



**Submission to the Gas Industry Company
on the Gas Outage and Contingency
Management Arrangements Supplementary
Consultation Paper: December 2007**

From

Contact Energy Limited

11 February 2008

Introduction

Contact Energy Limited (**Contact**) welcomes the opportunity to comment on the Gas Industry Company's (**GIC**) Gas Outage and Contingency Management Arrangements Supplementary Consultation Paper.

In Contact's view the Gas Outage and Contingency Management Regulations 2008 (OCMRs) are being established to ensure the effective management of contingency events to achieve the best outcomes for the industry and end users. The objective then in the development of the Outage and Contingency Management Plans (OCMPs) is to specify the details about how the OCMPs will give effect to the OCMRs.

To ensure that optimal arrangements are put in place for the industry, Contact believes that the process to develop the OCMPs would be more effective and robust with greater utilisation of industry expertise and knowledge at a number of stages during the process. Contact believes that the development process for the OCMPs is a critical part of these arrangements and hence this is the main focus of our submission.

Contact believes that further industry consultation is required before the details of contingency management arrangements are finalised.

This submission also contains our answers to the specific questions contained in the Supplementary Consultation Paper.

For any questions related to this submission, please contact:

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OCMP development process

Contact believes that the process to develop the OCMPs is the most crucial part of these arrangements. Having robust process for OCMP development will ensure that during Critical Contingency (CC) events, commercial incentives are usurped by incentives to allocate gas to where it is most highly valued, and to operate the system in a manner which will limit the extent of the CC events. We therefore want to ensure that the process to develop the OCMPs is not solely focussed on TSOs and that the involvement of users is combined with regulatory oversight to provide appropriate checks and balances.

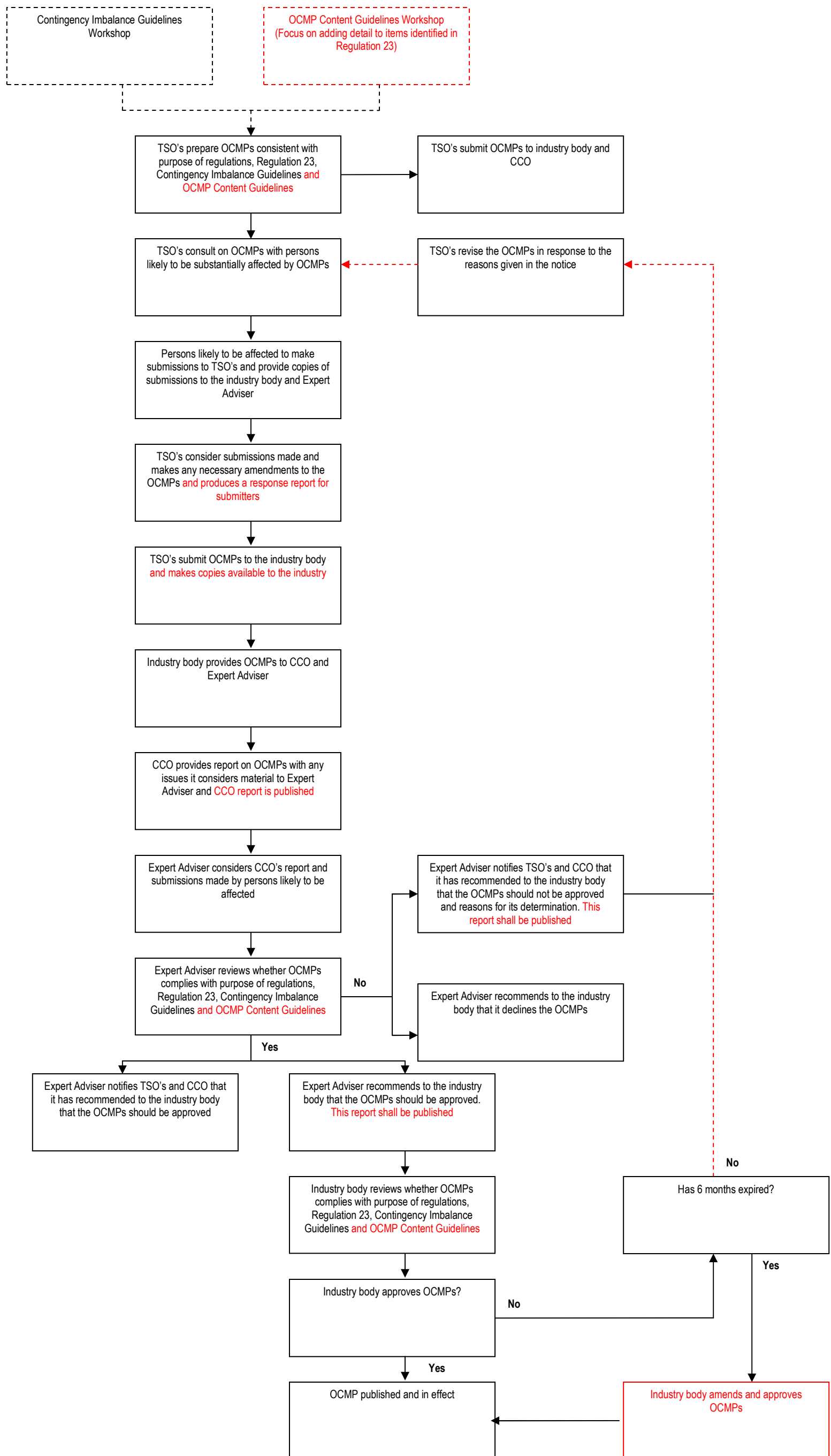
Contact believes that the GIC's proposed process for preparing and approving OCMPs can be modified to ensure that:

- i. industry expertise and experience is fully utilised in the development of the OCMPs by developing a set of OCMP content guidelines. These guidelines would specify the detail of the OCMP content required under Regulation 23 through a consultation process with input from shippers, TSO's, users and the GIC;
- ii. no one party with a vested interest should determine how the OCMPs work;
- iii. perverse incentives are not created for individual participants but ensure that optimal arrangements are in place for the industry;
- iv. the expected outputs from working groups and workshops are clear, and that they are effectively facilitated.

The following schematic describes how the process could work with Contact's suggested changes (the changes we have suggested are highlighted in red). It should be noted that we are not proposing that the GIC 're-invent the wheel'. We are confident that the reasoning behind the GIC's proposed process for the development of the OCMPs is largely sound, but believe they could be better represented with greater industry input and transparency.

The key changes suggested by Contact are summarised as follows:

- i. consultation and preparation of OCMP content guidelines;
- ii. requirement for TSO's to produce a response report after industry participants have made submissions on the OCMPs;
- iii. copies of OCMPs submitted to the industry body shall be made available to the industry;
- iv. CCO's report shall be published;
- v. the expert adviser's report to approve or decline the OCMPs shall be published;
- vi. the expert adviser's notification to TSO's and CCO of its recommendation shall be published;
- vii. industry participants shall be given another opportunity to make submissions to TSO's if the OCMPs are revised in response to the expert adviser's notification;
- viii. references to 'proposed OCMPs' have been replaced by 'OCMPs' because the process should apply to both the original OCMPs and any amendments;



Determining the critical contingency price

Contact believes there are issues with regards to the determination of the critical contingency price that have not been satisfactorily resolved to a point where it can be finalised in the regulations.

The regulations propose that a critical contingency price would be determined ex-post of a critical contingency, but in Contact's view it seems that insufficient analysis has been carried out to date to support this approach to pricing as the most appropriate.

It is unclear how the ex-post pricing approach will achieve the objectives set out in regulation 62 for determining a critical contingency price; in fact the ex-ante pricing approach seems more appropriate for producing a signal to the industry that there is a gas scarcity and to incentivise consumers prior to a critical contingency to make alternative fuel arrangements where it is efficient to do so.

Contact does however agree with the GIC that the regulations should set out how the critical contingency price is determined and should not form part of the OCMPs.

Contact recommends that the GIC consults with an industry group on contingency pricing issues to develop a set of pricing guidelines. The benefit of this consultation process is that the issues are exposed to industry scrutiny. This process is also consistent with processes proposed for the development of contingency imbalance guidelines and the OCMP content guidelines.

