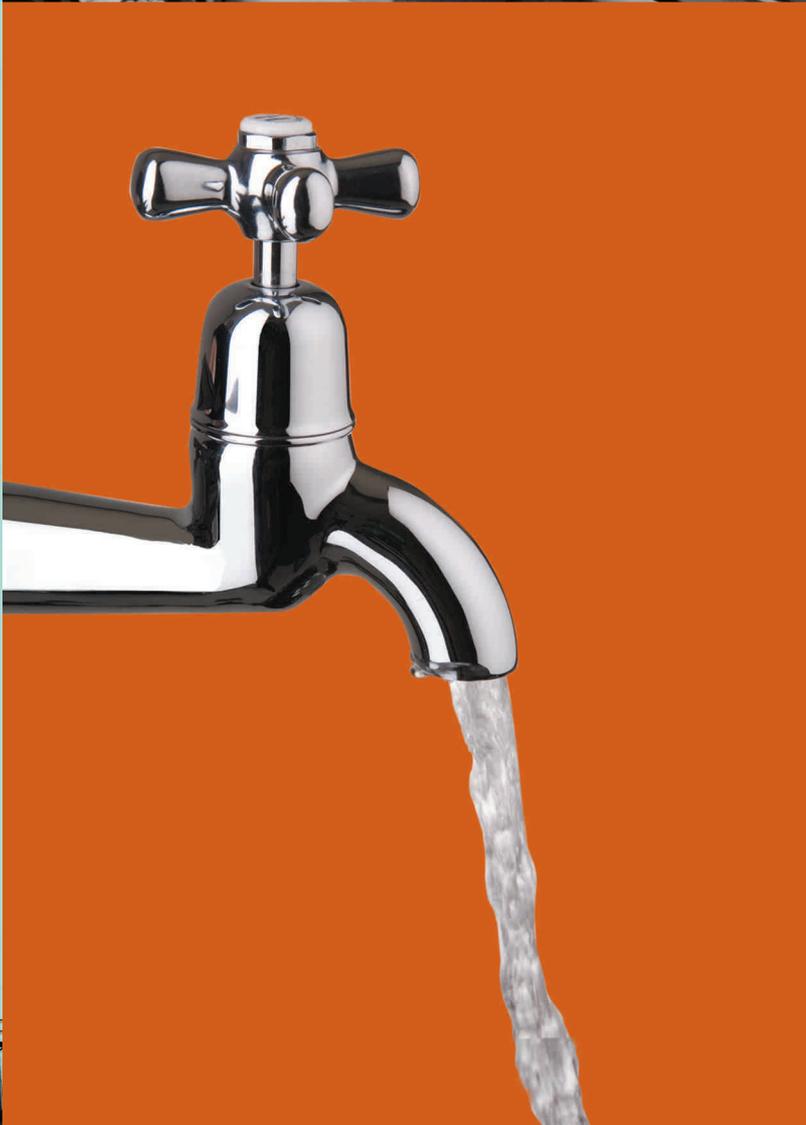


06  
07



# Annual Report

# natural gas



Changes to the Gas Act 1992 (Act) in late 2004 provided for the co-regulation of the gas industry by the Government and an industry body. Gas Industry Company Limited (Gas Industry Co) was established to fulfil the role of the industry body under the Act and was approved by Order in Council on 22 December 2004.

### Gas Industry Co's roles are to:

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

Gas Industry Co's principal objective, in recommending gas governance arrangements, is to ensure gas is delivered to existing and new customers in a safe, efficient, fair, reliable, and environmentally sustainable manner.

<b>01</b>	<b>Chair's foreword</b>	<b>2</b>
<b>02</b>	<b>The year in review—from the Chief Executive</b>	<b>4</b>
<b>03</b>	<b>Significant achievements 2006/07</b>	<b>8</b>
<b>04</b>	<b>Regulatory and policy framework</b>	<b>10</b>
<b>05</b>	<b>Governance overview</b>	<b>16</b>
<b>06</b>	<b>Operations review</b>	<b>22</b>
<b>07</b>	<b>Financial overview</b>	<b>38</b>
<b>08</b>	<b>Financial statements</b>	<b>41</b>
	<b>Abbreviations</b>	<b>52</b>
	<b>Directory</b>	<b>53</b>



**Rt Hon James B Bolger, ONZ, Chair**  
Date: 14 September 2007



**R G Hill, Deputy Chair**  
Date: 14 September 2007

# 01 | Chair's foreword

## Introduction

New Zealand faces two major long-term energy challenges:

- responding to climate change and tackling carbon emissions from the country's energy production and use; and
- delivering secure, clean energy at affordable prices to support economic development, while being environmentally responsible.<sup>1</sup>

Gas has, and I believe will continue to have, a cornerstone role in meeting these twin energy challenges in New Zealand.

## Importance of markets

New Zealand's energy policy framework is based on competitive markets providing the best long-term outcomes for consumers. New Zealand enjoys relatively low energy prices and relatively high levels of security of supply. This suggests the market framework has been successful in the past and should continue to serve the country well into the future.

The Government's requirements for the gas industry are explained in its policy statements issued from time to time. The October 2004 *Government Policy Statement on Gas Governance* (GPS) sets specific tasks for Gas Industry Co to improve market outcomes. These include developing market structures and systems for wholesale and retail operations, and ensuring efficient access to the infrastructure that connects the wholesale and retail markets.

## 2006/07 achievements

This annual report details Gas Industry Co's progress in meeting its published strategic priorities and milestones in the period to 30 June 2007. As the principal activity of the company is policy development, its milestones primarily relate to the delivery of policy recommendations within specific timeframes.

However, as our knowledge of the issues deepens, analysis is completed, and feedback from consultation is considered, adjustments to the milestones are appropriate. This

<sup>1</sup> MED (December 2006). *Powering Our Future: Draft Energy Strategy*, page 5.



# Around 230,000 residential consumers use natural gas

is sensible. The Board believes a decision made based on quality analysis, but delivered after the set milestones, potentially can be more beneficial to the industry, than a decision made on insufficient analysis, but delivered within the set timeframes.

Although not all the targets in the company's strategic plan have been met, the Board is very pleased with the quality of the policy work that has been completed. This work, along with that which has been significantly progressed but not completed during the year, makes substantial steps towards the outcomes required by the GPS. Further details of the work programme progress and achievements are covered in the Chief Executive's review (pages 4-6).

## Baseline review

In addition to our core policy development work, the Board has also been considering the appropriateness of the tasks it has been set. An independent policy analysis and business advisory group, The Allen Consulting Group (ACG), was engaged to undertake a baseline review and report on the current state and performance of the New Zealand gas industry.

ACG's report focuses on the facilitation of competitive outcomes and assesses industry performance against this measure. It endorses the tasks and priorities set out in the GPS and comments positively on Gas Industry Co's progress towards implementing the various specified tasks.

The report observes that:

—The model of co-regulation in the New Zealand gas industry is innovative and brings with it a great opportunity for the gas industry to bring forward practical and effective market and regulatory development solutions... The success of Gas Industry Co will largely depend on the insight and expertise it brings to bear on its challenges and the willingness of its board and membership to support the new initiatives necessary to bring about the outcomes the Government expects.<sup>2</sup>

The report notes the high level of engagement from the industry to date and suggests this will be a key determinant of the success of the co-regulatory approach going forward.

## In conclusion

The Board was pleased to receive independent confirmation of our work programme priorities as the company continues to make positive progress towards achieving the outcomes set out in the GPS. This progress is heavily dependent on the contributions of our shareholders, industry participants, other stakeholders, consultants, and staff. I would like to personally thank these people for their support during the year and, in particular, Christine Southey for her leadership as Chief Executive.

I would also like to thank each of my Board members for their efforts during the past 12 months. Dr Ajit Bansal resigned from the Board in June 2007 to take up a role with Shell's head office in The Hague. I would like to thank Ajit for his significant contribution to the Board.



Rt Hon James B Bolger, ONZ Chair

<sup>2</sup> The Allen Consulting Group (15 November 2006). *The New Zealand gas industry in 2006: Review of its state and performance*, executive summary, page vi.

# 02 | The year in review —from the Chief Executive

Gas Industry Co's third annual report provides a useful opportunity to reflect on progress in the last 12 months towards meeting the company's six strategic priorities, as articulated in its 2007–2009 strategic plan.

## During the past financial year

### Gas Industry Co made formal recommendations to the Minister on:

- the specification for reticulated natural gas;
- new rules for switching gas customers through a central registry;
- new regulations for enforcement of the gas switching rules;
- proposed levy arrangements for the 2007/08 financial year; and
- a contract-based information-disclosure regime for gas processing facility owners.

### Gas Industry Co also gave advice to the Minister on:

- the present state and performance of the gas industry;
- the draft *New Zealand Energy Strategy to 2050* (NZES);
- its proposed solution for wholesale trading; and
- its proposed approach to addressing transmission access issues.

In addition, Gas Industry Co undertook a significant amount of policy analysis for future recommendations to the Minister. In total, the company developed and released 13 papers for consultation. These papers covered a range of issues across the gas supply chain.

The complexity of issues in the areas of wholesale markets, reconciliation, and outage and contingency management—and the level of consultation necessary—has meant that some milestones have taken longer to reach than originally forecast in our 2007–2009 strategic plan. Nevertheless, in all work streams significant progress has been made toward the outcomes



# 83.3 percent of New Zealand's heavy industry uses natural gas

required in the GPS. This progress will provide substantial groundwork for recommendations to the Minister in the coming year on some of the industry's longstanding issues.

## Looking back on the year, two matters stand out.

The first matter is the challenge we have had in progressing industry arrangements within the agreed timeframes. Our ability to recommend non-regulatory arrangements, where 'reasonably practicable', is a key feature of the co-regulatory model. Accordingly, when Gas Industry Co is developing and recommending fit-for-purpose arrangements, it considers all available policy instruments, including: voluntary guidelines; codes of practice; industry agreements; and regulatory arrangements passed under the Act.

While industry participants often debate that industry-agreed arrangements should be preferred to regulated arrangements, in practice, we have found obtaining agreement is not necessarily straightforward. Two such examples occurred during the past financial year in relation to our work on disconnections and access to gas processing facilities. Our experience is outlined in the operations review section of this annual report and illustrates the difficulty we have had in implementing industry agreements within the prescribed timeframes (pages 24-26).

The second matter is the conclusion of our policy advice on the arrangements for switching gas customers and the enforcement of those arrangements—following the release of five papers on switching rules and three papers on compliance. These arrangements are expected to deliver cost savings and improved levels of service to gas customers. However, the need to amend the Act has delayed the implementation of these arrangements. Gas Industry Co has worked closely with Ministry of Economic

## Gas Industry Co's 2007-2009 strategic priorities are:

- effective operation of the co-regulatory model;
- improvements to consumer outcomes;
- improvements to the retail market;
- development of wholesale market trading arrangements;
- review of infrastructure access arrangements; and
- development of gas outage and contingency management arrangements.<sup>3</sup>

<sup>3</sup> *Gas Industry Company Limited Strategic Plan 2007-2009*, section 4.2: page 12.

# There are over 11,600 km of distribution pipelines in the North Island

Development (MED) officials on the necessary amendments to the Act and these are now expected to be passed early in the 2007/08 year.

I believe Gas Industry Co continues to deliver cost-effective policy advice to the Minister and to the industry. The total expenditure for Gas Industry Co in the current financial year was modest at \$3.6 million. Given the complexity and longstanding nature of many of the issues we are addressing, and the economic, legal, and technical input required to develop and progress solutions to these issues, I consider this represents excellent value for the industry.

