Consultation on

Proposed Gas (Levy of Participants) Regulations 2010

Date issued: 23 December 2009
Submissions close: 5 February 2010

151679.9

About Gas Industry Co.

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

As such, its role is to:

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

Authorship

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Submissions close: 5 February 2010

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Executive summary

This consultation paper explains the development of the FY2011 levy, describes the work Gas Industry Co expects to undertake in FY2011 and its associated cost, calculates the levy funding requirement for that year, and proposes the FY2011 levy. In addition, some amendments to certain provisions of the levy regulations are proposed. Gas Industry Co is also seeking feedback from industry participants on suggested amendments to the Statement of Levy Principles for possible inclusion into the FY2012 levy.

In general, the work expected to be undertaken in FY2011 includes:

- Implementation of the policy recommendations on balancing, interconnection and capacity on transmission pipelines, retail contracts, and initial advice on arrangements for access to distribution networks. This effectively completes all anticipated recommendations for gas governance in the April 2008 GPS, although the Company will still be responsible for monitoring the effectiveness of the existing arrangements, which may result in further governance recommendations.

- Facilitating industry resolution of infrastructure access issues to avoid regulation where practical.

- Fulfilling the various roles set out for the Company under approved gas governance arrangements, and helping industry participants to comply with the new arrangements.

- Conducting the Wholesale Market Trial and providing advice to the Associate Minister on whether the platform should be established permanently.

- Reviewing the downstream reconciliation rules to improve the accuracy of the reconciliation process using data delivered during the transition period.

- Overseeing the industry complaints scheme and monitoring compliance with benchmark retail contract terms.

- Providing advice on sector issues and input into the MED’s industry performance review as required.

The work programme cost for FY2011 is $7,878,286. The FY2011 levy funding requirement is $5,075,300. The balance will be met through Market Fees ($2,155,400), and Gas Industry Co reserves ($211,096 from the Industry Advances Reserve and $436,490 from the Industry Asset Depreciation Reserve).

The proposed levies for FY2011 are:

- Retail levy of $8.20 per annum payable on each ICP. This is a 28% increase on the FY2010 rate of $6.40; and

- Wholesale levy of 2.13 cents per GJ of gas purchased directly from gas producers. This is a 28% increase on the FY2009 rate of 1.67 cents.

Submissions on the proposals in this discussion paper should be provided by **5.00pm on Friday, 5 February 2010**. Submissions can be made by registering on Gas Industry Co's website www.gasindustry.co.nz and uploading your submission, preferably in the form of the submissions template attached to the consultation document. All submissions will be published on this website after the closing date. Submissions may be amended up to closure date.

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1 Introduction

1.1 Background

Amendments to the Gas Act 1992 (the 'Act'), introduced in 2004, provided for the co-regulation of the gas industry by the Government and an industry body. Gas Industry Company Ltd (Gas Industry Co) was established by the gas industry to fulfil the role of the industry body, as set out in the Act. It was approved as the industry body by Order in Council on 22 December 2004. In March 2009, the warrant for administration of the Act was passed to the Associate Minister of Energy & Resources (Associate Minister).

Gas Industry Co is responsible for proposing arrangements, which may include rules and regulations, in a range of areas relating to the gas industry, including wholesale markets and processing, transmission and distribution networks, and retail and consumer protection. Where appropriate, it is involved in the implementation of market arrangements, and in the surveillance and enforcement of market rules.

The principal source of funding for this work is through a levy on industry participants. Section 43ZZB of the Act enables Gas Industry Co to recommend to the Associate Minister that levy regulations be made requiring industry participants to pay a levy to it. The levy is to recover the estimated costs of the Company exercising its functions as the industry body under Section 43ZZC of the Act.

The proposed amount and structure of this levy are based on Gas Industry Co's work programme, including its statutory roles, and budget.

1.2 Levy process

The timing of the levy-setting process is dictated by the requirement in the Act for the levy to be set through annual regulations. This requires it to be set before the work programme for the coming year has been finalised. For that reason, Gas Industry Co emphasises that the work programmes and budgets in this paper are indicative, and are provided only for the purposes of levy setting. Changes are possible before the start of FY2011.

1.3 Overall timetable

Table 1 presents the indicative timetable for the FY2011 levy process.

Table 1 FY2011 Levy timetable

Activity	Timing
Levy consultation paper released.	Wednesday, 23 December 2010
Levy workshop held for industry participants.	Tuesday, 26 January 2010
Closing date for submissions.	Friday, 5 February 2010
Report on submissions and proposed levy recommendation to Gas Industry Co Board for approval.	Board meeting Monday, 22 March 2010
Levy recommendation to the Minister.	Monday, 29 March 2010
Levy proposal confirmed by Cabinet.	April 2010
Levy regulations promulgated and take effect.	Thursday, 1 July 2010

1.4 Contents of consultation paper

This consultation paper:

- describes the work that Gas Industry Co intends to undertake in FY2011 and the associated estimate of costs
- outlines the calculation of the levy funding requirement for FY2011
- proposes the levy for FY2011
- suggests amendments to certain provisions of the levy regulations
- suggests amendments to the Statement of Levy Principles for consideration
- invites submissions on all of the above, as a precursor to formulating a recommendation to the Associate Minister of Energy and Resources for the required levy regulations.

2 Call for Submissions

Gas Industry Co invites submissions on the proposed annual levy and the associated issues set out in this paper. Specific matters on which submissions are sought are set out in each section of the paper, and a suggested format for submissions is set out in the template in Appendix A.

Submissions can be made by registering on Gas Industry Co's website www.gasindustry.co.nz and uploading your submission, preferably in the form of the submissions template attached to the consultation document. All submissions will be published on this website after the closing date. Submissions may be amended up to closure date.

Gas Industry Co will acknowledge receipt of all submissions electronically. Please contact Jay Jefferies (Ph: +64 4 472 1800 or email: jay.jefferies@gasindustry.co.nz) if you do not receive electronic acknowledgment of your submission within two business days.

The closing time for submissions is 5pm on Friday 5 February 2010. Please note that submissions received after this date may not be able to be considered.

Gas Industry Co values openness and transparency and therefore submissions will be made available to the public on Gas Industry Co's website. Submitters should discuss any intended provision of confidential information with Gas Industry Co prior to submitting the information.

To assist industry participants with submissions and to provide a prior indication of matters that will require consideration by Gas Industry Co, an industry workshop will be held at Gas Industry Co's office in Wellington, from 10am to 12 noon on Tuesday, 26 January 2010. If you plan to attend the workshop, please register on Gas Industry Co's website by 5pm on Monday 25 January 2010.

3 Work Programme

This indicative work programme and budget provides an outline of the Company's proposed scope of operations, milestones, and expenditure for FY2011. It has been prepared to support the Company's consultation on its proposed levy regulations for FY2011.

