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Keston Ruxton
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Dear Keston Ruxton

RESPONSE TO INPUT METHODOLOGIES REVIEW: RELATED PARTY TRANSACTIONS DRAFT DECISION

Wellington Electricity Lines Limited (**WELL**) welcomes the opportunity to respond to the Commerce Commission's (**Commission**) draft decision regarding the related party transactions framework.

WELL supports the policy intent of the related party transactions framework, and considers the Commission's draft decision is an improvement on the existing regime.

Our submission focuses on two components of the Commission's draft decision:

- ensuring the definition of a related party is workable; and
- the need for a proportionate level of information disclosure.

WELL also supports the Energy Networks Association's (**ENA**) submission on this issue.

1. Definition of a related party

The Commission's proposed definition of a related party includes any part, branch or division of the regulated business that does not supply regulated services. As drafted, this may capture, for example, internal legal or regulatory services (i.e. these services may form part of the entity that operates the regulated service, but do not supply the regulated service).

The proposed definition, therefore, may impose significant regulatory burden on valuing all the services required to operate the network. It is not clear that imposing these costs on electricity distribution businesses (**EDBs**), and ultimately consumers, is necessary to ensure related party transactions are no higher than would be obtained in an arm's length transaction.

Consistent with the ENA's submission in response to the Commission's draft, WELL considers internal divisions are not related parties. The Commission's definition should be amended accordingly.

2. Proportionate level of information disclosure

WELL recognises the need for a level of information disclosure that allows the Commission and other stakeholders to assess the efficiency of related party transactions. These disclosure requirements should be flexible for individual business practices, and proportionate.

Independent assessor

WELL does not support the proposed requirement for an independent assessor where related party transactions exceed 65 per cent of a disclosure year's total operating or capital expenditure. The quantum of related party transactions should not be of concern to the Commission, so long as these transactions are efficient.

To ensure efficiency, the draft decision already includes requirements on EDBs to disclose their procurement policies, and demonstrate the market terms of related party transactions. The application of these policies, as

well as details of how and when the regulated supplier last tested the market must be audited and accompanied by Director certification.

To provide certification, Directors themselves require evidence that related party transactions are at arms-length. Notably, there are strong incentives on Directors (penalties and other punitive measures) for ensuring they have sufficient evidence when making such representations.¹ The rigour and discipline this demands of EDBs to demonstrate why related party transactions are at arms-length should not be underestimated.

The regulatory framework (e.g. the incremental rolling incentive scheme) also provides EDBs with strong incentives to minimise expenditure. This includes structuring related party transactions to only incur efficient costs. The Commission's draft decision on related party transactions should have regard to this broader context; as ultimately, duplicative regulatory obligations will only expose customers to higher prices.

Map of network expenditure and constraints

The draft decision requires EDBs disclose a map of anticipated network expenditure and network constraints. The requirement for any such disclosures is more appropriately considered as an asset management plan issue, as network expenditure and constraints can clearly be independent of related party transactions.

Where appropriate, the input methodologies should promote simplicity and consistency, and the Commission should ensure regulatory obligations are specified where they are most relevant.

3. Conclusion

WELL supports a principles based approach to assessing the efficiency of related party transactions, and subject to the comments above and in the ENA's submission, the Commission's draft decision is an improvement on the existing regime.

If the Commission has any queries regarding WELL's submission, please do not hesitate to contact Jeff Anderson, Regulatory Projects Manager, at janderson@welectricity.co.nz.

Yours faithfully



Greg Skelton
CHIEF EXECUTIVE OFFICER

¹ Under the *Companies Act 1993*, Directors who knowingly make false or misleading statements are liable for penalties of up to five years imprisonment or a fine of up to \$200,000.