Total levy revenues this year were \$4.2 million, resulting in an over recovery of \$395,000, after taking into account losses carried forward. This was due to a combination of greater-than-expected wholesale revenues and lower-than-expected work stream expenditure. This over recovery will be offset against future revenue requirements.

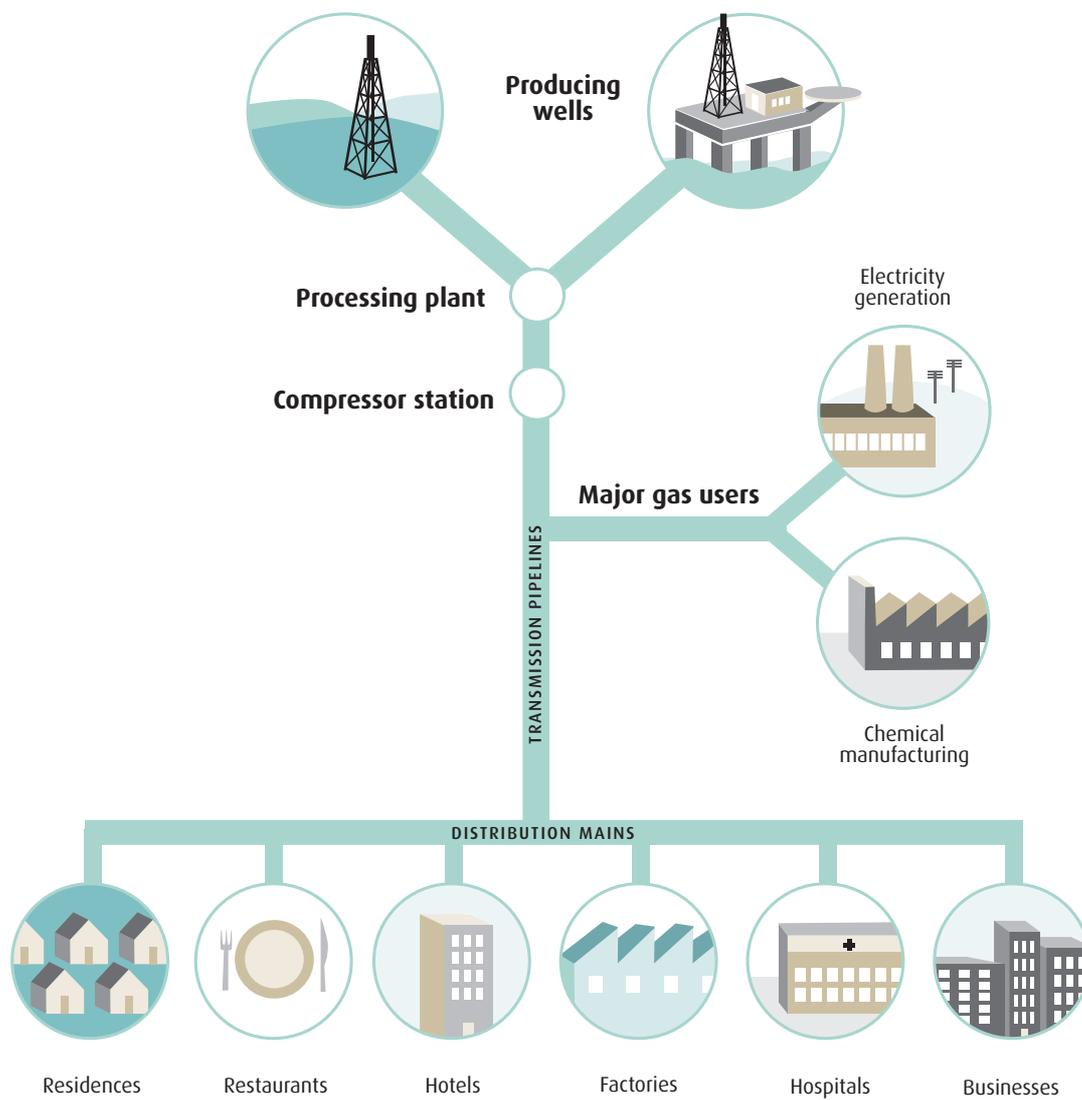
The achievements in the 2006/07 financial year are excellent, particularly when considering the small size of the executive team—nine full-time equivalents in the financial year. These achievements have only been possible because of the commitment of the executive team combined with the support we have had from the industry, officials, and expert external advisers (page 53).

Looking ahead to the next financial year, we anticipate making recommendations to the Minister on disconnection practices, rules for downstream reconciliation, and new regulatory frameworks for transmission access and contingency management. We also expect to be overseeing the implementation of the new switching arrangements and a trial for trading of spot gas.



**Christine Southey**, Chief Executive

# New Zealand gas system



# 03

## Significant achievements 2006/07



### First quarter 2006/07

Discussion paper *Review of Gas Emergency Management Arrangements*

Discussion paper *Access to Gas Processing Facilities*

Statement of proposal *Switching Arrangements for New Zealand Gas Industry*

Statement of proposal *Compliance and Enforcement Arrangements*

Discussion paper *Wholesale Market Design*

**Recommendation to the Minister on review of specifications for reticulated natural gas**

Discussion paper *Submissions Analysis on Transmission Access Issues Review*

*Gas Industry Company Limited Annual Report 2005–2006*

### Second quarter 2006/07

Progress report to the Minister on transmission access issues review

Industry conference *Co-Regulation in Action*

Report to the Minister on performance and present state of the gas industry

Progress report to the Minister on wholesale market development

Discussion paper *Feedback on Wholesale Market Design Part 2 Further Consultation*

**Recommendation to the Minister on access arrangements for gas processing facilities**



### Third quarter 2006/07

Discussion paper *Reconciliation of Downstream Gas Quantities*

Discussion paper *Proposed 2006/07 Levy*

Decision paper *Modified Arrangements for Compliance and Enforcements Arrangements for Retail Gas Market Registry and Switching*

**Recommendation to the Minister on 2007/08 Gas Industry Co levy**

Discussion paper *Analysis of Options for an Access Framework for Governance of Gas Transmission*

Submission to MED on the draft *New Zealand Energy Strategy to 2050*

### Final quarter 2006/07

Discussion paper *Revised Proposal for Allocation of Switching and Registry Costs*

**Recommendation to the Minister on switching arrangements for New Zealand gas industry**

**Recommendation to the Minister on regulations for enforcement of switching arrangements**

Released standard contract for short-term trading of gas quantities

Completed tender process for wholesale trading platform

*Gas Industry Company Limited Strategic Plan 2008–2010*

The discussion papers and publications listed above are on Gas Industry Co's website: [www.gasindustry.co.nz](http://www.gasindustry.co.nz)

# 04 | Regulatory and policy framework

## 4.1 Co-regulation

The New Zealand gas industry sector is governed by a co-regulatory model that enables an industry body, Gas Industry Co, to recommend arrangements to the Minister on gas matters. The co-regulatory model occurred as a result of the Government wanting the gas sector to be involved in developing new policy settings for the industry, as it transitions from a market dominated by a few players with a single supply source, to a market with multiple participants and many supply sources.

The key features of the co-regulatory regime are:

- the regulatory vehicle is a special purpose entity—called the ‘industry body’ in the Act—that can provide a mix of industry expertise and an independent perspective to the Minister;
- the industry body is a private company with constitutional limits on its activities and specific obligations under the Act and the Companies Act;
- the directors are appointed by industry voting and the majority of directors must be independent;
- the industry body has a range of policy instruments available to it, including recommending regulations and rules or non-regulatory arrangements, where these are the most practicable option;
- the industry body has the power to levy industry participants for its costs; and
- there is an expectation for industry participants to have input, through project teams and consultation processes, into the development of governance arrangements.

In developing new gas governance arrangements, Gas Industry Co must operate within the collective framework of the Act, any policy statement on gas governance issued by the Government, and the company’s constitution.

# The gas market provides 20 percent of New Zealand's primary energy

## 4.2 The Gas Act 1992

The co-regulatory regime was established in amendments made to the Act in late 2004. These amendments provide for the establishment of an industry body to advise the Government on a range of matters affecting governance of the gas industry sector. This includes gas wholesaling, retailing, processing, transmission, and distribution.

The Act also sets out certain powers and duties for the approved industry body in respect of the GPS, reporting to the Government, the company's constitution, and its funding. Gas Industry Co was incorporated in July 2004 and was approved as the industry body under the Act by Order in Council on 22 December 2004.

During the 2006/07 financial year, Gas Industry Co exercised its powers to recommend to the Minister under sections:

- 43J(2) rules on switching gas customers between retailers;
- 43M(1)(d) regulations for enforcement of the new switching rules; and
- 43ZZB the levy for the 2007/08 financial year.

## 4.3 Government Policy Statement on Gas Governance

The Minister has set the objectives and outcomes for Gas Industry Co and the gas industry by issuing a GPS. The GPS was published in the *Gazette* and presented to the House of Representatives in October 2004.

The GPS affirms that the Government's overall policy objective for the gas industry is:

To ensure that gas is delivered to existing and new customers in a safe, efficient, fair, reliable, and environmentally sustainable manner.<sup>4</sup>

Consistent with this overall objective, the GPS defines specific objectives and outcomes Gas Industry Co is expected to pursue. The GPS also itemises a series of tasks for Gas Industry Co to progress (table 1, pages 14–15).

The operations review in this report describes Gas Industry Co's progress towards delivering these outcomes and meeting the Government's objectives and outcomes for the sector (pages 22–37).

<sup>4</sup> GPS: para 4.

# There are 3,400 km of high-pressure transmission pipelines in New Zealand's North Island

## 4.4 Gas Industry Co's constitution

Gas Industry Co's original constitution restricts the company's purpose to performing the functions and duties, and exercising the powers of the industry body under Part 4A of the Act.<sup>5</sup> The constitution was designed to ensure Gas Industry Co complies with the approval requirements of an industry body under the Act, and will continue to do so over time.

The Act requires that any body to be approved as the industry body needs to:

- be broadly inclusive of industry participants—membership is not compulsory;
- have a board with a majority of independent members, including an independent chair;
- be capable of delivering outcomes that meet the Government's objectives for the gas industry;
- have governing rules with objectives consistent with those set out in section 43ZN of the Act and that relate to developing recommendations on the wholesaling, processing, transmission, distribution, and retailing of gas;
- allow all industry participants, except service providers appointed under any gas governance regulation, to become members of the industry body; and
- have rules requiring it to report regularly to the Minister on the performance and state of the gas industry, the industry body's performance and achievement of its objectives, and other relevant matters.

