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_10** (Interest During Construction – 75th percentile WACC cap)
Date of request	14 June 2013
Party requesting clarification or amendment	Transpower
Relevant determination (Decision number)	IM – NZCC 17
Clause reference	IM Clause 2.2.7(2)(b)
Description of clarification or amendment sought. If an amendment is proposed, provide the suggested wording of the determination.	2.2.7(2) When applying **GAAP** for the purpose of subclause (1), the cost of financing (a) is applicable only in respect of the period commencing on the date the asset becomes a **works under construction** and terminating on its **commissioning date**; and (b) is calculated at the rate prescribed by GAAP ~~using, subject to subclause (3), a rate no greater than the **75th percentile estimate of WACC** applying in respect of the relevant date for its calculation under **GAAP**~~. On balance we prefer this approach as it avoids the need for separate accounting treatment and EV adjustment as is currently required.
Reason why clarification or amendment is required	At a substantive level, asymmetric treatment of interest rate costs for IDC results in Transpower under-recovering IDC costs. That is because, when interest rates fall these automatically flow through into the calculation of IDC costs but when interest rates rise the flow through is capped at the 75th percentile WACC. From a process / administrative perspective the status quo is cumbersome and inefficient as it necessitates separate accounting treatment to comply with GAAP and to meet the 75th percentile cap. We do not think the concerns in the Reasons Paper to justify the 75th percentile cap are valid because: 1. Transpower's accounting policy, consistent with GAAP, is to assign an average cost of debt to capital projects, not to assign specific tranches to specific projects. 2. Allied to this, Transpower's has a strong incentive to secure the most favourable funding options in every instance. Together, these factors mean that Transpower there is no incentive to favour 'easier' but higher-cost sources of project funding as this would increase our total average cost of debt and reduce shareholder returns. In the event that the amendment proposed above is not

	made, it may be appropriate to formalise the EV adjustment currently used when interest costs exceed the 75th percentile WACC.
Reasons Paper reference (if applicable)	Paragraph 4.4.40-4.4.48
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)