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Ms. Anna McKinlay
Chief Advisor
Regulation Branch
Commerce Commission
PO Box 2351
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Dear Anna,

Please regard this letter as our submission to the Commerce Commission ("the Commission") on the Technical Paper for Consultation on "Information Disclosure: Approaches for Understanding EDB and GPB Cost Efficiency". In this letter I will use MDL to refer to the Gas Transmission Business (GTB) of Maui Development Limited. I will start with general remarks and then provide responses to the specific questions in the Commission's paper.

General Remarks

MDL is one of two GTBs in New Zealand. However, all of its technical and system operations are contracted out to Vector Gas Limited, which operates the other GTB. From a technical and system perspective, therefore, Vector is the only GTB operator in NZ.

MDL's commercial regime is based on open access with non-discriminatory tariffs on nominated shipments of gas. MDL does not have capacity charges or any form of fixed income. This is different from a regime based on capacity reservation like Vector's. Furthermore, as we have previously noted MDL's pipeline is different to Vector's in that it runs for a relatively short distance, but is of much higher capacity. As a result, MDL's commercial operations and the drivers for its operating and capital expenditure are unique in NZ.

This means that we do not believe that MDL's business can be directly compared with any other business in NZ. We do not expect that comparison with distribution businesses would be particularly useful. Perhaps the only other business in NZ that could offer useful insights in how to assess a transmission infrastructure business would be Transpower.

Responses to Questions

[Q.1 How much insight would an assessment of operating expenditure based on NZ comparators alone provide, for EDBs and for GPBs?](#)

We will not provide comments in this submission for EDBs and GDBs. As was explained in our opening remarks, there are no useful comparators in NZ for GTBs.

[Q.2 How insightful could international comparators be in assessing EDB and GPB expenditure?](#)

At present, data to allow international comparisons for GTBs seems to be inadequate. We have reviewed the 2006 report on International benchmarking and regulation of European gas transmission utilities cited by the Commission. Despite the enthusiasm of its authors, we could not discern any practically useful benchmarks that could be applied to our business. We have looked for useful international benchmarks for our own purposes but have found little of use so far.

Q.3 What companies, countries or datasets should be included in the analysis?

We do not know of any company, country or dataset that would be particularly applicable to analyse gas transmission in New Zealand. In particular, there is little similarity between most parts of Australia's gas transmission infrastructure and that of NZ. The NZ infrastructure is relatively small in scale by international standards. In the absence of any obvious comparables the dataset of gas transmission businesses should be as large as possible.

Q.4 How appropriate are sub-company comparisons of costs?

MDL has only one pipeline and does not have any internal operations, other than those that have been contracted out. There is no sub-company model that could be applied.

Q.5 How feasible and costly would it be to collect sub-company cost and characteristic data to enable sub-company comparisons?

Not applicable to MDL.

Q.6 What factors (outside management control) drive industry wide opex?

In general we expect that significant drivers of opex for any GTB would be: length of pipeline, topography, proximity to sensitive areas, throughput, number of customers, number and capacity of compressor stations, infrastructure age and the cost of complying with regulatory oversight.

Q.7 To what extent does the current information disclosure data capture these factors?

Current information disclosure in NZ captures pipeline, throughput and customer information. It does not capture information on topography, proximity to sensitive areas, or compressor information.

Q.8 What cost drivers, if any, (outside management control) are unique to your EDB or GPB?

MDL has benefitted since 12 December 2008 from the availability of 860,405 GJ of low-cost gas, provided through a settlement facility, to be used for balancing and compressor fuel. This facility is almost exhausted and we expect OPEX to increase as gas is sourced at market prices.

Q.9 To what extent does the current information disclosure data capture these factors?

Current information disclosure does not distinguish whether balancing or fuel gas was purchased at market prices or from the settlement facility. Because the volume of settlement gas is expected to be fully used by 2012, however, this is probably not a concern for future disclosures.

Q.10 What factors (other than changes in input prices) influence opex over time?

MDL's costs are mostly fixed, except for balancing and compressor fuel gas. The characteristics of MDL's infrastructure are static and MDL does not currently have any plans to expand infrastructure. MDL deals directly with only about a dozen large customers. The addition or removal of a customer does not materially affect MDL's costs.

We believe balancing gas should be treated as a recoverable cost instead of as opex. It can be a net cost or a net income, depending on the balancing regime of MDL, balancing behaviour by Welded Parties, the availability of settlement gas, and market prices for gas.

The only significant variable cost of MDL is compressor fuel gas. MDL's compressor station at Mokau only needs to run for gas flows to the North (of the station) of more than 260 TJ per day, i.e. 11 TJ per hour. The Mokau station can support gas flows North up to 330 TJ per day, i.e. 14 TJ per hour, by running one compressor. The station has two compressors. The use of compressor fuel is non-linearly related to throughput, rising steeply as output approaches capacity. The cost of compressor fuel depends on availability of settlement gas and on market prices.

Finally, at the margin, increases in regulatory requirements and the associated levies have significantly increased opex over time.

Q.11 To what extent should quality be taken into account when assessing cost efficiency?

In a strict sense cost efficiency can be improved by taking measures such as reducing compressor use and reducing the use of balancing gas as far as possible, however these actions would have a significant detrimental effect on the reliability of the gas transmission service MDL provides.

