

Input methodologies review decisions

Topic paper 2: CPP requirements

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Associated documents

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20 December 2016	978-1-869455-43-9	Input methodologies review decisions: Summary paper
20 December 2016	978-1-869455-44-6	Input methodologies review decisions: Introduction and process paper
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20 December 2016	978-1-869455-45-3	Input methodologies review decisions: Topic paper 1 – Form of control and RAB indexation for EDBs, GPBs and Transpower
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20 December 2016	1178-2560	<i>Electricity Distribution Services Input Methodologies Amendments Determination 2016 [2016] NZCC 24</i>
20 December 2016	1178-2560	<i>Gas Distribution Services Input Methodologies Amendments Determination 2016 [2016] NZCC 25</i>
20 December 2016	1178-2560	<i>Gas Transmission Services Input Methodologies Amendments Determination 2016 [2016] NZCC 26</i>
20 December 2016	1178-2560	<i>Transpower Input Methodologies Amendments Determination 2016 [2016] NZCC 27</i>
20 December 2016	1178-2560	<i>Airport Services Input Methodologies Amendments Determination 2016 [2016] NZCC 28</i>
20 December 2016	1178-2560	<i>Airport Services Information Disclosure Amendments Determination 2016 [2016] NZCC 29</i>

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CONTENTS

EXECUTIVE SUMMARY	2
PURPOSE OF THIS PAPER.....	2
OVERVIEW OF THE CPP REQUIREMENTS TOPIC	2
SUMMARY OF CHANGES THAT ARE PART OF THE CPP REQUIREMENTS TOPIC	3
RELATIONSHIP WITH THE FINAL DECISION PACKAGE	9
CHAPTER 1: INTRODUCTION	10
PURPOSE OF THIS PAPER.....	10
WHERE THIS PAPER FITS IN TO OUR PACKAGE OF DECISIONS PAPERS	10
INTRODUCTION TO THIS TOPIC.....	11
STRUCTURE OF THIS PAPER.....	12
WHO DOES THIS PAPER APPLY TO?	13
CHAPTER 2: OVERVIEW OF THE DEFAULT/CUSTOMISED PRICE-QUALITY REGIME.....	14
PURPOSE OF THIS CHAPTER	14
STRUCTURE OF THIS CHAPTER	14
OVERVIEW AND EVOLUTION OF THE DEFAULT/CUSTOMISED PRICE-QUALITY REGIME.....	14
OVERVIEW OF THE CURRENT REGULATORY SETTINGS AND IM CHANGES.....	19
CHAPTER 3: IMPROVEMENTS TO THE WAY THE DPP AND CPP WORK TOGETHER.....	23
PURPOSE OF THIS CHAPTER	23
STRUCTURE OF THIS CHAPTER	23
EARLY EMERGING VIEWS	23
EMERGING VIEWS PAPER.....	23
DEVELOPING OUR EMERGING VIEWS.....	25
A MORE TAILORED APPROACH TO SETTING THE DPP WHERE THIS CAN BE DONE WITHOUT SIGNIFICANTLY INCREASING COST	25
‘SINGLE-ISSUE’ CPPS ARE NOT APPROPRIATE.....	26
EXPANDING THE ROLE OF DPP REOPENERS.....	27
REOPENERS NOT LINKED TO OUR EMERGING VIEWS.....	32
INTRODUCING A CPP REOPENER FOR CONTINGENT AND UNFORESEEN PROJECTS	33
APPROVAL OF COSTS INCURRED PRIOR TO CPP APPROVAL.....	34
EXPANDING THE RANGE OF PASS-THROUGH COSTS THAT CAN BE ADDED WHEN SETTING THE DPP	35
COSTS OF PREPARING A CPP	35
WE HAVE APPLIED THE PROPORTIONATE SCRUTINY PRINCIPLE IN CONTINUING TO REFINE THE CPP REQUIREMENTS AND IN ASSESSING CPP PROPOSALS.....	37
CHAPTER 4: EVALUATION OF CPP PROPOSALS	41
PURPOSE OF THIS CHAPTER	41
STRUCTURE OF THIS CHAPTER	41
OBJECTIVES FOR CPPS	41
HOW WE ASSESS CPP PROPOSALS	43
ASSESSMENT OF EXPENDITURE	44
EVALUATION OF PRICE PATH INFORMATION	47
EVALUATION OF QUALITY STANDARD VARIATION INFORMATION	47
CPP REQUIREMENTS THAT SUPPORT OUR EVALUATION USING THIS APPROACH.....	48
THE CPP SUBMISSION TIMELINE – HOW THE PROCESS COMES TOGETHER	53
SUMMARY OF IMPROVEMENTS TO THE CPP REQUIREMENTS.....	53
CHAPTER 5: INFORMATION REQUIREMENTS.....	56
PURPOSE OF THIS CHAPTER	56
STRUCTURE OF THIS CHAPTER	56
SUMMARY OF CHANGES	56

MISALIGNMENT BETWEEN REQUIREMENTS IN SCHEDULE D AND ID	57
CONSIDERING THE OVERALL DELIVERABILITY OF THE WORK PLAN	61
REMOVING DUPLICATION OF PRICE PATH INFORMATION.....	62
REDUCING THE LEVEL OF DISAGGREGATION OF INFORMATION	63
GREATER FLEXIBILITY AFFORDED WHEN PROVIDING INFORMATION	67
INFORMATION ON QUALITY STANDARDS.....	69
FURTHER IMPROVEMENTS TO INFORMATION REQUIREMENTS	70
CHAPTER 6: VERIFICATION REQUIREMENTS	72
PURPOSE OF THIS CHAPTER	72
STRUCTURE OF THIS CHAPTER	72
SUMMARY OF CHANGES	72
VERIFIER’S PURPOSE AND ROLE.....	73
COMMUNICATION BETWEEN THE APPLICANT AND VERIFIER.....	77
NUMBER OF IDENTIFIED PROGRAMMES	78
ROLE OF THE INDEPENDENT ENGINEER.....	80
VERIFICATION OF NON-STANDARD DEPRECIATION, COST ALLOCATION AND INSURANCE INFORMATION.....	81
OTHER ISSUES RAISED BY STAKEHOLDERS	82
CHAPTER 7: AUDIT REQUIREMENTS.....	85
PURPOSE OF THIS CHAPTER	85
STRUCTURE OF THIS CHAPTER	85
SUMMARY OF PROPOSED CHANGES	85
POLICY INTENT OF THE AUDIT REQUIREMENTS.....	85
CLARIFYING THE ROLE OF THE AUDITOR WITH RESPECT TO FINANCIAL, NON-FINANCIAL, AND FORECAST INFORMATION.....	86
AUDIT REQUIREMENTS CONTAIN UNCLEAR OR AMBIGUOUS TERMINOLOGY WHICH CAN CONFUSE THE ROLE OF THE AUDITOR	89
LACK OF EXPLICIT REQUIREMENT FOR AUDITOR TO PROVIDE AUDIT REPORT.....	91
ROLE IN REVIEWING COST ALLOCATION INFORMATION.....	91
CHAPTER 8: CONSUMER CONSULTATION REQUIREMENTS	92
PURPOSE OF THIS CHAPTER	92
STRUCTURE OF THIS CHAPTER	92
SUMMARY OF CHANGES	92
INTENT OF THE CONSUMER CONSULTATION REQUIREMENTS	92
FEEDBACK IDENTIFIED WE SHOULD FURTHER CLARIFY OUR EXPECTATIONS CONCERNING CONSUMER CONSULTATION.....	93
ATTACHMENT A: INDICATIVE CPP APPLICATION PROCESS DIAGRAM.....	98
PURPOSE OF THIS ATTACHMENT	98
KEY CONSIDERATIONS IN USING THE DIAGRAM.....	98
ATTACHMENT B: SUMMARY OF THE REVIEW OF CPP IMS	100
PURPOSE OF THIS ATTACHMENT	100
RELATIONSHIP WITH THE REPORT ON THE IM REVIEW.....	100
WHY WE HAVE PRESENTED OUR DECISIONS IN RESPECT OF THE CPP IMS SEPARATELY.....	100
STRUCTURE AND FORMAT OF THIS ATTACHMENT.....	101
REVIEW OF EXISTING DECISIONS RELATING TO THE CONTENT OF CPP APPLICATIONS	102
REVIEW OF EXISTING DECISIONS RELATING TO PROCESSES FOR CPP PROPOSALS.....	111
REVIEW OF EXISTING DECISIONS RELATING TO PROCESSES FOR ASSESSING AND EVALUATING CPP PROPOSALS	116
REVIEW OF EXISTING DECISIONS RELATING TO PROCESSES FOR DETERMINING A CPP	116

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Executive summary

Purpose of this paper

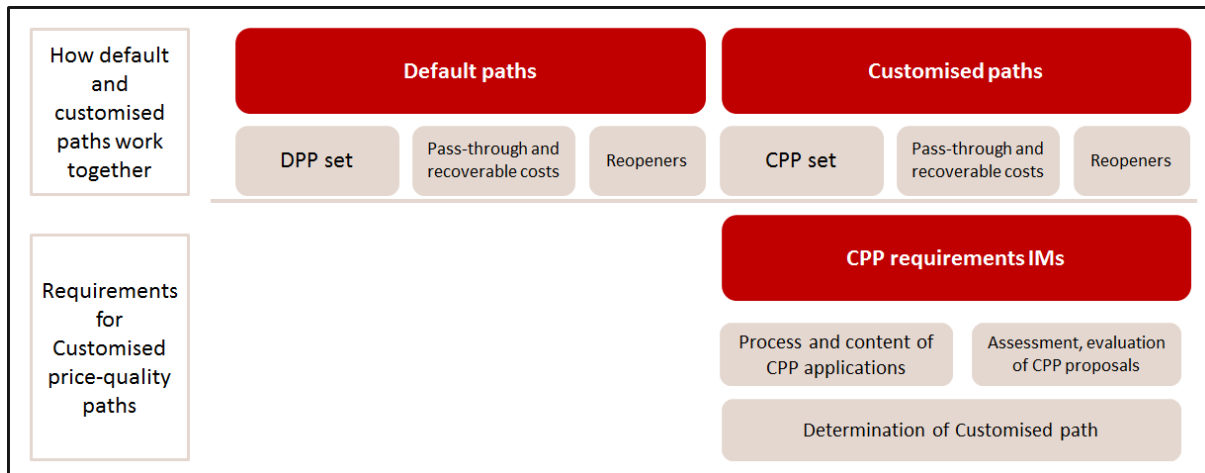
- X1. The purpose of this paper is to set out:
- X1.1 our views on the default/customised price-quality regime – including how default and customised paths work together, and changes to areas where improvements can be made; and
 - X1.2 our changes to the detailed requirements for customised price-quality paths (**CPPs**) set out in the input methodologies (**CPP requirements**).
- X2. This paper relates to electricity distribution businesses (**EDBs**) and gas pipeline businesses (**GPBs**) that are subject to price-quality regulation.
- X3. However, at this stage, we have not considered changes to the CPP requirements specific to GPBs that set out the information that is required to be included in a CPP proposal.¹

Overview of the CPP requirements topic

- X4. The review of the input methodologies (**IMs**) has provided us with an opportunity to consider what improvements can be made to how we implement the default/customised price-quality regime, as well as the specific requirements for CPPs. In particular, we have considered:
- X4.1 How default price-quality paths (**DPPs**) and CPPs work together — when setting the initial IMs in 2010, we did not have practical experience of how the two mechanisms would interact.
 - X4.2 Specific improvements to the CPP requirements — utilising experience with the first CPP proposal, and taking account of developments in information disclosure since the IMs were set in 2010.
- X5. Figure X1 illustrates the two different levels of this review and the components involved.

¹ As noted at paragraph 34 of this paper, we have not yet reached draft decisions on the CPP information requirements for gas pipeline businesses. This work remains within the IM review and we are currently planning to have a final decision for this work by quarter four of 2017.

Figure X1: Overview of the components of the review of CPP requirements topic



X6. This paper follows our consultation on this topic:

- X6.1 Topic 8 of our IM review problem definition paper in June 2015.
- X6.2 CPP fast track amendments in November 2015.
- X6.3 Emerging views paper in February 2016 on opportunities to improve the way DPPs and CPPs work together.
- X6.4 Technical workshop on CPP information requirements in April 2016.
- X6.5 Our draft decisions on the IM review.²
- X6.6 The technical consultation update paper we put out in October 2016.

Summary of changes that are part of the CPP requirements topic

- X7. The changes explained in this topic paper are in the context of our view that fundamentally the underlying intent of our IMs for the DPP/ CPP regime remains sound. We consider the IM changes we have made to be improvements aimed at giving better effect to this intent.
- X8. Accordingly, the majority of our changes are to reduce cost and complexity, and improve the certainty provided by how we specify the IMs.

² Commerce Commission "Input methodologies review draft decisions – Consolidated package of 16 June 2016 draft decisions papers" (16 June 2016).

- X9. A summary of the changes is set out in the series of tables X1-X5 that follow. Note, the change to align the DPP and CPP weighted average cost of capital (**WACC**) is explained in the cost of capital topic paper and included in Table X1 for summary purposes only.³

³ Commerce Commission "Input methodologies review decisions: Topic paper 4 – Cost of capital issues" (20 December 2016).

Table X1: Summary of changes in relation to how DPPs and CPPs work together

Topic	Change	Reason for the change	Chapter
Quality-only CPP	Option for EDBs to apply for a quality-only CPP removed and replaced by a quality standard DPP reopener.	Reduced cost and complexity – suppliers are able to apply for a variation to their quality standards without the full cost of the CPP process. This also accounts for practical difficulties in assessing and evaluating 'single-issue' CPPs.	Chapter 3
Pass-through costs	Certain pass-through costs may be specified in advance for the forthcoming DPP period as part of the DPP reset process – no longer restricted to specifying these costs during the affected regulatory period.	Reduced cost and complexity – allows a greater number of pass-through costs to be specified through a DPP or CPP determination where the cost is outside of the control of the supplier, instead of requiring a change to the IMs.	Chapter 3
Prudently incurred expenditure	Allowing the recovery of prudently incurred costs, in response to an urgent project, between when a CPP is applied for and when it comes into effect. We have also extended the capex wash-up mechanism to CPPs.	Promotes the purpose of Part 4 – creates incentives to invest where urgent work is needed while the Commission is assessing a CPP proposal.	Chapter 3
CPP contingent projects	Allowing the CPP to be reopened for contingent and unforeseen projects, for EDBs and GDBs.	Promotion of the purpose of Part 4 – provides incentives for suppliers to innovate and invest by allowing a mechanism for the consideration of large incremental expenditure (to be approved where appropriate) in addition to the expenditure originally provided for in a CPP.	Chapter 3
Difference in DPP and CPP WACC rates	A single WACC should apply to all suppliers on DPPs and CPPs for the duration of each DPP regulatory period.	Promotion of the purpose of Part 4 – removing the separate WACC for CPPs so we do not dis-incentivise CPPs where they are in the long-term benefit of consumers or perversely incentivise CPPs where WACC increases.	Topic paper 4 – Cost of capital issues

Table X2: Summary of changes to information requirements for EDBs

Topic	Change	Reason for the change	Chapter
Modifications and exemptions	Exemption and modification provisions (completed November 2015 as part of IM review) explicitly specify scale as a potential consideration in the approval of exemption and modification requests. This change also applies to GPBs.	Additional certainty – now clear that Commission considers scale an important consideration in allowing CPP applicants to reduce the cost of preparing CPP application by applying for modifications and exemptions to the existing requirements.	Chapter 5
Duplication	Removing the need to duplicate information between documents, by aligning Schedules D and E with the relevant information disclosure requirements.	Reduced cost and complexity – applicants able to rely more on already existing information when making a CPP proposal.	Chapter 5
Deliverability	Including new requirements for a deliverability plan for the proposed expenditure; and improving the way in which applicants demonstrate the deliverability of their proposed expenditure with existing requirements.	Additional certainty – deliverability expectations now clearer for applicants upfront.	Chapter 5
Level of disaggregation	Reducing the level of disaggregation required for certain information requirement – such as, related party transactions, capital contributions, depreciation and tax.	Reduced cost and complexity – applicants are no longer required to provide information at a more detailed level.	Chapter 5
Alignment with ID	Aligning the information requirements with EDBs' information disclosure requirements – such as the qualitative and quantitative information required in Schedules D and E.	Reduced cost and complexity – applicants are not required to reformat information already provided under ID, to comply with the CPP information requirements.	Chapter 5
Quality standard variation information	Updating the information requirements for when a supplier proposes a quality standard variation as part of a CPP proposal, to reflect how we currently set quality standards.	Promotes the purpose of Part 4 – ensures that we have the quality information to set CPP quality standards that deliver long term benefits to consumers.	Chapter 5

Table X3: Summary of changes to verification requirements

Topic	Change	Reason for the change	Chapter
Role and purpose	Adding a new section to the verifier's terms of reference in Schedule G of the IMs that defines the verifier's role, purpose, and obligations.	Additional certainty – both applicant and verifier have more information upfront on the verifier's role in the verification process.	Chapter 6
High level summary	Requiring the CPP applicant to provide us with a high level summary of their application by the time the verifier is engaged. Applicants will also have the option of providing this information by way of a workshop, with our agreement.	Reduced cost and complexity – contributes towards a more efficient process by allowing us information upfront to better prepare for the type of CPP proposal being developed.	Chapter 6
Communication protocol	Amending the tripartite deed requirements in Schedule F5 to include a communication protocol that sets out the roles and obligations of the parties during the verification process, and to allow meeting minutes to be used as the evidential basis for any verifier technical opinions.	Additional certainty – provides certainty to applicant that they can have confidence that they can engage openly with the verifier in the knowledge we will not view draft material.	Chapter 6
Flexibility in number of identified programmes	Allowing the verifier greater flexibility in the number of identified programmes that are selected to be verified in detail as part of the verification process.	Reduced cost and complexity – applicants not required to artificially allocate expenditure into projects and the verifier can focus detailed assessment on the most material parts of a CPP proposal.	Chapter 6
Non-standard depreciation and cost allocation	Removing the obligation for the verifier to consider non-standard depreciation and cost allocation.	Reduced cost and complexity – verifier no longer required to assess an area where its expert opinion adds little value.	Chapter 6
Removal of independent engineer	Removing requirement for an independent engineer, and allowing suppliers to prepare the quality standard variation report themselves, subject to verification by the verifier (EDBs only).	Reduced cost and complexity – removing need for separate roles where a verifier is likely to be able to provide an appropriate opinion on any quality standard variation.	Chapter 6

Table X4: Summary of changes to audit requirements

Topic	Change	Reason for the change	Chapter
Audit report	Clarifying the requirement for the auditor to provide a report with the auditor's opinion on specified matters.	Additional certainty – now clear the auditor must provide a report as part of the audit process.	Chapter 7
Clarified role – historical v forecast data	Differentiating the role of the auditor with respect to <i>historical</i> financial information and <i>forecast</i> financial information.	Additional certainty – now clear the specific type of assurance the auditor is expected to provide in respect of different types of information.	Chapter 7
Spreadsheets	Removing ambiguity around quantitative information provided in spreadsheets.	Additional certainty – now clear the specific type of assurance the auditor is expected to provide in respect of different types of information.	Chapter 7
Proper records	Clarifying the requirement on the auditor to provide a view in respect of proper records being kept.	Additional certainty – the scope of audit requirements is now clearer.	Chapter 7
Auditing cost allocation	Clarifying our expectations from the auditor regarding cost allocation information.	Additional certainty – the scope of audit requirements is now clearer.	Chapter 7

Table X5: Summary of changes to consumer consultation requirements

Topic	Change	Reason for the change	Chapter
Price-quality impact of alternative investment options	Amending the consumer consultation IMs to require CPP applicants to notify consumers of the price and quality impact of key alternative investment options in their CPP proposal, and why any proposed quality standard variation has been chosen.	Additional certainty – applicants have more information upfront on our expectations for the consumer consultation process.	Chapter 8
Verifier's view	In support of the change set out above, we have amended the verifier Terms of Reference in Schedule G of the IMs to require the verifier to report on the extent and effectiveness of the applicant's consumer consultation.	Reduced cost and complexity – contributes towards a more efficient process by allowing assessment of applicant's consumer consultation earlier in the process.	Chapter 8

Relationship with the final decision package

X10. This topic paper forms part of our package of decisions papers on the IM review. As part of the package of papers, we have also published:

X10.1 a summary paper of our decisions;

X10.2 an introduction and process paper which provides an explanation of how the papers in our decisions package fit together;

X10.3 a framework paper, which explains the framework we have applied in reaching our decisions on the IM review; and

X10.4 amendment determinations, which give effect to our decisions.

Chapter 1: Introduction

Purpose of this paper

1. The purpose of this paper is twofold. It sets out:
 - 1.1 our views on the default/customised price-quality regime – including how default and customised paths work together, and areas where improvements might be made; and
 - 1.2 our changes to the requirements for customised price-quality paths (**CPPs**) set out in the input methodologies (**CPP requirements**).
2. In respect of the CPP requirements, it explains:
 - 2.1 the problems we have identified within this topic area;
 - 2.2 our solutions to these problems;
 - 2.3 the reasons for our solutions; and
 - 2.4 how we have taken stakeholders' submissions into account in considering the above.

Where this paper fits in to our package of decisions papers

3. This topic paper forms part of our package of final decision papers on the input methodology review. For an overview of the package of papers and an explanation of how they fit together, see the Introduction and process paper published as part of our decision package.⁴
4. To the extent our solutions involve changes to the input methodologies (**IMs**), this paper explains how we have changed our previous IM decisions to account for our solutions to problems within this topic area.
5. Our drafting changes to the IMs, including any resulting from this topic area, are shown in the amended determinations.
6. The framework we have applied in reaching our decisions on the IM review is set out in a separate paper, published alongside this paper.⁵ The framework paper explains that we have only changed the IMs where it is likely to:
 - 6.1 promote the Part 4 purpose in s 52A more effectively;

⁴ Commerce Commission "Input methodologies review decisions: Introduction and process paper" (20 December 2016).

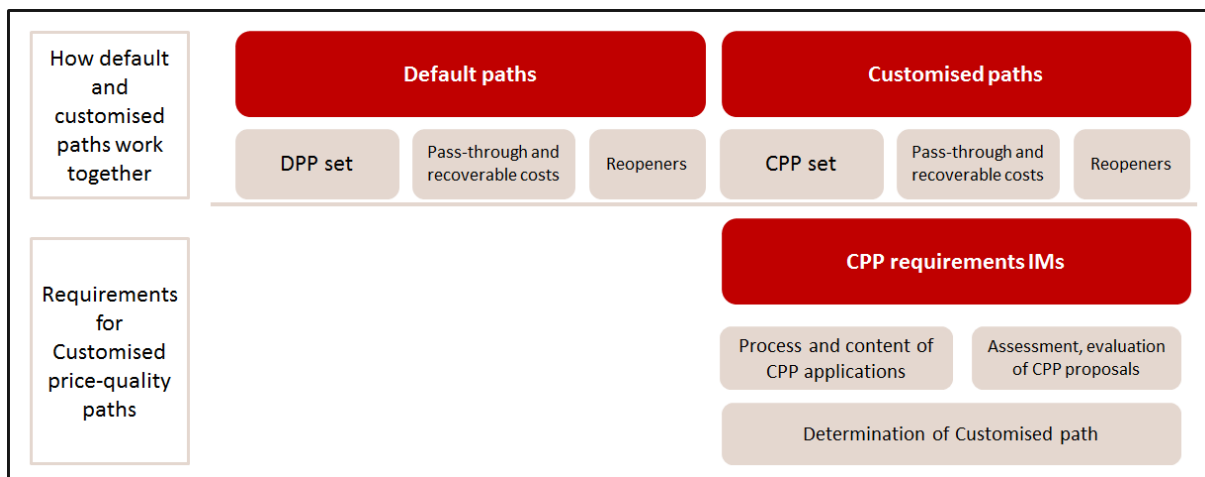
⁵ Commerce Commission "Input methodologies review decisions: Framework for the IM review" (20 December 2016).

- 6.2 promote the IM purpose in s 52R more effectively (without detrimentally affecting the promotion of the s 52A purpose); or
 - 6.3 significantly reduce compliance costs, other regulatory costs or complexity (without detrimentally affecting the promotion of the s 52A purpose).
7. The framework paper also describes key economic principles that can provide guidance as to how we might best promote the Part 4 purpose.

Introduction to this topic

8. While Part 4 (**Part 4**) of the Commerce Act 1986 (the **Act**) specifies at a high level how the regime functions, it also gives significant discretion as to how we design and set the default price-quality path (**DPP**) and CPP mechanisms.
- 8.1 The DPP is the low-cost arm of DPP/ CPP regulation. We are required to set a low-cost default path for all suppliers.
 - 8.2 The CPP offers suppliers the opportunity to propose a price-quality path that better meets their individual circumstances.
9. This topic paper considers both a regime level view of how default and customised paths work together, and the specific IM requirements for customised paths. Figure 1.1 illustrates the two different levels of this review and the different components involved.

Figure 1.1: Overview of the components of the default customised price-quality regime



10. This paper follows our consultation on this topic:
- 10.1 Topic 8 of our IM review problem definition paper in June 2015.⁶
 - 10.2 CPP fast track amendments in November 2015.⁷

⁶ Commerce Commission "Invitation to contribute to problem definition" (16 June 2015).

- 10.3 Emerging views paper in February 2016 on opportunities to improve the way DPPs and CPPs work together.⁸
 - 10.4 Technical workshop on CPP information requirements in April 2016.
 - 10.5 Our draft decision on the IM review.⁹
11. Note, the CPP fast track amendment process originally considered issues relating to the differences in WACC between DPP and CPP. These issues were discontinued as part of the fast track process in October 2015 and have been considered alongside other cost of capital issues as part of the main IM review. This paper includes the changes for this issue in summary form as it is an important feature of the total package of improvements to how the DPP and CPP work together. The cost of capital paper provides detailed discussion of the specific issue and our solution.¹⁰

Structure of this paper

- 12. The first part of the paper sets out the context for the default/customised price-quality regime (Chapter 2), and the opportunities for improvements we have taken as part of the review (Chapter 3).
- 13. In the second part of this paper we introduce the solutions to the problems that we have identified with the CPP requirements. This includes IM changes that are designed to improve the CPP process, by increasing clarity and removing unnecessary cost and complexity. We focus on each of the key requirements of a CPP proposal in individual chapters:
 - 13.1 evaluation of proposals (Chapter 4);
 - 13.2 information requirements (Chapter 5);
 - 13.3 verification requirements (Chapter 6);
 - 13.4 audit requirements (Chapter 7); and
 - 13.5 consumer consultation requirements (Chapter 8).
- 14. These specific CPP discussions are part of a broader, iterative, longer term set of refinements we will continue to make to the DPP/ CPP regime as our experience

⁷ Commerce Commission "Amendments to input methodologies for customised price-quality paths – Final reasons paper for Limb 1 of the CPP fast track" (12 November 2015).

