



Recommendation to the Minister of Energy on Critical Contingency Amendments to Gas Compliance Regulations

June 2008





About Gas the Industry Co

Gas Industry Co was formed to be the co-regulator under the Gas Act.

As such, its role is to:

- recommend arrangements, including rules and regulations where appropriate, which improve:
 - the operation of gas markets;
 - access to infrastructure;
 - and consumer outcomes;
- administer, oversee compliance with, and review such arrangements; and
- report regularly to the Minister of Energy on the performance and present state of the New Zealand gas industry, and the achievement of Government's policy objectives for the gas sector.

Authorship

This paper was prepared by Ian Dempster and Tristan Meo of Gas Industry Co, and Ben Farrington and Lee Wilson of Concept Consulting Group.

Executive summary

Gas Industry Co is recommending regulations providing for the effective management of critical gas contingencies, called the Gas Governance (Critical Contingency Management) Regulations (the 'proposed Regulations'). The proposed Regulations include mandatory processes for the management of critical contingencies, including compliance with curtailment instructions. An effective compliance regime is crucial to ensuring that the proposed Regulations achieve their purpose.

In May 2007, Gas Industry Co recommended that it establish a regime for enforcement of the Gas (Switching Arrangements) Rules 2008 through the Gas (Compliance) Regulations – now called the Gas Governance (Compliance) Regulations (the 'Compliance Regulations'). The proposed Compliance Regulations provide for:

- a Market Administrator which has responsibility for receiving notices of reported breaches of the rules, attending to administrative tasks, determining the materiality of breaches, and attempting to resolve any immaterial breach with the agreement of the parties;
- an Investigator who investigates material or unresolved immaterial breaches, endeavours to settle the matter, and refers settlements and unresolved breaches to the Rulings Panel; and
- a one-member Rulings Panel which approves or rejects settlements, determines unresolved breaches and orders remedies.

The proposed Compliance Regulations have since been amended to apply to the Gas (Processing Facilities Information Disclosure) Rules 2008 and Gas (Downstream Reconciliation) Rules 2008, and are currently before the Minister awaiting approval.

In a Statement of Proposal on critical contingency management arrangements issued in August 2007, Gas Industry Co proposed that the Compliance Regulations be further amended to apply to the proposed Regulations.

The amendments in this recommendation:

- amend the proposed Compliance Regulations to include references to the proposed Regulations, critical contingency operator and participants subject to the proposed Regulations;
- require the critical contingency operator and auditors to notify the market administrator of alleged breaches and allow the market administrator to request further information from the critical contingency operator;

- in relation to the various matters that the market administrator is to consider when considering the materiality of an alleged breach, including a requirement to consider the extent to which the breach was caused by an event or circumstance beyond the reasonable control of the participant;
- include a new provision allowing Gas Industry Co to apply to the High Court for the grant of an interim injunction requiring compliance with the proposed Regulations; and
- include a new provision limiting the liability of the critical contingency for breaches of certain clauses of the proposed Regulations.

The proposed amendments to the Compliance Regulations are set out in full in the attached Appendix A.

Gas Industry Co considers that the application of the amended Compliance Regulations to the proposed Regulations will provide a high degree of confidence that the proposed Regulations will be adhered to, and thereby contribute to the better achievement of the Government's objectives for the wholesale market and better manage the risks surrounding security of gas supply.

Accordingly, Gas Industry Co recommends that the proposed Gas Governance (Compliance) Regulations 2008 be amended as set out in Appendix A of this recommendation.

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Introduction

1.1 Purpose

This recommendation accompanies a recommendation by Gas Industry Co to the Minister of Energy for regulations providing for the effective management of critical gas contingencies, called the Gas Governance (Critical Contingency Management) Regulations (the 'proposed Regulations').

The purpose of the proposed Regulations is to achieve the effective handling of critical gas outages and contingencies without compromising long-term security of supply. An effective compliance regime is crucial to ensuring that the proposed Regulations achieve their purpose.

Gas Industry Co is recommending regulations that:

- establish procedures for effective management of a critical contingency;
- identify the onset of a critical contingency;
- provide for the appointment of a Critical Contingency Operator (CCO) whose primary role is to restore the supply/demand balance by targeted curtailment of load; and
- establish a price which is used to settle inadvertent trading between those parties whose suppliers have failed and those parties who have access to supplies but whose customers have been curtailed.

In order to achieve the purpose of the proposed Regulations, it will be necessary to enforce compliance with them. In May 2007, Gas Industry Co made a recommendation to the Minister of Energy (the Minister) for Gas (Compliance) Regulations (the 'Compliance Regulations') to enforce the recommended Gas (Switching Arrangements) Rules ('Switching rules').

In February 2008, the Minister approved the Switching Rules which are now in effect. In May 2008, the Minister also approved the following rules recommended by Gas Industry Co:

- Gas (Processing Facilities Information Disclosure) Rules, which require disclosure of certain information by owners of gas processing facilities; and

- Gas (Downstream Reconciliation) Rules, relating to the downstream allocation and reconciliation of gas.

