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Part 4 Input Methodologies Review

Submission to the Commerce Commission

From the Electricity Networks Association

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1. Introduction

The Electricity Networks Association (ENA) appreciates the opportunity to submit to the Commerce Commission (Commission) on the draft framework paper¹ and process and issues paper² as part of its Part 4 Input Methodologies (IMs) Review. This submission is on behalf of ENA's members (listed in the appendix to this submission), the electricity distribution businesses (EDBs) of New Zealand. This submission is not confidential.

New Zealand's push to decarbonise its economy will have significant consequences for the future of EDBs, Transpower and the other sectors covered by the IMs. However, the consequences for each of these sectors will be very different.

ENA members are helping deliver a low-carbon future for New Zealanders — a future based on reliable, resilient, safe, and affordable electricity networks. Demand for EDB services will increase as transport, process heat and home heating transition away from fossil-fuel sources to electricity. This will necessitate increased investment and changes to the way EDBs' assets are used. This submission focuses on issues relevant to EDBs. However, many of the issues are also relevant to other sectors covered by the IMs.

Electrification means that consumers' expenditure on electricity needs to be considered as part of their total energy expenditure. As consumers increasingly turn to electricity for transport and heating homes, their electricity costs are likely to increase. However, their total individual energy expenditure will decline as they will spend less on petrol, gas, and firewood over time.

Chapter 2 of this submission responds to the Commission's Draft Framework paper, while the more detailed chapter 3 sets out ENA's response to the Process and Issues paper.

2. Draft framework

ENA supports the substantive retention of the review framework adopted by the Commission in its 2016 IM review. The two-element approach set out in the draft framework paper is well understood, practical and deliverable, and is therefore supported by the ENA.

ENA agrees the objectives of Part 52A of the Commerce Act 1986 (Commerce Act) should be given priority in the Commission's decision-making framework. It is clear from the Climate Change Commission³, and IPCC⁴ reports that failing to address climate change would have terrible consequences for New Zealanders. The Commission therefore must give substantial weighting to

¹ Commerce Commission, Part 4 Input Methodologies Review 2023 Draft Framework paper May 2022

² Commerce Commission, Part 4 Input Methodologies Review 2023 Process and Issues-paper May 2022

³ Climate Change Commission, Ināia tonu nei: a low emissions future for Aotearoa, 2021

⁴ IPCC, Climate Change 2022: Impacts, Adaptation and Vulnerability, 2022

addressing climate change when considering the “long-term benefit of consumers” under Part 52A of the Commerce Act. The consequences for New Zealanders of businesses covered by Part 4, underinvesting due to inadequate expenditure allowances to enable decarbonisation would not be in the long-term interests of consumers.

ENA is firmly of the view that in interpreting the 52A objective to promote the long-term benefit of consumers, the Commission should explicitly recognise that addressing climate change is in the long-term interest of consumers.

The draft framework sets out how the Commission “may” have regard to the permissive considerations under section 5ZN of the Climate Change Response Act 2002 (CCRA). As set out above, the ENA believes that addressing climate change is not optional and is fundamentally in the long-term benefit of consumers. Therefore, it is inconsistent that the framework only includes optional consideration of 5ZN of the CCRA. The ENA recommends the IM framework require consideration be given to 5ZN instead of the current discretionary approach.

The three overarching objectives (X18.1, X18.2 & X18.3) of the decision-making framework appropriately cover the key considerations for the Commission in assessing changes to the IMs. ENA does, however, question whether the Commission has given sufficient focus to the third of these objectives: significantly reducing compliance costs, other regulatory costs, or complexity. The ENA notes the recent Information Disclosure Process and Issues paper (also under Part 4 of the Commerce Act) proposed the inclusion of 33 additional reporting measures, but not a single removal.

ENA and its members also support the three key economic principles set out in the draft framework. As discussed below in the ENA response to the process and issues paper, the asymmetric consequences of over/underinvestment are increasingly critical in the context of climate change, and should be given greater emphasis.

Repercussions of failing to address climate change are dire. Similarly, the consequences of EDBs’ underinvestment have grown substantially. While the historical effects of underinvestment remain (that is, reduced reliability and service quality), the failure to facilitate New Zealand achieving its zero-carbon goal will be significant and irreversible. By contrast, the consequences of overinvestment have not changed and remain constrained by other features of the IM regime such as the regulated WACC.

