OPTIMISING GAS IN NEW ZEALAND.

ANNUAL REPORT 2011

GAS INDUSTRY COMPANY LIMITED


40 YEARS SUPPLYING
NEW ZEALAND


SECURITY
OF SUPPLY


QUALITY
OF LIFE

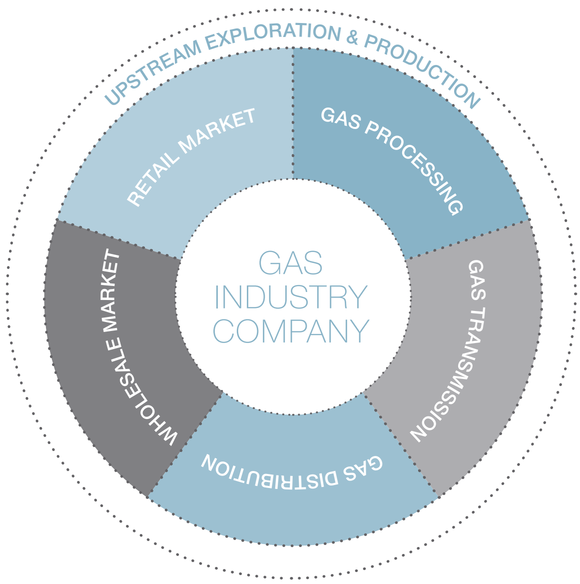
CONTENTS

Gas industry Co is the approved gas industry body, responsible for developing industry arrangements that ensure gas is delivered safely, efficiently and reliably to new and existing customers.

Its strategy is to optimise the contribution of gas to New Zealand by:

- Delivering effectively on its accountabilities as the industry body, and in particular on the provisions of the Government Policy Statement on Gas Governance.
- Building the New Zealand gas story, including through increased disclosure and communication.
- Facilitating efficient investment in, and efficient use of gas infrastructure.
- Ensuring efficient, competitive, and confident gas markets.

Gas Industry Co's role focuses on the mid-downstream sectors of the New Zealand gas industry.



GAS PROCESSING
- Processing plant access

GAS TRANSMISSION
- Access/Balancing/Interconnection/Critical contingencies/Investment

GAS DISTRIBUTION
- Access/Network agreements/Contract benchmarks/Reconciliation

WHOLESALE MARKET
- Wholesale trading/Gas quality

RETAIL MARKET
- Customer switching/Complaints resolution/Consumer protection

KEY STATISTICS

GAS INDUSTRY IN NEW ZEALAND

15 GAS PRODUCING FIELDS
The Pohokura Field is the largest, contributing approximately 36 percent of annual production.

170 PETAJOULES
Annual production (net)

2,000 PETAJOULES
Remaining gas reserves (P50)

Unconventional gas developments emerging, with first in-coal-seam lateral drilling operations.

2,500 KILOMETRES OF TRANSMISSION PIPELINES
Gas demand growth is resulting in some constraints on the transmission system servicing the Auckland region.

16,500 KILOMETRES OF DISTRIBUTION NETWORKS
Annual unaccounted-for gas (UFG) is declining and currently represents 1.5% of injected volumes.

During 2010/11 the Ahuroa gas storage facility, the first of its kind in New Zealand was commissioned. It enables flexibility in the utilisation of gas reserves.

Just over 51% of gas is used in electricity generation and supports supply security. Peaker plants, such as the recently commissioned facility at Stratford, incorporate modern technologies to generate power quickly and efficiently when needed.

255,500 CUSTOMERS

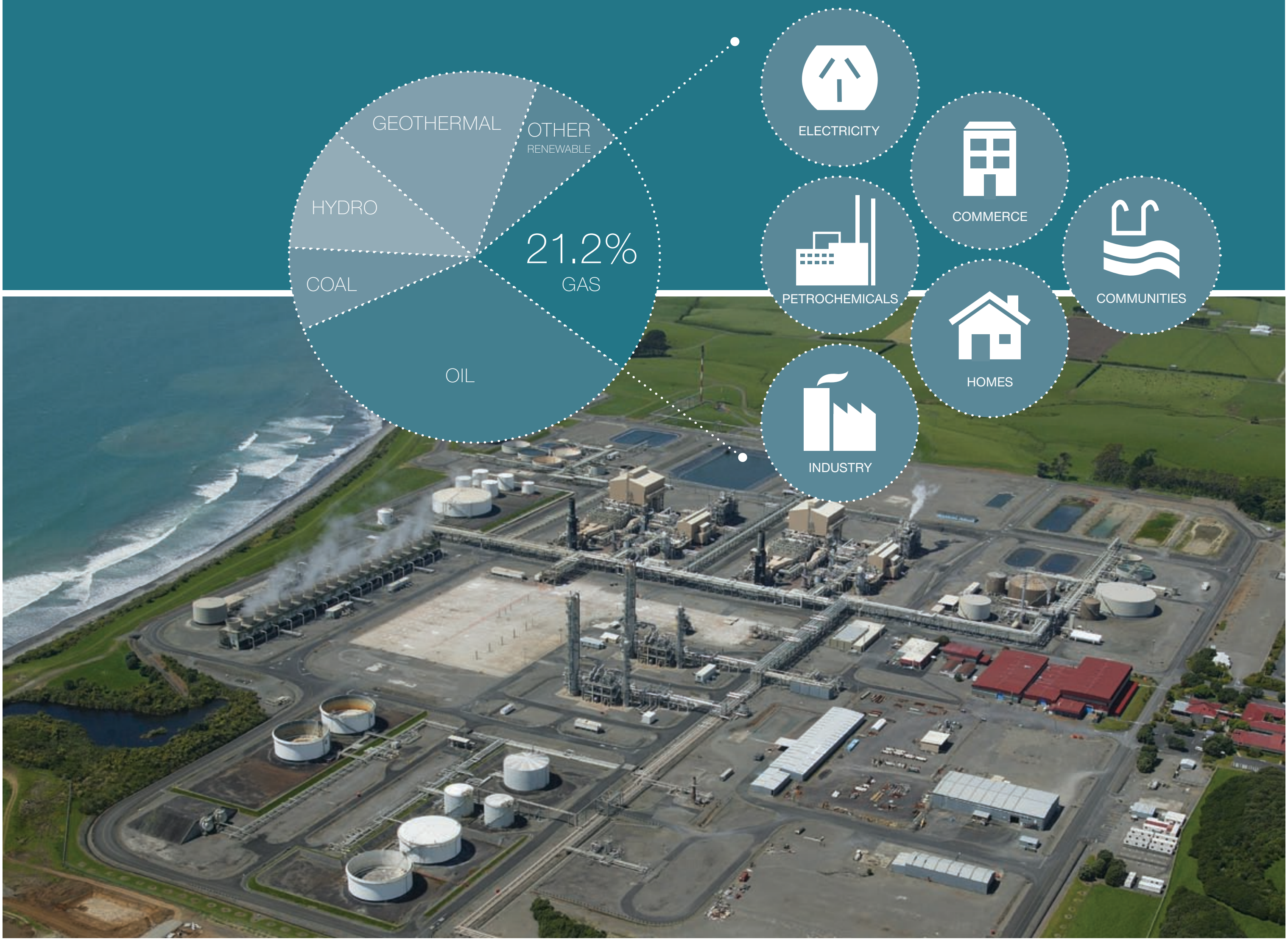
93% OF CUSTOMERS HAVE A CHOICE OF 6 OR MORE RETAILERS AT THEIR GAS GATE

36,000 CUSTOMER SWITCHES BETWEEN COMPETING RETAILERS EACH YEAR

6 DAYS AVERAGE SWITCHING TIME

OPTIMISING GAS IN NEW ZEALAND.

40 YEARS SUPPLYING NEW ZEALAND



CHAPTER 1.

CHAIR'S FOREWORD

"A wide appreciation of the contribution of gas to New Zealand's economy and quality of life, as well as the industry's dynamics, structure, governance and performance, is fundamental to fostering confidence among existing and potential participants."

Gas continues to make a steady and significant contribution to New Zealand of over 20 percent of primary energy supply. More than half of annual gas production supports electricity generation and associated supply security at a time when New Zealand's use of renewable generation has grown to around 75 percent, one of the highest in the OECD. At the same time, gas fuels large and small businesses, and about 245,000 households.

The country's progress towards achieving its environmental sustainability goals is commendable. It is clear, however, that New Zealand will rely on gas for a significant portion of its energy needs well into the future.

As the Government seeks to achieve economic growth as well as environmental sustainability through its Energy Strategy, the future importance of gas is recognised in the Government's commitment to find and develop more of New Zealand's petroleum and gas resources. It is a policy balance that carries an associated need for resources to be used efficiently. For gas, that means contributing to economic efficiency by providing a cost-effective, competitive direct-use energy choice for consumers, fuelling the productive sector, and underpinning supply security.

In the 40 years that natural gas has been part of New Zealand's energy supply mix, it has brought immense benefits to the country. It had the immediate environmental advantage of rendering aging coal-based town gas plants obsolete, while presenting a cleaner-burning premium fuel option for many industrial processes, commercial businesses and households.

During the past year, the Gas Industry Co Board reviewed its strategy as the industry body with a particular focus on looking ahead to the next phase of the gas story in New Zealand, and how the Company can provide industry leadership to optimise the ongoing contribution of gas to this country.

As the gas industry body and co-regulator, Gas Industry Co can do this by:

» Developing market and regulatory settings that achieve the over-arching policy objective for gas to be delivered in a safe, efficient, fair, reliable and environmentally sustainable manner. Gas Industry Co will continue to build on the governance arrangements, both regulatory and non-regulatory, that have created more efficient and confident markets, with consequent benefits to participants and consumers.

» Facilitating efficient use of, and timely investment in, gas infrastructure.

» Leading the communication and development of the New Zealand gas story. Gas Industry Co believes that a wide appreciation of the contribution of gas to the country's economy and quality of life, as well as the industry's dynamics, structure, governance and performance, is fundamental to fostering confidence among existing and potential participants, from upstream explorers to the downstream consumers. There is also a key task in shaping and leading the next phase of the story.

These goals are at the core of Gas Industry Co's work programmes.

The operational priorities for 2011/12 are set out in the Company's Strategic Plan and are consistent with industry participants' assessment of where the Company's focus should lie. In addition to addressing remaining policy matters, they include the Company's growing market administration and compliance monitoring role for arrangements already in place, and working with the industry to identify pathways to infrastructure investment.

Key among current issues is the capacity constraint on the North Pipeline, which has raised concerns among some large end users. The constraint was identified as an area of concern in the recently-published National Infrastructure Plan 2011, which otherwise commented favourably on the gas industry's long record of infrastructure reliability.

Gas Industry Co has worked with industry participants and large end users to address the immediate issues arising from the constraint, resulting in a set of voluntary changes to the market aimed at addressing end users' concerns. In parallel, the Company, with industry support, has commenced a longer term Gas Transmission Investment Programme aimed at ensuring efficient arrangements are in place to support investment, and developing a clear pathway for any investment to occur.

Acknowledgements

During the year, David Baldwin resigned from the Board to take up a new position with Origin Energy in Australia, and Simon Mackenzie resigned having completed a three-year term. Both were industry-associated Directors, being senior executives of industry participant shareholders, and I record my appreciation to them for their services. Ron Kelly and Dennis Barnes were subsequently welcomed to the Board as industry-associated Directors.

In January 2011, Steve Bielby joined Gas Industry Co as Chief Executive, replacing the foundation Chief Executive, Christine Southey. Steve has a strong background in the energy sector, with commercial, regulatory and governance experience at senior executive level. He is well qualified to lead the Company into the next phase of its work and is well under way with implementing the gas optimisation strategy. On behalf of the Board, I thank the Company's executive and wider Gas Industry Co team for their achievements during 2010/11, and particularly for their continuing efforts in developing governance arrangements to foster competitive markets and infrastructure access.

Gas Industry Co remains well positioned to fulfil the roles prescribed by statutory and Government policy objectives for the gas industry, and to successfully implement the Company's wider strategy.

Rt Hon James B Bolger, ONZ
CHAIR

Priorities for 2011/12

KEY AREAS OF FOCUS FOR GAS INDUSTRY CO IN 2011/12 ARE TO:

» Work with the industry to deliver benefits from the Bridge Commitments to address short-term issues arising from the North Pipeline constraint.

» Progress the Gas Transmission Investment Programme to provide longer term solutions to transmission capacity constraints.

» Improve gas distribution contract arrangements through the use of benchmark principles.

» Further ensure small customers are protected through a third annual review of retail consumer contracts against benchmarks. Publish for the first time reports on individual retailers' alignment with those benchmarks.

» Protect gas and gas pipeline integrity by evaluating industry arrangements for monitoring gas quality.

» Assess the potential for improved shipper information through daily allocations.

» Improve Gas Industry Co's access to information to support its policy development process.

» Further develop and implement the Company's broader strategy to optimise gas's contribution to New Zealand, and to increase general awareness of gas's role in the economy.

CHAPTER 2.

CHIEF EXECUTIVE'S REVIEW

"A richness of information is essential to a healthy market. Gas Industry Co will continue to promote improved information availability to enable participants to make informed decisions and allocate resources efficiently."

Gas Industry Co's role as the industry body, and its broader strategy to optimise gas's contribution to New Zealand, necessarily entail identifying arrangements that are appropriate for an optional fuel in a highly competitive and changing energy market.

It requires balanced arrangements that ensure accessible, efficient and competitive gas markets, while encouraging efficient investment and avoiding stifling industry initiative.

The co-regulatory governance model for the gas industry, which includes industry representation and powers for the Company to recommend regulations, provides a robust framework in which a balance can continue to be developed.

Governance arrangements introduced in recent years have comprised a healthy mix of regulated and non-regulated mechanisms to achieve policy objectives and resolve operational and commercial issues.

Where prudent, Gas Industry Co continues to seek non-regulated solutions. Most recently, the Company deferred a proposal to recommend rules to address short-term issues associated with the capacity constraint on Vector's North Pipeline in favour of an industry-developed market arrangement.

However, formal rules and regulations are at times inevitable in order to achieve market improvements.

During 2010/11, Gas Industry Co further consolidated the benefits of the rules that flowed from the Company's early focus on achieving Government policy objectives for an efficient and competitive gas market.

A significant number of customers are taking advantage of the switching arrangements. Switching rates, an indicator of contestability in the market, remain at about 15 percent, as nearly 37,000 customers switched retailer in 2010/11. Customers also benefit from the shorter processing time that switches now take – on average just over six days – a far cry from the much longer periods taken to complete some customer switches before the Switching Rules took effect.

The introduction of the Reconciliation Rules in 2009 shed light where its predecessor regime, an industry Reconciliation Code, did not. It was through the transparency afforded by the Rules and their associated audit provisions that misreporting of consumption figures by E-Gas became apparent during the 2009/10 year. The Compliance Regulations allowed this breach to be formally addressed. E-Gas entered voluntary liquidation during 2010/11 before the Rulings Panel could make a determination on penalty and any compensation, and its customer book was purchased by Nova Energy. However, arrangements put in place by Gas Industry Co some five months before the liquidation meant that, in large part, the costs associated with unaccounted-for-gas (UFG) caused by E-Gas were rectified.