All of the above rules were accompanied by recommendations to amend the Compliance Regulations to apply to those rules. The Compliance Regulations, and the amendments described above, are currently awaiting final approval by the Minister before going through the formal regulation-making process.

This recommendation proposes that the Compliance Regulations be further amended to apply to the proposed Regulations.

1.2 Background

In its May 2007 recommendation, Gas Industry Co recommended that it establish, through regulations, a regime for enforcement of the Switching rules. The work undertaken to design, and consult upon, the proposed compliance regime is set out in detail in the May 2007 recommendation.

The compliance regime is made up of:

- a Market Administrator which has responsibility for receiving notices of reported breaches of the rules or regulations, attending to administrative tasks, determining the materiality of breaches, and attempting to resolve any immaterial breach with the agreement of the parties;
- an Investigator who investigates material or unresolved immaterial breaches, endeavours to settle the matter, and refers settlements and unresolved breaches to the Rulings Panel; and
- A one-member Rulings Panel which approves or rejects settlements, determines unresolved breaches and orders remedies.

In a Statement of Proposal on the arrangements for managing critical contingencies issued in August 2007, Gas Industry Co defined the regulatory objective as being to achieve the effective handling of critical gas contingencies without compromising long-term security of supply. Gas Industry Co considered that the reasonably practicable option that best met the regulatory objective was to develop regulations to govern critical contingency management. In section 10 of the Statement of Proposal, it was suggested that, in order to enforce compliance with the proposed Regulations, the Compliance Regulations be amended to apply to the proposed Regulations.

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Process to establish regulations

2.1 Legislative powers

Power to make regulations for compliance and enforcement

The specific powers in the Gas Act 1992 (the Act) which allow Gas Industry Co to recommend regulations in respect of the management of critical contingencies are described in section 3.1 of the recommendation for proposed Regulations.

In addition, section 43G(2) of the Act provides that the Minister of Energy can recommend to the Governor-General the making of regulations for the purpose of:

- (i) providing procedures for resolving disputes between industry participants;
- (j) providing for the operation and facilitation of those dispute resolution procedures by a person, and the powers and procedures of that person;
- (k) providing for compliance with gas governance regulations and rules to be monitored and enforced by the industry body or the Commission or any other person or court, and the powers and procedures of that person or court;

Specific provisions relating to enforcement and compliance

Subpart 1 of Part 4A of the Act sets out a broad framework for enforcing compliance with any gas governance rules and regulations made pursuant to Part 4A. The provisions within the Act:

- contemplate that a Rulings Panel may be established;
- include limits on investigation powers for monitoring and enforcing compliance with gas governance regulations and rules, obligations on industry participants to co-operate with any investigation, and privileges protection (sections 43U to 43W);
- contain a list of the orders that the Rulings Panel can make (sections 43X and 43Y);
- impose limits on tort claims against service providers (section 43Z); and
- establish rights of judicial review and appeal to the Courts (sections 43ZA to 43ZJ).

Supplementary powers

In addition, section 43S of the Act includes supplementary empowering provisions applying to any regulation or rule made under Subpart 1 of Part 4A of the Act (which includes the proposed Regulations). Those provisions include the ability for rules or regulations to:

- (a) provide for 1 or more persons or bodies or groups of persons to carry out functions in relation to those regulations or rules, and for matters concerning their establishment, constitution, functions, members (including their appointment, removal, duties, and protection from liability), procedures, employees, administration and operation, funding by participants, and reporting requirements:
- (b) provide for systems, processes and procedures (including dispute resolution procedures), and the keeping, supply and disclosure of information, in relation to any matters specified in this subpart:
- (c) prescribe the form and manner in which information is to be disclosed:
- (d) require disclosed information, or information from which disclosed information is derived (in whole or in part), to be certified, in the prescribed form, by persons belonging to any specified class of persons:
- (e) prescribe when and for how long information must be disclosed:
- (f) exempt or provide for exemptions (including provide for the revocation of exemptions), on any terms and conditions, of any person or class of persons from all or any of the requirements in regulations or rules made under this subpart:
- (g) provide for the supply of information for the purpose of administration and enforcement of this Act, and regulations and rules made under this Act:
- (h) provide for transitional provisions:
- (i) provide for any other matters contemplated by this Act or necessary for its administration or necessary for giving it full effect.

2.2 Legal requirements when recommending rules or regulations

Section 43L – consultation

Before recommending rules or regulations to the Minister, Gas Industry Co must comply with section 43L(1) of the Act. That section requires Gas Industry Co to:

- (a) undertake an assessment under section 43N; and
- (b) consult with persons the recommending body thinks are representative of the interests of persons likely to be substantially affected by the proposed regulations; and
- (c) give those persons an opportunity to make submissions; and
- (d) consider those submissions.

A summary of the consultation undertaken by Gas Industry Co is provided in section 4 of this recommendation.

