



Consultation on Rule 37 Determination under the Gas (Downstream Reconciliation) Rules 2008

Date issued: 15 September 2014
Submissions close: 26 September 2014





About Gas Industry Co.

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

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

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

Gas Industry Co's corporate strategy is to 'optimise the contribution of gas to New Zealand'.

Submissions close: 26 September 2014

Submit to: www.gasindustry.co.nz

Enquiries: Andrew Walker
04 472 1800

Contents

1	Introduction	6
1.1	Purpose	6
1.2	Submissions	6
<hr/>		
2	Rule 37 determination	7
2.1	Background	7
2.2	Past performance	8
2.3	Proposal	11
<hr/>		
	Appendix A Submissions template	14

1

Introduction

1.1 Purpose

Rule 37 of the Gas (Downstream Reconciliation) Rules 2008 (the Rules) requires Gas Industry Co to determine and publish the percentage of error for the accuracy of initial consumption information prior to the beginning of each gas year. The purpose of this paper is to consult on the accuracy threshold for the 2014/15 gas year (the 12 months beginning 1 October 2014).

The proposal for the 2014/15 gas year is to maintain the current threshold of $\pm 10\%$ for a fifth consecutive year.

1.2 Submissions

Feedback is sought from participants on the appropriate accuracy threshold for the 2014/15 gas year. The deadline for submissions is 5pm on Friday, 26th September 2014. This is a short-form consultation on the basis that the matters covered in the paper have been consulted on several times before and the proposal will maintain the status quo operation of the Rules.

Submissions can be made by logging on to the Gas Industry Co website, navigating to the Downstream Reconciliation work programme and uploading your submission in the Consultation section. All submissions will be published on the website after the closing date. Submitters should discuss any intended provision of confidential information with Gas Industry Co prior to uploading their submissions.

2

Rule 37 determination

2.1 Background

Each year Gas Industry Co is required to determine and publish an accuracy threshold, in the form of a permissible percentage of error, for the non-TOU consumption information submitted to the allocation agent for the initial allocation. For each gas gate, the aggregated consumption information in allocation groups three to six must, when compared with submissions for the final allocation, fall within the required percentage of error. This requirement is set out in rule 37 of the Rules. Table 1 shows the accuracy threshold for each year since the commencement of allocations under the Rules.

Table 1. Previous rule 37 accuracy thresholds

Gas year	Accuracy threshold
1 October 2008 to 30 September 2009	±15.0%
1 October 2009 to 30 September 2010	±12.5%
1 October 2010 to 30 September 2011	±10.0%
1 October 2011 to 30 September 2012	±10.0%
1 October 2012 to 30 September 2013	±10.0%
1 October 2013 to 30 September 2014	±10.0%

In making a determination, Gas Industry Co must have regard to the following matters:

- the primary aim of ensuring consumption information provided for initial allocation is as accurate as possible when compared with consumption information provided for final allocation;
- the extent to which retailers are able to comply with the percentage of error for the accuracy of consumption information provided for initial allocation;
- any expected costs that would be reasonably incurred by retailers to achieve compliance with the percentage of error for the accuracy of consumption information provided for initial allocation; and
- any other matter it considers relevant to its determination.

The 2014/15 gas year will be the seventh year of the operation of the reconciliation arrangements under the Rules. With the go-live of the new reconciliation arrangements there was scope for

improvements to be made. The threshold was therefore gradually tightened for the first three years, to provide a strong incentive to retailers to do all they reasonably can to improve estimation accuracy. Last year's determination maintained the threshold at $\pm 10\%$ on the basis that a further tightening was expected to lead to only a marginally greater level of accuracy, which would be outweighed by the burden created by a larger number of breaches.

Themes in the submissions on the 2013 consultation paper (which proposed maintaining the $\pm 10\%$ threshold) included:

- all submitters supported (or were not opposed to) maintaining the $\pm 10\%$ threshold;
- one submitter¹ noted that any further tightening of the percentage threshold would not incentivise improved accuracy and
- one submitter² suggested a GJ threshold to be used as well as a percentage threshold in order to decrease the number of non-material breaches, especially by retailers operating at gas gates where they have relatively few customers.

