



**Submission on the Commerce Commission's  
Initial Default Price-Quality Path for Gas Pipeline  
Businesses: Discussion Paper**

**27 May 2011**

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## INTRODUCTION

1. Vector welcomes the opportunity to make this submission on the Commerce Commission's ("the Commission") Initial Default Price-Quality Path ("DPP") for Gas Pipeline Businesses ("GPBs") Discussion Paper.
2. Vector's contact person in relation to this submission is:  
  
Ian Ferguson  
Regulatory Advisor  
Tel: 09 978 8277  
Email: [Ian.Ferguson@vector.co.nz](mailto:Ian.Ferguson@vector.co.nz)
3. Accompanying this submission is a separate submission on Gas Transmission Asset Investment Issues, which proposes a Regulatory Investment Test ("RIT") within the DPP to enable efficient and timely investment in gas transmission infrastructure, as and when required.
4. We commend the RIT approach to the Commission as a Customised Price-Quality Path is an inefficient way of approving major gas transmission investments. The RIT will provide sufficient flexibility and certainty for gas transmission businesses ("GTBs") that they can recover the costs of their investments and undertake the investments in a timely manner, while providing surety to the Commission that only reasonable and prudent investments will be undertaken.

## EXECUTIVE SUMMARY AND RECOMMENDATIONS

### *Form of control*

5. Vector agrees that a weighted average price cap should apply to its gas distribution business ("GDB").
6. Vector considers that a revenue cap should apply to its gas transmission business. This is a shift in position from our previous preliminary view. However, we consider that a revenue cap better suits the circumstances of Vector's transmission business and is materially better at achieving the Part 4 Purpose.
7. Unlike electricity or gas distribution, gas transmission networks are reliant on a small number of very large customers and GTBs have no control over their entry or exit to the market. This is true for Vector, even under what is often labelled as contract carriage arrangements.
8. The Commission has stated that a contractual regime should provide Vector with the ability to control access to, and demand on, its system by offering bi-lateral non-standard terms. However, for customers on the Vector Transmission Code, the contracting regime closely resembles a common carriage approach. Whilst it is possible to enter into new contracts for those customers that are currently un-contracted, transmission customers are generally large and typically possess countervailing power when negotiating contractual agreements.
9. Further, significant factors driving demand on Vector's transmission network are beyond Vector's control making it subject to a high degree of uncertainty.
10. These factors make it more difficult for Vector as a GTB to have confidence that its revenue requirements will be met. A revenue cap will better mitigate this risk than a price cap, thus incentivising investment. A contract carriage regime does not reduce the risk significantly.
11. A revenue cap better meets the Part 4 Purpose because under a price cap arrangement:
  - a) Major customers may exit the market, reducing the ability of a GTB to recover costs of an investment and earn at least a normal return (inconsistent with section 52A(1)(a)); or
  - b) Major customers may enter the market on an unconstrained pipeline, increasing revenues of the GTB above those necessary to fund investments and earn at least a normal return (inconsistent with section 52A(1)(d)).

12. It is also important to recognise that Vector is not inextricably bound to a contract carriage regime. It would be difficult to operate a common carriage regime under a weighted average price cap due to the investment and revenue risks. The Commission should be careful not to lock Vector into a particular contractual regime through its choice of the form of control.

#### *Quality standards*

13. Vector supports response times to emergencies ("RTE") as the sole quality standard for the first regulatory period for both GDBs and GTBs. RTE is an important safety-related indicator that is relatively straightforward to measure. We particularly welcome the decision not to use SAIDI as a quality standard due to the lack of relevance of this measure to GPBs.
14. Vector submits that only the RTE standard should be reported through the price-quality compliance statement. The Commerce Act anticipates that quality standards will be meaningful targets with penalties applied for non-compliance. Where information only is being required, the appropriate form for that information to be provided is information disclosure.
15. In relation to compliance requirements, Vector recommends that the Commission introduce a "two out of three" rule, as is currently in place for electricity quality standards, where a GPB would only be in breach of the quality standards if targets were missed in two out of every three years. Vector also recommends some changes to the Commission's proposal on the timing thresholds for the standards.
16. In relation to the quality information reporting requirements, Vector submits that some of the requirements are of limited relevance to the operation of a GTB and / or are excessive. These requirements will result in substantial cost (to prepare, audit and publish) but with limited, if any, benefit in terms of the purposes of the Act
17. For gas distribution businesses, Vector:
  - a) supports the reporting of information on publicly reported escapes, outage events, outage events caused by third party damage, leaks and SAIFI; and
  - b) Does not support the reporting of information on the other quality measures for GDBs suggested by the Commission (e.g. poor pressure, SAIDI, unaccounted for gas). These do not provide a true indication of quality on gas distribution networks and the cost of gathering and reporting the data to auditable standards is not a good allocation of resources.
18. In terms of the capacity information proposed for GTBs, Vector is happy to provide the Commission with the information it requires to determine if the purpose of

Part 4 is being met. However, it is not clear that the information listed will achieve that aim. Vector recommends that the Commission meet with GTBs to discuss the requirements for capacity-based information to identify what is required and what can be provided.

19. Whatever measures are audited must be accompanied by clearly set out materiality standards for accuracy and completeness. Vector has experienced significant difficulties with the audit of our gas quality information due to unrealistic auditor views of the required data accuracy.

*Other matters*

20. Vector strongly supports the Commission's view that claw-back need not be applied to Vector's controlled or non-controlled GPBs as there is no risk that their prices will increase by more than CPI until the start of the new regulatory regime.
21. Vector welcomes the Commission's decision to align the pricing and regulatory years of the majority of GPBs. However, we consider that a partial compliance period from 2 July to 30 September 2012 is unnecessary. Vector has no intention of raising its prices within that period and no sensible business would take the reputational and regulatory risks inherent in such actions.
22. Vector recommends that the Commission does not make a starting price adjustment for the first regulatory period. The quality of data available means it will be difficult to make robust starting price adjustments for GPBs in 2012 (even with allowance for error). A better approach would be for the Commission to gather the necessary data over the first regulatory period and then consider making starting price adjustments in 2016. The Commission's statement that it must set prices under section 53P(3)(b) because there is no preceding regulatory period on which to base prices is simply incorrect – the Commission appears to have overlooked the provisions of section 55F(1).
23. Vector supports the Commission's view that the X-factor for the first regulatory period should be zero and there is no need to undertake further work on the rate of change for the 2012 reset.
24. Vector does not support the provisions of the full list of information the Commission has identified for future TFP studies. Approximately 140 separate data lines for gas distribution and approximately 90 for gas transmission are excessive and unnecessary when TFP studies can be carried out at an aggregate level.
25. Vector also suggests a revision of the definitions of gas transmission business and gas pipeline business in both the DPP and the IMs.

