MAJOR ELECTRICITY USERS' GROUP

17 March 2006

Mr Ian Wilson
Gas Industry Company
By email to info@gasindustry.co.nz

Dear Ian

Submission on Gas Levy proposal

1. This is a submission by the Major Electricity Users' Group (MEUG) on the Gas Industry Company (GIC) *"Levy discussion paper*" released 24 February 2006.

2. The work programme for the year commencing 1 July 2006 (2006/07), expected outputs and hence budget is set out in section 7.4, pages 22 to 29 of the levy paper. There is insufficient information to assess whether the $3.8m budget proposed for 2006/07 is reasonable because:

    a) There is no comparison of proposed 2006/07 expenditure against forecast outturn for 2005/06. For example details should have been provided of the make-up of 2005/06 overheads and an explanation of changes compared to the 2006/07 budget proposal. With this information MEUG and others would have been able to test the expectation that while overheads in 2005/06 would be relatively high as the GIC office was established, after that start-up year overhead costs should have decreased.

    b) The level of financial budget information set out on page 29 is much less than required to assess the appropriateness of the aggregate budget.

        For example it is surprising fees paid to directors have not been disclosed. MEUG would be alarmed if the directors of GIC raised their fees knowing that decision would not be transparent before-the-fact and their decision on Director Fees would be recoverable through regulation.

        Another useful piece of information would have been the split between consulting costs and staff costs. This information would have allowed an assessment of whether the GIC was largely outsourcing or building capacity within the company and whether that strategy was the most efficient for each work programme activity.

    c) There should have been projections of expected costs for at least two further years (2007/08 and 2008/09). Having a longer term view of likely output and cost trends would be useful to understand how underlying costs might change over time and hence what levy options best fit that trend.

    d) The levy paper assumes costs are recovered as expensed. Some of these costs could have been capitalised and expensed as changes are realised. For example why should retail consumers today pay for registry development costs that consumers will only start to benefit from in 2007?

e) The discussion paper notes (p7) that total levy revenue collected will be more than that budgeted for 2005/06 of $3.6m but there is no comment on whether actual costs will equal or differ from budget and hence whether there will be a surplus or deficit to carry over. This information should have been presented in the discussion paper.

3. The paper discusses the pros and cons of variable ($/GJ consumed) versus fixed ($/ICP) for recovery of retail costs plus retail share of overheads and concludes[1], "*there is no clear cut case*" either way and "*neither the per ICP nor the per GJ approach is theoretically correct.*" For 2005/06 a 50:50 split of variable to fixed costs was applied. For 2006/07 the 50:50 split (option 1 and 2) is considered as well as fully variable scenarios (option 3 and 4). Even though the levy paper acknowledged there was no compelling evidence for variable over fixed levy, only fully variable options have been considered. Based on the analysis of the levy paper itself MEUG believe a fully fixed option for recovery of retail related costs should also have been considered.

Yours sincerely

Ralph Matthes
Executive Director

[1] GIC, Levy discussion paper, February 2006, conclusions 1 and 2, p15