GREYMOUTH GAS

23 October 2018

Ian Wilson
Senior Technical Adviser
Gas Industry Company Limited
By email

Dear Ian,

Re: GIC Consultation

1 Introduction

1.1 Greymouth Gas New Zealand Limited ('GGNZ') raises the following matters for GIC consideration:

2 Aside from matters covered in your feedback to First Gas ('FG') on the GTAC draft, are there any elements of the proposed arrangements that you think require particular attention in GIC's assessment?

GIC needs to get in the game, and play it appropriately

2.1 The *Electricity Price Review – First Report For Discussion* dated 30 August 2018, overseen by MBIE, says "there may be merit in considering a single regulator for energy if New Zealand's changing energy mix warrants it".[1]

2.2 GGNZ considers that this proposition will find full support if GIC supports the GTAC, and the GTAC and FG do not facilitate growth in natural gas and support natural gas' transitional role in New Zealand.

The GTAC is currently being misdescribed as a single Code

2.3 Section 1.1 of the GTAC defines 'Code' as being the [GTAC] including all its schedules. Section 4.1 of Schedule 1 (which will become a TSA) defines 'Code' as being the [GTAC] including all schedules *apart from* Schedules 5 and 6.

2.4 This means that there will effectively be two GTACs, one including all schedules, and one excluding schedules 5 and 6. GGNZ considers this a gross inefficiency. FG has failed to create a single gas transmission and access code. If the GTAC is approved, there will be two codes.

[1] Refer to page 77 of the report.

Greymouth Gas New Zealand Limited
Level 9, 151 Queen Street / PO Box 1394, Auckland 1140
New Zealand
Tel: (+649) 320 0422 Fax: (+649) 373 4228

There are a plethora of pricing issues

Huntly and Delivery Zones

2.5 Draft DNC prices for Huntly Town are estimated at $1.87/GJ and draft DNC prices for Huntly Power Station are estimated at $0.46/GJ. This is inequitable, these prices should be the same.

2.6 FG has discretion to choose which Delivery Points go into which Delivery Zones (having regard to a set of factors),[2] and FG has an obligation not to prefer any Shipper or Interconnected Party except as *expressly* provided for in the GTAC. The factors do not provide for FG to give preferential pricing to a particular Delivery Point by keeping it outside an otherwise geographically proximate Delivery Zone.

2.7 There are other issues with Delivery Zones:

- Section 3.3 of the GTAC requires FG to consider factors "in determining Delivery Zones". This suggests that FG must be consistent with its application of factors across all Delivery Points otherwise the wording would have been "in determining each Delivery Zone …".
- Delivery Points with OBAs are excluded from Delivery Zones. This makes no sense – e.g. why should the balancing regime chosen influence whether or not a point is in a Delivery Zone for the purposes of capacity pricing?
- Not all Delivery Points are required to be in a Delivery Zone, which reduces pricing certainty ahead of a particular year. Delivery Points excluded from estimated DNC pricing include Kaimiro and Stratford 3.
- FG is required to publish Delivery Zones by 30 June each year. However, it may not know which Delivery Points have OBAs at that time.
- Transporting to the far end of a Delivery Zone will cost the same as transporting to the end closest to the Receipt Zone. This has less allocative efficiency than the MPOC pricing model.

2.8 These issues are relevant to GIC's assessment (the GTPM will be published later) because the issues relate to fairness, certainty, structure, and disputes.

Other agreements are problematic

2.9 If Huntly Power Station is to receive special pricing, then the GTAC may permit the Supplementary Agreement process to be utilised for special pricing.

2.10 The GTAC should not allow FG to prefer some Shippers (via non-standard pricing in a Supplementary Agreement) because section 7.1 only allows changes to the definition of 'transmission fees' (undefined). Even if this meant 'Transmission Charges', then

[2] I.e. per section 3.3 of the GTAC the factors are capacity, geography and other Delivery Point similarities, demand, and the merits of constituent Delivery Points having the same transmission fees.

amending the definition of that would not release FG from its obligation not to give preferential pricing to one Shipper (via a Supplementary Agreement) in a Delivery Zone over other Shippers (without SAs) in the same zone even if the definition is changed. This means that where there is a Supplementary Agreement in respect of a Delivery Point, then standard prices in the Delivery Zone that contains that Delivery Point will need to be lowered to match the pricing in that Supplementary Agreement (defeating the need for such an agreement). GIC must have continued oversight of these issues.

