COMMERCE COMMISSION NEW ZEALAND
Te Komihana Tauhokohoko

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Reconsideration of default price-quality path for Unison Networks Limited – unforeseeable major capex project to supply Tauhara geothermal power station

Draft decision

Date: 1 December 2021

Contents

Executive summary

Unison has applied to reopen the default price-quality path to increase its allowable revenue to cover an unforeseeable major capex project

X1 In early 2021, Contact Energy Limited (**Contact**) entered into an agreement with Unison Networks Limited (**Unison**) for the supply of electricity from Unison's network for the construction and operation of Contact's Tauhara generation station near Taupo (**project**).

X2 On 29 June 2021, Unison applied to us to reopen the *Electricity Distribution Services Default Price-Quality Path Determination 2020* [2019] NZCC 21 (**DPP3**)[1] to increase its allowable revenue to cover the cost of the project of $7.3 million.[2] Unison plans to commission $2.1 million and $5.2 million of project assets in disclosures year two and three of the DPP3 regulatory period, which ends in March 2025.

X3 Unison considers the project meets the relevant criteria for a 'unforeseeable major capex project' under the *Electricity Distribution Services Input Methodologies Determination 2012* [2012] NZCC 26 (**EDB IMs**),[3] justifying reopening Unison's DPP3 price path.

Our draft decision is to accept Unison's request and amend Unison's DPP3 price path

X4 Our draft decision is to accept Unison's request. This paper sets out:

X4.1 our draft decision that the project is an unforeseeable major capex project and justifies us reconsidering and reopening Unison's DPP3 price path on this basis; and

X4.2 our draft amendment under s 52Q of the Commerce Act 1986 (**Act**) to Unison's price path to include the costs that a prudent non-exempt electricity distribution business (**EDB**)[4] would incur in undertaking the project.

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1 Commerce Commission, *Electricity Distribution Services Default Price-Quality Path Determination 2020* [2019] NZCC 21, 27 November 2019 (**DPP3**), available at: https://comcom.govt.nz/__data/assets/pdf_file/0029/191972/2019-NZCC-21-Electricity-distribution-services-default-price-quality-path-determination-2020-27-November-2019.pdf.

2 Unison, *Application for unforeseen major customer capex reopener*, 29 June 2021 (**application**).

3 Clause 4.5.5A of the EDB IMs defines and sets out the criteria for an 'unforeseeable major capex project'. A consolidated version of the EDB IMs is available at: https://comcom.govt.nz/__data/assets/pdf_file/0017/60542/Electricity-distribution-services-input-methodologies-determination-2012-consolidated-20-May-2020-20-May-2020.pdf.

4 Under clause 1.1.4(2) of the EDB IMs, a 'non-exempt EDB' is an EDB other than a consumer-owned EDB exempt under s 54G(2) of the Act.

We seek views from interested parties ahead of our final decision

X5 Interested parties may provide their views by no later than 15 December 2021. Further details on how views can be provided are set out below at paragraphs 1.8 to 1.11.

1. Introduction

1.1 On 29 June 2021, Unison applied to us to 'reopen' its DPP3 price path to increase Unison's allowable revenue to cover a project Unison considers is a 'unforeseeable major capex project'.[5]

1.2 The project is to provide an electricity network connection between Contact's Tauhara generation station and Unison's distribution network.[6] The first phase of the project will supply electricity for the construction of the generation station, and the second phase will supply electricity for the generation station's operation when it is commissioned.

1.3 Under the EDB IMs, we may:

1.3.1 reconsider DPP3 if we are satisfied the project meets the criteria for an 'unforeseeable major capex project';[7] and

1.3.2 after reconsidering, reopen and amend Unison's DPP3 price path to include the efficient costs that a prudent non-exempt electricity distribution business (**EDB**) would incur in undertaking the project.[8]

Purpose of this paper

1.4 This paper sets out:

1.4.1 our draft decision to reconsider Unison's DPP3 price path because the project meets the EDB IMs' criteria for an unforeseeable major capex project; and

1.4.2 a draft s 52Q amendment to reopen DPP3 and amend Unison's price path in line with clause 4.5.7(1) and (3) of the EDB IMs.

1.5 We seek submissions by 15 December 2021 from interested parties on our draft decision and draft s 52Q amendment to inform our final decisions on the same matters.

Structure of this paper

1.6 The paper first explains how interested parties can submit their written views on our draft decision and draft s 52Q amendment. In the following order, the paper then:

1.6.1 sets out our legal framework and criteria for reconsidering and amending Unison's DPP3 price path; and

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[5] Clause 4.5.5A of the EDB IMs defines 'unforeseeable major capex project'. The definition's criteria are set out and analysed later in this draft decision.

