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5 September 2011

Cross-Submission on Electricity Distribution Starting Price Adjustments Draft Decisions Paper

Introduction

1. Vector welcomes the opportunity to provide this cross-submission in response to submissions received on the Commerce Commission ("Commission") *2010-2015 Default Price-Quality Path for Electricity Distribution: Draft Decisions Paper*.
2. Vector's contact person for this submission is:

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3. This submission makes further comments regarding asset valuation adjustments and insurance premiums. It also responds to comments made by certain submitters regarding claw-back.

Asset valuation adjustments

4. Vector notes the Commission's latest correspondence regarding asset valuation adjustments and insurance premium information.¹
5. Vector remains of the view that the Commission must ensure that all electricity distribution businesses ("EDBs) are treated equally through the

¹ Letter from Sue Begg to Simon Mackenzie, *Insurance premiums and amendments to disclosed data*, 2 September 2011.

asset valuation process. To ensure equal treatment, EDBs must be given the opportunity to resubmit corrected information on the basis of principles that have now clearly emerged. It is unclear how the approach proposed by the Commission in its letter of 2 September will ensure equal treatment for all EDBs as the Commission may have limited visibility regarding the detail of the approaches that are used.

6. Vector has no issue with the Commission's acceptance of the asset valuation adjustments that have been made by EDBs or with the Final Review Report². We seek only the opportunity to correct errors in our asset valuation adjustments that arose as a result of a misinterpretation of previously unclear requirements.

Insurance premiums

7. Vector welcomes the Commission's request for information regarding an increase in insurance premiums due to recent natural disasters. However, as discussed in our previous submission³, Vector considers that the recent natural disasters will not only impact on the cost of insurance on a like for like cover basis but will also cause EDB Boards to reconsider their risk profile. Overall insurance costs may well increase due to a change in Board perspectives of prudent risk management. Additional costs resulting from this change should also be encapsulated in the insurance information that is provided in accordance with Schedule A of the letter of 2 September.

Claw-back

8. Unison and MEUG have both argued for the application of claw-back.
9. MEUG suggest claw-back should apply to EDBs that the Commission deems are earning supranormal profits but not to EDBs that are operating at a loss. There would be short-term benefits to MEUG's members from such an approach, but we consider they would be outweighed by longer-term losses due to weakened investment and efficiency incentives.
10. Unison argues that "claw-back amounts could readily be established through the roll-forward of regulatory information in the 2011 and 2012 years"⁴. Vector does not agree. The RAB roll-forward and deferred tax calculations relate to capital expenditure and not to operational expenditure so any analysis based on this information alone would necessarily be incomplete.

² Nel Consulting Ltd., *The Review of the Independent Engineer's Reports on the Asset Adjustment Process of Electricity Distribution Businesses: Final Review Report*, July 2011.

³ Vector Ltd., *Submission on 2010-2015 Default Price-Quality Path for Electricity Distribution Draft Decisions Paper*, 24 August 2011, paragraph 146.

⁴ Unison Networks Ltd., *Submission on 2010-2015 Default Price-Quality Path for Electricity Distribution Draft Decisions Paper*, 24 August 2011, paragraph 40.

We also do not see how information about any roll-forward for the 2011 and 2012 years would be of use as no 2012 information will be available prior to 20 October 2011 and the 2011 disclosure information will not be consistent with the input methodologies or statutory notice data.

11. Vector agrees with the Commission that claw-back in a CPP application could be based on an assessment of actual expenditures; this is because sufficient information will be available in a CPP application to make such an assessment. Equivalent information is not available under a DPP.
12. Vector does not agree with Unison that the Commission has sufficient data to compare 2009/10 and 2010/11 and establish whether any efficiency gains were made in the first year of the regulatory period. The 2010/11 information disclosures are not consistent with the 2009/10 statutory notice data or with the input methodologies, which makes comparisons challenging. We also do not see how an efficiency gain could be readily identified from any other change in the inputs into the return on investment calculation.
13. Vector does not believe the "safety margin" concept addresses the Commission's concerns regarding the potential to inadvertently claw-back efficiency gains. Assessing a margin would not be straightforward and would be likely to under- and over-reward certain EDBs.
14. In conclusion, Vector considers that Unison has over-stated the ease with which claw-back could be assessed, especially in the presence of efficiency gains. Vector continues to support the Commission's view that claw-back should not be applied in the forthcoming reset.

Yours sincerely,



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