



**Submission to Commerce Commission on  
Information Disclosure Discussion Paper**

**11 September 2009**

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## INTRODUCTION

1. Vector welcomes the opportunity to provide this submission to the Commerce Commission on the *Information Disclosure Discussion Paper* (the "Discussion Paper"), released 29 June.
2. Vector comments primarily on: the timing for consultation and development of Information Disclosures (or alternative "Disclosures") for electricity distribution businesses ("EDBs") and gas pipeline businesses ("GPBs") (Part A); the regulatory context for Information Disclosure (Part B); and on several significant high-level issues raised in the Discussion Paper (Part C).
3. Vector has not submitted on any detail raised in the Discussion Paper or answered the Commission's specific questions. This is because we consider that Disclosures should be informed by determinations made under input methodologies and default price-quality paths ("DPP"). Detailed consultation on Disclosures prior to this seems out of sequence and it would seem more efficient to delay any detailed consultation. We argue in Part A our reasons for why consultation on Disclosures for EDBs and GPBs should be delayed.
4. Vector is happy to discuss this submission further if required. Please contact Nathan Strong, Manager Regulatory Affairs, on 04 803 9039 or at [nathan.strong@vector.co.nz](mailto:nathan.strong@vector.co.nz).

## **EXECUTIVE SUMMARY**

### **Deferral of consultation on Information Disclosures (Part A)**

5. In Part A of our submission, Vector notes that the Commission does not intend to set Information Disclosure determinations until after the input methodologies are determined. While the Commission states that the consultation leading up to the determination will run in parallel with the input methodologies consultation for airports (unlike the position for EDBs and GPBs), it's makes no decision on the appropriate sequencing of consultations for EDBs and GPBs.
6. Vector submits that there are compelling reasons in support of the Commission deferring commencement of the Disclosures consultation process for EDBs and GPBs until after the input methodologies have been set. That is, delaying consultation on Disclosures until after input methodologies are set will:
  - a) best ensure the development of an effective and enduring Information Disclosure regime for EDBs and GPBs that is informed by all relevant information;
  - b) enable meaningful consultation on the detail of the Disclosure requirements (and therefore a more effective and enduring regime);
  - c) enable resources and time to be more effectively focussed on the input methodology process in the first instance; and
  - d) avoid the substantial risk of costly rework and re-consultation on the Information Disclosures.
7. On this basis Vector has not addressed the Commission's specific questions in the Discussion Paper in our submission.
8. As an alternative, Vector considers there are certain components that could potentially be consulted on prior to input methodologies being established, which do not rely on input methodology decisions. However, in our view, this piecemeal strategy would be inefficient.

## **Developing a robust regulatory framework (Part B)**

9. A key feature of the Information Disclosure regime is that it is intended to be one of the most light-handed regulatory instruments available under the Act. In this context the Commission should seek to implement the least cost means of achieving the Information Disclosure purpose.
10. The cost of Information Disclosure for regulated firms and the Commission is potentially considerable depending on the extent of the information sought. In order to establish a least cost regime, only the minimum information necessary to achieve the purposes of the regime should be required.
11. Vector submits that, in order to determine minimum requirements, the Commission should:
  - a) Consider the scope of the new purpose statement for Information Disclosure and the extent that it differs from the previous Part 4A regime. Vector submits that the new purpose statement is considerably more limited in scope than under the previous regime for EDBs.
  - b) Consider the other regulatory instruments that apply in relation to a particular sector. Information Disclosure is not the only mechanism by which interested parties can access information to assess whether the purposes of Part 4 are being met. Less detailed information should be required in order to meet the section 53A purpose statement as increasingly detailed information about how the Part 4 purpose statement is being met is provided under default price-quality path ("DPP") and customised price quality path ("CPP") regulation.
12. Vector's key concern is that the Commission's preliminary views do not reflect the adoption of least cost approach. Specifically:
  - a) The Commission has not considered whether the Information Disclosure components and requirements identified in the Discussion Paper are the minimum necessary with reference to the new purpose statement and other regulatory instruments that apply to the sector. Some form of cost-benefit analysis should be undertaken in order to determine the least cost form of regulation.
  - b) The Commission is seeking to apply the previous Part 4A Information Disclosure regime for electricity, as well as to gas, without first considering how the new regime differs from Part 4A, specifically in

relation to the new purpose statement and the other regulatory instruments that apply.

### **Significant Issues (Part C)**

13. While Vector believes it to be premature to discuss specific Disclosure requirements in detail before input methodologies and DPPs are set, there are several significant issues raised in the Discussion Paper that justify comment at this early stage. Part C discusses the following high-level issues:
- a) *Financial and asset statement Disclosures* – which discusses consolidated financial statements, opex and capex forecast statements, disaggregated roll-forward reports, and the role of audit in showing compliance.
  - b) *Defining business units for Disclosures* – which discusses the need for separate gas transmission and distribution Disclosure requirements, the usefulness of Disclosures by non-contiguous network, and the rationale for including administration of gas balancing services in the regulatory definition of GPBs.
  - c) *AMP Disclosures* – which discusses AMP reviews, performance measures and appropriate standards.
  - d) *Quality Disclosures* – which discusses the role of consumer engagement in informing quality incentives under DPP resets.
  - e) *Pricing Disclosures* – which discusses the unreliability of pricing statistics to provide meaningful insight into pricing efficiency, how actual prices should be disclosed to customers, and the form of pricing methodologies under Information Disclosures.
  - f) *Other Disclosures* – which discusses why prescribed contract and policy Disclosures should not be required.

