

23 June 2017

Ben Gerritsen  
General Manager – Commercial and Regulation  
First Gas Ltd  
(via email to [info@gasindustry.co.nz](mailto:info@gasindustry.co.nz) )

Dear Ben

**RE: Submission on GTAC: Emerging Views on Detailed Design of Access Products, Pricing, Balancing and Allocation.**

1. This is a submission on behalf of the Major Gas Users Group (MGUG) on the above paper released on 12 May 2017 and discussions at the industry workshop of 17 May.
2. Nothing in this submission is confidential and some members may choose to make separate submissions.
3. MGUG was established in 2010 as a consumer voice for the interests of a number of industrials who are major consumers of natural gas. Membership of the Group includes:
  - Ballance Agri-Nutrients Ltd
  - Oji Fibre Solutions (NZ) Ltd
  - Fonterra Co-operative Group
  - Goodman Fielder New Zealand Limited
  - New Zealand Steel Ltd
  - New Zealand Sugar Company Ltd
  - Refining NZ
4. Our submission covers the following points of interest for our group:
  - a. We see a stronger argument in favour of Delivery zones vs Delivery Points
  - b. We support Priority Rights (PR) as a signal for capacity investment, not as an insurance product for FM events.
  - c. We seek further information and clarity on how and when PRs are made available.
  - d. In the interest of maintaining downstream retail competition and lowest cost to end user we believe that PR should be able to be owned by end users.
  - e. We are concerned that non-standard capacity product terms might undermine PR market and would seek to ensure that this risk is minimised in non-standard capacity product terms.
  - f. We support a tiered approach to Over-run and Excess Running Mismatch (ERM) charges but want to see how that fits in with the nominations regime before commenting further on the tolerances.
  - g. We do not support Maximum Hourly Quantity (MHQ) Peak Charge.
  - h. We support the concept of a single balancing pool for the pipeline.
  - i. We do not see any value in a Park and Loan product.

### **Delivery Zones vs Delivery Points**

5. We have noted First Gas' (FG) change of position in going from a receipt zone/zone delivery product to receipt zone/delivery point (DP) product for Daily Nominated Capacity (DNC) and PRs. We are not convinced that this is a better outcome for transmission customers or FG.
6. Our key concern stems from how PRs will be allocated and traded if it is assigned to a DP. If there is a dedicated connection, which is common with our members, how do they ensure that they are able to buy sufficient PR if it is being rationed to less than the capacity they want the PR on?
7. Furthermore there will be no competitive market for primary allocation of units. The price will always be the reserve price which provides no price signal for investment in capacity.
8. A further problem relates to PR trading. There will be no market for PRs on dedicated delivery points since they are of no value to other parties and other parties cannot trade their surpluses to the dedicated delivery point either.
9. We understand that FG' shift in its position on zones vs DPs is related to concerns that FG may be approving DNCs for a zone but being unable to assure that DNC within a zone will be effective on a DP.
10. We think that concern is overstated and within FG's ability to manage through how zones are defined in the network.
11. Firstly FG can make reasonable assumptions of likelihood of physical curtailment at a DP based on DP reconciliation data and history in comparison with nominations received as part of provisional cycles.
12. To the extent that a zone is approaching capacity, FG could simply redefine the zone to give greater granularity and therefore visibility on problematic DPs.

### **Purpose of PR**

13. Although the draft terms clarify that PRs do not apply in an FM event there was some discussion at the workshop that they should. We disagree with changing the purpose of PR products.
14. In our view PRs provide the appropriate price signals to FG to invest in increasing pipeline capacity. These signals will be significantly muted if PRs are acquired for the purpose of providing priority in unforeseeable events as an insurance product.

### **PR availability**

15. The proposal is to make PRs available for each delivery point regardless of whether there appears to be a need for them, and to allow the market to decide whether they have any value by either participating in an auction to acquire PRs, or to abstain from the bidding

process. MGUG members prefer PRs to be a mechanism for congestion management, only triggered once there is a real problem perceived.

16. The concern from members is that they will be diverted in spending resources to assess the risks of curtailment where none seems likely. There are further concerns on whether this approach might lead to unintended consequences in the market for PRs such as PR hoarding and speculation.
17. This is further clouded by lack of clarity on what tools and information will be available to provide for an informed decision. One example is whether FG would be at liberty to communicate contingent demand from parties they are in negotiation with but are prevented under confidentiality from signalling to the market.
18. MGUG would look for more complete information on how PR availability will be varied across auction cycles and how these might also be influenced by other factors including those made available under non-standard arrangements before fully supporting the PR mechanisms.

#### **Ownership of PRs**

19. The draft code proposes that only shippers should be able to have title to and trade PRs. We disagree. PRs benefit end users who value certainty of supply. It is a separate product from DNC. If PRs are limited to shippers, most of whom are also retailers, this has the potential to limit downstream competition for gas, or alternatively raise the price of PRs to profit incumbent retailers.
20. The anticompetitive and increased cost scenarios can occur if a downstream user is looking to switch suppliers who hold a PR on their behalf. This is analogous to the situation on the Northern pipeline in 2011 when no new capacity was being offered and retail incumbents were not required to let capacity follow the end user. A similar situation is possible with PRs where end users are bound to hold PRs as part of their risk governance arrangements. An incumbent, who may not be the favoured supplier for a new gas supply contract, may simply hold on to the PR to force a deal in their favour, or alternatively sell the PR at a profit to the new supplier. Under both scenarios the end user pays more for delivered gas than they would if they held title themselves to the PR.
21. Ownership of a PR creates greater transparency to the end user of the actual price of the product. This is because invoicing from a supplier does not always make it clear whether a particular transmission product or levy is being passed through at cost or with mark-up.

