

Gas Industry Company Limited

Statement of Intent

2020 - 2022



Gas Industry Company Limited's Statement of Intent is available on our website: www.gasindustry.co.nz

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Statement of Intent for financial years 2020-2022

The 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 section 43ZQ of the Gas Act. It sets out the intended scope and objectives of Gas Industry Co's operations for the financial year ended 30 June 2020 and the following two financial years (30 June 2021 and 30 June 2022), 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 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 of ensuring 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 report on the achievement of those objectives and on the performance and the current state of the New Zealand gas industry.



Rt Hon James B. Bolger, ONZ
CHAIR



Robin Hill
DEPUTY CHAIR

June 2019

Foreword

Gas Industry Co's central statutory obligation is to develop governance arrangements that ensure gas is delivered to existing and new customers in a safe, efficient, fair, reliable and environmentally sustainable manner.

Our work programme and budget set out in this Statement of Intent have been prepared in consultation with the industry, and in the context of considerable ongoing change in the downstream gas sector driven by a number of factors in New Zealand and globally.

Climate change policies, technological developments, and the availability of natural gas will influence the future shape of the gas industry in New Zealand.

Gas Industry Co's work programme in the immediate future involves a combination of implementing new arrangements concluded recently, refining existing arrangements to reflect changes, instigating an inquiry into information disclosure, and ensuring current market rules and regulations continue to serve the industry efficiently.

We especially look forward to the implementation in October 2019 of a single Gas Transmission Access Code (GTAC), which is expected to provide more efficient and streamlined services for transporting gas at high pressure around the North Island, improve gas market trading and create greater transmission information transparency.

The development of a single code, to replace the two separate access code arrangements, was brought to completion in early 2019 following an extensive industry-led consultation process. While the two pipeline systems have historically been operated as a single integrated system, implementation of a single code will see them for the first time also operate with one contractual model.

The process involved for developing the GTAC was consistent with the industry co-regulatory model and is a perfect example of that framework in action – which requires that all potential solutions to an issue, regulated and non-regulated, are assessed before determining the best course of action.

The move to a single code will require changes to other arrangements and processes, including changes to the Reconciliation Rules, adjustments to aspects of managing gas critical contingencies, updating gas quality requirements and procedures information, and adjusting transmission balancing mechanisms. These are further detailed in the work programme description section of this Statement of Intent.

Also closely associated with transmission access developments has been Gas Industry Co's ongoing daily allocation pilot scheme, which emerged as a response to the market-based balancing regime introduced in 2016. It is aimed at helping transmission customers more effectively manage their balancing positions in a timely way.

A new workstream set out in this Statement of Intent – an inquiry into the adequacy of current information disclosure arrangements was initiated by Gas Industry Co at the request of the Minister of Energy and Resources.

Our work commenced in August 2018 when the Minister asked us to consider whether the existing market arrangements relating to information disclosure are sufficient or if further arrangements are required.

The information disclosure workstream has progressed through initial problem scoping and analysis of both the domestic and international markets. A discussion paper has been released to test the problem scoping, develop a greater understanding of the concerns, opportunities for improvement and provide robust input for cost benefit analysis.

The upstream gas sector has important implications for New Zealand's energy future. Relative to the rest of the world, New Zealand has the challenge of managing energy supply security during climate change-driven transitions, while at the same time being isolated from global energy markets.

How natural gas is used in New Zealand in the future will reflect climate change policies that are still emerging, but for now gas contributes over 20 percent of New Zealand's primary energy. With the decline of production from the previously dominant Maui field, New Zealand has developed a broader supply base through additional smaller fields but has lost much of the flexibility provided by Maui. A fuller understanding of future gas supply scenarios is important for stakeholders.

In this regard, Gas Industry Co plans to release its biennial Long-Term Gas Supply and Demand Study during 2019. It will provide a picture and outlook for the natural gas market and will analyse the main drivers behind gas prices and demand and investigate factors that will influence the market. Key factors driving the supply and demand update are the changing gas supply situation – through limited exploration success in the last decade and current gas fields entering the latter stages of their lives – and the implications as we seek to meet our climate change commitments.

Our Statement of Intent reflects that the platform of regulated and non-regulated governance arrangements is largely in place to meet the requirements of the Gas Act, the GPS and the industry more broadly. Gas Industry Co remains committed to delivering value in both its operational workstreams and organisational arrangements. There is strong focus at Board and Management level on prioritising workstreams to ensure available funds are used wisely and efficiently.

We record our appreciation to our industry stakeholders for their valuable input into the work programme development during the consultation process that began with the annual Co-regulatory Forum in November 2018.

We look forward to embracing the challenges outlined in this Statement of Intent.



Rt Hon James B. Bolger, ONZ

CHAIR

June 2019



Andrew Knight

CHIEF EXECUTIVE

Work programme priorities

This section sets out the main elements of Gas Industry Co's work programme for FY2020, and indicatively for the following two financial years. These elements are summarised in Table 1.

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 the industry and other stakeholders, and facilitating forward-looking discussion on future strategic issues.

Efficient governance arrangements

- » administer existing rules and regulations:
 - 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 monitoring 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 compliance of industry participants and take enforcement action only where necessary; and
- » monitor and report on metrics arising from the market and regulatory processes to enhance transparency and foster a well-informed market.

Priority or committed and ongoing projects

A number of important projects are in train or in prospect, some at the request of the Minister of Energy and Resources. These projects aim to resolve priority issues within the industry and better meet the Gas Act and GPS objectives.

Key workstreams in FY2020 are expected to arise from the industry initiative to improve transmission access arrangements by implementing a single Gas Transmission Access Code (GTAC). During FY2020, Gas Industry Co expects that work will entail supporting and assisting the tailoring of the new code and supporting arrangements.

Workstreams closely associated with the GTAC arrangements which will require review in light of the change, include downstream reconciliation, critical contingency management, gas balancing, gas quality, and transmission interconnection.

Other priority projects include:

- » the D+1 pilot project (that was put in place for market-based balancing) will need to continue until the new code is implemented and then amended to align with the GTAC;
- » information disclosure; and
- » the biennial update of the Long-Term Gas Supply and Demand Study.

Future strategic issues

As part of our requirements to report on the performance and current state of the New Zealand gas industry, as well as our strategic objective to communicate the role of gas in meeting the country's energy needs, Gas Industry Co develops discussion and papers on the role of gas in New Zealand.

Past reports commissioned by Gas Industry Co have focused on consumer energy options, options for gas commercialisation, supply and demand study to assist participants make informed decisions, and the potential for demand management as a tool for managing transmission pipeline congestion. The work programme provides an ongoing focus on identifying and advancing such issues.

Table 1: Work programme objectives and activities

| STRATEGIC OBJECTIVE 1 | STRATEGIC OBJECTIVE 2 | STRATEGIC OBJECTIVE 3 | STRATEGIC OBJECTIVE 4 |
|--|--|--|--|
| <p>Promote efficient, competitive and confident gas markets</p> <p><i>Comprising:</i></p> <ul style="list-style-type: none"> » Retail Gas Contracts Oversight Scheme » Gas Distribution Contracts Oversight Scheme » Retailer insolvency » Gas quality » Regulation and rule changes » Gas measurement » Supply/demand study » Wholesale market » Information disclosure | <p>Facilitate efficient use of, and investment in, gas infrastructure</p> <p><i>Comprising:</i></p> <ul style="list-style-type: none"> » Transmission access » Transmission pipeline balancing » Transmission code changes » Transmission pipeline interconnection » Transmission security and reliability | <p>Deliver effectively on Gas Industry Co's accountabilities as the industry body</p> <p><i>Comprising:</i></p> <ul style="list-style-type: none"> » Downstream reconciliation » Switching and registry » Critical contingency management » Compliance and enforcement » Statement of Intent and Annual Report | <p>Communicate the role of gas in meeting New Zealand's energy needs</p> <p><i>Comprising:</i></p> <ul style="list-style-type: none"> » New Zealand Gas Story » Other reporting |