## **PART A: FORM OF CONTROL**

### **FORM OF CONTROL FOR GAS DISTRIBUTION BUSINESSES**

26. The Commission proposes that a weighted average price cap will apply to GDBs.
27. Vector supports this proposal. A weighted average price cap form of control is appropriate for the gas distribution sector.

### **FORM OF CONTROL FOR GAS TRANSMISSION BUSINESSES**

28. The IMs provide that either a revenue cap or a weighted average price cap may apply to GTBs.<sup>1</sup> The Commission's current view is that a revenue cap is appropriate for MDL and a weighted average price cap for Vector.

#### ***Vector's preference is for a revenue cap***

29. Vector considers that a revenue cap should be applied to its gas transmission business. We have reached this view on the basis of recent business analysis and ongoing industry developments, combined with our assessment of the price formulae proposals put forward by the Commission.
30. In our previous submission on the form of control for gas pipeline businesses<sup>2</sup>, Vector argued that GPBs should have the option to choose between a weighted average price cap and a revenue cap. We also noted that Vector was unable to make a choice between the price cap and revenue cap options on the basis of the information that was then available. However, Vector did indicate that its preliminary view was a preference for a weighted average price cap.
31. Vector also put forward a series of arguments against the Commission's then views that both GTBs must necessarily be subject to the same form of control and that a revenue cap was necessarily better suited to Vector's gas transmission business.
32. Vector has further assessed the nature of its gas transmission business and has re-considered the suitability of the different forms of control. Vector's firm view (no longer preliminary) is that its gas transmission business should be subject to a revenue cap.
33. This view has also been informed by Vector's desire to avoid a situation which hampers its ability to address pipeline constraints due to uncertainty regarding the

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<sup>1</sup> *Commerce Act (Gas Transmission Services Input Methodologies) Determination 2010*, clause 3.1.1(1).

<sup>2</sup> *Vector submission on Gas DPP Issues Paper – Form of Control*, 30 April 2010.

ability to receive a return on investments. The capacity issues on Vector's North Pipeline bring this issue into sharp focus. The specific reasons for supporting a revenue cap are set out in further detail below.

***A revenue cap is more consistent with the Part 4 Purpose***

34. The Commission is obliged to set the form of control for gas transmission businesses to promote the Part 4 Purpose. Vector considers that a revenue cap arrangement better promotes the Part 4 Purpose, notably the objectives set out in section 52A(1)(a) and (d), than a weighted average price cap.
35. Unlike electricity or gas distribution, much of the capacity on Vector's transmission system is used by relatively few customers (for example, 65% of the capacity from Rotowaro North is used by 3 customers: Otahuhu B, Southdown and NZ Steel). GTBs have very little (if any) control over whether users of this scale enter or exit the market.
36. Under a weighted average price cap the gas transmission market structure creates two risks:
  - a) If a major customer exited the market the GTB would earn insufficient revenues to earn at least a normal return on its investment (at least until the next price reset). With this risk, it would be less willing to make investments<sup>3</sup>. This would be inconsistent with section 52A(1)(a).
  - b) If a new large customer enters on an unconstrained pipeline, creating a large uplift in revenues for the GTB without requiring them to carry out (much) further investment, the GTB may be able to extract excessive profits. The GTB could earn more revenues than it requires to earn at least a normal return on its network (at least until the next price reset). This could be inconsistent with section 52A(1)(d)
37. Vector, in general, would be more likely to be willing to make new investments in our gas transmission business under a revenue cap than under a price cap as a revenue cap is materially better at mitigating the risk that we may not be able to meet our revenue requirements.
38. In support of this analysis, we discuss in more detail below why a revenue cap is more suitable for Vector's gas transmission business.

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<sup>3</sup> At least unless the GTB is compensated for the additional risk through an increased WACC.

### ***Future Flexibility***

39. It is important to recognise that Vector is not inextricably bound to its current carriage regime and the needs of the gas market are changing, which means flexibility to adjust pipeline arrangements is important. To list some examples:
- a) Maui open access has been embedded;
  - b) Alternative gas fields have come on line;
  - c) significant end-user plant is aging and in a number of cases is struggling with variations in the gas specification;
  - d) changes to pricing methodologies are being developed to better signal scarcity and encourage trading; and
  - e) large investments in pipeline infrastructure may be required in future if there are persistent constraints.
40. Vector considers that it would be difficult to operate a common carriage approach under a weighted average price cap as it increases GTBs' risks of failing to raise sufficient revenue to meet investment requirements, particularly given the market changes that are underway. Any future move by Vector to common carriage would be better supported through a revenue cap regime.
41. It would be prudent for the Commission not to construct the DPP to exclude the possibility of an alternative regime (including in transitional steps over time) and to allow for market change.

### ***Contract carriage arrangements provide little additional ability for a GTB to manage consumer demand***

42. The IMs set out two criteria<sup>4</sup> to be taken into account when determining whether a weighted average price cap or a revenue cap will apply. These are:
- a) the extent to which capacity is managed through contract carriage arrangements (as opposed to common carriage arrangements); and
  - b) the extent to which the GTB supplies services on the basis of non-standard pricing arrangements.
43. The IMs do not stipulate how these criteria must be used in determining whether a weighted average price cap or a revenue cap will apply and the Commission has stated that a matter of judgement is required on their part when applying these criteria.
44. Vector submits that these criteria must be considered in light of how Vector's transmission network actually operates. As explained below, for Vector the contracting regime closely resembles a common carriage approach where Vector

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<sup>4</sup> *Commerce Act (Gas Transmission Services Input Methodologies) Determination 2010*, clause 3.1.1(2).

has very limited ability to set prices and influence demand outside of existing contractual terms. We note that the Commission is required by the IMs to take these criteria into account but the IMs do not prevent the Commission from considering and placing greater weight on other, more relevant, criteria.

