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Greig Hinds
Gas Industry Company Secretary
PO Box 10-646
Wellington

Dear Greig

Submission on the GIC's Proposed FY2014 Strategy, Work Programme and Levy

Introduction

1. Vector Limited ("Vector") welcomes the opportunity to make this submission on the Gas Industry Company's ("GIC") *Statement of Proposal on FY2014 Strategy, Work Programme & Levy*, dated 20 December 2012.

2. No part of this submission is confidential and Vector is happy for it to be made publicly available.

3. Vector's contact person for this submission is:

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A reduced budget

4. Vector broadly supports the GIC's proposed Work Programme for FY2014. The proposed 6.7% reduction in total work programme costs relative to FY2013 level is commendable, translating to reductions in retail and wholesale levies of 3.5% and 7.5%, respectively.

5. Vector understands this is the first time since the GIC's establishment that a smaller budget relative to the preceding year is being proposed. This is indeed

consistent with the Government's policy of providing "value for money" and "reducing business and household costs".[1]

Priorities for FY2014

6. Vector supports the GIC's continued focus on the Gas Transmission Investment Programme ("GTIP"), review of the Gas Governance (Critical Contingency Management) Regulations 2008 ("CCM Regulations"), review of the Gas (Downstream Reconciliation) Rules 2008, and the development of retailer insolvency arrangements. Vector, however, is concerned that not all of these initiatives have progressed as quickly as they should.

   a. GTIP

      The GTIP paved the way for broad industry and GIC agreement that new gas transmission investment is not required for the foreseeable future.

      The Panel of Expert Advisers has been working for a long time and needs to make conclusions about desired outcomes and recommendations for the management of pipeline congestion.

      Vector has pointed out that the GIC and the Commerce Commission have overlapping responsibilities in relation to providing incentives for transmission investment[2] and believes this is something the GIC should address as part of the GTIP.

   b. Review of the CCM Regulations

      Vector supports the tighter definitions of Essential Service Provider ("ESP") and Minimal Load Consumer ("MLC") in the GIC's *SoP on Amendments to the Gas (Critical Contingency Management) Regulations 2008*, dated 12 November 2012. Vector further supports the GIC making ESP and MLC designations, instead of retailers.

      Vector wishes to see the CCM review being progressed expeditiously. This would ensure that lessons learned from the Maui Pipeline Outage of October 2011, informed by the outcomes of three consultations on CCM since that event, are adopted in a timely manner.

[1] Statement of Proposal, page 15

[2] http://www.vector.co.nz/sites/vector.co.nz/files/20110607VectorSubmission-Long-termCapacityProject.pdf, paragraphs 11-19

c. Review of the Downstream Reconciliation Rules

The establishment of the Downstream Reconciliation Advisory Group ("DRAG") was helpful in the development of proposed amendments to the Rules and reduced the number of stakeholder consultations that would have been required otherwise.

Vector generally supports the GIC's proposed amendments to the Rules with the objective of reducing compliance costs, particularly in managing the massive number of breaches that are likely to raise material issues.

Vector, however, does not support retaining the allocation of ongoing downstream allocation fees based solely on volume. While the GIC argues that there is no compelling evidence to shift to a 50:50 allocation based on volume and number of ICPs, there is similarly no compelling evidence for allocation to be based entirely on volume. While the benefit of reduced Unaccounted-for-Gas ("UFG") from efficiency gains arising from the review of the Rules would mostly accrue to those trading bigger volumes, this will diminish over time as the reconciliation system becomes more efficient (the 'new normal'). If there was no UFG, those retailers would have avoided those costs anyway.[3] There is therefore room for significant efficiency gains in the allocation of ongoing fees.

d. Gas retailer insolvency arrangements

Vector agrees with the *Castalia Discussion Paper on Gas Retailer Insolvency*, dated June 2012, that there are residual market failures that are more pronounced in, if not unique to, gas retailer insolvencies that could require sector-specific solutions in addition to normal insolvency legislation.

Vector argues that the development of permanent backstop regulations on retailer insolvency is warranted to specifically address residual market failures, particularly to guarantee the efficient transfer of an insolvent retailer's customers to other retailers. In addition, this is warranted on the grounds that 1) parties' ability to address residual risks through bilateral contracts are constrained by multilateral contractual arrangements in the gas industry, for example, the Vector Transmission Code ("VTC"), 2) regulations could be crafted so as not to interfere with normal insolvency processes, and 3) the benefits of

[3] http://gasindustry.co.nz/sites/default/files/submissions/181/vector_submission_-_downstream_reconciliation_sop.pdf, paragraphs 10-13

providing market confidence outweigh the minimal costs of developing and maintaining permanent backstop regulations.[4]

Vector believes it is neither impossible nor costly to achieve permanent and flexible regulations to address future retailer insolvencies, including aligning the GIC's work on retailer insolvency with that of the Electricity Authority ("EA"). Vector's position on this matter is discussed in its upcoming submission on the GIC's *Insolvent Retailers – Options Paper*, dated 17 December 2012.

