



**Initial Default Price-Quality Paths for Gas  
Pipelines Businesses: Draft Determination and  
Reasons Paper**

**19 December 2011**

## Introduction

1. Powerco welcomes the opportunity to comment on the *Initial Default Price-Quality Paths for Gas Pipelines Businesses: Draft Determination and Reasons Paper* (the Draft Determination), published on 21 November 2011.
2. This submission does not comment on the gas P0 reset process. Our response to the *Additional Input Methodologies for Default Price-Quality Paths: Process and Issues* paper will be covered in our submission of 27 January 2012.
3. The contact person for this submission is:

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## Summary

4. The open approach the Commission has taken to developing the DPP is to be commended and means that GDBs have been able to provide detailed input at various stages and this is reflected in the final document.
5. Overall Powerco views the Commission’s proposal as a pragmatic solution, given the challenges of incomplete datasets on which to establish the price path and the complexity of measuring ‘quality’ of gas networks. We hope that the Commission will continue to take opportunities to work with distribution businesses over the DPP period to develop the model further for subsequent price periods.
6. The table below summarises Powerco’s response to the key aspects of the Draft Determination.

Commission Proposal	Powerco response
<b>Structure of DPP</b> <ul style="list-style-type: none"> <li>• Gas distribution and transmission pipeline services considered to be different types of gas pipeline services for the purpose of the initial DPP.</li> </ul>	<ul style="list-style-type: none"> <li>• Support</li> </ul>
<ul style="list-style-type: none"> <li>• Initial DPP should have separate price and quality paths.</li> </ul>	<ul style="list-style-type: none"> <li>• Support</li> </ul>
<b>Quality Standards</b> The quality path shall be: <ul style="list-style-type: none"> <li>• 80% of responses to emergencies in no more than 60 minutes</li> <li>• 100% of response to emergencies in no more than 180 minutes</li> <li>• No definitional changes from Gas Authorisation</li> </ul>	<ul style="list-style-type: none"> <li>• Support 80% limit.</li> <li>• It is feasible that an event could happen where it is not possible to respond to an emergency in 3 hours. Recommend an exemption criteria is added to 100% limit.</li> <li>• Recommend definition of “emergency” is changed to avoid events that are no longer emergencies being prioritised over events which might present a greater safety risks.</li> </ul>
<b>Form of control</b> <ul style="list-style-type: none"> <li>• Apply weighted average price cap to gas distribution businesses.</li> </ul>	<ul style="list-style-type: none"> <li>• Support</li> <li>• Recommend non-material and competitive services are excluded from the DPP, consistent with the approach taken in the Gas Authorisation.</li> </ul>
<b>Rates of change</b> <ul style="list-style-type: none"> <li>• X=0 as no conclusive evidence exists to support any other value of the X factor.</li> </ul>	<ul style="list-style-type: none"> <li>• Support</li> </ul>

<p><b>Price and regulatory periods under initial DPP</b></p> <ul style="list-style-type: none"> <li>Regulatory period from 1 July 2012 to 30 September 2016 (four years and three months)</li> </ul>	<ul style="list-style-type: none"> <li>Support</li> </ul>
<p><b>Monitoring of compliance</b></p> <ul style="list-style-type: none"> <li>Assessment period from 1 October – 30 September</li> <li>Ex post compliance for quality</li> <li>Ex ante compliance to prices: Statement due 30 November each year, two months after prices are set.</li> </ul>	<ul style="list-style-type: none"> <li>Support</li> <li>Support</li> <li>Recommend Statement is due 30 January, to allow more time to audit quality path.</li> </ul>

## Quality Path

### Powerco supports a quality path based on “responses to emergencies”

7. Powerco continues to support using “response to emergencies” as the quality path. This is the most pragmatic solution, given the data limitations. While using an average response target continues to be our preference, we are comfortable with the threshold of responding to 80% of emergencies within 60 minutes. This is a stringent quality path, but allows for years where exceptional circumstances eventuate. As the Commission has not adopted a “two out of three years” breach rule, 80% is appropriate.

### A 100% target with no exemptions is a safety risk

8. The Commission has set a second limit – to respond to all emergencies in three hours. This is to address a concern that if the target was not in place, GPBs would have no incentive to respond to emergencies once 60 minutes had passed.
9. Powerco takes emergencies very seriously, and do not consider an upper limit is necessary. Once 60 minutes has elapsed, we will still endeavour to reach the emergency as quickly as possible. Factors that delay reaching emergencies are often beyond our control eg weather and traffic. For every emergency we respond as quickly as possible, without putting our staff, service providers or the public at risk.
10. Since the Gas Authorisation has been in place, the longest it has taken Powerco to respond to an emergency is 2hrs 40 mins. If the Commission did proceed with an upper limit, three hours is reasonable. However, a limit of 100% may lead to Powerco breaching the DPP as a result of circumstances over which it has not control eventuate. For example, it is reasonable to expect a situation in the North Island in the next five to ten years that washes out a bridge or road meaning engineers are not able to reach an incident within three hours.
11. In the absence of defined exemption criteria, a 100% target is unreasonable and could lead to gas personnel taking unnecessary safety risks to meet the target. An exemption criteria to the 100% target should be added such as:

“The Commission may grant an exemption to the response to emergency if there are circumstances outside of the GPBs reasonable control which the Commission is satisfied means that three hours would not be practicable. A GPB may request an exemption at any time during the assessment period, to be assessed by the Commission within 30 days.”

### A situation is not an emergency if the fire service fix the fault

12. Powerco and MDL suggested changes to the definition of emergency in previous submissions<sup>1</sup>. Powerco recommends the following is added.