[6] Application, above n 2.

[7] Clause 4.5.6(1)(a)(vi) of the EDB IMs.

[8] Clause 4.5.7(1) and (3) of the EDB IMs.

1.6.2 applies the legal framework and criteria to Unison's application, giving reasons for our draft decision and explaining our draft s 52Q amendment.

1.7 Accompanying this paper are copies of Unison's application and a draft of an s 52Q amendment to provide for the price-path change based on our draft decision.

How you can provide your views on our draft decision and draft s 52Q amendment

1.8 Before making our final decision, we seek your written views on:

1.8.1 our draft decision set out in Chapter 4; and

1.8.2 our draft s 52Q amendment, published alongside this paper.

1.9 Table 1 below sets out the timeframes for you to provide your submissions, and when we expect to make our final decision.

Table 1: Dates for responses and process from here

Date	Event
15 December 2021	Submissions due on this paper
Q1 2022	Expected final decision

1.10 Please address your submission to Dane Gunnell c/o regulation.branch@comcom.govt.nz with 'Unison DPP MCP reopener consultation' in the subject line of your email.

1.11 While we discourage requests for non-disclosure of submissions so that all information can be tested in an open and transparent manner, there may be cases in which submitters wish to provide information in confidence. We offer the following guidance:

1.11.1 if it is necessary to include confidential material in a submission, the information should be clearly marked, with reasons why it is confidential;

1.11.2 if commercial sensitivity is asserted, submitters must explain why publishing the relevant information would be likely to unreasonably prejudice their commercial position or that of another person who is the subject of the information;

1.11.3 both confidential and public versions of the submission are required to be provided. The responsibility for ensuring that confidential information is not included in a public version of a submission rests entirely with the party making the submission;[9] and

[9] Parties can also request that we make orders under s 100 of the Act in respect of information that should not be made public. Any request for an s 100 order must be made when the relevant information is supplied to us and must identify

1.11.4 we request that you provide multiple versions of your submission if it contains confidential information or if you wish for the published electronic copies to be 'locked'. This is because we intend to publish all submissions on our website. Where relevant, please provide both an 'unlocked' electronic copy of your submission, and a clearly labelled 'public version'.

the reasons why the relevant information should not be made public. We will provide further information on s 100 orders if requested by parties. A key benefit of such orders is to enable confidential information to be shared with specified parties on a restricted basis for the purpose of making submissions. Any s 100 order will apply for a limited time only as specified in the order. Once an order expires, we will follow our usual process in applying the Official Information Act 1982 in respect of any request for information provided to us in relation to this matter.

2. Legal framework and criteria for reconsidering and amending Unison's DPP3 price path

DPP3's price path and quality standards may only be reconsidered in limited circumstances

2.1 We determined DPP3 under the EDB IMs on a forecast, *ex-ante* basis to cover the regulatory period of 2020 to 2025. Once determined, DPP3's price path and quality standards may not be reconsidered (or reopened) within the regulatory period except in limited circumstances,[10] which, under s 52T(1)(c)(ii) of the Act, include those specified in Subpart 5 of Part 4 of the EDB IMs.

2.2 Under clause 4.5.6(1)(a)(vi) of the EDB IMs, one of the specified circumstances where we may reconsider the DPP3 price path is if an EDB identifies a project or programme that meets the criteria for an 'unforeseeable major capex project' under clause 4.5.5A of the EDB IMs. Unison has applied on this basis, contending that the project meets the criteria under clause 4.5.5A.[11]

2.3 We set out the policy basis and the legal criteria for the 'unforeseeable major capex project' reopener under the next two subheadings.

The unforeseeable major capex project reopener enables an EDB to undertake a significant capex project that was unforeseeable at the DPP3 reset

2.4 When setting DPP3, we recognised that the changing nature of the electricity sector, largely driven by decarbonisation and the uptake of new technology, may require additional investments in electricity networks during the DPP3 regulatory period, beyond that provided for in the price path. The extent, timing and impact of these changes is uncertain, and the need or cost of such investments may have been unforeseeable at the DPP3 reset.[12]

2.5 In our consideration of this uncertainty at the DPP3 reset, we amended the EDB IMs to introduce reopeners for large system growth and new connection projects and programmes that were unforeseeable, or for which the costs were under forecast, at the reset.[13]

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[10] Sections 52T(1)(c)(ii) and 53ZB of the Act.

[11] Application, above n 2, at [1].

