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RECOMMENDATION

# Gas Industry Co Recommendation to Minister of Energy and Resources to make Gas (Levy of Industry Participants) Regulations 2019

# Executive Summary

Pursuant to section 43ZZB of the Gas Act 1992 (the Act), Gas Industry Co recommends to the Minister of Energy and Resources that regulations be made under section 43ZZE to require industry participants to pay levies to the industry body in respect of the year commencing 1 July 2019, totalling \$3,774,336 on the following basis:

- From every gas retailer who is an industry participant on the last day of each month, a retail levy based on one twelfth of the annual retail levy of \$6.12 for each ICP for each retail customer.
- From every industry participant on the first day of each month, a wholesale levy rate of 1.1279c/GJ based on gas purchases made directly from gas producers during the previous month.

Gas Industry Co remains principally reliant on annual levies to provide the effective governance of the downstream gas sector that Part 4A of the Act requires. Gas Industry Co believes that the recommended levy rates are reasonable, and present good value for gas consumers and the wider industry.

The contents of this Levy Recommendation achieved broad support from industry stakeholders, through a robust annual consultation process.

This Levy Recommendation has been approved by Gas Industry Co's Board of Directors.

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# 1. Introduction

The Government and the gas industry have implemented a unique co-regulatory model in which a specially established 'industry body' develops and maintains governance arrangements for consumers and other participants in gas markets. Gas Industry Co was established in 2004 to perform the role of the industry body as set out in Part 4A of the Act. Gas Industry Co has two main sources of funding to meet the total costs of delivering its work programme and other aspects of its role as the industry body – market fees and the levy.

## 1.1 Market fees

Established gas governance rules and regulations include provisions to recover costs directly required to meet Gas Industry Co's obligations under those arrangements (referred to as 'market fees'). These cover the contractually agreed costs of any service providers (particularly the Allocation Agent, the Registry Operator and the Critical Contingency Operator) and any other expected direct costs related to the monitoring of those arrangements.

A formal estimate of market fees for each set of rules or regulations is published two months before they apply with each new financial year commencing on 1 July. Market fees collected are applied to actual expenses incurred for each set of rules or regulations. Any shortfall or excess fees are invoiced/credited to the market fee payers in a year-end 'wash-up'.

## 1.2 Industry levy

The levy funds the industry body's costs that are not covered by market fees, including the direct costs of workstreams and non-operational expenditure for the business.

The Act provides for the levy to be collected through annual regulations, on recommendation to the Minister by the industry body. Gas Industry Co develops its annual Levy Recommendation through a consultation process with levy payers and other stakeholders. This process includes development of an annual Work Programme, an indication of future activity, and the resulting estimated Total Work Programme Costs covering all activities to be undertaken by the industry body.

This paper provides that recommendation for the year commencing 1 July 2019 (FY2020).

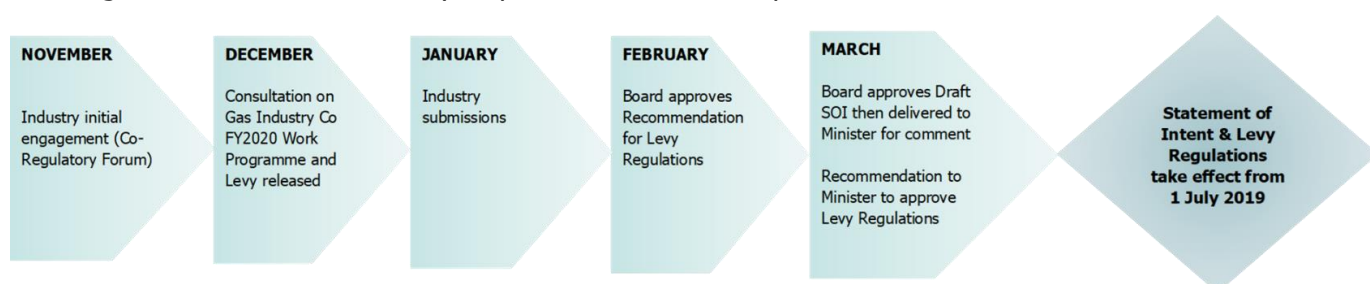
## 2. Consultation Process and Outcomes

### 2.1 Levy Consultation Process

In developing its annual Levy Recommendation to the Minister, Gas Industry Co consults on all aspects of its Work Programme, including costs and any forward indication for subsequent requests to be included in the Statement of Intent, and engages with interested stakeholders, including gas industry participants and major gas users. The process includes consultation on the proposed levy rate and amount, consistent with section 43ZZD(2)(b).

