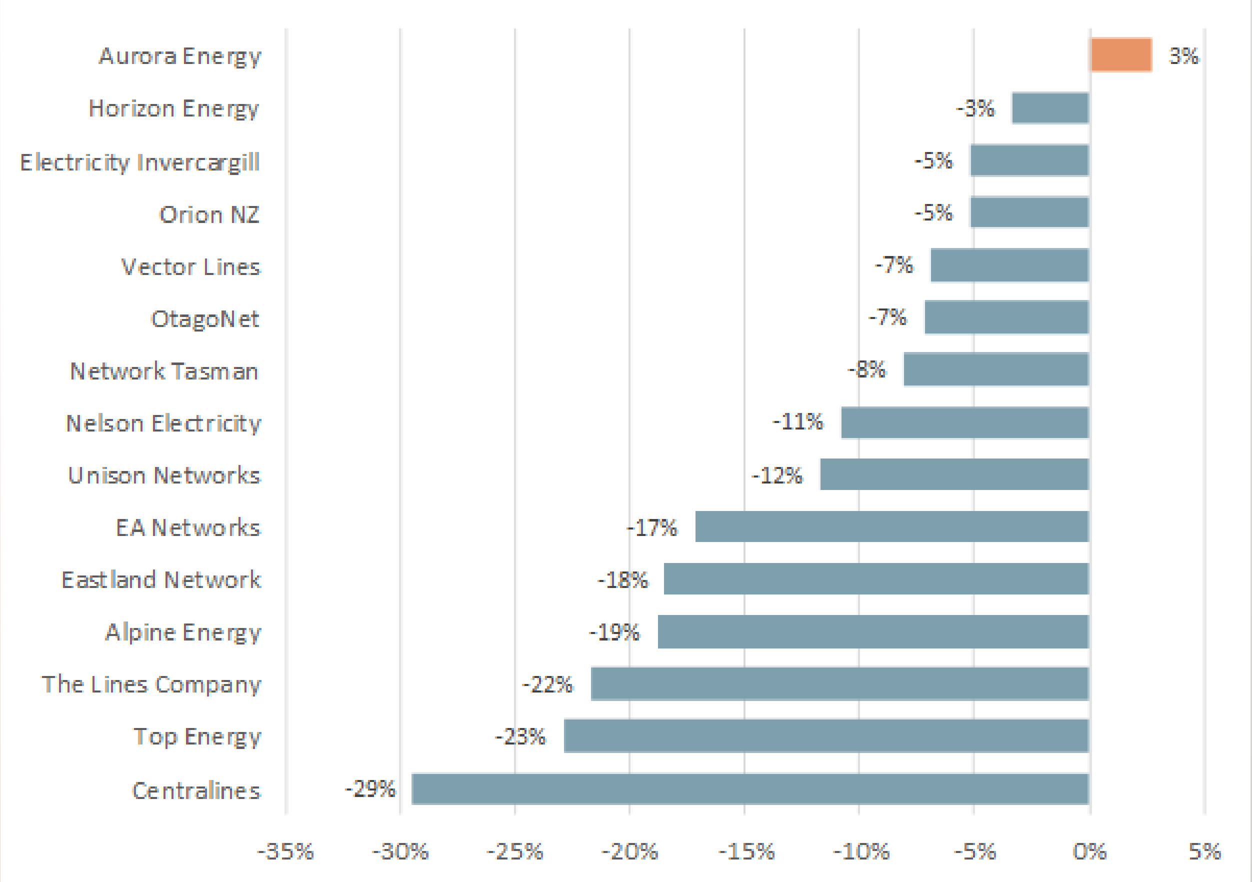
- EDB figures do not include pass-through and recoverable costs
- Chart excludes Powerco and Wellington Electricity as they are subject to customised price-quality paths (CPPs) and 12 other consumer trust owned EDBs
- Includes Orion revenue in DPP2 and DPP3

Revenue by EDB and rates of change

Distributor	Allowable revenue in 2020/21 ($m)	Increase in allowable revenue from Draft decision (%)
Alpine Energy	42.35	-6.65%
Aurora Energy	87.33	21.25%
Centralines	9.37	-0.34%
EA Networks	33.26	-11.77%
Eastland Network	24.03	-4.10%
Electricity Invercargill	12.26	-0.28%
Horizon Energy	23.91	-4.38%
Nelson Electricity	5.50	-1.55%
Network Tasman	26.46	-8.08%
Orion NZ	158.50	-1.66%
OtagoNet	25.78	2.77%
The Lines Company	34.71	2.25%
Top Energy	38.01	-9.90%
Unison Networks	100.02	-2.18%
Vector Lines	389.38	-3.46%
Total	1,010.86	-1.78%