2.11 In a similar vein, the GTAC does not enable FG to prefer some Shippers (via non-standard pricing in an Existing Supplementary Agreement) over other Shippers (without one). In addition to the conclusion in 2.10 above, the issue is whether Shippers with Existing Supplementary Agreements will not be required to have TSAs in respect of those agreements (meaning there will be two classes of shipper), or whether TSAs relating to VTC will be required (thus the VTC cannot expire and the GTAC cannot commence). This needs unbundling.

2.12 The FG-Genesis Letter of Understanding dated 10 January 2018[3] is a supporting arrangement that the GIC is to consider when assessing the GTAC. The LoU requires FG to consider applying specific HQ/DQ at Huntly Power Station. The issue is that the HQ/DQ concept has been removed from the GTAC and replaced with an alternative peaking regime, yet section 7.4 of the GTAC allows FG to consider alternative definitions of MHQ and transmission fees payable. FG appears bound to consider the old HQ/DQ regime for Huntly. GGNZ considers that this is unacceptable and it needs to be fixed.

Interconnection pricing is uncertain

2.13 Section 1.2 of Schedule 5 of the GTAC defines Interconnection Fee as "[●]" [sic]. While ICA templates further define "Interconnection Fee" (and that definition prevails in the ICA), it is not appropriate to have a term defined in the GTAC with a symbol.

2.14 GGNZ has been significantly disadvantaged by "interconnection pricing" at Kaimiro. While FG is required to publish an interconnection policy – there is nothing to establish how FG is to set fees relating to interconnection. Where those fees contain a capex component, interconnected parties must have certainty that the capex cost is actual "best practice" cost without hidden margins, and that payments over time are fair or regulated. That has not been the experience at Kaimiro where an interconnection capital cost was circa NZD700,000 pre 2000; and where FG has recovered interconnection revenue of circa $3million to date and where FG continues to claim ongoing interconnections fees, against threats of disconnection. This is wrong and this charging abuse must not be allowed under the GTAC or any new Code.

2.15 A party must be able to resolve pricing disputes prior to entering into an ICA. To be materially better than the MPOC and VTC, the GTAC should provide for a party to submit to the GIC or a GIC appointed independent expert to resolve all matters of interconnection pricing whenever arising and to resolve disputes in relation to current or proposed ICAs.

[3] Publically available at https://gasindustry.co.nz/assets/Consultations/Uploads/Genesis-Energy-GTAC-Letter-of-Understanding-signed.pdf

It is unclear whether pricing is subsidy-free

2.16 In explaining the methodology behind its most recent prices, FG has considered 'revenue generated from each shipper [that] should be consistent with previous years [sic] revenue to avoid shocks to individual businesses from the change', and 'pricing at the zone and delivery point level should continue along the same trajectory established under the VTC and MPOC to ensure there are consistent incentives for gas usage in a particular region and any tariff shock is minimised'. The problem is that this is not possible because Delivery Zones are unique to the GTAC. There should be nothing in GTAC allowing FG to avoid tariff shocks or avoid incurring normal business risks.

2.17 GGNZ has attempted to reconcile the pricing charged per Delivery Zone with the pro-rata gas flows and pipeline asset values included in those zones. However, the latter data is not available. We recommend GIC obtain individual pipeline asset values from FG, in order for it to assess FG's draft pricing using first principles for allocative efficiency (i.e. whether or not it is subsidy free).

2.18 Pricing from a Receipt Zone, rather than from each Receipt Point, will also create allocative inefficiency because Receipt Points at the extremity of the Receipt Zone which are delivering to Delivery Zones in the other direction will receive subsidised transmission compared to Receipt Points located much closer to that Delivery Zone.

2.19 To be materially better than the current arrangements, the GTAC should <u>require</u> FG to comply with the ComCom's pricing principles and disclose calculations in support of this (with GIC/Independent expert oversight).

GIC needs to reassess its approach to GTPM

2.20 In the FAP, GIC said the MPOC "tariff principles" are a description of cost allocation, rather than a pricing methodology. GGNZ considers this is wrong. At the start of the original GTAC process, the GIC said "The MPOC [tariff] principles lay out how tariffs will be set to recover capital and operating costs, and therefore <u>are better described as a Pricing Methodology</u>"[4] (emphasis added).

2.21 GIC went on to conclude that placing the GTPM outside the GTAC did not raise major concerns relative to the status quo. GGNZ considers this wrong – having pricing sit outside the code, rather than inside the MPOC on a pay-as-you-go basis has less certainty and less allocative efficiency.