“An emergency would be defined as an incident for which one of the emergency services (police, fire service, etc.) is called *and deems the immediate attendance of a gas distribution business engineer is required.*”

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<sup>1</sup> See Powerco, *Submission on Initial Default Price-Quality Path for Gas Pipeline Businesses: Discussion Paper*, 27 May 2011, paragraph 23, p. 7.

13. Examples where this might apply would be the emergency services call Powerco to inform them of the emergency, but on arrival:
- find there is no gas leak
  - identify a non-network source of a leak (e.g. bottled gas); or
  - are able to safely isolate the supply without the need for an engineer (a task often undertaken by the fire service).
14. As an example, Powerco had a large outage in the Hutt Valley in 2008/09 where all available gas engineers were working to restore supply to consumers as quickly as possible. The fire service called and informed Powerco it had responded to an incident in Wellington and made safe the premises. Under existing rules the safe Wellington incident would be classed as an emergency and would take priority over restoring supply to customers in the Hutt Valley (some of which may be elderly and require heating). This does not seem to be in consumers' best interests.
15. We do not think the change creates any ambiguity or significantly alters the time series of information. The emergency services are qualified to judge if an emergency requires immediate assistance from Powerco, or turn off valves to premises and make safe.

## Price Path

### Support ex ante pricing reporting

16. Powerco is comfortable with ex ante pricing reporting. Our pricing compliance is effectively ready to be audited and approved when final prices are sent to retailers in June each year. The period October – January is also free of other disclosures (assuming Gas Information Disclosure moves to publication in February/March) .

### Deadline should be mid December or 50 business days after end of assessment period

17. The main constraint of the deadline is the time needed to compile and audit the quality path, as it is an ex post assessment. Powerco recommends that date is changed to 30 January each year to allow more time for this audit.

### Lagged pass through cost and recoverable costs

18. Powerco supports the WAPC formula and the lagged approach to pass through and recoverable costs. However, the drafting of the Determination does not make it completely clear that all pass through costs and recoverable costs are lagged. We note Schedule 6 states, “The individual pass-through cost or recoverable cost amounts that are included in  $K_t$  and  $V_t$  are the most recent annual amounts of each cost that are known at the time prices are being set for an assessment period.  $K_t$  and  $V_t$  therefore are not necessarily the individual pass-through cost or recoverable cost amounts that are to be incurred in year  $t$ , as the amounts can be lagged”.
19. The definitions of  $V$  and  $K$  in Schedules 3 states “ [...]is the sum of all pass-through costs during the 15 month period from 1 July 2012 to 30 September 2013 ”. This is confusing. Powerco recommends that the definitions of  $V$  and  $K$  in schedule 3 specifically reference Schedule 6 to provide maximum clarity.

### Excluded services – consistency with Gas Authorisation

20. The Gas Authorisation excluded the following services from the price path:
- disconnection services
  - reconnection services
  - decommissioned services
  - gas connection services
  - non-standard distribution services that Powerco commenced supplying after 30 September 2007.
21. The rationale for this was strong: The Commission stated that there was little risk of Powerco or Vector charging excessive prices for these services as there was sufficient competition and the materiality of revenue was small.
22. Powerco recommends that these services are also excluded from the Gas DPP as the same logic applies. The rationales in the Gas Authorisation are provided below.

*Connection Services (including disconnection, reconnection and decommissioning)*

23. The Commission stated in paragraph 1122 and 1123 of the Gas Authorisation Reasons Paper that,

*The Commission considers that there is competition for the supply of connection services that do not require laying a service pipe to the property. New connection services that require a service pipe to be laid to the property from an existing network face a competitive constraint from other fuels as the costs of connection are likely to play a significant role in the decision to connect or not connect to natural gas.*

*The Commission considers that the incentives on the businesses to minimise these costs should be sufficient to ensure that the businesses do not charge excessive prices to connect new customers. These incentives arise from the incentive to connect customers in order to increase penetration rates on their networks. The Commission has also considered the materiality of this revenue in terms of the total revenue for controlled services. The Commission considers that the connection services provided by the controlled businesses should be controlled as excluded services under the Authorisation.*

*Non-standard distribution services that Powerco commenced supplying after 30 September 2007*

24. The Commission stated in paragraph 1138 in the Gas Authorisation Reasons Paper that,

*The Commission considers that it is appropriate to not require Powerco and Vector to incorporate new non-standard services during the control period, as prices for nonstandard services should be lower than for comparable standard services, and these customers have the option of a standard contract if the non-standard pricing is unfavourable. Non-standard customers are also more likely to have bypass opportunities available to them (depending on their location). Adding the new nonstandard services will not affect the price path. These new non-standard services are therefore being controlled as 'excluded services' during the control period.*

## Compliance Statement

### Remove requirement to produce Gas Authorisation Statement on 1 May 2012

25. Clause 10.1.1 of the Gas Authorisation requires Powerco to provide a Gas Authorisation Annual Compliance Statement (Statement) to the Commission by 1 May 2012. This requirement is now superseded by the Gas DPP. We recommend the Commission rescind clause 10.1.1, as otherwise we would have to produce two gas annual compliance statements in 2012.
26. We recognise the May 2012 Statement provides data on the 15 gas quality measures for 2010/11. We recommend that the quality information is disclosed as part of the first new gas information disclosure (in 2012). This has the benefits of:
- ensuring the quality definitions are the same as those going forward – ie if the definitions change, there is potential to disclose the statistics by the new definitions (depending on the extent of change);
  - providing more options of how to transition from a July/June disclosure to a October/ September disclosure year;
  - only delay the publication of the information by around five months (depending on when the gas information disclosure is due); and
  - key indicators, such as SAIDI, SAIFI and UFG, will be published in February 2012 as part of the 2010/11 Ministry of Economic Development Gas Information Disclosure.