Discussion Paper

Part One

Feedback on Wholesale Market Design

Part Two

Further Consultation

December 2006

The Gas Industry Co was formed to be the co-regulator under the Gas Act. As such, its role is to:

- recommend arrangements, including rules and regulations where appropriate, which improve:
  - the operation of gas markets;
  - access to key infrastructure; and
  - consumer outcomes;
- administer, oversee compliance with, and review such arrangements; and
- report regularly to the Minister of Energy on the performance and present state of the New Zealand gas industry, and the achievement of Government's policy objectives for the gas sector.

Authorship

This discussion paper has been prepared by Ian Dempster of Gas Industry Co, and David Hunt of Concept Consulting Limited.

Table of Contents

1 Executive Summary

1.1 This paper sets out the Gas Industry Co's views on wholesale market arrangements in light of stakeholder feedback received on the *Wholesale Market Design* paper released in September 2006. This paper also describes some of the key issues to be addressed in the next phase of work.

1.2 The *Wholesale Market Design* paper focussed on six main areas. These are set out below along with a summary of stakeholder feedback, and the position reached by Gas Industry Co in light of that feedback (see Sections 4, 5 and 6).

Regulatory Objective

1.3 The *Wholesale Market Design* paper recommended that the specific regulatory objective for this component of the wider wholesale work stream should be to facilitate transactional efficiency in gas trading. There was near universal support for this proposal, and Gas Industry Co will move forward on this basis.

Approach to Longer Term Trading

1.4 The *Wholesale Market Design* paper set out a range of possible approaches to longer term trading, and concluded that there was no case for introducing any formalised arrangements to improve transactional efficiency at this time.

1.5 Respondents generally supported this view, although a number of suggestions for further work in related areas were made. Gas Industry Co affirms its earlier view, and will consider the proposed areas for further related work in its forward planning.

Short-Term Trading Contract

1.6 The *Wholesale Market Design* paper recommended the development of a standardised short-term trading contract for use on a voluntary basis. It also appended a draft form of the proposed contract.

1.7 Respondents indicated general support for the development of a standard contract – however, there was extensive and varied comment on the proposed terms of the contract. While feedback varied by issue, a recurring theme was that it would be useful to distinguish between a 'standard' contract that might be used without a platform, and a commoditised contract for use solely with a platform. The latter could not be varied by parties, and would be likely to be used for trades of relatively short duration (days/weeks). Accordingly it could adopt simpler terms.

1.8 Gas Industry Co supports the approach of distinguishing between the two different requirements, and will pursue this in the next phase of work.

Platform for Trading a Short-Term Contract

1.9 The *Wholesale Market Design* paper set out two broad options for a platform to support trading of a standard contract. They were:

- **Matching Platform** - development of a relatively simple platform that facilitates the matching of buyers and sellers, but leaves participants to make the arrangements necessary to execute and support a trade (such as transmission nominations, billing etc); and
- **Trading Platform** - development of a more sophisticated platform that both facilitates matching of buyers and sellers, and automates the essential processes to execute and support a trade.

1.10 Because of its relatively simple functionality and self-contained nature, a matching platform was expected to be less expensive to develop than a trading platform. However, it was expected to have less potential benefit because of its reduced functionality. Indicative estimates of the costs and benefits were provided for each, and a recommendation was made to move forward with a matching platform.

1.11 Submitters generally supported this approach in principle, though a number emphasised the importance of managing the process to minimise the risk of unexpected cost escalation. Some also considered that the benefits of a simple platform might be understated relative to a more sophisticated platform.

1.12 Overall, Gas Industry Co considers that there is a reasonable case for progressing a simple platform to facilitate trading. It intends to adopt a staged approach to manage costs, and a final decision to proceed will be contingent on a satisfactory cost benefit assessment.

Prudential Issues

1.13 The *Wholesale Market Design* paper proposed that the management of prudential risk for platform trading be dealt with through a 'whitelist' approach – in essence each participant would decide the maximum exposure it could accept with each other party and this information would be logged into the platform. Only trades that meet both parties' prudential limits would be matched.

1.14 The majority of respondents supported a whitelist approach – although some parties registered concern to ensure that it did not become an undue barrier to trade.

1.15 Overall, the Gas Industry Co believes that the whitelist is workable, and will proceed on the basis that this is the preferred approach.

Further Analysis of Balancing Issues

1.16 Although the *Wholesale Market Design* paper recommended against developing a sophisticated trading platform at this time, it noted that such a platform could more easily allow trading very close to, or in, real time. The paper also noted that the potential incremental benefit of any real time trading functionality was closely linked to the difficulty or ease with which physical pipeline balancing will occur in future, especially post-2009 when legacy Maui gas is exhausted. For this reason, it recommended that work be undertaken to better understand the underlying physical issues involved in balancing in the future.

1.17 Gas Industry Co confirms that this issue will be pursued within a future work programme.

Overview of Platform Processes

1.18 While the main purpose of this paper is to respond to the stakeholder feedback on the Wholesale Market Design paper issued in September 2006, Gas Industry Co management also wish to use release of this paper as an opportunity to start the engagement process on the next phase of design work.

1.19 Accordingly, Section 8 of the paper describes the main building blocks for a platform at the process level, and seeks feedback on certain design issues. This information will provide an input to the development of the platform functional specification.

Next steps

1.20 On the contract front, the goal is to complete the work on the standard GSA and make it available for use by industry early in the New Year. In particular, the focus is on resolving the outstanding issues in relation to liability and force majeure.

1.21 Gas Industry Co will also seek amendment to section 41 of the Crown Minerals Act in respect of the requirement for Ministerial consent.

1.22 In relation to the platform, work will be carried forward in stages, with progress through each phase contingent on Gas Industry Co remaining satisfied that a platform can be developed at reasonable cost. The main stages are:

- prepare a functional specification for a platform, incorporating input from the Wholesale Markets Working Group and other stakeholder feedback;
- seek non-binding cost estimates from platform developers/operators based on the functional specification, in particular seeking information to enable any trade-offs to be made around functionality (e.g. service standards in relation to allowable downtime);
- if necessary, amend the functional specification in light of information on expected costs;
- obtain firm cost proposals from service providers and select a preferred provider; and
- undertake final cost benefit assessment, and decide whether to proceed.

1.23 In parallel with this work, Gas Industry Co will develop the detail of the implementation mechanisms, the form of the platform contract and the governance arrangements for a platform.

1.24 Assuming a final decision is taken to proceed with a platform, this would lead into the actual development process, acceptance testing and user training, with an expected go-live date in 2007/08.

Part One

Feedback on Wholesale Market Design

2 Introduction

Purpose

2.1 This paper is the third in a series issued by Gas Industry Co on core wholesale market arrangements. The two previous papers were:

- "Concept Design for Wholesale Gas Market" issued in March 2006; and
- "Wholesale Market Design" issued in September 2006.

2.2 Gas Industry Co received stakeholder feedback on the second paper in early November 2006.

2.3 The primary purpose of this paper is to set out the Gas Industry Co's view on proposed wholesale market arrangements in light of stakeholder feedback[1].

2.4 This paper also describes some of the key issues to be addressed in the next phase of the work, along with potential options. Stakeholder views are sought on these issues.

2.5 The paper concludes with a description of the work programme and planned timetable for moving forward.

Structure of this Paper

2.6 This paper is structured as follows:

Section		Key Points
1	Executive summary	• Sets out an overview of the paper and its conclusions.
2	Introduction	• Outlines the purpose of the paper and how it fits with the Gas Industry Co's overall work programme.
3	Objectives and assessment framework	• Sets out the wholesale gas market objectives that Gas Industry Co is seeking to meet.
4	Response to Stakeholder Feedback	• Summarises stakeholder feedback and sets out the Gas Industry Co's current views in light of feedback
5	Feedback on Standardised Gas Trading Contract(s)	• Considers feedback on specific issues in relation to standardised contract(s).
6	Feedback on Matching Platform	• Considers feedback on specific issues in relation to a matching platform.
7	Mechanism for Platform Funding	• Compares and contrasts user pays and levy-funding options.
8	Overview of Platform Processes	• Describes the key processes associated with a simple platform, and seeks stakeholder feedback on specific issues.

[1] This report back is a milestone in the 2007-09 Strategic Plan.

9	Next Steps	• Sets out the proposed path forward.

Submission Requirements

2.7 The bulk of this paper is focussed on setting out the views reached by Gas Industry Co in light of feedback on the September Discussion Paper.

2.8 The paper also includes a brief section outlining key issues for the next phase of work, and seeking views on specific questions. Parties who wish to respond to these questions or comment on other relevant issues are invited to respond by 5:00 pm on Friday, 16th February 2007. Please note that submissions received after this date may not be able to be considered.

2.9 The Gas Industry Co's preference is to receive submissions in electronic form (Microsoft Word format and pdf) with "Submission on Wholesale Market Design" in the subject header to submissions@gasindustry.co.nz. A hard copy would also be appreciated and should be posted to:

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2.10 The Gas Industry Co will acknowledge receipt of all submissions electronically. Please contact Ian Dempster if you do not receive electronic acknowledgement of your submission within two business days.

2.11 Submissions should be provided in the format shown in Appendix A. The Gas Industry Co values openness and transparency and therefore submissions will generally be made available to the public on the Gas Industry Co's website. Submitters should discuss any intended provision of confidential information with the Gas Industry Co prior to submitting the information.

3 Objectives and Assessment Framework

Gas Act, GPS and Strategic Plan objectives

3.1 The Gas Act sets out the objectives of the Gas Industry Co in recommending gas governance regulations for the wholesale market, as follows:

- *The principal objective is to ensure that gas is delivered to existing and new customers in a safe, efficient and reliable manner*;
- The other objectives are:
  - *The facilitation and promotion of the ongoing supply of gas to meet New Zealand's energy needs, by providing access to essential infrastructure and competitive market arrangements;*
  - *Barriers to competition in the gas industry are minimised;*
  - *Incentives for investment in gas processing facilities, transmission, and distribution are maintained or enhanced;*
  - *Delivered gas costs and prices are subject to sustained downward pressure;*
  - *Risks relating to security of supply, including transport arrangements, are properly and efficiently managed by all parties; and*
  - *Consistency with the Government's gas safety regime is maintained*.

3.2 The current Government Policy Statement (GPS)[2] repeats and expands these objectives, and then sets out the areas where the Minister of Energy is expecting recommendations on proposed arrangements from the Gas Industry Co. In the wholesale market context, it states these will include recommendations on:

- "*The development of protocols and standards applying to wholesale gas trading, including quality standards, balancing and reconciliation.*
- *The development of a secondary market for the trading of excess and shortfall quantities of gas*."

Gas Industry Co has considered these factors in its deliberations on the development of wholesale gas market arrangements. It has also used these factors as the basis for deriving the regulatory objective for this work stream. This is discussed in detail in the September Discussion Paper and is also covered in Section 4 of the current paper.

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[2] Government Policy Statement on Gas Governance, dated October 2004; see www.med.govt.nz

4 Response to Stakeholder Feedback

Conceptual Design - Discussion Paper I

4.1 In March 2006 Gas Industry Co released a paper titled *Concept Design for Wholesale Gas Market* for stakeholder comment. That document outlined five broad options for development of the wholesale gas market. The paper assessed the options against a set of qualitative criteria, and concluded that the platform bilateral option should be pursued for further development.

4.2 Stakeholder feedback was sought on the paper, which indicated that:

- qualified support existed among stakeholders for taking the preferred option forward to the next stage;
- a staged approach would be favoured, based on the development of building blocks which can be utilised in the existing informal market; and
- a robust cost benefit analysis should be undertaken before committing to proceed with a development.

4.3 In light of this feedback, Gas Industry Co embarked on a phased development of the platform bilateral option.

Wholesale Market Design - Discussion Paper II

4.4 More detailed work on the platform bilateral option was undertaken by the Gas Industry Co between May and August 2006, with significant input from the Wholesale Markets Working Group.

4.5 This work was presented to stakeholders in a Discussion Paper released in September 2006. Submissions were subsequently received from nine parties representing a broad cross-section of stakeholder interests.

4.6 While the paper covered a range of detailed issues and posed 30 specific questions, it focussed on six key areas:

- the proposed regulatory objective for the work stream;
- treatment of longer term trades;
- potential development of a standardised short-term contract;
- potential development of an IT platform for trading gas;
- treatment of prudential risk with such a platform; and
- analysis of how balancing issues might change through time.

4.7 The following sections describe the approach proposed for each major category of issue in the Discussion Paper, summarise stakeholder feedback, and set out the position that the Gas Industry Co has reached on each issue at this point.

Gas Industry Position on Proposed Regulatory Objective

4.8 The Discussion Paper recommended that the specific regulatory objective for this component of the wider wholesale work stream should be to facilitate transactional efficiency in gas trading. All but one submitter who commented on this issue supported the proposed objective, and that submitter considered that a better objective might be "the creation of a market structure where prices for gas reflect fair value that can be used as a reference for investment decisions".

4.9 Gas Industry Co acknowledges that correct investment signals are an important consideration, but also wishes to ensure that prices provide appropriate signals for consumption and production decisions.

4.10 On this basis, Gas Industry Co affirms its support for the regulatory objective of facilitating transactional efficiency in gas trading.

Gas Industry Co Position on Proposed Approach to Longer Term Trading

4.11 The Discussion Paper set out a range of possible approaches to longer term trading (greater than one year, although in practice the distinction relates more to the function of the contract rather than the duration), and concluded that there was no case for introducing any formalised arrangements to improve transactional efficiency at this time.

4.12 Respondents generally supported this view, although some specific comments were made. These include:

- the exercise of market power could be an issue that reduces efficiency in trading;
- Gas Industry Co could consider a bulletin board where parties describe their longer term requirements;
- there would be benefits in obtaining a higher level of transparency in respect of key terms, for example along lines of the EnergyHedge proposals in the electricity market; and
- long term contracts could cross-reference industry model contracts for technical and gas delivery terms.

4.13 The Discussion Paper noted that any market power issues were outside its scope. Instead, it sought to ensure that proposed arrangements did not enhance, and preferably constrained, any such power.

4.14 In relation to the bulletin board and increased disclosure comments, these appear worthy of consideration to increase transparency. However, it would appear likely that the transparency benefits from a short-term trading platform would be larger, given that longer term contracts are more likely to be highly tailored (e.g. treatment of reserves risk, escalation provisions etc), making disclosure of 'headline' terms less informative.

4.15 Given its finite resources, Gas Industry Co considers that it should continue to pursue the development of a platform designed to facilitate trading and consider other potential initiatives such as enhanced contract transparency once a short-term platform is operational. This is consistent with the specific outcome sought by the Government in the GPS: "*The development of a **secondary** market for the trading of excess and shortfall quantities of gas*" (emphasis added).

4.16 Lastly, the recommendation to allow importation of technical and other provisions from model short-term contracts into longer term contract forms appears sound. The Gas Industry Co intends to make its model contract terms widely available, and parties entering longer term contracts will be encouraged to use them as they see fit.