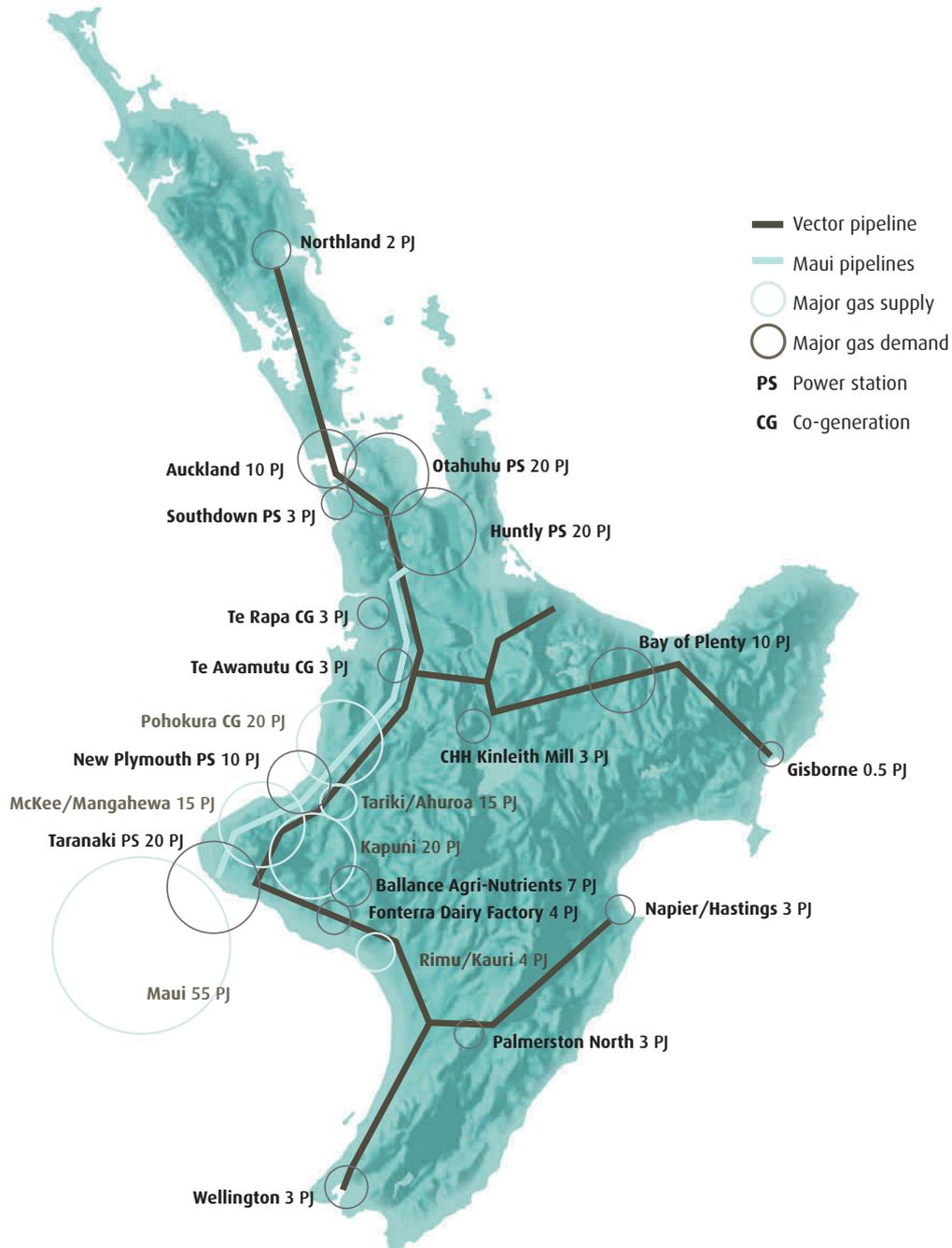
The constitution was amended in May 2006 to allow for Gas Industry Co to undertake specific roles in relation to existing agreements for reconciliation, contingency management, and open access, and also to allow it to take on new roles under industry arrangements approved by the Minister. Any additional expansion of the company's functions requires a special resolution of shareholders with a 75 percent majority.

## 4.5 Summary

The combination of the above key documents—the Act, the GPS, and the constitution—provides the co-regulatory framework within which Gas Industry Co is required to operate. This framework clearly sets out Gas Industry Co's role, which involves leading the gas sector to develop gas governance arrangements for the Minister's approval and then to implement and review those arrangements.

<sup>5</sup> *Constitution of Gas Industry Company Limited* (amended on 1 May 2006), section 4.1: page 2.

# Annual gas supply and demand



Source: Gas Industry Co.

**Table 1: Gas Industry Co performance requirements from the *Government***

<b>Overall objective</b>	'To ensure that gas is delivered to existing and new customers in a safe, efficient,				
<b>Specific outcomes</b>	Facilitation and promotion of ongoing gas supply to meet New Zealand's energy needs, by providing access to essential infrastructure and competitive market arrangements	Energy and other resources are used efficiently	Barriers to competition in the gas industry are minimised to the long-term benefit of end-users	Incentives for investment in gas processing facilities, transmission and distribution, energy efficiency, and demand-side management are maintained or enhanced	Full costs of producing and transporting gas are signalled to consumers
<b>Tasks</b>	<b>Improvements to market arrangements</b>				
	Development of protocols and standards applying to wholesale gas trading, including quality standards, balancing, and reconciliation	Development of a secondary market for the trading of excess and shortfall quantities of gas	Development of capacity trading arrangements	Standardisation and upgrading of protocols relating to customer switching, so that barriers to customer switching are minimised	Establishment of gas flow measurement arrangements to enable effective control and management of gas

## Policy Statement on Gas Governance October 2004

fair, reliable, and environmentally sustainable manner.'

Delivered gas costs and prices are subject to sustained downward pressure	Quality of gas services and, in particular, trade-offs between quality and price, as far as is possible, reflect customers' preferences	Risks relating to security of supply, including transport arrangements, are properly and efficiently managed by all parties	Consistency with the Government's gas safety regime is maintained	Gas sector contributes to achieving the Government's climate-change objectives by minimising gas losses and promoting demand-side management and energy efficiency
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Infrastructure access			Consumer outcomes	
Establishment of consistent standards and protocols across distribution pipelines so that gas market participants can access distribution pipelines on reasonable terms and conditions	Establishment of an open access regime across transmission pipelines so that gas market participants can access transmission pipelines on reasonable terms and conditions	Protocols that set reasonable terms and conditions for access to gas processing facilities	Development of efficient and effective arrangements for the handling of consumer complaints	Development of model contract terms and conditions between consumers and retailers



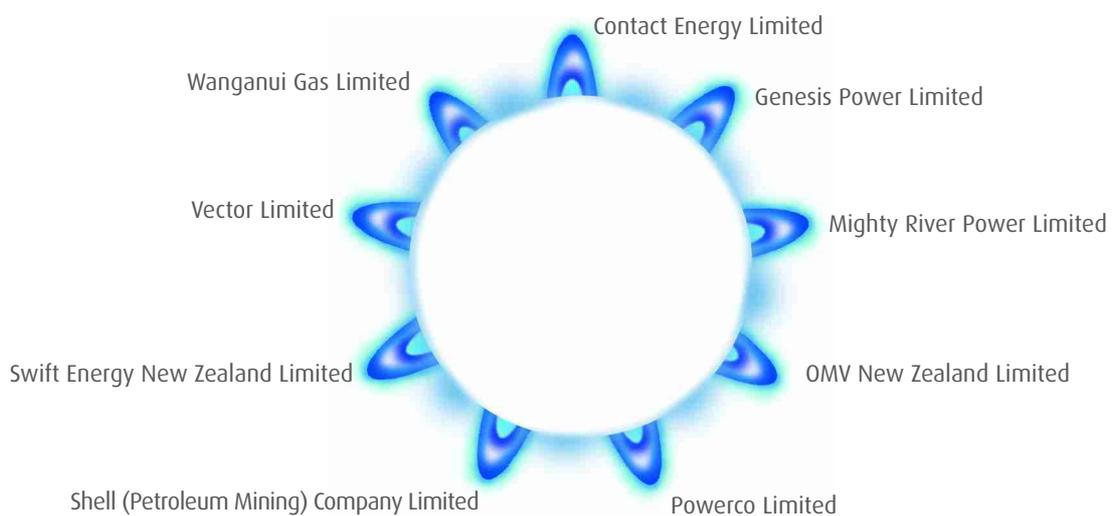
# 05 | Governance overview

## 5.1 Company shareholders

Gas Industry Co encourages all industry participants to become shareholders in the company. Every shareholder holds a \$1 share, which is redeemable at the option of the shareholder. Every shareholder is entitled to one vote on a poll on resolutions at shareholders' meetings, including those that appoint directors and change the constitution.

In addition, becoming a shareholder shows an industry participant's visible support for the co-regulatory model of governance. Gas Industry Co's shareholders are listed in the directory (page 53). One of the company's major strengths is the diversity of its shareholders across all sectors of the gas industry—production, transmission, distribution, wholesaling, retailing, and consumption.

### Gas Industry Co shareholders



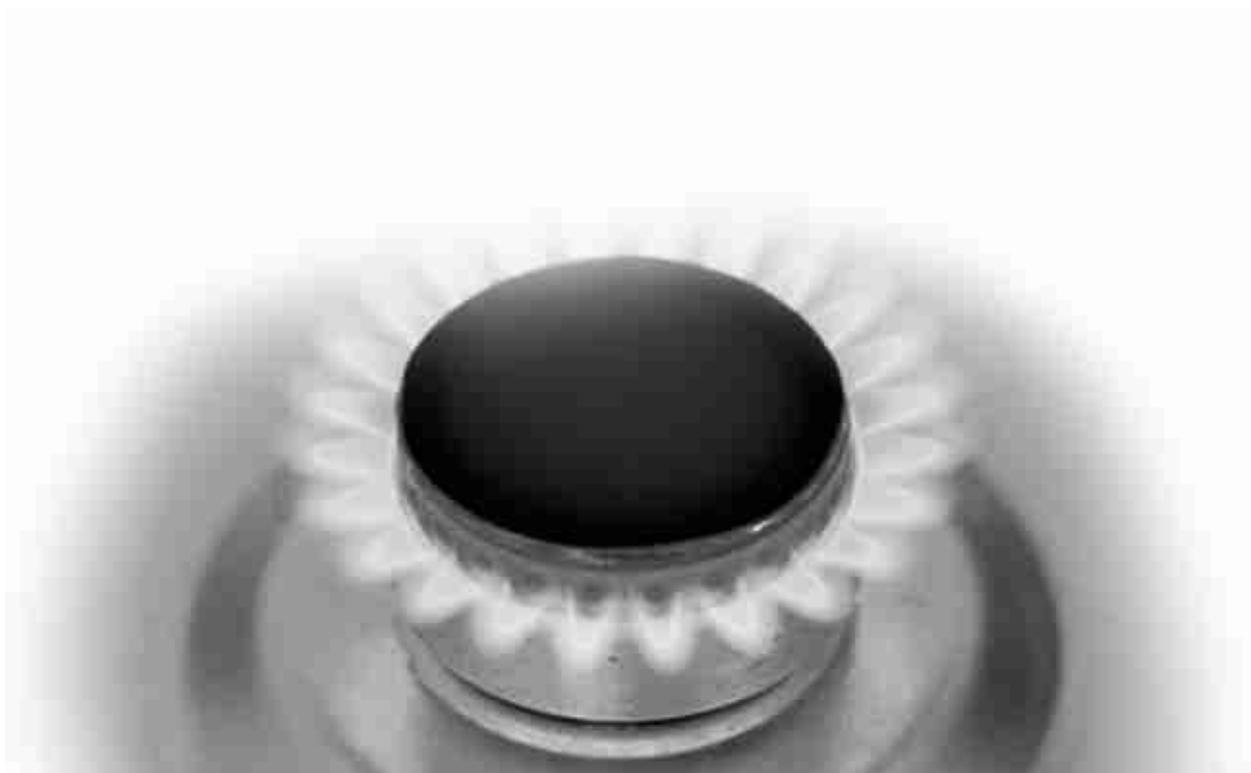
## Gas Industry Co recommends gas governance arrangements to the Minister of Energy

### 5.2 Board of directors

The Board meets monthly throughout the year to consider operational reports and recommendations from Gas Industry Co's executive. The Board is appointed by industry shareholders and is a mix of independent and non-independent directors. Under the company's constitution, the Board cannot have more than seven directors, four of whom (including the chair) must be independent of the gas industry. The number of independent directors voting on a matter must exceed the number of non-independent directors voting on the same matter.