⁸ Commerce Commission "Emerging views on opportunities to improve the way default and customised price-quality paths work together" (29 February 2016).

⁹ Commerce Commission "Input methodologies review decisions: Topic paper 2 – CPP requirements" (16 June 2016).

¹⁰ Commerce Commission "Input methodologies review draft decisions: Topic paper 4 – Cost of capital issues" (16 June 2016).

grows and we complete more CPPs. Importantly, not all of these refinements will come through IM changes, but will also occur through improving our engagement with prospective and actual CPP applicants.

15. There are two attachments to this paper:
 - 15.1 Attachment A – sets out the high level process of CPP preparation and evaluation;
 - 15.2 Attachment B – explains, in respect of each CPP requirement IM decision, whether/how we have changed it and why/why not.

Who does this paper apply to?

16. This paper applies to:
 - 16.1 electricity distribution businesses (**EDBs**) that are subject to price-quality regulation; and
 - 16.2 gas pipeline businesses (**GPBs**), although at this stage, we have not made changes to the detailed information requirements for either gas distribution businesses (**GDBs**) or gas transmission businesses (**GTBs**).¹¹

¹¹ We have not yet reached draft decisions on the CPP information requirements IMs for gas pipeline businesses. Further discussion on this matter is found at para 34.

Chapter 2: Overview of the default/customised price-quality regime

Purpose of this chapter

17. This chapter provides an overview of the default/customised price-quality regime (**DPP/ CPP regime**), and summarises, at a high level, our view of the current regulatory settings, including the changes we have made as part of the IM review.

Structure of this chapter

18. This chapter is split into two sections:
- 18.1 overview and evolution of the DPP/ CPP regime; and
 - 18.2 overview of the current regulatory settings and the IM changes we have made.

Overview and evolution of the default/customised price-quality regime

19. This section illustrates how the default/customised regime has evolved over time, and can continue to evolve as our experience develops.

The legislative context for DPP/ CPP regulation

20. Electricity distributors, gas distributors, and gas transmission businesses are subject to default/customised price-quality regulation under Part 4.¹²
21. The purpose of default/customised price-quality regulation is:¹³
- To provide a relatively low-cost way of setting price-quality paths for suppliers of regulated goods or services, while allowing the opportunity for individual regulated suppliers to have alternative price-quality paths that better meet their particular circumstances.
22. There are also a number of other key statutory considerations specific to default and customised paths that we must take account of when setting default paths and the requirements for customised paths. These are set out in the table overleaf.

¹² Some electricity distributors are exempt from default/customised price-quality regulation where they meet the requirements set out in s 54G of the Act.

¹³ Commerce Act 1986, s 53K.

Table 2.1: Key statutory characteristics of DPPs and CPPs

DPP (as set)	DPP pass-through/ recoverable costs	DPP reopener (reconsideration)	CPP (as set)	CPP pass-through/ recoverable costs	CPP reopener (reconsideration)
<ul style="list-style-type: none"> • Relatively low-cost. • Commerce Commission (CC) bears the cost of determination (passed on to industry through general levies). • Section 53P limitations on how the CC sets a DPP – eg, restriction on benchmarking. • IMs must specify key inputs, eg, asset valuation, cost of capital. • 4-5 year regulatory period. 	<ul style="list-style-type: none"> • Costs that can be passed through to prices must be specified in the IMs. 	<ul style="list-style-type: none"> • Circumstances in which DPPs can be reconsidered within a regulatory period must be specified in the IMs. • Only affects path for the remainder of the DPP period. • Should generally accommodate issues affecting multiple suppliers (4+) that arise after the DPP is set (per High Court in Wellington International Airport Ltd & Ors v CC). • Potentially supplier, CC, or consumer initiated. • We bear the cost of reconsidering the DPP (passed onto industry through levies). 	<ul style="list-style-type: none"> • IMs must set out relevant scrutiny requirements and key inputs. • New regulatory period can be 3-5 years. • Only suppliers can apply and only once during a DPP period. • Cannot withdraw CPP proposal once submitted. • CC can agree with supplier on IM variations. • Applicant bears the cost of determining CPP. • CPP can extend across two DPP periods. 	<ul style="list-style-type: none"> • Costs that can be passed through to prices must be specified in the IMs. 	<ul style="list-style-type: none"> • Circumstances in which CPPs can be reconsidered within a regulatory period must be specified in the IMs. • Changes will only affect path for the remainder of the CPP period. • Potentially supplier, CC, or consumer initiated.

23. Within the bounds of Part 4, taking into account the statutory considerations above, there remains significant discretion for how we give effect to default and customised paths. This discretion includes how we set the IMs that underpin default/customised regulation, but also includes a number of other processes outside the IMs. For example:
- 23.1 periodic resets of default paths;
 - 23.2 mid-period reconsideration of price paths triggered by reopener provisions; and
 - 23.3 general engagement and guidance in reset processes and during the regulatory period.

Our approach to setting default paths has evolved over time

24. To set a default path we must set starting prices for each supplier based on the range of circumstances that we consider appropriate for default paths,¹⁴ noting that suppliers have the option to apply for a customised path where the default path does not meet their particular circumstances.
25. Over time both our approach to setting starting prices and the range of circumstances we have considered in setting default paths has changed. For example:
- 25.1 When we first set the IMs for default paths, we determined that a fairly simple ‘banded return on investment’ approach would likely be an appropriate low-cost approach to setting starting prices.¹⁵ However, we subsequently decided that the greater accuracy offered under a ‘building blocks’ approach was likely to better promote the s 52A purpose, when we reset the 2010-2015 DPP for EDBs after setting the IMs.¹⁶
 - 25.2 Since we first set the default path for EDBs in 2009 we have increased the range of supplier-specific circumstances taken into account in subsequent default paths, while maintaining the relatively low-cost purpose of the DPP. These include reopeners for catastrophic and change events, and an expanded range of recoverable and pass-through costs.¹⁷

¹⁴ That is, taking into account the low-cost purpose of DPP/CPD regulation and the outcomes sought more broadly under the purpose of Part 4.

¹⁵ A banded approach sets prices based on whether the supplier’s return on investment falls within a band of return values considered to be appropriate.

¹⁶ A building block approach to setting prices relies on an estimation of different costs faced by a supplier to keep network running, and uses these different components to forecast the revenue and prices that an efficient supplier would require.

¹⁷ We initially only allowed a DPP to be reopened for either an error, or misleading information.

Lessons from setting the first customised path

26. Setting a customised path naturally lends itself to a more intensive and complex process when compared to the default path.¹⁸ To support this process we are required to set the requirements for customised path applications as IMs.
27. When we originally set the CPP requirement IMs in 2010, our aim was to adopt a cost-effective approach, which still allowed us to apply an appropriate level of scrutiny to effectively assess the CPP proposal. Some of the areas we considered at the time included:¹⁹
 - 27.1 building on information that is required under information disclosure obligations;
 - 27.2 targeting the provision of more detailed information on proposed expenditure that is expected to be material to the proposal;
 - 27.3 generally, only requiring information on proposed expenditure that is consistent with the level of detail that would be expected to already be held in a well-run, well-governed business;
 - 27.4 focussing on requiring information that would be required for all CPP proposals;
 - 27.5 allowing some flexibility in how the applicant engages with consumers prior to submitting a proposal; and
 - 27.6 including audit and verification requirements, only where audit and verification will add value.
28. While we set the CPP requirements with these considerations in mind, we acknowledged that there would be need for refinements to the requirements as our experience with CPPs grew and the regime developed.²⁰
29. To date we have only set one CPP, which was for Orion New Zealand Limited (Orion), in 2013. Following Orion's CPP, we asked for feedback on the determination

¹⁸ For example, the Act requires us to specify verification, consumer consultation, and information requirements.

¹⁹ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), at 9.2.5.

²⁰ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), at 9.2.8.

process.²¹ This feedback has informed our problem definitions and the CPP changes that are explained in this topic paper.²²

We intend to continue to refine the regime over time

30. As highlighted by the changes we have made that are explained in this paper, there are opportunities for improvement in the DPP/ CPP regime. While we consider that the changes we have made go some way to improving the regime, we do not consider that these changes made as part of the IM review will eliminate the need for future changes.
31. This is in part because some issues and solutions lie outside of the IMs, but also because we do not consider that there is a single optimal setting for the DPP/ CPP regime that will hold true over time.
32. As we continue to reset DPPs and receive CPP proposals we will identify further opportunities for improvement and continue to refine our solutions to issues. Longer term we also expect there to be scope for change to suit a landscape where we have better knowledge of performance and are able to rely more on existing information.
33. In the short term, we intend to continue to evolve the regime by increasing consideration of supplier-specific circumstances in the default path where possible, and reducing the cost and complexity of the CPP process.

Areas for further work

34. We have not yet reached decisions on the CPP information requirements IMs for GPBs. This work remains within the IM review and we are currently planning to have a final decision for this work by quarter four of 2017.²³ We will continue to keep stakeholders updated on this process. As noted in our 29 February 2016 process update paper the reasons why this work has not been included in our current decisions on IMs are:²⁴
 - 34.1 there are no GDBs contemplating a CPP application in the near future;
 - 34.2 the GTB will be in a better position to engage next year as it will provide more time for it to establish an understanding of the business demands following the recent ownership change; and

²¹ A summary of this feedback, as well as individual submissions, is available at:

<http://www.comcom.govt.nz/regulated-industries/electricity/cpp/orion-cpp/>.

²² Commerce Commission "Input methodologies review invitation to contribute to problem definition" (16 June 2015) at para 416-435; and [Commerce Commission "Summary of feedback on Orion customised price-quality path process" \(4 August 2014\)](#).

²³ Commerce Commission "Input methodologies review – Process update paper" (14 September 2016).

²⁴ Commerce Commission "Input methodologies review – Process update paper" (29 February 2016) at para 59-65.

- 34.3 the modification and exemptions provisions will allow for flexibility if needed in the interim.

Overview of the current regulatory settings and IM changes

35. In presenting our final decisions for the IM review, we think it is useful to explain how we have approached the review of the CPP requirements, in addition to the IM review framework, and provide a summary of our findings to help illustrate where we currently sit in the development of the DPP/ CPP regime.

The intent of the IMs underlying the default/customised regime remains sound

36. The review of the IMs has provided us with an opportunity to consider what improvements can be made to the DPP/ CPP regime.
37. In particular, we have considered:
- 37.1 how DPPs and CPPs complement each other. When setting the initial IMs in 2010, we did not have the experience of how these would work together in practice; and
 - 37.2 specific improvements we can make to the CPP regime, based on our experience in processing the first CPP proposal, and how we have implemented other regulatory instruments under Part 4 (eg, information disclosure) since setting the initial IMs in 2010.
38. To provide context for our changes, we consider it important to provide our view of the package of IMs underlying the DPP/ CPP regime.
39. Our view is that fundamentally the IMs for DPPs and CPPs are sound, and our changes are incremental improvements aimed at giving better effect to our intent since setting the IMs in 2010.
40. For default paths, we consider the current building blocks approach, and range of supplier-specific circumstances we are able to take account of, strikes an appropriate balance between its relatively low-cost intent and the outcomes sought by Part 4. We set out our views on how our approach to setting default paths meets the purpose of Part 4 in our Main Policy paper for the 2015-2020 default price-quality paths for electricity distributors.²⁵
41. For customised paths, we consider that they remain a viable alternative for suppliers who consider the default path does not meet their particular circumstances. This is illustrated in setting a customised path for Orion in 2013.
42. The Orion experience was potentially the most difficult first-up test the CPP regime could have had – a catastrophic event requiring a substantial network rebuild.

²⁵ Commerce Commission "Default price-quality paths for electricity distributors from 1 April 2015 to 31 March 2020 – Main policy paper" (28 November 2015).

Despite time pressures and teething issues with the CPP process, we were able to successfully set a path for Orion.

43. We have confidence that future CPP processes will benefit from this experience to run more smoothly, and while we could face a CPP under similar circumstances in the future, we do not expect that a typical CPP proposal would face these issues to the same extent.

Summary of IM changes

44. Table 2.2 presents, at a high level, the package of IM changes we have made to the DPP/ CPP regime.
45. Note that the table is intended to be a summary only and the individual changes are discussed in more detail in the chapters that follow. The exception is the change to remove the separate WACC for CPPs which is explained in the Cost of capital topic paper.²⁶

Table 2.2: Summary of package of IM changes to the default/customised regime

How DPP and CPP work together	
Quality-only CPP	Option for EDBs to apply for a quality-only CPP removed and replaced by a quality standard DPP reopener.
Pass-through costs	Certain pass-through costs may be specified in advance for the forthcoming DPP period as part of the DPP reset process – no longer restricted to specifying these costs during the affected regulatory period.
Prudently incurred expenditure	Allowing the recovery of prudently incurred costs, in response to an urgent project, between when a CPP is applied for and when it comes into effect. We have also extended the capex wash-up mechanism to CPPs.
CPP contingent projects	Allowing the CPP to be reopened for contingent and unforeseen projects, for EDBs and GDBs.
Difference in DPP and CPP WACC rates	A single WACC will apply to all suppliers for the duration of each DPP regulatory period. We have removed the CPP WACC and will reopen CPPs that straddle DPP regulatory periods to take account of the new DPP WACC rate. The reopener is applied mechanically for the sole purpose of taking account of the change in WACC.
Information requirements for EDBs	
Modifications and exemptions	Exemption and modification provisions (completed November 2015 as part of IM review) explicitly specify scale as a potential consideration in the approval of exemption and modification requests. This change also applies to GPBs
Duplication	Removing the need to duplicate information between documents, by aligning Schedules D and E with the relevant information disclosure requirements.

²⁶ Commerce Commission "Input methodologies review decisions: Topic paper 4 – Cost of capital issues" (20 December 2016).

Deliverability	Including new requirements for a deliverability plan for the proposed expenditure; and improving the way in which applicants demonstrate the deliverability of their proposed expenditure with existing requirements.
Level of disaggregation	Reducing the level of disaggregation required for certain information requirement – such as, related party transactions, capital contributions, depreciation and tax.
Alignment with ID	Aligning the information requirements with EDBs' information disclosure requirements – such as the qualitative and quantitative information required in Schedules D and E.
Quality standard variation information	Updating the information requirements for when a supplier proposes a quality standard variation as part of a CPP proposal, to reflect how we currently set quality standards.
Verifier	
Role and purpose	Adding a new section to the verifier's terms of reference in Schedule G of the IMs that defines the verifier's role, purpose, and obligations.
High level summary	Requiring the CPP applicant to provide us with a high level summary of their application by the time the verifier is engaged. Applicants will also have the option of providing this information by way of a workshop, with our agreement.
Communication protocol	Amending the tripartite deed requirements in Schedule F5 to include a communication protocol that sets out the roles and obligations of the parties during the verification process regarding communication and to allow meeting minutes to be used as the evidential basis for any verifier technical opinions.
Flexibility in number of identified programmes	Allowing the verifier greater flexibility in the number of identified programmes that are selected to be verified in detail as part of the verification process.
Non-standard depreciation and cost allocation	Removing the obligation for the verifier to consider non-standard depreciation and cost allocation.
Removal of independent engineer	Removing requirement for an independent engineer, and allowing suppliers to prepare the quality standard variation report themselves, subject to verification by the verifier (EDBs only).
Audit	
Audit report	Clarifying the requirement for the auditor to provide a report setting out the auditor's opinion on specified matters.
Clarified role – historical v forecast data	Differentiating the role of the auditor with respect to <i>historical</i> financial information and <i>forecast</i> financial information.
Spreadsheets	Removing ambiguity around quantitative information provided in spreadsheets.
Clarified role – proper records	Clarifying the requirement on the auditor to provide a view in respect of proper records being kept.
Role in auditing cost allocation	Clarifying our expectations from the auditor regarding cost allocation information.

Consumer consultation	
Price-quality impact of alternative investment options	Amending the consumer consultation IMs to require CPP applicants to notify consumers of the price and quality (EDBs) impact of key alternative investment options in their CPP proposal, and why any proposed quality standard variation has been chosen.
Verifier's view	In support of the change proposed above, we propose amending the verifier Terms of Reference in Schedule G of the IMs to require the verifier to report on the extent and effectiveness of the applicant's consumer consultation.

46. The majority of these changes are to reduce cost and complexity, and to improve the certainty provided by how we specify the IMs.
47. There are also a number of other areas of work outside the IMs discussed in this paper that can be considered improvements to the default/customised regime that are not represented in Table 2.2. These include:
- 47.1 greater tailoring for individual suppliers when setting default paths; and
 - 47.2 upfront engagement and additional guidance for intending CPP applicants.

Chapter 3: Improvements to the way the DPP and CPP work together

Purpose of this chapter

48. This chapter explains a number of changes that we have made to improve the way default and customised price-quality paths work together.

Structure of this chapter

49. This chapter starts by briefly explaining the background to our work on how the DPP and CPP work together. It then sets out changes we have made to improve the way the DPP and CPP work together to accommodate supplier-specific circumstances.

Early emerging views

50. In our problem definition paper, Topic 8 focussed on exploring opportunities to reduce the cost involved in making and assessing a CPP application.²⁷
51. That topic chapter noted a range of options for reducing the cost of better tailoring the price-quality path, including opportunities to reduce the CPP application and assessment requirements, where this could be achieved without compromising our ability to appropriately assess the application. Our decisions on these opportunities are set out in the second part of this paper (Chapters 4-8).
52. Topic 8 of the problem definition paper also touched on the possibility, raised by suppliers, of introducing 'single-issue' CPPs, which would be reduced in scope compared to a regular CPP where customisation is only sought in respect of one part of the supplier's DPP.
53. Rather than considering this suggestion in isolation, we thought it appropriate to step back and consider the range of options that currently exist for tailoring default/customised price-quality paths, and their effectiveness, before considering new mechanisms, such as single-issue CPPs that might provide for factors other than our existing quality-only CPP option.

Emerging views paper

54. On 29 February 2016 we published an emerging views paper on opportunities to improve the way default and customised price-quality paths, including the path change mechanisms within them (ie, pass-through costs, recoverable costs, and reopeners), work together to promote the long-term benefit of consumers.

²⁷ Commerce Commission "Input methodologies review invitation to contribute to problem definition" (16 June 2015).

55. In that paper we explained how promoting the long-term benefit of consumers in this context involves striking the right balance of scrutiny in our design and implementation of the DPP, CPP, and the path change mechanisms within them. This is because:
- 55.1 greater scrutiny can impose higher costs on both us and regulated suppliers, which can ultimately be passed on to consumers; but
 - 55.2 greater scrutiny can also benefit consumers by ensuring that regulated suppliers deliver services at more cost reflective price levels for the quality demanded.
56. This recognition of the costs and benefits of scrutiny, together with our experience of having now set a CPP and set and reset DPPs, informs the proportionate scrutiny principle.²⁸ The configuration of the DPP, CPP, and the path change mechanisms within them, should generally aim to accommodate suppliers' circumstances at a level of cost and scrutiny that is commensurate with the materiality of the changes to prices or quality experienced by consumers, within the constraints of the DPP/ CPP regime. Changes that would lead to material increases in prices or a material change in the quality of service should attract greater scrutiny.
57. There are also a number of other factors we will take into account when considering the appropriate level of scrutiny, such as the level of confidence we already have that the proposed tailoring delivers long-term benefits to consumers. This could be increased by:
- 57.1 the extent to which the supplier's previous forecasts were fit for purpose;²⁹
 - 57.2 scrutiny already applied – for example through summary and analysis, or under a previous CPP;
 - 57.3 the extent to which a forecast departs from historical trends; and
 - 57.4 the level of control the supplier has over a cost.³⁰

²⁸ As well as being consistent with promoting the long-term benefit of consumers in a cost effective manner, it is also consistent with Treasury's regulatory good practice principle of proportionality. That is, "the burden of rules and their enforcement should be proportional to the benefits that are expected to result", see: <http://www.treasury.govt.nz/regulation/bpr/bpregpa-feb15.pdf>, at p. 80.

²⁹ Forecasts will never be completely accurate. However, a supplier's ability to justify the difference between actuals and forecasts will contribute to our assessment of whether that forecast was fit for purpose.

³⁰ Where outside the control of a supplier, little is gained from scrutiny, as the supplier does not have the opportunity to affect that cost – hence, it may be appropriate to recover *ex-post*, or to provide *ex-ante* for it to be recovered (eg, through a pass-through cost mechanism).

Developing our emerging views

58. With this approach to scrutiny in mind, we considered opportunities to provide for greater supplier-specific tailoring in the DPP or price change mechanisms, while still providing an appropriate level of scrutiny, within the legislative bounds of the regime.³¹ We presented eight emerging views on how we thought the DPP and CPP could be improved to better accommodate supplier-specific circumstances and deliver greater long-term benefits to consumers:³²
- 58.1 Taking a more tailored approach to setting the DPP where this can be done without significantly increasing cost.
 - 58.2 'Single-issue' CPPs are not appropriate.
 - 58.3 Expanding the role of DPP reopeners.
 - 58.4 The quality-only CPP option should be replaced with a DPP reopener.
 - 58.5 Considering a CPP reopener for contingent and unforeseen projects.
 - 58.6 Considering approval of costs incurred prior to CPP approval.
 - 58.7 Providing for the expansion of the range of pass-through costs that can be added when setting the DPP.
 - 58.8 Applying a proportionate scrutiny principle in continuing to refine the CPP requirements and in assessing CPP proposals.
59. In our draft decision we explained these views and the changes to the IMs that we proposed to make to implement them.³³
60. The remainder of this chapter explains our final views and the changes we have made in relation to those views.

A more tailored approach to setting the DPP where this can be done without significantly increasing cost

61. We will look to take a more tailored approach to setting the DPP where it could be done without significantly increasing cost.
62. Suppliers have generally agreed with this view, in principle. For example in submissions on our emerging views paper Vector and Wellington Electricity submitted that we should not exclude the possibility that it may be appropriate to

³¹ Such as the need to ensure that DPP mechanism is low-cost.

³² Commerce Commission "Input methodologies review – Emerging views on opportunities to improve the way default and customised price-quality paths work together" (29 February 2016).

³³ Commerce Commission "Input methodologies review draft decisions: Topic paper 2 – CPP requirements" (16 June 2016).

tailor a DPP for a subset of EDBs in some circumstances.³⁴ We agree that in some circumstances it may be appropriate to treat some groups of suppliers differently under a DPP. For example, it may be appropriate to rely more on the capital and operating forecasts of a subset of smaller EDBs where we have increased confidence in the data (ie, summary and analysis supporting those forecasts is available).

63. For example, as part of the 2017 DPP reset for GPBs, we are looking to use an approach where we will use suppliers' own forecasts as a starting point for setting expenditure allowances.³⁵ That process is ongoing and we intend to release our draft decision in February 2017, which will include our responses to submissions on that approach.
64. We will continue to look for opportunities to tailor the DPP, where it can be achieved without significantly increasing costs. At this stage, we consider that the DPP IMs offer sufficient flexibility to allow this, and therefore no changes are needed.

'Single-issue' CPPs are not appropriate

65. A number of submitters continue to support single-issue CPPs³⁶ for a range of issues and reasons. However, we consider that single-issue CPPs are problematic due to:³⁷
- 65.1 problems with DPP/PPP regulatory period alignment;
 - 65.2 asymmetry between suppliers and consumers – suppliers could apply to tailor unfavourable elements of a DPP, but consumers could not apply to tailor overly favourable elements;
 - 65.3 interdependencies of inputs with other aspects of the path; and
 - 65.4 suppliers using their one CPP opportunity for the regulatory period to tailor a single parameter.
66. We consider that there are other mechanisms (such as the DPP quality standard reopener that we have introduced) that we can develop to address some of the issues that could have been addressed by a single-issue CPP instead. In some cases, however, a CPP will be the appropriate mechanism to address the issue, and while

³⁴ Comments on the emerging views paper are available at: <http://comcom.govt.nz/regulated-industries/input-methodologies-2/input-methodologies-review/interactions-between-dpps-and-cpps-and-the-requirements-for-cpps/>.

³⁵ Commerce Commission "Default price-quality paths for gas pipeline services from 1 October 2017 – Policy for setting price paths and quality standards paper" (30 August 2016).

³⁶ See, for example: Aurora "Submission – Input methodologies review: Draft decision and determination papers" (4 August 2016), p. 13.

³⁷ This is discussed in more detail in our emerging views paper: Commerce Commission "Emerging views on opportunities to improve the way default and customised price-quality paths work together" (29 February 2016).

we consider that it is appropriate for all CPPs to be full scope, we will look to adjust the depth of our scrutiny in line with the proportionate scrutiny principle.³⁸

67. We continue to hold the view that CPPs should always be full scope. By ‘full scope’, we mean that the scope of the application will encompass all inputs needed to set the price-quality path. This means that all inputs are potentially subject to scrutiny. Accordingly, we do not consider single-issue CPPs to be appropriate, and, as such we have removed the provisions in the IMs that allow EDBs to apply for a quality-only CPP (although we have replaced that option with a new DPP reopener).^{39, 40}

Expanding the role of DPP reopeners

68. We have expanded the range of circumstances under which we can reopen a supplier’s DPP.
69. Suppliers, submitting on our emerging views and draft decision, have generally been supportive of expanding the scope of reopener provisions provided for in the IMs.
70. In line with our draft decision, we have introduced a new reopener allowing an EDB to apply to vary its quality standards (this reopener will replace the option of applying for a quality-only CPP).
71. A number of suppliers have submitted that we should introduce a DPP reopener for contingent and unforeseen projects.⁴¹ GDBs have requested that we introduce a DPP reopener for constant price revenue growth. We have decided not to introduce these reopeners. Our reasons for this are discussed in this section.
72. We address the following reopeners in turn:
- 72.1 contingent and unforeseen projects for EDBs;
 - 72.2 contingent and unforeseen projects for GTBs;
 - 72.3 quality standard for EDBs; and
 - 72.4 constant price revenue growth.
73. For completeness, we note that we have introduced several other reopeners:
- 73.1 expanded error;

³⁸ The principle that the level of scrutiny applied should generally be commensurate with the price and quality impact on consumers of the tailoring being sought.

³⁹ We discuss in more detail under the ‘Quality standards for EDBs’ sub-section of the following section on DPP reopeners.

⁴⁰ See paragraphs 86-94.

⁴¹ The IMs for gas transmission currently provide for a CPP reopener for contingent and unforeseen projects. This allows the customised path to be reopened to build in incremental expenditure for major projects which were not foreseeable at the time the CPP was set, or which were foreseeable, but the timing, scope or cost of the project was uncertain at the time the CPP was set.

