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RECOMMENDATION TO MINISTER

# Recommendation to the Minister of Energy and Resources on proposed amendments to the Gas Governance (Critical Contingency Management) Regulations 2008

**21 July 2021**

# Executive summary

This recommendation relates to the Gas Governance (Critical Contingency Management) Regulations 2008 (CCM Regulations), an existing gas governance arrangement.

The recommendation relates to specific aspects of the compliance arrangements in the CCM Regulations that will be revoked by amendments to the Gas Act.

Gas Industry Co is recommending that the Minister make new gas governance regulations to replace regulations 82A and 82B of the CCM Regulations that will be revoked by the Gas (Information Disclosure and Penalties) Amendment Act 2021 (Amendment Act). The new regulations would enable the High Court to impose civil pecuniary penalties of up to \$200,000 on consumers who are not industry participants (other than domestic consumers) for specific breaches of the CCM Regulations.

The intention of the gas governance regulations proposed in this recommendation is to ensure that:

1. the compliance framework in the CCM Regulations provides adequate incentives for consumers who are not industry participants (excluding domestic consumers) to provide accurate information and comply with the directions of the critical contingency operator
2. to the extent possible, the compliance framework in the CCM Regulations is aligned for industry participants and consumers (excluding domestic consumers) who are not industry participants

The recommendation follows Gas Industry Co's issue of a Statement of Proposal and consultation with industry participants on a broader package of reforms to the CCM Regulations. This proposal is being progressed ahead of other proposed changes to align with the amendments to the Gas Act and avoid any possible regulatory gap. We anticipate a further recommendation on proposed amendments to the CCM Regulations relating to other aspects of our consultation following the completion of our consultation and assessment process on those proposed amendments.

# Contents

<b>1. INTRODUCTION AND PURPOSE</b>	<b>4</b>
1.1 Introduction	4
1.2 Purpose	4
<b>2. BACKGROUND</b>	<b>5</b>
2.1 CCM Regulations	5
2.1.1 The need for regulations	5
2.1.2 Purpose and function of the CCM Regulations	5
2.2 Gas Act amendments	6
2.3 Gas Industry Co's process	7
<b>3. PROBLEM ASSESSMENT</b>	<b>8</b>
3.1 Problem statement	8
3.2 Regulatory objective	8
<b>4. PROCESS TO AMEND REGULATIONS</b>	<b>9</b>
4.1 Power to regulate critical contingency arrangements	9
4.2 Requirements when recommending regulations	10
4.3 Rules or regulations	11
<b>5. STATEMENT OF PROPOSAL</b>	<b>12</b>
<b>6. ASSESSMENT</b>	<b>14</b>
6.1 Reasonably practicable options	14
6.2 Costs and benefits	14
<b>7. RECOMMENDATION</b>	<b>15</b>

# 1. Introduction and purpose

## 1.1 Introduction

This recommendation relates to the Gas Governance (Critical Contingency Management) Regulations 2008 (CCM Regulations), an existing gas governance arrangement. The regulations are concerned with the effective management of gas outages and other security of supply contingencies to avoid compromising long-term security of supply.

In mid-2020, Gas Industry Co consulted with stakeholders on a number of proposed amendments to the CCM Regulations to improve their efficiency and effectiveness. The consultation related to a number of elements of the CCM Regulations, including the offence provisions in regulations 82A and 82B that were proposed to be revoked by the Gas (Information Disclosure and Penalties) Amendment Bill (the Bill). These provisions provided for criminal offences for the provision of incorrect information and failure to comply with curtailment instructions issued by the Critical Contingency Operator (CCO).

Gas Industry Co has decided to advance the proposed amendments to the CCM Regulations contained in this recommendation ahead of other elements of its wider CCM Regulations review to ensure that there is no regulatory gap due to amendments to the Gas Act 1992 that revoke existing offence provisions. We anticipate a further recommendation on proposed amendments to the CCM Regulations relating to other aspects of our consultation following the completion of our consultation and assessment process on those proposed amendments.