The electrification of transport and space heating will result in electricity usage growing with a consequential increase in electricity cost, even in the absence of price increases. In considering the long-term benefit of consumers the Commission must recognise that electricity costs are one component of a consumer’s total energy cost and that rises in electricity costs will be more than offset by the reduction or elimination of other energy costs, including petroleum products for transport and gas for space heating.

The Task Force on Climate-Related Financial Disclosures (TCFD) framework is an internationally recognised regime and is being embedded into New Zealand’s financial disclosure regime via the

Financial Markets Conduct Act 2013. It is therefore appropriate that it be incorporated into the decision-making framework. ENA requests that the Commission provide further details and practical examples of how it intends to apply the TCFD framework.

In conclusion, the ENA views the draft framework as appropriate. However, it is not optional for EDBs to support decarbonisation, nor is it optional that they adapt in the face of the consequences of climate change. The Commission's decision-making framework must reflect this via the mandatory consideration of 5ZN of the CCRA.

3. Process and issues

3.1. Overview

ENA members are encouraged to see the Commission has accurately and comprehensively captured the main issues that stakeholders identified in response to the Commission's open letter⁵ and workshop.

Throughout this submission, ENA has commented at a high level on the issues the Commission has identified. These responses are intended to highlight areas for further examination in the upcoming problem definition papers for discrete issues. The responses are not intended as comprehensive solutions which carefully balance a closely scrutinised set of costs and benefits against the Commission's draft decision-making framework. ENA looks forward to actively engaging with the Commission, both in-person through workshops or other engagement methods besides submissions, and other stakeholders on how the IMs can best address the issues identified.

Not all the issues identified by the Commission are of equal consequence, materiality, and impact. Throughout this response, ENA has summarised key issues and assigned a priority rating to each issue to guide the focus the Commission should give. Broadly speaking, those issues with high priority relate to ensuring the regime has sufficient mechanisms to support EDBs in enabling New Zealand's decarbonisation and dealing with the uncertain timing, location, and scale of climate change-related investment.

In place for more than a decade, the IM regime has evolved and matured. As a result, many of the historical issues related to the regime have been settled and their application via the price-quality and information disclosure regimes bedded down. ENA's view is the Commission's IM review should be forward focused to address issues and opportunities associated with decarbonisation rather than re-litigating past debates.

The IM regime must balance regulatory certainty with over-prescription. ENA acknowledges this is not easy. However, this balance can be achieved by incorporating key principles and high-level design

⁵ [Commerce Commission, Open letter – Ensuring our energy and airports regulation is fit for purpose, April 2021](#)

features into the IMs. Detailed design and application of these principles is best left to the price-quality (CPP/DPP/IPP) and information disclosure determinations.

A wide gulf exists between the current low-cost (generic) DPP process and the bespoke, high-cost CPP process. ENA believes there is scope for the IMs to enable regulatory tools that bridge this gulf by allowing the Commission's determinations to adapt during a regulatory period to respond to changing circumstances and new information.

3.2. Risk allocation and incentives under price-quality regulation

I. Outcomes and issues in the market for electricity lines services

ENA fundamentally disagrees with the Commission's supposition that EDBs' performance and efficiency has reduced since 2008. The Commission's limited analysis neglects the material changes to the environment in which EDBs operate. This operating environment has grown vastly more complex, costly, and less permissive, resulting in profound changes to EDBs cost to deliver their core operations, maintenance, and infrastructure development activities.

Changes to EDB's operating environment which have resulted in higher costs include increased occupational health and safety requirements, such as a drastic reduction in live line work, resource and environmental consent and management obligations (e.g. wetlands, significant natural areas, and kauri dieback), and traffic management requirements and costs which have expanded to account for more than 15% of total project costs. The Infrastructure Commission recently highlighted the increasing cost environment for the delivery of infrastructure, stating that "The costs to consent and build infrastructure are rising [...] This makes it difficult to deliver infrastructure efficiently."⁶

Alongside this more complex and costly operating environment are clear societal and Government expectations that the electricity sector, including EDBs, will support New Zealand's climate change ambitions (decarbonisation and adaptation). This will come at a cost.