Section 43N(1) – identification and assessment of options

Under section 43N(1) of the Act Gas Industry Co is required to:

- (a) seek to identify all reasonably practicable options for achieving the objective of the regulation; and
- (b) assess those options by considering-
 - (i) the benefits and costs of each option; and
 - (ii) the extent to which the objective would be promoted or achieved by each option; and
 - (iii) any other matters that the industry body or the Commission considers relevant; and
- (c) ensure that the objective of the regulation is unlikely to be satisfactorily achieved by any reasonably practicable means other than the making of the regulation (for example, by education, information, or voluntary compliance); and
- (d) prepare a statement of the proposal for the purpose of consultation under section 43L(1).

Section 43N(2) – statement of proposal

Section 43N(2) requires that the statement of proposal referred to in section 43N(1)(d) must contain:

- (a) a detailed statement of the proposal; and
- (b) a statement of the reasons for the proposal; and
- (c) an assessment of the reasonably practicable options, including the proposal, identified under subsection (1); and
- (d) other information that the industry body or the Commission considers relevant.

A summary of Gas Industry Co's Statement of Proposal, including the assessment of the options identified, is provided in section 3 of this recommendation.

Conclusion

Gas Industry Co considers that it has complied with all of the requirements of sections 43L and 43N of the Act.

2.3 Rules or regulations

Section 43Q

Under section 43Q(1) of the Act, the Minister may make a rule for all or any of the purposes for which a gas governance regulation may be made.

When deciding to make a rule rather than a regulation, under section 43Q(2) of the Act the Minister must have regard to only:

- (a) the importance of the rule, including whether the rule has a material effect on the rights and interests of individuals:
- (b) the subject matter of the rule, including whether the rule contains detailed or technical matters rather than matters of general principle:
- (c) the application of the rule, including-
 - (i) whether the rule applies principally to a particular group (e.g. industry participants) rather than the general public:
 - (ii) whether the benefits of publication in accordance with section 43R rather than the Acts and Regulations Publication Act 1989 outweigh the costs of publication by that method:
- (d) the expertise and rule-making procedures of the recommending body.

Conclusion

Gas Industry Co considers that the proposed amended compliance and enforcement arrangements are important in that they:

- govern the rights of individuals in respect of the imposition of remedies;
- govern investigative powers and obligations to co-operate with investigations, including a right of entry into industry participants' premises, as specified by the Act;
- govern the possible remedies, including compensation, available to a person affected by a participant's breach of the proposed Regulations, as specified by the Act; and
- create a dispute resolution body defined by the Act for the purposes of the proposed Regulations.

Given that the proposed compliance regime:

- contains matters of general principle in the determination of regulation breaches and disputes rather than technical or detailed matters;

- governs how disputes between industry participants will be resolved, and the integrity of the regulations maintained; and
- has a wider application than industry participants (as some aspects of the compliance framework for critical contingency management can affect consumers, who also have a right to report regulation breaches);

Gas Industry Co has recommended that compliance and enforcement of the proposed Regulations should be implemented by way of amending the current Compliance Regulations.

Publication of notice in Gazette

Gas Industry Co must, no later than 10 working days after it gives a recommendation to the Minister for a gas governance rule or regulation, publicise that recommendation and the assessment completed under section 43N. The recommendation will be made available on Gas Industry Co's website and notified in the Gazette for that purpose. A copy of the website and Gazette notices are set out in Appendices C and D respectively.

3

Statement of Proposal and Assessment

3.1 Statement of proposal

One of the potential issues with any regime for managing critical contingencies is the difficulty of enforcing ongoing compliance with the regime.

As required by the Act, section 10 of the August 2007 Statement of Proposal contained a detailed proposal for enforcement of the proposed Regulations, a statement of the reasons for the proposal, an assessment of the reasonably practicable options, including the proposal, and confirmation that there is no other information that Gas Industry Co considers is relevant. A copy of the proposed Compliance Regulations, as amended, was attached as Appendix D to the Statement of Proposal. In the Supplementary Consultation Paper issued in December 2007, a further amendment to the Compliance Regulations was proposed allowing Gas Industry Co to seek urgent injunctive relief from the High Court in respect of breaches of the proposed Regulations.

The proposed amendments to the Compliance Regulations:

- add a reference to the proposed Regulations to the purpose statement in regulation 3.
- in regulation 4:
 - insert a definition of 'critical contingency operator';
 - amend the definition of 'participants' to include industry participants, the industry expert and expert adviser subject to the proposed Regulations; and
 - amend the definition of 'rules' in regulation 4 to include the proposed Regulations;
- in regulation 11, require the critical contingency operator and auditors to notify the market administrator of alleged breaches;

- in regulation 14, allow the market administrator to request further information from the critical contingency operator;
- in regulation 19(1), inserting a new subclause to ensure the market administrator also considers the extent to which the breach was caused by an event or circumstance beyond the reasonable control of the participant when considering the materiality of an alleged breach:
- include a new provision limiting the liability of the critical contingency operator for breaches of certain clauses of the proposed Regulations; and
- include a new provision allowing Gas Industry Co to apply to the High Court for the grant of an interim injunction requiring compliance with the proposed Regulations.