The exit of E-Gas raised another challenge for the industry, and Gas Industry Co assisted the Ministry of Economic Development in drafting back-stop regulations to protect consumers who, with no retailer to sell to them, faced the potential loss of gas supply. The sale of E-Gas customers to Nova Energy meant these regulations did not need to be used. Gas Industry Co also worked hard to ensure the efficient transfer of E-Gas customers to Nova Energy and is reviewing the need for some form of long-term backstop regulations.

Despite the exit of E-Gas, over 93 percent of consumers are connected to gas gates where six or more retailers operate, and therefore still have a broad choice of supplier.

Retailer performance and special event audits, conducted under the Reconciliation Rules, are delivering considerable value in identifying data management weaknesses and errors in the conversion of meter readings into energy. Gas Industry Co is working to develop improved consistency and accuracy in meter readings and allocations submissions, which will bring further benefits for consumers and the industry generally.

Pleasingly, the audits otherwise show a good level of compliance with the Rules, which have prompted market participants to improve their management systems. Consequently, the Rules are accomplishing the desired outcome of reducing the economic deadweight of UFG, which has declined from more than 2 percent to less than 1.5 percent of annual consumption over the past two years.

Where once there was an understanding, but no binding process, for managing major gas supply emergencies, clear rules now apply to the industry's response to critical contingency events. A critical event exercise during 2010/11 showed that participants are generally aware of their obligations, and that the industry will respond positively to a serious event.

With the regulated and non-regulated arrangements already in place, the downstream gas markets are generally working very well. There is always room for improvement and this remains a core focus of the Company's work.

In parallel, the Company is becoming more actively engaged with the wider gas industry to contribute to the ongoing success of gas, and of the complex industry that searches for, produces, transports, markets and consumes it.

The gas industry, like any other, is ultimately dependent on confident participants, efficient and attractive markets, and ongoing investment at all stages. As a richness of information is essential to a healthy market, Gas Industry Co will continue to promote improved information availability to enable participants to make informed decisions and allocate resources efficiently.

As part of fostering improved information, and in leading the overall gas story, Gas Industry Co will continue to work closely with the Government, which has oversight of the upstream exploration and production sector, and with the Commerce Commission, on economic regulation of transmission and distribution owners. The outcomes of both are critical to the gas industry as a whole.

The Company is also well placed to contribute to efficient gas transportation, in which transmission access and pricing arrangements allocate capacity efficiently and signal the need for new investment, as well as to the development of appropriate regulatory arrangements that support investment where it is required.

As this Annual Report shows, the gas industry co-regulatory model continues to provide a solid platform. In the words of Professor Stanford Levin in a report released in July 2011 on "Policy Considerations for the New Zealand Natural Gas Industry", the "system of co-regulation... is unique to New Zealand. It does, however, seem to be working".

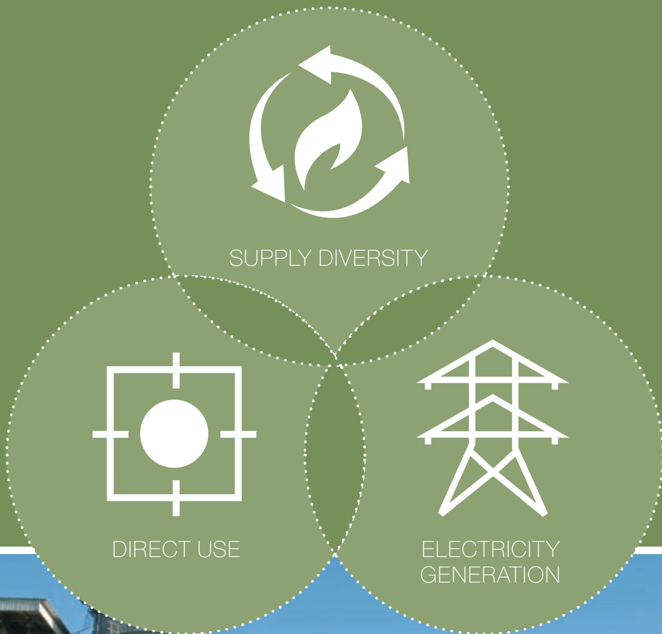
I am confident that Gas Industry Co has the key issues in hand and the tools to deliver outcomes for the industry and for New Zealand.

Steve Bielby
CHIEF EXECUTIVE

KEY ACHIEVEMENTS IN 2010/11		
ACTIVITY	MEASURE	ACHIEVEMENT
CONSUMER ISSUES	Undertake baseline assessments of retail gas contracts and monitor voluntary adoption of benchmarks.	Baseline assessments completed as initial phase of retail contracts oversight scheme to protect the long-term interests of small gas customers.
DISTRIBUTION CONTRACTS	Develop a consultation paper on key issues by May 2011.	Consultation Paper concludes regulations are not required at this time, but improvements can be made. Benchmarks are being developed to align with policy objectives for efficient market structures, reasonable access, and clarity of roles involved in the provision of services.
TRANSMISSION – CAPACITY	If regulations to address capacity constraints on the transmission North Pipeline are required, develop and consult on preferred options by December 2010.	Proposals to address short and long-term capacity constraints developed. Commitment-based industry arrangement implemented after balance date to resolve short-term issues. Gas Transmission Investment Programme established to ensure efficient use of existing capacity and provide a pathway to future investment.
GAS GOVERNANCE (CRITICAL CONTINGENCY MANAGEMENT) REGULATIONS 2008	Set performance standards and review performance of the Critical Contingency Operator (CCO); monitor results of annual exercise.	CCO function working efficiently and arrangements tested in an annual exercise in March 2011.
GAS (SWITCHING ARRANGEMENTS) RULES 2008	Manage Registry Operator and conduct an annual performance review.	The Switching Rules are highly effective and the Registry is delivering on performance measures.
GAS (DOWNSTREAM RECONCILIATION) RULES 2008	Manage the Allocation Agent and conduct a performance review.	Allocation Rules effective in monitoring and identifying reconciliation practices, and will be reviewed for improvements in 2011/12. Audit of Allocation Agent in progress.

OPTIMISING GAS IN NEW ZEALAND.

SECURITY OF SUPPLY



CHAPTER 3.

OPERATIONS

– COMPETITIVE MARKETS

Gas industry Co develops, oversees and administers industry arrangements designed to create efficient, competitive customer markets. Through tailored processes, information disclosure and constant monitoring, these arrangements provide a clear governance framework for participants and are delivering benefits to gas users.

Switching and Gas Registry

The Switching Rules are highly effective and the Gas Registry is operating to its performance standards.

During 2010/11, gas customer switches averaged about 3,000 per month. The switching rate increased to over 3,600 in the month of June, most likely due to the effect of the Electricity Authority's "What's my Number" campaign on switching rates for dual fuel customers. The Registry processed 36,795 switches during 2010/11, slightly more than the 36,650 in the previous financial year. Prior to the Gas Registry going live in March 2009, monthly switches averaged about 1,000, with an annual switching rate of 4.8 percent.

Currently, the annual switching rate among gas consumers is about 15 percent, compared with 18.7 percent in the electricity sector.

Switches are also being completed faster since the advent of the Switching Rules. Since October 2010, the average time for processing switches has been consistently below seven days, compared with periods of weeks and, in some cases, months to complete switches previously.

Governance Systems

GAS INDUSTRY CO INTRODUCED, AND NOW OVERSEES, THE FOLLOWING GOVERNANCE SYSTEMS FOR KEY SECTORS OF THE GAS INDUSTRY:

» Gas (Switching Arrangements) Rules 2008 (Switching Rules), which provide for a central registry of ICP data, and facilitate customer switching among retailers;

» Gas (Downstream Reconciliation) Rules 2008 (Reconciliation Rules), which prescribe the process for volumes of gas consumed to be appropriately attributed to the retailers responsible for them;

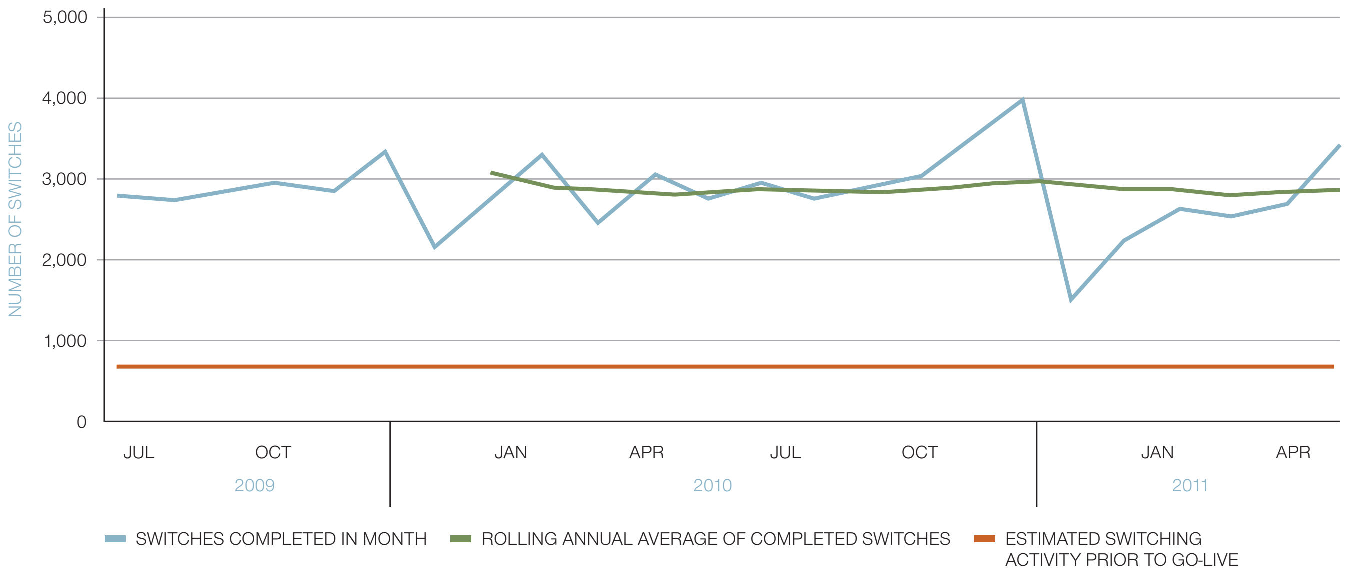
» Gas Governance (Critical Contingency Management) Regulations 2008 (CCM Regulations), which set out how industry participants plan for and respond to a serious incident affecting gas supply via the gas transmission pipelines; and

» Gas (Processing Facilities Information Disclosure) Rules 2008 (Processing Information Disclosure Rules), which detail information to be provided by owners of gas processing facilities.

All of these are underpinned by the Gas Governance (Compliance) Regulations 2008 (Compliance Regulations), under which alleged breaches of the rules and regulations are determined and settled efficiently.

Gas Industry Co monitors the effectiveness of the governance arrangements through a set of industry performance measures. Results of the industry's performance are published regularly on the Company's website.

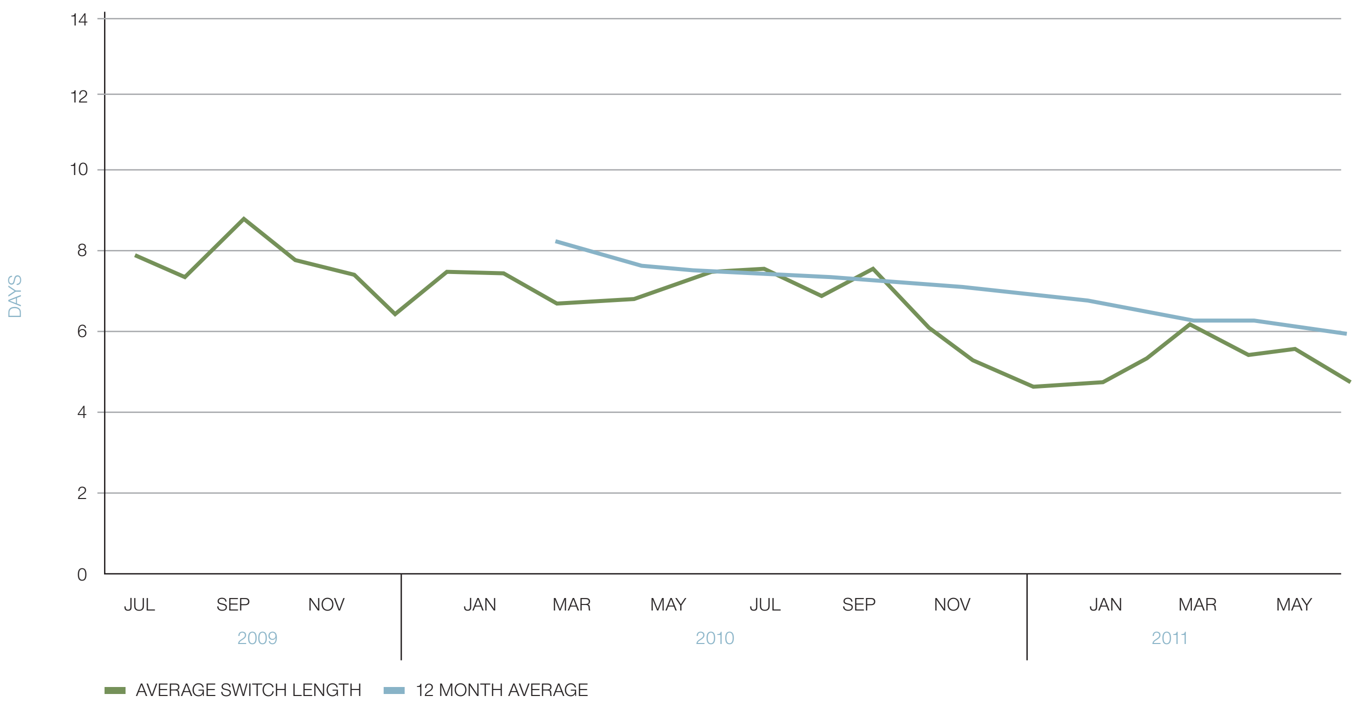
FIGURE 1: MONTHLY SWITCHING ACTIVITY 2009-2011



NOTES:

Switching figures exclude approximately 6,350 E-Gas customers transferred to Nova Energy in November 2010 as a result of Nova purchasing the customer base from E-Gas's liquidator. The figures also exclude 2,243 "re-branding" transfers from Auckland Gas to Nova Energy in June 2011, as both retailers are part of the Todd Group.

