

28 August 2017

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By email: regulation.branch@comcom.govt.nz

Dear Matthew,

Default price-quality paths for gas pipeline businesses for the 2017-2022 period

1. This letter is our response to the Commerce Commission's (Commission) request for feedback on the process for setting the gas pipeline business (GPB) default price path (DPP) for 1 October 2017 to 30 September 2017.

Process

2. Vector sees mutual benefit with ensuring DPP consultation processes are constructive, collaborative and less adversarial. This approach has also recently been championed by Chair of the Australian Energy Regulator who noted:

The opportunity is clear: we all need to engage earlier with each other in a more proactive fashion. We need to identify issues in dispute and work together to resolve them.¹

3. We are encouraged by the Commission taking the opportunity to initiate its engagement with the sector early and to discover as much information through the consultation process as it needs to make a considered decision.
4. However, we also note there are times when the sector and the macro environment can change rapidly. In such instances, we encourage the Commission to have regard to the impact of such changes on DPP decisions, where relevant, and not to rigidly adhere to a process where relevant information may become out of date.

¹ Paula Conboy, Energy Networks Australia Regulation Seminar 2017 Speech *Working together to restore confidence in energy regulation*, 26 July 2017

Workshops

5. We welcome the Commission's endeavour to improve engagement in the DPP consultation process by facilitating workshops on matters. However, we note these workshops appear to have limited utility given how early in the consultation process they were organised.
6. We recommend in the future the Commission consider timing workshops after it has consulted on the topic. An example of where this was successful was in the Commission's Input Methodology review weighted average cost of capital (WACC) workshop. The discussion in the WACC workshop was informative to issues parties had put on the record in the Commission's consultation process. Therefore, the workshop fulfilled the role of elucidating and testing information received during written consultation as opposed to fact finding.

Expenditure forecasting

7. Vector welcomed the willingness of the Commission to consider innovations in its approach for expenditure forecasting. We found the Commission's willingness to provide greater reliance on supplier asset management plan (AMP) forecasts as a positive development for ensuring the regulated service can meet customer needs for the DPP period.

Operating expenditures

8. The Commission's approach of assessing supplier AMP expenditures worked well for determining appropriate operating expenditures. The use of supplier AMP forecasts supplemented by expenditures against regulatory information disclosure filings provides an analytically valid basis determining reasonable operating expenditure forecast.
9. The opportunity for the supplier to provide an explanation for expenditure forecasts that are different to historical information disclosures (described as supplier scrutiny) ensures the Commission is not arbitrarily denying expenditure merely because it was not incurred in previous years.
10. This additional lever, if effectively executed, gives the supplier an opportunity to demonstrate why such changes are needed. The Commission is then able to appreciate whether the change in expenditure reflects innovations or changes (including changes in the operating environment) in providing the service.

11. Examples of changes to the service delivery model include cloud computing where IT software expenditure would have been capitalised now becomes part of the operating expenditures for the supplier. This change to the service delivery model will not be adequately represented in historical regulatory filings.
12. We discuss later in this letter our experience with the supplier scrutiny process and the expectations of the type of information to support the expenditures from the Commission.

Commissioned assets expenditure

13. The Commission's approach for assessing commissioned assets expenditure does not reflect a significant innovation from the previous approach used in the initial electricity distribution and gas pipeline resets. This is despite expectations from the Commission that it could make improvements for the 2017 reset. We recognise commissioned assets expenditure has different underlying characteristics to operating expenditures and therefore is more complicated given its forward-looking nature.
14. Previously, the Commission capped AMP expenditures at 120 percent of historical expenditures. For this DPP the Commission appears to have relied on substantially the same methodology but has capped AMP forecasts at 110 percent of historical expenditures.
15. Given the Commission has now determined multiple DPPs for electricity distribution and GPBs, we consider it investigate the possibility of relying on supplier AMP forecasts without a cap based on historical performance. Where the Commission has clear evidence of systemic forecasting issues then it may continue to consider some general limitation on forecasts in addition to interrogating specific expenditures.

Supplier scrutiny

16. As was noted to the Commission during the consultation, the expectation that suppliers will retain board papers, executive documents for all expenditure changes does not align with business practice. We encourage the Commission to have less rigid expectations for considering supplier scrutiny. As discussed above, we see great merit in a continuous dialogue on matters the Commission considers warrant further scrutiny from AMP forecasts.

17. Our experience of supplier scrutiny in this DPP of being provided a list of questions for further scrutiny without context does little to bridge the divide of expectations and reasoning. We recommend the Commission consider a more collaborative process where there is less risk of misinterpretation. A more constructive dialogue and greater engagement with suppliers and interested parties will ensure such issues can be resolved in a manner less reflecting inquisition.
18. If you have any further questions in relation to this submission, please contact me at Richard.Sharp@vector.co.nz or on 021 790 864.

Regards

For and behalf of Vector Limited

A handwritten signature in blue ink, appearing to read "Richard Sharp".

Richard Sharp
Head of Regulatory and Pricing