

OTAGONET JOINT VENTURE

THRESHOLD COMPLIANCE STATEMENT

FOR THE ASSESSMENT DATE, 31 MARCH 2010

*Pursuant to the Commerce Act (Electricity Distribution Thresholds) Notice
2004
and Amendment Notice 2006*

21 MAY 2010

CONTENTS

- 1) Disclosure of Information Required (Clause 7(1)(a)(i) – The Price Path Threshold)
 - a) Notional revenue at each assessment date – (Clause 5(1)(a))
 - b) Notional revenue during each assessment period – (Clause 5(1)(b))
- 2) Disclosure of Information Required (Clause 7(1)(a)(ii) – The Quality Threshold)
 - a) Interruption duration – SAIDI (Clause 6(1)(a))
 - b) Interruption frequency – SAIFI (Clause 6(1)(b))
- 3) Disclosure of Information Required (Clause 7(1)(a)(iii) – Policies and Procedures for Recording SAIDI and SAIFI)
- 4) Auditors' Report on Threshold Compliance Statement (Clause 7(1)(b))
- 5) Certification of Threshold Compliance Statement (Clause 7(1)(c))

APPENDIX A	Notional revenue at the 31 March 2010 assessment date
APPENDIX B	Allowable notional revenue under the CPI-X price path at the 31 March 2010 assessment date
APPENDIX C	Maximum notional revenue during the assessment period
APPENDIX D	SAIDI and SAIFI statistics (Explanation of Breach of Quality Threshold (SAIDI/SAIFI))

**1. DISCLOSURE OF INFORMATION REQUIRED
(CLAUSE 7(1)(a)(i) - THE PRICE PATH THRESHOLD)**

OtagoNet Joint Venture (OJV) does not comply with all requirements of the price path threshold at the 31 March 2010 assessment date as specified in the Commerce Act (Electricity Distribution Thresholds) Notice 2004 and Amendment Notice 2006 (The Notice).

Clause 5 (1) (a) notional revenue at each assessment date. The Notional Revenue of a distribution business at each assessment date (calculated in accordance with the numerator of the left-hand side of the following expression) is not to exceed the Allowable Notional Revenue of the distribution business under the CPI-X price path at that assessment date (calculated in accordance with the denominator of the left-hand side of the following expression):

Test:	$\frac{NR_{2010}}{R_{2010}}$	≤ 1
Result:	\$21,155,682 / \$10,499,239	> 1
Result:	2.015	> 1
Result:	Threshold is breached by \$10,656,443	

The OtagoNet Joint Venture increased its line charges during the assessment period ended 31 March 2010. The increases were made subsequent to a three year price freeze ending on 1 July 2005 and the clearance by the Commerce Commission of the price path breach for the assessment period ended 31 March 2009.

The high level reasons for OtagoNet increasing its prices that resulted in the continued price path breach for the assessment period ended 31 March 2010 are:

- OtagoNet's network assets are amongst some of the oldest in the country and as identified in the asset management plan there is a need to reinvest in the network assets in the long term interest of the stakeholders.
- The past levels of return on investment and prices were unsustainably low and given the planned level of reinvestment in the network could result in the revenue streams being insufficient to sustain the value of the network.
- OtagoNet is entering into a new regulatory period and regime with network reinvestment plans that significantly exceed the level of depreciation on the network. Price increases during that regulatory period are capped at CPI and subject to a potentially lengthy and relatively expensive customised price path process. At present that process poses significant uncertainty and cost. With a price path capped at CPI and capital expenditure planned at a level that will increase the regulatory asset base at a rate in excess of CPI OtagoNet is forecasting that its return on investment will reduce over the regulatory period.

Supporting evidence is presented in Appendices A and B.

Clause 5 (1) (b) notional revenue during each assessment period. The notional revenue of a distribution business at any time during an assessment period is not to exceed the greater of the Allowable Notional Revenue of the distribution business at the assessment date on which that assessment period ends and the Allowable Notional Revenue of the distribution business at the previous assessment date under this clause (or, if the previous assessment date is the reference date, under clause 5 of the initial Notice).