FIGURE 2: SWITCH TIME LENGTH 2009-2011



Downstream Reconciliation

Under the Reconciliation Rules, the amount of gas that retailers estimate their customers have used is compared with the amount leaving the transmission system. The difference is unaccounted-for-gas (UFG), which usually arises from technical losses on the system, metering inaccuracies, and retailer estimation errors. UFG imposes a cost on the market and is therefore a measure of market efficiency.

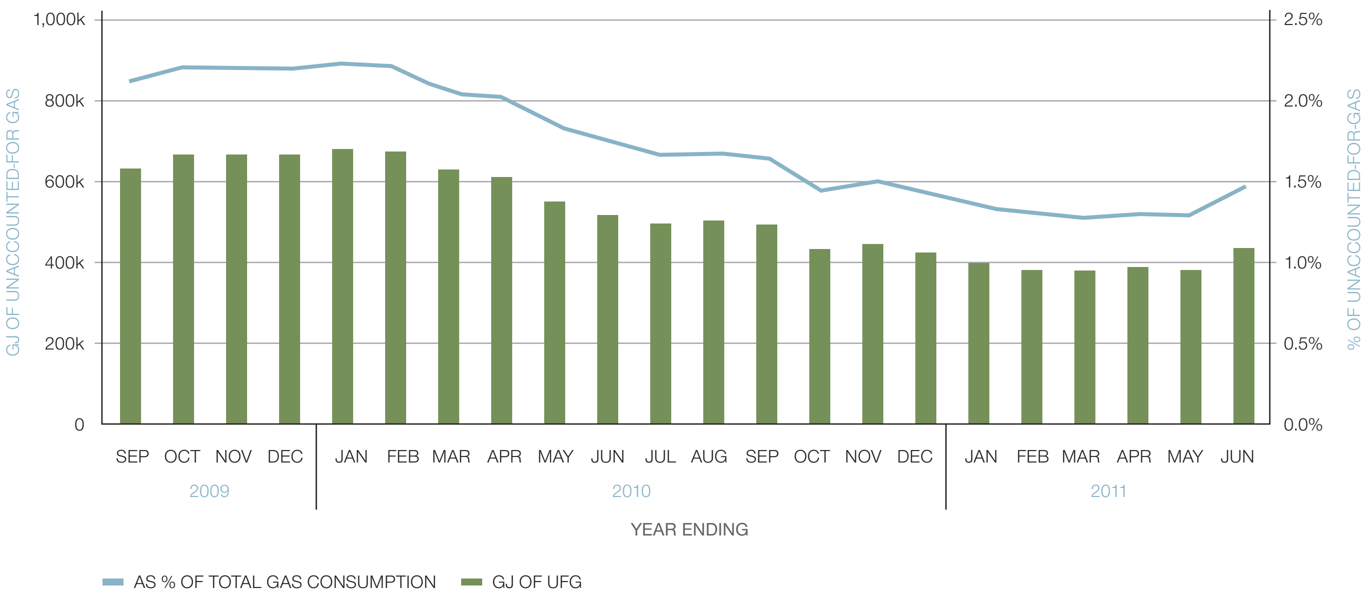
UFG is allocated to all retailers at a gas gate in proportion to their consumption submissions and the resulting totals are used in determining the wholesale charges they are responsible for.

Gas Industry Co regularly monitors gas reconciliation and UFG at all gate stations through monthly reports received from the Allocation Agent, NZX Energy.

In the past two years, annual UFG has declined from over 2 percent of annual consumption to less than 1.5 percent. Figure 3 shows the rolling 12-month UFG since September 2009, both in volume (GJ) and as a percentage of gas consumed.

Gas Industry Co will review the Reconciliation Rules during 2011/12 to see whether improvements can be made in the allocation process, cost allocations and overall compliance costs.

FIGURE 3: ANNUAL UNACCOUNTED-FOR GAS 2009-2011



CASE STUDY.

RECONCILIATION AUDITS PROVE EFFECTIVE

Independent performance audits are conducted to assess retailers' compliance with the Reconciliation Rules. In addition, "event" audits are held to ascertain the causes of a particular issue or event in relation to the allocation of gas.

Reconciliation was among the first issues addressed by Gas Industry Co, as the previous arrangement (the Reconciliation Code), was proving unfair to incumbent retailers, and suffered from a lack of information transparency.

Baseline performance audits of all retailers under the Reconciliation Rules commenced in 2010/11 and were completed shortly after balance date. The audits showed that retailers generally are achieving a high level of compliance; that they have good processes for receiving and storing metering data and validating customers' consumption volumes; and that they are producing information required by the Allocation Agent.

However, the audits also highlighted areas where retailers can make improvements, especially in converting meter readings into the amount of energy used. Measuring energy in a gas flow must factor in a number of parameters, including the temperature of the gas, its pressure, and the altitude at which it is measured. The audits have revealed inaccuracies in converting meter readings into energy, and the need for some retailers to take better account of temperature and altitude in their calculations. Many of these inaccuracies result in under-reporting of customer volumes, thereby increasing the incidence of UFG.

These factors, along with case-specific operating errors, were evident in two event audits held during 2010/11 to examine abnormally high UFG for distribution networks in Hamilton and Palmerston North.

In one case a meter was found to be recording only 10 percent of the gas volume, and, in the other, only half was being measured. Uncovering these errors allowed the retailers to correct them, eliminating causes of UFG and enabling more accurate billing of customers.

A year previously, it was a major spike to unprecedented UFG levels during a sudden cold snap that alerted Gas Industry Co to erroneous consumption reporting by retailers, and revealed serious and systemic misreporting by E-Gas.

Event audits, and a subsequent performance audit, found other discrepancies in E-Gas data over a period of months. The matter was referred to the Investigator, and then to the Rulings Panel for determination. However, just prior to a scheduled hearing before the Rulings Panel in 2010/11, E-Gas declared itself insolvent and went into liquidation.

Following the audits, Gas Industry Co is progressing an energy conversion guideline note to achieve consistency in retailers' energy conversion calculations.

Critical Contingency Management

Gas Industry Co oversees arrangements prescribing how the industry responds to serious supply emergencies. In March 2011, the Critical Contingency Operator (CCO) successfully completed a critical contingency management simulation to test the arrangements put in place under the CCM Regulations. The CCO identified some minor improvements to the critical contingency curtailment processes, and recommendations are being progressed by the industry.

The CCM Regulations were activated in July 2010 in response to a short-lived pressure drop on the Maui pipeline as a result of an unplanned production outage associated with the Pohokura Field, combined with higher than expected market offtakes at Rotowaro. No demand curtailment was required.

Gas Processing Information Disclosure

The Processing Information Disclosure Rules are intended to assist Gas Industry Co to determine whether it is necessary to recommend rules or regulations for setting terms and conditions for access to, and use of, gas processing facilities. They were introduced in June 2008, and are effective for six years.

They require owners to make publicly available annual information on the capacity, capability and availability at their gas processing facilities, and to enable Gas Industry Co to monitor their responses to requests for third party access to those facilities.

Gas Industry Co monitors the disclosures, and no significant processing facility access issues have been identified to date. The Company is required to report to the Minister on the effectiveness of the Rules by 27 June 2013.

Wholesale Market Trading Platform

During the year, Gas Industry Co recommended to the Minister the discontinuation of a gas wholesale market trial, commenced in 2009/10. The trial was intended to provide a formal and transparent platform for short-term trading of relatively small wholesale gas volumes. It involved the creation of a low-cost electronic trading platform that allowed potential traders to post offers to buy and/or sell gas for up to six months. Disappointingly, the trial attracted little interest from gas wholesalers and was discontinued.

However, Gas Industry Co considers that a recent proposal by Maui Development Limited to extend the functionality of an existing Balancing Gas Exchange (BGX) may provide an industry-led solution to achieving Government Policy Statement objectives for a short-term wholesale gas market. These objectives are to provide wholesale price transparency as well as create an avenue for parties with take-or-pay contracts to readily adjust their positions.

The indicated BGX extension would accommodate wholesalers making spot trades, introduce a form of price signalling, and apply market rules similar to those proposed by Gas Industry Co for the trial. In addition, the creation of a "trading hub" within the Maui pipeline would provide the basis for a system of title tracking, which is essential in such a market.

Gas Industry Co will maintain a close watching brief on the BGX developments.

LPG

Gas Industry Co's scope covers the bottled LPG markets and gaseous LPG supplied via reticulated networks. It does not extend to bottles themselves, the supply and bulk storage of LPG, or to pipelines carrying LPG in liquid form between transport depots and bulk storage facilities. The Company is not aware of any issues in the LPG markets that would warrant regulatory intervention, and continues to monitor these markets.

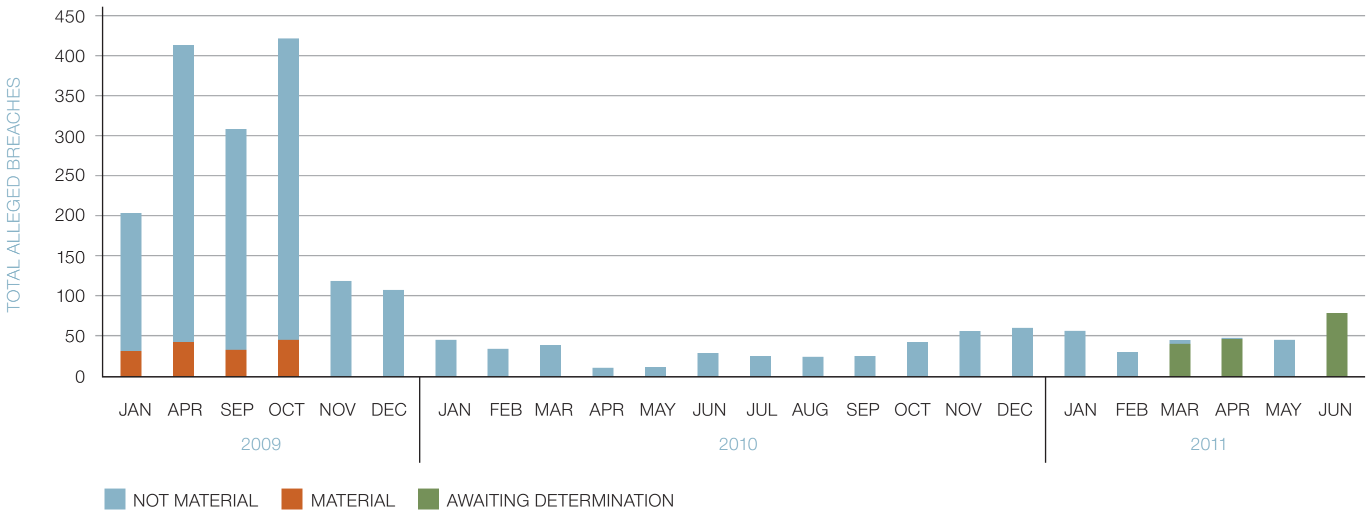
Compliance

Gas Industry Co administers the Compliance Regulations arrangements that provide for the monitoring and enforcement of rules which ensure the integrity of key markets.

Of the 2,742 breach allegations considered during 2010/11 by Gas Industry Co in its role as the Market Administrator, 1,478 (54 percent) were determined to be not material, 285 (10 percent) were referred to the Investigator, and 979 (36 percent) are awaiting determination. This compares with a total of 3,176 allegations in 2009/10, of which 2,784 (88 percent) were deemed not material, and 392 (12 percent) were referred to the Investigator.

Breach allegations to date have related almost exclusively to the Switching Rules and Reconciliation Rules.

FIGURE 4: SWITCHING RULES BREACHES 2009-2011



The number of switching breaches, and their severity, has fallen significantly since the inception of the Switching Rules. Switching breaches made up 20 percent of all breaches during 2010/11, and related primarily to the timeliness of notices required to be submitted to the Registry as part of the switching process. The Market Administrator has not determined a breach of the Switching Rules to be material since October 2009. The slight rise in breaches from March 2011 can likely be attributed to retailers adjusting to the minor amendments to the Switching Rules which came into effect in February 2011.

Reconciliation Rules breaches are shown in Figure 5 on Page 16. The marked increase in alleged breaches from December 2009 onwards represents breaches of rule 37. This is the rule that requires the accuracy of consumption information provided at the initial allocation stage to be within the specified tolerance level of the information provided at the final allocation stage. In the 2010/11 financial year, rule 37 breaches made up 86 percent of Reconciliation Rules breaches, and Reconciliation Rules breaches accounted for 80 percent of all breaches.

Although the levels of Reconciliation Rules breaches remained consistent with the previous year, industry participants appear to have a good understanding of the Reconciliation Rules, and most breaches do not have a material impact on the market. A review of the Reconciliation Rules in 2011/12 will consider whether some of the more trivial breaches currently alleged can be minimised.

Investigator and Rulings Panel – Approved Settlements and Determinations

The number of approved settlements and determinations by the Rulings Panel are shown in Figure 6 on Page 16. The Investigator is independent from Gas Industry Co and has a range of powers under the Gas Act 1992 to investigate and report on breach allegations. The Investigator is able to effect settlements, which must be referred to the Rulings Panel for approval or rejection.

The Rulings Panel is an independent body appointed by the Minister of Energy under the Compliance Regulations. The current Rulings Panel is the Hon Sir John Hansen, KNZM. In a quasi-judicial process, the Rulings Panel approves or rejects settlements referred by the Investigator and determines breach allegations that are unable to be settled, or in respect of which a settlement has not been approved.