## 1.2 Purpose

Gas Industry Co is recommending that the Minister make new gas governance regulations to replace the revoked regulations 82A and 82B of the CCM Regulations.

The purpose of the gas governance regulations proposed in this recommendation is to ensure that:

1. the compliance framework in the CCM Regulations provides adequate incentives for consumers who are not industry participants (excluding domestic consumers) to provide accurate information and comply with the directions of the critical contingency operator
2. to the extent possible, the compliance framework in the CCM Regulations is aligned for industry participants and consumers (excluding domestic consumers) who are not industry participants

## 2. Background

### 2.1 CCM Regulations

#### 2.1.1 The need for regulations

When a gas supply event (such as gas production station failure or a pipeline rupture) occurs, it reduces or stops the flow of gas into or through the affected pipeline. The remaining gas pressure in the transmission and distribution systems will cause the gas to keep flowing to delivery points or customer premises, at least until the pressure is no longer sufficient to maintain the flow.

When a gas supply event occurs, in the absence of a requirement that consumers stop (or in some cases reduce) their use of gas, there is a risk that pressure in the gas transmission and gas distribution systems could fall to a level where gas is unable to flow.

If sufficient pressure is not maintained in downstream networks, it is estimated that recovering a distribution network serving a large urban area could take many months. Falling system pressures may also impact the delivery of gas to certain designated consumers who require gas for certain essential and critical care services or providing time for an orderly shutdown of a plant to prevent or mitigate major plant or environmental damage.

The most significant gas supply event to date is the five-day Maui pipeline outage that occurred in October 2011. There have also been several shorter-term gas supply events.

#### 2.1.2 Purpose and function of the CCM Regulations

The CCM Regulations were made in 2008 and came fully into force in January 2010. With a purpose of achieving 'the effective management of critical gas outages and other security of supply contingencies without compromising long-term security of supply', the CCM Regulations provide for:

1. a Critical Contingency Operator (CCO) which is tasked with:
  - (a) determining the onset of a gas supply event (termed a "critical contingency")
  - (b) using the power to direct and revise customer curtailment arrangements so as to ration available gas to balance remaining supply and demand
  - (c) directing restoration of load once it is safe to do so
  - (d) communicating with key stakeholders throughout the incident
  - (e) terminating the critical contingency
  - (f) reporting on the incident and the CCO's performance after the incident is resolved
2. Each Transmission System Owner ('TSO') to create a Critical Contingency Management Plan that defines the processes and procedures it will follow so as to implement the CCO's curtailment and other directions. TSOs are required to pass the

CCO's curtailment directions on to the retailers that use their pipelines to convey gas to customers.

3. A system of classifying customers into groups defined by consumption – curtailment bands – so that the process of load curtailment can be efficiently managed.
4. Processes for deferring curtailment for certain classes of customers that provide essential and critical care services, or where providing time for an orderly shutdown of the plant would prevent or mitigate major plant or environmental damage.
5. A post-facto settlement among pipeline users and interconnected parties that is designed to ensure suppliers are paid for the gas used during a critical contingency whether that gas was used by their customers or those of another retailer.

A number of amendments to the CCM Regulations were made in 2014 following Gas Industry Co's review of Maui pipeline outage.

## 2.2 Gas Act amendments

The Amendment Act received Royal assent on 12 July 2021. The Amendment Act amends the penalty regime for gas governance regulations in the Gas Act by:

1. increasing the maximum civil pecuniary penalty able to be imposed by the Rulings Panel from \$20,000 to \$200,000
2. repealing a provision that allows the making of gas governance regulations to provide for offences and fines of up to \$20,000 and revoking existing offences in regulations 82A and 82B of the CCM Regulations
3. allowing the making of gas governance regulations that provide for the High Court to impose a pecuniary penalty on consumers (other than domestic consumers) of up to \$200,000