45. Vector understands that a GTB's ability to control access to, and capacity/volumes of gas shipped on, its network might be relevant when determining which cap is the most appropriate. Accordingly, Vector considers that the substance of its service arrangements, taken in context with how those arrangements operate, is the most useful criterion. Conclusions based on the theory of contract versus common carriage, which the above criteria appear to be more focused on, are less useful.
46. Vector acknowledges that, in contrast to MDL, it operates a carriage regime that is often labelled as contract carriage – in fact it is not a pure contract carriage regime, but more of a hybrid arrangement. The Commission has stated that this contractual regime provides Vector with the ability to control access to, and demand on, its system by offering bi-lateral non-standard terms. In theory this would be correct if Vector operated a pure contract carriage regime, consisting only of bi-lateral agreements and in the absence of open access and any regulatory overview (including by the Gas Industry Company ("GIC")). However, in practice none of this is true. The context in which Vector operates means that the contract and common carriage labels do not translate into material differences in the ability to influence the presence or absence of demand or service terms.
47. Significant factors driving demand on our transmission network are beyond Vector's control, making it subject to a high degree of uncertainty. These include:
  - a) Vector operates an open access system. Interconnection terms are posted and the GIC has recently re-affirmed its view, through its Interconnection work stream, that interconnection rights must be granted to a party that is able to meet reasonable terms of interconnection. So Vector may not have the final say on whether a load is connected to its system.
  - b) Transmission terms are set out in the Vector Transmission Code ("VTC"), which is an industry negotiated code that can only be changed by industry agreement and/or determination by the GIC based on Gas Act and Government Policy Statement objectives.
  - c) Several service offerings are available and the terms for these are all covered by the VTC. Presently, the standard offering is Reserved Capacity which is available for a year and able to be grandfathered for the next year if the Shipper desires that. Term arrangements (e.g. 2 or 3 year contracts) for Supplementary Capacity can be entered into with Shippers for specific end users provided the terms of the VTC and Vector's

Supplementary Capacity Policy are met. However, a strong case must be made for this variation and the contract terms for these arrangements are not able to be varied greatly<sup>5</sup>. Vector does not lead the offering of Supplementary Capacity on a term basis. Shippers do this and are largely motivated to align the term of their transmission arrangements with their end user and energy supply contract, allowing for the back-to-backing of arrangements.

- d) The entities involved in these Supplementary Capacity discussions are large and hold significant countervailing power. Therefore, Vector's customers ensure that the prices for Supplementary Capacity are indeed heavily negotiated.
- e) The addition of, or reduction in, load is therefore the product of other parties' initiatives rather than Vector's.
- f) At the wholesale level transmission costs are currently in the vicinity of 13% of the wholesale gas price. At the retail end-user level they are approximately 2%. As a result, factors other than transmission costs tend to determine whether a project continues to completion or not<sup>6</sup> – for example, the economic climate, the regulatory environment, companies' own commercial interests and the New Zealand Energy Strategy.
- g) Even amongst those loads that remain on the system, significant variability in demand can arise as a result of the weather or the changing nature of an asset within a Shipper's portfolio. By way of example, a significant drop in throughput can and has occurred with the varied operation of Otahuhu B, Southdown and TCC. Otahuhu B and TCC are no longer being operated as base load stations; and this may change again if the portfolios of the major generators change in the future. The Commission itself notes the difficulty of forecasting demand accurately<sup>7</sup>.
- h) As noted above, the majority of throughput on Vector's gas transmission system resides with a small number of end users – for example, Otahuhu B, Southdown, Taranaki Combined Cycle, Stratford plant and storage, NZ Steel, Fonterra, Carter Holt Harvey and NZ Refining Company. The exit of any one of these users will have a significant effect on demand and therefore, capacity. The commercial nature and operation of these large end users means supply cessation is a genuine and present risk to Vector.

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<sup>5</sup> Section 2.7 of the VTC: [www.oatis.co.nz](http://www.oatis.co.nz)

<sup>6</sup> Unless the project would create new demand for gas that would require new investment in order to supply it – in these instances the cost of gas transmission could be substantial.

<sup>7</sup> Paragraph 5.43 of the Discussion Paper.

- i) For large loads such as electricity generation plant there is competition between gas transmission and electricity transmission (i.e. the loads have the choice of locating in Taranaki and transporting electrons to their customers over Transpower's network; or they could locate close to the demand and pipe gas to their plant from Taranaki).

48. In summary, the context in which Vector's gas transmission business operates means it has almost no ability to control demand (despite the contract carriage label) and as a result it is difficult for Vector to have confidence that its revenue requirements will be met.

### ***Geographic dispersal***

49. The Commission contends<sup>8</sup> that because Vector's gas transmission system covers a large geographical area and because it delivers smaller volumes to a (relatively) large number of delivery points, a weighted average price cap is the most appropriate form of control.

50. Vector does not agree that the geographically disperse nature of its network means that a weighted average price cap is necessarily the appropriate form of control. Vector notes that, similar to MDL, it has a high fixed cost base made up of significant investment in sunk assets. Similar to MDL, under a weighted average price cap Vector is exposed to demand variability which may result in insufficient revenues to recover costs. A revenue cap is an appropriate means of managing that risk.

### ***Incentive effect of a revenue cap***

51. A revenue cap does not remove a pipeline owner's incentive to 'protect' and grow demand. If an owner simply puts up prices when load exits the system so as to recover the allowable revenue, further load may be lost as the economics of gas use will change to the point that further players may exit the market. Therefore a GTB must be careful in adjusting prices when volume changes to avoid a "race to the exit".

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<sup>8</sup> In paragraph 4.40 of the Discussion Paper.

## **PART B: QUALITY STANDARDS**

### **QUALITY STANDARDS: GENERAL COMMENTS**

#### ***Response time to emergencies – general comments***

52. The Commission considers that only one quality standard will be set for the initial regulatory period. This will be response times to emergencies (“RTE”) for both GDBs and GTBs.
53. Vector supports RTE as the single quality standard for the initial regulatory period, with the proposed threshold adjustments set out below. We note there are only two quality standards for EDBs and consider that two standards should apply to GPBs from the second regulatory period.
54. In addition, we recommend the Commission limit the scope of its information requirements. The broad suite of information the Commission proposes to require is in some places unnecessary and overall is an excessive amount of information to report on.
55. Further, Vector recommends that the Commission introduce a “two out of three” rule, as is currently in place for electricity quality standards, where a GPB would only be in breach of the quality standards if targets were missed in two years out of every three.
56. Vector also supports Powerco’s suggestion of collecting data based on average response times as this may be a better measure of performance over time. It would incentivise GPBs to improve response times on every emergency event, not just those that may take approximately sixty minutes to reach the site.

#### ***Auditability of quality information***

57. Vector is concerned that the standards of accuracy and completeness of quality information necessary to secure an unqualified audit opinion is often materially above the standard of quality information required to run a network as a reasonable and prudent operator and generally achievable given the nature of field service work.
58. The Commission has previously acknowledged that the collection of quality related data in the gas sector historically has been poor. Issues with quality performance data was recognised in the Gas Authorisation.<sup>9</sup> Many of these issues are symptomatic of the nature of the industry. The primary focus of field staff is on

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<sup>9</sup> For example: paras 1191 and 1202 Gas Authorisation “Decisions Paper”; 30 October 2008

the identification of the fault and the safe restoration of supply - recording the specifics of the incident is, by necessity, a secondary consideration.

