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Submission on Setting the Default Price-Quality Path for suppliers of Gas Pipeline Services: Process Paper

1. Vector welcomes the opportunity to provide this submission on the Commerce Commission's (Commission) consultation on the Process Paper for setting the Default Price-Quality Path (DPP) for suppliers of gas pipeline services.

Timetable for consultation

2. Vector welcomes the Commission's proposal that the initial DPP for gas pipelines will come into effect on 1 July 2011 as a more practicable approach, given the effort currently going into the electricity DPP and input methodology processes. We believe this is the correct interpretation of the Act, will allow more time to build up knowledge of the gas pipelines industry and will make the timeframes involved in implementing the provisions of Part 4 of the amended Commerce Act 1986 easier to manage.

3. Vector urges the Commission to make full use of the time now available to develop well founded Default Price-Quality arrangements for gas pipeline services. Vector notes that the proposed consultation timeframes for the gas DPP are only slightly longer than those proposed for the electricity DPP despite the Commission having an additional 18 months to determine the gas DPP. Vector recommends that, in order to foster well-informed debate and decisions, the Commission allow

significantly more time for each consultation stage for the gas DPP than it has allowed for the electricity DPP.

Details of the consultation process

4. Vector also strongly recommends that the Commission hold at least one conference with interested parties to discuss issues during the development of the gas DPP. Vector believes that the conference should be held at an early stage so the Commission can discuss issues with stakeholders as early in the process as possible, preferably before significant decisions have been made. Vector therefore recommends a conference be held before the Discussion Paper is published.

5. Vector submits that the Commission should provide specific details of its proposals to GPBs as early in the process as possible, and test these using actual data and information, so GPBs can assess the likely impact of the Commission's proposals on their business at an early stage. Vector is concerned that the Commission's proposed "Decision Stage" will only include preliminary views on rates of change and quality standards. Vector submits that preliminary views should be reached much earlier (a public conference will assist in this regard) and near-final views should be available by the Decision Stage.

Vector's approach to the CPI cap on prices from 1 January 2008

6. Section 55F(2) of the Commerce Amendment Act 2008 (CAA) dictates that weighted average price increases should be no more than the movement in the forecast or actual CPI between 1 January 2008 and 30 June 2010. The CAA does not provide detail on how this provision should be interpreted, implemented or assessed. Vector has sought guidance from other regulatory decisions and legislation.¹

7. Below we set out the approach we are taking to meet the CPI limit – an approach we have taken to mitigate regulatory risk in an environment of uncertainty about input methodologies. We request confirmation from the Commission that our methodological approach (which is based on the Gas Authorisation approach to demonstrating compliance with a price path) would satisfy the CPI limit from 1 January 2008.

¹ These include the Commerce Act (Natural Gas Services) Provisional Authorisation 2005, the Commerce Act (Electricity Distribution Thresholds) Notice 2004 and the Commerce Act (Vector Natural Gas Services) Authorisation 2008.

8. Each year Vector intends demonstrating compliance with clause 55F(2) of the CAA through the following mechanism:

$$\sum Q_{ij} P_{ij,t} \leq \sum Q_{ij} P_{ij,t-1} \Delta CPI_t$$

Where:

Q_{ij} is the base quantity corresponding to component j of service i for the period ending 30 September $t-2$ (the most recent available annual quantity data);

t denotes the calendar year during which a price assessment is made;

$P_{ij,t}$ is the price for component j of service i in year t ;

$P_{ij,t-1}$ is the price for component j of service i in year $t-1$;

i is service i

j is component j of service i

ΔCPI_t is the lagged historical average change in the consumer price index applied to prices effective in year t calculated in accordance with:

$$\Delta CPI_t = \frac{CPI_{Mar,t-1} + CPI_{Dec,t-2} + CPI_{Sep,t-2} + CPI_{Jun,t-2}}{CPI_{Mar,t-2} + CPI_{Dec,t-3} + CPI_{Sep,t-3} + CPI_{Jun,t-3}} - 1$$

9. For the 1 October 2008 pricing process, Vector adopted an approach to determining the CPI based on the Commerce Act (Electricity Distribution Thresholds) Notice 2004. This required CPI forecasts to be used in the compliance calculations.

10. Since the price setting process for 1 October 2008, the Commission has released the Commerce Act (Vector Natural Gas Services) Authorisation 2008. This determination adopted a revised approach to indexation by using lagged historical CPI, which mitigated the risk of non-compliance.

11. To account for the change in CPI approaches, Vector has modified the CPI used in 2009 to ensure that over the 2008 and 2009 price changes Vector would in effect have adopted a lagged CPI approach in both years.

12. Despite the changes outlined above, Vector has continued to use forecast PPI to model changes in non-standard prices; because the contractual price change for the vast majority of Vector's non-standard contracts is partly determined by the June quarter PPI index. Any difference between actual and forecast PPI is to be adjusted in the following year to ensure the overall CPI cap is met.

Contact details

13. Thank-you for considering this submission. If you require further information please contact me on 04 803 9039 or at nathan.strong@vector.co.nz, in the first instance.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Nathan Strong". The signature is written in a cursive style with a horizontal line at the end.

Nathan Strong
Manager Regulatory Affairs