



4 June 2010

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Dear Ian

## **MPOC 17 December 2009 Change Request Draft Recommendation**

### **Introduction**

1. Contact appreciates the opportunity to comment on the GIC's paper "*MPOC 17 December 2009 Change Request Draft Recommendation*" issued May 2010 (Draft Determination).
2. Contact and other industry participants have already commented on MDL's 17 December 2009 MPOC Change Request (MDL Change Request).
3. Although, as indicated previously, Contact supports some aspects of the MDL Change Request it also strongly opposes many sections of the MDL Change Request.
4. Contact does not find the aspects of the MDL Change Request that it supports sufficiently attractive to allow it to overlook the aspects of the MDL Change Request that it does not support.
5. To avoid the need to accept the unattractive aspects of MDL's Change Request in order to gain the attractive aspects Contact, and other shippers and welded parties, encouraged MDL to resubmit the MDL Change Request as a number of subsidiary change requests with narrower scope. Contact continues to encourage MDL to follow that approach.
6. Some aspects of the MDL Change Request require further development and consideration.
7. Contact confirms that it does not support the MDL Change Request.
8. In this submission Contact:
  - comments on the GIC's method of assessing the MDL Change Request;
  - considers the relationship of the MDL Change Request to the proposed "*Gas Governance (Balancing) Rules*" (Rules);

- evaluates the MDL Change Request;
- proposes a design framework for balancing arrangements to enable consistent development of the detail of balancing arrangements; and
- proposes an alternative change request that develops balancing arrangements within the proposed design framework.

### **Assessment of the MDL Change Request**

9. Contact agrees that the GIC can only indicate whether it supports or does not support the MDL Change Request.
10. Contact also agrees that the GIC is required to assess the MDL Change Request against the objectives specified in Section 43ZN of the Gas Act and against any additional objectives or outcomes set out in relevant Government Policy Statements.
11. Contact remains of the view that the secondary set of criteria, developed by the GIC to evaluate balancing proposals and set out in section 3 of the Draft Determination, is not helpful. As indicated in previous submissions, that approach overlooks and alters significant aspects of the objectives specified in section 43ZN of the Gas Act. In addition, the GIC's secondary set of criteria is too distant from the principles of balancing to assist the GIC, and industry participants, evaluate balancing proposals.
12. The development of a secondary set of criteria to assess balancing proposals would be helpful if it established a design framework and clear and consistent objectives for balancing. Contact proposes this approach in this submission.
13. The MPOC was implemented following extensive commercial negotiations. MPOC change requests can lead to a number of outcomes. Outcomes from change requests may:
  - provide overall MPOC improvements that benefit all parties contracted under the MPOC; or
  - improve the position of one party contracted under the MPOC at the expense of another party contracted under the MPOC.
14. The latter outcome creates unmanageable risks for all parties contracted under the MPOC and potentially barriers to competition. To avoid this, the GIC must assess change requests to the same standard that it determines proposals for regulatory intervention and must reject change requests that benefit parties contracted under the MPOC at the expense of other contracted parties. The GIC seems to acknowledge this requirement in section 2 of its Draft Determination.
15. Each unlinked aspect of a MPOC change request should be separately assessed. If that approach is not followed there is a danger that aspects of a change request that alter the risk profile of the MPOC, or are detrimental, will slip through under cover of higher profile issues addressed in a change request.
16. The MDL Change Request creates a high risk of introducing changes to the MPOC that are harmful because of:
  - the complexity of the MDL Change Request;
  - the wide ranging scope of the issues addressed in the MDL Change Request; and

- the lack of linkage between some of the issues included within the scope of the MDL Change Request.
17. MDL seems to have included matters in the MDL Change Request that are designed to make overall improvements to the MPOC as well as matters that appear designed to shift risk away from MDL. Inevitably that transfers risk to welded parties. Some of these matters are related to balancing, others are not related to balancing.
  18. The GIC has attempted to address the mix of matters tackled in the MDL Change Request by assigning a qualitatively determined score to the balancing related matters then adding those scores. That approach is unsatisfactory as it is impossible to assign meaningful scores to aspects of a change request that are unrelated. It's unclear what the numerical ratings represent. Do they represent the GIC's assessment of the financial implications of each aspect of the MDL Change Request or the GIC's assessment of some other single or mix of consequences? That requires full explanation. The GIC says that its approach requires it to weight the various aspects of balancing but has avoided applying any weightings in its Draft Determination.
  19. In addition, the GIC has not rated issues included in the MDL Change Request that are unrelated to balancing. It is difficult to envisage how the GIC will combine ratings for balancing and non-balancing issues into an overall assessment of the MDL Change Request.
  20. At best the assessment the GIC has attempted in the Draft Determination is unfinished. It is also inadequate.
  21. Instead of following the approach developed in the Draft Determination, the GIC must separately and independently assess each individual aspect of the MDL Change Request. If any single aspect does not meet the objectives of the Gas Act or Government Policy Statement then the GIC should reject the MDL Change Request in entirety.

### **Relationship of the Change Request to the GIC's Proposed Balancing Rules**

22. The GIC has made a proposal to the Minister that transmission pipeline balancing should be governed by Rules. At this stage it is unclear whether the GIC's proposal will be accepted by the Minister.
23. Nevertheless, it seems appropriate to assume that the Rules represent the GIC's view of ideal balancing arrangements to the extent balancing mechanisms are covered by the Rules. It is therefore surprising that the GIC has not assessed the MDL Change Request against the Rules.
24. The MDL Change Request seems deficient in meeting the following provisions of the Rules:
  - the requirement for unified management of balancing across the transmission system;
  - the appointment of a single balancing operator;
  - the obligation of transmission system owners to facilitate balancing;
  - the obligation of the transmission system owners to provide transmission services for balancing gas;
  - the establishment of balancing thresholds;

- the setting of the clearing price for balancing services at the marginal cost of providing those services;
- the provision of open access to the balancing market;
- the allocation of balancing gas costs to the transmission system owner;
- the provision for corrections to balancing allocations; and
- the establishment of procedures for implementing and modifying balancing arrangements.

