GasNet
Connecting communities

10 March 2022

New Zealand Commerce Commission
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Regulation Branch
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RE: Non Weighted Average Cost of Capital (WACC) components of the IM Reasons Paper

1.0 GasNet Limited (GasNet) thanks the NZ Commerce Commission (NZCC) for the opportunity to respond in regard to non WACC components of the 'Proposed amendments to input methodologies for gas pipeline businesses related to the 2022 default price-quality paths Draft reasons paper Date of publication: 10 February 2022' (IM Paper).

2.0 GasNet has concluded that sections 3.10 to 3.12 inclusive at page 16 (and context elsewhere in the IM Paper) are outside the response requested at this time. Thus GasNet is responding to sections 3.4 to 3.9 inclusive at page 15-16 (and context elsewhere) of the IM GPB 2022 DPP Paper.

3.0 GasNet notes the need for consideration of these matters is triggered by the proposed shorter DDP period and supports the proposed amendments to enable alignment with the DPP3 period. On this basis GasNet would also support the Commerce Act 1986 (Act) being amended to remove a minimum DPP period.

4.0 GasNet is supportive of the proposed amendments relating to asset stranding, treatment of operating leases and the capacity events and risk events capital expenditure reopeners.

5.0 Economic network stranding – adjusting depreciation

5.1 GasNet welcomes the potential introduction of network stranding to the IMs as it is a logical concern under any regulatory context. The NZCC has indicated that it is introducing this to mitigate "… the risk of economic network stranding from long-term declining use of gas networks." (section 3.5, page 15 of the IM Paper). Currently the long term decline of natural gas use is dependent on macro-economic matters around upstream field economics and industrial usage at transmission level.

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Potentially this will be augmented by climate response mandates by Government. At that point climate change would be a "material risk" as discussed at section 3.25.3 page 21 of the IM Paper. These are all reasons to support having an IM available for possible network stranded being "… central to defining the balance of risk and benefits between suppliers and consumers." (section 2.22, page 13 of the IM Paper).

5.2 What is less unclear to GasNet is the NZCC's intention to use this now, via accelerated depreciation, while excluding existing/new change event reopeners "… to address climate change policy uncertainty." (section 1.8, page 7 of the IM Paper). The NZCC has stated that it is constrained by Commerce Act 1986 to limited consideration to natural gas as discussed in the Reset DPP3 Paper, so is it not also reasonable to be constrained to existing market settings at the time of the DPP3 reset?

5.3 Regarding the NZCC interest in submitter views at section 3.23, page 20 of the IM Paper regarding application of accelerated depreciation to assets or asset classes as outlined, GasNet notes that the Gas Distribution Services Input Methodologies Determination 2012 (Consolidated April 2018) at Schedule A, Standard Physical Asset Lives specifies 'Standard Physical Asset Life (years)'. On this basis HP, IP and MP Mains, Services, Valves, Crossings and spares appear relevant together with Station site developments and buildings. GasNet continues to operate significant low pressure (LP) Mains, Services, Valves, Crossings and spares and Station site developments and buildings.

6.0 Treatment of operating leases

GasNet agrees with this approach. Currently this would mean a small number of treatments for GasNet, relating to some DRS (station) land leases, some office equipment and our office/depot location. GasNet notes that short leases of significant value will introduce depreciation spikes.

7.0 Capital expenditure reopeners

7.1 GasNet welcomes the potential introduction of capital expenditure reopeners to the IMs as it is a logical concern under any regulatory context. GasNet notes that the NZCC is looking to provide price path DPP reopeners under capacity events and risk events. For GasNet it is envisaged that the minimum/maximum trigger in any DPP year would be $100,000/$350,000. In addition, the NZCC appears to be looking to provide capex reopeners where "… the risk that the capex allowances we set in this DPP are insufficient to deal with network asset risk or projects that are unknown or uncertain at the time the DPP was set, …" (section 3.61, page 28-9 of the IM Paper).

7.2 GasNet makes the following observations:

- are NZCC levies envisaged to increase to administer reopeners
- are there to be specific transaction costs applied by the NZCC regarding a DPP reopeners and/or the capex reopener

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- what constitutes the 'test of prudency and efficiency' and/or for a risk event a "… remediation investment needs to be prudent and efficient supported by a probabilistic risk assessment, where appropriate." (section 3.47, page 26 of the IM Paper)

- GasNet is unclear from the IM Paper that there is a difference between a "risk event" reopener and a capex reopener in a material sense as the NZCC has indicated that are both are dealing with risk. In regard to the latter the NZCC appears to find this necessary as it has dropped "… add[ing] margins to historical average capex projections to account for typical year-on-year functions that tend to occur in capex." (section 3.59, page 28 of the IM Paper).

- GasNet respectfully request that the NZCC reconsider the intent to drop the concept of adding margins to historical average capex projections to account for typical year-on-year functions that tend to occur in capex as thus observation remains as valid today as it did in 2012. In fact, GasNet considers that the NZCC has focused only on ex-post GID data and GasNet would draw the NZCC's attention to its 2021-2031 AMP at Schedule 11a (page 77) where we have indicated an intention to spend around $1,000,000 per annum across the forecast period. GasNet's capex spend for the 2020-21 GID year was circa $1,000,000 + WIP. GasNet respectfully requests that the NZCC reconsider its $700,000 assumption based on GasNet's ex-post 2020-21 GID year data and its 2021-2031 AMP ex-ante data. On this basis our suggestion would be $950,000.

- Assuming capex reopeners remain, GasNet is not clear from the IM Paper whether the NZCC intent a capex reopener to have the same minimum/maximum triggers as capacity events and risk events. Assuming this is the case, then it suggests to GasNet that it may decide to apply for a capex reopener each year of DPP3. However, adding internal/external costs to document a case under the prudency and efficiency test appears a disincentive and a similar, albeit a cheaper process, to that associated with a CPP application. GasNet has historically maintained that for it, the costs of applying for a CPP outweigh the benefits sought notwithstanding the risk of the NZCC declining approval.

- For GasNet, the NZCC has set the capacity events and risk events reopener at $100,000/$350,000 minimum/maximum triggers in any DPP year based on an ex-post DPP2 average (at 2021) of $700,000. Given the narrative above, GasNet respectfully requests that the NZCC reconsider these trigger values based on GasNet's ex-post 2020-21 GID year data and its 2021-2031 AMP ex-ante data. Our suggestion would be $200,000/$500,000 minimum/maximum triggers in any DPP year.

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- More generally, GasNet is concerned at the level of administration that is likely to be involved in preparing reopener applications and thus resource diversion and associated costs that will need to be expensed as opex irrespective of the NZCC decision on the application.

8.0 GasNet looks forward to contributing further.

Regards

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