3.1 Strategic Priorities

In April 2008, the Government issued a new GPS with a list of outcomes that it wanted Gas Industry Co to pursue and report against. These amount to a statement of work priorities for the Company and form a key input to its work programming for FY2011.

The Company's Board has decided its strategic priorities for FY2011 and, in general, the work expected to be undertaken includes:

- Implementing the policy recommendations on balancing, interconnection, and capacity on transmission pipelines, retail contracts, and initial advice on arrangements for access to distribution networks. This effectively completes all anticipated recommendations for gas governance in the April 2008 GPS, although the Company will still be responsible for monitoring the effectiveness of the existing arrangements, which may result in further governance recommendations.

- Facilitating industry resolution of infrastructure access issues to avoid regulation where practical.

- Fulfilling the various roles set out for the Company under approved gas governance arrangements, and helping industry participants to comply with the new arrangements.

- Conducting the Wholesale Market Trial and providing advice to the Associate Minister on whether the platform should be established permanently.

- Reviewing the downstream reconciliation rules to improve the accuracy of the reconciliation process using data delivered during the transition period.

- Overseeing the industry complaints scheme and monitoring compliance with benchmark retail terms.

- Providing advice on sector issues and input into the MED's industry performance review as required.

A co-regulatory forum was held with industry participants on 5th October 2009 to discuss, amongst other things, the FY2011 strategic priorities and indicative work programme. In general, participants at the forum were supportive of the proposed work programme, although some had reservations about the level of corporate costs. This issue is discussed further in section 9. MED subsequently informed Gas Industry Co that the work programme seemed reasonable and was broadly in line with its expectations.

3.2 Infrastructure Access Group

The Infrastructure Access Group (IAG) is required to ensure that arrangements exist for market participants to access transmission and distribution pipeline networks and gas processing facilities under reasonable terms. IAG's approach involves facilitating industry agreement on access issues and, where necessary, recommending regulatory solutions.

Following industry feedback, Gas Industry Co has prioritised transmission pipeline access over distribution pipeline access. In FY2011, the Company intends to give priority to pipeline balancing, interconnection and access to short-term capacity on transmission pipelines. It will also continue a variety of industry-initiated activities including facilitating industry forums on contentious issues; commissioning expert reports; developing and issuing best practice guidelines; and performing its rule change roles under the Maui Pipeline Operating Code (MPOC), and the Vector Transmission Code (VTC). Rules providing for information disclosure about gas processing facilities have already been implemented.

The estimated cost for IAG activities in FY2011 is $1,063,227. This includes external consultancy costs of $588,325 but does not include governance or corporate costs, which are discussed separately below. In FY2010, the costs of IAG activities are expected to be $827,665.

Access to Gas Processing Facilities

Access to key infrastructure is an essential part of effective open access arrangements. This work stream seeks to determine whether any issues are preventing open access to processing plants and thus hindering the effectiveness of the regime. The key deliverable is meeting the regulatory requirements of the Gas (Processing Facilities Information Disclosure) Rules 2008.

During FY2011, information supplied about surplus capacity under the Rules will be collated and published on Gas Industry Co's website for the benefit of access seekers. This will enable the Company to report to the Associate Minister on access constraints and recommend whether more extensive regulation is necessary. The Rules are set to expire in June 2014; however in April 2013, the Company will advise the Associate Minister whether further activity is required.

Work stream	Act/GPS objectives & outcomes	Ongoing activity	Budget
Access to Gas Processing Facilities	Gas industry participants and new entrants are able to access third-party gas processing facilities under reasonable terms and conditions	Ensure all disclosures are kept up to date, report to the Associate Minister on access seekers and, in the event of non-disclosure, assist in any enforcement actions Collect, monitor, and publish disclosed information Document any access issues that are brought to the attention of Gas Industry Co	$11,873

Pipeline balancing

A problem identified early in the Company's work on access to transmission pipelines was that of pipeline balancing. Balancing refers to the management of the inventory of gas in a pipeline within acceptable limits. Effective balancing arrangements are a necessary component of open access.

Although industry participants have recognised that the Maui and Vector pipeline balancing regimes are not operating as intended, they have found it difficult to unravel the issues. In December 2009, Gas Industry Co made a recommendation to the Associate Minister on transmission pipeline balancing.

The recommendation was to introduce the Gas Governance (Balancing) Rules 2009, subject to providing the industry more time to study the detail of the Rules and how they will be implemented.

Work Stream	Act/GPS objectives & outcomes	Activity	Milestones	Budget
Pipeline Balancing	Gas industry participants and new entrants are able to access transmission pipelines under reasonable terms and conditions	Consider/approve the TSOs' Balancing Plan or, if TSOs can't agree, develop a Balancing Plan	Approve Balancing Plan in August 2010	$488,285
		Further work on D+1 feasibility	D+1 options paper in March 2011	

Interconnection

Interconnection to transmission pipelines was identified by the industry as an issue in the work that Gas Industry Co undertook on access to transmission pipelines. The ability to establish a physical connection to a transmission pipeline in an efficient and timely manner is a key element in ensuring that new sources of gas are able to be brought to market.

In February 2009, Gas Industry Co issued the Transmission Pipeline Interconnection Guidelines (the Guidelines). These set out the Company's view on the features of good interconnection practice. They were the first Guidelines issued as a means of influencing outcomes to achieve a regulatory objective. In December 2009, the Company will advise the Associate Minister that the TSOs have made good progress towards complying with the Guidelines and should be given more time to bring their policies and documentation into better alignment.

Work Stream	Act/GPS objectives & outcomes	Activity	Milestones	Budget
Interconnection	Gas industry participants and new entrants are able to access transmission pipelines under reasonable terms and conditions	If regulations are required, develop and consult on draft regulations	Issue Options paper in December 2010	$89,363

Distribution contracts

The purpose of this workstream is to identify distribution sector arrangements that are resulting in outcomes inconsistent with those sought under the Gas Act and the GPS, and to develop options to address shortcomings. These could include prescribing reasonable terms and conditions of access to distribution pipelines, providing for information disclosure, or facilitating pan-industry agreement on relevant issues.

Work Stream	Act/GPS objectives & outcomes	Activity	Milestones	Budget
Distribution Contracts	Gas industry participants and new entrants are able to access distribution pipelines under reasonable terms and conditions Consistent standards and protocols apply to the operations relating to access for all distribution pipelines	Develop issues paper Develop SoP Develop next steps documents	Release Distribution Contracts Issues Paper in August 2010 Release SoP in February 2011 Approval to develop next steps documents June 2011	$107,490

Industry facilitation

Gas Industry Co has contractual obligations under MOUs with both MDL and Vector to assist with rule changes to their respective industry codes. The FY2011 work programme assumes that code change activity will continue at a similar level to that for FY2010.

