

15 March 2018

Gas Industry Company Ltd
Level 8
The Todd Building
95 Customhouse Quay
PO Box 10-646
Wellington 6143

Preliminary Assessment of Gas Transmission Access Code (GTAC)

PART I: OVERVIEW

1 Introduction

- 1.1.1 Trustpower Limited (**Trustpower**) thanks Gas Industry Co (**GIC**) for the opportunity to submit on its 13 February 2018 *Preliminary Assessment of Transmission Access Code* consultation paper (**Preliminary Assessment paper**).
- 1.1.2 The Gas Transmission Access Code (**GTAC**) was developed by First Gas to replace the Maui Pipeline Operating Code (**MPOC**) and Vector Transmission Code (**VTC**).
- 1.1.3 Trustpower's participation in that process has comprised:
 - a) Formal responses to GTAC consultations;
 - b) Attendance at the various industry meetings listed in Appendix B of the Preliminary Assessment paper; and
 - c) Informal discussions and correspondence including calls between shippers and one on one meetings with both the GIC and First Gas.

2 Background

- 2.1.1 VTC will terminate on 30 September 2018 (unless extended) whereas MPOC will terminate when certain pre-conditions are met.
- 2.1.2 These pre-conditions include a GIC determination that GTAC is materially better than the current access terms having regard to the objectives and set out in Part 4A of the Gas Act 1992 and the April 2008 Government Policy Statement on Gas Governance (**Objectives and Outcomes**).
- 2.1.3 The Preliminary Assessment paper constitutes the GIC's *draft* determination. Following consultation a *final* determination will be published and, if positive, will trigger the MPOC code replacement process.

- 2.1.4 The GIC's preliminary assessment is that GTAC is not materially better than the status quo with four areas of concern 'tipping the balance'.
- 2.1.5 Those areas are GTAC's:
- a) Provision for substantial daily overrun and underrun charges. The GIC is concerned that these charges may inefficiently discourage pipeline use when capacity is not scarce (which appears to be the case for the foreseeable future);
 - b) Inclusion of a new subrogation process that *purports* to give rights to shippers and interconnected parties to enforce breaches of the GTAC against other shippers and interconnected parties (in First Gas' name). There are issues whether this is effective and/or improves existing arrangements. There is also a concern that reduced rights in relation to non-specification gas will adversely affect reliability;
 - c) Failure to provide access seekers with significant certainty about the terms on which the interconnection service will be provided, and enforced, for the benefit of all access seekers; and
 - d) Failure to provide access seekers with sufficient certainty about how line pack flexibility will be managed in the context of a park and loan transmission product and/or clarity about whether this will be a regulated or unregulated service (as the difference affects the incentives of the pipeline owner).
- 2.1.6 To assist it with its *final* determination the GIC has asked stakeholders two questions:
- 1. Do they agree/disagree with the GIC's preliminary assessment of GTAC, and why?
 - 2. Do they support GTAC?
- 2.1.7 It is not clear from the Preliminary Assessment paper what the next steps will be for the reform of the access arrangements if the GIC confirms its preliminary assessment.
- 2.1.8 At the GIC's workshop on 1 March:
- a) The GIC said that there was no restriction on the number of access proposals which First Gas, or indeed any other participants, could present under the MPOC Code change process.
 - b) First Gas said it remained of the view that the access code it developed was materially better than the current access arrangements and had not yet decided if would withdraw GTAC and resubmit an amended version in the light of the GIC's preliminary assessment.
 - c) First Gas said it would be helpful to them in reaching a decision on this matter if stakeholders answered three questions in their responses:
 - *How far away from the materially better standard do you think we are?*
 - *How long do you think it will take to re-engage and achieve materially better?*
 - *Do you have any preferences on how the process should be run from here on in?*
 - d) Stakeholders appeared to have various views ranging from
 - A desire to stop the reform process and retain the status quo (MPOC and VTC);
 - Support for the further refinement of GTAC to address the matters highlighted in the Preliminary Assessment paper;
 - Starting again on a new industry code with a different development process; and
 - Support for a regulatory solution developed by GIC using GTAC as a base.

