

Company Name Vector – Gas Distribution business

For Year Ended 30 June 2014

## **Schedule 14 Mandatory Explanatory Notes**

*(In this Schedule, clause references are to the Gas Distribution Information Disclosure Determination 2012)*

1. This Schedule requires GDBs to provide explanatory notes to information provided in accordance with clauses 2.3.1, 2.4.21, 2.4.22, 2.5.1, and 2.5.2.
2. This Schedule is mandatory—GDBs must provide the explanatory comment specified below, in accordance with clause 2.7.1. Information provided in boxes 1 to 12 of this schedule is part of the audited disclosure information, and so is subject to the assurance requirements specified in section 2.8.
3. Schedule 15 (Voluntary Explanatory Notes to Schedules) provides for GDBs to give additional explanation of disclosed information should they elect to do so.

### *Return on Investment (Schedule 2)*

4. In the box below, comment on return on investment as disclosed in Schedule 2. This comment must include information on reclassified items in accordance with clause 2.7.2.

**Box 1: Explanatory comment on return on investment**

The Disclosure ROI calculation is not compatible with IRR calculation included in the Commerce Commission's draft electricity distribution DPP model released on 4 July 2014. This IRR calculation has been demonstrated to be consistent with the basis of setting starting revenues. Therefore, the disclosure ROI of 8.20% is not comparable to the 75th percentile vanilla WACC of 7.44% used for the first price reset or the 2014 disclosure year 75th percentile vanilla WACC of 7.65%.

If the 2014 ROI is restated using the DPP IRR calculation, it would be ~8.93%. This is higher than the 75th percentile vanilla WACC used for the price reset due to the following two key reasons:

1. Opex lower by \$5.1m relative to the DPP forecast; and
2. Commissioned assets lower by \$5.1m relative to the DPP forecast during the year

There has been no re-classification of items in the disclosure year, other than as set out elsewhere in this schedule.

The actual IRR (consistent with the DPP model) is higher than the DPP forecast mainly due to:

- Higher revenue
- Lower opex
- Lower additions and starting RAB impact

This is offset by the lower actual revaluation rate (actual 1.62% v forecast 2.01% which reduces the closing RAB (terminal cash flow).

***Regulatory Profit (Schedule 3)***

5. In the box below, comment on regulatory profit for the disclosure year as disclosed in Schedule 3. This comment must include:
  - 5.1 a description of material items included in 'other regulatory line income' other than gains and losses on asset sales, as disclosed in 3(i) of Schedule 3
  - 5.2 information on reclassified items in accordance with clause 2.7.2.

**Box 2: Explanatory comment on regulatory profit**

There has been no re-classification of items in the disclosure year.

Other regulated income has been derived from the recovery of bad debt.

*Merger and acquisition expenses (3(iv) of Schedule 3)*

6. If the GDB incurred merger and acquisitions expenditure during the disclosure year, provide the following information in the box below:
  - 6.1 information on reclassified items in accordance with clause 2.7.2
  - 6.2 any other commentary on the benefits of the merger and acquisition expenditure to the GDB.

**Box 3: Explanatory comment on merger and acquisition expenditure**

No merger and acquisition expenditure has been incurred during the disclosure year.

*Value of the Regulatory Asset Base (Schedule 4)*

7. In the box below, comment on the value of the regulatory asset base (rolled forward) in Schedule 4. This comment must include information on reclassified items in accordance with clause 2.7.2.

**Box 4: Explanatory comment on the value of the regulatory asset based (rolled forward)**

The value of the regulatory asset base has been determined by rolling forward the initial regulatory asset base with allowance made for additions, disposals, depreciation and revaluation in accordance with the Gas Distribution Services Input Methodologies Determination 2012 (IM).

**Reclassifications**

To comply with the asset classifications prescribed in the Information Disclosure input methodology (and therefore in Schedule 4(vii)) the following reclassifications of values are reported in the 2014 disclosure year.

Special crossings are now reported in the special crossings asset category whereas they were previously included in the pipeline asset category to which the special crossing related (i.e. intermediate pressure main pipelines, medium pressure main pipelines, low pressure main pipelines). The value of the special crossings assets in the 2014 disclosure year is \$4.8m and in the 2013 disclosure year was \$4.7m.

Weighted average lives were calculated for the special crossing using their standard asset lives as per the IM, and their RAB value at the end of the disclosure year.