59. The non-financial nature of the quality data requires an attribute-based approach to the audit of quality data. In such cases the audit focus seeks to confirm the reliability of the data set with little or no regard to the materiality of any errors that might be identified. For example, a one minute discrepancy between the electronic record and the paper record in recording an outage time may be of little significance to the end user, to the overall value of the quality measure or to the compliance position. There is also often a significant degree of interlinked and interdependent information that is used to derive the measures.
60. Under the Gas Authorisation, Vector and Powerco have had to invest in far more precise systems, leading to a step change in the level of the measures being reported. The cost of recording information has now increased by \$40 per record<sup>10</sup> to improve Vector's audit performance. These costs will ultimately be felt by consumers, but we are unconvinced they will perceive any benefits.
61. Vector recommends that the Commission consults with audit firms on the nature of the auditing standards they apply to determine whether this is appropriate to the nature of the information and costs associated with materially improving data gathering processes. The Commission should also work with the industry and auditors to develop, for each measure, clear requirements for the completeness and accuracy of data for audit purposes (reported data against supporting documentation). This might result in, for instance:
  - a) consideration of the appropriate level of significance (number of decimal places) it is appropriate to report to; and
  - b) setting a materiality threshold below which data discrepancies would be discounted in compiling/auditing reported measures.

***Legislative framework does not support information provision as a quality standard***

62. The Commission proposes that GDBs also disclose a set of 14 quality measures on an annual basis. These measures are closely related to the quality measures that Vector and Powerco are required to disclose under the Gas Final Authorisation. In addition, the Commission is proposing that Vector's gas transmission business discloses a suite of capacity information as part of the quality standard.
63. The Commission appears to be proposing that these measures are disclosed as part of the annual price-quality compliance statement for the DPP. Vector

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<sup>10</sup> This cost comprises \$20 additional costs in service provider collection, quality control and administration; plus \$20 additional costs for Vector's quality assurance, audit and management.

considers that information which is not part of a quality standard should be disclosed under information disclosure only.

64. Section 53M of the Act sets out the requirements for the content of price-quality paths:

(1) Every price-quality path (whether a default price-quality path or a customised price-quality path under this subpart, or an individual price-quality path under subpart 7) must specify,—

(a) in relation to prices, either or both of the following with ...

(b) the quality standards that must be met by the regulated supplier; ...

(2) A price-quality path may include incentives for an individual supplier to maintain or improve its quality of supply, and those incentives may include (without limitation) any of the following:

(a) penalties by way of a reduction in the supplier's maximum prices or revenues based on whether, or by what amount, the supplier fails to meet the required quality standards:

(b) rewards by way of an increase in the supplier's maximum prices or revenue based on whether, or by what amount, the supplier meets or exceeds the required quality standards:

(c) consumer compensation schemes that set minimum standards of performance and require the supplier to pay prescribed amounts of compensation to consumers if it fails to meet those standards:

(d) reporting requirements, including special reporting requirements in asset management plans, if the supplier fails to meet the quality standards

(3) Quality standards may be prescribed in any way the Commission considers appropriate (such as targets, bands, or formulae) and may include (without limitation)—

(a) responsiveness to consumers; and

(b) in relation to electricity lines services, reliability of supply, reduction in energy losses, and voltage stability or other technical requirements

65. These sections demonstrate that Parliament intended quality standards to have an active impact on supplier behaviour. The references to incentives, targets, bands and formulae all point towards a measurable target or targets that suppliers will have to meet or risk facing penalties.

66. There is no legislative support for a quality standard comprising information requirements only. Reporting of information is a light-handed form of regulation that is best suited to information disclosure. It is likely that the Commission would use this broader quality information to assess if the Part 4 Purpose is being met (consistent with section 53A). Indeed, our understanding is that the gas transmission capacity information is wanted because the Commission considers that it needs the information in order to identify whether the Purpose of Part 4 is being met. This is clearly the purpose of information disclosure regulation and it should therefore be requested through that regulatory mechanism.

67. Vector recommends that any quality information that is not a quality standard should be required under the Information Disclosure Determination rather than the GPB DPP Determination.

## **QUALITY STANDARDS FOR GAS DISTRIBUTION BUSINESSES**

### ***Response times to emergencies***

68. Vector supports the use of RTE (with a threshold) as a quality standard for the initial regulatory period for GDBs. We have made improvements to our systems and processes related to the recording of RTE data over the past two years.
69. The number of pipeline emergencies is low (approximately 200 per year in total) across Vector's distribution networks. This means that actual performance can vary significantly as a result of small changes in actual performance. If the quality standards for GDBs are broken down into non-contiguous networks then the probability of breaching the standards due to one unusual event (e.g. delays caused by heavy traffic) could be much higher. We recommend that, even if quality is reported at a non-contiguous level, the standard(s) should apply to the gas distribution network as a single entity.
70. In addition, there are some locations on our network where it is not possible for a response team to reach the pipeline within sixty minutes (at least not without breaking speed limits, which is also unsafe).
71. The RTE threshold should reflect geographical realities and there should be a different threshold for rural areas. This would reflect the fact that in smaller towns (e.g. Te Awamutu), there is generally no crew present locally. We propose a threshold of 80% within 60 minutes for rural areas<sup>11</sup> and 90% within 60 minutes elsewhere.
72. Vector supports the Commission's definition of an emergency as "an incident for which one of the emergency services (police, fire service, etc.) is called".

### ***Other quality requirements***

73. The quality information reporting requirements identified by the Commission are excessive and will create substantial costs to prepare, audit and publish while having (in some cases) little relevance to the operation of a GDB. We strongly recommend that the list of measures be streamlined to focus on those that have the greatest impact on consumer outcomes (e.g. safety).
74. Vector recommends the following five items are reported as quality indicators for GDBs through information disclosure (RTE will be reported through the gas price-quality compliance statement):

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<sup>11</sup> Vector will provide a proposed definition of rural areas in our cross-submission on the Gas DPP Discussion Paper by 10 June 2011.