3 Trustpower's views

- 3.1.1 Trustpower is a multi-product retailer which trades in a number of regulated sectors. As far as practicable we seek alignment in the way similar issues are regulated across those sectors.
- 3.1.2 In the gas sector we are seeking a transmission access code which fosters competition in highly concentrated markets by providing access on terms which are fair and reasonable to a trader operating solely at the retail level.
- 3.1.3 This is not a novel concept: as we have noted in previous correspondence on GTAC, this has been a government policy goal for many decades.
- 3.1.4 We also care about the process by which decisions are reached. Our experience, is that sound process produces sound decision- making.
- 3.1.5 Based on this criteria, we have reservations on the following matters:
- a) The quality of the process run by First Gas;
 - b) Elements of the GIC preliminary assessment on:
 - i. Gas transmission products, pricing and congestion management;
 - ii. Energy quantity determination, allocation and balancing;
 - iii. Arrangements for curtailment; and
 - iv. Governance; and
 - c) The overall results of the selected assessment methodology.
- 3.1.6 We explain our reason for these reservations in sections 5 to 10 of this submission.
- 3.1.7 More significant perhaps, is the question of whether Trustpower supports:
- a) GTAC in its present form and/or
 - b) a further round of “refinement and retuning” to address the matters raised by the GIC in its Preliminary Assessment paper.
- 3.1.8 We do not support GTAC as presently constituted.
- 3.1.9 Our current preference is for the GIC to develop a regulated solution using GTAC as a guide.
- 3.1.10 However if there is strong evidence from First Gas and other stakeholders that they will support an access code that more satisfactorily addresses the mass market and governance issues we have been raising since consultation began we might be persuaded to commit to another round of negotiations.

4 Structure of our submission

- 4.1.1 We have addressed the substantial majority but not all GIC questions. Our submission focusses on matters which directly affect mass market retailing and downstream competition.
- 4.1.2 Some of these matters are covered in more than one section in the Preliminary Assessment paper. However we have found it more efficient to respond on subject topics. As a consequence we have not responded following the submission template.
- 4.1.3 However, we trust the following table will assist the GIC to analyse our response:

GIC assessment	Trustpower's submission response	Question numbers
Methodology and its outcomes	Section 6	Q1, Q12
Gas transmission products, pricing and congestion management	Section 7	Q2, Q3, Q8,Q14, Q15, Q16,Q20,Q21
Energy quantity determination, allocation and balancing	Section 8 (balancing)	Q4, Q5, Q6,Q20
Curtailement	Section 10	Q7,
Governance	Section 11	Q10, Q18,

4.1.4 In section 12 we provide answers to First Gas's supplementary questions (as tabled at the GIC's 1 March workshop).

PART II: COMMENTS ON GIC'S PRELIMINARY ASSESSMENT

5 First Gas process

- 5.1.1 Process is important and one of the key mechanisms by which:
- a) A regulator, or as is the case with First Gas a *de facto* regulator, can obtain and sustain a mandate to determine access rules and
 - b) Access seekers can be “heard” and through that “hearing” process hold a regulator or *de facto* regulator, to account for its decision-making.
- 5.1.2 From our perspective the following elements of First Gas’s GTAC development process did not meet our expectations of sound process:
- a) Failure to engage on governance topics we raised at the outset. We note that compliance issues have proved a significant stumbling block in the GIC’s preliminary assessment and at least to our mind there are still unresolved issues regarding the:
 - i. need for Commerce Act authorisation of GTAC as it is now evident the GIC and First Gas’s preferred access code arrangements differ;
 - ii. suitability of the rule change process given the current (predictable) GTAC outcomes;
 - b) Failure to engage with expert reports by explaining what part of our expert’s views are incorrect and why;
 - c) Timeframes for responses, particularly the lack of opportunity to express views on the final version of GTAC developed by First Gas.
- 5.1.3 Therefore we do not agree with GIC’s assessment that the process has been “comprehensive and inclusive”.
- 5.1.4 We raised some of these matters directly with First Gas in a bilateral meeting on 2 March 2018.
- 5.1.5 We were advised that:
- a) First Gas had received legal advice that it was not bound by the legal obligations to consult and follow the rules of natural justice (although it also contended that it had in practice followed these rules);
 - b) There were constraints on the degree to which First Gas could meet “best practice” standards of consultation and engagement as it was a commercial entity operating under a regulated price path.
- 5.1.6 This troubles us given the industry’s apparent willingness to allow First Gas to “hold the pen” on the transmission access code and its ongoing evolution. [We note that this is not the approach Transpower takes when it determines access arrangements to its network such as its recent review of its transmission pricing methodology].
- 5.1.7 We encourage the GIC to review its preliminary assessment in the light of this advice.