## PART A: DEFERRAL OF CONSULTATION FOR INFORMATION DISCLOSURES

14. In relation to EDBs and GPBs, the Commission states that it intends to set Information Disclosure requirements after the applicable input methodologies have been determined. This is because section 53C(1)(g) requires such determinations to "specify the input methodologies".<sup>1</sup>
15. In relation to airports, the Information Disclosure requirements must be set no later than 1 July 2010, one day after the statutory deadline for the input methodologies. The Commission notes that this requires that consultation on the Disclosure regime necessarily take place in parallel with consultation on the input methodologies.<sup>2</sup> This is clearly less than ideal but specifically required by the Act.
16. As noted by the Commission, no such statutory constraint applies in relation to EDBs and GPBs.<sup>3</sup> The Information Disclosure requirements can be set "as soon as practicable" after the applicable input methodologies have been set. Unlike the position with airports, the Commission does not suggest that consultation take place in parallel. However, the Commission intends to outline the proposed timeframe for making initial Information Disclosure determinations for EDBs and GPBs following review of submissions on the Discussion Paper.
17. In relation to the proposed timeframe for EDBs and GPBs, Vector submits that a clear decision should be made now to defer the *consultation* (not just the determination) on Information Disclosures for EDBs and GPBs until *after* the input methodologies are set. Many components of the Information Disclosure regime are inextricably linked to the wider regulatory framework, including input methodologies and DPPs. This wider information will need to be considered when the specific details of the Disclosure requirements are being developed.
18. Under this approach, the Commission would continue to consult on the Disclosure requirements for airports only at this stage. Vector submits that it makes sense to develop Information Disclosure requirements for airports separately from the requirements for EDBs and GPBs given:

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<sup>1</sup> See Appendix B of the Discussion Paper, B11, B22 and B35.

<sup>2</sup> Ibid at B42.

<sup>3</sup> Ibid at B21 and B34.

- a) The very different nature of the airport sector and its form of regulation, whereas for non-exempt EDBs and GPBs, DPP and CPP regulation are the regulatory instruments to be used to achieve the purpose statement. The Commission notes that the requirements for each sector will vary given their unique characteristics. Vector submits further that the characteristics of airports are significantly different from those of EDBs and GPBs
  - b) There is no requirement under the Act to apply consistent approaches across sectors for Information Disclosure (even to apply the same high level components to airports and to EDBs and GPBs). The purpose is to provide sufficient information to interested parties to be able to determine whether the Part 4 purpose statement is being met. The nature and extent of this information will necessarily be different across sectors depending on the nature of the assets and how that sector is regulated under the Act as a whole.
  - c) The implementation principle of consistency is not relevant to Information Disclosure across sectors (including for the reasons set out above). Applying consistent approaches across airports and other sectors will not promote regulatory certainty and confidence (the key reason why consistent approaches should be taken). To the contrary, applying consistent approaches in these circumstances could undermine regulatory confidence given the unique factors that must be considered.
19. Pending development of Information Disclosure determinations for EDBs and GPBs, existing Disclosure requirements<sup>4</sup> would continue to apply under s54W (electricity) and s55J (gas). This means that information will be available to interested parties while the Information Disclosure requirements are developed.
20. Consulting on Information Disclosure for EDBs and GPBs after input methodologies are set:
- a) best ensures the development of an effective and enduring Information Disclosure regime for EDBs and GPBs that is informed by all relevant information;

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<sup>4</sup> Part 4A information disclosures for EDBs and "Gas (Information Disclosure) Regulations 1997" for GPBs

- b) enables meaningful consultation on the detail of the Disclosure requirements (and therefore a more effective and enduring regime);
  - c) enables resources and time to be more effectively focussed on the input methodology process in the first instance; and
  - d) avoids the substantial risk of costly rework and re-consultation on Information Disclosures.
21. Alternatively, if the Commission considers that the consultation on Disclosure requirements for EDBs and GPBs should commence now (which Vector strongly disagrees), then Vector submits that it should only be in relation to those parts of the Disclosure regime that are not connected to the input methodologies. Vector notes the Commission's view that it may be necessary to defer development of certain Disclosure requirements given the development work required to implement an effective Information Disclosure regime. The Commission identifies that all matters do not have to be included in an initial determination and that subsequent amendment can be made (following consultation where the amendment is material).
22. Vector considers there are certain components that could be consulted on prior to completion of the input methodologies (such as some financial information (not related to input methodologies), publication, retention, certification, statutory declaration, audit, AMP structure). Under such an approach the Commission should then defer consultation and development of Disclosures on return on investment; regulated asset base; quality; and pricing methodologies, until after the input methodologies. However, Vector emphasises that this piecemeal approach is likely to be less effective than consulting on all Information Disclosure requirements at the same time after input methodologies have been established.
23. In conclusion, Vector urges that the Commission to defer not just the Information Disclosure determination but the commencement of consultation on the entire Information Disclosure regime for EDBs and GPBs until after the input methodologies are set. Developing some or all aspects of the Information Disclosure regime before the detail of the input methodologies is known (given the strong correlation between input methodologies and Information Disclosure) is unlikely to be an effective or efficient process.

## **PART B: REGULATORY FRAMEWORK**

24. In this section Vector discusses:

- a) The importance of developing a Disclosure regime that meets the purposes of Part 4 at the least cost and the extent to which the Commission's preliminary views and analysis is consistent with this approach;
- b) Key differences between the previous Part 4A information disclosure purpose statement and the purpose statement under the current regime;
- c) Why information disclosures should be aligned with other regulatory instruments in order to implement a regime that achieves the purpose statement at least cost;
- d) The Commission's proposal that the Part 4A information disclosure regime should apply under the new regime and why further analysis is required before such a proposal made;
- e) Section 54Q (energy efficiency) and why information relating to this provision goes beyond what is required under the Information Disclosure regime.

### **A least cost - fit for purpose regime is required**

25. Implementation of the Information Disclosure regime under the Act requires detailed consideration of: the relevant statutory provisions; the operation of Information Disclosure in the context of other regulatory instruments; and the policy objectives underlying the regime. This analysis is particularly important in the context of a new reformed regulatory regime.