Vector notes the EA's decision of December 2012 to adopt the Retail Advisory Group's recommendation "to establish a regulated process for ensuring that the defaulting retailer's customers are transferred to another retailer".[5]

7. Vector notes that gas transmission pipeline balancing, a Vector priority last year, is in the process of being addressed commercially and through proposed changes to the Maui Pipeline Operating Code and the VTC.

Unwarranted rules and regulations

8. Vector particularly commends the GIC exercising restraint by:

   a. not pursuing a regulated approach to information gathering. In principle, Vector supports the adoption of the GIC's proposed voluntary information request protocol.

      Vector agrees that a voluntary approach worked effectively in the information request to retailers to inform the development of ESP and MLC definitions as part of the CCM Regulations review;

   b. not adopting a regulatory approach in relation to gas quality at this time. Vector reiterates its view that, as a matter of practice, it has zero tolerance for non-Specification gas entering its transmission and distribution systems, and takes action as soon as any issue comes to its attention.[6] Vector agrees that opportunities for new industry-led arrangements that would address the GIC's objective of improving transparency in gas quality could be explored;

   c. proposing to make a recommendation to the Minister of Energy and Resources to allow the Gas (Processing Facilities Information Disclosure)

[4] http://www.vector.co.nz/sites/vector.co.nz/files/PUBLIC%20Vector%20Submission%20Castalia%20Report%20on%20Retailer%20Insolvency.pdf, paragraph 17a-e
[5] http://www.ea.govt.nz/our-work/programmes/market/consumer-rights-policy/assuring-supply/
[6] http://gasindustry.co.nz/sites/default/files/submissions/181/vector_submission_-_gas_quality_governance.pdf, paragraphs 5-6

Rules 2008 to lapse after 27 June 2014. Vector agrees with the GIC's proposal for the reasons that 1) there is no market failure in the gas processing facilities market, 2) it has been shown that commercial arrangements can be reached in this market, and 3) industry had very little use of the information that has been disclosed;[7] and

d. suggesting an approach of assessing retail contracts against benchmarks by exception, to avoid unnecessary assessment of contracts that are already aligned with the benchmark terms developed by the GIC with industry. It would be cost-effective if such an approach would similarly be adopted for the assessment of gas distribution agreements in due course.

9. The deferral or removal of unnecessary regulations is consistent with good policy making and undoubtedly contributes to the reduction of the proposed budget for FY2014. This would enable greater focus on the GIC and industry's topmost priorities.

10. Vector further commends the GIC's recognition of the need to align its work streams with those of the Commerce Commission and the EA, to the extent possible. Aside from overlaps between the GIC and the Commerce Commission's regulatory responsibilities in relation to gas transmission investment, there are overlaps in responsibilities between the GIC and the EA in matters such as retail competition, distribution contracts, consumer complaints, retailer insolvency, etc. The GIC should investigate how these could be managed and whether coordination between regulators is needed or desirable.

Consultation guidelines

11. In its submission on Concept Consulting's draft report, *Gas Supply & Demand Scenarios 2012-2027*, dated 24 September 2012, Vector proposed that the GIC develop consultation guidelines (or a consultation charter), which would set out principles and standards for stakeholder consultation.[8]

12. Consultation guidelines would enhance the GIC's engagements with stakeholders by ensuring that consultation processes are meaningful and provide greater certainty to potential submitters, e.g. by ensuring reasonable consultation timeframes. This is particularly relevant to issues that would have a profound impact on particular industry participants or on the entire industry. Not allowing ample time for consideration, particularly of complex issues, belittles the

[7] http://gasindustry.co.nz/sites/default/files/submissions/181/vector_submission_-_gas_processing_information_disclosure.pdf, paragraphs 3-4
[8] http://gasindustry.co.nz/sites/default/files/submissions/181/vector_submission_-_gas_demand_and_supply_outlook.pdf, paragraphs 8-9

importance of potentially 'ground-breaking' or 'game-changing' regulatory proposals.

13. Vector notes that consultation principles have been adopted by the EA (EA Consultation Charter). It further notes that consultation timeframes of the Commerce Commission's work in relation to price and quality regulation of electricity and gas transmission and distribution businesses are provided for under Part 4 of the Commerce Act.

14. A recent review of the EA Consultation Charter confirms that the EA now allocates six weeks, rather than four weeks, for consultation.[9] Vector considers that while consultations on technical and non-controversial issues could require a shorter timeframe, consultations on proposals that are likely to have a profound impact on industry participants would require at least four to six weeks for proper consideration.

15. It should not be difficult for a particular consultation to be coordinated with other GIC consultations to ensure a 'staggered' submission schedule and optimal utilisation by submitters of their resources. For example, it would be desirable not to have more than one submission due on the same day or week, and to have at least a full-week interval between submission deadlines.

Responses to specific questions

16. Vector's responses to specific questions in the SoP are set out below.

Q1: Do you consider there to be any other items that should be included in the Company's intended work programme for FY2014? If so, please describe the work required and how that work achieves the outcomes sought under the Gas Act and GPS.

17. Vector proposes that the GIC include in its work programme the development of guidelines in relation to 1) the GIC's consultation process, and 2) requests for access to registry information by non-industry participants.