6 GIC’s process and outcomes

- 6.1.1 The Preliminary Assessment paper explains the GIC’s “bottom up” (subject area) assessment and its top down (principle) assessment of GTAC versus the status quo.
- 6.1.2 It also outlines the GIC’s views that:
- a) there is a hierarchy in the Objectives and Outcomes (based on originating document and the use of the word ‘principal’ in section 43ZN(a));

- b) the Objectives and Outcomes are very broad;
 - c) it is required to consider all of the Objectives and Outcomes and make a holistic assessment of benefits and detriments¹; and
 - d) “materially better” does not mean “most appropriate access terms” as all that is required is an “on average” significant improvement on the status quo.
- 6.1.3 Under its contractual code change role, the GIC is not tasked with considering alternative access terms on any topic which:
- a) provide access to the transmission network on terms which are more reasonable to shippers or which better reflect the Objectives and Outcomes; and/or
 - b) do not have the same level of detriment or disadvantage to a group of shippers or an individual stakeholder.
- 6.1.4 This creates the prospect that the GTAC could disadvantage a group of shippers or an individual stakeholder but still be approved by the GIC as being materially better as a whole for the majority of shippers or on the majority of issues.
- 6.1.5 This also means if there is a simple solution to an issue affecting an individual shipper or a group of shippers, it will not necessarily be adopted.
- 6.1.6 Trustpower accepts this is permissible interpretation of GIC’s MPOC role. However we do not think it is the only possible interpretation or indeed the most desirable interpretation.
- 6.1.7 At best it represents an inexorably slow transition towards a modern regulatory environment which recognises the value of competition and openly supports new entrants².
- 6.1.8 At worst it invites cynical trade-offs with persons with market power to get just within the approval thresholds.

7 Gas transmission products and pricing

- 7.1.1 Trustpower does not consider the proposed gas transmission products, including the new products to manage congestion, and the associated pricing arrangements:
- a) meet the Objectives and Outcomes or
 - b) provide reasonable terms and conditions of access for retailers who predominantly supply the mass market.

Product design for core service

- 7.1.2 We accept there some efficiency improvements in the proposed GTAC product design such as Daily Nominated capacity (**DNC**) and use of delivery zones.
- 7.1.3 However, we have concerns about the cost-benefit trade off of the new nomination regime, particularly in relation to the delivery zone nominations where capacity is not constrained.
- 7.1.4 We agree with Genesis that:

The strict requirements for accuracy under GTAC will increase costs for shippers and ultimately consumers; this is particularly true for mass market customers with loads difficult to predict and demand profiles that differ from season-to-season. This is

¹ Preliminary Assessment paper page 7

² In the interests of transparency we should record that our view that, this pace of change offends against the Objectives and Outcomes the GIC is required by the Act and its constitution to “pursue”, has not changed.

inconsistent with a system designed with a degree of tolerance in-built, and materially worse compared with the status quo in our view.

We repeat our call for conforming load to be modelled and managed by First Gas. We agree with the GIC that this approach would be consistent with the UK gas market, but also it would align with how Fixed Price Variable Volume customers are managed in the New Zealand electricity market.

- 7.1.5 We also note that whilst the number of points requiring daily nominations is the same as the status quo, there will be a substantial increase in the number of points which any mass market retailer will be required to nominate to as a result of the way zones have been defined to a more granular level.

Product pricing

- 7.1.6 In relation to pricing, we agree with the GIC's view that the level of overrun and underrun fees could deter pipeline use and/or excessive effort by shippers to forecast their capacity needs where there is no operational requirements to do so.
- 7.1.7 We also continue to hold a concern that the revised rebate scheme means smaller shippers will face higher incentive charges than larger shippers (because rebates are proportional to shares of lower DNC charges) and this factor in combination with a higher overall level of incentive charges will "*lessen competition in the downstream gas retail markets*"
- 7.1.8 This appears to be a case of pipeline owner designing a regime which removes the risk of it having to account for rebate revenue in its price path at the cost of new entrants and smaller players.

Congestion management products

- 7.1.9 GTAC contains new options to manage congestion including:
- a) Supplementary Agreements (**SAs**) which could provide bespoke capacity allocations;
 - b) Interruptible Agreements (**IAs**) which provide for a paid demand response;
 - c) auctioned Priority Rights (**PRs**) which give holders priority for their nominated quantities over other shippers
- 7.1.10 We acknowledge that the GIC finds these new products conceptually appealing as a tool for managing congestion, but we urge it to place greater weight on market context (highly concentrated industry) and practice (risk of strategic PR auction behaviour) in its assessment.
- 7.1.11 Our view is that these arrangements are not a significant improvement on the status quo.
- 7.1.12 We are concerned about the level of discretion afforded to First Gas to set terms of SAs and IAs and the potential impact its bilateral decision-making may have on capacity and prices in the PR auctions.
- 7.1.13 We are also concerned that the need for mass market retailers to acquire PRs will over-signal the value of capacity. This does not appear to have been taken into account in the GIC's analysis.
- 7.1.14 We are pleased GIC and other submitters recognise our concerns that:
- a) the PR auctions may not result in an efficient allocation of risk because if mass market shippers are unable to secure PRs in either the primary or secondary markets they have no effective means of reducing their demand.³