### 2.2 Key Steps in FY2020 Consultation Process

The diagram below sets out the key steps in the consultation process:



The consultation process commenced at the annual Co-Regulatory Forum on 30 November 2018. Feedback from this Forum was generally positive, and the paper Consultation on Gas Industry Co FY2020 Work Programme and Levy (Consultation Paper) was published on 18 December 2018.

The Consultation Paper:

1. Sets out Gas Industry Co's strategic direction and supporting rationale;
2. Describes the work that Gas Industry Co will undertake in FY2020 and the estimated costs to carry out this work;
3. Outlines the amount of the Levy Funding Requirement for FY2020; and
4. Outlines the proposed levy rates for FY2020.

The Consultation Paper notes that elements of the Work Programme for FY2020 and its overall cost estimate will depend on whether the Gas Transmission Access Code (GTAC) is assessed as being materially better and a new code is in place from 1 October 2019. This meant consulting on two scenarios – each requiring their own programmes of work and budgets (referred to in the Consultation Paper as the "New Code" scenario and the "Status Quo" scenario).

Under both scenarios, the proposed FY2020 Work Programme includes meeting statutory requirements, such as administration of existing gas governance regulations, and seeks to address Government and industry priorities through the completion of key project deliverables. It continues existing multi-year workstreams and reflects significant progress already made in addressing the objectives and outcome set for Gas Industry Co and the industry in the Act and the GPS.

Submissions were invited by 11 February 2019, and were received from First Gas Limited, Genesis Energy Limited, the Major Gas Users Group, Nova Energy Limited, Trustpower Limited and Vector Limited.

Each submission and an Analysis of Submissions have been published on Gas Industry Co's website. In summary, there was broad support for Gas Industry Co's role, Work Programme, estimated costs, and associated levy rates.

### **2.3 GTAC assessment update**

At its meeting on 21 February 2019, Gas Industry Co's Board approved the release of the GTAC final assessment paper which concluded that the GTAC is materially better than the status quo, with a new code expected to be in place from 1 October 2019.

As a result, the Levy Recommendation to the Minister is based on the work programme and associated costs under the "New Code" scenario included in the Consultation Paper, with a proposed levy funding requirement of \$3,774,336 (\$208,215 less than the corresponding budgeted costs for FY2019).

## 3. FY2020 Levy Funding

### 3.1 FY2020 Levy funding summary

The costs corresponding to the Work Programme (set out in Appendix A) and the steps involved in the levy methodology are set out in the following tables. In summary:

- The levy funding requirement is \$3.77m. This is 5.2% lower than the same figure for FY2019 (\$3.98m);
- Total Work Programme costs - based on a combination of the levy funding requirement and market fees are \$5.23m. These have decreased 3.5% from FY2019 (\$5.42m);
- The levy methodology is the same as that used in previous years and is based on the principle of beneficiary pays;
- The retail levy rate is \$6.12/ICP. This is down from \$6.18/ICP in FY2019, a difference of \$0.06/ICP per annum; and
- The wholesale levy is 1.1279c/GJ. This is down from 1.2374c/GJ in FY2019 (an 8.85% decrease).

### 3.2 Levy funding calculation and trends

The following table provides details of the levy funding calculation:

Strategic Objective	TWPC	Indicative Market Fees		Levy Funding Requirement	
		Wholesale	Retail	Wholesale	Retail
<b>Strategic Objective 1</b> Promote efficient, competitive and confident gas markets	758,361				758,361
<b>Strategic Objective 2</b> Facilitate efficient use of, and investment in, gas infrastructure	1,222,002			1,222,002	
<b>Strategic Objective 3</b> Deliver effectively on Gas Industry Co's accountabilities as the gas industry body	3,092,010	891,000	567,000	723,426	910,584
<b>Strategic Objective 4</b> Develop and communicate the role of gas in meeting New Zealand's energy needs	159,963			82,566	77,397
<b>TOTAL</b>	<b>5,232,336</b>	<b>1,458,000</b>		<b>3,774,336</b>	

The following table shows the actual Levy Funding Requirement for FY2015-19, and the recommended Levy Funding Requirement for FY2020, along with published market fees to FY2019 and the indicative estimate for FY2020.