The company's constitution requires, at every annual meeting, that at least a third of the directors (to the nearest whole number) must retire from office. Accordingly, Robin Hill (an independent director) and Mark Franklin (a non-independent director) retired at the annual meeting on 19 October 2006 and subsequently were re-elected. At the same meeting, Keith Davis was also elected to the Board, as an independent director, to fill the vacancy created by the departure of Denis Clifford on 21 April 2006, following his appointment to the High Court.

In June 2007, Dr Ajit Bansal resigned as director of Gas Industry Co and left his position as Country Chair for Shell New Zealand Limited to take up an international appointment with Shell's head office in The Hague. Shortly thereafter, the Board appointed David Baldwin (Chief Executive, Contact Energy Limited) to fill this casual vacancy for a non-independent director.



<b>Rt Hon James (Jim) B Bolger</b>	<b>Robin G Hill</b>	<b>Keith Davis</b>	<b>Mark J Verbiest</b>
ONZ	B Comm, FCA		LLB
Chair and independent director	Deputy Chair and independent director	Independent director	Independent director

Jim Bolger has had a distinguished career in politics that includes being Prime Minister of New Zealand from October 1990 to December 1997, holding ministerial positions for 16 years, and leading the New Zealand National Party for 12 years. In 1983 he was president of the International Labour Organisation, and was New Zealand's Ambassador to the United States of America from June 1998 to January 2002. Jim is the chairman of several organisations in addition to Gas Industry Co, including New Zealand Post Limited and its subsidiary Kiwibank, Express Couriers Limited, the Advisory Board of the World Agricultural Forum, Trustees Executors Limited, and the Ian Axford Fellowships in Public Policy. He is also a trustee of the Rutherford Trust, President of the NZ/US Council, a patron of the Institute of Rural Health, and Chancellor of the University of Waikato.

Robin Hill has an extensive background in financial and business management. He was Chairman and Chief Executive of PricewaterhouseCoopers New Zealand from 1992 to 2003. He was also a member of the firm's Global Board from 1992 to 1995 and its Executive Advisory Group from 1999 to 2000. Robin has provided a wide range of advisory services to a number of large corporates including several energy companies. He is currently a director of the Public Trust.

Keith Davis has extensive experience in the information technology, telecommunications, and venture-funding industries, including having held senior management roles with McDonnell Douglas, Compaq Computers, and BellSouth. He has worked in several countries in addition to New Zealand, including the UK, South Africa, Singapore, Japan and, more recently, Australia. Keith was previously Chairman of the Electricity Retailers' Forum during the time the industry was deregulated. He was also a director of Prime Television Limited.

Mark Verbiest has extensive experience of regulatory structures and competition law, as well as involvement in the energy sector. Mark is Group General Counsel for Telecom Corporation of New Zealand Limited and is a member of the Telecom Senior Executive Committee. He is also responsible for regulatory affairs, has executive operational responsibility for Telecom's international division, is Chairman of the Southern Cross cable joint venture, and is a director of Yahoo!xtra. Prior to joining Telecom in 2000, Mark was a senior partner at Simpson Grierson specialising in corporate, securities, competition, and energy-related law.

Left to right standing are: Mr Murray Jackson; Mr Mark Verbiest; Mr David Baldwin; Ms Christine Southey, Chief Executive; Mr Mark Franklin; and Mr Keith Davis; seated are: Rt Hon James Bolger, ONZ, Chair; and Mr Robin Hill, Deputy Chair.

Absent: Dr Ajit Bansal.



<b>Dr Ajit Bansal</b>	<b>David Baldwin</b>	<b>Mark X Franklin</b>	<b>Murray E Jackson</b>
PhD, BSc (Hons), DipM	MBA, BE (Chemical)	BE (Electrical)	MBA, BEc, FTSE, FIEAust
Non-independent director	Non-independent director	Non-independent director	Non-independent director

Up until June 2007, Dr Ajit Bansal was Commercial Manager for Shell's exploration and production activity and Country Chairman for Shell New Zealand Limited. Ajit left this position to take up a role with Shell's head office in The Hague and resigned from Gas Industry Co at the same time. While in New Zealand, Ajit was also Chairman of Amur Development Limited, the service company for Maui Joint Venture. Ajit has 20 years' industry experience and has worked on various Shell projects based in Thailand, The Hague, China, and Singapore.

David Baldwin was appointed to the Board on 27 June 2007, effective from 1 July 2007. He was appointed as Chief Executive of Contact Energy Limited in May 2006. Prior to that, David was based in Asia and the United States overseeing the energy asset interests of a US-based investment fund. David has held senior roles in Asia and the United States with Mid-American Energy Holdings Company, a US-based global energy company, and with Shell in New Zealand and the Netherlands.

Mark Franklin was Chief Executive Officer of Vector Limited from January 2003 until August 2007. He has experience in the energy and technology sectors in New Zealand, Australia, and Japan. Mark has held a number of leadership roles including Chief Executive of Orion Energy in the Hunter Valley, NSW, Australia, and Asia Pacific General Manager of IBM Global Services Australia for utilities. Mark spent 10 years with the Electricity Commission of NSW, Australia, and three years with Pacific Power, Australia. He was also General Manager of WELNet, a subsidiary of WEL Energy Group.

Murray Jackson is the Chief Executive of Genesis Energy, after establishing it as a state-owned enterprise in 1999. His engineering career has included the commissioning of 200 MW, 500 MW, and 660 MW coal fired power plants in Victoria and NSW, Australia. Prior to establishing Genesis Energy, Murray was the Commissioner of the Snowy Mountains Hydro-Electric Authority—a 3,600 MW dual electricity generation and irrigation scheme located within Australia's high-alpine Kosciusko National Park. Murray is a guarantor member of the Mt Eliza Business School in Melbourne, Chairman of the Genesis Oncology Trust, and Chairman of Energy Online—a wholly-owned subsidiary of Genesis Energy.



## 5.3 Executive

Gas Industry Co has a small executive team that works closely with expert external advisers and industry project teams to deliver on its work programme.

### Christine Southey

BA (Hons), LLB

Chief Executive

Christine Southey is responsible for the overall delivery of Gas Industry Co's work programme.

### Helen Brown

CA

Senior Adviser, Finance

Helen Brown is a chartered accountant and is responsible for Gas Industry Co's financial matters.

### Kate Conaglen

BA

Team Secretary/Receptionist

Kate Conaglen provides secretarial support to the executive team.

### Ian Dempster

BE (Electrical) (Hons), MCom (Hons)

Senior Adviser, Wholesale Markets

Ian Dempster's responsibilities include wholesale market design and monitoring, security of supply, and gas trading and processing arrangements.

### Lucy Elwood

BSc, LLB (Hons)

Strategy and Policy

Lucy Elwood works part-time and assists in a range of strategy and policy issues.

### Jay Jefferies

BJuris

Office Administrator/  
Team Secretary

Jay Jefferies is responsible for secretarial assistance for the executive team and is also involved in office and financial administration.

### Nicki Lau Young

BA, LLB

Senior Adviser, Legal

Nicki Lau Young works part-time and is responsible for company secretarial matters, legal advice to the Board, and also manages some consumer projects.



### Nicole MacFarlane

BA, LLB (Hons)

General Counsel

Nicole MacFarlane is Gas Industry Co's General Counsel with responsibility for legal and regulatory issues across all work streams.

### Mark Soper

BA (Hons), MIntSt

Adviser, Strategy and Corporate

Mark Soper supports the Chief Executive in the implementation of the work programme and also has particular responsibility for projects in the retail work stream.

### Gael Webster

BSc, LLB

Human Resources

Gael Webster works part-time and is responsible for the management of human resources. Gael also developed the compliance regime, which supports the proposed new gas switching arrangements.

### Ian Wilson

BSc (Structural Engineering) (Hons),

BBS (Economics)

Senior Adviser, Pipelines

Ian Wilson is mainly concerned with regulation of access to and operation of existing gas pipeline arrangements.

Left to right are: Helen Brown; Jay Jefferies; Nicki Lau Young; Ian Dempster; Kate Conaglen (seated); Nicole MacFarlane; Ian Wilson; and Mark Soper. Christine Southey is photographed with the Board (page 19).

Absent: Lucy Elwood and Gael Webster.



# 06 | Operations review

## 6.1 Introduction

Gas Industry Co's strategic plan for 2007–2009 sets out six strategic priority areas of action for the company and a number of work streams that relate to those priority areas.<sup>6</sup> These are summarised in the table below.

**Table 2: Gas Industry Co strategic priorities and workstreams**

Strategic priorities	Work streams
Effective operation of the co-regulatory model	<ul style="list-style-type: none"> <li>• Corporate accountability</li> </ul>
Improvements to consumer outcomes	<ul style="list-style-type: none"> <li>• Consumer issues</li> <li>• Distribution contracts</li> <li>• Switching and registry</li> </ul>
Improvements to the retail market	<ul style="list-style-type: none"> <li>• Distribution contracts</li> <li>• Switching and registry</li> <li>• Reconciliation</li> </ul>
Development of wholesale market trading arrangements	<ul style="list-style-type: none"> <li>• Wholesale market</li> <li>• Reconciliation</li> </ul>
Review of infrastructure access arrangements	<ul style="list-style-type: none"> <li>• Open access review</li> <li>• Access to gas processing facilities</li> <li>• Distribution contracts</li> </ul>
Development of gas outage and contingency management arrangements	<ul style="list-style-type: none"> <li>• Gas outage contingency management</li> </ul>

The following sections outline Gas Industry Co's progress on each of these strategic priorities during the financial year.

<sup>6</sup> Gas Industry Company Limited Strategic Plan 2007–2009, section 4.2: page 12.

## 6.2 Effective operation of the co-regulatory model

### a) Strategic priority assessment

As noted in the Chair's foreword (pages 2-3), Gas Industry Co hired ACG to review and report on industry efficiency. The report was commissioned to fulfil the company's obligations under the Act to advise the Minister on the performance and present state of the gas industry. The report *The New Zealand Gas Industry in 2006, Review of its State and Performance* is available on Gas Industry Co's website.

The report concluded that it was inappropriate, at this stage, to assess the efficiency of the industry because of data limitations and the lack of market systems. Instead, the authors suggested that the gas industry should be measured by the level of activity towards improving competitive outcomes.<sup>7</sup> The industry scored favourably on this matter because of its high level of engagement with Gas Industry Co's activities to deliver the outcomes under the GPS.

Although the company's strategic plan originally envisaged a September 2006 completion date for the baseline performance review, this date was extended to November 2006 because of the difficulties of obtaining and analysing certain industry information.

### b) Levy development

Another significant activity in the corporate work stream was the annual levy development process. Arrangements for Gas Industry Co's 2007/08 funding were completed with the gazetting on 29 June 2007 of the Gas (Levy of Industry Participants) Regulation 2007. Details of the 2007/08 levy are set out on pages 39-40 of this annual report.

### c) Communications with stakeholders

Gas Industry Co met its strategic reporting requirements. However, it seeks to do more than this. As the co-regulator, the company is committed to communicating proactively, openly, and inclusively through frequent use of its website, newsletters, discussion and consultation papers, and project teams. In October 2006, it held its second industry conference *Co-regulation in Action*. This was a valuable forum for the company to communicate its goals, its progress on the GPS outcomes, and to hear directly from stakeholders.