The Commission must recognise that productivity decline is not the same as increased inefficiency. Productivity measures a ratio of outputs to inputs. In the case of EDBs, only simple measures of productivity can be produced. These measure ratios of inputs such as opex, km of network, to outputs, such as customers served, and kWh delivered. These simple productivity measures omit any consideration of quality, resilience, safety, legislative or regulatory compliance or any other factor that has impacted how EDBs deliver their services.

⁶ [New Zealand Infrastructure commission / Te Waihanga, Infrastructure Insights, December 2021](#)

For example, an EDB that efficiently invests in cyber-security defences will inherently become less productive (there are no more kWh delivered or customers served, but IT inputs have increased). The same would be true for the following examples:

- Strengthened health and safety systems in response to the Health and Safety at Work Act 2015.
- Investment in network resilience (e.g. seismic strengthening of sub-station buildings).
- Replacement of an asset that has reached its full capacity with a new asset with higher capacity that caters for future growth.
- Customers' investments in energy efficiency (less kWh delivered over the same lines).
- Investment in future readiness projects such as monitoring of LV networks.

ENA's members are concerned that the Commission has formed a view that because of productivity decline, EDBs are inefficient. The challenge EDBs face is in demonstrating, quantitatively, the impact that all the myriad changes in regulations and expectations have had on EDBs' cost structures. One approach to this quantification is to make point-in-time comparisons of businesses and what they weren't doing in the past, and compare it with what they are now required or expected to do. To attempt this would be an expensive exercise, and may not provide a complete explanation of the variance in cost structures.

While ENA's members feel compelled to undertake such a study to defend the industry's efficiency record, we are extremely wary of incurring significant expense on such a study, given the Commission's cursory rejection of the conclusions from the NERA study on productivity in the DPP3 reset. We would welcome engagement with the Commission on the value of such work before proceeding.

The Commission's own analysis shows that EDBs' profitability has been below its estimates of reasonable returns. This lack of excess returns while quality services are continuing to be delivered is clear evidence EDBs are achieving Part 4 objectives despite their operating environment being increasingly complex and fluid.

Figure 5.1 of the process and issues paper illustrates that depreciation has been by far the largest positive contributor to the movement in the maximum allowable revenues (MAR). Depreciation is a product of asset infrastructure renewal and replacement required to maintain reliable, resilient, safe, and affordable electricity networks. Increased depreciation is not evidence of the efficiency or otherwise of EDBs.

The Commission has noted concerns that the changing interest rate environment will result in the return on capital component of the MAR increasing substantially at the next price-quality reset. EDBs have no control over the level of the WACC. It is by design an exogenous component of the Part 4 regime. While the falling WACC has offset rising expenditure levels in past resets, with this now expected to reverse in DPP4, this change in the external environment should not be a factor in driving changes in input methodologies to avoid or offset such external changes.

The Commission has long been a promoter of the on-the-day approach to the cost of debt. Variability in the WACC between price-quality resets is a design feature of the Commission’s preferred approach. It is inappropriate for the Commission to raise the prospect of a significant increase in the MAR as evidence of the inefficiency of EDBs, when the true drivers of the rise are unrelated to EDBs’ efficiency.

That said, the IM framework has a clear role in providing regulated businesses incentives to innovate. Innovation is not a riskless or costless process. Any innovation incentive mechanism within the IM regime must accept the risk of failure as a natural and intrinsic component of innovation. The innovation incentives should also recognise that not all innovation delivers cost reductions.

ENA supports the inclusion of innovation allowances in the IM regime. The current iteration of the innovation allowance, however, does not fully deliver on its objectives or potential. ENA believes that its design can be significantly improved to more appropriately incentivise innovation, and reduce its complexity and administrative burden.