Consultation process

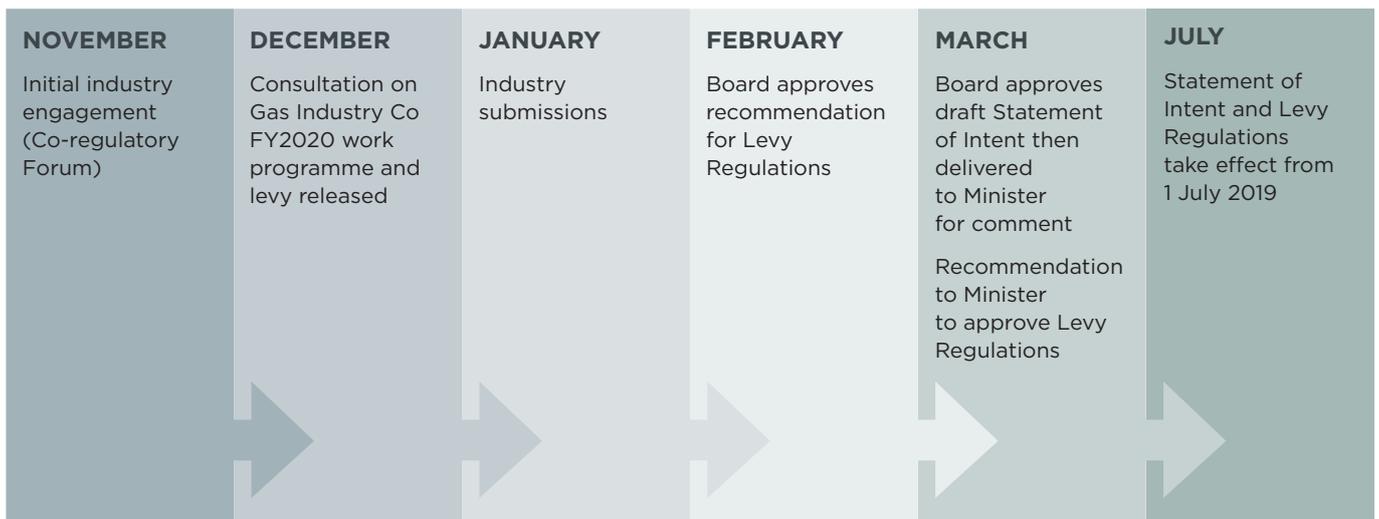
Consultation with industry stakeholders on Gas Industry Co’s intended work programme and budget requirement commenced with the Co-regulatory Forum, held in November 2018.

The work programme and budget addressing the Company’s strategic priorities were detailed in a Consultation Paper¹, which was issued in December 2018. Submissions on the Consultation Paper were taken into account in finalising the recommendation to the Minister for levy funding through regulations (Levy Recommendation) for the financial year ending 30 June 2020.

The consultation process led to the development of this Statement of Intent which, along with the Levy Recommendation², provides the basis for Gas Industry Co to deliver robust outcomes for gas consumers and the wider industry as part of our mandate as the industry body. The Levy Recommendation and draft Statement of Intent are presented to the Minister in March each year.

Figure 1 sets out the consultation and approval processes leading to the annual promulgation of Levy Regulations.

Figure 1: Consultation process



¹ Consultation on Gas Industry Co FY2020 work programme and levy found at www.gasindustry.co.nz

² Gas Industry Co Recommendation to Minister of Energy and Resources to make Gas (Levy of Participants) Regulations 2020 found at www.gasindustry.co.nz

Operating environment

Gas Industry Co's work programme is directly influenced by the industry structure, and the legislative and policy framework. 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 over 285,000 industrial, commercial and residential consumers.

Natural gas has a wide range of applications: cooking and heating in homes, providing energy for a variety of businesses and community amenities, and supplying process heat and serving as a feedstock for large industries.

The baseload gas demand further supports the wider energy sector as, through thermal power plants, gas 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 fields. This evolution has significantly changed the market's dynamics, with a marked increase in the number of participants.

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 system and local distribution networks.

Natural gas is available only in the North Island. Gas in the form of LPG (liquefied petroleum gas) is available in the North and South Islands in bulk and in bottles. LPG is also supplied to some city centres and residential subdivisions via local reticulated networks.

Legislative and policy framework

Since 2004, the gas industry downstream of the exploration and production sector has been governed by a co-regulatory model. As the industry body, Gas Industry Co creates the link 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 2 gas industry structure).

Gas Industry Co's role in relation to the gas transmission and distribution sector focuses on terms and conditions of access to open access pipelines. The Commerce Commission has a complementary role in relation to economic regulation of those assets. As provided for in the Gas Act, the two agencies work closely together on any areas of potential overlap.

The Gas Act empowers Gas Industry Co to make recommendations to the Minister on certain matters, having regard to the objectives for the industry body in the Gas Act, and the objectives and outcomes in 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 has a broader policy objective: it sets, for the entire gas industry, the objective of ensuring that gas is delivered to existing and new customers in a safe, efficient, fair, reliable and environmentally sustainable manner.

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; and
- » risks relating to security of supply, including transport arrangements, are properly and efficiently managed by all parties.

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 customers' 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 are refined as necessary.

Gas Industry Co vision, mission and values

Consistent with the legislative and policy framework described above, Gas Industry Co's Board has put in place the following vision, mission and values which assists in the delivery of the Company's statutory role.

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 Chair, are independent (having no material or financial interest in an industry participant), and three are non-independent Directors (usually senior executives of industry participants).

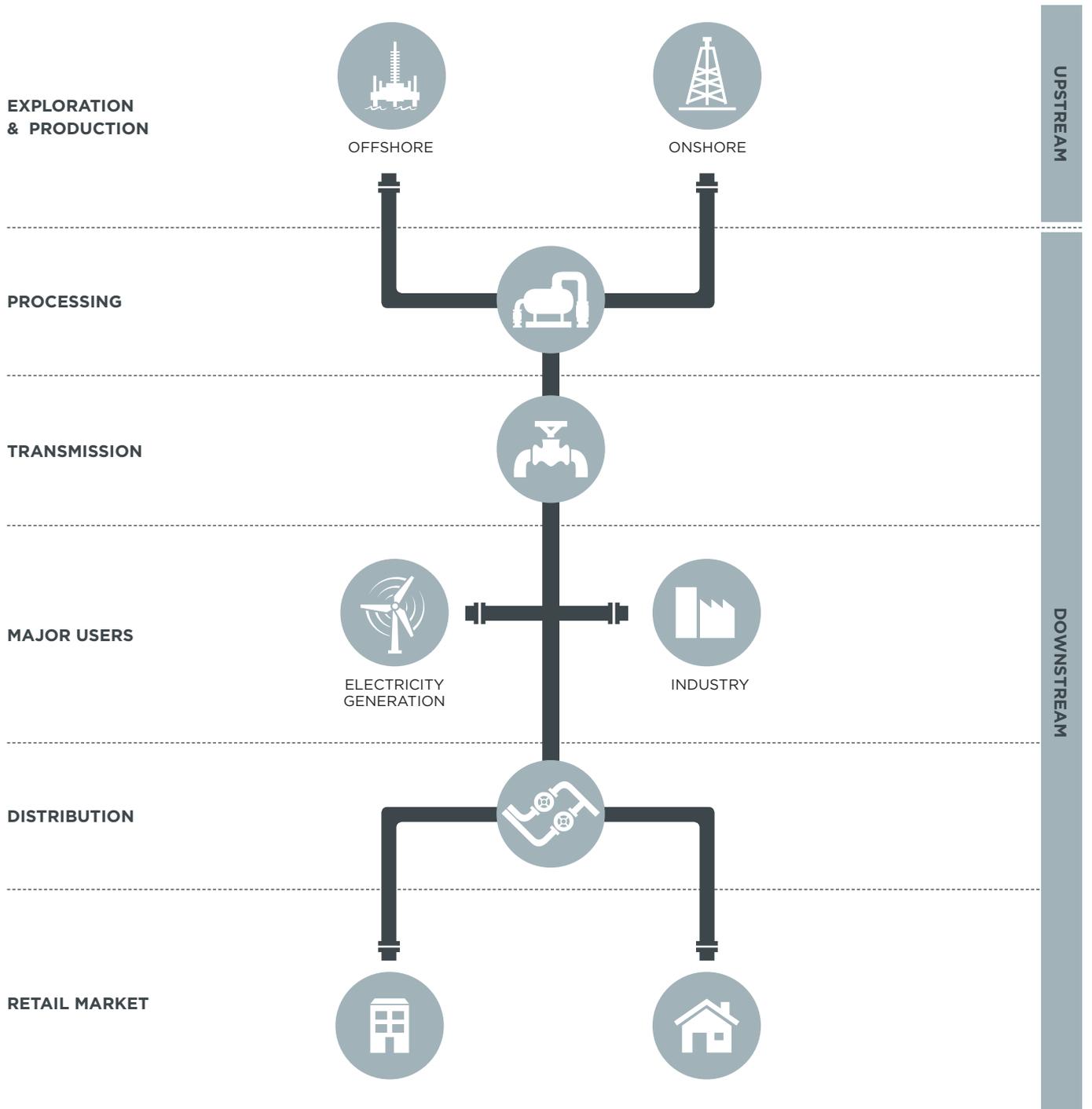
The Board meets on around eight scheduled occasions each year and holds unscheduled meetings to consider matters requiring immediate attention as needed.