[12] Commerce Commission, *Default price-quality paths for electricity distribution businesses from 1 April 2020 – Final decision Reasons paper*, 27 November 2019 (**DPP3 reasons paper**), at [4.1] and [4.37], available at: https://comcom.govt.nz/__data/assets/pdf_file/0020/191810/Default-price-quality-paths-for-electricity-distribution-businesses-from-1-April-2020-Final-decision-Reasons-paper-27-November-2019.PDF.

[13] DPP3 reasons paper, above n 12, at [4.18] – [4.20].

2.6 The aim of the reopeners is to ensure, where possible, that distributors are able and incentivised to undertake the investment required to meet the one-off sporadic and changing needs of external stakeholders. The reopeners enable distributors to connect and manage significant new demand and low-carbon technologies as New Zealand increases its focus on decarbonisation, while maintaining network reliability and meeting the long-term interests of consumers.[14]

Reopener criteria under clause 4.5.5A of the EDB IMs

2.7 Clause 4.5.5A of the EDB IMs define an 'unforeseeable major capex project' as an EDB's project or programme that has a primary driver of meeting demand for:

2.7.1 connection capex;

2.7.2 system growth capex;

2.7.3 asset relocation capex; or

2.7.4 a combination of connection capex and system growth capex,

2.8 where,

2.8.1 the EDB's capex forecast used by the Commission for setting the DPP to which the reopener relates did not include that project or programme;

2.8.2 it was reasonable for that EDB not to have included that project or programme in that capex forecast;

2.8.3 the amount of capital contributions to be received by the EDB for that project or programme is sufficient in the circumstances, and is in accordance with that EDB's usual policy on capital contributions;

2.8.4 subject to clause 4.5.6(4) of the EDB IMs, forecast total value of commissioned assets for that project or programme, but excluding capital contributions, exceeds either:

(a) 1% of that EDB's forecast net allowable revenue for the DPP regulatory period in which the asset is forecast to be commissioned; or

(b) two million dollars;

2.8.5 for connection capex (as is case for the project), an authorised officer of the connecting party has confirmed in writing to the Commission that it is committed to the project or programme; and

2.8.6 the EDB will apportion any proposed additional revenue sought approximately between different parties.

[14] DPP3 reasons paper, above n 12, at [4.37].

2.9 Clause 4.5.6(4) of the EDB IMs also states that we will not reconsider a reopener in respect of an unforeseeable major capex project if the total forecast value of commissioned assets attributable to projects, which either have already resulted in a reconsideration of the DPP by the Commission or are the subject of a reconsideration application by that EDB, in a disclosure year exceeds thirty million dollars.

Our discretion to reopen and amend the DPP3 price path

2.10 Our decision making to reopen and amend the DPP3 price path is a two-step process: first, we assess whether the project meets the criteria for an 'unforeseeable major capex project' under clause 4.5.5A of the EDB IM. Then, if we decide the project meets the clause 4.5.5A criteria, under clauses 4.5.6(1)(a)(vi) and 4.5.7(1) of the EDB IMs, we exercise our discretion on whether to reopen and amend Unison's price path.

2.11 Our discretion on whether to reopen the price path is guided by the extent to which reopening the price path in these circumstances would promote the s 52A purpose of Part 4 of the Act.

2.12 If we decide to reopen the price path under clause 4.5.7(1), then under clause 4.5.7(3) of the EDB IMs, we must not amend the price path in respect of an unforeseeable major capex project by more than an amount that reflects the efficient costs that a prudent non-exempt EDB would incur in undertaking that project.

Reopening the DPP3 price path would involve amending forecast and actual net allowable revenue, and forecast aggregate value of commissioned assets for calculating capex incentives

2.13 If we reopen Unison's price path, then we must amend the components of the price path that together set Unison's allowable revenue, which are:

2.13.1 forecast net allowable revenue (**FNAR**) from disclosure years two to five of the regulatory period, that Unison will use *ex ante* to set its prices for each of those disclosure years;[15]

2.13.2 forecast aggregate value of commissioned assets for calculating capex incentives (**FAVCA**) for the disclosure years in which project assets are forecast to be commissioned;[16] and

2.13.3 actual net allowable revenue (**ANAR**) for disclosure years two to five of the regulatory period, which determines the revenue that Unison can retain for each of those disclosure years.[17]

[15] DPP3, above n 1, at Schedule 1.4.

[16] Above n 1, at paragraph (2) of Schedule 2.2.

[17] At paragraph (3) of Schedule 1.6.