25. This inconsistency means that if the GIC supports the Change Request, and its recommendation to impose the Rules is accepted, further substantial changes to MPOC balancing arrangements will be required to make the MPOC meet the requirements of the Rules. That creates risk and uncertainty for parties contracted under the MPOC.

### **Comments on the GIC's Assessment**

26. The GIC has assessed the MDL Change Request under the following headings:

- back-to back allocation;
- peaking;
- removal of TP welded party balancing gas;
- tariff 3;
- balancing operator role and responsibility;
- operation of balancing gas market;
- operator instructions; and
- "pay now, dispute later".

### **Back-to-back Allocation**

27. All balancing costs should be allocated on a consistent basis to ensure that welded parties, MDL and the balancing operator manage balancing in a coordinated manner.

28. Balancing action and costs include:

- gas bought and sold by the balancing operator to manage line-pack;
- gas takes curtailed to manage line-pack; and
- flows of gas scheduled and caused by welded parties and MDL (self balancing).

29. Under the MPOC the requirement that shippers submit balanced nominations means shippers are not responsible for imbalance.

30. In a perfect world balancing costs, incurred by parties other than a party self balancing would be allocated across running imbalances at the time the balancing action was

committed. That would require continuous determination of imbalances. That continuous determination is probably impractical.

31. For the purposes of allocating balancing costs under the current MPOC, both daily and running imbalance positions are determined at day end. In addition, rolling average three hourly imbalance positions are determined for the purposes of peaking.
32. Implementation of the MDL Change Request would mean the Balancing Operator could recover balancing costs against:
  - running imbalance;
  - daily imbalance; and
  - rolling average three hourly imbalance.
33. Welded parties could recover their balancing costs (loss of potential margin on curtailed gas deliveries) against:
  - daily imbalance; and
  - rolling three hourly imbalance.

Inconsistently with the rights of the balancing operator, welded parties could not recover their balancing costs against running imbalance: the cause of imbalance.

34. There is no provision under the current MPOC arrangements or the MDL Change Request for a welded party to make a claim against another welded party for losses resulting from that other welded party's over injection of gas at a receipt point or undertake of gas at a delivery point.
35. This mix of allocation methods creates incomplete, confusing hotchpotch and conflicting mechanisms for recovering balancing costs. For example, often (and whenever a welded party is correcting imbalance) its daily imbalance will be opposite in direction to its running imbalance. Under the MPOC and the MDL Change Request a welded party could face concurrent and conflicting claims against positive running operational imbalance, offsetting negative daily operational imbalance and rolling three hourly average imbalance.
36. It is, therefore, incorrect and misleading to characterise balancing under the MDL Change Request as back-to-back balancing.
37. It is understood that back-to-back balancing means allocation of balancing costs to the causers of imbalance. The causers of imbalance are welded parties who generate running imbalance. In addition, MDL can cause imbalance if it fails to correct running UFG.
38. Back-to-back balancing requires allocation of all balancing costs on the same consistent basis, either on the basis of running imbalances calculated on a daily basis, or on the basis of running imbalances determined at shorter time intervals if that is necessary to fully capture the cause of imbalance.
39. MDL proposes to determine hourly running imbalances under the MDL Change Request. If allocation of balancing costs against running imbalance determined on a daily basis is too crude, and as a result MDL is not able to allocate the majority of balancing costs, through that mechanism, to causers of imbalance, then use of the hourly running

imbalance information for allocation of balancing costs should be considered. A cost/benefit analysis for allocation of balancing costs on hourly running imbalance positions should be undertaken before a decision is made to adopt that more refined approach.

40. A consistent approach to allocating balancing costs could be simply implemented by:
- allocation of cash-outs on the basis of running imbalance;
  - allocation of costs incurred by welded parties as a result of curtailments via the incentives pool with debits determined from running imbalance; and
  - removal of the provisions that result in welded parties incurring incentive pool debits as a result of peaking.

### **Removal of ILON Process**

41. Contact supports the removal of the ILON provisions. The ILON provisions were designed to give welded parties access to balancing flexibility in an environment where MDL had access to gas supply flexibility allowing it to provide balancing services beyond the flexibility afforded by pipeline line-pack.
42. With the end of the Maui Gas White Paper Gas Sale and Purchase Agreement it comes as no surprise that MDL has found providing access to gas supply flexibility causes MDL to incur costs and that MDL is no longer willing to provide such a service for free.
43. That means the assumptions behind the design of MPOC arrangements such as the ILON process are no longer valid and arrangements built on those assumptions should be changed.
44. The ILON process also allows MDL to cash-out positive and negative imbalances that occur at the same time rather than limiting cash-outs to net imbalance. The cash-out of offsetting imbalance is inefficient and unnecessary.
45. In designing the current MPOC arrangements it was envisaged that cash-out of offsetting imbalances would not occur because welded parties would trade offsetting running imbalance.
46. In the event, imbalance trades at shared TP welded points have proved largely ineffective in managing imbalance because of the impact of those trades on VTC shippers taking gas at TP welded points. Allocation of imbalance at TP welded points in accordance with imbalance at downstream welded points (remote welded points) would make trade of imbalance more sensible and should overcome this impediment that discourages imbalance trade.
47. Contact supports the removal of the ILON process as proposed by MDL because cash-out of offsetting running imbalances should no longer occur.

### **Consequences of Operational Imbalances**

48. Section 12.1 of the current MPOC makes it clear that the consequences of a welded parties failure to inject or not off-take a quantity of gas equal to the relevant scheduled quantity are limited to those set out in section 12 of the MPOC. In the MDL Change Request, MDL proposes to delete this provision.
49. Removal of section 12.1 exposes welded parties to wider balancing risk including a possible claim for breach of the MPOC as a result of not injecting or not off-taking a

quantity of gas equal to a scheduled quantity. This could mean that welded parties would not be limited to paying liquidated damages via the incentives pool if the resulting imbalance caused MDL to curtail the schedule quantity of another shipper. This destroys part of the rationale for the incentives pool.

