

SETTLEMENT AGREEMENT

Agreement dated 7 July 2017

PARTIES

Commerce Commission, a Crown Entity established under section 8 of the Commerce Act 1986 (**Commission**)

Vector Limited, a company incorporated under the Companies Act 1993 and having its registered office at Level 4, 101 Carlton Gore Road, Newmarket, Auckland, New Zealand (**Vector**)

RECITALS

- A. Part 4 of the Commerce Act 1986 (**Act**) provides that all suppliers of electricity distribution services are subject to default/customised price-quality regulation, unless they are exempt.
- B. Vector is not exempt from price-quality regulation and is currently subject to a default price-quality path that limits the amount of notional revenue that it can earn in each annual assessment period (**Price Path**).
- C. For the annual assessment periods ending 31 March 2014 (**2014 Assessment Period**) and 31 March 2015 (**2015 Assessment Period**), Vector's Price Path was set by the Electricity Distribution Services Default Price-Quality Path Determination 2012 (**DPP Determination 2012**).
- D. The Price Path set by the DPP Determination 2012 was reset in 2015 by the Electricity Distribution Services Default Price-Quality Path Determination 2015 (**DPP Determination 2015**). The DPP Determination 2015 set Vector's Price Path for the annual assessment periods between 1 April 2015 and 31 March 2020.
- E. Vector carried out a restructuring of its Prices for residential consumers on 1 April 2013 by introducing a new 'standard' fixed charge tariff which applied from the start of the 2014 Assessment Period. The new tariff consisted of a higher daily fixed charge and a lower variable charge based on the electricity consumption at the premises.
- F. Under this price restructure, the residential consumers supplied by Vector were subject to either the new standard fixed charge tariff or the low use fixed charge tariff, which Vector is required to offer under the *Electricity (Low Fixed Charge Tariff Option for Domestic Consumers) Regulations 2004*. Consumers who used less than 8,000kWh per annum would incur lower annual charges if placed on the low use fixed charge tariff. However, Vector was prevented from unilaterally switching consumers between tariffs. It therefore fell to electricity retailers to identify and actively request Vector to switch consumers for whom the low use fixed charge tariff would be more advantageous.

- G. When setting its prices for the 2014 Assessment Period, Vector acted on an assumption that virtually all residential consumers would be placed by retailers on the least cost tariff, based on their historic or expected consumption, from the start of the 2014 Assessment Period, i.e., the point at which the restructure was implemented. Vector also adopted this assumption for the purposes of reporting to the Commission on its compliance with the Price Path for the 2014 Assessment Period and the 2015 Assessment Period. Vector's assumption was that competition in the electricity retail market would ensure retailers selected the least-cost tariffs for their customers.
- H. A substantial number of residential consumers who qualified for the low use fixed charge tariff based on their electricity consumption were not, and in the Commission's view could not reasonably have been expected to have been, transferred immediately by retailers to that option and instead remained on the more expensive standard fixed charge tariff.
- I. The Commission's position is that Vector's assumption that virtually all residential consumers would be subject to the least cost tariff from the start of the 2014 Assessment Period, and that the related Quantities were appropriate for representing compliance with the Price Path for the 2014 Assessment Period, was unreasonable.
- J. Vector's position is that it did not intend to breach the DPP Determination 2012 and did not anticipate the extent to which competition in the retail market would fail to encourage retailers to transfer more residential consumers to an option which was most suitable to their consumption and lower cost to them.
- K. This disjunct between the way in which Vector's tariff restructure was implemented and residential consumers were billed, and Vector's assumption for Price Path compliance purposes, meant that Vector earned extra revenue, beyond that envisaged in the Price Path. Vector consequently breached the Price Path for the 2014 Assessment Period. The breach in the 2014 Assessment Period also resulted in a consequential breach in the 2015 Assessment Period.
- L. The Commission considers, and Vector hereby acknowledges, that Vector did not comply with its Price Path for the 2014 Assessment Period and for the 2015 Assessment Period, and that each such instance of non-compliance amounted to a contravention of a price-quality requirement applying to regulated goods or services as described in section 87(1)(a) of the Act (together, the **Breaches**).
- M. The purpose of this agreement is to resolve the Breaches without litigation. In consideration of the Commission agreeing not to bring proceedings in relation to the Breaches, Vector has agreed to reduce its Notional Revenue below the Allowable Notional Revenue in its Price Path by \$4,641,248 (**2019 Adjustment Value**) in the assessment period ending 31 March 2019 (**2019 Assessment Period**) and by \$9,282,495 (**2020 Adjustment Value**) in the assessment period ending 31 March 2020 (**2020 Assessment Period**) (or alternative relative values calculated in accordance with clauses 8 and 9 of this agreement) through changes to Prices charged for services supplied to consumers in Vector's Northern Region and Auckland Region (**Relevant Consumers**).