A copy of the recommended amendments to the Compliance Regulations is attached as Appendix A.

3.2 Assessment

As with other regulatory arrangements proposed by Gas Industry Co, consideration needs to be given to whether the compliance regime should be effected through an industry agreement or regulations. The objective of any compliance regime is to provide a high degree of confidence that any proposed rules or regulations will be adhered to, thereby contributing to the overall achievement of the Government's policy objectives for the gas industry.

Having concluded that the proposed Regulations are required for the effective management of critical contingencies, it follows that it would be most effective for the compliance regime to also be regulated under the Act. Further, as a compliance regime affects people's rights, including empowering a decision-making body to make determinations and impose penalties on parties to such determinations, it is appropriate that the regime should be implemented through regulations under the Act rather than rules.

The costs and benefits of a compliance regime are necessarily linked to ensuring that the benefits of the arrangements which they enforce are achieved. The benefits of the compliance regime are therefore the achievement of the benefits derived from the implementation of those arrangements.

In this case, the benefits of a regime for compliance with, and enforcement of, regulations for critical contingency management is ensuring the achievement of the benefits described in the recommendation for the proposed Regulations (see section 5 of that recommendation). In particular, it is important that compliance be achieved in the most efficient manner possible.

The likely range of costs for a compliance regime was set out in Appendix 3 of the May 2007 Compliance recommendation for the Switching rules. These covered all of the initial establishment and set up costs for the regime, including appointment of investigators and the Rulings Panel.

As those costs will have already been incurred, the costs of providing for compliance with the proposed Regulations will only consist of the incremental cost of amending the Compliance Regulations to apply to those regulations, and any additional workload for the compliance roles set out in section 1.2 above. It is not envisaged, for example, that application of the Compliance Regulations to the proposed Regulations will require appointment of additional personnel to any of those roles.

Gas Industry Co notes, though, that any increased compliance costs will be able to be recovered from industry participants through the ongoing fees set out in the Compliance Regulations.

4 Consultation

4.1 Section 43L

Section 43L of the Act requires Gas Industry Co to:

- consult with persons that Gas Industry Co thinks are representative of the interests of persons likely to be substantially affected by the proposal;
- give those persons the opportunity to make submissions; and
- consider those submissions.

These consultation obligations also apply to a recommendation to amend rules or regulations.

4.2 Consultation undertaken

A number of documents have been issued in the process of developing this recommendation. The first document was issued in July 2006 and discussed the framework for analysis and a proposed approach for dealing with the issues. Feedback on that paper caused Gas Industry Co to revise its approach and that resulted in a series of consultations, described below, which led to this recommendation.

Statement of Proposal

A Statement of Proposal was issued in August 2007 and submissions were sought from all of the persons listed in Appendix A. Submissions on the Statement of Proposal were received from 7 industry participants:

- Contact Energy Ltd (Contact);
- Genesis Power Ltd (Genesis);
- Maui Development Ltd (MDL);
- Methanex New Zealand Ltd (Methanex);

- Mighty River Power Ltd (Mighty River Power);
- Nova Gas Ltd (Nova); and
- Vector Ltd (Vector)

Submitters generally supported the proposed approach for the application of the Compliance Regulations to the proposed Regulations and indicated acceptance that a regulated solution was the appropriate mechanism for enforcing the proposed Regulations.

Genesis had a concern over the proposed limitation of the CCO's liability under the Compliance Regulations i.e. liability limited to the amount of the CCO's annual service provider fee. Genesis considered that some thought should be given to other remedies, given the immunity from tort liability afforded to service providers under the Act.

Gas Industry Co acknowledges the concerns expressed by Genesis, but believes that it would not be appropriate to seek to impose significant liability on the CCO, as this would either be reflected in the price charged under the relevant service provider agreement, or make it impossible to find a party willing to take on the role. It is for this reason that Gas Industry Co is proposing a limit on the CCO liability to provide an appropriate balance between the likely cost to a participant of a breach by the CCO, and the level of risk that the CCO is prepared to bear without adversely impacting upon service provision.

Supplementary consultation paper

Following the submissions analysis on the Statement of Proposal an industry workshop was held to discuss the amendments which Gas Industry Co was proposing to address the issues raised in submissions. In December 2007 a further paper was released for consultation: *Gas Outage and Contingency Management Arrangements—Supplementary Consultation Paper*.

This paper also proposed that an additional amendment be made to the Compliance Regulations to provide for Gas Industry Co to either seek urgent injunctive relief from the High Court or obtain urgent orders from the Rulings Panel, where the proposed Regulations were not being complied with. An equivalent provision exists under the Electricity Governance Regulations 2003 providing for the Electricity Commission to seek interim injunctions from the High Court for regulation or rule breaches.