³ Ibid page 24

- b) it is also not *fair* that retailers may not be able to buy affordable PRs and so could become caught in a squeeze between their customers and the competing priorities of the network owner and/or other access seekers.
- 7.1.15 We are disappointed that the GIC appears to have discounted these risks in its assessment because it has a view that there is no immediate congestion concerns affecting mass market shippers.
- 7.1.16 This rationale could equally support a delayed start date or deletion of this aspect of the Code particularly in the light of the GIC's agreement with Greymouth's submission that the PRs are unworkable until the PR auction rules are developed.⁴
- 7.1.17 We have less confidence than the GIC that the proposed PR auction rule development and approval process will:
 - a) identify all the rules needed to protect the position of mass market retailers at the outset; and
 - b) ensure that those rules are appropriately monitored, administered and enforced.
- 7.1.18 It is far more likely the rules will need to evolve to address inefficiencies and inequities and we have no appetite for being the trigger for future corrective action, albeit this may only occur occasionally!
- 7.1.19 As a result we disagree with the GIC's overall assessment of gas transmission and products and pricing and congestion management. For Mass Market retailers we believe that GTAC is demonstrably worse than the status quo.

8 Energy quantity determination, allocation and balancing

- 8.1.1 Trustpower has nothing to add to the GIC's assessment of the issues around energy quantity determination and allocation in the Preliminary Assessment paper.
- 8.1.2 In relation to balancing we agree with the GIC that the asymmetrical excess running mismatch fees (**ERM**) raise potential efficiency concerns as these fees incentivise shippers to carry positive ERM.
- 8.1.3 However, we have another concern namely the risk that the proposal will provide sustained upward pressure onto market prices by incentivising market offers to be \$0.60/GJ ABOVE the last trade, while bids will only be \$0.20/GJ BELOW the last trade.
- 8.1.4 We request that the GIC review its assessment in the light of this risk.

9 Curtailment

- 9.1.1 GTAC uses the term curtailment to address both the curtailment of physical flow and curtailment of nominations.
- 9.1.2 In relation to physical flow, GTAC contemplates First Gas issuing operational flow orders to curtail physical injection, flow or the offtake of gas. If a shipper fails to comply with such an order it is deemed not to have acted as a reasonable and prudent operator and has to indemnify First Gas for any resulting losses.
- 9.1.3 We agree with Contact that this provision is unfair to shippers who supply to end users who are unable to curtail their demand.

⁴ Preliminary assessment paper page 16

- 9.1.4 The GIC suggests that it should be sufficient if a shippers “*end users contracts make provision for an appropriate end user response*”
- 9.1.5 This is not what GTAC says and in any event just leaves open the question of what is an appropriate response from a mass market customer.
- 9.1.6 We would like First Gas or the GIC to clarify what steps we would need to take with our mass market customers to meet the test of “*using best endeavours to immediately comply with*” an operational flow order.
- 9.1.7 Failure to provide such clarification, leaves mass market retailers with an unreasonable indemnity risk.
- 9.1.8 In relation to curtailment of nominations, we are comfortable with the proposed pro rata approach.

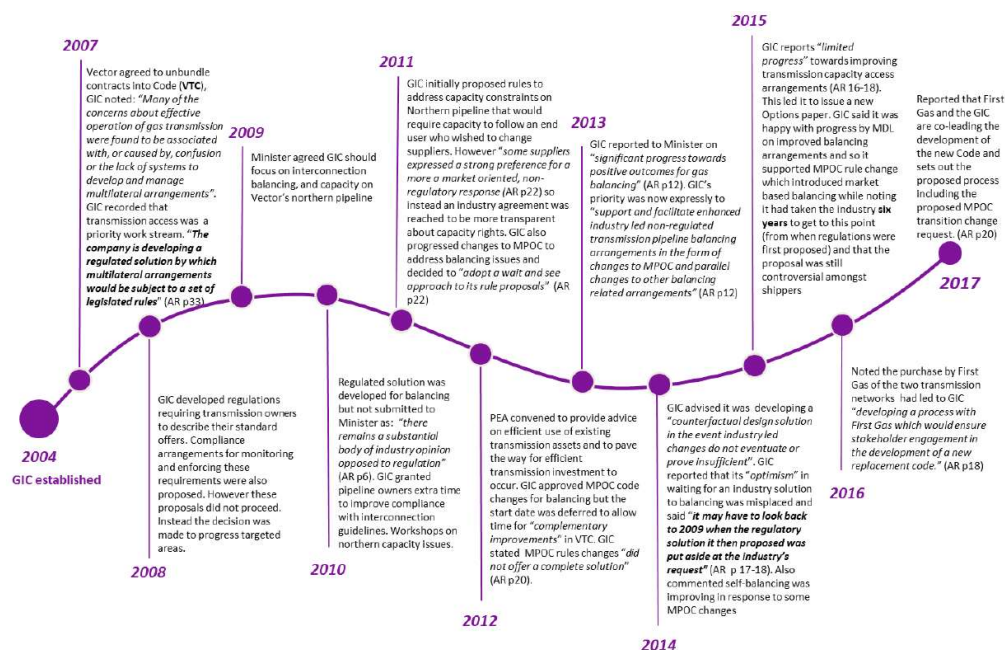
10 Governance:

- 10.1.1 Trustpower’s concerns about the governance structure of GTAC have been raised in previous submissions and correspondence. Our views have not changed.
- 10.1.2 We acknowledge that the GIC considers GTAC’s proposed liability arrangements, have a negative effect on efficiency, reliability, and fairness particularly in relation to the injection of non-specification gas and that this was a key factor in its preliminary assessment that GTAC is not materially better than the current access codes.
- 10.1.3 However our concerns with “governance” matters are deeper and broader than this.
- 10.1.4 We think that an application of the materially better criteria should have addressed the issues we have raised in previous submissions in relation to the:
 - a) benefits of a sound consultation process including through the use of advisory groups;
 - b) advantages of having a more targeted regulatory objective to guide the development of an access code over the “kitchen sink” Objectives and Outcomes;
 - c) need to adopt reasonable access terms having regard to the costs and benefits of alternatives rather than terms which are simply an improvement from legacy status quo arrangements which themselves evolved from closed access contracts in 2005;
 - d) advantages of a proper multilateral monitoring and compliance regime for what are at their core multilateral access obligations;
 - e) prohibitive costs of self-enforcement/dispute resolution by individual shippers for parties with smaller market shares;
 - f) value of having an access agreement approved by the Minister as a further “check and balance” on industry design processes [particularly in the light of the way the views of mass market retailers have been treated in the current process]; and the
 - g) risk of an industry agreement needing authorisation under the Commerce Act;
- 10.1.5 We therefore invite the GIC to reconsider its preliminary assessment in the light of these factors.

PART III: SUPPORT FOR GTAC AND “A FURTHER ROUND”

11 Support for GTAC

- 11.1.1 The process to date has required a significant resource commitment for an organisation whose involvement in the gas sector is limited to the retail supply of gas to around 30,000 mass market customers.
- 11.1.2 We have applied this effort in good faith but do not think we are any closer to having our issues addressed than we were at the beginning of the process.
- 11.1.3 This surprises us as we would have thought:
- the relatively low market share of mass market retailers in New Zealand lends itself to a “carve out” solution; and
 - the desirability of promoting competition and new entry were axiomatic to a modern regulatory world and a pre-condition for the continuation of self-regulation.
- 11.1.4 We do not support GTAC. This is because we not think it ensures retail gas market participants can access the transmission pipeline on reasonable terms.
- 11.1.5 We think all that has been achieved is another dot on the timeline we sent to the GIC in our open letter.



12 Response to First Gas supplementary questions

- 12.1.1 This section addresses the questions First Gas asked stakeholder in the GIC's workshop.

How far away from the materially better standard do you think we are?

- 12.1.2 As noted above we have not seen any significant progress towards resolving our issues and so we think we are still some distance from achieving a materially better standard offering fair and reasonable access terms to mass market retailers.

How long do you think it will take to re-engage and achieve materially better?

- 12.1.3 Given the level of disagreement we witnessed at the last workshop we think that it will take months rather than weeks to resolve outstanding issues.
- 12.1.4 We observe that submitters' views are likely to have become more entrenched by First Gas's apparent unwillingness to commit at the recent workshop to address the concerns raised by the GIC in its Preliminary Assessment paper. [What does that imply for future rule change processes?]

Do you have any preferences on how the process should be run from here on in

- 12.1.5 Yes. We think the Code should be handed over to the GIC for completion as regulated access terms.

13 Concluding remarks

- 13.1.1 The 2008 GPS includes a stated outcome that gas industry participants and new entrants can access transmission pipelines on reasonable terms and conditions.
- 13.1.2 How long do we have to wait?

For any questions relating to the material in this submission, please contact me on 07 572 9888.

Regards,



CRAIG SCHUBAUER

WHOLESALE MARKET MANAGER