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**Vector Limited**  
101 Carlton Gore Road  
PO Box 99882, Newmarket  
Auckland 1149,  
New Zealand  
[www.vector.co.nz](http://www.vector.co.nz)  
Corporate Telephone  
+64-9-978 7788  
Corporate Facsimile  
+64-9-978 7799

Regulation Branch  
Commerce Commission  
Wellington

Sent by email to: [regulation.branch@comcom.govt.nz](mailto:regulation.branch@comcom.govt.nz)

### **Submission on Draft Section 53ZD Statutory Notices for Gas Pipeline Businesses**

1. Vector welcomes the opportunity to provide this submission on the Commerce Commission's ("Commission") consultation on draft statutory notice information requests under Section 53ZD, which apply to regulated Gas Distribution Businesses ("GDBs") and Gas Transmission Businesses ("GTBs").
2. Vector welcomes the Commission's approach of consulting on the draft notices before they are issued, which should improve the quality of and ease of compliance with the final version of the notices.
3. We have seen and endorse the submission from PriceWaterhouseCoopers, commissioned by Vector and Powerco, on the draft statutory notice requirements.

#### **Timeframe for responses**

4. Vector's primary concern with the draft notices is the proposed timeframe for completing them; the Commission has proposed to issue the final notices in "early July" with a response date of 30 September. This timeframe is similar to the timeframe provided for the statutory notice for electricity distribution businesses ("EDBs") (16 March to 27 May), which Vector managed to meet. However, in this instance the three-month reporting period coincides with both electricity and gas information disclosure timeframes and, most importantly, Vector's financial end-year reporting.
5. It is Vector's view that completion of the statutory notice *on its own* within the timeframe provided is extremely challenging. Completion of the statutory notice *as well as* the other statutory tasks that are required is, in our view,

not possible within the timeframe provided by the Commission. We explain how we reach our view in the following paragraphs.

6. Vector is required under New Zealand Stock Exchange ("NZSX") Listing Rule 10.4 to provide information to the market about Vector's financial performance in the financial year ending 30 June. This must be provided not later than sixty (calendar) days after the end of the financial year. To comply with this requirement, Vector must prepare, review and audit its annual financial statements and the other statutory information required for Vector's annual report (which the NZSX rules require to be released to the NZSX by 23 September). These are Vector's highest priority disclosures.
7. In addition, we need to prepare information for analyst briefings on the annual results.
8. Other reporting requirements in the July-September period are:
  - a) EDB information disclosure requirements, which require disclosures to be reported to the Commerce Commission by late August each year. Vector has previously recommended<sup>1</sup> that these disclosure requirements be deferred until after the new information disclosure requirements are set.
  - b) Lender compliance statements to our banks, investors and their respective trustees, which need to be prepared within 90 days of the end of the financial year. This includes preparation, review and audit of a set of guaranteeing group accounts.
  - c) Vector's 2011 Gas Information Disclosures (which require a full set of financial statements for four gas businesses to be prepared, reviewed and audited), which are due to be provided by November 2011. The work to prepare these disclosures must be undertaken in September and October 2011.
9. We point out that it is mostly the same people (both within Vector and KPMG) that are involved in all of these statutory reporting tasks and their associated audits.
10. During the same period, Vector will be considering and responding to the Commission's consultations on the next Gas DPP discussion paper, the draft decisions relating to the electricity starting price adjustment, and the new information disclosure requirements. Again, some of the same personnel will be involved in these tasks.

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<sup>1</sup> Vector Ltd., *Submission to Commerce Commission on Information Disclosure Process and Issues Paper*, 9 March 2011, paragraph 30.