The Board has one standing committee, the Independent Directors' Committee, comprising the four independent Directors. The Committee addresses matters where the non-independent Directors have potential or actual conflicts of interest.

Vision, Mission and Values



Figure 2: Gas industry structure



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 tracks, and reports regularly upon, the performance of the Switching Rules, Reconciliation Rules and CCM Regulations in terms of their ongoing effectiveness, the competitive outcomes they foster, and industry participants' adherence to them.

Customer Switching

Since the implementation of the Switching Rules in 2009, a competitive, vibrant retail market has developed. Annual switching rates, an indicator of contestability in the market, have ranged from 15 percent to 18 percent in the last five years, as shown in Figure 3.

Figure 3: Monthly switching rates

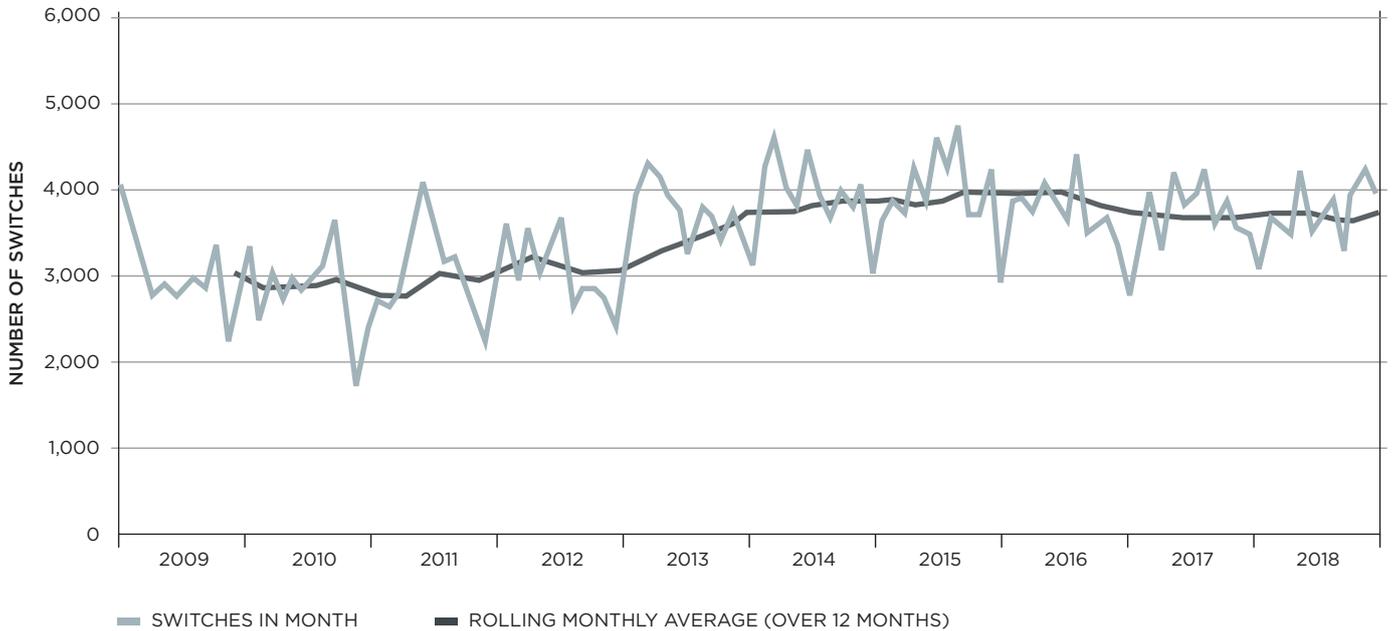
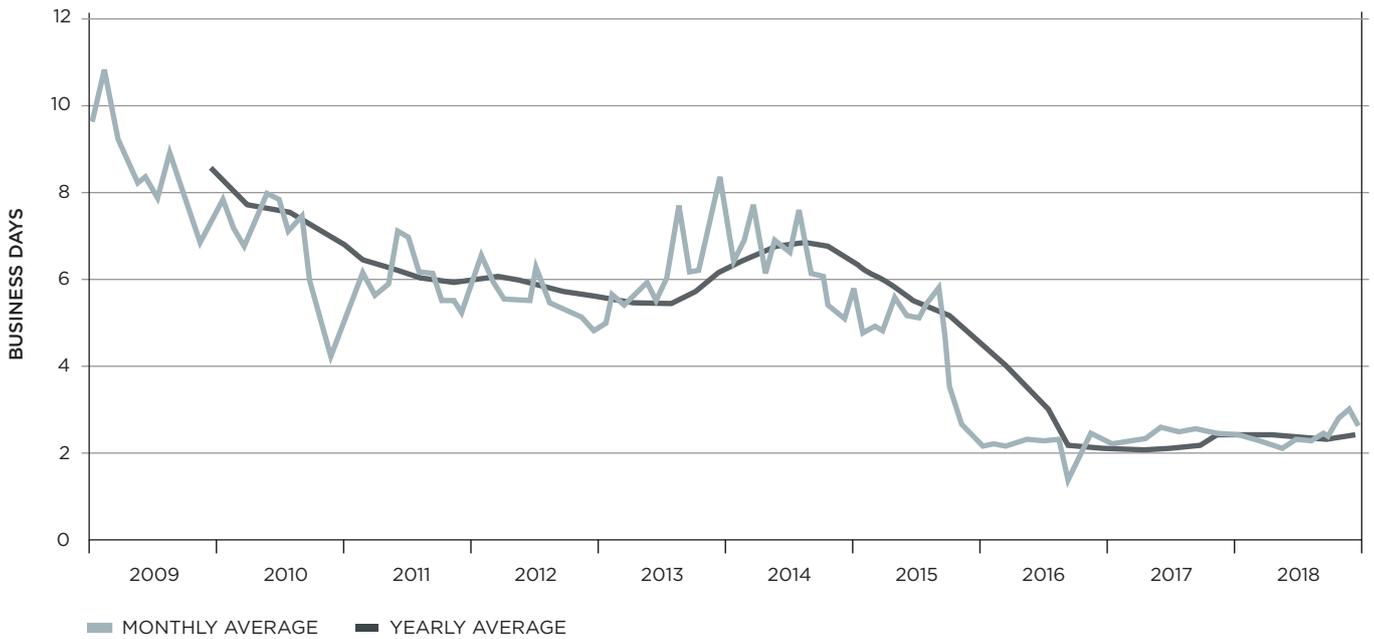


Figure 4: Average time to switch a customer



Another positive outcome of the Switching Rules is that switches are completed much faster than previously. Currently, switches take place in just over two business days on average, as shown in Figure 4.

