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CONTACT ENERGY VTC CHANGE REQUEST: VECTOR WITHHOLDS CONSENT

Vector does not consent to the Change Request

- 1 The purpose of this letter is to inform you that Vector Gas Limited (*Vector*) does not consent to Contact Energy Limited's (*Contact Energy*) 6 May 2013 Vector Transmission Code (*VTC*) change request (*Change Request*).
- 2 Below we give our reasons for withholding consent.

Reasons for withholding consent

- 3 Vector is aware that the VTC provides that Vector's consent to a change request shall not be unreasonably withheld.¹
- 4 Vector has good reasons for not consenting to the Change Request. We explain these reasons below, but, in summary:
 - 4.1 the problem that the Change Request purports to address does not in fact exist;
 - 4.2 the Change Request will create an inefficient change process which, among other things, will increase the cost for all parties and is likely to unnecessarily increase the Gas Industry Company's (*GIC*) workload;

¹ Clause 25.5(b), VTC.

- 4.3 the Change Request will undermine the ability of the parties to the VTC – a commercial contract – to negotiate varied terms;
- 4.4 the Change Request will hinder and potentially halt the implementation of wide ranging market reforms, such as those recommended by the Panel of Expert Advisers; and
- 4.5 the Change Request will create ambiguity and uncertainty around what a “single issue” or “related series of issues”, and this will result in more disputes.

No problem to be fixed

- 5 Vector is aware of the risk that the ability to propose package change requests (i.e. those dealing with multiple issues, not necessarily related) could be taken advantage of. However, the GIC is alive to the potential issues in dealing with package change requests and has managed the issues effectively in the past without an amendment to the VTC to restrict what change requests parties can and cannot make.
- 6 We have in mind the way the GIC dealt with Maui Development Limited’s (MDL) 17 October 2009 change request. In that case, the wide-ranging nature of the change request made it difficult for the GIC to assess its net benefit and it was not supported because of the uncertainty in the assessment. We expect the GIC will continue to manage change requests in a similar way, although we do note that if all proposed amendments in a package change request are clearly positive, the GIC should have little problem in supporting the change request. The key is that the GIC is alive to this issue and is dealing with it in a common sense way.
- 7 It seems that the trigger for the Change Request is Vector’s 27 November 2012 change request which proposed amendments to the VTC balancing arrangements. If that change request is the sort of perceived problem that Contact Energy is seeking to address, then we are strengthened in our view that there is no problem to be fixed. As we explained in our submission on the GIC’s draft recommendation supporting that change request, the amendments were aimed at maximising the efficiency of the new balancing arrangements, and were clearly related:²

The gains in efficiency will be generated by a set of balancing arrangements that implement a causer pays objective. Thus, the arrangements:

- (a) ensure that balancing costs are more accurately allocated to those parties whose actions (or inactions) cause the balancing costs. This is achieved by the amendments to replace the ILON process with a B2B process and also modifying the VTC to include the MPOC Peaking Charge; and
- (b) ensure that those parties allocated balancing costs are unable to avoid or delay paying those costs. This is achieved by limiting the scope for disputing invoices relating to balancing to circumstances where there is a manifest error.

² Vector Submission on Draft Recommendation on 27 November 2012 VTC Change Request (Balancing) (25 March 2013), pp. 1-2.

Change Request will create inefficient change process and increase cost

- 8 While we see no gain to be made from the Change Request which seeks to address a non-existent problem, there will be a number of costly consequences.
- 9 Most obviously, parties will incur greater costs in needing to formulate and assess a greater number of change requests. This is extra cost that is simply not necessary.
- 10 The workload of the GIC is likely to also increase. Each change request appealed to the GIC requires the GIC to set an agenda, receive submissions and cross submissions, evaluate the change request, and write draft and final recommendations. The Change Request is likely to increase that workload by multiples. This would result in increased costs and the diversion of scarce resources, and also longer timeframes for change requests to be assessed.
- 11 In summary, the change process provided for in the VTC would become more inefficient and costly, for no certain benefit.

Change Request will undermine the ability of parties to a commercial contract to negotiate varied terms

- 12 The Change Request would undermine the nature of the VTC as a commercial contract. In a commercial contractual relationship, parties are free to negotiate varied terms. There is no restraint on what changes they can seek. The key is that parties have the freedom to suggest changes and make the trade-offs that are typical of commercial agreements.
- 13 Progress in a commercial context can be made by agreeing a package of unrelated changes that is acceptable overall to each party. This option should be available with the VTC. By constraining change requests to "single issues" or a "related series of issues", parties to the VTC would lose the ability to advance trade-off solutions.

Change Request will hinder and potentially halt wide ranging market reforms

- 14 The Change Request would undermine Vector's ability to implement wide ranging market reforms, such as those likely to be required following any Panel of Expert Advisers (PEA) advice.
- 15 Vector expects that implementing such reforms would require multiple change requests, as the reforms would cover a number of discrete parts of the VTC. In the first instance, this will hinder the progress of the reforms by requiring large amounts of work to draft the change requests and, as would likely be the case, to be assessed by the GIC.
- 16 More fundamentally, it is possible that splitting up market reforms into multiple change requests would mean that the net benefits test could not be satisfied. The interdependent relationships between different amendments can generate the benefits – some amendments will simply not show benefits if their relationship with other amendments is arbitrarily severed by the requirement that change requests be limited to a single or related series of issues.

Change Request creates ambiguity and uncertainty – disputes will result

- 17 Finally, we believe the wording of the Change Request is ambiguous, and will only give parties another opportunity to raise disputes.

18 Reasonable parties will differ on where they draw the line between single and multiple issue requests. For example:

18.1 was Vector's 9 November 2010 "Typos" change request "multiple issue" because it addressed (albeit in a minor way) alignment of the Code with the requirements of the Gas (Downstream Reconciliation) Rules 2008, correction of several minor errors in the Code and clarification of inconsistencies regarding the requirement to have a Gas Transfer Agreement at an Inter-Pipeline Point?

18.2 as above, we don't believe our 27 November 2012 change request was a multiple issue request, but understand others believe it to be;

18.3 would Vector be able to save time and money by including some minor drafting clarifications in an otherwise unrelated change request?

18.4 would change requests be able to cover multiple sections of the VTC e.g. changes to section 4 (Capacity Reservation) and section 16 (Invoices and Payment) or would there need to be a separate change request for each section?

19 Disputes over the application of the "single issue" rule could be used tactically to frustrate the passage of efficiency-enhancing change requests.

The Change Request is inconsistent with the Gas Act and GPS objectives

20 In short, our view is that there is no benefit to be had from pursuing a change request which seeks to address a problem which does not exist, and which has a number of costly and inefficient unintended consequences. The increased costs that would arise from the Change Request are incompatible with the objective of efficiency, and for this reason, we consider the Change Request is inconsistent with the Gas Act and GPS objectives.

21 Ultimately, we find it compelling that the GIC has used common sense to successfully deal with this issue in the past, and we see no reason to cut across that by imposing an inflexible hard and fast rule about what change requests can and can't be made.

Yours sincerely,



Katherine Shufflebotham