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Dear Ian

**Submission on the Proposed Revised Guidelines
for ESP and MLC Designations**

Introduction

1. Vector Limited ("Vector") welcomes the opportunity to make this submission on the Gas Industry Company's ("GIC") *Proposed Revised Guidelines for Essential Service Providers and Minimal Load Users 2012* ("the Revised Guidelines"), dated 2 August 2012.
2. No part of this submission is confidential and Vector is happy for it to be made publicly available.
3. Vector's contact person for this submission is:

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Reviewing the Guidelines

4. Vector appreciates the GIC's initiative of reviewing the existing Guidelines, in response to industry participants' desire for an interim measure so "the lessons from the Maui Pipeline Outage are implemented in a timely manner and as far as possible within the scope of the current CCM Regulations".
5. The GIC's proposals are a substantial improvement on the existing Guidelines. Vector agrees that the existing Guidelines are far too loose and "open to an

inappropriately wide interpretation, and that there are inconsistencies among retailers in how the criteria are interpreted and applied".¹

6. Any changes to the Guidelines, however, should only be seen as a stop-gap solution pending revision of the Gas Governance (Critical Contingency Management) Regulations 2008 ("CCM Regulations"). Vector's preference is for the CCM Regulations to stipulate that the GIC designate ESPs and MLCs.

ESP designation criteria

7. Vector agrees with the GIC that applying the ESP designation criteria too loosely:

...would lead to a broad group of ESP designations with a large combined gas demand. If this happens, then it would be difficult for the CCO to allow ESPs to take gas at times of shortages. For the Regulations to be effective, the ESPs need to have a relatively small combined demand, so that they can be allowed to take gas in a range of circumstances.²

8. Vector broadly supports the GIC's proposed revisions to the criteria for ESP designation, which more clearly reflect the limited nature of this designation. The Revised Guidelines are consistent with Vector's recommendation for the development of tighter sets of definitions for curtailment bands.³
9. In this connection, Vector agrees that the ESP designations "should be assessed in the context of a critical contingency lasting only a matter of days".⁴ Any assessment in the context of an extended duration or broader coverage would lead to excessive designations and should therefore be addressed through the National Civil Defence Emergency Management Plan Order 2005, as per Schedule 2 of the CCM Regulations.
10. Vector agrees with the considerations the GIC has taken into account in the development of the Revised Guidelines, in particular, the:
 - a. essentiality of the service;
 - b. availability of and requirement for back-up arrangements;
 - c. distinction between the essential and non-essential services provided by the same consumer; and

¹ Consultation document, page 3

² Consultation document, page 3

³ http://gasindustry.co.nz/sites/default/files/submissions/180/vector - submission - gic - concept_consulting_review_of_gccm - 2012_07_02.pdf, paragraph 36

⁴ Proposed Revised Guidelines, page 5,

- d. disqualification of non-direct providers of the essential service.

Essentiality of the service

- 11. Vector supports the GIC's interpretation that it is "the '*essential*' nature of the services provided by gas users that is the relevant consideration in determining an ESP designation" and that "it is the *service itself* that is the subject of any designation, rather than the possible consequences of curtailing a particular gas user". This is consistent with the suggestion in the Concept Report on critical contingency management, which Vector agrees with, that further consideration be given "to require consumers who wish to be designated as ESP to supply information on the essential nature of the service".⁵
- 12. Vector agrees with the GIC that the types of food producers that should qualify for ESP designation are those producing "such short shelf-life staples as fresh bread and fresh milk for domestic consumption".
- 13. In relation to the objective of "preservation of economic activity", Vector agrees that this should "be interpreted in light of services that are necessary to further the emergency response objectives". Further, it "should not be construed as seeking to preserve the range of 'normal' economic activity", for example, the Reserve Bank should be an ESP but not a clothing shop.
- 14. Narrowing the types of consumers that would qualify for the "protection of natural and physical resources" criterion would be consistent with the consideration that it is not the possible consequences of the curtailment that is relevant but the nature of the service in question. Alternatively, customers could apply for MLC designation for the orderly shutdown of their plant or facilities.