FIGURE 5: RECONCILIATION RULES BREACHES 2009-2011

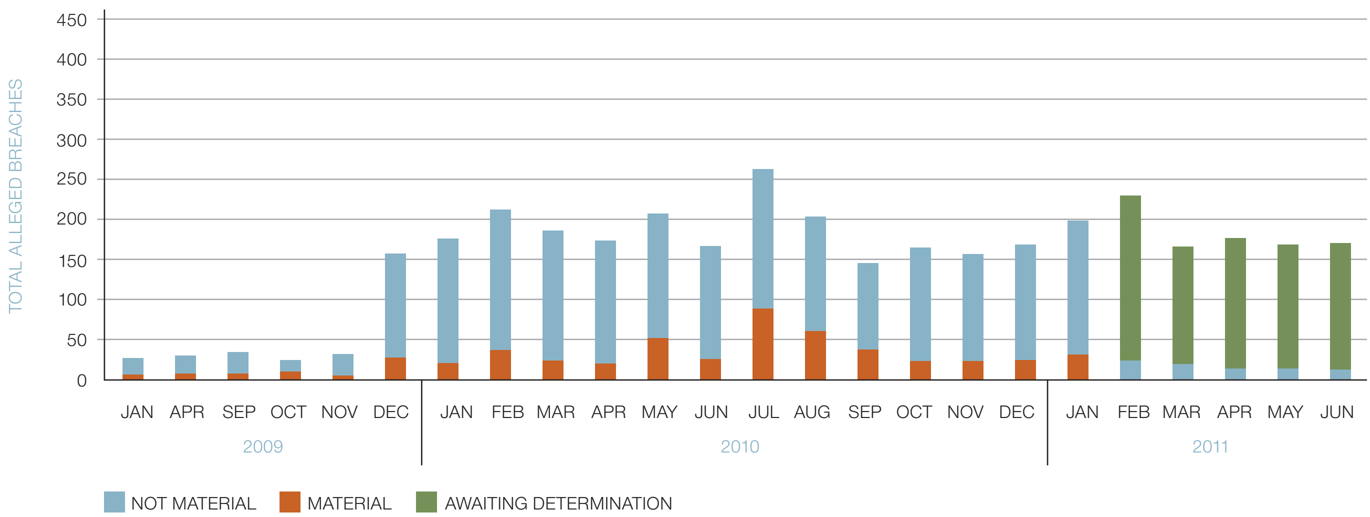
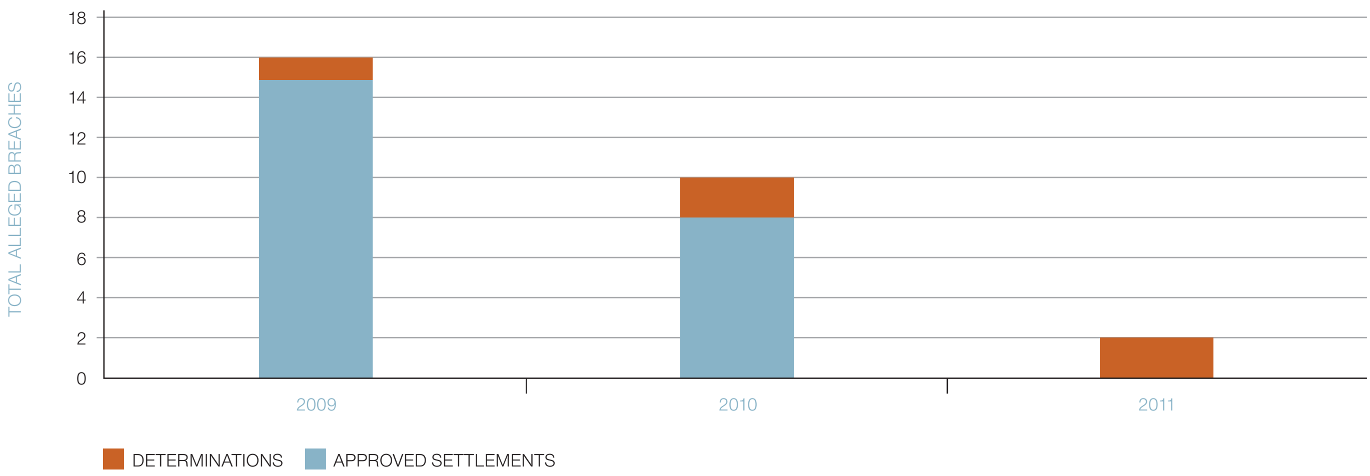
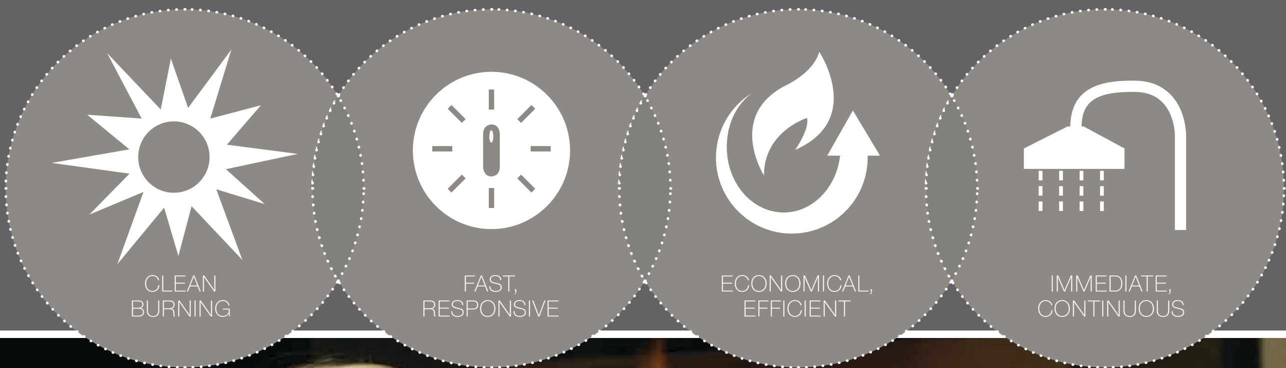


FIGURE 6: RULINGS PANEL APPROVED SETTLEMENTS AND DETERMINATIONS 2009-2011



OPTIMISING GAS IN NEW ZEALAND.

QUALITY OF LIFE



CHAPTER 4.

OPERATIONS

– IMPROVING CONSUMER OUTCOMES

In addition to the Company's work to promote competitive markets, including more timely and efficient switching, which delivers a range of benefits for consumers, moves to improve retail gas supply arrangements and the availability of a complaints resolution process are also aimed at enhancing consumer outcomes.

Retail Contracts

Gas Industry Co operates a retail contracts oversight scheme, involving annual assessments of the alignment of retail gas supply arrangements with outcome-based benchmark objectives. These are to ensure consumer contracts are in the long-term interests of consumers, clearly set out retailer and consumer obligations, reflect market structures, and support an effective complaints resolution process.

The scheme was endorsed by the Minister in May 2010 and, in September 2010, Gas Industry Co issued a baseline assessment of retail contracts. The assessment, undertaken by an independent assessor, Elwood Law, reviewed publicly available retail contract arrangements as at 15 June 2010. The independent assessor rated the industry's alignment with the benchmarks overall as "moderate". However, although identifying some areas of poor alignment with the benchmarks in the written arrangements, the independent assessor reported that, in practice, gas retailers' operations appeared to achieve the intent of the benchmarks.

Areas requiring improved clarity included:

» rights to exit a contractual arrangement;

» reasons for price increases over 5 percent when notifying customers of such a change;

» metering obligations, especially the frequency of readings;

» disconnection processes; and

» where customers may access information about supply interruptions.

A transitional assessment of arrangements is being undertaken early in the 2011/12 financial year to establish the degree of progress being made by each retailer in aligning their contractual arrangements with the benchmarks since the baseline assessment.

Consumer Complaints Scheme

An effective, free and independent complaints resolution process for gas consumers is provided by the Electricity and Gas Complaints Commission (EGCC).

The EGCC was approved as the consumer complaint resolution scheme for the electricity and gas industries, effective from 1 April 2010, and is overseen by the Ministry of Consumer Affairs. Gas Industry Co liaises closely with EGCC, the Electricity Authority and the Ministry to stay informed of issues relevant to consumers.

In its Annual Report for 2010/11, EGCC has reported that its workload generally had increased dramatically due to more industry members joining the scheme, higher consumer awareness, and increased consumer switching between retailers.

Consumer enquiries relating specifically to gas increased from 84 in 2009/10 to 173, and gas-related complaints rose by 23 to 47. In addition, dual fuel (electricity and gas) consumer enquiries and complaints increased from 29 to 46, and 18 to 27 respectively. However, the rate of gas complaints per ICP is less than half of that for electricity, and that ratio has been improving over recent years (see Figure 8 on Page 19).The most common grounds for consumer inquiries and complaints were supply, billing, and connection/disconnection issues.

In December 2010, the scheme was expanded to include reticulated LPG. No reticulated LPG cases were reported by EGCC between then and 30 June 2011.

FIGURE 7: GAS-RELATED INQUIRIES AND COMPLAINTS

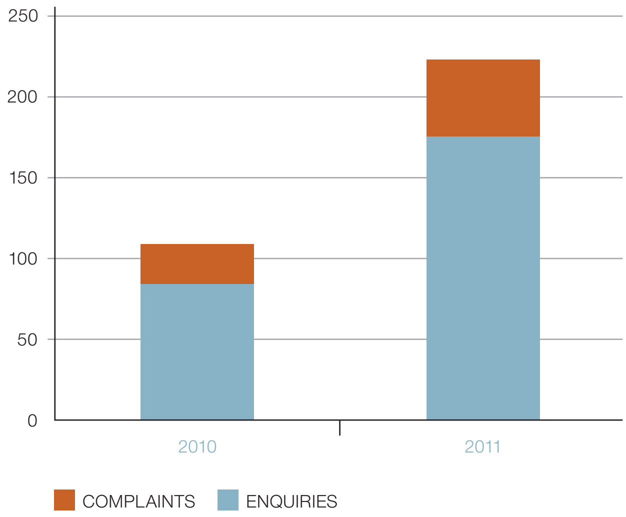
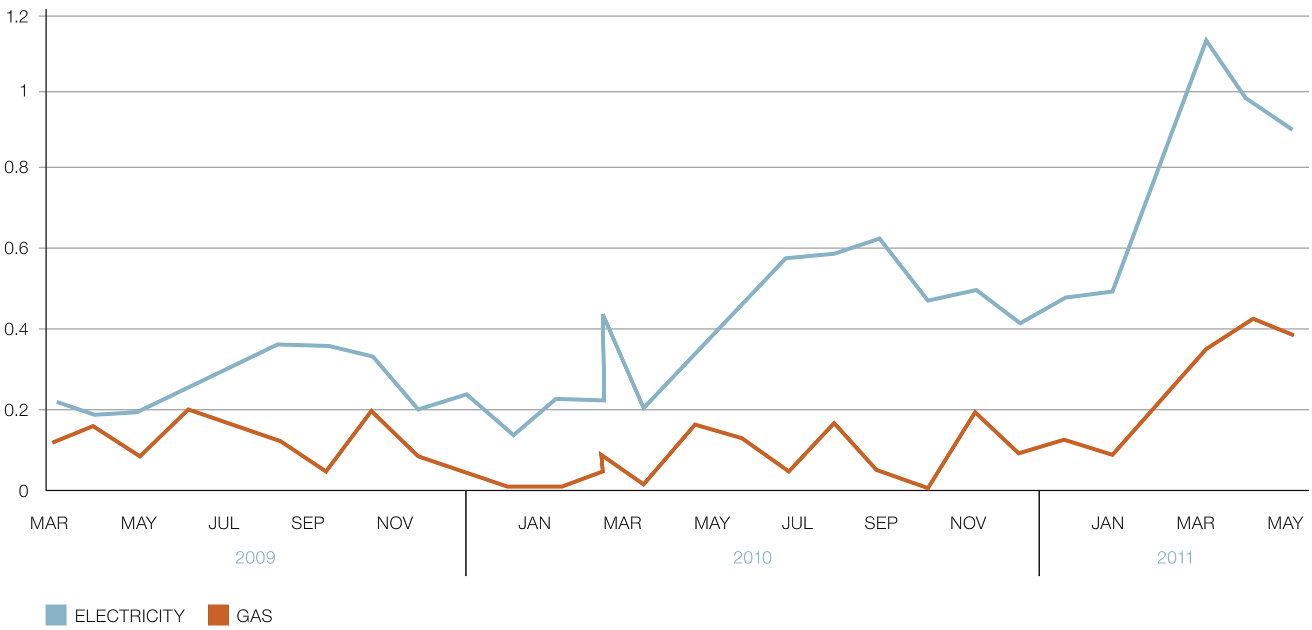


FIGURE 8: ELECTRICITY AND GAS COMPLAINTS PER 10,000 ICPs



CHAPTER 5.

OPERATIONS

– ACCESS TO INFRASTRUCTURE

Access to key infrastructure on reasonable terms and conditions is essential to competitive and efficient markets.

While issues arising over transmission capacity and investment needs have prominence among Gas Industry Co's priorities, the Company's attention was also directed to a range of other infrastructure issues during 2010/11. This included gas quality, pipeline balancing, gas distribution contract arrangements, interconnection to open access and private transmission pipelines, and proposed changes to the Maui Pipeline Operating Code.

Capacity Constraints

As reported in 2009/10, Gas Industry Co commenced a review of transmission pipeline capacity arrangements when it became clear that a capacity constraint on Vector's North Pipeline might be affecting competition and growth in the Auckland gas market. Some large end users raised concerns that the constraint, together with "grandfathered" capacity entitlements held by a small number of suppliers, limited the number of competitive, unconditional bids they can attract when tendering their gas supply.

During 2010/11, Gas Industry Co conducted several industry workshops to examine the competition issue and to identify solutions that would provide existing large end users a greater choice of supplier. To address the issue, Gas Industry Co initially proposed rules that would require transmission capacity to follow the end user, where that end user wished to change supplier. However, some suppliers expressed a strong preference for a more market oriented, non-regulatory response. They believed this would have the additional benefit of providing a transitional bridge to longer term solutions. To achieve this, these suppliers agreed to a package of arrangements called the "Bridge Commitments".

Gas Industry Co agreed that these Bridge Commitments, if honoured, should significantly change the market and provide large end users on the North Pipeline greater supplier choice. The Company also considered the Bridge Commitments to be consistent with broader reforms over the next two years to improve transmission access and pricing arrangements, and to provide incentives for future investment. The Bridge Commitments, which were implemented after balance date, removed the immediate need for rules.

The Bridge Commitments require key North Pipeline suppliers holding grandfathered gas transmission capacity entitlements to offer capacity to competitor suppliers, where large end users wish to change supplier.

Suppliers have also committed to disclose for the first time details of capacity offers in tender processes, to enable the effectiveness of the commitments to be fully assessed. The commitments also allow for capacity secured under long-term gas-fired power station contracts to become available to other users when not required for power generation.

The package also includes the development of a bulletin board that will improve transparency around capacity trades.

Gas Industry Co will monitor the arrangements very closely over coming months.

In parallel, the industry has asked the Company to develop and lead a Gas Transmission Investment Programme (GTIP). The objective of the GTIP is to:

- ensure that existing and future gas transmission assets are used efficiently;
- establish the need for gas transmission investment; and
- develop an effective pathway for efficient gas transmission investment to take place.

The GTIP comprises three project areas: information, markets, and regulatory. Work under these projects will include consideration of:

- how to ensure arrangements for transmission access and pricing allocate capacity efficiently, and effectively signal the need for investment in additional capacity;
- what increased market information is required to allow stakeholders to take informed decisions about the allocation of resources; and
- what regulatory arrangements will best support efficient investment in transmission infrastructure.

Two advisory panels have been created to provide advice to Gas Industry Co in relation to the GTIP. The GTIP is expected to last 18-24 months.

Pipeline Balancing

Transmission pipeline balancing involves managing the inventory of gas in a pipeline within acceptable limits. Gas Industry Co's objective is to provide an efficient, unified balancing arrangement for managing pipeline imbalances.

Achieving this is a priority for the Company, which has coordinated a process to explore alternatives, including both regulated and voluntary options. Changes to the Maui Pipeline Operating Code to improve balancing arrangements have been proposed as preferable to regulated alternatives, and there is evidence that the extent of balancing activity, and associated costs, have reduced substantially over recent years.

