

STATEMENT OF INTENT 2017-2019

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STATEMENT OF INTENT 2017-2019

Gas Industry Company Limited (Gas Industry Co) was established in 2004 as the 'industry body' under Part 4A of the Gas Act 1992 (Gas Act).

This Statement of Intent has been prepared by Gas Industry Co to meet the requirements of sections 43ZQ to 43ZV of the Gas Act. Among other things, it sets the intended scope and objectives of Gas Industry Co's operations for the financial years ended 30 June 2017 to 2019 (inclusive), and provides information about the Company and its operating environment. The Work Programme described in this Statement of Intent is designed to meet the governance objectives set out in section 43ZN of the Gas Act, with regard also to the objectives and outcomes of the April 2008 Government Policy Statement on Gas Governance (GPS), as well as the wider strategic objectives of the Company.

The Company's role includes:

- » developing arrangements, including regulations where appropriate, which improve:
 - the operation of gas markets;
 - access to infrastructure; and
 - consumer outcomes;
- » developing 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
- » overseeing compliance with, and reviewing 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 current state and performance of the New Zealand gas industry.

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



Rt Hon James B. Bolger, ONZ
CHAIR



Robin Hill
DEPUTY CHAIR

June 2016

FOREWORD

Gas Industry Co's strategy and Work Programme set out in this Statement of Intent have been prepared in consultation with the industry, and in the context of considerable changes occurring in the downstream gas markets.

In the past year we have seen the closure of two large gas-fired power stations, at Otahuhu and Southdown, as renewable generation strengthens and the move away from thermal baseload to peaker generation accelerates.

The sales of the Vector transmission pipelines, and the Maui pipeline to First Gas have brought New Zealand's two open access transmission systems under single ownership for the first time. This will significantly influence Gas Industry Co's work on transmission access arrangements. In particular, consolidation of ownership has potential efficiency benefits in the area of transmission code convergence, which is a central focus for Gas Industry Co's Gas Transmission Work Programme. In this regard, Gas Industry Co will continue to work closely with other regulatory agencies, in particular the Commerce Commission, with interests in gas pipeline operations and performance.

More broadly, exploration production activity in New Zealand has not escaped the effects of the substantial global downturn in oil prices, which is affecting investment in the upstream sector. While Gas Industry Co is not directly involved in upstream work, the success or otherwise of exploration efforts flows into the downstream sector, with a specific influence on supply and demand and the adequacy of downstream infrastructure. A key role for Gas Industry Co lies in supporting ongoing investment by ensuring the downstream gas market is well-governed and remains a good 'sink' for future gas finds.

Notwithstanding what is happening in the industry, Gas Industry Co's activities remain firmly directed at addressing the objectives and outcomes for the downstream gas sector as set out in the Gas Act and GPS.

Central to our planning process is our statutory obligation to develop and administer industry arrangements that ensure gas is delivered to consumers in a safe, efficient, fair, reliable and environmentally sustainable manner, supported by our over-arching corporate strategy to *optimise the contribution of gas to New Zealand*.

The reference to 'sustainable' arrangements links Gas Industry Co's work to work led by the New Zealand Government to address climate change issues and transition to a lower carbon future.

Nevertheless, gas continues to play an important role in New Zealand's primary energy mix and to the economy generally. As New Zealand pursues its goal of 90 percent renewable electricity generation by 2025 (currently 80 percent), gas is still seen as a complementary form of energy, especially for weather-sensitive renewables, and as an integral component of smart infrastructure network systems of the future.

Gas remains an important energy option for consumers and has a particular 'heavy lifting' strength for industrial heating loads. And gas continues to provide space heating, water heating and cooking for around a quarter of a million New Zealand homes, in many cases with a lower carbon footprint than alternatives.

Gas Industry Co's strategy seeks to lead forward thinking, in conjunction with industry stakeholders, to anticipate future opportunities and challenges within the industry.

In this respect we continue to generate a range of documents and other activities that enrich understanding of the industry and its contribution to the economy, as well as assist participants with their planning and to provide our assessment of how the industry is performing.

This Statement of Intent sets out the Company's detailed Work Programme for the financial year ended 30 June 2017 (FY2017) with indicative activities for the subsequent two years in the three-year planning cycle. Our Work Programme and the associated budget for FY2017 has been subject to broad consultation with industry stakeholders and is generally supported by them.

Industry input into our Work Programme and budgeting process has been robust and successfully underpins the co-regulatory model for the downstream gas sector.

Gas Industry Co continues to closely manage its costs and is able to deliver the FY2017 Work Programme at essentially the same cost level as in FY2016. The Work Programme itself comprises the continuation of committed deliverables in the administration of existing governance arrangements and a focus on progressing 'live' workstreams towards a successful conclusion. There is no substantial new work envisaged in the immediate future.

Overall, the downstream gas sector in New Zealand is well advanced in meeting consumer needs and Government policy objectives for the sector. We are confident our Work Programme will continue to support a well-functioning sector for the benefit of consumers and other participants.



Rt Hon James B. Bolger, ONZ
CHAIR

June 2016



Steve Bielby
CHIEF EXECUTIVE

“Ensuring the downstream gas market is well-governed and remains a good ‘sink’ for future gas finds”

WORK PROGRAMME PRIORITIES

Figure 1 sets out the main elements of Gas Industry Co's Work Programme objectives and the activities designed to meet those objectives with budget estimates for FY2017, and indicatively for the following two financial years.

The Work Programme structure is designed to fulfil our statutory role through efficient governance arrangements, progressing new or committed/ongoing projects that are important to industry and other stakeholders, and facilitating forward-looking discussion on future strategic issues.

EFFICIENT GOVERNANCE ARRANGEMENTS

- » administer existing rules and regulations, notably:
 - Gas (Switching Arrangements) Rules 2008 (Switching Rules)
 - Gas (Downstream Reconciliation) Rules 2008 (Reconciliation Rules)
 - Gas Governance (Critical Contingency Management) Regulations 2008 (CCM Regulations)
 - Gas Governance (Compliance Regulations) 2008 (Compliance Regulations);
- » administer non-regulated governance arrangements, including:
 - Retail Gas Contracts Oversight Scheme
 - Gas Distribution Contracts Oversight Scheme;
- » review governance arrangements to ensure they remain fit for purpose and recommend changes where improvements can be made efficiently;
- » monitor the performance of industry participants and encourage, or enforce, compliance; and
- » monitor and report on metrics arising from these regulatory processes to enhance transparency and foster a well-informed market.

NEW OR COMMITTED/ ONGOING PROJECTS

There are a number of projects to which Gas Industry Co was committed prior to the FY2017 Work Programme. These are regarded as important by stakeholders and Gas Industry Co, or have been requested by the Minister, and are being undertaken to resolve priority issues within the downstream industry:

- » supporting the day-after-delivery (D+1) pilot scheme that has been put in place to provide retailers with the information they need to operate successfully under market-based balancing (MBB) regime;
- » based on the outcomes of the D+1 pilot, moving to codify the D+1 allocation process into the Downstream Reconciliation Rules and associated changes to the Allocation Agent's role and system;
- » completing the vision for transmission code convergence and moving on to bringing about a converged set of arrangements so as to eliminate current inefficiencies;
- » monitoring the recent changes to transmission pipeline balancing arrangements and, if necessary, identifying any necessary changes;
- » working through tender arrangements for the Gas Registry operator role beyond February 2018; and
- » further improving downstream reconciliation processes.

FUTURE STRATEGIC ISSUES

As part of its Corporate Strategy to provide leadership for the gas industry and the New Zealand gas story, Gas Industry Co generates ideas and information that encourage stakeholder discussion on the future shape and role of the gas industry in New Zealand.

This work builds on past reports commissioned by Gas Industry Co which look at consumer energy options, opportunities and challenges of commercialising a large new gas find, supply and demand, and the potential for demand management as a tool for managing transmission pipeline congestion. The Work Programme provides for an ongoing future focus, involving updating and expanding on these studies.

STRATEGIC OBJECTIVE 1

PROMOTE EFFICIENT, COMPETITIVE AND CONFIDENT GAS MARKETS

COMPRISING:

- » Retail Contracts Oversight Scheme
- » Gas Distribution Contracts Oversight Scheme
- » Retailer insolvency
- » Gas quality
- » Regulation and rule changes
- » Gas measurement
- » Information gathering protocol

\$804,669

STRATEGIC OBJECTIVE 2

FACILITATE EFFICIENT USE OF, AND INVESTMENT IN, GAS INFRASTRUCTURE

COMPRISING:

- » Transmission access and pricing
- » Supply/demand model
- » Wholesale market
- » Transmission pipeline balancing
- » Transmission code changes and appeals
- » Transmission pipeline interconnection
- » Gas transmission security and reliability

\$1,240,384

STRATEGIC OBJECTIVE 3

DELIVER EFFECTIVELY ON GAS INDUSTRY CO'S ACCOUNTABILITIES AS THE GAS INDUSTRY BODY

COMPRISING:

- » Downstream reconciliation
- » Switching and registry
- » Critical contingency management
- » Compliance and enforcement
- » Statement of Intent and Annual Report

\$3,191,076

STRATEGIC OBJECTIVE 4

DEVELOP AND COMMUNICATE THE ROLE OF GAS IN MEETING NEW ZEALAND'S ENERGY NEEDS

COMPRISING:

- » New Zealand Gas Story
- » Other reporting

\$165,931

CONSULTATION PROCESS

Consultation with industry stakeholders on Gas Industry Co's intended Work Programme and budget requirements commences with a Co-Regulatory Forum, held in November of the year preceding the financial year for which they are to apply. The process leads to the development of a Statement of Intent for the period ahead, and a recommendation to the Minister¹ for levy funding through regulations (Levy Recommendation) for the first financial year in the prospective three-year period covered by the Statement of Intent.

The Statement of Intent and Levy Recommendation provide the basis for equipping Gas Industry Co to deliver robust outcomes for gas consumers and the wider industry, and to otherwise fulfil its mandate as the industry body. They are presented to the Minister in March each year.

