Vector Limited
101 Carlton Gore Road
PO Box 99882, Newmarket
Auckland 1149, New Zealand
www.vector.co.nz
Corporate Telephone
+64-9-978 7788
Corporate Facsimile
+64-9-978 7799

16 March 2012

Ian Wilson
Gas Industry Company
PO Box 10-646
Wellington

Dear Ian

Submission on the Draft Recommendation on the 13 October 2011 MPOC Change Request

1. Vector Limited ("Vector") welcomes the opportunity to make this submission on the Gas Industry Company's ("GIC") *Draft Recommendation on 13 October 2011 MPOC Change Request* ("Draft Recommendation"), dated February 2012. No part of this submission is confidential and Vector is happy for it to be made publicly available.

2. Vector does not support the Change Request, as presently drafted, or the GIC's Draft Recommendation to accept it. Vector reaffirms its view that the Change Request would have a material adverse effect on its transmission pipeline business, and the compatibility of Maui Development Limited ("MDL") and Vector's open access regimes.

Changes that should be considered

3. Vector shares submitters' views, as reflected in their earlier submissions[1] and cross submissions[2] on the Change Request, that there are specific proposals in the Change Request that would enable some efficiency improvements eg back-to-back allocation of balancing costs.

4. That is why Vector was and continues to be willing to work with MDL to progress submitters' favoured changes subject to the following conditions being agreed:

   a) The inclusion in the current Change Request (or another Change Request that is effective from the same date as the Change Request), clauses which:

      - explicitly give Vector the right to pay balancing costs to MDL only to the extent to which Vector is paid by the causers of the balancing cost

[1] October 2011
[2] January 2012

(to expressly reflect current practices and the position under the MPOC); and

- acknowledge that all balancing costs are caused by the users of the pipeline downstream of the TP Welded Points, and not the TP Welded Party.

b) The removal of the peaking mechanism.

c) The implementation of the Change Request must be contingent on:

- the implementation of a VTC change request effective from the same date as the Change Request to ensure that the MDL and Vector open access regimes remain compatible at all times; and
- the successful implementation of changes to Non-Code Agreements effective from the same date as the Change Request to ensure that the MDL and Vector open access regimes remain compatible at all times.

5. Adopting the above conditions would lead to balancing arrangements that are more integrated across the Maui and Vector transmission systems, and more consistent with the 'causer pays' principle.

Notice of material adverse effect

6. In November 2011, Vector formally raised with MDL, under the parties' Interconnection Agreement ("ICA"),[3] the material adverse effect the Change Request would cause on Vector's transmission business. The specific adverse effects are identified and described in Vector's previous submission on the Change Request.[4]

7. Vector considers that the implementation of the Change Request would not be sustainable and is therefore an unacceptable long-term solution. It is noted that the Draft Recommendation itself states that:

> ... the change would not provide a complete answer to balancing issues and will have flow-on effects, including to the Vector transmission system, which should be addressed" [Executive summary].

8. The effect of the Change Request would be a diminution of Vector's rights and an increase in its costs and obligations under the Maui Pipeline Operating Code ("MPOC").

9. While the proposed back-to-back mechanism may be more efficient than the status quo, the Change Request seeks to introduce a peaking mechanism which will lead to higher costs than the status quo and will not see the costs of peaking allocated to causers.

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[3] https://www.oatis.co.nz/Ngc.Oatis.UI.Web.Internet/Common/Publications.aspx, under Special Terms and Conditions – TSA/ICA, 2005-09-21 NGC NZ Ltd ICA

[4] http://gasindustry.co.nz/sites/default/files/submissions/254/vector_submission_-_mpoc_cr_balancing.pdf, pages 4-5

10. One argument used to diminish the importance of achieving an efficient balancing issue is that the volumes of balancing gas have been going down over time. Vector considers that the fact the balancing agent is buying historically low volumes of balancing gas is no guarantee this will continue to be the case.

11. Although balancing volumes have been going down, this does not mean the current balancing regime efficient. The underlying problem still exists and the value of balancing gas could go up at anytime.

12. Current arrangements do not allocate balancing costs to causers, which is inefficient, and does not incentivise <u>all</u> parties to act efficiently. The Change Request does not provide the fundamental rethink that Vector considers is required to address the issue.