Gas Industry Co has consequently decided to defer a final recommendation on balancing and adopt a wait and see approach. Industry balancing arrangements will be further reviewed by February 2012.

Interconnection to Transmission Pipelines

Gas Industry Co conducted a review of the interconnection arrangements of the two open access transmission system owners, Maui Development Limited and Vector Limited, against Gas Industry Co's Guidelines on Interconnection with Transmission Pipelines (the Interconnection Guidelines). The review showed both owners' arrangements were generally well aligned with the Guidelines. Regulation is not considered necessary at present, and the Company will continue to evaluate new interconnections.

Gas Industry Co also provided advice to the Minister on interconnection to private transmission pipelines. The advice concluded that, as the Interconnection Guidelines were designed for open access pipelines, they would need to be amended in order to apply to private pipelines. It concluded that further regulatory reform is not warranted at this time.

Gas Quality

Maintaining an acceptable standard of gas quality is important for the entire gas industry, as quality affects combustion performance, safety, the reliability of gas supply, and the long-term integrity of the gas transportation system. The gas standard is established by NZS 5442:2008 Specification for Reticulated Natural Gas (the Gas Specification).

During 2010/11, Gas Industry Co reviewed industry arrangements for gas quality to assess whether appropriate arrangements are in place to prevent gas quality incidents, and if contractual arrangements allow the costs of a gas quality incident to be met efficiently.

A gas quality issues paper by Gas Industry Co highlighted the concern of some participants that the parties with the legislative responsibility for achieving compliance with the Gas Specification may not have sufficient influence over the parties who physically control the gas quality. The contractual linkages between those parties can be complex and may not provide proper incentives for good control, monitoring, reporting and auditing of gas quality. It was a further concern that, in the event of a quality-related outage, the costs may not be borne by the party who caused the quality problem.

While Gas Industry Co concluded that regulation was not required at this time, the Company considers continued work across the supply chain is necessary to improve existing arrangements, including monitoring, testing, reporting and auditing practices. Consideration is also being given to introducing greater transparency on gas quality incidents, such as a quality complaints process.

Gas Industry Co is aware that, in parallel with its own activities, some retailers have combined to work with producers, wholesalers, transmission owners and distributors to obtain information required for them to demonstrate they are meeting their obligations under the Gas (Safety and Measurement) Regulations 2010. In light of this, the Company will further consider its own work on gas quality following the outcome of the retailers' initiative.

Distribution Contracts

An initial assessment during the year of terms and conditions for access to distribution networks concluded that regulation is not required at this time.

However, improvements can be made to ensure arrangements meet the objectives of the Gas Act 1992 and the Government Policy Statement to ensure that gas distribution is safe, efficient and reliable; there is an efficient market structure for gas metering, pipeline services and energy services; the respective roles of metering, pipeline and retailer service providers are understood; and there is reasonable access by new and existing retailers to distribution services.

The review found that some distribution contracts are out of date, and others are not published.

A consultation paper, *Draft Principles for Arrangements on Gas Distribution Systems*, was published by Gas Industry Co in June 2011, with submissions invited by 29 July. Gas Industry Co will work towards finalising the principles during 2011/12, and will monitor, and report on, distributors' progress with updating their contracts.

Code changes

Changes to the Maui Pipeline Operating Code, proposed by parties to the code, require Gas Industry Co's support before they can proceed. In the case of the separate Vector Transmission Code, Gas Industry Co's role is to consider any appeals in respect of code changes.

In April 2011, Gas Industry Co published a draft recommendation on a request by Maui Development Limited for amendments to the Maui Pipeline Operating Code. The request includes changes to prudential requirements, and the improvement of information to all parties on real time pipeline operations and operational imbalances at welded points. After considering submissions, Gas Industry Co's draft recommendation concluded that, overall, the proposed changes provide a net benefit. The final recommendation, issued by Gas Industry Co post balance date, confirms this conclusion.

CHAPTER 6.

EFFECTIVE CO-REGULATION

Gas Industry Co was established in 2004 and was approved that year as the gas industry's co-regulatory body under Part 4A of the Gas Act 1992. The Company fully commenced operations in 2005 and works with both the Government and the industry to develop recommendations on governance arrangements that meet the objectives of the Act and the April 2008 Government Policy Statement on Gas Governance.

The Company's oversight encompasses the gas wholesale and retail markets, processing facilities, and the transmission and distribution sectors of the industry.

Gas Industry Co is also progressing a broader corporate strategy, involving closer liaison with all participants in the industry, to optimise the contribution of gas to New Zealand.

External Relations

Gas Industry Co works closely with other regulatory bodies, including the Ministry of Economic Development and the Commerce Commission, whose responsibilities also encompass the gas industry, and maintains relationships with many other agencies engaged in the energy and related sectors. These include the Electricity Authority, Energy Efficiency and Conservation Authority, the Petroleum Exploration and Production Association of New Zealand, the Gas Association, LPG Association, the Electricity and Gas Complaints Commission, Energy Safety, and environmental agencies.

Facilitating industry contributions and debate is an important function for the smooth operation of the co-regulatory model and Gas Industry Co conducts an annual Co-regulatory Forum to discuss the matters that will form the forthcoming year's work programme, upon which the Company's levy funding is calculated. The Company will also convene special workshops to engage with the industry and consumers on particular issues arising from ongoing workstream activity.

Stratgic Priorities and Levy Consultation

Between October and May each financial year, Gas Industry Co conducts a detailed consultation programme to establish its strategic priorities for the coming year and, from that, to develop its Strategic Plan and recommend levies needed to fund the planned activities. The consultation with industry participants overlays with the Company's views, as the industry body, on the overall role of gas in New Zealand and the governance requirements for ensuring efficient and competitive markets.

Gas Industry Co is committed to ensuring that the levies are well justified and used carefully.

The composition of the Company's total levy revenue has changed in the last three years as user-targeted market fees have been introduced to fund the administration of certain rules and regulations, including the recovery of the costs of external service providers and consultants. In addition, retail and wholesale levies are applied each year to cover the costs of the Company's policy and market administration work, and the Company's Constitution enables the Board to charge shareholders an annual fee. This is currently set at $10,000 per shareholder per annum.

FIGURE 9: LEVY AND FEE REVENUE 2005-2011

* 8 months. 2005 revenue comprised only the annual shareholders' fee.

Financial Discussion

During the year, the Board reviewed both the level of its reserves – in particular the Industry Advances Reserve, representing net over-recoveries of levies from previous years – and the policy of using these to offset levies in subsequent financial years.

In its initial years, the Company took a cautious approach to its reserves while its role and the costs of addressing industry governance needs were worked through. During 2010/11, the Board reached the view that it could reduce the level of reserves held and to generally return any surpluses each year, subject to retaining a prudent level of reserves to address unplanned matters.

Consequently, the Board decided to return $1,501,829 of accumulated surplus levy revenue to industry participants.

Surplus levy revenue for the 2010/11 financial year amounted to $364,188. When considering whether it is prudent to return all or part of this sum, the Board will particularly take account of costs associated with the new Gas Transmission Investment Programme.

Total operating revenue for the year ended 30 June 2011 amounted to $5,971,489, compared with $7,339,924 in the 2009/10 financial year, and the $6,535,400 budgeted in the FY2011-13 Strategic Plan. The variance in Market Fee revenue against budget is attributable mainly to a mid-year revision in estimated costs leading to reduced market fee collection, and the payment of refunds for the previous year's wash-ups. The Market Fee adjustment was partly offset by additional Wholesale Levy income of $140,446.

Operating expenses totalled $5,998,907, compared with $6,288,704 in the corresponding previous financial year, and budgeted expenses of $7,029,809. As with the year's revenue, most of the expense variance related to revised expectations for cost recoveries, resulting in an expenditure reduction of $1,231,644. This was partly offset by a $74,527 bad debt expense from the liquidation of the E-Gas group of companies.

Gas Industry Co's equity reserve as at 30 June 2011 consisted of three components – the Industry Advances Reserve of $364,188, the Industry Amortisation Reserve of $1,227,662, and Retained Earnings of $350,000.

The Industry Amortisation Reserve represents the unexpended amortisation on capital items purchased with Market Fees, including the Switching Registry and Downstream Reconciliation systems. The ongoing annual amortisation costs of $363,804 associated with these assets is met from the Amortisation Reserve and, over time, the value of both the assets and the reserve will reduce to zero.

Retained Earnings are the accumulation of the shareholders' annual fees, and are set aside as a reserve against future contingencies. They do not impact on the levy calculation.

OPTIMISING GAS IN NEW ZEALAND.

INDUSTRY PERFORMANCE

CUSTOMER SWITCHING

TRANSPARENCY

CONTINGENCY MANAGEMENT

COMPLIANCE

CHAPTER 7.

CORPORATE GOVERNANCE

Gas Industry Co is owned by industry participant shareholders and is funded by levies on industry participants. It is incorporated as a company under the Companies Act 1993, and operates in accordance with the Gas Act 1992, the 2008 Government Policy Statement on Gas Governance, and the Company's Constitution.

Gas Industry Co encourages all industry participants to become shareholders of the Company. Each shareholder holds a $1 share, which is redeemable at the option of the shareholder. Shareholders are entitled to one vote on resolutions at shareholders' meetings, including those that appoint directors and change the Constitution.

Shareholders

THE COMPANY'S SHAREHOLDERS REPRESENT SECTORS ACROSS THE GAS INDUSTRY – PRODUCTION, TRANSMISSION, DISTRIBUTION, WHOLESALE, RETAIL AND CONSUMPTION. THERE WERE EIGHT SHAREHOLDERS AS AT 30 JUNE 2011:

» Contact Energy Limited
» Greymouth Gas New Zealand Limited
» Genesis Power Limited (trading as Genesis Energy)
» Mighty River Power Limited
» OMV New Zealand Limited
» Powerco Limited
» Shell (Petroleum Mining) Limited
» Vector Limited

Board of Directors

The Board of Gas Industry Co normally meets on up to 10 scheduled occasions per year to consider operational reports and recommendations from Gas Industry Co's management. Unscheduled meetings are held from time to time to consider matters requiring immediate attention. Directors will attend either in person or via teleconference.

The Board is a mix of Independent and non-independent directors, all appointed by the shareholders, and its composition accords with a Gas Act requirement to have a majority of Independent Directors, including the Chair. This requirement reflects the aim of creating a co-regulatory gas industry body, which benefits from industry director participation and experience, balanced by a range of independent expertise. The Company's Constitution limits the Board to no more than seven directors, four of whom are independent of the gas industry. The number of Independent Directors voting on an issue must exceed the number of non-independent directors voting on the same matter.

Simon Mackenzie stepped down at the 17 November 2010 Annual General Meeting and his seat on the Board was filled by Ron Kelly. In April 2011, David Baldwin resigned as a Director. The Board appointed Dennis Barnes to fill the resulting casual vacancy, and his appointment was finalised on 13 May 2011. Mr Barnes is required to retire at the 2011 Annual General Meeting and can stand for re-election.

Directors as at 30 June 2011:

RT HON JAMES (JIM) B BOLGER, ONZ

CHAIR AND INDEPENDENT DIRECTOR

// APPOINTED 4 NOVEMBER 2004

Jim Bolger has had a distinguished career in politics that includes being Prime Minister of New Zealand from October 1990 to December 1997, holding ministerial positions for 16 years, and leading the New Zealand National Party for 12 years. He has been the Chair since the Company's establishment.

INTERESTS REGISTER

// CHAIR
Trustees Executors Limited,
Mt Cook Alpine Salmon Limited

// CHANCELLOR
Waikato University

ROBIN G HILL, B COMM, FCA

DEPUTY CHAIR AND INDEPENDENT DIRECTOR

// APPOINTED 4 NOVEMBER 2004

Robin Hill has an extensive background in financial and business management. He was Chairman and Chief Executive of PricewaterhouseCoopers New Zealand from 1992 to 2003. He has been the Deputy Chair since the Company's establishment.

INTERESTS REGISTER

// DIRECTOR
Public Trust

// ADVISORY TRUSTEE
NZ Defence Force

ANDREW BROWN, LLB

INDEPENDENT DIRECTOR

// APPOINTED 10 JUNE 2010

Andrew Brown is recognised as one of New Zealand's leading corporate lawyers. He has particular expertise and experience in advising energy sector companies.

INTERESTS REGISTER

// CONSULTANT
Bell Gully

// INDEPENDENT EXPERT ADVISOR
The Treasury

// CONTRACT NEGOTIATOR
Ministry of Foreign Affairs

// COMMERCIAL NEGOTIATOR
Crown Fibre Holdings Limited

KEITH DAVIS, PGDipBus

INDEPENDENT DIRECTOR

// APPOINTED 31 JULY 2006

Keith Davis has extensive experience in the information technology, telecommunications and venture-funding industries, and has held senior management roles with McDonnell Douglas, Compaq Computers, and BellSouth.

INTERESTS REGISTER

No interests relevant to Gas Industry Co

DENNIS BARNES

NON-INDEPENDENT DIRECTOR

// APPOINTED 13 MAY 2011

Dennis Barnes is Chief Executive Officer of Contact Energy. His role followed 13 years in Australia with Origin Energy, including in a range of gas-related roles and serving on the boards of two Australian gas regulators. Prior to that, Mr Barnes worked in various international energy markets, including managerial roles with Scottish and English electricity companies.

INTERESTS REGISTER

// CHIEF EXECUTIVE OFFICER
Contact Energy Limited

// DIRECTOR
Various Contact Energy subsidiaries

// EMPLOYEE
Origin Energy Limited

ALBERT BRANTLEY, BSc, P Geol, F AuSIMM

NON-INDEPENDENT DIRECTOR

// APPOINTED 14 NOVEMBER 2008

Albert Brantley is Chief Executive of Genesis Energy. He also serves as Chairman of the Genesis Oncology Trust and is the Chairman of Energy Online. Mr Brantley has had more than 35 years' experience in New Zealand and internationally in technical, operational and senior management positions, concentrated particularly in the power industry over the past decade. He has had considerable experience in leading businesses requiring political, regulatory and environmental management, both in New Zealand and overseas.

INTERESTS REGISTER

// CHIEF EXECUTIVE OFFICER
Genesis Energy Limited

// CHAIRMAN
Energy Online

// DIRECTOR
Various subsidiaries, including those holding Genesis Energy's 31% interest in Kupe Project

RON KELLY, PhD

NON-INDEPENDENT DIRECTOR

// APPOINTED 17 NOVEMBER 2010

Ron Kelly is the Upstream International Commercial Lead for Shell Exploration NZ Limited. As well as a PhD in Theoretical Physics from Oxford University, he has a broad range of experience from more than 15 years across the natural gas value chain, from the upstream commercial environment including LNG, via multifaceted regulatory regimes, to midstream/ downstream gas sales, marketing and trading. He has been involved in developing and executing Shell's commercial strategy for its interests in several upstream gas-condensate assets in New Zealand (Maui, Pohokura, and Kapuni).