26. A key feature of the Information Disclosure regime is that it is intended to be one of the most light-handed regulatory instruments available under the Act. The reason for having light-handed instruments is that they are relatively low cost, compared to alternative instruments such as DPPs and CPPs. Parliament specifically designed the regime to be cost-effective given the small-scale of the New Zealand infrastructure sector and the businesses

operating within it<sup>5</sup>. This requires that the Commission seek to implement an Information Disclosure regime that achieves the relevant purpose under Part 4 at the least-cost required to do so. The extent of information required to be disclosed in order to show that the purposes of Part 4 are met is a critical tension the Commission will need to address for each Disclosure requirement.

27. In addition to being a key feature of a light handed regime design, cost efficiency is also a best practice regulatory principle (referred to by the Commission as one of its implementation principles). As set out above, cost efficiency is a critical consideration in relation to Information Disclosure. The on-going cost of producing disclosures is significant for both regulated businesses and the Commission alike and can be significantly increased by additional requirements.
28. The Commission should not underestimate the costs suppliers face in recording, preparing, auditing, signing-off and publishing Information Disclosures either. Meeting Disclosures requirements can be a significant drain on resources for other business as usual activities for both staff and director's. Indeed, Vector itself employs several full time staff whose sole purpose is to prepare Disclosures and, even then, many other staff are required to fulfil Disclosure requirement functions in addition to their usual jobs. New Disclosures requirement will also create one-off implementation costs related to setting up new information systems, standards, and procedures, which should also not be underestimated. Many of these costs are also not allowed to be treated as pass through costs under DPPs either. In light of these significant costs, Vector believes the Commission should seek to minimise Information Disclosure requirement to only what is required to meet the purposes of Part 4; superfluous information only leads to unnecessary costs.
29. In the context of the Discussion Paper, though, while the Commission has considered the interpretation of the new purpose statement for Information Disclosure and its relationship to the Part 4 purpose statement, Vector is concerned that:
  - a) The Commission has not specifically considered whether the Information Disclosure components and requirements identified in the Discussion Paper are the minimum necessary with reference to the new purpose statement and other regulatory instruments that apply to

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<sup>5</sup> As noted in the Explanatory Note to the Bill, a key objective of underlying the reforms was to tailor the regime to New Zealand's small size (with small firms and limited resources).

the sector. Some form of cost-benefit analysis should be undertaken in order to determine the least cost form of regulation.

- b) The Commission is seeking to apply Part 4A from the previous regime without considering how the new regime differs from Part 4A, specifically in relation to the new purpose statement and the other regulatory instruments that apply (as set out in greater detail below).
30. In order to be a fit-for-purpose least cost regime, Information Disclosure requirements should include only the minimum (in terms of quantity of data) requirements necessary to show that the purpose of Part 4 is being met. Vector is concerned the Commission is seeking to require information that goes beyond the minimum required, possibly because cost-benefit analysis has been undertaken in this regard.
31. One example is pricing statistics, which, in Vector's view, are arbitrary and misleading in showing efficient prices. A more effective and cost efficient approach would be to remove this requirement in favour of disclosure of actual prices and pricing methodologies (as discussed in more detail in Part C) that better show pricing efficiencies between different consumer groups.

### **New purpose statement**

32. The Act introduces a new information disclosure regime purpose, which is set out in s53A of the Act, as follows:

“...to ensure that sufficient information is readily available to interested persons to assess whether the purpose of this Part is being met.”

33. This represents a significant and deliberate change from the previous Part 4A disclosures purpose statement:

“...to promote the efficient operation of markets directly related to electricity distribution and transmission services by ensuring that large line owners and large electricity distributors make publicly available reliable and timely information about the operation and behaviour of those businesses, so that a wide range of people are informed about such factors as profits, costs, asset values, price (including terms and conditions of supply), quality, security, and reliability of supply of those businesses.”

34. Specifically:

- a) Under Part 4A there was an express requirement for the Commission to promote the efficient operation of markets by ensuring that

regulated businesses disclose a range of reliable and timely information about the operation and behaviour of their businesses. Essentially, previous disclosures were intended to provide broad information on market operations, as a means in itself of placing pressure on EDBs and GPBs to perform.

- b) Under the new Part 4 regime, however, the Commission is required to ensure information is available to enable interested parties (as opposed to the more broad 'wide range of people') to assess performance against the Part 4 purpose statement (s52A). This is more targeted than the previous purpose statement and implies a narrower scope for the Information Disclosure. It is no longer a means for promoting efficient operation of markets.
35. In analysing whether a Disclosure assists an interested person in assessing whether the purpose of Part 4 is met, it is important for the Commission to specifically link a particular disclosure item to a component of the Part 4 purpose statement.
36. The limbs of the purpose statement - s52A(1)(a)-(d) - essentially represent the characteristics of competitive markets that regulation should attempt to replicate to promote the long-term benefit of consumers. The Commission's focus in developing new Disclosure requirements should, therefore, be on developing appropriate evidence-based information and metrics that enable assessment of performance against s52A(1)(a)-(d). This would ensure competitive market outcomes are replicated that would ultimately promote the long-term benefit of consumers.
37. Overall, Vector believes that the Act represents a significant shift from the previous Part 4A that the Commission needs to take account of in developing new Disclosure requirements. While the Commission refers to the purpose statement in Chapter 2 of the Discussion Paper, it is not applied to some of its key preliminary positions. In particular, and as set out below, the Commission proposed adopting the previous Part 4A disclosure regime without considering whether all the information is still required under the new purpose statement.

### **Aligning Information Disclosures with other regulatory instruments**

38. In order to determine the minimum information required to meet the purpose statement it is necessary to consider what information is required in the context of the DPP and CPP regulatory tools available to the

Commission (these are also intended to be relatively low cost instruments as set out in section 53K).