Issue summary table

Issue	Priority for IM Review	ENA view
Efficiency and innovation and the pace required to lift performance	Low	EDBs have not stood still but continue to deliver reliable and affordable services in the face of increased complexity in their operating environment including ever-growing regulatory, planning and OH&S compliance.
Role of IMs to incentivise innovation	Medium	The IM’s role in innovation has been constrained by the current innovation allowance’s design complexity, compliance burden and small size.
Dimension of quality not measured	Medium	As discussed in the ENA’s recent response to the ID review process and issues paper, EDBs support reporting on the dimensions of service quality beyond the current technical measures (SAIFI/SAIDI).
Incentive mechanism	Medium	The IMs should include high-level descriptions of the incentive mechanisms. The detailed design and operationalisation of these mechanisms are best left to the DPP/CPP process.
Innovation	High	Innovation is not costless or risk-free. The current innovation allowance mechanism creates disincentives to innovate through its time and resource-intensive application process. EDBs also currently carry the entire risk burden.

Risk allocation of innovation	Medium	The current ex-post innovation allowance mechanism places the upfront risk entirely on EDBs.
Pandemic risk	Low	The IM and DPP frameworks have proven to be robust during the pandemic. Legacy impacts may prove more of a test (e.g. ongoing supply chain challenges, removal of fiscal and monetary stimulus).

II. Incentive mechanisms to improve expenditure efficiency for EDBs and Transpower

Incentives for efficient expenditure are fundamental to the effectiveness of the Part 4 regime. Our members report that they actively respond to and consider performance relative to the opex and capex allowances. However, there is a lack of confidence that opex-capex substitutions are financially neutral. There is also frustration among members that incurring customer driven capex above the allowance results in efficiency penalties when this area of expenditure is driven by non-controllable customer connection volumes and complexity.

A misfiring, complex efficiency scheme risks perverse outcomes, including embedding inefficiencies and derailing New Zealand's progress toward net-zero. The effectiveness of an incentive mechanism is as much a reflection of its workability, simplicity, and practicality, as it is of EDBs' efforts to deliver services prudently and efficiently.

The intent of the current Incremental Rolling Incentive Scheme (IRIS) is clear, as too are its efforts to eliminate any capex-opex bias. However, the current IRIS falls short in its implementation and delivery of this intent due to its complexity and the inclusion of inappropriate drivers. This prevents it from delivering actionable signals to EDB decision makers.

The global inflationary environment is driven by factors external to EDBs and New Zealand more broadly. While beyond EDBs' control, this general cost inflation has resulted in EDBs effectively being punished by the current IRIS scheme, as non-controllable cost increases are deemed to be an inefficiency that EDBs must carry forward.

The implementation of IRIS results in significant volatility in annual opex incentive amounts. ENA therefore recommends that review of the IRIS schemes forms a substantive part of the IM review.

Issue summary table

Issue	Priority for IM Review	ENA view
IRIS reform	High	<p>IRIS has the potential to deliver the risk-reward balance and incentives to achieve efficiencies. It can also provide incentives to innovate.</p> <p>ENA believes IRIS has significant potential to better achieve its objectives.</p> <p>IRIS should apply only to those costs that can be controlled by EDBs. This is implicitly recognised by the existing cost pass-throughs for some opex costs, including transmission charges, rates, and insurance. No such mechanism exists for capex. The post-pandemic input cost spike demonstrates that the IRIS punishes EDBs for factors beyond their influence.</p> <p>Customer-driven capex (particularly large load/DG) is driven by the conscious and informed decisions of customers. While EDBs have some opportunity to shape and inform these decisions, ultimately it is up to the customers to make their own commercial decisions on where, how, and when to invest and connect. EDBs should not be penalised through IRIS for meeting the needs of customers.</p> <p>Complexity is a key challenge. ENA believes the review should look for opportunities to simplify the IRIS mechanisms. The complexity of the opex IRIS has muted its ability to act as a catalyst for efficiency.</p> <p>Another challenge with the current IRIS is volatility. The Commission should investigate options to mitigate the fluctuation in annual incentive amounts to avoid fluctuations in prices.</p> <p>While the current (highly complex) IRIS, in theory, achieves parity of incentives between opex and capex, ENA believes there is value in the Commission examining the comparative benefits of a totex approach.</p> <p>There may indeed be lessons learned from the Australian Energy Regulator’s (AER) BESS and other</p>

		<p>international incentive regimes to improve the delivery of the intent of IRIS.</p> <p>Introducing regulatory sandboxes is one way the IMs can encourage innovation, and these should be considered by the Commission.</p>
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III. Form of control (short-term demand risk)

The move to a revenue cap under the 2020-2025 DPP has addressed short-term demand risk for EDBs. As with any significant change to the regulatory regime, there is scope to learn lessons from its implementation and refine its operation.