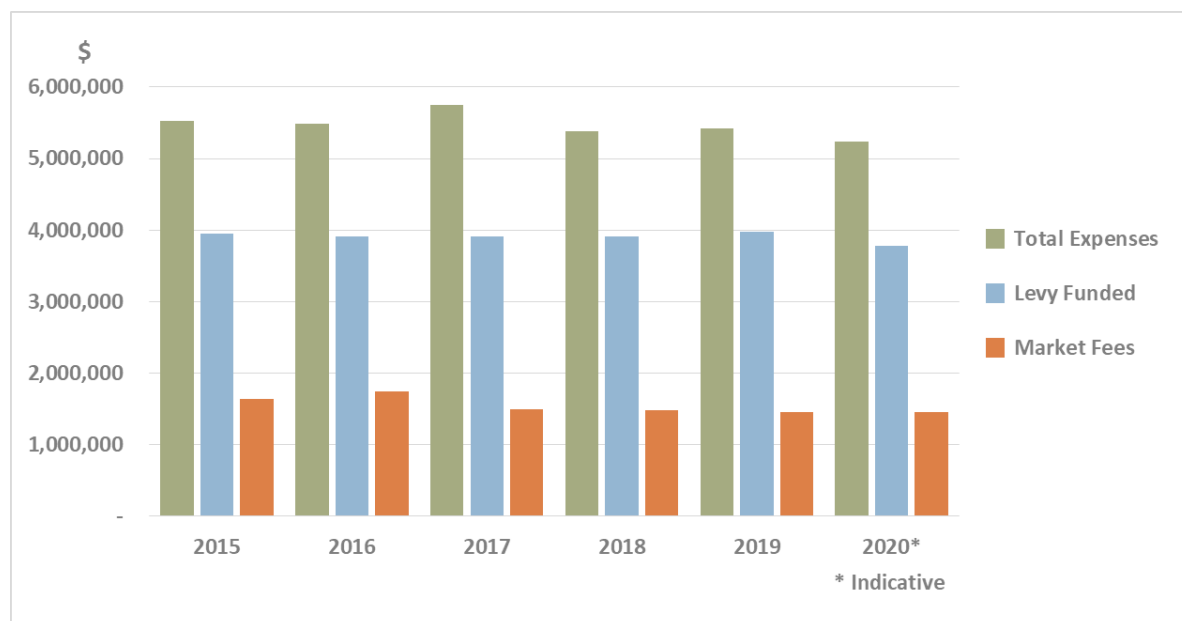
**Table 2: Levy Funding Requirement and Market Fees - FY2015-20**

	Levy Funding Requirement	Market Fees
<b>2015</b>	3,948,818	1,635,396
<b>2016</b>	3,916,821	1,750,000
<b>2017</b>	3,913,060	1,489,000
<b>2018</b>	3,911,481	1,482,000
<b>2019</b>	3,982,551	1,441,169
<b>2020*</b>	3,774,336	1,458,000

1. \*recommended levy funding requirement/indicative market fees

Based on the combination of the FY2020 Levy Recommendation and indicative market fees in table 2, Total Work Programme Costs are expected to be \$5,232,336 for FY2020, compared to \$5,423,720 in FY2019.

**Chart 1: Total Work Programme Costs**



### 3.3 Proposed levy methodology and rates

Gas Industry Co's existing levy methodology:

1. Is based on a set of Levy Principles. In summary, those Principles are economic efficiency, rationality, simplicity, equity, and revenue sufficiency. The full Principles are available on Gas Industry Co's website.
2. Has two components: a wholesale component and a retail component. These components are apportioned according to the cost allocated to each part of the



annual Work Programme, and apportioned among levy payers pro rata with either their wholesale levy volumes or ICP market shares. In years when the Work Programme focusses on retail issues, for instance, the retail levy rate will increase while the wholesale levy will decrease.

These arrangements have remained unchanged since 2007.

**In summary:**

1. The wholesale levy rate has been calculated using an assumption of 180PJ (180,000,000 GJ) of gas consumption during the year (FY2019 182PJ).
2. The retail levy rate is calculated using the current number of ACTIVE-CONTRACTED entries in the gas registry of 285,000 (FY2019 280,000).