73.2 major transactions; and

73.3 DPP/CPP WACC alignment.

74. These reopeners are discussed in the Report on the IM review or the topic paper they relate to. We provide a summary of these at the end of this sub-section.

Contingent and unforeseen projects for electricity distribution businesses

75. In submissions on the emerging views paper, a number of EDBs suggested including contingent and unforeseen project reopeners under the DPP (or some other type of DPP reopener which would allow a supplier's default path to be reopened to provide for additional capex).⁴²

76. Wellington Electricity disagreed with our position in our draft decision that such a reopener would not be appropriate.⁴³ It gave the example of a \$40 network capex programme which it considered could be accommodated through a DPP reopener, and suggested that the cost of considering the reopener could be reduced by limiting our assessment to this project.

77. We do not consider that an appropriate level of scrutiny could be applied to such a significant value programme, under the relatively low-cost DPP mechanism.

78. We consider that our draft decision on this matter is still appropriate – we do not consider that reopeners for incremental capex are appropriate. This is because:

78.1 we may not have thoroughly scrutinised the base DPP expenditure, so will not know the extent to which the incremental expenditure is already accommodated in the DPP;

78.2 capex is likely to be strongly linked with other inputs such as opex. As such, it would be difficult to adjust in isolation; and

78.3 capex projects are likely to have a significant impact on the price and quality observed by consumers. Therefore they will require a level of scrutiny which we consider is not appropriate under a relatively low-cost DPP mechanism.

79. This view was supported by Powerco.⁴⁴

Contingent and unforeseen projects for gas transmission

80. In its submission on the emerging views paper Maui Development Limited (**MDL**) submitted that we should introduce DPP contingent and unforeseen project

⁴² See comments from Wellington Electricity, Orion, the ENA and PwC, available at: <http://comcom.govt.nz/regulated-industries/input-methodologies-2/input-methodologies-review/interactions-between-dpps-and-cpps-and-the-requirements-for-cpps/>.

⁴³ Wellington Electricity "Input methodologies review: Response to draft decisions" (4 August 2016), p. 9.

⁴⁴ Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 34.

reopeners for gas transmission businesses along with greater tailoring of the base DPP.

81. They suggested that gas transmission could be distinguished from electricity and gas distribution on the basis that there would be only a single supplier in the industry. They submitted that for a single supplier, the appropriate or proportionate depth of scrutiny could be applied both under a DPP reopener or a CPP.
82. First Gas supported this proposal in their submission on our draft decision.⁴⁵ As did Methanex:⁴⁶

We note the draft decision that GTBs should not be able to apply for a contingent projects reopener as part of the DPP. We submit that for GTBs, which have lumpy capex profiles, contingent project reopeners may be appropriate for modestly-sized replacement and renewal projects. This is subject to there being sufficient scrutiny of the expenditure to ensure it is reasonable and the project is justified, which may be manageable within the DPP. The benefit would be increased scrutiny over projects that may not be large enough to justify a CPP but still represent a step-change in expenditure. We consider that in the event that large, one-off, projects are contemplated, a CPP approach remains a suitable basis.

83. While we understand there would be benefits of allowing this sort of expenditure to be accommodated through a DPP reopener process, we do not think it is appropriate under the DPP/ CPP regime.
84. If a project of the magnitude that MDL suggests could be accommodated under a DPP reopener, it would still require significant scrutiny – necessitating information, consumer consultation and verification requirements in the vein of what we require under a CPP. We do not think that sufficient scrutiny could be applied to contingent projects, in keeping with the relatively low-cost purpose of the DPP mechanism, and we are not set up to apply this type of scrutiny during the DPP period.⁴⁷
85. There is also the issue of who pays for the tailoring under each mechanism. Our costs of considering a DPP reopener are funded through general gas levies which are paid for by both gas distribution and transmission businesses. Under a CPP however our costs can be billed back to the applicant.⁴⁸

⁴⁵ First Gas "Submission on Input methodologies review draft decisions (excluding cost of capital)" (4 August 2016).

⁴⁶ Methanex "Input methodologies review and Gas DPP consultation" (4 August 2016), p. 5.

⁴⁷ For example, unlike under a CPP, we do not have the ability to pass our costs of scrutinising a DPP reopener onto the supplier.

⁴⁸ Refer to section 53Y(1).

Quality standards for EDBs

86. We have introduced a quality standard reopener, which allows us, based on an application from a supplier, to reopen the DPP to vary the quality standards applying to an EDB where:
- 86.1 an EDB submits a quality standard variation proposal that complies with the requirements set out in the IM; and
 - 86.2 the EDB demonstrates that the proposed quality standards better reflects the realistically achievable performance of the EDB over the regulatory period.
87. These requirements are similar to those that were required for a quality-only CPP, which include justifications for the variation, estimations of its effect, and the provision of an engineer's report supporting the variation. However, consistent with a DPP, the extent of upfront requirements needed to support a DPP quality standard reopener will be less than for the existing quality-only CPP.
88. The supplier will be required to provide evidence of the consumer consultation it has undertaken in respect of the proposed standards and the results of that consultation. We have not prescribed what consultation is necessary to justify a reopener. We consider that this is appropriate given that we have the ability to request further information or consultation before we reopen the path, and that there is a natural incentive for the supplier to provide this information to support their quality variation proposal.
89. Given that the basis for the quality standard variation will be a report from an independent registered engineer, we do not consider that audit or certification will be necessary in all cases. However, we are retaining our ability to require audit or certification of the information before reopening the path if we consider it appropriate.
90. Submissions on our draft decision requested that we remove the requirement for the supplier to provide a report from an independent engineer.⁴⁹ However, we have retained this requirement in order to reduce the our burden in assessing a quality-standard reopener application and frontload some of the work required in assessing the proposed quality standard variation.⁵⁰
91. In response to submissions we have updated the information required from suppliers proposing a quality standard variation as part of a CPP proposal or DPP reopener, to better reflect how we currently set quality standards. We have also removed the requirement to demonstrate the effect of the proposed change over the past five

⁴⁹ See, for example: ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), p. 11.

⁵⁰ We note that we cannot recover the costs of considering a reopener from the EDB, as we previously could under a quality only CPP.

years, to allow some flexibility in how the supplier demonstrates the estimated historical effect of the proposed quality standard variation. These changes are explained in more detail in relation to CPP quality standard variations in para 303-309.

92. For the purposes of clarity, we have set out the criteria that we will consider when assessing a quality standard variation reopener, as suggested in submissions.⁵¹ These criteria are based on the criteria used to assess quality standard variations for CPPs.
93. In submissions on the draft decision PwC suggested that if a supplier comes in for a quality standard reopener, a decision to change the quality standards could be applied retrospectively, from the beginning of the DPP period.⁵² We do not think it is appropriate to apply the quality standard variation reopener to retrospectively alter the quality standards applicable in previous disclosure years. Suppliers who identify that the quality standards applicable under the DPP are not suitable should apply for a quality reopener in a timely manner. The quality standards set under the DPP are intended to provide *ex-ante* incentives to provide quality at a certain level. Adjusting these standards *ex-post* would remove these incentives.
94. The timing of when this reopener will take effect is discussed in the Report on the IM Review, in Attachment C – Timing and Transition Provisions in the IM Amendments determinations.

Constant price revenue growth

95. In the emerging views paper we identified constant price revenue growth (**CPRG**) as an input that could potentially be adjusted independently of others, and reopened in certain circumstances under a DPP.
96. We have considered the possibility of introducing a CPRG reopener, for early in the period. Although we consider that CPRG could potentially be an input that is appropriate for tailoring separately from the other inputs, we do not consider that there is an obvious need to introduce such a reopener.
97. This is because the issue it was initially designed to address (ie, where new information comes to light early in the DPP period which demonstrates that the CPRG forecast for and EDB is inappropriate) would largely be fixed by changing the form of control to a revenue cap for EDBs.⁵³ Submitting on the draft decision, Electricity Networks Association (**ENA**) suggested that if a revenue cap was selected as the form of control applying to EDBs then we should introduce a reopener for

⁵¹ ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), p. 11.

⁵² PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers" (4 August 2016), table at para 14.

⁵³ ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016).

unforeseen major connections.⁵⁴ We do not consider that this would be appropriate. Seeking a CPP or capital contributions would be an available options in such circumstances.

98. Submissions on our draft decisions suggested introducing a CPRG reopener for GDBs if we retained our draft decision that they would be subject to a weighted average price cap, following the next reset.⁵⁵ Submissions acknowledged that there are currently no significant issues with forecasting CPRG for GDBs, but still considered that there would be value in removing the risk of over and under-recovery for CPRG issues found early in the period.⁵⁶
99. If we were to introduce a DPP reopener for CPRG, we consider that:
- 99.1 There could be a disincentive for the supplier to provide all evidence upfront, as they would still have the opportunity for a reopener if they received an unfavourable CPRG forecast;
- 99.2 If the reopener was only able to be triggered by the applicant, we would have concerns regarding the asymmetry of the reopener – that is, suppliers would be incentivised to reopen the path to correct unfavourable CPRG forecasts, but not to correct overly favourable CPRG forecasts.
- 99.3 If the reopener was able to be triggered by the applicant and the Commission, submissions have identified that this could create material regulatory uncertainty for suppliers.⁵⁷
100. Given the limited circumstances in which a CPRG reopener would be available (only for issues identified very early in the DPP period, that were reasonably unforeseeable by the applicant and not considered during the setting of the DPP), and the lack of issues with CPRG forecasting for GDBs, we do not think a CPRG reopener is warranted.

Reopeners not linked to our emerging views

101. For completeness, we have briefly explained the other reopeners that we have introduced. These reopeners are discussed in the Report on the IM review or the topic paper they relate to.

⁵⁴ ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), p. 15.

⁵⁵ Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), para 128-131. Vector "Submission to Commerce Commission on the IM review draft decision and IM report" (4 August 2016), p. 34.

⁵⁶ Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 35. Vector "Submission to Commerce Commission on the IM review draft decision and IM report" (4 August 2016), p. 34.

⁵⁷ See, for example: Vector "Emerging views on customised and default price paths" (24 March 2016), para 12.

Expanded error

102. We have expanded the pre-review error reopener to address the situation where the price-quality path was set on the basis of any type of error. This could include such cases where the data used was incorrect, or the data was correct, but was applied incorrectly. Previously, the error provisions were limited to incorrect data and could not be used to fix cases where, for example, the data was incorrectly or mistakenly applied.⁵⁸

Workability

103. As part of our draft decision we proposed to introduce a mechanism that would allow us and suppliers to apply the "next closest alternative" approach where an IM becomes unworkable. We also proposed that in the limited circumstances where making the IM workable would involve a change to an existing DPP (or the same occurs because a provision in the relevant s 52P determination becomes unworkable) that we would allow for a reopener to allow us to reopen the path where necessary, to enable suppliers to be able to implement the alternative approach.
104. We have decided not to introduce this reopener or provision, as discussed in the Report on the IM review.⁵⁹

Major transactions

105. This change provides a reopener to address the consequences of a major transaction which makes the price path unworkable.⁶⁰

DPP/ CPP WACC alignment

106. As discussed in Topic paper 4 – Cost of capital issues, we have made changes to align the CPP and DPP WACC rates for suppliers on a CPP. To implement this we have introduced a CPP reopener for when the DPP WACC changes.

Introducing a CPP reopener for contingent and unforeseen projects

107. We have introduced new CPP reopeners for contingent and unforeseen projects, for gas and electricity distribution businesses.⁶¹

⁵⁸ This change applies to both DPP and CPPs, and is discussed in more detail in the Report on the IM review at decision RP01. See: Commerce Commission "Input methodologies review decisions: Report on the IM review" (20 December 2016).

⁵⁹ This change applies to both DPP and CPPs, and is discussed in more detail the Report on the IM review at decision RP01. See: Commerce Commission "Input methodologies review decisions: Report on the IM review" (20 December 2016).

⁶⁰ This change applies to both DPP and CPPs, and is discussed in more detail the Report on the IM review at decision RP01. See: Commerce Commission "Input methodologies review decisions: Report on the IM review" (20 December 2016).

⁶¹ The IMs for gas transmission currently provide for a CPP reopener for contingent and unforeseen projects. This allows the customised path to be reopened to build in incremental expenditure for major projects which were not foreseeable at the time the CPP was set, or which were foreseeable, but the timing, scope or cost of the project was uncertain at the time the CPP was set.

108. We consider that this is appropriate under a CPP as we have already scrutinised the underlying expenditure when we set the initial CPP. This means that we can build on incremental expenditure for projects where timing, cost and scope were not known at the time we set the CPP, without concerns that the project may be already provided for in the path.⁶²
109. Submissions on our emerging views paper and draft decision have supported this change, although a number of suppliers suggested that these reopeners should also be available under a DPP as well. As set out above, we do not consider that it is appropriate to provide for contingent and unforeseen project reopeners under a DPP.

Allowing contingent and unforeseen projects to include opex

110. Under the pre-review GTB IMs, contingent and unforeseen projects were defined by reference to the need for major capital expenditure. Consistent with our consideration of 'non-transmission solutions' when we evaluate a major capex project for Transpower under the terms of the Transpower Capex IM Determination, we have changed the IMs so that the contingent and unforeseen project provisions can apply where major operating expenditure is required as well.⁶³
111. This change should remove any incentives for a supplier to inefficiently class projects as capital expenditure for the purposes of allowing a reopener, even though incurring operating expenditure may be a more appropriate option in the circumstances.

Approval of costs incurred prior to CPP approval

112. We have introduced a new recoverable cost which will allow suppliers to recover prudently incurred costs in response to an urgent project where:
- 112.1 the costs are, or will be, incurred between the submission of a CPP application and the CPP coming into effect,⁶⁴
 - 112.2 we accept the CPP for our consideration; and
 - 112.3 we approve the cost by specifying it in the CPP determination.
113. We would retain the discretion to decline the recovery of pre-determination costs that were not considered to be consistent with the "investment case" submitted and approved as part of a CPP application.
114. Submissions were supportive of this change, though a number of suppliers requested that the recoverable cost should extend to expenditure incurred prior to a CPP being

⁶² More details on how this reopener works can be found in our original 2010 IM reasons paper: Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.5.25-9.5.37.

⁶³ This includes the new provisions we have included for EDBs and GDBs.

⁶⁴ We note that our draft decision was only for costs incurred between submission and determination.

submitted. For example, Powerco suggested that we broaden this provision to allow CPP applicants to recover prudently incurred costs up to 24 months prior to submitting a CPP application.⁶⁵

115. As we outlined in our draft decision, we do not consider it appropriate to extend the recovery of costs to costs incurred prior to the CPP submission. We consider that this would remove the incentive for applicants to submit a proposal in a timely manner. Further, we consider that it is desirable to minimise the level of controllable expenditure that is approved *ex-post*.
116. PwC and ENA noted, in submissions on the draft decision, that the urgent project allowance excludes any costs which are treated as commissioned assets. They supported this exclusion on the condition that the capex wash-up recoverable cost, which was introduced for DPPs prior to the 2015 DPP Determination, is extended to CPPs.⁶⁶ We agree with this submission and have extended this mechanism to CPPs. This change is discussed in the Report on the IM review.⁶⁷

Expanding the range of pass-through costs that can be added when setting the DPP

117. We have widened the criteria-based pass-through costs,⁶⁸ which could previously only be specified *during* the regulatory period, so they are also able to be specified in a DPP or CPP determination at the time the DPP or CPP is determined. We have also changed the IMs so that any type of cost, which meets the pass-through cost criteria in the IMs, can be specified as a pass-through cost in a DPP determination, rather than just levies.⁶⁹
118. Submissions were supportive of this change.⁷⁰

Costs of preparing a CPP

119. Some suppliers have suggested that we widen the definition of recoverable costs to include certain additional costs associated with preparing a CPP application, such as

⁶⁵ Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 6.

⁶⁶ ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016). PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers" (4 August 2016), para 115, table item 2.

⁶⁷ Commerce Commission "Input methodologies review decisions: Report on the IM review" (20 December 2016).

⁶⁸ The pre-review IMs provide the opportunity for us to specify new pass-through costs during a regulatory period in circumstances where a levy or other cost meets the criteria for a pass-through cost, set out in the IMs (criteria-based pass-through costs).

⁶⁹ This option has always been available for CPPs.

⁷⁰ See, for example: ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), p. 15; First Gas "Submission on Input methodologies review draft decisions (excluding cost of capital)" (4 August 2016), p. 2.

costs of consumer consultation, costs of developing a financial model, consultant reports and project management.^{71, 72}

120. PwC, in its submission on the draft decision, noted that smaller suppliers which do not have teams which are geared up to manage complex regulatory projects will be particularly disadvantaged by not being able to recover these costs.⁷³
121. We do not consider that it is appropriate to introduce these proposed recoverable costs. While we consider that it is appropriate that some of the costs of applying for a CPP can be recovered from consumers, we consider that having the supplier bear some of the cost of preparing a CPP application creates appropriate incentives for the supplier to minimise the costs of preparing a CPP.
122. We also note that, following the introduction of an incremental rolling incentive scheme (**IRIS**) that applies to EDBs subject to a DPP, the impact of any temporary costs not directly recoverable from consumers, will be shared between consumers and suppliers. Under the current IRIS rules suppliers only bear about 34% of these temporary costs.⁷⁴
123. In submissions on our draft decision First Gas noted that the lack of an IRIS for gas pipeline businesses means that any additional costs incurred applying for a CPP are not shared with consumers and suggested that we introduce a mechanism whereby these costs would be shared with consumers.⁷⁵
124. We do not consider that this suggestion is appropriate. We have made a decision not to introduce an IRIS mechanism for gas, which was supported by stakeholders. Further, we do not consider that we would be able to clearly identify these efficient costs, in order to specify them in a CPP determination.

⁷¹ See, for example: ENA "Feedback on Orion customised price-quality path process" (14 April 2014), Orion Limited "Feedback on Orion customised price-quality path process" (14 April 2014), PwC "Submission to the Commerce Commission on input methodologies review: Invitation to contribute to problem definition (21 August 2015); ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), p. 5.

⁷² We currently allow audit, verification and independent engineer fees to be recovered.

⁷³ PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers" (4 August 2016).

⁷⁴ Commerce Commission "Further amendments to input methodologies for electricity distributors subject to price-quality regulation – Incremental Rolling Incentive Scheme" (25 November 2015).

⁷⁵ First Gas "Submission on Input methodologies review draft decisions (excluding cost of capital)" (4 August 2016), p. 5.

We have applied the proportionate scrutiny principle in continuing to refine the CPP requirements and in assessing CPP proposals

125. In our emerging views and draft decision papers, we presented the view that there are opportunities for us to be more targeted in the depth of scrutiny we apply when assessing a CPP proposal informed by:
- 125.1 the proportionate scrutiny principle (ie, the level of scrutiny applied should be commensurate with the price and quality impact on consumers of the tailoring being sought);⁷⁶ and
 - 125.2 the extent to which we have confidence in the supplier's own forecasts.⁷⁷
126. The proportionate scrutiny principle has also guided our approach to the changes to reduce unnecessary cost and complexity in the CPP requirements by:
- 126.1 making improvements to the scope and specificity of the information requirements for CPPs;
 - 126.2 clarifying the roles of the independent verifier, auditor and independent engineer, consistent with s 52R; and
 - 126.3 clarifying our consumer consultation expectations, also consistent with s 52R.
127. Submissions have been generally supportive of this view, though there were a number of requests for clarification as to how the proportionate scrutiny principle would work in practice.⁷⁸ There were also a number of suggestions by submitters that are dealt with in turn below.
128. We conclude this section with our views on the aims and benefits of applying the proportionate scrutiny principle to CPPs.

Case by case negotiation of information requirements

129. Orion suggested that the IMs could usefully include a process for suppliers to engage with the Commission on which items within a CPP would and would not need detailed scrutiny (in accordance with the proportionate scrutiny principle).⁷⁹ The

⁷⁶ Commerce Commission "Input methodologies review: Emerging views on opportunities to improve the way default and customised price-quality paths work together" (29 February 2016), para 35.

⁷⁷ Our level of confidence in each input will depend on the extent to which that input has already been scrutinised when we set the base DPP, or through summary and analysis. For example, if a supplier is seeking a CPP to accommodate a large, one-off, item of project expenditure, it might appropriate for the verifier and ourselves to apply a lower level of scrutiny to business-as-usual expenditure, and for scrutiny to be focused on the increment being sought.

⁷⁸ See, for example: Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 32.

⁷⁹ Orion "Submission on emerging views on opportunities to improve the way default and customised price-quality paths work together" (23 March 2016), para 15.

supplier could then tailor their proposal accordingly and only incur significant costs in preparing those aspects of the application that are most material.

130. Conversely though, Vector submitted that while the proportionate scrutiny principle could reduce barriers of cost and complexity for parties seeking a CPP, it is still important that when setting the process to strike the right balance between prescription and the ability of the Commission to exercise discretion.⁸⁰ Vector commented that if there was inconsistency in the level of scrutiny applied to individual cases, this will lead to a lessening of confidence in the process.
131. We considered the possibility of introducing a process which would allow us to, on a case by case basis, agree to reduce the information requirements for non-material aspects of a proposal. This could operate in a similar way to the exemption and modification provisions introduced as part of the CPP fast track amendments.
132. However, bearing in mind Vector's submission and the need to promote certainty under s 52R, we consider that it is appropriate to retain the full set of base information requirements (that is information required for all expenditure categories – not the detailed information that needs to be provided for the identified projects). This is because we consider:
- 132.1 this information should, generally, be relatively easy to compile (does not contribute significantly to cost); and
- 132.2 this information is likely to be valuable to our assessment of the proposal and will be crucial if we need to determine revenues that differ from the CPP proposal. Given the limited time available to determine a CPP, we consider that it is beneficial to have this information upfront, rather than to request it during the assessment process.
133. We also consider that it is appropriate to apply the modification and exemption provisions,⁸¹ on a case by case basis, where it will not materially detract from our ability to assess a proposal.⁸² This is likely to include the application of the proportionate scrutiny principle.

Rolling over information requirements for subsequent CPP applications

134. Vector requested that we provide for a CPP rollover mechanism, where a supplier already subject to a CPP wishes to apply for a second or subsequent CPP on substantially similar grounds.⁸³ They suggest that in these cases the supplier would

⁸⁰ Vector "Emerging views on customised and default price paths" (24 March 2016), para 9.

⁸¹ These allow suppliers to agree with the Commission to exemptions and modifications from the requirements for a CPP proposal application, where it will not detract, in more than a minor way, from the Commission's ability to evaluate and determine a CPP proposal, or the ability of interested persons to consider a provide views on the proposal.

⁸² For example where specific information requirement is not readily available, but adds little to our assessment of the proposal.

⁸³ Vector "Emerging views on customised and default price paths" (24 March 2016), para 10.

not need to replicate the original application. Rather, the application would focus only on updating the information supplied in the original application.

135. Where scrutiny has already been applied through a previous CPP, we think it is appropriate to consider using the exemptions and modification provisions to reduce the scrutiny requirements,⁸⁴ to the extent that it does not materially detract from our ability to assess a proposal.
136. For example, where historical information, which is required as part of a CPP proposal, has already been audited under a previous CPP, we may consider exempting an applicant from those audit requirements for the same information in a subsequent CPP application.
137. We consider this to be a practical approach to the issue, taking advantage of our existing provisions that allow for flexibility.
138. We recognise the potential benefits in doing sequential CPPs and may look to develop a more specific process in the future. When we have more experience in setting CPPs we will be in a better position to assess the extent to which a prior CPP can give us greater confidence in a supplier's forecasts for a subsequent CPP (and the extent to which we can relax the requirements as a result).
139. Some stakeholders have suggested that we develop IMs to govern the process for how we will treat a supplier who is transitioning from a CPP back onto a DPP.⁸⁵
140. As explained in our paper on Orion's transition to the 2015-2020 DPP,⁸⁶ we do not consider that it is necessary to include a prescriptive process for the transition from CPPs to DPPs in the IMs.
141. We consider a better transition option is to address this as part of our engagement process outside of the IMs, which provides flexibility to consider the specific supplier's circumstances at the time of the transition.⁸⁷

Aims and benefits of a proportionate scrutiny principle

142. When considering the appropriate mechanism for tailoring an aspect of a CPP, the level of scrutiny that is appropriate for that tailoring will be a key factor.
143. Where the benefits of scrutiny (that is the benefits received by consumers due to a path which results in a level of revenue that is more commensurate with the level of

⁸⁴ The IM requirements for information, consumer consultation, audit and verification, as well as how we assess an application.

⁸⁵ Orion New Zealand Limited "Submission on the IM Review" (21 August 2015), para 37; ENA "Response to the Commerce Commission's Input Methodologies review paper" (21 August 2015), para 124.

⁸⁶ Commerce Commission "Orion's transition to the 2015-2020 DPP – Key considerations and possible approaches" (14 March 2016).

⁸⁷ Refer paragraphs 28-35 of: Commerce Commission "Orion's transition to the 2015-2020 DPP – Key considerations and possible approaches" (14 March 2016).

quality demanded) are outweighed by the regulatory costs of the scrutiny, then a lower level will likely be more appropriate. This is more likely to be the case for small suppliers where they do not have the scale to spread the regulatory costs, and therefore the cost of scrutiny may itself have a potentially material price effect. We discuss the possible challenges faced by smaller suppliers in applying for a CPP and our approach in Chapter 4.

144. We consider that there are opportunities to apply the proportionate scrutiny principle when setting the requirements for, and assessing, the different elements of a CPP, ie, we will focus our assessment on the more material parts of a proposal, including:
 - 144.1 the scope and specificity of information requirements;
 - 144.2 verification and audit requirements;
 - 144.3 consumer consultation expectations; and
 - 144.4 our evaluation of the CPP proposal to satisfy the evaluation criteria.
145. We have looked to apply the proportionate scrutiny principle to CPPs, where possible, through our design of the CPP requirements and our changes.
146. We will also apply the principle in exercising our discretion and judgement, particularly in relation to the flexibility provided for under the modifications and exemptions provisions (introduced in the fast track part of this review).

Chapter 4: Evaluation of CPP proposals

Purpose of this chapter

147. The purpose of this chapter is to explain and clarify our approach to evaluating CPPs, including how the CPP requirements support that approach. It also introduces the changes we are making to the CPP requirements.

Structure of this chapter

148. This chapter begins by setting out our high level objectives for CPPs. It then explains how we evaluate CPP proposals, and how the CPP requirements, set out in the IMs, support that evaluation. Finally, it introduces the changes that we have made to the CPP requirements to better achieve our objectives and better support our evaluation and determination of CPP proposals. We also explain our changes to address the possible challenges that a smaller supplier might face when applying for a CPP.