The value of \$0.7m of intangible assets has been reclassified from the other network assets category to the non-network assets category. The value of these in the 2013 disclosure year was \$0.7m.

**RAB indexation**

RAB indexation is carried out in accordance with the information disclosure IMs using actual inflation rates. The revaluation rate that Vector has used for rolling forward the RAB is 1.62%.

In determining the starting price adjustment at the beginning of the regulatory period, the Commission assumed a revaluation rate of 2.01% in the 2014 year.

If the RAB had been rolled forward from 01/07/2012 using the Commission's forecast revaluation rates for 2013 and 2014 (the 2013 forecast revaluation rate was 2.14% compared with the revaluation required to be used under the input methodology of 0.68%) the 2014 closing RAB would be \$492m, an increase of \$8m.

Variations between the Commission's forecast indexation rate and actual CPI (applied to revalue the RAB for information disclosure purposes) results in revenue adjustments not being matched by changes in RAB. On this basis the value of financial capital is not maintained in the way it would be if the RAB was not subject to indexation for either information disclosure or price setting purposes. Inflation is outside the control or influence of GDBs, and in our view there is no reason for GDBs to be exposed to this risk as they cannot take steps to mitigate it.

*Regulatory tax allowance: disclosure of permanent differences (5a(i) of Schedule 5a)*

8. In the box below, provide descriptions and workings of the following items, as recorded in the asterisked categories in 5a(i) of Schedule 5a:

- 8.1 Income not included in regulatory profit / (loss) before tax but taxable
- 8.2 Expenditure or loss in regulatory profit / (loss) before tax but not deductible
- 8.3 Income included in regulatory profit / (loss) before tax but not taxable
- 8.4 Expenditure or loss deductible but not in regulatory profit / (loss) before tax

<b>Box 5: Regulatory tax allowance: permanent differences</b>		
	5a(ii) Disclosure of Permanent Differences	<i>(\$000s)</i>
	<b>Positive permanent differences</b>	
Row 11	<b><i>Expenditure or loss in regulatory profit /(loss) before tax but not deductible</i></b>	
	Non-deductible entertainment	11
	Non-deductible legal & professional fees	8
		<hr/> 19 <hr/>
	<b>Negative permanent differences</b>	
Row 16	<b><i>Income included in regulatory profit /(loss) before tax but not taxable</i></b>	
	Revaluation	7,548
		<hr/> 7,548 <hr/>

*Regulatory tax allowance: disclosure of temporary differences (5a(vi) of Schedule 5a)*

9. In the box below, provide descriptions and workings of items recorded in the asterisked category 'Tax effect of other temporary differences' in 5a(vi) of Schedule 5a.

**Box 6: Tax effect of other temporary differences (current disclosure year)**

	<b>Tax effect 28%</b> <b>(\$000s)</b>
<b>Positive Temporary Differences</b>	
<u>Provision &amp; accruals:</u>	
Accrued employee entitlements & related expenses	56
Accruals - general	<u>4</u>
	60
<b>Negative Temporary differences</b>	
<u>Provision &amp; accruals:</u>	
Provision for doubtful debts	<u>22</u>
Net of positive less negative temporary differences	38

*Related party transactions: disclosure of related party transactions (Schedule 5b)*

10. In the box below, provide descriptions of related party transactions beyond those disclosed on schedule 5b including identification and descriptions as to the nature of directly attributable costs disclosed under clause 2.3.6(2)(b).

**Box 7: Related party transactions**

A detailed description of related party transactions has been disclosed on Schedule 5b.

There have been no related party transactions within the disclosure year disclosed under clause 2.3.6 (2) (b).

*Cost allocation (Schedule 5d)*

11. In the box below, comment on cost allocation as disclosed in Schedule 5d. This comment must include information on reclassified items in accordance with clause 2.7.2.

**Box 8: Cost allocation**

There have been no re-classification of items in the disclosure year.

ABAA (accounting-based allocation approach) has been applied in accordance with the IM determination, to allocate not directly attributable costs in the disclosure year.

*Asset allocation (Schedule 5e)*

12. In the box below, comment on asset allocation as disclosed in Schedule 5e. This comment must include information on reclassified items in accordance with clause 2.7.2.

**Box 9: Commentary on asset allocation**

There has been no re-classification of items in the disclosure year.