This results in the following levy rates:

**Table 3: FY2020 Levy rates**

<b>FY2020 Levy rates</b>			
	<b>Retail</b>	<b>Wholesale</b>	<b>Total</b>
Direct costs	1,149,392	1,323,229	2,472,621
Indirect costs	596,950	704,765	1,301,715
<b>Total Levy Funding Requirement</b>	<b>1,746,342</b>	<b>2,027,994</b>	<b>3,774,336</b>
Basis of apportionment:	Per ICP	Per GJ	
Number	285,000	180,000,000	
Levy rate	\$6.12/ICP	1.1279c/GJ	

The impact of the levy on gas consumers is relatively small. Assuming the levy is passed through to end users, residential gas consumers would each pay approximately \$6.40 per annum, or around 0.67% of their annual gas bill. For larger consumers, the amount of levy paid is proportionate to wholesale gas purchases and adds about 0.2% or less to the unit cost of gas. The largest consumers, who together consume the majority of the gas supply, are active participants in consultation and have raised no objections to the levy rate.

Gas Industry Co has determined that it should refund unutilised levies as soon as the annual accounts have been received by shareholders at the Annual Meeting. This also has some similarity with the wash-up arrangements collected under Market Fees. This policy encourages a predictable and stable levy by removing from the levy calculations any variability resulting from a fluctuating level of reserves.

## 4. Recommendation

Pursuant to section 43ZZB of the Gas Act 1992, Gas Industry Co recommends to the Minister of Energy and Resources that regulations be made to require industry participants to pay levies to the industry body in respect of the year commencing 1 July 2019, totalling \$3,982,551, on the following basis:

1. From every gas retailer who is an industry participant on the last day of each month, a retail levy based on one twelfth of the annual retail levy of \$6.12 for each ICP for each retail customer.
2. From every industry participant on the first day of each month, a wholesale levy rate of 1.1279c /GJ based on gas purchases made directly from gas producers during the previous month.

# Appendix A Work Programme

## 4.1 Strategic objective: provide efficient, competitive and confident gas markets

### Retail contracts oversight scheme (Retail Scheme)

In 2010, Gas Industry Co established a Retail Gas Contracts Oversight Scheme that 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 with the last full review in 2018 having shown 'substantial' compliance.

#### Contingent Activities FY2020

1. Review new-entrant retail contracts and/or amended existing contracts as required.
2. Augment/amend published compliance levels for individual retailers.
3. Provide additional information to assist new entrant retailers to understand their obligations and governance processes.

#### Resources

This work may require 0.05 FTE to liaise with retailers on possible amendments and future assessments and to oversee any required assessment work. A modest budget is additionally provided for the Independent Assessor. This funding can be redeployed if not needed.

### Gas distribution contracts oversight scheme (Distribution Scheme)

In 2012, Gas Industry Co established the Distribution Scheme under which gas distributors' contracts with gas retailers are assessed 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.

#### Forecast Activities FY2020

1. Continue to assess progress with executing new distribution contracts consistent with the Distribution Scheme principles.
2. If required, review the Distribution Scheme, consider any changes or other actions needed, and report.

#### Resources

This work will require 0.2 FTE for considering whether the scheme requires any amendment because many retailers are operating with out of date, or expired, contracts.

## Retailer insolvency

Following a request from the Minister in 2010, 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 a 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 FY2020 beyond that already provided for within the audits under the Switching Rules (i.e. checking that registry participants are able to meet their obligations for reports under those rules). As discussed later, once the shape of any new transmission access arrangements becomes clear, it might be necessary to make amendments to affected aspects of the drafting instructions. Those changes are likely to be minor.

### Contingent activities FY2019

1. Implement the retailer insolvency arrangements as necessary in the unlikely event of a retailer insolvency.
2. Make any necessary amendment to the drafting instructions if/when new transmission arrangements are known.

### Resources

Insolvency-related activities would be addressed by re-prioritisation in the event of a retailer insolvency. Amending the drafting instructions is not specifically provided for, as this is expected to be a low-level activity.

## Gas quality

This workstream originally 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, the Company published a [Gas Quality Requirements and Procedures](#) document aimed at clarifying current arrangements and making them accessible. An update was published in March 2017. The GTAC work has a bearing on this workstream, and Gas Industry Company will consider whether further action is required following either implementation of a single transmission code, or other transmission solution.