Test:	$\frac{NR_{Max}}{Max(R_{2009}, R_{2010})}$	≤ 1
Result:	\$21,155,682 / \$10,499,239	> 1
Result:	2.015	> 1
Result:	Threshold is breached by	\$10,656,443

Supporting evidence is presented in Appendix C.

NOTIONAL REVENUE

The following information used in determining the calculation of notional revenue of OJV in accordance with The Notice is disclosed.

1. GOODS AND SERVICES:

Goods and services included in the calculation of notional revenue of OJV include charges to electricity retailers or customers for the conveyance of electricity services.

2. EXCLUDED SERVICES:

The following are excluded services for the calculation of notional revenue:

- (a) Connection, disconnection, or reconnection services: OJV obtains no revenue from these services as other parties perform them.
- (b) "Non conveyance" goods and services: OJV obtains no revenue from the provision of energy use monitoring, consultancy or the provision of information not directly related to the provision of electricity distribution as it does not carry out such services.
- (c) Asset additions that are uneconomic to supply: OJV is required to make additions to the network for newly connected customers. The cost of any uneconomic portion of the network addition is borne by the consumer. In all cases the costs of constructing the network addition for the new connection are incurred using independent contractors in a competitive market.
- (d) Other miscellaneous revenue: miscellaneous revenue such as rent, interest and gain on sale of assets are excluded, as they are non-conveyancing revenue.

3. PASS THROUGH COSTS

The following costs have been included in the calculation of notional revenue:

(a) TRANSMISSION CHARGES:

These include embedded generator avoided transmission charges, Transpower Connection, Interconnection charges less Loss Constraint Excess Payments.

(b) RATES:

Territorial Local Authority rates applying to system fixed assets including lines, cables, equipment and substation land and buildings.

(c) ELECTRICITY COMMISSION LEVIES.

**2. DISCLOSURE OF INFORMATION REQUIRED
(CLAUSE 7(1)(a)(ii) – THE QUALITY THRESHOLD)**

OJV does not comply with all requirements of the quality threshold at the 31 March 2010 assessment date, as specified in The Notice.

a. INTERRUPTION DURATION – SAIDI CLAUSE 6 (1) (a)

<p>TEST: $SAIDI_{2010} \leq \left(\frac{SAIDI_{1999} + SAIDI_{2000} + SAIDI_{2001} + SAIDI_{2002} + SAIDI_{2003}}{5} \right)$</p> <p>332.72 minutes > 249.30 minutes</p> <p>RESULT: Class B and Class C SAIDI for the twelve months ending on the Assessment Date, 31 March 2010 is greater than the five year average Class B and Class C SAIDI (1999 – 2003) by 83.42 minutes.</p> <p>The Threshold is breached.</p>

Supporting evidence is presented in Appendix D.

b. INTERRUPTION FREQUENCY – SAIFI - CLAUSE 6 (1) (b)

<p>TEST: $SAIFI_{2010} \leq \left(\frac{SAIFI_{1999} + SAIFI_{2000} + SAIFI_{2001} + SAIFI_{2002} + SAIFI_{2003}}{5} \right)$</p> <p>3.26 times > 2.38 times</p> <p>RESULT: Class B and Class C SAIFI for the twelve months ending on the Assessment Date, 31 March 2010 is greater than the five year average Class B and Class C SAIFI (1999 – 2003) by 0.88 times.</p> <p>The Threshold is breached.</p>
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Supporting evidence is presented in Appendix D.

3. DISCLOSURE OF INFORMATION REQUIRED (CLAUSE 7(1)(a)(iii) - POLICIES AND PROCEDURES FOR RECORDING SAIDI AND SAIFI)

OJV contracts PowerNet to manage its network via an Outsourcing Agreement.