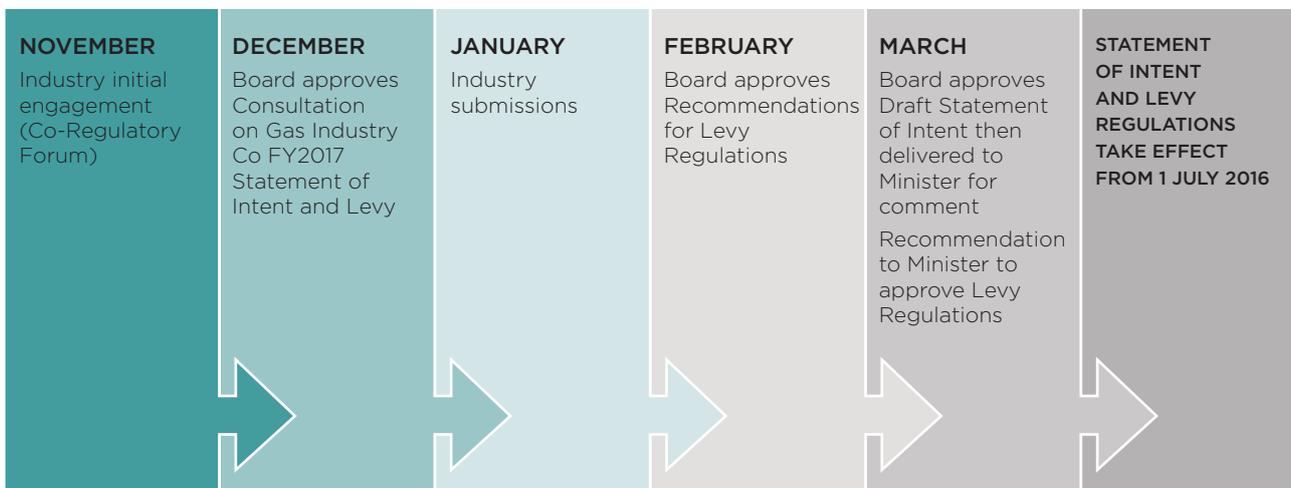
These two documents are developed after consulting with stakeholders on strategic priorities. The Work Programme and budget addressing those priorities are detailed in a Consultation Paper, normally issued in December of the year preceding the financial year to which they are to apply. Submissions on the Consultation Paper are taken into account prior to the Board finalising the Levy Recommendation to the Minister. Submitters generally supported the Work Programme and budget proposed in the document *Consultation on Gas Industry Co FY2017 Statement of Intent and Levy*².

Figure 2 sets out the consultation and approval processes leading to the annual promulgation of Levy Regulations.

^{1/} 'Minister' is defined in the Gas Act as the Minister with responsibility for administration of the Gas Act. As at the date of this Statement of Intent, the ministerial warrant for Gas Industry Co was held by the Minister of Energy and Resources. References to 'Minister' should read as references to the Minister of Energy and Resources, unless the context indicates otherwise.

^{2/} Available with submissions and Gas Industry Co responses on the website: www.gasindustry.co.nz

FIGURE 2 - CONSULTATION AND LEVY-SETTING PROCESS



INDUSTRY PERFORMANCE

Gas Industry Co's Work Programme supports competitive activity within the downstream gas markets. Since the introduction of formal governance arrangements in 2009, industry performance indicators in the key areas of consumer switching, downstream reconciliation, and compliance have improved substantially. Together, they reflect a healthy downstream gas market, and include:

RETAILERS

An increasing number of retailers. There are now 11 retail gas brands owned by nine different retail companies.

CUSTOMERS

Nearly 99 percent of gas customers are connected to a gate where eight or more retailers trade, demonstrating that gas retailing is generally competitive throughout the North Island.

MARKET CONCENTRATION

Market concentration, as measured by the Herfindahl-Herschman Index (HHI) has decreased significantly in all regions since the commencement of the formal switching regime in 2009 as new retailers increase market share and incumbent retailers' share has declined.

SWITCHING RATE

The annual rate of switching by gas consumers for the past 12 months is 19.6 percent compared with 22 percent in the electricity sector. Gas consumer switching rates have been over 17 percent for the past two years.

SWITCHING LEVEL

In FY2015 49,743 gas consumers changed retailer. Fifty-six percent of residential consumers, 64 percent of small commercial customers and 72 percent of large commercial sites have switched retailer at least once in the past five years.

AVERAGE SWITCHING TIME

The average time for a switch to be completed is 4.4 business days, compared with weeks or months before the Switching Rules took effect in 2009.

UFG

Average annual unaccounted-for-gas (UFG) at shared gates has halved to about 1.0 percent of delivered gas volumes since 2009.

EMERGENCY MANAGEMENT

More efficient and effective critical contingency management arrangements.

COMPLIANCE ACTIVITY

Reduced compliance activity as participants adjust to the requirements of new rules and regulations.

These indicators are discussed under 'Industry Performance', on page 24.

OPERATING ENVIRONMENT

Gas Industry Co's Work Programme is directly influenced by the industry structure, the legislative and policy framework, and its own corporate strategy. Together these form the Company's operating environment.

INDUSTRY CONTEXT

Natural gas makes a substantial contribution to New Zealand's economy and quality of life. It is a vital input for some of the country's largest industries, including dairy, steel, forestry and petrochemicals; and it provides energy to approximately 268,000 industrial, commercial and residential consumers.

Natural gas has a wide range of applications, from cooking and heating in homes, to providing energy for a variety of businesses and community amenities, as well as process heat for large industries.

Through thermal power plants, it has an important role in supporting electricity supply security.

Over the past decade, as production from the formerly predominant Maui field has declined, the New Zealand gas market has transitioned to sourcing gas from multiple smaller fields. This has significantly changed the market's dynamics, with a marked increase in the number of participants at all levels, and greater complexity in arrangements for transporting gas and selling it at the wholesale and retail levels.

The gas industry comprises a number of interdependent segments: exploration and production, processing, and wholesale and retail markets. These segments are connected via the high pressure gas transmission systems and local distribution networks.

Natural gas is available only in the North Island. Gas in the form of liquefied petroleum gas (LPG) is available in the North and South Islands in bulk and in bottles. In parts of the South Island LPG is also supplied through small reticulated LPG networks.

LEGISLATIVE AND POLICY FRAMEWORK

Since 2004, the gas industry downstream of the exploration and production sector has been governed by a unique co-regulatory model. As the industry body, Gas Industry Co facilitates the nexus between Government and industry to deliver improved governance arrangements for participants and consumers in gas markets.

Gas Industry Co's regulatory oversight encompasses the natural gas wholesale and retail markets, processing facilities, and the transmission and distribution sectors of the industry (see Figure 3, Gas Industry Structure). It does not include the upstream exploration and production sector, where the Ministry of Business, Innovation and Employment (MBIE) has regulatory and policy oversight through the Crown Minerals Act. Gas Industry Co's jurisdiction also covers aspects of the LPG market. We continue to monitor those, but there are no gas governance arrangements administered by Gas Industry Co and at this time we do not see a need for a dedicated LPG workstream.

The Gas Act empowers Gas Industry Co to make recommendations to the Minister on certain matters set out in the Gas Act, having regard to the objectives for the industry body in the Gas Act and the objectives and outcomes of the GPS.

The Gas Act specifies that the industry body's principal objective in recommending regulations is to ensure that gas is delivered to existing and new customers in a safe, efficient and reliable manner. The GPS adds to that principal objective consideration of fairness and environmental sustainability, and makes that an objective for the whole industry.

One aspect of the principal statutory objective is that formal gas governance arrangements ensure that 'gas is delivered to existing and new customers in a *safe*... manner'. Gas Industry Co does not have powers and functions directed to safety per se, but it is required to ensure that gas governance arrangements it proposes are 'consistent with the Government's gas safety regime'. It does this by, where appropriate, scrutinising potential safety implications of proposed gas governance arrangements.

The Government's gas safety regime is principally administered by WorkSafe New Zealand, and incorporates safety of gas appliances, standards for gas pipelines, and the occupational licensing system for gasfitters³.

OTHER OBJECTIVES SPECIFIED BY THE GAS ACT FOR THE INDUSTRY BODY IN RECOMMENDING REGULATIONS INCLUDE:

- » the facilitation and promotion of the ongoing supply of gas to meet New Zealand's energy needs, by providing access to essential infrastructure and competitive market arrangements;
- » barriers to competition are minimised;
- » incentives for investment in gas processing facilities, transmission, and distribution are maintained or enhanced;
- » delivered gas costs and prices are subject to sustained downward pressure;
- » risks relating to security of supply, including transport arrangements, are properly and efficiently managed by all parties; and
- » consistency with the Government's gas safety regime is maintained.

^{3/} A more detailed description of the gas safety regime and Gas Industry Co's relationships with these other agencies can be found in Gas Industry Co's comprehensive review of the industry: *The New Zealand Gas Story* on the Company's website www.gasindustry.co.nz.

ADDITIONAL OBJECTIVES FOR GAS INDUSTRY CO AND THE GAS INDUSTRY ARE SET OUT IN THE GPS AND INCLUDE:

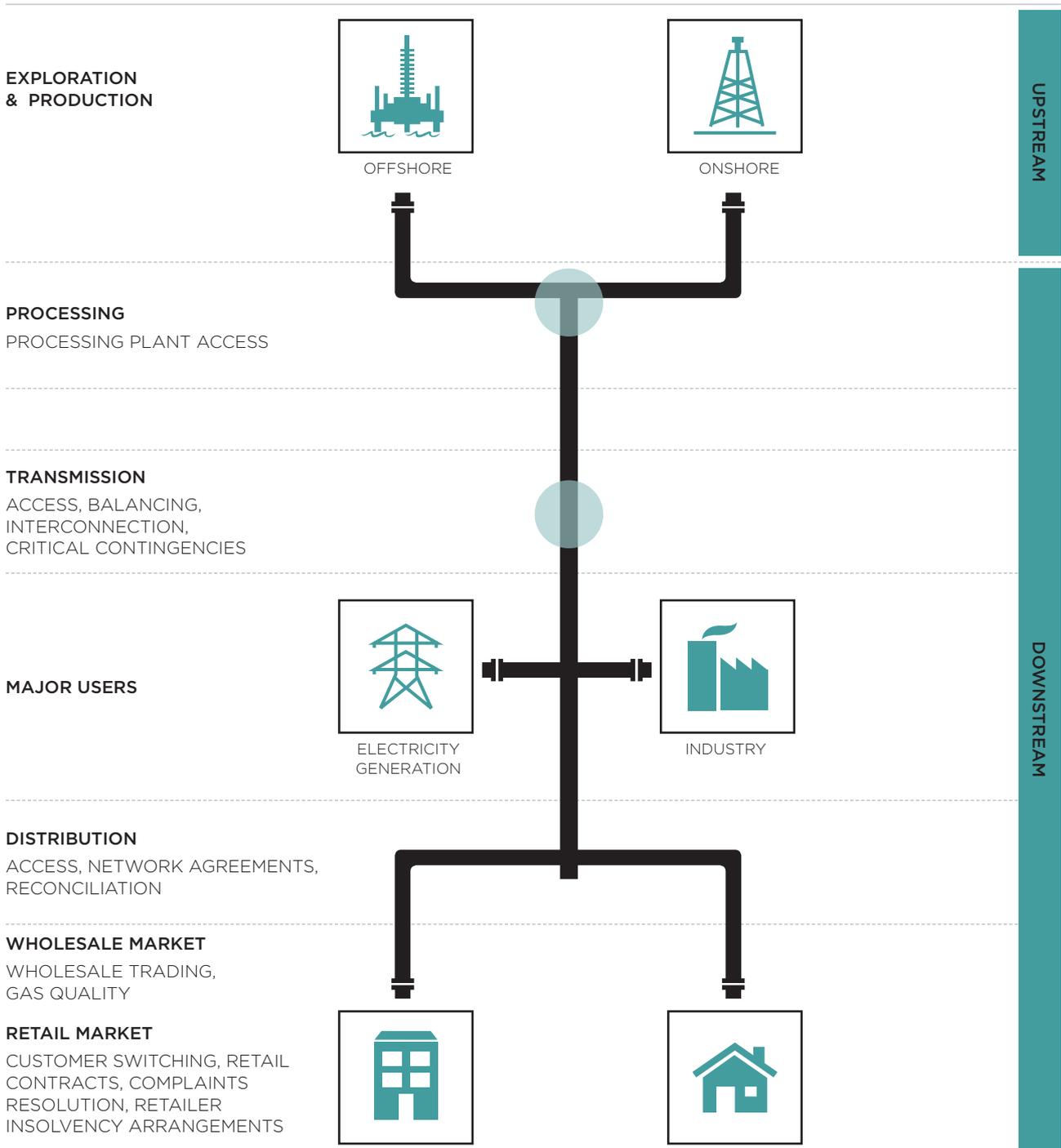
- » energy and other resources used to deliver gas to consumers are used efficiently;
- » competition is facilitated in upstream and downstream gas markets by minimising barriers to access to essential infrastructure to the long-term benefit of end-users;
- » the full costs of producing and transporting gas are signalled to consumers;
- » the quality of gas services, where those services include a trade-off between quality and price, as far as possible, reflect end-users' preferences; and
- » the gas sector contributes to the Government's climate change objectives as set out in the New Zealand Energy Strategy, or any other document the Minister may specify from time to time, by minimising gas losses and promoting demand-side management and energy efficiency.