INTERESTS REGISTER

// UPSTREAM INTERNATIONAL COMMERCIAL LEAD/ DIRECTOR
Shell Exploration NZ Limited

Shell Energy Asia Limited

// DIRECTOR
Maui Development Limited

Various subsidiaries of Shell

Interest Disclosures

The following general disclosures were made in respect of other directors who served on the Board during the year.

DAVID BALDWIN

NON-INDEPENDENT DIRECTOR

// TILL 20 APRIL 2011

INTERESTS REGISTER

// MANAGING DIRECTOR
Contact Energy Limited

// DIRECTOR
Various Contact Energy subsidiaries

// EMPLOYEE
Origin Energy Limited

SIMON MACKENZIE

NON-INDEPENDENT DIRECTOR

// TILL 17 NOVEMBER 2010

INTERESTS REGISTER

// CHIEF EXECUTIVE OFFICER
Vector Limited

// DIRECTOR
Various Vector subsidiaries

The Board has one standing committee: the Independent Directors' Committee.

The Independent Directors' Committee comprises the four independent directors. Among other tasks, the Independent Directors' Committee considers certain technical and administrative issues arising from the operation of gas governance arrangements, such as exemption applications under the Reconciliation Rules.

Attendance

DIRECTORS	MEETINGS ATTENDED
J BOLGER	8
R HILL	8
A BROWN	8
K DAVIS	8
S MACKENZIE (TO NOV 2010)	2
D BALDWIN (TO APRIL 2011)	5
A BRANTLEY	6
R KELLY (FROM NOV 2010)	5
D BARNES (FROM MAY 2011)	2

ALTERNATES	MEETINGS ATTENDED
D MCCARTHY (ALTERNATE FOR S MACKENZIE)	1
J WOODS (ALTERNATE FOR D BALDWIN)	1
M ALEXANDER (ALTERNATE FOR A BRANTLEY)	2

INDEPENDENT DIRECTORS' COMMITTEE	MEETINGS ATTENDED
J BOLGER	2
R HILL	2
A BROWN	2
K DAVIS	2

Directors' Remuneration

Directors' remuneration is authorised by ordinary resolution of shareholders and is paid to the Independent Directors only. The current maximum level of Directors' fees, being $275,000, was authorised by shareholders in 2004. Annual fee payments of $93,500 for the Chair, $63,360 for the Deputy Chair, and $52,800 for each other Independent Director were set by the Board in June 2007. Directors' remuneration payments for 2010/11 were:

	YEAR ENDED 30 JUNE 2011 $	YEAR ENDED 30 JUNE 2010 $
RT HON JAMES BOLGER, ONZ (CHAIR)	93,500	93,500
ROBIN HILL (DEPUTY CHAIR)	63,360	63,360
ANDREW BROWN	52,800	–
KEITH DAVIS	52,800	52,800
DAVID BALDWIN (RESIGNED 20 APRIL 2011)	–	–
DENNIS BARNES (APPOINTED 13 MAY 2011)	–	–
ALBERT BRANTLEY	–	–
RON KELLY (APPOINTED 17 NOVEMBER 2010)	–	–
SIMON MACKENZIE (RESIGNED 17 NOVEMBER 2010)	–	–

Other than Directors' fees paid, no other transactions with Directors occurred.

Indemnification of Directors

As permitted by the Constitution and the Companies Act 1993, Gas Industry Co has indemnified its directors, and has provided directors' liability insurance for officers and directors. This insurance and indemnity is with respect to potential liabilities and costs they may incur for acts or omissions in their capacity as directors and officers.

During the financial year, Gas Industry Co paid insurance premiums in respect of directors' and officers' liability insurance. In accordance with the Companies Act, the Directors have certified that the cost of this insurance is fair to the Company.

Annual General Meeting

The Company's Annual General Meeting was held on 17 November 2010. In accordance with the Company's Constitution, Mr Andrew Brown, having been appointed to fill a casual vacancy, retired at the meeting, stood for election, and was elected as an Independent Director. Three candidates were put forward for two non-independent Director vacancies on the Board. Mr Simon Mackenzie, who retired at the meeting in accordance with the rotation provisions of the constitution, did not stand for re-election. Mr David Baldwin, who also retired by rotation, stood for re-election as a non-independent Director, and was re-elected. Mr Ron Kelly was elected as a non-independent Director.

In his address to the meeting, the Chair referred to the numerous issues addressed by Gas Industry Co during the year, including transmission pipeline balancing, capacity on the North Pipeline, the wholesale gas market trial and monitoring a breach of the downstream reconciliation rules by a retailer, E-Gas, that subsequently went into liquidation. He also signalled that the Company would be making a refund to industry participants of levy over-recoveries.

Delegations

The Board delegates to the Chief Executive the right to exercise all the financial powers of the Board in relation to the operation of Gas Industry Co in accordance with Board policies and directives, as well as defined financial delegations for business operations. The Board reserves to itself certain powers, including the approval of strategic and business plans, budgets, accounting policies and other financial matters, and transactions or contracts over specified thresholds.

Executive

Gas Industry Co has a small Senior Management Team that leads a total staff of 16 employees to deliver on the Company's Strategic Plan and strategy.

STEVE BIELBY, BA LLB (Hons) LLM (Lond)

CHIEF EXECUTIVE

Steve Bielby commenced as Gas Industry Co's Chief Executive in January 2011. Prior to that he held executive positions in several New Zealand energy companies over more than 10 years and spanning most parts of the energy sector. Mr Bielby has followed the development of Gas Industry Co since its inception. He began his career as a lawyer and was a partner in a leading national law firm.

IAN DEMPSTER, BE (Hons) M Comm (Hons)

GENERAL MANAGER OPERATIONS

Ian Dempster, a foundation member of the Gas Industry Co's Executive since 2005, leads the Operations Group, a team of advisers with responsibilities for access and operation of gas pipelines, switching, downstream reconciliation, the wholesale market, critical contingency management, and compliance and enforcement.

Mr Dempster was previously a consultant for network industries including water, gas, ports and telecommunications. His energy sector experience also includes corporate finance and mergers, acquisitions and divestments arising from legislation-driven industry restructuring. He has a background in electricity generation planning.

GREIG HINDS, BA LLB Post Grad Cert in Commerce (Lincoln)

PRINCIPAL LEGAL COUNSEL

Greig Hinds leads the Corporate Services Group, which is responsible for providing legal, financial and administrative support, including human resources, IT and property management. Mr Hinds joined Gas Industry Co as Legal Adviser (Corporate) in 2009, having previously worked in New Zealand, Hong Kong, and Canada in various professional roles in the energy sector and in university administration. He also performs the role of Company Secretary.

Employee Remuneration and Benefits

Employees receiving remuneration and related benefits over $100,000 per annum:

	YEAR ENDED 30 JUNE 2011
$100,001 – $110,000	1
$110,001 – $120,000	4
$140,001 – $150,000	1
$160,001 – $170,000	1
$220,001 – $230,000	1
$240,001 – $250,000	1
$250,001 – $260,000	1

The remuneration and benefits received by the former Chief Executive are in the $100,001 – $110,000 band, and reflect an end date of 30 September 2010.

The remuneration and benefits received by the current Chief Executive are in the $160,001 – $170,000 band, and reflect a start date of 17 January 2011.

During the financial year, a total of $42,500 was paid to one employee by way of redundancy compensation.

Business Governance and Corporate Responsibility

Gas Industry Co maintains a comprehensive suite of policies and procedures to govern standards, behaviour and employee wellbeing. These include:

Conflicts of Interest

Employees must inform the Company in writing where they enter into any business arrangement or have personal interests that may conflict with either the Company's business or affect the full, effective, and impartial discharge of the employee's obligations with the Company, as the industry body and co-regulator.

Gifts and Hospitality

Gas Industry Co requires that its employees do not solicit, accept or offer money, gifts, favours, or entertainment that might influence, or appear to influence, their business judgment, particularly given the Company's role as the industry body and co-regulator.

Health and Safety

The Company is committed to providing and maintaining a safe and healthy work environment for employees and visitors to its premises.

Information Confidentiality

While Gas Industry Co receives information from industry participants that should be used in an open, accessible, and transparent manner, this policy includes provisions for information that may be treated as commercially sensitive in some cases.

Insider Trading

Employees are informed of their responsibilities should they become aware of inside information about publicly listed companies, including trading in the securities of industry participants that are publicly listed. Employees are also restricted in terms of ownership of shares of industry participants.

Remuneration and Performance Review

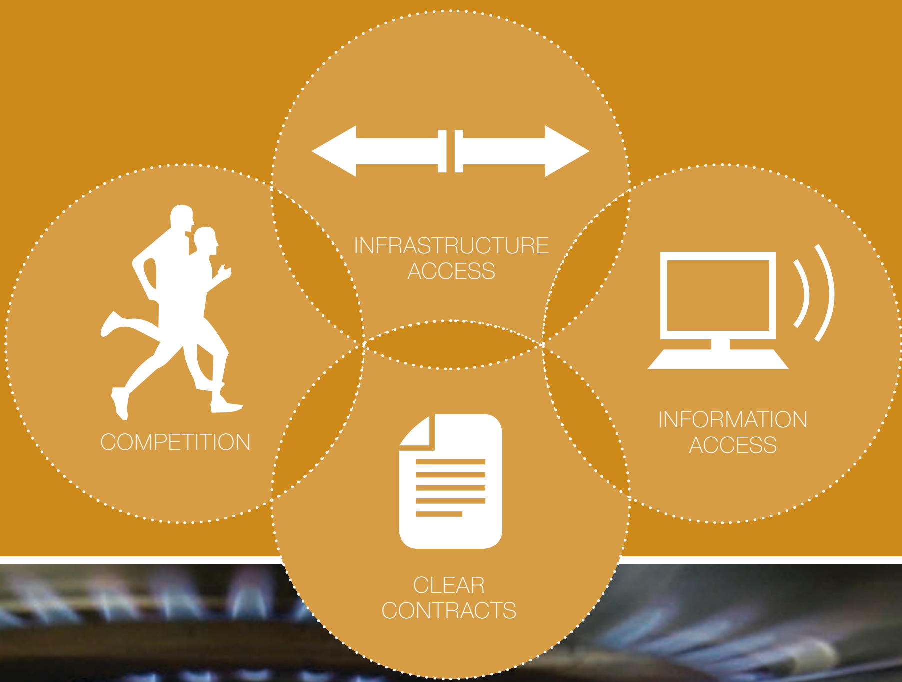
The Company is committed to providing its employees with fair and appropriate remuneration relative to the market rate for each position. Employee remuneration is reviewed annually, with any movements reflecting the results of individual performance reviews.

Risk Management

Gas Industry Co operates a risk register to record and mitigate strategic, operational, and physical risks that could affect its business. The Company maintains business continuity and emergency preparedness plans.

OPTIMISING GAS IN NEW ZEALAND.

EFFICIENT MARKETS



CHAPTER 8.

FINANCIAL STATEMENTS

DIRECTORS' REPORT

The Board of Directors have pleasure in presenting the Annual Report of Gas Industry Company Limited, incorporating the financial statements and the auditors' report, for the year ended 30 June 2011.

The Board of Directors of the Company authorised the financial statements presented on pages 36 to 55 for issue on 25 August 2011.

For and on behalf of the Board.

Rt Hon James B Bolger, ONZ
CHAIR
15 September 2011

Robin G Hill
DEPUTY CHAIR
15 September 2011

AUDITORS' REPORT

To the Shareholders of Gas Industry Company Limited

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of Gas Industry Company Limited ("the company") on pages 36 to 55. The financial statements comprise the statement of financial position as at 30 June 2011, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors are responsible for the preparation of financial statements in accordance with generally accepted accounting practice in New Zealand that give a true and fair view of the matters to which they relate, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation of the financial statements that give a true and fair view of the matters to which they relate in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Other than in our capacity as auditors we have no relationship with, or interests in, the company.

OPINION

In our opinion the financial statements on pages 36 to 55:

» comply with generally accepted accounting practice in New Zealand;

» give a true and fair view of the financial position of the company as at 30 June 2011 and of its financial performance and cash flows for the year then ended.

OTHER MATTER

The financial statements of Gas Industry Company Limited, for the year ended 30 June 2010, were audited by another auditor who expressed an unmodified opinion on those statements on 21 September 2010.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

In accordance with the requirements of sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993, we report that:

» we have obtained all the information and explanations that we have required; and

» in our opinion, proper accounting records have been kept by Gas Industry Company Limited as far as appears from our examination of those records.

KPMG

Wellington

25 August 2011

STATEMENT

OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2011

	NOTES	ACTUAL 2011 $	BUDGET 2011 $	ACTUAL 2010 $
INCOME				
Operating income	4	5,971,489	6,535,400	7,339,924
Interest income		53,029	27,645	43,277
		6,024,518	6,563,045	7,383,201
Refunded levy income	4	(1,501,829)	–	–
NET INCOME		4,522,689	6,563,045	7,383,201
EXPENDITURE				
Operating expenditure	5	5,998,908	7,029,809	6,288,704
Finance costs	12	2,631	–	2,352
		6,001,539	7,029,809	6,291,056
PROFIT/(LOSS) BEFORE TAX		(1,478,850)	(466,764)	1,092,145
Income tax expense	6	14,848	8,000	12,983
PROFIT/(LOSS) FOR THE YEAR		(1,493,698)	(474,764)	1,079,162
Other comprehensive income		–	–	–
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		(1,493,698)	(474,764)	1,079,162

The accompanying notes form an integral part of these financial statements

STATEMENT
OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2011

	INDUSTRY RESERVES $	RETAINED EARNINGS $	TOTAL EQUITY $	BUDGET $
BALANCE AT 1 JULY 2009	2,166,386	190,000	2,356,386	2,346,490
TOTAL COMPREHENSIVE INCOME FOR THE YEAR				
Profit/(loss) for the year	–	1,079,162	1,079,162	(193,955)
Other comprehensive income	–	–	–	–
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**–**	**1,079,162**	**1,079,162**	**(193,955)**
TRANSFER BETWEEN EQUITY RESERVES				
Industry Advances Reserve transfers	1,362,976	(1,362,976)	–	–
Industry Asset Amortisation Reserve transfers	(363,814)	363,814	–	–
BALANCE AT 30 JUNE 2010	**3,165,548**	**270,000**	**3,435,548**	**2,152,535**
BALANCE AT 1 JULY 2010	3,165,548	270,000	3,435,548	2,152,535
TOTAL COMPREHENSIVE INCOME FOR THE YEAR				
Profit/(loss) for the year	–	(1,493,698)	(1,493,698)	(474,764)
Other comprehensive income	–	–	–	
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**–**	**(1,493,698)**	**(1,493,698)**	**(474,764)**
Industry Advances Reserve transfers	(1,209,884)	1,209,884	–	–
Industry Asset Amortisation Reserve transfers	(363,814)	363,814	–	–
BALANCE AT 30 JUNE 2011	**1,591,850**	**350,000**	**1,941,850**	**1,677,771**