The policy given effect to by the Gas Act amendments was informed by a discussion document released by the Ministry of Business, Innovation and Employment (MBIE) in 2019, *Options for amending the Gas Act 1992*.<sup>1</sup> The amendments address:

1. concerns about the low level of civil pecuniary penalty able to be awarded by the Rulings Panel providing an inadequate incentive for compliance and the misalignment with the equivalent penalty in the Electricity Industry Act 2010
2. concerns around the appropriateness of imposing a criminal penalty on non-industry participants and a civil pecuniary penalty on industry participants

As well as repealing section 43T of the Gas Act, which allows the making of gas governance regulations to provide for offences and fines of up to \$20,000, the Gas Act amendments also revoke regulations 82A and 82B of the CCM Regulations that contain offences and fines for:

1. a consumer knowingly providing false or misleading information in an application for a designation or to the critical contingency operator
2. a consumer, other than an industry participant, fails to comply with a direction of the critical contingency operator that affects, or may affect, the operation of wholesale markets for gas

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<sup>1</sup> Refer to <https://www.mbie.govt.nz/dmsdocument/5478-discussion-document-options-for-amending-the-gas-act-1992>.

The revocation of regulations 82A and 82B of the CCM Regulations is necessary to reflect the removal of the empowering provision for making those regulations (section 43T of the Gas Act).

The Gas Act amendments introduce a new section 43TA and subpart 5 into Part 4A of the Gas Act to empower gas governance regulations that allow the High Court to order payment of a civil pecuniary for breaches of gas governance regulations by consumers who are not classified as industry participants. As the industry body responsible for making recommendations to the Minister for gas governance regulations, the new section 43TA enables Gas Industry Co to recommend gas governance regulations that include a civil pecuniary penalty for consumers who are not industry participants. Prior to the introduction of section 43TA, Gas Industry Co could only recommend a criminal penalty.

### **2.3 Gas Industry Co's process**

Gas Industry Co has followed MBIE's consultation on its 2019 discussion document and the passage of the Gas (Information Disclosure and Penalties) Amendment Bill.

In parallel with the passage of the Bill, we released a Statement of Proposal that included the amendments proposed in this recommendation.<sup>2</sup> 11 parties responded to Gas Industry Co's consultation with four submitters providing a view on the proposed amendments to the penalty provisions in the CCM Regulations. All four submitters agreed with Gas Industry Co's proposal.

Gas Industry Co has decided to advance the proposed amendments to the CCM Regulations contained in this recommendation ahead of other elements of its wider CCM Regulations review to ensure that there is no regulatory gap following amendments to the Gas Act 1992 that revoke existing offence provisions. We anticipate a further recommendation on proposed amendments to the CCM Regulations relating to other aspects of our consultation following the completion of our consultation and assessment process on those proposed amendments.

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<sup>2</sup> The Statement of Proposal for amending the CCM Regulation and stakeholder submissions are available at <https://www.gasindustry.co.nz/work-programmes/critical-contingency-management/consultation-statement-of-proposal-for-amending-ccm-regulations/document/6966>

## 3. Problem Assessment

### 3.1 Problem statement

Gas Industry Co considers that there are inadequate incentives for consumers who are not industry participants (excluding domestic consumers) to provide accurate information and comply the directions of the critical contingency operator. There is also a fairness issue as some large gas consumers will potentially face civil pecuniary penalty issued by the Rulings Panel for non-compliance, while other consumers will face no consequences for similar conduct following the revocation of regulations 82A and 82B of the CCM Regulations.

### 3.2 Regulatory objective

In its Statement of Proposal, Gas Industry Co proposed a regulatory objective aligned with the purpose of the CCM Regulations:

“The purpose of these regulations is to achieve the effective management of critical gas outages and other security of supply contingencies without compromising long-term security of supply” (regulation 3)

The proposed amendments to the CCM Regulations contained in this recommendation are intended to further achieve this objective.