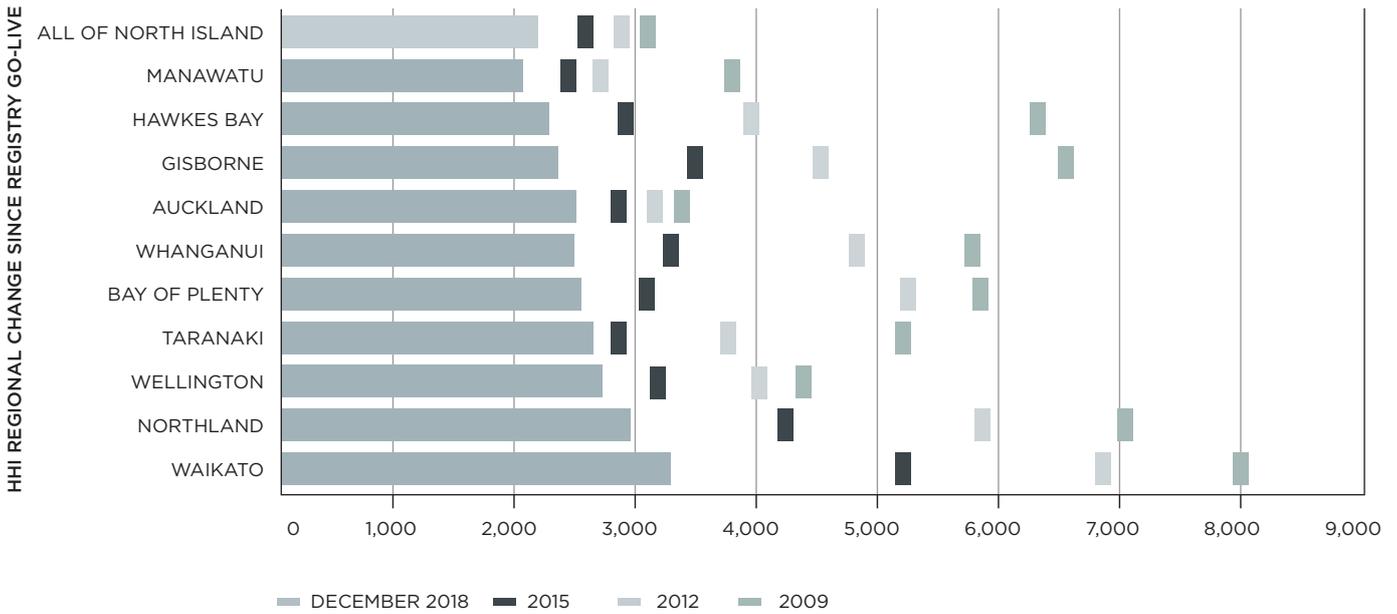
As a comparison, gas switches in the UK take about 17 days for domestic consumers.³

The increased switching activity reflects, in part, greater consumer choice as more retailers have joined the market. In the past 10 years, six retailer brands have entered the gas market: Energy Online (owned by Genesis Energy); Trustpower; Pulse Energy; Switch Utilities; Scholarship NZ; and, most recently, Hanergy; and energyclubnz.

Gas customers generally have access to multiple retailers. The 10 largest retailers are active at gas gates (where gas leaves the high pressure transmission system and enters the local gas distribution networks) that together represent over 50 percent of consumers. Over 99 percent of consumers are connected at a gas gate where at least seven retailers trade.

³ The UK regulator Office of Gas and Electricity Markets (Ofgem) publishes a number of retail market indicators, including switching times, on its website at <https://www.ofgem.gov.uk/data-portal/retail-market-indicators>

Figure 5: Retail market concentration



Market concentration, as measured by the Herfindahl-Hirschman Index (HHI), has decreased, both in the gas market as a whole and in the regions where gas is available (Figure 5). This change has been particularly striking in areas such as Waikato, Northland, Gisborne, and Hawke’s Bay, where the HHI in 2009 was greater than 6,000. The HHI is now less than 2,200 nationally and less than 3,000 in most regions. (As a point of reference, the United States Department of Justice considers markets in which the HHI is between 1,500 and 2,500 to be moderately concentrated. Markets with an HHI of greater than 2,500 are considered highly concentrated⁴).

The changes in HHI show the decreasing concentration of national and regional retail gas markets 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 strengthen further as more niche retailers join the market. 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.

Downstream Reconciliation

Introduced in 2009, the Reconciliation Rules provide a formal process for attributing volumes of gas used by consumers at shared gas gates to the retailers responsible for them.

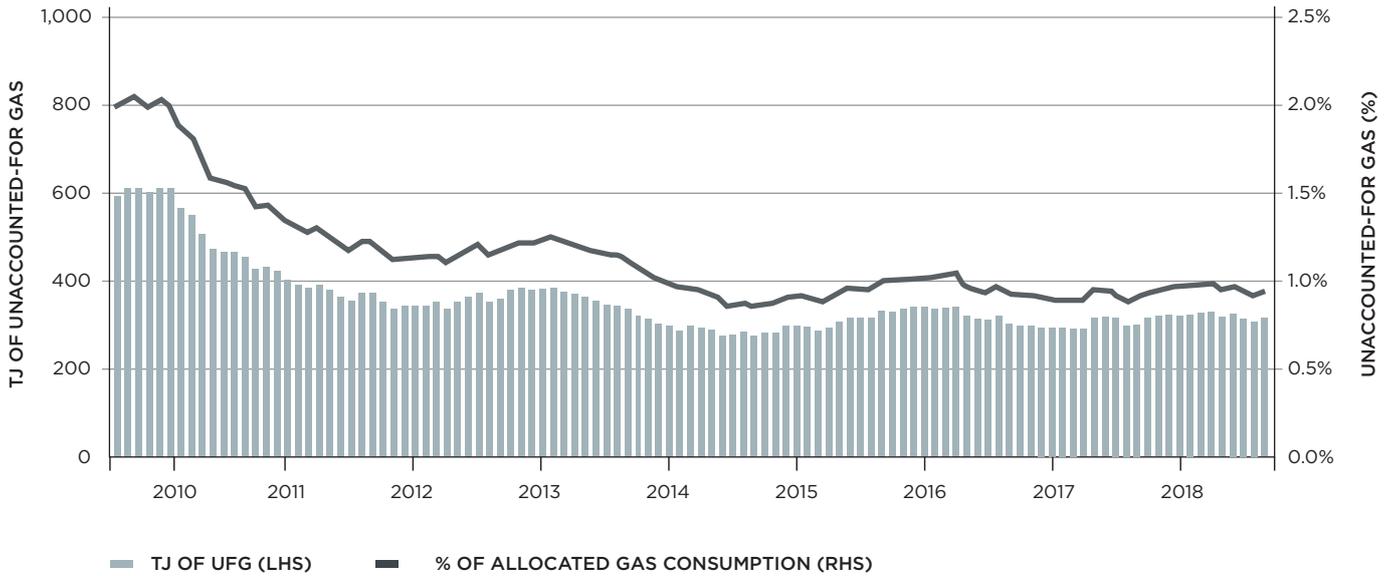
The Reconciliation Rules have been instrumental in reducing the level of unaccounted-for gas (UFG), which is the difference between the amounts of gas that retailers estimate their customers have used and the actual gas volume leaving the transmission system at a gas gate and entering the local distribution 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.

Since 2009, annual UFG has fallen from 600,000 gigajoules (GJ) to about 300,000 GJ, or from about two percent of gas consumed to about one percent (Figure 6).

The move to a rules-based regime, and the lower amounts of UFG associated with it, have delivered an ongoing stream of cost savings to the industry worth several million dollars a year. Benefits include improved market efficiency, more accurate retailer reporting, more equitable allocation of UFG among retailers, greater information transparency, and both performance and event auditing that can more readily identify anomalies in consumption data.