PowerNet has a number of ISO 9002 procedures that govern the operational processes that surround the interruption, restoration and quality of supply to its customers. These procedures document the process by which managing, recording and reporting of outages is performed by PowerNet. This is carried out by following a series of flow charts, documents, forms and instructions contained within the following procedures:

- PNM 65 – Planned Outages
- PNM 69 – Network Faults, Defects and Supply Complaints
- PNM 71 – Use of Operating Orders

Key items within these procedures that relate to the recording and reporting of SAIDI and SAIFI statistics include:

- Responsibilities for recording faults and outages at the system control operator level through to reviewing and reporting of faults and outages daily by management, weekly at operations meetings and monthly at board meetings.
- Methods by which notification of planned and unplanned outages are identified and captured from various sources such as customers, network equipment, contractors, Transpower, the public or emergency services.
- The use of Operating Orders for planned maintenance and unplanned fault restoration and how the information from these orders flow through to the Outage Reporting System in the form of duration of outages and number of customers affected.
- The recording of all faults and outages, however for the reporting of SAIDI and SAIFI only the inclusion of outages of a duration exceeding one minute or affecting more than three customers is recorded.
- The method of calculating SAIDI and SAIFI for outages which are progressively restored.
- The preparation, retention and archiving of supporting records and data.

Disclaimer

The information presented in this Threshold Compliance Statement has been prepared solely for the purpose of complying with the requirements of the Commerce Act (Electricity Distribution Thresholds) Notice 2004 and Amendment Notice 2006. This statement has not been prepared for any other purpose and OtagoNet Joint Venture expressly disclaims any liability to any other party who may rely on this statement for any other purpose.

AUDITORS' REPORT ON THRESHOLD COMPLIANCE STATEMENT

To the readers of the threshold compliance statement of OtagoNet Joint Venture Limited for the assessment period ended on 31 March 2010

We have examined the attached statement, which is a threshold compliance statement in respect of the price path threshold and the quality threshold prepared by OtagoNet Joint Venture Limited for assessment as at 31 March 2010 and dated 21 May 2010 for the purposes of information requirements set out in clause 7 of the Commerce Act (Electricity Lines Thresholds) Notice 2004 ("the Notice"). In this report the attached statement is called "the threshold compliance statement".

Directors' Responsibilities

Directors of OtagoNet Joint Venture Limited are responsible for the certification, confirming the compliance or otherwise, of the threshold compliance statement in accordance with the Notice.

Auditors' Responsibilities

It is our responsibility to express an independent opinion (in the form prescribed in the Notice) on the threshold compliance statement and report our opinion to you.

We conducted our audit in accordance with the Auditing Standards issued by the Institute of Chartered Accountants of New Zealand.

Basis of Opinion - Price Path Threshold and Quality Threshold: SAIDI and SAIFI Statistics for the Assessment Period ended 31 March 2010

Our audit included examination, on a test basis, of evidence relevant to the amounts and disclosures contained on pages 2 to 6 and Appendices A to D of the threshold compliance statement and which relate to:

- the price path threshold set out in clause 5 of the Notice; and
- the SAIDI and SAIFI statistics for the assessment period ended on 31 March 2010 which are relevant to those parts of the quality threshold that are set out in clauses 6(1)(a) and 6(1)(b) of the Notice.

It also included an assessment of the significant estimates and judgements, if any, made by OtagoNet Joint Venture Limited in the preparation of the threshold compliance statement and an assessment of whether the basis of preparation has been adequately disclosed.

We planned and performed our audit of the threshold compliance statement so as to obtain all the information and explanation which we considered necessary, including for the purpose of obtaining sufficient evidence to give reasonable assurance that the threshold compliance statement is free from material misstatements (whether caused by fraud or error), except that our work was limited in respect of the quality threshold: SAIDI and SAIFI statistics as explained below. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the threshold compliance statement.

AUDITORS' REPORT ON THRESHOLD COMPLIANCE STATEMENT

OtagoNet Joint Venture Limited

Basis of Opinion - Quality Threshold: SAIDI and SAIFI Statistics for the Years Ended 31 March 1999, 2000, 2001, 2002 and 2003.

In relation to the SAIDI and SAIFI statistics for the years ended 31 March 1999, 2000, 2001, 2002 and 2003 which are relevant to those parts of the quality threshold that are set out in clauses 6(1)(a) and 6(1)(b) of the Notice. We have undertaken procedures to provide reasonable assurance that:

- the amounts and disclosures in the threshold compliance statement relating to those statistics have been correctly taken from the information disclosed by OtagoNet Joint Venture Limited in accordance with the Electricity (Information Disclosure) Regulations 1999; and
- those statistics have been calculated based on the source data provided to us. We have not performed audit procedures on the source data.