### Forecast activities FY2020

1. If GTAC is found to be materially better than the terms and conditions under the Maui Pipeline Operating Code (MPOC) and Vector Transmission Code (VTC), then review adequacy of industry arrangements for notifying gas quality excursions and procedures for managing gas quality incidents; and
2. Update the Requirements and Procedures document as required.

### Resources

For budgeting purposes, this workstream is assumed to require 0.1 FTE.

## Regulation and rule changes

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

The largest influence on this workstream is the question of whether or not the final assessment of the GTAC finds it to be materially better than existing terms and conditions for transmission access.

Details of all regulations and rules administered by Gas Industry Co can be found [here](#).

## **Forecast activities FY2020**

### ***Downstream Reconciliation***

1. Keep the D+1 Pilot Scheme running and consider/implement any worthwhile refinements.
2. If the GTAC is found to be materially better:
  - (a) revise Pilot Scheme to provide data at Zone and Dedicated Delivery Point levels; and
  - (b) begin the process of amending the Downstream Reconciliation Rules (DRRs):
    - (i) develop any required changes to the DRRs and consult;
    - (ii) After considering submissions and making any further amendments, make a recommendation to the Minister to amend the Downstream Reconciliation Rules; and
    - (iii) Subject to Ministerial approval, develop, test and implement the supporting systems.

### ***Critical Contingency Management (CCM)***

1. Review contingency pricing and imbalance arrangements.
2. Consult and work with stakeholders on any improvements to these arrangements.
3. If the GTAC is found to be materially better, consult and work with stakeholders to ensure alignment with the final GTAC.
4. Recommend amendments and implement as required

## **Resources**

In respect of downstream reconciliation, this workstream will require a significant amount of internal resource of 1 to 1.5 FTE in FY2020 to keep the D+1 pilot running successfully and, once the direction of any new GTAC is known, commence working with industry working groups and the Allocation Agent to design the necessary rules changes, and address implementation and transition issues.

The CCM review will be comparatively less resource intensive, but it involves a reasonably contentious issue and—due to being regulations rather than rules—requires a longer process. We expect it will require 0.5 FTE in FY2020.

## **Gas measurement**

A technical advisory group was established in FY2018 with the objective of developing 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.

## **Contingent activities FY2020**

1. Review/update of advanced metering standards document if required.

### **Resources**

A minor budget provision has been provided for this workstream in FY2020 along with 0.05 FTE. If not required, those resources will be redirected.

## **Supply/demand model**

Gas Industry Co first published a study on long-term gas supply and demand scenarios in 2012. It is clear that the contribution of the report is significant, and it has been updated biennially since then. The next update will be published in FY2019.

### **Forecast activities FY2020**

1. Review and update the *Report* every two years after first publication.

### **Resources**

As the work for this is outsourced, there will only be a modest requirement of 0.1 FTE for contract administration, stakeholder liaison and communication. Typically, the work spans two financial years, so the update scheduled to be published in FY2021 will commence in FY2020.

## **Wholesale market**

The emsTradepoint Wholesale Market (eTp) has now been in operation for over four years and has increased in both membership and volume over that time (although FY2019 saw reduced throughput due to supply-side issues). We note that the GPS seeks an outcome of "Efficient arrangements for the short-term trading of gas" and eTp makes a transparent contribution to that outcome.

As an industry initiative, Gas Industry Co is pleased with the progress to date.

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

### **Forecast activities FY2020**

1. Monitor Wholesale Market activity and developments; and
2. Ensure that market information is provided to Gas Industry Co in a timely fashion to support this monitoring.

### **Resources**

This workstream is expected to require 0.1 FTE. However, that might increase if we identify transparency issues that cannot be resolved by agreement.

## **Information disclosure**

Concerns have been expressed by some market participants regarding asymmetric access to information, particularly information regarding upstream outages (both planned and unplanned). This issue was given a great deal of consideration during the work on developing the GTAC, but no resolution has been reached among stakeholders.

In parallel, the Minister of Energy and Resources has written 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 work stream 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 remove the information asymmetry. By the end of FY2019, we will have consulted on an options paper and analysed submissions, and we expect to be in a position to identify whether a non-regulated solution is feasible or if regulation is likely to be required.

### **Forecast activities FY2020**

If the FY2019 work indicates a non-regulated solution is feasible, proceed to implement that solution; and

Alternatively, if a non-regulated solution is infeasible, prepare and consult on a statement of proposal for regulation.

### **Resources**

This workstream is expected to require 0.6 FTE. However, that may be subject to adjustment as the work proceeds.