STATEMENT

OF FINANCIAL POSITION

AS AT 30 JUNE 2011

	NOTES	ACTUAL 2011 $	BUDGET 2011 $	ACTUAL 2010 $
ASSETS				
Current assets				
Cash and cash equivalents	7	1,238,985	2,189,884	2,259,887
Trade and other receivables	8	157,595	90,372	186,871
Prepayments		47,234	26,795	38,275
Income tax receivable	6	872	–	611
TOTAL CURRENT ASSETS		**1,444,686**	**2,307,051**	**2,485,644**
Non-current assets				
Property, plant and equipment	10	135,017	177,118	171,172
Intangible Assets	11	1,239,052	1,227,661	1,667,677
TOTAL NON-CURRENT ASSETS		**1,374,069**	**1,404,779**	**1,838,849**
TOTAL ASSETS		**2,818,755**	**3,711,830**	**4,324,493**
LIABILITIES				
Current liabilities				
Trade and other payables	9	643,100	545,278	649,696
Asset restoration provision	12	25,017	31,869	22,386
Employee entitlements		208,780	211,832	216,855
Income in advance		-	-	-
Redeemable shares	14	8	8	8
TOTAL CURRENT LIABILITIES		**876,905**	**788,987**	**888,945**
TOTAL LIABILITIES		**876,905**	**788,987**	**888,945**
EQUITY				
Industry Reserves	15	1,591,850	2,572,843	3,165,548
Retained Earnings	15	350,000	350,000	270,000
TOTAL EQUITY		**1,941,850**	**2,922,843**	**3,435,548**

These financial statements were authorised for issue by the signatories below on 25 August 2011:

On behalf of the Board:

Rt Hon James B Bolger, ONZ
CHAIR
25 August 2011

Robin G Hill
DEPUTY CHAIR
25 August 2011

The accompanying notes form an integral part of these financial statements

STATEMENT
OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2011

	ACTUAL 2011 $	BUDGET 2011 $	ACTUAL 2010 $
OPERATING ACTIVITIES			
Cash was provided from			
Levy revenue	4,454,855	4,300,000	4,538,105
Market fee revenue	1,412,153	2,155,400	2,910,877
Annual fees	80,000	80,000	80,000
Interest received	53,029	27,645	43,277
	6,000,037	6,563,045	7,572,259
Cash was applied to			
Payments to suppliers	(3,173,384)	(4,564,196)	(3,666,619)
Payments to employees	(2,105,513)	(2,094,430)	(2,081,894)
Payments to directors	(253,238)	(262,460)	(275,468)
Refund of levy to industry participants	(1,441,338)	–	–
Taxes paid	(15,720)	–	(12,025)
Net GST	(21,093)	–	(5,535)
	(7,010,286)	(6,921,086)	(6,041,541)
NET CASH INFLOWS FROM OPERATING ACTIVITIES	(1,010,249)	(358,041)	1,530,718
INVESTING ACTIVITIES			
Cash was applied to			
Purchase of property, plant and equipment	(10,653)	–	(17,278)
Purchase of intangible assets	–	–	–
NET CASH OUTFLOWS FROM INVESTING ACTIVITIES	(10,653)	–	(17,278)
Net increase/(decease) in cash and cash equivalents	(1,020,902)	(358,041)	1,513,440
OPENING CASH AND CASH EQUIVALENTS	2,259,887	2,547,925	746,447
CLOSING CASH AND CASH EQUIVALENTS	1,238,985	2,189,884	2,259,887

The accompanying notes form an integral part of these financial statements

NOTES

TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2011

1. Reporting Entity

These financial statements comprise the financial statements of the Gas Industry Company Limited (the "Company") for the year ended 30 June 2011.

Changes to the Gas Act 1992 (the "Act") in late 2004 provided for the co-regulation of the gas industry by the Government and an industry body. The Company was established to fulfil the role of the industry body under the Act and was approved by Order in Council on 22 December 2004.

The Company is a limited liability company incorporated and domiciled in New Zealand and is registered under the Companies Act 2003. The address of its registered office is 95 Customhouse Quay, Wellington.

The financial statements have been prepared in accordance with the requirements of the Gas Act 1992, the Financial Reporting Act 1993 and the Companies Act 1993.

The principal activity of the Company is to act as a co-regulatory body for the gas industry in New Zealand. This includes making recommendations to the Minister of Energy on a wide range of industry matters, including the making of rules and regulations in relation to the wholesaling, processing, transmission, distribution and retailing of gas.

The financial statements have been approved for issue by the Board of Directors on 25 August 2011.

2. Basis of preparation

(a) Statement of compliance

The financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP). They comply with the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards, as appropriate for public benefit entities.

(b) Basis of measurement

The financial statements have been prepared on a historical costs basis, except for financial assets and liabilities that have been measured at fair value. The accrual basis of accounting has been used unless otherwise stated and the financial statements have been prepared on a going concern basis.

(c) Presentation currency

The financial statements are presented in New Zealand dollars ($), which is the Company's functional currency.

(d) Comparatives

The comparative financial period is 12 months. Comparatives have been reclassified from that reported in the 30 June 2010 financial statements where appropriate to ensure consistency with the presentation of the current year's financial position, performance and cash flows.

(e) Budget figures

The budget figures are approved by the Board of Directors in line with Company's strategic plans. The budget figures have been prepared in accordance with NZ GAAP, using accounting policies that are consistent with those used in preparing these financial statements.

(f) Judgments and estimations

The preparation of financial statements in conformity with NZ IFRS requires judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. Where material, information on significant assumptions and estimates is provided in the relevant accounting policy or will be provided in the relevant note.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Subsequent actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimates is revised and in any future years affected.

(g) Changes in accounting policy and disclosures

The accounting policies adopted are consistent with those of the previous financial year.

(h) New NZ IFRS standards and interpretations not yet adopted

At the date of authorisation of these financial statements, the following new standards and interpretations to existing standards have been published but are not yet effective, and have not been adopted early by the Company.

NZ IFRS 9 Financial Instruments is effective for periods beginning on or after 1 January 2013 and relates to the classification and measurement of financial instruments.

Management anticipates that all pronouncements will be adopted by the Company for the first year beginning after the effective date of the pronouncement. The new standards and interpretations issued are not expected to have a material impact on the Company's financial statements, given the nature of its operations and financial instruments held.

3. Summary of significant accounting policies

(a) Cash and cash equivalents

Cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

(b) Trade debtors and other receivables

Trade debtors and other receivables are measured at amortised cost using the effective interest method less any impairment losses.

A provision for impairment is established where there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivable.

Receivables with a short duration are not discounted.

(c) Property, plant and equipment

All property, plant and equipment is stated at historical cost less depreciation and impairment. Historical cost includes expenditure that is directly attributable to the acquisition of the items and an estimate of any asset restoration obligations.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the profit/(loss) in the Statement of Comprehensive Income in the year in which the expense is incurred.

Depreciation is calculated on the straight-line basis to write-off the cost of the assets to their residual values over their estimated useful lives as follows:

	ESTIMATED USEFUL LIFE
Leasehold improvements	Amortised over period of lease
Furniture and office equipment	4 to 10 years
Computer equipment	4 years

The residual value of property, plant and equipment is reassessed annually.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount of the asset. These are included in the Statement of Comprehensive Income.

(d) Intangible assets

Intangible assets acquired by the Company, which have finite useful life, are measured at cost less accumulated amortisation and accumulated impairment losses. Amortisation is recognised in the Statement of Comprehensive Income on a straight-line basis over the estimated useful life of the asset.

Software costs, which include those items classified as "Industry Assets" have a finite useful life. Software costs are capitalised and amortised over an economic useful life of between 4 and 6 years.

"Industry Assets" relate to the databases created and established for the Downstream Reconciliation and Switching & Registry rules

Costs associated with developing or maintaining software programmes are recognised as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the Company, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include the costs of software development employees and an appropriate portion of relevant overheads.

(e) Financial instruments

Financial instruments are comprised of trade debtors and other receivables, cash and cash equivalents, and trade creditors and other payables. The Company does not hold or issue derivative financial instruments (i.e. hedging instruments).

The Company has no off-balance sheet financial instruments.

RECOGNITION AND DE-RECOGNITION OF FINANCIAL ASSETS AND LIABILITIES

Financial assets and financial liabilities are recognised when the Company becomes a party to the contractual provisions of the financial instrument.

Financial assets are derecognised when the contractual rights to the cash flows from the financial asset expire, or when the financial asset and all substantial risks and rewards are transferred.

A financial liability is derecognised when it is extinguished, discharged, cancelled or expires.

Financial assets and financial liabilities are measured initially at fair value plus transaction costs, except for those carried at fair value through profit or loss, which are measured at fair value. Fair value is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date for similar financial instruments of similar maturity and credit risk.

SUBSEQUENT MEASUREMENT OF FINANCIAL ASSETS

All financial assets of the Company are classified as loans and receivables. Loans and receivables are non derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for those with maturities greater than 12 months after the balance sheet date which are classified as non-current assets. Loans and receivables are initially recognised at fair value plus transaction costs. Loans and receivables are carried at amortised cost using the effective interest method.

IMPAIRMENT OF FINANCIAL ASSETS

All financial assets are subject to review for impairment at least once each reporting year. Accounts receivable are reviewed for impairment when accounts are past due or when other objective evidence is received that a specific counterparty will default. Impairment of trade receivables are presented in the Statement of Comprehensive Income, within expenses.

SUBSEQUENT MEASUREMENT OF FINANCIAL LIABILITIES

Trade payables and other payables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest method.

(f) Impairment of non financial assets

Property, plant and equipment and other non-current assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the greater of an asset's net selling price and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identified cash flows. Where the company would, if deprived of the asset, replace its remaining future benefits, value in use is determined as the depreciated replacement cost.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indicators exist, the Company estimates the asset's recoverable amount, to measure the reversal of any previous period impairment charges. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Reversals of impairment are recognised in the Statement of Comprehensive Income.

(g) Trade creditors and other payables

These amounts represent liabilities for goods and services provided to the Company prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

(h) Provisions

A provision is recognised when the Company has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market rates and, where appropriate, the risks specific to the liability. Provisions are not recognised for future operating losses.

A provision for onerous contracts is recognised when the expected benefits from the contract are lower than the unavoidable costs of meeting contract obligations.

(i) Employee entitlements

SHORT TERM BENEFITS

Employee benefits that the Company expects to be settled within 12 months of balance date are measured at nominal value based on accrued entitlements at current rates of pay.

These include salaries and wages accrued up to balance date, annual leave earned, but not yet taken at balance date, and sick leave.

The Company recognises a liability for sick leave. The amount is calculated based on the unused sick leave entitlements that can be carried forward at balance date, to the extent that the Company anticipates that it will be used by staff to cover those future absences.

The Company recognises a liability and expense for bonuses where they are contractually obliged or where there is a past practice that has created a constructive obligation.

LONG-TERM BENEFITS

The Company does not provide long service leave to employees or members of the governing body and has not entered into any defined benefit/contribution pension plans.

(j) Preference shares

Preference share capital (disclosed as "Redeemable Shares") are classified as a liability if it is redeemable on a specific date or at the option of the shareholders.

(k) Revenue

Revenue is recognised to the extent that it is probable that the economic benefit will flow to the Company and the revenue can be reliably measured. Revenue is measured at the fair value of consideration received. The Company assesses its revenue arrangements against specific criteria to determine if it is acting as the principal or agent in a revenue transaction. In an agency relationship only the portion of revenue earned on the Company's own account is recognised as gross revenue in the Statement of Comprehensive Income.

The following specific recognition criteria must be met before revenue is recognised:

LEVY REVENUE

Levy revenue comprises amounts received or due in accordance with the applicable Gas (Levy of Industry Participants) Regulations. Levy revenue is recognised when the underlying activities upon which the levy is raised have occurred and the amount of levy revenue can be reliably measured.

MARKET FEE REVENUE

Market fees raised to recoup the capital and operating costs of implementing gas governance regulations are recognised in conformance with International Public Sector Board standard 23: Non-reciprocal transfers in the following manner:

» Market fees to recoup operating costs to be recognised as revenue at the time the invoice is raised as a proxy for recognising it at the time the leviable event occurs.
» Market fees to recover capital costs to be recognised as revenue once the expenditure the fees were raised to cover has been incurred.

ANNUAL FEES

Annual fees are recognised when invoiced.

INTEREST INCOME

Interest income is recognised as it accrues, using the effective interest method.

(l) Operating leases

Leases of assets under which all the risks and benefits of ownership are effectively retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the Statement of Comprehensive Income on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

(m) Foreign currency translations

Transactions in foreign currencies that are settled in the accounting period are translated at the settlement rate. Transactions in foreign currencies that are not settled in the accounting period, resulting in monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to NZD at the foreign exchange rate ruling at that date. Foreign exchange differences arising on their translation are recognised in the Statement of Comprehensive Income.

(n) Income tax

Taxation expense in the Statement of Comprehensive Income comprises current tax charges. Industry participation levies, annual fees and market fees received are not regarded as gross income, in terms of section CB 1 of the Income Tax Act 2007 and therefore are not taxable. Deductions are not available in respect of the costs incurred in providing services.
Current tax charges are based on taxable profits for the year, which differ from the profit before tax reported because it excludes items that are taxable or deductible in other years, and items that are never taxable or deductible.

The Company has no material deferred tax balances as the majority of assets and liabilities are used to provide non-taxable activities.

(o) Goods and Services Tax (GST)

All amounts are shown exclusive of Goods and Services Tax (GST), except for receivables and payables that are stated inclusive of GST.

The net amount of GST recoverable from, or payable to, the Inland Revenue Department (IRD) is included as part of receivables or payables in the Statement of Financial Position.

(p) Statement of cash flows

The following are the definitions of the terms used in the Cash Flow Statement:

» Operating activities include all transactions and other events that are not investing or financing activities.

» Investing activities are those activities relating to the acquisition, holding and disposal of investments. Investments can include securities not falling within the definition of cash.

» Financing activities are those activities that result in changes in the size and composition of the capital structure. This includes both equity and debt not falling within the definition of cash. Dividends paid in relation to the capital structure are included in financing activities.

(q) Reserves/Equity Policy

The Board holds surplus levy income in a dedicated industry advance reserve for the future reduction of levy income.

4. Operating Income

	ACTUAL 2011 $	ACTUAL 2010 $
Wholesale levy revenue	2,807,446	2,862,998
Retail levy revenue	1,663,395	1,649,662
Market fee revenue	1,420,648	2,747,264
Annual fees	80,000	80,000
TOTAL OPERATING INCOME	**5,971,489**	**7,339,924**
Refunded levy income	(1,501,829)	–

During the financial year a decision was made to refund back to the industry participants, over collected levy revenues.

