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Submission on DPP refinements consultation

1. Vector welcomes the opportunity to provide this submission on the Commerce Commission's ("**Commission**") consultation paper *2010-2015 Electricity Distribution Default Price-Quality Path refinements Discussion and Draft Decisions Paper*. Vector has seen and fully supports the submission from the Electricity Networks Association ("**ENA**") on this topic.

Regulatory requirements for re-opening a DPP

2. Vector endorses the submission of the ENA regarding circumstances in which a Default Price-Quality Path ("**DPP**") may be re-opened within a regulatory period. The DPP must only be re-opened in accordance with the circumstances set out in input methodologies or where there is an error (which, of course, is a circumstance set out in the draft input methodology determinations). In addition, the Commission may only reset the DPP in light of the final input methodologies if they would have resulted in a materially different price-quality path had they been in place when the DPP was determined.

3. Vector submits that the revenue adjustment term is a correction to an error or omission in the DPP and it is therefore lawful to re-open the DPP to adjust for this term. It is also lawful to reset the DPP in accordance with input methodologies, if the input methodologies would have resulted in a materially different price-quality path being set had they been in place prior to 1 April 2010 (although this should not be consulted on further until after the input methodologies are determined).

4. However, it is unlawful to amend the price path to remove the impact of a change in GST on the consumer price index as this is not a correction of an error or necessary to reflect the input methodologies.

5. In this submission, we consider the Commission's proposals for making adjustments to the DPP as they were proposed by the Commission (i.e. the starting price adjustment will go ahead in 2012). However, Vector's position remains that, if an input methodology is appealed, the Commission should place the starting price adjustment process on hold until the outcome of the appeal is known¹.

Revenue adjustment term

6. Vector welcomes the Commission's intention to resolve the "headroom" issue in a practical way and in time for Electricity Distribution Businesses ("**EDB**") to set prices for the year starting 1 April 2011. The Commission's proposed solution to the problem is appropriate and Vector supports the proposed amendment to the price-path formula.

GST amendment to derivation of CPI

7. As noted above, the Commission's proposal to remove the impact of the GST increase on CPI is unlawful. It is inconsistent with the requirements set out in the input methodologies and the Commerce Act 1986 ("**the Act**") regarding when a price-quality path may be reopened. In addition, Section 530(b) of the Act requires that a DPP must include rates of change in prices relative to the consumer price index. To set prices based on an index that is different from CPI is therefore contrary to section 530(b).

8. In addition, the Commission's proposal amounts to regulatory opportunism, because if the GST change had happened outside of this consultation timeframe the Commission would not have been able to make the adjustment.

9. The Commission argues that the adjustment is appropriate as EDB prices are typically GST exclusive. That is irrelevant. There are many components of CPI which are not directly included or reflected in EDB prices and it was never intended that the CPI would be a measure of input cost inflation for EDBs.

¹ Vector Ltd, Submission to Commerce Commission on Starting Price Adjustments for DPPs, 10 September 2010, paragraphs 74-75.

Timing of changes to reflect input methodologies

10. The consultation paper reflects the input methodologies as they were set out in the draft determinations. Suppliers have made a series of submissions on those determinations and put forward significant alternatives to the Commission's proposals. Vector agrees with the ENA that the Commission should defer further consultation on giving effect to the input methodology determinations until the determinations have been finalised.

11. In addition, some of the final input methodologies may not have a sufficiently large impact on EDB revenues to meet the "materially different" test in section 54K and therefore they may not justify an amendment to the DPP. See Vector's previous submission for our detailed views on when and how a DPP may be adjusted in accordance with the Act.²

Pass-through and recoverable costs

12. For the reasons specified in our submission on the Rules and Process Input Methodologies³, Vector continues to disagree with the need for a separate recoverable cost category and believes that these costs should be included in the definition of pass-through costs. However, if the recoverable cost category remains, the Commission's proposed method of providing for it in the price path formula is reasonable (i.e. by using a 'V' term that will be subtracted from the function of price and quantities in the same way as the 'K' term for pass-through costs).

