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John McLaren
Chief Advisor
Regulatory Branch
Commerce Commission
WELLINGTON

Dear Mr McLaren,

Feedback on the process for setting default price-quality paths

Introduction

1. Vector welcomes the opportunity to submit to the Commerce Commission in response to the letter seeking "Feedback on the process for setting default price-quality paths", dated 23 April 2013.
2. Vector supports the submission of the Electricity Networks Association.
3. No part of our submission is confidential and we are happy for it to be publicly released.
4. Vector's contact person for this submission is:

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Opening comments

5. The current consultation is a constructive and positive step that could improve aspects of the price reset process. However, it will have only minor impact on certainty of the regulatory process given the significant freedom the Commission has to change the process from reset to reset.
6. Although Vector and the Commission have divergent views on various material aspects of the electricity and gas default price-quality path (DPP) resets, Vector would like to acknowledge that we found the Commission staff helpful and constructive in dealing with the many queries we had in relation to the DPP resets. The Commission's proactive engagement with our consultant, Castalia, in relation to the use of econometrics for forecasting was also a constructive and pragmatic addition to the consultation process for the electricity DPPs.
7. Setting the DPPs under the new Part 4 was and is inevitably a complex task, which required a substantial amount of upfront design and work, e.g. development of Input Methodologies, in constrained timeframes. There will be lessons that can be learnt that should be useful for future DPPs and Commission processes more generally.
8. We recognise the Commission was operating under constrained timeframes, which should not be such an issue for the second round of DPP resets, but there were elements of the Commission's process which we felt created unnecessary pressure

on our business and staff; particularly around 53ZD notices and announcement of decisions by the Commission.

9. There were a number of delays in the timing of the Commission issuing consultation material and 53ZD notices which placed pressure on the time that was available for responses.
10. Vector raised concerns in writing to the Commission about its 53ZD notices, including that “the completion of 53ZD notices ... is costly and time consuming and should not be imposed on regulated suppliers unless fully justified” and about the impact on the wellbeing of our staff that a high number of 53ZD notices can have, particularly when they coincide with our financial reporting requirements. (The matter of 53ZD notices is discussed in more detail later in this submission.)
11. When the Commission issues decisions under Part 4 they, inevitably, result in a large amount of market analyst and media interest and queries. In order to ensure the market and general public are well informed, with accurate information, Vector believes the Commission should issue its decisions on an embargoed basis to regulated suppliers in advance of public release.¹ There are a number of ways the Commission could do this including requiring undertakings from each regulated supplier that they would treat the information as confidential until a time preset by the Commission or through a lockdown process, as is used for Government Budget announcements. This would also be helpful as we are required to make market releases about major decisions that impact our return given we are a listed company.
12. The Commission’s decision to issue its final electricity reset decision the day before Vector made its full year profit announcement heightened these problems. Interest was inevitably on how the Commission’s decision would impact on Vector’s results in the future, but we did not have time to properly assess this as part of our profit announcement.

Early engagement and consultation

13. One of the easiest and simplest ways of improving consultation processes is to undertake early engagement.
14. It can be helpful to seek views from interested parties prior to the Commission forming its own views, or establishing a formal position, on a particular matter.
15. This type of consultation can be undertaken before or in parallel with the Commission’s own internal policy development. This should not be seen as a substitute for consultation once the regulator has formed views on a matter, but rather as a complement which can help guide and assist the regulator as it develops its initial thinking.
16. The current consultation is a good example of this. The Commission did not need to wait until it had formed views on what aspects of the process for setting the DPPs did not work well and how the process could be improved before consulting. The consultation instead left it open to submitters to provide “feedback on any aspect of our process”.
17. Early consultation, before the regulator has committed a lot of time and resources to the development of a policy initiative, and before it has formed views on a matter, can help ensure the regulator is seen to be entering the consultation with an open mind.

¹ Bruce Girdwood (Regulatory Affairs Manager) has raised this verbally with the Commission on previous occasion.