⁴ <http://www.justice.gov/atr/public/guidelines/hhi.html>

Figure 6: Annual unaccounted for gas



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 five times since they came into full effect in 2010. The most recent event was in May 2017, caused by a system imbalance related to excess demand during a planned production station outage. Gas Industry Co maintains a close watch on the effectiveness of the CCM Regulations through the monitoring of critical contingency events and annual exercises. Experience from events and exercises is used to refine the critical contingency arrangements in a process of continual improvement.

Compliance with Governance Rules and Regulations

The Compliance Regulations provide for the monitoring and enforcement of the other gas governance rules and regulations. They are designed as an efficient, low-cost means of determining and, where appropriate, settling rule 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. The Rulings Panel can issue fines, make orders for compensation, make orders directing compliance, and suspend or terminate the rights of an industry participant under any gas governance regulation or rule.

Gas Industry Co liaises closely with participants to ensure there is a good understanding of regulatory requirements. The amount of enforcement activity that we need to undertake is typically low, as participants are generally diligent in ensuring their business processes are compliant with regulatory requirements.

Work programme & indicative activities

FY2020 – 2022

This section outlines the scope of Gas Industry Co's operations for the financial years ended 30 June 2020 to 2022.

The FY2020 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, the changing nature of the industry and the 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, which was broadly supported in submissions. The submissions themselves, and the Analysis of Submissions, can be found on Gas Industry Co's website.

STRATEGIC OBJECTIVE 1

Promote efficient, competitive and confident gas markets

Retail Gas Contracts Oversight Scheme

The Retail Gas Contracts Oversight Scheme assesses 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. The most recent full assessment was undertaken in late 2018, which concluded that retail contracts showed 'substantial' compliance with the benchmarks.

Gas Industry Co aims to conduct full reviews at three-yearly intervals, and the next one is scheduled for FY2022. Gas Industry Co will also provide information to assist new entrant retailers to understand their obligations and governance processes.

Gas Distribution Contracts Oversight Scheme

The Gas Distribution Contracts Oversight Scheme assesses gas distributors' contracts with gas retailers against a common 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.

Gas Industry Co will continue to assess progress with executing new distribution contracts consistent with the Distribution Scheme principles. If required, Gas Industry Co will review the Distribution Scheme, with a focus on its effectiveness in facilitating reasonable terms and conditions for access to and use of distribution pipelines. Gas Industry Co will consider any changes or other actions that arise from this review and report our findings to stakeholders.

Retailer insolvency

This workstream aims to manage the market issues created when a gas retailer becomes insolvent. Because an instance of retailer insolvency can unfold quickly, Gas Industry Co has developed an agile approach that would allow us to quickly develop a recommendation for urgent regulations that are tailored to the specific situation, in the case of a retailer becoming insolvent. To do this, Gas Industry Co has developed a framework that sets out the steps we would take in the event of a retailer insolvency and provides a template for urgent regulation drafting instructions.

With the implementation of the GTAC, Gas Industry Co intends to revisit the framework arrangements to identify any minor amendments that need to be made to the drafting instructions. It is not expected that any routine activity will be required in FY2020 beyond that already provided for within the audits under the Switching Rules (ie checking that registry participants are able to meet their obligations under those rules).

Gas Industry Co will maintain a watching brief in this area and will implement retailer insolvency arrangements as necessary in the unlikely event of a retailer insolvency. Retailer insolvencies are very low-frequency events, but they have a potentially high impact on the retail market, which is why, if intervention is required, they need to take place in an orderly and timely manner.

Gas quality

In FY2015, Gas Industry Co published a Gas Quality Requirements and Procedures document describing the legal landscape in relation to gas quality, clarifying the responsibilities of industry participants, and relating how those parties were performing their respective roles. This work was in response to stakeholder concerns that the supply chain participants may not have clear and comprehensive responsibility and liability for gas quality.

Stakeholders have re-visited some aspects of gas quality while developing the GTAC arrangements. As well as simplifying those arrangements by bringing them under a single code, the GTAC would also bring improved transparency. We will revise the Gas Quality Requirements and Procedures document to reflect these changes.

Gas Industry Co also intends to pursue improvements to the notification of gas quality excursions and procedures for managing gas quality incidents.

Regulation and rule changes

The objective of this workstream is to ensure efficient, effective regulatory arrangements. Details of all regulations and rules administered by Gas Industry Co can be found on our website.

Downstream reconciliation

Gas Industry Co intends to keep the D+1 Pilot Scheme running and to continue to make refinements to its calculation and operation.

The calculations underlying the D+1 Pilot Scheme are based on the transmission access arrangements in place at the time of their development. With the implementation of the GTAC, Gas Industry Co will revise the Pilot Scheme to provide data at Zone and Dedicated Delivery Point levels, as required under the GTAC.

We will also begin the process of amending the Reconciliation Rules to formalise the requirements and procedures for daily day-after allocations, in consultation with stakeholders. Subject to Ministerial approval of a recommendation to amend the Reconciliation Rules, Gas Industry Co will work to implement the changes, including developing and testing new supporting allocation systems.

Critical contingency management

The CCM Regulations is another set of arrangements that Gas Industry Co intends to review to ensure that it is aligned with the GTAC.

Gas Industry Co has also identified a number of other matters that potentially need updating in the CCM Regulations, including the considerations that feed into setting the critical contingency price and the way in which contingency imbalances are calculated. Other potential amendments may be identified through the process of consulting with stakeholders.

Gas measurement

High-level work to review the current contracting arrangements between metering equipment providers and retailers, as well as consider the outlook for the introduction of gas smart metering technology was completed in 2017. A technical advisory group was established to develop a minimum voluntary standard for gas advanced metering. However, that work is pending further information on the capabilities of devices that are likely to be deployed by meter owners. Once the standard is developed and consulted upon, it is anticipated that it will be reviewed on an annual basis. Current indications are that there will be little, if any, work required of Gas Industry Co in FY2020 in this area.

Gas Industry Co intends to keep a watching brief and will review and update the advanced metering standards document if required.

Long-term gas supply/demand study

Gas Industry Co first published a study on long-term gas supply and demand scenarios in 2012, and updated reports have been published in 2014 and 2016. The reports survey the gas supply and demand landscape in New Zealand and analyse a range of supply scenarios. Each report also takes an in-depth look at a topic relevant to natural gas: gas supply, pipeline capacity, electricity generation, industrial demand and distribution-level demand projections. Gas Industry Co intends to continue to publish an updated report biennially. The next report is due to be published in 2019.

Wholesale market

The emsTradepoint Wholesale Market (eTp) has now been in operation for over five years and has increased in both membership and volume over that time. We note that the GPS seeks an outcome of 'efficient arrangements for the short-term trading of gas' and eTp makes a clear contribution to that outcome.

Gas Industry Co intends to continue to monitor activity and developments in the wholesale market with a focus on the market's role as the source of volume and pricing for transmission balancing.

Information disclosure

Concerns have been expressed by some energy sector participants regarding information transparency in the gas wholesale market, particularly information regarding upstream and major user outages (both planned and unplanned). This issue was given some consideration during the work on developing the GTAC, but no resolution has been reached among stakeholders.

In parallel, the Minister wrote to Gas Industry Co expressing concern with the lack of transparency regarding upstream activities and asking whether the Gas Act provides the necessary tools to address this issue. We have responded that the Gas Act would need to be amended to support any enduring, stand-alone regulation. At the same time, we have commenced a workstream to consider options for addressing this issue as well as seeking information as to what the upstream sector, together with large end-users, may be willing to do to improve information transparency.

By the end of FY2019, Gas Industry Co will have consulted on an options paper and analysed stakeholder submissions, and we expect to be able to identify whether an issue exists and if a non-regulated solution is feasible or if regulation is likely to be required. If the outcome of our analysis indicates a non-regulated solution is feasible, we will proceed to implement that solution. Alternatively, if a non-regulated solution is not feasible, we will prepare and consult on a statement of proposal for regulation.

STRATEGIC OBJECTIVE 2

Facilitate efficient use of, and investment in, gas infrastructure

Gas transmission access

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.