2.14 Recalculating and amending Unison's FNAR and FAVCA is straightforward, since these price path components are specified values in the DPP3 determination. However, amending the ANAR is less straightforward. This is because, under the EDB IMs, changes to the FNAR for disclosure years two to five will not automatically flow into ANAR for those years because:

2.14.1 under clause 3.1.3(13)(h) of the EDB IMs, ANAR for the first disclosure year is calculated using the FNAR for the first disclosure year; but

2.14.2 under clause 3.1.3(13)(i) of the EDB IMs, ANAR for each disclosure year after the first disclosure year is ANAR for the preceding disclosure year adjusted for the actual CPI for that year and any applicable X factor.

2.15 If an EDB's ANAR does not change, the EDB will not retain any additional revenue from the reopener.[18] Accordingly, if we decided to reopen Unison's price path, we would need to amend Unison's ANAR for the first disclosure year to allow Unison to retain the additional revenue for the reopener and give effect to our policy intent for the reopener. This would align with the approach we took to implement the change in the weighted average cost of capital which we determined and published for DPP3 for EDBs on customised price-quality paths.[19]

2.16 Below we analyse whether the project meets the criteria for an unforeseeable major capex project under clause 4.5.5A of the EDB IMs, and whether we should reopen Unison's price path. Based on that analysis, we explain our draft decision to reopen the price path and how our draft s 52Q amendment would achieve that.

[18] In effect, unchanged ANAR means that increased revenues (from FNAR changes) for each of disclosure years three to five are washed up under Schedule 1.7 of DPP3 and do not flow into forecast allowable revenue. Under Schedule 1.7, there is a two-year delay between calculating a wash-up amount and the disclosure year in which that amount becomes part of an EDB's forecast allowable revenue.

[19] Commerce Commission, *Reconsideration of customised price-quality paths of Powerco Limited and Wellington Electricity Lines Limited following change to weighted average cost of capital – Final decision*, 31 March 2020, at [6.1] – [6.5], available at: https://comcom.govt.nz/__data/assets/pdf_file/0024/213774/Reconsideration-of-Powerco-Limited-and-Wellington-Electricity-Lines-Limiteds-CPPs-following-change-to-WACC-Final-decision-31-March-2020.pdf.

3. Assessment of Unison's project against the criteria for an unforeseeable major capex project

The project has a primary driver of meeting demand for connection capex

3.1 The first criterion under clause 4.5.5A is that Unison's project must be a major capex project or programme that has a primary driver of meeting demand for one of several types of capital expenditure, including 'connection capex'.[20]

3.2 Unison has stated that the project will provide a construction supply to enable Contact to construct the Tauhara power station and subsequently provide a permanent supply from Unison's network for operating the Tauhara power station.[21]

3.3 We are satisfied the primary driver for the project's capex is to establish a new connection point to supply the Tauhara power station, and therefore meets the definition of 'connection capex' and the first criterion under clause 4.5.5A.

Unison's DPP3 capex forecast did not include the project, and it was reasonable for Unison not to have included the project in its capex forecast

3.4 Under clause 4.5.5A(e) and (f), the project must not have been included in Unison's capex forecast that we used for setting DPP3, and it must have been reasonable for Unison not to have included the project in its capex forecast.

3.5 We used the capex forecast in Unison's 2019 Asset Management Plan (**2019 AMP**) as the basis for setting Unison's capex allowance for DPP3.[22] Unison's 2019 AMP did not include the project.

3.6 Unison has stated that it has been aware of Contact's plan to construct the Tauhara power station for some time. However, by the time of finalising the forecast for Unison's 2019 AMP, Contact had not made any firm commitment to proceed with its project or any firm enquiry for a new connection.[23]

3.7 We agree with Unison that there was reasonable uncertainty that Contact would:

3.7.1 start construction of the Tauhara power station in the DPP3 regulatory control period. The uncertainty on timing of construction was also exacerbated by the potential closure of the Tiwai Point smelter; and

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20 Under clause 1.1.4(2) of the EDB IMs, 'connection capex' is capex on assets to establish a new, or alter an existing, connection point or other connection point at the request of a connecting party. This includes capex relating to-

a) parts of the network for which the capex is recoverable in total, or in part, by a capital contribution from the connecting party requesting the new or altered connection point; and

b) both electricity injection and offtake connection points.

21 Application, above n 2, at pg. 1.

22 DPP3 reasons paper, above n 12, at [X51] and [198].

23 Application, above n 2, at pg. 2.

3.7.2 take supply from Unison because power stations can use the electricity they generate to supply the electricity the need to operate, and do not necessarily require electricity supply from a third party.