- a) PRE (we agree that an initial threshold is not meaningful). We note that leaks and PRE are in balance. When leaks increase it can be a reflection of the nature of the assets being inspected in that year. Inspections of pipelines that have more leaks in any one year would be expected to reduce the amount of PRE in that year.
  - b) Outage events (without initial threshold).
  - c) Outage events caused by third party damage (without initial threshold).
  - d) Leaks (without threshold). Applying a threshold would be unhelpful because the number of leaks detected is a function not only of the length of pipeline surveyed but also of the condition of the specific assets surveyed. It is efficient to plan leak detection surveys around the network over a period of years and, inevitably, more leaks will be identified in some years compared to others. Fundamentally, reporting of leaks should be encouraged, not disincentivised for fear of financial penalties.
  - e) SAIFI (without initial threshold).
75. One of these measures (currently we support PRE) would then become an additional quality standard from 2016.
76. We do not believe any of the other measures proposed by the Commission are useful measures of quality for GDBs and consider that any requirement to gather and report the data to auditable standards would be an inefficient use of resources. Some indicators, such as unplanned SAIDI, have extremely low values (in absolute terms), are highly sensitive to individual events, and are potentially misleading in terms of indicating asset condition. Poor pressure is also of limited relevance as this is a rare event for GDBs and has little impact on consumers that is not already reported.
77. Unaccounted for Gas ("UFG") may be easy to measure but is not a true reflection of quality or network performance. Numerous factors make up UFG, including inaccurate metering, third party damage and theft. Safety devices such as over-pressure relief valves also contribute to UFG, but are essential for the safe operation of network pressure reduction facilities. In short, UFG has very limited value as a quality measure.
78. We note that consumers can seek resolutions of their complaints through the Electricity and Gas Complaints Commission ("EGCC) and separate reporting requirements under a DPP would be a duplication.
79. Importantly, any information that is not useful for demonstrating that quality standards have been met or that the Purpose of Part 4 is being met should not be required. The Commission must not seek to regulate more than is necessary and

we consider it is over-reaching with its proposal to require information on 14 “quality” measures.

### ***Potential future changes in gas quality indicators***

80. Under the Government’s Ultra-fast broadband initiative, the roll out of “fibre to the door” in urban areas across New Zealand is expected to start very soon. One consequence of this is likely to be an increase in third party damage events, outage events and emergency call-outs as trenchless operations such as directional drilling are likely to damage gas pipes. Vector takes steps to advise crews working in road corridors and other areas of the location of pipelines, but accidents do occur. Therefore historic data of the number of these types of events may under-forecast their likely frequency over the coming decade.

### **QUALITY STANDARDS FOR GAS TRANSMISSION BUSINESSES**

81. We consider RTE to be a reasonable quality standard for GTBs for the first regulatory period. Unlike a Gas Distribution system which is predominantly polyethylene (plastic) with multiple branches and connections, a Gas Transmission system is entirely welded steel and, consequently, leaks are very rare. Most incidents that involve emergency services have been the result of controlled gas venting (within a station) being interpreted by the public as an uncontrolled release of gas. Vector responds to these incidents and therefore the RTE could be applied.

82. The definition of emergencies on the Gas Transmission system should include all uncontrolled gas releases.

83. The response time required should recognise that many parts of the transmission system are remote, with limited or no road access. An emergency in a remote location does not pose an immediate safety risk so a slower response has no impact on safety. Consequently, a tiered approach to RTE is proposed<sup>12</sup>.

84. RTEs should take into account the different circumstances for remote locations. Vector recommends RTE compliance thresholds are categorised as follows<sup>13</sup>:

- a) Pipelines or stations within the city boundary of a “Main Urban” centre - RTE of 60 minutes achieved 90% of the time;

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<sup>12</sup> We acknowledge that we are proposing a different set of measures than would apply for distribution. We consider that this is appropriate for the following reasons: the chance of an emergency occurring on a distribution network is higher than on a transmission network; the transmission pipelines tend to be more strongly constructed than distribution pipelines so emergencies occur less frequently; and transmission emergencies are more likely to occur in remote locations with less risk of damaging lives and property.

<sup>13</sup> References to “main urban centre” and “secondary urban centre” rely on definitions from Statistics New Zealand.

- b) Pipelines or stations within the town boundary of a "Secondary Urban" centre – RTE of 90 minutes achieved 90% of the time; and
  - c) All other pipelines and stations – RTE of 120 minutes achieved 80% of the time.
85. Vector's historical data for response times to emergencies for gas transmission is captured in our incident management system ("IMS"). Some previous incidents that involved emergency services were not classified as emergencies and have not been recorded in the IMS.
86. Exceptions should also apply where responding would compromise the safety of the personnel responding, such as during an extreme weather event.
87. Importantly, the number of emergencies on the gas transmission system is much lower than on the distribution system (approximately 10 per year on average). It is challenging to set a meaningful target when the average number of events is so low. Vector recommends that the Commission give serious consideration to assessing compliance over a multi-year period. Ten events per year would equate to 50 events over a regulatory period<sup>14</sup>. Assessing compliance over an entire regulatory period rather than annually would be statistically more meaningful. Given the low frequency of emergencies on the transmission system, this may be the best measure available.

***Proposed quality measure for gas transmission***

88. The capability to supply gas is a fundamental quality measure. Historically, there have been very few interruptions to supply, so SAIDI and SAIFI are not appropriate measures, unless averaged over long intervals. Transmission pressures (at strategic points) can be used as quality measures to identify supply interruption near-misses.
89. The Gas Governance (Critical Contingency Management) Regulations 2008 established minimum pressures for normal operation at strategic points on the transmission system. The regulations also set thresholds for declaring a Critical Contingency based on the time to reach those pressures. Critical Contingency pressure data is generally robust and has been collected since 2009. We therefore propose as a future quality measure:

*The declaration of a Critical Contingency (as defined in the Critical Contingency Regulations) where the initiating event occurred on the GTB's pipeline system and was within the GTB's reasonable control. For the avoidance of doubt, any Critical Contingency arising from a gas production outage or a supply/demand mismatch is excluded.*

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<sup>14</sup> Or 42 events over the first regulatory period if it runs from 2 July 2012 to 30 September 2016.

90. The wording “reasonable control” is important as there are critical contingency events that are entirely outside Vector’s control. For example, production plant outages are outside Vector’s control, so critical contingencies where the initiating event was a production outage would be excluded. Pipeline damage is not directly within Vector’s control, but Vector does have some influence over these events.

***Capacity information for gas transmission***

91. As discussed above, Vector recommends any additional information regarding quality should be sought under information disclosure. The Commission is seeking from Vector a variety of capacity-related information as quality measures, specifically:

- a) Gas Demand by Gas Gate;
- b) Total Gas Reservations that have been Issued by Gas Gate;
- c) Total Gas Reservations that have been Requested by Gas Gate;
- d) Total number of Gas Reservation Requests that have been Granted in Full by Gas Gate; and
- e) Total number of Users of a Transmission Pipeline.

92. We understand that the Commission considers that it needs this information in order to assess whether the purpose of Part 4 is being met. If that is the case, then we submit that these data have little to do with the price-quality path and should be required through information disclosure as they are being required for the section 53A Purpose.

93. We also understand that the Commission is primarily seeking this information from Vector. It believes that the information is already available on OATIS as it relates to Maui Development Ltd.

