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25 August 2006

## **SUBMISSION ON REVIEW OF GAS EMERGENCY ARRANGEMENTS**

### **Introduction**

1. Vector welcomes the opportunity to submit on the Gas Industry Company's (GIC) paper discussing the review of gas emergency arrangements.
2. Vector generally supports the GIC's approach to evolving the current industry arrangements to meet the challenges of the new gas supply environment.
3. In summary, Vector's view is that:
  - The evolution of the gas emergency arrangements is a matter of high priority for the industry and the GIC;
  - The new arrangements will have to be mandatory to be effective and should be recommended as regulations to the Minister of Energy;
  - An ex post fair price determination is the most appropriate form of emergency pricing; and
  - The definition of a "fair" pricing outcome needs to be developed ex ante.
4. Vector has provided more detailed discussion of these points (among others) in the attached feedback form. The development of these arrangements will require further detailed analysis and discussion. Vector is happy engage with the GIC to assist its process.

Yours sincerely

A handwritten signature in black ink, appearing to read "P. Hodgson".

Paul Hodgson

**Group Manager Regulatory Strategy**

## Appendix A: Comments

Questions	Comments
<p>Q1 Do you agree that mechanisms to implement arrangements for emergency or contingency situations must be mandatory? If not, please explain.</p>	<p>Yes. Industry experience has demonstrated that some participants will not agree to, and/or comply, with voluntary arrangements. The effectiveness of the emergency arrangements is dependent on full participation so in Vector's view a mandatory solution is the only option in this case.</p>
<p>Q2 Do you agree Gas Industry Co has identified the most likely alternatives for mechanisms to implement arrangements for emergency or contingency situations? If not, please provide details of any other likely alternative mechanisms.</p>	<p>Yes.</p>
<p>Q3 Do you agree with Gas Industry Co's analysis of a Pan-Industry Agreement as a mechanism to implement arrangements for emergency or contingency situations? If not, please explain.</p>	<p>Yes. Industry experience has demonstrated that consensus on policy issues is very difficult to achieve. In fact, the establishment of the GIC itself was recognition of the need for an industry wide decision-making body.</p>
<p>Q4 Do you agree with Gas Industry Co's analysis of rules or regulations as a mechanism to implement arrangements for emergency or contingency situations? If not, please explain.</p>	<p>Yes. As the mandatory arrangements are likely to have wide impact when they are invoked, Vector believes that it is appropriate that they are promulgated as regulations and considered by Cabinet. In particular, they are likely to impose obligations on parties to forego or supply gas for public good reasons such as maintaining supply to essential customers.</p>

Questions	Comments
Q5 Do you believe the gas emergency arrangements are most appropriately implemented by rules or regulations recommended to the Minister of Energy? If not, please explain..	Vector believes that it is appropriate that they are promulgated as regulations and considered by Cabinet. In particular, they are likely to impose obligations on parties to forego or supply gas for public good reasons such as maintaining supply to essential customers.
Q6 Do you agree with Gas Industry Co's analysis of the framework design for emergency management arrangements? If not, please explain.	Yes, except that the definition of transmission systems should cover only the systems transporting specification gas (i.e. the Maui and Vector Transmission systems) and not transmission pipelines which carry non-specification gas.
Q7 Are there any other principles you believe should be included? If so, please provide details of those additional principles.	Not at this stage. However the development of the detailed arrangements may identify areas where a framework principle is required to resolve issues.
Q8 Do you agree with Gas Industry Co's approach? If not, please explain.	Yes. However, the existing NGOCP really only covers the first 24 hours or so of a contingency. It then leaves the participants to re-establish their supply position. The GIC's proposal for a formal restoration process will help ameliorate potential risks to distribution systems and priority customers until normal supply conditions are achieved.