3.8 For the reasons above, we are satisfied that it was reasonable for Unison to not include this project in the 2019 AMP we used for the DPP3 capex forecast.

Capital contributions are sufficient and consistent with Unison's capital contributions policy

3.9 Clause 4.5.5A(g) requires us to assess whether the amount of capital contributions Unison will receive for the project are sufficient in the circumstances and accord with Unison's usual policy on capital contributions.

3.10 Unison states that no capital contribution was required as Contact is considered a financially strong counter party.[24] Unison considers this is consistent with its capital contributions policy which entitles Unison to approach capital contributions for large projects on a case-by-case basis.

3.11 Unison's policy on capital contribution from connecting parties is discretionary. The policy states that:

3.11.1 Unison reserves the right to review customer connection projects and associated capital contributions on a case-by-case basis;[25]

3.11.2 Unison may require its customers to pay a capital contribution when they request a new or altered connection to its electricity distribution network;[26] and

3.11.3 the capital contribution required will be calculated based on the net present value (**NPV**) of the project. This includes all associated costs and revenue streams over an appropriate period. A negative NPV indicates the investment would be uneconomic for Unison, therefore a capital contribution payment is required from the customer.[27]

3.12 Unison has further advised that it considered the following matters when applying its capital contribution policy:[28]

3.12.1 Unison is managing its commercial risk via a contractual arrangement with Contact. Unison considers that in a situation of a large, financially strong counterparty, it makes sense to spread the entire project cost over the life

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24 At pg. 2.

25 Unison, *FC0021 Capital Contributions policy* (**capital contributions policy**), 10 September 2019, at clause 2.1, available at: https://www.unison.co.nz/docs/default-source/default-document-library/tell-me-about/unison-group/fc0021-capital-contributions-policy.pdf?sfvrsn=5f0dc40b_4.

26 Above n 25, at pg. 7.

27 At pg. 9.

28 Unison email response of 22 September 2021 to Commission queries.

of the contract, as Unison has no need to manage any financial default risk or stranded asset risk through an up-front capital contribution;

3.12.2 this is a non-standard connection to the network because it is a connection into the network for back-up supplies and for operating the power station. No standard price applies, so Unison must determine a combination of revenues from prices and capital contribution; and

3.12.3 in other complex projects (eg, a subdivision) the long-term revenues from prices would be generated from standard published prices, in which case the capital contribution is derived from the difference between the project cost and the NPV of revenues from standard prices.

3.13 In considering the application, we are not taking any particular view on Unison's connection and capital contribution policy; we are only establishing whether the contributions are sufficient and consistent with that policy. Based on Unison's response above and its intended pricing approach (which we analyse from paragraph 3.17) to recover the costs of the project, we are satisfied that Unison is not putting consumers at risk by not asking for a capital contribution from Contact. Based on the life of other geothermal power stations in the region, the Tauhara power station is likely to remain operational long enough for Unison to recover the cost of this investment.

The forecast value of commissioned assets for the project exceeds $2 million

3.14 Under clause 4.5.5A(h), the forecast value of commissioned assets for the project must exceed (excluding capital contributions) either 1% of Unison's FNAR for the DPP regulatory period in which the assets are forecast to be commissioned, or $2 million.

3.15 Unison has advised the forecast value of commissioned assets will be $7.3 million, which is the same as the expected project cost. Unison plans to commission $2.1 million value of assets in disclosure year two and $5.2 million in disclosure year three of the DPP3 regulatory period. We are therefore satisfied the project meets the requirement under clause 4.5.5A(h).

Contact has confirmed it is committed to the project

3.16 Under clause 4.5.5A(i), an authorising officer from Contact must confirm in writing to us that Contact is committed to the project. Unison's application includes a written confirmation from Contact's Programme Manager for Contact's Tauhara power station project, who is an appropriately authorised officer. Unison's application therefore meets this requirement.

Additional revenue sought will be apportioned appropriately between different parties

3.17 Clause 4.5.5A(m) requires that any proposed additional revenue sought be apportioned appropriately between different parties. Our intent behind this requirement is that:[29]

> We expect distributors to take a reasonable approach to allocating the costs of the project or programme to customers through a reasonable capital contributions policy and future pricing, ideally in line with the pricing principles published by the Electricity Authority.