94. Vector is happy to provide the Commission with information that it reasonably requires to assess whether the Purpose of Part 4 is being met. We do not fully understand why the Commission considers that the information it has listed is necessary for that purpose. It seems that some of the information the Commission has requested is not necessary for the Commission to achieve the purposes of information disclosure and / or Part 4. Also, if the measures were implemented in the way they are described they would create a large degree of effort to develop the data into the format in which it has been requested. As a result, we do not support the Commission’s proposal to require this information from GTBs at this time.

95. Further, Vector considers that the information being requested relates primarily to areas that are properly within the purview of the GIC. We are yet to be convinced by the Commission’s statement in paragraph 7.38 of the Discussion Paper that it is not seeking to replicate the work of the GIC. If the Commission requires this

information and uses it to make regulatory judgements, it seems likely that it would be replicating the work of the GIC. That would be an inefficient duplication of regulatory activity.

96. However, Vector does not see any of these issues as necessarily insurmountable. We recommend that relevant personnel from the Commission and Vector meet to discuss what is required, what can be provided and the most appropriate format for information provision. This should be done prior to further formal consultation on this issue.
97. We set out some initial comments on the Commission's suggested capacity information requirements below:
  - a) Capacity reservation, a feature of contract carriage, does not directly relate to how well a pipeline is being maintained and operated. As indicated in the discussion above on the form of control, Vector is not inextricably tied to a contract carriage regime. The regime could transition to common carriage or a "mixed carriage" regime, and we would prefer that the initial DPP not be constructed in a way to exclude this possibility.
  - b) The Commission appears to view technical pipeline capacity and capacity available for reservation as the same thing. This is not the case.
  - c) In the current capacity information disclosures, the hourly flows are provided for each delivery gate station for the system peak week. Capacity reservations are also published, so this information is already in the public domain. The Commission is looking for this information for every day of the year at injection points (so about 30 times more data than is currently disclosed). The costs of preparing these data for disclosure are likely to be substantial and Vector is unclear what the value would be.
  - d) We understand that the Commission is attempting to identify the "balance position for each gate station". Vector considers that this term would benefit from some additional clarity. Balance at a gate station implies a flow against a nomination, which is how the Maui pipeline operates. In contrast, the Vector system flows to demand, not nominations.
  - e) Vector does not see any clear linkage between the quantity of reservations applied for and the "balance position".
  - f) Historically, we are not aware of any incidents where complete compressor failure has resulted in a restriction of gas supply. However, the availability of a spare compressor may provide a reasonable measure of the level of its resilience.

## **PART C: OTHER MATTERS**

### **CLAW-BACK**

#### ***Revenue Assessment and Application of Claw-Back***

98. The Commission believes that applying claw-back under section 55F(2) is unlikely to be necessary. Vector strongly supports this view as there is no risk of prices increasing by more than CPI on either Vector's controlled or uncontrolled gas pipeline networks.
99. Vector confirms it has continued to set gas transmission prices and gas distribution prices on its North Island network in the same manner that we outlined to the Commission in our previous correspondence<sup>15</sup> and will continue to do so until the determination is made and the DPP applies. The Commission considers that if Vector applies Gas Authorisation methodology for price changes on uncontrolled networks, it will not be subject to claw-back. Vector supports this view.
100. The Commission also considers that networks subject to control will not be subject to claw-back. We support this view and agree with the Commission that Vector should not have to demonstrate that the CPI criterion has been met for the Auckland gas distribution network.

### **SETTING THE REGULATORY AND ASSESSMENT PERIODS**

#### ***Starting point for the first regulatory period***

101. The Commission proposes a regulatory period starting on 2 July 2012 that will last for four years and three months, with Assessment periods beginning on 1 October each year. We welcome the Commission's decision to align the regulatory and pricing years of the majority of GPBs. We agree that the assessment periods should begin on 1 October each year from 2012 to align with the pricing years<sup>16</sup>. This is in line with Vector's previous submission.
102. Vector's preference is for the regulatory period to start on 1 October 2012. There is no risk of prices in Vector's Auckland network or Powerco's network being increased at this time. Price changing is a complicated and time-consuming process and no sensible business would risk the reputational damage that would

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<sup>15</sup> Vector Ltd, *Submission on Setting the Default Price-Quality Path for suppliers of Gas Pipeline Services: Process Paper, 10 August 2009*, pages 2-3.

<sup>16</sup> See comment below regarding the timing of Asset Management Plan disclosures.

be caused by attempting to raise prices dramatically in a short period of no regulatory control.

103. The benefit of beginning the regulatory year on 1 October is that it avoids the cost of a partial year audit. Partial year audits tend to be just as costly as full year audits, but by definition will only produce ¼ of the value. We are not convinced these costs are justified for such a short and low-risk period.

### ***Partial year compliance audit***

104. However, if the Commission decides that there must be a partial year compliance period, we recommend that the price-quality compliance audit for the partial year be merged with the price-quality compliance audit for the first full regulatory year of the Gas DPP (i.e. the year ending 30 September 2013). This would minimise audit and reporting costs.

105. If a partial year compliance period is required, Vector recommends that a separate commencement period be included in the default price path to cover the period from 2 July to 30 September 2012. The default price path over the commencement period should require gas pipeline businesses to demonstrate that prices had not increased between 2 July and 30 September 2012. As Vector does not intend on increasing prices during this period, this could be demonstrated without reference to quantities or pass through costs in a manner similar to the formula below.

For each service  $i$ :

$$P_{ij,t^*} \leq P_{ij,t}$$

Where:

$j$  is component  $j$  of service  $i$

$i$  is service  $i$

$t^*$  denotes the commencement period beginning 2 July 2012 to 30 September 2012

$t$  denotes the day prior to the commencement period, 1 July 2012

$P_{ij,t^*}$  is the price of component  $j$  of service  $i$  during any part of the commencement period  $t^*$

$P_{ij,t}$  is the price of component  $j$  of service  $i$  on the date  $t$

106. The intention of the above formula is that each GPB would merely have to demonstrate for each individual price that it was less than or equal at the end of the commencement period to the price prior to the commencement period.

107. Vector recommends that demonstrating compliance with the default price path for the commencement period be required at the same time as the compliance statement for the first period following the commencement period, i.e. 15 months following the beginning of the regulatory period to take advantage of combined audit and verification costs.

## **COMMENTS ON INFORMATION DISCLOSURE**

108. While not specifically covered in the Discussion Paper, several issues raised relate to information disclosure. We also understand that, as a result of the Gas Asset Management Plan ("AMP") Information Disclosure Workshop held on 20 May 2011, the Commission is expecting comments in this submission on the timing of AMP disclosures and a sensible regional reporting structure for gas distribution networks<sup>17</sup>.