4.17 Overall, Gas Industry Co concludes that there is no case at this time for introducing formalised arrangements to improve transactional efficiency for longer term (i.e. greater than one year) trading of gas.

Response to Proposed Short-Term Trading Contract

4.18 The Discussion Paper recommended the development of a standardised short-term trading contract for use on a voluntary basis. It also appended a draft form of the proposed contract.

4.19 Respondents indicated general support for the development of a standard contract – however, there was extensive and varied comment on the proposed terms of the contract. While feedback varied by issue, a recurring theme was that it would be useful to distinguish between a 'standard' contract that might be used without a platform, and a commoditised contract for use solely with a platform. The latter could not be varied by parties, and would be likely to be used for trades of relatively short duration (days/weeks). Accordingly it could adopt simpler terms.

4.20 Gas Industry Co supports this approach of distinguishing between the two different requirements, and will pursue this in the next phase of work.

4.21 In relation to the matters of contract detail raised in submissions, these are explored further in 'Section 5 – Feedback on Standardised Gas Trading Contract(s)'.

Response to Proposed Platform for Trading a Short-Term Contract

4.22 The Discussion Paper set out two broad options for a platform to support trading of a standard contract. They were:

- **Matching Platform** - development of a relatively simple platform that facilitates the matching of buyers and sellers, but leaves participants to make the arrangements necessary to execute and support a trade (such as transmission nominations, billing etc); and
- **Trading Platform** - development of a more sophisticated platform that both facilitates matching of buyers and sellers, and automates the essential processes to execute and support a trade.

4.23 Because of its relatively simple functionality and self-contained nature, a matching platform would be less expensive to develop than a trading platform. However, it would also have less potential benefit because of its reduced functionality.

4.24 The Discussion Paper set out indicative estimates of the costs and benefits for each and, based on those estimates, recommended that it would be worthwhile proceeding with a matching platform and that work on a more sophisticated platform should not proceed at this time.

4.25 Submitters generally supported this approach in principle, though a number emphasised the importance of managing the process to minimise the risk of unexpected cost escalation.

4.26 Overall, Gas Industry Co considers that there is a reasonable case for progressing a simple platform to facilitate trading. It intends to adopt a staged approach to manage costs, and the key issues associated with a platform are explored further in Sections 6, 7 and 8.

Response to Proposed Approach for Managing Prudential Issues

4.27 The Discussion Paper proposed that the management of prudential risk for platform trading be dealt with through a 'whitelist' approach – in essence each participant would decide the maximum exposure it could accept with each other party and this information would be logged into the platform. Only trades that meet both parties' prudential limits would be matched.

4.28 The majority of respondents supported a whitelist approach – although some parties registered concern to ensure that it did not become a competitive barrier.

4.29 Overall, the Gas Industry Co believes that the whitelist is workable, and will proceed on the basis that this is the preferred approach.

Response to Proposed Analysis of Balancing Issues

4.30 Although the Discussion Paper recommended against developing a sophisticated trading platform at this time, it noted that such a platform could more easily allow trading very close to or in real time[3]. The Discussion Paper also noted that the potential incremental benefit of any real time trading functionality was closely linked to the difficulty or ease with which physical pipeline balancing will occur in future, especially in the post 2009 era when legacy Maui gas is exhausted. For this reason, the Paper recommended that work be undertaken to better understand the underlying physical issues involved in balancing in the future.

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[3] In this context, balancing refers to taking physical actions to maintain appropriate pressures in the transmission pipeline system. Some submitters rightly noted a matching platform could be used to trade mismatch ex post between parties (where one is high, and another low). However, those trades don't affect real time balancing.

4.31 While some submitters may have misinterpreted the question (with hindsight, it could have been better framed), there appeared to be support for further analysis of balancing issues, provided this did not extend into development of a platform.

4.32 Gas Industry Co regards this issue as an important matter, and is examining issues in respect of balancing as part of the transmission access work stream.

Additional Issues Raised by Submitters

4.33 In the course of responding to the Discussion Paper, submitters also raised matters which were not formally part of the consultation process. Two issues in particular were commented on by multiple submitters:

- transmission capacity – when parties trade physical gas, they also need to be able to arrange for transmission service to ship the gas to a useful location. This is relatively straightforward on the Maui system because users can procure transmission services on a 'spot' basis. In contrast, some submitters considered that Vector's current transmission arrangements act as an impediment in some circumstances; and
- exclusive supply arrangements – it was stated that some industrial Gas Supply Agreements (GSAs) have exclusivity clauses prohibiting the customer from purchasing gas from other suppliers – this was viewed as reducing the potential to trade gas.

4.34 Gas Industry Co has discussed the transmission capacity issue in the *Gas Transmission Access Issues Review Discussion Paper*[4]. In essence, some parties believe the lack of a spot transmission product seriously inhibits trading on the Vector network. Conversely, others believe that the current ability to either relocate pre-booked capacity or trade capacity with another shipper generally provides the ability to obtain short-term capacity on the Vector system. While this is an important issue, resolution will ultimately be determined within the transmission work stream.

4.35 In relation to exclusivity clauses in GSAs, it is not possible to discern whether they reflect an asymmetry in bargaining power between gas sellers and buyers, or a reasonable trade-off freely accepted *at the time* by the parties, but *subsequently* regretted by one party. The former would raise potential policy concerns, whereas the latter would not. The term and prevalence of such clauses is also difficult to discern[5]. Furthermore, even if such clauses were to prove a significant barrier to trading, it is not clear whether Gas Industry Co has any authority or powers to override or alter the terms of GSAs.

4.36 In light of these factors, Gas Industry Co has concluded that it will seek further information on this issue, but that this should not delay the effort to progress wholesale market development.

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4 For more information refer pages 25-28 of the document, which is available from www.gasindustry.co.nz in the consultation section.

5 Anecdotal evidence suggests that such clauses affect a number of industrial customers – but it also appears that industrial customers may not be likely traders in the short-term because their needs don't justify the costs of allocating the internal resources for trading.

5 Feedback on Standardised Gas Trading Contract(s)

Standard GSA and Platform Contract

5.1 As indicated in Section 4, stakeholders generally supported the development of a standardised form of contracting, but wished to see a clear distinction between a standard contract ('standard GSA') for use without a platform, and a commoditised contract ('platform contract') for use solely with a platform. Gas Industry Co will adopt this suggestion going forward.

5.2 In most areas, the two forms of agreement are expected to be the same or very similar. The key difference is that the platform contract will need to further standardise most of the remaining variables in a standard GSA (e.g. form of dispute resolution). This may leave price, time period and volume as the only variables to be specified by the parties in a platform contract.

Specific Contract Terms

5.3 The Discussion Paper included a proposed draft form for the standard contract, and submitters made a number of detailed comments on the draft. These comments are explored in the table below. Note that in some cases the issues raised by submitters will be addressed by distinguishing between platform and non-platform contracts.

Table 1: Summary of Comments on Draft Contract[6]

Discussion Paper proposal	Stakeholder response	Gas Industry Co view in light of feedback
Fixed daily quantity or maximum daily quantity.	Contract should provide for both approaches.	• Standard GSA to allow for both approaches by requiring parties to specify maximum and minimum daily takes. • Platform contract to provide for fixed quantity (max=min).
Contract should not include provision for automatic price adjustments for taxes and government charges.	Mixed views.	• Standard GSA will be silent on issue – form of price to be specified in schedule by parties. • Platform contract will provide for a fixed price.
Amendment should be sought to s.41 of Crown Minerals Act to remove need for Minister's consent.	Supported.	Under action.
Contract should exclude any conditions precedent.	Generally supported.	Endorsed.

6 This table does not seek to cover every issue raised, but focuses instead on the broad thrust of comments. Readers seeking more detail are referred to Appendix B.

Discussion Paper proposal	Stakeholder response	Gas Industry Co view in light of feedback
Contract should not make seller liable for gas specification as that is handled under agreements between pipelines and injecting parties.	Generally supported.	Endorsed.
Contract should not provide for priority rights.	Supported.	Endorsed[7].
Contract should set out broad obligations on buyer/seller to ensure valid transport rights.	Generally seen as straightforward on Maui – not clear-cut for Vector system.	Given the desire to minimise cost & complexity and the central role of the Maui system, a relatively simple approach can be adopted by focussing on MPOC – this can be expanded later to include the Vector system as required.
Liability provisions should exclude indirect losses and direct losses should be capped at gas mismatch/imbalance price.	General support for exclusion of indirect losses – concern about detail of cap.	See detailed discussion below.
Force majeure provisions should be based on principle that FM can only be invoked when balancing is suspended.	Not generally supported – preference for a wider FM provision.	See detailed discussion below.
Contractual disputes that can't be resolved bilaterally should be referred to Rulings Panel.	Mixed views – some parties endorse Rulings Panel – others prefer court system. In any case, if Rulings Panel is created, it is still some away.	• Standard contract – given that Panel could not be operational for some months, allow parties to specify Courts or alternative procedure by agreement. • Platform contract – to be resolved.
Contract should have standard right of assignment.	Supported.	Endorsed.
Contract should be available for use once Discussion Paper feedback has been considered.	Supported.	Endorsed.

Default Risk

5.4 As is evident above, divergent views were expressed in relation to treatment of default risk in the context of liability and force majeure provisions. The Discussion Paper only considered these issues at a high level, and it was apparent that submitters wished to drill down on the issues.

5.5 To assist in that process, it is useful to consider the objectives of these provisions. In principle, such provisions should be designed to achieve:

- **clarity** - enabling parties to understand the risks they face – and hence providing the base information to manage those risks;

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7 While no priority is proposed in respect of gas *supply*, there might be value in allowing parties to distinguish different levels of *transmission* priority where relevant. In particular, the platform contract might allow parties to distinguish between 'firm' transmission under MPOC AQ provisions, and non-firm arrangements. This will be explored further in the next phase of development.

- **flexibility** - to deal with all possible eventualities, some of which will not be foreseeable; and
- **alignment** – avoiding perverse incentives, which increase the risk of default with local and possible systemic consequences. For example, the contract should not make it less costly for a party to default than to perform its obligations.

5.6 With these objectives in mind, it is useful to 'unpack' the key risks that can arise in a trading context once an agreement has been entered into. These risks are shown in Table 2 below, along with a proposed mechanism for addressing each issue.

5.7 As will be evident in the table, the basic proposition is that where a party's own action causes a default, it should *at least* keep the other party whole in value terms. In contrast, where default arises due to external reasons (e.g. the operator has scaled back approved nominations for reasons outside the parties' control), neither party should be liable to the other.

5.8 Where an obligation arises to keep the other party whole, it is proposed that this make use of the buy/sell prices for balancing gas. This is based on the premise that as a last resort, the innocent party can put gas into, or take gas out of, the balancing pool when the other party has failed to perform its obligations.

5.9 Arguably, the use of balancing prices could over-compensate the innocent party at times, relative to its actual loss. For example, this would occur where a seller failed to supply, and the buyer arranged an alternative source of gas that was cheaper than balancing gas.

5.10 While a more accurate measurement of loss might be desirable, some trade-off is required. Provided the potential for over-compensation does not create a perverse incentive (e.g. avoiding trading at all, which appears unlikely), there is a reasonable case for adopting balancing prices due to their clarity. Parties will have better knowledge of these prices than the value for actual loss, and this clarity should help to provide strong incentives to manage risk.

5.11 Furthermore, there appears to be little likelihood that balancing prices will under-compensate[8], and this would be the more serious concern. Any significant under-compensation could create perverse incentives because parties could gain by defaulting on their obligations.

[8] Except where a system wide issue arises, and balancing prices cease to be meaningful. However, that situation raises broader issues, considered under the Force Majeure section.

Table 2: Key contractual performance risks

Nature of failure	Consequence	Quantum of damage	Proposed approach
Buyer fails to nominate sufficient gas take	Seller can't inject (except into balancing pool)	Gas price less proceeds from alternative disposal of gas	Buyer pays seller (gas price – balancing price) x shortfall quantity *Rationale – proceeds from alternative disposal will be difficult to estimate – balancing price is visible and to some extent provides a floor value.* *Arguably this approach may overcompensate seller at times, but should not create perverse incentives, because the buyer can limit risk by performing its obligations*
Seller fails to nominate sufficient gas injection	Buyer can't lift (except from balancing pool)	Lower of: cost of alternative gas; or value of lost opportunity	Seller pays buyer balancing price x shortfall quantity *Rationale – difficult to quantify value of lost opportunity. More straightforward to enable buyer to use balancing gas price without penalty – balancing price is visible and to some extent provides a ceiling value.* *Arguably this approach may overcompensate buyer at times, but should not create perverse incentives, because the seller can limit risk by performing its obligations*
Buyer & seller nominations reduced due to system issue	Buyer & seller both scaled back	Seller - gas price on lost volume less proceeds on alternative disposal Buyer – lower of cost of alternative gas (if available) or value of lost opportunity	Parties pay and receive contract price for actual quantity of gas shipped *Rationale - Unlike previous cases, this situation arises due to external influences rather than non-performance by one of these parties.*

Buyer fails to lift gas (seller still injects)	Seller provides balancing service with gas, or is curtailed	Gas price on lost volume less proceeds on alternative disposal	Buyer pays seller (gas price – balancing price) x shortfall quantity *Rationale – proceeds from alternative disposal will be difficult to estimate – balancing price is visible and to some extent provides a floor value.* *Arguably this approach may overcompensate seller at times, but should not create perverse incentives, because the buyer can limit risk by performing its obligations*
Seller fails to inject gas (buyer still takes)	Buyer uses balancing service gas or is curtailed	Lower of cost of alternative gas (if available) or value of lost opportunity	Seller pays buyer balancing price x shortfall quantity *Rationale – difficult to quantify value of lost opportunity. More straightforward to enable buyer to use balancing gas price without penalty – balancing price is visible and to some extent provides a ceiling value.* *Arguably this approach may overcompensate buyer at times, but should not create perverse incentives, because the seller can limit risk by performing its obligations*
Buyer fails to pay	Seller out of pocket	Price set in contract	Buyer pays buyer the contract price x contract quantity

5.12 For these reasons, the Gas Industry Co's current thinking is that the contract should include liability provisions based around balancing prices where default is caused by one of the parties. The contract would exclude provision to recover consequential losses, except to the extent that there was wilful default.

5.13 Whilst the use of balancing price does seem to set the appropriate benchmark, it would not be appropriate to use the pipeline as the gas source or sink of last resort. The balancing service exists, primarily, to promote efficient use of the transmission service. It would not be efficient to put the pipeline operator in the position of effectively underwriting the physical aspects of trading in the wholesale market. Instead, trading systems need to be designed to ensure that traders of gas have the correct incentives to fulfil their contractual obligations.

5.14 This approach will need to be tested in detail, particularly in relation to mapping the interaction between a standard contract and (say) MPOC to ensure that incentives are appropriately aligned.