Questions	Comments
<p>Q9 Do you agree that the gas emergency arrangements should be progressed now, rather than waiting for completion of the wholesale market review? If not, please explain.</p>	<p>Yes. These arrangements are a matter of priority to enable the orderly operation of the industry under emergency conditions. The wholesale market may take some time to progress and furthermore:</p> <ul style="list-style-type: none"> <li>• It is not clear whence the additional gas would be sourced physically;</li> <li>• The resultant market may not send the appropriate signals under emergency conditions, since only a small proportion of the total gas supply is likely to pass through it;</li> <li>• Participants may not respond in time to stabilise the system, noting the first few hours are critical in preventing an emergency becoming a crisis situation; and</li> <li>• The long established electricity market has recently experienced difficulties under emergency conditions.</li> </ul> <p>A market-based solution in an emergency may result in a shipper only being able to access gas at a price they can not afford which raises the issue of who supplies that shipper's "uninterruptible" customers.</p>
<p>Q10 Do you agree that the current definition of "Gas Contingency" should be amended? If not, please provide reasons.</p>	<p>Probably. However, the definitions are likely to be an outcome of the policy process, i.e. are determined to give effect to the intended arrangements, rather than being a starting point.</p>

Questions	Comments
<p>Q11 If you agree that the definition should be amended:</p> <p>(a) do you agree that an 'effects-based' decision is most appropriate?</p> <p>(b) do you have any suggestion as to a basic operational minimum level to underpin the definition?</p> <p>(c) what, if any, degree of discretion should there be to determine that a Gas Contingency has occurred?</p> <p>(d) how would you define "Gas Contingency"?</p>	<p>The definitions are likely to be an outcome of the policy process, i.e. are determined to give effect to the intended arrangements, rather than being a starting point.</p>
<p>Q12 Do you consider there should be a separate definition for regional and national contingencies, or some other split? If yes, please indicate how and why (including draft definitions)</p>	<p>Some distinction is likely to be warranted. The discussion document and workshop appeared to result in general agreement that there is a distinction between a supply failure and a pipeline failure.</p> <p>Currently, a regional contingency is, almost by definition, a pipeline problem. The issue is not gas supply but the ability to get the gas through. In the Pohangina bridge incident, the restriction resulted in load shedding and allocating line pack amongst shippers on the downstream side of the pipeline constraint.</p> <p>The detailed policy may result in different approaches to managing the emergency and subsequent emergency pricing regime. The definitions should reflect the intent of the policy and be clear enough to support the desired outcomes.</p>

Questions	Comments
<p>Q13 Do you agree that the current definition of "Transmission System" should be amended? If not, please provide reasons. If yes, please provide a draft definition.</p>	<p>Yes. As far as possible it is appropriate to define the system in neutral terms. In this respect a link to physical infrastructure would appear logical. The definition of transmission systems should cover only Transmission systems that deliver specification gas to distribution networks and direct connected users..</p>
<p>Q14 Do you agree that the current definition of "NGC Transmission" should be replaced with a more generic definition of "System Operator" (or similar) as proposed? If not, please provide reasons.</p>	<p>Yes.</p>
<p>Q15 Do you agree with the scope of the proposed obligations to be imposed upon industry participants? If not, please provide reasons.</p>	<p>Yes.</p>
<p>Q16 What, if any, other carve-outs to the proposed obligations of industry participants do you believe are necessary?</p>	<p>Any carve-outs need to be explicitly defined ex ante. As for definitions, any carve-outs are likely to be an outcome of the policy process, i.e. are determined to give effect to the intended arrangements, rather than being a starting point.</p>
<p>Q17 Do you agree with the proposed approach to the liability of industry participants? If not, please provide reasons.</p>	<p>Yes.</p>