Submissions were received from 8 industry participants (those who submitted on the Statement of Proposal plus Energy Direct NZ), and 5 submitters directly addressed this issue. Submissions demonstrated general support for the suggested amendment with access to the High Court being the preferred option, although one submitter considered the Rulings Panel option would be equally effective.

Gas Industry Co considers that it is desirable for it to have the ability to seek urgent injunctive relief from the High Court to ensure compliance with the proposed Regulations (for example, any obligations to curtail). This is particularly so in longer term or more severe critical contingencies, even if that option should be (as is hoped) rarely needed. This additional amendment has therefore been included in the recommended amendments to the Compliance Regulations.

Short-form consultation paper

Following release of the Supplementary Consultation Paper, Gas Industry Co also consulted with MED and PCO regarding the form and content of the proposed Regulations and amendments to the Compliance Regulations. Issues were identified in respect of the proposed Regulations that needed to be addressed and some of these were of such significance that further consultation was warranted. No such issues arose for the proposed amendments to the Compliance Regulations.

In May 2008 Gas Industry Co released *Gas Critical Contingency Management Arrangements—Short-form Consultation Paper*. Submissions were received from 9 industry participants (those who submitted on the Supplementary Consultation Paper plus PowerCo). No major concerns regarding the proposed amendments to the Compliance Regulations were raised in those submissions.

One submitter queried who urgent injunctive relief may apply to but no further amendment to the Compliance Regulations is considered necessary. Vector, who are to be appointed as the initial CCO under the proposed Regulations, also had some queries regard the scope of the CCO's potential liability under the Compliance Regulations. Gas Industry Co has discussed those queries in detail with Vector. While satisfied that no substantial amendments should be made to the Compliance Regulations to address those queries, Gas Industry Co has included an additional clarification to ensure the market administrator also considers the extent to which a breach was caused by an event or circumstance beyond the reasonable control of the participant when considering the materiality of an alleged breach.

4.3 Conclusion

Gas Industry Co considers it has complied with its obligations under section 43L of the Act.

The consultation process undertaken by Gas Industry Co has allowed extensive opportunity for industry and consumer comment. In addition to the formal consultations outlined above, Gas Industry Co has also held four industry workshops on the proposed arrangements in July 2006, May 2007, August 2007 and November 2007 and frequently met with various industry participants to discuss their views on the proposed arrangements. Since April 2008, Gas Industry Co has also been engaging and consulting with the Contingency Management

Implementation Group (CMIG) on matters concerning the implementation and refinement of the proposed Regulations and Compliance Regulations.

5

Potential risks

The key risks identified by Gas Industry Co with the proposal for the Compliance Regulations to cover the proposed Regulations are:

- Greater implementation costs for compliance than the range predicted resulting from less efficient processes than anticipated, and/or greater reported non-compliance with the proposed Regulations than expected, and/or a greater number of breaches than anticipated which are determined to be 'material' and referred to an Investigator for investigation. Such additional compliance costs could erode some of the benefits for participants (and, indirectly, potentially consumers) in introducing the proposed Regulations.
- The voluntary reporting of breaches by industry participants may result in undetected non-compliance with the proposed Regulations, which may ultimately erode confidence in the regime.
- The possibility that some consumers (those who do not purchase gas from a gas wholesaler or off the wholesale market) do not comply with a direction to curtail the use of gas. While these types of consumers are covered by the Compliance Regulations, the Rulings Panel may not make the orders specified in section 43X of the Act in respect of these consumers. There is arguably potential here for some consumers to exploit this aspect of the compliance regime.

Gas Industry Co considers that these risks are not sufficiently material to detract from the overall benefit of the proposal because of the following:

- Gas Industry Co is confident that participants can comply with the proposed Regulations, as they have been recommended after extensive industry, government and consumer involvement in their development. It must also be remembered that it is anticipated that critical contingencies are expected to occur rarely.¹
- The risk associated with introducing a voluntary reporting regime is balanced by the mandatory obligation on the CCO and auditors to report breaches that they detect.

¹ Under the existing NGCOP arrangements, Gas Industry Co understands that the last equivalent Phase2 contingency occurred in June 2007, and prior to that in February 2005.

- Gas Industry Co notes that only in very severe critical contingencies will consumers who do not purchase gas from a gas wholesaler or from the wholesale market need to be curtailed. Such consumers fall within the last bands of consumers that can be curtailed. As such, this risk will very rarely arise – perhaps once every 3-4 years.² Moreover, the risk does not arise in relation to domestic consumers, as the Compliance Regulations and the proposed Regulations do not apply to domestic consumers. In addition, any residual risk is mitigated by the following:
 - Gas Industry Co has the ability to seek an urgent injunction against any non-complying consumers.
 - Previous experience also suggests high levels of consumer compliance in accordance with curtailment requests.
 - Gas Industry Co understands most retailers’ contractual arrangements with their consumers require compliance with any curtailment directions issued by the retailer.
 - There are existing powers in the Act for distributors to enter land to maintain the continuity or safety of the supply and distribution of gas.