Force Majeure

5.15 The other issue that is closely related to liability provisions is the extent to which parties should be relieved of their obligations due to force majeure situations.

5.16 The proposal in the September Discussion Paper was to adopt a tightly constrained definition of force majeure, limiting it to situations where an industry contingency plan had been invoked. The logic for this position was that force majeure should only be invoked when balancing service is not available (and hence the parties no longer have the ability to address any mismatch between plans and actions via the balancing pool).

5.17 There was dissent from many submitters, with a majority favouring a broader definition. In particular, parties were concerned that contracts could extend out 12 months and provide little prospect of relief. The adoption of a broader definition appears workable for a standard contract for use without a platform, and Gas Industry Co will redraft the contract along those lines.

5.18 In respect of a platform contract, there may be benefits in adopting a narrower force majeure provision. The durations of trades on a platform are likely to be significantly shorter than direct bilateral deals, making exposure less onerous. Furthermore, to the extent that a broader force majeure provision is adopted, it may need to include a cascade provision that allows parties to declare relief if a counterparty on whom they are relying has been relieved by force majeure. This would create a chain of default and in the context of a platform-based market it could become difficult to track and trace the contracts affected by one event.

5.19 A broad force majeure provision may also undermine one of the benefits of a platform, which is to provide more dynamic price signalling in periods of tight/over supply. If parties have limited ability to declare force majeure, they will need to rely more on price based mechanisms to clear their position, either by re-entering the market to buy or sell gas, or through the balancing mechanism. Conversely, a

broader provision is more likely to create uncertainty, making it less likely that exposure will be managed through trading.

5.20 Gas Industry Co is still considering the best treatment of force majeure for a platform contract and will be refining its view in the next phase of work.

6 Feedback on Matching Platform

Management of Costs

6.1 As indicated in Section 4, stakeholders generally supported the proposal to develop a simple platform that would be available for use on a voluntary basis. The key qualification was a concern to minimise the risk of unexpected cost escalation.

6.2 Gas Industry Co is also very mindful of this risk, and will rigorously apply the following principles:

- **keep it simple** - ensure that the platform functionality remains simple, and resist pressure to import complexity from other arrangements into the trading platform as far as possible. Where participants desire, they can adapt their own systems to address complexity, or use manual processes;
- **adopt conventional approaches** – wherever possible, the arrangements should adopt orthodox approaches to issues. This enhances contestability by allowing existing solutions to be utilised without heavy tailoring;
- **lock in costs** - seek firm costs from platform providers – both in terms of development and ongoing costs; and
- **preserve do nothing option** – a platform development will not proceed unless expected benefits exceed expected costs. If necessary, the design will be re-scoped or even not proceed if costs turn out to be larger than benefits.

Implementation Mechanism

6.3 As noted in the September Discussion Paper, users of the platform would need to be bound by a common set of 'rules'. These would cover matters such as any admission and ongoing usage criteria, determination of the form of the standard trading contract, dispute resolution etc.

6.4 Such rules could be put in place by an industry arrangement (e.g. participation agreement with Gas Industry Co) or by rules/regulations under the Gas Act. The September Discussion paper noted that the choice of preferred mechanism should be made once detailed design issues are settled, enabling a robust assessment of the alternatives (e.g. the potential cost of obtaining a Commerce Act authorisation or clearance).

6.5 Submitters did not offer any specific views on this issue, and it remains Gas Industry Co's view that the choice of preferred implementation mechanism should be made once the other design details are settled.

Compliance & Enforcement Mechanism

6.6 The September Discussion Paper noted that the platform would require a compliance and enforcement regime to ensure users abide by the platform rules. Rather than create a bespoke arrangement, the Paper proposed that oversight of platform rules

be handled within the broader compliance framework being developed by Gas Industry Co.

6.7 The majority of submitters supported this approach, subject to seeing the detail of the proposed arrangements. This information will be made available in the forthcoming final *Statement of Proposal* which is due to be published in 2007.

Part Two

Further Consultation

7 Mechanism for Platform Funding

7.1 While the September Discussion Paper did not raise funding mechanisms as an issue, a number of submitters sought Gas Industry Co's views on this matter.

7.2 In respect of who should pay, the broad options are:

- a full 'user pays' arrangement with both initial platform set-up costs and annual operating costs charged to users;
- levy funding to cover both initial platform set-up costs and ongoing operational costs; and
- levy funding for initial platform set-up costs with ongoing operational costs met from usage fees.

Option 1 – User Pays

7.3 The user pays option is characterised by the fact that all costs involved in creating and operating a platform will be charged to the traders who use that platform.

7.4 In principle, a 'user pays' approach is to be preferred because it tends to allocate costs to the parties who cause the cost to be incurred and who benefit from an action. These parties can then make choices in light of the costs and benefits *that accrue to them*.

7.5 There are also options about the structure of any user-based fee payments. These could be fixed per participant, or vary with the number of trades, the volume of gas traded or some other variable.

7.6 The structure of the platform charges is important as there is a connection between the charging structure and the incentives which parties have to minimise costs. There is also a tension between the efficient recovery of costs from users and the objective of having a market that is seen to be inclusive. A wholesale market that exhibited high entry fees and/or high transaction fees relative to the volume of gas traded by a user might be seen as effectively excluding certain classes of participant. Conversely, a charging structure that heavily cross-subsidised certain classes of users might be seen as inefficient.

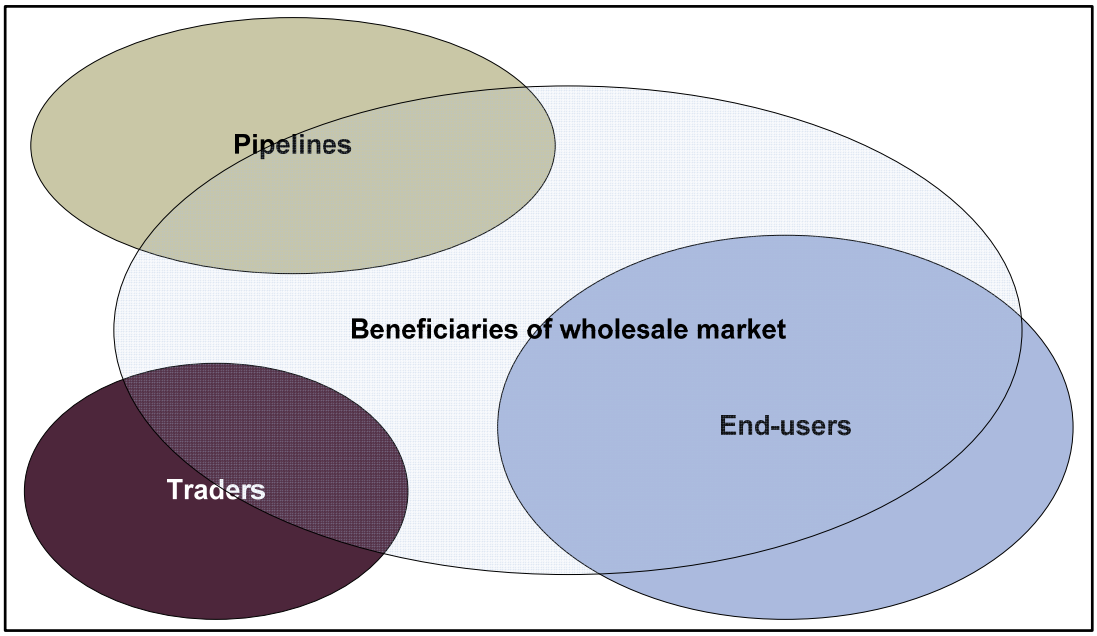
7.7 Gas Industry Co is of the view that, subject to addressing the above issues, a user pays approach to funding the development and operation of the wholesale market is preferable.

Option 2 – Levy Funding

7.8 While 'user pays' is sound in principle, there may be a number of practical difficulties in this instance. Firstly, the direct 'user' group does not represent the full universe of beneficiaries. As shown in the Chart below, the benefits from increased price

transparency are diffuse and can be obtained by parties without trading on the platform, and therefore without paying a fee[9].

Chart 1: Beneficiaries of Wholesale Gas Market



7.9 Increased price transparency and ease of trade may even be detrimental for some platform users. For example, traders who currently enjoy a relative information advantage may experience greater pressure on margins, and pipelines may have lower firm capacity bookings.

7.10 Accordingly, there is a risk that funding the development cost from only the traders who voluntarily use the platform might not prove to be a workable option. Some parties may choose to "free ride" by standing back from funding initial platform development in the hope that they can enter the market at a later without incurring the set-up costs. If sufficient parties chose that route it may even compromise establishment of the market.

7.11 Second, fees based on trading activity will not necessarily be efficient as there is no direct linkage between the volume of platform usage and the resource cost incurred (or the level of benefit obtained). Indeed, most operating costs are unlikely to vary with usage. Examples where this doesn't apply would be compliance and enforcement actions, where decisions by individual users can result in substantial resource costs being incurred.

7.12 As a result, charging platform users for general operating costs based on trading activity (whether per trade or by volume traded) is likely to be inefficient. It will risk under use of the market as parties who would otherwise trade are put off by the cost.

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9 In principle, these parties could be charged a different fee for simply viewing information from the platform. However, this is unlikely to be practical due to the number of parties involved, the difficulty of preventing further re-transmittal of that information. It is also unlikely to meet the objectives in the GPS.

7.13 In light of these factors, there is arguably a case for funding the platform development cost from the general industry levy, as there is a heavy overlap between levy payers and platform beneficiaries.

7.14 Similar arguments can be made in respect of general operating costs, at least in the early phase while transactional volumes are relatively low.

7.15 As an indication of the effect on the industry levy, if a platform cost of $150k was recovered in one year, this would imply an increase in the overall levy of approximately 4%.

7.16 This suggests an approach along the following lines:

- development cost and initial fixed operating costs would be met through the industry levy;
- operating costs that vary according to participant action should be charged to users (e.g. compliance actions, admission costs); and
- the recovery of ongoing costs should be reviewed once the platform has been operating for a period to assess whether there will be efficiency benefits from moving to a more transactionally based charging regime.

Q1: Do you agree that user pays is the preferred option for funding the establishment and ongoing operation of a wholesale market for gas? If not, what funding mechanism do you consider most appropriate and why?

8 Overview of Platform Processes

8.1 The previous section set out Gas Industry Co's views in light of feedback on the principal 'architectural' elements a platform based trading arrangement.

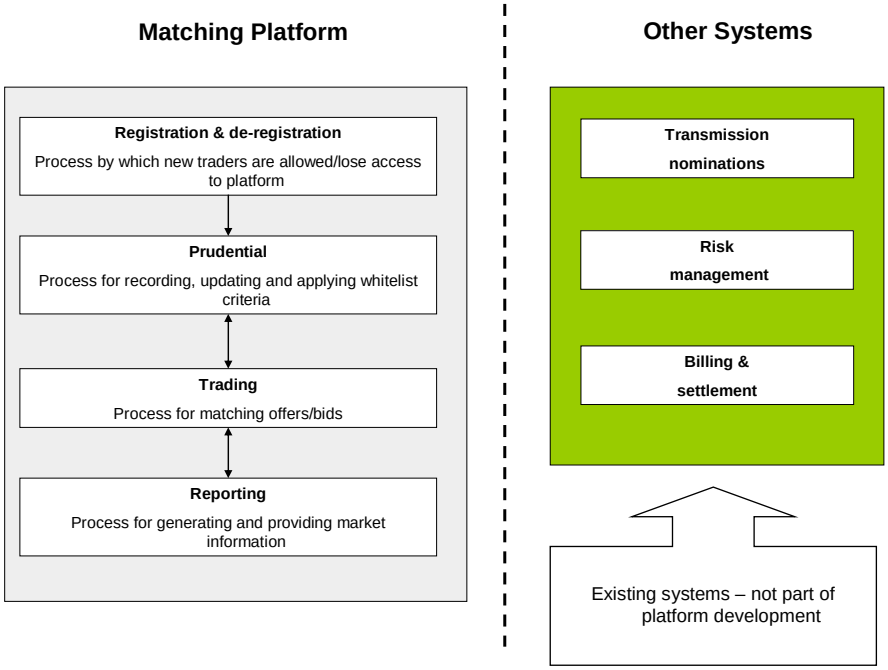
8.2 This Section builds on that foundation, and starts to flesh out some of the detail at a process level. It identifies key areas of choice and seeks stakeholder feedback. This will be used as input to development of a functional specification.

Key Processes

8.3 The key processes associated with a platform are illustrated in Chart 2 below.

8.4 The chart also shows the processes that will occur outside the platform. These processes are expected to operate on the same basis as they do at present for paper-based trading.

Chart 2 – Key Processes for Simple Trading Platform



Registration Process

8.5 This process covers three main activities:

- **Admission** - allowing an organisation to use the platform – and hence accept offers from, and make offers to, the other parties using the platform;
- **Suspension** – suspending the rights of an existing organisation to use the platform; and
- **User controls** - controlling the usage rights by individuals within an organisation.

8.6 The following paragraphs set out features in these areas that are fairly conventional, and which would not be expected to impose significant cost.

8.7 An admission process for a market would typically require organisations seeking user rights to satisfy certain initial criteria to prove their bona fides, especially in relation to credit risk. In effect, admission criteria form the first layer of prudential requirements.

8.8 However, in the current proposed 'whitelist' model where participants will make their own assessments of all other parties' standings, there would not appear to be a need for stringent admission criteria. Instead, admission can be largely self-policing as contracts can only be formed if both parties make a positive decision to accept default risk with each other. The main requirement would be for new parties to provide some information to allow other to assess them.

8.9 There does not appear to be a need to proscribe the form of this information, as a joining party should have incentives to provide sufficient relevant information to make itself attractive as a potential counterparty (e.g. directors' identities, recent financial statements).

8.10 Accordingly, the admission process could be very simple, based around the collection of information on an organisations' legal identity (for contract purposes), verification by a proper authority that the organisation wishes to join the arrangement (e.g. a directors certificate), and the provision of supporting information on the organisation's standing. The cost of administering these steps should be relatively modest, and because they are attributable to a specific party, could be charged to that user.

Q2: Do you support the proposed approach to admission? If not, what alternative would you want and why?

8.11 The revocation process can also be very simple. Because participants themselves will make ongoing assessments of their willingness to trade with each other party, the arrangement can be self-policing to a large extent. So for example, were one party to engage in and acquire a reputation for poor behaviour, it is likely to find an increasingly small pool of counterparties with which to trade. This approach also allows flexibility to deal with differing risk appetites by different parties.

8.12 The principle area where self-policing will not work is where a party offends against a basic platform rule. While the scope of such rules is expected to be limited, there might for example be instances where a party had not paid fees or fines. In such instances the operator should have the ability to suspend that organisation's usage rights.

Q3: Do you support the proposed approach to suspension? If not, what alternative would you want and why?

8.13 The last activity is the process to control user rights within a trading organisation. This is required to ensure the integrity of electronic instructions being issued to the

platform, because once an instruction is issued, it can form a contract that is binding on the trading organisation represented by the user.