Availability of and requirement for back-up arrangements

- 15. It is Vector's view that an ESP should not assume it can continue to consume gas at unrestricted levels. This is due to the low level of interconnection in the New Zealand gas system, and it is not impossible to contemplate a critical contingency where there is no gas supply at all.⁶
- 16. Vector believes that a genuine ESP:

...should reasonably and prudently be expected to have considered its back-up arrangements within the specific context of the transmission system's ability to

⁵ http://gasindustry.co.nz/sites/default/files/submissions/180/vector - submission - gic - concept consulting review of gccm - 2012_07_02.pdf, paragraph 42c

⁶ http://gasindustry.co.nz/sites/default/files/submissions/180/vector - submission - gic - concept consulting review of gccm - 2012_07_02.pdf, paragraph 40

deliver any gas during a supply failure, and not all of its gas consumption would necessarily qualify as an essential service.⁷

17. Tightening the criteria for ESP designation would generally provide incentives for consumers to arrange for back-up supply arrangements. While ESP designation would normally be granted for gas needed in the production of essential services for which there are no alternative fuel sources, such cases may be rare.

Distinction between essential and non-essential services provided by the same consumer

18. The GIC has stated that "an ESP designation relates to the gas necessary to provide the essential services themselves" and "where a consumer provides both essential and non-essential services, it is only the gas supply required to provide those services that is protected under the designation".
19. Vector agrees with this view. However, the current CCM Regulations may not provide for a distinction to be made between the essential and non-essential services provided by the same consumer. A consumer is either an ESP (with indivisible rights) or not, and there is no distinction between an ESP's essential and non-essential consumption. Therefore, an ESP may be able to continue consuming gas for both its essential and non-essential services.
20. Vector believes this should be remedied through amendment of the CCM Regulations, which reinforces its view that the comprehensive review of the CCM Regulations should be progressed expeditiously.

Disqualification of non-direct providers of the essential service

21. Vector supports the granting of ESP designation only to parties who are themselves providing essential services. Akin to the requirement for ESPs (and many other businesses) to ensure they have back-up arrangements in times of emergency, this would provide the right incentives for parties to make the necessary arrangements with their suppliers.

Reset process

22. Vector recommends that existing designations are re-assessed when the Revised Guidelines are agreed. It is not unexpected that there would be consumers currently designated as ESPs or MLCs that would not qualify as such under the Revised Guidelines. To ensure that all consumers interested in becoming an ESP/MLC, or in retaining their current designation, are assessed using the same

⁷ http://gasindustry.co.nz/sites/default/files/submissions/180/vector - submission - gic - concept_consulting_review_of_gccm - 2012_07_02.pdf, paragraph 40

criteria, Vector recommends that the GIC request retailers to implement a “reset” or “re-classification” process.

23. Retailers should request their ESP consumers who they reasonably consider no longer meet the criteria of the Revised Guidelines to re-apply for ESP/MLC designation in accordance with CCM Regulation 44(5). Under CCM Regulation 44(6), a consumer requested to re-apply that fails to do so within 20 days of receiving such notice would no longer qualify for such designation.
24. As a first step, the GIC could produce an information pack for retailers to use in communications with their consumers, setting out the Revised Guidelines and the steps in the application process.

Recommendations for the Revised Guidelines

25. By setting tighter criteria for ESP designation, the Revised Guidelines are a significant improvement on the current criteria.
26. For greater clarity and effectiveness, Vector recommends that the GIC include in the Revised Guidelines provisions that:
 - a. recognise that the CCM Regulations are concurrently being reviewed, which could have a significant impact on how some of the Revised Guidelines would be applied in the future;
 - b. acknowledge that CCM Regulation 50 authorises the Critical Contingency Operator (“CCO”) to issue directions to transmission system operators (“TSOs”) that are necessary to “achieve the purpose of the regulations...and mitigate the severity of the critical contingency”, and suggest that TSOs notify retailers and large consumers that they should comply with such directions;
 - c. retailers evaluate the status of their customers with ESP or designation and request those that they reasonably consider no longer meet the criteria of the Revised Guidelines to re-apply for approval as an ESP or MLC;
 - d. retailers, in evaluating applications for ESP status, consider only the essential services and not the non-essential services provided by the same consumer;
 - e. further specify what information consumers should provide to demonstrate that their gas consumption and the nature of their business meet and will continue to meet the prescribed thresholds for ESP or MLC designation; and