Note: Estimates exclude effect IRIS

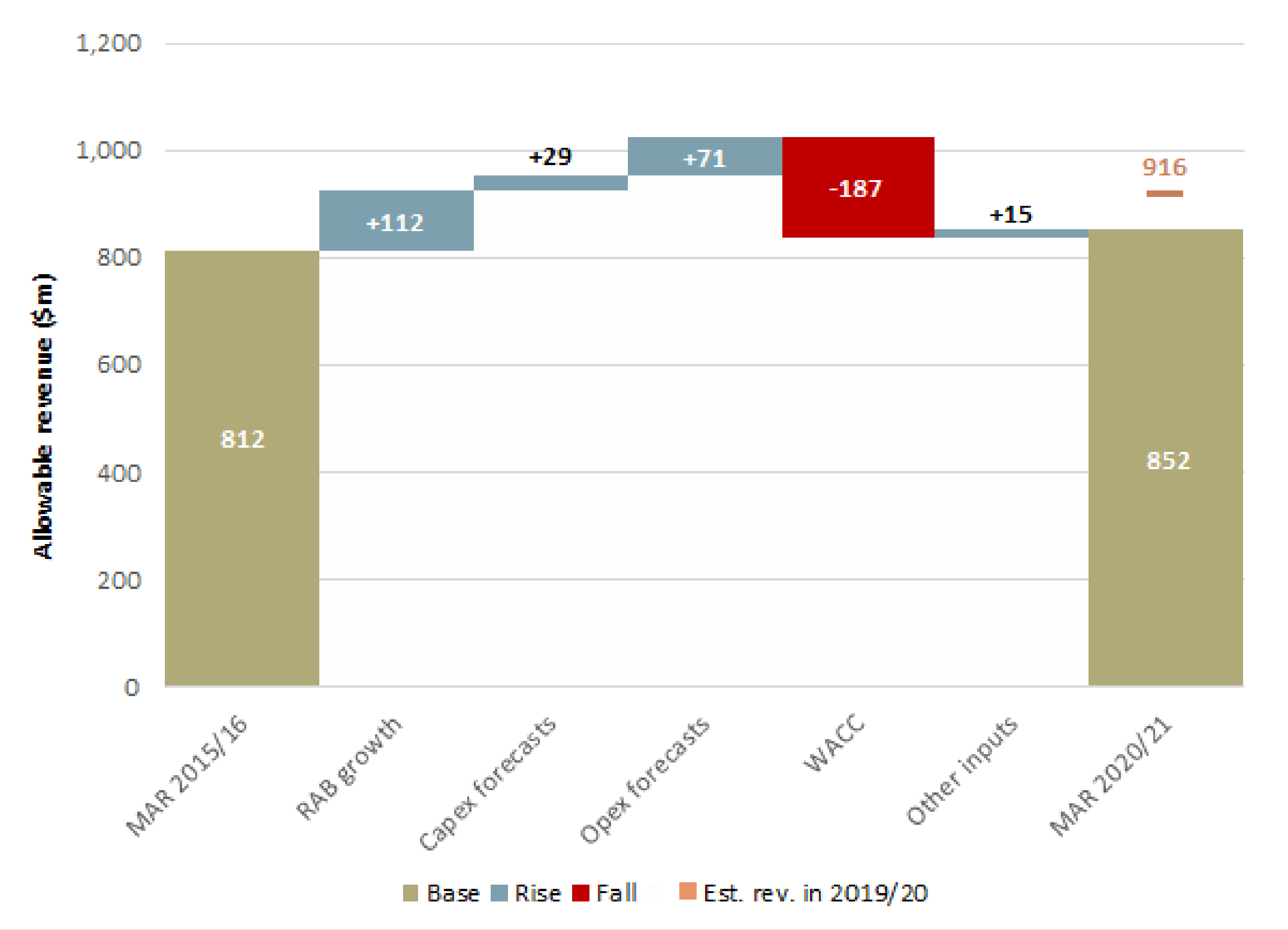
Change in allowable revenue between 2019/20 and 2020/21