Objectives for CPPs

149. This section sets out our current and forward-looking high level objectives in respect of CPPs. They are as follows:
- 149.1 We consider that CPPs should be used where they can better promote the long-term benefits of consumers than a DPP.
 - 149.2 When a supplier applies for a CPP we have the opportunity to set a more tailored price-quality path than under a DPP.⁸⁸ This allows us to better match the path to the supplier's specific circumstances and better promote long-term benefits for consumers.
 - 149.3 In applying scrutiny to the tailoring proposed and developing or approving comprehensive capex and opex forecasts, we ensure that the CPP applicant is able to undertake efficient expenditure to provide a level of quality that reflects consumer demands, while also being limited in its ability to extract excessive profits, consistent with the s 52A purpose.
 - 149.4 Our aim is to make the CPP application process as cost-effective and straightforward as possible, while still ensuring that we are able to evaluate and determine a CPP in the statutory timeframes, at an appropriate level of scrutiny (in line with the proportionate scrutiny principle, discussed above in para 56).

⁸⁸ By "tailored" we mean a price-quality path that better takes into account the supplier's specific circumstances. Greater tailoring can better promote the long-term benefit of consumers where it ensures that the price-quality path provides for efficient investment and rewards superior performance with greater profits, but not to the point that those profits are excessive.

150. To support a CPP regime that gives effect to these objectives:
- 150.1 We understand a degree of flexibility is desirable in the format and level of information suppliers are required to supply. We have already introduced a level of flexibility as part of the CPP fast track amendments.⁸⁹ These IM amendments were aimed at improving the cost-effectiveness of preparation, assessment and determination of CPP applications by allowing:
 - 150.1.1 modifications or exemptions to the process for preparing, and the content of, CPP proposals;
 - 150.1.2 the use of alternative methodologies with equivalent effect (**AMWEEs**) for certain elements of CPP proposals; and
 - 150.1.3 allowing us to accept CPP applications for consideration if they comply with the process and content IMs "in all material respects".
 - 150.2 We consider it important that we provide clarity as to the role and purpose of the verifier, auditor, and our expectations for consumer consultation.
 - 150.3 We will focus our evaluation, where possible, on the drivers and most material elements of proposals (in line with the proportionate scrutiny principle).
 - 150.4 We are making a change to ensure there are no perverse incentives created through a misalignment between the DPP and CPP WACC rates (our solution to the DPP/CPP WACC misalignment issue is discussed in Topic paper 4 – Cost of capital issues).
151. Apart from making improvements to the CPP requirements as part of the IM review, there are opportunities for us to make it more likely suppliers will apply for a CPP where that results in greater benefits to consumers, including through:
- 151.1 clarifying for suppliers the opportunities for tailoring provided by the CPP option and other available tailoring mechanisms, through ongoing engagement;
 - 151.2 building on the lessons learned during the Orion CPP process, and improving our internal processes for the next CPP application we receive; and
 - 151.3 improving and encouraging upfront engagement with suppliers considering and preparing CPP proposals.

⁸⁹ Commerce Commission "Input methodologies review: Amendments to input methodologies for customised price-quality paths – Final reasons paper for limb 1 of the CPP fast track" (12 November 2015).

How we assess CPP proposals

152. This section explains our approach to how we evaluate CPP proposals against the evaluation criteria set out in the IMs. The evaluation criteria are set at a high level. Our approach to *how* we carry out our evaluation is not set out in the IM requirements for CPP proposals – rather the IM requirements support our evaluation of a CPP proposal using this approach.

High level components of a CPP proposal

153. At any time after a DPP is set,⁹⁰ a supplier that is (or is likely to be) subject to a DPP may make a proposal to the Commission for a CPP.⁹¹

154. We have broad discretion under Part 4, as to exactly how we determine a CPP and we may determine any CPP that we consider appropriate, applying the relevant IMs.⁹² This means that once we have received a CPP proposal there are two steps we must undertake:

154.1 evaluating the applicant's proposal; and

154.2 determining a customised path that we consider to be appropriate. This may be the path proposed by the supplier, or a higher or lower path, if we consider that the proposal is not appropriate.^{93, 94}

155. In undertaking this exercise we assess the applicant's CPP proposal against the evaluation criteria set out in the IMs.

156. We consider that the use of a building blocks approach to determining expenditure, with a greater emphasis on supplier-specific costs than under a DPP, continues to be necessary to determine a CPP that is appropriately tailored to the supplier's specific circumstances.

157. A proposal to support a building blocks approach for determining a CPP broadly is comprised of three parts:

157.1 Price path information – this comprises the financial information – such as information on cost allocation, valuation, depreciation, tax, forecast opex, forecast commissioned assets and other income – that is used to create the price path. The compilation of this information is primarily governed by the input methodologies.

⁹⁰ Within the application windows specified in a 52P determination, and not in the final year of a DPP.

⁹¹ Commerce Act 1986, s 53(Q)(1).

⁹² Unless a variation to the IMs has been agreed with the supplier, under section 53V(2)(c) of the Act.

⁹³ Commerce Act 1986, s 53V.

⁹⁴ This will involve determining and explaining what we consider to be an appropriate level of expenditure that meets the expenditure objective.

- 157.2 Proposed expenditure information – this comprises forecasts of capital expenditure and operating expenditure and information on policies, strategies, assumptions, data, processes used to develop these forecasts.
- 157.3 Quality variation information – where a quality standard variation is proposed, information to justify the variation must also be provided.

Assessment of expenditure

158. A key component of our evaluation of a CPP proposal is the assessment of the applicant's expenditure forecasts.
159. Expenditure will often be the driver of a CPP application, and as such, will require specific focus when evaluating a CPP to ensure the path provides for a level of expenditure that allows the supplier to meet consumer demands at an efficient cost.⁹⁵ Forecasting appropriate levels of expenditure will require the exercise of judgement by both the supplier as well as the Commission.
160. We consider the approach to assessing expenditure that we set out in the 2010 IM reasons paper is still broadly appropriate. This section clarifies some elements of our approach, particularly in light of our experience in evaluating Orion's CPP application, and explains how it links with the proportionate scrutiny principle.⁹⁶ This guidance is intended to give potential CPP applicants an insight into how we think and go about assessing expenditure against the expenditure objective, which is set out in the CPP evaluation criteria IMs.⁹⁷ It is not intended to be a substitute for the evaluation criteria, or to impose further requirements than those set out in the IMs.

What we are trying to establish when assessing expenditure

161. Broadly, we need to be satisfied that the proposed expenditure is consistent with what would, and could, be delivered by a prudent supplier:⁹⁸ the right expenditure, at the right time, at the right cost. Ensuring the CPP applicant recovers the costs that a prudent supplier would incur to efficiently provide the regulated services at a quality that consumers demand is consistent with s 52A(1)(a), (b) and (d).⁹⁹
162. To establish if the proposed expenditure under a CPP is consistent with this objective, we consider it appropriate to use a predominantly top-down assessment approach. This requires us to obtain assurance that the proposed expenditure is

⁹⁵ In line with s 52A(1)(b) of the Commerce Act 1986.

⁹⁶ Explained above under sub-section 'We should apply a proportionate scrutiny principle in continuing to refine the CPP requirements and in assessing CPP proposals'.

⁹⁷ The expenditure objective means objective that capex and opex reflect the efficient costs that a prudent supplier would require to meet or manage expected demand for the regulated services, at appropriate service standards, during the CPP regulatory period and over the longer term; and comply with applicable regulatory obligations associated with those services.

⁹⁸ As required by the expenditure objective, see: clause 5.2.1 of the EDB IM Determination.

⁹⁹ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), p. iv.

appropriate to meet consumer demands¹⁰⁰ (including quality), and regulatory requirements (including those outside of Part 4 regulation), that the supplier must meet.¹⁰¹

163. In assessing whether the proposed expenditure in a CPP proposal meets the expenditure objective, we are likely to consider whether:
- 163.1 the proposed investments align with the service outcomes;
 - 163.2 the projects can be delivered at the right time, within the bounds of the planning uncertainties;¹⁰²
 - 163.3 the processes for delivering the expenditure are efficient; and
 - 163.4 the supplier has adequate strategies for accessing the necessary resource to undertake an increased level of expenditure.¹⁰³
164. PwC submitted on the draft decision that these "additional criteria" were unhelpful to be included in the topic paper, without recognition of the existing criteria, particularly as it is unclear what the status of these new criteria is.¹⁰⁴
165. For the avoidance of doubt, the factors listed above are aspects that we are likely to consider when evaluating whether proposed expenditure meets the expenditure objective set out in the evaluation criteria – we consider that these factors would be considered by a prudent supplier in determining the efficient levels of opex and capex. The expenditure objective is high level and these are only intended to provide transparency and give insight into some of the more detailed factors that we may consider when applying the criteria set out in the IMs.

Our approach

166. While we consider that it is appropriate to obtain assurance that the proposed expenditure is consistent with the expenditure objective set out in the IMs,¹⁰⁵ this does not mean that we will undertake a detailed assessment of the supplier's entire spending programme. Rather we will undertake a "top-down" approach to assessing expenditure supported with a limited "bottom-up" review of selected projects and programmes.

¹⁰⁰ Meeting consumer demands means that the supplier will deliver appropriate service (quality) standards, to meet expected demand.

¹⁰¹ Suppliers must also be able to meet any regulatory requirements outside Part 4 – such as health and safety regulations.

¹⁰² For the purposes this paper references to projects may also include programmes, which are defined in the IMs as a group of related projects with a common purpose.

¹⁰³ We would not consider it appropriate to increase prices to consumers if the investments are unlikely to occur due to resource constraints.

¹⁰⁴ PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers – Made on behalf of 17 Electricity Distribution Businesses" (4 August 2016), para 118-119.

¹⁰⁵ That is, the efficient costs that would be incurred by a prudent supplier facing the same circumstances as the applicant.

167. The top-down approach initially focusses on the supplier's policies, strategies and processes. This provides us with an understanding of how the business says that it will manage its assets to deliver the services required by consumers. We assess the supplier's policies, strategies and processes to ensure that, if they are implemented in practice, they will produce appropriate expenditure forecasts.
168. We then assess whether the development of the proposed expenditure forecast has been consistent with the policies strategies and processes. We would do this by sampling a subset of projects and programmes. This assures us that high level policies, strategies, and processes are being implemented consistently and that the right investments are being proposed.
169. A further step in our top-down approach is to assess the appropriateness of the input assumptions used by the business when forecasting expenditure. We would also expect to consider the level of confidence that can be placed on any data used by the supplier when forecasting expenditure. This will include consideration of the source, reliability and quality of the information together with the reasonableness of any assumptions made to fill data gaps.
170. As is discussed further below, a key aspect of our expenditure assessment approach is the use of a pre-application verification of proposed expenditure by an approved independent verifier. The independent verifier is responsible for selecting the sample of projects and programmes, and focusses on the most material projects, in line with the proportionate scrutiny principle. This pre-application verification process is intended to promote certainty for suppliers as to how their expenditure is likely to be assessed, as well as to assist us to make the most effective use of the tight statutory timeframes for evaluating CPP proposals, by highlighting which areas of a proposal we should focus on.
171. We will supplement our top-down assessment with a limited bottom-up review of areas highlighted by the verifier. We expect this review will complement, rather than repeat, the verifier's assessment. For example, where the verifier's final report identifies that the applicant does not appear to have followed its own planning standards for network or asset replacement, it would highlight this was an area that we needed to review.
172. We, rather than the verifier, are required to determine the appropriate level of expenditure. Therefore, we would also expect to review the models used to prepare the forecasts, and consider if the outputs and conclusions from the models are reasonable.

Proportionate scrutiny/materiality

173. We expect that in applying this top-down approach, we will require a higher level of assurance for more material elements of a proposal, in terms of the potential impact on price and quality. This is consistent with the proportionate scrutiny principle which provides that the scrutiny that an element of a CPP proposal receives should be commensurate with the potential impact of that element on price and quality.

174. The more material elements of a proposal may or may not be a small number of large individual projects. It is possible that the material elements will be formed by one or more programmes made up of several smaller work parcels.
175. As discussed in the verification chapter, we consider that the verifier should apply the proportionate scrutiny principle as part of its choice of projects that require more specific information on and which have a greater level of scrutiny applied.

Evaluation of price path information

176. In addition to assessing the applicant's expenditure forecasts, our evaluation involves ensuring that IM-compliant financial information relating to key 'building blocks' components is used appropriately to calculate the proposed price-quality path.
177. The way the price path is compiled is defined by the various building block IMs, and the process is largely mechanistic. As noted in our 2010 reasons paper, this promotes certainty and predictability of processes for both suppliers and the Commission.
178. However, there are some areas where the IMs provide flexibility for particular cases, which requires us to exercise our judgement. There are also instances where suppliers may propose variations to the building block IMs under s 53V(2)(c) of the Act, and we will assess these proposals in order to determine an appropriate price-quality path.
179. Our assessment of the price path typically involves a number of steps, such as conducting high level reasonableness checks that forecast information is consistent with the disclosure of past financial data (or, if not, that the applicant has satisfactorily explained why). We would also seek to establish that expenditure forecasts have the appropriate effect on building block elements such as the regulatory asset base (**RAB**), depreciation and revaluations, and we would assess the overall profile of the price path to understand whether 'in-period' smoothing of revenues via the price path 'X-factor' is desirable.

Evaluation of quality standard variation information

180. Suppliers may request a quality standard variation to either decrease, or in some circumstances increase, their quality standards. Where a CPP applicant applies for a quality standard variation as part of a CPP, we will also evaluate the proposed variation. At the highest level we will consider the extent to which the proposed quality standard reflects the realistically achievable performance of the EDB.¹⁰⁶

¹⁰⁶ As required by the evaluation criteria, set out in the IMs.

181. As part of our evaluation of whether a proposed quality standard variation better reflects the realistically achievable performance of an EDB we are likely to consider the following factors.
- 181.1 The components of reliability that are driving the change in quality performance.¹⁰⁷ This may include a consideration of any historical reasons for deterioration in quality and the decisions made to manage deterioration.¹⁰⁸
 - 181.2 The extent to which the proposed quality standards align with the level of investment proposed in the proposal.
 - 181.3 Statistical analysis of past SAIDI and SAIFI performance.
182. We will also consider the extent that the quality standard variation and the cost (trade-off) is supported by consumers (and if not, why not).¹⁰⁹

CPP requirements that support our evaluation using this approach

183. This section explains the CPP requirements that support our evaluation of a CPP proposal in line with the approach discussed above, and how they should be designed to ensure we are able to evaluate and determine a CPP that delivers long-term benefits to consumers.

Supplier must provide a proposal

184. A supplier is required to supply us with a proposal which sets out their proposed expenditure and must contain certain information that supports the expenditure. This proposal must be fit for purpose – that is it must allow us to undertake an assessment of the proposed expenditure and determine an appropriate customised price-quality path.
185. A proposal that is fit for purpose will clearly demonstrate that the expenditure forecast represents the efficient costs that the supplier needs to incur to meet the services required by the consumers. To do this a fit for purpose proposal will have:
- 185.1 Appropriate scope and specificity of information (specifying information requirements helps ensure this);

¹⁰⁷ For example: failure rates due to vegetation, equipment failure, or human error.

¹⁰⁸ ENA and PwC submitted that these factors did not align with the test required under the IMs. We disagree – these factors are likely to be relevant to establishing the level of performance that is realistically achievable by the EDB going forward. Understanding these factors allows us to consider whether the proposed level of investment (and if necessary policies) are targeted appropriately, to achieve the level of performance proposed.

¹⁰⁹ In line with the evaluation criteria, see for example the EDB IMs 5.2.1(f).

- 185.2 Information that we have confidence in and can rely on (this is assisted by requiring the supplier to have the proposal independently verified and audited); and
- 185.3 Evidence of how the supplier has determined the services required by consumers (as specified in the consumer consultation requirements).

186. We discuss each of the above requirements below.

Information requirements – appropriate scope and specificity of information

- 187. The CPP information requirements should ensure that we have sufficient information to be able to assess the applicant’s proposal and minimise the need to seek additional information after it has been submitted, and set an appropriate level of expenditure.
- 188. We consider that there is a place for both flexibility and prescription in the IM requirements.
 - 188.1 Prescription helps us ensure that we have the information we need in a CPP proposal to determine a path in the short statutory timeframe and provide an appropriate degree of certainty.
 - 188.2 However, flexibility can be used to focus the information required on the elements of the proposal that are most material (such as those driving the application or that have the greatest potential impact on price and quality). It can also allow suppliers to provide information in a timely and cost-effective way that aligns with their existing business practices.
- 189. The following paragraphs explain how we provide for both flexibility and prescription in our information requirements.

Base information – prescription

- 190. While the level of scrutiny that we apply to some elements may vary depending on the level of assurance we attain at a high level, and the materiality/impact of the element on price and quality, we consider that the base information requirements should be the same for all expenditure elements of a CPP proposal (this does not include the detailed information required for specific projects that are selected by the verifier).
- 191. It will not always be possible to determine what elements of a CPP proposal will require specific focus until we receive a completed application. Given this it is appropriate that all base information is required to be provided with a proposal to enable a top-down assessment to be undertaken.

Modifications and exemptions – flexibility

- 192. While we consider that it is generally preferable to have prescriptive information requirements to ensure we are able to determine a CPP in the statutory timeframes in some circumstances added flexibility is appropriate.

193. The exemption and modification provisions that we introduced as part of the CPP fast track process, allow us to agree with an applicant to modify or remove specific information requirements, provided it does not detract from our ability to assess a CPP proposal in a way that is more than minor.
194. We will use these provisions, where appropriate, to further reduce the cost and complexity of the information requirements, in line with the proportionate scrutiny principle, for example, where a supplier can provide the same information in a different format which better aligns with their existing business practices. If the provision of the information in that way does not impair our ability to evaluate the proposal, we are likely to agree to a modification to the information requirements to allow this.
195. We also consider that it will be appropriate to use the modification and exemption provisions to take account of supplier scale (discussed below in paragraph 202).

Detailed information – flexibility

196. We also provide for flexibility in the more specific detailed information which we require from a sample of "identified" programmes in order to ensure that high level policies and strategies are implemented (discussed at paras 353-361). This information is required from a sample of material/high impact projects selected by the verifier, rather than all projects. The selection of projects will depend on the specific proposal. We consider that the verifier is in the best position to decide how this flexibility should be exercised to ensure that a fair sample is taken that will allow the verifier to gain sufficient assurance.
197. In our 2010 IM reasons paper we stated that the expenditure information required in a CPP proposal was likely to be analogous to that typically supplied to a supplier's Board. On reflection, the provision of more detailed information will likely be necessary in order to determine the appropriate level of expenditure proposed in a CPP.

The relevance of supplier scale

198. In our 2010 IM decisions we also stated that we considered that the same information requirements should be set for suppliers of all sizes, as the same type of supporting information for proposed expenditure is relevant to all suppliers. We also said that we expected to apply the same degree of scrutiny to all proposals, regardless of size.
199. In theory, if a supplier was proposing a major increase in expenditure under a CPP we would ideally want to undertake a detailed review of that expenditure, regardless of the supplier's size – and only apply a reduced level of scrutiny if the expenditure under consideration is relatively low. If the CPP proposes to impose a material impact on consumer prices then, it is appropriate that the supplier would have to fully justify the increase. Consumers should be entitled to the same level of scrutiny irrespective of the size of the regulated supplier.

200. However, in practice, many of the costs associated with preparing, verifying and evaluating a CPP might not reduce significantly for a smaller supplier. Therefore, for smaller suppliers, the cost of applying for a CPP, could be significantly high compared to the supplier's total revenue, and subsequently the cost of applying for a CPP will have a material impact on the price path (as some of the costs of applying for a CPP can be passed directly on to consumers). In these cases the regulatory cost of higher scrutiny on a per consumer basis may well outweigh the benefit of that scrutiny to the consumer (through determining a "better", more robustly scrutinised, price-quality path).¹¹⁰
201. On reflection, we acknowledge the increased burden that a CPP could potentially be for small suppliers.
202. We consider that it may be appropriate in some circumstances to take account of the supplier's size when exercising our judgement in applying the modification and exemption provisions introduced as part of the CPP fast track.¹¹¹ For example, where a small business simply did not hold the information required, or it was completely unrelated to their proposal. Accordingly, we propose that we expressly specify in the IMs that the scale of the business and materiality of the CPP proposal on consumers will be factors that we will consider when deciding on whether to approve an exemption or modification.
203. We also consider that the scale of the supplier could be taken into account by the verifier in exercising their judgement in choosing identified projects for detailed review and for which more detailed information must be provided (discussed further below in Chapter 6).
204. In its submission on our draft decision, Aurora submitted that it was positive that we acknowledged the increased burden that a CPP could be for smaller suppliers. However, it considered that our proposed changes only went part way to removing the barriers faced by small and mid-sized EDBs.¹¹²
205. As we laid out in our draft decision, looking forward, we will continue to assess the ongoing viability of CPPs as the regime develops – including whether they are viable for smaller businesses (there could be a role here for summary and analysis to determine this). However, we consider that the exemption and modification provisions will be a useful tool to remove barriers for smaller suppliers. We encourage any suppliers considering a CPP to approach us to discuss how these provisions could be used to lessen the barriers to a CPP.

¹¹⁰ The example of Centralines coming in for a CPP demonstrates the extreme end of the scale. If the CPP preparation, verification and evaluation cost were \$1m (possibly a conservative estimate), this would be a regulatory cost of \$120 per consumer, across Centralines' 8,500 strong consumer base.

¹¹¹ Commerce Commission "Input methodologies review: Amendments to input methodologies for customised price-quality paths – Final reasons paper for limb 1 of the CPP fast track" (12 November 2015).

¹¹² Aurora "Submission – Input methodologies review: Draft decision and determination papers" (4 August 2016), p. 13.

Information that we can rely on – verification and audit

206. In order to ensure that we can evaluate and determine an appropriate customised price-quality path, we need to be able to rely on the information contained in a CPP proposal. As already discussed, we have a limited statutory timeframe in which we are able to do this.
207. The use of an independent verifier and auditor helps us ensure that we can rely on the information provided as part of a CPP proposal, so we can focus our evaluation on the key drivers of a CPP proposal.

Verification

208. We have a verifier to help support our assessment by ensuring that we can rely on the forecast capital expenditure, and operating expenditure included in the proposal that we receive from an applicant.
209. The key tasks assigned to the verifier are to:
- 209.1 provide an assessment of whether the CPP applicant's policies, strategies, and procedures are appropriate such that services will be provided efficiently and align with consumer demands;
 - 209.2 ascertain whether these policies, strategies, and procedures have been applied in practice;
 - 209.3 review the material aspects of the proposed CPP to ensure that it is sufficiently complete in content and that it supports the expenditure objective,¹¹³ prior to the Commission review;
 - 209.4 assess and report on the reasonableness of the assumptions made or practices used in developing the information that supports the CPP application, and to then report on any aspects that may warrant an in depth review by the Commission; and
 - 209.5 comment on the extent and effectiveness of the applicant's consumer consultation.
210. The verifier also has a role in selecting a sample of "identified" programmes for which more detailed information is required (as discussed in Chapter 6).

Audit

211. The auditor has a similar role to the verifier, but with a focus on providing us confidence in the quality of financial and quantitative information. The auditor's role is to ensure that financial and quantitative information provided is robust, reliable, and in compliance with applicable IMs.

¹¹³ The expenditure objective is one of the evaluation criteria discussed in para 220-222.

Consumer consultation

212. Setting a price-quality path that reflects consumer demands is an important consideration in determining a CPP that delivers long-term benefits to consumers.
213. Accordingly, we require that suppliers notify consumers of their proposed CPP application, and provide an opportunity for consumers to comment. This consultation should be meaningful and the supplier should, where possible, use it to support its proposed expenditure. This is particularly important when a supplier is proposing expenditure that will have a material impact on the price paid for services by consumers, or there is likely to be a significant change in the service quality experienced by consumers, or both.
214. The consumer consultation IMs require suppliers to inform and engage with consumers on the implications of the CPP proposal for consumers. We have previously seen that consumer consultation has been undertaken at a relatively high level, often with a starting presumption that consumers demand the current level of service, and survey questions that do not allow consumers to provide informed views on the trade-off between price and quality.
215. To support a CPP proposal, which by its nature is likely to include some step change in expenditure and/or service, we would expect that affected consumers will have been supplied with sufficient information on the likely outcomes for a range of investment scenarios. As a minimum, the information should allow consumers to make informed choices on relevant price and quality trade-offs.
216. We acknowledge that the supplier may have a better understanding of the need for network investment than its consumers, which is why we do not require consumer agreement. Rather, we will take the extent of consumer support into account when assessing the proposal, along with the supplier's explanation of this support (or opposition).

The CPP submission timeline – how the process comes together

217. All of these components come together as part of the CPP process. We have published a diagram at Attachment A which sets out a high level, indicative timeline, to illustrate how the process is intended to work in practice.

Summary of improvements to the CPP requirements

218. This section summarises the changes that we are proposing to make to the CPP requirements that support our evaluation of CPP proposals, which are explained in greater detail in the following chapters.
219. We consider that the intent of the CPP requirements IMs is generally still sound. However we are proposing to make a number of amendments to provide greater clarity and certainty, and to reduce the cost and complexity of the CPP process, in line with the IM review framework.

Evaluation criteria

220. We have reviewed the CPP evaluation criteria set out in the IMs and consider that it supports our approach to evaluating CPP proposals outlined above.
221. We have not made any changes to the evaluation criteria, as set out in the IMs.
222. We have provided some additional clarification as to how we intend to evaluate CPP proposals against these criteria within this paper as guidance.

Information requirements

223. At a high level, the changes we have made to the CPP information requirements are mostly intended to reduce the complexity and compliance costs of the CPP information requirements, and to focus these requirements on what is most material to price and quality.¹¹⁴ Where possible, our intent is for the information required in CPP applications to leverage off existing regulatory disclosures under information disclosure (**ID**), including asset management plans (**AMP**). At this stage, our changes relate to EDBs only, as we are deferring consideration of changes to the detailed information requirements for GPBs.
224. We have made the following changes to Schedules D and E to reduce the cost and complexity of preparing a CPP proposal, and ensure we have the information required to assess and determine a CPP. We have:
- 224.1 removed the need to duplicate information between documents, by aligning Schedules D and E with the relevant information disclosure requirements;
 - 224.2 aligned the cost allocation information requirements in the IMs and the ID Determination;
 - 224.3 improved the way in which applicants demonstrate the deliverability of their proposed expenditure;
 - 224.4 removed the perceived need to duplicate price path information;¹¹⁵
 - 224.5 reduced the level of disaggregation of information;
 - 224.6 allowed increased flexibility in providing information, and
 - 224.7 refined the information requirements for quality standards.
225. We have also clarified that the information presented in the financial spreadsheets referred to in the IMs does not need to be duplicated.
226. These changes are discussed in more detail in Chapter 5.