3.18 Unison's capital contributions policy advises Unison's approach to determining capital contributions outlined is consistent with Unison's Pricing Objectives and Principles,[30] which Unison states is consistent with the Electricity Authority's 2019 distribution pricing principles (**pricing principles**).[31] Unison has advised its approach as:[32]

> Projected future revenue is based on the applicable price category and price options from any new customer connection. For a project investment to be economic, future revenue must cover:
>
> - the cost to operate and maintain any proposed new extension (including indirect administration costs), and
> - an appropriate share of the cost to operate and maintain electrical distribution assets upstream from the Network Connection Point. This approach ensures existing customers are no worse off following the connection of a new user. As the expected network revenue from the new customer (in the form of additional charges and/or capital contribution) will cover the incremental cost of supply.

3.19 Unison sets out at Appendix A of its *DS1001 Pricing Methodology Disclosure 2021* why its pricing is consistent with the Electricity Authority's pricing principles.[33]

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29 DPP3 reasons paper, above n 12, at [G16].

30 Capital contributions policy, above n 25, at pg. 15.

31 Above n 25, at pg. 15.

32 At pg. 9.

33 Unison, *DS1001 Electricity Pricing Methodology Disclosure Statement 2021* (**Unison pricing methodology**), 31 March 2021, at Appendix A, available at: https://www.unison.co.nz/docs/default-source/default-document-library/tell-me-about/unison-group/pricing-information/2021-pricing/ds1001-unison-pricing-methodology-disclosure-2021-v2.pdf?sfvrsn=54bae0b_4.

3.20 Unison advises that in delivering the project, consumers in the Taupo region will receive some security of supply benefits.[34] Unison has indicated that it will apportion distribution charges appropriately between Contact and consumers in the Taupo region, in proportion to their use of the project.[35] This would be consistent with principle (a) of the Electricity Authority's pricing principles,[36] particularly in reflecting differences in network service provided to Contact and consumers in the Taupo region. As a consequence, we are satisfied this is a reasonable basis for apportioning the revenue sought from the project, consistent with clause 4.5.5A(m).

The total value of Unison assets attributable to unforeseeable major capex project reopeners is less than $30m

3.21 Clause 4.5.6(4) of the EDB IMs caps the total forecast VCA attributable to unforeseeable major capex projects or foreseeable major capex projects at $30m per disclosure year. This cap reflects the fact that larger projects and programmes that are out of step with historic expenditure or forecasts require a level of scrutiny from us that is distinct from the purpose of DPP regulation under s 53K of the Act.[37]

3.22 This is Unison's first application for an unforeseeable major capex project reopener, the total forecast value of commissioned assets attributable to the project is $7.3m, which is substantially less than the $30m cap under clause 4.5.6(4).

[34] Unison email response of 22 September 2021 to Commission queries, above n 28.

[35] Unison pricing methodology, above n 33, at Appendix A, pg. 59.

[36] Principle (a) of the Electricity Authority's 2019 distribution pricing principles, available at: https://www.ea.govt.nz/operations/distribution/pricing/, provides:

(a) Prices are to signal the economic costs of service provision, including by:

(i) being subsidy free (equal to or greater than avoidable costs, and less than or equal to standalone costs);

(ii) reflecting the impacts of network use on economic costs;

(iii) reflecting differences in network service provided to (or by) consumers; and

(iv) encouraging efficient network alternatives.

[37] Section 53K of the Act states that: "The purpose of default/customised price-quality regulation is 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."

4. Our draft decision is to reopen Unison's DPP3 price path

4.1 Having established that Unison's application meets the criteria under clauses 4.5.5A and 4.5.6(4) of the EDM IMs, our draft decision under clause 4.5.7(1) of the EDB IMs is to reconsider and reopen Unison's DPP3 price path to provide for the efficient costs a prudent non-exempt EDB would incur in undertaking the project.

4.2 Consistent with the aim of clause 4.5.5A,[38] we consider our draft decision will enable Unison to undertake investment required to meet a one-off sporadic need that it was reasonable for Unison not to have included in its DPP3 capex forecast.

4.3 We likewise consider that reopening Unison's DPP3 price path in these circumstances promotes, in particular, the s 52A(1)(a) and (b) limbs of the Part 4 purpose. It does so by, respectively enabling Unison to:[39]

4.3.1 invest and, without undue delay, recover revenue for costs that were not reasonably foreseeable at the DPP3 reset. This in turn gives Unison incentives to innovate and to invest, including in replacement, upgraded, and new assets; and

4.3.2 provide services in a timely manner at a quality that reflects Contact's demands.

4.4 Under the following subheadings, we set out:

4.4.1 the impact of our draft decision on Unison's DPP3 price path;

4.4.2 why our draft decision does not provide for operating expenditure sought by Unison for the project; and

4.4.3 why our draft decision provides for an amount that, under clause 4.5.7(3) of the EDB IMs, reflects the efficient costs a prudent non-exempt EDB would incur in undertaking the project.