Note: Estimates include effect IRIS but exclude transmission pass through

Breakdown of revenue changes for EDBs

DPP2 starting prices v DPP3 starting prices



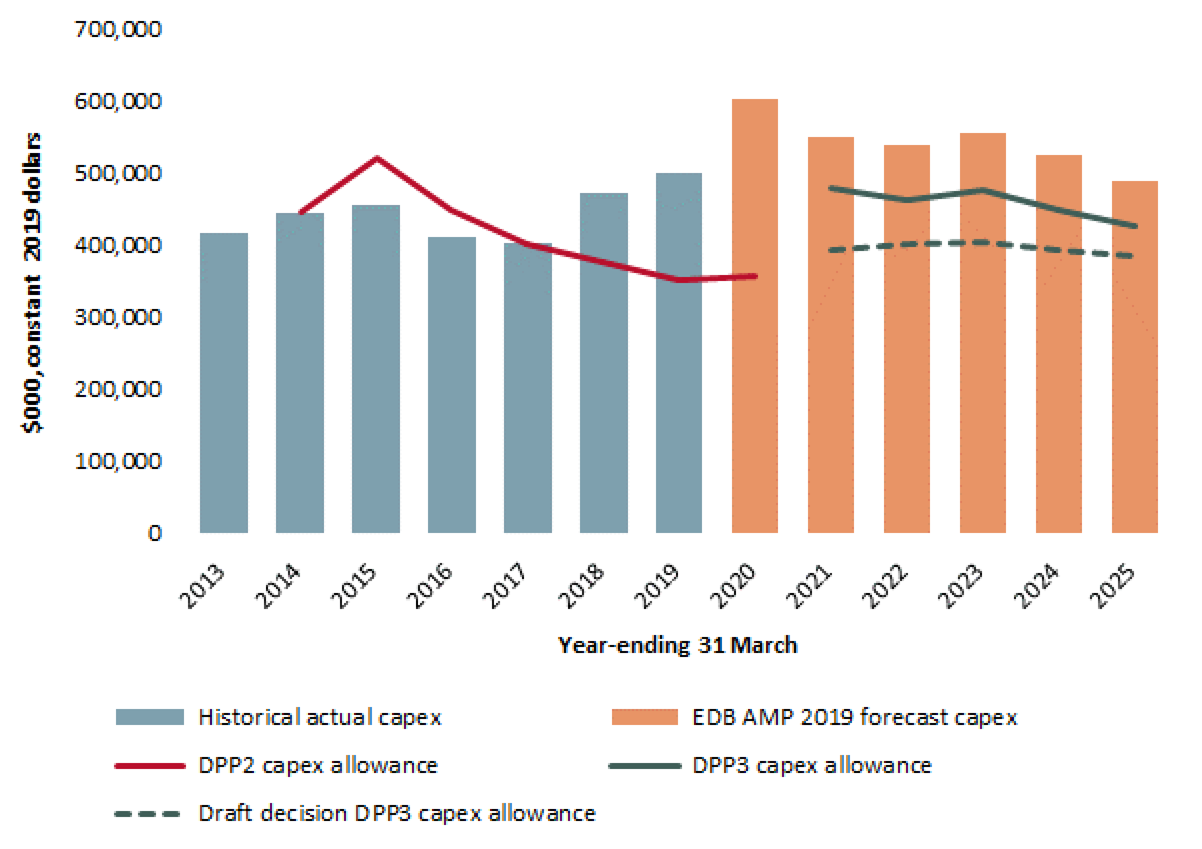
- Change driven largely by WACC
- Partially off-set by RAB and opex growth
- Revenue in 2019/20 higher than in 2015/16 because of CPI, CPRG, and X-factors