50. Contact does not support the removal of section 12.1 from the MPOC.

### **Management of Gas Flow**

51. Under section 12.9 of the current MPOC welded parties have an obligation to manage gas flows so that running imbalance at each welded point tends to zero over a reasonable period of time.
52. MDL proposes to amend this obligation to manage gas flows so that welded parties are required to use reasonable endeavours so that running operational imbalance tends towards zero at all times. Welded parties do not have the information necessary to manage such an obligation.
53. Moreover, the concept of tending to zero at every instant of time doesn't make sense. A tendency means a move or a change in a direction and must involve measurement of imbalance at least at two points in time. A tendency can only occur over a period of time.
54. Placing this ambiguous obligation on welded parties creates unmanageable risk. Contact does not support this change.

### **Removal of Tolerance**

55. Under the MDL Change Request MDL proposes to allocate the balancing operator's costs for buying or selling balancing gas in accordance with welded parties' running operational imbalance. There will be no allowance for the tolerance provided under the current arrangements through allocation of cash-outs against accumulated excess operational imbalance.
56. Access to pipeline balancing flexibility is linked to the provision of tolerance and the trigger of line pack limits set to determine the circumstances when the balancing operator undertakes balancing action. These mechanisms for accessing pipeline balancing flexibility must be coordinated to avoid socialisation of balancing costs. Socialisation of balancing costs will occur if pipeline balancing flexibility is released to welded parties by setting wide line pack limits for initiating balancing action and releasing that same flexibility through setting large tolerances.
57. Contact supports the eventual removal of tolerances but coordinated with the introduction of transparent line pack limits describing circumstances in which MDL will undertake balancing action. Those limits should be set so that the balancing flexibility afforded by line pack is fully exploited.
58. However, MDL goes too far in proposing to remove all cash-out tolerance flexibility in a single step at this time, particularly when that removal is not well linked to description of the circumstances in which MDL will undertake balancing action. Contact therefore does not support the full removal of tolerances, at this time, as proposed by MDL.
59. Inconsistently with its approach to cash-outs, MDL proposes that incentive pool debits will only be incurred to the extent of excess daily imbalance (includes allowance for tolerance).

### **Provision for Corrections**

60. Making provision for corrections to balancing positions as a result of metering errors and allocation errors is a vexed problem when balancing costs are allocated on the basis of running imbalance. A correction of historic running imbalance changes the running imbalance position from the date of the correction and makes welded parties' management of running imbalance positions invalid from the date the correction was applied. That creates unacceptable risk for welded parties.
61. The current MPOC allows these corrections, but that creates unnecessary risk and frustrates management of imbalance.
62. There are two possible approaches to address this issue:
  - to close-off imbalance positions at the end of a set period, say at the end of each day, so that the allocation of imbalance positions is calculated independently for each day; or
  - to roll corrections into the future rather than correcting past positions.
63. The first approach may create additional balancing costs through unnecessary balancing activity and may delink balancing action revenues from balancing action costs. Imbalances may be unnecessarily cashed-out when they could have been self-balanced within line pack flexibility. The creation of additional balancing costs is not inevitable as MDL could return any additional revenues through tariff adjustments.
64. In the MDL Change Request MDL proposes a new section 12.5 that would prevent any corrections. The proposed new section does not indicate whether future running operational imbalances would or would not include provision for historic corrections.
65. MDL's proposal creates uncertainty and is inadequate.
66. The MPOC should make explicit provision for the take-up of historic corrections to running imbalance in future running imbalance positions but only once welded parties have been forewarned of the correction and the consequences of the corrections. To avoid imbalance shocks there should be an upper limit to the size of any correction that can be applied to the imbalance position for a single day. Again, subject to the upper limit, any correction in excess of that limit should be taken-up in running imbalance for the following days until the total correction has been absorbed.

### **Removal of Shipper Mismatch**

67. The purpose of the shipper mismatch provisions of the current MPOC were to increase gas transmission flexibility available to shippers by allowing shippers to draw on pipeline line pack at no cost in circumstances when it was necessary to curtail a shipper's approved nominations at a receipt point or a delivery point.
68. MDL now says that it is unable to provide this service at no cost. That is not surprising.
69. Under the MDL Change Request MDL proposes to retain the shipper mismatch provisions but render the provision valueless. MDL proposes that shipper mismatch will be addressed as running operational imbalance. The cash-out provisions of the MPOC already offer that option.
70. In the extreme, retention of these provisions could trap shippers into incorrectly thinking that MDL was providing a service at no cost.



71. In the interests of simplification of the MPOC, eliminating ambiguity and eradicating redundant provisions the mismatch provisions should be removed from the MPOC rather than retained as proposed in the MDL Change Request.
72. It is noted that MDL's proposed changes to the shipper mismatch provisions, rendering those provisions redundant, means that shipper mismatch would no longer provide MDL with a tool to help manage changes in line pack. For example and because of section 8.30 of the MPOC, MDL could not manage excess draw down of pipeline line pack by curtailing gas take at delivery points without curtailing gas injection at receipt points. This may mean MDL's proposals related to shipper mismatch require further consideration.