Q.12 What level of opex should be assessed? Should the current sub-categories of EDB and GPB opex (e.g. general management, administration and overheads) be separately assessed, should further disaggregated cost data beyond these categories be collected and assessed, or should the analysis focus on total opex only?

It would not be very informative to analyse total opex only. The main cost categories for MDL would be as follows.

- Net Balancing Gas Income/Cost (this can be positive or negative)

- Compressor Fuel

- Technical Operator Costs

 - Gas Control Centre

 - Routine Maintenance

 - Exceptional Maintenance

 - Other TO Costs

- System Operator Costs

 - Open Access Transmission Information System (OATIS)

 - Scheduling

- Commercial Operator Costs

- Office Costs

- Corporate and other costs

Q.13 What components of opex should be separately benchmarked?

As discussed before, most cost components are effectively fixed and depend mostly on the scale of operations. With the possible exception of routine maintenance costs, we do not see any obvious benchmarking candidates. We note that non—routine maintenance expenditure may vary considerably from year to year as one-off tasks are identified and approved.

Q.14 How much insight would external comparisons of common functions provide?

None. MDL itself does not have common functions and does not employ any staff; all its operations are contracted out.

Q.15 What functions should be benchmarked and how easily available is cost data at a function-level?

Not applicable.

Q.16 What industries and operators should be included when benchmarking these functions?

Not applicable.

Q.17 Should nature-of-work comparisons be further considered in assessing EDB and GPB opex efficiency? If so, what sectors should be included in the analysis?

We do not believe this would be practical for Gas Transmission Businesses in NZ. Maintenance of gas transmission pipelines in New Zealand is all carried out by one company.

Q.18 To what extent should assessments of historical capex based on direct comparisons be considered as part of summary and analysis?

We do not believe historical capex provides a good guide for future requirements. With the exception of the relatively small component that would represent routine replacement capex, it has little predictive relevance for future capex.

Q.19 What are the material assets and activities that should be included in a capex assessment?

The main asset classes and categories for MDL are as follows.

- Pipeline

 - Main pipeline segments

 - Lateral pipeline segments

- Compressor Stations

 - Compressors

 - Other compressor station assets

- Other Stations

- Spares and parts

- Other assets

It should be noted that the distinction between main pipeline segments and laterals may not be relevant for the Commission. The Other Stations class includes main line valve stations, metering stations, pigging stations and offtake stations. A strict separation between these may not be meaningful, however, because metering can be installed at any station and pigging facilities could be installed at any station too.

Q.20 What are the drivers of activity on these assets?

Capex is mostly driven by need to maintain compliance with safety requirements and regulations. Major projects to replace segments of the pipeline have been driven by erosion and movement of land along the pipeline trajectory. Capacity constraints have historically not been a concern for MDL, but may need to be considered if Vector takes steps to increase its capacity on its Northern pipeline.

Q.21 How can capex effectiveness be measured?

Major capex projects are lumpy and infrequent. They are prepared, budgeted, approved and assessed on a case-by-case basis. As noted in our previous submissions, we believe an agreed investment test process carried out prior to the investment would provide the best guarantee in this area. We also note that effectiveness of capex cannot necessarily be measured in financial terms. Many projects are carried out for safety reasons, to meet revised compliance standards or to ensure better reliability of supply.

Q.22 How suitable is the proposed approach for assessing capex?

We do not believe the proposed approach is suitable for assessing capex of a Gas Transmission Business.

Q.23 To what extent do suppliers consider the opex-capex trade-off could distort an assessment of expenditure that is based on separate reviews of opex and capex?

In the context of the Maui Pipeline most significant capex is represented by pipe in the ground and by associated pipeline facilities for metering and control systems. Once an asset is installed, however, there is generally no more capability to trade investments against opex. Any possible trade-offs should be examined at the time a capex investment is being considered. We think an investment test has a role in ensuring this.

Q.24 Which components of expenditure have significant opex-capex trade-offs?

See above.

Q.25 How should the cost analysis take into account any opex-capex trade-offs?

We do not believe any generic model can be applicable. To the extent that capex-opex trade-offs can be made at a GTB they should be assessed and analysed on a case-by-case basis.

We should also mention that opex-capex reviews need to consider lease-buy and similar trade-offs. This has no impact on efficiency, because actual expenditure remains the same regardless of how it is classified. In analysing efficiencies, however, these effects would need to be taken into account.

Closing Remarks

In closing, we urge the Commission to maintain maximum consistency and compatibility between the Information Disclosure requirements that will be established after the current consultation and:

- a) the disclosure requirements for GPBs under the Gas (Information Disclosure) Regulations 1997;
- b) the definitions and approaches set out in Input Methodologies by the Commission, particularly those for Customised Price-quality Paths.

In both cases we strongly encourage the Commission to take steps to have those previous requirements and Input Methodologies updated for consistency with the new Information Disclosure Requirements.

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

Yours sincerely,

A handwritten signature in purple ink that reads "Don Gray". The signature is written in a cursive style with a large, stylized initial "D".

Don Gray
General Manager, Commercial Operator Maui Pipeline
for Maui Development Limited