31 March 2015

Mr Ian Wilson
Gas Industry Company
Level 8, The Todd Building
95 Customhouse Quay
PO Box 10 646
Wellington 6143

Emailed: Ian.Wilson@gasindustry.co.nz

Dear Ian

Market Based Balancing Change Request draft recommendation – submission

Thank you for the opportunity to provide a submission on the Gas Industry Company's (GIC's) draft recommendation on daily cash-outs lodged by MDL (***Recommendation***).

On the balance of the material put forward, Contact recommends the change request is declined on the basis that there is evidence to show that under the Market Based Balancing Change Request (MBB CR) costs to shippers will exceed the corresponding benefits. Further a collaborative process should be put in place to address the issues in a way that works for all parties. This is something we would welcome the opportunity to discuss with you.

General comments

There has been a large number of comments on the MBB CR process around whether to compare the MBB CR to the status quo or to the previously approved but not implemented change requests. There were also comments on the fact that the use of market based balancing is already allowed for under the status quo and therefore irrelevant under the MBB CR.

While we appreciate the GIC's comment that it is not its concern that the other change requests have not been implemented and that parties to the Code had opportunity to raise a dispute under the MPOC[1], we note that Contact (and indeed others) did not support the B2B CR. This was largely because shippers could see increased costs with no ability to mitigate by way of an open market for balancing gas, something MDL had ruled out unless certain prescribed conditions were adhered to. For many, the stance by MDL was seen as adding uncertainty to an open market implementation with the result being a subsequent change request developed by a number of parties in an attempt to

[1] Recommendation p20

solve this uncertainty. Unfortunately, however, the issue of the MBB CR has meant that this subsequent change request has not been able to be put forward.

In respect to the use of a gas market, the GIC claims that MDL saw potential issues with implementing trading of balancing gas under the current MPOC[2]. Contact believes MDL did not satisfactorily substantiate the issues or look for compromised solutions through its consultation with its shippers.

Improved balancing gas procurement

From Contact's perspective, the Recommendation places much weight on the MBB CR improving the procurement of balancing gas. We note the Gas Industry Company's comment that it would "*allow MDL to procure the Balancing Gas from a Balancing Platform that all Parties would have access to*". That outcome would therefore "*significantly reduce barriers to competition in the supply of Balancing Gas and create downward pressure on prices*"[3].

The Recommendation also states[4] that, while the market benefits could be achieved by another means, such as regulation, this would be uncertain and likely delay improvements by several years. In Contact's view, a relatively simple regulatory change to the procurement of balancing gas, if needed, should not be overlooked, especially when the current MPOC (s. 11.10) already allows for this.

Cost benefit analysis

Contact is pleased to see a cost benefit analysis (CBA) has been undertaken; however, we have some concerns with the assumptions that have been made. For example, it does not necessarily follow that *"if shippers invest in extra administrative effort to better manage their positions under MBB CR, it is reasonable to assume they expect profit from that investment"*.[5] While Contact sees a value in decreased uncertainty, it does not see a profit in this particular investment. Covec makes no allowance for such costs. While the outcome may or may not result in behaviour change, it appears likely that some will halt primary balancing in favour of market cash-outs, which defeats the objective of the MBB CR.

It is worth noting that shippers see increased risk in their balancing exposure with the lack of tools to manage their positions, particularly daily allocations. In fact the cost and timing of introducing daily allocations is likely to be high in terms of both money and time. In our view, this concern is valid and should be addressed prior to any daily cash-out mechanism being implemented.

---

[2] Recommendation p20
[3] Recommendation p66
[4] Recommendation p66
[5] Covec's cost benefit analysis p2

Recommendation

Contact recommends the GIC declines the change request as there is sufficient evidence that under the MBB CR costs to shippers will increase. Further, if the GIC believes there are efficiencies to be gained with daily balancing then it should work with industry to implement the tools with which shippers can meaningfully balance.

We also recommend that any change implemented must be approved with at least 6 months' notice so that shippers can make any required technical changes to their systems.

Please contact me should you wish to discuss any of the matters raised in this submission.

Yours sincerely

Sharon Wray
Manager, Fuels Trading

Contact Energy Limited

PO Box 10742
Wellington 6143

Level 2 Harbour City Tower
29 Brandon St, Wellington 6011

P: +64 4 499 4001
F: +64 4 499 4003

www.contactenergy.co.nz