¹¹⁴ This approach is consistent with the proportionate scrutiny principle set out at paragraph 56.

¹¹⁵ By clarifying that information provided in spreadsheets can form part of the CPP proposal.

Verifier

227. The changes we have made to the verifier requirements clarify the verifier's role, and simplify the way suppliers and the Commission engage with the verifier.
228. The specific changes we have made are:
- 228.1 adding a new section to the verifier's Terms of Reference that defines the verifier's role, purpose, and obligations;
 - 228.2 removing the obligation for the verifier to consider non-standard depreciation and cost allocation;
 - 228.3 requiring the CPP applicant to provide us with a high level summary of their application;
 - 228.4 amending the tripartite deed requirements to include a communication protocol setting out the roles and obligations of the parties during the verification process regarding communication;
 - 228.5 Allowing the verifier greater flexibility in the number of identified programmes that are selected to be verified in detail as part of the verification process; and
 - 228.6 removing the requirement for an independent engineer, and allowing suppliers to prepare the quality standard variation report themselves, subject to verification by the verifier (EDBs only).
229. These changes are discussed in more detail in Chapter 6.

Audit

230. We propose to expressly require the auditor to provide an audit report, clarify the audit standards and quantitative accuracy, and align the scope of audit requirements with the information requirements.
231. These changes are discussed in more detail in Chapter 7.

Consumer consultation

232. Where possible, we expect that meaningful consultation with consumers should require the consideration of price/quality trade-offs by consumers. We are proposing to expressly require this as part of an applicant's consumer consultation requirements.
233. These changes are discussed in more detail in Chapter 8.

Chapter 5: Information requirements

Purpose of this chapter

234. This chapter explains the problems we have identified with the information requirements for CPP proposals, and our solutions to these problems.
235. These problems and solutions predominantly concerns the EDB CPP IMs, because we are deferring consideration of changes to the detailed information requirements for GDBs and GTBs.¹¹⁶ The exception is the requirements relating to cost allocation in Schedules B and C, which we have considered for EDBs and GPBs.

Structure of this chapter

236. The first section of this chapter summarises the changes we are making to the CPP information requirements. The remaining sections focus on specific problems we have identified with the information requirements, and our solutions to those problems. The key problems are:
- 236.1 misalignment of CPP information requirements and ID requirements;
 - 236.2 misalignment between the cost allocation information requirements in the IMs and the ID Determination.
 - 236.3 applicants were not required to demonstrate that they are able to deliver their proposed expenditure at a business-wide level;
 - 236.4 duplication of price path information within the CPP application;
 - 236.5 unnecessary disaggregation of certain information increasing the cost and complexity of CPP proposals;
 - 236.6 insufficient flexibility for suppliers providing the information, particularly for smaller suppliers increasing cost and complexity; and
 - 236.7 the quality standard variation information does not reflect how we set quality standards.

Summary of changes

237. At a high level, we consider that the policy intent behind the information requirements which we set out in 2010 remains relevant.¹¹⁷ The intent behind the information requirements is that the applicant will provide information which will allow us to test whether the CPP application meets the evaluation criteria and to determine a CPP.

¹¹⁶ Commerce Commission "Input methodologies review – Process update paper" (29 February 2016), para 59-66.

¹¹⁷ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.3.14-15.

238. The changes we have made are intended to reduce the cost and complexity of complying with the CPP information requirements, and to focus these requirements on information that explains, and is required to assess, the parts of the proposal that have the most material impact on price and quality. Our aim is for the information required in CPP applications to, where possible, better leverage off existing regulatory disclosures under ID, including suppliers' AMPs.

Changes discussed in this chapter

239. We have made a number of changes to address the problems we have identified through reviewing the CPP information requirements IMs, namely:
- 239.1 removing the need to duplicate information between documents, by aligning Schedules D and E with the relevant information disclosure requirements;
 - 239.2 aligning cost allocation information requirements in the IMs and the ID Determination;
 - 239.3 improving the way in which applicants demonstrate the deliverability of their proposed expenditure;
 - 239.4 removing the perceived need to duplicate price path information;¹¹⁸
 - 239.5 reducing the level of disaggregation of information on depreciation and tax;
 - 239.6 allowing flexibility in providing information, and
 - 239.7 refining the information requirements for quality standards.

Misalignment between requirements in Schedule D and ID

240. Schedule D of the IM Determination specifies the qualitative information to support the expenditure proposal. Qualitative information allows the supplier to provide context, reasoning, and justification for the quantitative data used in its proposal.¹¹⁹

Problem definition

241. Previously the information requirements in Schedule D were not aligned with the requirements for AMPs. For example, information provided in the AMPs was required to be recast and re-grouped in order to comply with the CPP IMs. This created a compliance burden for applicants, with limited benefit in terms of scrutiny.
242. In feedback on the Orion process, the ENA submitted that:

¹¹⁸ By clarifying that information provided in spreadsheets can form part of the CPP proposal.

¹¹⁹ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para K3.7.

We suggest that the CPP application process could be significantly simplified if the information requirements for a CPP proposal were better aligned to the information each business already has available for its operations, planning and compliance activities. This could include removing the compulsory status of some of the IM requirements, and linking the proposal content better to existing regulatory information, in particular AMPs.¹²⁰

243. PwC, submitting on behalf of 20 EDBs on our Problem definition paper, made a similar comment:¹²¹

[W]e consider that the CPP IMs should... enable EDBs to use their Asset Management Plans as the basis for their CPP applications. The key factors supporting the application should already be present in the AMP and the CPP application should build on this information incrementally in support of the proposed CPP price path and quality standards.

244. However, as Geoff Brown noted at our 19 April 2016 CPP workshop, the depth of information required for a CPP application goes beyond that required for AMPs.¹²²
245. In other words, the information we require to evaluate a CPP application is wider in scope than an AMP, which is focussed on asset management planning.

Solution

246. Our solution is to follow an 'AMP-plus' approach to Schedule D. To implement the AMP-plus approach, we have amended Schedule D to:

- 246.1 align its structure with the AMP requirements in Schedule A of the ID requirements; and
- 246.2 require additional information over and above the AMP requirements where it is necessary to justify the expenditure proposed in the CPP.

247. This approach was developed after discussions with stakeholders at our CPP workshop on 19 April 2016, and is based in part on a structure the ENA proposed.¹²³
248. The scope of the information that we require to be provided is summarised in the table below.

¹²⁰ ENA "Feedback on Orion customised price quality path process" (August 2014) para 33. Orion raised the same issue, Orion, "Feedback on Orion customised price quality path process" (August 2014) para 43, as did other submitters, Vector, "Feedback on Orion customised price quality path process" (August 2014) para 12; Powerco "Feedback on Orion customised price quality path process" (August 2014), para 20.

¹²¹ PwC "Submission to the Commerce Commission on input methodologies review: Invitation to contribute to problem definition (21 August 2015), para 121.

¹²² Commerce Commission "Input methodologies review – Summary of views from CPP workshop held 19 April 2016" (22 June 2016).

¹²³ PwC on behalf of ENA "CPP IM Reducing Cost and Complexity – Schedule D" (6 May 2016).

Table 5.1: Scope of Schedule D requirements

Information we require	Reason for inclusion
Information on policies on governance and descriptions of systems, management of information and data, treatment of risks and uncertainties.	To give us an understanding that the expenditure forecast is prepared using good practice asset management principles and methodologies expected of a prudent supplier.
An overview of any internal challenge, review and approval process applied before the forecasts were finalised for inclusion in the CPP proposal.	To ensure that the proposal has been properly challenged. Different business units prepare parts of the expenditure plan. This can result in duplication of expenditure items or resource requirements. A robust challenge process at a business-wide level can remedy this.
Key assumptions and information on data and models used to prepare the forecast.	To ensure that the inputs used to prepare the forecasts are sound, and that the investments are made at the right time. This includes the reliance we can place on data used and how data deficiencies have been addressed.
Strategies, policies, rationale for policies and planning standards.	To ensure that the relevant strategies are in place and that they are appropriate and sufficiently robust to ensure that the services will be provided efficiently.
The process or approach used to develop the forecasts.	To assess the validity of the forecasts.
Detailed information on identified programmes.	To ensure that the forecast expenditure is consistent with the applicant's strategies, policies and processes.
Forecasts of consumer connections, distributed generation, electricity volumes carried, and maximum demand.	To provide the background necessary for an informed assessment of the application.
A high level description of all network development projects included in the forecast.	To provide an overview of the development projects included in the CPP proposal.
A description of how the business support and system operations and network support operations are organised, and the extent that these operations are shared with unregulated business activities and the extent to which the cost of these activities are capitalised.	To provide an insight into the relevance of existing costs and how they are split between opex and capex, and between regulated and unregulated business activities.
A description of any anticipated changes to this information over the forecast period.	To provide a high level understanding of the reasons for increases in the forecast expenditure over the forecast period, particularly if they are step changes.

Information we require	Reason for inclusion
A detailed description of the drivers for opex programmes and explanation of the basis for determining the forecast increased or new expenditure requirement.	To assess the reasonableness of opex expenditure forecasts.
Information that demonstrates the deliverability of the applicant's work volumes represented by a CPP expenditure forecast (to the extent that these are higher than current levels).	To show that they have considered delivering the work volumes in the CPP, where these are higher than current levels. This is to avoid setting revenue based on expenditure that an applicant does not have the capacity to deliver.

249. As these changes draw an explicit link between Schedule D of the IMs and Attachment A of the ID determination, adopting this AMP-plus approach will also have the following flow-on effects:

- 249.1 we will have to reconsider and potentially amend the Schedule D of the IMs when we review the ID determination (increasing our resource requirement at that time);
- 249.2 there could be a degree of uncertainty for a prospective CPP applicant during any period when we review the ID determination. In their response to the draft decision, submitters disagreed that this would be an issue;¹²⁴ and
- 249.3 the completeness assessment of a CPP will not be mechanistic, and may require a greater degree of communication between the applicant and the Commission during this phase of assessing a CPP proposal.¹²⁵

Improvements to cost allocation information- Schedules B and C

- 250. We did not propose any changes as part of our draft decision, to the cost allocation information required in Schedules B and C.
- 251. Submissions on the draft decision suggested that these schedules should be replaced by the equivalent tables in the ID determination and suggested a number of drafting refinements that could improve the consistency and workability of the schedules.¹²⁶

¹²⁴ For example: ENA "Submission on IM review draft decision – CPP requirements" (4 August 2016), para 73.

¹²⁵ The applicant could reduce this by thorough cross-referencing and presenting the AMP in manner suitable for assessing completeness.

¹²⁶ See, for example: PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers" (4 August 2016) para 189.

252. We have now changed the tables in Schedules B and C and amended relevant subclauses of 5.4.9 to ensure that they:¹²⁷
- 252.1 align with the requirements under the ID determination; and
 - 252.2 clearly specify what information is required.
253. We consider that these changes will reduce the cost and complexity of compiling this information for CPP applicants.

Introducing a materiality threshold for updated information

254. We have also introduced a materiality threshold so the CPP applicant does not need to submit updated information, for Schedules B and C, during the assessment of the CPP application unless the value allocated to the regulated service changes by 5% or more. This is intended to reduce compliance costs on the CPP applicant during the CPP application process, where the change in value is not significant, and is therefore less likely to have a material impact on price.

Considering the overall deliverability of the work plan

255. The CPP information requirements require suppliers to explain the deliverability of each opex and capex category and identified programme.¹²⁸ This requirement was included in the IMs to ensure that the applicant is able to demonstrate that it is not constrained in its ability to carry out the work in the timeframes.¹²⁹

Problem definition

256. The pre-review CPP information requirements did not require the supplier to report on deliverability at a whole-of-business level. This meant that while each category or programme of expenditure may be deliverable, when taken as a whole the proposal may not be.
257. This created a significant risk that expenditure would be approved for work that is both prudent and efficient, yet due to insufficient resources the EDB would be unable to deliver it. The result of non-delivery would be that consumers would pay for beneficial outcomes that would not be realised.

¹²⁷ We consulted on the drafting of these tables as part of our technical consultation. See Commerce Commission "Input methodologies review – Technical consultation update paper" (13 October 2016).

¹²⁸ Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26, Schedule D7(1)(b), D7(2)(b), D12(1)(b), and D12(2)(a)(ii).

¹²⁹ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.5.12.

Solution – requirement to report on overall deliverability

258. Our solution to this problem is to require applicants provide a deliverability risk assessment that takes account of:
- 258.1 regulatory consents required;
 - 258.2 accommodating a step change in workload above historical levels;
 - 258.3 alignment of resource schedules where shared resources are utilised for different opex and capex-related tasks;
 - 258.4 the extent of outsourcing required; and
 - 258.5 contractor and skilled personnel availability and ability.
259. We expect that CPP applicants will have fully assessed the deliverability of the proposed work-plan required to achieve the objectives set out in their CPP application. Accordingly, the provision of this information should not require the applicant to create any additional information.
260. In submissions on our draft decision Powerco, PwC and ENA supported the consideration of deliverability as part of our CPP evaluation, and the inclusion of information requirements to support this.¹³⁰ As suggested in these submissions, we have made minor changes to these requirements to ensure that deliverability is considered as a whole and not at the individual project level.

Removing duplication of price path information

261. The information requirements require CPP applicants to include annual dollar amounts (in nominal terms) for the applicant's proposed building blocks allowable revenue (BBAR) for each year of the proposed CPP regulatory period. The IMs also require the applicant to provide all the supporting information used to calculate the proposed BBAR amounts.

Problem definition

262. The pre-review CPP requirements were not explicit about whether the spreadsheets are part of the CPP proposal. This omission led Orion to duplicate the information, increasing the cost of preparing its application.

¹³⁰ Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016); PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers – Made on behalf of 17 Electricity Distribution Businesses" (4 August 2016); ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016).

263. The IMs state that the applicant must provide the calculations for BBAR and maximum allowable revenue (MAR) in spreadsheet form.¹³¹ However, the IMs did not explicitly state that these spreadsheets form part of the CPP proposal.¹³²
264. In feedback on the Orion process, the ENA indicated that the IMs were not flexible enough, and prevent information in the price path model from forming part of the CPP application. Therefore, Orion needed to replicate all of the outputs for each of the building blocks.¹³³

Solution – clarify that information can be provided in spreadsheets

265. Our solution to this problem is to clarify that the information included in the spreadsheets does form part of the CPP proposal. Applicants have the option of relying on information provided elsewhere, provided certain usability requirements for providing information in spreadsheet form are met.
266. As part of our draft decision we set out these expectations for how this information should be provided, but did not make a change to the IMs. Submissions suggested that we should expressly set out how this information must be provided in spreadsheets, in the IMs.¹³⁴
267. We have now changed the IMs to set out the criteria that must be met by an applicant when providing information in spreadsheet form. For example the applicant must provide cross-references.¹³⁵ We consider that this change will allow us to better assess CPP proposals, by ensuring that we receive spreadsheet information presented in an appropriate and useful way.

Reducing the level of disaggregation of information

268. The pre-review CPP IMs required information to be provided at a highly disaggregated level, including the very granular asset type level.

Problem definition

269. We consider the requirements to provide certain information at a highly disaggregated level imposes additional cost and complexity, while producing little value in terms of assessing the proposal and determining the price path.

¹³¹ *Electricity Distribution Services Input Methodologies Determination 2012* [2012] NZCC 26, clause 5.4.7-5.4.8.

¹³² Commerce Commission "Electricity and gas input methodologies determination amendments (No.2) 2012, Reasons paper" (15 November 2012), paragraph K2.8 states that the Commission intends to develop a revenue model template that is consistent with the IMs, which a supplier may use in preparing its proposal. The spreadsheet model will not be part of the IM. However, this note is referring to the Commission's revenue model.

¹³³ ENA "Feedback on setting Orion's customised price-quality path" (14 April 2014), Attachment 1, Section 3.

¹³⁴ See, for example: ENA "[DRAFT] Electricity Distribution Services Input Methodologies Determination 2012" (18 August 2016), p. 151-152.

¹³⁵ These criteria are set out in the EDB IMs at 5.4.7 and the GDB and GTB IMs at 5.5.5.

270. Specifically, we were concerned with suppliers needing to provide:
- 270.1 forecasts of capex disaggregated by asset type, for the purposes of asset valuation, depreciation and regulatory tax;¹³⁶
 - 270.2 expenditure forecasts disaggregated by service categories;
 - 270.3 opex disaggregated into controllable and uncontrollable opex;¹³⁷ and
 - 270.4 related party transaction information that must be disclosed by forecast capex programmes and projects;¹³⁸ and
 - 270.5 forecasts of capital contributions by asset type.

Depreciation and tax

271. Forecasting on an asset type basis adds complexity to CPP proposals, and increases the cost to applicants. While this level of disaggregation is consistent with the requirements under ID, the ID requirements are completed on an *ex-post* basis. Those requirements are necessary for *ex-post* reporting of commissioned assets. Since the CPP information requirements are completed on an *ex-ante* basis, the value of forecasting in such detail is questionable given its complexity.

272. Orion suggested that:

In addition, the IMs require material to be presented in a specific way that did not align with processes and information sources we hold. For example:

The asset valuation and regulatory tax IMs which are components of the price path require a great deal of disaggregation of forecast data which creates model complexity and it is questionable whether this is necessary.¹³⁹

273. The ENA echoed this, suggesting that the Commission:

Reduces the level of disaggregation inherent in the forecasting methods for the regulatory asset base and regulatory tax allowance/adjustments. These are currently based on the ID methods, which are relatively precise (given they are prepared *ex-post*). We question whether this is necessary or appropriate for *ex-ante* forecasts, and a more simple/aggregated forecasting approach may be reasonable (i.e. generate sensible forecasts) and, importantly, is likely to be less costly to prepare and support. We note that the DPP methods are extremely aggregated, and we do not consider this level of aggregation is a reasonable approach for a CPP.¹⁴⁰

¹³⁶ *Electricity Distribution Services Input Methodologies Determination 2012* [2012] NZCC 26, cl 5.4.12.

¹³⁷ *Electricity Distribution Services Input Methodologies Determination 2012* [2012] NZCC 26, cl 5.4.30(3); Schedule D16; Schedule E, Table 3(b).

¹³⁸ *Electricity Distribution Services Input Methodologies Determination 2012* [2012] NZCC 26, Schedule E, Table 4 and Table 5.

¹³⁹ Orion "Orion feedback on customised price quality path process 14 April 2014" (August 2014), para 41.

¹⁴⁰ ENA "ENA feedback on Orion customised price quality path process" (August 2014), para 6.1 (b).

274. We have changed the IMs to reduce the level of disaggregation for this information. We now require a breakdown for depreciation by asset category, and only require aggregated values for regulatory tax asset values.
275. We consider that the aggregated levels we have specified will still provide a reasonable estimate of forecast depreciation and tax for the purpose of determining the price path. We now require:
- 275.1 forecast depreciation to be provided by asset category; and
 - 275.2 the forecast regulatory tax asset value to be provided at the aggregated level as the sum of tax asset values.¹⁴¹
276. However, given the variability in timing of projects, the value of more detailed forecasting is questionable. For example, a supplier cannot forecast exactly when it will commission a given power transformer, and using an estimate will not make the resulting calculations any more accurate.¹⁴²
277. While we have specified that information on the forecast regulatory tax should be provided at the aggregate level in the CPP proposal, we may request information at a more disaggregated level when assessing the proposal, if we consider that more disaggregated information is necessary for us to determine the CPP.
278. In coming to our solution on forecast depreciation, we also considered the following alternatives:
- 278.1 using the DPP approach of assuming a 45 year asset life to estimate the value of depreciation of forecast commissioned assets;
 - 278.2 disaggregating by asset type at an aggregate value of commissioned assets level rather than at a project level; and
 - 278.3 disaggregating by asset expenditure categories at aggregate value of commissioned assets level.¹⁴³
279. We consider that the solution that we have chosen provides the best balance of sufficient accuracy and without undue cost and complexity.

Controllable and uncontrollable opex

280. Disaggregation of opex forecasts as controllable and uncontrollable was originally included in the information requirements to make allowance for IRIS. However, our approach to IRIS has changed, and this type of disaggregation is no longer required.

¹⁴¹ Both Powerco and ENZ have submitted that disaggregation tax information by asset category is costly.

¹⁴² However, we note that, at a macro level, a supplier should be able to forecast the increased number and capacity of its transformer assets and how the utilisation will change over time.

¹⁴³ These alternatives were discussed at our CPP information requirements workshop (held 19 April).

281. We have removed the requirement on suppliers to disaggregate based on service categories or into controllable and uncontrollable opex. These changes bring the CPP information requirements in line with the requirements under ID, eliminating the need to recast information in an unnecessary way.

Related party transactions

282. Forecasts on a project-by-project basis are appropriate in other instances, but it is not feasible to forecast related party transactions on this basis. It is not possible to forecast who will deliver which projects if the projects are awarded via competitive tendering.¹⁴⁴ Tenders are called after a project is set up and scoped and would normally be at the time of implementation, not several years in advance.
283. We have removed the requirement to disaggregate forecasts project-by-project, and instead to require forecasts on an aggregated basis across the business.
284. In response to submissions on our draft decision we have also made further changes to the related party information requirements.¹⁴⁵
285. Schedule D of the IM seeks information on related parties such as the nature of service provided, contractual terms and method of valuing the contract.
286. ENA proposed that the related party information requirements in Schedule D should focus on information on contracts that are in place in the last year of the current period, those that will be ongoing into the future, the process used to procure the services and the basis of valuing that service.
287. We have decided to adopt the ENA's suggestions. These changes clarify the information requirements for related parties. Specifically the CPP applicant is required to:
- 287.1 identify and describe any current, ongoing or potential future contracts with related parties or anticipated related parties;
 - 287.2 describe the relationships with, and services provided by, related parties; and
 - 287.3 describe the processes for procuring services from related parties or anticipated related parties, including the methodology used to value the services.

Capital contributions

288. Stakeholders have submitted that it may not be practical to forecast capital contributions at an asset level as currently required and that it is more practical to

¹⁴⁴ The exception is if there is a long term service agreement with the related party.

¹⁴⁵ See, for example: ENA "Submission to the Commerce Commission on input methodologies review: Draft decisions papers" (4 August 2016), p. 22.

forecast capital contributions at an aggregate level. The changes to information requirements in Schedule E have simplified the information requirements for forecast capital contributions by netting them off against forecast total values of the capex expenditure categories.¹⁴⁶

Greater flexibility afforded when providing information

289. As mentioned in Chapter 4 there is significant diversity in the size of price-quality regulated EDBs, which has practical implications for the relative cost/benefits of making of CPP application.¹⁴⁷

Problem definition

290. The IMs specify the provision of expenditure information, policies, procedures, and strategies at a scope and depth that may exceed the levels of information that a prudent supplier of that size would maintain.
291. In such cases, the supplier will either incur costs to create the information, or will decide that the compliance cost outweighs the benefits that might be expected to accrue from a CPP application.
292. Requiring suppliers to create expenditure information, policies, procedures, or strategies solely to apply for a CPP might not benefit our evaluation of the proposed expenditure. If the supplier's investment decision has been made independent of some of the information required for a CPP application, creating and including this information might not improve the scrutiny we can apply, or to benefit consumers.
293. PwC, submitting on behalf of 20 EDBs (including several smaller price-quality regulated EDBs), commented in submissions on the problem definition for the IMs review:

In order to make the CPP a more viable option we suggest that the CPP IM should be less prescriptive. The IM should allow an applicant to present their case for an alternative price path and quality standards using information which is directly relevant to their application, and is based on information retained by the EDB which supports the EDB's own planning and operating practices. While we understand the need for the Commission to receive comprehensive information in support of a CPP proposal, we consider the IMs can be substantially improved by allowing EDBs more flexibility in how they compile this information. This is not inconsistent with the expectation that well run EDBs will have sufficient information available in support of their application.¹⁴⁸

294. However, in contrast to PwC's observation, we are commonly asked to be more specific about the information we require.

¹⁴⁶ Capital contributions are netted off as they are not part of the regulated revenue.

¹⁴⁷ Other issues related to supplier scale and CPP applications are discussed in Chapter 4.

¹⁴⁸ PwC "Submission to the Commerce Commission on input methodologies review: Invitation to contribute to problem definition (21 August 2015).

295. Accordingly, there is clearly a trade-off between the certainty provided through greater specificity, and allowing for greater flexibility where the applicant proposes the appropriate level of information.

Solutions

296. We consider that greater flexibility for suppliers, in particular smaller ones, is warranted. The extent of the flexibility we propose providing will depend on the specific circumstances of an application.
297. Where an applicant has not relied on a particular policy, procedure, or strategy in preparing its CPP application, we do not expect the applicant to create these for completeness sake. The pre-review IMs did not require this.
298. Where an applicant has relied on a particular policy, procedure, or strategy in justifying its expenditure, but that policy is not formally documented, we require the applicant to provide an explanation. For example, if the CPP application includes an increase in capex to support an increase in security and reliability to part of its network (eg, inner CBD), and this was driven by a change to the applicant's planning criteria, we would require that policy to be provided with the CPP application. However, if there was no policy underpinning this decision, we would likely question the basis on which the applicant decided to change the level of security.
299. Therefore, regardless of the size of the supplier's business, we expect applications will provide sufficient supporting justification commensurate with the materiality of the expenditure.
300. In addition, the Limb 1 CPP fast track amendments introduced provisions which allow for exemptions and modifications from the CPP information requirements. These provisions will also help mitigate any specific information requirement challenges facing smaller suppliers.¹⁴⁹
301. To make our intent clear, we have amended the IMs to expressly specify that we will consider the scale of businesses when deciding whether to approve an exemption or modification.
302. In order to keep the IMs less prescriptive we have decided not to make some of the changes requested in submissions on our draft decision. These include:
- 302.1 Powerco submitted that we need to clarify what is deemed to be 'sufficient information' in subclause D10(1).¹⁵⁰ We did not make this change. We consider that the IM explains the purpose of this information and we are leaving it to the applicant to provide the extent of information that in their view will allow us to assess the information provided it meets that purpose.

¹⁴⁹ Commerce Commission "Input methodologies review: Amendments to input methodologies for customised price-quality paths – Final reasons paper for limb 1 of the CPP fast track" (12 November 2015).

¹⁵⁰ Powerco "IM review draft determinations submission" (4 August 2016), paragraph 13.

- 302.2 ENA submitted that we should clarify how ‘constant prices’ are to be presented for the ‘current period’. We have not made this change and prefer to provide the applicant with flexibility to present this in a manner consistent with its business practice.