11. An additional challenge is created as the information required under the statutory notice includes information from the 2010-2011 gas disclosure year that ends on 30 June 2011. The data for 30 June 2011 will not be ready until Vector's 2011 Annual Report is completed (in late August). This narrows the window within which work can be done to meet the statutory notice request, increasing the challenge to meet the Commission's deadline.
12. In addition, the input methodology applies to the system assets and non-system assets for years 2010 and 2011, instead of only year 2010. It will therefore take double the time to prepare the information. The auditor will also take longer to audit the data because the data for 30 June 2011 has not been audited before. This contrasts with the electricity information request which used data that had previously been disclosed and audited as part of the 2010 information disclosures.
13. Vector recommends that the Commission does not force regulated suppliers into a position where they have no choice but to fail to comply with a statutory requirement because the timeframes are not achievable.
14. Specifically, we recommend that:
  - a) The deadline for providing information under the statutory notice is extended to 30 November 2011; and
  - b) The requirement to provide electricity information disclosures for those EDBs that are also gas pipeline businesses are at least delayed until 24 December 2011. Vector continues to maintain that these disclosures should be delayed until the new information disclosure requirements are completed so they can be developed in accordance with the input methodologies. The Commission's proposal to continue to report under the old information disclosure requirements will lead to an inconsistent time series of data and will create further work for EDBs as the asset valuation information reported in 2011 will have to be re-cast in light of the input methodologies for the 2012 disclosures.
15. The Commission should not consider that acceding to request (b) above will be sufficient to resolve the timeframe problems. The main benefit will be provided by extending the deadline for the statutory notice.
16. Vector is aware that the Commission has set its deadline with a view to meeting its own deadline of final GDB and GTB determinations by 29 February 2012. However, we consider that the Commission could set a later deadline for statutory notice information for these reasons:
  - a) The statutory notice data will be used as input into a model used to determine starting price adjustments for each GPB. As the information has been audited, the Commission will not need to check its accuracy.

It can therefore just be added to the Commission's model to derive starting price adjustments. We are unclear why the Commission *must* have the data for an essentially mechanistic activity five months prior to the final determination. There could be a moral hazard in the Commission developing the model to fit the data, rather than the other way round.

- b) The 29 February 2012 deadline is driven by the Commission's view that the DPP for GPBs should begin on 2 July 2012. However, Vector's pricing year (like all GPBs other than Maui Development Ltd.) begins on 1 October each year. We would strongly recommend that, even if the DPP begins on 2 July 2012, the Commission should not require any price adjustment until 1 October. Otherwise GPBs would be required to make two price adjustments within a three-month period, which would cause problems for GPBs, retailers and consumers. The Commission could therefore make a DPP determination on 29 February 2012 and make an amendment to the determination to provide for the starting price adjustments three months after that date.
  - c) Further, Vector has previously submitted that the DPP should begin on 1 October 2012<sup>2</sup>. The Commission has argued<sup>3</sup> that delaying the start of the DPP to 1 October 2012 may not be consistent with section 55H(2) of the Commerce Act 1986 as setting the DPP to begin on that date would mean the DPP begins later than "as soon as reasonably practicable". In our view, given the data issues that have been identified, if the Commission really does need this information at least five months prior to a final determination, then it is not reasonably practicable to start the DPP on 2 July 2012.
17. If the Commission accepts either our point (b) or (c) above, it should realise that it is requiring information to inform a price reset 12 months before that reset will be implemented. We consider this excessive.

### **Division of responsibility between auditor and engineer**

- 18. As in the electricity distribution statutory notice, the division of responsibilities between the auditor and the independent engineer in the draft gas pipeline statutory notice is less clear than is desirable.
- 19. Vector will need to seek engineer approval for the asset valuation adjustments in the year they enter the asset register. Then auditors will need to approve the roll forward process (additions, disposals, depreciation and

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<sup>2</sup> Vector Ltd., *Submission on Initial Default Price-Quality Path for Gas Pipeline Businesses: Discussion Paper*, 14 May 2010, paragraph 47.

<sup>3</sup> Commerce Commission, *Initial Default Price-Quality Path for Gas Pipeline Businesses: Discussion Paper*, 1 April 2011, paragraph 8.22.

indexation) to 2009. This is the appropriate division of expertise as the engineer is best placed to decide if the asset adjustments are appropriate and the auditors are best placed to roll forward the asset adjustments. Auditors are also best placed to assess the arithmetical accuracy of the asset adjustment calculations. However, the draft statutory notice does not quite set out this clean division of responsibilities, which creates complexity and confusion over the responsibilities of different parties.

20. Vector recommends that Schedule C be amended to make it clear that the engineer is responsible for approving asset adjustments and the auditor is responsible for confirming the arithmetical accuracy of the adjustments and for approving the roll forward process.