8.14 The key desirable features would appear to be:

- designating administrator(s) for each organisation with the power to create/revoke/amend user rights within the organisation and set prudential limits for other trading organisations;
- provision for limits to be placed on an individual trader's authority (by value and/or quantity), which can only be adjusted by the organisation's administrator; and
- provision for reporting of all offers/bids/trades to traders, the administrator(s) and other selected individuals within an organisation.

Q4: Do you support the proposed approach to user controls? If not, what alternative would you want and why?

Prudential Process

8.15 A party buying or selling gas is exposed to the risk of non-performance by the contract counterparty. In the current 'paper-based' market arrangements, this risk is managed by traders making selections among the potential counterparties and by the bespoke nature of contract terms.

8.16 Under a platform market, the contracts have to be standardised, and revealing the identity of the bidders and offerors has drawbacks. In particular, it would reduce the ability of participants to mask their trading position, and hence increase the scope for opportunistic behaviour. It would also make it easier for traders to act in a collusive manner or exclude new entrants[10]. For these reasons, a blind market has been envisaged, provided it does not add undue cost.

8.17 To address prudential risk, a 'whitelist' is proposed where parties will nominate the maximum exposure they are prepared to accept with other parties. The system would be loaded with parties' criteria and only allow deals to form which meet both parties' requirements.

8.18 The main areas of design choice cover: the extent to which non-conforming bids/offers are displayed; the form of prudential criteria; the ability of participants to modify their prudential preferences through time; and a participant's ability to over-ride preferences logged into the system.

8.19 In respect of display options, the system could present participants with all the bids and offers that are currently live, or simply those that are capable of being matched

[10] There may also be some other flow-on consequences. For example, Gas Industry Co is seeking amendment to s.41 of the Crown Minerals Act to remove the need for Ministerial consent to certain gas trades. The prime reason for the consent requirement is to protect the royalty base by ensuring that gas contract pricing reflects arms-length terms. Gas Industry Co has argued that a platform will achieve this outcome without the need for Ministerial consent, but this argument could undermined if the market did not operate in a blind manner.

given the respective parties' selected criteria at that time. There would appear to be merit in the former approach, as the price/volume information is likely to be of value to participants even if a deal can't be accepted. Furthermore, display of such information would not appear to have any detriments.

8.20 The provision of this information may also facilitate the participation[11] by organisations which can manage credit risk efficiently, and therefore bridge the difference between parties who might otherwise be unable to transact directly with each other.

Q5:	*Do you support the proposed approach to display of bids/offers? If not, what alternative would you want and why?*

8.21 Prudential criteria could be expressed in monetary and/or gas volume terms, and in gross or net terms (i.e. purchases and sales between the parties that offset each other could be excluded for calculating available limits).

8.22 The use of net limits would create more 'headroom' for trading, but parties may be concerned about gross exposures (since netting may be of little practical value as most deals are likely to cover different time periods).

8.23 In respect of sales, a financial limit probably makes the most sense because the risk is essentially credit exposure. In respect of purchases, limits could also be expressed in financial terms, but parties may also be concerned about the volumetric exposure. Stakeholder feedback on this issue would be useful.

8.24 To be meaningful, the criteria should be applied in a way to take account of deals that have occurred between the parties – so that the 'headroom' of available exposure is amended as deals are formed, and as they roll off. This appears straightforward for new deals, but tracking of deals as they roll off would be more difficult, particularly if the platform seeks to track actual performance. However, if deals are simply deemed to have rolled-off at their value date, this should be fairly straightforward as the dates, volumes and prices will be in the system.

8.25 This suggests that criteria should be expressed in gross terms, with sales exposures based on a maximum dollar value, while those for purchases would allow for financial and volume limits. Limits should also be updated to take account of deals struck, and deals that roll-off (based on a deeming provision).

Q6:	*Do you support the proposed form of prudential criteria? If not, what alternative would you want and why?*

8.26 Trading organisations are likely to want the ability to amend prudential criteria through time to take account of new information about counterparty capability or performance. While this is desirable, there would also need to be some constraint on changing the

[11] This is just one issue affecting participation by such parties. A number of other factors will be relevant including admission criteria, transport provisions and liability rules.

criteria, otherwise participants could use this flexibility to unmask the identity of parties to offers/bids. This suggests that provision should be made for periodic adjustment to prudential criteria.

8.27 However, if a previously acceptable organisation were to suffer a significant adverse event, and counterparties were not able to adjust their criteria (and hence potential exposure) until the next periodic reset, this could act as a significant disincentive to making any bids or offers. This would be an undesirable outcome, and it seems reasonable for parties to have the ability to close out any potential additional exposure to such a party at any time.

8.28 This suggests that prudential criteria should stay fixed once they are set, with adjustments allowed only during periodic windows (perhaps bi-annually or annually). The other exception would be a right to set any further exposure to zero. However, once this right had been exercised, it could not be revoked until the next reset period.

Q7: Do you support the proposed approach to adjusting prudential criteria? If not, what alternative would you want and why?

8.29 A related issue is whether users should be allowed to override their own prudential criteria if that will allow them to accept a deal. Note that the distinction between over-riding and amending criteria is important, because the latter could be used to reveal the identity of bidders/offerors without forming a contract. It could therefore be used to discriminate among traders.

8.30 An override cannot be used to discriminate because it will simply form a contract despite the participant's pre-selected criteria. This provision could be useful if a party's desire to transact was so great that it over-rode the prudential risk inherent in its whitelist preferences. Of course, an override will have no effect if the other party's preferences precluded a deal.

Q8: Do you support the proposed provision of an override? If not, what alternative would you want and why?

8.31 While it is too early to assess the cost of providing whitelist functionality, it would nonetheless be useful at this point to obtain participants' views on the perceived merits of blind trading.

Q9: Is your use of a platform likely to be significantly affected by whether the market operated on a blind basis or not? If so, in what way?

Trading Process

8.32 The high level design choices cover: the scope of what is being 'automated', whether both buy and sell offers are permitted, the size and duration of standard contracts, and the location for trading.

8.33 One of the most important issues is the scope of 'automation'. At present, parties form contracts via phone, email and face to face contact, and record these in written agreements. The fulfilment of the bargain is effected via the transmission and nomination system.

8.34 A platform will allow a degree of automation to the process of forming a contract, but will not affect the fulfilment phase.

8.35 Put another way, once the contract is formed electronically, the trade will be handled through the same systems that currently address paper-based deals. This distinction is necessary because parties cannot sell identifiable blocks of gas (due to the 'pool' nature of the transmission system).

8.36 Instead, when parties enter into a bilateral trade across the transmission system (i.e. with or without a platform), they are not promising to provide and take a specific block of gas, but instead are *promising to make nominations* consistent with that trade, and then *act consistently with the nominations* on the gas delivery day.

8.37 Whether those nominations ultimately result in the planned gas injections and withdrawals is dependent on a whole series of actions by multiple parties (including the buyer and seller) on the transmission system.

8.38 A trading platform cannot overcome the potential for differences to arise between promises and outcomes. Instead, the focus should be on ensuring parties are clear about what rights and obligations are attached to trades, and what happens when differences arise between plans and outcomes. To a large extent this is determined by the form of the standard contract rather than the platform itself.

8.39 Applying this thinking in the present situation, traders would be undertaking to make MPOC nominations consistent with the deals they have struck, and then act consistent with nominations on the day. The contract would also set out the rights/obligations when differences arise between trade quantities and MPOC approved nominations.

Q10:	*Do you support the underlying philosophy in relation to the nature of the rights and obligations associated with a trade? If not, what alternative would you want and why?*

8.40 Trading could be based on sell offers, or both buy and sell offers. While the latter adds a little more complexity, it is a common market feature and is not expected to significantly alter the level of costs. Furthermore, given the relatively small market size, it would be preferable to allow both buy and sell offers to maximize the level of potential participation.

Q11: Do you support the proposed provision of buy and sell offers? If not, what alternative would you want and why?

8.41 The development of a platform will be simplified by adopting a degree of standardisation in respect of contract durations and volumes (rather than allowing users complete flexibility on these variables).

8.42 The basic 'time unit' could be aggregated to form contracts of longer durations, but could not be divided to provide shorter duration trades. The choice of basic unit should be compatible with the arrangements for transmission and wholesale reconciliation. Using Maui arrangements as a foundation would suggest that the basic unit should be a day according to the MPOC definition.

8.43 The basic volume unit needs to be sufficiently small to accommodate the needs of traders with modest requirements, but not so small that it adds cost without real value.

8.44 There is no 'right' answer, and it is ultimately a matter of judgement. One possibility would be a minimum increment size of say 0.1 TJ/day (approximately $700 of gas @$7/GJ).

Q12: Do you support the proposed use of 0.1 TJ/day as the basic trade unit? If not, what alternative would you want and why?

8.45 Parties could offer to buy or sell larger parcels by nominating the required number of standard parcels. For example, 5TJ/day for a week would be a strip of 50 standard contracts each day for the relevant period.

8.46 If the approach of using standard parcels is adopted, the platform could allow participants to indicate whether they will accept partial sales (i.e. for a strip to be broken by volume or time). This sort of flexibility is conventional, and is not expected to significantly alter cost.

Q13: Do you support the proposed ability to indicate whether partial acceptances will be permissible? If not, what alternative do you prefer and why?

8.47 The September Discussion Paper proposed that the platform should allow participants to nominate their preferred location for making a bid or offer, provided it did not add undue cost to a platform development.

8.48 There was support from a majority of submitters for this approach, provided it was limited to the Maui system. However, a number also pointed to the benefits of concentrating trades at a single point to enhance liquidity.

8.49 An alternative variant would be to trade at a virtual point on the Maui system that is located near (but not at) the main injection points. This approach would concentrate trading at a single point, but would also have some other flow-on consequences.

8.50 In particular, some parties believe that allowing trade at Maui injection points has disadvantages because welded parties will need to receive information on trades at that injection point in order to confirm nominations. This could raise competitive concerns.

8.51 If trade occurs away from those points, the welded party process should be simpler, with the bulk of gas transfers occurring between shippers at the trading point. It has been suggested that a neutral operator could be designated for that point, with that party receiving the information on trades without the same competitive issues being raised.

Q14: Do you support the proposal to adopt a virtual trading point? If not, what alternative do you prefer and why?

Information Processes

8.52 The platform will need to provide information for a number of purposes, including for trading, reconciliation, billing and for wider stakeholder dissemination.

8.53 The information most useful for trading will be live bid and offer information, and historic information such as volume weighted prices or price for the last trade for that time period.

8.54 Traders will probably also wish to use information from other systems (e.g. MDL IX) to assist in their trading decisions. However, there would not appear to be any particular merit in incurring cost to replicate those other information sources.

Q15: What sort of information would your organisation want from a platform for trading purposes?

8.55 As well as information about live bids and offers, participants are likely to require information for billing, governance and reporting purposes.

8.56 Information on trades as they occur can be provided to trader organisations for tracking within their billing/nominations/risk management systems.

8.57 The platform could also provide summaries for internal reporting/governance purposes (e.g. monthly or weekly). This could cover deals concluded with details of volumes, prices and authorisers, available headroom against current prudential limits, change to prudential criteria, and notification of any attempted deals that were not transacted (e.g. because a trader sought to deal outside their limits). These reports would be available only to each participating organisation through a secure electronic link.

Q16: What sort of information would your organisation want from a platform for billing, reporting and governance purposes?

8.58 To provide the price transparency benefits desired by stakeholders, the platform would also need to generate summary market statistics (as distinct from organisation specific information) available on a 'broadcast' basis. This information could cover matters such as:

- bids and offers that are live
- historic information on prices and volumes transacted
- information on the level of trader participation (e.g. number of trades, number of traders etc)

Q17: What sort of information should a platform provide for general dissemination to stakeholders?

Administration/IT Issues

8.59 There will also be a range of decisions to be made surrounding the administration/IT issues for a platform. These cover matters such as security arrangements, provision of information for auditing purposes, hours of operation, disaster recovery, ownership of data and intellectual property, information exchange protocol standards etc.

8.60 It would also be desirable to provide for the future evolution of the platform in a way that provides appropriate cost incentives.

8.61 These categories of issues are under consideration, but will be fleshed out once the operational elements of the functional specification are settled.

9 Next Steps

Standardised Contract(s)

9.1 The goal is to complete the work on the standard GSA and make it available for use by industry early in the New Year. In particular, the focus is on resolving the remaining issues outstanding in relation to liability and force majeure.

9.2 Gas Industry Co will also seek amendment to section 41 of the Crown Minerals Act in respect of the requirement for Ministerial consent where one of the parties to a gas sale agreement is a permit holder and the gas is being sold for the first time.

Platform

9.3 It is envisaged the work on evaluating feasibility of a platform will be carried forward in the following stages:

- Targeted consultation on certain aspects of design;
- prepare a functional specification for a platform, incorporating input from the Wholesale Markets Working Group and other stakeholder feedback;
- seek non-binding cost estimates from platform developers/operators based on the functional specification, in particular seeking information to enable any trade-offs to be made around functionality (e.g. service standards in relation to allowable downtime);
- if necessary, amend the functional specification in light of information on expected costs;
- obtain firm cost proposals from service providers and select a preferred provider; and
- undertake final cost benefit assessment, and decide whether to proceed.

9.4 In parallel with this work, Gas Industry Co will develop the detail of the implementation mechanisms, the form of the platform contract and the governance arrangements for a platform.

9.5 If a final decision is taken to proceed with a platform, this would lead into the actual development process, acceptance testing and user training, with an expected go-live date in 2007/08.

Appendix A: Recommended Format for Submissions

To assist the Gas Industry Co in the orderly and efficient consideration of stakeholders' responses, a suggested format for submissions has been prepared. This is drawn from the questions posed throughout the body of this consultation document. Respondents are also free to include other material in their responses.

Submission prepared by:..... (company name and contact)

QUESTION	COMMENT
Q1: Do you agree that user pays is the preferred option for funding the establishment and ongoing operation of a wholesale market for gas? If not, what funding mechanism do you consider most appropriate and why?	
Q2: Do you support the proposed approach to admission? If not, what alternative would you want and why?	
Q3: Do you support the proposed approach to suspension? If not, what alternative would you want and why?	
Q4: Do you support the proposed approach to user controls? If not, what alternative would you want and why?	
Q5: Do you support the proposed approach to display of bids/offers? If not, what alternative would you want and why?	

Q6: Do you support the proposed form of prudential criteria? If not, what alternative would you want and why?	
Q7: Do you support the proposed approach to adjusting prudential criteria? If not, what alternative would you want and why?	
Q8: Do you support the proposed provision of an override? If not, what alternative would you want and why?	
Q9: Is your use of a platform likely to be significantly affected by whether the market operated on a blind basis or not? If so, in what way?	
Q10: Do you support the underlying philosophy in relation to the nature of the rights and obligations associated with a trade? If not, what alternative would you want and why?	
Q11: Do you support the proposed provision of buy and sell offers? If not, what alternative would you want and why?	
Q12: Do you support the proposed use of 0.1 TJ/day as the basic trade unit? If not, what alternative would you want and why?	