## 4. Process to amend regulations

### 4.1 Power to regulate critical contingency arrangements

Section 43F of the Gas Act provides:

(1) The Governor-General may, by Order in Council made on the recommendation of the Minister in accordance with sections 43I to 43P, make regulations for all or any of the purposes in subsection (2).

(2) The purposes are—

*Wholesale gas market*

(a) providing for the establishment and operation of wholesale markets for gas, including for—

(i) protocols and standards for reconciling and balancing gas:

(ii) clearing, settling, and reconciling market transactions:

(iii) the provision and disclosure of data and other market information:

(iv) minimum prudential standards of market participation:

(v) minimum standards of market conduct:

...

*Arrangements relating to outages and other security of supply risks*

(e) providing, in relation to wholesale or any other markets for gas, for arrangements relating to outages and other security of supply risks, including imposing requirements in connection with those matters on any industry participant or consumer (other than a domestic consumer):

Section 43TA of the Gas Act provides:

(1) Any regulations made under this subpart may do 1 or more of the following:

(a) identify provisions of regulations made under this subpart, or provisions of rules made under section 43Q, for the purposes of subpart 5 (which allows the High Court to impose a pecuniary penalty on a consumer (other than a domestic consumer) for a breach of those identified provisions):

(b) prescribe, in relation to each of those provisions, the maximum pecuniary penalty that may be imposed under subpart 5 for a breach:

(c) prescribe a defence to a proceeding under subpart 5 or prescribe other matters relating to when a breach gives rise to liability for a pecuniary penalty under that subpart.

(2) A maximum pecuniary penalty referred to in subsection (1)(b) must not exceed \$200,000.

Gas Industry Co considers that the Minister is empowered to make the proposed amendments to the CCM Regulations contained in this recommendation under sections 43F(2)(e) and 43TA. Gas Industry Co notes that the CCM Regulations were made in reliance on section 43F and the proposed amendments do not vary the scope of the CCM Regulations in any material way.

## 4.2 Requirements when recommending regulations

Section 43L(1) of the Act requires the body recommending gas governance regulations to the Minister to:

1. undertake an assessment under section 43N of the Act; and
2. consult with persons that the recommending body thinks are representative of the interests of persons likely to be substantially affected by the proposed regulations; and
3. give those persons the opportunity to make submissions;
4. consider those submissions.

A summary of the consultation undertaken by Gas Industry Co is set out in section 2 of this recommendation.

Section 43N(1) of the Act requires that, before making a recommendation to the Minister, Gas Industry Co must:

1. seek to identify all reasonably practicable options for achieving the objective of the regulation;
2. assess those options by considering—
  - (a) the benefits and costs of each option
  - (b) the extent to which the objective would be promoted or achieved by each option
  - (c) any other matters that the industry body considers relevant
3. 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)
4. prepare a statement of the proposal for the purpose of consultation under section 43L(1).

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

1. a detailed statement of the proposal
2. a statement of the reasons for the proposal
3. an assessment of the reasonably practicable options, including the proposal, identified under subsection (1)
4. other information that the industry body or the Commission considers relevant.

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

### 4.3 Rules or regulations

Section 43Q of the Act empowers the Minister to make a rule for all or any of the purposes for which a gas governance regulation may be made. In deciding whether to make a rule rather than a regulation, the Minister must have regard to:

1. the importance of the rule, including whether the rule has a material effect on the rights and interests of individuals
2. the subject matter of the rule, including whether the rule contains detailed or technical matters rather than matters of general principle
3. the application of the rule, including—
  - (a) whether the rule applies principally to a particular group (eg, industry participants) rather than the general public
  - (b) whether the benefits of publication in accordance with section 43R rather than the Legislation Act 2012 outweigh the costs of publication by that method
4. the expertise and rule-making procedures of the recommending body.

