



Final Recommendation on the MPOC Change Request proposed by MDL on 20 June 2008

Date issued: October 2008
Effective date: 11 November 2008





About Gas Industry Co.

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 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 paper was prepared by Ian Wilson

Enquiries: Ian Wilson
ian.wilson@gasindustry.co.nz
04 472 1800

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Introduction

Section 29 of the Maui Pipeline Operating Code (MPOC) assigns Gas Industry Co a role in respect of any proposed amendment to the MPOC (Change Request). Gas Industry Co has agreed a memorandum of understanding (MoU) with MDL describing how this role will be performed. The MoU sets out a process under which Gas Industry Co receives a Change Request, calls for submissions, issues a draft recommendation, considers further submissions, and finally makes a recommendation to MDL. For further information (including a copy of the MoU) please refer to Gas Industry Co's website at www.gasindustry.co.nz.

The purpose of this paper is to make a final recommendation to MDL in respect of a Change Request proposed by MDL on 20 June 2008.

2 Process

The process followed by Gas Industry Co in consulting on and considering the Change Request was:

- 20 June 2008 Gas Industry Co received the Change Request from MDL.
- 24 June 2008 Gas Industry Co called for submissions on the Change Request.
- 15 July 2008 Close of submissions on Change Request.

Submissions were received from:

- Contact Energy Limited (Contact);
- Might River Power (Mighty River)¹;
- Vector Limited (Vector); and
- Maui Development Limited (MDL).

Late submissions were received from:

- Nova Gas Limited (Nova);
- Genesis Power Limited, trading as Genesis Energy (Genesis); and
- Greymouth Gas New Zealand Limited (Greymouth).

Although these submissions were late Gas Industry Co was able to consider them in the analysis section of its Draft Recommendation.

Subsequently, further late submissions were received from:

- Energy Direct NZ;
- Mighty River; and
- Todd Energy (Todd).

¹ This submission from Mighty River, dated 30 June 2008, simply stated that '...Mighty River supports the proposed changes.' However, it has subsequently come to light that this submission related to the 21 May Change Request and not the 20 June Change Request. Mighty River's actual submission on the Legacy Change Request was received later (dated 26 August 2008), and is considered here for the first time. It does not support the deletion of section 3 of the MPOC. Gas Industry Co apologises to Mighty River for the confusion.

Gas Industry Co was not able to consider these before issuing its Draft Recommendation on the Change Request, but has considered them in the analysis section of this final recommendation.

- 1 September 2008 Gas Industry Co released its Draft Recommendation on the Change Request and called for submissions.
- 22 September 2008 Close of submissions on Draft Recommendation. Submissions were received from:
- Genesis;
 - Mighty River; and
 - Vector.

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Draft Recommendation

In respect of the Change Request, Gas Industry Co's Draft Recommendation supported:

- deletion of the following parts of MPOC relating to Maui Legacy Gas:
 - all of section 3 apart from sections 3.2 and 3.3(b);
 - the relevant parts of the definitions in section 1.1;
 - parts of sections 2.1, 2.1(a), 2.1(b), 2.2, 2.14, 7.1, 7.3, 7.4, 12.9, 12.16, 14.1(a), 14.6, 14.7, 15.3(e), 15.6, 24.8 and 29.4(b)(iv);
 - all of sections 8.18(a), 8.18(b), 8.19(a), 8.19(b), 8.20(a), 8.20(b), 8.24(a), 8.24(b), 8.26(a), 8.26(b), 8.28(b), 8.28(c), 14.9, 14.10(b)(iii), 15.11, 16.1, 18.1(a), and 38.2;
- section 2.19 being amended to read as follows:

The Target Taranaki Pressure shall be between 42 and 48 bar gauge, except as may be required as a result of a Contingency Event, Force Majeure Event or Maintenance. MDL shall give each Shipper and Welded Party not less than 12 months notice if it proposes to change the Target Taranaki Pressure below 42 bar gauge or above 48 bar gauge and any such change may only be implemented through a Change Request in accordance with section 29;

- the deletion of section 2A.1(4) in the event that section 2A has not already been deleted in its entirety in response to the previous Change Request dated 21 May 2008 (May Change Request);
- the deletion of section 2.21; and
- in section 1.1 deletion of the words '(including the facilities connecting the Maui Gas production station at Oaonui to the Maui Pipeline).' from the definition of Welded Point.

All of the supported changes were marked up in a copy of MPOC available on Gas Industry Co's website (note that this document does not include changes proposed by Gas Industry Co in response to MDL's May Change Request).

