Vector

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Keston Ruxton
Manager, Input Methodologies Review
Regulation Branch
Commerce Commission
44 the Terrace, Wellington 6140

By email: im.review@comcom.govt.nz

Dear Keston,

Vector cross-submission on the draft decision on cost allocation for electricity distribution and gas pipelines

1. This is Vector's cross-submission on the Commerce Commission's (Commission) Input Methodology (IM) review draft decision on cost allocation for electricity distribution and gas pipeline businesses, published on 22 September 2016.

2. Vector's contact person for this submission is:

   Richard Sharp
   Head of Regulatory and Pricing
   09 978 7547
   Richard.Sharp@vector.co.nz

3. No part of this submission is confidential.

Lack of evidence on removing the avoided cost allocation methodology for cost and asset allocation

4. A consistent theme across submissions was the lack of any compelling evidence for the Commission's draft decision to remove the avoided cost allocation methodology (ACAM). The Commission's proposal for removing ACAM rests on matters that are not new and do not conflict with the reasons for its inclusion as a permissible cost allocation method when the Input Methodologies were first set.

5. In this regard, Vector supports Contact Energy's statement:

   "*We encourage the Commission to consider the practical, rather than theoretical, outcomes of removing ACAM.*"

6. The practical outcome of removing ACAM will be to discourage electricity infrastructure sharing with other providers of essential infrastructure such as telecommunications networks

(including: copper pairs providing DSL and circuit switched telephony, ultra-fast broadband, cellular telephony and broadband networks and local WiFi networks) and transport infrastructure (such as public road lighting).

7. The theoretical concerns about the impact of ACAM are those which suggest:

> *"EDBs will invest hundreds of millions of dollars in emerging technology assets operated in contestable markets using regulated funding."*

8. We strongly encourage the Commission to act on evidence rather than hearsay or conjecture about EDBs distorting new technology markets. The removal of ACAM is likely to derogate from the statutory requirements of section 52T(3) of not unduly deterring investment in the provision of other goods or services, and the requirement of section 52R for IMs to provide certainty for suppliers and consumers. In this respect, EDBs will likely need to review the terms of asset sharing arrangements in light of the proposed change to ACAM for cost allocation.

The optional variation accounting based allocation approach

9. We support submissions recommending a simplification of the optional variation accounting based allocation approach (OVABAA). The Electricity Networks Authority (ENA) notes the current application of OVABAA is unnecessarily overcomplicated which is a key reason for it not being used successfully to date. To this end, we support suggestions to reduce the complexity for the application of OVABAA. This may include clear guidelines for OVABAA as suggested by the Electricity Retailers Association of New Zealand (ERANZ), displacing the need for director certification.

The costs of transitioning from ACAM

10. As discussed above, Vector is concerned about the Commission taking action on the basis of hearsay or conjecture as opposed real evidence. To this end, we find statements such as the following from ERANZ to be misleading:

> *"it is the understanding of ERANZ based on expert advice that the changes required to accounting systems are likely to be minor."*

11. The transition away from ACAM will require assets that had previously been treated as dedicated assets to now have some value apportioned to them between different services. This will also need to be done on a continual basis where EDBs have agreed to continue to share assets – such as with UFB providers going forward. Unison has estimated system

development costs to be $50K-$150K. Even where suppliers apply “low technology” approaches by maintaining spreadsheets, as suggested by ERANZ, these will require dedicated resources to apportion value at a point in time and for future shared services. These costs are real and should not be considered trivial.

Research and development

12. Vector recommends the Commission refrains from putting limitations on the research and development (R & D) activities of EDBs. Again the concern raised by ERANZ about R & D is not based on fact as there is no evidence to suggest R & D is being misused.

13. R & D is an important tool for businesses, including regulated suppliers. R & D allows businesses to test the impact of new technologies, alternative technologies and, more importantly, new processes. Accordingly, Vector would be concerned if its ability to use R & D was limited. There are multiple risks from limiting the use of R & D, including compromising the operation of the network, the health and safety of persons working on or near the network, and the end-user service experience.

14. We also do not believe R & D duplication is a legitimate issue for the Commission to be guarding against. It would be imprudent, or even negligent, for businesses to develop new processes, adopt or exclude new technologies or develop new communications protocols by only relying on the results of another supplier operating in a different part of the country. Similar to any other business operating in a competitive environment, regulated suppliers must be confident that any changes to their business (caused by internal or external factors) do not compromise the end-user experience.

Conclusion

15. Vector encourages the Commission not to make significant changes to IMs such as the proposed removal of ACAM at this late stage of the IM review especially when reasons for change are based on speculation rather than any evidence of misuse.

Yours sincerely
For and on behalf of Vector Ltd

Richard Sharp
Head of Regulatory and Pricing