Gas Industry Co considers that the proposed amendments should be made by gas governance regulations for the following reasons:

1. The proposed amendments replace regulations included in the CCM Regulations, but which will be revoked by the Amendment Act
2. The amendments have an impact on the rights of individuals, address matters of general principle, and apply to consumers who do not meet the definition of an industry participant.

## 5. Statement of Proposal

Gas Industry Co considers that good information and timely compliance with curtailment instructions are vital to the effectiveness of the CCM Regulations in managing critical contingency events.

Gas Industry Co proposes that new civil pecuniary penalties are included in the Gas Act to ensure that:

1. the compliance framework in the CCM Regulations provides adequate incentives for consumers who are not industry participants (excluding domestic consumers) to provide accurate information and comply the directions of the critical contingency operator
2. industry participants and consumers (excluding domestic consumers) who are not industry participants are treated fairly in the compliance framework in the CCM Regulations.

In accordance with section 43TA of the Gas Act, the new regulations would provide the High Court with the power to impose a civil pecuniary penalties on consumers (other than domestic consumers). The new civil pecuniary penalties should apply to the offences that are within the scope of regulations 82A and 82B that will be revoked. These are:

1. knowingly providing false or misleading information to the industry body in an application for a designation under regulation 46E
2. knowingly providing false or misleading information to the Critical Contingency Operator under regulation 40
3. failure to comply with a direction during a critical contingency where the failure affects, or may affect, the operation of wholesale markets for gas.

The prescribed defences provided for in the revoked regulation 82B(2) should apply.

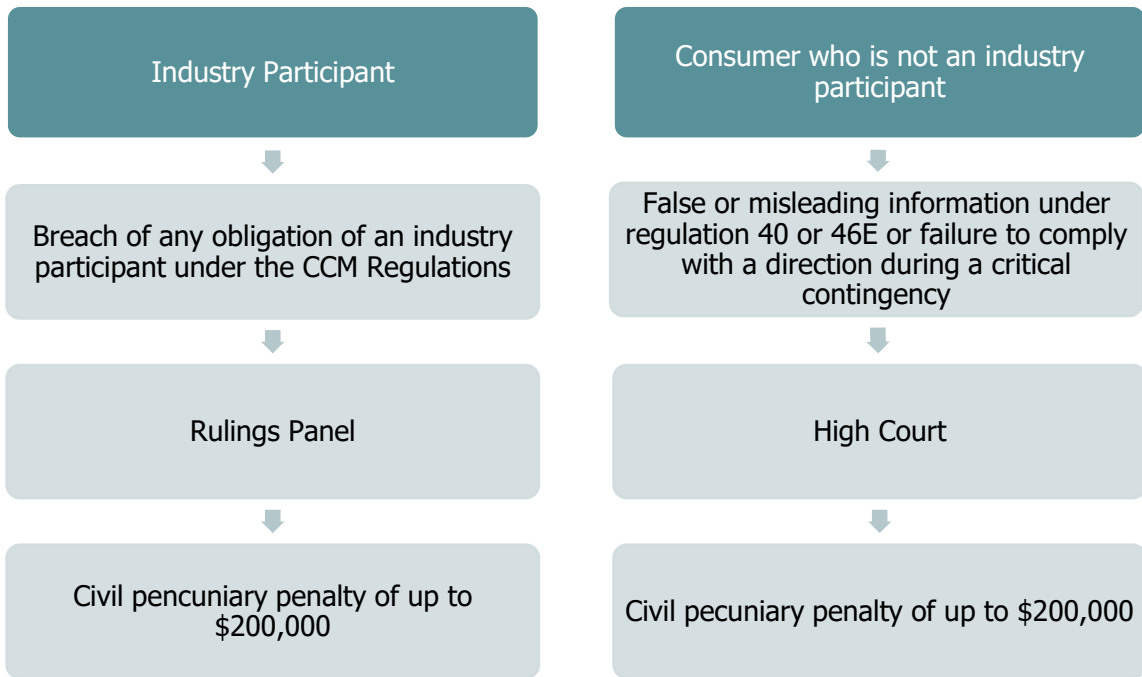
The maximum penalties should be \$200,000 to provide larger consumers with appropriate incentives for compliance. This will also ensure alignment with maximum penalty that the Rulings Panel may award for industry participants for breaches of their obligations.