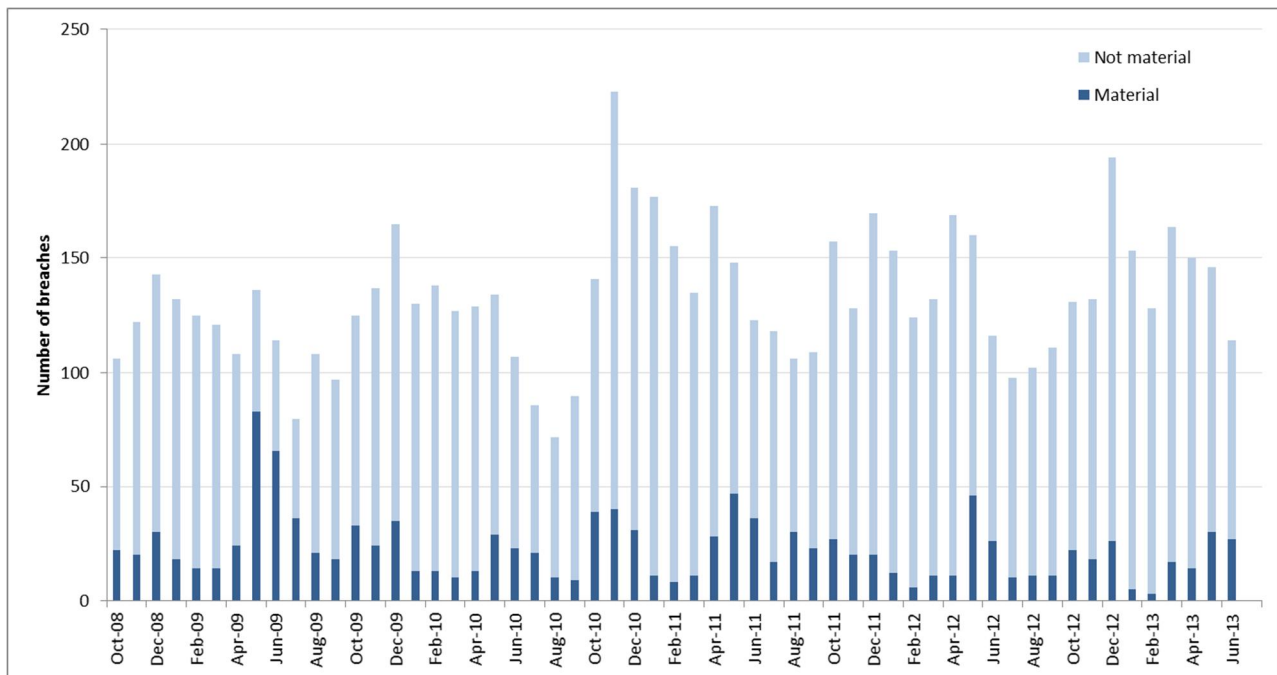
2.2 Past performance

In previous years, Gas Industry Co has provided a high-level analysis of the incidence of breaches to date. This breach analysis is repeated below, with the addition of information from the last 12 months of allocation data. **Error! Reference source not found.** shows the total number of breaches, with those found to be material represented by darker shading. Note that the percentage threshold for breaches was different in previous gas years as presented in Table 1. The materiality of the breaches has so far been determined by the application of a gigajoule threshold, that is, where the difference between the initial and the final submissions is greater than 200 GJ for a retailer at a gas gate, the breach is considered to raise a material issue.

¹ Vector Limited submission on Consultation on Rule 37 Determination, available [here](#)

² Mighty River Power submission on Consultation on Rule 37 Determination, available [here](#)

Chart 1. Total number of breaches of rule 37, October 2008 to July 2013



In the years commencing October 2008 and 2009, the accuracy thresholds were $\pm 15\%$ and $\pm 12.5\%$, respectively. The threshold narrowed to $\pm 10\%$ commencing October 2010, hence the higher overall level of breach activity from that point onwards. The incidence of material breaches did not see the same step change after October 2010 but instead displays a cyclical pattern with peaks around May-June and October-December.

The seasonal trend in the number of breaches is more visible in Chart 2 which separates breaches due to underestimation or overestimation. The pattern of underestimation going into winter and overestimation during early summer continues with noticeable spikes centred around the shoulder periods of May 2009, October 2010, May 2011, October 2011 and May 2012. The volumes associated with these breaches in gigajoules are shown in Chart 3.

Error! Reference source not found. gives the retailer level performance, showing the proportion of all gas gate submissions which fall inside and outside the accuracy threshold. The chart includes all data series since go-live so it does not give an indication of recent improvements. The differences in individual retailer's breach statistics highlight that market share, frequency of meter reading and target market all play a role in the ability to provide accurate initial submissions. For example, mass market retailers have higher numbers of breaches than retailers focusing more on industrial and commercial sector.