## **4.2 Strategic objective: 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 three years have seen an intense amount of activity dedicated to the development of a single transmission access code, from First Gas, industry stakeholders, and Gas Industry Co. This work is expected to continue in FY2020. At this stage, it is not possible to say whether that activity will focus on implementation of a new, single transmission code or whether the focus will remain on developing a single transmission code. If it is the latter, there is also the question of how the development process will unfold: whether it will continue to be led by First Gas, or whether Gas Industry Co will lead a workstream to determine whether a regulated solution is required. What is certain is that this topic will remain a high-intensity workstream requiring considerable resources.

### **Forecast Activities FY2020**

1. Oversee implementation of new transmission access code; or
2. Prepare to evaluate another version of GTAC (under an industry-led process); or
3. If industry process has stalled, design and consult on options for implementation, including regulation; and
4. Move to recommend/implement.

### **Resources**

At a minimum, this workstream will require 1.5 FTE across the year, but there will likely also be periods where additional resources are required. Accordingly, we are budgeting an internal requirement of 1.75 FTE.

## Transmission pipeline balancing

Market-based balancing (MBB) was implemented in FY2016 and Gas Industry Co has published a review that points to a number of areas of improvement. Those improvements have required improved information availability – the D+1 Pilot Programme plus daily cash-out information delivered on business days – as well as making First Gas the buyer/seller of last resort. The GTAC, if approved, would reorient the approach to pipeline balancing.

### Forecast activities FY2020

Work with stakeholders on balancing-related matters and monitor new arrangements if/when implemented.

### Resources

This workstream has connections with a number of other workstreams. Accordingly, although no specific allocation of external resources has been made for the workstream, any requirement for external advice will need to come from a pool that has been set aside for balancing, interconnection, and code changes.

## Transmission code changes

Under a Memorandum of Understanding with First Gas, Gas Industry Co has a role in processing MPOC change requests on an 'as required' basis. In addition, the Company is invited to submit on change requests under the VTC. As it was submitted, the GTAC envisages a similar role for Gas Industry Co with respect to processing and approving/declining code changes

### Forecast activities FY2020

1. Perform agreed role(s) in relation to proposed code changes.

### Resources

Although there has been significant activity in this area in previous years, given the focus on balancing through that period, it is likely that there will be little or no activity in that area in FY2020 under the existing Codes. However, if a new code is implemented, there may be issues identified and/or tidy-ups required that might require code changes. The resource requirement will be provided from the shared pool for balancing, interconnection, and code changes.

## Transmission pipeline interconnection

Gas Industry Co has established *Interconnection Guidelines* that set out our expectations with regard to transmission system owners' policies and procedures for connecting to their pipelines. We have previously commissioned independent reviews of new interconnections and, in recent years, these have shown that the Guidelines have been adopted by the (then) transmission system owners.

Given this, we do not consider that formal reviews of each new interconnection are required. We will monitor interconnections at a high level and expect that any issues will be brought to our attention.

### Forecast activities FY2020

1. Review interconnections as required;
2. Address any concerns regarding reasonable access;
3. Review new transmission system owner's interconnection policies; and
4. Amend the *Guidelines* as required.



## Resources

There is no specific provision for this work as there is no forward information on the rate of new connections. However, given the sporadic nature of interconnections and the small amount of work required to undertake high-level monitoring it is considered that it is unnecessary to make a specific allowance. If required, external advice will be provisioned from a pool shared with balancing and code changes.

## Gas transmission security and reliability

Gas Industry Co undertook a review of existing information and requirements associated with gas transmission security and reliability in FY2016/17. These requirements are found in several locations, span responsibilities of several regulators, and can be difficult to bring together and interpret.

Our findings were that existing information and arrangements give significant assurance about both standards and performance. With the change in ownership of the transmission systems, Gas Industry Co published an update paper in March 2017. That paper canvassed issues that had been raised by stakeholders and found that they had been substantially addressed. However, we expect that matters with a strong security and reliability component will emerge from time to time, and these matters will be dealt with then they arise. Gas Industry Company will continue to monitor successive asset management plans.

### Activity FY2019

1. Continue to monitor asset management plans for gas transmission and report on any significant matters.

## Resources

There is no specific provision for this work in FY2019, as the most likely scenario is that transmission disclosures are fit for purpose and informative for stakeholders. It is accordingly considered that this can be fitted within the available resources, or priorities adjusted.