Accordingly, in light of all of these factors, Gas Industry Co does not consider this risk to negatively impair the operation of the Compliance Regulations or the proposed Regulations. Gas Industry Co will, however, monitor this situation over the coming years and, if the risk is in fact greater than anticipated, consider possible regulatory or legislative changes to address this concern.

² It is worth noting that this risk only relates to curtailment where there is a critical contingency in the transmission system, as declared under the proposed Regulations. There may be other situations where domestic consumers are asked by distributors or retailers to curtail their gas supply due to a problem with the distribution system – however such situations are outside the ambit of the proposed Regulations and the Compliance Regulations.

6

Gas Act objectives

6.1 General objectives

The Government Policy Statement (“GPS”) sets out the Government’s objectives and outcomes for governance of the New Zealand gas industry. Under section 43ZO of the Act, Gas Industry Co must have regard to those objectives and outcomes when making recommendations for gas governance rules or regulations.

The Government’s overall policy objective for the gas industry, as stated in the Act and the GPS, is:

“To ensure that gas is delivered to existing and new customers in a safe, efficient, fair, reliable, and environmentally sustainable manner.”

Section 43ZN(b) of the Act sets out the other objectives which are:

- (i) the facilitation and promotion of the ongoing supply of gas to meet New Zealand’s energy needs, by providing access to essential infrastructure and competitive market arrangements:
- (ii) barriers to competition in the gas industry are minimised:
- (iii) incentives for investment in gas processing facilities, transmission, distribution, energy efficiency and demand-side management are maintained or enhanced:
- (iv) delivered gas costs and prices are subject to sustained downward pressure:
- (v) risks relating to security of supply, including transport arrangements, are properly and efficiently managed by all parties:
- (vi) consistency with the Government’s gas safety regime is maintained.

The 2004 GPS was the applicable GPS under which the critical contingency arrangements were developed until April of this year when the 2008 GPS was issued. The relevant key outcome in the 2004 GPS is that “(h) *Risks relating to security of supply, including transport arrangements, are properly and efficiently managed by all parties*”.³

³ Other relevant specific outcomes listed include:

The 2008 GPS repeats the same overall policy objective for the gas industry as set out in the 2004 GPS, as well as the same specific objective regarding the proper and effective management of risks relating to security of supply.

However, the specific outcomes sought by the Government for critical contingency management and compliance arrangements are even more clearly expressed in paragraph 13 of the 2008 GPS:

Critical contingency management

Sound arrangements for the management of critical gas contingencies....

Other outcomes

Gas governance arrangements are supported by appropriate compliance and dispute resolution processes.

In the Statement of Proposal, the objective of the proposal was stated to be to recommend arrangements to *“achieve the effective handling of critical gas contingencies without compromising long-term security of supply”*. Further, that such arrangements should:

- explicitly recognise the value of gas during critical contingencies and include provisions for parties to pay, and be paid for, inadvertent gas trades;
- provide incentives for parties to factor in security of supply as one of the inputs for business planning;
- be transparent and provide for reasonably predictable outcomes in the way that critical contingencies are managed; and
- wherever possible, be compatible with the commercial arrangements that operate under “business as usual” circumstances.

Gas Industry Co concludes in the recommendation on the proposed Regulations that establishing critical contingency management arrangements in accordance with that recommendation is consistent with the regulatory objective (see section 8.1 of that recommendation).

-
- (a) The facilitation and promotion of the ongoing supply of gas to meet New Zealand's energy needs, by providing access to essential infrastructure and competitive market arrangements;
 - (b) Energy and other resources are used efficiently;...
 - (e) The full costs of producing and transporting gas are signalled to consumers;...
 - (i) Consistency with the Government's gas safety regime is maintained.
 - (j) The gas sector contributes to achieving the Government's climate change objectives by minimising gas losses and promoting demand-side management and energy efficiency.

6.2 Objectives for compliance and enforcement

Consideration of any compliance and enforcement arrangements to support the proposed Regulations needs to fit within the Government's overall policy objective for the gas industry and the specific outcomes it is seeking for critical contingency management as outlined above.

The regulatory objective for the Compliance Regulations is⁴:

To provide a high degree of confidence that the proposed switching rules will be adhered to, and thereby contribute to the better achievement of the Government's policy objectives for the retail sector of the gas industry.

Gas Industry Co believes that the same regulatory objective should apply to any compliance and enforcement regime proposed in relation to the proposed Regulations.

The specific outcome sought by the Government for compliance arrangements expressed in paragraph 13 of the 2008 GPS is also relevant here. Gas Industry Co considers the amendments to the Compliance Regulations are appropriate to support the gas governance arrangements set out in the proposed Regulations.

Gas Industry Co considers that the proposed amendments to the Compliance Regulations will meet both the regulatory objective and the specific compliance outcome expressed in the 2008 GPS.