The past two years have seen an intense amount of activity dedicated to the development of a single transmission access code, from First Gas, stakeholders, and Gas Industry Co. This work is expected to continue in FY2020 with a focus on implementation of the new, single transmission code – the GTAC. This will remain a significant workstream requiring continued attention.

Transmission pipeline balancing

The last significant improvement to transmission pipeline balancing occurred in FY2016 when market-based balancing (MBB) was implemented. Implementation of the GTAC will significantly reorient the approach to pipeline balancing. While Gas Industry Co believes that the changes will bring further improvements some stakeholders have expressed some concerns and have asked that Gas Industry Co continues to monitor balancing outcomes. Given the importance of efficient pipeline balancing, we agree that this is necessary and will be continuing to track and report on balancing performance.

Hydrogen-related matters

Gas Industry Co will keep a watching brief on new and emerging developments around hydrogen and ensure it can address any specific requests from the Minister. Our preliminary view is that there appear to be no barriers in the Gas Act to Gas Industry Co being involved in relation to hydrogen matters.

Accordingly, this work can be accommodated within the Company's available resources or by adjusting our priorities for FY2020.

Transmission code changes

Under a Memorandum of Understanding with First Gas, Gas Industry Co has a role in processing Maui Pipeline Operating Code (MPOC) change requests on an 'as required' basis. The GTAC envisages a similar role for Gas Industry Co with respect to processing and approving/declining code changes.

Transmission pipeline interconnection

To address earlier concerns about poorly defined interconnection processes, uncertain technical requirements, and confusing roles and responsibilities, Gas Industry Co established Guidelines on Interconnection with Transmission Pipelines (Guidelines). We have also formally reviewed improvements the previous pipeline owners have made to their interconnection arrangements in response to those Guidelines.

The new transmission system owner, First Gas, has merged the interconnection arrangements for the Maui and non-Maui pipelines. Once the GTAC is implemented, the core provisions of interconnection will be as set out in that code. This should greatly simplify the interconnection process for anyone looking to interconnect their facilities with the transmission system.

We will re-visit the Guidelines and, if they still add value, will update them accordingly. If they have served their purpose, we will consider whether anything else is required to ensure that the resulting improvements are not lost.

Gas transmission security and reliability

Gas Industry Co has previously developed and consulted on a Gas Transmission Security and Reliability Issues Paper, dated April 2016. Following the First Gas acquisition of the transmission pipelines, we issued a Gas Transmission Security and Reliability Update in March 2017. That paper canvassed issues that had been raised by stakeholders and found that they had been substantially addressed, particularly in First Gas's consolidated and improved Asset Management Plan (AMP).

In the wake of wider energy sector concerns about risk management and the resilience of key infrastructure, we note that the Commerce Commission has recently commissioned a review of risk management practices in the gas pipeline business. We will follow progress of this review to see how industry practice measures up to external scrutiny. If concerns arise, we will consider whether Gas Industry Co can usefully contribute to addressing those. In addition, we expect that matters with a strong security and reliability component will emerge from time to time, and these matters will be dealt with when they arise. Gas Industry Co will continue to monitor successive asset management plans.

STRATEGIC OBJECTIVE 3

Deliver effectively on Gas Industry Co's accountabilities as the industry body

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'. The Reconciliation Rules have been instrumental in reducing the level of unaccounted-for gas (UFG) at the final allocation stage (see the discussion under Industry Performance for details).

The Reconciliation Rules require Gas Industry Co to appoint and manage the allocation agent as a service provider. Gas Industry Co also closely monitors the allocation results, with an eye to identifying issues that need attention or situations that warrant the commissioning of an event audit.

The Reconciliation Rules also oblige Gas Industry Co to commission performance audits of the allocation agent and allocation participants at regular intervals. Performance audits are generally commissioned every two to three years. Event audits, which investigate particular issues or events, are commissioned as required.

In addition to the tasks that are required under the Reconciliation Rules, Gas Industry Co expects to continue the pilot project for D+1 allocations until it is either overtaken by changes to the Reconciliation Rules or a better solution identified. The D+1 project is discussed further in the Regulation and Rule Changes section.

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 have facilitated a marked increase in customer switching since their inception (see the discussion under Industry Performance for details).

Under the Switching Rules, Gas Industry Co appoints and monitors the registry operator as a service provider, and we monitor and report on switching statistics. Performance auditing provisions were added to the Switching Rules in 2015, and performance audits of retailers, distributors, and meter owners are done in conjunction with audits under the Reconciliation Rules.

Over the past few years Gas Industry Co, along with the Electricity Authority, has provided modest support to Consumer NZ's 'Powerswitch' to ensure the continued existence of an independent, credible source of information for consumers. This support will continue through FY2020.

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 CCM Regulations have been activated five times since they came into full effect in 2010: three have been caused by production station outages, one by a break in the Maui pipeline, and, in May 2017, a system imbalance event.

Under the CCM Regulations, Gas Industry Co appoints and monitors the performance of the critical contingency operator (CCO), who is responsible for determining, managing, and terminating critical contingencies, as well as associated activities such as offering stakeholder training and running exercises. Gas Industry Co is also responsible for processing gas consumers' applications for designations for critical care, essential services, critical processing, and electricity supply. We also appoint expert advisers to analyse critical contingency management plans when required.

In the case of a critical contingency, Gas Industry Co considers the performance of the CCO and the effectiveness of the CCM Regulations in managing the situation, with a view to implementing improvements if appropriate. Following non-regional critical contingencies (ie, those that involve the entire transmission system), Gas Industry Co appoints an industry expert to determine a critical contingency price and administers the contingency pool used to settle contingency imbalances.

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 and 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.

Consistent with obligations under the Compliance Regulations, Gas Industry Co performs the market administrator role, appoints and monitors the market investigator. The Rulings Panel is appointed by the Minister. We provide assistance to the market investigator and the Rulings Panel as required. Gas Industry Co also monitors compliance trends for indications of regulatory inefficiency.

Statement of Intent and Annual Report

The Gas Act requires that the industry body provide its Annual Report to the Minister within three months of the end of the financial year (the Minister then tables the Annual Report in the House of Representatives). Similarly, annual statements of intent are required to be submitted to the Minister for comment prior to being finalised and published.

STRATEGIC OBJECTIVE 4

Develop and communicate the role of gas in meeting New Zealand's energy needs

New Zealand Gas Story

During FY2013, Gas Industry Co published the first New Zealand Gas Story. Since then, the publication has been updated annually to ensure it remains current and topical. Apart from fulfilling Gas Industry Co's statutory reporting requirement, this work is intended to help stakeholders to understand the industry and to assist industry participants 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.

Gas Industry Co intends to continue its periodic update of The New Zealand Gas Story.

Other reports

Gas Industry Co is required by the Gas Act to report on the present state and performance of the gas industry. It does this through a number of publications including the Quarterly Reports, Switching Statistics and Industry Performance Measures. Further occasional reports will be published, and existing reports updated, where then can add value to the industry.

Financial matters

Gas Industry Co develops funding budgets to support its work programme proposals as part of the consultation process discussed in the section Work Programme Priorities above.

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

Levy Funding

Section 43ZZB of the Gas Act enables Gas Industry Co to recommend to the Minister that regulations be made to require industry participants 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 levy payers in the following year unless special circumstances warrant otherwise.

Details of funding for FY2020 are included in industry consultation and the annual recommendation to the Minister, which results in annual levy regulations. In summary for FY2020:

- » an annual levy of \$3,774,336 from 1 July 2019, comprising a wholesale levy and a retail levy.
- » the wholesale levy revenue is \$2,027,994 for FY2020 and will be collected each month from the relevant levy payers at a rate of 1.1279 c/GJ based on each industry participant's volume of gas purchased from gas producers.
- » the retail levy revenue is \$1,746,342. This is calculated based on Gas Industry Co's estimate of 285,000 active ICPs, at a levy rate of \$6.12/ICP per annum.

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 Compliance Regulations contain market fee provisions. These fees are used to recover costs of external service providers and consultants, as provided for in the relevant regulations.