## 4.3 Strategic objective: deliver effectively on Gas Industry Co's accountabilities as the gas industry body

There are various functions that the industry body is required to perform either under the Gas Act or under gas governance rules or regulations. The activities associated with these are described in this section.

### Downstream reconciliation

The purpose of the Gas (Downstream Reconciliation) Rules 2008 (Reconciliation Rules) is to 'establish a set of uniform processes that will enable the fair, efficient, and reliable downstream allocation and reconciliation of downstream gas quantities'. Gas Industry Co has an ongoing obligation to oversee the operation of the Allocation Agent and fulfill its duties under the Reconciliation Rules. Gas Industry Co monitors allocation results so as 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 the Allocation Agent.

The Reconciliation Rules have been instrumental in reducing the level of unaccounted for gas (UFG) at the final allocation stage. 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. Collectively, this reduction in UFG represents an ongoing stream of cost savings in excess of \$5 million per annum.

### **Forecast activities FY2020**

1. Monitor Allocation Agent;
2. Assess ongoing performance of the Rules;
3. Monitor allocation results;
4. Commission performance and event audits as required; and
5. Make determinations under the Rules as required.

In addition to the tasks that are required under the Reconciliation Rules, Gas Industry Co expects to continue the pilot scheme 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 above under the 'Regulation and rule changes' section.

### **Resources**

Because allocation is a complex, bottom-up process involving large amounts of data, significant resources are required for this workstream. Because of the need to run and monitor the D+1 Pilot Scheme, we estimate that this workstream will continue to require a full FTE. The Allocation Agent is funded from market fees.

### **Switching and registry**

The Gas (Switching Arrangements) Rules 2008 (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.

The introduction of the Switching Rules tripled the rate of switching. In recent years, switching has stabilised to between 3,500 and 4,000 per month (in comparison to the 1,000 or so switches prior to the Switching Rules). Over the past few years Gas Industry Co, in conjunction with the Electricity Authority, has provided modest support to Powerswitch to ensure the continued existence of an independent, credible source of information for consumers.

Amendments made to the Switching Rules in September 2015 introduced the requirement for the industry body to arrange performance audits of registry participants. Baseline audits of retailers and distributors have now been completed.

### **Forecast activities FY2020**

1. Monitor Gas Registry Operator;
2. Assess the ongoing performance of the Switching Rules;
3. Monitor and report on switching statistics;
4. Make determinations under the Switching Rules as required;
5. Commission performance and event audits as required;
6. Continue to provide support to Powerswitch pending new arrangements and/or emergence of sustainable retailer commissions; and
7. Follow up on any issues identified in the switching audits.

## Resources

Although this was previously resource-intensive, particularly in the first year of operation, administering the Switching Rules is now more of a routine activity (outside of any activities related to changes to the Rules). Gas Industry Co has allowed for 0.25 FTE internally. The service provider is funded from market fees under the Rules.

## Critical contingency management

The purpose of the Gas Governance (Critical Contingency Management) Regulations 2008 (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 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.

The CCM Regulations and further details about CCM can be found [here](#).

### Forecast activities for FY2019

1. Monitor CCO;
2. Assess ongoing performance of the CCM Regulations;
3. Appoint/monitor experts as required;
4. Monitor exercises and events as required;
5. Administer contingency pool as required; and
6. Process applications and renewals for priority designations in the areas of critical care, essential services, critical processing and electricity supply as required.

As outlined above in the 'Regulation and rule changes' section, Gas Industry Co also intends to review aspects of the CCM Regulations and to consider what amendments are necessary to ensure consistency in the event of a new transmission code.

## Resources

The CCO function is performed by a service provider funded through market fees, which also include funding for one annual contingency event. Gas Industry Co considers that its 'business as usual' arrangements will require approximately 0.2 FTE. However, that may be subject to increase depending on the rate and type of applications and renewals received for priority designations. Given that gas critical contingencies are relatively rare events, Gas Industry Co does not budget internal resources to cover those. Rather, should a critical contingency eventuate, we will re-prioritise resources to meet our obligations under the CCM Regulations for the period concerned.

## Compliance and enforcement

The Gas Governance (Compliance) Regulations 2008 (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.

The Compliance Regulations and further details about compliance can be found [here](#).

