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Ms. Tricia Jennings
Project Manager, Gas DPP reset 2017
Regulation Branch
Commerce Commission
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Dear Tricia,

Please regard this letter as our cross-submission on the "Default price-quality paths for gas pipeline services from 1 October 2017" process and issues paper dated 29 February 2016. In this letter we will use the terms "MDL", "we", "us" or "our" to refer to the Gas Transmission Business (GTB) of Maui Development Limited. We will focus on submissions made in relation to the 'form of control' topic for gas transmission.

We support the statement made by Methanex that "the proposal to introduce a pure revenue cap should create a more efficient means of dealing with over/under recovery resulting from variability in gas supply/demand which is a feature of the New Zealand natural gas market". We also agree with their view that wash-ups for over- and under-recoveries of revenue should include a time-value-of-money adjustment.

We are surprised by the view from the Major Gas Users Group (MGUG) to argue for a weighted average price cap (WAPC) for all gas pipeline businesses. MGUG refers to its submission of 24 March 2016 on the Commission's paper with "Emerging views on form of control". Based on a review of that submission as well, we offer the following comments.

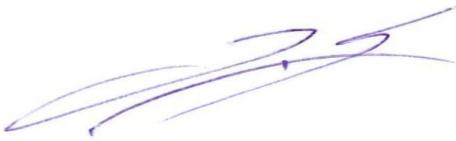
- MGUG correctly points out that distribution demand is a subset of transmission demand. In other words, all gas flowing through distribution pipelines must have flowed through transmission pipelines first.
- The graphs provided in MGUG's submission show that the aggregate of all distribution demand is currently less than 20% of total transmission demand. Contrary to their view, we do not consider this to be a large degree of overlap.
- This means that over 80% of current gas transmission demand is from direct connect consumers. These are all petrochemical plants, power stations, and other industrial scale consumers.
- One of MGUG's main arguments is that this demand is not difficult to forecast. We submit that the evidence demonstrates the opposite.
 - MGUG's graphs demonstrate the variability of the bulk of gas transmission demand (this would be visually obvious if all graphs were set to the same scale).
 - Actual demand has developed quite differently from forecasts made 5 years ago.
 - In 2010, for example, we were concerned about potential capacity constraints caused by additionally planned power stations in Auckland. Due to similar concerns about transmission capacity shortages, Gas Industry Co (GIC) initiated its Gas Transmission Investment Programme in 2011. The reversal of those concerns, and the subsequent closures of power stations in Auckland, were completely unforeseen at the time.

- MGUG suggests that this problem can be resolved because: "... there is no reason why a prudent GTB would not request and rely on consumer forecasts to remove potential information asymmetry." The difficulty with that suggestion is that the relevant industrial consumers did not foresee the actual demand trends, i.e. reopening of methanol trains and closure of power stations, 5 years in advance either.
- The issue with gas transmission forecasting is a lack of overall predictability of gas production and bulk consumption. Long-term exploration and production trends for gas fields are driven to a significant degree by international oil prices, which have obviously proven to be highly unpredictable. Bulk gas consumption trends are driven mainly by demand and prices for methanol, milk, urea, steel, and electricity generation. In the case of electricity the need for gas-fired generation will be increasingly driven by peak demands and peak pricing. None of these can be considered as reliably predictable over a 5-year period.
- In summary: nobody knows what gas transmission demand will look like 5 years from now.
- MGUG's other main argument is that GTBs can set tariffs to influence demand and to encourage transmission volumes to stay and grow. Again, we submit the evidence demonstrates the opposite.
 - If MGUG's statement were correct it seems unlikely that demand over the last 6½ years would have changed as it actually did. In reality, we doubt that any material correlation between transmission throughput and transmission pricing can be found.
 - As we have submitted earlier, in our submission of 28 January 2016, our transmission fees for gas deliveries to Methanex are 0.08 to 0.18 \$/GJ and to the Huntly Power Station are 0.44 to 0.55 \$/GJ (depending on the origin of gas). Those transmission fees represent a small fraction of the actual price of delivered gas.
 - To provide perspective, those transmission fees can be compared against the wholesale spot market price of gas as reported by emsTradepoint. Their quarterly index price (FRQI) as per 31 March 2016 was 4.97 \$/GJ. The standard deviation of their Daily Volume Weighted Average Price (for days with trades) during the first quarter of 2016 was 1.31 \$/GJ.
 - This means our transmission fees are less than a typical daily fluctuation in wholesale spot market prices. As a result, it seems extremely unlikely that our fees could be materially influencing demand.
 - The actual driver of demand for gas is the price of gas. More specifically, for the bulk of transmission demand the driver is the ratio between the price of gas and the price of methanol, or electricity, or urea. The transmission fee is only a tiny fraction of this, and any change in transmission pricing would be dwarfed by changes to the wholesale price of gas.
 - This is also supported in the "Long term gas supply and demand scenarios" prepared by Concept Consulting Group for GIC. The demand scenarios in this paper depend on the wholesale price of gas. The report does not even mention transmission fees or tariffs as a relevant consideration.

- It appears to us that MGUG's evidence actually strengthens the case for a revenue cap for gas transmission. The bulk of gas transmission demand is variable, subject to lumpy changes which were not projected in advance; certainly not over a 5-year time frame. At the same time, there is no link between historical changes in gas transmission demand and changes in gas transmission tariffs.
- We also note that a WAPC would make it more difficult to adjust gas transmission tariff structures and would strengthen the desire for a GTB to set a pricing methodology to insulate itself from demand risk (over which it has no control). This in turn could create barriers for operating code convergence between gas transmission pipelines. We expect this is the opposite of what MGUG would want to see.

We have appreciated the opportunity to provide this cross-submission. For any additional questions or clarifications please do not hesitate to contact us.

Yours sincerely,



Jelle Sjoerdsma
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for Maui Development Limited