### **Fuel Gas and Balancing Gas**

73. In the MDL Change Request MDL proposes to include a new definition for UFG. However, the proposed definition leaves the calculation of UFG entirely to MDL's discretion. That seems inappropriate.
74. Gas injection to line pack or a gas withdrawal from line pack is required to address UFG. If MDL, through its balancing operator, fails to arrange the appropriate action to offset the change in line pack caused by UFG then that failure may require balancing action and incur balancing costs. The allocation mechanism for those costs should be clearly set out in the MPOC.
75. UFG should be defined in the MPOC in the manner set out in the VTC and should be calculated on a daily basis. If MDL fails to address UFG then it should be liable for the costs of any resulting balancing action.
76. Under the current MPOC and the MDL Change Request MDL has no liability for balancing costs resulting from its failure to address UFG. That is inconsistent with the causer pays principle.
77. Also under the current MPOC and the MDL Change Request MDL will not be allocated the cost of balancing actions that it causes through removal of gas from line pack for use as compressor fuel or its other requirements. That is inappropriate, being inconsistent with the causer pays principle, and creates unmanageable risks for welded parties.
78. MDL's avoidance of responsibility for balancing costs related to the management of UFG and use of fuel gas arises from its proposal to use the payback point as the receipt and delivery point for management of UFG and withdrawal of gas from line pack for use as fuel gas. The payback point is defined as a notional welded point. Under the definition of operational imbalance, and because the actual flow of gas cannot be measured at a notional welded point, there can be no operational imbalance at the payback point. Hence MDL could not be allocated any balancing costs at that point.
79. Instead of MDL's proposal to use the payback point, a separate notional welded point should be defined for management of UFG. MDL should be allocated balancing costs at that point resulting from its failure to manage UFG. For the purposes of calculating operational imbalance at that point for a day the deemed gas flow could be defined as the UFG at the end of the previous day.
80. In addition, fuel gas should be scheduled and measured at the physical welded point where fuel gas is withdrawn from the Maui pipeline. For the purposes of providing information, allocating balancing costs and other welded point provisions under the MPOC that welded point should be treated in the same way as other physical welded points are treated under the MPOC.

81. Contact does not support the treatment of UFG and fuel gas proposed by MDL under the MDL Change Request.

### **Circumstances Balancing Action Undertaken**

82. Under the MDL Change Request, MDL proposes to add a new section 3 to the MPOC that sets out:

- the functions of the balancing operator;
- how it will instruct the balancing operator to carry out those functions;
- the information MDL will require the balancing operator to publish relating to balancing actions; and
- the standard terms under which the balancing operator will buy and sell balancing gas.

83. In addition, MDL also proposes to add a new section 2.18 requiring MDL to consult with its shippers and welded parties on the content of standard operating procedures.

84. Contact supports the direction of MDL's proposal, however, MDL's proposal has a number of shortcomings and because of that it is inadequate and may have limited effect.

85. The limitations include:

- the lack of recognition of standard operating procedures under the MDL Change Request and the MPOC;
- the lack of any specification of the consultation process;
- the lack of description of the matters that must be covered by a standard operating procedure;
- the lack of description of the circumstances when the balancing operator would undertake balancing action; and
- the lack of description of the circumstances when the balancing operator would not undertake balancing action but would instead curtail gas flows at welded points.

86. Contact does not support MDL's proposal because of these shortcomings.

### **Incentive Pool Mechanism**

87. Under the MDL Change Request, MDL proposes to change section 14.1 (section 14.2 in the amended MPOC) so that if incentive pool claims on a day exceed incentive pool debits for that same day, on a GJ basis, then incentive pool claims will be pro rated so that they equal incentive pool debits.

88. This change, coupled with changes to section 14.5 (section 14.7 in the amended MPOC), mean that welded parties unable to take gas to their full scheduled quantity may not receive full compensation for that lost gas. That is unacceptable, although it is also acknowledged that it is appropriate to limit welded parties' liability in respect of incentive pool debits.

89. The means of compensating welded parties for failure to deliver gas requires further evaluation. An option that requires consideration is whether welded parties should have a residual claim against MDL as the provider of transmission services.
90. It has been suggested that it is unnecessary to include a provision in the MPOC that allows welded parties to claim compensation for their inability to flow gas to the relevant scheduled quantity as that is addressed by the Critical Contingency Regulations.
91. Contact disagrees with that proposition on two counts:
  - the MPOC arrangements and the curtailment provisions are designed to control gas flows so that exercise of the Critical Contingency Regulations is avoided; and
  - it is fundamental to an agreement to provide a service (in the example of the MPOC a transmission service) that the party receiving the service should be able to claim damages if the provider of the service fails to provide the agreed service.

### **Peaking**

92. Under the current MPOC arrangements, the peaking provisions allow the balancing operator and welded parties incurring incentive pool credits to make a claim for balancing costs against welded parties with a rolling three hour average imbalance.
93. As indicated above, such imbalances do not create a need for balancing action. It is also unclear why rolling three hourly imbalance is used rather than hourly imbalance.
94. The GIC's conclusion that such imbalances can contribute to the need to take balancing action is only correct in circumstances when those imbalances are in the same direction as the welded parties' running operational imbalance.
95. Together with the calculation of incentive pool debits on a daily basis, the peaking provisions provide a secondary method for the balancing operator to recover the costs of balancing action. But that mechanism lacks any logical foundation and creates conflicting imbalance management drivers for welded parties.
96. The peaking provisions, relating to the recovery of balancing costs, should be removed from the MPOC. If following that removal, the level of balancing costs that the balancing operator is unable to recover via cash-out of running operational imbalances is significant then the costs and benefits of allocating balancing costs on the basis of running operational imbalances at the close off of each intra day nomination cycle or at hourly intervals should be evaluated.
97. We agree with the GIC that there is no logic in only being able to claim against the peaking provisions or the incentive pool for a decline in line pack. A build up in line pack can also cause curtailment of injections and loss of income for welded parties injecting gas. The incentives pool should allow those unable to inject gas to make claims against welded parties in positive running imbalance.
98. The GIC concludes that the inability of the balancing operator to pass title to gas when it claims incentive pool credits against the incentives pool creates confusion. We agree with that but allowing the balancing operator to pass title only provides some relief for the welded party incurring the incentive pool debits and doesn't fix the underlying confusion and problem created by the balancing operator being able to claim against running operational imbalances via cash-outs and also against daily operational imbalances via the incentives pool.

99. If incentive pool debits were determined from negative running operational imbalance, then the confusion would be avoided. In those circumstances, there would be no point in allowing the balancing operator to claim against the incentive pool as that would duplicate the cash-out mechanism.
100. There appears merit in retaining the peaking arrangements to the extent they permit submission of a daily nomination profiled across a day. That ability to do that would have increased importance if balancing costs were allocated against hourly running imbalance. The alternative, and better approach, would be to require hourly nominations.