Annual Fees

Gas Industry Co's Constitution provides that the Board may set an annual fee each year in respect of each share issued. The annual fee is currently \$2,000 per shareholder per annum. The Board has resolved that these fees will be set aside to establish cash reserves.

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 FY2020 Gas Industry Co levy.

Further details about the assumptions, revenue calculations and workstream expenses used to calculate the FY2020 levy can be found in the document, Consultation on Gas Industry Co FY2020 work programme and Levy, issued in December 2018.

The FY2019 forecast was approved by Gas Industry Co's Board and includes actual results for the period 1 July 2018 to 28 February 2019, and an up-to-date forecast to 30 June 2019.

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 FY2019 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 2019



Robin Hill
DEPUTY CHAIR

FORECAST STATEMENT OF FINANCIAL PERFORMANCE

| | Budget FY2020 \$ | Forecast FY2019 \$ | Actual FY2018 \$ |
|---|------------------------|--------------------------|------------------------|
| REVENUE | | | |
| Wholesale Levy | 2,030,136 | 2,138,820 | 2,297,692 |
| Retail Levy | 1,744,200 | 1,762,118 | 1,736,464 |
| <i>Levy Revenue Subtotal</i> | <i>3,774,336</i> | <i>3,900,938</i> | <i>4,034,156</i> |
| Market Fees | 1,458,000 | 1,270,182 | 1,268,887 |
| Annual Fees | 26,000 | 26,000 | 28,000 |
| Interest Income | 35,000 | 25,451 | 33,559 |
| <i>Subtotal Other Revenue</i> | <i>1,519,000</i> | <i>1,321,633</i> | <i>1,330,446</i> |
| TOTAL REVENUE | 5,293,336 | 5,222,571 | 5,364,602 |
| Refunded Levies | - | (704,085) | (667,243) |
| Net Revenue | 5,293,336 | 4,518,486 | 4,697,359 |
| EXPENSES | | | |
| Depreciation & Amortisation | 37,873 | 32,624 | 36,692 |
| Operating lease expenses | 235,730 | 237,097 | 233,664 |
| Fees paid to audit firm - financial statement audit | 15,750 | 15,750 | 15,756 |
| Fees paid to audit firm - other services | 12,949 | - | - |
| Directors' fees | 262,460 | 262,460 | 262,460 |
| General expenses | 318,142 | 332,361 | 239,931 |
| Recruitment expenses | - | 8,750 | 79,164 |
| Technical, economic, and legal advice | 673,500 | 585,135 | 511,604 |
| Service Provider Fees | 1,458,000 | 1,270,182 | 1,225,277 |
| Kiwisaver contributions | 53,024 | 51,405 | 51,771 |
| Employee benefit expense | 2,186,312 | 2,124,142 | 2,214,811 |
| TOTAL EXPENSES | 5,253,740 | 4,919,906 | 4,871,130 |
| Finance Costs | - | - | 2,810 |
| TOTAL EXPENDITURE | 5,253,740 | 4,919,906 | 4,873,940 |
| PROFIT / (LOSS) BEFORE TAX | 39,596 | (401,420) | (176,581) |
| Income Tax Expense | 9,800 | 7,126 | 9,396 |
| PROFIT / (LOSS) FOR THE YEAR | 29,796 | (408,546) | (185,977) |

FORECAST STATEMENT OF FINANCIAL POSITION

| | Budget FY2020 \$ | Forecast FY2019 \$ | Actual FY2018 \$ |
|----------------------------------|------------------------|--------------------------|------------------------|
| CURRENT ASSETS | | | |
| Cash and cash equivalents | 208,909 | 171,240 | 1,202,308 |
| Term Deposit | 1,100,000 | 1,100,000 | 700,000 |
| Trade and other receivables | 145,871 | 75,756 | 57,911 |
| Prepayments | 50,798 | 51,344 | 68,168 |
| Income tax receivable | 9,800 | 7,126 | - |
| TOTAL CURRENT ASSETS | 1,515,378 | 1,405,466 | 2,028,387 |
| NON-CURRENT ASSETS | | | |
| Property, plant & equipment | 104,778 | 80,290 | 107,625 |
| Intangible assets | 2,853 | 11,957 | 5,554 |
| TOTAL NON-CURRENT ASSETS | 107,631 | 92,247 | 113,179 |
| TOTAL ASSETS | 1,623,009 | 1,497,713 | 2,141,566 |
| CURRENT LIABILITIES | | | |
| Trade and other payables | 391,201 | 342,757 | 544,431 |
| Employee entitlements | 202,460 | 155,404 | 189,036 |
| Redemable Shares | 13 | 13 | 14 |
| TOTAL CURRENT LIABILITIES | 593,674 | 498,174 | 733,481 |
| TOTAL LIABILITIES | 593,674 | 498,174 | 733,481 |
| NET ASSETS | 1,029,335 | 999,539 | 1,408,085 |
| <i>Represented by</i> | | | |
| Industry Reserves | 273,335 | 269,539 | 704,085 |
| Retained Earnings | 756,000 | 730,000 | 704,000 |
| TOTAL SHAREHOLDERS' FUNDS | 1,029,335 | 999,539 | 1,408,085 |

FORECAST STATEMENT OF MOVEMENT IN EQUITY

| | Industry Reserves | Retained Earnings | Total | Industry Reserves | Retained Earnings | Total |
|-------------------------------------|----------------------|----------------------|------------------|----------------------|----------------------|------------------|
| | Budget FY2020 | | | Forecast FY2019 | | |
| OPENING BALANCE | 269,539 | 730,000 | 999,539 | 704,085 | 704,000 | 1,408,085 |
| Net surplus/(deficit) for the year | - | 29,796 | 29,796 | - | (408,546) | (408,546) |
| Industry Advances Reserves transfer | 3,796 | (3,796) | - | (434,546) | 434,546 | - |
| FORECAST CLOSING BALANCE | 273,335 | 756,000 | 1,029,335 | 269,539 | 730,000 | 999,539 |

FORECAST STATEMENT OF CASH FLOWS

| | Budget FY2020 \$ | Forecast FY2019 \$ | Actual FY2018 \$ |
|---|------------------------|--------------------------|------------------------|
| <i>CASH FLOWS FROM OPERATING ACTIVITIES</i> | | | |
| Levy revenue | 3,774,336 | 3,908,685 | 4,052,231 |
| Market fee revenue | 1,458,000 | 1,253,367 | 1,162,647 |
| Annual fees | 26,000 | 26,000 | 28,000 |
| Interest received | 35,000 | 25,451 | 29,046 |
| Net GST | - | - | 107,646 |
| | 5,293,336 | 5,213,503 | 5,379,570 |
| <i>CASH WAS APPLIED TO</i> | | | |
| Payments to suppliers | (2,723,871) | (2,729,637) | (2,365,861) |
| Payments to employees | (2,239,336) | (2,165,052) | (2,307,968) |
| Payments to directors | (262,460) | (262,460) | (262,460) |
| Refund of levy to industry participants | - | (693,527) | (655,635) |
| Taxes paid | - | (3,860) | (8,133) |
| Net GST | - | (1,728) | - |
| | (5,225,667) | (5,856,264) | (5,600,057) |
| NET CASH INFLOWS FROM OPERATING ACTIVITIES | 67,669 | (642,761) | (220,487) |
| <i>CASH FLOWS FROM INVESTING ACTIVITIES</i> | | | |
| Purchase of property, plant and equipment | (30,000) | - | (57,674) |
| Purchase of intangible assets | - | 11,693 | - |
| Term Deposit | - | (400,000) | (700,000) |
| NET CASH FLOWS FROM INVESTING ACTIVITIES | (30,000) | (388,307) | (757,674) |
| NET CASH FLOWS | 37,669 | (1,031,068) | (978,161) |
| Opening cash balance | 171,240 | 1,202,308 | 2,180,469 |
| CLOSING CASH BALANCE | 208,909 | 171,240 | 1,202,308 |

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 2017 and expires on 30 November 2023 at an annual rental of approximately \$251,330.

