

31 May 2010

Jo Murray
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Dear Jo

Review of Vector Interconnection Arrangements against Gas Act and GPS objectives

On 2 December 2009, Gas Industry Co wrote to you about our September 2009 review of Vector's interconnection arrangements. A copy of the review was attached to the letter. We indicated areas of Vector's interconnection arrangements that could be developed to better align with Gas Industry Co's February 2009 *Transmission Pipeline Interconnection Guidelines* (the Guidelines).

In December 2009, Gas Industry Co wrote to the Associate Minister of Energy and Resources, the Hon Pansy Wong, to update her on the results of the review. We notified her that progress, while slow, was being made and a further review should be held in June 2010. We suggested this review assess the transmission system owners' interconnection arrangements against the Gas Act 1992 (Gas Act) and Government Policy Statement on Gas Governance (GPS) objectives. If the review were to show the arrangements fall short of meeting the objectives, the next step would be for Gas Industry Co to consider options for addressing these shortcomings.

The Associate Minister accepted our advice and indicated that, if necessary, Gas Industry Co make a statement of proposal by the end of the year.

As discussed with you, part of the review of Vector's Interconnection Arrangements against the Gas Act and GPS objectives will take the form of an interview. I would like to confirm this interview will take place on Monday June 21, 2010 from 2.15-4.45 pm at Gas Industry Co's offices. In preparation, I have attached some questions for you to consider in advance. I have also attached the evaluation criteria for the review. If you have any supporting documents it would be helpful if you can send them to us before the interview; alternatively, you can bring them to the interview.

Yours sincerely

Melanie Strokes

Adviser – Infrastructure Access Group

On behalf of Ian Wilson

Attached: Review Questions and Evaluation criteria for interconnection review

Review questions

On the basis of the evaluation criteria we have developed (attached for your reference), we will ask you the following questions at the review.

Safety and Reliability

Do Vector's interconnection arrangements:

1. specify technical standards for interconnection equipment, including by covering the design, construction, commissioning, testing, and operation of those assets?
2. provide a clear process for agreeing and maintaining the operational parameters (such as minimum and maximum delivery pressure and the operating flow range)?
3. provide Vector the ability to reject arrangements that would adversely affect the safety or the long-term integrity of the pipeline, or the pipeline's certificate of fitness?
4. assign responsibility for design and approval activities?
5. identify risks and assign liability for losses associated with those risks? If so, what are the risks and how is liability assigned?
6. place liability with the party who has the ability to control the risk?

Efficiency

Do Vector's interconnection arrangements:

7. provide open access to the gas transmission system for new interconnections?
8. identify the principles and standard terms and conditions for an interconnection? In what ways are these terms and conditions consistent with the objectives of the section 43ZN of the Gas Act?
9. identify the overall process steps, milestones, and criteria for progressing the interconnection process?
10. identify the personnel responsible for contract negotiation?
11. set reasonable timeframes and deadlines for commercial negotiations and technical reviews?
12. support the use of existing infrastructure, subject to technical suitability?
13. not needlessly duplicate facilities?

14. allow matters in dispute to be referred to a suitable decision maker (for example, technical expert)?
15. allow TSOs to recover reasonable costs incurred?
16. not socialise costs unless there are social benefits?
17. promote contestability for the design and construction of equipment to provide downward pressure on cost, unless there are compelling technical or legal reasons against doing so?
18. allow for the independent negotiation of transportation arrangements; unless both parties agree there are compelling technical reasons to negotiate both arrangements together?
19. publish an interconnection policy including details of its interconnection process, information requirements, pro-forma contracts, policies and standards, technical review, principles, commercial prerequisites, and a dispute resolution process?
20. provide an interconnecting party with sufficient information to enable it to assess the likely availability of transmission capacity to or from the interconnection point?
21. provide a suitable dispute resolution process, which is available to both parties throughout the interconnection process?

Evaluation criteria for Interconnection Review

Gas Industry Co, as the 'industry body', may recommend gas governance regulations for this purpose and must consider the objectives specified in section 43ZN of the Gas Act. The principal objective is to:

ensure gas is delivered to existing and new customers in a safe, efficient and reliable manner

Other objectives specified in section 43ZN of the Gas Act are to:

- facilitate and promote the ongoing supply of gas to meet New Zealand's energy needs by providing access to essential infrastructure and competitive market arrangements;
- minimise barriers to competition;
- maintain and advance incentives for investment in gas processing facilities, transmission and distribution;
- ensure delivered gas costs and prices are subjected to sustained downward pressure;
- ensure risk relating to security of supply, including transport arrangements, are properly and efficiently managed by all parties; and
- maintain consistency with the Government's gas safety regime.