The Minister has statutory powers to make rules or to recommend regulations on a wide range of gas governance matters. Under the co-regulatory model, the industry body advises the Minister on the exercise of many of these powers and must follow prescribed procedures before making a recommendation. The procedures include requirements for consultation with affected stakeholders, and an obligation to assess the costs and benefits associated with any recommendation.

When developing advice on governance arrangements, Gas Industry Co must consider all reasonably practicable options, including non-regulated options that achieve the same outcome.

Existing arrangements are monitored for their ongoing effectiveness and relevance, and refined as necessary.

FIGURE 3 - GAS INDUSTRY STRUCTURE



GAS INDUSTRY CO CORPORATE STRATEGY

Consistent with the legislative and policy framework described above, Gas Industry Co's Board has set a Corporate Strategy that assists in the delivery of its statutory role. Supporting objectives frame the Work Programme set out for FY2017, and, indicatively, the following two years.

STRATEGIC GOAL:

Optimise the contribution of gas to New Zealand

Gas has made a key contribution to New Zealand since the development of the natural gas industry in the 1960s. There is an important future role for gas, particularly in terms of providing electricity supply security and supporting the New Zealand economy, all consistent with environmental sustainability goals. However, there is a range of scenarios as to future supply and demand. The challenge, in line with Government energy policy, is how New Zealand can make the most of its gas resources, for the benefit of all New Zealanders.

PURPOSE:

Provide effective governance and leadership for the gas industry

The gas industry is complex and ever-changing. It is dependent on a range of players from upstream explorers and producers through to consumers, and on competitive markets and ongoing investment at all stages. Gas Industry Co will be a leader, building on its statutory role as the industry body.

OBJECTIVES:

- » promote efficient, competitive, and confident gas markets;
- » facilitate efficient use of, and investment in, gas infrastructure;
- » deliver effectively on Gas Industry Co's accountabilities as the gas industry body; and
- » develop and communicate the role of gas in meeting New Zealand's energy needs.

In pursuing its strategic goal, purpose and objectives, Gas Industry Co conducts itself in accordance with the following key principles:

- » fairness;
- » independence;
- » openness and transparency;
- » impartiality; and
- » evidence-based decision-making.

GAS INDUSTRY CO GOVERNANCE

Gas Industry Co is owned by industry participant shareholders and is incorporated as a company under the Companies Act 1993. Strategic oversight of the Company is provided by the Board of seven Directors, all elected by the shareholders. Four Directors, including the Chairman, are independent (having no material or financial interest in an industry participant), and three are industry-associated Directors (usually senior executives of industry participants).

The Board normally meets on up to 10 scheduled occasions each year and will hold unscheduled meetings from time to time to consider matters requiring immediate attention. The Board has one standing committee, the Independent Directors' Committee, comprising the four Independent Directors. The Committee addresses matters where the industry-associated Directors have potential or actual conflicts of interest.

WORK PROGRAMME FY2017 & INDICATIVE ACTIVITIES FY2018-19

This section outlines the scope of Gas Industry Co's operations for the financial years ended 30 June 2017 to 2019 inclusive.

The FY2017 Work Programme has been developed having regard to the Gas Act and GPS objectives and outcomes for the gas industry, Gas Industry Co's statutory accountabilities under existing governance arrangements, and reporting requirements under the Gas Act and Companies Act. The multi-year scope of the Statement of Intent, with a focus on the first year of the three-year period and indicative activity in the subsequent years, reflects the requirement for Gas Industry Co's funding to be approved by regulation

each year, as well as the changing nature of the industry and the Company's co-regulatory role. Further, it recognises that policy development requires comprehensive consultation which provides the opportunity for continuous improvements in policy thinking, and consequently the Work Programme, year-on-year.

The Work Programme is substantially in the form consulted on with stakeholders, and which was largely supported in submissions. The submissions themselves, and the Company's Analysis of Submissions can be found on Gas Industry Co's website www.gasindustry.co.nz.

STRATEGIC OBJECTIVE 1

PROMOTE EFFICIENT, COMPETITIVE AND CONFIDENT GAS MARKETS

RETAIL GAS CONTRACTS OVERSIGHT SCHEME (RETAIL SCHEME)

In 2010, Gas Industry Co established the Retail Scheme to assess retailers' posted contracts for residential and small commercial/industrial consumers against a series of benchmarks consistent with satisfactory customer expectations and outcomes. Reviews are undertaken by an Independent Assessor with the most recent full review in 2015 having shown 'substantial' compliance.

FORECAST ACTIVITIES FY2017-19

- (a) Review retailers' contracts on an exceptions basis (i.e. new entrants and changed contracts).
- (b) Publish compliance levels for individual retailers by exception.
- (c) Conduct a full review in FY2018.
- (d) Provide additional information to assist new entrant retailers to understand their obligations and governance processes.

GAS DISTRIBUTION CONTRACTS OVERSIGHT SCHEME (DISTRIBUTION SCHEME)

In 2012, Gas Industry Co established the Distribution Scheme in which gas distributors' contracts with gas retailers are assessed against a set of distribution principles. Over recent years, distributors have developed new agreements in consultation with their customers. The second assessment by an Independent Assessor in FY2014 found that the contracts offered by distributors exhibited 'substantial' alignment with the distribution principles. Checks with retailers and distributors in FY2015 and FY2016 identified that incremental changes continue to be made. In addition,

the practice is to make those incremental changes available to retailers that have executed earlier versions of the distribution contracts.

FORECAST ACTIVITIES FY2017-19

- (a) Continue to assess progress with executing new distribution contracts consistent with the Distribution Scheme principles.
- (b) Review the Distribution Scheme, consider any changes or other actions required, and report.
- (c) In FY2017, undertake preliminary work seeking the views of retailers and network owners about whether currently 'closed' LPG reticulated networks should be available to other parties under open access arrangements.

RETAILER INSOLVENCY

Following a request from the Minister, this workstream was formed to consider the market issues created when a gas retailer becomes insolvent. The Minister accepted the Company's advice that the best solution is an agile approach that would see a recommendation for urgent regulations, as and when required, and tailored to the specific situation. Gas Industry Co consulted on drafting instructions in FY2015 and issued its *Final Decision Paper – Framework for Gas Retailer Insolvency Arrangements* in the same year. With the framework set, it is not expected that any routine activity will be required in FY2017 beyond that already provided for within the audits under the Switching Rules.

CONTINGENT ACTIVITIES FY2017-19

- (a) Implement the new retailer insolvency arrangements as necessary in the unlikely event of a retailer insolvency.

GAS QUALITY

This workstream was developed in response to industry participant and large end-user concerns about the responsibility and liability for gas quality in New Zealand. Some participants believe responsibilities are unclear, or not well aligned with liabilities. In FY2015, Gas Industry Co published *Gas Quality Requirements and Procedures*, a document aimed at clarifying current arrangements and making them accessible.

FORECAST ACTIVITIES FY2017-19

- (a) Oversee industry-led work on gas quality.
- (b) Determine actions to address any remaining gas quality issues.
- (c) Update the Requirements and Procedures document as required.

REGULATION AND RULE CHANGES

The objective of this workstream is to ensure efficient, effective regulatory arrangements.

A trial of a D+1 methodology commenced during FY2016, and the nature of further work will be determined once the outcome of this pilot scheme is known. FY2017 will involve an intensive period of reviewing aspects of the daily allocation process and developing improvements, including the provision of tools to assist shippers to better manage their daily balancing positions.

FORECAST ACTIVITIES FY2017-19

- (a) Consider any refinements to the D+1 methodology identified under the pilot scheme.
- (b) If the pilot scheme is successful, move to the implementation phase, including:
 - issue a Statement of Proposal proposing amendments to the Downstream Reconciliation Rules.
 - subject to submissions, make a recommendation to the Minister to amend the Downstream Reconciliation Rules.
 - subject to Ministerial approval, develop, test and implement the supporting systems.

GAS MEASUREMENT

In FY2016, Gas Industry Co proposed a high-level review of current contracting arrangements between metering equipment providers and retailers, and to consider any implications associated with the introduction of smart gas metering technology.

Accordingly, the need for any work in this area in FY2017 will depend on the conclusions from the FY2016 work, whether that work identifies any issues that need to be addressed, and the relative urgency of those.

FORECAST ACTIVITIES FY2017-19

- (a) Develop any future activity required in light of the findings from the initial review, which was ongoing in FY2016.

INFORMATION GATHERING

In 2012, Gas Industry Co established an *Information Gathering Protocol* (Protocol) as an industry arrangement, instead of a formal regulated process as initially proposed. Various information requests to industry participants since then have generally received a positive response. In particular, the good progress on the D+1 workstream reflects a willingness by allocation participants to provide the information required. An exception has been a less than full response to Gas Industry Co's request for information needed to analyse the circumstances surrounding a potential critical contingency event in April 2015. Gas Industry Co subsequently reported that it would review the effectiveness of the voluntary Protocol.

Subsequently, Gas Industry Co has made information requests to transmission system owners and the wholesale gas market operator for information that would enable Gas Industry Co to monitor the development of MBB arrangements, introduced on 1 October 2015, and to undertake a post-implementation review of MBB in FY2017. This work is aimed at ensuring balancing arrangements are efficient and fit for purpose.

Other workstreams that are likely to involve requests for information are transmission access and pricing, and transmission security and reliability.

Gas Industry Co is concerned to ensure it is prepared for the possibility that required information may not be forthcoming and that it is positioned to make a recommendation to the Minister for appropriate regulations requiring participants to provide relevant information.

FORECAST ACTIVITIES FY2017-19

- (a) If required due to non-compliance with the Protocol, consult on regulations for the mandatory supply of information by participants to inform relevant issues analysed by Gas Industry Co.
- (b) Subject to the outcome of consultation, make a recommendation to the Minister for regulations for the provision of information.

STRATEGIC OBJECTIVE 2

FACILITATE EFFICIENT USE OF, AND INVESTMENT IN, GAS INFRASTRUCTURE

TRANSMISSION ACCESS AND PRICING

The objective of this workstream is to ensure that transmission pipeline access arrangements transparently provide for the efficient utilisation of physical capacity and effectively signal any need for efficient investment in additional capacity.