### **Removal of TP Welded Party Balancing Gas**

101. We agree with the GIC's conclusion that deletion of the balancing gas provisions available to TP welded parties removes balancing flexibility available to TP welded parties including Vector. That deletion potentially increases the cost of balancing to shippers using Vector's pipeline.
102. We understand that Vector did not exercise these provisions because of the potential conflict with Vector shippers correcting their own imbalance positions following the issue of an ILON. However, removal of the ILON provisions may make the TP welded party balancing gas provisions more attractive to Vector shippers.
103. Allocation of balancing costs at TP welded points in accordance with downstream imbalance at connected welded points (remote welded points) would also make the TP welded party balancing gas provisions more useful.
104. We note that exercise of the TP welded party balancing gas arrangements would seem to require Vector to arrange a flexible supply of balancing gas. It potentially could do that through an arrangement similar to the BGX. It seems possible, with the help of the TP welded party balancing gas provisions, that Vector could create a market where balancing services for its pipelines could be offered by MPOC welded parties and by VTC shippers. Consistent with the Rules, this would help open the market for balancing services to all parties able to offer balancing services.
105. Section 9.10 of the MPOC, that MDL also proposes to delete through the MDL Change Request, should ensure that at least at the end of the day that the TP welded party only retains relief on the requirement to nominate to the extent its receipts and deliveries are in balance. The retrospective nature of these nominations, therefore, does not raise the same concern as the Maui legacy gas balancing arrangements.
106. The value of the TP welded party balancing gas provisions, and their relevance to balancing arrangements as the MPOC and VTC evolve, requires further evaluation before they are removed from the MPOC.

### **Tariff 3**

107. MDL proposes to recover balancing costs, that are not allocated via cash-outs or through the incentives pool, through tariff 3. MDL also proposes to recover the costs of the balancing operator performing its role through tariff 3. MDL proposes to publish the level of balancing costs recovered each month via tariff 3. The level of tariff 3 will fluctuate each month depending on the level of balancing costs incurred in that month.
108. Contact supports these proposals as the publication of the level of socialised balancing costs should provide an improved basis for determining whether or not there is net benefit in spending more resources to further improve balancing arrangements.

109. MDL proposes to allocate the total costs used to determine tariff 3 to shippers in accordance with gas deliveries made to shippers. The alternative is to allocate tariff 3 to welded parties on the basis of gas flows at welded points. That seems preferable as under the MPOC welded parties are responsible for balancing rather than shippers. Allocation to welded parties should ensure that the parties able to manage and control balancing costs pay those costs.
110. Our expectation is that tariff 3 should be insignificant because most balancing costs should be recovered via cash-outs.

### **Balancing Operator's Role and Responsibility**

111. We agree with the GIC's conclusion that the arrangements MDL proposes to set out in section 3 of the MPOC are an improvement on the status quo.
112. However, as indicated above, MDL's proposals are deficient in a number of areas including:
- the lack of recognition of standard operating procedures under the MDL Change Request and the MPOC;
  - the lack of any specification of the consultation process;
  - despite the consultation process, MDL's ability to introduce new operating procedures or to change existing operating procedures at any time;
  - the lack of description of the matters that must be covered by standard operating procedures;
  - the lack of description of the circumstances when the balancing operator would undertake balancing action; and
  - the lack of description of the circumstances when the balancing operator would curtail gas flows rather than undertake balancing action.
113. Because of these deficiencies we doubt that the provisions will be of much benefit to welded parties and shippers. MDL's proposal is inadequate

### **Operation of Balancing Gas Market**

114. The provisions included in the MDL Change Request relating to how MDL will instruct the balancing operator to operate the balancing market are not detrimental but lack detail as identified by the GIC.
115. It is also unclear whether MDL has any obligation to consult with shippers and welded parties related to the detail of these arrangements since the arrangements do not seem to be covered by MDL's obligation to consult under MDL's proposed section 2.18. That means that MDL could change the way the high level principles are implemented at any time.
116. MDL already has many of the obligations under the current MPOC related to the operation of a balancing market. The balancing operator, as MDL's agent, is already required to act as a reasonable and prudent operator. Under Section 4, MDL is required to publish any instructions that it issues to its operators and is also required to publish the relevant operator's procedures for implementing MDL's instructions.

117. We conclude that MDL's proposal is directionally correct but may in reality provide nothing more than the current arrangements.

### **Operator Instructions**

118. As indicated above and identified by the GIC, MDL's proposal to add a new section 2.18 requiring MDL to consult will not ensure improved operating instructions.
119. In addition, it's unclear what sections of MDL's proposed section 3 are covered by the obligation to consult.
120. A careful read of MDL's proposed section 3 suggests that the only part of section 3 covered by section 2.18 is section 3.5(c) which relates "*to the performance of the balancing operator's role*". Section 3.5(c) contains the only reference to "*standard operating procedures*" in section 3. Moreover, section 3 provides no assistance in determining the contents of standard operating procedures related to the performance of the balancing operator's role.
121. The meaning of "*consultation*" under section 2.18 is unspecified. Meaningful consultation requires a specified and transparent process to ensure the views expressed through consultation are considered by MDL.
122. We agree with the GIC that consultation should allow shippers and welded parties to express their views, but only to the extent that is made possible under the consultation process established by MDL. MDL would have no obligation to consider the views generated through the consultation or to describe how it reached its conclusions following the consultation.
123. The extremely narrow scope of application of section 2.18 and the lack of any prescribed consultation process makes section 2.18 largely ineffective.