- N. The Commission has entered into this agreement to resolve the Breaches in part because:
- a. Vector has approached discussions with the Commission about remediation of the Breaches in a constructive manner, including accepting the Breaches;
 - b. Vector identified the treatment of its price restructure in its compliance statements for the 2014 Assessment Period and the 2015 Assessment Period; and
 - c. The agreement contributes to remediation of the effects of the Breaches without the need for costly and time-consuming litigation.

AGREEMENT

Interpretation

1. The terms “**Allowable Notional Revenue**”, “**Annual Compliance Statement**”, “**Notional Revenue**”, “**Prices**” and “**Quantities**” have the same meanings as in the DPP Determination 2015, and the term “working day” has the meaning given in section 29 of the *Interpretation Act* 1999.
2. Unless otherwise indicated, any reference to “**clause**” is to a clause of this agreement.

Acknowledgement by Vector

3. Vector acknowledges that it did not comply with its Price Path for the 2014 Assessment Period or its Price Path for the 2015 Assessment Period, and that each such instance of non-compliance amounted to a contravention of a price-quality requirement applying to regulated goods or services as described in section 87(1)(a) of the Act.
4. The Commission and Vector acknowledge that either of them may refer to the Breaches and this agreement (in particular, the Commission may rely on Vector’s acknowledgement in clause 3) in any enforcement action brought by the Commission against Vector for the Breaches, or in relation to any other contravention or alleged contraventions of the Act.

Disposition of Breaches

5. Upon execution of this agreement, save as is provided for in this agreement, the Commission will not take any further enforcement action (through court proceedings or otherwise) against Vector in relation to the Breaches. This agreement is sufficient to resolve the Breaches.

Remediation by Vector

6. Vector will set its Prices for services supplied to Relevant Consumers for the 2019 Assessment Period so that its Notional Revenue for the 2019 Assessment Period is less than or equal to its Allowable Notional Revenue for the 2019 Assessment Period minus the **2019 Adjustment Value** (\$4,641,248).
7. Vector will set its Prices for services supplied to Relevant Consumers for the 2020 Assessment Period so that its Notional Revenue for the 2020 Assessment Period is less than or equal to its Allowable Notional Revenue for the 2020 Assessment Period minus the **2020 Adjustment Value** (\$9,282,495).
8. Vector may elect to adopt an alternative higher **2019 Adjustment Value** for the 2019 Assessment Period (**2019 Alternative Value**).

9. If Vector elects to adopt a **2019 Alternative Value** for the 2019 Assessment Period, then for the purposes of clause 7, Vector will adopt a revised 2020 Adjustment Value (**2020 Alternative Value**) determined as follows:

$$2020 \text{ Alternative Value} = 2020 \text{ Adjustment Value} + [(2019 \text{ Adjustment Value} - 2019 \text{ Alternative Value}) \times (1.0643)]$$

10. By 5.00pm on 31 January 2018, Vector will provide a written submission to the Commission showing whether it has complied with clause 6 or clause 8 (as the case may be).
11. By 5.00pm on 11 January 2019, Vector will provide a written submission to the Commission showing whether it has complied with clause 7 or clause 9 (as the case may be).
12. The written submission referred to in clauses 10 and 11 will include any information reasonably necessary to enable the Commission to assess that Vector has complied with its obligations under this agreement with regard to the setting of prices for the 2019 Assessment Period or 2020 Assessment Period.
13. In its Annual Compliance Statement for the 2019 Assessment Period and the 2020 Assessment Period, Vector will:
- 13.1 state whether it complied with clause 6 or clause 8, or clause 7 or clause 9, (as the case may be); and
 - 13.2 provide any information reasonably necessary to assess whether Vector has complied with clause 6 or clause 8, or clause 7 or clause 9, (as the case may be), as well as the reasons for any non-compliance.
14. For the avoidance of doubt, the director's certification and assurance report referred to in clause 11 of the DPP Determination 2015 will also cover the material included in the Annual Compliance Statement by virtue of clause 13 of this agreement.
15. In setting Prices for services supplied to Relevant Consumers so as to comply with clause 6 or clause 8, or clause 7 or clause 9, (as the case may be) Vector will:
- 15.1 prioritise reductions in Prices for residential consumers; and
 - 15.2 only adjust Prices for industrial or commercial consumers if achieving the reduction in Notional Revenue required by clause 6 or clause 8 or clause 7 or clause 9 (as the case may be) would otherwise necessitate decreases in nominal Prices for residential consumers.