Avoided transmission charges

13. Vector refers the Commission to previous submissions that have been made on this issue.⁴ The Commission should not have a role in adjudicating on the nature of avoided transmission investments. This level of scrutiny is inconsistent with the intended low-cost nature of a DPP and will have the effect that EDBs will not enter into avoided transmission investments (such as the spur line transfer with Transpower that the Commission uses as an example) due to the risk that the

² Vector *Submission to Commerce Commission on Starting Price Adjustments for DPPs*, 10 September 2010, pp. 16-17.

³ Vector Input Methodology submission, Cost Allocation, Pricing Methodologies, Treatment of Taxation and Rules and Processes, 9 August 2010, pp. 68-69.

⁴ Vector Ltd, *Submission in Response to the Commerce Commission's Input Methodologies*, 9 August 2010, p.69. Unison Networks Ltd, *Submission on Commerce Commission Draft Input Methodology Determinations*, 9 August 2010, pp. 31-35. Electricity Networks Association, *Submission 5: Processes and Rules Input Methodology*, 9 August 2010, pp. 13-17.

Commission may not approve the pass-through of the avoided transmission charges.

14. In addition, the Commission has not addressed the concerns raised in the input methodology submissions regarding avoided transmission costs associated with distributed generation. Where distributed generation reduces transmission charges to a distributor, the distributor must pay those avoided transmission costs to the distributed generator. A five-year time limit on passing through these costs is unrealistic as the avoided transmission payments to the distributed generator may continue indefinitely. The Commission must re-instate avoided transmission payments to distributed generators as pass-through or recoverable costs and not impose a five-year time limit on the pass through of these costs.

IRIS

15. Vector agrees with the Commission's view that EDBs will specify any amounts consistent with the IRIS input methodology in their annual compliance statements consistent with those provided in information disclosure. Vector also agrees that any IRIS amount carried forward from a CPP to a DPP should be recovered under a DPP and the Commission will not need any further information to ensure the amounts to be recovered are appropriate.

16. The paragraph above is without prejudice to our view that IRIS should apply to DPPs as well as CPPs and have a wider scope than controllable opex only.

Transactions between EDBs

17. The draft IM Determination for transactions between EDBs seems incorrect where it applies to transfers of assets between EDBs. The draft IM requires EDBs that have engaged in a transaction to be subject to a joint price-quality path at the end of the current regulatory period or the next regulatory period (depending on whether the suppliers are currently on a CPP). This is appropriate in principle for mergers, although we have some concerns with how the rules are specified. However, the draft IM also applies to acquisitions of electric lines of a prescribed voltage⁵ that:

- are 25 kilometres or more in length; or
- serve 500 customers or more; or
- convey at least 20GWh of electricity per year.

⁵ A prescribed voltage electric line is defined as a line that is capable of conveying electricity at a voltage equal to or greater than 3.3 kilovolts.

18. Thus if one EDB purchased 25 kilometres of line above 3.3kV from a neighbouring EDB, the two EDBs would need to be subject to a joint price-quality path from the start of the next regulatory period. While such transactions are likely to be rare, to require the EDBs to be subject to a joint price-quality path in these circumstances does not seem to be a sensible outcome.

CPP application window

19. It is unclear what benefit would be achieved by specifying the CPP application window by March 2011 rather than December 2011. As the window will be in January each year, this would seem to have little practical effect. However, the Commission should provide that, where less than four applications are received within a CPP application window, applications received thereafter (except those in response to a Catastrophic Event) should be progressed on a first-come first-served basis until at least four applications are under consideration.

Transpower pricing notification

20. The Commission's proposal to set the Individual Price-Quality Path Determination for Transpower in December 2010 (which will take effect on 1 April 2011) is inconsistent with section 53M(7) of the Act, which requires at least four months notice to be given. Vector is concerned that the clear and specific regulatory requirements of the Act are being breached and considers that this sets a dangerous precedent. Vector recommends that the Commission changes its decision regarding the timing of the Transpower IPP Determination to ensure that it complies with the provisions of the Act.

Contact details

21. Thank-you for considering this submission. If you require further information please contact me on 09 978 8340, or at allan.carvell@vector.co.nz.

Yours sincerely,



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