Transmission netbacks are subject to upwards pressure

2.22 Natural gas supply is tight, and likely to get tighter given the government's proposed ban on new offshore exploration permits. During the 2020s, industry may be looking at a 'scarce' world rather than a 'plentiful' world, referencing GIC's own work.[5]

2.23 The ComCom model will not work in a low demand world (if FG is entitled to recover a bucket of money, spread over the GJs of demand). To illustrate this, if industry demand approaches 1 GJ/pa and FG attempts to recover all its revenue, the cost to

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[4] Refer to page 5 of the GIC's 'Transmission Prices – Roles and Responsibilities' paper dated August 2016.
[5] Refer to page 106 of Concept's Long Term Gas Supply and Demand Scenarios – 2016 update.

transmit gas would be >$100m/GJ. The picture is that as allowable revenue stays relatively constant, the more demand reduces, the higher transmission fees will be (and vice versa). There will be a tipping point where increased transmission netbacks will beget further demand reductions if FG is able to pursue full revenue recovery (which FG should not be entitled to do – that is the business risk it has taken).

2.24 A materially better code (compared to the existing arrangements) would put a price cap on increases in tariffs (and tariffs should go down where the pipeline owner has recovered its capital and the regulated rate of return). From a GTAC assessment perspective, the absence of a price cap should weigh negatively.

Hydrogen is here, now, and the GTAC could displace natural gas

2.25 FG is considering network use for hydrogen.[6] Hydrogen is more than a pipe dream.[7]

2.26 The GIC and the Gas Act encapsulate all types of gasses, yet the Commerce Act covers natural gas. This 'gap' must be fixed. This potential GIC conflict must be appropriately managed.

2.27 A hydrogen / natural gas transition must be predictable and not discriminate against natural gas which has been paying for the pipelines for many decades.

2.28 The GTAC provisions need to be changed so that:

- The*Transmission System* is defined as the pipeline system for natural gas transmission.
- The definition of *RPO* gives prior regard for current pipeline users.

Confidentiality and Ahuroa need further work

2.29 GGNZ agrees with emsTradepoint that the GTAC should ring-fence information between FG (and related company) commercial and operational teams.

2.30 The GIC should set out how the Ahuroa arrangements will work. E.g. who is the Interconnected Party, is there an Existing ICA (and if so when does it expire), which FG company owns Ahuroa, does that company own any or some of the gas, if so is it possible that that company will need to purchase gas to prop up pad gas from time to time? On the latter point, it is a detriment to the GTAC that not all non-FG parties are required to have TSAs. If FG ends up transporting gas to its related company, for non-pipeline management purposes, without a TSA, that would be a perverse outcome.

2.31 The GTAC must not enable FG to deal with itself, or with a related company that does not have a TSA, on a non-arms' length basis.

3 Are there any aspects of the previous FAP analysis you think could be improved?

[6] Refer to pages 17 and 36 of the Gas Transmission Asset Management Plan Summary Document 2018.
[7] http://www.hylink.co.nz/ and https://www.hiringa.co.nz/

3.1 The previous FAP analysis missed some items (for example downstream allocations), so these must be assessed now.

3.2 GGNZ considers that the three level colour-coded concept works. The analysis can be improved by retaining this logic to allow for comparison with the old FAP. The new PAP (and FAP) should be readable as a standalone document but the commentary should allow easy comparison with the FAP.

3.3 The process that underpins GIC's GTAC assessment should be improved, e.g.:

- Appropriate consultation periods should exclude Christmas to mid-January;
- Arrangements should be tested for simplicity and workability, which map to Gas Act objectives;[8]
- End-users not represented by MGUG should be surveyed on key matters such as the impact of daily nominations and accuracy targets / incentives;
- An external lawyer should be commissioned; and
- Mr Bush or Mr Bolton (ex-employees of Vector or FG) should be commissioned to advise on workability of the numerical concepts and calculations.

3.4 All matters that GGNZ and other parties raise that require particular attention by GIC should be given particular attention by GIC.

4 Conclusion

4.1 In funnelling its work programme and selectively deciding not to discuss items such as hydrogen or price caps that were raised during workshops, FG (and through FG, the GTAC) do not give sufficient regard to material changes that have set the industry, natural gas prices, and the economy, on a different forward trajectory.

4.2 GGNZ requests GIC give full consideration to the matters raised in this submission.

Yours sincerely

Chris Boxall
Commercial Manager

Cc: – Matthew Lewer and Keston Ruxton, Commerce Commission
– Ben Gerritsen and Angela Ogier, First Gas Limited

[8] Refer to page 13 of FG's November 2016 paper 'Gas Transmission Access: Single Code Options Paper.