- f. amend (or revoke, as necessary) the Revised Guidelines, soon after the amended CCM Regulations take effect.
27. Vector also recommends the following amendments to Table 2 in the Revised Guidelines:
- a. insert the word “only” under “Care of sick, injured etc” so it reads “Facilities listed that are engaged **only** in elective and/or cosmetic procedures that can be deferred”; and
 - b. insert the word “essential” at the start of the sentence “facilities operated by the Department of Conservation...”

Recommendations for the wider review of the CCM Regulations

28. While the Revised Guidelines are an interim improvement, it is Vector’s view that the CCM Regulations, not the Revised Guidelines, should define the criteria for ESP and MLC designation.
29. In the context of the wider review of the CCM Regulations, Vector reiterates its recommendation that all ESP and MLC designations, and changes to those designations, should be approved by the GIC, not by retailers.⁸ Vector notes that this view is widely held by submitters on the Concept Report.
30. The GIC, rather than retailers, should be responsible for the classification of all consumers, for these reasons:
- a. Gas retailers have weak incentives to self-regulate as there is considerable benefit to their consumers from being designated;
 - b. Conflict of interest: Gas retailers can risk losing consumers over an ESP or MLC status disagreement, but do not bear any of the negative effects of mis-categorisation;
 - c. The current regime also results in a consumer’s ESP or MLC status being reviewed when they change retailers (by the new retailer);⁹ and
 - d. It seems more likely that gas retailers’ resources during a critical contingency are better used to manage the risks associated with the event, rather than having to consider ESP and MLC applications or changes to existing designations.

⁸ http://gasindustry.co.nz/sites/default/files/submissions/180/vector - submission - gic - concept consulting review of gccm - 2012_07_02.pdf, paragraph 42f

⁹ http://gasindustry.co.nz/sites/default/files/submissions/180/vector - submission - gic - concept consulting review of gccm - 2012_07_02.pdf, paragraph 37.

31. Importantly, a stable list of independently designated ESPs and MLCs would enable the CCO to focus its attention in resolving critical contingency issues rather than attending to changes in designations. Vector considers the number of businesses reclassified as ESPs during the Maui Pipeline Outage of October 2011 (33 cases) to be excessive. Reclassifications need to be limited to exceptional cases, for example, those that would enable the purpose of the CCM Regulations to be met.
32. The above reasons indicate that the assessment and approval by gas retailers of their consumers' ESP and MLC applications distort the incentives of the concerned parties, reducing the efficacy of commercial drivers and the efficiency of the gas market as a whole. For the same reason, "whether a retailer assists consumers with preparation of applications should also be a commercial decision for retailers and not a regulatory requirement".¹⁰
33. Vector recommends that the GIC, as part of its review of the CCM Regulations:
 - a. propose amendments to the CCM Regulations that would reflect the intent (if not the actual wording of some) of the Revised Guidelines;
 - b. propose that the assessment and approval of applications for ESP and MLC designation be undertaken by the GIC or an independent body, not by retailers; and
 - c. require a regular review of consumers' ESP and MLC designations, say every two years.
34. Vector looks forward to the Revised Guidelines being finalised and the CCM Regulations being reviewed expeditiously. It would be helpful if the GIC could provide stakeholders an update on the timelines for these two work streams.

Yours sincerely



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¹⁰ http://gasindustry.co.nz/sites/default/files/submissions/180/vector - submission - gic - concept_consulting_review_of_gccm - 2012_07_02.pdf, paragraph 42f