4 Submissions Received

Previous Submissions Received on Change Request

Before discussing submissions on Gas Industry Co's Draft Recommendation, it is helpful to recall the content of submissions received in the first round of consultation (closed on 15 July 2008).

Gas Industry Co considered seven submissions on the Change Request in its Draft Recommendation. These submissions were received from:

- Contact;
- Mighty River;
- Vector;
- MDL;
- Nova;
- Genesis; and
- Greymouth.

Contact supported the Change Request, and considered that it was largely directed towards removing provisions from MPOC made redundant by agreement (between the Crown, Maui Mining Companies, Vector and Contact) that the Operational Balancing Agreement principles should apply for the allocation of Maui Gas taken under the Maui Legacy Contracts and removing provisions from MPOC that required MDL to give some priority to Maui Gas taken under Maui Legacy Contracts.

The submission received from Mighty River dated 30 June 2008 '... supporting the proposed changes' actually related to MDL's earlier May Change Request, not this Change Request. In fact Mighty River's later submission (which is considered in the Late Submissions Received on Change Request section below) did not support the deletion of section 3 of the MPOC until a means is found to manage Shippers' Mismatch risks.

Vector did not support the Change Request, largely on the basis that 'the removal of section 3 and references to Maui Legacy Contracts from MPOC should not occur until the wider dispute over the

issue and cashing-out of ILONs at Vector Transmission Welded Points was settled'. Gas Industry Co has received notification that settlement of these issues has now occurred.

Also, in relation to the proposed change to section 2.19 of MPOC, Vector believed that 12 months notice of any increase in the Target Taranaki Pressure was too short.

In its original submission, dated 17 July 2008, Nova stated that while it supports the objectives behind the removal of section 3 and other references to Maui Legacy Gas in MPOC it did not support the Change Request in its current form because it '... fails to address how pipeline balancing will occur in the absence of section 3'. In its supplementary submission, dated 23 July 2008, Nova proposed further changes to MPOC which it considered would provide the basis for more robust balancing arrangements.

Genesis supported the objectives behind the removal of the Maui Legacy Gas arrangements, including the provisions that relate to priority and retrospective allocations. Genesis noted the shortcomings of MPOC in relation to balancing arrangements, but on balance considered the Change Request should be recommended.

Greymouth objected to the proposed change to section 2.19 (relating to the Taranaki Target Pressure) on various grounds. In particular, it considered that an increase in the Taranaki Target Pressure should be subject to more rigorous debate than that under an MPOC Change Request as it is a fundamental parameter. It also noted that an increase in the Taranaki Target Pressure would require significant changes to its upstream plant. Greymouth did not comment on any other aspect of the Change Request.

Late Submissions Received on Change Request

Although submissions closed on 15 July 2008, late submissions from Nova, Genesis, and Greymouth were considered in Gas Industry Co's Draft Recommendation paper released on 1 September 2008. However, even later submissions received from Energy Direct NZ (dated 29 August 2008), Mighty River (dated 26 August 2008), and Todd (dated 29 August 2008) were not able to be considered. These last three late submissions are discussed here.

Energy Direct NZ late submission

Energy Direct generally accepted the proposed changes, however it believed that further work is needed to confirm that balancing would be adequately addressed in the absence of section 3 and other references to Legacy Gas.

Mighty River late submission

Mighty River supported the proposed amendments except for the removal of the section 3 provisions relating to the retrospective allocations of Maui Legacy Gas. It noted that:

‘The effect of removing section 3 of the MPOC would be to allow MDL to issue both Mismatch Notices to their shippers and Imbalance Limit Overrun Notices to their Welded Parties on a daily basis. The ultimate result of the issuing of these notices is that parties are required to correct their positions within periods of between 1 and 7 days or be faced with their positions being “cashed out”’.

Mighty River considered that this would expose Shippers to unreasonable, unacceptable and unmanageable risks until the industry agreed a methodology to allow Shippers to determine their daily balance positions (particularly for mass market deliveries). It described how Shipper estimation of Mismatch positions could lead to inefficient results. It also considered the setting of cash out prices, in the absence of a wholesale market, to be of concern.

Mighty River proposes that the removal of section 3 could be approved in principle but not implemented until the other balancing issues have been addressed.