Q13: Do you support the proposed ability to indicate whether partial acceptances will be permissible? If not, what alternative do you prefer and why?	
Q14: Do you support the proposal to adopt a virtual trading point? If not, what alternative do you prefer and why?	
Q15: What sort of information would your organisation want from a platform for trading purposes?	
Q16: What sort of information would your organisation want from a platform for billing, reporting and governance purposes?	
Q17: What sort of information should a platform provide for general dissemination to stakeholders?	

Appendix B: Feedback on Previous Discussion Paper

This appendix summarises the submissions received to the Gas Industry Co Discussion Paper "Wholesale Market Design" released in September 2006.

Level of Response

Submissions were received from nine parties, covering a broad range of interests as set out in Table 3.

Table 3: Submissions received

Stakeholder	Nature of organisation
Contact Energy	Retailer/wholesaler/user
Genesis Energy	Retailer/wholesaler/user
Mighty River Power	Retailer/wholesaler/user
MEUG	User representative
Multigas	Retailer
NZX	Potential platform provider
Shell	Producer/wholesaler/pipeline owner
PHI	Canadian submitter – detail unknown
Vector	Producer/wholesaler/pipeline owner & operator

Overall Thrust of Responses

While all stakeholders raised specific issues, there was a general level of endorsement for the thrust the Discussion Paper. This is reflected by comments made in submitters' covering letters, such as:

> *"Genesis Energy is generally supportive of the approach taken in the discussion paper and wishes to congratulate the Gas Industry Company in the work it has done. The discussion paper methodically addressed the issues within a rigorous analytical framework then moves to an even-handed assessment of the mechanisms by which the preferred options could be implemented"*
>
> *"…MEUG members support the general approach being adopted by the GIC, namely making further progress on a standard contract, a measured development of a simple matching platform and analysis and investigation of a more sophisticated platform"*
>
> *"In brief, Vector supports the development of a matching platform for short-term gas trades"*
>
> "*We [Shell] are supportive of the Gas Industry Company's work in Wholesale Market Design and see [the] direction as positive*"
>
> "*Contact largely agrees with the conclusions set out in the Discussion Paper*"
>
> "*Mighty River Power congratulates the GIC on a well written, logical and sound consultation paper. We agree with the GIC's approach and conclusions, namely*…"

Responses on Key Proposals

As noted above, while submitters supported the general direction of the Paper, questions and concerns were raised about issues of detail. The table below sets out the key proposals contained in the Discussion Paper and the broad stakeholder response on that issue.

Table 4 - Key proposals in Discussion Paper and stakeholder response

Gas Industry Co proposal	Broad stakeholder response[12]
Regulatory objective – the specific regulatory objective for this component of the wider wholesale work stream should be to facilitate transactional efficiency in gas trading;	Generally endorsed
Long term trading - there is no case for introducing any formalised arrangements for longer term (i.e. greater than one year) trading of gas to improve transactional efficiency at this time	Generally endorsed
Short-term trading contract – there is a case for developing a standardised short-term contract for use on a voluntary basis (and a draft form of contract was enclosed)	Rather than develop a single contract for bilateral trading and standardised platform trading, it would be preferable to develop two separate contracts. A significant number of comments were made on the detail of the contract (see later section).
Platform to support trading of a standard contract – subject to confirming costs, there is a reasonable case for putting a simple platform in place to facilitate trading – the case for a more sophisticated platform that could more easily support trading close to real time is not supported at this time	Endorsed in principle – provided staged approach adopted with robust cost benefit assessment
Prudential issues – if a simple platform is put in place, the preferred means of addressing prudential issues would be for participants to pre-select individual trading limits that they are comfortable with for each counterparty (so-called 'whitelist') – this would allow blind trading and avoid the need for complex limits and margin arrangements;	Endorsed in principle – provided it does not raise competitive barrier
Balancing issues – further analysis should be undertaken on balancing issues, as this will have a major influence on the extent of any need for real time trading, and hence the evolution of a platform over time	Generally endorsed – provided it is clear that further work confined to analysis rather than development of a more sophisticated platform

12 This summary does not attempt to reflect the detail of every submitter's response. Rather it presents the broad view or themes that emerge from the responses. Refer to next section for detail of stakeholder views.

Additional Issues Raised by Submitters

In the course of responding to the Discussion Paper, some submitters raised issues which were not formally part of the consultation process, but which nonetheless were seen by those submitters as being significant in the wholesale market context. These were:

- the current pricing regime on the Maui system was seen to facilitate trading because it is based on usage, whereas most of the Vector system operates on a pre-booked capacity system. Some participants considered that Vector should also offer a 'spot' transmission product similar to the Maui arrangement (MRP, MEUG); and
- some industrial Gas Supply Agreements (GSAs) are said to have exclusivity clauses prohibiting purchase of gas from other suppliers – this was seen as limiting the potential for trading gas (MRP, MEUG).

Table 5 Responses to Specific Questions

Q1: Do you agree with regulatory objective for the component of the Wholesale Market work stream? If not, what objective should the Gas Industry Co be considering?	
Contact Energy Ltd	Contact agrees with the regulatory objective set out in the discussion paper "Wholesale Market Design" dated September 2006 (the "Discussion Paper").
Genesis Energy Ltd	Yes.
Mighty River Power Ltd	Yes.
Major Electricity Users' Group	Yes but feel that the GIC objectives including regulatory components need to be expressly stated.
Multigas NZ Limited	Yes
PHI Developments Ltd	Yes. There appears to be competing objectives as laid out in The Gas Act. In a market, producers will always want higher prices (facilitation of ongoing gas supply) and consumers will always want lower prices (sustained downward pressure). A better objective, as implied by the desire to encourage transactional efficiency, may be the creation of a market structure where prices for gas reflect fair value that can be used as a reference for investment decisions.
Shell Limited	Agree. The issue of the development of protocols and standards for wholesale trading is the key provision.
Vector Limited	Vector agrees that a wholesale market will provide better market efficiency and align with regulatory objectives

Q2: Do you agree with the general approach to assessing the different options using both quantitative and qualitative criteria? If not, what alternative approach, that also complies with the Gas Act, would you suggest?	
Contact Energy Ltd	Contact agrees with the use of quantitative and qualitative criteria to assess the options.
Genesis Energy Ltd	Yes.
Mighty River Power Ltd	Yes.
Major Electricity Users' Group	Yes.
Multigas NZ Limited	Both options satisfactorily cover industry requirements and with benefit of experience it may be necessary to incorporate some refinements and that being the case should be mandatory review period?

PHI Developments Ltd	Not entirely. Markets reflect, by their very nature, the interaction of individuals seeking to maximize gain. Although economic models and charts (a quantitative framework) are effective conceptual tools, there are inherent risks in using them as a proxy for future human behaviour. It is suggested that a review be made of the existence and evolution of similar markets to determine appropriate market structures.
Shell Limited	We do not object to this approach. Quantification of any reliable nature difficult and can be indicative only because the assessment is made on current perspectives which will be changed be market development.
Vector Limited	Applying qualitative and quantitative assessment criteria to a relatively small market with limited players, adds a high subjectivity to the exercise. Vector would suggest that while the methodology seems valid the results should be viewed with caution.

Q3: Are there other time horizons that should be considered for the trading of gas? If so, what are those time horizons?	
Contact Energy Ltd	Contact considers that the risks related to a trade under a contract with a term of a day to a week are substantially different to the risks related to a trade with a term of a month or more. Many provisions normally found in a gas trade contract such as those to address assignment, termination, confidentiality, dispute resolution are not required in very short-term arrangements and many other provisions can be significantly simplified. It may therefore be worth considering the effect on contract provisions of time horizons of up to a week and in excess of a week but less than a year. A number of parties have recently developed trading relationships governed by a set of enduring master terms that apply to on going individual trades that are of very short duration, usually no greater than one week and sometimes as short as a day. Either of the parties can withdraw from such a relationship by not accepting individual trading opportunities but are fully committed for the duration of each individual trade. It seems that master terms could be agreed by a number of parties who wished to be involved in bilateral trades. This approach of short-term trades incorporating master terms greatly minimises risks for both contracting parties and significantly avoids the need to address issues that are only likely to arise in a longer time relationship such as assignment and credit worthiness. This appears consistent with the structure of the Short-term Trading Contract set out in Appendix F of the Discussion Paper although the detail of that contract appears unnecessarily complex if it is used in that way.
Genesis Energy Ltd	The split based on contracts with durations of less than and greater than one year seems appropriate. It does not, for example, hinder parties if they so desire to use the standard contract as the basis for contracts of a longer term.
Mighty River Power Ltd	No. Given the Maui Pipeline Operating Code (MPOC) balances on a daily basis there seems no reason for short-term trades to occur more frequently than daily.
Major Electricity Users' Group	No.
Multigas NZ Limited	The time horizon offered appears to be suitable at this stage.
PHI Developments Ltd	Yes. An alternative way to define short-term trading is all transactions that flow for a period of one month or less, and they can be agreed to within a day of the actual start date. An alternative way to define long term trading is all transactions that flow for longer than one month, and they too can be agreed to within a day of the actual start date.
Shell Limited	Market development should concentrate on the short-tem trading market, long term arrangements can be private bilaterals referencing the standard contract of the short-term market in respect of technical issues of gas management, transport, measurement and allocation.
Vector Limited	The time horizon of one year is too long. Vector has observed that most gas trades usually range from a few weeks to a few months. In the future weekend / weekday trading is possible. Vector would suggest short-term trading is anything under 3-6 months, with an upper bound limit of 6 months.

Q4: Are there any other reasonably practicable alternatives for longer term trading of gas that should be considered and if so, what are they?	
Contact Energy Ltd	The listed options adequately cover the possibilities.
Genesis Energy Ltd	No.
Mighty River Power Ltd	We agree that executing a longer term trade via a trading market would not be practical. However, the GIC could consider a bulletin board where parties can describe their longer term requirements. In all likelihood this would not benefit large scale (power station) contracting because these parties are keenly aware of any large parcels coming to market by industrial sized users may benefit.
Major Electricity Users' Group	No, but the industry would benefit from there being a high level of transparency in respect of key terms of long term contracts. New entrants into the market would find this information of considerable importance.
Multigas NZ Limited	As the industry gains better experiences with MPOC, Oatis and other incorporated co-regulated models other options may surface, so the models applied today should have flexible policies. As per our answer in Q2.
PHI Developments Ltd	Yes. It is common for buyers to secure gas for a specific term and allow the price paid during that term to float with short-term prices (daily prices at an agreed upon point usually referred to as the "index"). With this arrangement, buyers agree to pay "market" prices for gas they take title to, and preserve the ability to lock-in future prices if they are able to agree on a value with the seller.
Shell Limited	We have no additional suggestions.
Vector Limited	No

Q5: Are you satisfied with this evaluation of options for longer term trading of gas, and if not, what aspects would you alter and why?	
Contact Energy Ltd	In relation to "Formalised auction/tender", "Posted Prices" and "Formalised negotiation" in the row headed "Costs and prices subject to downward pressure" we would change "standardised" to "customised". Apart from this change we are satisfied with the analysis.
Genesis Energy Ltd	Yes.
Mighty River Power Ltd	In general yes, although the analysis is very subjective. For example, table 7 suggests that voluntary contracting will lead to downward pressure on costs and prices. This outcome is contingent on the buyer and seller having equivalent market power (i.e. in a perfectly competitive market), which is unlikely in the New Zealand gas market given the small number of players who all have differing levels of market share, market power and negotiating tactics.
Major Electricity Users' Group	Satisfied but see also answer to Q4.
Multigas NZ Limited	Generally speaking we are in agreement with the evaluation provided.
PHI Developments Ltd	Not entirely. Given the limited number of market participants, some consideration may need to be given to the ability to exercise market power (i.e.; conduct transactions in a manner that could be considered inefficient).
Shell Limited	No, long term contracts could refer to industry model contracts for technical and gas delivery terms. Standard contract terms for technical issues of gas management, transport, measurement and allocation should refer to industry standards and protocols (see answer to Q6 below).
Vector Limited	No comment

Q6: Do you agree that there is no case for formalising arrangements for longer term trading of gas to improve transactional efficiency? If not, what alternative do you prefer and why?	
Contact Energy Ltd	Contact agrees that this is case for formalising longer term trading of gas to improve.
Genesis Energy Ltd	Yes. Longer term gas contracts are generally based around the unique circumstances of a gas field development or the requirements of a gas consumer to support an investment decision on new plant and/or the operational requirements of new or existing plant or retail market loads and there are different relationships between buyer and seller across different contracts (for example gas supply agreements, farm-in arrangements etc.) It is therefore not appropriate to formalise such long term arrangements.
Mighty River Power Ltd	Yes, subject to the suggestion in Q4.
Major Electricity Users' Group	Agree there is no case for formalising arrangements for longer term trading but there would be a lot of support from some MEUG members if a database of bilateral contracts entered into was developed as has been proposed for the Electricity Hedge Market. See also answer to Q4.
Multigas NZ Limited	Agreed.
PHI Developments Ltd	Not entirely. Transactional efficiency can be encouraged in the long term market by addressing issues such as: the need for standard contracts, the development and reporting of index prices, and capacity release bulletin boards.
Shell Limited	While price, pricing structures, term, liability, and quantity are all appropriate for voluntary contracting for long-term contracts, it would be most efficient if the technical matters were dealt with be reference to the current industry standards and protocols. Technical matters could be addressed be reference to the "then current" standard industry contract for short-term trading. This would allow term contracts to evolve with industry gas delivery standards and protocols.
Vector Limited	Yes

Q7: Are there any other options that should be considered for short-term gas trading, and if so, what are the options?	
Contact Energy Ltd	Contact is not aware of other options.
Genesis Energy Ltd	The options considered cover the normal range of trading options applying in commodity markets.
Mighty River Power Ltd	Yes. Regarding 5.1 Mighty River Power recommends that balancing is not excluded from short-term trading. Generally the re-balancing of a pipeline occurs after the day an imbalance occurs. Excluding balancing unnecessarily restricts the value that can be derived from a trading market.
Major Electricity Users' Group	No other option which appeal to industrial users. The theme of transparency and information is reiterated.
Multigas NZ Limited	Spot trading still required fine tuning and again only through experiences will we then understand whether tighter or broader policies need to be developed and the opportunity for a review process.
PHI Developments Ltd	It is common in short-term markets to use brokers (i.e.; indirect bilateral) to provide anonymity and liquidity. The use of brokers also attracts speculators that can play a very important role in any efficient market.
Shell Limited	We have no additional suggestions at this time.
Vector Limited	No