### ***Timing of Asset Management Plan disclosures***

109. For clarity, while Vector considers that regulatory and pricing years should align, we do not believe the AMP disclosures need to align with the regulatory year. Vector's financial year runs from 1 July to 30 June. Our budget process, of which planned network investments are a major component, is structured to that timetable. Our experience of providing the electricity disclosure AMPs to the March year has been that we have needed to take annual expenditure forecasts from the budget process and provided alternative numbers based on  $\frac{3}{4}$  of one of Vector's financial years and  $\frac{1}{4}$  of another. This can require significant additional work but does not provide a particularly meaningful outcome.
110. Any attempt to build the AMP into the standard process would mean that some network investment planning is required to occur outside of the normal budget process, which would be inefficient. As AMPs are a 10-year forecast, we do not see any value in incurring costs to match their data to the regulatory and pricing years.

### ***Regional reporting***

111. Applying the technical definition of non-contiguous networks to Vector's gas distribution network would require the reporting of quality and other measures over 50 separate networks. This would be costly and excessive and we welcome

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<sup>17</sup> Minutes of Information Disclosure Regulation under Part 4 of the Commerce Act 1986 Workshop 1: Gas Asset Management Plan Requirements.

the Commission's agreement that it is not seeking to apply the technical definition<sup>18</sup>.

112. At this time Vector does not have a firm view of what level of disaggregated regional reporting would be reasonable. We will provide our views to the Commission in our cross-submission on the Discussion Paper by 10 June 2011.

## **STARTING PRICE ADJUSTMENTS**

113. There is no indication in the Discussion Paper of what the starting price adjustment process for GPBs will be. However, the Commission indicates that there will be a starting price adjustment (i.e. it will not just rely on existing prices).

114. Vector disagrees with the Commission's view that it must rely on section 53P(3)(b) of the Act to set starting prices for GPBs. Section 53P(3) provides that:

(3) The starting prices must be either–

(a) the prices that applied at the end of the preceding regulatory period;

or

(b) prices, determined by the Commission, that are based on the current and projected profitability of each supplier.

115. The Commission's view is that it must set prices under section 53P(3)(b) because there is no previous regulatory period on which to base starting prices under section 53P(3)(a). This view is incorrect. The Commission appears to have misinterpreted the Act on this point, as the Act makes provision for the transitional nature of the gas regulatory regime and sets out what should be viewed as the end of the preceding regulatory period when making the first GPB DPP Determination under Part 4. Specifically, section 55F(1) provides that:

The Commission must use the processes set out in section 53P in making the first section 52P determinations that set out how default price-quality regulation applies to suppliers of gas pipeline services ***as if 30 June 2010 were the end of the previous regulatory period.*** [emphasis added]

116. The Commerce Act clearly views 30 June 2010 as the end of the preceding regulatory period for the purpose of the section 53P processes and the section 52P determination. The Commission does have the option of using prices from a previous regulatory period should it choose to exercise its option in section

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<sup>18</sup> <sup>18</sup> Minutes of Information Disclosure Regulation under Part 4 of the Commerce Act 1986 Workshop 1: Gas Asset Management Plan Requirements, page 6.

53P(3)(a) and set starting prices equal to those that applied at the end of the previous regulatory period.

117. Vector notes that the Commission has yet to publish a proposed starting price methodology for GPBs, but that it will most likely be informed by the starting price methodology for EDBs. We note that the information available to the Commission, both for assessing the initial conditions for each EDB and for rolling forward those initial conditions based on industry-wide assumptions will be challenging for GPBs given that historical data is less robust for GPBs than for EDBs. It is unclear if the Commission can make a credible starting price adjustment for GPBs as at 2012. Vector strongly recommends that the Commission set starting prices for GPBs under section 53P(3)(a), use the first regulatory period to gather necessary data, and then make a starting price adjustment if required at 1 October 2016.
118. If the Commission does make a starting price adjustment for GPBs in 2012, Vector submits that the Commission should provide for the high degree of data uncertainty (for example through a band mechanism of greater than 1%).

## **RATE OF CHANGE**

### ***Setting the X-factor***

119. The Commission proposes to set the X-factor for GPBs at zero. This is based on the results from an Economic Insights study that considered a measure of New Zealand GPB total factor productivity ("TFP"), an assessment of overseas gas network TFP and an assessment of other industry TFP, including recent TFP analysis of the New Zealand electricity distribution sector.
120. We consider that an X factor of zero for the first regulatory period is possibly too high but recognise that the available data does not support another outcome.
121. As discussed in previous submissions<sup>19</sup>, Vector has concerns with Economic Insights' methodology. We do not repeat these points here but note that the industry's concerns with the Economic Insights methodology have not been resolved. We also note that the outcomes are clearly sensitive to the method and data selected.
122. However, Vector recognises that there are significant challenges in developing robust TFP studies for GPBs and considers that Economic Insights' work was a reasonable attempt given the available data series. On that basis, we agree with the Commission that no further analysis of an appropriate X-factor for GPBs is required for the 2012 reset.

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<sup>19</sup> Vector Ltd, *Submission to Commerce Commission on Productivity Measurement*, 31 July 2009.

123. Finally, Vector notes that Economic Insights data for electricity distribution businesses was considered by the Commission as it developed industry-wide assumptions for the non-exempt EDBs in order to inform starting price adjustments for those EDBs. Vector reserves the right to comment further on Economic Insights' analysis should the Commission rely on it for developing starting price adjustments for GPBs.

***Data Requirements for Calculating Future TFPs for GPBs***

124. The Commission intends to require GPBs to disclose additional information to inform future TFP studies. The Commission is seeking views on the viability of reporting equivalent data to that currently required in Australia.

125. Vector is able to provide information at an aggregate level for our gas pipeline businesses – e.g. we can provide total opex, total capex, etc. However, we do not use the cost categories suggested by the Commission and we are unclear why such detail is necessary for the purpose of determining inputs and outputs into a TFP equation. Requiring 130 line items of information for a TFP study would be excessive and inconsistent with the intended low-cost nature of a DPP. We note that the information listed is not what is actually provided by regulated GPBs in Australia but an idealistic view of what a party that undertakes TFP studies would like to receive.

126. Vector considers that the high-level costs of each category should be all that is required. In general, sufficient data types are generally already in the public domain to develop gas TFP studies in New Zealand. The problem has been the reliability of the data over a time series rather than its absence.

127. We note that many of the cost categories put forward by the Commission are in fact shared costs as Vector has achieved efficiencies by leveraging across business units – billing, regulatory, customer connections, etc, are all shared costs so reporting these would be primarily a cost allocation exercise. Some initial specific comments on the line items are:

- a) Our understanding is that “Change in provisions” is not an expense line used by any New Zealand company.
- b) Cathodic protection tends to sit in other projects rather than being a single project of its own.
- c) Requirements to report the number of direct employees would be misleading as very different results would be provided depending on whether the GPB operated an insource or outsource business model.

