GREYMOUTH GAS

14 March 2022

Attn: Regulation branch
Commerce Commission
PO Box 2351
Wellington 6140

By email: regulation.branch@comcom.govt.nz

RE: Default price-quality paths for gas pipeline businesses from 1 October 2022

1. Greymouth Gas New Zealand Limited (**Greymouth**) welcomes the opportunity to provide this submission on the Commerce Commission's (**Commission**) Default price-quality paths for gas pipelines businesses from 1 October 2022 – Draft Reasons Paper dated 10 February 2022 (**Draft DPP decision**).

2. Greymouth notes the Commission's recently published report on competition amongst New Zealand supermarkets. Greymouth expects that the Commission will be cognisant of regulated gas pipeline businesses (**GPBs**) (mostly foreign-owned) enjoying windfall revenues[1] at the cost of Aotearoa businesses and consumers.

3. Greymouth's submission focuses on climate change matters and accelerated depreciation of pipeline assets.

Further consideration for climate change is imperative

4. The Commission has not fully considered climate change in its Draft DPP decision, preferring to push that to its Input Methodologies Review process (**IM process**).[2] Therefore any result from the comprehensive consideration of climate change will manifest in the Default Price-Quality Path (**DPP**) 4 starting in 2026. Nevertheless, the Commission has considered the increased risk of asset stranding due to declining natural gas as New Zealand pursues its 2050 target. This is the basis for a proposed amendment to the input methodologies for the DPP period commencing 1 October 2022 (**DPP3**) to allow implementation of its proposal for accelerated depreciation. To enable this, the Draft DPP decision references s5ZN of the Climate Change Response Act 2002 (**CCRA**) which allows the Commission to take into

[1] Page 6 of 'Draft default price-quality paths for gas pipeline businesses from 1 October 2022 to 30 September 2026' dated 10 February 2022, by Vhari McWha, Associate Commissioner
[2] Draft DPP Decision at X62 and X63

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account New Zealand's 2050 target. Greymouth submits that the Commission should consider the following points, in the context of the 2050 target:

a. The 2050 target[3] pertains to *net* emissions, not *gross* emissions. There is no evidence in the 2050 target definition to support the Commission's underlying assumption that natural gas will not be piped in New Zealand beyond 2050. Therefore the 2050 target should not be a basis to argue for accelerated depreciation.

b. Having elected to optionally consider the 2050 target, the Commission must then:

   i. Take that wholly into account. E.g., if pipelines are deemed to have an end date without a replacement use, then 'taking into account' should consider both accelerated depreciation *and* redistribution to consumers of accrued depreciation funds if there is no subsequent gas infrastructure investment.

   ii. Consider how that affects the purpose of Part 4 of the Act. E.g., with reference to the sub-parts of s52A of the Act, (a) investment incentives for gas pipeline infrastructure are not applicable if gas use is ending, (b) and (c) efficiency and quality incentives are either not applicable for the same reason or do not themselves justify accelerated depreciation, and (d) whether or not pipeline businesses extract excessive profits will depend on the accounting treatment further to i. above.

c. The 2050 target also requires alternatives gases to be considered. This point is discussed later in this submission.

5. Greymouth submits that the Commission should not consider one matter (accelerated depreciation) from the forthcoming IM process early (in DPP3) in the absence of considering interrelated matters, especially in the context of consumers facing billions of dollars of cost increases through to 2050, and up to $0.3 billion of cost increases in 2023-2026.[4]

6. The current regulatory framework is not fit for purpose in a declining gas market.[5] If climate change is considered in a DPP using the current Act, the purpose of Part 4 of the Act is obsolete and unworkable – because climate change will lead to inefficient markets for carbon-rich fuels (and one day no market). It is therefore critical that the Commission urgently and actively seeks necessary legislative changes to enable it to properly consider how to manage regulated pricing for GPBs in the context of the net zero carbon transition. This may even be a prerequisite to completing the forthcoming IM process.