### **"Pay Now Dispute Later"**

124. Under the MDL Change Request, MDL proposes to amend section 21.11 of the MPOC so that an invoiced party is required to pay the full amount stated in an invoice despite the invoiced party disputing all or some of the invoiced amount. That change is supported by proposed changes to sections 23.5 and section 23.6.
125. The key issue related to payment is that once part of an invoice becomes subject to a dispute there is no agreed, low cost effective means of resolving the dispute.
126. Under the current arrangements a party involved in a dispute can hold out for determination of the dispute by the courts. The cost, the time consuming nature and the uncertain outcome of a court determination inhibits resolution of disputes.
127. There is a need for the MPOC to contain a binding low cost effective dispute resolution process. It may be necessary to limit the use of that dispute resolution process to technical and well defined disputes so that more complex disputes involving issues of law can be determined by the courts.
128. The dispute resolution must be supported by the obligation to pay interest on disputed invoiced amounts once dispute resolution determines those amounts are payable.
129. MDL's proposal that disputed invoiced amounts should be paid before resolution of the underlying dispute is resolved does nothing to ensure that disputes are quickly and effectively resolved. It's unclear why MDL does not take action under the current arrangements if it wants to resolve disputes.

130. We are also concerned that the imbalance in information, related to a dispute, held by MDL and welded parties or shippers means that welded parties or shippers are in a weaker position in attempting to resolve disputes than is MDL.
131. In the absence of a binding dispute resolution process, MDL's proposal does nothing to ensure disputes are efficiently resolved. We do not support MDL's proposal.
132. Responsibility for imbalance at TP welded points and identification of the parties best able to manage that flow requires further consideration:
  - is MDL responsible because it allowed or caused the gas to flow;
  - is it the TP welded party because it allowed or caused the gas to flow;
  - is it the VTC shippers;
  - is it the VTC interconnected parties when gas flows from the MDL pipeline to Vector pipelines; or
  - is it MPOC welded parties when gas flows from Vector pipelines to MDL pipeline; and
  - do welded parties upstream of a TOP welded point influence gas flows at the TP welded point?

### **Proposed Non-balancing Changes**

133. The MDL Change Request includes a number of proposals that seem designed to reduce MDL's risk at the expense of shippers and welded parties. The changes are neither related to improving balancing arrangements nor related to improving the efficiency of the MPOC.

### **Maui Legacy Arrangements**

134. The current MPOC contains provisions that derive from the Maui legacy arrangements. These relate to obligations to provide a number of receipt and delivery points and the nature of metering at those points. Examples include the requirements of sections 16.2 and 16.5 of the current MPOC.
135. Changes to the current provisions may have cost implications for all shippers and welded parties.
136. The provisions relating to Maui legacy arrangements should not be removed until there is a full understanding of the implications of that. Removal of these provisions should be the subject of a separate change request.

### **Status of the Incentives Pool Trustee**

137. Through the MDL Change Request MDL proposes to redefine the incentives pool trustee as a "*person appointed by MDL*". The incentives pool trustee would no longer be the commercial operator as under the current MPOC.
138. The proposed definition of party under the MDL Change Request would mean that MPOC operators are MDL. Under the current MPOC, MDL includes the incentives pool trustee. Under the MDL Change Request the incentives pool trustee would be a person or party separate and distinct from MDL.

139. That proposed change seems to completely alter the status of the incentives pool trustee so that the incentives pool trustee and its role sit outside the MPOC arrangements. Those arrangements would instead be governed by the appointment arrangements between MDL and the incentives pool trustee.
140. Welded parties are dependent on the incentives pool trustee effectively recovering payments related to incentives pool debits from other welded parties in order to recover the liquidated damages payable if they are curtailed.
141. Despite the change in status of the incentives pool trustee proposed by MDL it has allowed the incentives pool trustee to continue to have obligations under the MPOC. For example, under section 14.4 the incentives pool trustee is required to warrant that the incentives pool account is an account separate from all the incentive pool trustee's other bank accounts. Such provisions and that warranty seem meaningless if the incentive pool trustee is not MDL and not a signatory to the MPOC.
142. Under MDL's proposed changes the liability of the incentive pool trustee would be limited to the funds payable to the incentives pool even in the event of the incentive pool trustee's negligence or wilful default. Is that consistent with the obligations of a trustee? Under the current MPOC the liability of the incentive pool trustee is not limited in that way.
143. MDL proposes to amend section 23.1 of the MPOC so that disputes with the incentives pool trustee are not disputes with MDL. MDL also proposes to amend section 38.2 so that the incentives pool trustee can enforce the provisions of the MPOC against welded parties. There is no provision allowing welded parties to enforce the provisions of the MPOC against the incentives pool trustee.
144. These changes are not directly related to balancing and seem designed to reduce MDL risk at the expense of welded parties. It is inappropriate for the GIC to support changes to the MPOC that change the risk profile of parties contracted under the MPOC.

### **Notional Welded Point**

145. Under the MDL Change Request, MDL proposes to delete the "*Notional Welded Point*" definition and to introduce new definitions for trading hub welded party and trading hub welded point. The reasons for these changes are unclear and the changes seem unnecessary. The changes seem unrelated to balancing.

### **MDL Liability for Gas Deliveries at TP Welded Points**

146. Under the MDL Change Request, MDL proposes to change section 2.13 (section 2.14 in the amended MPOC) and section 2.14 (section 2.15 in the amended MPOC) removing MDL's liability for gas deliveries at a TP welded point where that gas is not delivered to a VTC shipper.
147. The proposed changes to these sections seem designed to shift potential risk from MDL to TP welded parties. It is inappropriate for the GIC to support such changes that change the risk profile of the MPOC but do not result in overall improvement consistent with the Gas Act and Government Policy Statement objectives.
148. Furthermore, the proposed changes to section 2.15 of the current MPOC removing MDL's obligation to indemnify TP welded parties for its breach of section 2.14 of the current MPOC would make all of section 2.14 to section 2.16 largely valueless in the changed MPOC.



149. However, these sections should be unnecessary as Vector should ensure that allocation arrangements under the VTC are sufficiently robust to prevent parties, who are not shippers under the VTC, shipping gas through Vector transmission pipelines.
150. Subject to Vector confirmation that its allocation arrangements are effective, it should be possible to delete sections 2.14 to section 2.16. That should be accomplished by means of a separate change request to address this issue. Sections 2.13 to 2.16 are not directly related to balancing.