These refinements should give consideration to the merits of establishing a financeability⁷ test to ensure the IM regime (via either the cost of capital framework or application of the revenue cap) enables EDBs to maintain appropriate levels of financial sustainability over multiple regulatory periods.

In addition, the current high-inflation environment combined with the implementation of the Electricity Authority’s transmission pricing methodology has resulted in EDBs confronting the 10 per cent cap on annual MAR increases. In the final decision on Aurora’s CPP, the Commission instituted a mechanism to exclude transmission costs from the pass-through of Aurora’s MAR cap. This mechanism should apply to all EDBs via the IMs.

Issue summary table

Issue	Priority for IM Review	ENA view
Operation of revenue cap	High	<p>Introducing the revenue cap for EDBs has delivered the benefits foreseen at the time of introduction. That said there is some scope for refining the revenue cap. The following should be examined as part of the IM Review:</p> <ul style="list-style-type: none"> • The 10 per cent MAR cap at times of high inflation and significant movements in pass-through costs including the new TPM. • Financeability: climate change-related capex is likely to shift the depreciation/capex balance. Consideration should be given to introducing a financeability assessment like that used by overseas regulators including Ofgem/Ofwat/IPART.

⁷ Financeability refers to a business’s ability to meet its financing requirements and to raise new capital efficiently

IV. Longer-term demand risk

Long-term, electricity demand will grow substantially because of electrification of process heat and transport. As a result, the risk of systematic asset stranding is low for EDBs, and the existing accelerated depreciation provisions are adequate to deal with these risks.

While the risk of wholesale asset stranding is low, adaptation to the impacts of climate change will have long-term consequences for EDBs. For example, some assets may become uninsurable.

Mechanisms to deal with upside demand risk are critically important. Section 3.4 below covers the ENA's view on how the IM regime can best address the impacts on opex and capex from the uncertainty in timing and scale of demand increases stemming from electrification.

Issue summary table

Issue	Priority for IM Review	ENA view
Longer-term demand risk	Low	Long-term demand risk for EDBs is appropriately allocated. The current arrangements for accelerated depreciation and maintenance of ex-ante FCM are appropriate for the sector.

V. RAB indexation and inflation forecasting

ENA and members submitted comprehensively on RAB indexation and inflation forecasting in the 2016 IM review. The current high-inflation environment has not diminished the concerns raised previously.

The ENA recognises the forecasting of inflation is not easy. It believes there is value in the Commission investigating if its current approach is fit for purpose. Various approaches have been investigated and/or adopted in other jurisdictions. ENA strongly recommends the Commission conduct a review of best practices for inflation forecasting.

The current CPP/DPP roll-off framework has potential to cause a significant lag between the actual CPI being determined and the forecast being replaced by it. ENA believes there is no justification for not closing this gap.

The Commission has rightfully highlighted the problem of nominal debt compensation. ENA suggests that the Commission also consider whether it is appropriate that equity holders bear the entire inflation forecasting risk. ENA looks forward to addressing these issues with the Commission as part of the IM review process.

Issue summary table

Issue	Priority for IM Review	ENA view
Inflation forecast risk	High	ENA supports the Commission exploring alternate methodologies for forecasting inflation. Regardless of the approach taken, there is scope within the IM to reduce the impact of unavoidable forecast error.
Debt compensation	High	As highlighted in past submissions and accurately captured in the process and issues paper, the disconnect between the nominal debt issued by EDBs and the indexed RAB should be addressed.
RAB indexation	High	The approach to the indexation of EDBs' RAB is well established. There does not appear to be a significant issue with its application because EDBs pay nominal interest rates on their debt, with no realistic alternative. As part of the review, the Commission should consider a hybrid model alongside the indexed and unindexed approaches.

3.3. Issues relating to the cost of capital

The Commission's cost of capital methodology is well established. ENA members view it as being broadly appropriate for the purposes of Part 4 but retain some long-standing concerns about aspects of the approach. ENA accepts the Commission will review the WACC methodology and components as a matter of course.

