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The Secretariat
Gas Industry Company Limited
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**FURTHER RESPONSE ON GIC LEVY PROPOSAL**

**Introduction**

1. Vector welcomes the opportunity to comment on the follow up consultation paper regarding the GIC's proposed design of the levy to recover the costs of its activities. The GIC's response has clarified certain areas, which Vector appreciated. There are, however, three remaining points we wish to raise; two substantive and one procedural.

**Summary of Vector's view**

2. Overall, Vector is pleased with the follow up report, and continues to support the GIC's proposed levy. In particular, Vector agrees that there is no strong reason as to why pipeline companies should pay a levy contribution, as such parties – while interested parties – are not the direct beneficiaries of the GIC's work at present. To the extent they are in future, the levy could change, or a direct fee be imposed. Furthermore, as evidenced by the Commerce Commission's treatment (under the regulatory regime for electricity lines businesses) of the Electricity Commission's levy – a direct pass through to retailers/consumers – there is no point in levying intermediate parties (pipeline operators) if the cost is simply passed on.

3. Vector agrees that further specification of the levy will become easier over time once the GIC has operated for a few years. That said, there is every reason for the industry to ensure that the processes set in place now are robust and efficient, because they will set the standard practice for future years and for any other regulatory bodies controlling the industry. Within that framework, our two substantive points are (further substantiated below):

- o we have some concerns about the perceived nature (implicit in the paper) of the relationship between the GIC and industry. The paper implies that the primary relationship for the GIC to manage is with the Minister, and that its relationship with the industry is secondary; and

- o we are concerned that the GIC appears to be missing an opportunity to establish conventions through standard practice that would protect the industry in the event an Energy Commission were formed.

4. Our procedural point is that we encourage the GIC to think-through how it would deal with levying for any additional activities during the financial year not contemplated when the levy regulations were prepared.

**Primary relationship**

5. The paper suggests that the key relationship for the GIC to manage in preparing its strategic plan and budget is with the Minister. For example, the paper advises that:

> "The GIC strategic plan and budget will be published when they are submitted to Government for approval".

6. Another example is that the paper says that a comparison of the GIC levy recommendations with those of similar bodies overseas and with earlier NZ gas sector levies is *"a good idea for the recommendations paper"*. Vector understands the reference to "recommendations paper" to be a reference to the recommended levy from the GIC to the Minister. In Vector's view, if this comparison is relevant information for the Minister in determining the levy (which it is), it is relevant for industry participants in commenting on the proposed levy. The GIC needs to take the industry with it, as well as the Minister.

7. Vector's view is that the GIC should consult industry participants on its strategic plan and budget prior to submission to the Government for approval. For the GIC to be a success, it needs to advance the interests of the industry as well as meet the Government's objectives, because under a co-regulatory model the GIC is more than an instrument of government policy.

8. To maintain its mandate, the GIC should consult with the industry on its strategic plan and budget. In this way, the industry can comment on whether the GIC is prioritizing its tasks and objectives in a manner that meets the industry's needs, as well

as the Government’s, before the plan is finalised. The Electricity Commission is required to consult with the industry on its budget. Vector expected the GIC to be at least as open as the Electricity Commission.

9. As well as the potential risk of opening a gap between the GIC and the industry, by not consulting on its strategic plan and budget, the GIC also risks criticism, notwithstanding its majority independent Board, that it is being managed by ‘a select club’, ‘its an industry jack-up’ and so on. Such criticisms can, over time, undermine industry arrangements, as experienced with the NZEM. Criticisms of this nature can be minimised by ensuring the strategic planning process is open and subject to comment.

**Establishing safeguards for the industry**

10. Section 43ZZF of the Gas Act 1992 provides that if the Government implements an Energy Commission, then such an action:

> “does not affect any gas governance regulations or rules made on the recommendation of the industry body.”

11. Hence, any process the industry would want to continue if an Energy Commission were implemented should be established by the GIC in order to set standard industry practice. Creating standard industry practice that is based on robust process and analysis increases the likelihood that such work becomes an ongoing convention (lowering the risk of change by another body). This is an approach the banking industry has successfully followed for numerous years.

12. An obvious candidate for such a convention would be that the GIC consults with the industry on its strategic plan and budget prior to submitting to the Government.

**Levying for additional activities**

13. Our procedural suggestion is that the GIC consider how it might deal with levying additional activities during its financial year, which are not covered by the levy regulations for that year. This may become necessary where a new activity requires funding earlier than the annual levy process time frame allows.

14. Although section 43ZZC(3) allows for the levy to add under-recoveries to the levy payable in subsequent financial years, Vector is not sure that “additional activities” would fall into the “under-recovery” category.

15. Admittedly the constitution of the GIC allows for an annual fee to be charged equally to shareholders, which could be used to recover levies outside of the regulations. However, not all industry participants may be shareholders (so the annual fee could be unfair); further, different allocations for different industry participants may be more

appropriate for the new activity (not possible with a standard annual fee). Therefore, ideally levies for additional activities should instead be dealt with in the levy regulations

16. Vector has raised this issue because it is a problem dealt with by the electricity industry. In a change from the 2004 regulations, the 2005 regulations allow the Electricity Commission to carry out additional activities not covered by the regulations and levy for those activities, at any time during the financial year. The Electricity Commission would still have to apply for further appropriation under section 172ZCA of the Electricity Act 1992, which requires prior consultation with industry participants, before it receives funding for any new activity.

17. The Gas Act 1992 does not have an equivalent appropriation section, since the GIC is an industry body and does not receive public money under the government appropriation process. Hence, there is presently a gap in the levy control process, albeit the GIC could proactively address this itself.

18. Levying without consultation and without allocation based on costs and outputs are practices that should not be encouraged for the gas industry. Therefore, Vector's preferred approach is for the GIC to clarify the consultation issue by recommending a regulation be added requiring the GIC to (at least):

> "...consult with industry participants and the Minister on any new levy rate and amount relating to an additional activity to be undertaken during the financial year after the regulations for that year have come into force."

**Closing comment**

19. If you would like further assistance or wish to discuss this submission, please contact Peter Alsop, Vector's Regulatory Manager, in the first instance (021 370 869).

Kind regards

**Simon Mackenzie**
Group General Manager Networks