Auckland Energy Consumer Trust

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31 May 2010

Matthew Lewer
Regulation Branch
Commerce Commission
PO Box 2351
WELLINGTON

Dear Matthew,

Re: Cross-submission on the Commerce Commission's Issues Paper on the Initial Default Price-Quality Path for Gas Pipeline Businesses

On 12 April 2010, the Commerce Commission (the Commission) released an issues paper setting out its preliminary views on how the initial default price-quality path (DPP) for gas pipeline businesses (GPBs) should be determined (the Issues Paper). The Commission invited submissions from interested parties on the form of control by 30 April 2010 and on all other sections of the Issues Paper by 14 May 2010.

The Commission is now inviting cross-submissions by 31 May 2010 on matters raised in these submissions, to ensure that it is aware of points of agreement and disagreement between submitters.

The Auckland Energy Consumer Trust (AECT), as a majority shareholder in Vector, which owns electricity and gas distribution assets and gas transmission assets, will be affected by the initial DPP and welcomes the opportunity to participate in this consultation process. AECT makes this cross-submission to help the Commission understand the concerns that arise from the Commission's proposals, from the perspective of an owner and unique perspective as a trust.

To inform AECT's cross-submission, AECT asked NZIER to review the submissions made by other submitters and to identify points of agreement and disagreement with AECT's submission. Please find NZIER's report attached to this cross-submission. For further details of AECT's concerns and recommendations, we refer you to our previous submissions of 30 April and 14 May 2010.

In conclusion, this comparison of submissions indicates general agreement on:

- Section 2: Nature of gas pipeline services, subject to recognition that this differentiation between gas distribution services and gas transmission services does not necessarily extend to a need for different forms of control.
- Section 8: Data requirements, subject to these being relevant and least cost.

The main points of disagreement between submitters are:

- Section 3: Structure of the initial DPP:
  - AECT considers an integrated price-quality path feasible and in the interests of consumers, GPBs and investors, given the fundamental link between price and quality.
  - AECT recommends that the Commission investigate including an S-factor quality incentive in the DPP.
  - AECT accepts the setting of separate standards to the extent that it is not practical, feasible or consistent with the low-cost regulatory option to integrate price and quality in the initial DPP.
- Section 4: Form of price control:
  - AECT supports application of a weighted average price cap for gas distribution businesses (GDBs).
  - AECT considers that the appropriate form of control will differ between the two gas transmission businesses (GTBs) due to their very different systems.
  - AECT recommends application of a total revenue cap for gas transmission services where the cost structure is largely fixed and the revenue driver is variable (as typically occurs with common carriage, as on MDL's system) and a weighted average price cap for gas transmission services where the cost structure (including investment in connections and capacity) is variable and the revenue driver is manageable (as typically occurs with contract carriage, as on Vector Transmission's system).
  - If it is not possible for the two GTBs to have different forms of control, AECT favours a weighted average price path for both, for greater compliance with the regulatory objectives.
- Section 5: Pricing arrangements prior to initial DPP:
  - AECT does not consider claw-back to be needed or in the interests of achieving competitive market outcomes.
  - AECT considers the proposed assessment methodology to undermine regulatory and investor certainty, given that the Commission is still determining how asset valuation and cost of capital will be applied in determining whether or not revenue has been over-recovered.
  - AECT recommends that claw-back not apply in the case of technical breaches or where price increases can be justified in terms of incremental investment or providing an adequate return.
- Section 6: Productivity analysis:
  - AECT supports use of New Zealand gas sector data, in the first instance.
  - AECT suggests that the Commission seek to corroborate and/or adjust New Zealand gas sector productivity trends with reference to productivity trends for New Zealand electricity distribution businesses.
  - AECT recommends that the Commission use the B-factor approach to estimating total factor productivity (TFP) in both cases.
  - AECT supports a non-mechanistic, pragmatic approach to using the results of TFP analysis in determining the X-factor, due to data limitations and methodological difficulties.

- Section 7: Quality standards:
  - AECT accepts the setting of separate quality standards to the extent that it is not practical, feasible or consistent with the low-cost regulatory option to integrate price and quality in the initial DPP.
  - AECT recommends that these quality standards be limited to indicators of reliability, more suited to gas than are SAIDI and SAIFI, and allow for variation to avoid causing technical breaches.
- Section 9: Annual assessment and regulatory periods:
  - AECT recommends an assessment period of 1 October to 30 September, to align with the pricing year for GDBs and Vector's GTB.

AECT requests that the Commission take into account our concerns and recommendations on the setting of the initial DPP. If our concerns are not adequately addressed, we believe there is a danger that the new regulatory regime will not be effective in ensuring that the intent of the Commerce Amendment Act 2008 and purpose statement of Part 4 of the Commerce Act 1986 are served.

Yours sincerely,

Ian R Ward
Executive Officer