



# Final Recommendation on 24 April 2015 MPOC Amendment Process Change Request

Date issued: 6 October 2015



## **About Gas Industry Co.**

Gas Industry Co is the gas industry body and co-regulator under the Gas Act. Its role is to:

- develop arrangements, including regulations where appropriate, which improve:
  - the operation of gas markets;
  - access to infrastructure; and
  - consumer outcomes;
- develop these arrangements with the principal objective to ensure that gas is delivered to existing and new customers in a safe, efficient, reliable, fair and environmentally sustainable manner; and
- oversee compliance with, and review such arrangements.

Gas Industry Co is required to have regard to the Government's policy objectives for the gas sector, and to report on the achievement of those objectives and on the state of the New Zealand gas industry.

Gas Industry Co's corporate strategy is to 'optimise the contribution of gas to New Zealand'.

## Executive summary

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Mighty River Power (MRP) has requested a change to the Maui Pipeline Operating Code (MPOC) to introduce a new code amendment process. In essence, MRP's Amendment Process Change Request (APCR) proposes to replace the current code change approval mechanism, where Gas Industry Co considers each proposed change and makes a recommendation on whether it should be adopted or not, with a voting based regime, where changes would be adopted if they receive sufficient votes from MPOC Parties.

On 12 August 2015, Gas Industry Co published a Draft Recommendation<sup>1</sup> which did not support the APCR, and called for submissions. The APCR, Gas Industry Co's Draft Recommendation, and all submissions are available on Gas Industry Co's website at <http://gasindustry.co.nz/work-programmes/mpoc-change-requests/mpoc-change-request-apcr-24-april-2015/>

Five submissions were received. Four agreed with Gas Industry Co's conclusion, and one continued to support the APCR. On further considerations, no new arguments or evidence have caused Gas Industry Co to change the conclusion of the Draft Recommendation.

**On the basis of our analysis of the APCR, all the information provided to us, and with due consideration of the objectives in the Gas Act and the GPS, this Final Recommendation does not support the APCR.**

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<sup>1</sup> <http://gasindustry.co.nz/dmsdocument/4984>

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# 1 Introduction

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## 1.1 Purpose

This paper presents Gas Industry Co's Final Recommendation on the MPOC APCR submitted by MRP on 24 April 2015.

Unless otherwise noted, capitalised terms used in this Final Recommendation have the same meaning given to those terms in the MPOC.

## 1.2 Proposed Change

The proposed changes relate to the process for making amendments to the MPOC. MRP says its proposal '... is designed to promote an inclusive and collaborative change process as opposed to the current arrangement which can become adversarial'. Broadly, the proposal aims to align the MPOC code change processes with the new code change process introduced into the Vector Transmission Code (VTC) on 1 April 2015.

## 1.3 Process to date

In a letter dated 24 April 2015, Mighty River Power (MRP) submitted the APCR to Gas Industry Co for consideration.

On 5 May 2015, Gas Industry Co notified industry stakeholders of the APCR. It also advised of a potential conflict of interest because Gas Industry Co's role in considering the APCR would require it to opine on a matter that could significantly change that role. However, both MRP and the pipeline owner, Maui Development Limited (MDL), requested that Gas Industry Co continue to process the application and, following legal review, Gas Industry Co concluded that the situation could be effectively managed.

On 12 August 2015 Gas Industry Co issued a Draft Recommendation. To manage the potential conflict of interest, the Draft Recommendation was independently reviewed by former High Court judge Sir John Hansen<sup>2</sup> who found that there were likely no grounds for finding an actual or a perceived conflict and that the Draft Recommendation was robust and reasonable.

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<sup>2</sup> Sir John Hansen also performs the role of the Rulings Panel under the Gas Governance (Compliance) Regulations

## **1.4 Assessment of Draft Recommendation**

The Draft Recommendation concluded that APCR benefits could arise from:

- Requiring early engagement on code changes;
- Enabling Gas Industry Co to participate in the design of code changes; and
- Alignment of the codes.

However, we assessed that these would be outweighed by the APCR's dis-benefits of:

- Poor definition of the voting arrangement;
- Potential for inequitable voting outcomes;
- Potential for inefficient voting outcomes; and
- Increasing the scope for disputes.

In essence, the Draft Recommendation concluded that the proposed new MPOC code change arrangements are not sufficiently well defined by the APCR, and have the potential to deliver inequitable and inefficient outcomes.

## 2 Submissions on Draft Recommendation

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### 2.1 Summary of submitter views

The five submissions on the Draft Recommendation were from:

- Gas Management Advisors Limited (GMA);
- Maui Development Limited (MDL);
- OMV Limited (OMV);
- Trustpower Limited (Trustpower); and
- Vector Limited (Vector).

A summary of submissions is provided in Appendix A. Full submissions are available at the Gas Industry Co website.