Chart 2. Breaches of positive and negative thresholds, October 2008 to July 2013

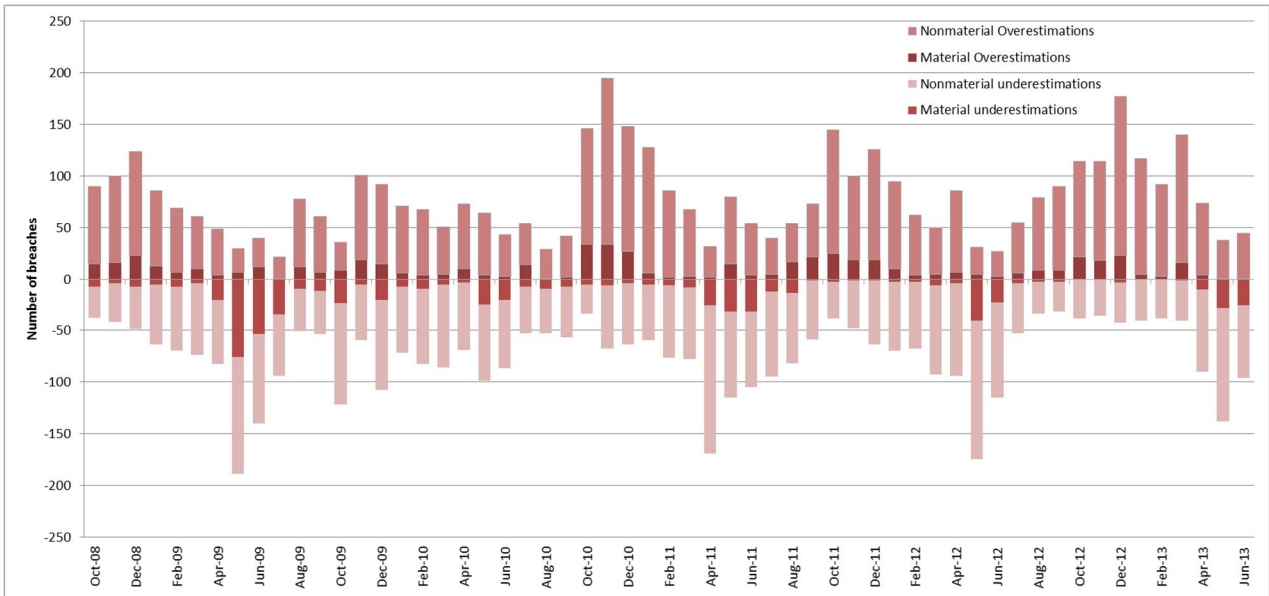


Chart 3. Volumes associated with material and nonmaterial breaches, October 2008 to July 2013