Vector satisfies the thresholds in the IM determination to enable the application of ACAM to allocate not directly attributable fixed assets.

*Capital Expenditure for the Disclosure Year (Schedule 6a)*

13. In the box below, comment on expenditure on assets for the disclosure year, as disclosed in Schedule 6a. This comment must include:
- 13.1 a description of the materiality threshold applied to identify material projects and programmes described in Schedule 6a;
  - 13.2 information on reclassified items in accordance with clause 2.7.2.

**Box 10: Explanation of capital expenditure for the disclosure year**

A materiality threshold of \$500k has been applied to identify material projects and programmes described in schedule 6a. Projects or programmes where there has been expenditure above \$500k in DY14 have been separately disclosed.

Where an item disclosed in accordance with 2.3.1 of the Gas Distribution Information Disclosure Determination is classified differently from the previous year, 2.7.2 of the determination requires that the GDB provide details of the item in Schedule 14, box 10.

Vector has reclassified one item. In accordance with 2.7.2 we provide the required details:

- (1) The nature of the item is expenditure associated with Telemetry for Network Monitoring
- (2) The value of the item in DY13 was \$18k, and in DY14 is \$40k.
- (3) In DY13 this item was classified as System Growth
- (4) In DY14 this item was reclassified as Quality of Supply
- (5) This item was reclassified because further analysis of the expenditure determined Quality of Supply as a more appropriate primary driver.

*Operational Expenditure for the Disclosure Year (Schedule 6b)*

14. In the box below, comment on operational expenditure for the disclosure year, as disclosed in Schedule 6b. This comment must include:

- 14.1 Commentary on assets replaced or renewed with Asset replacement and renewal operating expenditure, as reported in 6b(i) of Schedule 6b
- 14.2 Information on reclassified items in accordance with clause 2.7.2
- 14.3 Commentary on any material atypical expenditure included in operational expenditure disclosed in Schedule 6b, including the value of the expenditure, the purpose of the expenditure, and the operational expenditure categories the expenditure relates to.

**Box 11: Explanation of operational expenditure for the disclosure year**

No assets were replaced or renewed under operational expenditure in the disclosure year.

There has been no re-classification of items in the disclosure year.

There is no material atypical expenditure to be declared in the disclosure year.



*Variance between forecast and actual expenditure (Schedule 7)*

15. In the box below, comment on variance in actual to forecast expenditure for the disclosure year, as reported in Schedule 7. This comment must include information on reclassified items in accordance with clause 2.7.2.

**Box 12: Explanatory comment on variance in actual to forecast expenditure****Expenditure on Assets:**

Overall, Vector's expenditure on assets is close to that forecast. However, there has been some variance between categories as explained below:

- Consumer connection expenditure increased due to increases on forecast population, higher connection numbers and to provide a new supply to a large customer in Pokeno, South Auckland
- System growth expenditure decreased against forecast due to the cancellation of a DY14 project to link the proposed Waikumete and Bruce McLaren gate stations
- Asset replacement and renewal expenditure decreased due to the delay and reclassification of several Hamilton pipeline projects and other minor replacement projects
- Other reliability, safety and environment incurred expenditure as a result of a reclassification of a Hamilton pipeline project (as mentioned above)
- Asset relocation expenditure decreased due to delays in third party road relocation projects
- Non network asset costs decreased due to a lower allocation to GDB of shared assets cost and fewer non-network projects for GDB

**Operational Expenditure:**

The decrease in Network Operational Expenditure is largely due to a change in process that led to a reduction in the number of mark outs and stand overs performed.

Decrease in Non Network Operational Expenditure is due to less corporate overhead costs being allocated to Gas Distribution than forecast.

The operational expenditure forecast was prepared on the basis that the business applied a markup of certain services of up to 17.2% This markup was not applied in the disclosure year.

*Information relating to revenues and quantities for the disclosure year*

16. In the box below please explain reasons for any material differences between target revenue disclosed before the start of the pricing year in accordance with clauses 2.4.1 and 2.4.3(3), and total billed line charge revenue for the disclosure year as disclosed in Schedule 8.

**Box 13: Explanatory comment relating to revenue for the disclosure year**

Target revenue in Schedule 7(i) of this disclosure is required to be the revenue as previously disclosed under clause 2.4.3(3) of the ID determination and relates to the pricing year (ending 30 September).