Gas Industry Co has undertaken significant facilitation roles with improved transmission access in mind. It convenes industry meetings (eg over-pressurisation forums), commissions independent research (eg on UFG, capacity trading on the Vector network), and holds talks with industry participants on specific issues. The Company's aim in these activities is to improve the quality of the debate and thereby facilitate industry solutions to infrastructure access. The work is an important way of delivering value to stakeholders and the work programme therefore assumes the Company will receive one such request in FY2011.

Work Stream	Act/GPS objectives & outcomes	Activity	Milestones	Budget
Industry facilitation	Facilitating nexus between industry and government Multilateral terms of access need a process to evolve to ensure ongoing relevance and efficiency	Facilitating, influencing and communicating with industry to enhance debate over best-practice solutions on industry issues Three rule changes and three rule change appeals were received in FY2010, a similar number of requests are expected in FY2011	Facilitate industry issues (if requested) Progress all rule changes in accordance with MOU Seek feedback from MPOC / VTC parties about the effectiveness of GIC role in rule change process	$251,853

Capacity

Gas Industry Co identified access to short-term capacity on the Vector pipeline as an issue in its 2006 Transmission Access Issues Review paper. In June 2009, Vector notified shippers that it was unable to accept new capacity bookings on its North Pipeline as all its capacity was committed to existing contracts. Gas Industry Co has consequently re-prioritised this workstream so that, by the end of FY2010, it can advise its Board whether regulation is required to address capacity issues, and release a subsequent Statement of Proposal.

In FY2011, the Company plans to further progress this work by developing and consulting on draft regulations, if they are required.

Work stream	Act/GPS objectives & outcomes	Activity	Milestones	Budget
Capacity	Access to short-term capacity on pipeline networks is required by shippers for short-term trading	If regulations are required, develop and consult on draft regulations	Issue consultation paper in December 2010	$31,873

Upstream reconciliation

The Gas Act provides for regulations to be made for the purpose of 'providing for the establishment and operation of wholesale markets for gas, including for (i) protocols and standards for reconciling and balancing gas; and (ii) clearing, setting, and reconciling market transactions'. Upstream reconciliation/title tracking is the name given to the process of transferring legal title, or ownership, to a tranche of gas. The objective of the project is to consider whether the arrangements for upstream reconciliation/title tracking are fair and efficient, and to recommend alternative arrangements if they are not. Specific objectives are to identify issues related to upstream reconciliation/title tracking and, if necessary, to describe and evaluate options to address the issues.

Work stream area	Act/GPS objectives & outcomes	Activity	Milestones	Budget
Upstream Reconciliation	Title-tracking may impose efficiency of transmission access	Develop Title Tracking Issues paper	Release Title Tracking issues paper in December 2010	$82,490

3.3 Market Operations Group

The objective for the Market Operations Group (MOG) is to improve the efficiency of the wholesale and retail markets. The estimated cost for its activities in FY2011 is $3,824,141. This includes external service provider costs of $1,966,400, external consulting costs of $734,000 and depreciation of $436,490[1], but does not include governance or corporate costs, which are discussed separately below.

The work of the MOG can be divided into wholesale, retail, and other work streams.

Wholesale activity

Planned activity for FY2011 includes operation of a wholesale market trial, oversight of the Gas Governance (Critical Contingency Management) Regulations 2008 (CCM Regulations), and anticipated rule changes. The total cost of wholesale markets activity for FY2011 is $1,147,322, including service provider costs of $710,000. This compares with an expected $936,647 (including service provider costs of $600,000) in FY2010.

Wholesale Market Trading Platform

Although Minister Parker approved a 'trial' of the wholesale market trading platform in December 2007, it has taken time to implement due to the need to interface the proposed trading hub with the Maui Pipeline Operating Code ('MPOC'). At the end of FY2010, it is expected that an MPOC change request will have been processed that provides for two non-physical welded points that will form the basis of a trading hub. In addition, it is assumed that Gas Industry Co will have signed an Inter-Connection Agreement (ICA) in respect of those welded points and that industry participants will have been invited to join the wholesale market and have signed up in sufficient numbers to justify commencing a trial.

Although the Associate Minister has indicated that she wishes the wholesale market to be given equal priority with balancing and interconnection, the degree to which industry participants will support the trial is not yet clear. In spite of this uncertainty, the indicative work programme assumes that the trial has commenced in FY2010 and is continuing into FY2011. On that basis, the projected activities will encompass hub balancing and market operation as well as assessing and reporting on the trial. It should be noted that it may be necessary for Gas Industry Co to continue as hub operator pro tem while the trial is assessed and, pending a decision on a longer-term hub operator solution.

[1] The depreciation costs of the downstream reconciliation and switching systems have been pre-funded by one-off development fees and are accordingly excluded from the levy calculation.

Work stream area	Act/GPS objectives & outcomes	Activity	Milestones	Budget
Wholesale Market	Efficient arrangements for the short-term trading of gas	Administer, monitor, and evaluate wholesale market platform	Report to the Associate Minister on the outcomes of the 'trial' market within 12 months of platform commencement	$275,888

Critical Contingency Management

The focus of this work stream for FY2010 was to complete the process of approving TSOs' Critical Contingency Management (CCM) plans so that the regulations could go live. In FY2011, this work stream will focus on Gas Industry Co's statutory roles under the CCM Regulations as well as management of the service provider agreement with the Critical Contingency Operator (CCO). Actual activities will depend on whether there are critical contingencies declared during the year. Typically, the CCO will be required to run an annual exercise to test the TSO plans and associated communication processes. However, if an actual critical contingency event occurs, then that is sufficient to substitute for the annual exercise.

Work stream area	Act/GPS objectives & outcomes	Ongoing activity	Budget
Critical Contingency Management	Sound arrangements for the management of critical gas contingencies	Oversight of critical contingency management regulations Manage service provider contract and monitor results of annual exercises Ad hoc appointment of Independent Expert and Expert Adviser as required under the Regulations Operation of critical contingency pool following an event	$784,660

Rule Changes

Changes will be required to the Rules from time to time and for a variety of reasons; variations in market circumstances, the need to correct aspects that are not operating as intended, and to reflect changes in policy. In general, individual rule change proposals will be accumulated until there are sufficient proposals in hand to justify initiating the rule change process. Budget constraints permitting, it is envisaged that this process will take no longer than six to nine months.

Work stream area	Act/GPS objectives & outcomes	Activity	Budget
Rule Changes - Wholesale	Amending gas governance arrangements to ensure their ongoing relevance and effectiveness	Post-implementation review of contingency management regulations Review of Wholesale Market rules post-trial	$86,774

Retail Activity

The proposed activity for FY2011 is the fulfilment of the statutory roles under the Gas (Switching Arrangements) Rules 2008 (Switching Rules) and the Gas (Downstream Reconciliation) Rules 2008 (Reconciliation Rules); a significant review of the Reconciliation Rules; and implementation of other rule changes as required. The total cost of this activity in FY2011 is expected to be $2,213,924, including service provider costs of $1,090,000 and depreciation of $436,490. FY2010 costs are expected to be $1,663,950 ($2,100,440 if depreciation costs are included).