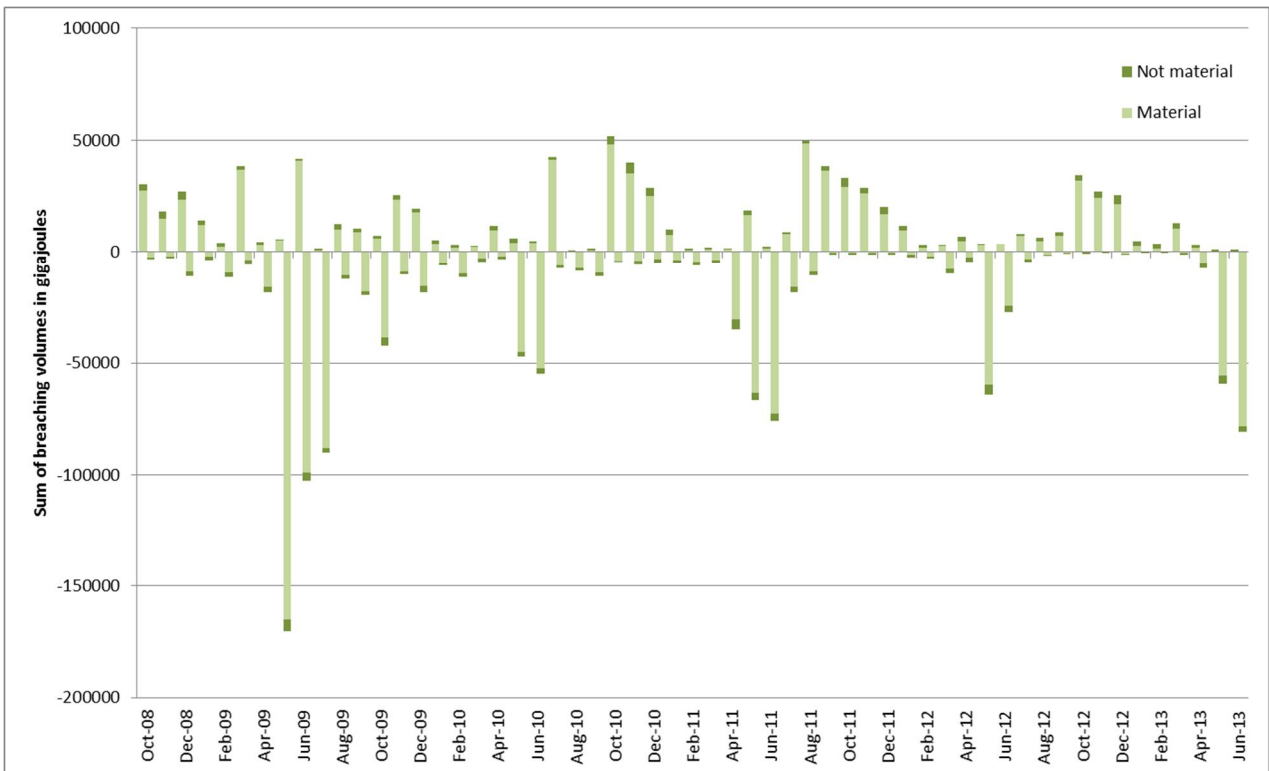
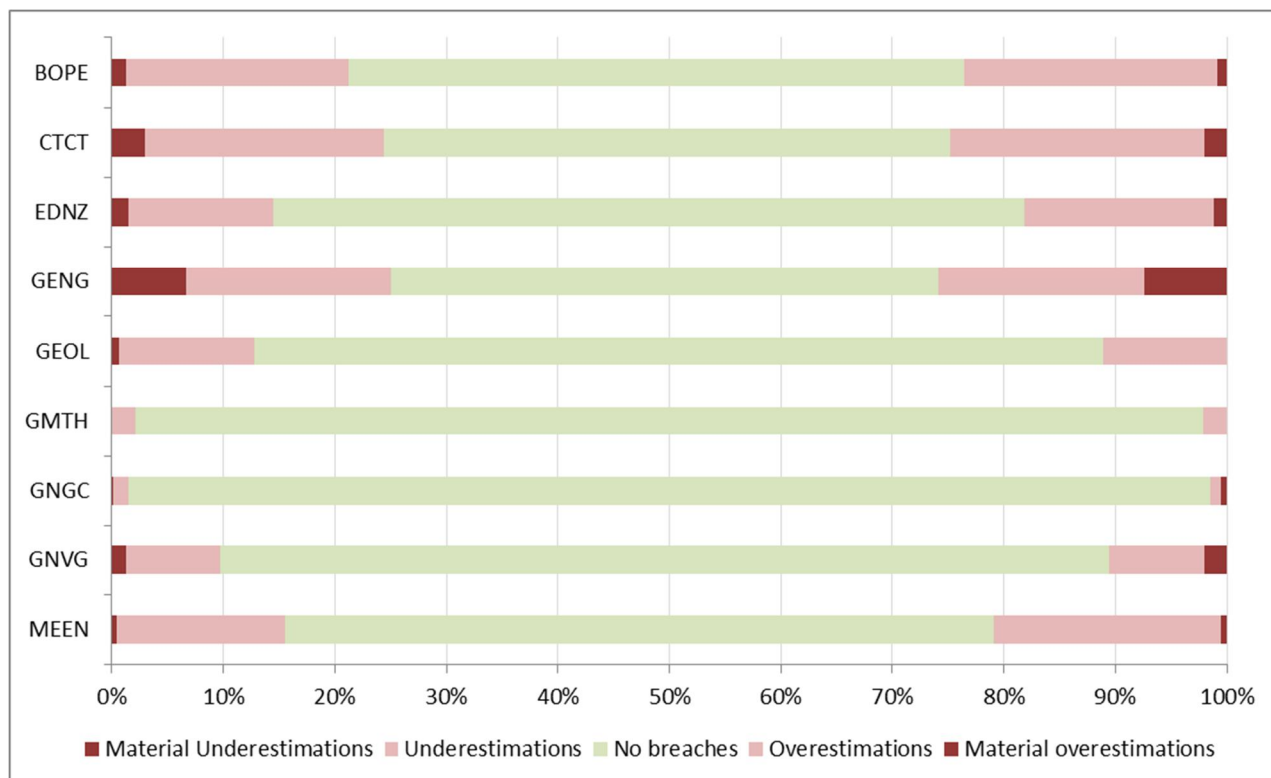