During FY2015, Gas Industry Co consulted on a further options paper, *Transmission Access: Options for Improvement Paper 2*, and, after considering submissions concluded that work on a vision for converged transmission arrangements would be a valuable next step towards achieving improved gas transmission capacity access arrangements.

FORECAST ACTIVITIES FY2017-19

- (a) Complete work on developing an industry vision.
- (b) Move to detailed design, consultation and implementation of the agreed vision.

SUPPLY/DEMAND MODEL

As part of its Gas Transmission Work Programme work, Gas Industry Co commissioned New Zealand's first dedicated study of future gas supply and demand. An update, including a toolset for stakeholders to model their own scenarios, was published in FY2015. This study has been well received by industry stakeholders as a valuable information resource for their own planning purposes. Accordingly, Gas Industry Co sees value in updating the study and its related model every two years.

FORECAST ACTIVITIES FY2017-19

- (a) Publish an updated study and model in FY2017.
- (b) Review and update the supply/demand model biannually.

WHOLESALE MARKET

The emsTradepoint (eTp) wholesale gas market commenced in 2013 and has achieved increases in both membership and traded volumes.

Gas Industry Co is pleased with the progress of this industry-led initiative, which represents a more transparent market mechanism while contributing to the delivery of a GPS outcome for 'efficient arrangements for the short-term trading of gas'.

Gas Industry Co will continue to monitor activity and developments in the wholesale spot market with a particular focus on volumes and prices associated with its role in transmission balancing transactions.

FORECAST ACTIVITIES FY2017-19

- (a) Monitor wholesale market activity and developments, particularly in relation to MBB.
- (b) Ensure that market information is provided to Gas Industry Co in a timely fashion to support this monitoring.

TRANSMISSION PIPELINE BALANCING

Immediately following the introduction of MBB in October 2015, a significant reduction in non-balancing-related trading on the eTp platform raised concerns among a number of participants. This reflected shippers being unaware of their daily balancing positions, and a flaw in the default rule applied by the Maui pipeline owner, Maui Development Limited (MDL).

The first matter is being addressed through the D+1 day-after-delivery process currently being trialed, and the second matter has been resolved by a change to the default rule by MDL.

FORECAST ACTIVITIES FY2017-19

- (a) Continue to monitor MBB.
- (b) Undertake a post-implementation review of MBB (subject to obtaining the necessary information).
- (c) Consider appropriate mechanisms for resolving any issues identified by the post-implementation review.

TRANSMISSION CODE CHANGES AND APPEALS

Under a Memorandum of Understanding with the owner of the Maui pipeline, Gas Industry Co has a role in processing Maui Pipeline Operating Code (MPOC) change requests on an as-required basis. Gas Industry Co is also able to make submissions on change requests under the Vector Transmission Code (VTC).

FORECAST ACTIVITIES FY2017-19

- (a) Process MPOC change requests as required.
- (b) Submit on VTC change requests as appropriate.

TRANSMISSION PIPELINE INTERCONNECTION

Gas Industry Co has established *Interconnection Guidelines* (Guidelines) setting out expectations for transmission system owners' policies and procedures for third parties connecting to their pipelines to either inject or extract gas. Previous independent reviews commissioned by Gas Industry Co of new interconnections have shown that the Guidelines have largely been applied by the transmission system owners.

Accordingly, Gas Industry Co does not consider formal reviews of new interconnections are required. Rather, it will conduct high level monitoring of interconnections in anticipation that participants will draw Gas Industry Co's attention to any issues they may experience.

FORECAST ACTIVITIES FY2017-19

- (a) Review interconnections as required.
- (b) Address any concerns regarding reasonable access.
- (c) Amend the Guidelines if required.

GAS TRANSMISSION SECURITY AND RELIABILITY

Gas Industry Co is currently undertaking a review of existing information and requirements associated with gas transmission security and reliability. These are found in several locations, span responsibilities of several regulators, and can be difficult to bring together and interpret.

We expect the review to be completed and it to be discussed with stakeholders during FY2016. Our initial findings are that existing information and arrangements give significant assurance about both standards and performance. However, it is possible that further work may be required around provision of information and oversight of significant transmission investments.

The latter falls within the jurisdictions of the Commerce Commission and Worksafe, but might be relevant to Gas Industry Co's powers, including to recommend regulations that require expansions, upgrades or service quality improvements and who should pay for these.

CONTINGENT ACTIVITIES FY2017

- » Consider outcomes of the Commerce Commission's planned work relevant to gas transmission disclosure and whether any further improvements are appropriate/necessary to achieve relevant objectives/outcomes of the Gas Act and GPS.
- » In the unlikely event that agreed arrangements are not achieved or existing regulatory arrangements are inadequate, consider the need for additional governance arrangements.

STRATEGIC OBJECTIVE 3

DELIVER EFFECTIVELY ON GAS INDUSTRY CO'S ACCOUNTABILITIES AS THE GAS INDUSTRY BODY

As the industry body, Gas Industry Co is required to perform a number of functions either under the Gas Act or under gas governance rules or regulations. The activities associated with these functions are:

DOWNSTREAM RECONCILIATION

The purpose of the Reconciliation Rules is to 'establish a set of uniform processes that will enable the fair, efficient, and reliable allocation and reconciliation of downstream gas quantities'. Under the Reconciliation Rules, Gas Industry Co oversees the operation of the Allocation Agent and other Rule provisions. Gas Industry Co also monitors allocation results in order to identify, at an early stage, any issues and ensure

these are addressed in an appropriate and timely fashion. This work complements that of a number of industry participants who also undertake monitoring and, from time-to-time, bring issues to the attention of Gas Industry Co and/or the Allocation Agent.

The Reconciliation Rules have been instrumental in reducing the level of UFG and this is largely due to the efforts of industry participants, the increased transparency of the processes for reconciliation, the application of the global allocation methodology, incentives provided by the compliance and enforcement activities, and issues identified and resolved through the performance and event audits undertaken to date.

Downstream reconciliation is discussed further in the Industry Performance section (below).

Collectively, this reduction in UFG represents an ongoing stream of cost savings in excess of \$2.5 million per annum.

FORECAST ACTIVITIES FY2017-19

- (a) Monitor the Allocation Agent.
- (b) Assess the ongoing performance of the Reconciliation Rules.
- (c) Monitor the allocation results.
- (d) Commission performance and event audits as required.
- (e) Make determinations under the Reconciliation Rules as required.

SWITCHING AND REGISTRY

The Switching Rules have the purpose of enabling 'consumers to choose, and alternate, efficiently and satisfactorily between competing retailers'. The Switching Rules provide for a centralised database, the Gas Registry, which stores key technical parameters about every customer installation and facilitates and monitors each customer switch from initiation through to completion.

Recent changes to the Switching Rules enable Gas Industry Co to conduct performance audits of registry participants.

Gas consumer switching is discussed further in the Industry Performance section (below).

FORECAST ACTIVITIES FY2017-19

- (a) Monitor the Gas Registry Operator.
- (b) Complete a Registry Operator tender and, if required, manage the transition to the new service provider.
- (c) Assess the ongoing performance of the Switching Rules.
- (d) Monitor and report on switching statistics.
- (e) Make determinations under the Switching Rules as required.
- (f) In FY2017, complete baseline audits commenced in FY2016.

CRITICAL CONTINGENCY MANAGEMENT

The purpose of the CCM Regulations is to 'achieve the effective management of critical gas outages and other security of supply contingencies without compromising long-term security of supply'. The nature of the gas system means that it is not possible to turn off customers remotely as is done in the electricity industry. Accordingly, to manage a reduction in gas supplies it is necessary to instruct consumers themselves to turn off their gas-using equipment and that, in turn, requires regulatory backing. These Regulations provide for the appointment of a Critical Contingency Operator (CCO) and that role is responsible for determining, managing, and terminating critical contingencies, as well as associated activities such as stakeholder training and running exercises.

The CCM Regulations have been activated four times since they came into full effect in 2010, with one of those being a five-day outage as a result of a break in the Maui pipeline in October 2011.

The CCM Regulations were reviewed following the 2011 critical contingency and found to be soundly-based and fit for purpose. However, a number of improvements were developed and implemented in March 2014. In particular, the review found that many 'essential service providers' were not actually providing essential services. To address this, the system of providing designations for priority access to gas was overhauled and the responsibility for approving those was moved to Gas Industry Co. As a result, FY2015 was a busy year in this area and, as a result of the designations granted in that year requiring renewal in December 2016, there will be a requirement to provide for that work in FY2017.

Critical contingency arrangements are discussed further in the Industry Performance section (below).

FORECAST ACTIVITIES FOR FY2017-19

- (a) Monitor the CCO.
- (b) Assess the ongoing performance of the CCM Regulations.
- (c) Appoint/monitor experts as required.
- (d) Monitor exercises and events as required.
- (e) Administer the contingency pool as required.
- (f) Process applications for designations and/or renewals for critical care, essential services, critical processing, and electricity supply as required.

COMPLIANCE AND ENFORCEMENT

The Compliance Regulations provide for monitoring and enforcement of the other gas governance rules and regulations. The compliance arrangements are designed as an efficient, low-cost means of determining or, where appropriate, settling rules/regulations breaches that raise material issues. Where parties are unable to settle breaches, the last resort is a hearing before a one-person Rulings Panel, a quasi-judicial body. The Rulings Panel can issue fines, make orders for compensation, and make orders directing compliance and/or suspending or terminating participants.

Introduction of gas governance rules and regulations has typically been associated with an increased level of compliance activity as participants adjust to the new arrangements. The breach statistics reported in Gas Industry Co's Quarterly Performance Reports demonstrate that 'teething troubles' with new rules and regulations have been short-lived and enforcement activity currently sits at a fairly low level. This reflects the facts that industry participants make great efforts to ensure their business processes are compliant and Gas Industry Co staff work hard with industry participants to ensure a good understanding of the various rules and regulations.

Compliance arrangements are discussed further in the Industry Performance section (below).

FORECAST ACTIVITIES FY2017-19

- (a) Perform the Market Administrator role.
- (b) Assess the ongoing performance of the Compliance Regulations.
- (c) Assist the Investigator and Rulings Panel as required.
- (d) Monitor compliance trends for indications of regulatory inefficiency.

STATEMENT OF INTENT AND ANNUAL REPORT

The Gas Act requires that the industry body provide an Annual Report to the Minister within three months of the end of the financial year. The Annual Report is then tabled in the House of Representatives. Gas Industry Co is also required to produce an annual Statement of Intent, which is submitted to the Minister for comment prior to being finalised and published.

FORECAST ACTIVITIES FY2017-19

- (a) Prepare and publish Annual Reports that meet statutory requirements.
- (b) Prepare and publish an annual Statement of Intent that meets statutory requirements.
- (c) Prepare and publish Quarterly Reports to the Minister.

STRATEGIC OBJECTIVE 4

DEVELOP AND COMMUNICATE THE ROLE OF GAS IN MEETING NEW ZEALAND'S ENERGY NEEDS

NEW ZEALAND GAS STORY

Gas Industry Co is required by the Gas Act to report on the performance and present state of the gas industry.

