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Electricity Authority
Level 7, Harbour Tower
2 Hunter Street
Wellington

Vector Limited
101 Carlton Gore Rd
PO BOX 99882
Auckland 1149
New Zealand
+64 9 978 7788 / vector.co.nz

By email: wholesaleconsultation@ea.govt.nz

Submission on Internal Transfer Prices and Segmented Profitability Reporting

Introduction

1. This is Vector Limited's (Vector) submission on the Electricity Authority's (the Authority) consultation paper on *Internal transfer prices and segmented profitability reporting*, published on 8 April 2021 and updated on 20 April 2021.

Vector's feedback

2. Vector supports the proposed change to the *Electricity Industry Participation Code* as a **minimum** step in improving visibility, but believes segment reporting should be mandated with clearly defined segments, including generation (noting that the listed companies already do this but not in a standardised way, limiting its value for market participant, consumer and Authority purposes).
3. The disclosure of total revenue, relevant costs, volumes and average prices to a minimum of the gross margin level (including clear specification of discounts, etc where relevant) should be made for both the electricity retail and generation components, including all consumer segments. This is consistent with the actual practice of most of the listed entities in their public disclosures, albeit with differing implementation. The Authority should be seeking a solution that provides no less information than the large participants already provide publicly¹, but in a standardised manner and with sufficient explanation of methodologies to allow comparison and analysis.
4. We support full Internal Transfer Price (ITP) and methodology disclosure and recommend that the data should be disclosed at the financial half year as well, noting that the listed companies provide monthly operational updates (segmented) and significant information on performance at their half year results. The administrative cost to the large participants should be very low. It would also allow a better time series to be developed, with more quickly available information.
5. We support the segmented profitability reporting specific to electricity to the gross margin level, but for both retail and generation. We note that despite its potential complexities, most of the parties expected to be subject to this already report "Customer" EBITDAF or gross margin (and by segment, such as Mass Market, Business Customers, C&I and CFD sales²) or provide sufficient information from which a capable analyst can derive margins.

¹ For example see slides 14 to 21 on Contact's 2021 interim presentation <https://contact.co.nz/aboutus/investor-centre/reports-and-presentations#Annual-and-half-year-reports> or monthly operating report for April 2021 <https://contact.co.nz/aboutus/investor-centre/reports-and-presentations#Operating-reports>, slides 6 and 7.

² See Contact's Monthly Operating Report as an example.

6. It is clear from the listed companies' external reporting that they already have significant segment and cost reporting capabilities. As their internal profitability and pricing will be built from the cost of goods level, it should not be difficult for them to provide this level of information. For example, the electricity costs, lines, and metering are unique to electricity, and gas meters can be identified; hedges, FTRs are unique to electricity, etc and sales will already be classified by product and units, etc. Many of the issues the Authority is considering are already explained in public disclosures, e.g. different cash flows/segment EBITDAFs, etc and this disclosure by the parties at the levels required should not be a challenge for them.
7. The Authority should ensure that any disclosing parties' shared costs are clearly identified in determining segmented gross margins and methods disclosed (if relevant).
8. Other parts of the industry are subject to significant disclosure to ensure appropriate performance and behaviour. Given recent Authority investigations (UTS, ongoing concerns about pricing, etc) a greater level of disclosure is required from the competitive participants to improve confidence in the market.
9. The Authority should not consider this to be one off "set and forget" decision and should commit to reviewing the information disclosed and the requirements at least annually. This is necessary to ensure the disclosure it implements is fit for purpose. A review of the actual disclosures by the Authority will ensure the disclosing parties are subject to more than peer review.
10. The Authority should ensure that all of the information is available via the EMI website.

Concluding comments

11. We are happy to discuss this submission with the Authority. Please contact me at Neil.Williams@vector.co.nz or 09 978 7633.
12. No part of this submission is confidential, and we are happy for the Authority to publish it in its entirety.

Yours sincerely
For and on behalf of Vector Limited



Neil Williams
GM Market Regulation