Q8: Are you satisfied with the qualitative assessment of short-term trading options? If not, what aspects would you change and why?	
Contact Energy Ltd	Contact is satisfied with the qualitative assessment.
Genesis Energy Ltd	Yes.
Mighty River Power Ltd	Yes. The primary consideration for Mighty River Power is whether the trading mechanism will deliver sensible pricing signals i.e. pricing high enough to encourage or at least not discourage exploration and low enough to encourage/ not discourage electricity generation, industrial and retail use of gas. If this is not the outcome then a voluntary market will probably not be utilised. Platform bilateral and direct bilateral are more likely to achieve this outcome than the alternatives.
Major Electricity Users' Group	Yes see also answer to Q7.
Multigas NZ Limited	Yes.
PHI Developments Ltd	Not entirely. Given the limited number of market participants, some consideration may need to be given to the ability to exercise market power. Also, the short-term market must have adequate liquidity in order for it to be transactionally efficient, and qualitative assessments likely need to allow for this.
Shell Limited	The benefits of developing a "Platform bilateral" and its contribution to establishing necessary industry standards and protocols supporting the wholesale gas market might have been underestimated.
Vector Limited	To a degree – please refer to Q2

Q9: Do you agree that the standard contract should allow for both types of approaches? If not, what would you prefer and why?	
Contact Energy Ltd	Both approaches should be addressed. From Contact's experience and considering contracts of up to one year's duration there are essentially two types of contracts: • fully featured contracts that contain rights to sell and purchase a fixed volume of gas within a fixed period with some daily take flexibility; and • much simpler contracts usually comprising master terms with renewal of the agreement on usually a weekly but sometimes daily basis providing for the sale and purchase of a fixed quantity of gas on each day of the term of the renewed contract. • In designing a standard contract it may be worthwhile for the GIC to distinguish between these two types of arrangements and to accordingly design separate standard agreements to meet the separate requirements.
Genesis Energy Ltd	The standard contract should allow for either: 1. Fixed daily quantities; or 2. Maximum contract volume with minimum and maximum daily quantities.
Mighty River Power Ltd	Yes
Major Electricity Users' Group	Yes. However it is not clear that the standard contract will be widely used. If supply parties wish to use bespoke contracts it may be necessary to require the publication of key summary information sop everybody knows where the market is at and what types of key terms and conditions apply in contracts that are actually signed.
Multigas NZ Limited	Yes.
PHI Developments Ltd	Yes.
Shell Limited	Yes

Vector Limited	Yes. A standard contract needs to not only cover both the determination of volumes and terms of trade but also needs to specify how it intends to integrate with existing reconciliation processes. An example would be – does a trade occur before or after the gas transfer process? How is change of ownership tracked and communicated to the transmission provider? Can the same volume of gas be traded more than once on the same day?

Q10: Do you agree that the standard contract should not provide for price adjustments for taxes and government charges? If not, what changes would you prefer and why?	
Contact Energy Ltd	The purpose of price adjustments and provisions covering changes in taxes and government charges are to remove risk for buyer and seller. These provisions are appropriate in contracts with duration of say greater than a month. Such provisions are unnecessary in contracts with duration of less than a month where it should be possible to foresee any changes in taxes and government charges.
Genesis Energy Ltd	Genesis Energy considers that the standard contract should provide for such price adjustments and considers in fact, given its prevalence in long term contracts, that its omission from the contract would increase uncertainty in pricing of standard trade contracts in particular in light of proposed carbon charges and changes in the Gas Industry Company levy. As noted by the Gas Industry Company in this and previous discussion papers, the trading contracts are likely to be used to enable downstream parties to trade 'unders' and 'overs' which arise under the relatively inflexible long term supply contracts. To the extent that these long term contracts include the ability for the seller to adjust prices for taxes and government charges a failure to pass these on under the short-term trade contract exposes the buyer under the long term contract (who is the seller under the short-term contract) to a cost exposure for the amount of such taxes and charges (which includes in many cases liability for any carbon tax or equivalent charge if it is introduced). Buyers under the long term contract are likely to seek to mitigate this exposure through the price they charge for the gas under the short-term contract. Genesis Energy considers the ability for the taxes and charges to effectively be a "pass through" cost (as opposed to an uplift on the price akin to a risk premium) will result in more efficient pricing of short-term contracts and that therefore the standard contract should provide for price adjustments for taxes and government charges.
Mighty River Power Ltd	It should not cover changes in taxes or government charges but the contract should state whether it is inclusive or exclusive of the GIC levy (as set at the trade date).
Major Electricity Users' Group	Yes see answer to Q9.
Multigas NZ Limited	Yes – We believe that any aspect of a supply arrangement that may have a material effect on the content structure and delivery outcome of the product or services needs to be at least outlines or referred to in ant contract.
PHI Developments Ltd	Yes.
Shell Limited	Yes, some indication of standard practice would be useful for quickly establishing contracts. However, it should be recognised that parties can vary all commercial terms by ancillary agreement (price, price indices, taxes, government charges, pricing structure, and liability).
Vector Limited	If the contract term is longer than 6 months then a price adjustment mechanism should be included. Most major contracts are moving to 1/4'ly ppi movements. There may also be a need for an additional clause to take into account a change in other taxes/levies etc such as a GIC levy during the contract term. However, contracting parties will always be free to add any additional clauses they feel are necessary for their particular transaction.

Q11: Are you satisfied with the proposed approach for addressing s.41 of the Crown Minerals Act in the standard contract? If not, what alternative would you prefer and why?	
Contact Energy Ltd	The application of section 41 of the Crown Minerals Act clearly requires clarification as it leaves the status of many contracts uncertain while the contract is operational. That problem arises because of the time required to gain approvals. Contact supports the action the GIC is taking to attempt to resolve the issue. It is difficult to see why the issues that section 41 attempts to address need to be addressed in contracts that are agreed in an open competitive market.
Genesis Energy Ltd	Genesis Energy is satisfied with, and supports, the approach adopted by the Gas Industry Company with respect to s41. Genesis Energy notes in particular that given the significant consequence of failing to comply with s41 that the issue must resolved by way of legislation. In the view of Genesis Energy, any degree of uncertainty as to the validity of contractual obligations in this area is unacceptable and industry participants would be unable to trade by way of a bilateral platform (or any of the other mechanisms considered by the Gas Industry Company under this review) if such uncertainty remained.
Mighty River Power Ltd	Yes – a blanket exemption is required. The Crown may need to be satisfied that the buyer and seller are not related parties.
Major Electricity Users' Group	The approach must include a resolution of this issue i.e. a change to s41. or a legally acceptable code of practice or binding rule that precludes any retrospective consequences to participants in wholesale gas trading.
Multigas NZ Limited	Yes.
PHI Developments Ltd	No. A standard contract should require the seller to warrant that they have title to the gas that they are selling. If the seller does not hold title to a sufficient volume of gas once their contractual obligation commences, then the seller is obligated to buy the necessary volumes from someone else. This is a core contractual concept that allows speculators to participate in the market (i.e.; people can sell gas they don't have if they think they can buy it for less money later).
Shell Limited	We support the GIC clarifying the situation with the Ministry of Economic Development to accommodate gas trading arrangements of short duration.
Vector Limited	Yes – but Vector is unsure that the original intentions of s.41 are valid in today's environment. Vector has noted that short-term trading in the market is already occurring without s.41 approval hence it seems the wording in the Act needs clarification.

Q12: Do you agree that the standard contract should not provide for any conditions precedent? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Contact agrees that the standard contracts should not provide for conditions precedent. Such conditions are usually specific to a particular contract and should only be necessary when the contract is executed significantly prior to delivery of gas under the contract and physical projects must be completed or third party approvals gained before gas can be delivered or taken. It seems unnecessary to provide for such uncertainties in a short duration contract.
Genesis Energy Ltd	Yes (with the exception of the s41 issue, as noted).
Mighty River Power Ltd	Yes
Major Electricity Users' Group	See cover letter re carriage/right to trade. "Paragraph 4 of covering letter - The requirements for industrial users (see last sentence of paragraph 2 above) include the explicit right to trade being included in all supply contracts plus the necessary transmission/carriage rights to enable a short-term sale or purchase to be effected. MEUG is aware of a number of gas supply contracts between industrial users and gas suppliers which specify that the customer shall not purchase or obtain gas from any other source. These two items (the right to trade and carriage arrangements) are necessary pre conditions before industrial users could participate in any wholesale market. The comments made by MEUG in April 2006 on conceptual aspects remain relevant, in particular the need for pro-competitive outcomes and maximum transparency."
Multigas NZ Limited	Broadly agree with the question.
PHI Developments Ltd	Yes.
Shell Limited	No, once executed the contract should be unconditional.
Vector Limited	Yes

Q13: Do you agree that the standard contract should not make seller liable for gas specification? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Gas quality should be addressed through open access arrangements as it is under both the MPOC and Vector arrangements although not satisfactorily under Vector arrangements. It is pointless the buyer seeking to make the seller responsible for gas quality under a bilateral trade since under open access arrangements the buyer is fully exposed to the quality of gas injected by all parties into the relevant open access system. The buyer requires protection from all gas injections and that can only be provided under the open access arrangements.
Genesis Energy Ltd	Genesis Energy agrees that a Shipper should not be liable for gas specification, which is consistent with the position set out in the Vector standard TSA and MPOC (and the requirement under each transmission arrangement that the buyer under the short-term trade has a TSA). Genesis Energy is however concerned that the buyer using the standard contract is able to exercise remedies for non-specification gas and in particular the indemnities given by MDL and Vector. Genesis Energy would like to discuss the liability chain in the upcoming workshop. If the seller is a Welded Party at a Maui receipt point then it will be liable for gas specification but under its Interconnection Agreement rather than the gas sales agreement. If the seller is a shipper at a Maui delivery point then it should not be liable for gas specification. Genesis Energy would like to discuss how this position is effected through the standard short-term contract at the upcoming workshop (in particular with respect to clause 5.1.)
Mighty River Power Ltd	Liability for non-specification has not been inconsistent with the MPOC. Under the MPOC Injecting Welded Parties and MDL may be liable for non-specification gas.
Major Electricity Users' Group	Yes but compliance with gas specs. Must be enforced.
Multigas NZ Limited	Yes if the Seller in whatever context also has a reference or requirement for gas specification in its contracts.

PHI Developments Ltd	No. A product that has a broad range of specifications is, by definition, no longer a commodity. In order for price discovery to have any meaning at all, pricing must refer to a product that has known and unchanging characteristics. Seller should be responsible for delivering gas to buyer as per a specific set of requirements. It is the responsibility of the seller, then, to have contractual arrangements in place that ensures pipeline deliveries meet a predetermined set of specifications.
Shell Limited	While the interconnection agreements between interconnected systems should cover this point sufficiently, it could be helpful for that standard gas contract to specify that seller will be obliged to deliver gas meeting pipeline specification.
Vector Limited	Yes. Liability for gas specifications is captured in other contractual arrangements (such as ICAs) and is being discussed in other GIC work streams.

Q14: Do you agree that the standard contract should not provide for any priority rights? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Priorities are likely to be specific to a particular trade. Contact agrees that there should be no generic priority provisions in the standard contract.
Genesis Energy Ltd	Yes, although this may be a matter which parties wish to negotiate for short-term trades of longer duration. Genesis Energy would like to discuss at the workshop the ability for the standard contract to accommodate special conditions (which may be selected for example from a list of standard clauses) so that the contract is suitable for trades of duration.
Mighty River Power Ltd	Yes
Major Electricity Users' Group	Yes.
Multigas NZ Limited	Unless there is a requirement from the Sellers contract requiring such priority to be called on and under what conditions these priorities take precedence then again an option for terms of reference.
PHI Developments Ltd	Yes.
Shell Limited	Yes.
Vector Limited	Priority rights are important but they don't need to be contained in the standard contract – it can be captured in the Gas Transfer Agreement.

Q15: Do you agree that the standard contract should set out a broad description of the transport obligations/rights on buyer and seller? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Contact considers that transportation in a gas trade contract should be restricted to establishing responsibility for arranging transportation and dealing with the consequences of failure to make those transportation arrangements. It is only possible for a trade to occur at a defined delivery point and for the seller to warrant transfer of title at that point if the seller delivers the relevant quantity of gas to the delivery point. The buyer will only be able to make use of the same quantity of gas to which title is transferred if it transports that quantity of gas away from the delivery point. Therefore the seller should be liable for the consequences of its failure to deliver to the delivery point and buyer should be liable for its failure to transport from the delivery point. We note that the MPOC makes it very clear how gas is delivered and title is transferred at Maui receipt points and delivery points. That is through establishment of an Approved Nomination. Hence for a trade made at a MPOC receipt or delivery point it only seems necessary to establish liability for failing to make an Approved Nomination consistent with the agreed traded quantity. The MPOC addresses failure to deliver or to take in accordance with an Approved Nomination. The Vector arrangements are substantially less satisfactory because of Vector's requirement that transportation capacity must be purchased on an annual basis. That may preclude short-term trades involving transport on Vector pipelines. However, putting that aside and assuming one of the parties holds sufficient capacity, it is only necessary to address the consequences of the seller's failure to deliver the correct quantity to the delivery point and the buyer's failure to take the correct quantity from the delivery point. That would be established through payments made for mismatch. The standard agreement may need to include a provision to cover situations when the seller was unable to deliver the gas to the delivery point or the buyer was unable to take the gas at the delivery point for reasons outside their control. A standard force majeure/maintenance clause would cover this.
Genesis Energy Ltd	In Genesis Energy's view, this is not required provided the delivery point is defined and is limited to the Maui pipeline. It is more relevant that allocation based on nominated quantities and the need to execute Gas Transfer Agreements is covered.
Mighty River Power Ltd	The parties should warrant that they have sufficient transmission capacity in their transmission contracts to effect the trade.
Major Electricity Users' Group	Yes – resolution of carriage/transmission issue is critical and therefore the standard contract must specify obligations and rights.
Multigas NZ Limited	Yes – We believe that any aspect of a supply arrangement that may have a material effect on the content structure and delivery outcome of the product or services needs to be defined or referred to in any contract.
PHI Developments Ltd	No. Fundamentally, the standard contract should be a title transfer document only. Prices agreed to under the contract reflect change in ownership, and are an accurate measure for the fair value of the gas. Transport obligations/rights should be described in separate transportation agreements.
Shell Limited	No. The contract should simply provide that Seller is responsible for bringing the gas to the trading point using available open access systems, and Buyer is responsible for taking it away.
Vector Limited	Need to be reasonably specific as to the obligations of parties. Not only for their own transmission arrangements but also obligations to enter Gas Transfer Agreements etc and any other allocation/reconciliation arrangements that need to be made.