No changes are proposed for the compliance process for industry participants who are subject to the Rulings Panel's jurisdiction for breaches of the CCM Regulations.<sup>3</sup> We note that the Gas Act amendments increase the maximum civil pecuniary penalty that the Rulings Panel can order to \$200,000.

If the Minister approves the recommendation, then the following processes may apply to breaches of the CCM Regulations:

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<sup>3</sup> Only industry participants are subject to the Rulings Panel's jurisdiction for breaches of gas governance rules and regulations.



Gas Industry Co considers that the amendments proposed in this recommendation will result in a compliance framework under the CCM Regulations that is, to the extent possible, aligned for industry participants and non-industry participants.

## 6. Assessment

Section 43N of the Act requires that, before making a recommendation to the Minister, Gas Industry Co must assess:

1. the costs and benefits of each reasonably practicable option, including the proposal
2. the extent to which the regulatory objective ('to achieve the effective management of critical gas outages and other security of supply contingencies without compromising long-term security of supply') would be promoted or achieved by each option;
3. any other matters which Gas Industry Co considers relevant.

### 6.1 Reasonably practicable options

In the Statement of Proposal, we noted that the proposed amendments involved refinement of the existing CCM Regulations. Given that the regulatory framework is already in place, we do not believe that there are other reasonably practicable options, or that the regulatory objective can be better achieved by a means other than an amendment to the CCM Regulations.

We asked for stakeholder feedback on our view as part of our consultation on the Statement of Proposal. Six parties agreed that amending the CCM Regulations is the most practicable option to achieve the regulatory objective. The remaining five parties did not provide a view on this aspect of the consultation.

### 6.2 Costs and benefits

The original Statement of Proposal for the initial development of the CCM Regulations contained an assessment of costs and benefits that compared the (then) status quo – a scheme that relied on voluntary cooperation – with a regulated scheme that would require compliance with directions to curtail demand.<sup>4</sup>

This recommendation proposes modification to one aspect of the CCM Regulations.

We do not consider that it is possible to quantitatively describe the costs and benefits associated with the proposed amendments. In the Statement of Proposal, we noted the following benefits:

1. enhancing the effectiveness of the CCM Regulations by providing incentives for good information and timely compliance with curtailment instructions
2. consistent treatment of consumers who are industry participants and consumers who are not industry participants

We do not consider that the proposed amendments to the CCM Regulations would create any new or additional compliance and enforcement costs.

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<sup>4</sup> The original Statement of Proposal can be found at <https://www.gasindustry.co.nz/work-programmes/critical-contingency-management/background/original-development-2006-2008/statement-of-proposal-gas-outage-and-contingency-management-arrangements/>

## 7. Recommendation

Gas Industry Co recommends to the Minister of Energy and Resources, under sections 43F(2)(e) and 43TA of the Gas Act 1992, amending the Gas Governance (Critical Contingency Management) Regulations 2008 as set out in section 5 of this recommendation.

## ABOUT GAS INDUSTRY CO

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Gas Industry Co is the gas industry body and co-regulator under the Gas Act. Its role is to:

- develop arrangements, including regulations where appropriate, which improve:
  - the operation of gas markets;
  - access to infrastructure; and
  - consumer outcomes;
- develop these arrangements with the principal objective to ensure that gas is delivered to existing and new customers in a safe, efficient, reliable, fair and environmentally sustainable manner; and
- oversee compliance with, and review such arrangements.

Gas Industry Co is required to have regard to the Government's policy objectives for the gas sector, and to report on the achievement of those objectives and on the state of the New Zealand gas industry.

ENQUIRIES:  
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