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30 October 2009

Ian Wilson
Gas Industry Company
Level 8, Todd Building
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By email: submissions@gasindustry.co.nz

Dear Ian

Transmission Pipeline Balancing – Statement of Proposal

Genesis Power Limited, trading as Genesis Energy, welcomes the opportunity to provide a submission to the Gas Industry Company (GIC) on the paper “Statement of Proposal: Transmission Pipeline Balancing” dated October 2009.

Genesis Energy recommends that the GIC should delay its decision on whether to proceed with its proposed rules until the middle of 2010. This would allow the GIC to bring forward other items on its work programme and would provide the Industry Code Development (ICD) process time to run its course. The ICD process is making good progress and its efforts will not be in vain even if the GIC ultimately decides to transfer the work of improving balancing arrangements into its “participative regulation” process.

Genesis Energy expects that the most likely outcome of the ICD process is that it will be successful at significantly reducing the scope of any residual regulatory concerns to the point where a different, more limited, regulatory intervention is more appropriate. Genesis Energy expects that this approach will lead to arrangements that are more efficient and that better meet the needs of pipeline owners, operators and users.

Genesis Energy’s responses to the consultation questions are in Appendix A.

If you would like to discuss any of these matters further, please contact me on 04 495 3348.

Yours sincerely

A handwritten signature in black ink that reads "R Parry". The signature is written in a cursive, flowing style.

Ross Parry
Regulatory Affairs Manager
Genesis Energy

Appendix A: Responses to Consultation Questions

QUESTION	COMMENT
<p>Q1: Do you agree with the Gas Industry Co's decision to pursue the ICD process?</p>	<p>Yes.</p> <p>If the ICD process is successful then it will preserve the desirable attributes of having transmission arrangements that participants have developed and agreed upon themselves, and are able to adapt as the market evolves.</p> <p>A successful process should also limit the necessary scope of any future regulatory intervention to those areas where participants truly cannot come to an agreement that is in the long-term interest of consumers.</p> <p>Even if the ICD process is not successful and the GIC implements the participative regulation option, the progress made during the ICD process should help to improve the balancing plan process under the regulations by giving participants a better "running start".</p>
<p>Q2: Do you agree with the Gas Industry Co's proposal to pursue the participative regulation option?</p>	<p>No.</p> <p>At this stage, Genesis Energy considers that the ICD process is making good progress and that the GIC should allow it more time to run its course.</p> <p>If the ICD process is able to deliver on most of the outcomes that the GIC seeks to achieve via regulation, then this will be a significantly better outcome than halting the ICD process now and essentially transferring a subset of the same work into a different "regulated participation" forum that primarily relies on the TSOs</p>

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	<p>to develop a balancing plan.</p> <p>Genesis Energy expects there may be some residual problems that the ICD process cannot resolve adequately. If this proves to be the case, then the appropriate regulatory approach for resolving residual market failures could differ significantly from the participative regulation option proposed now. For example, a more tightly defined regulatory problem could suit a more targeted regulatory intervention.</p> <p>Genesis Energy understands that the Minister and officials may be impatient given that pipeline balancing has been on the government policy statement for gas governance for some time. However, it is important to remember that post-legacy balancing arrangements will reach their first anniversary in December. As such, the industry has made good progress at understanding and resolving balancing problems in a short timeframe.</p> <p>If the ICD process continues to make good progress then participants are likely to make material improvements to balancing arrangements well ahead of the implementation timeframes under regulations. This will be a successful outcome in terms of avoiding an unnecessary regulatory impost. In other words, there is significant option value to waiting before intervening. Genesis Energy expects that a rigorous cost benefit analysis would demonstrate this option value.</p> <p>If the GIC is determined to pursue a regulatory option immediately, then Genesis Energy agrees that the</p>

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	participative regulation option appears to be the best option to pursue.
Q3: Do you agree that the draft rules adequately address issues with respect to residual pipeline imbalance?	<p>This is difficult to determine in advance of the transmission system owners (TSOs) developing and implementing their balancing plan under the rules.</p> <p>The ICD process should help to identify whether there are any issues the draft rules do not adequately address.</p>
Q4: Do you have any comments on the major operational provisions?	<p>Genesis Energy expects that the ICD process will shed more light on the workability and desirability of the major operational provisions proposed in the rules. For example:</p> <ul style="list-style-type: none"> • it may be the case that marginal pricing of balancing gas is the best approach in the long run, but Genesis Energy considers that the state of balancing market development probably favours weighted-average pricing for now; • a different allocation of roles may prove more cost-effective by, for example, separating functions requiring 24-7 operation from functions such as procurement and allocation that can be performed in normal hours; and • the provisions need to be consistent with the reality that, absent major investment in metering infrastructure, balancing will continue to occur on the basis of daily values.