During FY2013 Gas Industry Co published the first *New Zealand Gas Story*. The document is updated at least annually to ensure the information is current and topical. Apart from fulfilling the statutory reporting requirement, this work is intended to help stakeholders to better understand the industry and to assist industry participants to make informed investment and energy use decisions. In addition to the document itself, Gas Industry Co communicates the New Zealand gas story through such other channels as its website, the Company's annual and quarterly reports, and presentations to various stakeholder groups. The latter has been highly successful throughout FY2015 and FY2016 with a large number of stakeholders attending presentations in Wellington, Auckland, and Taranaki.

FORECAST ACTIVITIES FY2017-19

- (a) Maintain the currency of the *New Zealand Gas Story* as new information comes to hand.
- (b) Continue seminars and other communications for interested stakeholders.

OTHER REPORTING

The purpose of this reporting is to fulfil a statutory requirement for good information to be available on the performance and present state of the gas industry. During FY2015 and FY2016 Gas Industry Co published three 'requirements and procedures' documents dealing with:

- » Gas quality
- » Gas measurement
- » Gas reconciliation

Those documents serve as reference material and as an introductory information resource for new entrants to the industry.

Gas Industry Co has also commissioned reports focussing on particular aspects of the industry, such as the *Consumer Energy Options Report* (Concept Consulting, 2016). There is also strong stakeholder support for reporting that explores scenarios for the industry's development, such as *Commercialisation issues, opportunities and challenges in the event of substantive gas-rich exploration success in New Zealand* (Woodward Partners, 2013) and *Possible Commercialisation Options for New Gas Discoveries* (Concept Consulting, 2015).

FORECAST ACTIVITIES FY2017-19

- (a) Publish industry performance measures.
- (b) Publish switching statistics.

STRATEGIC ALIGNMENT WITH GOVERNMENT POLICY OBJECTIVES AND OUTCOMES

GAS ACT (AND GAS INDUSTRY CO CONSTITUTION) OBJECTIVES	GPS OBJECTIVES	GPS OUTCOMES
ENSURE THAT GAS IS DELIVERED IN A SAFE, EFFICIENT, RELIABLE, AND ENVIRONMENTALLY SUSTAINABLE MANNER	<ul style="list-style-type: none"> » The full costs of producing and transporting gas are signalled to consumers and the quality of gas services, where those services include a trade-off between quality and price, reflect consumers' preferences as far as possible » The gas sector contributes to achieving the Government's climate change objectives by minimising gas losses and promoting demand-side management and energy efficiency » Energy and other resources used to deliver gas to consumers are used efficiently 	<ul style="list-style-type: none"> » Providing small consumers with an effective complaints process » Ensure contracts adequately protect the long-term interests of small consumers
FACILITATE AND PROMOTE THE ONGOING SUPPLY OF GAS TO MEET NEW ZEALAND'S ENERGY NEEDS, BY PROVIDING ACCESS TO ESSENTIAL INFRASTRUCTURE AND COMPETITIVE MARKET ARRANGEMENTS		<ul style="list-style-type: none"> » Provide efficient arrangements for short-term gas trading » Enable accurate, efficient, and timely arrangements for the allocation and reconciliation of upstream gas quantities
MINIMISE BARRIERS TO COMPETITION IN THE GAS INDUSTRY	<ul style="list-style-type: none"> » Competition is facilitated in upstream and downstream gas markets by minimising barriers to access to essential infrastructure to the long-term benefit of end-users 	<ul style="list-style-type: none"> » Enable accurate, efficient, and timely arrangements for the allocation and reconciliation of downstream gas quantities » Minimise barriers to customer switching » Ensure gas governance arrangements are supported by appropriate compliance and dispute resolution processes
MAINTAIN OR ENHANCE INCENTIVES FOR INVESTMENT IN GAS PROCESSING FACILITIES, TRANSMISSION, AND DISTRIBUTION		<ul style="list-style-type: none"> » Provide an efficient market structure for the provision of gas metering, pipeline, and energy services
SUBJECT DELIVERED GAS COSTS TO SUSTAINED DOWNWARD PRESSURE	<ul style="list-style-type: none"> » The full costs of producing and transporting gas are signalled to consumers and the quality of gas services, where those services include a trade-off between quality and price, reflect consumers' preferences as far as possible 	<ul style="list-style-type: none"> » Minimise barriers to customer switching » Provide efficient arrangements for short-term gas trading
HAVE ALL PARTIES PROPERLY AND EFFICIENTLY MANAGE RISKS RELATING TO SECURITY OF SUPPLY, INCLUDING TRANSPORT ARRANGEMENTS		<ul style="list-style-type: none"> » Produce sound arrangements for the management of critical gas contingencies
MAINTAIN CONSISTENCY WITH THE GOVERNMENT'S GAS SAFETY REGIME		<ul style="list-style-type: none"> » Produce sound arrangements for the management of critical gas contingencies » Provide public information on the performance and state of the gas sector

WHAT WE HAVE DONE	FY2017 WORK PROGRAMME	FUTURE WORK AREAS
<ul style="list-style-type: none"> » Created the Retail Gas Contracts Oversight Scheme in 2010. It provides assurance that standard contracts protect small consumers' long-term interests » Carried out assessments in 2010, 2011, 2012 and 2015 » Considered that further LPG regulation is not currently needed (FY2015) 	<ul style="list-style-type: none"> » Assessing new entrant retailers » Continue to work with EGCC to identify and address any systemic issues that gas consumers raise » Monitor the LPG market to determine if current non-regulatory arrangements are satisfactory 	<ul style="list-style-type: none"> » Next full Retail Gas Contracts Oversight Scheme assessment will occur in FY2018 » Work with pipeline owners on transmission code changes and convergence
<ul style="list-style-type: none"> » A private company created a gas trading market in 2013 » D+1 trial implemented in December 2015 	<ul style="list-style-type: none"> » Refinement of D+1 and beginning the process to introduce D+1 rules into the Downstream Reconciliation Rules 	<ul style="list-style-type: none"> » Implement D+1 rules in FY2018 » Reviewing the efficiency of short-term gas trading and whether gas governance arrangements could improve the market
<ul style="list-style-type: none"> » Recommended the Gas (Downstream Reconciliation) Rules 2008; ongoing administration through the Allocation Agent » Recommended the Gas (Switching Arrangements) Rules 2008 » Recommended the Gas Governance (Compliance) Regulations 2008; ongoing administration through Market Administrator, Independent Investigator, and Rulings Panel » Continuing work on Gas Transmission Work Programme 	<ul style="list-style-type: none"> » Refinement of D+1 » Market-based balancing post-implementation assessment » Wholesale market monitoring » Determine the extent to which Gas Industry Co should support Powerswitch » Continuing Market Administrator work » Progress Transmission Code convergence work 	<ul style="list-style-type: none"> » Reviewing the efficiency of short-term gas trading and whether gas governance arrangements could improve the market » Progress transmission code convergence work
<ul style="list-style-type: none"> » Addressed in multiple workstreams, including switching, downstream reconciliation, and Gas Transmission Work Programme » Administered Gas Processing Information Disclosure Rules 2010 (revoked in 2014) 		
<ul style="list-style-type: none"> » Recommended the Gas (Switching Arrangements) Rules 2008 » A private company created a gas trading market in 2013 	<ul style="list-style-type: none"> » Determine the extent to which Gas Industry Co should support Powerswitch » Continue to publish monthly switching statistics 	<ul style="list-style-type: none"> » Reviewing the efficiency of short-term gas trading and whether gas governance arrangements could improve the market
<ul style="list-style-type: none"> » Recommended the Gas Governance (Critical Contingency Management) Regulations 2008; continuing to address this through the CCM designation process » Released Gas Transmission Security and Reliability Issues Paper in April 2016 	<ul style="list-style-type: none"> » Critical contingency designations expire in FY2017. Renewal applications will be considered and determined during FY2017 » Working closely with the Commerce Commission to ensure that security and reliability are adequately reported on 	
<ul style="list-style-type: none"> » Recommended the Gas Governance (Critical Contingency Management) Regulations 2008; continuing to address this through the CCM designation process » The Company publishes the <i>New Zealand Gas Story</i> annually in addition to information available through Company Quarterly and Annual Reports and other publications » Released Gas Transmission Security and Reliability Issues Paper in April 2016 	<ul style="list-style-type: none"> » Working closely with the Commerce Commission to ensure that security and reliability are adequately reported on » Transmission code convergence work 	<ul style="list-style-type: none"> » Transmission code convergence work

Gas Industry Co's Strategic Objectives — delivering effectively on the Company's accountabilities as the industry body; building and communicating the *New Zealand Gas Story*; facilitating efficient use of, and investment in, gas infrastructure; and promoting efficient, competitive, and confident gas markets — stretch across all of the Company's objectives and are aligned with the objectives and outcomes contained in the Gas Act and GPS. The Company's diverse workstreams all help the Company move toward meeting those objectives and outcomes.

INDUSTRY PERFORMANCE

In addition to alignment with Government policy objectives and outcomes, Gas Industry Co's strategic and Work Programme objectives seek to support key areas of industry performance, particularly in relation to consumer switching, downstream reconciliation, critical contingency management and transmission system balancing.

The Company continually tracks, and reports regularly upon, the performance of the Switching Rules, Downstream Reconciliation Rules and CCM Regulations in terms of their ongoing effectiveness, the competitive outcomes they foster, and industry participants' adherence to them. Gas Industry Co has also been seeking improvements to pipeline balancing and is monitoring the new, industry-led market-based balancing arrangements.

CUSTOMER SWITCHING

The Switching Rules became effective in 2009 and replaced an industry protocol incorporated within a former Reconciliation Code. The previous arrangement had no formal enforcement provisions, whereas the Switching Rules introduced a formal binding governance regime for customer switching between competing retailers.

Switching rates, which are an indicator of contestability in the market, have since increased from less than 1,000 to more than 4,000 a month. Annual customer churn has increased from 5 percent to over 19 percent. In parallel, the disciplines of the Switching Rules have seen the time taken for consumer switching to be completed reduced from weeks or months, to around four business days.

