



7 March 2019

Dane Gunnell  
Manager, Price-quality Regulation  
Commerce Commission  
Wellington

By email: [regulation.branch@comcom.govt.nz](mailto:regulation.branch@comcom.govt.nz)

Dear Dane

## ***Cross-submission on Transpower's individual price-quality path for the next regulatory control period: issues paper***

We welcome the opportunity to cross-submit on other stakeholders' submissions on the Commerce Commission's paper published 7 February 2019, *Transpower's individual price-quality path for the next regulatory control period: issues paper*.

This cross-submission comments on two specific areas where we consider additional information would be helpful for the Commission's evaluation, and for stakeholders' consideration of our proposal. In this cross-submission, we discuss:

- the robust nature of our process to procure an independent verifier, and
- our approach to calculating our proposed incentive rates.

### **Procurement of independent verifier**

In its submission, Meridian queried whether the potential for conflict of interest was adequately managed through the process of engaging the independent verifier.

Independence, including the avoidance of actual or perceived conflict of interest, was a key consideration in the procurement process for the independent verifier. We undertook a robust process, which included the Commission's input, to assess potential conflicts in relation to both self-review (reluctance to criticise one's own work) and ongoing business (reluctance to criticise a major client). We consider the potential for conflict of interest was well managed.

Under the tripartite deed between Transpower, the independent verifier and the Commission, the independent verifier had a duty of care to act as an independent expert and with reasonable care.<sup>1</sup> We consider that verification added value to the preparation of our RCP3 proposal. We look forward to working with the Commission and stakeholders to determine the role of independent verification in future RCP proposal development processes.

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<sup>1</sup> The deed is available on our website at: [https://www.transpower.co.nz/sites/default/files/uncontrolled\\_docs/Verification%20Deed%20%28REDACTED%29.pdf](https://www.transpower.co.nz/sites/default/files/uncontrolled_docs/Verification%20Deed%20%28REDACTED%29.pdf).

## Calculation of incentive rates

MEUG included a report prepared by NZIER with its submission. The report discusses the setting of quality standards and grid output measures. Among other matters, the report comments on the proposed revenue at risk for revenue-linked output measures. As a sense-check on our incentive rates, NZIER suggests using the ratio of the interruption frequency and interruption duration-based incentive rates (the rate for GP1 divided by the rate for GP2).<sup>2</sup> The applicability of this sense-check relies on the assumption that the outcomes for GP1 and GP2 are independently correlated with respect to our totex investment in any given year, and that we could therefore target investment independently at GP1 and GP2 to achieve a set outcome.

We have shown in Regulatory Template RT02 how we have set the incentive rates for GP1 and GP2. We have assumed that there is a correlation between the outcomes for those measures and our totex investment on the basis that, if we stop investing in the grid, both the number of interruptions (GP1) and the average duration (GP2) will worsen. This is the most reasonable working assumption. Given this assumption, we consider that NZIER's ratio does not give a result that can be used in the way that NZIER suggests.

## Other matters

Where submitters raised issues that are relevant to work being led elsewhere within Transpower, and outside of the scope of the RCP3 proposal process, submissions have been brought to the attention of key staff to follow up with submitters directly.

## Conclusion

We appreciate stakeholders' engagement in the Commission's process of evaluating our RCP3 proposal, and the valuable feedback provided. We continue to be available to provide further information as required.

Yours sincerely



Alison Andrew  
Chief Executive

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<sup>2</sup> Table 6, NZIER report to MEUG, *Transpower IPP 2020-25 Comment on Issues Paper*, 25 February 2019.