<sup>7</sup> The Allen Consulting Group (15 November 2006). *The New Zealand gas industry in 2006, Review of its state and performance*, chapter 7: page 95.

The exchange with stakeholders was also enhanced through a series of meetings between the company's independent directors and its shareholding chief executives, held in the fourth quarter of the financial year. These meetings were aimed at strengthening mutual understanding of the sector and expectations of the co-regulatory model.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Corporate accountability	Prepare quarterly reports	Provide quarterly reports to the Minister	Within 60 days of the end of each quarter	Achieved
	Undertake baseline performance review	Complete baseline performance review	September 2006	Achieved at a later date—reported to the Minister in December 2006
	Prepare annual report for 2005/06	Annual report for 2006/07 to the Minister	September 2006	Achieved
	Prepare strategic plan for 2008–2010	Strategic plan for 2008–2010 to the Minister	June 2007	Achieved
	Develop and consult on 2007/08 levy	Recommendation on 2007/08 levy to the Minister	May 2007	Achieved

### 6.3 Improvements to consumer outcomes

Gas Industry Co's 2007–2009 strategic plan envisaged the development of a report on a range of issues identified by consumer representatives at Gas Industry Co's annual consumer forum. In fact, all of the issues identified at the forum were already being considered as part of existing work streams. The issues raised were:

- effective dispute resolution;
- model contract terms;
- low fixed charges;
- transparency of invoices; and
- industry practices for disconnection and reconnection.

Progress during the financial year in implementing Gas Industry Co's recommendations for these consumer issues has been mixed.

In early 2005, Gas Industry Co recommended to the Minister that adding gas to the electricity complaints scheme was the most cost-effective disputes resolution arrangement, given the size of the gas market in New Zealand. In April 2005, the Electricity & Gas Complaints Commission

(EGCC) was formed from the previous Electricity Complaints Commission. This scheme was further expanded in October 2006 to include land owner/occupier disputes. However, the Minister has not yet approved the EGCC scheme under the Gas Act as he considers that it should be approved concurrently with approval of the scheme for electricity complaints. This means that some gas consumers are outside the ambit of the EGCC complaints scheme, although the majority are covered.

Gas Industry Co recommended to the Minister in June 2006 that the EGCC code of practice, with some amendments, could be an adequate substitute for a model contract. However, the EGCC scheme members have not yet considered the amendments requested by Gas Industry Co. This delay raises questions about whether the EGCC *Gas Consumer Code of Practice*, over the long term, is an adequate substitute for a model contract established and monitored by Gas Industry Co.<sup>8</sup>

Gas Industry Co provided its consumer issues report to the Minister in June 2006.<sup>9</sup> In this report, Gas Industry Co recommended no changes to the arrangements for low fixed charges and transparency of consumer invoices. The company did, however, recommend that a project team be established to develop standard practices across the industry for disconnection and reconnection of gas services. The Minister agreed that if standardised industry arrangements were not established by 1 December 2006, Gas Industry Co would recommend regulations or rules.

In order to meet this timeframe and before committing to the project team, the proposed members were each asked to acknowledge if the company he/she represented was amenable to an industry arrangement; and if the member had authority to progress negotiation of such an arrangement to a near final stage. The project team was formed but made limited progress and by December 2006 was a long way from reaching agreement. At the team's request, Gas Industry Co independently developed a proposed solution, which aims to provide sufficient commercial incentive for retailers to modify their approach to triggering disconnections soon after a vacancy of a premise.

Gas Industry Co's preferred means to implementing the proposed solution is to encourage industry agreement. Despite the delays, the company is optimistic industry agreed arrangements will be in place by late 2007.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Consumer issues	Develop consumer issues report	Issue consultation paper on consumer issues	September 2006	Not applicable as issues covered in previous reports to the Minister
	Prepare consumer issues recommendations report	Consumer issues report to the Minister	December 2006	Not applicable as issues covered in previous reports to the Minister

<sup>8</sup> Electricity & Gas Complaints Commission. Schedule CA: *Gas Consumer Code of Practice*.

<sup>9</sup> Recommendation to the Minister of Energy by Gas Industry Co (16 June 2006). *Fixed Charges for Small Users and other Consumer Issues*.

## 6.4 Improvements to the retail market

Gas Industry Co has two work streams to improve the efficient operation of the retail gas market:

- the establishment of a central registry and new rules for switching gas consumers and the development of a tailor-made compliance regime to support the new switching arrangements; and
- the development of more efficient reconciliation arrangements.

### a) Switching and registry arrangements

Under the GPS, the Government expects Gas Industry Co to propose arrangements for:

*The standardisation and upgrading of protocols relating to customer switching, so that barriers to customer switching are minimised.<sup>10</sup>*

Gas customers are involved in a 'switch' when they move house, start or terminate supply, or elect to change their retailer. To effect a switch, information needs to be exchanged between gas customers, retailers, distributors, and meter owners.

The purpose of the switching and registry rules is to establish a central gas registry and associated rules for switching customers between gas retailers. The central registry will collectively provide effective arrangements for gas customers to readily switch between retailers. Improved switching arrangements will ensure better service levels and enhanced retail market competitiveness. An accurate central registry will benefit retailers and distributors by reducing costs of tracking switching progress. It will also improve the process for allocating and reconciling downstream gas quantities through more accurate allocation of energy network and metering services usage between participants.

Following an extensive development and consultation process, Gas Industry Co made recommendations to the Minister in May 2007 for new rules and regulations. This was five months later than the original milestone because the company elected to undertake two additional consultation rounds to 'fine-tune' the new arrangements. The additional consultation rounds related to specific cost benefit analysis and cost allocation issues.

As noted in the Chair's foreword of this annual report (pages 2-3), Gas Industry Co considers that while achievement of key milestones is an important performance measure for the company, this should not be done where there has been insufficient consultation or analysis of key issues.

An amendment to the Act is required before the Minister can make the recommended switching rules. That amendment was included in the Statutes Amendment Bill introduced in February 2007. It is expected to be passed in September 2007 and implementation will occur as soon as the Minister confirms acceptance of the recommendation.

<sup>10</sup> GPS: para 11.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Switching and registry	Develop registry and compliance arrangements	Issue proposal on switching and registry arrangements	September 2006	Achieved—issued statements of proposal on switching and compliance in August 2006
	Prepare recommendations on new arrangements	Recommendation on registry arrangements to the Minister	December 2006	Achieved at a later date—issued recommendations to the Minister on switching and compliance in May 2007
	Implement central registry and associated compliance regime, if required	Registry system to 'go live'	June 2007	Not achieved—awaiting amendment of the Act

#### b) Allocation and reconciliation

Efficient markets require a system to allocate the various quantities of gas being injected, transported, and delivered to industry participants, that is, allocation and reconciliation. The GPS, includes two Government expectations on Gas Industry Co in relation to allocation and reconciliation arrangements:

The development of protocols and standards applying to wholesale gas trading, including quality standards, balancing and reconciliation.<sup>11</sup>

The establishment of gas flow measurement arrangements to enable effective control and management of gas.<sup>12</sup>

The original milestones were based on the assumption that existing industry codes could be used as a basis for new arrangements. Following analysis and industry consultation this approach was revised. Instead, it was decided a regulatory solution would be required and that it was appropriate to progress the development of downstream reconciliation separately from upstream reconciliation.

<sup>11</sup> GPS: para 13.

<sup>12</sup> GPS: para 9.



The company released a consultation paper in January 2007 *Reconciliation of Downstream Gas Quantities*. The paper presented Gas Industry Co's analysis of the key issues and proposed a number of solutions. The issues discussed were:

- poor compliance and ineffective governance;
- the need for all parties using a gas gate to agree on an allocation agent;
- inequitable allocations of unaccounted for gas (UFG); and
- misalignment between consumption data for time-of-use customers provided for month-end allocation and annual reconciliation.

Following analysis of submissions received in response to this paper, the company drafted rules for allocation and reconciliation of downstream gas quantities that will:

- implement a number of mandatory information quality measures;
- provide for the appointment of a single downstream allocation agent by Gas Industry Co;
- establish for the month-end a daily allocation service, using a form of global allocation on all gas gates, to ensure gas quantities and UFG are more fairly and accurately allocated across all retailers;
- provide for greater transparency through the publication of a range of information, including UFG quantities;
- mandate clear, transparent, governance structures and related processes;
- allow for the performance of audits and the establishment of a compliance regime; and
- provide for the granting of exemptions by Gas Industry Co where appropriate.

The proposed draft rules will apply to all parties involved in gas supply to consumers downstream of a gas gate, including meter owners, distributors, retailers, and transmission system owners. These will be formally consulted on during the next financial year.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Allocation and reconciliation	Implement short-term reconciliation fixes	Revised gas transfer code and reconciliation code operational	September 2006	Not applicable—policy approach revised
	Develop proposal on long-term reconciliation arrangements	Issue consultation document on proposed reconciliation arrangements	December 2006	Achieved at a later date—consultation paper issued in January 2007
	Prepare recommendation on reconciliation arrangements	Recommendation on efficient arrangements to the Minister	June 2007	Not achieved—recommendation delayed by complexity of issues

## 6.5 Development of wholesale market trading arrangements

The GPS expects Gas Industry Co to propose arrangements for:

The development of protocols and standards applying to wholesale gas trading, including quality standards, balancing and reconciliation.<sup>13</sup>

The development of a secondary market for the trading of excess and shortfall quantities of gas.<sup>14</sup>

### a) Quality standards

In the past financial year, Gas Industry Co made a recommendation to the Minister that the limits on gas specification do not need to change as the existing standard is not considered a barrier to new gas fields coming on stream. This recommendation was consistent with earlier advice received from an independent engineering design consultancy—Plant & Platform Consultants Ltd—and analysis of the submissions received during the industry consultation process. Gas Industry Co's report noted that the enforcement of the existing standard was an issue for some industry participants. The company proposes to address this issue as part of its transmission access review work stream. The Minister accepted the company's recommendation. In his letter of 8 August 2006, the Minister wrote:

I am pleased to see that Gas Industry Co has conducted an investigation into this matter and has determined that the current specification provides an appropriate compromise between the diverse needs of participants across the supply chain. In particular, your finding that the current specification is adequate for the gas from new fields that will come on stream is welcome. I support your suggestion to conduct further periodic reviews to ensure that the specification remains adequate.

### b) Wholesale market development

The other main activity has been in relation to the short-term market for the trading of gas at the wholesale level. The company has adopted a two-stage approach to improving the transactional efficiency of gas trading.

The first stage is the development of a standard contract. The purpose of a standard contract is to remove a significant barrier identified in an industry survey; namely, the transaction costs of negotiating a separate contract for each tranche of short-term gas traded. A standard contract was developed in workshops with industry participants and was released on 30 April 2007. This contract is on the company's website and is available for use, free of charge, to any party that wishes to trade gas.<sup>15</sup>

<sup>13</sup> GPS: para 13.

<sup>14</sup> GPS: para 9.

<sup>15</sup> [http://www.gasindustry.co.nz/Standard\\_Contract.php](http://www.gasindustry.co.nz/Standard_Contract.php)

The second stage is to establish a simple, cost-effective electronic platform to facilitate spot trades of gas on a standard platform contract. During the financial year, Gas Industry Co issued two discussion papers on aspects of the design of trading platforms *Wholesale Market Design* and *Wholesale Market Design: Further Consultation* and significantly advanced the detailed design of the preferred option. The company also developed a functional specification for an IT platform, conducted a successful RFP process for a preferred vendor, and progressed the drafting of the market rules and supporting contracts.

