



11 September 2003

Mr David Steele  
Gas Pipelines Inquiry  
Commerce Commission  
PO Box 2351  
WELLINGTON

Dear David,

**REQUEST FOR ADDITIONAL INFORMATION**

Wanganui Gas Limited (“WGL”) gave a presentation to the Commerce Commission (“the Commission”) on 2 September 2003 at its Conference on the Gas Control Inquiry Draft Framework Paper. At the Conference the Commission raised a number of questions in relation to WGL’s presentation and we respond to each of these questions below. For the purpose of this letter, we have used the paragraph numbering from the “Information To Be Provided” notice provided by the Commission.

**Question 22**

*“(a) By-pass pricing information including percentage of customers subject to by-pass pricing, the difference between by-pass prices and non by-pass prices and, (b) the by-pass guidelines/protocols that are used to identify consumers that may be subject to by-pass and set prices for those consumers.”*

*(a) By-pass pricing information including percentage of customers subject to by-pass pricing, the difference between by-pass prices and non by-pass prices*

GasNet, (the Network Division of WGL), has a by-pass policy, as supplied in response to question 22 (b) below.

GasNet's approach to by-pass is to consider the underlying value of the assets that are subject to by-pass threat. GasNet values the assets based on the least cost alternative option of supply to the consumer, then applies normal pricing methodologies to this asset base to arrive at an appropriate by-pass price. In total fewer than 1% of end-users have been identified as potential by-pass candidates and their distribution prices reflect the least-cost alternative supply option.

*(b) the by-pass guidelines/protocols that are used to identify consumers that may be subject to by-pass and set prices for those consumers*

The following is an extract from GasNet Policy dated 9 December 1999 that addresses the by-pass pricing guidelines. Please note that in 1999 GasNet was known as WGL – Distribution. There have been no changes to this policy since that date.

***“Treatment of WGL - Distribution Service Enquires: Rules and Related Rationale***

*General*

*In all cases, provision of any agreement with a retailer covered by this document will be dependent on that retailer providing a pass-through to the end-user of the equivalent value. These agreements are to promote the use of the distribution network(s) not retailer profit margins.*

*The options are set up so that either the retailer (and hence the end-user) takes a short-term gain (volume discount) or a long-term gain (long-term agreement) but not both.*

*It is assumed that the increased service required can be met without any capacity enhancement being required. If this is not the case then the normal capital contribution process is applicable and if paid, then the arrangements discussed below remain applicable. If no capital contribution is forthcoming either the work will not proceed or at WGL-D's discretion it would, without any discounting being applicable.*

*There are a number of cases that require a general rule to be provided so that all parties (and their enquires) are dealt with even-handedly and hence in a non-discriminatory way. The following cases are discussed below:*

- *By-pass*
- *Longer Term Deal*
- *High Annual Consumption*
- *Load Profile*
- *High Throughput*
- *New Service*

1. *By-pass*

*A candidate for by-pass is one that:*

- *is physically close to the gate*
- *has high consumption*
- *close proximity to other medium to high consumption gas users*
- *there is fuel switching capability which “caps” the acceptable gas service cost (inter-fuel competition)*
- *and/or it is considered highly possible that RMA consents would be gained*

*On a case-by-case basis, apply our by-pass model to determine the charge including operating cost recovery over the required period (say 5-10 years). The resulting by-pass price would be checked against the equivalent tariff given known/forecast consumption to ensure that the price offered is least cost.*

*The Division will not have its assets by-passed on defensible economic grounds provided to it by the retailer.”*

Question 23

*“The treatment of intangible assets (including easements) by WGL in statutory accounts.”*

WGL do not consider that easements are ‘intangible’ in nature but rather reflect an interest in land. Therefore, we have considered easements separately from intangible assets in our response to this question.

For the purpose of valuing the system fixed assets in the Annual Accounts, WGL values current easements at a conservative estimate of the transaction costs to obtain the rights conferred by the easement. This estimate is arrived at by considering the breakdown of

the costs associated with acquiring easements, including legal fees, survey fees and where known land purchase costs.

WGL does not currently report any intangible assets in its Annual Accounts.

Question 24

*“The Accounting Rate of Profit (ARP) and Return on Investment (ROI) figures for Wanganui Gas since 1997 and an explanation of the difference between them.”*

Indicated below are the ARP and ROI for WGL since 1997. The ARP figures have been calculated and disclosed annually in accordance with the Gas (Information Disclosure) Regulations 1997. The ROI figures have been calculated using the methodology promulgated in the Electricity (Information Disclosure) Regulations 1999 as a proxy for the ROI for a Gas Pipeline Business (“GPB”).

	1997	1998	1999	2000	2001	2002
ARP	9.3%	8.1%	7.0%	25.1%	8.9%	8.6%
ROI	9.3%	7.7%	6.6%	24.6%	8.6%	8.5%

The ARP and ROI for WGL are similar. The differences between the two numbers reflects different definitions of the inputs used in the calculations, such as working capital and taxation and the treatment of interest income, rather than the use of different methodologies.

It should be noted that the underlying financial information used to calculate the above percentages for the network business, are extracted from the integrated operations of WGL. While the electricity line businesses have prescribed methodologies such as ACAM, for extracting standalone network business results, such methodologies are not prescribed for GPBs, and GPB reported numbers may contain imperfections.

The high level of ARP and ROI for 2000 is due to the inclusion of the ODV revaluation of \$2.1 million. Excluding the effect of the revaluation from the numerator, the ARP and ROI for 2000 would have been 9.0% and 8.4% respectively.

Question 25

*“The target rate of return on fixed assets used by WGL and whether this target rate was reached.”*

WGL may or may not reach its WACC year on year due to factors outside the control of WGL, such as changes in demand and consumption. While there is a fixed element to WGL’s revenues, the variable component of revenues exposes WGL to risks. Unexpected increases in volumes may allow WGL to over-recover their capital and operating costs, whereas decreasing volumes expose WGL to revenue under-recoveries.

In regard to the specific WACC used by WGL (as distinct from disclosed financial figures) WGL is prepared to provide this information to the Commission if the same information is provided by all GPBs.

Question 26

*“A progress report on Gas Industry Steering Group.”*

We have requested, through the GISG Secretariat, that a meeting be arranged between the respective Chair’s of the Commission and the GISG.

Question 27

*The EECA report on barriers to growth for natural gas direct use.*

We have arranged for a copy of this report to be sent to the Commission under cover letter from the Gas Association of New Zealand.

If you have any queries in relation to issues raised in this submission, please contact Geoff Evans on (06) 349 0131.

Yours sincerely



Trevor Goodwin  
Chief Executive  
Wanganui Gas Limited