Q16: Do you agree that the standard contract should have liability provisions that exclude indirect losses, and that direct losses (in equivalent $/GJ terms) would be capped at the pipeline mismatch/imbalance price? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Contact agrees with this approach. In fact a trade effected at a Maui receipt point or delivery point does not require liability provisions apart from provisions to address the situation when either the seller or the buyer fails to establish an Approved Nomination that allows transfer of title to the agreed traded volume. If the seller fails to take action to establish the correct Approved Nomination then buyer is kept whole if it draws on balancing gas and is compensated by the seller for the difference in cost between balancing gas and the price of the traded gas. If the buyer fails to take action to establish the correct Approved Nomination then seller is kept whole to the extent that buyer compensates seller for the difference between the price for put balancing gas and the sales price of gas under the trade. The Vector mismatch arrangements should work in the same manner
Genesis Energy Ltd	Yes.
Mighty River Power Ltd	We agree that the standard contract should have liability provisions that exclude indirect and consequential losses. However, we believe direct losses should be linked to (not necessarily equal to) the value of the traded gas rather than based on the mismatch/imbalance price for a few reasons. First the traded gas price is always known whereas a mismatch/imbalance price may only be determined after a Welded Party has conducted a tender process for balancing gas. Therefore it may not be clear what the mismatch/imbalance price is at any point in time. Second a party may breach a contract provision without creating a mismatch/imbalance for example by not nominating for and not supplying/taking gas as agreed in a trade. Third, a party who breaches a trade may put themselves in mismatch or imbalance and in this case is likely to already be responsible for and assume the potential liability for their own position. Therefore the mismatch/imbalance price may not be a reasonable estimate or linked to the other party's loss.
Major Electricity Users' Group	Further work on this area is required because it appears that a pipeline/mismatch price can be set unilaterally. This does not appear appropriate if it becomes the default or capping price.
Multigas NZ Limited	Yes to indirect losses because this would be too difficult to pin down under terms of reference and opens up counterfactual claims. Direct Losses – clear definitions are required because capping at the mis-match price may not be satisfactory compensation for losses incurred. The concept of mis-match gas needs to be controlled in order that excessive margins do not eventuate resulting in increased flow on charges to the end consumer.
PHI Developments Ltd	Generally, yes. It may be simpler to define the direct loss as the replacement cost for the gas.
Shell Limited	It would seem to be efficient to have model terms on commercial issues if such can be identified, although these may be revised by agreement provided they do not clash with necessary industry standards and protocols for gas nominations, delivery, measurement and allocation. Direct losses should include any Incentive Fee costs if applicable, a cap at the negative mismatch price may not be adequate.
Vector Limited	Liability provisions won't be sufficient. There needs to be significant disincentives to defaulting on a trade. Alternatively, an integrated reconciliation mechanism that forces a trade to occur should be investigated (see comments in cover letter).

Q17: Do you agree that the standard contract should have FM provisions based on the principle that for very short-term trades FM cannot be invoked unless balancing has been suspended – i.e. curtailment is occurring? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Contact believes the standard contract could include force majeure provisions that grant relief to the buyer from the obligation to take and pay for gas for reasons that are beyond its control and that grant relief to the seller if it is unable to deliver gas for reasons outside its control. We think this may be necessary in longer-term arrangements and for contracts of significant size. Excluding a standard provision granting force majeure relief from the standard contract is likely to increase risk associated with a trade over the longer term under the standard contract and may therefore limit the usefulness of the standard contract. Conversely there may be situations where certainty of performance may be appropriate and buyers and sellers may be willing to price the risk. Inclusion of a force majeure is less necessary if the parties are able to adjust the agreed traded quantity in the event an unforeseen event arises that hinders the gas trade. The intraday notification provisions of the MPOC go some way to achieving that but this need to be reflected in the standard terms. Effectively provisions allowing adjustment of the agreed traded are force majeure provisions in another guise. We note that under the MPOC a welded party is able to seek force majeure relief through amendment of Approved Nominations whereas a shipper cannot seek that relief. It seems more likely that a seller will be a welded party rather than a shipper and that a buyer will be a shipper rather than a welded party. Exclusion of a force majeure from the standard terms would mean the buyer and seller would often have asymmetric protection from risk under the standard terms. That is unreasonable.
Genesis Energy Ltd	Genesis Energy does not agree that that *force majeure* raises the same issues discussed in the section title 'Liability provisions', particularly as the contracts could be for periods of months.
Mighty River Power Ltd	We would be interested in hearing a pipeline owner's perspective on this. A trading platform should not increase the likelihood of a contingent event occurring because of a lack of FM provisions. It seems that the GIC is suggestion that an event cannot be called an FM event until the point where there is a system wide situation (i.e. the damage is already done). It seems more wise to call an FM if it is known that not doing so may result in a system wide event (i.e. before the damage has been done). This is especially the case given short-term trades may be up to a year long in the GIC's definition.
Major Electricity Users' Group	Yes in principle. However further work on "curtailment" is necessary.
Multigas NZ Limited	Yes – agreed to this.
PHI Developments Ltd	Generally, yes. It may make sense to broaden the Force Majeure clause beyond the simple definition that balancing has been suspended.
Shell Limited	FM should apply. The limitation to only one scenario is too limiting. Perhaps it could be widened to any curtailment imposed by the delivery system according to Code, force majeure on transmission systems, imposition of contingency plans, or force majeure on major interconnected systems or injection points.
Vector Limited	FM provisions should be allowed for but there needs to be clarification over when FM can be invoked. If the FM provisions are too weak they will undermine the certainty of the trading process. Excluding FM will only work for very short trades, maybe less than 1 week otherwise exposure is too high

Q18: Do you agree with the proposed dispute resolution provisions for the standard contract? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Contact believes the best method for resolving well-defined technical disputes such as those related to invoices is through resolution by a technical expert. Compared with other options such a process is low cost and produces a timely outcome. Where the dispute is more complex and involves contract interpretation Contact believes the courts provide the best resolution process. In a short-term contract disputes requiring resolution by the courts should be a remote possibility. At this stage, the expertise and the effectiveness of the proposed Ruling's Panel is unclear. Contact is also reluctant to commit to pay fixed charges that may be necessary to establish and maintain the Panel without a clear understanding of the benefits that may accrue.
Genesis Energy Ltd	Genesis Energy agrees that invoice disputes should be referred to an independent expert with the appropriate technical expertise. With respect to all other disputes, Genesis Energy does not support the use of the Rulings Panel. These disputes may be complex (if unable to be resolved at senior management level) and Genesis Energy prefers that such disputes are referred to a forum with appropriate rules and due procedure for timely and appropriate resolution. Genesis Energy considers either the courts or arbitration to be appropriate and would provide parties with more transactional certainty than the as yet untried processes of a Rulings Panel. Finally Genesis Energy does not consider that use of the Rulings Panel would be more cost effective for parties than the other dispute resolution mechanisms.
Mighty River Power Ltd	We agree that the Ruling Panel is the preferred option.
Major Electricity Users' Group	Yes
Multigas NZ Limited	Consideration for clause 11.5 – the buyer should pay what is **NOT** in dispute. If however, at the conclusion of the DR process the buyer is liable for the balance then that difference as well as interest should be paid at bank overdraft rates to the Seller.
PHI Developments Ltd	No. The standard contract is a legal document that, in all likelihood, will realize incremental changes as the gas market itself evolves. Many potential counterparties will not want to forfeit their legal right to have disputes settled in a Court of law. It is desirable to have a standard contract that does not restrict market liquidity by excluding potential counterparties.
Shell Limited	This depends on the structure of Rulings Panel. Such a panel should have access to good wholesale gas market practice from an international perspective.
Vector Limited	Yes. While a disputes process may be inevitable, both the contractual provisions and resolution process itself should remain as streamlined as possible.

Q19: Do you agree that the standard contract should provide a standard assignment provision? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Contact agrees that a contract with a term of more than say one moth should include a simple assignment provision. We consider that an assignment provision is unnecessary in a shorter-term arrangement.
Genesis Energy Ltd	Yes provided that the right of buyers to on-sell and use the gas for any purpose is unrestricted.
Mighty River Power Ltd	Yes
Major Electricity Users' Group	Yes
Multigas NZ Limited	Yes – Assignment should not be unreasonably withheld if that assignment has no material effect on the other party.
PHI Developments Ltd	Yes.
Shell Limited	Given the contract is short-term, transfer mechanisms may not be necessary unless the contracts themselves are intended to be traded.
Vector Limited	Yes, consent not to be unreasonable withheld.

Q20: Do you agree that the Gas Industry Co should make the standard contract available for use (once the feedback from this discussion paper has been considered and incorporated)? If not, what alternative path forward would you prefer and why?	
Contact Energy Ltd	Contact agrees that it would be helpful for the GIC to make available a contract that could be used for short-term gas trades. It may also be helpful for the GIC to seek comments on its proposed standard contract before the standard contract is offered by the GIC. The more the standard contract is attuned to the needs of gas market participants the more likely it will be used.
Genesis Energy Ltd	Yes. As a matter of good practice, the Gas Industry Company should also invite and accept proposals for changes on an ad-hoc basis and be prepared to issue new versions if significant issues arise.
Mighty River Power Ltd	Yes
Major Electricity Users' Group	Yes
Multigas NZ Limited	Yes – As it would provide a good starting point from which parties negotiate terms for a final contract allowing the incorporation of flexible parameters under the bi-lateral platform philosophy that has been unanimously agreed by the industry participants.
PHI Developments Ltd	Yes.
Shell Limited	The development and availability of a Model Contract will of course be useful to establish and promulgate the standardisation and protocols necessary to support the wholesale market.
Vector Limited	Yes

Q21: Do you agree that a platform should extend the compliance regime being developed by the Gas Industry Co in order to keep costs to a minimum? If not, what alternative would you prefer and why?	
Contact Energy Ltd	The form of compliance regime that the GIC is developing is unclear. Until that is clear it is difficult to determine whether use of the proposed compliance regime to manage the proposed platform is appropriate. Contact, nevertheless, supports an approach that minimises costs. Indeed Contact considers it inappropriate to proceed to develop a platform until it is clear what costs will be incurred in that development and until it is also clear how those costs will be recovered. We also question whether it is necessary to have a compliance regime associated with a matching platform because, we assume that no rights or obligations would be created until the bilateral contract was executed. It seems that a matching platform could be as simple as a standard email sent to parties interested in trades and advising fundamentals such as price, quantity and term.
Genesis Energy Ltd	With respect to the two aspects of the compliance regime, Genesis Energy is of the view that the governance regime discussed in this section of the discussion paper should extend only to the operation of the platform (i.e. enforcement of the platform governance rules) and not to the deals themselves (i.e. enforcement of the bilateral trades). Genesis Energy reserves its position as to whether the compliance regime currently being developed by the Gas Industry Company is appropriate for governance of the operation of the trading platform until the details (and in particular the specific rules that would be applied) are made available.
Mighty River Power Ltd	It is difficult to answer this question prior to seeing the GIC's compliance regime Regarding 7.1 the seller may be willing to sell part of a gas parcel rather than only the whole parcel. Consideration should be given to allowing this as an option for the seller.
Major Electricity Users' Group	Yes
Multigas NZ Limited	Possibly.
PHI Developments Ltd	Yes.

Shell Limited	No comment.
Vector Limited	Yes

Q22: Do you agree that the preferred approach to prudential management is the white-list? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Balancing the need to ensure trades do not involve unacceptable financial risk whilst ensuring trades are not unnecessarily restricted is difficult particularly when the financial exposures across trades could vary widely. Contact agrees that the white-list appears the preferred approach but the approach should be carefully designed to avoid any unnecessary limit on trades.
Genesis Energy Ltd	Yes.
Mighty River Power Ltd	Generally agree with the white-list approach. However it may also be of benefit to allow parties to disclose their financial details (as in the frosted glass approach). This may benefit a new entrant or a company that does not make public financial reports.
Major Electricity Users' Group	Support in principle but prudential requirements can be anti-competitive or barriers to participation. Further consideration is necessary.
Multigas NZ Limited	We are not entirely convinced that this "White List" option should be the base method from which the prudential criteria is based upon. Prudential qualification based on "face value preference" does not necessarily mean that a party will meet its commitments or obligations. A combination of the White Lines and the Minimum prudential standards may represent a fairer landscape for development on this issue. Either way Prudential needs to be applied responsibly and conscious of any restriction it may have governing entry to participate in the gas market. It is important to recognise that in any trading situation parties have to be prepared to accept the risk of doing business and not transfer this risk by way of prudential requirements to trading partners. There needs to be a responsible attitude applied to the amount of prudential support required in each situation.
NZX	The While list is a workable situation and technology is available to only allow trading with a participant on your list. This list can either be updated daily or trade dynamically. However, to encourage non-physical players a fully cleared market with central counter-party would be preferable.
PHI Developments Ltd	No. A matching platform that facilitates transactional efficiency is one where bids and offers reflect only the inherent commodity value of the gas. To achieve this end, specifications for the gas must be consistent, and prices must not include any risk premium related to the ability of a counterparty to perform. Minimum prudential standards are required to ensure transactional efficiency of a matching platform. If the minimum prudential standards greatly restrict the number of counterparties able to use the matching platform, then another market structure (brokers, for example) should be considered.
Shell Limited	We have no additional suggestions at this time.
Vector Limited	Yes although with limited players in the gas market selective criteria applied to the white list should be overly onerous or specific. Even the blacklisted participants may become attracting to white listed players given the appropriate price incentive.

