GREYMOUTH GAS

15 February 2013

John McLaren
Chief Adviser
Regulation Branch
Commerce Commission

By email: regulation.branch@comcom.govt.nz

Dear John,

RE: Gas Transmission Services Default Price-Quality Path Determination 2013

Following an invitation from the Commerce Commission ("ComCom") on 8 February 2013, Greymouth Gas New Zealand Limited ("Greymouth Gas") is pleased to make a submission on:

- The Gas Transmission Services Default Price-Quality Path Determination 2013 Technical Consultation Draft dated 8 February 2013 (the "**paper**"), and
- How we (the ComCom) propose to implement the Default Price-Quality Paths for Gas Pipeline Services dated 8 February 2013 (the "**implementation paper**")

Greymouth Gas is a significant player in the New Zealand gas industry, and we currently supply about 10% of New Zealand's natural gas market. Greymouth Gas is also a shareholder of the Gas Industry Company Limited ("**GIC**").

Greymouth Gas supports the work of the ComCom and we limit our submission to clause 12 of the paper (re balancing gas).

Brief history of balancing gas and its operation

The issue of balancing gas has been contentious in recent years, more particularly prior to 2009 when different legacy and contractual arrangements saw much larger volumes of balancing gas required. Since then, the quantum of balancing gas required by the gas industry has significantly reduced.

In our opinion, the current balancing gas environment works like this at a high-level:

- Maui Development Limited ("MDL") buys or sells balancing gas depending on line pack in the pipeline, and these costs are allocated to Welded Parties (as defined in the Maui Pipeline Operating Code ("MPOC")) via two day process commonly referred to as Cash-Out (as per s12.11 of the MPOC), and via Imbalance Limit Overrun Notice, Peaking Tolerance and Excess Daily Imbalance tools (all as defined in the MPOC).

Greymouth Gas New Zealand Limited
Level 26, 151 Queen Street / PO Box 1394, Shortland Street
Auckland, New Zealand
Tel: (+649) 373 4222 Fax: (+649) 373 4228

- While the relationship between the cause of balancing gas and the tools/cost recovery under the MPOC is not perfect on a day-by-day basis, it should be noted that, to the extent that there is a discrepancy between balancing gas costs to MDL and cost recovery from its Welded Parties, MDL is cost-neutral over time due to the wash-up of over/under prior year recovery via the Tariff 2 mechanism (as defined in the MPOC).

- Vector Gas Limited acting as a transmission system operator ("Vector"[1]), as Welded Party, then take any cost allocations from MDL and wholly allocate this to itself, its Shippers and its Non-Code Shippers (as defined in the Vector Transmission Code ("VTC")). At a basic level, Vector should be cost-neutral on a day-by-day basis. Vector also has the option of buying/selling its own balancing gas in accordance with the VTC, but Vector has not done so for at least the previous three years, instead relying on MDL to pragmatically act as the default balancing agent for the gas industry.

Notwithstanding the current set-up, balancing gas remains a contentious issue. In April 2012, the GIC gave a final recommendation on an MDL change request (dated 13 October 2011) to the Maui Pipeline Operating Code ("MPOC"), which may be implemented on 1 June 2013[2].

If implemented, the balancing gas environment (but probably not the volumes) will, in our opinion, change as follows:

- MDL will still buy or sell balancing gas depending on line pack in the pipeline, but these costs and quanta will be Cashed-Out on the day and a form of Peaking Tolerance will remain.

- This is an allocative solution, unlikely to result in a productive benefit. However, the reallocation should reduce any day-by-day discrepancies between MDL's costs and cost recovery, although it will not change the fact that MDL will still remain cost-neutral over time.

- Vector and the VTC will likely be amended to reflect the new MPOC tools, but Vector should remain cost-neutral on a day-by-day basis.

Greymouth Gas considers it relevant to advise the ComCom of the current and potential future balancing gas environment.

Definition of balancing gas

Balancing Gas is defined in the MPOC as 'Gas used to manage line pack on a Transmission Pipeline'. The definition of Balancing Gas in the VTC can be set aside for the time being as Vector relies on MDL to buy/sell balancing gas under the MPOC as a means of balancing New Zealand's transmission pipelines.

Greymouth Gas is surprised that balancing gas is prima facie not defined in the paper, the implementation paper or in the Gas Transmission Services Input Methodologies Determination 2012 as it has implications on how to interpret the paper.

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[1] With exclusive reference to Vector in its role as a transmission system owner and operator

[2] Greymouth Gas reserves its position regarding this change request

Comments on part 12 of the paper

Greymouth Gas comments as follows:

12.2.1

Prima facie, but subject to our comments on clause 12.3, this clause 12.2.1:

- Makes sense pertaining to MDL under the current balancing gas environment, but only if amended for the fact that MDL does not allocate any balancing gas to Shippers (as defined in the MPOC), only to Welded Parties,

- Would only make sense pertaining to MDL under the potential future balancing gas environment if ComCom was satisfied that MDL would contractually be able to have unallocated balancing gas or unrecoverable costs on a day-by-day basis,

- Does not make sense pertaining to Vector under the current or potential future balancing gas environments.