Information on quality standards

303. We have made two changes to the information requirements on quality standard variations.

Removing the requirement to show effect of variation if applied for previous 5 years

304. When a supplier proposes a quality standard variation as part of a CPP proposal, the IMs previously required that the supplier provide information demonstrating the estimated effect of the proposed quality standards had the proposed quality standards applied over the previous 5 years. We have also removed the reference to 5 years, to allow some flexibility in how the supplier demonstrates the estimated historical effect of the proposed quality standard variation, as suggested by submissions.¹⁵¹

305. We may still request further information if the supplier does not provide adequate information for us to assess the quality standard variation proposal.

Updating quality standard variation information to reflect how we set quality standards

306. Where an EDB CPP applicant proposes a change to the quality standards set under the DPP, as part of a CPP proposal (a quality standard variation), they are required to submit certain information relating to the proposed quality standard variation.

307. In response to our draft decision, PwC submitted that information on proposed quality standard variations could be improved to:

307.1 reflect the changes to how we set quality standards which were introduced in the recent EDB DPP Determination;

307.2 remove references to earlier DPP quality standard terms; and

307.3 reflect the fact that alternative methods of setting quality standards may have different properties.¹⁵²

308. In line with PwC’s submission we have updated the information required for suppliers proposing a quality standard variation as part of a CPP proposal to better reflect how we currently set quality standards.

¹⁵¹ See, for example: ENA "[DRAFT] Electricity Distribution Services Input Methodologies Determination 2012" (18 August 2016), p. 151.

¹⁵² PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers – Made on behalf of 17 Electricity Distribution Businesses" (4 August 2016), para 189.

309. However we have also retained the reference to earlier DPP quality standard terms – namely the mean and standard deviation of the proposed SAIDI and SAIFI. While we may no longer set the quality standards using these metrics, we consider that this information can be easily generated by the EDB and can be useful in our assessment.

Further improvements to information requirements

310. We have made a number of additional changes to further reduce the cost and complexity of complying with these information requirements and improve clarity in the schedule.

Areas where we have made further improvements

311. Submissions identified parts of the information requirements that created unnecessary cost and complexity, and that lacked clarity. Specifically we have addressed issues with:
- 311.1 the information requirements for unit costs and cost escalators;
 - 311.2 the information requirements for industry costs; and
 - 311.3 the alignment of the definition of asset category with the ID determination.

Unit costs and expenditure escalators

312. We have increased flexibility in the manner in which CPP applicants can provide information on cost escalation. This should reduce cost by allowing suppliers to provide this information in a way that is better suited to their existing practices.
313. To support increased flexibility, we are also requiring the applicant to justify its methodology, key assumptions and the resulting values and explain why these are reasonable.
314. We have removed the requirement to provide detailed information on unit costs as part of the proposal. However, when assessing a CPP proposal the Commission may require the applicant to provide this information, if it is pertinent to the specific CPP proposal.

Industry costs

315. We have removed the requirement for the applicant to compare its unit costs with average industry-wide unit costs, because submissions stated that average industry-wide unit costs were not available. We consider that we will be able to deduce this information from the data on industry costs available either to us or in the public domain.

Aligned definition of asset category with the ID determination

316. We have made changes to the definition of asset category. The new definition aligns with the manner in which asset category is used in the EDB ID Schedules 4 and 5.

317. Powerco submitted that we should remove the definition of asset category from the IMs. Instead of removing this definition, we decided to redefine 'asset category'.
318. By aligning the usage of asset category in the EDB ID Determination and the EDB IM, we have improved clarity and reduced the complexity of providing information.

Chapter 6: Verification requirements

Purpose of this chapter

319. This chapter explains the problems we have identified with the verification requirements for CPP proposals, and our solutions to these problems.¹⁵³

Structure of this chapter

320. The first section of this chapter summarises our changes to the CPP verification requirements. The next section addresses the common problems we have identified with the verifier's role and purpose.
321. The following sections focus on specific problems we have identified with the verifier requirements, and our solutions to them. These problems relate to:
- 321.1 the way the applicant and the verifier communicate;
 - 321.2 the number of identified programmes the verifier scrutinises;
 - 321.3 the role of the independent engineer; and
 - 321.4 the verifier's review of non-standard depreciation and cost allocation information.
322. The final section responds to other issues raised by stakeholders, where we consider no change to the IMs is required. These issues are:
- 322.1 the way the verifier is selected and engaged;
 - 322.2 the time available for verification; and
 - 322.3 the verification of the extent and effectiveness of consumer consultation.

Summary of changes

323. We consider that the intent behind the verifier requirements set out in 2010 remains appropriate.¹⁵⁴ The pre-application verification process is intended to promote certainty for suppliers as to how their expenditure is likely to be assessed, as well as to assist us to make the most effective use of the tight statutory timeframes for evaluating CPP proposals, through the verifier highlighting which areas of a proposal we should focus on.
324. The changes we have made to the verification requirements are intended to clarify the verifier's role, and simplify the way suppliers and the Commission engage with the verifier. The overall intent of these changes is to provide greater certainty for

¹⁵³ Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26, clause 5.5.2 and Schedule F.

¹⁵⁴ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.6.3 and 9.5.13.

suppliers – consistent with the s 52R purpose – while at the same time reducing the cost and complexity of CPP proposals.

325. The specific changes we have made are:

- 325.1 adding a new section to the verifier’s Terms of Reference in Schedule G of the IMs that defines the verifier’s role, purpose, and obligations;
- 325.2 requiring the CPP applicant to provide us with a high level summary of their application by the time the verifier is engaged;
- 325.3 amending the requirements in Schedule F5 to require the tripartite deed to include a communication protocol. This change will require the deed to set out the roles and obligations of the parties during the verification process regarding communication, and will allow meeting minutes to be used as the evidential basis for any of the verifier’s technical opinions;
- 325.4 allowing the verifier greater flexibility in the number of identified programmes that are reviewed,
- 325.5 removing the obligation for the verifier to consider non-standard depreciation and cost allocation information;
- 325.6 removing requirement for an independent engineer to review any proposed quality standard variation, and instead allowing suppliers to prepare the report themselves, subject to verification by the verifier (EDBs only); and
- 325.7 limiting the requirement for the verifier to provide us with a list of all information provided to it by the applicant, to information *relied upon* by the verifier in fulfilling its obligations under Schedule G.

Verifier’s purpose and role

- 326. A common problem across the issues stakeholders have identified with the current verifier requirements is that the purpose of the verifier and their role is not clear.
- 327. In 2010 we explained that the purpose of the verifier had two key components:
 - 327.1 ensuring we can rely on the information supporting the CPP; and
 - 327.2 highlighting the key issues we should focus on during our assessment, to avoid duplication of effort.

328. We explained the reliability point in our 2010 IMs reasons paper saying:¹⁵⁵

It is also important that the Commission is able to rely on information contained in a CPP proposal. Therefore, the Commission considers that the proposal should be verified in some way before it is submitted to the Commission. The key considerations when selecting the appropriate form of verification are how critical the information is to the decision and the amenability of the information to the different types of verification [including] independent opinions on information by a subject matter expert (referred to as 'independent verification').

329. In addition, we explained that:¹⁵⁶

A key aspect of the Commission's expenditure approach is the use of pre-submission verification (prescribed by the Commission) of proposed expenditure by an independent verifier. This should promote certainty for suppliers as to how their expenditure will be assessed, as well as assist the Commission in managing the tight statutory timeframes for assessment. Suppliers have an opportunity to rectify any concerns raised by the verifier before it applies for a CPP and the process should allow the Commission to focus on the most important aspects of the CPP proposal during its assessment period.

330. We also stated that where possible, we would not seek to duplicate the effort expended in the verification of a CPP proposal:¹⁵⁷

The Commission will need to undertake its own assessment of the proposal in order to make a s 52P determination as is required under the Act. In doing so, to the extent practicable, the Commission will seek to avoid duplication of effort and to rely on the professional opinion expressed by the verifier.

Problem definition

331. Our experience with the Orion CPP suggests that we have not made it entirely clear that the intent behind the verifier role is to 'frontload' as much of the evaluation work as possible to reduce the pressure on the Commission of evaluating the CPP proposal and determining a CPP in a tight statutory timeframe. This lack of clarity in intent led to issues during the Orion CPP process. For example, we expected that the verifier would assess the reliability of the input data used to form the expenditure forecast, and the key assumptions made by Orion. Equally, we expected that the verifier would have understood and assessed the extent to which the proposed expenditure was required to meet service level requirements and quality demanded by customers.
332. Submissions on the Orion CPP process show the importance of frontloading and avoiding duplication, with several submissions questioning the necessity of the

¹⁵⁵ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.6.3.

¹⁵⁶ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.5.13.

¹⁵⁷ Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.6.1.

verification process where there was a perceived duplication of effort by the Commission.¹⁵⁸

333. For example, Vector submitted:¹⁵⁹

In practice, it seems that the IM requirement for a verifier has resulted in duplication of effort, unnecessary expense and confused expectations. We therefore question the need for a verifier as specified in the IMs; although the verifier role may be worth retaining if the verifier was also utilised throughout in the process to assist the Commission in reviewing the CPP application.

334. Another reason that frontloading is important is because potentially we may evaluate four (or more) EDB CPP proposals in any one year, and these must be considered within 150 working days. Understanding resource requirements and the nature of the proposal(s) will be crucial to us planning a cost-effective evaluation process.

335. Orion observed that there was some confusion about whether we should have had sight of the draft version of its application provided to the verifier. In addition, the verifier for Orion's proposal considered we would have liked some advance notice of the proposal, so we could have planned our evaluation around the likely contents of what was going to come in, but it considered the draft to be confidential.¹⁶⁰

Solution – Expressly lay out verifier's key purpose and role

336. Our solution to the lack of clarity about the purpose and role of the verifier is to add an additional section to the verifier's Terms of Reference (Schedule G2 of the IMs) that clearly sets out expectations for the verifier's role.

337. The new section of Schedule G explains that the role of the verifier is to:

337.1 provide an assessment of whether the CPP applicant's policies, strategies, and procedures meet the expenditure objective;

337.2 ascertain whether these policies, strategies, and procedures have been applied in practice;

337.3 review the CPP proposal to ensure that it is sufficiently complete in content, prior to the Commission review;

¹⁵⁸ ENA "Feedback on Orion customised price-quality path process" (14 April 2014), para 20; Powerco "Feedback on Orion customised price-quality path process" (14 April 2014), para 25. We note that Orion described the role of the verifier as a "valuable" one, while at the same time expressing concern about the duplication of effort, Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 19-20.

¹⁵⁹ Vector "Feedback on Orion customised price-quality path process" (14 April 2014), para 13.

¹⁶⁰ Orion's submission on the problem definition paper "Submission on the IM review" (21 August 2015), para 62; Denis Jones (Orion) "Cost-effectiveness of the rules and processes for CPP application" (presentation at the Commerce Commission input methodologies review forum, Wellington, 29 July 2015), p. 252.

- 337.4 assess the extent to which the CPP applicant is able to deliver its capex and opex forecasts during the regulatory period;
 - 337.5 to report on the extent and effectiveness of the supplier's consultation with consumers; and
 - 337.6 provide a list of the key issues which the Commission should focus on when assessing the CPP proposal.
338. In response to submissions on our draft determination, we have made several changes to our draft proposals to improve clarity of the role and ensure consistency with the terminology used elsewhere in the IMs, for example, by linking the verifier's assessment of the applicant's policies to the expenditure objective.¹⁶¹

Solution – High level summary

339. We have introduced a requirement for the applicant to provide us with a high level summary of its proposal, prior to engaging the verifier, to enable us to undertake our preliminary resource planning for our evaluation of the CPP proposal.
340. Some suggested not including this requirement.¹⁶² They considered that the level of detail required was too high and was required to be provided too early in the process.
341. Submissions also considered that the value of the summary would not outweigh the increased cost and complexity. Some submitters also suggested that the information could be better provided in other ways, such as through a workshop with the Commission.¹⁶³
342. We consider that the provision of a high level summary, early in the CPP process will allow us to plan appropriate resources for the evaluation of the CPP proposal, which occurs in a tight statutory timeframe. It is not intended to be a burdensome requirement. To ensure this is not the case, we have made some refinements to reduce the level of information required and allow the information to be provided through a workshop instead, with our agreement. We consider that these changes should ensure that we have access to the information we need to plan our evaluation process, without placing undue cost and complexity on the supplier.

¹⁶¹ See, for example: ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), para 91.

¹⁶² See ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), p. 7 and 24; Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 29 and 45; Orion "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 86-88.

¹⁶³ Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 29 and 45.

343. The high level CPP proposal summary will require information on:
- 343.1 at a high level, the rationale for seeking a CPP, including a brief explanation of key projects linked to this rationale;
 - 343.2 when the proposed CPP will take effect;
 - 343.3 an estimate of the capex and opex forecasts for the intended CPP proposal;
 - 343.4 the likely anticipated change/effect on prices;
 - 343.5 whether the supplier intends to propose a quality standard variation as part of the CPP proposal, and if so, the indicative impact on quality standards of the intended variation;
 - 343.6 the supplier's proposed approach to engaging with consumers on the proposal; and
 - 343.7 any other information it considers would assist us in planning the assessment of its CPP proposal.

Communication between the applicant and verifier

Problem definition

344. In the Orion CPP, we required that the verifier's conclusions in the verification reports were supported by a verifiable paper trail. Geoff Brown Associates (GBA) – the verifier for Orion – stated that this requirement created an onerous "paper trail" of information. GBA stated that the technical judgements made by the verifier need to be recognised as such, without reference to detailed supporting information.¹⁶⁴
345. However we are concerned that we may need to make reference to conversations between the applicant and the verifier during the consultation process, and that doing so in a transparent way may be difficult in the absence of a written record.

Solution

346. The verifier and applicant need to have the ability to have open technical discussions to resolve issues on an informal basis. We acknowledge that requiring documentation of every verifier opinion is costly and onerous. However, we do need to reference these discussions if they have been used to form verifier opinions.
347. We expect that, in most cases, the verifier will form its views and technical judgements on documented information and data. Providing references to support technical judgements is expected for an expert witness report, and we expect this level of diligence from the verifier.

¹⁶⁴ Geoff Brown (Geoff Brown Associates) "Cost-effectiveness of the rules and processes for CPP application" (presentation at the Commerce Commission input methodologies review forum, Wellington, 29 July 2015), p. 254.

348. We have amended the tripartite deed requirements in Schedule F5 of the IMs to include a communication protocol that sets out the roles and obligations of the parties during the verification process regarding communication and to allow meeting minutes to be used as the evidential basis for any verifier technical opinions.
349. The main reason for this change is that it will result in a more efficient and cost-effective verification process. For example we may agree with the parties that the verifier may contact us to discuss our interpretation of the IMs and the verifier's obligations under Schedule G, in order to provide greater clarity of how we will assess the applicant's proposal.
350. We have also changed the requirement for the verifier to provide us with a list of all information provided to it by the applicant.
351. We have limited the list required in the verifier's report to information relied upon by the verifier in fulfilling its obligations under Schedule G.
352. This will remove the requirement for the verifier to record all information provided to it by the CPP applicant, but will still ensure that the information relied on is documented for the Commission's assessment.

Number of identified programmes

Problem definition

353. Submitting on the Orion CPP, stakeholders suggested that the IMs should allow the verifier to pre-select sample projects or programmes ('identified programmes') for review, rather than have the sample projects selected later in the process. This would allow sufficient evidence on the pre-selected projects to be prepared in advance, making the process more efficient.¹⁶⁵
354. Orion also pointed to the fact that had there been a smaller number of projects to require detailed review, the cost of the application would have been reduced. In Orion's case, projects had to be artificially constructed and defended to meet the requirements.¹⁶⁶
355. Stakeholders have also commented that the reference to "identified programmes" in the IMs is excessive, and does not reflect the capex and opex budgets of small networks. These smaller networks may not be sufficiently resourced to meet this task.¹⁶⁷ Additionally, MDL commented that some businesses simply will not have this many projects in total.¹⁶⁸

¹⁶⁵ Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 30(d).

¹⁶⁶ Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 25-28.

¹⁶⁷ ENA "Feedback on Orion customised price-quality path process" (14 April 2014), para 13-14.

¹⁶⁸ MDL, Untitled submission on problem definition paper (21 May 2015), para 12.

Solution

356. Our solution is to allow a level of flexibility in the number of identified programmes that are verified in detail as part of verification process. We will do this by allowing the verifier to judge on a case by case basis the appropriate number of identified programmes for which more detailed information must be provided (also forming part of the CPP proposal), and which will be scrutinised by the verifier at greater depth. The current number of identified programmes (20) required will remain as the maximum.¹⁶⁹
357. This change will directly reduce the cost and complexity of CPP applications for the verifier, the applicant, and the Commission, and is consistent with the proportionate scrutiny principle, as it allows the verifier's detailed assessment to be targeted at the programmes that most affect the price, quality, and investment aspects of the applicant's business. We first proposed this change as part of our draft decision, and we also set out our proposed criteria that the verifier would use to select the number of identified programmes for verification.
358. As suggested by submissions, we have refined the criteria to ensure that the considerations are directly relevant to the verifier's selection of an appropriate sample.¹⁷⁰
359. For example, we have removed the requirement for the verifier to consider the extent to which the number of projects or programmes in the CPP proposal is consistent with the number of projects or programmes in previous asset management plans.
360. We have also made some minor refinements to the drafting to improve clarity and ensure consistency with the terminology used elsewhere in the IMs and the Act.
361. When selecting the number of identified programmes the verifier will consider:
- 361.1 the long term interests of consumers;
 - 361.2 our ability to effectively review whether the applicant's forecasts are consistent with the expenditure objective;
 - 361.3 the applicant's rationale for seeking a CPP;

¹⁶⁹ We note that Powerco submitted that the maximum number of identified projects was excessive and should be capped at 10 as this number will be adequate. We consider that the draft number remains appropriate as this is only a maximum and the verifier will have discretion to choose a lesser number that it considers adequate. However, it will also allow the verifier to choose a number of projects, larger than ten, which may be suitable, for example, where a supplier has split its projects into many small projects.

¹⁷⁰ See: ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), para 96.

- 361.4 its ability to provide an opinion on whether the capex and opex forecasts have been prepared in accordance with the policies and planning standards of the applicant;
- 361.5 its ability to assess any quality standard variation proposed; and
- 361.6 the materiality of the projects or programmes to the CPP proposal, and the capex and opex forecasts.

Role of the independent engineer

Problem definition

- 362. The independent engineer preparing the report on network quality (for EDBs seeking a quality standard variation) adds unnecessary cost, and this role could be performed by the applicant.
- 363. The pre-review IMs required the applicant to engage an independent third-party (other than the verifier) to report on a proposed quality standard variation. Stakeholders have suggested this is a task that could be performed by the verifier.¹⁷¹

Solution

- 364. We have made changes to allow the applicant to prepare its own quality standard variation report, and have the verifier assess the report.
- 365. This change will eliminate the need for an independent engineer, which will reduce compliance costs. However it will still ensure that the report is subject to appropriate independent scrutiny, of the kind that the verifier will be well placed to provide.
- 366. Some submissions suggested that we merge the roles of the verifier and the independent engineer, however we do not consider this to be an appropriate alternative solution. Applicants are likely to have access to the right kind of expertise to prepare the quality standard variation report. However, it would be a departure from the verifier's independent status for them to prepare and then verify their own report.
- 367. In response to submissions, we have also made a change to the verifier's terms of reference, to clarify the verifier's role in reviewing any proposed quality standard variations.¹⁷²

¹⁷¹ ENA "Feedback on Orion customised price-quality path process" (14 April 2014), para 21-23; Dennis Jones (Orion) "Cost-effectiveness of the rules and processes for CPP application" (presentation at the Commerce Commission input methodologies review forum, Wellington, 29 July 2015), p. 247.

¹⁷² See: ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), para 97.

Verification of non-standard depreciation, cost allocation and insurance information

Problem definition

368. The verifier is required to produce an independent report on the CPP proposal based on the terms of reference in Schedule G of the IMs. Feedback on the scope of the verifier's report indicates that some of the material the IMs require should be excluded from the report.
369. Stakeholders have said that non-standard depreciation and cost allocation should not be included in the report. Their view is that these issues fit more comfortably within the Commission's review than within the verifier's.¹⁷³ Additionally, Orion has said that insurance costs should not be within the scope of the verifier's report.¹⁷⁴ Commenting on the draft decision, First Gas also identified that the verifier's role in assessing insurance was not completely clear.¹⁷⁵

Solution – remove requirement to review non-standard depreciation

370. Our solution is to remove the requirement to review non-standard depreciation and cost allocation information from the verifier's terms of reference.
371. Our main reason for this change is that the verifier would likely need to engage specialist economic advice to assess non-standard depreciation, which adds cost and complexity to the process. We agree with submissions that the review of non-standard depreciation is better suited to our own review rather than the verifier's review.

Solution – remove requirement to review cost allocation

372. As part of our draft decision we proposed to retain the requirement for the verifier to review the CPP applicant's cost allocation information.
373. In submissions on the draft decision ENA suggested that the auditor should audit the cost allocation information, rather than the verifier.
374. We agree that the auditor's skill set is likely to be better suited to performing this role than the verifier's. As such, we have removed the requirement for the verifier to provide a view on this information, and, for the avoidance of doubt, added this to the requirements of the audit report.

Verifier's role in assessing insurance decisions

375. We expect that insurance costs will be assessed by the verifier as these costs will form part of the applicant's proposed opex forecast – a key aspect of a CPP proposal. A specialist insurance report may be included as part of a CPP proposal. We consider

¹⁷³ ENA "Feedback on Orion customised price-quality path process" (14 April 2014), Attachment 1, p. 16.

¹⁷⁴ Dennis Jones (Orion) "Cost-effectiveness of the rules and processes for CPP application" (presentation at the Commerce Commission input methodologies review forum, Wellington, 29 July 2015), p. 246.

¹⁷⁵ First Gas "Submission on Input methodologies review draft decisions (excluding cost of capital)" (4 August 2016), p. 6.

that the verifier will be better placed than the Commission to provide an initial comment on:

- 375.1 the level of cost versus risk that the applicant is exposing certain assets to; and
 - 375.2 whether the balance between self-insurance and external insurance has been adequately made.
376. In circumstances where the verifier considers that more detailed analysis, from someone with specific expertise in the insurance field is required, we would expect the verifier to recommend that we engage an expert.
377. We consider that in some circumstances it may be useful to clarify our verification expectations, in relation to insurance, in the tri-partite deed – for example, where we think insurance decisions are likely to be pertinent to our evaluation of a CPP proposal.

Other issues raised by stakeholders

378. This section responds to a number of issues raised by stakeholders where we consider no changes to the information requirements are required.

Selection and engagement of the verifier

379. The CPP IMs require the applicant to engage the verifier using the process set out in Schedule F of the IM Determinations. Specific problems with the engagement process have focussed on how the verifier is approved, and on the tripartite deed between the verifier, the applicant, and the Commission.
380. Suppliers have submitted that the current process to select and approve the verifier is complex and time-consuming. Stakeholders have suggested that we could reduce the time and cost involved by providing a pre-approved list of verifiers, and through the use of a template deed.
381. Orion described selecting and obtaining approval for the verifier as "unduly onerous" when submitting on the problem definition paper for the IM review. It stated that the time spent on this process could have been better used elsewhere.¹⁷⁶
382. Orion previously submitted the approval process could benefit from being "streamlined", possibly by the use of a pre-approved verifier list.¹⁷⁷ They also commented that the small number of potential verifiers in New Zealand posed a

¹⁷⁶ Orion's submission on the problem definition paper "Submission on the IM review" (21 August 2015), para 66.

¹⁷⁷ Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 24.

practical issue for CPP applicants.¹⁷⁸ This sentiment was echoed by the ENA in its feedback on the Orion process, who characterised the process as "complex".¹⁷⁹

383. Regarding the tripartite deed, Orion suggested at the IMs forum that the preparation of a standard deed could reduce the time taken to develop and agreed the deed.¹⁸⁰ This suggestion was also supported in submissions on the draft decision.
384. While we agree with the issues highlighted by Orion and other submitters, we consider that differences in circumstance (when compared with the Orion CPP) and changes elsewhere in the IMs will mitigate these problems in future. We remain open to the solutions, that do not require changes to the IMs that submitters have suggested, specifically:
- 384.1 introducing a template tripartite deed; and
- 384.2 introducing a pre-approved verifier list in future, should this problem persist.
385. The issues Orion faced in approving the verifier were to some extent a result of the challenging circumstances of their application, and the fact that it was the first CPP application. Furthermore, the removal of the timing constraints imposed by the CPP WACC Determination allows for better pre-application engagement between the Commission and suppliers.
386. We are open to developing a template or "benchmark" tripartite deed outside of the IM review process. The deed used in the Orion process could form the basis of this, but the specifics of any template require input from stakeholders. In the interim we will work with potential CPP applicants to help develop a suitable deed, and reduce these costs where possible.

Time available for verification

387. For EDBs, the time allowed for the verifier to carry out their work was previously limited by the timing of the CPP WACC Determination in September and the CPP application windows in February and May. This led to a compressed timeframe for the verifier to prepare their report, which may have consequently reduced the quality of the CPP application.
388. Our change to eliminate the difference between the CPP WACC and the DPP WACC resolves this problem. With the need for the CPP WACC Determination removed, applicants, the verifier, and the Commission will have a wider time frame for both pre-application engagement and for the verification process. This change will help

¹⁷⁸ Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 21.

¹⁷⁹ ENA "Feedback on Orion customised price-quality path process" (14 April 2014), para 18.

¹⁸⁰ Dennis Jones (Orion) "Cost-effectiveness of the rules and processes for CPP application" (presentation at the Commerce Commission input methodologies review forum, Wellington, 29 July 2015), p. 245-246.

not only with this specific issue, but with some of the other timing problems outlined in previous sections.

Use of a separate verifier for consumer consultation

389. In their submission Major Electricity Users Group (**MEUG**) suggested that we should amend the IMs to allow for a separate verifier to scrutinise the applicant's consumer consultation process.¹⁸¹ They submitted that the verifier may not have the appropriate expertise to be able to provide an opinion on the appropriateness of the applicant's consumer consultation.
390. While we agree that the verifier may not have specific expertise in consumer consultation, the verifier is not limited to being a single person. We consider that if further expertise in consumer consultation is needed that the verifier could take on additional staff, or use external consultants in order to gain assurance over the consumer consultation steps. Further we are open to providing feedback to applicants on the appropriateness of their consumer consultation steps, and we will further scrutinise the process once the proposal is received.

¹⁸¹ MEUG "Submission on Input methodologies draft review decisions" (4 August 2016), para 15.

Chapter 7: Audit requirements

Purpose of this chapter

391. This chapter explains our solutions to the problems we have identified with the audit requirements for CPP proposals.