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[38] DPP3 reasons paper, above n 12, at [4.37].

[39] Section 52A(1) of the Act provides: the purpose of…Part [4] is to promote the long-term benefit of consumers in markets referred to in s 52 by promoting outcomes that are consistent with outcomes produced in competitive markets such that suppliers of regulated goods or services—

(a) have incentives to innovate and to invest, including in replacement, upgraded, and new assets; and

(b) have incentives to improve efficiency and provide services at a quality that reflects consumer demands; and

(c) share with consumers the benefits of efficiency gains in the supply of the regulated goods or services, including through lower prices; and

(d) are limited in their ability to extract excessive profits.

4.5 We then outline how our draft s 52Q amendment to DPP3 provides for our draft decision to reopen Unison's price path.

We propose amending Unison's FNAR, ANAR, and FAVCA to give effect to our draft decision

4.6 Table 2 and Table 3 show the impact of our draft decision on Unison's FNAR and FAVCA.

Table 2: FNAR ($000s) for Unison per assessment period[40]

	31 March 2021	31 March 2022	31 March 2023	31 March 2024	31 March 2025
FNAR in DPP3[41]	100,019	101,970	104,035	106,115	108,238
FNAR after reconsideration of the DPP3 PQ path	100,019	102,231	104,301	106,387	108,515

Table 3: FAVCA ($000s) for the DPP regulatory period

	31 March 2021	31 March 2022	31 March 2023	31 March 2024	31 March 2025
Capex allowance in DPP3[42]	46,746	52,525	50,531	46,852	48,041
Capex allowance after reconsideration of the PQ path	46,746	54,653	55,713	46,852	48,041

4.7 Since ANAR for each disclosure year following the first disclosure year is calculated from FNAR for the first disclosure year combined with adjustments for actual CPI value for the relevant year, we cannot determine ANAR values *ex-ante*. Under the penultimate subheading of this draft decision, we describe how we propose to amend ANAR to give effect to our draft decision.

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40 The DDP3 uses the term 'assessment period' which covers the same 12-month period (commencing 1 April and ending on 31 March of the following year) as the EDB IMs' term 'disclosure year'. For ease of reference, we have used 'disclosure year' in the rest of this paper.

41 DPP3, above n 1, at Schedule 1.4.

42 Above n 1, at paragraph (2) of Schedule 2.2.

Our draft decision does not provide for operating expenditure sought by Unison for the project

4.8 Unison's application sought additional operating expenditure (**opex**) of $4,400 per annum from the fourth disclosure year of the DPP3 regulatory period to cover insurance for the project's assets.[43]

4.9 Our position is that the reopeners under clauses 4.5.5A and 4.5.5B of the EDB IMs for unforeseeable and foreseeable major capex projects are limited to capex, and exclude opex.

4.10 Our reasoning for this is as follows:

4.10.1 both reopeners focus on the adequacy of an EDB's *capex* forecast used by the Commission for setting the DPP, requiring evidence that:

(a) it was reasonable for the EDB to not include the project in that capex forecast (clause 4.5.5A); or

(b) if the project was included in the capex forecast, it would have been reasonable for a prudent EDB not to have forecast the increase in the total value of the project assets (once commissioned) in the capex forecast used by the Commission for setting the DPP (clause 4.5.5B);

4.10.2 the focus above on the capex forecast is distinct from how EDBs' forecast opex is assessed and provided for in the DPP, which in DPP3's case, was done by applying the base-step-trend approach. Including opex in our draft decision would conflict with this approach and be at odds with the purpose of default/customised price-quality regulation under s 53K of the Act, which is 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;

4.10.3 consistent with the above policy intent, the two reopeners share the following characteristics:

(a) a common feature of the definitions of 'unforeseeable major capex project' and 'foreseeable major capex project' is that they are "an EDB's project or programme that has a primary driver of meeting demand for connection *capex*; system growth *capex*; asset relocation *capex*; or a combination of connection *capex* and system growth *capex*";[44]

[43] Application, above n 2, at pg. 2.

[44] EDB IMs, above n 3, at clauses 4.5.5A(a)-(d) and 4.5.5.B(a)-(d).

(b) a threshold used in both reopeners' criteria is 'value of commissioned assets',[45] which is capex under the EDB IMs;[46] and

(c) clause 4.5.7(3) of the EDB IMs refers to the costs that a prudent non-exempt EDB would incur in *undertaking* the project – as opposed to maintaining or operating it.