#### **Non-standard Agreements**

22. We remain concerned about the potential volume of non-standard agreements to transfer risks to standard agreement holders including; increased volatility of price swings under a revenue cap, and also through crowding out limited availability of PRs.

23. Under the code proposal non-standard agreements could include terms that include PRs/PR equivalents. PRs may be guaranteed for the term of the agreement, and the term may be much longer than the six months under a standard agreement.
24. This reduces the availability of PRs for auction and also values PRs under non-standard agreements at a price other than the market price.
25. We appreciate that FG will need to offer non-standard agreements under certain circumstances. We would however suggest that PRs are excluded from such arrangements in a way that doesn't create a two tier market for the product.

### **Nominations**

26. The current drafting of the GTAC shows that nomination provisions are still to be decided. The nomination regime, particularly the intra-day cycle, is closely linked to penalty charge risks (overrun, excess running mismatch). Our thoughts on these penalty charges, particularly the tolerances and tiers associated with these are caveated on needing a better understanding on what the nominations regime will be.

### **Tiered approach to Overrun and ERM charges**

27. We support a tiered approach to overrun and ERM charges. However without knowing what opportunities end users have to manage overrun and ERM risk through nomination cycle times we are unable to comment further on whether the tier ranges are reasonable in context of available intra-day cycles.

### **MHQ Peak Charge**

28. We don't believe that FG has created a case for introducing an MHQ charge at dedicated delivery points that justify the costs of introducing such a charge.
29. FG's argument for the new charge is based on transmission assets (delivery points, receipt points, compressors, and other assets) being sized according to MHQ parameter and that if allowable MHQ is exceeded "*there may be significant impact on the transmission system*"<sup>1</sup>.
30. It is not clear what that impact is and why only dedicated delivery points should be targeted. Exempted receipt points and allocated gas gates, which are equally sized for MHQ parameters, can presumably also impact significantly on the transmission system.
31. A peak hourly demand at a delivery point does not necessarily impact other assets as this seems to be a function of both the system demand diversity and line pack in the system as a whole.

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<sup>1</sup> P16- p23

32. FG make a broader statement that “*First Gas considers that at such Delivery Points there is no reason for exceeding MHQ*”.
33. There are a number of valid reasons why MHQ might be exceeded at dedicated delivery points:
- a. The dedicated delivery point may have a “peaky” daily demand profile that is typical of their operation.
  - b. The dedicated delivery point may have a peak created from other operational requirements, such as start-up after a plant trip or after a shutdown.
34. For situations where daily peaks exceed  $1/16^{\text{th}}$  of a typical DNC, the main impact will be to increase the administrative burden on nominations. Alternatively, users may end up consistently paying for DNC quantities nominated in excess of the actual requirement for the day. This depends on which part of the day the peak occurs relative to the intra-day nomination cycles.
- *Scenario 1 – Peak >  $1/16^{\text{th}}$  of total DNC is part of the site profile – Cost = changing intraday nominations or higher DNC charges.*
- MHQ charges can be avoided if they are included in the DNC nomination ahead of the peak, and then adjusted for the total DNC required after the peak has occurred. This follows from the definition of MHQ being  $1/16^{\text{th}}$  of the DNC. Where the peak occurs after the last intra-day nomination cycle the dedicated user will need to either incur a peak MHQ charge or pay for more DNC than they actually need.
- *Scenario 2 – Peak created by unstable plant conditions*
- MHQ charges are unable to be avoided because they occur without being anticipated. In these situations it is also not clear why this creates greater difficulties or costs for FG that are different from Scenario 1, or from events that might equally occur at allocated gas gates which are exempt this charge.
35. In summary, allowable MHQ appears to be a contractual concept that is a function of DNC rather than a function of the physical constraints of the pipeline. There is no clear rationale as to why allocated gas gates and receipt points should be exempt the charge, or why there is a charge if it can be avoided by adjusting intra-day nominations ahead of the anticipated peak. The costs to dedicated delivery points in managing MHQ nominations or incurring penalties are real and the benefits of the charge do not appear commensurate with that cost.
36. In conclusion we do not support the introduction of an MHQ charge without a stronger rationale from FG for introducing it.

### **Balancing Pool**

37. We support the idea of a single balancing pool for the pipeline system as a mechanism to minimise balancing costs.
38. We also support the provisions and mechanisms in the code to change the number of balancing pools as circumstances dictate.

### **Park and Loan Product**

39. We do not support a Park and Loan product. We believe that this will negatively affect the capacity of the pipeline to the detriment of balancing costs, PR availability, and Overrun and ERM tolerances.
40. We also see Park and Loan undermining the development of a deep and liquid trading market for gas commodity. Our preference is that surplus and deficits in gas is traded to generate the price signals for the value of the gas commodity itself.

### **Other Information**

41. In order to further assess the draft GTAC we think it would be helpful to understand the following supporting arrangements as well:
  - a. Gas quality assurance arrangements. (how is FG assuring compliance with ICA with respect to gas quality injected into the transmission system)
  - b. A demonstration of what information might be made available to assess system capacity vs demand forecast in order to inform views on the value of PRs.
  - c. PR auctioning, arrangements, rules, worked example
  - d. How PR trading arrangements on secondary market is expected to work.
  - e. The principles and criteria to be applied to re/negotiation of supplementary agreements.

Yours sincerely



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