

Meeting Date: 1 June 2022

## THE COMMERCE COMMISSION'S ROLE IN DISTRIBUTION ASSET MANAGEMENT AND RISK

## SECURITY AND RELIABILITY COUNCIL

This paper provides the SRC with information about the Commerce Commission's role in how distributors' approach asset management and risk, as part of the SRC's role to ensure reliable and secure energy for consumers.

**Note:** This paper has been prepared for the purpose of the Security and Reliability Council (SRC). Content should not be interpreted as representing the views or policy of the Electricity Authority.

## The Commerce Commission's role in distribution asset management and risk

- 1.1.1 As part of its theme of asset management and risk, the SRC has asked the secretariat to provide information on the Commerce Commission's (Commission's) role in how the distribution sector approaches asset management and risk.

### Monopoly regulation

- 1.1.2 The electricity distribution sector is an example of a geographic monopoly, where each distribution participant (with limited exceptions) operates the network in their location. In monopoly situations it is important to ensure consumers are not disadvantaged by a lack of competition.

### Context for the Commission's presentation

- 1.1.3 The Commission's role in the electricity sector is set out in Part 4 of the Commerce Act<sup>1</sup>. Their presentation sets the scene for this meeting's theme, complementing a report on distributor asset management from MartinJenkins, and a paper from the grid owner that follow.

### The Commission's vision and approach

- 1.1.4 The Commission's vision is New Zealanders are better off because markets work well, and consumers and businesses are confident market participants. In essence the Commission wants industry to lead asset management, which the Commission can facilitate with its range of tools, including price-quality regulation, information disclosure and leadership.
- 1.1.5 To achieve this vision, the Commission has a focus to promote competition and influence monopolies - allowing a reasonable return on investment while improving transparency and accountability for performance. This focus complements the Authority's role in generation and retail markets to promote competition in, reliable supply by, and the efficient operation of, the electricity industry for the long-term benefit of consumers.
- 1.1.6 The Commission's stated approach is:
- “Sound asset management is an integral part of ensuring that distributors improve efficiency and provide services at a price and quality that reflects the demands of electricity consumers. However, assessing whether distributors' asset management decisions result in over- or under-investment is a challenge, given the typically long lifetimes of network assets. In addition, there can be a significant lag between assets deteriorating and quality reducing, and it can be difficult to set leading performance indicators that appropriately reflect the risk of poorer quality in the future.”
- “As electricity distributors' asset management practices continue to mature, we would expect them to be increasingly focusing on, among other things:
- the health and criticality of their assets;

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<sup>1</sup> [Commerce Act 1986 No 5 \(as at 12 April 2022\), Public Act Contents – New Zealand Legislation](#)

- investment 'sufficiency'—the extent to which they are re-investing in assets at a prudent level; and
- appropriate levels of network resilience—the ability to maintain and restore electricity supply to consumers, particularly following high-impact, low-probability (HILP) events, such as earthquakes.”

1.1.7 The Commission will note, at an aggregated level, areas of current and future concern, including learnings from areas of previous concern that have been addressed.

1.1.8 The Commission notes they are very limited in their ability to discuss any open investigations of distributors not meeting their reliability targets.

1.1.9 Appendix A is the Commission's presentation.

## Questions for the SRC to consider

The SRC is asked to consider the following general questions.

- |     |  |
|-----|--|
| Q1. | What further information, if any, does the SRC wish to have provided to it by the secretariat? |
| Q2. | What feedback does the SRC have for the Commerce Commission?                                   |
| Q3. | What advice, if any, does the SRC wish to provide to the Authority?                            |

## **Appendix A: The Commerce Commission's role in Distributor Asset Management and Risk**

# Commerce Commission's ongoing focus on EDBs' asset management

Jo Perry, Tim Hewitt and John Rampton

## Briefing for Security and Reliability Council

1 June 2022



# Recap – we previously presented to the SRC on our focus on the asset management of electricity networks

- In June 2018 and again in 2019, Commission staff presented to the SRC on the Commission's focus on electricity networks' asset management practices
- The focus of this presentation is **what the Commission has done since mid 2018** on EDBs' asset management practices

