

19 July 2023

Commerce Commission
44 The Terrace
Wellington, 6140

By email: IM.Review@comcom.govt.nz

Horizon Energy Distribution Limited (Horizon Networks) submission on IM review decision papers

1. Thank you for providing us the opportunity to make a submission on the *IM Review 2023 Draft Decision, Cost of Capital topic paper, CPPs and In-period adjustments topic paper and Financing and incentivising efficient expenditure during the energy transition topic paper*.
2. Horizon Networks is a small trust-owned Electricity Distribution Business (EDB) serving over 25,000 consumers in the Eastern Bay of Plenty region. As a trust owned EDB, we have a strong consumer focus and seek to benefit both our Shareholder Trust Horizon and the communities we serve.
3. We appreciate the opportunity to provide feedback on the draft decisions. Given the limited time, and highly technical nature of some of the topics Horizon Networks is providing a non-technical targeted submission which emphasises the following:
 - There is no compelling reason to reduce the WACC below the 67th percentile.
 - Reopeners should not be restrictive or exclusive.
 - Horizon Networks supports retaining RAB indexation.

There is no compelling reason to reduce the WACC below the 67th percentile

4. In the *Cost of Capital topic paper*, the Commerce Commission is proposing to drop the WACC percentile for EDBs and Transpower from the 67th percentile to the 65th percentile.
5. In its draft *decision summary and context paper*, the Commerce Commission expresses that the 65th percentile reflects an updated assessment of the evidence, including consideration of regulatory changes that have reduced the risk of underinvestment.¹
6. The Commerce Commission used the loss analysis model developed by Oxera in 2014 to estimate empirically the cost and benefits of the WACC percentile. The Commerce Commission acknowledges that this model cannot provide a precise answer but is a useful guide for judgement. The Commerce Commission decision emphasises that the final outcome is judgment based.
7. In its 2014 *Amendment to the WACC percentile for the price quality regulation reasons paper*, the Commerce Commission defined the reasonable range between the 60th and 75th percentile, and their main analytical framework, produced by Oxera recommended a WACC between the 60th and 70th percentile.²
8. In the 2023 *Cost of Capital topic paper*, the Commerce Commission defined a reasonable range as between the 55th and 75th percentile. It is not clear to Horizon Networks how this range was calculated.
9. A submission on WACC produced by Oxera (who developed the 2014 model) for Aurora, Orion, Powerco, Unison, Vector, Wellington Electricity identified a WACC range of between the 65th and 75th percentile³. Despite assessing a higher WACC midpoint of the 70th percentile, Oxera recommended retaining a 67th percentile because of the value placed on regulatory certainty.

¹ Paragraph 4.13

² https://comcom.govt.nz/_data/assets/pdf_file/0029/88517/Commerce-Commission-Amendment-to-the-WACC-percentile-for-price-quality-regulation-Reasons-Paper-30-October-2014.PDF paragraph 6.46.2

³ https://comcom.govt.nz/_data/assets/pdf_file/0019/308503/27Big-Six27-EDBs-Oxera-report-Review-of-the-percentile-of-WACC-distribution-Submission-on-IM-Review-CEPA-report-31-January-2023.pdf executive summary,

10. Horizon Networks agrees that regulatory certainty has a high, unquantified value, particularly when EDBs are making long-term, generational investment decisions.
11. Regular minor, judgement-based adjustments to the WACC do not support evidence-based decision making. Instead, unnecessary, small judgement-based adjustments only undermine confidence in the stability of the regulatory regime. A decision to reduce the WACC to the 65th percentile does not promote the purpose of Part 4 because the decision to change risks incentivising under-investment due to increased uncertainty regarding the long-term stability of WACC percentiles.
12. Horizon Networks also notes that the arguments and reasonableness checks used by the Commerce Commission to support setting the WACC at the 65th percentile would equally apply to a decision to retain the WACC at the 67th percentile.
13. **Horizon Networks Recommends:** The Commerce Commission retain WACC at the 67th percentile. This will achieve the same benefits as the draft decision to set the WACC to the 65th percentile, while also signalling regulatory stability which is an important factor in long term investment decisions.