Structure of this chapter

392. This chapter begins with a summary of our changes to the audit requirements for CPP proposals and an explanation of the policy intent of the audit requirements. The following sections then identify specific problems with implementing that intent, and set out our solutions for each.

Summary of proposed changes

393. The changes we have made are intended to provide greater certainty for CPP applicants of our expectations for the audit requirements, consistent with s 52R. These are:

- 393.1 differentiating the role of the auditor with respect to historical financial information and forecast financial information;
- 393.2 removing ambiguity relating to quantitative information provided in spreadsheets;
- 393.3 clarifying the requirement on the auditor to provide a view in respect of proper records being kept;
- 393.4 clarifying the requirement that the auditor must provide a report setting out its opinion on specified matters; and
- 393.5 expressly setting out the auditor's role in auditing cost allocation information.

Policy intent of the audit requirements

394. We rely on the information provided by CPP applicants in assessing CPP proposals and making CPP determinations. In order to make appropriate and cost-effective CPP determinations we need to have confidence in the information provided by applicants.¹⁸²

395. One of the means by which we gain confidence over the quality of financial and quantitative information provided by CPP applicants is by requiring the information to be subject to examination by independent auditors (ie, audit).

¹⁸² Verification provides a complementary, but distinct role to audit. A key task of the verifier is to provide an assessment of whether the CPP applicant's policies, strategies, and procedures are appropriate such that services will be provided efficiently and align with consumer demands. Auditors are not qualified to form opinions on such matters.

396. The policy intent behind the audit IM requirements for CPPs is to ensure that financial and quantitative information provided as part of a CPP proposal is robust, reliable, and in compliance with applicable IMs.
397. Overall, we consider that the audit IM requirements for CPPs are fundamentally fit for purpose, but that we can make some clarifications and refinements to better meet their intent. Specifically, by referencing professional engagement standards, and clarifying the terminology used with respect to the role of the auditor, we can better align with the audit profession and clarify the role of the auditor with respect to CPP applications.
398. Through our review of the IMs, and drawing on feedback on the Orion CPP process, we have identified three problems related to the audit requirements. Specifically:
- 398.1 the role of the auditor with respect to financial, non-financial, and forecast information lacks a link to professional engagement standards;
 - 398.2 the audit requirements contain unclear or ambiguous terminology which can confuse the role of the auditor; and
 - 398.3 an audit must be conducted, but no audit report is explicitly required to be provided by the auditor.

Clarifying the role of the auditor with respect to financial, non-financial, and forecast information

Problem definition

399. The role of the auditor may vary depending on the nature of the information and the type of engagement sought. The professional engagement standards that auditors comply with reflect these differences:¹⁸³
- 399.1 Where a high standard of comfort is required over the reliability of historical financial information, an audit may be required involving the application of appropriate audit engagement standards. This is typical in cases where an organisation wishes to issue its financial statements publicly and therefore seeks an opinion as to their fair presentation.
 - 399.2 There are other engagements that may be undertaken involving a lesser standard of comfort and/or different types of information, regulations, rules, policies or guidelines, which may be performed under applicable assurance engagement standards. These engagements may include, for example, a review of an organisation's procurement practices.
400. A CPP proposal is required to contain a range of information, including historical financial information, forecast information, and other non-financial information.

¹⁸³ Auditing and Assurance Standards as issued by the External Reporting Board or the New Zealand Auditing and Assurance Standards Board (NZAuASB).

However, the pre-review audit IMs referred only to an *audit* being required, which has been interpreted to mean the high standard of assessment which applies in a typical audit of historical financial information.

401. Submitters had comments about the role of the auditor, particularly with respect to what is required under the audit IMs in relation to *historical* information and *forecast* information. For example, Orion stated that:¹⁸⁴

...there are limits to the extent that [forecast] information can be or should be audited. We suggest the focus of the audit should be on verifying actual/historical information and ensuring that the historical and forecast information has been prepared consistent with the IMs.

402. Similarly, ENA considered that the Commission should ensure that "the audit is focused on the areas where it can add the most value (such as confirmation of historical information and consistency with the IMs which are relevant to the price path)."¹⁸⁵ ENA also considered that the audit IMs could more appropriately reflect different assurance requirements for historical and forecast information.
403. We consider there is merit in clarifying and differentiating the obligations of the auditor under the audit IMs with respect to actual/historical financial information relative to those for forecast financial information. We consider an auditor can (and should) audit the veracity of historical/actual financial information in CPP applications against source information held by the applicant in accordance with relevant *audit engagement standards*, and provide an opinion on whether the CPP application information complies with the IMs.
404. However, a high audit standard applied to forecast financial information is problematic, as the accuracy of forecast information cannot be known by an auditor *ex-ante*, and the information cannot be verified back to source documentation (as this can only occur *ex-post*).

Solutions

405. Our solution is to amend the audit IMs for CPPs to differentiate the role of the auditor with respect to historical financial information and forecast financial information by linking to existing audit engagement standards and assurance engagement standards under the Financial Reporting Act 2013 (or other standards where appropriate).¹⁸⁶
406. In submissions on our draft decision PwC submitted that the linkage to audit and assurance engagement standards issued under the Financial Reporting Act 2013 was

¹⁸⁴ Orion "Feedback on setting Orion's customised price-quality path" (14 April 2014), p. 6.

¹⁸⁵ ENA "Feedback on setting Orion's customised price-quality path" (14 April 2014), p. 8.

¹⁸⁶ Where historical financial information is concerned, requiring an audit of this information under the IMs is appropriate – as the events giving rise to this information, and the associated amounts, can be verified. An auditor can (and should) audit the veracity of historical financial information in CPP proposals against source information held by the applicant in accordance with relevant audit engagement standards, and provide an opinion on whether the CPP proposal information complies with the IMs.

not appropriate. They submitted that the standards issued under that legislation are only applicable to audits of financial statements and would not be relevant to the audit of either the historical financial information or forecast financial information included in a CPP proposal.¹⁸⁷ We have made minor alterations to this provision to ensure that it is expressed accurately – by reference to the applicable auditing standards issued by the External Reporting Board in accordance with its functions under the Financial Reporting Act 2013.

407. PwC also recommended that we specifically reference the relevant audit and assurance standards in the IMs.¹⁸⁸ We do not consider this appropriate. We consider that the auditor will be best placed to judge the appropriate standards to apply to a CPP proposal. Further, audit and assurance standards are regularly changing. We consider that by keeping the requirements flexible and relying on the auditor's professional judgement, it is less likely that the IMs will become unworkable when standards are changed or removed – which would create uncertainty.
408. The effect of these changes will result in the following:
- 408.1 historical financial information will be audited in accordance with applicable audit engagement standards issued by the External Reporting Board under the Financial Reporting Act 2013 (or applicable successor);
 - 408.2 forecast financial information will be examined in accordance with applicable assurance engagement standards issued by the External Reporting Board under the Financial Reporting Act 2013 (or applicable successor), or other appropriate standards; and
 - 408.3 quantitative historical information provided in spreadsheets will be properly compiled on the basis of the relevant underlying source documentation.
409. Our main reason for these changes is to provide a greater level of certainty to CPP applicants (and their auditors) in relation to the audit standards we expect to be applied to a CPP proposal.

Submissions requested further clarity in the Audit IMs

410. While submissions on our draft changes to the audit IMs were generally supportive, some submitters suggested that they should be further amended to provide greater clarity and, in some cases, prescription.¹⁸⁹ For example, the specific change proposed by PwC discussed in paragraph 407 above.

¹⁸⁷ PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers – Made on behalf of 17 Electricity Distribution Businesses" (4 August 2016), para 154.

¹⁸⁸ PwC "Submission to the Commerce Commission on input methodologies review: Draft decisions papers – Made on behalf of 17 Electricity Distribution Businesses" (4 August 2016), para 155.

¹⁸⁹ See, for example: ENA "Input methodologies review – Topic paper 2, CPP requirements – Submission to the Commerce Commission" (4 August 2016), p. 27; PwC "Submission to the Commerce Commission on

411. We have considered all of these submissions and concluded that further changes are unnecessary. We consider that a number of the suggestions raised by submitters would result in very detailed IMs if implemented, which would add little value, while potentially unnecessarily limiting the scope of the audit or creating further uncertainty through added complexity.
412. We rely on the auditor to exercise their professional judgement when undertaking the audit, to provide a view on the robustness of the relevant information in a CPP proposal, so that we can assess the reliance we are able to place on that information.

Audit requirements contain unclear or ambiguous terminology which can confuse the role of the auditor

Problem definition

413. To gain confidence in the information provided by a CPP applicant, the policy intent of the IMs is to require the auditor to provide an opinion on whether 'proper records have been kept' by the applicant on which the CPP proposal information has been based.
414. Consequently, the IMs required an auditor to audit a CPP proposal as to whether proper records have been kept to enable the complete and accurate compilation of information by the applicant.
415. However, this requirement previously did not reflect the fact that some information required under the IMs may not be traditionally produced by applicants for business or regulatory purposes, meaning it may need to be created or developed from other information that is actually produced and kept by the applicant.
416. Given that the information may need to be created, the references to "proper records" and "complete and accurate compilation of information" had the potential to cause confusion and difficulty for applicants and auditors in terms of complying with the IMs.
417. Submissions also noted that the audit IMs require quantitative information provided in spreadsheets to be "accurately presented". In its submission of 14 April 2014 Orion noted that their auditors were not comfortable with the IM requirement "...for them to opine on whether information had been "accurately presented" as it was not clear what this term required in practice."¹⁹⁰ In its submission, ENA also questioned the use of the term "accurately presented" in a CPP context.¹⁹¹ These submissions are referring to clause 5.5.3(d) in the EDB IMs, and clause 5.6.3(d) in the GDB and GTB IMs.

input methodologies review: Draft decisions papers – Made on behalf of 17 Electricity Distribution Businesses" (4 August 2016), para 150–155.

¹⁹⁰ Orion "Feedback on setting Orion's customised price-quality path" (14 April 2014) p. 6.

¹⁹¹ ENA "Feedback on setting Orion's customised price-quality path" (14 April 2014) p. 16.

418. We consider that the expression "accurately presented" is problematic with respect to forecast quantitative information, as there is no way for the auditor to know *ex-ante* whether the information is indeed "accurate". This underlies the concerns of auditors as they are being required to provide an opinion that a forecast is accurate, when in fact this cannot be known at the time the opinion is provided (ie, before the fact).
419. Further, the expression "accurately presented" is unclear as to what dimension it is focussing on. For example, it is not clear whether the IM is requiring accurate presentation in terms of the underlying substantive information, or the presentation of that information (given there may be different ways to present the information), or both.
420. For the same reasons outlined earlier in terms of the Commission needing to be able to rely on the information provided in CPP applications, we consider that the intent of the relevant IMs is sound. However, the current wording of the IMs is problematic in the context of forecast financial information. We consider that a modification to the relevant IMs is needed to differentiate between what the auditor must exercise their judgment on with respect to *historical* quantitative information provided in spreadsheets and *forecast* quantitative information provided in spreadsheets.

Solution

421. We have added exemptions and modifications to the record-keeping requirements under the IMs relating to information requirements to address this problem. This change will allow a degree of flexibility in determining whether information may need to be created or developed from other information that is actually produced and kept by the applicant.
422. Our solution is to align the scope of audit requirements to the information requirements, ie, the auditor is required to provide their opinion as to "whether proper records have been kept to enable the compilation of information required for a CPP proposal".
423. We have also removed some of the ambiguity in assessing quantitative information provided in spreadsheets by removing the expression "accurately presented" from the audit IM requirements. PwC supported this change but suggested that we should provide further guidance for auditing spreadsheets. We do not consider that this suggestion is desirable for the reasons set out above in paras 410 to 412.
424. With respect to quantitative information provided in spreadsheets, we have modified the IMs to require the auditor's opinion on whether:
- 424.1 quantitative *historical* information provided in spreadsheets has been properly compiled on the basis of the relevant underlying source documentation; and

- 424.2 quantitative *forecast* information provided in spreadsheets has been properly compiled on the basis of relevant and reasonable disclosed assumptions.
425. Our main reason for these changes is to provide clarity on the scope of audit requirements.

Lack of explicit requirement for auditor to provide audit report

Problem definition

426. A report setting out the opinion of the auditor is a key part of the application package that we rely on when considering a CPP proposal. Being clear about the requirement for this report is important to ensure applicants and auditors know what the work of the auditor must culminate in.
427. The pre-review audit IMs stated that CPP proposals must be audited by an auditor, but did not explicitly require the auditor to provide a report setting out the auditor's views on specified matters contained in the IMs, as part of that audit (albeit that a different clause, clause 5.1.4, requires the supplier to provide one as part of the CPP application).
428. Accordingly, the need for a formal view to be provided by the auditor (in order for us to have confidence in the CPP proposal information), and the output required from the auditor under the IMs, was not as clear as it could be.

Solution

429. Our solution is to stipulate in clause 5.5.3 of the EDB IMs, and clause 5.6.3 of the GDB and GTB IMs that the auditor must provide a report setting out the its opinion on specified matters set out in those clauses. This will:
- 429.1 more easily enable us to assess the reliability of the financial and quantitative information provided in the CPP proposal;
- 429.2 make it clear to stakeholders and auditors what output is required under the IMs; and
- 429.3 improve the link between those IMs and clauses 5.1.1(2)(a) and 5.1.4.

Role in reviewing cost allocation information

430. As discussed above in paragraphs 372 to 374 we have removed the requirement for the verifier to review cost allocation information, as we consider this is a role better suited to the auditor.
431. While we consider that the auditor's role should already cover a review of this information, for the avoidance of doubt, we have changed the audit IMs to expressly lay out our audit expectations in relation to cost allocation. These expectations are aligned with the requirements that were previously required of the independent verifier.

Chapter 8: Consumer consultation requirements

Purpose of this chapter

432. This chapter explains our solutions to the problem we have identified with the consumer consultation requirements for CPP proposals.

Structure of this chapter

433. This chapter begins with a summary of our changes to the consumer consultation requirements. Following this, we explain the policy intent of the consumer consultation requirements. We then discuss the lack of clarity in those requirements, and set out our solutions to this problem.

Summary of changes

434. We have made two changes to the IMs to provide greater certainty of our expectations for consumer consultation, consistent with s 52R by:

- 434.1 amending the consumer consultation IMs to require CPP applicants to notify consumers of the price and quality impact of any alternative investment options in its CPP proposal; and
- 434.2 requiring the verifier to report on the extent and effectiveness of the applicant's consultation.

Intent of the consumer consultation requirements

435. Having reviewed the consumer consultation requirements for CPP proposals, we consider that the intent behind them remains appropriate.

436. The current consumer consultation requirements require suppliers to inform and engage with consumers on the implications of the CPP proposal for consumers. This means the proposal is more likely to reflect the service quality that consumers demand and are willing to pay for.

437. In our 2010 IMs reasons paper, we stated:

The requirement relating to consumer consultation is one of 'adequate notification', by which the Commission means that the process, the medium used and the information provided must be sufficient to enable consumers to engage. This will likely differ according to the specific consumer base and the nature of the CPP proposal, and the supplier has discretion as to how it engages with its consumers.

438. Some suppliers sought clarification of what is considered 'adequate'. We have intentionally left this broad to allow suppliers to exercise some discretion as to the proposed channel of communication, given the nature of their consumer base.¹⁹²

¹⁹² Commerce Commission "Input methodologies (electricity distribution and gas pipeline services) reasons paper" (22 December 2010), para 9.6.16-9.6.17.

439. Under Part 4, we must ensure that suppliers have incentives to supply services at a quality consumers demand.¹⁹³ The requirement that suppliers consult with consumers on a CPP application is a clear means of promoting this outcome.
440. A similar sentiment was expressed by the MEUG in submissions on our CPP emerging views paper:
- ...the long term benefits to consumers and the economy as a whole are, in the view of MEUG, likely to be higher if we can lift the level of engagement between monopoly service providers and end consumers and steer the response by the monopolies to that engagement towards that found in service-based sectors...
441. We consider that we can provide greater certainty to suppliers of the level of consumer engagement we expect under the consumer consultation IM requirements.

Feedback identified we should further clarify our expectations concerning consumer consultation

Issues identified by stakeholders

442. In both feedback on the Orion CPP process, and submissions on the IM review, stakeholders identified the following issues related to the consumer consultation requirements:
- 442.1 the lack of clarity about what we expect from consumer consultation;
 - 442.2 duplication between Orion's consultation and our consultation process; and
 - 442.3 the lack of time for adequate consultation due to the relative timing of the CPP WACC Determination and the CPP application windows for EDBs.
443. The ENA considered that in the Orion CPP, the Commission expected a more comprehensive consultation than specified in the IMs. The ENA suggested that a review of consultation IMs was required.¹⁹⁴
444. Orion submitted that the CPP IMs do not specifically require the applicant to consult on options and the impacts different options would have on price and quality. Orion

¹⁹³ Commerce Act 1986, s 52A(1)(b).

¹⁹⁴ ENA "Feedback on Orion customised price-quality path process" (14 April 2014), para 26.

recommended that the CPP IMs set out clearly what is required in this regard.¹⁹⁵ Other submitters have expressed similar views.¹⁹⁶

445. Submissions further argued that this lack of clarity contributed to the high cost of the CPP application process.¹⁹⁷
446. On the other hand, Vector noted in its feedback on the Orion CPP process that "it is appropriate for the IMs to require consultation to be carried out but to not be prescriptive of the form of the consultation – the regulated supplier should be able to judge the best mechanisms for gaining the views of their consumers". Vector suggested that our pre-engagement with the supplier could help ensure the consultation process will meet the needs of both parties.¹⁹⁸
447. Orion questioned whether the Commission was best placed to present the CPP proposal to consumers, and whether this duplication was necessary.¹⁹⁹ The ENA echoed this view, further suggesting that any overlap should be avoided, as it may confuse consumers, and impose unnecessary cost.²⁰⁰ While we will look to avoid any unnecessary duplication with the applicant's own consultation, under the Act, we are required to consult on an applicant's CPP proposal and our draft decision.
448. In addition, the timing of the WACC determination for CPP applications by EDBs (at the end of September) relative to the windows for EDBs to apply for a CPP (in February and May) limited the timeframe in which applicants can consult with consumers. Stakeholders have said that this timeframe is not sufficient for adequate consultation.²⁰¹

¹⁹⁵ Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 34. Orion reiterated this point during its presentation to the IM Review Forum and its submission on the problem definition paper, Dennis Jones (Industry Developments Manager (Commercial), Orion) "Cost-effectiveness of the rules and processes for CPP application" (presentation at the Commerce Commission input methodologies review forum, Wellington, 29 July 2015), pp. 247-248; Orion's submission on the problem definition paper "Submission on the IM review" (21 August 2015), para 70.

¹⁹⁶ PwC "Submission to the Commerce Commission on input methodologies review: Invitation to contribute to problem definition (21 August 2015), para 115 and 122; MDL, Untitled submission on problem definition paper" (21 May 2015), p. 12; Powerco "Feedback on Orion customised price-quality path process" (14 April 2014), para 9; Wellington Electricity's submission "Input methodologies review – Problem definition" (21 August 2015), p. 9.

¹⁹⁷ Commerce Commission "Input methodologies review draft decisions: Topic paper 2 – CPP requirements" (16 June 2016).

¹⁹⁸ Vector "Feedback on Orion customised price-quality path process" (14 April 2014), para 5.

¹⁹⁹ Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 38.

²⁰⁰ ENA "Feedback on Orion customised price-quality path process" (14 April 2014), para 26(d). See also: Powerco "Feedback on Orion customised price-quality path process" (14 April 2014), para 11. A similar point was raised during the IM review forum, Lynne Taylor (PwC) "Cost-effectiveness of the rules and processes for CPP application" (presentation at the Commerce Commission input methodologies review forum, Wellington, 29 July 2015), p. 269.

²⁰¹ Genesis "Feedback on Orion customised price-quality path process" (14 April 2014), p. 1-2; Orion "Feedback on Orion customised price-quality path process" (14 April 2014), para 36; Powerco "Feedback on Orion customised price-quality path process" (14 April 2014), para 10.

449. This last issue has been resolved by a change to the cost of capital IMs, aligning the CPP WACC with the underlying DPP WACC.²⁰²

Problem definition

450. The consumer consultation IMs did not provide enough clarity about our expectations. In particular, they did not specify that suppliers must consult on the price and quality impacts of any alternative investments the supplier proposes in its CPP. We consider that conclusions drawn from consumer consultation that have not clearly presented price/quality trade-offs are likely to be unreliable.
451. Consistent with the expenditure objective in our CPP evaluation criteria, we expect that a prudent supplier has weighed up the price/quality trade-offs when it considers various investment alternatives, where relevant, and would inform affected consumers of these trade-offs – providing an opportunity for affected consumers to comment.
452. However, in practice, the IMs do not explicitly set out this expectation, as we are not prescriptive about the content and form of consumer consultation, requiring "adequate notification".²⁰³ This is consistent with our view that suppliers are likely to be best placed to judge the best manner of engaging with their particular customer base.
453. However, the lack of prescription in the IMs appears to have resulted in a lack of certainty about our expectations for consumer consultation.
454. We agree with stakeholders that greater certainty of applicants' consumer consultation obligations is warranted. To provide this, we propose the solutions below.

Solution – explicitly lay out requirement to consult on price/quality trade-offs

455. As part of our draft decision we proposed to amend the IMs to explicitly require applicants to consult with consumers on the price/quality impact of any proposed investment alternatives.
456. Our main reason for this change was to provide greater clarity about our expectations for CPP consultation.
457. While submissions generally acknowledged the benefits of clarifying our consultation expectations in the IMs, a number of submitters suggested that it was not practically realistic for a supplier to consult on *all* alternative investment options.²⁰⁴

²⁰² Commerce Commission "Input methodologies review decisions: Topic paper 4 – Cost of capital issues" (20 December 2016).

²⁰³ Electricity Distribution Services Input Methodologies Determination 2012 [2012] NZCC 26, cl 5.5.1(1).

²⁰⁴ See: ENA "Submission to the Commerce Commission on input methodologies review: Draft decisions papers" (4 August 2016), p. 28; PwC "Submission to the Commerce Commission on input methodologies

458. We agree with these submissions, and in our final decision we have limited this requirement so that CPP applicants are only required to consult on price/quality trade-offs of expenditure alternatives where they are directly associated with the applicant's rationale for seeking the CPP proposal.²⁰⁵ This will reduce the cost and complexity for the CPP applicant and aims to focus the additional consumer scrutiny on the parts of the CPP proposal that are likely to have the greatest impact on consumers.
459. Some parties have submitted that further prescription or guidelines would be beneficial.²⁰⁶ However, we consider that this change is sufficient at this stage, and have not included any further prescriptive requirements for consumer consultation. We consider that any further requirements might limit supplier's ability to tailor its consultation to the circumstances of its customers and of their applications, or cause additional consultation costs that might provide little additional benefit. We consider that the best way to provide additional clarity of our expectations will be to provide feedback and guidance as part of our engagement with potential CPP applicants, prior to the submission of a CPP proposal.
460. Where we are not satisfied that the applicant's level or quality of consultation is sufficient, we retain the ability to undertake our own further consultation.

Solution – verifier to review consumer consultation

461. We are also proposing to add a requirement to the verifiers' Terms of Reference to support the change to the consultation requirements. This change will require the verifier to report on the extent and effectiveness of the supplier's consultation with consumers.
462. As part of the submissions on our draft decision, First Gas questioned the decision to include this as part of the verifier's role, as it is not something that would be in the normal scope of the verifier's capabilities.²⁰⁷ MEUG suggested that we should require a separate verifier with expertise in public consultation to be engaged, rather than relying on the normal verifier who may not have the expertise in consumer consultation to provide an informed expert view.²⁰⁸

review: Draft decisions papers – Made on behalf of 17 Electricity Distribution Businesses" (4 August 2016) para 162-164; Powerco "Submission on input methodologies review – Draft decisions" (4 August 2016), p. 47; Aurora "Submission – Input methodologies review: Draft decision and determination papers" (4 August 2016), p. 13.

²⁰⁵ An explanation of the applicant's reasons for applying for a CPP are required to be provided as part of the CPP proposal.

²⁰⁶ See, for example: MEUG "Submission on Input methodologies draft review decisions" (4 August 2016), p. 5-6; Aurora "Submission – Input methodologies review: Draft decision and determination papers" (4 August 2016), p. 13

²⁰⁷ First Gas "Submission on Input methodologies review draft decisions (excluding cost of capital)" (4 August 2016), p. 5.

²⁰⁸ MEUG "Submission on Input methodologies draft review decisions" (4 August 2016), para 15.

463. We do not consider that this step is necessary. If verifier does not have sufficient expertise to provide a view on the extent and effectiveness of the consumer consultation process, then it may be appropriate for the verifier to subcontract expertise in this area to provide input into that component of its review.
464. We consider that a separate verifier for consumer consultation would likely add unnecessary cost and complexity to the verification process. However, as a safeguard, where we are not satisfied with the verifier's assessment of an applicant's consumer consultation process, we are likely to undertake our own assessment as part of our CPP evaluation process.