Note

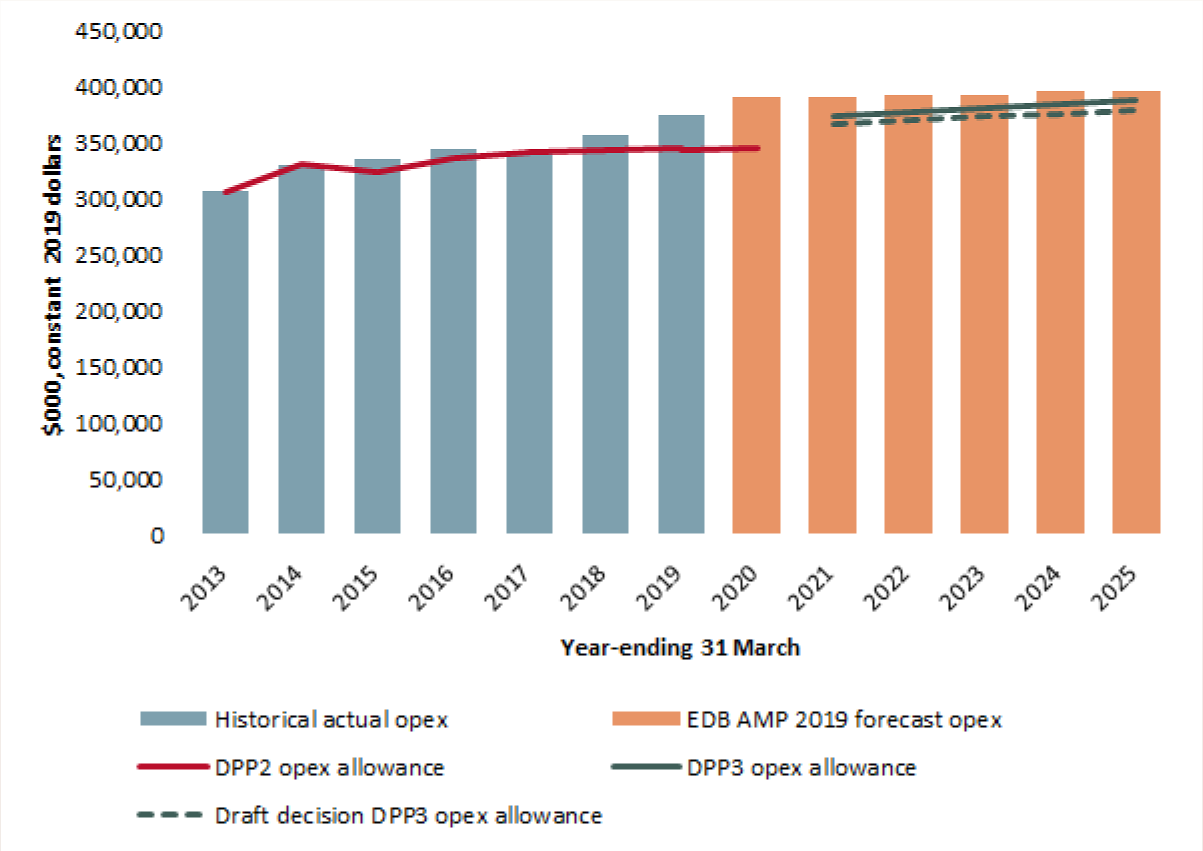
- Excludes Orion, Powerco and Wellington Electricity revenue in DPP2 and DPP3

Real trends in capex and opex for EDBs

Capex



Opex



Overview of DPP3 quality standards

- ‘No material deterioration’ still our starting point quality
- Retained SAIDI and SAIFI as measures of quality
- Separate standards for planned and unplanned interruptions
- Incentives apply to planned and unplanned SAIDI
- Enhanced reporting following a breach of a quality standard
- Redefined major events, reset boundary values and improved major event reporting
- New measures of quality to be dealt with in Information Disclosure before they can be added to the DPP

Expenditure and innovation incentives

- Opex IRIS incentive scheme retention factor of 23.5% (determined by the IMs – effect of lower WACC)
- Capex retention factor set equal to the opex retention factor (was 15% in DPP2)
- Introduced an innovation allowance that is recoverable from consumers, capped at 0.1% of revenue, or $150,000. This must be matched $1:$1 by the EDB, providing c. $11m available investment over the DPP period

Uncertainty mechanisms and reopeners

- In response to a changing environment and uncertainty we have introduced new DPP reopeners to account for certain types of capex projects:
  - Large connections to an EDB’s network like the electrification of an industrial plant or distributed generation
  - Substantial system growth projects
  - Major relocations of assets not able to be funded through capital contributions