FIGURE 4 - GAS CUSTOMER SWITCHING

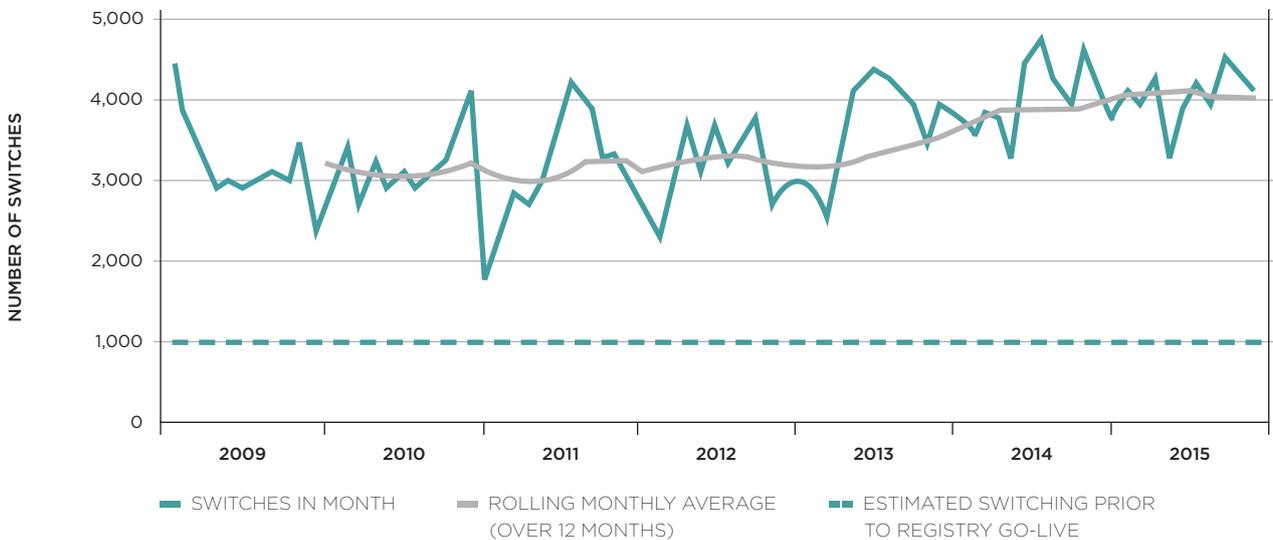
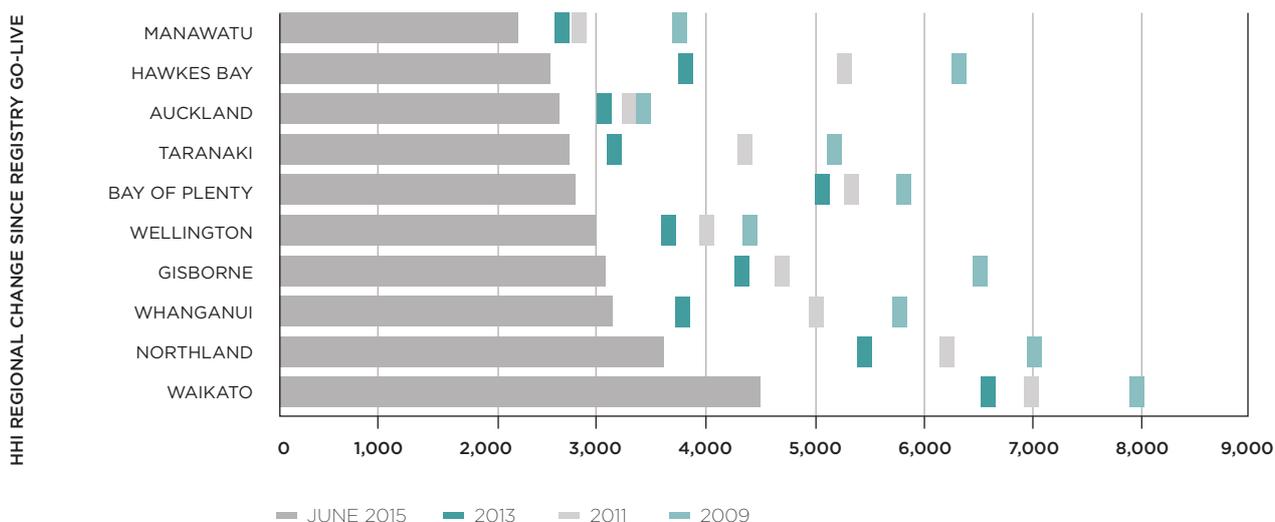


FIGURE 5 - RETAIL MARKET CONCENTRATION



The increased switching activity reflects, in part, greater consumer choice as more retailers have joined the market.

Gas customers generally have access to multiple retailers. Currently all eleven retailers are active at gas gates (where gas leaves the high pressure transmission system and enters the local gas distribution networks) that together represent approximately 40 percent of consumers. Approximately 99 percent of consumers are connected at a gas gate where at least eight retailers trade.

Gas Industry Co's monitoring has shown that market concentration, as measured by the Herfindahl-Hirschman Index (HHI), has decreased in all regions. The retail gas markets in these areas have become less concentrated as new retailers have gained market share, diluting the dominance of previously incumbent retailers.

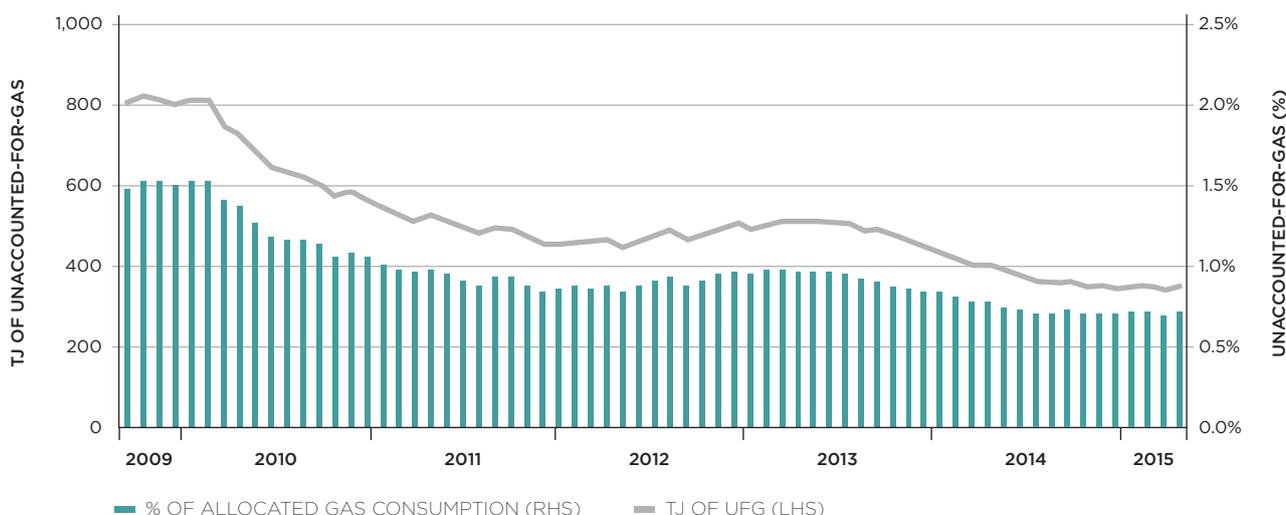
Gas Industry Co considers there is potential for retail competition to further strengthen as more niche retailers join the market. Such retailers often set out with an electricity offering but subsequently look to expand to a dual electricity/gas commercial platform to compete successfully.

While these sorts of market forces are outside Gas Industry Co's direct influence, the Company maintains a strong focus on ensuring market arrangements and associated mechanisms, such as the Gas Registry, effectively support competitive activity and the best interests of consumers.

Consumers' interests are also promoted through a range of other arrangements implemented under the co-regulatory regime, including:

- » implementation of the Retail Scheme that ensures contractual arrangements between gas retailers and small consumers adequately protect the long-term interests of small consumers; and
- » a *Framework for Gas Retailer Insolvency Arrangements*, which sets out the process Gas Industry Co will follow in the event of a retailer insolvency.

FIGURE 6 - UNACCOUNTED-FOR GAS



DOWNSTREAM RECONCILIATION

The Reconciliation Rules introduced formal arrangements to replace an industry code that was considered to be unfair to incumbent retailers and lacked transparency. These Rules provide a formal process for attributing volumes of gas used by consumers at shared gas gates to the retailers responsible for them.

The Reconciliation Rules have been instrumental in reducing the level of UFG, which is the difference between the amount of gas that retailers estimate their customers have used and the actual gas volume leaving the transmission system at a gas gate and entering the local distribution network. UFG imposes a cost on the market as it is gas that retailers must pay for, but cannot sell. As such, the extent of UFG is a measure of market efficiency.

The move to a rules-based regime has delivered an ongoing stream of cost savings to the industry in excess of \$2.5 million a year through more equitable allocation of UFG among retailers, more accurate retailer reporting that has reduced overall UFG, performance and event auditing, improved market efficiency and greater information transparency that more readily identifies anomalies in consumption data.

Since 2009 annual UFG has fallen from 600,000 gigajoules (GJ) to about 300,000 GJ, or from about 2 percent of gas consumed to about 1 percent.

Gas Industry Co's regular reviews of governance arrangements resulted in a number of minor amendments to the Reconciliation Rules in 2013, and further enhancements to improve the accuracy of initial allocations are being developed.

CRITICAL CONTINGENCY MANAGEMENT

In 2009, the CCM Regulations replaced a voluntary industry arrangement, reflecting the increasing complexity of the gas industry and the need for greater certainty around the industry's response, including demand curtailment, during a serious supply emergency.

The CCM Regulations have been activated four times since they came into full effect in 2010. One of these was a five-day outage of the Maui pipeline which caused a serious reduction in gas supply to the upper North Island in October 2011. While a post-Maui outage review found the CCM Regulations to be generally effective, and fit for purpose, lessons from the event were subsequently reflected in a number of amendments, particularly in the system for providing special designations for priority access to available gas.

The responsibility for assessing and approving special designation applications from consumers has moved from retailers to Gas Industry Co and the Company maintains a close watch on the effectiveness of the CCM Regulations through the monitoring of annual exercises, and actual events as they happen.

TRANSMISSION BALANCING

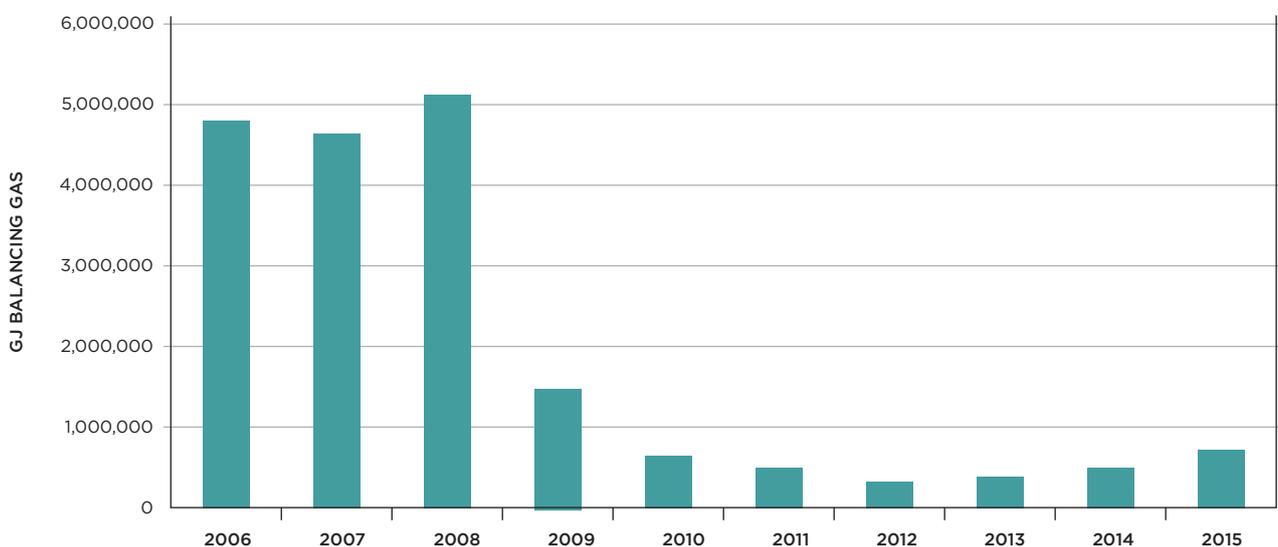
Pressures in the Maui pipeline must be maintained within prescribed safe operating parameters. Pressures will rise or fall as parties who inject gas into the pipeline over or under inject, or parties receiving gas from the pipeline over or under take relative to their scheduled quantities. MDL buys or sells 'balancing gas' to maintain gas pressure within the operational limits. Previously, the cost of this gas was largely socialised among all pipeline users, but with the introduction of the market-based balancing regime in October 2015 the costs are directed to the party or parties responsible for the imbalance.