# Our tools for improving asset management

- **Price-quality regulation, information disclosure regime** (including our analysis and publications), and our **influencing role** work together to incentivise better asset management practices
- **Price-quality regulation:** quality standards and an appropriate weighted average cost of capital (including uplift) provide a counter-balance to cost-minimisation incentives
- **Information disclosure:** disclosure and our analysis of the information reveals good and poor practices, particularly through asset management plans and core asset management data (eg, asset condition)
- **Influencing role in the sector:** working with lines businesses and their association to promote the long-term benefits of consumers, beyond our typical regulatory tools



# Commission's ongoing focus on EDBs' asset management practices



- As we signalled in our 2017 open letter, and in a subsequent open letter to EDBs in 2019, a key part of the Commission's focus on asset management effectiveness was (and still is) improving the transparency of EDBs' asset management practices – “shining a light”
- In this vein we have undertaken and published a number of performance and analysis reviews of EDBs' asset management since mid 2018 (see next slide)



# Commission's recent reviews of EDBs' asset management

- The Commission's recent reviews related to EDBs' asset management:
  - July 2018 – *Observations from Our Review of Electricity Distribution Businesses 2016 and 2017 Asset Management Plans*
  - May 2019 – Commissioned Partna Group to undertake *A Review of EDBs Risk Preparedness*
  - July 2021 – *Review of reporting of EDBs' Asset Management Practices*
  - November 2021 – *Review of Electricity Distribution Businesses' 2021 Asset Management Plans in Relation to Decarbonisation*
  - Currently undertaking a *Targeted Review of EDB Information Disclosure (ID)* in 4 key areas (one of which is asset management)
- These reviews (with the exception of the last one) have involved the Commission analysing ID data that has been disclosed by EDBs under Part 4 of the Commerce Act. This includes EDB asset management plans (AMPs)

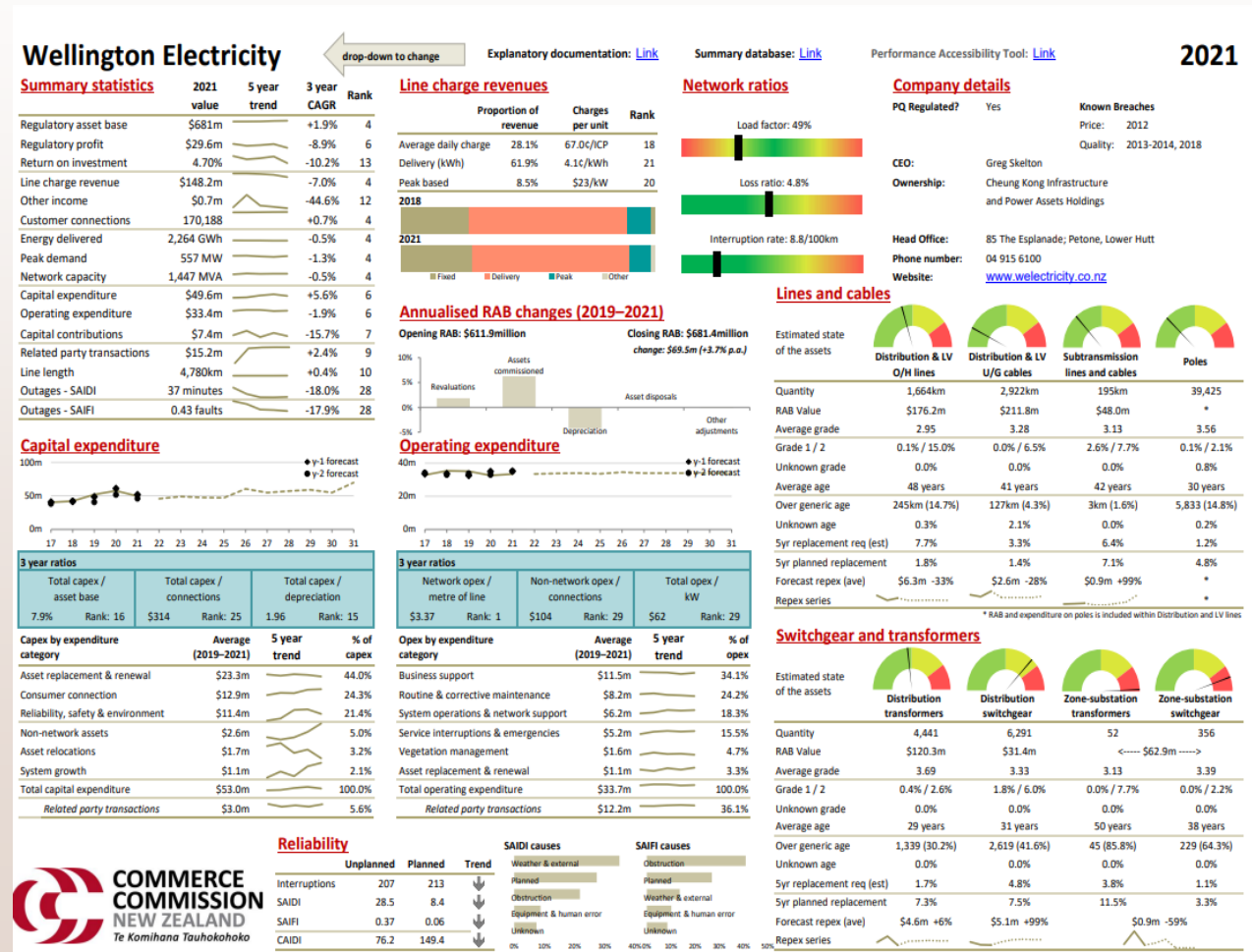
# Commission's influence and strategic leadership