Termination

16. If Vector fails to comply with clause 6 or clause 8, or clause 7 or clause 9 (as the case may be), then subject to clause 17, the Commission may elect to give Vector written notice that this agreement is terminated with immediate effect.

17. Before giving notice of termination to Vector under clause 16, the Commission will:
 - 17.1 notify Vector in writing that it considers that clause 16 applies and that it is contemplating terminating the agreement; and
 - 17.2 allow Vector 10 working days to respond in writing to its view that clause 16 applies; and
 - 17.3 have regard to any written response that it receives from Vector prior to the deadline specified in sub-clause 17.2.
18. For the avoidance of doubt, if this agreement is terminated by the Commission under clause 16, then the Commission may initiate court proceedings against Vector in relation to the Breaches, and clause 5 of this Agreement ceases to apply from the date of the notice of termination.
19. Clause 3, clause 4, clause 18, clause 19, clause 20, clause 21 and clause 22 will survive termination of this agreement.
20. For the avoidance of doubt, termination of this agreement does not discharge Vector from obligations already accrued under this agreement.

Waiver of limitation

21. If the Commission commences proceedings in relation to the Breaches within three months of termination of this agreement, Vector agrees that it will not raise by way of defence to those or any related proceedings any issue arising from any applicable limitation period.

Publicity

22. The Commission and Vector may publicise or make media comment in relation to this agreement, the Breaches and the acknowledged contraventions of section 87(1)(a) of the Act, and may subsequently refer to them publicly whenever it considers this appropriate. This may include, without limitation, publication by media statements, articles, or speeches prepared or given by Commission members or staff.
23. If either party intends to issue a press release announcing the execution of this agreement, then that party will provide the other party with an indication of the key elements of any proposed press release at least 48 hours before release.
24. Vector will not take any action, including by making any public statement, to dispute or deny the Breaches or the remediation set out in clause 6 and clause 7.

Miscellaneous

25. For the avoidance of doubt, all obligations under this agreement are in addition to any obligations under any enactment, regulation, determination or similar.
26. This agreement is governed by, and construed in accordance with, the laws of New Zealand.

27. This agreement constitutes the entire agreement between the Commission and Vector in relation to the Breaches. It supersedes all prior communications, understandings or representations whether oral or written between the Commission and Vector.
28. No amendment to this agreement will be effective unless it is in writing and signed by both of the parties.
29. The failure of a party to enforce any provision of this agreement at any time will not operate as a waiver of that provision in respect of that act or omission or any other act or omission.
30. The parties may enter into this agreement by signing any number of counterparts, each of which will be treated as an original. All of the counterparts taken together will constitute a single document. A party may execute this agreement by one signatory executing one counterpart and another signatory executing a different counterpart. A party's delivery of a signed pdf counterpart of this agreement will have the same legal effect as that party's delivery of a signed original counterpart.

Notices / Communications

31. Any notice or communication pursuant to this agreement (other than the Annual Compliance Statement referred to in clause 13) will be delivered to the physical or electronic mail address listed below:

For the Commission:

Commerce Commission
Level 9, 44 The Terrace
Wellington 6011
New Zealand
Attention: Andrew Riseley, General Counsel, Regulation Branch
[REDACTED]

For Vector:

Vector Limited
101 Carlton Gore Road
Newmarket
Auckland 1023
New Zealand
Attention: General Counsel and Company Secretary
E-mail: [REDACTED]

32. Either party may designate a different recipient and/or address for notices and communications delivered in accordance with clause 31.

EXECUTION

Signed by and on behalf of **Commerce Commission**



Susan Janice Begg
Name

7 July 2017
Date

Signed by and on behalf of **Vector Limited**

Authorised signatory

Name

Date

EXECUTION

**Signed by and on behalf of Commerce
Commission**

Authorized signatory

Name

Date



Signed by and on behalf of Vector Limited

Authorized signatory

Simon McKenzie

Name

7/7/2017

Date