31 March 2005

The Secretariat
Gas Industry Company Ltd
PO Box 10 646
WELLINGTON

Attention: Richard Longman,

RE: GIC LEVY PROPOSAL

This letter is in response to an invitation of 24 March 2005 to comment on the proposal for a Gas Industry Company levy.

The submission is made by:

Ballance Agri-Nutrients (Kapuni) Ltd (Ballance)
309 Palmer Rd
Hawera
Telephone: 06-272-6920
Facsimile: 06-272-6930
Attention: Len Houwers

Ballance owns and operates New Zealand's only Ammonia Urea manufacturing facility in South Taranaki. We are the largest single site user of natural gas in New Zealand after Methanex and the major gas fired power stations, consuming an annual energy base load of approximately 7 PJ.

Our comments are focussed on:

1. The wholesale market.
2. The proposed allocation mechanism in the wholesale sector.
3. The size of the proposed levy.

As a preface to further comment we would note that we acknowledge and support that some form of regulation is necessary for the industry. We also perceive the co-regulation approach as being a more cost effective solution to regulation than another Electricity Commission type Government Regulatory Authority.

Our context is as a 7 PJ pa gas consumer with the proposed levy of 1.5 c/ GJ introducing a new financial burden of approximately $105,000 pa on our organisation. This is at a time where our vulnerability to import substitution of our product has already increased significantly on the back of an adverse structural shift in wholesale gas pricing. The nature of our competition also means that any increase in domestic cost structure is unable to be passed on in any form to our customers and will have to be fully absorbed by our shareholders.

PROPOSED ALLOCATION MECHANISM IN THE WHOLESALE SECTOR.

Our perception of the variable cost proposal is probably best summed up by our following observations:

1. A new bureaucracy set up to deal with an industry that can't act within its own broad interests without a threat of a more heavy-handed regulatory approach.
2. The people imposing the costs are not going to pay for the cost of resolving this dysfunction.
3. The same parties will benefit from the proposed work of the Council and will not themselves be paying for that either.

This highlights our chief complaint, which is that the mechanism is faulty in its belief that pain and gain will be equally shared within the market. We believe that regardless of the intent to spread costs between those responsible for incurring them and those benefiting from any improvements in the market, that the practical outcome of the allocation mechanism is an almost exclusive burden on downstream parties.

We base this belief on our perception and experience that it would be typical to have within supply agreements, a clause specifying that any new imposts, levies etc imposed on the seller will be passed straight through to the buyer. Thus gas producers, gas wholesalers, and pipeline owners, are protected from paying this levy.

We would suggest that a more equitable arrangement is where the levy has to be seen to be absorbed equally between contracted upstream and downstream parties. This split can be evidenced within existing invoicing arrangements.

THE SIZE OF THE PROPOSED LEVY AND ONGOING COST

For the same reasons of where financial burden is placed, we also have concerns around whether the proposed budget for the Council will meet the criteria for effectiveness, efficiency, and economy. The figure of $3.6 million is promoted without justification. We can't see where the controls exist within the Council to promote efficiently priced quality outcomes if someone else's money is being spent.

Furthermore, despite the initial work scope on the Council, we are not aware that there exists a sunset clause on this body. Once set up, bureaucracies have a tendency to grow in scope and cost to run and will continue to justify their own existence.

We suggest that a clear, relatively short, timeframe is set to complete the needed work to overcome the current market mechanism failures. The threat of more heavy handed regulation of the industry in event of failure to achieve set objectives within the required timeframe should be sufficient incentive to keep the focus on what is relevant and important. After expiry date, the body is automatically dissolved, or a fresh mandate is sought from industry to keep it going.

I trust that you will find these comments useful in your consideration for a final proposal.

Len Houwers
General Manager