Questions	Comments
<p>Q18 Is Gas Industry Co's belief that the proposed gas emergency arrangements will not require significant additional processes and systems to be developed correct? If not, please explain.</p>	<p>The past arrangements are no longer adequate. Vector's view is that any additional processes that are required are likely to be necessary for the development and safe operation of the industry in the post-Maui Contract supply environment. In other words, the processes are likely to be the same in any comparison of forward looking factials and counterfactuals. The policy issue is to ensure the new arrangements as an overall package are cost effective and practical.</p>
<p>Q19 Do you agree that any gas emergency arrangements should be consistent with the processes set out in the MPOC in respect of contingency and emergency situations? If not, please indicate your preferred approach and reasons.</p>	<p>Yes. However, the primary policy objective should be to develop the best practicable emergency arrangements, i.e. developing robust arrangements is the key concern.</p>
<p>Q20 Do you have a preference for the point at which MPOC is superseded by the gas emergency arrangements (e.g. when Phase 2 commences under NGOCP?)</p>	<p>Vector believes the MPOC should be superseded when the gas emergency moves into Phase 2 as defined under the NGOCP.</p>
<p>Q21 Do you consider the Emergency Operator should automatically be the technical/system operator of the transmission system or an independent person? Please provide reasons for your views.</p>	<p>The Emergency Operator should be the System Operator. The SO is involved with the system at all times and a quick response is key under emergency conditions as the first few hours can prevent the situation deteriorating into a crisis. Any other party may be slow to react outside normal business hours. Furthermore the SO has the best understanding of the system and how it will respond.</p>

Questions	Comments
<p>Q22 Do you believe the CCT should be maintained or that the Emergency Operator, or other person, should undertake that role? Please explain your reasons.</p>	<p>Yes. It is useful to have one point of contact for the industry. In developing the detailed arrangements it will be important to review and define who is responsible for which communications. Some communications with parties external to the industry may be best centralised with the Emergency Operator, while other communications may be better handled by the CCT to allow the EO to focus on managing the emergency.</p>
<p>Q23 If you wish to retain the CCT, do you believe its current make-up is appropriate?</p>	<p>As with the definitions, the appropriate make-up of the CCT is likely to be an outcome of the policy process, i.e. is determined to give effect to the intended arrangements, rather than being a starting point.</p>
<p>Q24 What other changes, if any, would you make to the CCT role? Please explain your reasons.</p>	<p>The appropriate role for the CCT is likely to be an outcome of the policy process rather than being a starting point.</p>
<p>Q25 Do you agree with the scope of the proposed powers to be given to the Emergency Operator? If not, please provide reasons.</p>	<p>Yes. As for question 22, it may be that the EO should coordinate external communications with central, regional and local government while other communications are delegated to the CCT.</p>



Questions	Comments
<p>Q26 Do you agree with the proposed approach to the liability of the Emergency Operator? If not, please provide reasons.</p>	<p>Yes. The EO should be liable for acting negligently, fraudulently, or with wilful recklessness, but otherwise protected against claims made by industry participants or third parties in respect of exercising its rights as EO pursuant to the gas emergency arrangements (para 8.18).</p> <p>EO would require immunity against claims made by industry participants (or third parties) in relation to the valid exercise by the EO of its powers under any gas emergency arrangements (para 8.20).</p> <p>The EO will be required to act where an industry participant informs the EO of any event or circumstance which will or might reasonably be expected to give rise to an emergency or contingency situation, but otherwise will be under no obligation to take into account any input received from industry participants during an emergency or contingency situation (except where expressly required to do so by the gas emergency arrangements) (para 8.22)</p>
<p>Q27 Do you agree that the declaration process under the gas emergency arrangements should be more certain (as proposed)? If not, please indicate your preferred approach and reasons.</p>	<p>Yes. The process for declaring an emergency should be certain. In terms of definitions, care is required to not be too prescriptive as all emergency situations differ and involve a varying combination of loads, flows, line pack and pressures.</p>
<p>Q28 Do you agree that the process for moving between phases is currently clear/definite? If not, please indicate any proposed changes.</p>	<p>Yes. The process for moving between phases should be certain. In terms of definitions, care is required to not be too prescriptive as all emergency situations differ and involve a varying combination of loads, flows, line pack and pressures.</p>