The move to MBB was the latest development in industry efforts to resolve transmission balancing issues and improve arrangements since 2009. Once balancing charges were introduced, pipeline users took steps

to more effectively self-manage their individual gas balance positions and that contributed to a decline in balancing gas purchases from approximately 4.8 petajoules (PJ) in 2009 to as low as approximately 0.3PJ in 2012. Balancing gas requirements can fluctuate and a prime focus for Gas Industry Co in the immediate future is on monitoring and assessing the effectiveness of the newly-introduced MBB arrangement.

However, the move to market-based balancing with mandatory daily cash-out of excess imbalance has resulted in a significant increase in the volumes of balancing gas bought and sold by the balancing agent for the transmission system. It may be that this activity will decline to some extent over time as transmission customers become acclimatised to the new arrangements and, where able, choose to self-balance. However, it is equally the case that where balancing transactions occur at market prices it may be rational for some pipeline customers to simply accept the default balancing service provided by the pipeline. Accordingly, it should be noted that under the new arrangements the scale of balancing gas transactions by the transmission system is no longer, of itself, an indicator of efficiency.

FIGURE 7 -BALANCING GAS TRADING VOLUMES



COMPLIANCE WITH GOVERNANCE RULES AND REGULATIONS

The Compliance Regulations provide for the monitoring and enforcement of other gas governance rules and regulations. They are designed as an efficient, low-cost means of determining and, where appropriate, settling rules breaches that raise material issues.

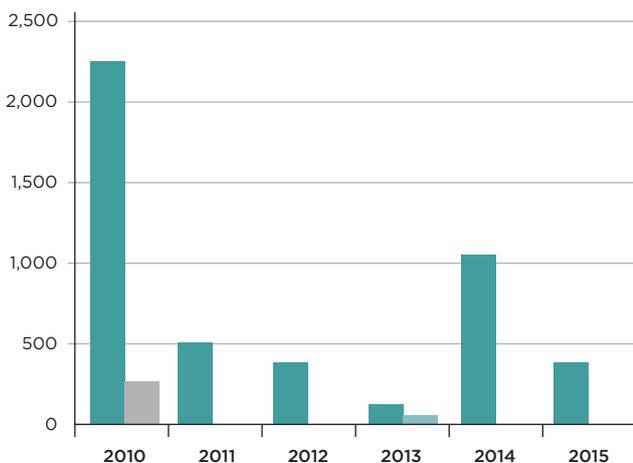
Breach allegations are considered first by the Market Administrator, a role performed by Gas Industry Co. Where a material issue is deemed to exist, the matter is referred to an independent Investigator for further examination and, where appropriate, settlement.

Settlements must be referred to the Rulings Panel for approval or rejection. The Rulings Panel, a one-person quasi-judicial body appointed by the Minister, also considers matters where parties are unable to settle breaches, and can issue fines, make orders for compensation, and make orders directing compliance or suspending or terminating participants.

Compliance activity is typically higher immediately following the introduction of regulated arrangements as industry participants adjust to those new arrangements. Breach statistics reported by Gas Industry Co demonstrate that 'teething troubles' with new rules and regulations are generally short-lived. At other times, enforcement activity is typically low, indicating that participants are generally diligent in ensuring their business processes are compliant.

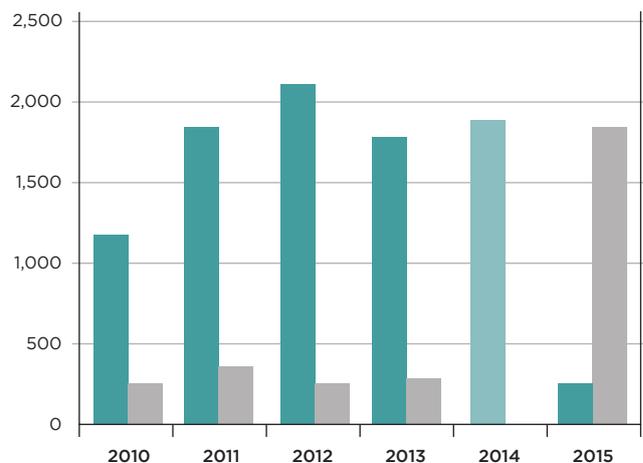
Gas Industry Co liaises closely with participants to ensure there is a good understanding of regulatory requirements.

FIGURE 8 - SWITCHING RULES BREACHES



■ NOT MATERIAL
 ■ MATERIAL
 ■ AWAITING DETERMINATION

FIGURE 9 - RECONCILIATION RULES BREACHES



Note: Almost all alleged breaches under the Reconciliation Rules relate to rule 37, which requires the accuracy of consumption provided at the initial allocation stage to be within a specified tolerance level of the information provided at the final stage.

OTHER INFORMATION

GAS INDUSTRY CO FUNDING

Gas Industry Co has three sources of funding to meet the costs expected to be incurred in delivering effective co-regulation and fulfilling its statutory and GPS obligations. They are:

- » a levy on industry participants pursuant to the Gas Act;
- » market fees imposed pursuant to various rules or regulations made under the Gas Act; and
- » an annual shareholder fee.

LEVY FUNDING

Section 43ZZB of the Gas Act enables Gas Industry Co to recommend to the Minister that industry participants be required to pay a levy to cover the costs of Gas Industry Co exercising its functions as the industry body. The levy covers the costs of the Company's policy work and market administration excluding external service providers and some consultants. Any excess levy recovered in a financial year is generally refunded to industry participants in the following year unless special circumstances warrant otherwise.

MARKET FEES

Section 43S of the Gas Act enables gas governance regulations or rules to be made that provide for the funding by industry participants of the operation of those regulations or rules. The Switching Rules, Reconciliation Rules, CCM Regulations, and the Compliance Regulations contain market fee provisions. These fees are used to recover costs of external service providers and consultants, as contemplated by the relevant regulations.

ANNUAL FEES

Gas Industry Co's Constitution requires all shareholders to pay an annual fee to Gas Industry Co. The fee is set by the Board and is \$5,000 per shareholder per annum. The Board has resolved that these fees will be set aside to establish cash reserves.

ADDITIONAL REPORTING

In addition to the reporting described earlier in this Statement of Intent, Gas Industry Co provides the Minister with briefings and advice as requested, or as necessary. There are no specific matters, outside those detailed in this Statement of Intent, on which Gas Industry Co expects to make a decision that would require it to consult or notify the Minister.

SERVICE PROVIDERS

The following entities and individuals provide specified services to Gas Industry Co:

GOVERNANCE ARRANGEMENT	ROLE	SERVICE PROVIDER
Switching Rules	Registry Operator	Jade Software Corporation
Reconciliation Rules	Allocation Agent	Energy Market Services (EMS)
CCM Regulations	Critical Contingency Operator	Core Group
Compliance Regulations	Rulings Panel	Hon Sir John Hansen, KNZM
	Independent Investigator	Jason McHerron, Barrister
Retail Gas Contracts Scheme	Independent Assessor	Roger Palairret
Distribution Contracts Scheme		

FINANCIAL STATEMENTS

In accordance with section 43ZR of the Gas Act, Gas Industry Co's forecast financial statements are set out as follows:

These statements have been prepared using information consistent with that used for the calculation of the FY2017 Gas Industry Co levy. Further details about the assumptions, revenue calculations and workstream expenses used to calculate the FY2017 levy can be found in the document, *Consultation on Gas Industry Co FY2017 Statement of Intent and Levy*, issued in December 2015 (available on Gas Industry Co's website, www.gasindustry.co.nz).

The FY2016 forecast was approved by Gas Industry Co's Board in March 2016 and includes actual results for the period July 2015 to April 2016, and an up-to-date forecast for May and June 2016.

We acknowledge responsibility for the forecast financial statements contained in this report and for the judgments used in their preparation.

We certify that the information in this report is, except where noted, consistent with the budget estimates contained in Gas Industry Co's *FY2017 Levy Recommendation* that has been made to the Minister of Energy and Resources under section 43ZZB of the Gas Act.



Rt Hon James B. Bolger, ONZ
CHAIR

June 2016



Robin Hill
DEPUTY CHAIR

FORECAST STATEMENT OF FINANCIAL PERFORMANCE

	BUDGET FY2017 \$	FORECAST FY2016 \$	ACTUAL FY2015 \$
REVENUE			
Wholesale Levy	2,058,500	2,427,774	2,371,755
Retail Levy	1,854,560	1,880,721	1,457,115
LEVY REVENUE SUBTOTAL	3,913,060	4,308,495	3,828,870
Market Fees	1,489,000	1,328,211	1,532,786
Annual Fees	55,000	55,000	55,000
Refunded Levies	(714,250)	(163,568)	(562,621)
Interest Income	35,000	43,411	63,684
SUBTOTAL OTHER REVENUE	864,750	1,263,054	1,088,849
TOTAL REVENUE	4,777,810	5,571,549	4,917,719
EXPENSES			
Depreciation & Amortisation	42,863	44,943	185,788
Operating lease expenses	270,000	268,780	305,028
Fees paid to audit firm – financial statement audit	15,225	14,593	14,543
Fees paid to audit firm – other services	12,949	14,133	-
Directors' fees	275,000	262,460	265,460
General expenses	337,311	419,236	248,301
Bad Debts	-	(6,325)	(46,579)
Recruitment expenses	20,000	54,178	-
Technical, economic, and legal advice	785,449	764,833	669,746
Service Provider Fees	1,489,000	1,328,211	1,486,137
KiwiSaver contributions	50,372	46,102	46,300
Foreign exchange loss	-	25	-
Employee benefit expense	2,098,762	1,932,943	1,981,117
TOTAL EXPENSES	5,396,931	5,144,112	5,155,841
Finance Costs	5,129	4,598	4,319
TOTAL EXPENDITURE	5,402,060	5,148,710	5,160,160
PROFIT / (LOSS) BEFORE TAX	(624,250)	422,839	(242,441)
Income Tax Expense	9,800	12,155	17,832
PROFIT / (LOSS) FOR THE YEAR	(634,050)	410,684	(260,273)

FORECAST STATEMENT OF MOVEMENT IN EQUITY

	INDUSTRY RESERVES	RETAINED EARNINGS	TOTAL	INDUSTRY RESERVES	RETAINED EARNINGS	TOTAL
	\$	\$	\$	\$	\$	\$
	BUDGET FY2017			FORECAST FY2016		
OPENING BALANCE	739,252	650,000	1,389,252	383,568	595,000	978,568
Net surplus/(deficit) for the year		(634,050)	(634,050)		410,684	410,684
Industry Advances	(689,050)	689,050	-	355,684	(355,684)	-
Reserves transfer						
FORECAST CLOSING BALANCE	50,202	705,000	755,202	739,252	650,000	1,389,252