The strategic plan milestones were substantially completed, although the recommendation to the Minister on the preferred option was not made in the financial year due to the timing of Board meetings.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Wholesale markets development	Develop detailed wholesale market trading arrangements, including any changes to gas specification	Issue discussion paper	September 2006	Achieved
		Revise arrangements to take account of industry feedback and issue discussion paper	December 2006	Achieved
		Report to the Minister	December 2006	Achieved
		Development of trading platform and detailed arrangements	March 2007	Substantially achieved—some details such as trading location need to be finalised
		Prepare recommendation on wholesale market	June 2007	Achieved at a later date—report to the Minister issued in August 2007



## 6.6 Review of infrastructure access arrangements

Gas Industry Co is required to review access to gas processing facilities and the transmission and distribution networks.

### a) Access to gas processing facilities

The GPS expects Gas Industry Co to propose arrangements for:

*Protocols that set reasonable terms and conditions for access to gas processing facilities.*<sup>16</sup>

Following extensive analysis of the need for protocols for access to gas processing facilities, Gas Industry Co made a recommendation to the Minister that:

- facility owners be invited to sign up to an industry arrangement to disclose annually the technical specifications of their processing plants as well as indicative forecasts of spare capacity; and
- if agreement could not be obtained, Gas Industry Co would make a further recommendation to the Minister to regulate for disclosure.

In his reply of 14 March 2007, the Minister advised Gas Industry Co:

*I recognise the merits of your recommendation to adopt a low cost industry-led voluntary information disclosure regime given the lack of evidence of any major inefficiencies in current access arrangements that would support introducing prescriptive access protocols...*

*I note that there is widespread industry support for... Gas Industry Co's... analysis and conclusions during the consultation process and that only one party... expressed strong disagreement...*

*I encourage Gas Industry Co to move forward and put in place its proposed information disclosure regime. However, if universal acceptance of the scheme is not forthcoming by mid-2007, I shall expect a formal recommendation from you to regulate for the supply of this information.*

Gas Industry Co wrote to the relevant industry participants in April 2007, with a deadline of 30 June 2007, seeking agreement to the proposed information disclosure measures.

Despite earlier consultation feedback and receipt of a number of informal positive responses, obtaining industry agreement was problematic and no industry participants had signed up to the proposed arrangements by the 30 June deadline. The various reasons for lack of agreement included delays in obtaining respective internal approvals and apparent unwillingness to be 'the first to sign'.

Gas Industry Co has requested a three-month extension from the Minister, but at the time of preparing this annual report it is not confident industry agreement will be achieved in the next financial year.

<sup>16</sup> GPS: para 9.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Access to gas processing facilities	Develop proposed access arrangements for gas processing facilities	Issue proposal on access arrangements for consultation	September 2006	Achieved
	Prepare recommendation on access to gas processing facilities	Recommendation on access rules, if required	December 2006	Achieved— recommendation was for implementation by way of industry arrangement
		Implementation	June 2007	Not achieved— facility owners have not responded within timeframes

#### b) Access to transmission pipelines

The GPS expects Gas Industry Co to propose arrangements for transport on New Zealand’s high pressure transmission pipelines:

The establishment of an open access regime across transmission pipelines so that gas market participants can access transmission pipelines on reasonable terms and conditions.<sup>17</sup>

During the financial year, a number of work programmes were commenced by both the industry itself and Gas Industry Co to address the matters raised in the company’s issues consultation process.

One issue is the bundling of multilateral and bilateral terms in Vector’s transmission services agreements and interconnection agreements. Vector has now agreed to separate out the multilateral terms into a Vector Transmission Code and has met with parties to these agreements to settle on the code’s form.

Another issue relates to the balancing of gas flows in and out of a pipeline. Pipeline balancing became a major operational issue in December 2006 and January 2007 when gas offtake from the Maui pipeline consistently fell short of injections, resulting in a build up of gas inventory in the pipeline and repeated interventions by the pipeline operator.

<sup>17</sup> GPS: para 9.

Pipeline owners ran a series of industry workshops to address the underlying causes of this situation. Each workshop reviewed a different factor influencing pipeline balancing. They included matters such as the influence of special arrangements—legacy arrangements—the commercial and technical arrangements for balancing gas flows, data availability, as well as other matters. While the workshops were a useful forum for information exchange, no firm proposals emerged. Gas Industry Co remains concerned about these aspects of pipeline balancing and it will continue to assist the industry to find solutions.

Many of the concerns about effective operation of gas transmission were found to be associated with, or caused by, confusion or lack of systems to develop and manage multilateral arrangements. This is a priority work stream for Gas Industry Co. The company is developing a regulated solution by which multilateral arrangements would be subject to a set of legislated rules. This solution would still allow pipeline owners to set their own terms of access, providing they are in accordance with the rules.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Open access review	Undertake high-level issues review	Issue discussion paper on transmission pipeline access review	September 2006	Achieved—discussion paper issued in June 2006
	Report findings of issues review	Report to the Minister on the outcomes of the issues review	December 2006	Achieved in October 2006
	Prepare proposal on access to transmission pipelines	Issue consultation document on proposed recommendation	March 2007	Achieved—consultation documents issued in October 2006 and March 2007



### c) Access to distribution pipelines

The GPS expects Gas Industry Co to propose arrangements for:

The establishment of consistent standards and protocols across distribution pipelines so that gas market participants can access distribution pipelines on reasonable terms and conditions.<sup>18</sup>

The strategic plan includes milestones on distribution contracts for an issues report by October 2006, a proposal for consultation by March 2007, and a recommendation to the Minister by June 2007.

In order to progress this work stream, the company has had informal discussions with a number of industry participants about the current distribution arrangements and also commissioned some research on the experience of model distribution contracts in the electricity sector.

At the same time as Gas Industry Co has been considering the possibility of model contracts for gas distribution, the Commerce Commission has been developing its proposals for control of the Vector and Powerco gas distribution businesses to replace the provisional controls that took effect on 25 August 2005.



<sup>18</sup> GPS: para 9.

The Vector and Powerco pipelines that are subject to control, in combination, supply 63 percent of the gas supplied through the distribution pipeline networks and provide 76 percent of distribution pipelines by length. This means the proposed controls will apply to the majority of the distribution pipeline networks and will provide a benchmark for the balance of the sector.

Gas Industry Co concluded it would be inefficient to investigate and recommend terms and conditions for access to distribution pipelines, until the nature of the gas control regime administered by the Commerce Commission is clearer. Therefore, Gas Industry Co, in consultation with the Minister, decided to defer this work in favour of other priority areas.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Distribution pipelines	Research distribution contract issues and design guidelines and model contracts	Complete report on distribution contract issues and develop guidelines and model contract arrangements	31 October 2005	Not achieved—work stream deferred until related Commerce Commission work in this area is completed
	Consult on proposed new arrangements and analyse submissions	Complete consultation and report on preferred arrangement	1 March 2006	
	Review uptake and effectiveness of proposed new arrangements	Report on distribution contract arrangements	1 March 2007	

## 6.7 Development of gas outage and contingency management arrangements

The GPS includes requirements that:

Gas is delivered to existing and new customers in a safe, efficient, fair, reliable and environmentally sustainable manner.

Risks relating to security of supply, including transport arrangements are properly and efficiently handled.<sup>20</sup>

Existing arrangements for dealing with security of supply are handled by the National Gas Outage Contingency Plan (NGOCP), a voluntary arrangement between industry participants.<sup>21</sup> However, the voluntary nature of the NGOCP means it is vulnerable to one or more parties not acting as required in a given situation. This risk is exacerbated by the NGOCP lacking any commercial arrangements to account for inadvertent gas trades between users as a result of a supply security incident.

In July 2006, Gas Industry Co issued a discussion paper *Review of Gas Emergency Arrangements* that:

- listed the shortcomings of the NGOCP, primarily its voluntary nature;
- in the absence of a deeply traded and transparent wholesale market, suggested use of an ex-post fair price determination as a means of deriving a gas price during supply security incidents; and
- proposed to codify the NGOCP arrangements and the pricing methodology in a set of regulations under the Act.

Submissions on this paper raised a number of issues including concerns about whether the NGOCP was a suitable base for the proposed new regulations. In response to the submissions, Gas Industry Co has reviewed its approach and developed a design it regards as optimising the balance between providing mandatory compliance and maximising responsiveness and flexibility, by using industry expertise and experience.



<sup>19</sup> GPS: para 4.

<sup>20</sup> GPS: para 5.8.

<sup>21</sup> <http://www.ganz.org.nz/ngocp-plan>

The new design uses a set of overarching regulations, made under the powers set out in the Act, to define the arrangements that will apply for national and regional contingencies. In summary, these comprise:

- the establishment of a Gas Contingency Operator who will be responsible for managing the system during an incident, ensuring all affected parties are kept informed, managing load on the transmission networks where required, and overseeing termination and restoration;
- an obligation on transmission network owners to prepare plans that will ensure they are able to follow the Gas Contingency Operator’s directions and, in turn, require curtailment of loads directly connected to their networks or issue instructions to retailers for load curtailment downstream of their networks; and
- all of the supporting systems required to implement, test, and maintain the contingency management arrangements.

The policy groundwork for these regulations has been complex. Consequently, Gas Industry Co has not met the milestones set out in the strategic plan. As at 30 June 2007, drafting was well advanced on a statement of proposal and draft regulations, due for release during the first quarter of the next financial year.

Future activity is expected to include implementation of the new arrangements and a review of curtailment bands.

Work stream	Activity	Performance measure 2006/07	Target	Comment
Gas outage contingency management	Develop contingency plan proposal	Issue proposal on gas outage contingency plan for consultation	September 2006	Partially achieved—consultation paper was issued in July 2006 but industry feedback indicated a revised approach was needed
	Develop recommendation on contingency arrangements	Recommendation to the Minister	March 2007	Not achieved—statement of proposal was issued in August 2007 with recommendation to the Minister expected in November 2007

# 07 | Financial overview

## 7.1 Introduction

Gas Industry Co has three sources of funding to meet the costs incurred to deliver effective co-regulation and fulfil its GPS obligations. They are:

- a levy on industry participants pursuant to the Act;
- loans from its shareholders; and
- an annual shareholder fee.

This section describes how this funding was applied over the current financial year and also notes the result of the financial structure review the company undertook during the year.

## 7.2 Shareholder loans

During its establishment phase, Gas Industry Co was funded by limited recourse loans from its shareholders. The original loans were for \$1.6 million and 75 percent of these loans have been repaid in the last two years. As at 30 June 2007, the balance of these loans totalled \$400,000.

The shareholder loan agreements required the loans to be repaid by 20 September 2007 if the company was able to meet all its financial obligations. The company had originally intended to repay the loans in the current financial year but after the review of its financial structure, as described under 7.5 of this section (page 40), it negotiated an extension of the original terms for a portion of the loans.

Gas Industry Co is grateful for the ongoing financial support it receives from its shareholders.

## 7.3 Annual fees

Gas Industry Co's constitution requires all shareholders to pay an annual fee to the company. That fee is set each year by the Board.

The Board set the annual fee for the 2006/07 financial year at \$10,000, plus GST, a shareholder. This income was used to fund a portion of the company's general operating expenses.

## 7.4 Levy funding

### 7.4.1 Power to levy

The Act provides in section 43ZZB for Gas Industry Co to recover the cost of fulfilling its industry body duties through a levy on industry participants. The levy requirements are set out in regulations made by the Governor-General each year based on a recommendation from Gas Industry Co.