5. Operating expenditure

	ACTUAL 2011 $	ACTUAL 2010 $
Depreciation & Amortisation	433,229	423,294
Operating lease expenses	311,691	317,349
Fees paid to audit firm - financial statement audit	13,800	9,900
Fees paid to audit firm - other services	–	–
Accounting and taxation advice	–	–
Directors' fees	262,460	244,860
General expenses	482,952	472,364
Bad Debts	74,527	–
Recruitment expenses	81,700	60,337
Technical, economic, and legal advice	652,323	1,249,234
Service Provider Fees	1,645,033	1,429,993
Kiwisaver contributions	39,756	42,370
Foreign exchange loss	1,923	1,797
Employee benefit expense	1,999,514	2,037,206
TOTAL OPERATING EXPENDITURE	**5,998,908**	**6,288,704**

6. Income tax

	ACTUAL 2011 $	ACTUAL 2010 $
(A) INCOME TAX EXPENSE		
Current year income tax expense	14,848	12,983
Deferred tax movement	–	–
TOTAL INCOME TAX EXPENSE	**14,848**	**12,983**
(B) RECONCILIATION OF CURRENT YEAR INCOME TAX EXPENSE		
Profit before tax	(1,493,698)	1,092,145
Income tax expense at 28 percent (2010: 30%)	(418,235)	327,643
Permanent differences	433,083	(314,660)
Timing differences	–	–
CURRENT YEAR INCOME TAX EXPENSE	**14,848**	**12,983**
(C) INCOME TAX RECEIVABLE		
Opening balance	611	1,569
Tax refunds received	(611)	(1,569)
Current year income tax expense	(14,848)	(12,983)
Income tax paid	15,720	13,594
CLOSING BALANCE	**872**	**611**

The Company has no material deferred tax balances on temporary or permanent timing differences.

7. Cash and cash equivalents

	ACTUAL 2011 $	ACTUAL 2010 $
Bank Account	38,485	259,387
Money Market Account	1,200,000	2,000,000
Petty Cash	500	500
TOTAL	**1,238,985**	**2,259,887**

The carrying amount of cash and cash equivalents approximates their fair value.

Cash at bank and the money market account earns interest at floating rates based on daily deposit balances.

8. Trade and other receivables

	ACTUAL 2011 $	ACTUAL 2010 $
Levy debtors	95,718	154,171
Other Receivables	61,877	32,700
TOTAL	**157,595**	**186,871**

Trade debtors and other receivables are non-interest bearing and receipt is normally on 30-day terms. Therefore, the carrying value of trade debtors and other receivables approximates their fair value.

As at 30 June 2011, all overdue receivables have been assessed for impairment and appropriate allowances applied. All trade receivables are subject to credit risk exposure.

The ageing profile of receivables at year-end is detailed below:

0-30 days	95,718	5,904
31-60 days	–	13,768
61-90 days	–	9,556
> 91 days	–	124,943
Total	95,718	154,171

No provision for doubtful debts has been required because all significant receivable balances have been subsequently receipted after the reporting date and before authorisation of the financial statements for release.

9. Trade and other payables

	ACTUAL 2011 $	ACTUAL 2010 $
Accounts payable	315,784	322,344
Accrued expenses	319,870	320,196
GST Payable	7,446	7,156
TOTAL	**643,100**	**649,696**

Trade creditors and other payables are non-interest bearing and are normally settled on 30-day terms; therefore the carrying value of trade creditors and other payables approximates their fair value.

10. Property, plant and equipment

	LEASEHOLD IMPROVEMENTS $	FURNITURE AND OFFICE EQUIPMENT $	COMPUTER EQUIPMENT $	TOTAL $
COST				
Balance at 1 July 2009	113,837	145,736	41,859	301,432
Additions	1,756	7,359	6,747	15,862
Transfers	–	–	–	–
Disposals	–	–	–	–
BALANCE AT 30 JUNE 2010	115,593	153,095	48,606	317,294
Balance at 1 July 2010	115,593	153,095	48,606	317,294
Additions	–	7,911	1,672	9,583
Transfers	–	–	–	–
Disposals	–	(3,758)	(1,932)	(5,690)
BALANCE AT 30 JUNE 2011	115,593	157,248	48,346	321,187
ACCUMULATED DEPRECIATION AND IMPAIRMENT LOSSES				
Balance at 1 July 2009	5,701	67,101	27,920	100,722
Depreciation expense	12,744	25,483	7,173	45,400
Disposals	–	–	–	–
Impairment losses	–	–	–	–
BALANCE AT 30 JUNE 2010	18,445	92,584	35,093	146,122
Balance at 1 July 2010	18,445	92,584	35,093	146,122
Depreciation expense	12,842	26,022	6,297	45,161
Disposals	–	(3,489)	(1,624)	(5,113)
Impairment losses	–	–	–	–
BALANCE AT 30 JUNE 2011	31,287	115,117	39,766	186,170
NET BOOK VALUE	84,306	42,131	8,580	135,017

11. Intangible Assets

	SOFTWARE $	INDUSTRY ASSETS $	CONSTRUCTION IN PROGRESS $	TOTAL $
COST				
Balance at 1 July 2009	51,472	2,182,448	54,000	2,287,920
Additions	59,942	–	–	59,942
Transfers	–	–	–	–
Disposals	–	–	(54,000)	(54,000)
BALANCE AT 30 JUNE 2010	**111,414**	**2,182,448**	**–**	**2,293,862**
Balance at 1 July 2010	111,414	2,182,448	–	2,293,862
Additions	1,069	–	–	1,069
Transfers	–	–	–	–
Disposals	(57,750)	–	–	(57,750)
BALANCE AT 30 JUNE 2011	54,733	2,182,448	–	2,237,181
ACCUMULATED AMORTISATION AND IMPAIRMENT LOSSES				
Balance at 1 July 2009	21,133	227,158	–	248,291
Amortisation expense	14,080	363,814	–	377,894
Disposals	–	–	–	–
Impairment losses	–	–	–	–
BALANCE AT 30 JUNE 2010	35,213	590,972	–	626,185
Balance at 1 July 2010	35,213	590,972	–	626,185
Amortisation expense	24,254	363,814	–	388,068
Disposals	(16,124)	–	–	(16,124)
Impairment losses	–	–	–	–
BALANCE AT 30 JUNE 2011	43,343	954,786	–	998,129
NET BOOK VALUE	**11,390**	**1,227,662**	**–**	**1,239,052**

12. Asset restoration provision

	ACTUAL 2011 $	ACTUAL 2010 $
GROSS BALANCE OF PROVISION		
Opening	51,571	64,571
Additions	–	–
Disposals	–	(13,000)
CLOSING GROSS PROVISION	**51,571**	**51,571**
DISCOUNT FOR TIME VALUE OF MONEY		
Opening	29,185	31,537
Additions	–	–
Movement due to change in discount rate	–	–
Unwinding of discount	2,631	2,352
CLOSING DISCOUNT	**26,554**	**29,185**
PROVISION NET CARRYING AMOUNT	**25,017**	**22,386**

The asset restoration provision relates to the make good clauses in the lease of the Company's premises. The provision has been accreted to account for the discounting and will be released when the expenditure occurs.

13. Related party transactions

(a) Transactions with shareholders

Levy payments (which are detailed in note 4) are made by industry participants who, in many cases, are also shareholders of Gas Industry Co.

(b) Transactions with key management personnel

	ACTUAL 2011 $	ACTUAL 2010 $
SALARIES AND OTHER SHORT-TERM EMPLOYEE BENEFITS	**1,214,239**	**1,035,010**

Key management personnel include the Chief Executive and his direct reports.

(c) Termination Benefits

During the financial year, a total of $42,500 was paid to one employee by way of redundancy compensation.

14. Redeemable shares

	ACTUAL 2011 $	ACTUAL 2010 $
Redeemable shares – Value in dollars	8	8
Redeemable shares – Number	8	8

All redeemable shares rank equally with one vote attached to each fully paid share. The shares are redeemable at any time for the consideration of $1 payable on redemption. The redeemable shares confer on the shareholders the rights set out in section 36(1) of the Companies Act 1993.

15. Reserves and retained earnings

	ACTUAL 2011 $	ACTUAL 2010 $
Industry advances reserve	364,188	1,574,072
Industry asset amortisation reserve	1,227,662	1,591,476
Retained earnings	350,000	270,000
TOTAL EQUITY RESERVES	**1,941,850**	**3,435,548**

(a) Industry advances reserve

	ACTUAL 2011 $	ACTUAL 2010 $
Opening balance	1,574,072	211,096
Transfer from retained earnings	(1,209,884)	1,362,976
CLOSING BALANCE	**364,188**	**1,574,072**

To allow for the timely enactment of the levy regulations each financial year, Gas Industry Co must set its budget and work programme nine months prior to the beginning of that year and prior to the completion of the Strategic Plan. In practice, this requires the Company to forecast where it expects to be in the policy development process before it has fully analysed the issues, or engaged with stakeholders on their concerns. This factor, and the fact that the levy is based in part on variable gas sales volumes, means every year there is a risk of over or under recovery of levy funds.

The Board holds surplus levy income in a dedicated industry advance reserve prior to any decision on its application (either being refunded or held for ongoing expenditure). Section 43ZZC(3) of the Gas Act provides that any over or under recoveries can be taken into account in setting the levy in subsequent financial years. However, to ensure transparency around the calculation of each year's levy, the Board has determined that, unless required for unanticipated, ongoing work programme costs, any surplus should be returned to levy payers by way of refund once the year-end accounts have been received by shareholders at the Annual General Meeting.

(b) Industry asset amortisation reserve

	ACTUAL 2011 $	ACTUAL 2010 $
Opening balance	1,591,476	1,955,290
Transfer from retained earnings	(363,814)	(363,814)
CLOSING BALANCE	**1,227,662**	**1,591,476**

The industry asset amortisation reserve represents capital items purchased with Market Fees recognised as an asset and amortised over their economic life. Its value is equal to the unexpired amortisation balances of the industry assets.

c) Retained earnings

	ACTUAL 2011 $	ACTUAL 2010 $
Opening balance	270,000	190,000
Profit for the year	(1,493,698)	1,079,162
Transfer to Industry advances reserve	1,209,884	(1,362,976)
Transfer to Industry asset amortisation reserve	363,814	363,814
CLOSING BALANCE	**350,000**	**270,000**

16. Contingencies

As at 30 June 2011, the Company has no contingent liabilities (2010: nil). There is an arrangement with Westpac Banking Corporation Limited whereby Gas Industry Company has a facility (limit $100,000) and a payroll Letter of Credit facility (limit $180,000).

17. Commitments

(a) Capital commitments

The Company has no material capital commitments (2010: nil)

(b) Operating lease commitments

	ACTUAL 2011 $	ACTUAL 2010 $
Commitments for minimum lease payments in relation to non-cancellable operating leases are payable as follows:		
Within one year	280,940	310,972
Later than one year but not later than five years	1,343,966	1,356,130
Later than five years	111,990	380,765
TOTAL	**1,736,896**	**2,047,867**

(c) Service provider commitments

	ACTUAL 2011 $	ACTUAL 2010 $
Service provider agreements for the Downstream Reconciliation, Switching and Registry and Critical Contingency Management Rules payable as follows:		
Within one year	1,351,709	920,408
Later than one year but not later than five years	2,222,414	2,171,088
Later than five years	–	–
TOTAL	**3,574,123**	**3,091,496**

18. Financial risk management

The Company's activities expose it to a variety of financial risks: currency risk, interest rate risk, credit risk and liquidity risk.

To manage and limit the effects of those financial risks, the Board of Directors has approved policy guidelines. The policies approved at balance date are outlined below:

Currency risk

During the normal course of business the Company contracts overseas consultants to provide services which are denominated in foreign currencies. The currency risk attached to these contracts (which are normally denominated in Australian dollars) is not actively managed by the Company and there is a resultant risk that creditors due in foreign currency will fluctuate because of changes in foreign exchange rates. No significant monetary assets were denominated in foreign currencies at year-end.

Interest rate risk

The Company is exposed to interest rate risk through the return on any funds it has invested and the cost of borrowed funds which will fluctuate due to changes in market interest rates. All cash and cash equivalents are held on floating interest rates and all shareholder liabilities attract floating interest rates. The Company does not hold any significant interest bearing liabilities, and therefore is not subject to interest rate risk on borrowings.

Credit risk

Credit risk is the risk that a third party defaults on its obligation to the Company, causing the Company to incur losses. The Company has no significant concentration of credit risk in relation to accounts receivable. The Company does not expect the non-performance of any obligations at balance date. The carrying value of trade debtors, other receivables, cash and cash equivalents and short-term bank deposits represents the Company's maximum exposure to credit risk at balance date.

Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and the availability of funding through an adequate amount of committed credit facilities. Management hold sufficient liquid assets in the form of cash and cash equivalents to meet expected outflows. All trade payables are expected to be settled within 30 days.

Fair values

The fair value of all financial instruments is equivalent to the carrying amount disclosed in the Statement of Financial Position.

19. Reconciliation of profit to net cash inflows from operating activities

	ACTUAL 2011 $	ACTUAL 2010 $
Profit/ (loss) for the year	(1,493,698)	1,079,162
Non cash items		
Depreciation and amortisation expense	433,229	423,294
Unwind of discount factor on restoration provision	2,631	2,352
Impact of changes in working capital items		
Prepayments	(11,590)	(19,106)
Trade and Other Payables	10,375	107,738
Employee entitlements	(8,075)	24,895
Trade and Other Receivables	58,454	(75,836)
GST payable	290	(14,492)
Income tax receivable	(1,865)	2,711
NET CASH FLOWS FROM OPERATING ACTIVITIES	**(1,010,249)**	**1,530,718**

20. Capital management

The Company's capital is its total equity, being the net asset of the Company, represented by retained earnings and other equity reserves. The primary objective of the Company's capital management policy is to ensure working capital is maintained in order to support its activities. The Company manages its capital structure and makes adjustments to it, in light of changes to funding requirements. To maintain or adjust the capital structure, budgeted discretionary expenditure is reduced to avoid the need for external borrowings.

21. Subsequent events

No significant events, which would materially affect the financial statements, have occurred subsequent to year end that require disclosure or adjustment to the carrying value of assets or liabilities in this set of financial statements.

OPTIMISING GAS IN NEW ZEALAND.

INDUSTRY LEADERSHIP

CONFIDENT MARKETS

INVESTMENT PATHWAYS

NZ GAS STORY

GAS INDUSTRY COMPANY LIMITED

Level 8, The Todd Building
95 Customhouse Quay
PO Box 10 646
Wellington 6143

T: +64 4 472 1800

F: + 64 4 472 1801

E: info@gasindustry.co.nz

W: www.gasindustry.co.nz

PHOTO ACKNOWLEDGEMENTS

Contact Energy: Inside front cover, page 2, 9
Genesis Energy: Page 1, 56
Methanex: Inside front cover, page 3
Mighty River Power: Page 1, 24
Powerco: Inside front cover, page 1, 17, 32