### **Publication of Information**

151. Through the MDL Change Request, MDL proposes extensive changes to information published on the MDL IX. There is a requirement to check the proposed list of information to ensure that it includes all the required information.
152. Unsatisfactorily, the frequency of posting of a number of items of listed information is not stated under the changes proposed by MDL. It is necessary that that frequency of posting should be stated for all the information listed in section 4.

### **Nominations for Balancing Gas**

153. MDL proposes changes to sections 8.23, 8.25 and 8.27 that remove the priority afforded to TP welded party balancing gas.
154. For the reasons indicated above those provisions should be reinstated.

### **Change Request Process**

155. MDL proposes to add a new section 29.5 and section 29.6 to section 29 that sets out the process for making modifications to the MPOC.
156. Section 29.5 would allow a change request to include:
  - a timetable for implementing the change request;
  - transitional provisions for implementing a change request; and
  - conditions that must be satisfied before a change request is implemented.
157. Section 29.6 recognises that the transitional provisions would form part of the MPOC.
158. Contact has no objection to the principles set out in the proposed new sections. However, the sections are completely unnecessary. There is nothing in the MPOC that constrains or limits the content of a change request. In addition, the proposed new sections are unrelated to balancing.
159. In the interests of simplifying the MPOC these unnecessary changes should not be made.

### **Concluding Remarks on the MDL Change Request**

160. The MDL Change Request contains a complex and confusing array of changes. The changes seem to fall into the following categories:
  - improvements to balancing procedures;
  - measures to reduce MDL risk at the expense of other parties contracted under the MPOC; and

- measures tidying up the MPOC such as the removal of redundant provisions.
161. Contact supports some of MDL's proposed changes to balancing procedures but overall the balancing proposals are deficient because the mechanisms:
- do not specify circumstances in which MDL will undertake balancing action;
  - do not ensure balancing services are obtained at least cost;
  - allocate balancing through a number of mechanisms that are inconsistent and confusing; and
  - do not ensure welded parties are fully compensated for gas that is not delivered.
162. Change requests that are designed to shift risk from one party contracted under the MPOC to another party under the MPOC should not be supported. For that reason Contact does not support the following changes:
- the removal of the provisions related to TP welded party balancing gas;
  - the obligation to manage imbalance to zero at all times;
  - the removal of the boundaries for liability related to imbalance;
  - the inability to correct errors related to balancing charges;
  - the inadequate definition of UFG;
  - lack of responsibility for imbalance related to UFG and fuel gas;
  - the introduction of "*pay now, dispute later*" provisions in the absence of a low cost efficient means of resolving disputes;
  - the removal of the Maui legacy gas provisions before the relevance of those provisions is considered; and
  - the changes to the status of the incentives pool trustee.
163. A number of the changes that seem designed to tidy up and remove redundant provisions from the MPOC require further analysis and consideration.

### **An Alternative Approach**

164. Contact agrees that the MPOC, and the VTC, should be changed to improve the balancing provisions.
165. Contact believes the first step in that change process should be to establish a design framework for balancing.
166. That design framework should be:
- derived from best practice;
  - take account of investment in existing balancing arrangements and infrastructure; and

- be subject to careful and thorough cost/benefit analysis.

167. From experience the design framework should include the following:

- arrangements that allow access to pipeline flexibility;
- recognition that balancing arrangements provide benefits for transmission system owners, welded parties and shippers;
- establishment of the same balancing arrangements across the transmission system;
- establishment of arrangements that makes it immaterial whether MDL and Vector employ separate balancing operators or a joint balancing operator;
- a requirement to source balancing services from a competitive, open and transparent market;
- clear description of the factors the balancing operator is required to consider in undertaking balancing action;
- consistent allocation of balancing costs across the transmission system;
- allocation of balancing costs in accordance with imbalance at the time the balancing action was undertaken but recognising that there is a trade-off between accurate allocation and the cost of achieving that;
- costs are best allocated at the point where they can be controlled;
- definition of the costs recoverable as balancing costs;
- definition of the constituents of a transmission service and a balancing service;
- full access to balancing tools to minimise balancing costs so that the need for residual balancing is avoided as far as possible and so that parties are able to self balance as far as possible;
- allocation of all gas injections and offtake at intervals consistent with the obligation to balance and consistent with the allocation of balancing costs;
- allocation of balancing costs related to pipeline operation and UFG to the pipeline operator in the same way that other parties are allocated balancing costs;
- provision for corrections but in a way that does not prevent parties meeting their obligation to balance;
- full and open access to all balancing related information that will enable parties to best manage balancing and that will allow unnecessary or inappropriate balancing action to be challenged;
- a welded party right to claim compensation for loss of gas or failure to provide transmission services;
- provision of a binding dispute resolution process that allows balancing related disputes to be settled promptly and at minimum cost; and

- arrangements simplified as far as possible.
168. Once the design framework is established then balancing related change requests could be consistently determined against that framework. It may be necessary to establish the design framework through regulation.
169. As demonstrated by responses to the MDL Change Request, the complexity of current balancing arrangements make it difficult to resolve balancing issues through a single change request. Limiting the matters covered by a change request to a single set of directly related issues should ensure the details of each change request receives appropriate consideration. Such separation should also reduce the burden, and simplify the analysis, of the change request.
170. Balancing arrangements should be improved through a number of separate change requests that are easy for the industry to digest and assess. The GIC appears to support that approach. To ensure that approach is followed the GIC should decline to support change requests that are wide in scope and that include proposals that are not linked.

### **Contact Balancing Change Request**

171. Contact has developed a new change request that is designed to address balancing issues and that is consistent with the principles indicated above (Contact Change Request).
172. The draft has been developed from the MDL Change Request. A draft of a revised MPOC incorporating the Contact Change Request is attached. A mark up against the current MPOC and a draft of the MPOC incorporating the MDL Change Request are also attached.
173. The Contact Change Request is a work in progress. That is consistent with evolution of the MPOC and the VTC as the surrounding environment evolves and develops. The Contact Change Request does not address areas such as the allocation of imbalance at receipt points and delivery points on the Vector transmission system and the allocation of imbalance at delivery points where determination of daily allocation is not possible under current arrangements. Nevertheless, these are essential elements of balancing and must be resolved.
174. In addition, the Contact Change Request must be sub-divided into a number of change requests to allow proper consideration of the elements of the change request.