Other operating lease commitments are for office equipment.

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

| | Budget FY2020 \$ | Forecast FY2019 \$ |
|---|------------------------|--------------------------|
| BUILDING LEASE COMMITMENTS | | |
| Within one year | 251,330 | 251,330 |
| Later than one year but not later than five years | 607,381 | 858,711 |
| Later than five years | - | - |
| TOTAL OPERATING LEASE COMMITMENTS | 858,711 | 1,110,041 |
| EQUIPMENT LEASE COMMITMENTS | | |
| Within one year | - | 580 |
| Later than one year but not later than five years | - | - |
| Later than five years | - | - |
| TOTAL EQUIPMENT LEASE COMMITMENTS | - | 580 |
| OPERATING LEASE COMMITMENTS | | |
| Within one year | 251,330 | 251,910 |
| Later than one year but not later than five years | 607,381 | 858,711 |
| Later than five years | - | - |
| TOTAL OPERATING LEASE COMMITMENTS | 858,711 | 1,110,621 |
| SERVICE PROVIDER COMMITMENTS | | |
| Within one year | 761,424 | 761,424 |
| Later than one year but not later than five years | 1,161,080 | 1,694,764 |
| Later than five years | - | 164,288 |
| TOTAL SERVICE PROVIDER COMMITMENTS | 1,922,504 | 2,620,476 |

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 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 2020-2022 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 \$3,774,336 is assumed to be effective from 1 July 2019 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 \$2,027,994 for FY2020 and will be collected each month from the relevant levy payers at a rate of 1.1279c/GJ based on each industry participant's volume of gas purchased from gas producers.
- » The retail levy revenue is budgeted to be \$1,746,342. This is calculated based on Gas Industry Co's estimate of 285,000 active ICPs, at a levy rate of \$6.12/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 FY2020 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 FY2020. 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 2019 is approximately \$999,539. Of this, \$269,539 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, \$730,000, 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 FY2020 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).

Alignment with government policy objectives and outcomes

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.

| 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 » 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"> » Provide small consumers with an effective complaints process » Ensure retail contracts adequately protect the long-term interests of small consumers » Provide public information on the performance and state of the gas sector » Ensure gas governance arrangements are supported by appropriate compliance and dispute resolution processes » Provide efficient arrangements for short-term gas trading » Enable accurate, efficient, and timely arrangements for the allocation and reconciliation of upstream gas quantities » Provide an efficient market structure for the provision of gas metering, pipeline, and energy services |
| 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"> » Gas industry participants and new entrants are able to access third party gas processing facilities; transmission pipelines; and distribution pipelines; on reasonable terms and conditions » Consistent standards and protocols apply to the operations relating to access to all distribution pipelines |
| 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"> » 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 |
| Delivered gas costs subject 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 |
| Proper and efficient management of 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 |

| What Gas Industry Co has done | Work programme FY2020 | Future Gas Industry Co work areas |
|---|--|---|
| <ul style="list-style-type: none"> » Created the Retail Contracts Oversight Scheme in 2010. It provides assurance that standard retail contracts protect small consumers' long-term interests » Carried out assessments in 2010, 2011, 2012, 2015 and 2018 » Considered that further LPG regulation is not currently needed (FY2015) and reviewed retail market arrangements for LPG (FY2019) » Published The New Zealand Gas Story and the Long-Term Gas Supply and Demand Study » Recommended the Gas (Downstream Reconciliation) Rules 2008; ongoing administration through the allocation agent » Recommended the Gas Governance (Compliance) Regulations 2008; ongoing administration through market administrator, independent investigator, and Rulings Panel » A private company created a gas trading market in 2013 » D+1 implemented in December 2015 to assist the more efficient arrangements for balancing gas » Completed a comparative assessment of First Gas's new gas transmission access code against the current arrangements applying the requirements of the Gas Act and GPS. » Established a technical advisory group to develop minimum voluntary standards for gas advanced metering. | <ul style="list-style-type: none"> » Assist new entrant retailers, including by reviewing new-entrant retail contracts » Continue to work with Utilities Disputes to identify and address any systemic issues raised by gas consumers » Update the Long-Term Gas Supply and Demand Study » Continue market administrator work » Refine D+1 and consider changes to the Downstream Reconciliation Rules to incorporate D+1 into the Rules » Oversee industry implementation of the GTAC » Respond to concerns regarding asymmetric information, particularly information regarding upstream outages, and consider whether a non-regulated solution or regulation is required | <ul style="list-style-type: none"> » Continue market administrator work » Continue to provide information on the state and performance of the gas sector in future editions of The New Zealand Gas Story, and supply/demand studies |
| <ul style="list-style-type: none"> » Reviewed gas distribution use-of-system agreements with retailers » Completed a comparative assessment of First Gas' new gas transmission access code against the current arrangements applying the requirements of the Gas Act and GPS. » A private company created a gas trading market in 2013 » Post-implementation review of market-based balancing | <ul style="list-style-type: none"> » Oversee industry implementation of the GTAC » Continue to assess progress with executing new gas distribution use-of-system agreements consistent with the Distribution Scheme principles | <ul style="list-style-type: none"> » Monitor short-term gas trading with a particular focus on the market's role as the source of volume and pricing for transmission balancing |
| <ul style="list-style-type: none"> » Recommended the Gas (Switching Arrangements) Rules 2008 » Completed a comparative assessment of First Gas's new gas transmission access code against the current arrangements applying the requirements of the Gas Act and GPS. | <ul style="list-style-type: none"> » Monitor the wholesale market » Oversee industry implementation of the GTAC | <ul style="list-style-type: none"> » Monitor short-term gas trading with a particular focus on the market's role as the source of volume and pricing for transmission balancing |
| <ul style="list-style-type: none"> » Addressed in multiple workstreams, including switching, downstream reconciliation, and single gas transmission code » Revoked Gas Processing Information Disclosure Rules 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 to replace the Company's trading platform | <ul style="list-style-type: none"> » Continue to publish monthly switching statistics | <ul style="list-style-type: none"> » Monitor short-term gas trading with a particular focus on the market's role as the source of volume and pricing for transmission balancing |
| <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 » Completed a comparative assessment of First Gas' new gas transmission access code against the current arrangements applying the requirements of the Gas Act and GPS. | <ul style="list-style-type: none"> » Review critical contingency price and imbalance arrangements. Ensure that the arrangements for the management of critical gas outages align with transmission access arrangements » Review the adequacy of industry arrangements for notifying gas quality excursions and procedures for managing gas quality incidents | <ul style="list-style-type: none"> » Work 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 » Completed a comparative assessment of First Gas's new gas transmission access code against the current arrangements from a safety perspective (in particular, the Gas (Safety and Measurement) Regulations) 2010. | | <ul style="list-style-type: none"> » Work closely with the Commerce Commission to ensure that security and reliability are adequately reported on |

Other information

Additional Reporting

In addition to the reporting described in 'Statement of Intent and Annual Report' and 'Other Reports' (page 18), Gas Industry Co also 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 |
| CCM Regulations | Critical contingency operator | Core Group |

Directory

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Board of Directors

Rt Hon James (Jim) Bolger, ONZ, *Chair, Independent Director*

Robin Hill, B Comm, *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

Gabriel Selischi, MSc (Power Engineering), MBA

Executive

Andrew Knight, BMS (Hons), CA, *Chief Executive*

Susan Dunne, LLB, BCA, CA, *General Manager Corporate Services*

Auditors

KPMG, Wellington

Bankers

Westpac New Zealand Limited

Shareholders

Contact Energy Limited

emsTradepoint Limited

First Gas Limited

Genesis Energy Limited

Greymouth Gas New Zealand Limited

Mercury NZ Limited

Methanex New Zealand Limited

New Zealand Oil & Gas Limited

Nova Energy Limited

OMV New Zealand Limited

Powerco Limited

Shell (Petroleum Mining) Company Limited

Trustpower Limited

Vector Limited