### 7.4.2 Possibility of over or under recovery of levy

To allow for the timely enactment of the levy regulations each financial year, Gas Industry Co must set its budget and work programme nine months prior to the beginning of that year. In practice, this requires the company to forecast where it expects to be in the policy development process before it has fully analysed the issues, or engaged with stakeholders on their concerns. This factor, and the fact that the levy is based in part on variable gas sales volumes, means every year there is a risk of over or under recovery of levy funds.

This prospect is anticipated by section 43ZZC(3) of the Act, which provides for any over or under recoveries to be taken into account in subsequent levies. The company considers any over or under recovery for a particular financial year should be attributed to the levy segment from which it has been gathered. For example, if there was an over recovery as a result of an increase in estimated wholesale gas volumes, or because of an over estimation of the costs of a work stream paid by the wholesale gas levy, this over recovery should be offset against the wholesale levy requirements of subsequent years.

### 7.4.3 2006/07 levy on industry participants

The Gas (Levy of Industry Participants) Regulations for the 2006/07 financial year were gazetted in June 2006. The levy comprised two parts:

- a wholesale gas levy of 1.78 cents, plus GST, for each GJ of gas purchased by an industry participant directly from gas producers during the relevant quarter, payable by three equal monthly instalments during each quarter; and
- a retail gas levy of \$6.30 a year, plus GST, for each installation control point (ICP) calculated monthly on the basis of the number of ICPs supplied by each retailer at the end of the previous month.

The total revenue raised under the 2006/07 levy regulations was \$4,204,598. This comprised a wholesale levy revenue of \$2,634,208 for wholesale gas volumes based on 148 GJs of gas, and a retail levy revenue of \$1,570,390 based on 249,268 ICPs.

### 7.4.4 2006/07 financial results

Adding interest income and shareholders' annual fees to the levy revenue gives Gas Industry Co a total revenue of \$4,367,824. This revenue is primarily applied to Gas Industry Co's salaries, and its corporate and consultancy activities. The net surplus after tax for the financial year ended 30 June 2007 is \$711,550, compared to a budget net surplus of \$316,880. The budgeted net surplus was necessary because of prior losses carried forward.

Therefore, for the financial year ended 30 June 2007, Gas Industry Co over recovered \$394,670 of levy funds. This was due to a combination of higher-than-expected wholesale gas volumes, and lower-than-expected work stream expenditure due in part to staff vacancies.

As the 2007/08 levy regulations have already been set, this over recovery will be offset against the revenue collection required in the 2008/09 financial year, in accordance with the principles outlined above (7.4.2).

Detailed accounts for the 2006/07 financial year are in section 08 of this report (pages 41–52).

## 7.5 Long-term funding requirements

### 7.5.1 Review of financial structure

A recent review of Gas Industry Co's financial structure highlighted a number of challenges the company faces around its cash flow management. These include:

- revenue variability—because part of Gas Industry Co's funding is based on wholesale gas volumes, it faces revenue uncertainty when wholesale gas usage varies from the forecasts used to set the levy;
- expenditure uncertainty—while the company's core costs, such as salaries, premises, and corporate office costs are reasonably predictable, every year there is inevitable uncertainty around issues that may be revealed in policy analysis and consultation on GPS tasks, and about requests from the Minister and industry participants for policy advice or rule changes; and
- limited ability to change the levy—the levy setting process results in a practical inability to change the levy once it has been established for a particular financial year.

Accordingly, the Board has determined it is appropriate and prudent for the company to build up sufficient cash reserves to provide a buffer against these contingencies.

### 7.5.2 Establishment of reserves

From the beginning of the 2007/08 financial year, shareholders' annual fees will be set aside to establish cash reserves, rather than using them to defray operational costs. The company will retain a portion of original shareholder loans until the reserves have reached an appropriate level.

## 7.6 2007/08 funding

The Board has confirmed the annual shareholder fees for the financial year ending 30 June 2008 will be the same as for the current financial year; namely, \$10,000 a shareholder. However, the primary source of revenue for the company will continue to be a levy on industry participants.

The levy for the financial year ending 30 June 2008, has been set and will comprise:

- a wholesale gas levy of 1.93 cents, plus GST, for each GJ of gas purchased by an industry participant directly from gas producers during the previous month; and
- a retail gas levy of \$8.18 a year, plus GST, for each ICP calculated monthly on the basis of the number of ICPs supplied by each retailer at the end of the previous month.

# 08

## Financial statements

Directors' report [42](#)

Audit report [43](#)

Statement of financial performance [44](#)

Statement of movements in equity [45](#)

Statement of financial position [46](#)

Statement of cash flows [47](#)

Statement of accounting policies [48](#)

Notes to the financial statements [49](#)



## Directors' report

Gas Industry Co is required to maintain an interests register, in which the particulars of certain transactions and matters involving the directors must be recorded. The company's interests register is available for inspection at its registered office at Level 9, State Insurance Tower, 1 Willis Street, Wellington. The following entries were made in the interests register about the directors who held office during the past financial year.

- **A Bansal**—he is an officer of Shell (Petroleum Mining) New Zealand Limited.
- **M X Franklin**—he is an officer of Vector Limited and subsidiaries.
- **M E Jackson**—he is an officer of Genesis Power Limited.
- **M J Verbiest**—he is an officer of Telecom Corporation of New Zealand Limited.
- **Messrs Bolger, Davis, Hill, Verbiest**—their interest with respect to their remuneration.

All directors noted their interest with respect to the Directors and Officers Insurance purchased by the company.

Where a director has declared an interest in a particular entity, as a shareholder and/or director, the declaration serves as notice the director may benefit from any transactions between the company and the identified entities.

### Information used by directors

No member of the Board of Gas Industry Co issued a notice requesting to use information received in their capacity as directors which would not otherwise have been available to them.

### Indemnification and insurance of current officers and directors

Gas Industry Co indemnifies all current directors named in this report and officers of the company against all liabilities, other than that to Gas Industry Co, which arise out of the performance of their normal duties as director or executive officer, unless the liability relates to conduct involving lack of good faith. Gas Industry Co has indemnity insurance to manage this risk. The total cost of this insurance within the financial period was \$28,222 (2006: \$15,500). The annual cost of this insurance is \$34,000.

Directors of Gas Industry Co	Directors' fees	
	2007 \$	2006 \$
Rt Hon J B Bolger, ONZ, Chair	85,708	85,000
R J Hill, Deputy Chair	58,080	70,800
M J Verbiest	48,400	48,000
D K Clifford (resigned 21 April 2006)	-	40,000
K Davis (appointed 31 July 2006)	44,400	-
A Bansal (resigned 15 June 2007)	-	-
M X Franklin	-	-
M E Jackson	-	-
<b>Total</b>	<b>236,588</b>	<b>243,800</b>

At the end of the financial year, the Board had a casual vacancy for a non-independent director, following the resignation of Dr Ajit Bansal on 15 June 2007. This vacancy was filled by Mr David Baldwin of Contact Energy Limited, in July 2007.

The fees and remuneration have been entered into the interests register. In accordance with the shareholders' resolution dated 22 December 2004, only independent directors have been remunerated.

### Auditors

The auditor for the company is Grant Thornton. Grant Thornton did not provide any additional services to the company other than audit services.

### Donations

The company did not make any donations during the period covered by this report.

The annual report and financial statements presented on pages 44-52 are signed for and on behalf of the Board and were authorised for issue on the date below.

### Directors' responsibility statement

The directors are responsible for ensuring the financial statements give a true and fair view of the company's financial position, as at 30 June 2007, and its financial performance and cash flows for the year ended on that date.

The directors consider the company's financial statements have been prepared using appropriate accounting policies, consistently applied and supported by reasonable judgements and estimates, and all relevant financial reporting and accounting standards have been followed. The directors believe proper accounting records have been kept that enable, with reasonable accuracy, the determination of the company's financial position and that facilitate the compliance of the financial statements with the Financial Reporting Act 1993 and the Companies Act 1993. The directors consider they have taken adequate steps to safeguard the company's assets and to prevent and detect fraud and other irregularities.

### For and on behalf of the Board



**Rt Hon James B Bolger, ONZ, Chair**

Date: 14 September 2007



**R G Hill, Deputy Chair**

Date: 14 September 2007

## Audit Report

### To the Shareholders of Gas Industry Company Limited

We have audited the financial report on pages 44 to 52. The financial report provides information about the past financial performance of Gas Industry Company Limited and its financial position as at 30 June 2007. This information is stated in accordance with the accounting policies set out on page 48.

#### Directors' Responsibilities

The Directors are responsible for the preparation of a financial report, which gives a true and fair view of the financial position of Gas Industry Company Limited as at 30 June 2007 and of the results of its operations and cashflow for the year ended on that date.

#### Auditors' Responsibilities

It is our responsibility to express to you an independent opinion on the financial report presented by the Directors.

#### Basis of Opinion

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial report. It also includes assessing:

- the significant estimates and judgements made by the Directors in the preparation of the financial report; and
- whether the accounting policies are appropriate to Gas Industry Company Limited's circumstances, consistently applied and adequately disclosed.

We conducted our audit in accordance with New Zealand Auditing Standards. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to obtain reasonable assurance that the financial report is free from material misstatements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial report. We have not audited the budget information and therefore pass no opinion on it.

Other than in our capacity as auditors we have no relationship with or interests in Gas Industry Company Limited.

#### Unqualified Opinion

We have obtained all the information and explanations that we have required.

In our opinion:

- proper accounting records have been kept by Gas Industry Company Limited as far as appears from our examination of those records; and
- the financial report on pages 44 to 52:
  - complies with generally accepted accounting practice in New Zealand; and
  - gives a true and fair view of the financial position of Gas Industry Company Limited as at 30 June 2007 and the results of its operations and cashflow for the year ended on that date.

Our audit was completed on 14 September 2007 and our unqualified opinion is expressed as at that date.



**Statement of financial performance**

for the financial year ended 30 June 2007

	Notes	2007 Actual \$	2006 Actual \$	2007 Budget \$
Operating revenue	1	4,367,824	4,283,748	3,900,834
Operating expenses	2	(3,635,409)	(3,500,122)	(3,583,954)
<b>Operating surplus before income tax</b>		<b>732,415</b>	<b>783,626</b>	<b>316,880</b>
Income tax	6	(20,865)	(20,109)	-
<b>New surplus/(deficit)</b>		<b>711,550</b>	<b>763,517</b>	<b>316,880</b>

## Statement of movements in equity

for the financial year ended 30 June 2007

2007 Actual				
	Notes	Share capital \$	Accumulated losses \$	Total \$
Balance at 30 June 2005		10	(1,095,313)	(1,095,303)
Share redeemed		-	-	-
<b>Net surplus for the year</b>		-	<b>763,517</b>	<b>763,517</b>
Balance at 30 June 2006	4,5	10	(331,796)	(331,786)
Share redeemed		(1)	-	(1)
<b>Net surplus for the year</b>		-	<b>711,550</b>	<b>711,550</b>
<b>Balance at 30 June 2007</b>	4,5	<b>9</b>	<b>379,754</b>	<b>379,763</b>

for the financial year ended 30 June 2007				
2007 Budget				
	Notes	Share capital \$	Accumulated losses \$	Total \$
Balance at 30 June 2005		10	(1,095,313)	(1,095,303)
Share redeemed		-	-	-
<b>Net surplus for the year</b>		-	<b>763,517</b>	<b>763,517</b>
Balance at 30 June 2006	4,5	10	(331,796)	(331,786)
Share redeemed		-	-	-
<b>Net surplus for the year</b>		-	<b>316,880</b>	<b>316,880</b>
<b>Balance at 30 June 2007</b>	4,5	<b>10</b>	<b>(14,916)</b>	<b>(14,906)</b>

The above statements should be read in conjunction with the accompanying notes.