### **The Main Provisions of the Contact Change Request**

175. The main provisions of the Contact Change Request are summarised in paragraphs 176 to 188 below.
176. The provisions relating to Mismatch are deleted.
177. The Mismatch provisions set out in section 11 of the MPOC are replaced by a new section titled "*Balancing Process*". This section is based on the new section 3 titled "*Balancing Principles*" that MDL proposes to insert in the MPOC via the MDL Change Request. A number of significant changes are made to MDL's drafting:
- MDL is required to issue any instructions related to balancing and the operation of the BGX as standard operating procedures;
  - standard operating procedure becomes a defined term so that these procedures have standing under the MPOC;

- MDL is required to issue a standard operating procedure that sets out the matters that MDL will consider in undertaking balancing action;
  - that standard operating procedure is also required to list matters MDL will consider in curtailing gas flows;
  - separate welded points are defined for correction of UFG and off-take of fuel gas;
  - MDL is responsible for balancing costs related to UFG and fuel gas imbalance at the relevant welded points; and
  - before standard operating procedures can be implemented, or changed once implemented, MDL must consult with shippers and welded parties using the change request process.
178. UFG is defined in the same way as in the VTC so that the determination of UFG is not at MDL's discretion.
179. All balancing costs, including costs resulting from welded party enforced imbalance, are allocated on the basis of accumulated excess operational imbalance at the time the balancing action was committed. Tolerances at each welded point are calculated as 3% of the scheduled quantity.
180. Initially cash-outs and incentive pool debits are determined from running imbalance calculated at daily intervals.
181. Any unrecovered balancing costs are recovered through tariff 3, from welded parties against gas flows at welded points.
182. MDL will report the magnitude of tariff 3 costs each month.
183. It is intended that if tariff 3 is significant, and includes substantial balancing costs not recovered through cash-outs, then running imbalance will be determined at more frequent intervals such as at the end of each intraday cycle or on an hourly basis.
184. The ILON provisions are removed.
185. Errors in the calculation of operational imbalance, and the allocation of balancing costs, are corrected in the future following notice of the error.
186. The inconsistent right to claim balancing costs against daily imbalance and peaking are removed.
187. The incentives pool mechanism is retained with incentive pool debits determined from accumulated excess operational imbalance. Only welded parties with curtailed scheduled quantity can make incentive pool claims.
188. As under the current MPOC there is no prorating of incentive pool claims so that the level of incentive pool debits equates to the level of incentive pool credits on a GJ basis.

### **Comparison of the MDL Change Request and the Contact Change Request**

189. The main differences between the MDL Change Request and the Contact Change Request are summarised in paragraphs 190 to 206.
190. All the changes in the Contact Change Request are directly related to balancing and the provisions of the current MPOC not related to balancing are retained.

191. The status of the incentives pool trustee remains unchanged.
192. UFG is better defined in accordance with the VTC provision.
193. MDL, as the provider of transmission services, is responsible for balancing costs resulting from its failure to address UFG or to nominate gas taken for fuel gas.
194. The Maui legacy gas provisions remain unchanged.
195. Standard operating procedures are given standing under the MPOC and the content of these are better specified, particularly the matters MDL is required to consider before undertaking balancing action.
196. The consultation that MDL must undertake before implementing or amending a standard operating procedure is prescribed.
197. The shipper mismatch provisions are removed.
198. The provisions related to TP welded party balancing gas are retained.
199. The limitations on welded party liability for imbalance set out in section 12.1 are retained.
200. Provision is made for corrections to running operational imbalance and corrections to the allocation of balancing costs.
201. There is no daily operational imbalance or excess daily operational imbalance.
202. Cash-outs are allocated against accumulated excess operational imbalance, with allowance for tolerance rather than allocated against running operational imbalance with no allowance for tolerance.
203. Incentive pool debits are incurred on accumulated excess operational imbalance rather than excess daily imbalance.
204. There is no prorating of incentive pool credits so that they equate to incentive pool debits on a GJ basis.
205. The ability to claim balancing costs against incentive pool debits incurred for exceeding a peaking limit is removed.
206. Welded parties, shippers and MDL are only required to pay invoices to the extent that the invoiced amount is not in dispute.

### **Progressing the Contact Change Request**

207. Despite the considerable narrowing of the scope of the Contact Change Request and the attempt to adhere to an overarching design framework, it is still a complex document that requires considerable analysis and debate. In respect of complexity, it suffers the same drawbacks as the MDL Change Request. Review is made more difficult by having to identify differences in comparison to the current MPOC and in comparison to the MDL Change Request.
208. Contact is still considering the best way forward but at this stage believes the best approach is to sub-divide the Contact Change Request into a number of separate and more digestible change requests.
209. The separate change requests could be the following:

- removal of Mismatch provisions;
- introduction of balancing standard operating procedures;
- transmission service providers obligations related to UFG and fuel gas;
- corrections to the calculation of running operational imbalance and balancing cost allocations;
- revision of tolerances;
- removal of the ILON process and the allocation of cash-outs against accumulated excess operational imbalance; and
- operation of the incentives pool and removal of incentive pool debits earned for exceeding the peaking limits.

210. Contact would appreciate the opportunity to further explain and discuss this submission.

Yours sincerely



Alex Love  
Senior Adviser

Senior Adviser  
Contact Energy Limited

Attachment 1

Redraft of the MPOC incorporating Contact's proposed Change Requests

Attachment 2

Redraft of the MPOC incorporating Contact's proposed Change Requests marked up against the Current MPOC

Attachment 3

Redraft of the MPOC incorporating Contact's proposed Change Requests marked up against the MPOC incorporating MDL's Change Request