Contact is currently carrying out analysis on the effects of a critical contingency on the wholesale electricity market, and what this could mean if the critical contingency price is imputed from the prices in the wholesale electricity market. Contact is happy to share this analysis with the GIC and proposes that this analysis be incorporated and considered during the

recommended industry consultation process on the contingency pricing issues.

Appointment of an expert adviser and industry expert

Contact is concerned about the lack of independent people in New Zealand who will also have the skills, experience and industry expertise to be appointed to the important roles of the expert adviser and industry expert.

Contact suggests that the GIC appoints independent persons with the relevant experience and industry expertise from outside New Zealand to ensure impartiality and remove any potential conflict of interest in these critical roles. It would also be useful to have a short-list of people for the role of industry expert at the ready prior to any critical contingency.

Consumer information

One of the issues in respect of existing NGOCP is a lack of reliable information available to pipeline operators about the level of reduction in gas offtake achievable through issuing instructions to curtail loads to various types of user. More reliable information is required to improve the efficiency of contingency management. How more reliable information related to gas usage at the time a contingency event arises can be made available, should be one of the matters for consideration at the industry workshops designed to establish contingency imbalance guidelines.

Contact also believes that the requirement under Regulation 37 for each retailer to provide a notice containing the number and aggregate total annual consumption of its consumers, and to notify the critical contingency operator (CCO) of a change in that consumption (if it is 20% or greater) is impractical and won't provide a meaningful representation of each retailer's share of the daily load relevant to a contingency event.

Contact recommends instead that each retailer provides a notice with average daily consumption for a summer month and a winter month to the CCO, given the variability of seasonal consumption and the fact that curtailment will be based on daily gas take information.

Contact also considers that this information should be supplied disaggregated by consumer together with the consumer's ANZSIC code and its minimal load requirement in accordance with Regulation 42. This additional information will promote transparency and fairness and will aid the CCO in determining whether any retailer's information is materially incorrect as required under Regulation 38. It is unclear how the CCO will make the determination otherwise.

Contact is also concerned about the timeframe in which retailers are required to update the emergency contact details of switched consumers. Contact suggests that Regulation 40 (2) be amended to allow retailers up to 40 business days rather than 5 business days as stated. Contact currently has a monthly process in place to identify any new consumers and collate their emergency details, which includes obtaining contact details and assigning those consumers to the appropriate curtailment band.

Going forward, Contact expects that distributors will make it a requirement in their Use of System Agreements that each retailer advises them on their consumers' curtailment band allocations to enable distributors to update the curtailment band in the registry.

Errors and discrepancies with regulations

Contact has noticed that there are some errors in the OCMRs and discrepancies between the Supplementary Consultation Paper and the OCMRs.

Examples of this include:

- i. regulation 15 (4) should refer to regulation 15 (2) not 14 (2).
- ii. regulation 24 (e) should write 'Consider the submissions made and *make* any necessary amendments...'

In some instances, recommendations made by the GIC in the Supplementary Consultation Paper are not supported through revisions to the OCMRs (for example section 5.10 of the Supplementary Consultation Paper is inconsistent with regulation 6 (c) of the OCMRs).

This list is not exhaustive, and Contact suggests that the GIC checks and reviews the proposed OCMRs in particular to ensure that they are accurate, complete and consistent.

Conclusion

Contact supports the GIC's proposed process for the development of the OCMPs but believes that the OCMPs could be more effective with greater input from the industry at a number of stages during the development process.

Contact also believes that further consideration and analysis needs to be carried out before any regulation to determine the critical contingency price is finalised. We are actively undertaking our own analysis on this issue to ensure that the optimal arrangements are established.

Contact is keen to participate in all workshops to develop these processes and regulations further, as we recognise the importance of the OCMP development process in particular to the efficient operation of the industry.