⁴ As specified in the May 2007 recommendation for the Compliance Regulations to enforce the Switching rules.

7

Other issues

7.1 Consultation with Ministry of Economic Development

Representatives of the MED have been briefed regularly by Gas Industry Co on the development of both the critical contingency management arrangements and the associated compliance and enforcement arrangements. MED has been issued with all relevant documents in conjunction with the industry stakeholders identified in Appendix B. Consultation has also occurred with the Parliamentary Counsel Office to ensure the proposed amendments to the Compliance Regulations are satisfactory for their purposes. MED officials were provided with a copy of this recommendation prior to it being approved by the Gas Industry Co Board for release to the Minister.

7.2 Communications

In accordance with section 43O of the Act, Gas Industry Co intends publishing, within 10 working days after providing it to the Minister, this recommendation and the assessment completed under section 43N in both the Gazette and on Gas Industry Co's website.

The notice of recommendation to be published in the Gazette is attached as Appendix C.

A draft of the notice to be published on Gas Industry Co's website is attached as Appendix D.

Gas Industry Co also intends to notify stakeholders of the fact that this recommendation has been made and that it is viewable on its website.

8

Recommendation

Under section 43G(2)(k) and section 43S of the Gas Act 1992, Gas Industry Co recommends to the Minister of Energy the amendment of the proposed Gas Governance (Compliance) Regulations as set out in Appendix A of this recommendation.

Appendices

The following appendices are attached to this recommendation:

- Appendix A: Recommended amendments to the proposed Gas Governance (Compliance) Regulations 2008
- Appendix B: List of stakeholders consulted
- Appendix C: Notice for Gazette
- Appendix D: Notice for website

Appendix A Recommended amendments to the proposed Gas Governance (Compliance) Regulations 2008⁵

- Regulation 3 is amended by including new subclause *“(d) Gas Governance (Critical Contingency Management) Regulations 2008.”*
- Regulation 4 is amended by including/amending the following definitions:
 - *“critical contingency operator means the service provider appointed by the industry body under regulation 6 of the Gas Governance (Critical Contingency Management) Regulations 2008”;*
 - The current definition of “participant” is revoked and substituted with the following definition:

“participant—

 - (a) means an industry participant, as defined in the Act; and*
 - (b) includes any of the following, as those terms are defined in the rules:*
 - (i) a registry participant and the registry operator; or*
 - (ii) a facility owner; or*
 - (iii) an allocation participant and the allocation agent; and*
 - (c) for the purposes of the monitoring and compliance of the Gas Governance (Critical Contingency Management) Regulations 2008, also includes a transmission system owner, retailer, shipper, interconnected party, consumer, industry expert, expert adviser and the critical contingency operator, as defined in those regulations.”*
 - The current definition of “rules” is amended by including new subclause *“(d) Gas Governance (Critical Contingency Management) Regulations 2008”*.
- Regulation 11 is amended:
 - by inserting *“or the critical contingency operator”* after “allocation agent” in each case where it appears in subclause (1) and (3);
 - by inserting *“or an audit carried out under regulations 40 and 76 of the Gas Governance (Critical Contingency Management) Regulations 2008”* after “an audit

⁵ Please note the references in these amendments to clause numbers in the proposed Regulations refer to the clause numbers as currently set out in the proposed Regulations as attached to the accompanying recommendation. It is likely that such clause number references will need to be updated as the proposed Regulations and Compliance Regulations amendments go through the formal regulation-making process.

carried out under Part 4 of the Gas (Downstream Reconciliation) Rules 2008” in subclause (4).

- Regulation 14(1)(c) is amended by adding “or the critical contingency operator”.
- Regulation 19(1) is amended by including a new subclause after subclause (h) to state:

“(ha) the extent to which the breach was caused by an event or circumstance beyond the reasonable control of the participant allegedly in breach:”

- The following new regulation is inserted after regulation 39 to enable Gas Industry Co to seek interim injunctions from the High Court:

Interim injunctions

“39A Interim injunctions in respect of actions in breach of Gas Governance (Critical Contingency Management) Regulations 2008

- (1) *The industry body may apply to the High Court for the grant of an interim injunction—*
 - (a) *restraining a participant from doing, or omitting to do, anything that is in breach of the Gas Governance (Critical Contingency Management) Regulations 2008; or*
 - (b) *requiring a participant to do, or omit to do, something in accordance with Gas Governance (Critical Contingency Management) Regulations 2008.*
- (2) *The Court may grant the injunction if, in the opinion of the Court, it is desirable to do so.*
- (3) *Subclause (2) applies, in the case of an injunction under subclause (1)(a),—*
 - (a) *whether or not the participant has done, or omitted to do, that thing; and*
 - (b) *whether or not there is an imminent danger of substantial damage to any person if the participant does, or omits to do, that thing.*
- (4) *The Court may rescind or vary the injunction on application by the industry body or any participant affected by the injunction.”*

- A new regulation is inserted after regulation 58 regarding the liability of the critical contingency operator:

“58A Liability of critical contingency operator

- (1) *The critical contingency operator is liable for any breach that it commits of regulations 9, 28, 32, 34 to 37, 37A, 39, 40, 45 to 50, 55 to 61 and 78 of the Gas Governance (Critical Contingency Management) Regulations 2008.*
- (2) *The critical contingency operator is not liable under these regulations for a sum in excess of the annual fee stipulated in the critical contingency operator service provider agreement in respect of all events occurring in any financial year.”*

Appendix B List of stakeholders consulted

Age Concern New Zealand Inc
Arete Limited
Auckland Gas Company
Austral Pacific Energy Limited
Australian Gas Light Company, The
Ballance Agri Nutrients (Kapuni) Ltd
Bay of Plenty Electricity
Bell Gully
BRG
Bridge Petroleum Limited
Carter Holt Harvey
Castalia
Clifford Chance Law Office
Commerce Commission
Concept Consulting
Consumers Institute
Contact Energy Limited
Craftware Computing Limited
Degussa Peroxide Ltd
E-Gas
E-Gas
Electricity & Gas Complaints Commission
Electricity Commission
Energy Link Limited
Energy Online
Exergi Consulting Ltd
Fletcher Building Limited
Fonterra Co-operative Group
Four Winds Communications Limited
Gas Association of New Zealand Inc
GasNet
Genesis Energy
Grey Power
Greymouth Gas New Zealand Limited
Greymouth Petroleum
Heinz Watties Limited
HP Consulting & Integration
JH Vernon Consultancy
Kensington Swan
LECG
Loyalty NZ Ltd
LPG Associations of New Zealand
Major Electricity Users Group (MEUG)
Marsh Limited
Maui Development Limited
M-co
MED Energy Safety
Methanex New Zealand Limited
Mighty River Power Limited
Ministry of Civil Defence and Emergency Management
Ministry of Consumer Affairs
Ministry of Economic Development
Ministry of Research, Science & Technology
Multigas (NZ) Limited
National Council of Women of New Zealand
Neil Walbran Consulting Limited
New Zealand Oil and Gas Limited
New Zealand Refining Co Ltd, The
New Zealand Steel Ltd
NGC Metering Ltd
Norske Skog Tasman Limited
Nova Gas Limited
NZ Water & Wastes Association
NZX
Office of Hon David Parker
O-I New Zealand Limited
OMV New Zealand Limited
On Gas Industrial and Commercial
Origin Energy New Zealand
Pan Pac Forest Products Ltd
Parsons Brinckerhoff Associates
Pat Cunniffe
PEPANZ
Powerco Limited
PricewaterhouseCoopers
Quentin Hay
RBZ Energy Limited
Russel McVeagh
SBT Group
Shell (Petroleum Mining) Company Limited
Simpson Grierson
Stigley & Co
Strata Energy Consulting
Swift Energy New Zealand Limited
Tatua Cooperative Dairy Company

Terrence Currie
Tetenburg & Associates Ltd
Thorndon Chambers
Todd Energy Limited
Transpower Ltd
Vector Limited
Wanganui Gas Limited
Wellington Community Law Centre
Wendell Slatter
Westech Energy New Zealand

Appendix C Notice for Gazette

Notice of Making of a Recommendation and Assessment for an Amendment to Gas Governance Regulations

This notice of a recommendation and assessment for an amendment to gas governance regulations is issued by Gas Industry Company Limited ('Gas Industry Co') approved as the industry body by Order in Council under section 43ZL of the Gas Act 1992 (the 'Act').

Section 43O of the Act provides that, no later than 10 working days after making a recommendation for a gas governance regulation to the Minister of Energy, Gas Industry Co must publicise the recommendation and the assessment completed under section 43N of the Act.

Recommendation

On 30 June 2008 Gas Industry Co made a recommendation to the Minister of Energy under sections 43G(2)(k) and 43S of the Act for approval of an amendment to the proposed Gas Governance (Compliance) Regulations to provide for compliance with regulations establishing arrangements for the management of critical contingencies.

A copy of Gas Industry Co's recommendation, including the assessment, is available at no cost on Gas Industry Co's website: <http://www.gasindustry.co.nz>

Dated at Wellington this 30th day of June 2008.

For and on behalf of Gas Industry Co

Rt. Hon. James Bolger ONZ, Chair

Appendix D Notice for website

Under section 43O of the Gas Act 1992, Gas Industry Co must, no later than 10 working days after making a recommendation to the Minister of Energy on gas governance arrangements, publicise that recommendation and the assessment completed under section 43N of the Act.

On 30 June 2008, Gas Industry Co made a recommendation for an amendment to the proposed Gas Governance (Compliance) Regulations for the compliance with and enforcement of the regulations establishing arrangements for the management of critical contingencies. The text of this recommendation, including the assessment under section 43N of the Act, is available below:

Recommendation to the Minister of Energy on Amendment to Gas Governance (Compliance) Regulations