- d) It seems that some of these inputs would not be provided by regulated parties. It is unclear why the regulated suppliers would be required to report the price indexes for labour, O&M and Network Assets. These should be derived by the Commission (or the Commission's consultant) when preparing a TFP analysis.
128. Vector notes that the information listed in Appendix A is lifted directly from an Australian document and has not been adjusted for the New Zealand context. For example, one of the operating expense categories is "meters". Section 55A(4) of the Act makes it clear that meters are not considered part of gas pipeline services in New Zealand. Vector would therefore not support disclosing meter expense data to inform a Gas TFP study.
129. In addition, the definitions also use Australian code terminology. New Zealand terminology and definitions of system physical data are different. For example, the pressure threshold between gas transmission pipelines and gas distribution networks is 2000 kPag in New Zealand, not 1050 kPag. We assume that the weighted averages are on a per km basis.
130. In conclusion, Vector is happy to provide additional information as required to inform future TFP studies. However, this information should not go into a greater level of granularity than is necessary for a TFP study and we consider that inputs and outputs at an aggregate level will be sufficient. A cost-benefit test should be applied to any additional information required.
131. Many of the line items in Appendix One are clearly unsuitable for New Zealand GPBs. We recommend that the Commission develop a proposal for information to inform future TFP studies in the New Zealand context that can then be the subject of informed consultation.

## **STRUCTURE OF THE DEFAULT PRICE-QUALITY PATH**

### ***Nature and Scope of the Determination***

132. The Commission's current position on the nature and scope of the DPP is that gas distribution and transmission should be considered as different types of services for the purposes of the DPP.
133. Vector supports this view. We agree that separate determinations are appropriate to allow issues that are specific to each type of gas pipeline service to be addressed separately.

### ***Differentiation of Distribution and Transmission Services***

134. The Commission considers that section 55A of the Gas Act and the Gas Distribution Services and Gas Transmission Services Input Methodologies sufficiently distinguish between transmission and distribution services and that no further definition is required.
135. Vector has considered this view in some detail. As a starting point, we consider that it is necessary for consistency and certainty that the definitions in the IMs and the DPP are the same. If a different definition was deemed necessary for the DPP, then the IMs should be amended.
136. Vector's view is that the definitions used in the IMs and proposed by the Commission for inclusion in the DPP contain some scope for ambiguity.

#### *Gas distribution network*

137. The definition of gas distribution network refers to "the pipelines and associated fittings between a delivery point from a transmission network and the point of supply". The "delivery point" from a transmission network is not defined. Vector's view is that the delivery point division between a transmission network and a distribution network is the "gate station outlet flange" (which reflects wording in definition of distribution system in the Gas Act).
138. "Point of supply" is as defined in regulation 5 of the Gas (Safety and Measurement) Regulations 2010, which refers to the "outlet of the gas measurement system". Gas measurement systems are not part of the distribution network as they are owned by the meter services provider. The Commerce Act regulatory framework does not include the gas measurement system, but by including the gas measurement system in the definition of network, there is an inconsistency/ambiguity.

#### *Gas transmission network*

139. The definition of gas transmission network refers to "the place where gas enters those transmission pipeline systems (commonly referred to as a 'receipt point') and the place where gas exits them". As above, the place where gas exits the transmission system is "the gate station outlet flange".

#### *Definition of "person"*

140. Both of the Commission's definitions contain a proviso that where transmission and distribution are owned by the same **person**, the delivery point is the place specified by that person. The effect of this may not be what the Commission had intended.

141. The Auckland gas distribution network is owned by Vector Limited and Vector's gas transmission network and North Island gas distribution network are owned by Vector Gas Limited. "Person" as defined in the Commerce Act would be **either** Vector Limited **or** Vector Gas Limited. As a result, the proviso would only apply in respect of the non-Auckland distribution/transmission relationship because the Commerce Act definition of person does not include related companies.
142. If the Commission's intention was to cover the connection points between Vector's transmission network and both of Vector's distribution networks, this has not been achieved. If the proviso is kept, it should be amended to reflect interconnected bodies corporate (as defined in the Commerce Act) rather than person so it can apply to the connection between Vector's gas transmission network and the Auckland gas distribution network.
143. However, Vector's preference and recommendation is for the definitions set out below to be adopted in both the DPP and the IMs:

#### **Transmission System**

"...the high pressure transmission pipeline systems under the control of one **person** between-

- (a) the place where gas enters those transmission pipeline systems (commonly referred to as a 'receipt point'); and
- (b) the gate station outlet flange where gas exits those transmission pipeline systems (commonly referred to as a 'delivery point')."

#### **Distribution System**

"...the system used to distribute gas to a **consumer**, comprising pipelines and associated **fittings** between-

- (a) the gate station outlet flange where gas enters those distribution pipeline systems from a **transmission network** (commonly referred to as a 'delivery point'); and
- (b) the point of supply."

### ***Integrated vs. Separate Price and Quality Standards***

144. The Commission considers that price and quality standards under the DPP should be separate.
145. While this is a pragmatic solution given the paucity of robust historical information, Vector recommends that the Commission aim towards developing an integrated price-quality path that includes incentives for better quality over time. An integrated approach is consistent with the objectives of the Commerce Act as it would mean that regulated suppliers have better incentives to innovate and invest (i.e. to improve quality of supply as well as to maintain it), and incentives to

provide services at a quality that reflects consumer demands (i.e. by providing integrated financial penalties and rewards linked to prices and quality targets).

### **Compliance with the Price Path**

146. The Commission proposes a weighted average price cap of the same form as that proposed for the electricity default price path. The submissions made below in response to this proposal are without prejudice to Vector's position that a revenue price cap is appropriate for GTBs.
147. In principle, Vector agrees that where a weighted average price path is appropriate there is no apparent reason to establish price caps that are materially different between electricity and gas. However, the Commission has proposed the exact same CPI formulae for gas default price paths as is used for electricity default price paths. Vector submits that this formula should be changed to the one below which reflects the most relevant quarters to the gas pricing year.
148. If a 1 October price implementation date is adopted, then the Commission should use a CPI formula as outlined below:

$$\Delta CPI_t = \frac{CPI_{Jun,t-1} + CPI_{Sep,t-1} + CPI_{Dec,t-1} + CPI_{Mar,t}}{CPI_{Jun,t-2} + CPI_{Sep,t-2} + CPI_{Dec,t-2} + CPI_{Mar,t-1}} - 1$$