Given the unprecedented economic environment of high inflation, moderate economic growth (giving rise to relatively perverse observed outcomes e.g. strongly negative real interest rates), and New Zealand's decarbonisation goals, there is a significant risk that adopting a mechanistic approach to updating WACC parameters would result in anomalous outcomes. Therefore, the Commission must carefully scrutinise the outputs from its cost of capital models to ensure they make economic/financial sense.

Issue summary table

Issue	Priority for IM Review	ENA view
Asset beta	Low	The Commission's approach to beta is well settled, widely understood and broadly appropriate.
TAMRP	Low	The Commission's approach to TAMRP is well settled, widely understood and broadly appropriate. There is no evidence to support a move away from it. For consistency, the 7.5% TAMRP should be applied to EDBs.
Cost of debt	Medium	The current on-the-day approach to cost of debt can result in step changes in MAR between regulatory periods, as noted in chapter 5 of the process and issues paper. The Commission should examine if the approach to estimating the cost of debt (trailing average) used in other jurisdictions (most notably the AER) would address this issue.
WACC percentile	Low	The WACC percentile has been examined thoroughly and there is no evidence to suggest that the consequences of under-investment have declined. If anything, given the decarbonisation imperative, the consequences of under-investment have increased.

3.4. CPPs and in-period adjustments to price-quality paths

The pace, scale, and order of electrification of process heat and transport and the roll-out of grid-scale DER creates uncertainty about expenditure required by EDBs to enable decarbonisation. This uncertainty makes in-period adjustment and CPPs a key priority for ENA and its members. Under the current IMs, the CPP process and in-period adjustments are not flexible and responsive enough to deal with this uncertainty.

All branches of the IM regime must work together to deliver long-term benefits to consumers. The upside demand risk associated with the timing and scale of electrification requires the CPPs, IPPs, DPPs and the ID to become more flexible. The Commission must also recognise a return to business-as-usual levels of uncertainty and investment is likely to be two to three regulatory cycles away.

In the current environment, using historical costs for establishing opex and capex allowances is inappropriate as they are not a suitable indicator of prudent and efficient expenditure going forward. Therefore, the Commission needs to adopt a forward-looking approach to the establishment of EDBs' opex and capex allowances.

Inadequate flexibility within the regime to manage unexpected changes in expenditure due to decarbonisation issues, climate change adaptation and changes in consumer demand, could result in many EDBs applying for CPPs concurrently, at great cost. This rush of applications would overwhelm the Commission's capacity to respond to each in a timely manner.

Another critical challenge for the Commission is ensuring the IM regime's regulatory burden does not obstruct EDBs enabling New Zealand's net-zero future.

The table below highlights the main tools for ensuring the price-quality determination (DPP, CPP, IPP) components of the IM regime are fit for purpose and flexible enough to keep pace with the change needed for the delivery of New Zealand's climate change objectives.

Issue summary table

Issue	Priority for IM Review	ENA view
Re-openers	High	<p>The current re-opener provisions exclude the recovery of opex. This is a significant oversight, as highlighted by the recent Unison re-opener decision. Opex must be included in all re-opener mechanisms to remove any potential capex bias and allow greater consideration of opex-based non-network solutions.</p> <p>Importantly, the re-opener process is too long. A more streamlined approach is needed to keep pace with the demands of decarbonisation.</p> <p>Re-opener provisions should only be for unforeseeable events. Other mechanisms, including contingent allowances, are better suited to events that were foreseeable but were uncertain at the time of the forecasting and/or were beyond the control of EDBs.</p>
Contingent allowances	High	<p>Contingent allowances should be incorporated into the IMs for events that were foreseeable at the time of forecasting but uncertain or were outside the control of EDBs. Typical trigger events for contingent allowances should include large-scale DG and load connections, as the timing and</p>

