



7 April 2005

The Secretariat  
Gas Industry Company Limited  
PO Box 10 646  
Wellington

Attention: Richard Longman

Dear Richard:

Thank you for the opportunity to comment on the Gas Industry Company (GIC) Levy Proposal Discussion paper, dated 24 March 2005.

### **General Comments**

Contact Energy supports the GIC's efforts to develop a levy framework that is equitable and practical. We support the GIC's proposed general allocation of costs, but we believe that there are ways to make the proposed levy mechanism both more equitable and more practical. From an equity point of view, we submit that the retail levy should be charged on a per installation basis (ICP), as all retail customers will benefit equally from the GIC's consumer protection measures. Such a framework will also be more practical to implement. On the wholesale side, from a practical point of view, Contact believes that the point at which the levy is applied should be as clear as possible, and we submit that the first point of sale should be reconsidered in this regard. Our detailed comments are below.

### **Proposed allocation of costs**

In terms of the benefits of GIC arrangements, we concur, as the paper states, that there will be benefits both for both wholesale and retail gas customers. Therefore, it makes sense that both portions of the market bear the costs of the GIC.

### **Wholesale Levy**

#### *Calculation of Charge*

On the wholesale side, Contact supports a \$/GJ levy. The wholesale arrangements to be developed by the GIC should lead to reduced transaction costs in the wholesale market, and market participants will benefit from these lower costs in proportion to their market share. It is therefore appropriate that the costs be levied in proportion to market share, through a fixed cost per GJ levy.

#### *Allocation of Charge*

In terms of where to charge the wholesale levy, Contact submits that the point of collection must be clear and unambiguous. The discussion paper suggests that the levy be collected at the offtake points from the transmission grids, but there is no specific transaction that is associated with the offtake. Gas can potentially be traded many times before it is actually

consumed, as wholesale gas buyers often onsell or swap gas in order to adjust their books. In such an environment, there is no clear way to determine which is the final sale of the gas before it leaves the pipeline.

In contrast, the injection of gas into the pipeline is always associated with a sales transaction. The first point of sale therefore provides a logical and unambiguous point where the levy could be applied. In addition, charging at the first point of sale would capture gas that is sold to wholesale customers but that does not enter either NGC's transmission system or the Maui onshore pipeline. In Contact's view, such gas will nevertheless benefit from the wholesale trading arrangements that will be developed by the GIC.

The discussion paper suggests that charging at the first point of sale would disadvantage producers with bulk contracts. Contact submits that this is an insufficient reason not to impose the levy at this point, as many downstream market participants also sell gas through large contracts and therefore could be equally disadvantaged by a levy on their sales. In any event, many contracts have provisions that allow taxes and levies to be passed through to the buyer, so that the sellers may not be as disadvantaged by the levy as the paper suggests. We recommend that the GIC reconsider the merits of imposing the wholesale levy at the first point of sale.

## **Retail**

### *Calculation of Charge*

In terms of GIC's benefits to the retail gas market, the situation is different than with the wholesale arrangements. The benefits on the retail side are to include retail switching mechanisms and allocation and reconciliation processes. These benefits, unlike the wholesale benefits, do not accrue on the basis of the amount of gas used; rather, they benefit all consumers equally.

Costs must also be considered. The costs of running the retail market are a function of the number of customers, not the amount of gas sold. Thus, it is important that the GIC's retail costs are recovered in a way that reflects this cost causation, otherwise you will get a situation of large customers cross-subsidising small customers.

Therefore, Contact submits that it would be more equitable to charge the retail levy on a per customer basis, rather than per gigajoule, as proposed. We note that such an arrangement would be consistent with the charging policy of the Electricity Commission, which recovers its costs through a per connection levy.

### *Allocation of Charge*

The discussion paper suggests that the retail levy should be paid by "small users", but this distinction does not recognise where the costs and benefits of the retail arrangements would lie. The benefits of the retail arrangements will accrue to both mass market and most large customers. Furthermore, the costs associated with switching and allocation processes do not vary significantly between mass market and large consumers. Therefore, there seems to be no rationale for distinguishing "small users" from other gas consumers in setting the retail levy. The only exceptions would be those consumers who have no need for the allocation and reconciliation processes or for the switching arrangements: very large consumers who take gas off the main transmission system, have separate metering systems, and have negotiated bilateral contracts with gas providers.

In addition, the proposed definition of "small user", those that consume less than 10 TJ per year, is an arbitrary threshold that we believe is impractical for a number of reasons. First, it would require a regular assessment of gas consumers to determine which fall below the threshold and are therefore subject to the levy. There are also issues of consistency, as

consumers who fall just within the definition one year may be above the threshold, and exempt from the retail levy, the next.

Contact submits that the retail levy should be charged on a per connection (ICP) basis. As noted above, such an arrangement would be the most equitable way of allocating retail costs; it would also be relatively simple to implement. The number of ICPs per retailer could be produced each month from NGC Transmission (for direct supply consumers) and from Distributors (for all ICPs connected to distribution networks) and provided to the GIC. If the industry decided to move to a single registry, then the Distributor information would be available from that registry.

#### **Responses to specific points raised in the discussion document:**

##### ***Proposed cost allocation:***

Contact supports a wholesale levy charged on a \$/GJ basis, but we submit that the best point of application for such a levy may be at the point of first sale.

For retail, we advocate a levy on a per ICP basis.

##### ***Proposed coverage:***

Contact supports the proposal that the levy should cover both specification and non-specification gas.

##### ***Initial attribution of costs:***

Contact supports levying the GIC's costs half on the wholesale sector and half on the retail sector.

##### ***Retail levy:***

As noted above, Contact submits that the retail levy should be configured as a \$/ICP charge. This framework represents the most equitable and most practical option for levying the retail charge. ICP data can be obtained from NGC Transmission and from Distributors.

If you have questions or would like further information about the points raised in this letter, please do not hesitate to contact me.

Yours sincerely,



Pamela Caird  
Regulatory Analyst