For both the Switching Rules and the Reconciliation Rules, Gas Industry Co is responsible for overseeing the performance of the service provider, providing guidance on the operation of the rules, and considering exemption requests. In addition, under the Reconciliation Rules, Gas Industry Co reviews monthly allocation results and can commission audits and special allocations. In the last 12 months, Gas Industry Co's role has included reviewing seven special allocation requests, two event audits, considering 53 exemption applications, and producing monthly market operations reports for the Board. A similar level of market activity is expected in FY2011.

Work stream area	Act/GPS objectives & outcomes	Ongoing activity	Budget
Switching & Registry	Effective and efficient customer switching arrangements	Oversight of Switching Rules including: • Managing the Registry Operator under the service provider agreement, including performance review • Provide the interface between the Registry Operator and participants, and dealing with issues surrounding the operation of the Switching Rules • Analysing registry reports and liaising with the Market Administrator in respect of alleged breaches • Monitoring and assessing the performance of the Switching Rules; developing a register of issues that may require rule changes at a later date	$657,141

Work stream area	Act/GPS objectives & outcomes	Ongoing activity	Budget
Downstream Reconciliation	Accurate, efficient and timely arrangements for the allocation and reconciliation of downstream gas quantities	Oversight of Reconciliation Rules including: • Managing the Allocation Agent under the service provider agreement, including performance review • Providing the interface between the Allocation Agent and participants, and dealing with issues around the operation of the Reconciliation Rules • Analysing reconciliation reports and liaising with the Market Administrator in respect of alleged breaches • Monitoring and assessing performance of the Reconciliation Rules; developing a register of issues that may require rule changes	$1,238,612

Rule Changes

Gas Industry Co plans a comprehensive review of the Reconciliation Rules in FY2011. Budgeted costs also include an allowance for implementing minor changes to the Switching Rules, should the need arise.

Work stream area	Act/GPS objectives & outcomes	Activity	Budget
Rule Changes - Retail	Amending gas governance arrangements to ensure their ongoing relevance and effectiveness	Review of Reconciliation Rules Progress rule changes as required Minor drafting changes to Switching Rules	$318,171

Other activity

Other activity encompasses those elements of the MOG that involve both wholesale and retail market activities. It includes the operation of the compliance regime and the development and monitoring of performance indicators for approved gas governance arrangements. The total cost for other market activities in FY2011 is $462,895, including external service provider costs of $166,400. In FY2010, the costs are expected to be $533,083, including external service provider costs of $311,400.

Compliance and Enforcement

The purpose of the Gas Governance (Compliance) Regulations 2008 is to provide for the monitoring and enforcement of the gas governance rules and regulations described in this section and the Gas (Processing Facilities Information Disclosure) Rules 2008 (see 3.2).

The compliance regime comprises three roles: a Rulings Panel; an Investigator; and a Market Administrator. The Rulings Panel and Investigator are out-sourced. Gas Industry Co's role is to help them perform their roles, and to oversee the effectiveness of the regime and consider any amendments to the regulations as required. The Company acts as the Market Administrator and the budget assumes a change from the FY2010 Business Plan in that the Market Administrator work is brought fully in-house.

Under the Compliance Regulations, Gas Industry Co looks into alleged breaches of market rules and regulations and supports the Investigator and Rulings Panel in their work in determining and settling breaches. In the past 12 months, almost 5,000 breaches have been alleged; at the time of writing, about 390 had been determined by the Market Administrator as raising a material issue and have been passed to the Investigator for action. A similar level of activity is expected in FY2011.

Work stream area	Act/GPS objectives & outcomes	Ongoing activity	Budget
Compliance	Gas governance arrangements are supported by appropriate compliance and dispute resolution processes	Oversight of Compliance Regulations including: • Assisting and enabling the Market Administrator, Investigator, and Rulings Panel to process alleged breaches • Amending and reviewing the compliance regime, as required, to support new gas governance arrangements • Reporting quarterly to the Board on compliance activities	$348,030

Performance measures

Another area of work for the MOG is the development and implementation of performance indicators for the market governance arrangements that Gas Industry Co administers.

Work stream area	Act/GPS objectives & outcomes	Activity	Budget
Performance Measures	Gas Governance arrangements are monitored by Gas Industry Co for ongoing relevance and effectiveness	Collect and publish information on performance indicators for each approved arrangement	$114,865

3.4 Office of the Chief Executive

The Office of the Chief Executive (OCE) is responsible for the relationship with the Associate Minister and MED, board reporting, and general oversight across all work streams. The OCE also has responsibility for GPS tasks relating to sector performance and consumer issues. The budget for this group in FY2011 is $1,139,750. It includes external consultancy costs of $314,290. The total costs for the OCE in FY2010 are expected to be $1,210,020.

In FY2011, the OCE will continue to hold bi-monthly meetings with the Associate Minister and MED to discuss gas industry and co-regulatory performance, act as the primary interface with other government agencies, and represent the Company at industry conferences and other events. The Board meets 10–12 times a year and the OCE's budget includes Board costs, as well as the internal salaries required to co-ordinate board reporting.

Work stream area	Act/GPS objectives & outcomes	Ongoing activity	Budget
Governance	Governance and external relationships	Achievement of business and strategic plans Reporting to MED / Associate Minister	$664,750

Activities in FY2011 are also expected to include advice on strategic matters affecting the gas sector and input into an MED project assessing industry performance. Gas Industry Co will also be involved in the oversight of an approved industry complaints scheme and the implementation of its recommendation on retail contract terms for the Associate Minister.

Work stream area	Act/GPS objectives & outcomes	Ongoing activity	Budget
Strategic Advice	Provide advice on the extent to which policies to enhance the direct use of gas in industrial, commercial and residential applications would mitigate greenhouse gas emissions and the likely costs of implementing those policies Good information is publicly available on the performance and present state of the gas sector	Advice to Associate Minister and Board as requested	$250,000

Work stream area	Act/GPS objectives & outcomes	Ongoing activity	Budget
Consumer Issues	All small gas consumers have effective access to a complaints resolution system	Oversight of industry complaints scheme	$225,000
	Contractual arrangements between gas retailers and small consumers adequately protect the long-term interests of small consumers	Advice to Associate Minister on benchmark retail contract terms	

3.5 Corporate Services Group

The Corporate Services Group (CSG) is responsible for the administrative and statutory reporting functions of Gas Industry Co. Specifically, its responsibilities include obtaining the annual levy, compliance with the Company's external accountability obligations (Strategic Plan, Quarterly Reports, Annual Reports, and AGM), stakeholder communications (industry and consumer conference, website, shareholder visits, and Company newsletter), and business planning and reporting (human resources, finances, project management and administrative support).