		investment decisions are determined by customers and therefore outside EDBs' control.
Pass-through	Medium	<p>The existing pass-through arrangements are well understood and operate as intended.</p> <p>The Commission should investigate the treatment of self-insurance costs under the insurance pass-through (see page 17).</p>
Forward-looking expenditure	High	<p>While expenditure allowances are the domain of DPP and CPP Determinations, the IM Review should consider how the Commission will undertake future expenditure forecasting requirements, as this has implications for re-openers, pass-through and contingent allowances. The base-step-trend approach for opex has not proved satisfactory in allowing for future expenditure requirements.</p>
Single issue CPP	Medium	<p>The current CPP process is time and resource-intensive and suitable only for extreme circumstances.</p> <p>Including a separate, more streamlined CPP process for a single issue would benefit the IM regime. ENA notes the delineation between a single-issue CPP and DPP re-opener will be narrow.</p>
Multiple applications (DPP, single-issue CPP or re-openers)	Medium	<p>Transitioning to a net-zero carbon economy may create situations that impact multiple EDBs concurrently. The current re-openers, pass-throughs and CPP process all require an individual application. ENA believes the IMs should introduce a way for the entire DPP to be re-opened or a co-joined application for a single-issue CPP to address issues impacting multiple EDBs that were not foreseen at the time of a DPP or CPP decision.</p>

3.5. Effectiveness of the IMs for each sector

As noted above, the IM framework for EDBs is mature and broadly appropriate, except for it being inflexible and unresponsive enough to deal with electrification and decarbonisation uncertainty.

One area where the effectiveness of the IMs could be improved is treatment of self-insurance. The present IM regime allows EDBs to pass insurance costs through in full. Climate change risks and new insurance industry practices have resulted in some EDB assets becoming uninsurable. At the same time, the cost of insurance for insurable assets has skyrocketed.

Increasingly, EDBs are turning to self-insurance to maintain reasonable levels of insurance premiums, but the costs of this are not covered by regulatory allowances (cost of capital or self-insurance premiums). Therefore, ENA recommends the Commission review mechanisms to cover the costs of managing risk.

Issue summary table

Issue	Priority for IM Review	ENA view
Self-insurance cost	Medium	The treatment of self-insurance costs should be reviewed to ensure EDBs are incentivised to manage risks effectively on behalf of consumers.

4. Conclusion

For EDBs, responding to the challenge of climate change is not optional. The Commission's decision-making framework must reflect this and, at a minimum, mandate the consideration of section 5ZN of the CCRA.

New Zealand's ambition to achieve a net-zero carbon economy is set in stone. There is, however, tremendous uncertainty over the path to achieving this. Electrification of process heat, transport, and space heating along with deployment of grid-scale DER will play a central role in delivering on this ambition. Uncertainty over the timing and scale of each of these requires building greater flexibility into the IM regime.

The difference in the level of cost, time and customisation involved in applying a DPP versus a CPP is stark. The IM regime must incorporate a greater range of tools, including contingent allowances and other flexibility mechanisms, to bridge this divide and ensure the IMs remain fit for purpose.

EDBs are striving constantly to deliver their services in a safe, reliable, resilient, and cost-efficient manner. An ever more complex operating environment, combined with escalating input costs, has caused EDBs to expend more in delivering their services. This is not inefficiency, but a reflection of the higher expectations and regulatory environment impacting on EDBs. ENA will continue to actively engage with the Commission on how best to demonstrate that its members continue to efficiently deliver reliable and affordable network services to their communities.

The intent of the IM regime's IRIS and innovation allowance is laudable. However, implementation of both is overly complex and restricts their benefit to consumers. ENA is eager to engage with the

Commission in the review to ensure innovation and efficiency incentives become more effective components of the IM regime.

ENA looks forward to engaging with the Commission and other stakeholders to shape an IM regime that meets the objectives of Part 4, and which enables New Zealand to achieve its net-zero ambitions.

The ENA's contact person for this submission is Keith Hutchinson (Keith@electricity.org.nz or (0)4 555 0074).

5. Appendix

The Electricity Networks Association makes this submission along with the support of its members, listed below.

Alpine Energy
Aurora Energy
Buller Electricity
Counties Energy
Centralines
Eastland Network
Electra
EA Networks
Horizon Energy Distribution
Mainpower NZ
Marlborough Lines
Nelson Electricity
Network Tasman
Network Waitaki
Northpower
Orion New Zealand
Powerco
PowerNet
Scanpower
The Lines Company
Top Energy
Unison Networks
Vector
Waipa Networks
WEL Networks
Wellington Electricity Lines
Westpower