39. In particular, unlike the thresholds regime, where information disclosure was intended to play a role in directly “promoting” the s57E Purpose Statement, the role of Information Disclosure under the Part 4 regime is more variable across different categories of regulated businesses.
40. In respect of non-exempt EDBs and GPBs, the primary means of achieving the Purpose Statement is intended to be through DPP and CPP regulation. The objective of price cap regulation is to remove the regulator from specifically making judgments on where efficiency gains can be made and setting prices accordingly (as under rate of return regulation) but using the profit incentive for non-exempt businesses to reveal their capability over time to improve their efficiency, (subject to meeting quality of service objectives) and sharing efficiency gains with consumers over time through the operation of resets.
41. These factors should also be reflected in the setting of Information Disclosure requirements. Sufficient information needs to be disclosed on non-exempt GPBs and EDBs to enable the Purpose Statement to be met in the setting of price and quality targets, but this should not include information designed to specifically identify where businesses can improve their performance. This is also reflected in the prohibition on using comparative efficiency methods for setting price and quality paths.
42. Information provided under default and customised price-quality paths also helps to meet the Information Disclosure purpose statement by providing interested parties with evidence, and a greater degree of comfort, that the purposes of Part 4 are being met. Accordingly, the Commission should design the Information Disclosure regime to meet the different requirements of exempt versus non-exempt businesses. For exempt businesses, the Commission should consider what information should be produced to enable consumer owners, or airlines to monitor performance relative to the Purpose Statement. Whereas less detailed information is required for non-exempt businesses, who are subject to incentives and sharing mechanisms that ensure that the purpose statement is met, and information disclosure is not the tool for achieving the Part 4 purpose
43. Under a CPP a supplier will be expected to provide sufficient information to the Commission in their proposal to justify their price and quality paths,

which we contend should translate to less evidence (e.g. financial, investment, quality, etc.) being required in ongoing information disclosures.

44. Vector, therefore, submits that the scope of Information Disclosures should be targeted to the relevant regulatory instrument by being less detailed as the incentive mechanisms become stronger. Dove-tailing Disclosure requirements with other regulatory instruments that suppliers face will significantly streamline the quantum of evidence required under Disclosures. This in-turn minimises unnecessary overlap and costs in preparing and auditing information. Following such an approach would align with implementation principles of cost effectiveness and flexibility as well as being fit-for-purpose.

**The Part 4A regime should not be applied to the new regime without detailed analysis of the extent the requirements still apply**

45. As referred to above, the Commission has formed the preliminary view that the Part 4A disclosure regime will continue to be applicable for EDBs ("albeit in a different form or established on a different basis"). The Commission simply states that it has "reviewed the disclosures under the current disclosure requirements for EDBs in light of the new purpose statements" but does not explain the basis for this review or the analysis applied. It goes on to say that the Part 4A disclosure requirements were "revised recently in line with the purpose of Part 4A" implying that the Part 4A purpose statement remains relevant under the new regime. A similar position is taken in relation to GPBs.
46. In line with this preliminary view, many of the proposals in the Discussion Paper appear to be a transposition of current electricity disclosures under Part 4A. In addition, further features are added by the Commission which make the regime even more onerous.
47. Although it can be efficient and convenient for the Commission to use its learning's from the current disclosure regime to assist in developing new ones, this should not be at the expense of a reassessment of the need for each disclosure item against the new purpose statement and in the context of the regime as a whole.
48. Vector submits that the previous information disclosure should not be applied to the new regime without the Commission undertaking an in depth analysis of each particular Information Disclosure component including an

analysis of the extent to which information aligns with the new purpose statement and the regulatory frameworks as a whole.

**Information disclosure requirements are not required to show the Commission's compliance with section 54Q**

49. The Commission also considers that the areas dealt with in s54Q, which applies only to electricity distribution businesses (EDBs), are also subject to Information Disclosures too:

“The Commission must promote incentives, and must avoid imposing disincentives, for suppliers of electricity lines services to invest in energy efficiency and demand side management, and to reduce energy losses, when applying this Part in relation to electricity lines services.”

50. Vector’s opinion is that s54Q is not part of the Part 4 purpose statement and therefore does not fall under the Information Disclosure purpose statement which requires relevant information to be disclosed to show the purpose of Part 4 is met. Consequently, Disclosure requirements are not specifically required to show information on energy efficiency, demand side management or reduction of energy losses. All s54Q requires is that the Commission must provide incentives and must avoid disincentives in its application of Part 4. The Commission has not explained how requiring information to be disclosed about energy efficiency will be an effective incentive on EDBs in line with section 54Q.

## **PART C: SIGNIFICANT ISSUES**

### **Overview**

51. While Vector believes it is premature to discuss specific Disclosures in detail before input methodologies and default price paths are set, there are several significant issues raised in the Discussion Paper that justify comment at this stage. This recognises that there are only a limited number of consultation rounds and that it would be helpful to provide the Commission with at least some high-level feedback early, especially given the short consultation timeframes under the Act.
52. In this section Vector comments on the following issues raised in the Discussion Paper:
- Financial and asset statement Disclosures
  - Defining gas business units for Disclosures
  - AMP reviews and applicable standards
  - Appropriate quality Disclosures
  - Pricing Disclosures; including pricing statistics, actual prices, and pricing methodologies
  - Other Disclosures; including of contracts and policies

### **Financial and asset statement disclosure**

53. The need for various financial and asset statements needs to be reviewed to align with a new interpretation of Part 4, be fit for purpose and least cost. Vector contends that several statements could be modified or removed to achieve these aims, as discussed below.

#### *Consolidated financial statements*

54. The Commission proposes that businesses with regulated and unregulated business units should disclose 'financial' and 'asset' statements for each regulated business, and aggregated financial statements for the remaining unregulated businesses. The statements proposed include the regulatory profit statement, regulatory asset statement, regulatory tax calculation, and capex and opex forecast statement. An additional consolidation statement will also be required to reconcile the regulatory accounts to statutory accounts, including a disclosure of differences in accounting treatments.