Transpower IPP Final decision: RCP3 in detail

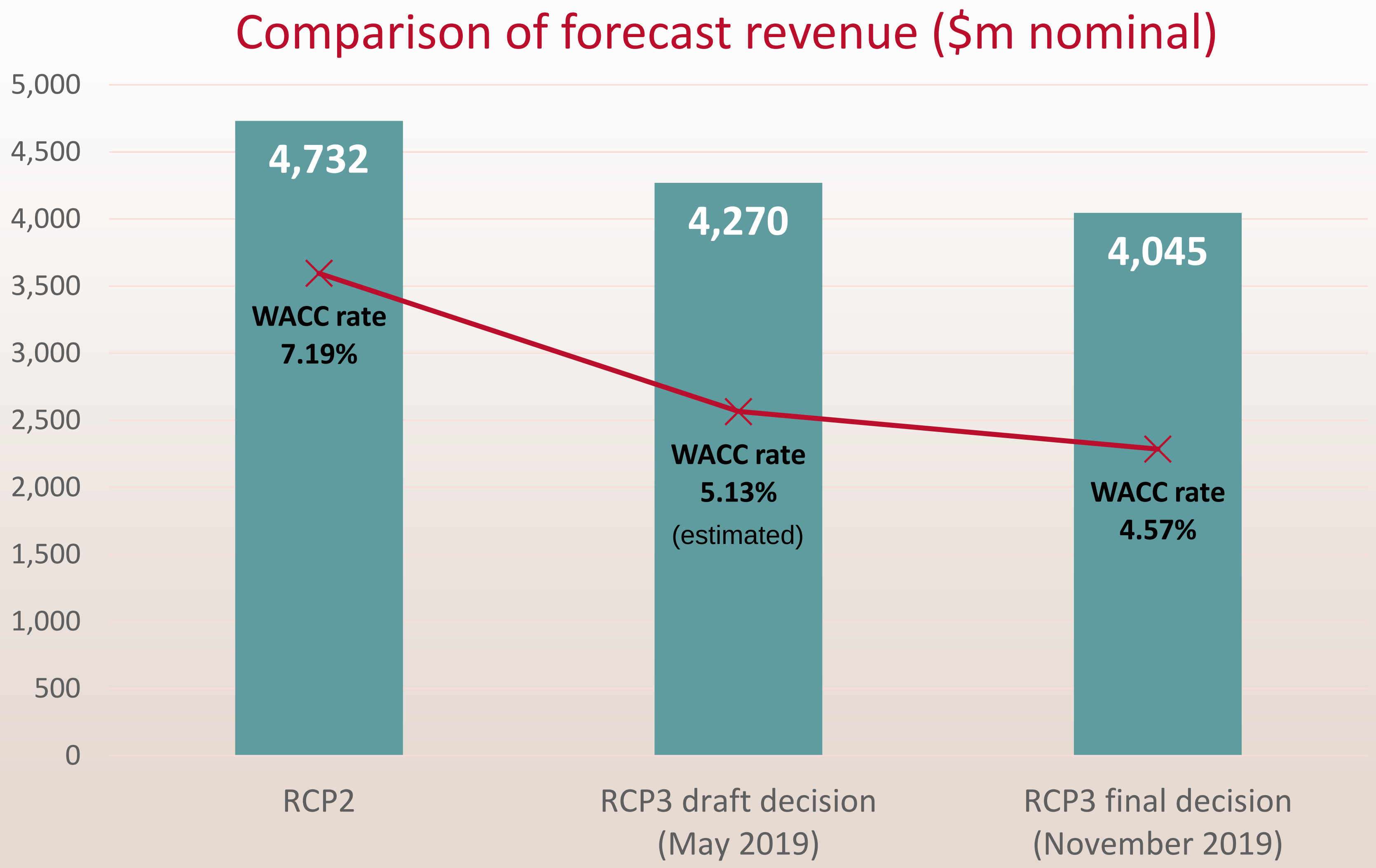
Expenditure

- We accepted 96% of Transpower’s proposed expenditure
- Our high acceptance rate reflects a high-quality proposal submitted by Transpower, which had the benefit of scrutiny by the independent verifier