The total line charge revenue in Schedule 8 of this disclosure is required to be the revenue that relates to the disclosure year (ending 30 June).

As the disclosure year and pricing year are different, target revenue and total line charge revenue, under the definitions above, will differ.

In respect of the overlapping 9 month period between October 2013 and June 2014, target revenue (\$47.1m) differs from actual revenue (\$45.9m) due to lower average prices (-\$1.1m) than anticipated, unfavourable prior period wash ups (-\$0.2m) and slightly higher volumes (\$0.1m).

17. If price category codes or consumer groups (as applicable) have been changed in a disclosure year, please explain in the box below the effect of this on the allocation of ICPs, quantities and revenues between consumer groups disclosed in Schedule 8.

**Box 14: Explanatory comment relating to changed price category codes or consumer groups**

During the disclosure year ending on 30 June 2014, Vector has amalgamated a number of price categories as part of our annual price change on 1 October 2013.

The price change included removing the historical distinction between the pressure system that some commercial and industrial consumers connect to and removing the pricing zones that applied to one pricing category. This has resulted in the consolidation of a number of pricing categories as follows:

GNS2 and GNT2 have been amalgamated into GN02  
 GNS3 and GNT3 have been amalgamated into GN03  
 GNS4 and GNT4 have been amalgamated into GN04  
 GA02 and GA12 have been amalgamated into GA02  
 GAS3 and GAT3 have been amalgamated into GA03  
 GAS4 and GAT4 have been amalgamated into GA04

In order to disclose the information in Schedule 8 we have used the revised price categories to disclose the required information. The effect of the mapping of price categories has been the amalgamation of ICP's, quantities and revenues from the previous pricing categories into the consolidated 2013/14 pricing categories.

*Network reliability for the disclosure year (Schedule 10a)*

18. In the box below, comment on network reliability for the disclosure year, as disclosed in Schedule 10a.

**Box 15: Commentary on network reliability for the disclosure year**

Vector's unplanned SAIDI and SAIFI performance in the Auckland sub-network is consistent with previous years'. However, in the North Island sub-network, a single third-party incident in November 2013 resulted in an outage which affected 546 customers for 8 hours, accounting for 90% of the yearly total unplanned SAIDI result, also significantly increasing the unplanned SAIFI measure.

Vector's planned SAIDI in the Auckland sub-network decreased due to the completion of the cast iron pipeline replacement projects in Auckland. In the North Island network, planned work was re-focused from ongoing pipeline replacement work to that of riser valve replacements. This change in project work type resulted in a slight increase in SAIFI, although the corresponding SAIDI measure decreased due to shorter duration interruptions for the affected customers.

*Insurance cover*

19. In the box below provide details of any insurance cover for the assets used to provide gas pipeline services, including-
- 19.1 The GDB's approaches and practices in regard to the insurance of assets, including the level of insurance;
- 19.2 In respect of any self insurance, the level of reserves, details of how reserves are managed and invested, and details of any reinsurance.

**Box 16: Explanation of insurance cover**

Insurance costs are allocated to the gas distribution segment through an assessment of the proportion of assets insured for property insurance. Assets covered

- Auckland Distribution Networks Gate stations and DRPS.

The types of cover purchased for these assets include material damage, business interruption and contract works insurance.

In respect of the insurance cover the information reflects "insurance years" running from 1 September to 30 August each year and premium costs are allocated to the appropriate regulatory years to derive the premium values.

Company Name Vector – gas distribution business

For Year Ended 30 June 2014

## **Schedule 14a Mandatory Explanatory Notes on Forecast Information**

*(In this Schedule, clause references are to the Gas Distribution Information Disclosure Determination 2012)*

1. This Schedule requires GDBs to provide explanatory notes to reports prepared in accordance with clause 2.6.5.
2. This Schedule is mandatory—GDBs must provide the explanatory comment specified below, in accordance with clause 2.7.3. This information is not part of the audited disclosure information, and so is not subject to the assurance requirements specified in section 2.8.

*Commentary on difference between nominal and constant price capital expenditure forecasts (Schedule 11a)*

3. In the box below, comment on the difference between nominal and constant price capital expenditure for the disclosure year, as disclosed in Schedule 11a.

**Box 1: Commentary on difference between nominal and constant price capital expenditure forecasts**

The constant price capital expenditure forecast is inflated by the PPI forecast to convert it to a nominal capital expenditure forecasts.