55. Vector questions the need and benefit of consolidation statements, especially in comparison to the costs imposed on regulated suppliers. There are many practical issues with this proposal that will create complexity and cost and undermine any benefit that interested parties may have derived from such a proposal. For example, Vector's statutory accounts are as at 30 June whereas our electricity regulatory accounts are as at 31 March, creating additional complexity and cost in reconciling year-end differences. Additionally, gas regulatory accounts are published several months after electricity meaning that Vector could not produce a reconciliation statement with our electricity Disclosures as gas Disclosures would not be complete. Vector's auditors have also conveyed to us that the preparation of the reconciliation statement would be time consuming, costly, and meaningless. That is, depreciation, tax, allocation of common costs, asset values are all different under statutory and regulatory accounting and may require new accounting systems and techniques to enable the information to be prepared.
56. Overall, Vector believes the Commission should carefully consider the benefits that will be derived from consolidation statement reconciliations in light of these costs. What real or underlying purpose is achieved by preparing such statements, and accordingly, are there alternative options that may deliver what is being sought more cost effectively. If adopted, Vector proposes that the reconciliation statement be qualitative - where reconciliation can be discussed in broad terms where high materiality thresholds apply (e.g. suppliers would not be required to discuss any differences of less than \$1m on any line item). Furthermore, there is an obligation in 53(D)(2) that these statements only provide the detail required to meet the purposes of 53D, so this detail should be minimal.
57. Consolidation statements are also only for the purpose of the Commission monitoring compliance with Disclosure regulation (see 53D(1)). Other interested stakeholders are not specifically mentioned in this section, so these statements, if required, should only be disclosed to the Commission on a confidential basis. Confidentiality will also be important for complying with securities regulation as listed businesses are required to disclose all new information to the market. Further complications would arise if a party requested this information under the Official Information Act as we would have to disclose it to the market not just the party that requested it, so more stringent confidentiality requirements would be required.

*Forecast statement*

58. The Commission has proposed that capex and opex forecasts and reconciliations of actual expenditure against previous forecasts should be

disclosed in the AMP. In our reading of the Discussion Paper we are uncertain as to whether the Commission requires this as a separate statement along with annual financial Disclosures, as is currently the case for electricity (statement AM1). In the interests of cost effectiveness and minimising duplication, Vector considers that an AM1 type forecast statement in annual Disclosures should be removed in favour of disclosure of these forecasts solely within the AMP. Opex and capex forecasts already naturally sit in the AMP, where they are informed by relevant detail on forecasting and how assets are managed.

59. In addition, Vector is strongly of the view the Commission's proposed use of the Securities Regulation 1983 prospectus-information assurance-standards for opex and capex forecasts<sup>6</sup> is unwarranted. This level of assurance would mean that auditors would need to assess all assumptions used in the AMP related to forecasting, which we believe would be far too onerous. Further, these assurance standards are designed to give potential investors a high level of comfort over the forecasts they rely on to make risk-based investment decisions. We do not consider that such a high level of assurance is required for interested parties to assess forecast information against the purposes of Part 4. It is also unclear, of what value audited forecast information will be for DPP or CPP regulation. DPP regulation is not intended to be based on detailed cost building blocks information, and under CPP regulation, a supplier will be required to provide much more detailed information and certification of their future expenditure plans.

#### *Disaggregated RAB roll-forward Disclosures*

60. The Commission proposes that the RAB roll-forward should be disaggregated to an *asset-class* level in an asset roll-forward report.
61. Vector considers that this level of detail is redundant and irrelevant for interested parties to assess whether the purposes of Part 4 are met. Interested parties are not in a position to assess the meaning of different levels of investment over time in different asset-classes, given they will not understand the underlying network dynamics that drive that investment. As we note above, in respect of audit standards for AMPs, there needs to be a clear use for such information in setting of DPPs and CPPs and the information should only be made available where relevant. Vector submits that disaggregated information will not inform interested parties on whether "incentives to invest" is being promoted any better than the aggregate of capital expenditures.

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<sup>6</sup>Commerce Commission, Information Disclosure Discussion Paper, Paragraph 536.

62. To illustrate, the level of asset-class detail provided by the current asset-class RAB roll-forward report used for electricity disclosures (i.e. AV2), provides very little roll-forward information at an asset-class level (apart from the base-year ODV which appears does not change year-on-year). Vector, therefore, questions the current statement's value to interested parties and its intended use in future Disclosure requirements give asset-class information on depreciation, revaluations and net additions will not disclosed.
63. Vector also believes it would be particularly difficult to show consistent and accurate asset-class level RAB roll-forward data for GPBs without developing a new 2010 ODV and accompanying handbook. There is currently no gas transmission and distribution ODV handbook (apart from the MED draft ODV handbook that was never approved) and there is likely to be significant disparity amongst Vector, Powerco, MDL and Gasnet in approaches to defining and valuing assets. As a result, asset-class specific roll-forward data, (e.g. depreciation) could not be disclosed consistently meaning any comparison would be meaningless.

#### *The role of audit*

64. The Commission generally views the disclosure of calculations and workings (e.g. regulatory tax calculation) as important in providing interested parties transparency and comfort that Disclosure requirements are being complied with. However, in support of the ENA view, Vector believes an independent audit affords sufficient *comfort* to the Commission and other interested parties over compliance and the audit statement provides *transparency* over this compliance. Further, any detailed calculations and workings appear superfluous in light of the role of audit as this information is not required to show the purpose of Part 4 is being met. If the Commission removed such detailed information requirements and relied on the audit, it would rationalise Disclosures and make it easier for interested persons to 'break through' the detail and access information that is more pertinent to assessing performance against the Part 4 purpose. This would provide for more targeted and 'fit for purpose' Disclosures that would align with the implementation principle of cost effectiveness.
65. A good example is the regulatory tax calculation. The proposed level of detail for this statement is not required, in our view, for an interested person to assess performance against the purpose of Part 4. Vector recommends that regulatory tax should only be required in the regulatory profit statement as a line-item. This would be sufficient to show performance against the purpose statement, whereas the audit could be

relied on to demonstrate compliance. Vector would extend this argument that detailed calculations and workings should not be required for the RAB roll-forward statement either.