Criteria for evaluating interconnection arrangements

To derive useful criteria for evaluating interconnection arrangements, we must consider what the Gas Act objectives would require in that context. We consider interconnection to be an integral part of the gas supply chain, and thus find that the principle objective provides guidance as to a broad classification of the evaluation criteria. Since safety and reliability are closely related we will classify the evaluation criteria under the categories of:

- safety and reliability; and
- efficiency.

Within each of these categories we consider the other objectives listed in section 43ZN of the Gas Act and what they imply for interconnection arrangements.

- where interconnection issues are bundled with gas transport issues (see 'Independence' below).

Contestability

Providing contestability, where appropriate, is an efficient means of providing competition and therefore supports the objectives of providing downwards pressure on pricing and minimising barriers to competition.

Although interconnection is a process involving an access seeker and a TSO, some aspects of that process do relate to competition in related markets. For example, delayed interconnection can negatively affect competition in upstream gas markets. Competition in the market for constructing interconnection facilities may be reduced if that work is not contestable. These outcomes would mean associated costs are not subject to competitive pressure.

Independence

Independence of interconnection and transport arrangements supports the objective of providing access to essential infrastructure and competitive market arrangements. While there may be technical reasons to negotiate these arrangements co-dependently, ensuring this co-dependency does not create a barrier to competition is an important consideration (See also 'Costs' above).

Innovation

Technical and commercial innovation, such as the specification of metering equipment, supports the objectives of providing downwards pressure on pricing and minimising barriers to competition.

Clarity of process

A clear process, with defined responsibilities and timelines, contribute to the objectives of providing incentives to invest and to achieve the lowest cost and shortest time to completion.

Enforcement

Without a means of enforcement, interconnection arrangements cannot reliably achieve the objectives and it is therefore an important evaluation criterion. Enforcement includes contractual and regulatory means of achieving compliance with the Gas Act objectives, and a process for resolving disputes.

Table 1 summarises the evaluation categories, and the relevant evaluation criteria within these categories.

- provide TSOs the ability to reject arrangements that would adversely affect the safety or the long-term integrity of the pipeline, or the pipeline's certificate of fitness.

Responsibility and liability

Interconnection arrangement should clearly define responsibilities and associated liabilities for all activities and approvals throughout the interconnection process. In particular, interconnection arrangements should:

- assign responsibility for design and approval activities;
- identify the personnel within each organisation who are responsible for contract negotiation;
- identify risks and assign liability for losses associated with those risks; and
- place liability with the party that has the ability to control the risk.

Efficiency

Access to essential infrastructure

- Interconnection arrangements should allow a party to access the transmission pipeline, subject to reasonable terms and conditions that are consistent with the objectives listed in section 43ZN of the Gas Act. To achieve this, interconnection arrangements should: provide open access to gas transmission pipelines;
- identify and publish the terms and conditions for providing access; and
- ensure that the terms and conditions are reasonable and consistent with the Gas Act objectives.

Cost

Interconnection arrangements should help to ensure that costs and prices are subject to sustained downward pressure. A TSO's arrangements should enable interconnections to take place as quickly as possible and at the least possible cost. To achieve this, interconnection arrangements should:

- identify the principles and standard terms for an interconnection;
- identify the overall process steps, milestones, and criteria for progressing the interconnection process;
- set reasonable timeframes and deadlines for commercial negotiations and technical reviews;
- support the use of existing infrastructure, subject to technical suitability;
- not needlessly duplicate facilities;
- allow matters in dispute to be referred to suitable decision maker (eg technical expert);

- require TSO's to publish an interconnection policy including details of its interconnection process, information requirements, pro-forma contracts, policies and standards, technical review, principles, commercial prerequisites, and a dispute resolution process; and
- require TSO's to provide an interconnecting party with sufficient information to enable it to assess the likely availability of transmission capacity to of from the interconnection point.

Enforcement

Interconnection arrangements should have a means of enforcement at all stages. This should include a suitable dispute resolution process, which is available to both parties throughout the interconnection process.

To counter the exercise of unequal bargaining power, a means of ensuring that the TSO's terms and conditions are consistent with the objectives listed in section 43ZN of the Gas Act is required.

To achieve this, interconnection arrangements should:

- set out the provisions for enforcement and dispute resolution; and
- provides dispute resolution processes that:
 - may be applied to a pre-contract dispute relating to the TSO's terms and conditions;
 - take place in a timely and economic manner; and
 - include a fair and effective escalation process.