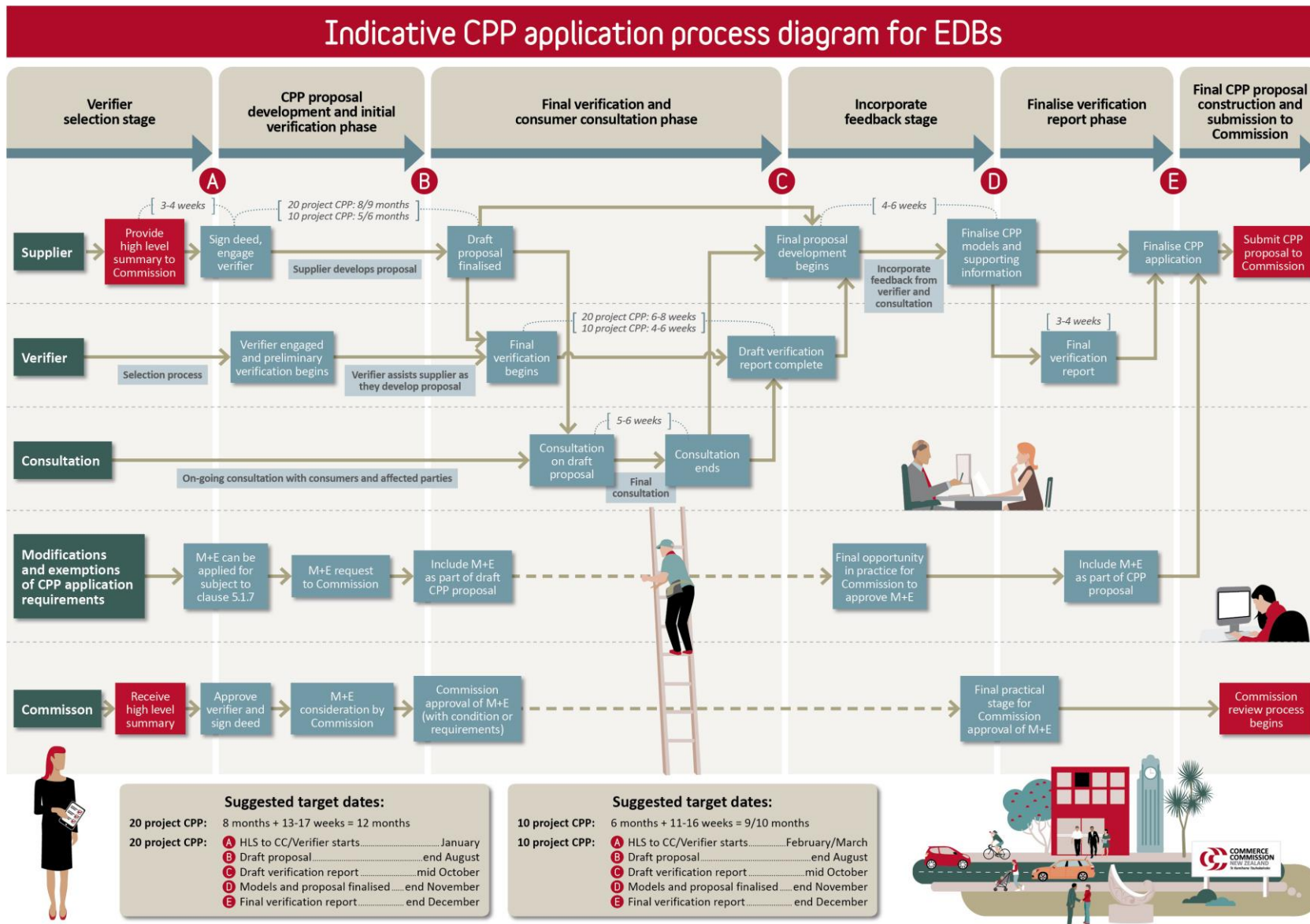
Attachment A: Indicative CPP application process diagram

Purpose of this attachment

465. This attachment contains an indicative diagram of the CPP application process that illustrates how the different components of the application process set out in the CPP IMs interact.
466. It is intended to be an aid for stakeholders to better understand how the CPP application process works in practice. In particular we think the diagram is a useful starting point for intending CPP applicants and a prompt for early discussion and engagement between the CPP applicant and the Commission.

Key considerations in using the diagram

467. Readers should note:
- 467.1 The timeframes provided in the diagram are indicative only, intended to be a guide at the early stages of a supplier's consideration of a CPP proposal in the absence of other information. We anticipate the stages of the process may vary in length depending on the nature of different proposals and the business practices of the particular applicant.
- 467.2 For simplicity we have represented the CPP application process from the viewpoint of an electricity distribution business. We expect the diagram to also be a useful starting point for GPBs but note that in the absence of a specified CPP application window for GPBs, there might be some nuances in the process that this diagram does not take account of. We encourage any suppliers contemplating a CPP to approach us to discuss more detailed timeframes, taking account of the specific circumstances.
- 467.3 We have used the following acronyms: HLS ('high level summary' – see Schedule F5 of EDB IM determination), CC ('Commerce Commission'), CPP ('customised price-quality path'), M+E ('modifications and exemptions' – see clause 5.1.7 of EDB IM determination), EDBs ('electricity distribution businesses').



Attachment B: Summary of the review of CPP IMs

Purpose of this attachment

468. The purpose of this attachment is to:
- 468.1 present the results of our review of the CPP requirements IMs for electricity lines services and gas pipeline services in accordance with our decision-making framework; and
 - 468.2 summarise our decisions on whether to change the CPP requirements IMs, and explain our reasons for changing or not changing them.
469. In doing so, this attachment performs, in respect of the CPP requirements IMs, the role that the report on the review performs in respect of all other areas of the IMs.²⁰⁹

Relationship with the Report on the IM review

470. The Report on the IM review is a separate paper that records our decisions on whether to change each of the existing IM decisions as a result of the IM review. For those existing IM decisions we have decided to change, it explains how and why. It also explains our reasons for not changing those decisions we propose not to change as part of the IM review.
471. As noted in the Report on the IM review, for some areas of the IMs, extracting the existing IM decisions was straightforward (for instance, for those chapters of the 2010 IM reasons papers that began with IM overview tables summarising decisions we made in that area).²¹⁰ In other areas, including for the CPP requirements IMs, we have extracted the pre-review decisions from descriptions in the text of the relevant reasons papers.

Why we have presented our decisions in respect of the CPP IMs separately

472. Rather than being included in the Report on the IM review, our decisions on the CPP requirements IMs are instead covered by this attachment, so that all information about our decisions regarding the CPP requirements is in one place.

²⁰⁹ Commerce Commission "Input methodologies review decisions: Report on the IM review" (20 December 2016).

²¹⁰ For example, for EDB and GPB cost allocation policy and implementation decisions, refer to Commerce Commission "Input methodologies (electricity distribution and gas pipeline services): Reasons paper" (22 December 2010), p. 55-56.

Structure and format of this attachment

473. We have structured the decisions relating to the CPP requirements IMs as follows:
- 473.1 content of CPP applications;
 - 473.2 process relating to CPP proposals;
 - 473.3 assessing and evaluating CPP proposals; and
 - 473.4 determining a CPP.
474. As in the Report on the IM review, we have assigned each pre-review decision with a unique code (eg, CP01) and presented each pre-review decision in the same tabular format.
475. For each pre-review decision, this attachment indicates whether or not we have changed it (either at a policy level, or in terms of the implementation of the decision).
476. For those pre-review decisions that we do propose changing, it summarises how and why, referring back to the body of this paper or other papers for more information.
477. It also presents those pre-review decisions that, having considered them in light of our framework, submissions on the IM, and all other relevant information before us, we have not changed.

Review of existing decisions relating to the content of CPP applications

Price path information

Decision CP01 Price path information	Original 2010 decision CPP application must contain sufficient information to support a building blocks analysis necessary to determine a price path. Building block information to be provided in spreadsheets. See section 9.2 of 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have made an implementation change for this decision

478. We have made an implementation change to IM decision CP01.
479. We have changed the IMs to explicitly set out the criteria that must be met by an applicant when providing price path information in spreadsheet form.

Why we have made an implementation change to this decision

480. We consider that this change will reduce ambiguity and provide greater certainty to CPP applicants. Further details are set out in Chapter 5 – Information requirements.

Expenditure information – qualitative

Decision CP02 Expenditure information – qualitative	Original 2010 decision CPP application must include information on capex, opex, demand and network in qualitative form as specified in Schedule D. See section 9.5 and Appendix K3 of 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have made an implementation change for this decision

481. We have made an implementation changes to IM decision CP02 as it applies to EDBs. We have yet to consider whether a change is required for GPBs at this stage.²¹¹

²¹¹ We have not yet reached draft decisions on the CPP information requirements IMs for gas pipeline businesses. Further discussion on this matter is found at paragraph 34.

482. We have:

- 482.1 better aligned the information requirements set out in Schedule D of the IMs with the EDB ID Determination;
- 482.2 reduced the level of disaggregation required for certain information; and
- 482.3 improved the requirements to provide information on the deliverability of proposed expenditure; and
- 482.4 simplified the information requirements on related parties and expenditure escalations.

Why we have made this implementation change

483. We consider that this change will reduce the cost and complexity of applying for a CPP, and provide additional certainty as to our expectations for deliverability information. Further details are set out in Chapter 5 – Information requirements.

Expenditure information – quantitative

Decision CP03 Expenditure information – quantitative	<p>Original 2010 decision</p> <p>CPP application must include information on capex, opex, demand and network in quantitative form.</p> <p>This information is quantitative and must be provided in spreadsheet format contained in schedule E.</p> <p>See section 9.5 and Appendix K3 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have made implementation changes for this decision

484. We have made implementation changes to IM decision CP03 as it applies to EDBs. We have yet to consider whether a change is required for GPBs at this stage.²¹²

485. We have:

- 485.1 better aligned the Schedule E information requirements with the EDB ID determination; and
- 485.2 reduced the level of disaggregation required for certain information.²¹³

²¹² We have not yet reached draft decisions on the CPP information requirements IMs for gas pipeline businesses. Further discussion on this matter is found at paragraph 34.

Why we have made these implementation changes

486. We consider that these changes will reduce the cost and complexity of applying for a CPP and clarify these areas of the CPP requirements IMs. Further details are set out in Chapter 5 – Information requirements.

Period of information required

Decision CP04 Period of information required	<p>Original 2010 decision</p> <p>CPP applicant must specify the period of the CPP that is sought and provide information sufficient to cover a 5 year CPP period and the preceding years for which ID information is not yet available.</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

487. We have not made any changes to IM decision CP04 or the way it is implemented.

Detail on material projects and programmes

Decision CP05 Detail on material projects and programmes	<p>Original 2010 decision</p> <p>CPP application must include detailed information on the most material projects and programmes relating to the CPP proposal.</p> <p>See section 9.5 and Appendix K3 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have made an implementation change for this decision

488. We have made an implementation change for IM decision CP05 as it applies to EDBs and GPBs.
489. We have allowed a level of flexibility in the number of identified programmes for which more in depth information is required, as part of the CPP proposal (these programmes are then able to be verified in greater detail). The verifier will judge on a case by case basis the appropriate number of "identified programmes".

²¹³ Such as the information required for capital contributions, related party transactions, and controllable and uncontrollable opex.

Why we have made this implementation change

490. We consider that this change will reduce the cost and complexity of applying for a CPP and ensure that the verifier is able to focus the detailed verification on the most material programmes in a CPP proposal.
491. Further details are set out in Chapter 6 – Verification requirements.

Information relevant to prices

Decision CP06 Information relevant to prices	<p>Original 2010 decision</p> <p>CPP application must contain information on proposed new pass-through costs, and proposed recoverable costs relating to costs of making CPP application.</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

492. We have not made any changes to IM decision CP06 or the way it is implemented.
493. We note that we are applying this IM decision CP06 by expanding the range of pass-through and recoverable costs for CPPs, as discussed in Chapter 3 – Improvements to the way the DPP and CPP work together.

Verification

Decision CP07 Verification report	<p>Original 2010 decision</p> <p>CPP application must include a verification report, all information provided to the verifier, and certification from the verifier.</p> <p>See section 9.6 and Appendix K4 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

494. We have not made any changes to IM decision CP07 or the way it is implemented.
495. We note that we have made changes to the verification process requirements (which results in the production of the verification report), as set out below in IM decision CP21.

Audit and assurance

Decision CP08 Audit and assurance report	Original 2010 decision CPP application must include an audit report signed by the auditor. See section 9.6 of 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

496. We have not changed IM decision CP08 or the way it is implemented.
497. We note that we have made changes to the audit and assurance process requirements (which result in the production of the audit report), as set out below in IM decision CP22.

Consumer consultation

Decision CP09 Consumer consultation evidence	Original 2010 decision CPP application must provide evidence of consumer consultation. See section 9.6 of 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

498. We have not made changes to IM decision CP09 or the way it is implemented.
499. We note that we have made changes to the consumer consultation process requirements, as set out below in CP23.

Certification

Decision CP10 Certification	Original 2010 decision CPP application must include the certificates recording Director's certification. See section 9.6 of 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

500. We have not made changes to IM decision CP10 or the way it is implemented.

Modifications and exemptions of CPP application requirements

Decision CP11 Modification or exemption of CPP application requirements (2015 decision)	<p>Original 2015 decision (as part of IM review fast track)</p> <p>CPP application must include information relating to all approved modifications and exemptions, including evidence any conditions of the approval have been met, and an indication of where the exemptions and modifications have been applied.</p> <p>Input methodologies review – Amendments to input methodologies for customised price-quality paths – Final reasons paper for Limb 1 of the CPP fast track (12 November 2015)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision as part of the main IM review

501. This decision was first introduced earlier in the IM review as part of the fast track process. We have not made any subsequent changes to CP11 or the way it is implemented.

Information regarding quality

Decision CP12 Information regarding quality	<p>Original 2010 decision</p> <p>If sought, a CPP application must include information to support a quality standard variation, including reasons for the change and an engineer's report (EDBs only).</p> <p>See section 9.3 and Appendix K2 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB

We have made implementation changes to this decision

502. We have made changes to the way that IM decision CP12 is implemented. We have updated the information requirements for CPP proposals where a quality standard variation is proposed, to reflect the most recent way we set quality standards. We have also removed the requirement to show the effect of the proposed quality standard variation if it had applied the previous 5 years.

Why we have made the implementation changes

503. These changes are discussed in more detail in Chapter 5 – Information requirements.

Cost allocation information

Decision CP13 Cost allocation information	<p>Original 2010 decision</p> <p>CPP application must include information on the allocation of operating costs and RAB values.</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have made implementation changes to this decision

504. We have made changes to the way that IM decision CP13 is implemented for EDBs and GPBs.
505. We have:
- 505.1 better aligned the cost allocation information requirements, including Schedules B and C, with the relevant ID Determinations; and
 - 505.2 added a materiality threshold that must be met, before providing certain cost allocation information; and
 - 505.3 included tables in Schedules B and C requiring the applicant to provide the rationale for selecting proxy cost allocators.

Why we have made these implementation changes

506. We consider that these changes will reduce the cost and complexity of applying for a CPP. Further details are set out in Chapter 5 – Information requirements

Asset valuation information

Decision CP14 Asset valuation information	<p>Original 2010 decision</p> <p>CPP application must include information on RAB roll forward, depreciation, revaluations, commissioned assets, asset disposals, and works under construction.</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

How we have changed this decision

507. We have made changes to IM decision CP14 and its implementation, as it applies to EDBs.

508. We have reduced the level of disaggregation of forecast depreciation. For example by:
- 508.1 grouping projects and programmes by asset categories and simplifying the calculation of depreciation for forecast commissioned assets; and
 - 508.2 amending the depreciation information requirements to reflect that depreciation is calculated using asset expenditure category which is a more aggregated category than asset types.

Why we have made these changes

509. We consider that these changes will reduce the cost and complexity of applying for a CPP. Further details are set out in Chapter 5 – Information requirements.

Tax information

Decision CP15 Tax information	<p>Original 2010 decision</p> <p>CPP application must include information on regulatory tax allowance, tax losses, permanent differences, amortisation of initial differences in asset values, deferred tax, temporary differences, and regulatory tax asset value.</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have made implementation changes to this decision

510. We have made changes to the way that IM decision CP15 is implemented.
511. We have removed the requirement to provide regulatory tax asset value information by asset categories.

Why we have made these changes

512. We consider that this change will reduce the cost and complexity of applying for a CPP. Further details are set out in Chapter 5 – Information requirements.

Information relevant to alternative methodologies

Decision CP16 Information relevant to alternative methodologies	<p>Original 2015 decision (as part of IM review fast track)</p> <p>CPP application must include information demonstrating alternative methodologies have equivalent effect.</p> <p>Input methodologies review – Amendments to input methodologies for customised price-quality paths – Final reasons paper for Limb 1 of the CPP fast track (12 November 2015)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision as part of the main IM review

513. This decision was first introduced earlier in the IM review as part of the fast track process. We have not made any subsequent changes to CP16 or the way it is implemented.

Cost of capital information

Decision CP17 Cost of capital information	Original 2010 decision CPP application must include information regarding WACC. Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

514. We have not made changes to IM decision 17 or the way it is implemented.²¹⁴

Gas pricing methodology to be submitted with CPP proposals – GDBs and GTBs

Decision CP18 Gas pricing methodology to be submitted with CPP proposal – GDBs and GTBs	Original 2010 decision GPB will be required to submit a pricing methodology as part of its CPP proposal if it has been identified through the most recent information disclosure summary and analysis as being required to do so, were it to apply for a CPP. See section 9.3 and Appendix I of 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	GDB/GTB

We have not made any changes to this decision

515. We have not made any changes to IM decision CP18 or the way it is implemented.

²¹⁴ We note that we have made some consequential changes to the WACC information requirements to reflect that a CPP WACC is no longer published, and that the DPP WACC applies instead.

Review of existing decisions relating to processes for CPP proposals

General matters

Decision CP19 General matters	Original 2010 decision A supplier may seek a CPP by submitting a CPP application that complies with the requirements specified in the IMs. CPP application must include the reasons for the proposal, information on priority of the proposal, and duration of the CPP period sought. Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

516. We have not made any changes to IM decision CP19 or the way it is implemented.

Quality-only CPP

Decision CP20 Quality-only CPP	Original 2010 decision A supplier may seek a quality-only CPP which does not require verification. The quality-only CPP must be reviewed by an independent engineer (EDBs only). See section 9 and Appendix K2 of the 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB

How we have changed this decision

517. We have made a change to IM decision CP20 to remove the option for EDBs to apply for a quality-only CPP.

Why we have made this change

518. We consider that we will be able to achieve a materially equivalent outcome to a quality-only CPP using a DPP reopener and we consider that this is a more appropriate mechanism for this type of change to the quality path. This change will not take effect until 2020.

519. Further details on our proposed decision to remove quality-only CPPs and introduce a quality standard variation reopener are set out in Chapter 3 – Improvements to the way the DPP and CPP work together.

Verification requirements

Decision CP21 Verification requirements	<p>Original 2010 decision</p> <p>A verifier must be engaged and all proposals must be verified, except quality-only proposals. Applicant must provide verifier with necessary information to verify the proposal.</p> <p>See section 9.6 and Appendix K4 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This original decision applies to (sectors):	EDB/GDB/GTB

We have made implementation changes for this decision

520. We have made implementation changes to IM decision CP21 as it applies to EDBs and GPBs.
521. We have made changes to clarify the role of the verifier, improve the verification process and allow a degree of flexibility in the verification process.
522. We have:
- 522.1 added a new section to the verifier's Terms of Reference in Schedule G of the IMs that defines the verifier's role, purpose, and obligations;
 - 522.2 required the CPP applicant to provide us with a high level summary of their application by the time the verifier is engaged;
 - 522.3 amended the tripartite deed requirements in Schedule F6 to include a communication protocol that sets out the roles and obligations of the parties during the verification process regarding communication, and to allow meeting minutes to be used as the evidential basis for any verifier technical opinions;
 - 522.4 allowed the verifier greater flexibility in the number of identified programmes that are selected;
 - 522.5 removed the obligation for the verifier to consider non-standard depreciation;
 - 522.6 removed the requirement for an independent engineer to provide a report on a quality standard variation, and instead allowing suppliers to prepare the report themselves, subject to verification by the verifier (EDB IMs only); and
 - 522.7 limited the requirement for the verifier to provide us with a list of all information provided to it by the applicant, to information *relied upon* by the verifier in fulfilling its obligations under Schedule G.

Why we have made these implementation changes

523. Further details are set out in Chapter 6 – Verification requirements.

Audit and assurance requirements

Decision CP22 Audit and assurance requirements	Original 2010 decision An auditor must be engaged and the CPP proposal must be audited. See section 9.6 of 2010 EDB-GPB IM reasons paper: Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This original decision applies to (sectors):	EDB/GDB/GTB

We have made implementation changes for this decision

524. We have made implementation changes for IM decision CP22 as it applies to EDBs and GPBs.

525. Our changes more clearly distinguish the auditor's role in respect of historical and forecast information, and better align the IM requirements with industry standards for audit under the Financial Reporting Act 2013.

526. We have:

- 526.1 modified the audit requirements to differentiate the role of the auditor with respect to historical financial information and forecast financial information;
- 526.2 clarified that the auditor needs to provide a report as part of the audit; and
- 526.3 set out our expressly lay out our expectations in relation to cost allocation information.

Why we have made these implementation changes

527. Further details are set out in Chapter 7 – Audit requirements.

Consumer consultation requirements

Decision CP23 Consumer consultation requirements	Original 2010 decision <p>A CPP applicant must consult with its consumers. Consumer feedback is particularly relevant where different price/quality trade-offs are available. Our requirement is that there should be adequate notification and promotion of consumer engagement. The applicant must report on the extent that consumer feedback has been taken into consideration but the Commission notes that consumer agreement to the proposed CPP is not required.</p> <p>See section 9.6 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This original decision applies to (sectors):	EDB/GDB/GTB

We have made implementation changes for this decision

528. We have made implementation changes for IM decision CP23 as it applies to EDB and GPBs.
529. We now:
- 529.1 require CPP applicants to notify consumers of the price and quality impact of any alternative investment options in their CPP proposal, that are linked to the applicant's rationale for applying for a CPP;
 - 529.2 require the applicant to notify consumers why any proposed quality standard variation had been chosen over alternative quality standards;
 - 529.3 require the verifier to report on the extent and effectiveness of the applicant's consultation; and
 - 529.4 require the applicant to provide us with its planned consultation strategy early in the CPP process.
530. Further details are set out in Chapter 8 – Consumer consultation requirements.

Certification requirements

Decision CP24 Certification requirements	<p>Original 2010 decision</p> <p>The Commission requires certification of the information in a proposal.</p> <p>See section 9.6 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This original decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

531. We have not made changes to this decision or the way it is implemented.

Reconsideration of a CPP

Decision CP25 Reconsideration of a CPP	<p>The IM decision in respect of reconsideration of a CPP is IM decision RP02, which is set out in the Report on the IM review. This CP25 reference is a placeholder only (ie, not a separate IM decision). We have included it in this attachment to ensure that reference to all decisions affecting CPPs are captured in one place.</p>
This decision applies to (sectors):	EDB/GDB/GTB

Modification or exemption of CPP application requirements

CP26 Modification or exemption of CPP application requirements (2015 decision)	<p>Original 2015 decision (as part of IM review fast track)</p> <p>Commission may approve modification and exemption to the content of a CPP application; information required in a CPP proposal; and consumer consultation, verification, and audit and certification requirements for CPP proposals.</p> <p>Input methodologies review – Amendments to input methodologies for customised price-quality paths – Final reasons paper for Limb 1 of the CPP fast track (12 November 2015)</p>
This decision applies to (sectors):	EDB/ GDB/GTB

We have made an implementation change to this decision

532. This decision was first introduced earlier in the IM review as part of the fast track process. We have since changed the way IM decision CP26 is implemented for EDBs as part of the main IM review.

533. We have explicitly identified that the scale of a supplier can be taken into account when deciding on requests for modifications and exemptions.

Why we have made this implementation change

534. Further details are in Chapter 4 – Evaluation of CPP proposals; and Chapter 5 – information requirements.

Review of existing decisions relating to processes for assessing and evaluating CPP proposals

Evaluation criteria

Decision CP27 Evaluation criteria	<p>Original 2010 decision</p> <p>Commission must assess all CPP proposals against the evaluation criteria specified in the IMs.</p> <p>See section 9.4 of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

535. We do have not made changes to IM decision CP27 or the way it is implemented.

536. Further discussion of how we apply the evaluation criteria is set out in Chapter 4 – Evaluation of proposals.

Review of existing decisions relating to processes for determining a CPP

Determination of annual allowable revenues

Decision CP28 Determination of annual allowable revenues	<p>Original 2010 decision</p> <p>Allowable revenue amounts by reference to building blocks components and a 'CPI-X' smoothing requirement.</p> <p>see section 9.3 and Appendix K of 2010 EDB-GPB IM reasons paper:</p> <p>Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)</p>
This original decision applies to (sectors):	EDB/GDB/GTB

How we have changed this decision

537. We have made changes to IM decision CP28 as it applies to GDBs, to codify the approach to claw-back that we used in making Orion's 2013 CPP determination.²¹⁵ In particular, we have:

537.1 reflected that the claw-back can be for historical over-recovery and under-recovery of revenue; and

537.2 that the present value of claw-back amounts would be used if adjusting for claw-back in the BBAR calculation.

538. In addition, to give effect to the change from a lagged revenue cap to a pure revenue cap for GTBs,²¹⁶ we have removed references to the ΔQ factor in the revenue-setting formula in the GTB CPP IMs.

Cost allocation and asset valuation

Decision CP29 Cost allocation and asset valuation	Original 2010 decision Allocation of forecast operating costs and calculation of rolled-forward asset values must largely follow rules applying to information disclosure. Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

539. We have not made any changes to IM decision CP29 or the way it is implemented in this paper. However, we note that this pre-review decision would be affected by changes we have made to the pre-review decisions on cost allocation and asset valuation. These changes are discussed in the Report on the IM review at Chapter 3 – Cost allocation decisions we have changed, and Chapter 4 – Asset valuation decisions we have changed.

²¹⁵ ENA and PwC have previously submitted that the wording of the formula that adjusts BBAR for any applicable claw-back could be clarified to reflect that the claw-back can be for historical over-recovery and under-recovery of revenue. See ENA and PwC "Review of Input Methodologies" (14 February 2014), para 31.

²¹⁶ See: Commerce Commission "Input methodologies review decisions: Topic paper 1 – Form of control and RAB indexation for EDBs, GPBs and Transpower" (20 December 2016); and Commerce Commission "Input methodologies review decisions: Report on the IM review" (20 December 2016), under existing decision SP02.

Treatment of taxation

Decision CP30 Treatment of taxation	Original 2010 decision Regulatory tax allowance is calculated using the modified deferred tax method for EDBs and GDBs and a tax payable method for GTBs. Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

540. We have not made any changes to IM decision CP30 or the way it is implemented in this paper. However, we note that this decision is affected by changes we have made changes to our IM decisions on taxation. These changes are discussed in the Report on the IM review at Chapter 5 – Treatment of taxation decisions we have changed.

Cost of capital

Decision CP31 Cost of capital	Original 2010 decision Method of determining cost of capital uses the simplified Brennan-Lally model. Input Methodologies (Electricity Distribution and Gas Pipeline Services): Reasons Paper (22 December 2010)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision

541. We have not made changes to IM decision CP31 in this paper. However, we note that this decision is affected by changes to our IM decisions on the cost of capital. These changes are discussed in the Report on the IM review at Chapter 6 – Cost of capital decisions we have changed.

Alternative methodologies with equivalent effect

Decision CP32 Alternative methodologies with equivalent effect (2015 decision)	Original 2015 decision (as part of IM review fast track) Alternative building block methodologies for cost allocation and asset valuation, treatment of taxation and the TCSD may be applied where they produce an equivalent effect. Input methodologies review – Amendments to input methodologies for customised price-quality paths – Final reasons paper for Limb 1 of the CPP fast track (12 November 2015)
This decision applies to (sectors):	EDB/GDB/GTB

We have not made any changes to this decision as part of the main IM review

542. This decision was first introduced earlier in the IM review as part of the fast track process. We have not made any subsequent changes to CP32 or the way it is implemented.