### **Defining business units for Disclosures**

66. There are various issues raised in the Discussion Paper related to how Disclosures are to be disaggregated by business units and non-contiguous networks, which have a particular impact on Vector's GPBs. Further, there is still some uncertainty over the scope of our regulated GPB, which we wish to address.

#### *Separate transmission Disclosures*

67. The Commission has proposed that there should be separate Disclosure requirements for gas transmission and distribution businesses. Vector agrees with this proposal on the grounds that the two types of networks have unique business and operational drivers and assessing performance against the Part 4 purposes is likely to require different information. However, we extend this proposal by submitting that transmission Disclosures (for MDL and Vector Transmission) should be bespoke, in a similar manner to Transpower's, in recognition that transmission businesses have unique characteristics compared to distribution businesses.
68. For example, Disclosures designed for comparison purposes between GPBs (e.g. Statistics, AMP reviews etc). are redundant for the purpose of comparison between gas transmission and distribution given these differences. That is, Vector Transmission's pricing structure is completely different to our gas distribution business, recognising different consumer types and their requirements. Any comparison would be meaningless and, as a result, Disclosure requirements for transmission can be significantly more concise. Comparison metrics may also be unnecessary between Transmission providers as Vector Transmission and MDL are both very different businesses (e.g. in terms of pricing, size, coverage, capacity, geographic reach etc.) and their performance cannot be effectively compared.

#### *Non-contiguous networks*

69. The Commission has proposed that quality and statistics Disclosures should be separately disclosed for each non-contiguous distribution network, subject to a size threshold. The stated reason is the supposed risk of one

network potentially subsidising another network or quality being compromised in one network in favour of another.

70. Vector disagrees with the reasoning behind this proposal and, therefore, with the need to make Disclosures by non-contiguous network. In our view, it would be impossible for interested parties to determine whether subsidisation was occurring between non-contiguous networks using the proposed pricing statistics, and in any case there are a variety of reasons why pricing may be different in one region over another (e.g. different costs, quality, network design). The proposed pricing statistics are merely average unit-prices based on aggregated load groups so any assessment does not reflect actual prices or how they are set.
71. Instead, pricing methodologies are more adept in demonstrating to interested parties that prices are efficient. As discussed further below, Vector supports the use of Gas Authorisation type pricing-principles under a principle-based pricing methodology approach. One of these principles is that efficient prices should be subsidy free being between incremental cost and stand-alone cost. Showing compliance with this pricing principle in the pricing-methodologies disclosed under Information Disclosures (as we propose in our input methodology submission) will best show prices are efficient between different regions and customers. In comparison, the use of pricing statistics by non-contiguous network is unable to achieve this.
72. Furthermore, disclosure of quality statistics by non-contiguous network would also not show, in itself, that quality is being compromised on one network over another. A network may naturally have higher or lower reliability linked to external influences (e.g. higher prevalence of third-party damage), natural events, historical design flaws in the network, or network age (e.g. newer networks less prone to failure). This information could not be detailed in simple metrics but AMP Disclosures may provide more relevant information on differences in quality and should instead be relied on.
73. If the Commission decided to adopt non-contiguous network quality and statistics Disclosures, Vector submits that our gas transmission and distribution networks are combined physically meaning all our individual distribution networks are *contiguous* by the transmission system. Therefore, separate disclosures should only be required for Vector Gas Transmission and Distribution (in addition to that already required under the Gas Authorisation for the controlled Auckland network until 2012).

### *Administration of gas balancing services*

74. In the Discussion Paper, the Commission proposed that administration of gas balancing services should be included in the regulatory definition of a GPB and disclosures should include this service. Vector does not view these services to be purely a gas transmission business function, nor does it believe competition is sufficiently limited for this service for it to be regulated under Part 4 of the Commerce Act. Fundamentally, the provision of gas balancing services is a contestable unbundled function that could be undertaken by a party that is separate from the Transmission System Owners (TSO), and paid for by shippers. Indeed, this is Vector's preference.
75. Balancing is effectively an externality on the transmission system caused by the interaction of shippers and consumers. The transmission system requires minimal balancing if shippers meet their obligation to balance (i.e. inject sufficient gas to meet their demand). For this reason, the GIC, who is charged with developing new improved gas balancing arrangements, has determined, based on the "causer-pays principle", that all users hold the primary responsibility for balancing. TSOs responsibilities will be of a merely residual nature, when physical actions are taken to restore balance.
76. The GIC's preferred approach to transmission balancing is a regulatory approach – the 'participative regulatory' option. This option explicitly allows for the appointment of a balancing agent - separate from the TSOs – which will undertake balancing actions through the purchase and sale of balancing gas across the transmission system. In accordance with the efficiency criteria contained in the Government Policy Statement on Gas Governance and the criteria in the Gas Act 1992 (especially section 43 ZN), the GIC is under an obligation that its rules or regulations ensure that balancing actions are undertaken in an efficient manner. This means that the TSOs, or the GIC if the TSOs cannot agree, will be required to appoint the balancing agent under a contestable process. Consequently, competition for this service would not be limited and would not need to be regulated under Part 4 of the Commerce Act. This is analogous to the contestable nature of the Electricity Transmission System-Operator role or the fact that embedded electricity networks are unregulated due to a similar contestable process.
77. Vector considers that any costs that a TSO incurs due to the regulatory obligation to assist remedying a residual balancing situation created by shippers could alternatively be viewed as pass through costs for regulatory purposes, similar to Transpower charges for EDBs.