- In 2017/2018 Commission staff visited all the EDBs with the primary focus on asset management
- Allowed us to appreciate the specific circumstances of different EDBs and their different asset management strategies responding to those circumstances
- We saw differing capability amongst individual EDBs relating to asset management
- While we haven't published a report on these visits, they have informed the reviews we have done such as our review of EDB's asset management plans
- We continue to visit EDBs and discuss asset management issues. To prepare for these visits we undertake a significant amount of internal Commission review of the EDB's asset management practices
- A number of EDBs have used our one-page performance dashboards as a starting point for some of the discussions in our engagements

# Supplier 'One Pagers'

- At a glance metrics and measures across a range of performance outcomes
- Try to provide a broad picture for each supplier
- Updated annually

<https://comcom.govt.nz/regulated-industries/electricity-lines/electricity-distributor-performance-and-data/performance-summaries-for-electricity-distributors>



# Performance accessibility tool

**Capital Expenditure (Capex)**

(Ctrl) click capex item(s) to filter graphs  
(Ctrl) click EDB(s) to filter table and time-series  
Use filter to view by year(s) or apply different inflator

Choose year: (All) | Choose index: constant | Choose view: Bar chart | Choose EDB grouping: Commission example | Choose ratio: Depreciation

Category	Selection	Spend	% of spend
Network assets	Asset relocations	\$247.39m	4.9%
	Asset replacement and renewal	\$1,826.74m	36.0%
	Consumer connection	\$1,058.72m	20.9%
	Reliability, safety and environment	\$406.78m	8.0%
	System growth	\$1,118.56m	22.1%
	Non-network assets	Non-network assets	\$410.03m
Total capital expenditure		\$5,068.22m	100.0%

**EDB**

EDB	Ratio
EA Networks	-0.75
Eastland Network	-0.85
Horizon Energy	-0.95
Marlborough Lines	-0.55
Network Waitaki	-0.45
Northpower	-0.95
Waipa Networks	-0.35
Orion NZ	-0.65
Vector Lines	-0.85
WEL Networks	-0.75
Wellington Electricity	-0.85
Aurora Energy	-1.15
Powerco	-0.85
Unison Networks	-0.65
Alpine Energy	-0.55
Counties Power	-0.65
Electra	-1.15
MainPower NZ	-0.45
Network Tasman	-0.55
OtagoNet	-0.85
The Lines Company	-0.85
The Power Company	-0.85
Top Energy	-0.85
Westpower	-0.35
Buller Electricity	-0.75
Centralines	-0.45
Scanpower	-0.85
Electricity Invercargill	-0.95
Nelson Electricity	-0.55