Accelerating depreciating further entrenches GPBs' 2013 asset windfall gain

7. The introduction of the DPP regime in 2013 resulted in GPBs setting their regulated asset bases based on an optimised depreciation replacement cost significantly higher than historical cost. This provided a profit windfall for pipeline owners and a transfer of wealth

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[3] s5Q of the CCRA

[4] Extrapolating, and inferring from, the Commission's graph referred to in footnote 3

[5] Greymouth's submission on Process and Issues Paper, 30 August 2021; Letter to the Minister of Energy, 6 August 2019

from consumers. At the same time, regulators did not properly consider the excess profits earned by GPBs prior to 2013.

8. While this may not have been a significant issue when the natural gas market was in a growth phase, Greymouth submits that the risk of GPB's earning excess profits increases as the industry declines. Greymouth has previously raised this issue with the Minister for Energy[6].

Accelerating depreciation allocates risk onto consumers and producers

9. The Commission's draft decision does not consider that consumers (particularly large consumers) and producers are facing asset-stranding risks because of the phasing out of natural gas, and in many cases do not have the same opportunities to repurpose those assets. Those consumers and producers do not have the luxury of a regulated price-setting process allowing them to recover their asset costs in full ahead of 2050.

10. Further, the draft DPP Decision has not found balance between the Part 4 purpose items it cites on page 44. This is because, respectively, a) GPBs will invest for safety and reliability regardless of the decision on accelerated depreciation, b) it is normal in business to have stranded asset risk and GPBs should be no different (that is a matter for the IM process), and c) in order for consumers to get predictable prices then the prices need to be affordable. Greymouth submits that proper balance here cannot be found outside of the IM process, and that the current balance proposed for DPP3 is tilted significantly in favour of GPBs.

Accelerating depreciation risks accelerating the decline of the natural gas market and is counter to sustainability and climate change principles

11. The impact of accelerated depreciation on transmission and distribution pricing over DPP3 will be significant and will be in addition to the increases to gas prices consequential on increasing carbon charges.

12. This may have the effect of artificially accelerating the decline of the natural gas market which, in the absence of alternative fuels for some, could be catastrophic for New Zealand's energy security during the transition to net zero, and/or may significantly increase reliance on coal for electricity generation and industrial processes as was seen in 2021.

13. Further, increased prices will impact disproportionately on consumers who do not have the financial capability to invest in alternative energy sources in the near term – such as low-income families who rely on gas for cooking, water and space heating.

The Commission should give greater consideration to alternative gases

14. Greymouth considers the Commission has overstated the likelihood of pipeline assets becoming stranded. Greymouth submits that the Commission should not exclusively consider 'natural gas' (which it concedes is not defined in the Commerce Act),[7] but that consideration should also be given to the possibility that the pipelines will be repurposed for alternative gases.

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[6] By letter dated 6 August 2019
[7] Draft DPP Decision para 3.30

15. There is a very high likelihood that gas pipelines will continue to be used long past 2050: see for example www.gasenergy.org.nz, of which First Gas is a campaign partner, which assures New Zealanders that 'gas energy' is here to stay, but will move to zero carbon.

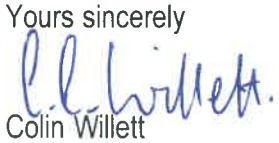
16. If the ability for pipelines to be repurposed and continue to be used after 2050 is ignored, current natural gas consumers will continue to subsidise future 'gas energy' consumers and will deliver further windfall gains to regulated GPBs. In a competitive market it would be expected that market participants would repurpose assets facing stranding risk rather than allow such assets to become stranded.

17. If the Commission considers it should take into account the 2050 target, it should also take into account the alternative gases that will form part of the transition to net zero. If it considers that it cannot do so under existing legislation, the Commission should defer any decision on asset stranding risk, and the consequences of it, until the next DPP period and seek legislative amendment in the meantime to enable it to take proper account of alternative gases.

18. For the reasons set out above, Greymouth considers that allowing accelerated depreciation in DPP3 will produce outcomes that are contrary to the purpose set out in Part 4 of the Act. Accelerated depreciation allowances should therefore be removed for DPP3.

19. No part of this submission is confidential. Greymouth will discuss any points in this letter with the Commission, and any queries should be directed to Chris Boxall (chris.boxall@greymouthpetroleum.co.nz) in the first instance with a copy to Colin Willett (colin@greymouthpetroleum.co.nz).

Yours sincerely



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