18. In addition, the GIC should consider making more use of advisory groups and technical working groups to facilitate some (or aspects of) particular work streams.

19. The above proposals would not involve big sums but would deliver significant benefits by providing certainty to stakeholders, and clarity and consistency in the GIC's processes and treatment of relevant issues.

[9] http://www.ea.govt.nz/dmsdocument/14245#mctoc1

Consultation guidelines

20. As indicated above, Vector believes it would be appropriate for the GIC to develop consultation principles or guidelines together with industry participants. This would avoid the setting of arbitrary timeframes (providing certainty for potential submitters) and ensure meaningful consultation.

21. Providing adequate time for consultation is fundamental to the policy making process. The OECD's guiding principles for engaging citizens in policy making states that "[a]dequate time must be available for consultation and participation to be effective".[10]

22. Section 43N of the Gas Act 1992 provides for a robust process of assessing regulatory proposals. The consideration of proposals to meet such a robust process cannot be reasonably expected to be undertaken in a very short period of time.

Registry access guidelines

23. Vector proposes that the GIC develop, with industry participants, guidelines on how to deal with future requests for access to the Gas Registry by non-industry participants.

24. This would ensure consistency in responding to access requests and avoid having to conduct a consultation every time a request is received.

Use of advisory/working groups

25. Advisory or working groups, such as the DRAG, are instrumental to the progress of particular work streams. They enable a wide range of potentially significant issues to be brought out to the surface for proper consideration, which would be impossible through intermittent formal submission processes.

26. Vector proposes that the GIC use advisory or working groups more often to facilitate work streams, for example, on gas retailer insolvency.

Q2: Do you consider there to be any items that should be excluded from the Company intended work programme for FY2014? Please provide reasons for your response.

27. As indicated above, Vector supports the GIC's decisions not to include in its FY2014 Work Programme work on unwarranted rules and regulations. These include the:

[10] http://www.oecd.org/governance/public-innovation/2384040.pdf, page 5

- adoption of a voluntary approach for the disclosure of particular information by industry participants instead of progressing the Information Gathering Project;

- decision not to regulate gas quality at this time; and

- proposed recommendation to the Minister to allow the Gas Processing Information Disclosure Rules to lapse from 27 June 2014.

28. In addition, Vector supports the idea of assessing retail contracts against benchmarks on a selective basis. This approach could then be applied to the assessment of gas distribution agreements against best practice principles. Vector proposes the removal of both assessments from the GIC's Work Programme once agreements are in substantial alignment with the benchmarks/principles.

Q3: In particular, do you consider that work should be undertaken with respect to metering arrangements? Please provide reasons for your response.

29. The GIC does not need to undertake work with respect to metering arrangements at this time.

30. Metering is fundamentally a contestable service, making more prescriptive arrangements in this market unnecessary. Commercial contracts are sufficient to address any issues between meter service providers and other parties.

31. The metering market is rapidly evolving, with the advent of smart meters. Regulating a market that is still taking shape would be premature and would send the wrong signal to those who are taking or willing to take the risk of investing in smart technologies.[11]

32. The Electricity Authority's review of the smart metering market stated that it:

> ...considers that the metering services market in New Zealand is workably competitive, with multiple retailers, distributors and other parties obtaining metering services from competing meter owners/operators...A regulatory intervention at this stage would likely hamper the efficient development and operation of the metering services market by diminishing the commercial and competitive incentives for the efficient provision and procurement of metering data and services.[12]

[11] http://gasindustry.co.nz/sites/default/files/submissions/181/vector_submission_-_downstream_reconciliation_sop.pdf, paragraph 5a

[12] Paragraph 7, Electricity Authority, Part 10 review: nomination of metering equipment provider and access to metering data, Decisions and reasons, 13 April 2012.

33. New Zealand's energy sector is experiencing a successful market-led transition to advanced metering. This contrasts starkly with the experience in parts of Australia where mandated rollouts imposed unwanted costs on consumers.

34. The GIC should only consider work in this area if evidence emerges that there are barriers to market competition in the provision of metering services.

Q4: Do you have any comment on the proposed levy for FY2014.

35. As indicated above, Vector commends the proposed reduction in the FY2014 levy relative to the FY2013 level.

Q5: Do you have any comment on the regulatory amendments described in section 5?

36. Vector is satisfied with the status quo, i.e. the GIC continuing to forecast a conservative level of gas volumes on which to base its wholesale gas levy rate and returning excess funds to levy payers at the end of the financial year.

37. Vector considers the other options (monthly allocation with year-end wash-up or intra-year refund/calibration) to be more complex for wholesale levy payers. Based on Vector's experience, the amounts that were over-collected from wholesale levy payers had been inconsequential compared to what it would cost levy payers to change their processes to accommodate either of these options, e.g. wholesalers having to agree estimated figures with their customers and doing a wash-up at the end of the year, once the GIC had completed its wash-up.

38. The GIC returning levy monies to levy payers is a 'nice problem' for the GIC to have, and an arrangement that Vector can live with.

Yours sincerely

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