Vector PPI forecast is based on the NZIER (New Zealand Institute of Economic Research) March 2014 PPI (Producer Price Index-outputs) forecast from 2014 to 2017. Thereafter, we have assumed a long-term PPI rate of 2.5%.

*Commentary on difference between nominal and constant price operational expenditure forecasts (Schedule 11b)*

4. In the box below, comment on the difference between nominal and constant price operational expenditure for the disclosure year, as disclosed in Schedule 11b.

**Box 2: Commentary on difference between nominal and constant price operational expenditure forecasts**

The constant price operational expenditure forecast is inflated by the PPI forecast to convert it to a nominal operational expenditure forecasts.

Vector PPI forecast is based on the NZIER (New Zealand Institute of Economic Research) March 2014 PPI (Producer Price Index-outputs) forecast from 2014 to 2017. Thereafter, we have assumed a long-term PPI rate of 2.5%.

Company Name Vector – gas distribution business

For Year Ended 30 June 2014

## **Schedule 15 Voluntary Explanatory Notes**

*(In this Schedule, clause references are to the Gas Distribution Information Disclosure Determination 2012)*

1. This Schedule enable GDBs to provide, should they wish to:
  - 1.1 additional explanatory comment to reports prepared in accordance with clauses 2.3.1, 2.4.21, 2.4.22, 2.5.1, 2.5.2, and 2.6.5.
  - 1.2 information on any substantial changes to information disclosed in relation to a prior disclosure year, as a result of final wash-ups.
2. Information in this Schedule is not part of the audited disclosure information, and so is not subject to the assurance requirements specified in section 2.8.
3. Provide additional explanatory comment in the box below.

**Box 1: Voluntary explanatory comment on disclosed information****Schedules 4(vii), 5e(i), 5g, 6a(iv), 9a, 9b, 11a, 12a – Special Crossings**

The definition of a special crossing is “*a section of main pipe or service pipe and associated assets (i.e., support structures, vents, casings etc.), where the associated assets are installed for the purpose of crossing a road, railway or river etc.*” We are not able to accurately ascertain from Vector’s historical records whether underground crossings have “associated assets”. In the absence of this information, we have not included any underground crossings as special crossings. More complete information is available in respect of overhead crossings and these have been assessed for associated assets and included in special crossings where appropriate.

**Schedules 9a and 9b – Asset Quantities**

A number of data quality improvements to the information in these schedules have been made since the previous 2013 disclosure. This means that for a number of asset classes, the quantity and age profile information of assets installed pre-2014 may not be identical to that disclosed last year.

**Schedule 9a and 9b – Asset Classes**

Service regulators are not included as an asset class in Schedules 9a and 9b. Per the ComCom External Issues Register #249, we have therefore fitted them into the class that most closely fits, being District Regulator Stations. Schedules 9a and 9b therefore include 232 service regulators in the medium pressure DRS class, and 15 service regulators in the intermediate pressure DRS class.

**Schedule 10a – Customer Disconnections**

Further to correspondence with the Commerce Commission over the period 8-25 October 2013, Vector reports customer requested disconnections in our interruption and reliability metrics where these interruption durations are under the control of the GDB (e.g. a requested relocation of a meter installation where the re-installation date desired by the customer for the said meter is as soon as possible).

Where a disconnection is requested either by the customer or by the emergency services and the reconnection time is beyond the control of the GDB (i.e. determined by the customer or other factors beyond the GDB’s control), these are treated as permanent disconnections from the perspective of interruption and reliability reporting and no interruption is recorded.

**Schedule 10b - Emergency Calls answered within 30 seconds**

Vector and Powerco jointly submitted a request to the Commission (29 September 2014) seeking an exemption from the requirement to disclose this metric at sub-network level. Vector subsequently received confirmation from the Commerce Commission (3 October 2014) that Vector has been provided an exemption (for the 2014 and 2015 disclosure years) from having to disclose the information on a regional basis. Therefore, the performance data for emergency call statistics is calculated at the overall network level;

this figure is then copied into both sub-network disclosures (i.e. both sub-networks show the same result as the overall network result).

**Schedule 11a – Capex Forecast:** Vector has made a correction to the forecast value of commissioned assets in Schedule 11a, which was disclosed in June 2014 in the Gas Asset Management Plan Update.