**Time Series**

Legend: ☒ Actuals, ☒ 2018 Forecast, ☐ 2017 Forecast, ☒ 2016 Forecast, ☐ 2015 Forecast, ☐ 2014 Forecast, ☒ 2013 Forecast

# Commission's influence and strategic leadership

- We engage with the Electricity Engineers' Association, especially their asset management subgroup. Initiatives include:
  - Engaging on an asset criticality framework with the intention that the advantages will be:
    - Providing estimates of asset outage impact
    - Informing investment decisions, timing, and prioritisation
    - Supports consultation and consideration of investment and reliability options
  - Presenting to them on the Commission's *Review of Electricity Distribution Businesses' 2021 Asset Management Plans in Relation to Decarbonisation*

# We have used our compliance powers

- In response to EDB breaches of quality standards we have undertaken many investigations and variously issued warning letters and sought fines for EDBs in some cases. Many of these breaches were caused by unsatisfactory EDB asset management practices, ranging from failure to plan and invest sufficiently in new and replacement assets to failure to effectively undertake vegetation management. Must notably:
  - 2020 - Aurora fined ca \$5 million for failing to meet quality standards. Underlying reason poor asset management practices especially underinvestment in new and replacement assets and poor asset management internal capability
  - 2019 – Vector fined ca \$3.6 million for failing to meet quality standards. Main reasons for breach was poor vegetation management and poor management of the life cycle of certain aging assets
  - 2019 Alpine Energy – Warning letter for failing to meet quality standards. Main reason for breach was failed to invest sufficiently in replacing or repairing overhead lines that it had identified as being old and below specification
  - 2021- Horizon Energy - Warning letter for failing to meet quality standards. Whilst investigation revealed that overall Horizon’s asset management practices were sound we found two specific instances where Horizon had failed to invest sufficiently to ensure sufficient reliability to groups of customers on its network

# Aurora Energy CPP

- 2018 – Commission encouraged Aurora to commission an independent investigation into the state of their network – WSP report. The WSP report found a number of problems with the network especially protection, poor asset conditions – eg rotten power poles etc. Problems caused by underinvestment and poor asset management practices over many years
- 2018/19 - Commission encouraged Aurora to apply for a customised price path (CPP) which provided for an uplift in expenditure to invest in new and replacement assets and improve internal asset management capability
- After detailed scrutiny by the Commission, the Commission approved in 2021 that Aurora could spend up to \$563 million over the next 5 years to improve its network. As part of this approval for investment we included a number of new specific ID requirements for Aurora to report on, over the course of CPP expenditure, so that “interested parties” had confidence that Aurora was making the required progress

# We are seeing improvements

- We continue, unsurprisingly to see differing capability amongst individual EDBs relating to asset management
- Generally the Commission staff see that EDBs as a group are improving their asset management capability and practices:
  - Improved reporting in asset management plans
  - More sharing of asset management practices across EDBs
  - *Review of Electricity Distribution Businesses' 2021 Asset Management Plans in Relation to Decarbonisation* revealed all EDBs variously planning for effect of decarbonisation
- Hard to know if these improvements are due to Commission focus or other factors – eg lessons learnt/highlighted from Aurora ("wake up call"), new technologies (ADMS) or combination of factors.
- Still plenty of scope for ongoing improvements to EDBs' asset management:
  - more opportunities for collaboration amongst EDBs
  - greater opportunities for EDBs to utilise risk based asset management
  - further improvements to EDBs' reporting - especially being clearer on key asset management practices they are undertaking and the effect that these are expected to have



# Final messages

- The asset management practices of EDBs is still a focus for the Commission. Especially as the economy transitions to greater electrification with accompanying increased demands on EDB networks
- Two of our current reviews:
  - The Targeted EDB ID review; and
  - the Input Methodologies reviewprovide us with the opportunity to modify the rules and change the incentives to achieve ongoing improvements in EDBs' asset management practices.
- We recently restructured our Economic Regulation Branch and created two new branches one of which is the Infrastructure Branch. A priority for the Infrastructure Branch is to focus on the performance and understanding of the sectors we regulate, especially EDBs. Intention is to undertake more regular reviews, reporting of EDBs performance etc

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