Questions	Comments
<p>Q29 Do you agree that all industry participants (and other affected entities, such as major plant owners/operators) should be obliged to comply with directions from the Emergency Operator? If not, please provide details of reasons and any other proposed alternatives for providing certainty.</p>	<p>Yes.</p>
<p>Q30 Do you consider there is any merit in a two-stage approach, with stage one allowing for voluntary response and stage two imposing binding instructions? If yes, why?</p>	<p>No. Vector believes voluntary notices may not be able to be relied upon for the reasons outlined in the discussion paper.</p>
<p>Q31 Should the Emergency Operator be required to maintain a detailed load shedding plan? If so, should all (relevant) industry participants be required to provide detailed supply, demand and load shedding information to the Emergency Operator?</p>	<p>Yes. However the load shedding plan as outlined in the NGOCP needs to be reviewed in light of the reality of distribution network layout, i.e. it may not be physically possible to distinguish between certain categories. It is worth reviewing for each network what can be implemented practically and using this as the basis for the plan.</p>
<p>Q32 Do you agree with the proposed obligations in relation to alternative gas suppliers? If not, please provide reasons.</p>	<p>Yes. Important that in the case of a field failure the emergency arrangements do not incentivise a shipper to instruct its suppliers to curtail production. It would be prudent to ensure the supply system is as far as possible protected from shippers and suppliers gaming the emergency arrangements in the gas or electricity markets.</p>
<p>Q33 Do you agree that a back up/reserve market is not merited? If not, please provide reasons.</p>	<p>Yes for the reasons outlined in the discussion document.</p>

Questions	Comments
Q34 Do you agree that the Emergency Operator should have the ability to direct the supply of non-specification gas? If not, please provide reasons.	No. The gas specification is already wide. Such a policy is likely to encounter problems with pipeline certifiers and OSH which would make it impossible to implement. If non-spec gas entered the system it would not be possible to estimate the flow on impacts for downstream parties. In addition there would be significant problems with purging the system to restore specification gas supply.
Q35 Do you agree with the factors that an Emergency Operator must have regard to in making any such direction? If not, please provide reasons.	Not applicable.
Q36 Are there any other factors the Emergency Operator should have regard to in making any such direction? If so, please detail those additional factors.	Not applicable.
Q37 Do you agree with the proposed approach to restoration? If not, please provide reasons.	Yes. It should be clear. The detailed approach needs further analysis and development.
Q38 Do you have a view on guidelines for establishing a restoration table? Please specify.	The detailed approach needs further analysis and development.
Q39 Do you agree that a post-contingency formal reconciliation process is appropriate? If not, please provide reasons.	Yes. A formal process will be necessary.

Questions	Comments
<p>Q40 Do you have any comments on the proposed groups of types of communications and related obligations? Are there any other communications protocols/information flows which you consider should be taken into account as part of this review?</p>	<p>Not at this stage. In developing the detailed arrangements it will be important to review and define who is responsible for which communications. Some communications with parties external to the industry may be best centralised with the Emergency Operator. For instance some communications and obligations may be most effectively implemented between the EO and distributors rather than via the retailers. In the electricity system the SO directs the lines companies directly on some system security issues.</p>
<p>Q41 Do you agree with the proposed treatment of review, testing and documentation obligations under the NGOCP? If not, please provide reasons. If so, do you have any specific suggestions for how these should be dealt with?</p>	<p>Yes. More detail needs to be developed. Vector is happy to contribute.</p>
<p>Q42 Please provide any comments on how best to set line pack limits and to review these over time.</p>	<p>Vector's view is that the SO (with specific technical input including transmission system simulation etc from the technical operator) is the appropriate party to set line pack limits. This is an asset specific issue rather than a policy issue. Vector has the sole discretion to determine acceptable line pack limits on its own transmission pipelines to support its normal commercial operations.</p> <p>Vector agrees there needs to be greater specification in general terms. This needs to be balanced with the SO's need for flexibility as the emergency conditions are likely to occur within an envelope of factors (i.e. combination of loads, flows, pressures and line pack) rather than simply as a single indicator.</p>
<p>Q43 Do you have views as to the appropriateness of any particular compliance regime? Please specify.</p>	<p>Since mandated by rules or regulations, non compliance should be dealt with by that regime in the Gas Act.</p>