Q23: Do you agree that the platform should allow participants to nominate their preferred location for making offers or bids (provided this does not add undue cost to a platform development)? If not, what alternative would you prefer and why?	
Contact Energy Ltd	Contact agrees that trading is much simpler at Maui receipt points and delivery points. In order to simplify the standard contracts it may be preferable to limit trading to those points. This would increase the reason for Vector to introduce a similar regime to the MPOC. There is an opportunity to achieve that through the consultation that Vector has agreed will take place in 2007. We note that Vector's requirement that pipeline capacity should be purchased annually limits the ability to effect short-term trades at Vector pipeline delivery points. Contact acknowledges that restricting trading to Maui receipt points and delivery points may at least initially limit the usefulness of the platform.
Genesis Energy Ltd	Yes, but be limited to Maui welded points.
Mighty River Power Ltd	Would not the origin of the gas need to be disclosed? If gas from Maui is sold at Rotowaro and the purchaser is delivering that gas to Frankley Rd the physical gas would not be transported to Rotowaro and then back to Frankley Rd. It makes sense to only pay for transportation between the origin and the delivery point and no further. Note that gas cannot be on-sold at Oaonui because it is currently only a delivery receipt point.
Major Electricity Users' Group	Yes
Multigas NZ Limited	We broadly agree with this method. The logistic obviously would need to be carefully managed.
NZX	Other successful markets have the concept of a notional balancing point for trading. The adoption of such a concept in New Zealand would be positive for liquidity.
PHI Developments Ltd	No. An efficient market is characterised by transparent prices and narrow bid-offer spreads. Increasing market liquidity is one of the most effective ways to increase market efficiency. Market liquidity can be increased by encouraging all transactions to take place at the same location. Transportation requirements can, and should, be negotiated separately.
Shell Limited	No, establishing proper trading locations is an important step in defining and establishing a viable trading market. While primary trading between producer and shipper is manageable at an injection point, secondary trading at injection points is likely to be unworkable and not conducive to the cost effective development of scalable gas trading platform. Development costs will be predictable only if specific trading locations are established remote from injection points and delivery points (other than major exchange points between interconnected pipeline systems, i.e. Rotowaro, Frankley Road).
Vector Limited	Yes

Q24: Do you consider the indicative cost ranges for the matching platform to be reasonable? If not, what amendments would you propose and why?	
Contact Energy Ltd	We are uncertain whether these estimates are reasonable. This is largely because the design specification of the matching platform is undeveloped. The source and justification for the cost estimates set out in Appendix H are not identified so that it is difficult to judge whether or not these are informed estimates. Based on Contact's experience of the cost of other internal and external customised IT developments the costs of IT projects can vary widely depending on the level of functionality and specialisation of the development. At one end of the spectrum of functionality, it should be possible to construct a matching platform that involves little more than designing a standard email to send to a list of market participants who have indicated interest in gas trade. That would involve virtually no costs. Another option would be to develop a website to publish trade opportunities. We believe the cost of that would also be negligible. We are aware of examples of matching platforms that have been developed at low cost and have satisfactory functionality. An example of that is Energyhedge which was developed relatively cheaply and possibly could be built on to meet the requirements of a gas market. Contact suggests the CIG should consider, at least initially, developing one of these very low cost options.
Genesis Energy Ltd	The indicative costs appear to be consistent with the cost of developing the electricity hedge market platform, and therefore reasonable. However, Genesis Energy is interested in the specific nature of the controls that the Gas Industry Company intends to place on such costs to ensure that they come within these ranges if the matching platform is developed.
Mighty River Power Ltd	We are cognisant of the many examples of cost “blowouts” in IT costs in the energy industry. We would be pleasantly surprised if the actual cost was within the suggested range.
Major Electricity Users’ Group	Yes
Multigas NZ Limited	Yes.
PHI Developments Ltd	Not able to comment.
Shell Limited	It is too early to tell. Costs should again be estimated after further design work has been completed, and interaction with existing gas delivery systems more clearly defined.
Vector Limited	It’s often hard to determine the exact cost of an IT platform if the exact design and scope is not entirely known. However the functionality is relatively simplistic so the medium to high case scenario would seem reasonable. Vector is keen to know how the GIC intends to fund the platform and allocate costs. Will this be funded out of levies? How is the ongoing cost to be paid for, per trade? Per GJ ?

Q25: Do you consider the indicative benefit ranges for the matching platform to be reasonable? If not, what amendments would you propose and why?	
Contact Energy Ltd	In light of the footnote concerning the proposed Australian bulletin board, the lack of any factual information supporting the calculations of benefits in Appendix H and that Appendix L indicates that there are only nine active short-term traders whose trades usually have a duration of between 1 to 6 months we are uncertain whether the quantified benefits set out in Appendix H are reasonable. In attempting to calculate the benefits of a matching platform the following matters require further consideration: • generally longer duration trades will be more customised for specific circumstances making a standard contract less useful for such trades; • the market is currently in a transition from long term stable contracts with a high level of flexibility to shorter term inflexible contracts and that growing inflexibility may generate more short-term trades; • until the market starts to experience the impact of inflexibility it is very difficult to assess the likely volume of trades; • because of the lack of participants and because users' requirements are dominated by one market, the electricity market, opportunities for trade will inevitably be very limited; and • we do not understand why the benefits of a matching platform should be substantially lower than the benefits of a trading platform. That conclusion seems based on the assumption that near real time trades cannot be effected using a matching platform. That assumption appears questionable.
Genesis Energy Ltd	Genesis Energy has no basis on which to make a judgement as to the reasonableness or otherwise of the benefit ranges but consider that the benefits of a matching platform are likely to be sufficiently great to warrant its development provided that the costs are within the indicative ranges referred to in the previous section of the discussion paper.
Mighty River Power Ltd	The value will greatly depend on the market liquidity, which is difficult to forecast. Given the purported difference between Maui gas prices and Pohokura gas prices, a $0.02/GJ benefit from the platform could well be a significant underestimation.
Major Electricity Users' Group	Yes
Multigas NZ Limited	They are reasonable but need to be measured against comparable other options that offer the same or better outcomes.
PHI Developments Ltd	As stated in 7.33, "it is impossible to verify whether this present value estimate is accurate". Rather than justifying the creation of a platform by estimating "improvement in pricing accuracy", it is suggested that consideration focus on qualitative benefits.
Shell Limited	At this stage it is difficult to assess, and market response is probably underestimated.
Vector Limited	7.33, states that "it is impossible to verify whether this present value estimate is accurate". Vector would agree as there are far too many variables to provide any quantitative certainty.

Q26: Do you support the conclusion that it would be reasonable to proceed with development of a matching platform, provided it can be progressed at modest cost? If not, what path forward would you propose and why?	
Contact Energy Ltd	As indicated, Contact is uncertain about the reliability of the assessed costs and benefits of a matching platform set out in the Discussion Paper. This partly arises because of the lack of attribution of those estimates. Contact supports the GIC's proposal to better assess those costs and benefits before deciding whether to proceed with expending resources on developing a platform. Contact supports the initial development of a platform at low cost. As indicated above we think that appears possible. The GIC should exercise caution in developing a platform on a shoestring if that is likely to cause the project to fail. That could cause the market to discredit development of a trading platform. We don't think that should happen if initially the matching platform was made extremely simple, transparent and low cost with users having a clear understanding of its limitations. Therefore Contact considers a preferred approach is: • to develop an agreed standard contract, • to offer an extremely simple matching platform such as a website; • proceed to develop a more highly specified platform when the take up of the standard contract has been reasonably assessed, the limitations of the simple arrangements are understood, the benefits of a more highly specified platform can be determined and the impact of more inflexible contracts is clearer. That approach would allow proper assessment of the costs and benefits and better specification of the platform required to meet market participants needs. It would also provide adequate opportunity for Vector and users of its pipelines to resolve the form of the regime it will implement from 1 October 2007 and so enable implementation of a platform better designed to meet market needs.
Genesis Energy Ltd	Yes, provided that the costs prove to be modest, budgets are managed and industry participants are involved in developing the system specification, its development and testing. One issue of direct relevance to the reasonableness or otherwise of the conclusion to proceed with the development of a matching platform is the impact, if any, of any alternative trading platforms. The Gas Industry Company will be aware that since the publication of its discussion paper, that Greymouth Petroleum has announced its plans to commence an internet-based spot market for gas from its Turangi filed in Taranaki. While Genesis Energy can only speculate as to whether this market will eventuate and if it does its level of success and ability to deliver on Government Policy Statement objectives, Genesis Energy urges the Gas Industry Company to monitor this development closely given its potential impact for the success or otherwise of the Gas Industry Company's platform and therefore the degree of effort required by the Gas Industry Company.
Mighty River Power Ltd	Yes.
Major Electricity Users' Group	Yes
Multigas NZ Limited	If there is a general consensus from industry participants that this is the way forward then it is worth considering. However, the parameters and definitive outcomes need to establish and agreed by the participants before investment is undertaken.
NZX	Yes, but ensure that any solution chosen could easily grow into a full trading platform in the future.
PHI Developments Ltd	If a majority of potential industry participants agree to fund the matching platform, then it would be reasonable to proceed with development. It is should be understood, however, that the platform may not able be able to achieve the same level of liquidity as other market structures (i.e.; a broker market).
Shell Limited	We support some additional design work before proceeding to development. It is not apparent that the ideas are sufficiently mature to maximise the benefit of working with arrangements already developed.
Vector Limited	If costs are kept to a minimum Vector would see the platform as beneficial.

Q27: Do you consider the indicative cost ranges for the trading platform to be reasonable? If not, what amendments would you propose and why?	
Contact Energy Ltd	It is difficult to assess whether the cost ranges are reasonable given the lack of specification of the trading platform and the lack of detail and justification for the estimates in Appendix I. If OATIS already incorporates the ability to function as a trading platform then the costs, may be over stated. We note, however, that the reduction in costs, attributed to a reduced number of trades, may not be realised as we imagine it probably costs about the same to build a trading platform for 10 participants as for 50 participants.
Genesis Energy Ltd	Genesis Energy currently has no basis on which to make a judgement and considers this will be able to be better estimated after the industry has had a reasonable period of experience with the matching platform.
Major Electricity Users' Group	Yes
Multigas NZ Limited	Yes
NZX	It appears very expensive in our experience. On the condition that there is a system operator in place, a system to allow trading up to gate closure could be built for substantially less than indicated.
PHI Developments Ltd	Experience has shown that it is common to underestimate the scope and cost of gas related information and trading systems.
Shell Limited	The platform requires additional design work, we are not clear as to how it works with existing gas delivery mechanisms. Costs could be reasonable if only a few trading points are selected. If multiple trading points are defined, costs could be substantial.
Vector Limited	Please refer to Q24 & 25

Q28: Do you consider the indicative benefit ranges for the trading platform to be reasonable? If not, what amendments would you propose and why?	
Contact Energy Ltd	It is difficult to assess whether the estimated cost benefits are real. It is not easy to understand why the difference in benefit between a matching platform and a trading platform should be so large. But this difference seems primarily because of the assumption that a matching platform cannot allow near real time trading whereas a trading platform is able to provide that. We question that assumption. Assuming a suitable ex ante standard agreement is in place there seems to be no reason why a matching platform could not allow near real time trading. We also note that as yet there is uncertainty about how contingencies are managed and rights and obligations in such circumstances. Until that is resolved it is difficult to assess how participants in gas markets will manage their exposures during such events and to assess the value associated with near real time trades.
Genesis Energy Ltd	Genesis Energy currently has no basis on which to make a judgement and considers this will be able to be better estimated after the industry has had a reasonable period of experience with the matching platform. Genesis Energy does not currently consider that such a platform is warranted.
Mighty River Power Ltd	If we were to guess the difference in economic benefit between a matching platform and a trading platform we would attribute more value to the matching of participants and the potential price discovery that a platform could provide and less value to benefit of being able to trade in real time. In other words the benefit of the matching platform seems understated in the GIC paper and the difference between the benefit of the trading platform and the matching platform seems overstated.
Major Electricity Users' Group	Yes
Multigas NZ Limited	Yes.
PHI Developments Ltd	No. Benefit analysis should not rely on concepts as esoteric as "price inaccuracy". Instead of investing funds in a theoretical end state, put sufficient rules and tools in place and let the market evolve naturally.
Shell Limited	At this stage it is difficult to assess, and market response is probably underestimated
Vector Limited	Please refer to Q24 & 25

Q29: Do you support the conclusion that it would be risky to proceed with development of a trading platform due to uncertainty over net benefits, but that it would be worthwhile to seek to narrow the uncertainties, and in particular to examine the costs and benefits of making the pipeline imbalance pricing mechanisms more responsive and dynamic? If not, what conclusion would you draw and why?	
Contact Energy Ltd	Inappropriate to progress the development of a trading platform at this time. Contact believes further work on developing a trading platform should not be progressed until: • the impact of the full balancing regime of the MPOC is understood; • the regime applying on Vector pipelines is settled; • the uptake of the proposed standard contract has been assessed; • contingency arrangements are in place; • the level of participation in trading market becomes clearer; and • the use of a simple matching platform has been assessed.
Genesis Energy Ltd	Yes. This is not relevant at this point in time. Given the history of the OATIS development (still ongoing) we have major concerns about automated systems development. Genesis Energy strongly recommend that no work is commissioned in this area until the industry has a reasonable period of experience with the matching platform (assuming it is developed). Genesis Energy do not see the need to automate the linkage with transmission arrangements for example. Depending on the delivery point of a trade the buyer is likely to want the option to re-optimise its overall transmission plan across its portfolio of gas supply and transmission contracts.
Mighty River Power Ltd	It would be risky to proceed with development of a trading platform at this point. Although the transmission system is balanced on a daily basis under the MPOC, in reality the transmission system is still balanced on pressure (i.e. by increasing and decreasing the flow from Maui in reaction to changes in pipeline pressure). An outcome is that "calls" for balancing gas only occur periodically and are used more for balancing the books than the pipeline. This may or may not continue beyond the conclusion of the legacy Maui gas contract in June 2009. If balancing by pressure will continue, investigating more responsive imbalance pricing mechanisms may be of little value. It is suggested that this is assessed prior to further study.
Major Electricity Users' Group	Agree with need for further work, analysis and consideration.
Multigas NZ Limited	We agree with the concept but require more information before giving a definitive answer.
NZX	It would be preferable to build the matching platform at this stage and then evolve into a complete trading platform once there is more certainty.
PHI Developments Ltd	Yes.
Shell Limited	More detailed design work is required. Decisions are needed on defining trading points. Costs will depend on the selection of appropriate trading points, and the extent to which market mechanisms build on gas delivery, allocation standards and protocols already established under MPOC.
Vector Limited	Yes

Q30: Do you consider the quantitative assessment methodology to be reasonable? If not, what amendments would you propose and why?	
Contact Energy Ltd	The context of this question is not clear because it does not seem to have been included in the body of the Discussion Paper. However, as indicated above Contact is uncertain that the quantitative analysis is correct because of: • the lack of specification of both the matching platform and the trading platform; • the lack of consideration of simple low cost matching platform; • the lack of analytical detail; • the lack of attribution of the cost estimates; and • Contact's experience of the costs associated with customised IT projects. Contact is also doubtful of the benefits identified in the quantitative analysis because of: • the lack of analytical detail; the comments related to the proposal to implement a trading bulletin board in some Australian states; and The wide difference in the assessed benefits of a matching platform and a trading platform. Because of the above doubts it is difficult to agree that the quantitative analysis provides sound grounds to progress either the matching platform or the trading platform. As indicated we think an appropriate approach is to complete and publish the standard contract, to test the market place uptake of that and to proceed with development of a very simple low cost matching platform. That will enable better specification and implementation of a more highly specified platform once the cost and benefits show that is appropriate.
Genesis Energy Ltd	Genesis Energy does not consider the quantitative assessment methodology applied by the Gas Industry Company to the calculation of net benefits, nor the assumptions used, to be unreasonable. However, while the methodology itself appears to be robust, as noted above, Genesis Energy urges the Gas Industry Company (as it itself notes in paragraph 7.45) to assure itself and industry participants that the indicative net benefit calculation remains robust as the various component-parts of the calculation crystallise.
Mighty River Power Ltd	See Q.28
Major Electricity Users' Group	Yes
Multigas NZ Limited	It seems the Quantitative assessment methodology is too rigid. We believe it possibly contains the process and lessens flexibility. For this reason we don't believe it's reasonable in its current format. We refer to our answer to Q2.
PHI Developments Ltd	No. Consistent with the objective of increasing transactional efficiency, it may make more sense to focus on qualitative benefits (for example, increased liquidity). From a qualitative point of view, it is not clear how the conclusion was reached in 10.10 that benefits could be constrained. All major gas producers and users need mid and back office functions to support their operating activities.
Shell Limited	Quantitative assessment is reasonable, but until design is more detailed, results are highly uncertain.
Vector Limited	Please refer to Q25