## AMP Disclosures

### *AMP reviews*

78. The Commission has proposed to regularly review AMPs to allow interested persons to “assess the efficiency of regulated suppliers investments, in terms of purpose statements 52A(1)(a) and (b)”<sup>7</sup>. This will include a performance indicator that will rank regulated suppliers AMPs. The review and performance indicator will consider investment and innovation, efficiency improvement and quality for all regulated suppliers, in addition to energy efficiency, demand side management and loss reduction for EDBs.
79. As discussed in Part A on the Regulatory Framework, the key defining words in the first two parts of the Part 4 purpose statement is “**that suppliers have incentives**”. The Act therefore does not envisage the Commission judging the *efficiency* of regulated suppliers asset management investment decisions in AMPs, rather it requires the Commission first to develop regulation that provides real incentives and to provide evidence to interested parties in Disclosures that regulated suppliers are responding to these incentives. If real incentives exist the Commission would not need to heavily scrutinise suppliers’ investment decisions via AMP reviews and performance indicators as suppliers seek to benefit from enhancing their capital management practices in the context of meeting regulated quality standards.
80. Vector, therefore, disagrees that AMP reviews and performance measures should measure the *efficiency* of suppliers’ investment decisions. They should instead report on AMP procedures and policies and how suppliers have increased their activity in investing, innovating, and improving efficiency in response to real incentives introduced under Part 4 regulation.

### *Use of AMP standards*

81. In Vector’s view, the Commission’s apparent future desire to adopt AMP standards, such as PAS55, is concerning. The Commission’s primary role in developing Disclosure requirements for AMPs is not to specifically mandate prescriptive AMP standards but to ensure interested persons have the necessary information to assess whether regulated suppliers have incentives to innovate and invest etc. Vector has assessed the use of PAS55 in a recent review of our AMP and decided that it was not necessarily any better than other standards but it involved considerably higher compliance and accreditation costs to meet the standard. The fact that this standard

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<sup>7</sup> Commerce Commission, Information Disclosure Discussion Paper, 29 July 2009, Paragraph 432

has been used in other jurisdictions by other regulators does not automatically mean that it is the most efficient way of exhibiting professionalism in managing assets in New Zealand. Most suppliers incorporate standards into their AMP development and have a number of recognised professionals (chartered and professional engineers) engaged in the management of network assets and the business. The Commission needs to undertake a cost-benefit analysis of this proposal, recognising the potentially significant imposition of costs (relative to the small size of New Zealand network businesses) relative to the benefits.

### **Appropriate quality disclosures**

82. The Commission has asked for feedback on a number of reliability, 'supply quality', and 'customer service' quality measures as well as the process for determining consumer demanded quality developed under consumer engagements in AMPs. Taking a step back from this detail, the second strand of the Part 4 purpose statement comments on quality by recognising that suppliers should "have incentives to ... provide services at a quality that reflects consumer demands" (s52A(b)). It, therefore, seems salient that quality Disclosures are based on reporting measures that reflect quality that consumers actually demand and how successfully suppliers deliver to those demands in response to quality based incentives regulation. The proposed consumer engagement process in the AMP, therefore, seems like a particularly important mechanism for quality Disclosures.
83. However, the suggestion that requisite quality should feed into the development of operational quality targets in AMPs is at odds with the separate quality thresholds developed under DPPs. Suppliers should align their operational quality targets with regulatory targets for consistency so developing new targets in the AMP would be inconsistent.
84. A more usefully arrangement consistent with the overall regulatory system would be for suppliers to undertake consumer engagement prior to the DPP reset to measure requisite quality that could inform how quality incentives and targets should be reset under DPPs. That is, if consumers were generally unhappy with the level of quality this could be taken into consideration by setting consistent price and quality paths to deliver service quality at the level consumers demand. In a similar way, consumer engagements could provide evidence under CPPs requests too for alteration of price and quality paths.

85. Consumer engagement is very expensive to undertake, however, so if it was done only once a regulatory period, as suggested above, it would significantly improve cost effectiveness.

## **Pricing Disclosures**

### *Pricing Statistics*

86. The Commission has proposed that regulated suppliers should provide pricing statistics by aggregated consumer-class and non-contiguous network. These would be calculated by dividing the gross income from each group by the total units creating an average unit price for each major consumer class and network region. The stated reason for adopting these pricing statistics is for interested parties to assess the pricing efficiency of each supplier at the customer level.<sup>8</sup>
87. As we have already discussed above, the disclosure of pricing statistics is meaningless for interested parties to assess pricing efficiency. Prices in themselves do not indicate their relative efficiency compared with other prices. This relationship is further weakened by the use of artificial averages that do not align with actual prices or how they are derived. More importantly, the Commission already recognise that efficient prices exist in a wide band between the incremental cost and stand-alone cost of offering the service<sup>9</sup>. It would be impossible, given this economic precept, for interested parties to accurately determine that prices are allocatively efficient or not by looking at prices themselves or simple customer-class average unit-prices. Efficient pricing is, therefore, best addressed in pricing methodologies as only this mechanism can cater for pricing complexity and provide assurances to interested parties over the efficiency of prices.
88. It appears the Commissions intent, rather than to demonstrate pricing efficiency, is to allow an interested party to compare average prices. Determining average prices necessitates the adoption of customer segments. The Commission has adopted customer segments for EDBs based on arbitrary capacity boundaries. This is an issue for a significant number of consumers because Vector does not have or maintain capacity information required to place consumers in one class or another. The proposed customer class definitions also conflict with other regulatory definitions, for

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<sup>8</sup> Discussion paper, Paragraph 477

<sup>9</sup> As Vector evidenced in our Pricing Methodology Report submitted to the Commission earlier this year in compliance with the Gas Authorisation

example the Low User Fixed Charge regulations, which have no capacity boundaries on the definition of residential consumers.

89. The Discussion Paper also makes specific reference to the consumer segments being considered by the Electricity Commission ("EC") under its Distribution Pricing Methodologies project. However, we note that the EC is now considering moving to a principles-based approach due to the concerns raised by a number of parties about unintended consequences of moving to a more prescriptive approach.
90. Overall, for the above reasons, pricing statistics should be abandoned in favour of the disclosure of pricing methodologies and actual prices (as discussed in more detail below).

