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Paul Mitchell
Regulation Branch
Commerce Commission
PO Box 2351
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CC: commercial.operator@mauipipeline.co.nz

Dear Mr. Mitchell,

Maui Development Limited (MDL) thanks the Commerce Commission (Commission) for the opportunity to provide a submission on the Draft Information Requests and Process Update for the Default Price-quality Paths for Gas Pipeline Businesses. We note the Commission's intention to set starting points for a DPP based on an assessment of our current and projected profitability. We have also noted the Commission's proposed schedule for the provision of the information it requires. MDL can meet this schedule principally because its Maui Pipeline business is conducted separately and ring-fenced from its other activities thus allowing the application of a much less complex cost allocation and categorisation process than will be faced by other businesses. Also much of the information requested regarding taxation and debt information does not seem to apply to MDL. Even then the resulting workload and costs faced by MDL will be significant. Given this we would appreciate a review by the Commission of its requirements for the detailed information requested as the usefulness of some of it is not immediately apparent to us.

With regard to the information requested from us we would like to make the following comments.

- For **"Transmission revenue through prices"** we intend to report the income collected from tariffs that were set under the provisions of the Maui Pipeline Operating Code (MPOC). As we presented in previous submissions, these tariffs for each year are smoothed to compensate for over- and under-recoveries in prior years of revenues allowed by the MPOC. Allowance needs to be made for these factors when using these figures as a basis for projections.

- We intend to report income from interconnection charges as **"Other regulated income".** These charges represent reimbursement of costs incurred by MDL for supervising and approving interconnections to the Maui pipeline. We would like to discuss the treatment of the matching costs with the Commission at a later point.

- We will treat unallocated balancing charges as a **recoverable cost**. As noted in previous submissions, MDL both buys and sells gas to maintain the pipeline conditions needed to meet gas transmission requirements. It also uses the mechanisms provided in the MPOC to charge pipeline users for some of the costs it incurs in balancing the pipeline. The methods for assessing balancing charges are currently under review, and the changes already introduced over past years have substantially altered pipeline users' behaviour which in turn has changed the overall impact of balancing charges on MDL.

    - We intend to assess unallocated balancing charges in terms of the total net financial impact on MDL, (either positive or negative), of the actual income and expenditure resulting from all gas purchased or sold for the purpose of meeting gas transmission requirements whether by direct purchase or sale by MDL or as a result of cash-outs. We will also include any actual recoveries of cost resulting from balancing or peaking charges made to pipeline users through the Incentives Pool Trust. In doing so we make the following points:

    - Fuel gas costs will be excluded from the calculation. They will be treated as an operating cost.

    - The impact of net Unallocated Balancing Charges on MDL has been very variable from month to month and year to year. Currently it is a significant cost, but there have been periods when the charges levied under the MPOC have exceeded expenditure. It should not be expected that the financial outcome experienced during any reference period will be useful in predicting future outcomes.

    - The balancing charging regime in the MPOC remains under review.

    - Charges for balancing gas, (and fuel gas), have been held to an artificially low level as a result of a negotiated settlement of a dispute between the Maui Mining Companies and pipeline users. This settlement requires the supply of a specified quantity of gas which is expected to be exhausted early in 2012. Prices for this gas have ranged between zero to 70 cents/GJ, (the ETS charge), while purchase of the same gas on the Balancing Gas Exchange would normally range between $6.00 to $8.00/GJ, but could be more in some circumstances. When full market prices have to be paid for the purchase of balancing gas, the net unallocated cost of balancing to MDL can be expected to increase.

- We do not regard the breakout of operating expenses proposed by the Commission as particularly useful. For example, MDL itself currently does not have any staff or administration. Instead, services have been provided to MDL's Gas Transmission Business by the Maui Mining Companies – without charge – or by independent operators. We have previously submitted on the expense categories that we actually do use. Nevertheless, we will endeavour to assign our operating expenses under headings requested by the Commission. In particular, where contracts entered into by MDL or its operators have a specified component or charge for overheads or administrative costs we intend to include

this charge as part of the **"General management, administration and overheads"** category. Where they do not the entire contract costs will be assigned to the appropriate Opex category.

- We also intend to identify operating expenses, for past and current reporting periods, to include costs borne by the Maui Mining Companies on behalf of MDL's Gas Transmission Business even though these have not been previously reported on. These costs include, but may not be limited to, the following items.

    - Insurance costs for the Maui pipeline. Different Maui Mining Companies have taken different views on the type of insurance cover that is appropriate and these include different levels of self-insurance, which nevertheless has a potential cost associated with it. The policies owned by the Maui Mining Companies cover a number of assets, sometimes world-wide, and it is difficult to extract an insurance cost specifically associated with the Maui Pipeline. We propose using an insurance broker to estimate the cost of the cover for our pipeline that would normally be taken out by a prudent pipeline operator.

    - Director's fees. We intend to estimate fees that would normally be payable to members of the Maui Pipeline Sub-committee of the MDL Board, which effectively acts as the Maui Pipeline governing body.

- We expect we may need to make adjustments to our Regulated Asset Base to include spares held for MDL by Vector, which were not previously counted.

- Our Regulated Asset Base is derived from reports that were initially prepared by Maunsell Limited. The first of these provided an inventory of assets used for MDL's Gas Transmission Business, and a valuation of their Optimised Depreciated Replacement Cost, as at 31 December 2006. Valuations before this date are not available.

- We should note that the costs and assets of MDL's Gas Transmission Business are not intermingled with any other business. Therefore, all of those costs and assets are directly attributable to the Gas Transmission Business only, and we have no need to determine allocations when completing Schedules A2 and A5.

- MDL is not a tax-paying entity. We assume a notional tax rate will be applied and that it will not be necessary to complete the Tax Permanent Differences and Tax Temporary Differences sections of Schedule A.6.

- Completion of Schedule B will not be required because MDL itself does not have a debt portfolio.

With regard to the future assessment of Starting Price Adjustments by the Commission we would like to make the following points.

- Based on previous communications we expect MDL will have a revenue cap instead of a price cap. Therefore, we assume the Commission will make

appropriate adjustments for that.

- As mentioned before, our current revenues include a discount to compensate for over-recoveries from levels allowed under MPOC in the past. In order to maintain smooth price adjustments for pipeline users we request the Commission to allow such under- and over-recoveries to be managed within the DPP.

- We believe interconnection charges should not be treated as revenue for the purposes of assessing MDL's performance against its allowable revenue. These charges are only made when a party wishes to make a physical interconnection with our pipeline. In such a case we only charge that specific party to recover costs we incur to facilitate that interconnection, without any margin for profit.

- As noted above, balancing costs and charges may change significantly in the future. Even though only the net unallocated balancing costs will be reported as a **Recoverable** cost, we expect this may change significantly too.

- Costs of fuel gas will also rise significantly in the future, for similar reasons. In recent times MDL has been able to purchase its fuel gas at a zero or nominal cost. When the quantity of gas available at a low price is exhausted MDL will have to pay full market price for all of its fuel gas. We propose to report fuel gas costs as a separate item in **Systems management and operations Opex** cost.

We trust the Commission will take these points into account when assessing the Starting Price Adjustments to be made. If it would be useful we will be happy to clarify or discuss these points in more detail with the Commission.

Yours sincerely,

Don Gray.

General Manager, Commercial Operator Maui Pipeline

for Maui Development Limited