



**Submission to Commerce Commission on
Initial Reset of the Default Price-Quality
Path for Electricity Distribution
Businesses: Initial Reset Determination
(DRAFT) Consultation Paper**

30 October 2009

INTRODUCTION

1. Vector welcomes the opportunity to provide this submission to the Commerce Commission on the *Initial Reset of the Default Price-Quality Path for Electricity Distribution Businesses: Initial Reset Determination (DRAFT) Consultation Paper* ("Draft Determination"). We are appreciative of this additional consultation step.

2. The Commission has based the Draft Determination on the 8 September draft decisions paper. Vector and other EDBs made comments on the draft decisions which had not yet been considered, accordingly, this submission focuses on the technical provisions of the Draft Determination, and we will make additional comments on further drafts of the Determination. In this relatively brief submission we set out our views on matters that we believe could be further clarified in the determination, and issues that we believe need to be addressed that do not appear to have been given significant consideration to date.

3. Vector's contact for this submission is Nathan Strong, Manager Regulatory Affairs, on 04 803 9039 or nathan.strong@vector.co.nz.

COMMENTS ON THE DRAFT DETERMINATION

Excluded services

4. The definition of Electricity Lines Services under section 54C of the Act provides only a limited provision for excluded services. However, under current thresholds requirements, Vector currently applies the definition of excluded services to a number of activities and services provided in competitive markets as described in our annual threshold compliance statements. In Vector's submission on the 19 June discussion paper we noted that clarity on what services could be excluded would be beneficial.

5. Vector submits that the Commission should include a definition of excluded services as currently set out in the Commerce Act (Electricity Distribution Thresholds) Notice 2004 to ensure that services provided in competitive markets are not unnecessarily caught by the DPP reset. Vector submits this would be consistent with the intent of regulation to allow outcomes consistent with those in competitive markets, and a general principle of only regulating where strictly necessary.

Pass-through costs - transmission

6. The definition of Pass-through Costs refers to Transmission Charges, which in turn refers to the Transmission Pricing Methodology ("TPM"). The TPM refers to charges for services as set out in Schedule F5 of Section IV of Part F of the EGRs 2003. However, the TPM does not include loss constraint excess payments (loss rental rebates), new investment contracts or ancillary service charges. These "other" transmission charges are not mentioned in the clauses elsewhere and Vector is concerned that we would not be able to pass these unavoidable costs on to customers under the proposed approach. Vector submits that the definition of transmission pass-through costs be expanded.

Pass-through costs - Commerce Act levies

7. Vector supports the inclusion of Commerce Act Levies as a pass-through cost item. However Vector is concerned that the levies, determined under the Commerce (Levy on Suppliers of Regulated Goods and Services) Regulations 2009, could be volatile, including the possibility of retrospective wash-ups. Depending on the magnitude of these levies, this could lead to an increased chance on technical breaches of the price path. It would be useful for the Commission to ensure that technical breaches do not occur because of variances in levy forecasts and actual levies. Potentially an 'overs and unders' mechanism could be useful in ensuring the intention of cost pass-through is achieved over time.

8. Clause 8.6 of the determination states that EDBs may amortise levies incurred in the 2009/2010 year over the regulatory period. Para B15 (page 136 of the draft decisions) discusses the amortisation intentions. These haven't directly been reflected in the draft decisions, and the requirements around amortisation are relatively unclear. It is likely that Vector's auditors would seek clarification of the approaches that are permissible for the avoidance of doubt. Vector submits that the Commission could avoid future requests for clarification by setting out more clearly the approach to amortising Commerce Act levies now (even if by way of guideline note).

Definition of price

9. The definition of Price refers to section 52C of the Act. In the Act the definition of price includes individual prices, aggregate prices or revenues (including formulas for deriving revenues). This definition of price does not make sense when it is read in the context of the determination, particularly the weighted average price formula. The reference to the Act could be removed (as with previous versions of the price thresholds).

Quantities

10. The draft determination quantities continue to be based on t-1 quantities. Vector reiterates its support for a t-2 approach to avoid unnecessary compliance costs.

11. Notwithstanding this view, if the Commission continue with a t-1 approach, EDBS will be required to establish forecasts for part of the period when setting prices. In the draft decisions paper the Commission discussed (at 4.84 on page 54) what would happen if an EDB's forecasts were consistently inaccurate. The Commission suggested a materiality threshold of 5% for differences between actual quantities and forecasts. This has not been translated into the draft determination, which currently requires an explanation of any variance between forecast and actual amounts to be explained (11.1(b)(ii)). No materiality threshold has been included, nor any process around what happens if the materiality threshold is breached, nor how to measure differences between actual and forecast: for example, is it an aggregate difference, or for individual quantities pertaining to each tariff? If the latter, this would require a significant amount of work. We also note that it will not always be possible for EDBs to explain why actual results differ from forecast given, for example, actual volumes are driven by customer decisions, which are not observed directly by EDBs. These issues would be avoided if a t-2 approach were adopted.

Price restructuring

12. The clause providing for restructuring of prices (8.5) of the DPP has the same intention as the existing price thresholds. Although this hasn't directly caused any issues it does possibly create unnecessary compliance activities which could possibly be avoided. Vector has typically restructured prices annually and will be doing so into the foreseeable future in response to retailers' demands for simpler tariff structures and a desire to lower overall transaction costs. This would necessitate additional information to be provided under clause 8.5. If some additional wording was incorporated into 8.5 such as "if a Non-Exempt EDB restructures its Prices applying during an Assessment Period and is unable to incorporate that price restructure into the Allowable Notional Revenue calculations as defined in clause 8.3 and 8.4, then it must.....". In many instances (for example, amalgamating tariff categories, which is a tariff restructure) it will still be possible to demonstrate compliance using the Allowable Notional Revenue calculations, without the additional proposed compliance steps.

Quality path

13. Our initial review of the quality path compliance requirements has uncovered no drafting issues. We continue to have reservations, as expressed in our submission on the Draft Decisions Paper, on the proposed mechanisms for developing quality targets and testing for compliance.

14. Vector does, however, have concerns regarding the period a MED can cover. Under the thresholds regime, the Commission allowed for 'multi-day storms' where a storm which clearly impacted more than one calendar day could be treated as one extreme event and replaced with one boundary value. Vector used this approach to account for a major storm in 2007 by rolling up several day's SAIDI as a single event (with relevant evidence to show the storm caused all the damage).

15. Vector submits that the Commission should make an allowance for multi-day storm events to be accounted for and normalised appropriately (noting that Vector's view is that substitution of the average value, or exclusion of the event entirely, is the most appropriate approach). For example, in the guidelines on assessments of compliance with the quality threshold the Commission provided:

e) Where an extreme event occurs over multiple days and supporting evidence is provided by the ELB, the Commission will consider whether to include those days in the extreme event. This would mean that the boundary value would replace multiple days, i.e., if an extreme event occurred on day one but it continued into day two, then day one's SAIDI value would be replaced with the boundary value and day two's SAIDI value would be set to zero.¹

¹ Commerce Commission (2007) *Supplementary Guidelines for Investigating Breaches of the Reliability Criterion of the Quality Threshold* page 11, para 48