Ensuring adequate information for submitters to understand the Commission's position

18. One of the most important aspects of any policy development process is to ensure interested parties are able to meaningfully engage with the regulator during consultation. This requires that interested parties have adequate information to respond to.
19. While Vector recognises the constraints the Commission sometimes faces, we believe there is scope for the Commission to provide improved information, so that interested parties better understand the Commission's position, including why the Commission disagrees with submitters on particular points.
20. In order for the Commission to receive meaningful and constructive feedback, during consultation, its reasoning needs to be clearly and transparently articulated, including reasons why it has accepted or rejected particular views held by interested parties.
21. If the Commission clearly responds to submission points, it can give submitters better surety that their submission points have not been missed, and provide submitters with a clearer idea how they can constructively submit in subsequent submissions.
22. One example where the Commission did not provide adequate information was in relation to consultation on Vector's Staggered Starting Price Adjustment proposal. The Commission's 2011 Process and Issues Paper referred to the Staggered Starting Price Adjustment causally as "staggering" and acknowledged that "one approach [to addressing efficiency considerations] could involve 'staggering' the sharing of efficiency gains over time". The Commission sought "views on whether a staggered sharing of efficiency gains, or an alternative, should be set out in the stand-alone SPA IM". The Commission, however, failed to explain what the stagger was, what the Commission's views on it were or even reference where the proposal originated from (previous Vector submission). This was unhelpful in terms of receiving submissions on the matter. Vector's subsequent discussions with other EDBs revealed they did not know what the Commission meant by a "stagger".²
23. Another example is the Commission's proposal for a mixed period discounting approach. The July 2011 consultation on this proposal contained just a single paragraph of discussion in the consultation paper. Given the magnitude and impact of the change we would have found more explanation and underpinning analysis to be helpful.
24. Another example again is the reference to allowable notional revenue in clause 8.5 of the EDB and GPB DPP determinations. In previous electricity price compliance statements, Vector had commented that this should read "notional revenue" but the Commission did not respond to our recommendation. When Vector and the Commission discussed this during the final stages of the gas DPP determination process, it became clear the Commission had considered Vector's recommendation but had misunderstood the point and hence had not made the necessary changes. This could also have been fixed earlier had the Commission published a response to Vector's concerns.

² It should also be noted that Vector first proposed the Staggered Starting Price Adjustment in a submission on the gas DPP reset, so parties interested only in electricity would not have necessarily seen it, even if they read all of the submissions on the DPP reset.

Avoiding unnecessary duplication

25. Vector believes the way the Commission staggered its consultation process for the electricity and gas reset consultations, with gas following electricity, resulted in unnecessary duplication.
26. It made sense for the Commission to prioritise completing the electricity price resets over the gas resets. This necessitated that the Commission would be at different stages in its process in relation to cost modelling and sector specific matters.
27. The problem was that the Commission's staggering also duplicated consultation on issues that were equally applicable to gas and electricity.
28. For example, on 21 August 2012 the Commerce Commission consulted on a "Revised Draft Reset of the 2010-15 Default Price-Quality Paths" for electricity distribution which included the section "Responses to submissions about incentive mechanisms".
29. Despite receiving submissions on this on 2 October and cross-submissions on 16 October, the Commerce Commission issued essentially the same material in its consultation paper "Revised Draft Decision on the Initial Default Price-Quality Paths for Gas Pipeline Services" on 24 October 2012. The latter paper made no reference to any of the electricity submissions despite them being directly relevant and being received before the gas consultation paper was released. This resulted in Vector cross-referencing our earlier electricity submission, rather than repeating our views.
30. The Commission should ensure generic issues, that have equal applicability in different sectors such as electricity and gas, are consulted on jointly rather than through separate consultation.
31. The Commission could have easily done this by consulting on generic issues at the same time, but sector specific matters such as modelling assumptions on a staggered basis.

Section 53ZD requests

32. We recognise that some of the issues with 53ZD notices may simply reflect teething problems associated with establishing a new Part 4 regime, and requiring provision of information regulated suppliers have not had to provide before.
33. The Commission should ensure, to the extent reasonably practicable that Information Disclosure is relied on to provide the individual regulated supplier specific information it needs for price resets, with less reliance on 53ZD notices.
34. Based on our experience, Vector believes the Commission should also ensure it:
(i) has regard to the time and resource constraints of the staff within regulated suppliers; (ii) determines the information it needs at the outset of the process; and (iii) is clear about the purpose for which the information is required.
35. In 2012 Vector received eight 53ZD gas and electricity notices, six of which were at the same time. These were delivered over a period of 3½ months, were extremely intensive and the period coincided with annual financial reporting obligations. This put Vector's staff under a lot of stress as many of the staff that had to deal with the 53ZD notices were also dealing with our financial reporting obligations. Vector expressed our concerns to the Commission in writing at the time:

Vector's financial year end activities align with the timeframes for the 53ZD notices. We require the same key staff involved in year end to prepare the information for the electricity distribution, gas transmission and gas distribution statutory notices. This places an overly heavy workload on our staff, and we have obligations to consider their health and safety. There is a practical limit to what we can ask them to do and the extent to which we can practicably (and with short notice) engage additional resources to assist. We have a similar issue with auditors

whom we engage to work on both year end and statutory notices. In both cases we rely on the specialised knowledge of specific people.