Questions from Supplementary Consultation Paper

| QUESTION | COMMENT |
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| <p>Q1: Do you consider the proposed deadlock breaker provision (which can only be exercised after a period of 6 months) is an appropriate mechanism to ensure the application of the regulations is not frustrated by any delay in getting the first OCMPs in place?</p> | <p>Contact agrees that the deadlock breaker provision is an appropriate mechanism for putting the OCMPs in place and preventing unnecessary delays.</p> <p>Contact believes that the deadlock breaker provision should also ensure that the OCMPs being put in place to manage a critical contingency are adequate and suitable for the then current circumstances in the industry.</p> <p>Therefore Contact suggests that the deadlock breaker provision should apply to both proposed amendments as well as the proposed OCMPs, because a significant amendment may be required which the existing OCMP might not adequately deal with and therefore could limit the effectiveness of the OCMP during a critical contingency.</p> <p>The deadlock breaker provision with modifications has been included in the schematic above.</p> |
| <p>Q2: What is your view of Gas Industry Co setting the line pack and pressure thresholds as part of recommending the regulations? Do you agree that the approach set out in 5.18 and 5.19 for the setting of the minimum pressure and linepack thresholds is preferred?</p> | <p>Contact's view is that the line pack and pressure thresholds should be set in the OCMPs and not in the regulations.</p> <p>The line pack and pressure thresholds would be specified as part of the OCMP content guidelines, as recommended by Contact above, and these guidelines would be produced in consultation with the industry to capitalise on industry experience and knowledge.</p> |

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| <p>Q3: Do you consider it essential for the CCO, through retailers, to be able to require domestic consumers to comply with curtailment directions or is Gas Industry Co's proposal to exclude domestic consumers adequate for the effective operation of the outage and contingency arrangements?</p> | <p>The current NGOCP load shedding arrangements require Retailers to allocate all commercial/industrial consumers > 2TJ to categories A-F with an expectation that consumers allocated to these categories could be shed in a controlled manner in the event of a supply or transmission constraint. The key purpose of having the various categories was to firstly ensure equitable treatment of Retailers' consumers with similar usage characteristics. It would be expected that Retailers would contact individual consumers and request that they curtail taking gas either immediately or within a defined or reasonable timeframe.</p> <p>All other consumers (domestic consumers and other consumers < 2TJ) by default are allocated to category G. There was never any expectation that consumers in category G would be shed following the same process as for categories A-F as it would be logistically impossible. However if curtailment was ever sought it would be by request via the media (TV, radio, newspaper) rather than demand. Accordingly there is an implicit expectation that Retailers include the right to curtail mass market consumers during a supply or transmission constraint in their retail T&C.</p> <p>The points that appear to have been missed is that for domestic and < 2TJ commercial consumers (group G):</p> <ul style="list-style-type: none"> • They would have very little load to offer to curtailment. • It would be a huge logistic exercise (of little value) to curtail them in a controlled manner. • It is a massive exercise to restore supply to them. • It was never envisaged that Retailers would effect controlled curtailment. <p>If curtailment was ever sought it would be by request via the media (TV, radio, newspaper), which has been done before in extreme circumstances (very limited linepack), rather than contacting individual consumers and requiring curtailment. Nevertheless the GIC should recommend to Retailers that they include the right in their retail T&C to require curtailment, rather than in regulation, which is clearly problematic.</p> <p>Contact therefore agrees that the GIC should exclude domestic consumers from the regulated curtailment bands, but should place an expectation on Retailers that they include the right in their retail T&C to require curtailment of such consumers in the event of supply or transmission constraints.</p> |