The Group's budget for FY2011 is $1,851,171. This includes external consultancy costs of $276,200. The estimated costs of the Group for FY2010 are $2,401,341. The anticipated reduction primarily relates to the re-assignment of the depreciation expense on industry assets to the MOG in FY2011 as well as some savings in other corporate costs.

Objective	Activity	Budget
Provide funding	Recommendations to Associate Minister on FY2012 Levy Regulations	92,438
Meet statutory accountability requirement	Publish Strategic Plan, Quarterly Reports, Annual Reports	131,008
Legal & risk	Manage legal risk (insurance, legal contingency etc)	228,150
Provide support to organisation	Human resources (ACC, recruitment, training & development, staff welfare, KiwiSaver and temps)	285,700
	Finance & project management (management & financial reporting)	238,118
	Information technology (equipment lease, external support)	80,760
	Communications (industry engagement activities and website)	55,160
	Indirect salaries	177,818
	Overhead (rent, depreciation, travel, photocopying, office supplies & stationery, repairs & maintenance, telephone, publications, postage, entertainment)	562,019

Q1: Do you consider there to be any other items that should be included in the Company's intended work programme for FY2011?

Q2: Do you consider there to be any items that should be excluded from the Company's intended work programme for FY2011?

4 Levy Principles

Gas Industry Co now has five years experience of setting an annual levy. During this time we have consulted extensively, receiving a number of submissions on both the structure of the levy and our methodology. Drawing on this experience, a robust set of general levy principles, covering levy setting, were codified into a formal Statement of Levy Principles and published in September 2009.

This document describes the legislative authority, levy principles, and levy structure Gas Industry Co uses when developing its levy recommendation for funding each year under the levy provisions of the Act. These have been used in the preparation of the FY2011 levy proposal).

However, we are also seeking feedback from industry participants on some suggested amendments to the Statement of Levy Principles, which is discussed in section 9. Any changes arising from that feedback will be included in the FY2012 levy consultation round.

5 Budget

The levy is structured so that particular levy components fund relevant parts of the Gas Industry Co work programme. The work programme is divided into two aggregated blocks of work corresponding to each of the retail and wholesale levies. For these purposes:

- work on those parts of the gas supply chain upstream of distribution comprise the wholesale gas aggregated block of work; and

- work on consumer issues, retail markets, and distribution comprise the retail gas aggregated block of work

Gas Industry Co's budget is based on a best estimate of the costs to deliver the work programme prepared for calculation of the FY2011 levy. Budgets are set significantly in advance of consultation on proposed new policy initiatives. Accordingly, actual expenditure may vary from budgeted expenditure as policy design is revised to reflect changes that may be required as a result of submissions received and further analysis.

Wholesale Levy

Table 1 **FY2011 Wholesale Levy Budget**

Work stream	Direct Costs				Overhead Allocation	Total Costs
	Service Providers	Consultants	Salaries	Total Direct Costs		
Balancing	0	298,325	189,960	**488,285**	356,320	844,605
Capacity Trading	0	20,000	11,873	**31,873**	23,310	55,183
Compliance	33,280	17,000	19,326	**69,606**	14,839	84,445
Critical Contingency Management	650,000	50,000	84,660	**784,660**	66,006	850,666
Gas Processing	0	0	11,873	**11,873**	7,953	19,826

Work stream	Direct Costs				Overhead Allocation	Total Costs
	Service Providers	Consultants	Salaries	Total Direct Costs		
Industry Facilitation	0	145,000	106,853	**251,853**	182,917	434,770
Interconnection	0	30,000	59,363	**89,363**	62,801	152,164
Rule Changes - Wholesale	0	75,000	11,774	**86,774**	65,569	152,343
Strategic Issues	0	65,675	59,325	**125,000**	135,910	260,910
Upstream Reconciliation	0	35,000	47,490	**82,490**	58,687	141,177
Wholesale Market	60,000	75,000	140,888	**275,888**	211,367	487,255
Total	**743,280**	**811,000**	**743,385**	**2,297,662**	**1,185,679**	**3,483,342**

Retail

Table 2 FY2011 Retail Levy Budget

Work stream	Direct Costs					Overhead Allocation	Total Costs
	Service Providers	Consultants	Depreciation	Salaries	Total Direct Costs		
Compliance	133,120	68,000	0	77,304	**278,424**	59,358	**337,782**
Consumer Issues	0	150,450	0	74,550	**225,000**	195,802	**420,802**
Distribution Contracts	0	60,000	0	47,490	**107,490**	77,884	**185,374**
Downstream Reconciliation	830,000	74,000	210,524	124,088	**1,238,612**	255,882	**1,494,494**
Performance Measures	0	60,000	0	54,865	**114,865**	88,139	**203,004**
Rule Changes - Retail	0	275,000	0	43,171	**318,171**	244,086	**562,257**
Strategic Issues	0	65,675	0	59,325	**125,000**	135,910	**260,910**
Switching	260,000	40,000	225,966	131,175	**657,141**	273,181	**930,322**
Total	**1,223,120**	**793,125**	**436,490**	**611,968**	**3,064,702**	**1,330,242**	**4,394,944**

Corporate

Corporate costs broadly comprise the indirect costs of Gas Industry Co, being governance, CEO, administrative support services, and office infrastructure. Work that is broadly related to gas governance, rather than to one of the two aggregated work streams, is also classified as indirect.

Table 3 Corporate Budget

Work area	Consultants	External Costs	Other	Salaries	Total Overhead
Governance	32,490	262,460	38,000	331,800	**664,750**
Finance & Project Management	96,000	15,000	5,580	121,538	**238,118**
Legal & Risk	125,000	0	28,600	74,550	**228,150**
Levy	15,000	0	0	77,438	**92,438**
Statutory Accountabilities	0	0	50,000	81,008	**131,008**
Communications	19,200	10,800	25,160	0	**55,160**
Human Resources	21,000	130,000	90,600	44,100	**285,700**
Information Technology	0	32,400	48,360	0	**80,760**
Overhead	0	0	562,019	177,818	**739,837**
Total	**308,690**	**450,660**	**848,319**	**908,252**	**2,515,921**

Gas Industry Co apportions its indirect costs on the basis of the total direct costs of each work stream. This approach is used as it is simple to apply and it better represents indirect costs that are unrelated to staff salaries, such as Board costs and work on general aspects of gas governance. It also better reflects the dominance of consultant costs in the non-salary component of direct costs, which have historically been incurred as a substitute for sufficient permanent staff.

Table 4 FY2011 Summary Levy Budget

Workstream	Direct Costs					Overhead Allocation	Total Costs
	Service Providers	Consultants	Depreciation	Salaries	Total Direct Costs		
Wholesale	743,280	811,000	0	743,382	**2,297,662**	1,185,679	**3,483,342**
Retail	1,223,120	793,125	436,489	611,968	**3,064,702**	1,330,242	**4,394,944**
Total	**1,966,400**	**1,604,125**	**436,489**	**1,355,350**	**5,362,365**	**2,515,921**	**7,878,286**

6 Levy Funding Requirement

6.1 Sources of funding

The levy funding requirement (LFR) is the amount of money Gas Industry Co seeks to recover from industry participants via the annual levy. In simple terms, it represents the Company's unfunded work programme costs, after applying its reserves and taking into account other revenue sources, such as market fees.