Last year the Commission issued the statutory notices for the gas and electricity businesses at separate times and this largely avoided the particularly busy year end period.

36. These concerns were exacerbated by the lack of prior warning of the 53ZD notices:

There was also, effectively, no prior warning and no draft notices issued, unlike last year. The draft notices effectively gave Vector a heads up on what to expect, allowing a good lead in time for planning and resource allocation, in addition to informing the Commission with the submissions that were made.

37. The Commission also issued a number of follow-up requests for information, within extremely tight timeframes, which reflected that it was continually developing its price reset modelling approach and realising more information was required. This exacerbated the internal resourcing pressures that our staff faced in complying with the Commission's 53ZD requirements.
38. We also note that some information the Commission required to be disclosed (i) was not used in the DPP reset e.g. MDL balancing information; and (ii) was not appropriately specified e.g. some gas transmission information requirements were written in distribution centric terms.³
39. It would also be helpful if the Commission is clear about the purpose for which the information is required. Various aspects of the 53ZD notices were open to substantive interpretation. A better understanding of how the information was to be used would have provided useful guidance as to how to interpret the information, and helped us to provide the most suitable information possible to the Commission.
40. For example, in February 2013 the Commission asked Vector for information relating to unrecovered balancing gas costs. Vector started a process of preparing this information but mid-way through the process asked the Commission to explain why they wanted the information. After that explanation was provided, Vector realised there was no need to provide the information if we agreed that pre-2013 balancing gas costs should not be treated as recoverable costs from 2013. The work in preparing the information could have been avoided had the Commission been clear in advance why it had been requested.

Other matters

41. Vector has the following additional comments:
- a. **Financial modelling:** Vector agrees with Powerco's proposal for changing the presentation of the Financial Model.
 - b. Vector does not agree that the Financial Model is only moderately complex. We believe that the Commission has made a number of judgements, such as modelling cash flow, that result in the model being extremely complex.
 - c. **Consultation time-frames:** Vector considered the length of time available for responses to consultations were tight. This inevitably impacted on submissions and the level of constructive feedback that was possible. This was partly due to the tight timeframes the Commission itself faced in implementing the new Part 4 regime. For the next resets, if the Commission prioritises the work, it should be able to allow for longer consultation periods.

³ Vector raised similar concerns about the Information Disclosure Requirements. The draft gas transmission pricing methodology disclosure requirements, for example, were clearly written in gas distribution centric terms without sufficient modification for gas transmission.

- d. **Briefings:** Market Analyst briefings are a worthwhile addition, but should be generalised as briefings for Market Analysts, industry participants and other interested parties. The opportunity to ask the Commission questions at these briefings should not be limited to Market Analysts.
- e. **Industry engagement:** Vector considers that use of Technical Working Groups is a constructive addition to the Commission's processes. We also observe that the Commission's reliance on the Telecommunications Carriers' Forum to establish Codes, which the Commission can then review and approve, has also been very successful. Similarly, the Electricity Authority and GIC both make use of Working Groups, consisting of industry participants. These Working Groups aren't limited to technical matters and also contribute to policy development matters.

We urge the Commission to consider how it could make greater use of industry support. This may be a matter the Commission could usefully have a dialogue with the ENA and industry participants on.

Concluding remarks

- 42. Vector trusts the Commission finds our comments helpful.
- 43. Key components of a strong and robust consultation process include:
 - a. Early engagement with interested parties;
 - b. A high degree of transparency around the Commission's reasoning; particularly on complex and contentious matters; and
 - c. Adequate information is provided to submitters to enable informed submissions, and responses to the Commission's views.
- 44. We urge the Commission to be conscious of the time and resource pressures in processes can place on interested parties, particularly for regulated suppliers who are required to provide information to the Commission, and to ensure that the timing for consultation and information requests are signalled well in advance.

Yours sincerely,



Bruce Girdwood
Regulatory Affairs Manager