

16 June 2008

Commerce Commission  
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**Wellington**

**Attention:** Chris Bishop

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#### **SUBMISSION ON DRAFT PROCESS PAPER (June 2008)**

1. Orion New Zealand Limited (Orion) has participated in the Electricity Networks' Association (ENA) deliberations and the ENA submission on the above draft process paper. Although Orion supports the ENA's submission, we would like to take the opportunity of this submission to outline the concerns that we have with the proposed sequential release of draft guidelines and sector-specific input methodologies. We wish also to highlight the importance of ensuring sufficient time is allowed for adequate consultation on these issues that are of central importance to New Zealand's electricity distribution sector.

#### **Process order**

2. We are concerned by the Commission's proposal to release draft guidelines and sector specific input methodologies sequentially when each of these matters would generally be determined concurrently. For example, when the Australian Energy Market Commission recently reviewed the regulation of electricity transmission services it released a single all-encompassing 'Rule' containing *all* of the relevant input methodologies.<sup>1</sup> The Ministerial Council on Energy is adopting a similar approach as it develops the new Australian National Gas Rules.<sup>2</sup>
3. The logic of employing such an approach is straightforward: most input methodologies do not exist in 'water-tight compartments'. The potential interdependencies between the cost of capital, asset valuation and taxation guidelines are especially apparent. For example, the risks attendant with different asset valuation methodologies can affect the appropriate regulatory cost of capital. Similarly, a key issue for electricity

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<sup>1</sup> Australian Energy Market Commission, *Rule Determination: National Electricity Amendment (Economic Regulation of Transmission Services) Rule 2006 No. 18*, 16 November 2006.

<sup>2</sup> See: <http://www.mce.gov.au>.

lines businesses is how the tax book value will relate to the regulatory asset base, and this relationship remains unspecified by the Commission.<sup>3</sup>

4. Until these critical linkages are apparent it will be impossible to make meaningful submissions on any guideline or sector-specific input methodologies in isolation, and the absence of these linkages will enhance the prospect for error in the Commission's rulings on these matters. Put simply, the guidelines and input methodologies amount to more than the sum of their parts and ELBs must first see how they all fit together for the consultation process to be effective. For this reason we support the ENA proposal that the draft guidelines and sector specific input methodologies each should be considered concurrently. However, if it is nonetheless considered necessary to manage the Commission's workload by staggering the release of guidelines and input methodologies the order in which they are released is critical if the process is to be robust.
5. Recognising the interrelationship between the cost of capital, asset valuation and taxation guidelines, we propose that the Commission release these together in Q4 2008. The Commission's current proposal to release the asset valuation guideline subsequently in Q1 2009 risks precluding meaningful consultation on the cost of capital and taxation guidelines since they are intrinsically related to the regulatory asset value. The guidelines pertaining to pricing principles and the allocation of common costs could then be released in Q1 2009, followed finally by the guideline on regulatory specifications in Q2 2009. Sector-specific input methodologies should be considered in the same succession.
6. Should the Commission persist with a sequential approach, we believe this alternative ordering represents a more sensible trade-off between managing the Commission's workload and ensuring a fully informed consultation process is able to occur. It will also serve to reduce the risk of regulatory error, which will be particularly significant if the Commission perseveres with its proposal to determine the cost of capital and taxation guidelines and sector-specific input methodologies before considering appropriate asset valuation guidelines and sector-specific input methodologies.
7. Accordingly, we strongly urge the Commission to reconsider the proposed order of the work streams as we have indicated above.

### **Process timing**

8. The Commission's proposal starts a process that will have far reaching consequences on investment decisions for monopoly network infrastructure businesses. We are therefore eager to ensure that the Commission has sufficient time to carry out a robust

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<sup>3</sup> We note that in the course of its review of the information disclosure regime relating to electricity lines businesses the Commission indicated a preference for a 'tax payable' basis for regulatory tax allowances. However, it did not broach the relationship between the tax book value and the regulatory asset base. See: Commerce Commission, *Regulation of Electricity Lines Businesses: Review of the Information Disclosure Regime, Companion Paper to the Exposure Draft of the Revised Information Disclosure Requirements*, 20 December 2007, p.37.

consultation process that provides interested parties with sufficient opportunity to provide their perspectives. We are conscious that the process also may be influenced by the passage of the Commerce Amendment Bill. This Bill has the potential to change fundamentally the current threshold regime applying to ELBs. This may require the Commission to develop further guidelines and input methodologies, including those pertaining to the default price-quality path proposed in the Bill.

9. Orion considers it is essential that the Commission and the industry takes the time through this process, however it unfolds, to develop a set of input methodologies that will result in continued efficient investment in an essential part of New Zealand's infrastructure. If this requires a longer timeframe for preparation of informative and considered consultation documents and for meaningful response from the industry then the consultation process should provide this time.
10. Thank you for the opportunity to make this submission. We look forward to seeing further details in relation to these vital matters for New Zealand's energy sector as they develop. Orion does not consider that any part of this submission is confidential. If you have any questions, please contact Dennis Jones (Industry Developments Manager), DDI 03 363 9526, email [dennis.jones@oriongroup.co.nz](mailto:dennis.jones@oriongroup.co.nz).

Yours sincerely

A handwritten signature in black ink, appearing to read 'Rob Jamieson', with a stylized flourish extending from the end.

Rob Jamieson  
**General Manager Commercial**