In FY2011, the Company will receive three sources of funds: the annual levy, shareholder fees, and market fees. The Company proposes to continue its policy of setting aside the annual shareholder fees as an equity reserve, providing a level of risk mitigation against unforeseen events. This means the primary source of revenue for the proposed FY2011 expenditure continues to be the annual levy. However, in addition to the annual levy, market fees also make a significant contribution towards the ongoing costs of the new gas governance arrangements.

6.2 Market fees

Gas Industry Co has estimated the costs that will be recovered through market fees. These are presented in the table below.

Regulations	Service Provider Contract	Other External Costs	Total
Switching	260,000	40,000	300,000
Reconciliation	830,000	74,000	904,000
Compliance	166,400	85,000	251,400
Critical Contingency Management	650,000	50,000	700,000
Total	**1,906,400**	**249,000**	**2,155,400**

Copies of the service provider contracts that comprise the major component of these costs are available on our website. The other costs proposed to be recovered under market fees in FY2011 are those of persons appointed under provisions in the rules and regulations, for example, independent experts and external consultants.

6.3 Other revenue and over- and under-recoveries of the levy

To determine the final levy funding requirement, work programme costs need to be adjusted for other revenue and over- and under-recoveries of prior years' levies. As at 30 June 2009, Gas Industry Co had a retained earnings balance of $2,356,386. Included in this figure was a net $211,096 from over-recoveries the Company has collected from the retail and wholesale levy in past years. It should be noted that in contrast to prior years, the wholesale component of the Company's activities was overspent in FY2009, while there was an underspend in the retail component. In accordance with guidelines laid out in the Statement of Levy Principles, the $211,096 over-recovery of past levies will be used to defray the FY2011 work programme costs, by applying $463,215 to the costs of the retail programme and recovering an additional $252,119 from the wholesale programme.

The balance of the Retained Earnings figure is made up of an amount of $1,955,290, being the depreciation pool relating to the industry assets[2], and $190,000 in accumulated annual shareholder fees. A portion of the depreciation pool will also be used to defray the depreciation expense of the industry assets, while the Board has determined the accumulated shareholder fees will continue to be held by the Company as a contingency amount. Adding these items together, the total amount available to apply against the FY2011 work programme cost is $647,586.

6.4 FY2011 Levy funding requirement

Calculation of the FY2011 levy funding requirement is based on the methodology contained in the levy principles document.

Table 6 FY2011 Levy Funding Requirement

	Retail	Wholesale	Total
Work programme direct costs	3,064,702	2,297,662	5,362,365
Work programme indirect costs	1,330,361	1,185,560	2,515,921
Total work programme costs	**4,395,064**	**3,483,222**	**7,878,286**
Less Over-recovery from prior levies	(463,215)	252,119	(211,096)
Less Pre-funded depreciation on industry assets	(436,490)	-	(436,490)
Sub-total	**3,495,359**	**3,735,341**	**7,230,700**
Less market fee recovery	(1,405,120)	(750,280)	(2,155,400)
Total levy funding requirement	**2,090,239**	**2,985,061**	**5,075,300**

Q3: Do you have any questions on the calculation of the levy funding requirement for FY2011?

[2] Downstream Reconciliation system and the Switching & Registry database

7 Proposed Levy

7.1 Levy assumptions

The following volume assumptions have been made to calculate the levy rates for FY2011:

- ICP numbers for FY2011 will be approximately 255,000. In FY2010, we estimated 250,000. The revised number is based on an independent analysis of the number of active ICPs contained in the Switching and Registry database.

- Wholesale gas volumes will be 140PJ in FY2011. The FY2010 budget assumed gas volumes of 145PJs. However, wholesale gas volumes in FY2010 have been declining relative to the budget estimate and the Board requested the Executive reassess the FY2011 budget assumption in light of the Company's established policy of conservatism in forecasting. The lower estimate of the volume of wholesale gas in FY2011 increases the Wholesale levy by .07c/GJ.

7.2 Retail and wholesale levies

Based on these assumptions, table 7 presents the calculation of the retail and wholesale levies for FY2011:

Table 7 FY2011 Levy Calculation

	FY2011 Retail	FY2011 Wholesale	FY2011 Total
Direct Costs	3,064,702	2,297,662	5,362,365
Proportion of Direct Costs to Total Costs	*57.2%*	*42.8%*	
Indirect Costs	1,330,242	1,185,679	2,515,921
Total Work Programme Costs	**4,394,944**	**3,483,342**	**7,878,286**
Deduction of Market Fees	(1,405,120)	(750,280)	(2,155,400)
Allocation of Other Revenue	-	-	-
Under (Over) Recovery of Levy	(463,215)	252,119	(211,096)
Depn. on Industry Assets	(436,490)	-	(436,490)
	(2,304,825)	**(498,161)**	**(2,802,986)**
Total Levy Funding Requirement	**2,090,120**	**2,985,181**	**5,075,300**
Volume Units	*ICPs*	*GJ*	
Volume	255,000	140,000,000	
Levy Unit	*$/ICP*	*cent/GJ*	
Levy Rate	**8.20**	**2.13**	
Projected Levy Revenue	**2,090,120**	**2,985,181**	**5,075,300**

The proposed levy rates for FY2011 are therefore:

- Retail levy of $8.20 per annum payable on each ICP. This is an increase of 28% on the FY2010 rate, which was $6.40 per annum payable on each ICP

- Wholesale levy of 2.13 cents per GJ of gas purchased directly from gas producers. This is a 28% increase the FY2010 rate, which was 1.67 cents per GJ.

7.3 Comparison with prior years

The table below compares the proposed levy for FY2011 with the preceding three years.

Year	Retail Levy	Wholesale Levy
FY2008	$8.18 per ICP	1.93 cents per GJ
FY2009	$7.42 per ICP	1.79 cents per GJ
FY2010	$6.40 per ICP	1.67 cents per GJ
FY2011	$8.20 per ICP	2.13 cents per GJ

Q4: Do you have any comment on the proposed levy for FY2011?

8 Proposed regulation amendments

8.1 Definition of gas producer

In its submission on the FY2010 Levy, Contact Energy expressed concern that the definition of ‘gas producer’, as defined in the Gas Act and incorporated into the levy regulations, created some uncertainty around the point in time at which the wholesale levy is payable.