The submissions that agreed with the conclusion of the Draft Recommendation were from:

- GMA<sup>3</sup>, who considers that Gas Industry Co should work with the industry to 'rescue' the positive aspects of the APCR, and renegotiate the Memorandum of Understanding (MoU) with MDL to allow it to be involved with the development of MPOC amendments, and to have the ability to approve changes conditionally;
- MDL, who nevertheless thinks that Gas Industry Co did not adequately deal with the central issue – the unsuitability of any voting arrangement as a code change gatekeeper – and did not think that any evidence had been provided for the claimed benefit in aligning the MPOC and VTC;
- OMV, who is satisfied that the current MPOC change provisions are robust and should not be changed; and
- Vector, who acknowledges that, because the MPOC applies to Welded Parties as well as to Shippers, the VTC code change arrangements may not be entirely suitable, but some features, such as more meaningful consultation, should be adopted.

The one submission that did not agree with the conclusion of the Draft Recommendation was from:

- Trustpower, who considered that, given all the positive features of the APCR, the flaws were minor and technical, and could be overcome.

In the next chapter we discuss the issues raised.

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<sup>3</sup> GMA is a new consultancy managed by Jim Raybould, previously an executive of MRP.

# 3 Discussion of issues raised

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## 3.1 The voting proposal

Trustpower argues that voting is superior to the current arrangements because the views of all Parties are represented and changes are not concentrated in a few people who need not consider the interests of others. If every Party to the MPOC has an equal vote, Trustpower believes that the influence of Shippers should not be disproportionate. Also, the interests of downstream Parties is satisfied by their ability to switch retailers if they wish.

Although MDL agrees with Gas Industry Co's conclusion that the current arrangements are superior to the voting proposal, it considers that the analysis should have gone further, to conclude that the current arrangements are superior to any voting proposal. This is because, in MDL's view, the process requires "...a clear change proposition; the opportunity to be heard; a set of independently determined guiding principles; and a decision by an independent suitably qualified decision maker which is itself subject to rules of conduct."

### GIC comment

We do not agree with Trustpower that the voting proposal is superior. We will not repeat the full analysis of the Draft Recommendation but, in brief, while we acknowledge that there would be countervailing restraints on the increased influence that voting rights would give Parties<sup>4</sup>, the arrangements raise concerns for both Parties and non-Parties:

- In regard to Parties, we agree with MDL<sup>5</sup> that the effect of the APCR would be that a bi-lateral contract could be subject to amendment by a process depending merely on the on the formation of a voting coalition. As noted in the Draft Recommendation, this is particularly a concern since Shippers would have more votes than Welded Parties.
- In regard to non-Parties, a coalition of voters could develop changes that benefit that coalition at the expense of others, including end users and potential new entrants. Trustpower's claim, that the ability of end users to switch retailers is a protection against this, in our view is not valid. End users do not know how a retailer will vote or has voted, and may not even be aware that a change is proposed or has been made, so they do not have the information necessary to select a retailer that best represents their interests.

In contrast to the proposed voting arrangements, the current arrangements allow Gas Industry Co, when considering a change proposal, to assess proposed changes with reference to the overall efficiency of the market, including the interests of existing pipeline users, end-users (including smaller stakeholders who may not have the resources to actively participate in a change process), and potential new entrants.

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<sup>4</sup> In particular, MDL would have broader grounds on which it may withhold its consent, Parties would be able to raise disputes in relation to code changes, and Gas Industry Co would retain its power to recommend regulation.

<sup>5</sup> MDL Submission on Draft Recommendation item 5.



We do not agree with MDL's view that the current change process would be superior to any voting regime. However, we acknowledge that it would be a challenge to design a voting regime that could fit within an overall change process that provides:

- clear objectives;
- a clear process, with sufficient flexibility to make improvements to change proposals;
- effective third-party participation; and
- credible and transparent analysis of the proposed change against the Gas Act and GPS objectives, including balancing the interests of Parties and non-Parties.

### **3.2 A broader role for Gas Industry Co in MPOC code changes**

Regardless of the APCR Final Recommendation, both GMA and Vector suggest that the MoU should be amended to:

- permit Gas Industry Co to make its support of proposed changes conditional on revisions that would make the proposed change materially better; and
- clarify Gas Industry Co's role to avoid further questions about conflict of interest

Trustpower also considers that Gas Industry Co's current code change role is too restricted and that it should have more influence over code changes.

MDL, on the other hand considers that, while the current code amendment process does not restrict the scope of Gas Industry Co's consultation, its powers are derived from Part 4A of the Act and it has been appointed as the 'industry body' under s43ZL to perform the functions of the industry body. In particular:

- to make recommendations to the Minister for any governance regulations, following the process set out in ss43L – P; and
- if gas governance regulations or rules are in force, to carry out investigations for the purposes of monitoring and enforcing those regulations or rules.

MDL believes that for Gas Industry Co to be involved in broader roles would be inconsistent with the Gas Act and Gas Industry Co's regulatory role and functions.

#### **GIC comment**

These matters are not directly relevant to consideration of the APCR, and are best addressed by a broad-based group of stakeholders that includes both Parties to the MPOC and other stakeholders. However, for future reference we note that the MoU was agreed between Gas Industry Co and MDL, mostly to clarify the process we would follow in order to make a recommendation on a change request. The matters Vector and GMA suggest dealing with in the MoU are wider ranging, and would significantly alter the code change landscape. Certainly they are matters that Parties to the MPOC and other stakeholders should be concerned about, and therefore matters that should be proposed and processed as changes to code arrangements, and not just as changes to the MoU.