#### *Disclosure of actual prices*

91. Vector supports the disclosure of actual prices but the requirement should be limited to standard consumers as non-standard consumers already receive disclosure of prices through their contracts and exert countervailing power in negotiating prices and non-standard arrangements. Furthermore, public disclosure of non-standard contracts would breach the confidentiality of individual non-standard consumers.
92. Vector strongly disagrees, though, with the Commission's proposal that actual price Disclosures should be notified to every standard consumer by which the charge is payable (question 72).<sup>10</sup>
93. Firstly, most gas and electricity distribution businesses have interposed relationships with retailers who themselves have the contractual relationship with end consumers. This relationship allows retailers to re-bundle distribution charges to end consumers and choose when they pass-on distributor price changes. Any subsequent disclosure by distributors would only serve to confuse consumers as the prices charged by the distributor to the retailer may not reflect the charges allocated to consumers.
94. Secondly, we believe that the proposal doubles up on existing provisions under the Electricity and Gas Complaints Commission (EGCC) code of conduct, which contains similar provisions for price changes in excess of 5% for gas and electricity. Under interposed retailer relationships, Vector does

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<sup>10</sup> We interpret this to mean that each consumer needs to be individually informed as opposed to relying on web-site disclosure or mass marketing.

not have access to end-consumer information in order to notify individual end-users so we contractually place this obligation to notify price changes under this code to retailers. However, under conveyance relationships we have had to pay retailers to put inserts in bills, which has been very costly, in the order of several hundred thousand dollars, so the Commission would need to provide for such a cost in pass-through costs or in setting the DPP.

### *Pricing Methodology*

95. Vector has submitted on pricing methodologies in our input methodology submission and the Commission should refer to this for more detail. We note, though, that there have been significant developments in this area by the EC and the Commission may need to reassess its position after reviewing submissions and communicating with the EC.
96. However, to summarise our position from our input methodologies submission, Vector supports the Commission's adoption of a principle-based approach to pricing methodologies for both electricity and gas businesses with compliance shown through Information Disclosures. In our view, Gas Authorisation type pricing principles are appropriate for all GPBs and could also be extended to electricity.
97. Vector supports the Commission's suggestion in both the Input Methodology<sup>11</sup> consultation and the Discussion Paper that "departures from"/"compliance with" pricing principles should be disclosed in Information Disclosures. This seems more appreciative of the weighting of the costs and benefits of regulated pricing methodologies and low cost nature of the DPPs and CPPs. Vector envisages a statement within the pricing methodology document, published under Disclosures, describing the extent to which distributors have "complied with" the pricing principles in developing their pricing methodologies. In our view, this level of detail should be appropriate for monitoring purposes for both the Commission and the EC. The latter could adopt a similar approach to the Commission's AMP review process for its own purposes.
98. Going forward, these Disclosure statements should *only* be updated when distributors have materially changed pricing structures and cost allocation methodologies. That is, re-disclosure should not be required simply due to an annual price change (e.g. that reflects continuation of a distributor's existing methodologies). This approach would significantly minimise

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<sup>11</sup> Commerce Commission, *Input Methodology Discussion Paper*, paragraph 11.104.

transaction costs for distributors and for the two regulators in terms of compliance and verification.

## **Other Disclosures**

### *Prescribed Contract Disclosures*

99. The Commission's preliminary view is that contract terms and conditions should be publicly disclosed within one month of taking effect and should include information on service description, quantity, price, payments and modifications to terms and conditions. Any such Disclosures should not compromise commercial confidentiality, though, in respect of any one customer. Further, director certification is no longer required.
100. The disclosure of prescribed contracts, in our view, is not suited to the DPP/CPD regulatory regime, where prices are capped and suppliers are required to demonstrate their prices conform to a set of pricing principles. Disclosure of prescribed contracts is more suited to a "light-handed" or monitoring regime, and even there it is highly questionable, whether the information proposed provides any meaningful information to consumers.
101. If Vector had to comply with the proposed approach we estimate that over the course of a year, the Commission could receive information on in excess of thousands new contracts, from Vector alone.
102. It is unclear to us what use this level of detail would be to the Commission and interested persons in assessing the performance in line with Part 4. If all EDBs, GPBs and airports disclose detail of thousands of contracts to the Commission each month we suspect that the Commission and other interested parties would not have enough resource to efficiently review these Disclosures. Further, in our experience no party has ever requested such information from us under previous Disclosure regimes where contracts were disclosed on request, suggesting there is either few interested parties or reviewing the level of detail is too onerous a task. Many suppliers also provide end-consumers with an overview of standard connection terms and conditions when they connect, which we believe to be sufficient. Ultimately, Vector submits that prescribed contracts should not be required under Information Disclosures for the above reasons.

### *Policy Disclosures*

103. The Commission has proposed the disclosure of policies that have the potential to affect the profitability or financial viability of a regulated business, including:
- Credit Policy
  - Delegate Authority Policy
  - Profit Distribution Policy
  - Sponsorship Policy
  - Insurance Policy
104. Vector considers that disclosure of these policies is unwarranted and unnecessary under the Act. These requirements stray into businesses providing details on their operational practices and suggests that the Commission or other parties will want to review or provide input into the operational decisions of the business. While that would be appropriate under a rate-of-return type regulatory regime, incentive regulation under DPP or CPP arrangements, is designed to leave businesses to enhance their efficiency over time in the pursuit of improved financial performance under the price path, and remove the regulator from making judgments on how a business should conduct its business.
105. We also do not believe that disclosure of the proposed policies will show that the purposes of Part 4 are being met. That is, they do not comment, in themselves, on incentives to invest, innovate, improve efficiency and provide consumer demanded quality, or on how efficiency gains are shared with consumers or a supplier's ability to extract excess profits. In summary, Vector does not agree any of these policies should be disclosed.