FORECAST STATEMENT OF FINANCIAL POSITION

	BUDGET FY2017	FORECAST FY2016	ACTUAL FY2015
	\$	\$	\$
<i>CURRENT ASSETS</i>			
Cash and cash equivalents	1,627,806	1,968,936	1,819,473
Trade and other receivables	87,813	490,918	22,007
Prepayments	52,865	45,905	39,591
Income tax receivable	9,800	12,155	-
TOTAL CURRENT ASSETS	1,778,284	2,517,914	1,881,071
<i>NON-CURRENT ASSETS</i>			
Property, plant & equipment	85,922	61,254	90,728
Intangible assets	12,273	9,161	16,059
TOTAL NON-CURRENT ASSETS	98,195	70,415	106,787
TOTAL ASSETS	1,876,479	2,588,329	1,987,858
<i>CURRENT LIABILITIES</i>			
Trade and other payables	834,764	890,089	723,558
Asset restoration provision	48,777	43,645	39,047
Employee entitlements	237,725	265,332	246,674
Redeemable Shares	11	11	11
TOTAL CURRENT LIABILITIES	1,121,277	1,199,077	1,009,290
TOTAL LIABILITIES	1,121,277	1,199,077	1,009,290
NET ASSETS	755,202	1,389,252	978,568
<i>REPRESENTED BY</i>			
Industry Reserves	50,202	739,252	383,568
Retained Earnings	705,000	650,000	595,000
TOTAL SHAREHOLDERS' FUNDS	755,202	1,389,252	978,568

FORECAST STATEMENT OF CASH FLOWS

	BUDGET FY2017 \$	FORECAST FY2016 \$	ACTUAL FY2015 \$
<i>CASH FLOWS FROM OPERATING ACTIVITIES</i>			
Levy revenue	4,257,617	3,993,629	3,851,099
Market fee revenue	1,489,000	1,690,677	1,364,356
Annual fees	55,000	55,000	55,000
Interest received	35,000	43,411	63,684
	5,836,617	5,782,717	5,334,139
<i>CASH WAS APPLIED TO</i>			
Payments to suppliers	(3,014,863)	(3,158,098)	(2,749,537)
Payments to employees	(2,149,634)	(2,040,326)	(2,019,171)
Payments to directors	(275,000)	(264,543)	(262,460)
Refund of levy to industry participants	(714,250)	(163,560)	(544,549)
Taxes paid	-	(10,251)	(17,832)
Net GST	-	11,705	(15,262)
	(6,153,747)	(5,625,073)	(5,608,811)
NET CASH INFLOWS FROM OPERATING ACTIVITIES	(317,130)	157,644	(274,672)
<i>CASH FLOWS FROM INVESTING ACTIVITIES</i>			
Purchase of property, plant and equipment	(24,000)	(8,181)	(28,555)
Purchase of intangible assets	-	-	(16,321)
NET CASH FLOWS FROM INVESTING ACTIVITIES	(24,000)	(8,181)	(44,876)
NET CASH FLOWS	(341,130)	149,463	(319,548)
Opening cash balance	1,968,936	1,819,473	2,139,021
CLOSING CASH BALANCE	1,627,806	1,968,936	1,819,473

STATEMENT OF CONTINGENT LIABILITIES AND COMMITMENTS

Gas Industry Co has no known contingent liabilities or assets.

Gas Industry Co's lease commitment in relation to its premises commenced on 1 December 2008 and expires on 30 November 2017 at an annual rental of approximately \$268,776.

Other operating lease commitments are for office equipment.

Gas Industry Co has various ongoing commitments for the operation of the Company.

	BUDGET FY2017 \$	FORECAST FY2016 \$
OPERATING LEASE COMMITMENTS		
Within one year	111,990	268,776
Later than one year but not later than five years	-	111,990
Later than five years	-	-
TOTAL OPERATING LEASE COMMITMENTS	111,990	380,766
EQUIPMENT LEASE COMMITMENTS		
Within one year	2,862	34,347
Later than one year but not later than five years	-	2,862
Later than five years	-	-
TOTAL EQUIPMENT LEASE COMMITMENTS	2,862	37,209
SERVICE PROVIDER COMMITMENTS		
Within one year	1,110,700	1,199,153
Later than one year but not later than five years	501,796	1,612,496
Later than five years	-	-
TOTAL SERVICE PROVIDER COMMITMENTS	1,612,496	2,811,649

STATEMENT OF ACCOUNTING POLICIES

The following accounting policies apply to these financial statements:

Reporting Entity: Gas Industry Co is a company incorporated under the Companies Act 1993 that was approved as the co-regulator of the gas industry by Order in Council on 22 December 2004. These prospective financial statements have been prepared in accordance with section 43ZR of the Gas Act 1992 and the Financial Reporting Act 1993.

Measurement Base: These financial statements have been prepared on an historical cost basis.

Particular Accounting Policies: These financial statements are prepared in accordance with New Zealand generally accepted accounting practice. The following particular accounting policies that materially affect the measurement of financial performance, financial position, and cash flows have been applied consistently.

Revenue: Revenue is derived from Gas Industry Co's levies and market fees imposed under Subpart 2 of Part 4A of the Gas Act 1992; from annual fees charged to shareholders and from interest on deposits. Such revenue is recognised when earned and is reported in the financial period to which it relates.

Taxation: With the exception of its interest income, Gas Industry Co's revenue is not regarded as gross income in terms of section CB 1 of the Income Tax Act 2007.

Goods and Services Tax (GST): The Statement of Financial Performance and Statement of Cash Flows have been prepared so that all components are stated exclusive of GST. All items in the Statement of Financial Position are stated net of GST.

Accounts Receivable: These are carried at estimated realisable value after providing for debts where collection is doubtful.

Employee Entitlements: Employee entitlements to salaries and wages, annual leave, and other benefits are recognised when they accrue to employees.

Financial Instruments: Financial instruments carried on the Statement of Financial Position include cash and bank balances, investments, receivables, trade creditors, and borrowings. Except for those items covered by a separate accounting policy, all financial instruments are shown at their estimated fair value.

Depreciation: Depreciation of fixed assets is provided on a straight line basis, so as to allocate the depreciable amount of assets over their useful lives. The depreciable amount is the historical cost. The estimated useful lives are:

CATEGORY	ESTIMATED USEFUL LIFE
IT-Hardware & Software	3-5 years
Office Equipment	4-10 years
Leasehold Improvements	Term of lease

STATEMENT OF CASH FLOWS

- » Operating activities include all transactions and other events that are not investing or financing activities.
- » Investing activities are those relating to the acquisition, holding and disposal of property, plant and equipment and 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 of Gas Industry Co. 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.
- » Cash is considered to be cash on hand and current accounts in banks, net of bank overdrafts.

STATEMENT OF SIGNIFICANT UNDERLYING ASSUMPTIONS

The following assumptions have been made in the development of the forecast financial statements. These assumptions were adopted by resolution of the Board of Directors in March 2016:

- » These forecast financial statements comply with New Zealand generally accepted accounting practice. The measurement base applied is historical cost.
- » Accrual accounting has been used to prepare these financial statements.
- » These statements have been prepared on a going-concern basis.
- » The forecast financial statements have been presented for the purpose of providing financial information that underlies the work programme as set out in the *2017-2019 Statement of Intent*. This financial information may not be appropriate for other purposes.
- » It is not intended that these financial forecasts will be re-issued.
- » Actual financial results achieved for the period covered are likely to vary from the information presented and the variations may be material.
- » There is limited ability to alter Gas Industry Co's revenue other than through the annual levy process.
- » Section 43S of the Gas Act enables Gas Industry Co to collect from industry participants fees relating to the ongoing costs associated with gas market rules and regulations.
- » An annual levy of \$3,913,060 is assumed to be effective from 1 July 2016 and is paid monthly. Any monthly levy not payable due to the date on which the levy regulations come into force will be paid on the 20th of the month following the levy regulations coming into force.
- » The wholesale levy revenue is budgeted to be \$2,058,500 for FY2017 and will be collected each month from the relevant levy payers at a rate of 1.15c/GJ based on each industry participant's volume of gas purchased from gas producers.
- » The retail levy revenue is budgeted to be \$1,854,560. This is calculated based on Gas Industry Co's estimate of 268,000 active ICP's, at a levy rate of \$6.92/ICP per annum. Active Contracted ICPs indicate a customer at the ICP has a contract with the retailer. The retail levy is payable only on active ICPs. If the actual number of ICPs substantially differs from the estimate, there may be a small difference in the retail levy revenue.
- » The FY2017 levy calculation is based on a work programme consistent with the Government Policy Statement on Gas Governance 2008 (GPS). If, during the plan period, the current GPS is amended, there may be an impact on our operating costs, resulting in the possible over- or under-recovery of levy revenue in FY2017. 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 or 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 Meeting.
- » The forecast equity for the year ending 30 June 2016 is approximately \$1,389,252. Of this, \$739,252 is classified as Industry Advances Reserve and will be either returned to levy payers after the end of the financial year or, if special circumstances warrant, retained for the application to work programmes in the subsequent year(s) as per Board policy. The remainder, \$650,000, is set aside to be held as cash reserves.
- » Gas Industry Co's budget is based on a best estimate of the costs to deliver the Work Programme prepared for calculation of the FY2017 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. This also applies to the administration of gas governance rules and regulations (funded through market fees).

DIRECTORY

GAS INDUSTRY COMPANY LIMITED

Level 8, The Todd Building

95 Customhouse Quay

PO Box 10 646

Wellington

Telephone: +64 4 472 1800

Facsimile: +64 4 472 1801

Email: info@gasindustry.co.nz

Website: www.gasindustry.co.nz

BOARD OF DIRECTORS

Rt Hon James (Jim) Bolger, ONZ

CHAIR, INDEPENDENT DIRECTOR

Robin Hill, B Comm FCA

DEPUTY CHAIR, INDEPENDENT DIRECTOR

Keith Davis, PGDipBus

INDEPENDENT DIRECTOR

Andrew Brown, LLB

INDEPENDENT DIRECTOR

Nigel Barbour, B Comm, LLB

Dennis Barnes, BSC (Hons), MBA, PGDipMktg

Andrew Knight, BMS (Hons), CA

EXECUTIVE

Steve Bielby, LLB (Hons), LLM (London),

CHIEF EXECUTIVE

Ian Dempster, BE (Hons), M Comm (Hons),

GENERAL MANAGER OPERATIONS

Glenda MacBain, DipOrgPsych, DipBM

CORPORATE SERVICES MANAGER

AUDITORS

KPMG, Wellington

BANKERS

Westpac New Zealand Limited

SHAREHOLDERS

Contact Energy Limited

emsTradepoint Limited

First Gas Limited

Genesis Energy Limited

Greymouth Gas Limited

Methanex New Zealand Limited

Mighty River Power Limited

New Zealand Oil & Gas Limited

Nova Energy Limited

OMV New Zealand Limited

Powerco Limited

Shell (Petroleum Mining) Limited

Vector Limited