4.11 Our draft decision therefore does not provide for the opex Unison sought for the project.

Our proposed price path amendment provides for the efficient costs a prudent non-exempt EDB would incur in undertaking the project.

4.12 If we decide to reconsider and reopen the price path, then our amendment must comply with clause 4.5.7(3) of the EDB IMs, which requires us to amend Unison's price path by no more than the amount reflecting the efficient costs a prudent non-exempt EDB would incur in undertaking the project.

4.13 Applying clause 4.5.7(3), we have considered the basis on which Unison determined the project costs and derived the VCA:

4.13.1 in its application, Unison advised that Contact approached Unison in August 2019 to tender a price of providing a construction supply to enable Contact to build the power station and provide a connection into Unison's network to meet operational requirements, including power station back-up auxiliary supply; and

4.13.2 Contact had alternatives to meet these needs, including constructing and owning the assets itself.[47]

4.14 Since Unison effectively tendered for the work on a competitive basis against a credible alternative, we are satisfied that the forecast VCA represents efficient costs for the purpose of clause 4.5.7(3). We therefore propose to amend Unison's price path to reflect those costs, excluding the opex Unison sought.

Our draft s 52Q amendment to amend FNAR, ANAR, and FAVCA gives effect to our draft decision to reopen Unison's DPP3 price path

4.15 Under clauses 4.5.6(1)(a)(vi) and 4.5.7(1) of the EBD IMs, we may amend the DPP3 price path to provide for an unforeseeable major capex project.

45 Above n 3, at clause 2.2.11 and the definition of 'capital expenditure' under clause 1.1.4(2).

46 At clauses 4.5.5A(h)-(i) and 4.5.5B(h), (g), and (i).

47 Application, above n 2, at pg. 2.

4.16 It is relatively straightforward to recalculate and amend Unison's FNAR and FAVCA in Schedules 1.4 and 2.2, respectively, which is what our draft s 52Q amendment provides for. Amending Unison's FNAR for disclosure years two to five of the regulatory period will increase the forecast revenue Unison may collect from its consumers, but not the actual revenue it can retain for those years, which is determined by the ANAR.

To amend ANAR for disclosure years two to five, we must amend the FNAR for the first disclosure year

4.17 As outlined above at paragraph 2.15, to give effect to our draft decision and amend ANAR for disclosure years two to five, our draft s 52Q amendment also needs to amend Unison's FNAR for the first disclosure year.

4.18 Amending FNAR for the first disclosure year entails making the following other minor consequential amendments to:

4.18.1 accommodate amending the FNAR for the first disclosure year of Unison's price path; and

4.18.2 ensure that there are no other implications for, or changes to, other provisions under DPP3.

Amending the FNAR for the first disclosure year of the DPP involves making minor adjustments to other DPP3 provisions relating to ANAR

4.19 In amending the FNAR for the first disclosure year of the DPP regulatory period:

4.19.1 clause 3.1.1(6) of the EDB IMs requires us to specify the FNAR at the start of a DPP regulatory period. However, under clause 4.5.7(1) of the EDB IMs, to give effect to our draft decision, we consider we must also amend DPP3 to specify an additional FNAR value for Unison for the first disclosure year to correctly calculate the ANAR for the second to fifth disclosure years;

4.19.2 the additional FNAR value we have specified for the first disclosure year is based on a CPI figure that does not exist at the time of this draft decision. We have accordingly specified a formula that will produce the additional FNAR value, and enable ANAR to be calculated in respect of that disclosure year and subsequent disclosure years once the CPI data becomes available;[48] and

4.19.3 we have ensured the additional FNAR value for Unison calculated for the first disclosure year will not affect price path compliance for that year.[49] We

[48] The formula produces the additional FNAR value for the first disclosure year by:
- taking the new FNAR value for the second disclosure year; and
- adjusting that new FNAR value by:
  - the actual CPI that applied for the second disclosure year; and
  - the X factor rate of change.

[49] DPP3, above n 1, at clause 8.3.

have done this by providing that the additional FNAR value specified for the first disclosure year only enables the calculation of Unison's ANAR for disclosure years two to five.

4.20 To provide for the above adjustments, our draft s 52Q amendment:

4.20.1 amends DPP3's definition of "forecast net allowable revenue" so that Unison has an additional FNAR value solely for the purpose of calculating Unison's ANAR for the second disclosure year (onwards); and

4.20.2 specifies in Schedule 1.6 of DPP3:

(a) the formula for calculating Unison's additional FNAR value for the first disclosure year; and

(b) how Unison's additional FNAR value fits into the formula for calculating ANAR for the remaining disclosure years of the DPP3 regulatory period.