Part 4 Determinations: Request for Clarification and/or Amendment

Please complete the table below and email to:

regulation.branch@comcom.govt.nz – **Attn: Dane Gunnell**

Transpower issue reference	**IM_11** (spend based allowance for base capex)
Date of request	14 June 2013
Party requesting clarification or amendment	Transpower
Relevant determination (Decision number)	Decision 714 and NZCC 2
Clause reference	Various (including Capex IM B1, IPP 5.3(4)(d))
Description of clarification or amendment sought. If an amendment is proposed, provide the suggested wording of the determination.	We propose that the Commission sets a base capex allowance relating to forecast expenditure for each year, rather than forecast value of assets to be commissioned each year, i.e. an *expenditure* allowance rather than a *commissioned value* allowance. We would still prepare forecast MAR figures based on commissioning (i.e., forecast RAB values) and calculate annual MAR wash-ups based on the timing and value of the assets we have commissioned. However the base capex incentive would be based on spend rather than commissioned value (i.e. actual expenditure vs. adjusted expenditure allowance) and the CPI and FX adjustment to the allowance (used above) would be assessed and applied on an expenditure basis. There are various ways that this amendment could be given effect to which we would like to discuss with Commission staff.
Reason why clarification or amendment is required	Like any business, it make sense for our financial controls and management processes to predominantly operate at an expenditure level rather than a commissioned value level. We have put in place systems and processes to deal with operating to a commissioned-value allowance for RCP1, however these do not replace processes that operate at an expenditure level, because expenditure is still the most important control point. Importantly, development of our RCP2 base capex proposal primarily operates at an expenditure level, with conversion to commissioning values carried out as the final calculation step. Forecasts are originated in expenditure terms, and adjustments (such as for escalation and FX rates) are made at an expenditure level. Within RCP2, we will have to adjust our base capex allowance each year for any disparity between forecast and actual CPI and FX rates. The adjustment is logically assessed on an expenditure basis but, as things stand, would be applied to a commissioned

	value allowance. This is likely to cause a timing mismatch between the driver (FX and CPI impact on spend) and the control (aggregate value of commissioned assets). For example, a fall in the NZD in the second half of a year will impact expenditure immediately but may largely flow through to commissioned values in the following year. We cannot see any problem with operating the base capex incentive on an expenditure basis. For base capex projects, expenditure generally flows through to commissioned values over a relatively short time period, so the timing of a reward for expenditure savings will more or less be matched by the timing of a MAR reduction (and vice versa). We understand that customers should pay for commissioned assets rather than expenditure, and that the MAR should be forecast and washed-up accordingly. The above proposal preserves this approach. Changing to an expenditure-based allowance would not alter incentives for timely commissioning of assets, because interest during construction is included in expenditure and the MAR is still driven by commissioning. If we had an expenditure allowance, then there would not be as direct a link between the approved annual allowance and the annual movement in our MAR. However, we do not think this will make the regime less transparent or stable on the whole than the status quo. Wash-ups would remain based on forecast vs. actual commissioning timing and values and we will still be able to publish a build-up of our forecast MAR along with our allowance proposal.
Reasons Paper reference (if applicable)	
Date amendment is required to be made by and why (if applicable)	The amendment should be made to apply from the beginning of RCP2 (in time to calculate the 2015/16 MAR)