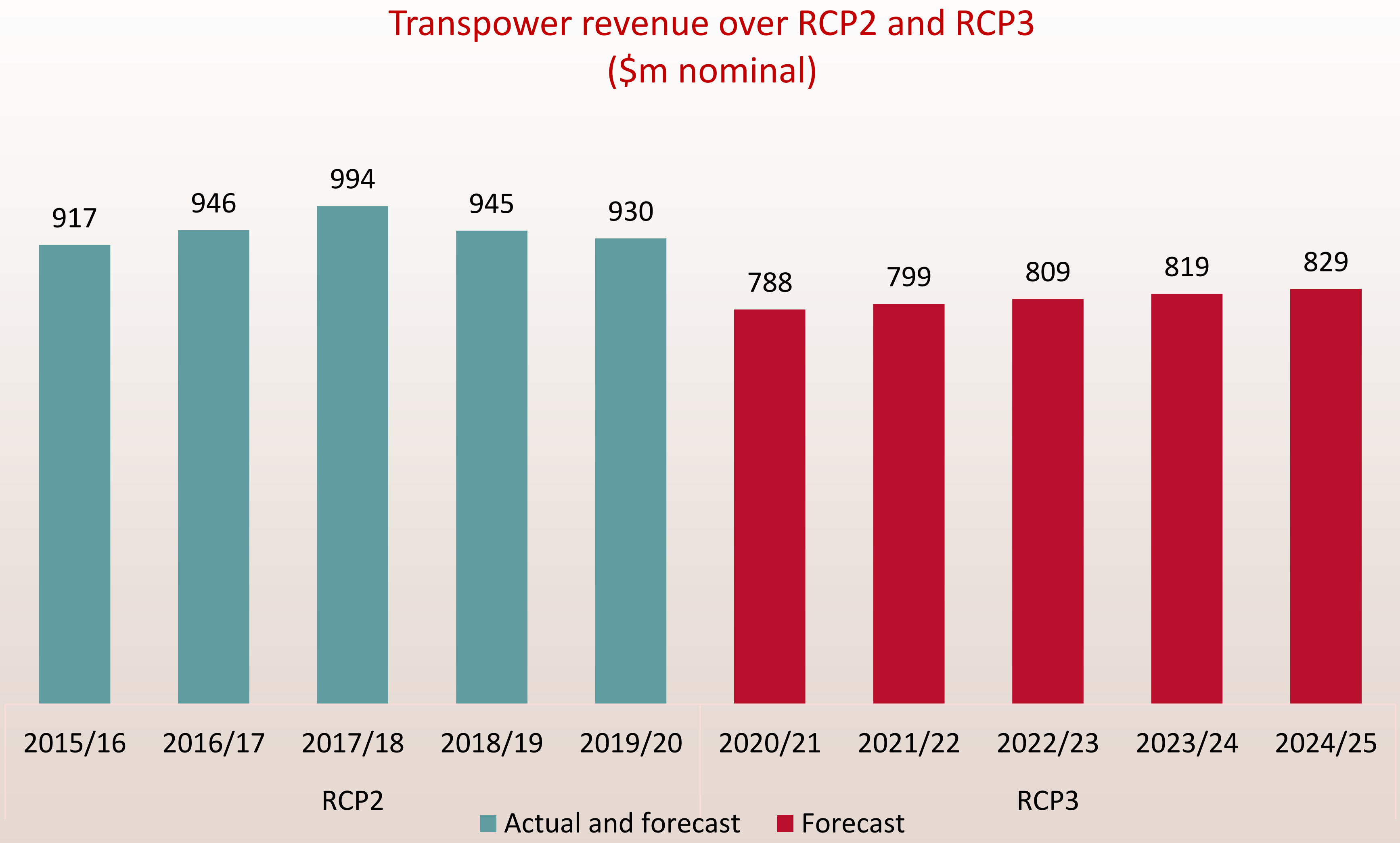
Capex category	Transpower proposal ($m)	Commission decision ($m)	Percent approved
Renewal	976.8	976.8	100%
ICT capex	146.1	127.5	87%
Adjustment for ICT capex benefits	-14.00	-14.0	100%
E&D	76.4	59.0	77%
Business support capex	17.1	17.1	100%
Total	**1,202.4**	**1,166.4**	**97%**

Opex category	Transpower proposal ($m)	Commission decision ($m)	Percent approved
Maintenance	552.1	538.9	98%
Deliverability adjustment	-29.1	-29.1	100%
AM&O	309.5	309.2	100%
Business support opex	226.5	209.1	92%
ICT opex	195.9	168.3	86%
Insurance	88.0	82.0	93%
Total	**1,342.9**	**1,278.4**	**95%**

Total forecast revenue



Annual forecast revenue



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