Auckland Energy
Consumer Trust

PO Box 109626, Newmarket, Auckland 1149, New Zealand
tel (09) 978 7673 **Fax** (09) 978 7516 **email** aect@aect.co.nz
www.aect.co.nz

12 November 2010

Karen Murray
Chief Adviser
Regulation Branch
Commerce Commission
P.O. Box 2351
WELLINGTON

Dear Karen,

Re: Submission on Revised Draft Determinations

On 22 October and 1 November 2010, the Commerce Commission (the Commission) released its revised draft determinations on input methodologies for electricity distribution services, gas distribution services and gas transmission services (the Revised Draft Determinations). The Commission has invited submissions from interested parties on Parts 1 to 4 and Schedule A by 12 November 2010 and on all other parts and schedules of the Revised Draft Determinations by 19 November 2010. The Commission expects this be the final consultative step before it determines the input methodologies for electricity distribution businesses (EDBs) and gas pipeline businesses (GPBs) by 31 December 2010.

The Auckland Energy Consumer Trust (AECT) holds 75% of the shares in Vector Limited, which owns electricity and gas distribution assets and gas transmission assets and will therefore be affected by the input methodologies. AECT is an elected body that operates on behalf of its income beneficiaries, who are consumers of Vector's services. As owner, AECT reflects consumers' concerns over the long-run outlook – more than 60 years – inherent in the lifetime of the trust. The need to satisfy its consumers requires its trustees to take an interest in the delivery of better service at appropriate prices. At the same time, sustaining and growing the business demands an emphasis by trustees on investment and efficiency.

In its previous submissions on the Commission's development of input methodologies, AECT focused on three areas of particular concern – cost allocation, cost of capital and asset allocation. The Commission's Revised Draft Determinations go some way towards allaying our concerns, but most remain. We would like to take this opportunity to remind the Commission of our main concerns in these areas.

In summary:

- Cost allocation – AECT remains concerned that the Commission's preferred method for treating existing assets when they become common capital, as an electricity distribution business (EDB) participates in the roll out of high speed broadband fibre, will inhibit efficient investment in the government's ultra-fast broadband initiative. AECT also considers that this treatment will create an uneven playing field for EDBs with and without investment in the broadband initiative.

- Cost of capital – AECT remains concerned about the Commission's preferred approach to estimating the cost of capital. The Commission has selected the simplified and counterintuitive Brennan-Lally version of the capital asset pricing model (CAPM) as the empirical framework and then estimated each of the model's parameters in isolation rather than estimated the model as a holistic system. AECT remains of the view that the Commission should estimate the parameters systematically and test the results against reality and results from other models.

- Asset valuation – AECT remains concerned over the use of the 2004 optimised deprival value (ODV – the deemed historic cost), updated using CPI-indexation, for asset valuation. Because this may have impacts on EDBs' cash flows, AECT recommended use of the 2004 ODV, adjusted, as proposed by the Commission, for new and retired capital and other changes that have come to light in the interim, but without updating using the CPI.

On cost allocation, AECT notes that, in its Revised Draft Determinations, the Commission has raised the threshold for the revenue materiality screening test from 5% to 20%. We consider this to be a move in the right direction, in terms of aligning EDBs' investment incentives in the broadband initiative, but we remain of the view that, in the case of investment in the broadband initiative, this investment should be treated according to the avoidable cost allocation methodology (ACAM) for the full period of the broadband fibre roll out regardless of its revenue share.

Our other concerns remain unabated.

AECT does not intend making a further submission on the Revised Draft Determinations by 19 November 2010.

Yours sincerely,

I R Ward.

Ian Ward
Executive Officer