Todd late submission

Todd supported the Nova submission, and similarly believed that, while the objective of removing references to Legacy Gas from the MPOC was desirable, the Change Request fails to address the wider balancing issues. Also, it believed MDL had no authority to submit a Change Request because:

- MDL had received no instruction from the owner of the Maui Pipeline to submit the Change Request;
- The proposed amendment had not been agreed by the MMCs; and
- Section 3 cannot be removed without a change to the Maui Gas Contract stating how Legacy Gas will be treated.

Submissions Received on Draft Recommendation

Genesis submission

Genesis supports the Draft Recommendation.

Mighty River submission

Mighty River points out the misunderstanding over its earlier submission (discussed above). Mighty River’s actual position is that it:

‘...is not opposed to the ultimate objectives of the MPOC with regards to daily balancing but we do not believe these can be achieved in any fair and equitable manner until the Industry agrees on a methodology that allows shippers to determine their daily balancing positions, in particular with regards to the downstream non time of use market. As we highlighted in our August submission, a gas retailer who supplies the retail non time of use market will be required to guess their mismatch position on a daily basis. The retailer will need to react to cash-outs with no information regarding their current mismatch position due to the lack of daily allocations’.

Vector submission

Vector rescinded its partial opposition to aspects of the Change Request on the basis of a series of settlement documents negotiated between Vector and MDL over ILON disputes. Vector also notes, and does not oppose, Gas Industry Co's amendments relating to Target Taranaki Pressure.

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Settlement of MDL-Vector Dispute

On 1 September 2008, MDL and Vector signed settlement and transition agreements in respect of their Imbalance Limit Overrun Notice (ILON) and Accumulated Excess Operational Imbalance (AEOI) dispute. The terms of this settlement and its significance to Gas Industry Co's final recommendation on the Change Request are discussed here.

Settlement arrangement

Under the transition agreement (Appendix A), a Transition Period is defined as the 30 Day period commencing when Gas Industry Co has made a recommendation supporting MDL's 20 June 2008 Change Request (MPOC section 29.4(a)), and MDL has given written consent to the Change Request (MPOC section 29.4(b)). On the Effective Date (the Day after the last day of the Transition Period), the MPOC, ICAs and TSAs will be amended to reflect the change, and the Running Operational Imbalance (ROI) and AEOI at each Vector Transmission Welded Point on the Maui pipeline will be reset to match the ROI and AEOI posted on the Vector Transmission OATIS in respect of the last Day of the Transition Period.

The transition agreement is intended to contain the dispute to the period before the Effective Date. However MDL and Vector have also agreed a settlement to the dispute, subject to MDL determining that there is an acceptable level of industry support for that settlement. In essence the settlement involves:

- all ILONs issued to Vector before the Effective Date being withdrawn/cancelled; and
- any ROI at Oaonui at the Effective Date being replaced with a Secondary Balancing Gas contract which will allow the MDL Commercial Operator to call on that gas at zero cost.

MDL is currently seeking support for the settlement from Maui pipeline users.

Significance of MDL-Vector settlement to this Final Recommendation

Vector's submission, dated 15 July 2008, on Gas Industry Co's Draft Recommendation considered that MPOC section 3 should not be removed until a settlement of the MDL-Vector ILON/AEOI dispute was achieved. If MDL can obtain sufficient support for the settlement from Maui pipeline users Vector's concern will have been met, and Vector would no longer object to the removal of section 3.

However, even if MDL cannot obtain sufficient support from its users, and the settlement agreement is therefore not consummated, the transition agreement will remain in effect. This will limit the dispute to the past, and allow an agreed AEOI starting position if the Change Request is brought into effect. In this way the benefits of a clean AEOI starting position will be obtained regardless of whether the dispute is settled. This should considerably enhance the benefit of a recommendation in favour of the Change Request since Vector will be able to pass through 'cash-outs' to its shippers. Balancing cost signals will then flow through to the parties who can best influence balancing outcomes.

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Gas Industry Co Analysis

Gas Industry Co considers that the matters raised in the three late submissions, which were not considered in the Draft Recommendation, were nevertheless generally addressed by the analysis in the Draft Recommendation.

In relation to concerns expressed in all three submissions that wider balancing issues should be addressed before Legacy Gas arrangements are considered, the Draft Recommendation noted that:

‘While Gas Industry Co welcomes submissions identifying issues that it should consider in respect of a Change Request, the fact that the June Change Request could have included additional improvements to the MPOC is not a ground for declining to recommend it. As discussed above, Gas Industry Co has had regard to the objectives specified in section 43ZN of the Gas Act 1992 and considers that the June Change Request is consistent with, and has aspects that further the objectives of the Gas Act. Accordingly, while Gas Industry Co values the feedback from Vector, Nova and Genesis regarding additional improvements to MPOC, Gas Industry Co cannot recommend that those changes be made in the context of the June Change Request. If submitters wish to pursue additional improvements to MPOC through the Change Request process, submitters should submit a separate Change Request.