If Vector continues to solely rely on MDL to balance the pipeline (and even if Vector bought Balancing Gas (as defined in the VTC) of its own accord under the VTC), then Vector has no option but to be cost neutral under the VTC. Thus any prima facie costs/credits arising would likely be cash flow issues, management issues or items subject to a dispute. As a pass-through agent, Vector could therefore be carved out of being allowed recoverable costs in this regard.

12.2.2(b)

Prima facie, but subject to our comments on clause 12.3 and notwithstanding our comments on clause 12.2.1, this clause 12.2.2(b):

- Fails to note that Non-Code Shippers (as defined in the VTC) can also be allocated balancing gas, in the case of the VTC,

- Fails to note that Vector can also be allocated balancing gas by itself in accordance with the VTC, under the definition of Vector Running Imbalance pursuant to the Shipper Allocation formula (both as defined in the VTC).

Incidentally, MDL is also a Welded Party with respect of the Mokau Compressor Station, although this is already captured by the current wording of the clause.

12.3

It could be argued that this whole section (i.e. permitting MDL (and Vector) to claim certain balancing gas costs as recoverable costs) is not relevant given that MDL is cost-neutral over time via the wash-up mechanism of Tariff 2.

Greymouth Gas is concerned that MDL (and Vector) do not double-claim balancing costs as recoverable costs from the gas industry. ComCom may want to make sure that incorporating Tariff 2 as part of the default price quality path *and* allowing balancing gas as a recoverable cost is not in fact double counting the cost given the cost-neutrality of balancing gas to MDL (and Vector) over time[3].

Further concerns due to lack of prima facie definition

The lack of a prima facie definition of balancing gas in the paper and the implementation paper poses a concern pertaining to the previous section, and pertaining to the following:

- As part of its Vector Imbalance and Vector Running Imbalance obligations (as defined in the VTC), Vector necessarily purchases Fuel gas and purchases/sells UFG gas as part of its further responsibility for UFG, Fuel and Gas Vented (as defined in the VTC).

    - To the extent that these variables become out of balance and contribute to an MDL cost, Vector allocates itself part of the cost. Greymouth Gas considers that this self-allocation should be excluded from the definition of balancing gas pertaining to Vector, as it is an incentive on Vector to reasonably and prudently manage their own-use exposure.

    - Likewise, Greymouth Gas considers that Vector's purchase of Fuel gas and their sale/purchase of UFG gas (which helps them manage their Vector Imbalance and Vector Running Imbalance) should also be excluded from the definition of balancing gas pertaining to Vector, as these are costs of running the pipeline which should already be factored into the prices Vector charges for gas transmission.

- The MPOC does not have the same imbalance or running imbalance concepts pertaining to MDL as the VTC does pertaining to Vector. In the current environment, the current definition of Balancing Gas in the MPOC does prima facie appear to be adequate as it pertains to gas used to manage the line pack in the pipeline. However, this could be said to be a smokescreen for the lack of a mechanism for MDL to account for its own imbalance as a transmission system operator. This leads to the question of what is the split of current Balancing Gas sales/purchases due to UFG (if the MPOC was to incorporate a similar concept to the VTC) and what was genuinely balancing gas sales/purchases necessary for supporting the line pack in the pipeline caused by Welded Party imbalance? The difference is subtle, but Greymouth Gas considers that a distinction should be made between genuine gas needed to be transacted by MDL because its Welded Parties haven't balanced properly ("balancing gas"), and gas MDL purchases for its own purposes to prop-up its running imbalance position (if it was to have one). The latter could be argued to be a cost of running the pipeline, thus a recovery of operating costs, thus its recovery is already included in the MPOC via Tariff 2. The lack of VTC-like concepts in the MPOC makes it very difficult to gain transparency on this issue[4].

- In addition to the above, in and subject to the potential future balancing gas environment, while there is a carve-out of Fuel Gas purchases in the definition of

[3] Regardless of whether the allocation methodologies change under the MPOC and VTC from the current to the potential future environment

[4] In general for any business there should come a point in time, and a point in contracts, whereby core costs of doing business need to be built-into the base price for service and not split out as add-on costs, e.g. what is and is not acceptable to consumers when purchasing an aeroplane ticket

Balancing Gas Call (as defined in the marked-up MPOC pursuant to the GIC's decision previously mentioned ("marked-up MPOC")), a Balancing Agent will have authority to purchase Fuel Gas and buy/sell gas for other activities (pursuant to s3A of the marked-up MPOC). Greymouth Gas considers that the latter two items should be excluded from the definition of balancing gas in the paper as they are costs of running the pipeline, not actions following imbalance caused by Welded Parties.

Please feel free to contact me, and/or discuss with Vector, MDL and/or the GIC, should you have any queries on this submission.

Yours sincerely,

Chris Boxall
Commercial Manager