QUESTION	COMMENT
<p>Q5: Do you agree with the Gas Industry Co's decision not to include curtailment, damages and tolerances?</p>	<p>Genesis Energy considers that tolerances should be included in the rules since they are a fundamental component of the balancing regime design.</p> <p>Genesis Energy considers that an optimal balancing regime would allow uniform small tolerances for each welded point sized to reflect the inherent operational limitations on the ability for transmission users to balance precisely within a day.</p>
<p>Q6: Do you agree with the details of the balancing plan?</p>	<p>It is difficult to assess the adequacy of the balancing plan at this stage.</p> <p>As with their recent experience developing critical contingency plans, it is likely that the TSOs will find it difficult to develop a plan within the proposed time limits that can reconcile the differences between the pipeline systems, and that will ensure integration of arrangements for balancing services with arrangements for basic transport services and contingency management.</p> <p>Genesis Energy expects that the technical and commercial difficulty of the task will preclude adequate involvement by pipeline users and end consumers in development of the balancing plan. The ICD process is superior to the participative regulation option in this respect.</p> <p>Vector is likely to find the process particularly difficult given that the definition of "users" in the rules is not consistent with the contractual arrangements that Vector has with its inter-connected customers.</p>

QUESTION	COMMENT
<p>Q7: Do you have any other comments on any aspects of the proposal?</p>	<p><u>Integrated vs. Unified</u></p> <p>Genesis Energy recommends that the term “integrated” would be preferable to the term “unified” as this better encapsulates the objective that the GIC is seeking.</p> <p>For example, a seamlessly integrated set of arrangements across pipelines and across agents may be able to deliver a more efficient and flexible outcome than a unified balancing agent. The GIC should be agnostic to which approach pipeline owners and users develop, provided the outcome is that pipeline balancing is efficient.</p> <p><u>Contingency Price Pre-Estimate</u></p> <p>Genesis Energy is concerned that it will not be practicable for the TSOs to develop a pre-estimate of critical contingency prices as required in clause D(c) of the schedule to the rules.</p> <p>The process for determining the critical contingency price is untested and relies on expert evaluation of complex criteria. It is unrealistic to expect the TSOs to “pre-estimate” this value.</p> <p><u>Balancing Agent Takeover</u></p> <p>Genesis Energy has some concerns about the provision in part three of the rules for the industry body to sever the balancing agent’s contract with the TSOs and establish itself as the principal in a new contractual arrangement with a new balancing agent.</p> <p>In particular:</p>

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	<ul style="list-style-type: none"> • this regulatory risk is likely to be priced into any contract for balancing agent services; • there would appear to be a case for stronger checks and balances on the industry body's ability to exercise this authority given the consequences for the TSOs and the incumbent balancing agent; • the statutory basis for this authority would need to be sufficiently robust to withstand the likelihood of the incumbent balancing agent challenging the industry body's authority; and • the industry body would need to be sure that it had the financial capacity to exercise this authority. <p><u>Balancing Market Suspension</u></p> <p>Genesis Energy has similar concerns to those set out above with respect to the authority in rule 17 for the industry body to suspend or terminate the balancing market.</p> <p>In addition, rule 17.2 should require the industry body to set out in detail why it believes the balancing market does not meet the purpose of the rules and what is considers needs to be done to ensure the market does meet the purpose of the rules.</p>
<p>Q8 Do you agree with the proposed next steps?</p>	<p>Genesis Energy believes that the GIC should recommend to the Minister a deferral of the decision on whether to regulate until mid-2010 to allow the ICD process more time to deliver on its early promise.</p>