Relationship and Interests

We have no relationship with or interests in OtagoNet Joint Venture Limited other than in our capacities as auditors of the threshold compliance statements, auditors pursuant to the Electricity Distribution (Information Disclosure) Requirements 2008 and under the Companies Act 1993, and in the provision of other professional advisory services. We are not aware of any relationships between our firm and OtagoNet Joint Venture Limited that, in our professional judgment, may reasonably be thought to impair our independence.

Opinions

Unqualified Opinion

We have obtained all the information and explanations we have required.

Price Path Threshold

In our opinion, having made all reasonable enquiry, to the best of our knowledge the amounts or details set out in the threshold compliance statement relating to the price path threshold set out in clause 5 of the Notice and related information have been prepared in accordance with the Notice, and give a true and fair view of the performance of OtagoNet Joint Venture Limited against that threshold for the assessment period ended on 31 March 2010.

Quality Threshold: SAIDI and SAIFI statistics

In our opinion, having made all reasonable enquiry, to the best of our knowledge:

- a) the SAIDI and SAIFI statistics for the assessment period ended on 31 March 2010 which are relevant to those parts of the quality threshold that are set out in clauses 6(1)(a) and 6(1)(b) of the Notice and related information have been calculated or prepared in accordance with OtagoNet Joint Venture Limited's policies and procedures for recording SAIDI and SAIFI statistics as disclosed in the threshold compliance statement, and fairly represent the performance of OtagoNet Joint Venture Limited for the assessment period ended on 31 March 2010;
- b) the SAIDI and SAIFI statistics for the years ended 31 March 1999, 2000, 2001, 2002 and 2003, which are relevant to those parts of the quality threshold that are set out in clauses 6(1)(a) and 6(1)(b) of the Notice, have been correctly taken from the information disclosed by OtagoNet Joint Venture Limited in accordance with the Electricity (Information Disclosure) Regulations 1999. Those statistics have been properly calculated based on the unaudited source data provided to us by OtagoNet Joint Venture Limited.

AUDITORS' REPORT ON THRESHOLD COMPLIANCE STATEMENT

OtagoNet Joint Venture Limited

Qualified Opinion

Our opinion is qualified as follows:

Quality Threshold: SAIDI and SAIFI statistics

The scope of our audit was subject to the following limitations:

- There is no independent evidence available for the period to support the completeness and accuracy of recorded faults; and
- Control over the completeness and accuracy of ICP data included in the SAIDI and SAIFI calculations is limited throughout the period.

Because of these limitations, there are no practical audit procedures that we could adopt to confirm independently that all outage and ICP data was properly recorded for the purposes of inclusion in the amounts or details set out in the quality threshold: SAIDI and SAIFI statistics.

In these respects alone we have not obtained all the information and explanations that we have required.

Because of the potential effect of the limitations in the evidence available to us, we are unable to form an opinion as to whether the amounts or details set out in the quality threshold: SAIDI and SAIFI statistics for the assessment period ended on 31 March 2010, together with the SAIDI and SAIFI statistics for the years ended 31 March 1999, 2000, 2001, 2002 and 2003, give a true and fair view of the performance of OtagoNet Joint Venture Limited against those parts of the quality threshold that are set out in clauses 6(1)(a) and 6(1)(b) of the Notice for the assessment period ended on 31 March 2010.

Our audit was completed on 21 May 2010 and our qualified and unqualified opinions are expressed as at that date.



PricewaterhouseCoopers
Christchurch
21 May 2010

5. CERTIFICATION OF THRESHOLD COMPLIANCE STATEMENT

We, Neil Douglas Boniface and Ross Lindsay Smith, being Directors of companies which are parties to the OtagoNet Joint Venture certify that, having made all reasonable enquiry, to the best of our knowledge and belief, the attached threshold compliance statement of OtagoNet Joint Venture and related information, prepared for the purposes of the Commerce Act (Electricity Distribution Thresholds) Notice 2004 and Amendment Notice 2006 complies with the requirements of that notice, except for Clauses 5(1)(a), 5(1)(b), 6(1)(a) and 6(1)(b).



Neil Douglas Boniface



Ross Lindsay Smith

21 May 2010