Reopeners should not be restrictive or exclusive

14. In the [CPPs and In-period adjustments topic paper](#) the Commerce Commission has decided to clarify that coverage of existing DPP system growth reopeners within the unforeseeable large project DPP reopener to not allow for applications that are driven by general growth.⁴
15. The rationale is that in the 2016 reasons paper it was inferred no general growth-based reopeners would be appropriate.
16. The Commerce Commission considers that system growth reopeners not relating to general growth are not required because:
 - System growth expenditure for specific growth from large individual connections is covered by Foreseeable or Unforeseeable major capex projects.⁵
 - Expenditure related to a change in network service requirements as a result of new or emerging technology is a Foreseeable or Unforeseeable major capex project reopeners.⁶
17. Horizon Networks is concerned that this decision will unnecessarily limit general growth-based reopeners when there are scenarios that may be appropriate.
18. For example, it is possible a future government may introduce incentive schemes for residential generation that causes significant demand for generation capacity that has not been forecast in the AMPs. This could be considered a growth-based reopener, as it is not related to a single large connection, and residential generation is neither a new nor emerging technology.
19. There is a low cost to retain the existing wording that allows for system growth within unforeseeable large project DPP reopener, and expectations can be tempered by issuing guidance similar to the 2016 decision indicating that there are unlikely to be many scenarios under which this type of reopener would apply.
20. Retaining the existing wording will promote the purpose of Part 4 by ensuring tools remain available to incentivise necessary investment to meet consumer demands while EDBs navigate increasing uncertainty around the exact pathway for New Zealand's energy future.
21. **Horizon Networks Recommends:** The Commerce Commission retain the ability to consider growth based unforeseeable major capex reopeners.
22. Additionally, the process to apply for a reopener, level of information and timeframes for the Commerce Commission to consider a reopener application remain unclear. This uncertainty makes it difficult for EDBs to make informed decisions regarding how to handle necessary and efficient expenditure that has not been allowed for within a DPP.

⁴ https://comcom.govt.nz/_data/assets/pdf_file/0025/318625/Part-4-IM-Review-2023-Draft-decision-CPPs-and-In-period-adjustments-topic-paper-14-June-2023.pdf paragraph 6.31.2

⁵ https://comcom.govt.nz/_data/assets/pdf_file/0025/318625/Part-4-IM-Review-2023-Draft-decision-CPPs-and-In-period-adjustments-topic-paper-14-June-2023.pdf paragraph 6.32.1

⁶ https://comcom.govt.nz/_data/assets/pdf_file/0025/318625/Part-4-IM-Review-2023-Draft-decision-CPPs-and-In-period-adjustments-topic-paper-14-June-2023.pdf paragraph 6.32.2

Horizon Networks supports retaining RAB indexation

23. In the [Financing and incentivising efficient expenditure during the energy transition topic paper](#) the Commerce Commission has decided to maintain RAB indexation for EDBs.
24. The rationale is that this provides a more efficient profile that approximates constant average real prices.
25. The Commerce Commission also notes that EDBs that face financeability risks and challenges due to an indexed RAB can apply for a customised price path (CPP) to meet their circumstances.
26. While Horizon Networks considers that a CPP is a very costly and blunt instrument that may not be suited to addressing a single issue such as financeability, Horizon Networks agrees that the Commerce Commission should retain its approach to requiring the indexation of RAB.

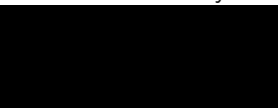
Horizon Networks notes an inconsistency between drafting and decision for RP03.4

27. In the [Report on the Input-methodologies review 2023 paper](#) paragraph 8.37 the Commerce Commission states its decision is to raise the existing thresholds that could apply to \$5 million for Vector Limited and Powerco Limited, or \$2.5 million for all other EDBs.
28. The decision is silent on if the alternative threshold of 1% of FNAR for the regulatory period will be retained, giving the reader the impression that this threshold has been removed. This impression is reinforced by earlier decisions such as paragraph 8.33 where the alternative threshold of 1% of FNAR for the regulatory period is included in the decision, even though this threshold does not change.
29. Reviewing the supporting papers [CPPs and In-period adjustments topic paper](#) and [Draft-Electricity-Distribution-Services-Input-Methodologies-IM-Review-2023-Amendment-Determination](#) it appears that the alternative threshold of 1% of FNAR for the regulatory period will be retained for Foreseeable and Unforeseeable large project reopeners.
30. **Horizon Networks Recommends:** The Commerce Commission update the [Report on the Input-methodologies review 2023 paper](#) paragraph 8.37 to clarify that the alternative threshold of 1% of FNAR for the regulatory period will be retained.
31. Horizon Networks does not support any change that will remove the alternative threshold of 1% of FNAR for the regulatory period for reopeners.

In conclusion Horizon Networks sees opportunities for the Commerce Commission to signal regulatory certainty through retaining existing WACC and providing a clearer path for reopeners

32. Horizon Networks supports the work the Commerce Commission has undertaken to review the input methodologies, as well as the technical analysis the ENA and our EDB peers have commissioned to communicate efficient inputs and outcomes as part of the IM review process.
33. While there are many areas of the decisions that given sufficient time and resource Horizon Networks could comment on, we wish to emphasise that positive consumer outcomes and incentives to make efficient investment decisions can be achieved through clarity and certainty.
34. In the context of the IM review decision this means:
 - Retaining the 67th percentile WACC – as there is no compelling evidence that the WACC percentile must change and there is a need to promote regulatory stability. Regulatory stability is an important factor in long term investment decisions.
 - Keeping the reopener tools as flexible as possible – to ensure the Commerce Commission can consider many unforeseen scenarios that impact an EDBs DPP.

Yours Sincerely


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