Questions	Comments
Q44 What is your view of WMWG's comment on the Farrier-Swier Consulting recommendations?	Vector agrees with the WMWG which has spent several months considering options for the wider industry good.
Q45 Do you agree the ex post fair price determination is a suitable model for developing emergency pricing? If not, please provide a description of your preferred approach to emergency pricing.	Yes.
Q46 Do you agree these are a comprehensive set of principles and objectives? If not please provide your augmentable list(s) and reasoning.	<p>Largely. Some issues need to be assessed particularly given the distinction between field outage and pipeline failure. In the former case, a shipper may have actively developed a portfolio of supply and so should not have to carry the costs of shippers who are reliant on a single supplier.</p> <p>The regime must recognise that gas supply is one element of the wider energy supply system so parties may experience impacts in other markets, i.e. a generator with supply obligations (i.e. hedges) in the electricity market may have to meet its shortfall by buying at the spot electricity price.</p> <p>At the same time, a gas supplier who is required to continue to supply to essential customers for social good reasons should not have to bear the costs of emergency priced gas which may be unrecoverable from the users.</p> <p>Consideration may have to be given to an ex post GIC levy for the purpose of reconciling these unavoidable costs of supply obligations under emergency conditions.</p> <p>Vector is happy to contribute to further analysis and discussion of this issue.</p>

Questions	Comments
<p>Q47 What is your view of the line pack being notionally allocated across shippers in proportion with their nominations? If you disagree, what would be your preferred approach and why?</p>	<p>This area needs further discussion and analysis. There is no nominations regime on the Vector transmission system so the proposal could only be applied to the Maui Pipeline. On the Vector system, allocation in proportion to reserved capacity may be an option. During an emergency allocation needs to be driven by system security considerations. These may vary between distribution networks. Clarity is necessary ex ante for each network as to which customers would need to be supplied as a priority. The ex post pricing determination needs to reflect these obligations. Vector is happy to contribute to further analysis and discussion of this issue.</p>
<p>Q48 In the absence of a transparent, short-term market for gas in New Zealand, what is your view of using an independent expert to set emergency prices ex post?</p>	<p>It is a good idea. The industry needs a practical solution.</p>
<p>Q49 If you disagree with the use of an independent expert, what should be used as the basis for determining emergency gas prices and how is this superior?</p>	<p>Not applicable.</p>
<p>Q50 In the event of a pipeline interruption, how do you view the pro rata allocation of line pack among shippers as a means of consistently applying the emergency pricing framework? If you disagree, what alternative arrangement would you suggest and why?</p>	<p>This issue needs further discussion and analysis. Vector reserves its position in relation to the details of the emergency pricing regime.</p>

Questions	Comments
Q51 Do you agree that for an emergency pricing framework to operate in a low-cost manner it will be essential for the overall emergency plan to be a mandatory arrangement (irrespective of whether that is implemented by rules, regulations or a multilateral contract)?	Yes.
Q52 What is your view of requiring parties to endeavour to settle their positions in the first instance by trading among themselves?	Not sure voluntary trading will be productive as parties may want to see what the independent expert comes up with. It may be more practical to simply have the expert determination, particularly if the regime addresses the issues raised in response to question 46.
Q53 Do you agree that there should be a limit below which parties are not able to enter the emergency pricing framework?	Yes.
Q54 What is your view of the price determination process? Do you agree that using a desktop study is the best approach?	It should be clearly defined and provide the opportunity to appear in person in a similar manner to an arbitration.
Q55 Please provide any other comments on the procedural steps.	No response.
Q56 What is your view of the appropriate body to undertake the role of determining emergency pricing whilst keeping the costs to a minimum?	Certainly needs to be an independent body using a similar approach as for a commercial arbitration. If the Rulings Panel is going to do the role, a procedure for co-opting lay experts should be developed ex ante so the process is clear for all parties.