Gas Industry Co notes that submitters are also welcome to suggest their view of a more robust balancing regime in the context of Gas Industry Co’s balancing work stream.’

In any event, it is very likely that the Legacy Gas arrangements will expire before Gas Industry Co could make any recommendation to the Minister of Energy in respect of the wider balancing issues. For this reason, declining the Change Request to wait for a more comprehensive solution to balancing issues is probably not a realistic option.

Gas Industry Co acknowledges that there are many shortcomings with current pipeline balancing arrangements, and that the removal of the Legacy Gas provisions will increase shippers’ balancing costs. The signalling of costs alone will not lead to efficient outcomes. Users also need good information systems to provide advice of day-to-day balance positions, and access to tools for managing those positions. The Legacy Gas arrangements have been a distortion which has obscured the real cost of balancing since the inception of Maui pipeline open access and discouraged the development of good information systems and balancing tools. The removal of these arrangements will allow users to put a value on further system enhancements, which is a step towards better future balancing arrangements.

In relation to Todd's first concern, that MDL has acted beyond its authority in submitting the Change Request, Gas Industry Co considers that matters of MDL's internal governance are best addressed by its shareholders.

In relation to Todd's second concern, Gas Industry Co notes that Todd as an MMC has not approved the proposed amendment. However, Gas Industry Co does not know what weight should be put on that fact. For example, it may be that unanimous agreement among the MMCs is not required to progress the Change Request. Gas Industry Co does not wish to, or see any need to, take a view on the internal decision making arrangements of the MMCs. No doubt this will be a matter to which MDL will give consideration when it is considering Gas Industry Co's final recommendation.

In relation to Todd's final concern, Gas Industry Co acknowledges that Todd considers that the removal of section 3 may result in a treatment of Legacy Gas which is inconsistent with the terms of the Maui Gas Contract. This is a legal issue for the parties to those contracts.

The clarification by Mighty River of its position in its submission on the Draft Recommendation has effectively been considered in respect of points raised in other submissions; however the clarification has been noted.

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Final recommendation

In accordance with section 29.4(a) of MPOC, Gas Industry Co recommends:

- deletion of (and where relevant, consequential amendment to) the following parts of MPOC relating to Maui Legacy Gas:
 - all of section 3 apart from sections 3.2 and 3.3(b);
 - the relevant parts of the definitions in section 1.1;
 - parts of sections 2.1, 2.1(a), 2.1(b), 2.2, 2.14, 2A.6, 7.1, 7.3, 7.4, 12.9, 12.16, 14.1(a), 14.6, 14.7, 15.3(e), 15.6, 24.8 and 29.4(b)(iv);
 - all of sections 8.18(a), 8.18(b), 8.19(a), 8.19(b), 8.20(b), 8.20(c), 8.24(a), 8.24(b), 8.26(a), 8.26(b), 8.28(b), 8.28(c), 14.9, 14.10(b)(iii), 15.11, 16.1, 18.1(a), and 38.2;

- section 2.19 being amended to read as follows:

The Target Taranaki Pressure shall be between 42 and 48 bar gauge, except as may be required as a result of a Contingency Event, Force Majeure Event or Maintenance. MDL shall give each Shipper and Welded Party not less than 12 months notice if it proposes to change the Target Taranaki Pressure below 42 bar gauge or above 48 bar gauge and any such change may only be implemented through a Change Request in accordance with section 29;

- the deletion of section 2A.1(4) in the event that section 2A has not already been deleted in its entirety in response to the May Change Request;
- the deletion of section 2.21; and
- in section 1.1 deletion of the words '(including the facilities connecting the Maui Gas production station at Oaonui to the Maui Pipeline).' from the definition of Welded Point.

All changes are marked up in the attached copy of MPOC.

This recommendation is effective from 11 November 2008.

