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Commerce Commission
Wellington, New Zealand

Re: GPB IM Amendments

Fonterra thanks the Commerce Commission for providing the opportunity to express our views on the "Proposed amendments to input methodologies for gas pipeline businesses related to the 2022 default price-quality paths" consultation paper ("Consultation Paper").

Fonterra uses 4.8PJ per annum of gas directly or via steam generated by our third-party cogeneration partners which use approximately 7.8PJ per annum to generate steam and electricity. This combined annual gas usage of approximately 12.6PJ is the largest industrial use volume on the gas pipeline network. Due to Fonterra's manufacturing sites being located throughout the regions represents that largest collective kilometres of pipeline use, from Kauri at the northern end of the gas pipeline to Pahiatua in the south, Edgecumbe in the eastern Bay of Plenty, to Whareroa in the Taranaki region.

Fonterra does not support the draft decision to amend the Gas Distribution Business's (GDB's) and Gas Transmission Business (GTB) Input Methodologies (IM's) to allow for accelerated depreciation via use of asset life adjustment factors.

Regulatory un/certainty

In section 2.4 of the Consultation Paper, it notes that the Commerce Commission has the statutory context to modify the depreciation rate as a way to promote certainty due to regulation or proposed regulation. We note that this assertion is flawed as there is currently no regulation or proposed regulation before Parliament that will accelerate the decline of gas usage. This is also shown by the subsequent discussion in section 4.6 of the Consultation Paper regarding the lack of need for a customised event reopener where it is stated that "it is also likely that climate change policy will have longer term impacts rather than have an immediate material impact on DPP3".

In section 2.5 of the Consultation Paper, it is acknowledged that the Court of Appeal has observed that "certainty is a relative rather than an absolute value". The proposed accelerated

depreciation IM is attempting to provide absolute certainty to one very small sector of New Zealand industry when the whole of New Zealand industry will face climate change policy regulation uncertainty without any similar regulatory backstop for stranded assets, such as the numerous coal or gas boiler assets that will become stranded.

FirstGas due diligence

FirstGas purchased the Maui and Vector pipelines in 2016. New Zealand's first Climate Change legislation was in 2002 with the passing of the "Climate Change Response Act 2002" (2002 No 40) whose purpose was to ratify the UNFCCC Kyoto Protocol. This was then amended in September 2008 to include the construct of the NZ Emission Trading Scheme (ETS), followed by New Zealand's first NDC to the UNIPCC in 2016 of 30% reduction by 2030 from 2005 baseline. This highlights that FirstGas purchased existing assets with full certainty that:

a) Climate Change was occurring;
b) the NZ Government had committed NZ to at first maintaining our GHG emissions to 1990 levels and then subsequently reducing them;
c) an emissions trading scheme had been implemented which put an additional cost of gas usage.

The prudent business owner would infer that all these Government regulations and commitments would result in the reduction in gas use in the long-term. To this end, FirstGas should not be compensated for purchasing an asset that potentially will face declining usage in the long-term future.

Section 2.12 and 2.13 of the Consultation Paper set out the obligations around the Commerce Act 1986 No 5 Part 4 section 52A with respect to the long-term benefit to consumers and not overriding that. Fonterra has the view that the accelerated depreciation does not meet the section 52A obligations in the following ways:

a) the accelerated depreciation is a wealth transfer from the consumers to the asset owners;
b) it will effectively encourage abandonment of gas pipeline assets as their capital is recovered, placing a risk on energy security and reliability for those users that remain using gas. Consumers (especially residential consumers) typically will not change assets in the face of increasing fuel costs due to the significant capital costs to change therefore it is in the consumers long term benefit to continue to support the operation of the gas transmission system and not force gas use change capital spend.

Stranded Assets

In section 3.4 of the Consultation Paper, the issue of asset stranding is raised and used as justification for the accelerated depreciation. The basis for this being the Concept Consulting report which does not independently analyse the potential for reducing gas use but instead just restates the Climate Change Commission modelling. Fonterra does not support using the Concept Consulting report to justify the evidence for asset stranding due to the following:

a) the timeframe for asset stranding occurring is further out timewise than the proposed DPP3 term;
b) the GDB's and GTB's own gas use view is significantly opposed to the Climate Change Commission modelling which shows that the asset owners themselves do not consider asset stranding as a risk;
c) that in the face of no Government regulation forcing gas use reduction, it would be expected that existing gas use would hold stable due to new residential consumers

potentially not choosing gas and existing commercial and industrial gas users status quo in the short term which matches the DPP3 term.

d) The work undertaken by many parties, including FirstGas, to identify renewable gas options that could be used in the pipeline and help with achieving New Zealand's decarbonisation objectives. For example, FirstGas published subsequent work regarding the vision to use hydrogen in the pipeline, and also published a study jointly with Fonterra, BECA, and EECA on the potential for biogas development and use in New Zealand. This suggests that there are renewable gas options that could result in ongoing continued use of this infrastructure.

e) That industrial users have entered into long term gas supply contracts that will span the proposed DPP3 also discredit the need for accelerated depreciation in this DPP3. This indicates that there will still be gas demand on the pipelines in the short term.

Treatment of new assets

Section 3.17.1 of the Consultation Paper discusses the handling of existing assets and new assets commissioned during the term of the proposed DPP3. Fonterra suggests that the Commerce Commission expands this section to minimise subjective reading of its meaning.

In Fonterra's view, existing assets must not receive accelerated depreciation as there is no evidential proof of asset stranding. New assets for safe reliable continued operation of the gas network also should not receive accelerated depreciation as these assets will typically have short life spans already and covered by DPP repairs and maintenance recovery cost allocations. New assets for expansion of gas network costs should be recovered from the users that has caused the need for expansion (i.e. following the examples set in the proposed transmission pricing methodology of a beneficiary pay model, or where Transpower can enter into connection investment contracts, or the existing EDB situation where new connections at commercial or industrial user level must pay for any network upgrade via individual connection contracts with agreed rates of capital cost recovery).

Alternative option to accelerated depreciation

In section 3.25.3 of the Consultation Paper, the Commerce Commission clearly states that they are making an assumption of expectation that gas use will fall in the medium to long term which means beyond the term of the DPP3 and again show no factual data supporting their position.

It is Fonterra's view that the GDB's and GTB have the ability under Part 4 to request a customised price path which then puts a more rigorous requirement for data and proof of asset stranding risk which can be independently verified. This would allow the accelerated depreciation if required in a new CPP to be match to the previous DPP or CPP period rate of gas use decline. This would also allow for individual situations to be analysed because effectively the GTB will be the last gas business standing as it must exist to transmit gas to the downstream GDB's and subsequent end users still remaining.

If there are any clarifications, or if there is any further information that would be of use to the Commerce Commission, please do not hesitate to contact us.