### Forecast activities FY2019

1. Perform Market Administrator role;
2. Assess ongoing performance of the Compliance Regulations;
3. Assist Investigator and Rulings Panel as required; and
4. Monitor compliance trends for indications of regulatory inefficiency.

### Resources

Each of the Investigator and Rulings Panel is engaged and funded by market fees as provided for in the Compliance Regulations. The Market Administrator role is undertaken by Gas Industry Co and, based on recent experience, is approximately 0.2 FTE. However, that level could rise in the event of any significant or complex material breaches. Once matters are referred for investigation or referred to the Rulings Panel, the input from Gas Industry Co will increase, potentially substantially, in significant and complex cases. Accordingly, the overall resources required in this area are almost entirely demand-driven. Based on the low level of enforcement activity over the past several years, we do not budget for any increased level of activity.

## Statement of intent and annual report

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

[Annual Reports](#) and [Statements of Intent](#) can be found on our website.

### Forecast activities FY2019

1. Prepare and publish SOI to meet statutory timeframes. Provide to Minister for comment prior to publication; and
2. Prepare and publish Annual Report; meet requirements for tabling in Parliament

## Resources

This work is predominantly carried out internally utilising staff resources from across the Company. External printing costs and some design work is required, although the first of these is controlled by shorter print runs and increased use of email and website communication.

### 4.4 Strategic objective: develop and communicate the role of gas in meeting NZ's energy needs

#### New Zealand gas story

During FY2013, Gas Industry Co published the first *New Zealand Gas Story*. It is intended that this document is updated annually to ensure the information is current and topical. The most recent edition was published in December 2017. Apart from fulfilling the statutory reporting requirement, this work is intended to help stakeholders to 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 channels as its website, the Company's annual and quarterly reports, and presentations to various stakeholder groups.

The *New Zealand Gas Story* can be found [here](#).

#### Other reporting

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 Quarterly Reports, Switching Statistics and Industry Performance Measures.

Gas Industry Co has also commissioned reports focussing on particular aspects of the industry, such as the *Consumer Energy Options Report* (Concept Consulting, 2012/2016), *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). Further occasional reports will be published, and existing reports updated, where they can be of value to the industry.

#### Forecast activities FY2019

1. Continue to prepare and publish Quarterly Reports, Switching Statistics and Industry Performance Measures;
2. Maintain the currency of the New Zealand Gas Story as new information comes to hand;
3. Continue seminars and other communications for interested stakeholders; and
4. Commission occasional reports and update existing reports as required.

## Resources

This work is predominantly carried out internally by communications staff, with a small budget retained for external experts assisting with specialist areas.

# Appendix B Key Industry Background

Key industry background is:

1. Gas is a key contributor to New Zealand, at around 21.2% of primary energy supply. In the past decade, the gas industry in New Zealand has undergone substantial change, transitioning from reliance on the large Maui field, to drawing supplies from multiple smaller fields. There are now 15 producing fields and around 10 years' P50 reserves.
2. Gas is an important fuel for industrial, commercial, and residential consumers. In 2009, there were about 250,000 gas consumers; today, there are over 280,000.
3. Gas Industry Co has developed a mix of formal rules and regulations (e.g. critical contingency management, reconciliation, switching) and non-regulated arrangements (e.g. retail contracts, distribution contracts) that are well-advanced in meeting the legislative and policy objectives and outcomes that the Government expects the industry to achieve.
4. These arrangements have contributed to the development of a healthy downstream gas market. Key indicators include:
  - (a) With recent new entries, there are now 11 retail gas brands owned by ten different retail companies.
  - (b) Over 99% of gas customers are connected to a network where seven or more retailers trade, demonstrating that gas retailers generally are competitive throughout the North Island.
  - (c) Market concentration, as measured by the Herfindahl-Herschman Index, has decreased significantly in all regions since the commencement of the formal switching regime in 2009, as new retailers have increased market share and incumbent retailers' share has declined.
  - (d) About 3,600 gas consumers switch gas supplier each month, which translates to an annual churn of about 15.4% of gas consumers. In 2018, nearly three quarters of customer switches were completed within three business days.
  - (e) 66% of residential consumers have switched retailer at least once in the past nine years; 68% of small commercial, 77% of large commercial sites, and 55% of large industrial sites have switched at least once.
  - (f) Average annual unaccounted-for gas (UFG) over the past year stands at about 1% (compared with about 2% in 2009).

## ABOUT GAS INDUSTRY CO

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

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

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