Way forward

13. Vector wishes to see balancing arrangements that are fairer and more efficient, and therefore enduring.

14. Vector shares the GIC and industry participants' desire to avoid prolonged and costly processes of developing new balancing arrangements, and resolve this long-standing issue in a timely manner. We are prepared to support the Change Request subject to MDL's agreement with our conditions and co-ordination with Vector in their implementation. We will continue to engage with MDL to resolve the material adverse effect we raised under our ICA.

15. Any resolution to the balancing issue would only be sustainable if it fixes the foundation of the regime on a principled basis. The GIC should not close the door on other balancing options.

16. Should it become untenable for the relevant parties to further pursue non-regulatory paths, Vector remains open to a targeted regulation that ensures the causers of imbalances pay for balancing costs.

17. Without prejudice to Vector's views above, and that it does not support the Draft Recommendation, there are particular sections in the document that Vector would like to comment on, and correct or clarify. These are identified in Appendix A.

18. If you have any questions, or require further information, please contact me on 04 803 9038 or Bruce.Girdwood@vector.co.nz.

Kind regards

RBGirdwood

Bruce Girdwood
Manager Regulatory Affairs

Appendix A: Specific Comments on the Draft Recommendation

Draft Recommendation	Vector's comment
Page 17 graph	The graph is inaccurate. Monthly balancing costs, and the amount recovered via the Incentives Pool are incorrect when compared to the monthly balancing costs published on the BGX and the Incentives Pool Debit calculation published on Maui OATIS. For example, for January 2011, the graph shows that approximately $220k was spent on balancing costs and about $80k was recovered via the Incentives Pool. However, the BGX and OATIS show this information to be $141k and $34k, respectively. Vector has further concerns about the basis of the graph. MDL invoices Welded Parties for balancing costs for both Incentives Pool Debits and cash outs. The premise of the graph is that anything not recovered via the Incentives Pool Debits is socialised through the tariff. This is inaccurate. The graph needs to show the total amount recovered via cash outs plus Incentive Pool Debits compared to total balancing costs. The percentage socialised via the tariff also needs to be recalculated, which we believe could be much lower than 57% and negative in some months, ie when total recovery is greater than balancing costs. For example, in February 2012, balancing costs amounted to $82k and the amount recovered was approximately $170k. The recommendation states that "the current arrangements involve substantial sharing of balancing costs through the transport tariff". This conclusion needs to be updated when the analysis has been corrected.
Page 20, first sentence, "The proposed arrangements extend the Schedule 7 Peaking	This is incorrect because the Peaking Limits do not apply to Small Stations. Vector suggests that this sentence be amended to:

Draft Recommendation	Vector's comment
Limits coverage from Large Stations to apply to all stations."	The proposed arrangements update the Schedule 7 Peaking Limits for new Large Stations since the MPOC was adopted.
Page 25, Section 5.1, Productive Efficiency	The first paragraph is based on the conclusion and percentages from the graph on page 17, which Vector has concerns about. It should be updated after the numbers in the graph are corrected. The third paragraph should be prefaced with the statement "[I]f there is a successful VTC Change Request, and changes to the Non-Code Shipper Agreements then" ... Regarding the fifth paragraph, Vector agrees that the Change Request does not change MDL's ability to change its SOPs. As noted in our previous submission[5], this ability becomes more significant and risky under back-to-back arrangements.
Page 26, Section 5.1 Allocative Efficiency, second sentence of the second paragraph	The sentence should be amended from "They would no longer have the opportunity..." to "They would have **less** opportunity to cause a balancing action and then balance their own position at a later **time**..." as parties will have the ability to balance their position during a day after a balancing action has been taken.
Page 26, Section 5.1 User Risks, second paragraph	The paper talks about Welded Parties being able to "participate in the balancing market to hedge their risk". Currently, only some Welded Parties are allowed to do this (excluding Vector Transmission) so this is not an option available to all Welded Parties. The GIC has asked MDL to assist parties to be able to do this but has not insisted that this happen. Similar comments occur elsewhere in the paper, eg at the end of the implementation cost section on page 28.

[5] http://gasindustry.co.nz/sites/default/files/submissions/254/vector_submission_-_mpoc_cr_balancing.pdf paragraph 12 d)

Draft Recommendation	Vector's comment
Page 31, Table 2, second sentence from the top, "In relation to peaking..."	This sentence fails to acknowledge the generally accepted concept that there is insufficient data to allocate peaking costs to responsible parties. A VTC Change Request would not fix this problem. This would require the availability of hourly data for all gas users, including households. This is unlikely to pass a cost-benefit test.