Chart 4. Proportion of retailer submissions which fall under, over or within the accuracy and materiality thresholds, October 2008 to July 2013



2.3 Proposal

Based on the analysis presented in this and the 2013 consultation papers and recognising the general intention of submissions on the earlier paper, Gas Industry Co is proposing to maintain the accuracy threshold at $\pm 10\%$ for a further year.

Gas Industry Co takes the following view against each of the matters it has to consider in determining the accuracy threshold:

Primary aim that consumption information is as accurate as possible

The intent of rule 37 is to ensure that initial submission accuracy is as accurate as possible, so as to mitigate the harm caused by under- and over-submissions. Analysis of available data suggests that, while retailers in general have improved in their forward estimations somewhat, they are still liable to mis-estimations during shoulder seasons and in times of unseasonal weather.

At the same time, Gas Industry Co understands that balancing and peaking pool charges have decreased over the past three years, so that the harm experienced due to inaccurate estimations is not as great as it was when the Rules were implemented.

Both of these factors suggest that $\pm 10\%$ is an appropriate threshold for the coming gas year.

Extent to which retailers are able to comply

Analysis of available data shows that, despite the tightening of the accuracy threshold on two occasions, there has only been a noticeable impact on general compliance with rule 37 after the threshold was tightened to $\pm 10\%$ in October 2010. Minor improvements have been made against the baseline, although given the small amount of actual data available (plus the lack of a baseline before rule 37 existed), the result is not statistically significant in terms of conclusions about changes in retailer accuracy.

It is clear from the pattern of material breaches and also from participant feedback that the factors which drive compliance are either unpredictable (in the case of domestic consumer response to temperature change) or involve significant cost (in the case of meter reading frequency).

Consideration of the extent to which retailers are able to comply also suggests that the accuracy threshold should remain at $\pm 10\%$ for the coming gas year.

Any expected costs to achieve compliance

Given the reported difficulty in forecasting gas demand, and the use of retrospective methodologies that involve calculating past average usage to determine forward estimates, it is not expected that further tightening will drive a step change in retailers' attempts to comply with the accuracy threshold. The data presented suggest that the most successful method of creating accurate submissions is to read meters more frequently. Given that balancing costs have trended downwards over the past couple of years, the benefit of increasing the frequency of meter reads for mass market retailers is not likely to offset the cost of doubling the number of meter reads. Gas Industry Co continues to investigate other approaches to the initial allocation in the hope of finding an alternative effective solution.

Any other relevant matters

Rule 37 breaches found material by the market administrator have previously been settled by the investigator in three batches. The settlements involved financial transactions that approximate compensation for the extra charges incurred as a result of over- or under-allocations at the initial stage due to breaching parties' estimation inaccuracies. Table 2 shows the magnitude of settlements that have occurred to date.

Table 2. Previous settlements of material rule 37 breaches

Consumption periods covered	Size of settlement
October 2008 to November 2009	\$380,000
December 2009 to March 2011	\$63,000
April 2011 to March 2012	\$76,000

The current proposal under discussion is for Gas Industry Co to use the same calculation methodology for the current set of breaches being considered (covering the period from April 2012 to May 2013) but to have the wash-up occur prior to the market administrator making its determination. The first draft of the payment calculations suggest a settlement in the order of \$40,000 to \$50,000.

Conclusion

Based on the above analysis, Gas Industry Co considers that the accuracy threshold should remain at 10% for the coming gas year.

Q1: *Do you agree with the proposal to maintain the rule 37 threshold at $\pm 10\%$ for the 2014/15 gas year?*

Appendix A Submissions template

Consultation on Rule 37 Determination under the Gas (Downstream Reconciliation) Rules 2008

Submission prepared by: (company name and contact)

QUESTION	COMMENT
Q1 Do you agree with the proposal to maintain the rule 37 threshold at $\pm 10\%$ for the gas year beginning 1 October 2014? If not, please provide your rationale.	