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| <p>Q4: Do you agree that the proposed curtailment arrangements outlined in 5.33 and as specified in the schedule to the regulations are appropriate?</p> | <p>Given the CCO's ability to curtail only a subset of load within a curtailment band, Contact is concerned as to how the CCO will determine which subset load to curtail as suggested in 5.34 of the paper. It should be noted that the in its attempt to stabilise the gas system, the CCO's decision could potentially have devastating effects on other industries reliant on gas.</p> <p>It is also unclear as to whether the CCO is the appropriate party to be making decisions that affect other industries, given the CCO's expertise lies within the gas industry. Nothing suggests that the CCO would seek advice from other parties to aid it in making a decision. For example 5.34 does not state that the CCO would seek advice from Transpower when determining which gas fired power stations to switch off.</p> <p>In Contact's view, the review of the curtailment bands is imperative to ensuring that optimal arrangements are in place to manage a critical contingency.</p> |
| <p>Q5: Do you agree that defining contingency imbalances on a sub-day period is more likely to fulfil the objectives, and that the feasibility of this should be examined further?</p> | <p>It is not clear how contingency imbalances on a sub day period could be determined in an environment where most metering is on a daily basis and some on a monthly basis. The example used by the GIC in its last Discussion Paper showed that use of sub day periods could result in those curtailing loads being penalised whereas those who caused the contingency could receive compensation. How that start point and the end point of a contingency are determined, whether use of sub day periods is appropriate and how contingency arrangements relate to the balancing regimes of pipeline codes all require further consideration.</p> |
| <p>Q6: Do you agree that the Gas Industry Co should develop a set of guidelines to clarify some of the detail and help TSOs prepare plans that are workable and consistent with the regulations for determining imbalances?</p> | <p>Yes.</p> |
| <p>Q7: Do you agree that in the case of a regional contingency there is no advantage to putting in place arrangements that would require payments between shippers? If not, please explain your rationale, the way any such payment arrangement would work, and how efficiency would be improved by the requirement for such payments.</p> | <p>It is difficult to determine logic or equity in arrangements that would compensate gas shippers for relinquishing their gas to other parties in some circumstances but not in others. The compensation mechanism developed should have application across all kinds on contingencies.</p> |
| <p>Q8: Do you agree that the independent expert should be required to apply the over-arching principle set out in 5.80 when determining the Contingency Price?</p> | <p>Contact agrees with section 5.80 of the Supplementary Consultation Paper.</p> |

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| Q9: Do you agree that the independent expert should be required to have regard to the issues set out in 5.81 when determining the Contingency Price? | Refer to comments above for determining the critical contingency price. |
| Q10: Do you agree that under the proposed arrangements where the TSO calculates the imbalances, that the TSO should operate a critical contingency cash pool? | The appropriate mechanism should be developed through the proposed industry workshop. |
| Q11: Do you agree that the CCO should be asked to spread its up-front costs over the duration of the agreement? | Yes. |
| Q12: Do you accept the proposed approach to spreading the development costs, and that the final outcome will be dependent on Gas Industry Co's balance sheet capability? | Yes. |
| Q13: Do you agree that it is necessary for the Compliance regulations to include an ability to obtain urgent orders where consumers fail to comply with directions to curtail demand? If not, why not? | <p>Firstly, sections 5.98 to 5.105 of the paper and questions 13 and 14 are inconsistent in their references to "participants" and "consumers", and it is unclear whether the GIC would seek to obtain injunctions/orders on participants, consumers or both.</p> <p>Contact does not think it necessary to include an ability to obtain injunctive relief from the High Court where participants fail to comply with directions to curtail demand.</p> <p>Participants are likely to incur operational costs and they are exposed to legal action as a result of a failure to ensure demand is curtailed. For example, gas supply agreements between suppliers and consumers would need to be checked and amended to include specific provisions to allow the supplier to curtail demand, potentially without notice, and without any liability to the consumer should specified contingency events occur.</p> <p>Injunctions can also be perceived to provide urgent and interim relief to a person who is, or is at risk of, suffering a wrong, but the concept does not automatically mean a right to an immediate court hearing, and therefore may limit the effectiveness of an injunction.</p> |

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| Q14: Do you agree that the ability for Gas Industry Co to apply for an interim injunction in the event that a consumer fails to comply with a direction to curtail demand would be the most effective incentive for compliance? If not, do you think the Rulings Panel would provide a sufficient incentive and if so, why? | It is Contact's view that the threat of applying for an interim injunction would not necessarily be the most effective incentive to ensure compliance with a curtailment order, as there could be a wide range of factors that affect a participant's ability or willingness to comply. The Rulings Panel could directly manage this factor just as effectively, but may need the right to impose more substantial penalties for its powers to be fully effective. |