The Gas Act defines a 'gas producer' as a 'person who supplies gas that is transmitted on gas transmission or distribution pipelines'. The levy regulations require that the wholesale levy is payable on every 'gigajoule of gas that was purchased by [an] industry participant directly from gas producers during the previous month'. Contact Energy suggests that the definition of gas producer means that the levy could be payable at any point where gas is 'purchased' on the gas supply chain. For example, the levy could be payable where the gas is purchased by a gas retailer from a gas wholesaler because the gas wholesaler could be defined as a person who is 'supplying gas that is transmitted on a gas transmission or distribution pipeline'.

Gas Industry Co does not agree with Contact Energy’s interpretation. The ordinary meaning of the term 'gas producer' is a person who produces gas from a gas field. The only proviso to this is that the gas must be transmitted on a gas transmission or distribution pipeline. This means that gas producers who do not transmit their gas (they may, for example, flare it or ship it as LNG) are not covered by the definition. Further, a 'gas producer' is distinguished in the Gas Act from a ‘gas wholesaler’ and a ‘gas retailer’, who are clearly intended to be persons operating downstream of the person who produces the gas from a gas field (although they may be subsidiaries of the gas producer, as is made clear in the definition of ‘gas wholesaler’).

Gas Industry Co’s intention is that the wholesale levy is payable only once, in respect of any gas purchased and transmitted to end users. This is the case even where that gas may be ‘traded’ more than once before it is received by the end user. It is intended that the levy should be payable by the purchaser at the initial point of purchase in the chain of downstream transactions. That is, the levy is payable at the point where the gas is purchased from the person who ‘produced’ the gas - whether it is purchased by a gas wholesaler (which may be a subsidiary of the gas producer), gas retailer, or end user. The levy is not payable at the point where a gas retailer purchases the gas from a gas wholesaler, or an end user purchases the gas from a gas wholesaler or gas retailer. It is, however, payable where an end user purchases gas directly from a gas producer.

Contact Energy points to two particular circumstances that may cause difficulties under the levy regulations. The first is where a gas producer is selling gas to a related party, such as a subsidiary, which acts as a wholesaler or retailer in the gas market. Contact Energy suggests in those circumstances, there may not be a 'purchase' for the purposes of the levy regulations.

The definition of 'gas wholesaler' includes any person, any subsidiary of which is a gas wholesaler. It appears that the purpose of this definition was to ensure that gas producers with subsidiaries that act as gas wholesalers are covered by the provisions of the Act. That definition preceded the addition of the definition of 'gas producer' in 2004. Gas Industry Co's intention is that the levy should be payable on 'purchases' of gas from gas producers and their subsidiaries that act as gas wholesalers or retailers - whatever form those transactions may take. Gas Industry Co therefore proposes to recommend to the Parliamentary Counsels Office that the FY2011 levy regulations make it clear that the levy is payable where a gas producer is supplying gas to a related party operating as a gas wholesaler or gas retailer, including making it clear from which gas producer that gas has been purchased.

8.2 Purchases from Gas Storage facilities

It has been suggested that the levy regulations need to clarify whether the levy is payable on gas purchased from gas storage facilities, such as the facility that Contact Energy is establishing at the Ahuroa field.

It is not Gas Industry Co's intention that the levy should be payable on purchases from a gas storage facility as the levy should have already been paid by the owner of the facility on the gas purchased by the owner from a gas producer (or by the party that purchased the gas from a gas producer and sold it to the facility owner). This is distinct from levies being recovered from the recoverable gas reserves of gas storage facilities that would, under normal circumstances, be subject to the Gas Industry Co levy once it is on-sold. Gas Industry Co therefore proposes to recommend to the Parliamentary Counsels Office that the FY2011 levy regulations provide clarity on issues relating to gas storage facilities.

8.3 Levying powers over recoverable gas reserves

During the FY2010 levy round, MED raised an associated point on the issue of gas storage facilities. It believed that Gas Industry Co faced a similar issue to that of the Crown in terms of extracting royalties from Tariki/Ahuroa. In the latter case, the Crown needed to be careful that it did not claim royalties twice for gas going in and gas going out of the storage facility. Nevertheless, the Crown is concerned that royalties are received for the amount of gas remaining in Tariki/Ahuroa and yet to be extracted. This remaining, yet-to-be extracted gas would also, under normal circumstances, be subject to the Gas Industry Co levy once the gas is on-sold.

MED has recommended that if Gas Industry Co amends the FY2011 levy regulations to account for gas storage facilities, it considers recommending words to the effect that it can recover levies on remaining recoverable gas at Tariki/Ahuroa.

8.4 Maui gas

Within the current (FY2010) levy regulations, a 'gas producer' is defined as having the same meaning as in section 43D(1) of the Act, except in terms of Maui gas when it means the Crown. 'Maui gas' refers to the contractual arrangements between the Crown and the Maui Mining Companies (Shell, Todd, and OMV), whereby the Crown purchases gas from them and on-sells it to Maui users (Vector, Contact, and Methanex). The effect of the definition in the levy regulation is to exempt the Crown from paying the wholesale levy on its purchases, transferring that responsibility to the Maui users. The contracts between the Crown and the Maui Mining Companies expire during FY2010, meaning this section will need to be removed from the FY2011 levy regulations.

8.5 Compliance arrangements

Under Regulation 13 of the Gas (Levy of Industry Participants) Regulations 2009, Gas Industry Co may, by notice in writing, require industry participants to supply certain information. Under Regulation 14, this information must be supplied in writing and must be certified as correct by a director or principal officer of the company. Recent events have given Gas Industry Co cause to consider the compliance arrangements for these regulations and whether some form of compliance regime needs to be in place to ensure the timely supply of such information once it has been requested.

At the next convenient time, Gas Industry Co proposes to amend the Gas Governance (Compliance) Regulations 2008 (the 'Compliance regulations') so that they also encompass the annual Levy Regulations.

Q5:	*Do you have any comment on regulatory amendments describe above?*

9 Suggested levy principles amendments

9.1 Indirect cost allocation

The issue of how Gas Industry Co's indirect costs should be allocated was consulted on with industry in both the FY2009 and FY2010 levy rounds. Under the current Statement of Levy Principles, staff salaries and consultancy costs that are directly related to a work stream are allocated to that work stream. Remaining costs, including salaries, are classified as overhead and allocated on the basis of the total direct costs of each work stream, excluding service provider costs.

It is acknowledged that there are different views on not only the classification of direct and indirect salary costs but also on the most appropriate methodology for allocating indirect costs. For example, allocating salary costs relating to HR, website administration, project management and CE review as well as a proportionate share of other expenses such as rent, insurance, and utilities would have shifted a total of $878,076 from the 'corporate' and 'governance' costs to the market, infrastructure access and GPS tasks work streams in FY2011, as illustrated in the table below.