**Appendix A Notification of Vector-MDL
ILON/AEOI dispute settlement**

MAUI DEVELOPMENT LIMITED



Please reply to:
Shell (Petroleum Mining) Company Ltd
3 Queens Wharf,
PO Box 1873,
Wellington,
New Zealand

Maui Development Ltd
PO Box 1873
Wellington

Fax: (04) 460 2549
Email :c/- commercial.operator@mauipipeline.co.nz

To: Vector Gas Limited
Private Bag 39980,
Wellington
Attention: Paul Hodgson

1 September 2008

ILON DISPUTE BETWEEN MAUI DEVELOPMENT LIMITED (*MDL*) AND VECTOR GAS LIMITED (*VT*)

Maui Development Limited (*MDL*) and VT acting as a Welded Party under MPOC in respect of the various VT Welded Points (*VT Welded Points*) are in dispute (*Dispute*) with respect to the issue of ILONs for AEOI at VT Welded Points.

MDL submitted an "MPOC Legacy Change Request" to the GIC on 20 June 2008 (*Change Request*). VT opposed aspects of the change request pending resolution of transition issues arising from the Dispute.

Since then MDL and VT have entered into a transition agreement (dated 1 September 2008) ensuring that there will be alignment of the ROI/AEOI numbers between MDL and VT systems to ensure that the Dispute is contained to the period prior to the change request coming into effect (*Transition Agreement*).

In this letter capitalised terms (eg *Day*) have their MPOC meanings (unless the context requires otherwise) and in addition *Effective Date* shall mean the Day following the last day of the Transition Period, in accordance with the Transition Agreement.

In respect of the Dispute, MDL offers the following settlement terms to VT as specified below (*VT Settlement Proposal*). The VT Settlement Proposal will only have effect, and this letter will be unconditional, when and if MDL determines, at its sole discretion, that it has received an acceptable level of industry support to the VT Settlement Proposal and notifies VT of such support (*MDL's Notice*).

VT Settlement Proposal

As soon as practicable following MDL's Notice, MDL will (and VT agrees to MDL so doing) effect or procure, or arrange for, the following:

- A. All ILONs issued under current processes to VT will be withdrawn/cancelled up to the Effective Date. The invoices or credit notes issued in respect of the currently disputed ROIs and related cash outs will be revoked and MDL will not seek to recover its balancing costs from VT in respect of any ILONs issued to VT prior to the Effective Date;
- B. The balance of the Oaonui ROI (if any) on the Effective Date will be removed/cancelled with effect on the Effective Date in exchange for a call option provided by the Maui Mining Companies acting through Shell Todd Oil Services Limited (under the terms, or substantially the terms, of the MDL Call Option Secondary Balancing Gas Agreement posted on OATIS on 11 June 2008) for an equivalent quantity of gas. The key terms of this call option are attached in the MMC proposal for resolution of the ROI (Attachment I).

Nothing in this letter is to be seen or taken as an admission by MDL or any other party or entity that its conduct has not complied with MPOC at any point in time. This letter is put forward for consideration on the basis that it may not be relied on or cited in evidence in any proceedings against MDL or any other party or entity. However this letter, once signed by VT and having become unconditional, is to be and will constitute a full and final settlement of the Dispute and each party agrees not to commence any proceedings against the other arising specifically in relation to the Dispute.

MDL will either give MDL's Notice or notify VT that this letter did not gain the necessary level of industry support, such support being requested by MDL to be received by 10 September 2008. MDL will notify VT as soon as practicable after that date, as MDL determines in its discretion.

Yours sincerely



for and on behalf of
Maui Development Limited

Terms of VT Settlement Proposal agreed by VT:



Signed for and on behalf of

Vector Gas Limited

Attachment I: MMC proposal for resolution of Oaonui ROI

MMC Proposal

The MMC's offer in support of the VT Settlement Proposal is made *without prejudice* to their views as to the proper resolution of the Oaonui ROI position.

Any negative ROI balance at Oaonui that exists on the Effective Date will be cashed out \$0.00/GJ.

That cashed out quantity will be the "Oaonui Quantity".

In exchange a call option (under the terms of the Call Option Master Agreement for the provision of Secondary Balancing Gas Services as posted on OATIS as at the Effective Date) for the "Oaonui Quantity" will be put in place with effect from the Effective Date to transfer that volume back to the Maui Pipeline Commercial Operator (CO) at \$0.00/GJ.

Basic contract terms:

- Zero cost for gas transfer;
- Maximum gas rate = 5 TJ/day, subject to capacity being available from the Maui Field after MMCs have met all other contractual obligations;
- MMCs may accept requests for delivery at rates greater than 5 TJ/day in their sole discretion;
- Terminates when the Oaonui Quantity is taken.