Also we note that:

- In our view, broader Gas Industry Co involvement in the development of code changes proposed by the code Parties is consistent with the co-regulatory scheme in Part 4A the Gas Act 1992, particularly since it allows for industry-led solutions to be considered and developed ahead of regulation.
- Gas Industry Co retains its powers to propose regulatory arrangements.
- We are proposing further work on convergence of current code arrangements – see <http://gasindustry.co.nz/work-programmes/gas-transmission-investment-programme/transmission-access/#options-for-improvement-paper-2/>

### **3.3 Conclusion**

We do not consider that any of the material submitted causes us to change the conclusion of the Draft Recommendation.

## 4 Final Recommendation

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On the basis of our analysis of the APCR, all the information provided to us, and with due consideration of the objectives in the Gas Act and the GPS, this Final Recommendation does not support the APCR.

## Appendix A - Summary of submissions on the APCR

This brief summary identifies the salient points of industry submissions, to provide context. However, it does not purport to cover all points made, or to represent any submission in a particular way, or to be the authoritative reference point on all submissions. All submissions are available for full reference at <http://gasindustry.co.nz/work-programmes/mpoc-change-requests/mpoc-change-request-apcr-24-april-2015/>.

<b>GMA</b>	<p>GMA accepts that GIC cannot support the APCR, but is pleased GIC agrees with some aspects of the proposal, including the front end consultation. Given this, and the level of industry dissatisfaction with the current MPOC change process, GMA suggests:</p> <ul style="list-style-type: none"> <li>• GIC renegotiate its Memorandum of Understanding with MDL to allow GIC to be involved with the development of MPOC amendments, and to allow it to support change requests subject to modifications being made; and</li> <li>• GIC agrees with the industry which amendments to the MPOC amendment process it would support.</li> </ul>
<b>MDL</b>	<p>MDL agrees with GIC's conclusion, but believes that:</p> <ul style="list-style-type: none"> <li>• <i>No voting arrangement would be superior to current arrangements since such arrangements would:</i> <ul style="list-style-type: none"> <li>○ forgo independent guiding principles and an independent decision maker;</li> <li>○ increase the likelihood of commercial bias towards incumbents;</li> <li>○ make bi-lateral contracts subject to change by coalitions of interest;</li> </ul> </li> <li>• The value of early engagement on MPOC changes is overstated (witness the Market Based Balancing Change Request);</li> <li>• As a regulator, GIC should not participate in code change design</li> <li>• GIC has provided no evidence that aligning the MPOC and VTC would reduce costs and, in any case, it is the VTC that has diverged from the PEA's preference for the GIC to be the final decision maker.</li> </ul>
<b>OMV</b>	<p>OMV agrees with GIC's decision not to support the AMCR. The current arrangements are robust and allow for MPOC evolution subject to regulatory objectives being met.</p>

<p><b>Trustpower</b></p>	<p>Trustpower continues to support the APCR. While it has some minor and technical deficiencies, these can be overcome. It believes that:</p> <ul style="list-style-type: none"> <li>• The proposal would encourage MDL to be more transparent and to consider Maui User views fairly;</li> <li>• GIC should have more say in changes – consistent with a co-regulatory role;</li> <li>• All Maui users should have a vote on changes that could materially affect their businesses;</li> <li>• Current arrangements leave too much power with MDL which can lead to sub-optimal results (witness the Market Based Balancing Change Request);</li> <li>• Since the APCR would improve transparency, open up industry discussion, and align with the principles of Evolutionary Convergence, discarding it is irrational.</li> </ul>
<p><b>Vector</b></p>	<p>Vector agrees with GIC’s conclusion. In particular, it agrees that the wider variance in commercial interests of MPOC Parties compared to the VTC makes the VTC change arrangements unsuitable. However, it believes that a more meaningful consultation process – allowing for stakeholder feedback – would be an improvement.</p> <p>Vector also suggests that a change in GIC’s Memorandum of Understanding with MDL could permit GIC should be able to be involved in the design of changes, to make its support for changes conditional, and remove conflict of interest concerns. This would give a degree of alignment between the MPOC and VTC, as the Panel of Expert Advisers envisaged.</p> <p>The summary of the VTC code change process in the introduction of the Draft Recommendation does not match the (correct) Appendix B description, and this should be noted in the Final Recommendation.</p>

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30 September 2015

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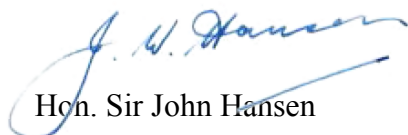
Dear Patrick

**RE: GAS INDUSTRY CODES' FINAL RECOMMENDATION ON THE  
PROPOSED AMENDMENT PROCESS CHANGE REQUEST**

I have considered submissions received on my draft report.

I see nothing whatsoever in any of the submissions that would lead me to change the conclusions I reached in that draft report. As a final report, I confirm the conclusions I reached in my draft report.

Yours sincerely



Hon. Sir John Hansen