### **Advice and guidance from the Commission**

21. When EDBs provided responses to the electricity distribution statutory notice, the Commission provided a very helpful Issues Register in which questions of clarification and guidance could be raised by parties completing the schedule. The Commission responded to these questions quickly.
22. Vector recommends that the Commission provide similar support to GPBs as they respond to the gas statutory notices.

### **Comments on the Schedules**

#### *General*

23. The draft statutory notice schedules do not let the GPBs determine their own key data (e.g. ROI or regulatory tax allowance) and have those results audited. Instead the Commission will take the data reported and make a judgement about how to use them, without visibility of this process for GPBs or other stakeholders. This is not good regulatory practice.
24. Vector recommends the Commission revise the schedules so GPBs and their auditors can assess the final set of regulatory financial statements that will determine any starting price adjustment. The Schedules should provide:
  - a) A full regulatory profit statement (including depreciation, tax, term credit spread allowance and revaluation);
  - b) A full (allocated) RAB roll forward, starting with the Initial RAB at 1 July 2009;
  - c) A full regulatory tax calculation inclusive of various components including the deferred tax balance and tax loss balance rolled forward from 1 July 2009; and
  - d) The derivation of the Regulatory Investment Value.

#### *Schedule A1*

25. The Schedule should require direct and indirect costs, which have been applied by GPBs historically. We do not support the use of EDB cost categories as suggested by the Commission as these have not been used previously by GPBs. Also, it is unclear why it is necessary to group opex into common categories for the starting price adjustment analysis.

#### *Schedule A2*

26. The Commission should allow flexibility for GPBs to designate the opex categories so appropriate categories can be chosen for each business.
27. On the public version of schedule A2, Vector is unclear about the purpose of the percentage allocation information. 'Line item' disclosures should be deleted.

#### *Schedule A3*

28. Vector considers that the initial RAB section is reasonable.
29. The RAB roll-forward section is confusing. The use of the word "unallocated" in row 35 when one of the boxes in that row must be the allocated value from Schedule A5 makes the meaning of the section unclear. We assume unallocated data will not be used for the starting price adjustments.
30. Rows 41 to 49 (for GDBs): Vector does not agree that it is necessary to show the detail of the 2010 revaluation calculation and considers that the Commission's method of carrying out this revaluation is sub-optimal. The Commission's approach requires a revaluation of assets that have been disposed (and therefore should not be included in the revaluation at all). Vector carries out the revaluation calculation properly in our asset register database by excluding revaluations on fully depreciated, disposed and lost assets. To fill in Rows 41 to 49 we would have to calculate revaluations on fully depreciated, disposed and lost assets for no benefit other than filling in the notice request. Thus the structure of these rows would create further work for Vector to get to the same outcome by a different route. Also, row 33 and row 49 seem to duplicate each other. One should be deleted.
31. Vector's interpretation of row 55 (for GDBs) is that it includes the value of row 57 (the opening RAB values of assets fully written off during the year), and similarly for the corresponding rows in the GTB Schedule A3. We request confirmation of this.

#### *Schedule A4*

32. Vector's asset adjustments all entered the regulatory asset register in 2003 (as this was the date of the most recent valuations that the Commission will accept). To try to complete this schedule without including 2003 data will be

very challenging. Vector recommends that schedule A4 include a column for 2003.

#### *Schedule A6*

33. The tax information is incomplete and difficult to follow for users. Vector suggests using the draft schedules designed for the new information disclosure requirements, which set out the roll forward and inputs in a more meaningful way. In addition, the date information is incomplete in some places.

#### *Schedule C*

34. Schedule C 2(e)(i) refers to "ODV rules" and "assets which had not had an ODV valuation calculated originally as required by clause 2.2.1 of the GDB IMs". However, the GDB input methodology does not refer to "ODV" at all, as there are no ODV rules for gas. The Schedule should be changed to match the use of disclosed values in the input methodologies.
35. Table 1: An option should be added for depreciated carrying value (where sufficient records do not exist to establish depreciated historic cost) consistent with input methodology clause 2.2.1(2)(b).

#### **Contact details**

36. Thank you for considering this submission. If you have any questions, or require further information, please contact Ian Ferguson, Regulatory Advisor, on 09 978 8277 or [Ian.Ferguson@vector.co.nz](mailto:Ian.Ferguson@vector.co.nz).

Kind regards



**Bruce Girdwood**  
Manager Regulatory Affairs