Table 8 Impact of allocating overhead costs to workstreams based on FY2011 budget

Work stream	Indicative Budget	Adjustment	Adjusted Budget
Infrastructure Access	$1,063,225	$333,905	$1,397,130
Market Operations	$1,668,740	$375,954	$2,044,694
Service Providers / Market Fees	$2,155,400	0	$2,155,400
GPS Tasks	$475,000	$193,048	$668,048
Governance	$664,750	($24,831)	$639,919
Corporate Services	$1,851,171	($878,076)	$973,095
Total	**$7,878,286**	**0**	**$7,878,286**

Under this scenario, the indicative Retail levy would have decreased $0.44/ICP to $7.76/ICP, while the indicative Wholesale levy would have increased 0.08 cents/GJ to 2.21cents/GJ. However, this allocation methodology does not decrease either the total WPC or LFR.

We prefer the current approach because it:

- is simple to apply
- achieves better transparency
- better represents those unallocated costs that are unrelated to staff salaries. These include the costs of the Board and work related to general aspects of gas governance
- better reflects the dominance of consultant costs in the non-salary component of direct cost. These costs have historically been incurred as a substitute for sufficient permanent staff.

However, the disadvantage with the current approach is that it gives the appearance of a particularly high direct/indirect cost ratio[3].

Q6:	*Do you consider that GIC should alter its current method of defining direct costs and allocate more of its indirect costs to work streams?*

9.2 Allocation of costs between annual levy and market fees

In FY2009, the Company recovered the costs of service providers, external costs, and a portion of its direct costs[4] under market fees (fees levied under specific gas governance arrangements). That was the first year market fees were received.

In FY2010, following industry consultation, legal advice from MED, Crown Law, and in-house counsel, this cost recovery policy was amended so that only service providers and external consultancy costs that directly relate to the new regulations were recovered through market fees.

Under the existing policy, the indirect costs incurred by Gas Industry Co as a consequence of undertaking its statutory roles, such as administrative support and the proportionate share of other expenses, such as rent, utilities and insurance, are paid by levy payers as opposed to the payers of market fees.

If an alternative policy allowing these costs to be reimbursed via market fees had been used for calculating the FY2011 levy, the indicative Retail levy would decrease $1.42/ICP to $6.78/ICP, and the indicative Wholesale levy would decrease 0.05 cents/GJ to 2.08 cents/GJ.

Q7:	*Do you support the inclusion of a portion of Gas Industry Co's indirect costs in market fees for FY2012, as opposed to their inclusion in the FY2011 levy?*

[3] The current ratio under the proposed budget is 56:44. Under the alternative approach proposed, the ratio would be 74:26

[4] Defined as only the salaries of staff primarily involved in a workstream.

9.3 Additional recovery of costs from industry

The Company has also been asked to assess whether there were any other areas where the Company could recover its costs directly from the industry, as opposed to the annual levy. Two items of cost recovery have been explored:

- The cost of facilitating rule change requests for the MPOC and VTC

- Additional recovery of our compliance cost from industry participants found in breach.

Rule change role for MPOC and VTC

Each Memorandum of Understanding with Maui Development Limited (MDL) and Vector, regarding the review of MPOC or VTC change requests, allows Gas Industry Co to charge the participant applying for a rule change for the Company's costs related to reviewing that request. However, Gas Industry Co has been reluctant to use this authority as it does not enable the recovery of its costs from the other participants who also benefit from the rule change. However, Gas Industry Co has now been asked to consider whether or not it should seek to recover its costs associated with MPOC/VTC rule changes from applicants, rather than through the annual levy.

An alternative to charging participants would be to charge each of MDL and Vector a retainer for Gas Industry Co services in reviewing code change requests, with a year-end wash up that could be carried over into the following financial year. The agreement of both transmission system owners (TSOs) would be needed to implement such an arrangement. The TSOs will in turn pass on the charges to shippers in similar proportions to the existing wholesale levy.

The FY2011 budget contains a forecast cost of $251,853 for rule changes and facilitation of industry evolution of its existing codes. If this was to be recovered directly from the industry, it would reduce the indicative Wholesale levy buy 0.25 cents/GJ. However, the indicative Retail levy would increase by $0.41/ICP because of the change that would occur in the allocation of overhead costs.

Q8:	*Do you agree that Gas Industry Co should recover its costs associated with MPOC/VTC outside of the levy regulations?*
Q9:	*If you agree with Q8, do you agree that Gas Industry Co should recover its costs associated with MPOC/VTC rule changes from applicants or from MDL and Vector?*

Additional recovery of compliance costs

The current policy for compliance costs is to recover through market fees only the direct external costs of the compliance regime (the Market Administrator, the Investigator, the Rulings Panel, and associated disbursements). A similar approach has been taken when seeking an order for costs in recent Ruling Panel hearings. Gas Industry Co have been asked to consider if the full direct internal costs of administering the compliance regime could be recovered in future proceedings. If this was undertaken in FY2011, the maximum amount that would have been recoverable is approximately $100,000. Experience with the compliance regime in FY2010 indicates our internal costs in relation to servicing these regulations is likely to become increasingly significant in future years. However, Gas Industry Co is wary of this approach.

The prime reason for originally limiting this recovery to direct external costs was the difficulty the Company would face in quantifying the amount of internal costs (probably salaries and disbursements such as printing) that could be attributed to the compliance process. This would be especially problematic when seeking cost recovery through an order for costs from the Ruling Panel in relation to a hearing because of the standard of proof to be met. Implementing such a policy would involve upgrading Gas Industry Co administrative systems to the standard required to meet an independent burden of proof criteria. It is doubtful if the ongoing complexity and use of resources in administering such a system would be of material benefit once the additional costs involved were taken into account.

Q10: Do you agree that Gas Industry Co should seek to recover its full internal costs associated with the compliance regime through orders for costs in relation to hearings?

Appendix A Recommended Format for Submissions

To assist Gas Industry Co in the orderly and efficient consideration of stakeholders' responses, a suggested format for submissions has been prepared. Respondents are also free to include other material in their responses.

Submission prepared by: (company name and contact)

QUESTION	COMMENT
Q1: Do you consider there to be any other items that should be included in the Company's intended work programme for FY2011?	
Q2: Do you consider there to be any items that should be excluded from the Company's intended work programme for FY2011?	
Q3: Do you have any questions on the calculation of the levy funding requirement for FY2011??	
Q4: Do you have any comment on the proposed levy for FY2011?	
Q5: Do you have any comment on regulatory amendments describe in section 8?	
Q6: Do you consider that GIC should alter its current method of defining direct costs and allocate more of its indirect costs to work streams?	

Q7: Do you support the inclusion of a portion of Gas Industry Co's indirect costs in market fees for FY2012, as opposed to their inclusion in the FY2011 levy?	
Q8: Do you agree that Gas Industry Co should recover its costs associated with MPOC/VTC outside the levy regulations?	
Q9: If you agree with Q8, do you agree that Gas industry Co should recover its costs associated with MPOC/VTC rule changes from applicants or MDL and Vector?	
Q10: Do you agree that Gas Industry Co should seek to recover its full internal costs associated with the compliance regime through orders for costs in relation to hearings?	