## Statement of financial position

as at 30 June 2007

	Notes	2007 Actual \$	2006 Actual \$	2007 Budget \$
<b>Equity</b>				
Share capital	4	9	10	10
Accumulated earnings/(losses)	5	379,754	(331,796)	(14,916)
<b>Total equity</b>		<b>379,763</b>	<b>(331,786)</b>	<b>(14,906)</b>
<b>Liabilities</b>				
<b>Non-current liabilities</b>				
Unsecured shareholder loans	3	337,500	800,000	-
<b>Total non-current liabilities</b>		<b>337,500</b>	<b>800,000</b>	<b>-</b>
<b>Current liabilities</b>				
Payables and accruals	7	394,560	524,152	240,933
Employee entitlements	8	23,020	19,253	19,253
Unsecured loan	3	62,500	-	-
<b>Total current liabilities</b>		<b>480,080</b>	<b>543,405</b>	<b>260,186</b>
<b>Total liabilities</b>		<b>817,580</b>	<b>1,343,405</b>	<b>260,186</b>
<b>Assets</b>				
<b>Non-current assets</b>				
Property, plant and equipment	9	208,013	246,282	228,280
<b>Total non-current assets</b>		<b>208,013</b>	<b>246,282</b>	<b>228,280</b>
<b>Current assets</b>				
Cash and bank balances		977,956	743,642	14,533
Accounts receivable	11	11,374	21,694	2,467
<b>Total current assets</b>		<b>989,330</b>	<b>765,336</b>	<b>17,000</b>
<b>Total assets</b>		<b>1,197,343</b>	<b>1,011,618</b>	<b>245,280</b>
<b>Net assets</b>		<b>379,763</b>	<b>(331,786)</b>	<b>(14,906)</b>



Rt Hon James B Bolger, ONZ, Chair

Date: 14 September 2007



R G Hill, Deputy Chair

Date: 14 September 2007

**Statement of cash flows**

for the financial year ended 30 June 2007

	2007 Actual \$	2006 Actual \$	2007 Budget \$
<b>Operating activities</b>			
<b>Cash was provided from</b>			
Levy revenue	4,202,007	3,940,349	3,789,662
Other income	-	175,000	-
Annual fees	100,000	100,000	100,000
Interest received	44,344	38,837	18,634
Net GST refund	20,501	26,034	11,766
Income tax refund	-	925	-
	<b>4,366,852</b>	<b>4,281,145</b>	<b>3,920,062</b>
<b>Cash was applied to</b>			
Payments to suppliers	(2,128,255)	(1,983,158)	(3,792,895)
Payments to employers	(1,331,478)	(916,300)	-
Payments to directors	(237,453)	(250,098)	-
Interest paid	(4,793)	-	-
	<b>(3,701,979)</b>	<b>(3,149,556)</b>	<b>(3,792,895)</b>
<b>Net cash inflows from operating activities</b>	<b>664,873</b>	<b>1,131,589</b>	<b>127,167</b>
<b>Investment activities</b>			
Purchase of property, plant and equipment	(30,558)	(272,101)	(56,276)
<b>Net cash inflows from investment activities</b>	<b>(30,558)</b>	<b>(272,101)</b>	<b>(56,276)</b>
<b>Financing activities</b>			
<b>Cash was provided from</b>			
Proceeds from shareholder loans	-	400,000	-
<b>Cash was applied to</b>			
Repay shareholder loans	(400,000)	(800,000)	(800,000)
Shares redeemed	(1)	-	-
	<b>(400,001)</b>	<b>(800,000)</b>	<b>(800,000)</b>
<b>Net cash inflows from financing activities</b>	<b>(400,001)</b>	<b>(400,000)</b>	<b>(800,000)</b>
Net increase in cash held	234,314	459,488	(729,109)
Cash at beginning of period	743,642	284,154	743,642
Cash at end of period	977,956	743,642	14,533
<b>Reconciliation with operating surplus</b>			
<b>Reported surplus/(deficit) after tax</b>	<b>711,550</b>	<b>763,517</b>	<b>316,880</b>
<b>Items not involving cash flows</b>			
Depreciation expense	67,356	46,103	74,278
<b>Impact of changes in working capital items</b>			
Prepayments	(318)	28,548	388
Accounts payable	(202,931)	273,846	(238,567)
Accruals	66,075	(33,608)	(44,651)
Employee entitlements	3,768	15,924	-
Debtors	(2,591)	(7,462)	7,462
GST receivable	20,501	45,874	11,766
Other receivables	(520)	(88)	(2,378)
Tax provision	1,983	(1,065)	1,990
	<b>(114,033)</b>	<b>321,969</b>	<b>(263,990)</b>
<b>Net cash flow from operating activities</b>	<b>664,873</b>	<b>1,131,589</b>	<b>127,167</b>

The above statements should be read in conjunction with the accompanying notes.

## Statement of accounting policies

### Reporting entity

The financial statements are for Gas Industry Company Limited (Gas Industry Co) as a separate legal entity. Gas Industry Co is a limited liability company registered under the Companies Act 1993. It was approved as the industry body under part 4A of the Gas Act on 22 December 2004 by the Gas (Approval of Industry Body) Order 2004. Gas Industry Co was incorporated on 27 July 2004.

### Statutory base

These financial statements have been prepared in accordance with sections 43ZW to 43ZY of the Gas Act 1992 and in accordance with the requirements of the Financial Reporting Act 1993 and the Companies Act 1993.

### Measurement base

The financial statements have been prepared on the historical cost basis.

### Accounting policies

The financial statements are prepared in accordance with New Zealand generally accepted accounting practice. The accounting policies that materially affect the measurement of financial performance, financial position, and cash flows are set out below.

### Revenue

#### Goods and services

Revenue comprises the levy income received and receivable in accordance with the Gas (Levy of Industry Participants) Regulations 2006.

#### Investment income

Interest income is accounted for as earned.

### Income tax

The income tax expense recognised for the year is based on the accounting surplus, adjusted for permanent differences between accounting and tax rules.

The impact of all timing differences between accounting and taxable income is recognised as a deferred tax liability or asset. This is the comprehensive basis for the calculation of deferred tax under the liability method. A deferred tax asset or the effect of losses carried forward that exceed the deferred tax liability, is recognised in the financial statements only where there is virtual certainty that the benefit of the timing differences, or losses, will be utilised.

### 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, with the exception of receivables and payables that include GST invoiced.

### Property, plant and equipment

#### Initial recording

The cost of purchased property, plant and equipment is the value of the consideration given to acquire the assets, and the value of other directly attributable costs that have been incurred in bringing the assets to the location and condition necessary for their intended service.

#### Depreciation

Depreciation is calculated on a straight-line basis so as to expense the cost of the assets, or the revalued amounts, to their residual values over their useful lives as follows:

Category	Estimated useful life
furniture and fittings	6 years
computer equipment	4 years
office equipment	4 to 10 years
leasehold improvements	amortised over period of lease

### Operating leases

Leases that are not finance leases are classified as operating leases. Operating lease payments are recognised as an expense in the periods the amounts are payable.

### Accounts receivable

Accounts receivable are carried at estimated realisable value after providing against 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.

### Statement of cash flows

The following are the definitions of the terms used in the statement of cash flows:

- Operating activities include all transactions and other events that are not investing or financing activities.
- Investing activities are those activities relating to the acquisition, holding, and disposal of non-current assets.
- Financing activities comprise changes in the capital structure.
- Cash is considered to be cash on hand and current accounts in banks, net of bank overdrafts.

### Changes in accounting policies

There are no changes in the accounting policy. All policies are consistent with those applied in previous years.

### Impact of adopting New Zealand equivalents to International Financial Reporting Standards for the financial year commencing 1 July 2007

The company will adopt the New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) for the financial year commencing 1 July 2007.

The transition to NZ IFRS is being managed internally by conducting a review of the NZ IFRS. This review will include expert external advice on the transition to NZ IFRS. It is unknown what key differences in accounting policies are expected to arise from adopting NZ IFRS. Had these accounts been prepared using NZ IFRS it is estimated that the impacts would have been immaterial to the overall result of Gas Industry Co. The actual impact of adopting NZ IFRS may vary from the information presented.

## Notes to the financial statements

### 1. Operating revenue

	2007 Actual \$	2006 Actual \$	2007 Budget \$
<b>Operating income</b>			
Wholesale levy revenue	2,634,208	2,175,520	2,207,200
Retail levy revenue	1,570,390	1,772,291	1,575,000
Annual fees	100,000	100,000	100,000
Other income	-	175,000	-
Interest received	63,226	60,937	18,634
<b>Total operating revenue</b>	<b>4,367,824</b>	<b>4,283,748</b>	<b>3,900,834</b>

### 2. Operating expenses

	2007 Actual \$	2006 Actual \$	2007 Budget \$
<b>Operating expenses</b>			
Depreciation	67,356	46,103	74,277
Office equipment lease	11,792	9,992	10,860
Premises	84,074	86,577	97,000
Auditor remuneration	5,535	5,000	7,500
Other expenses	3,466,652	3,352,450	3,394,317
<b>Total expenses</b>	<b>3,635,409</b>	<b>3,500,122</b>	<b>3,583,954</b>

To assist with the interpretation of the operating expenses for the financial year ended 30 June 2007, the following expense breakdown is provided.

	2007 Actual \$	2006 Actual \$	2007 Budget \$
Accounting and taxation advice	26,250	16,890	17,000
Directors' fees	236,588	243,800	237,600
General expenses	242,393	137,334	371,604
Recruitment expenses	40,496	192,401	20,000
Secretariat and establishment fees	-	160,915	-
Technical, economic, and legal advice	1,589,447	1,628,931	1,248,113
Wages and salaries	1,331,478	910,537	1,440,000
Working group expenses	-	61,642	60,000
<b>Total other expenses</b>	<b>3,466,652</b>	<b>3,352,450</b>	<b>3,394,317</b>

### 3. Shareholder loans

	2007 Actual \$	2006 Actual \$	2007 Budget \$
Shareholder loans	337,500	800,000	-
<b>Total</b>	<b>337,500</b>	<b>800,000</b>	<b>-</b>

Gas Industry Co has entered into limited recourse loans—shareholder loans—with the following shareholders.

	2007 Actual \$	2006 Actual \$
Contact Energy Limited	62,500	125,000
NGC Holdings Limited	62,500	125,000
Genesis Power Limited	62,500	125,000
Vector Limited	62,500	125,000
Energy Finance NZ Limited, related party to Shell (Petroleum Mining) Company Limited	62,500	125,000
Mighty River Power Limited	37,500	75,000
Powerco Limited	37,500	75,000
Wanganui Gas Limited	12,500	25,000

The terms of the shareholder loans recognise that the loans have been made to fund the establishment of Gas Industry Co and provide for the loans to be of a limited recourse repayable only if Gas Industry Co has sufficient cash resources to make repayment. Loan holders have agreed to an extension of these loans and to a variation of terms. The extension of the loans means that \$337,500 will be repaid proportionately in equal instalments from 2009 to 2011. The variation to the terms means that NGC Holdings will be repaid its balance of \$62,500, as it has redeemed its share and, therefore, is no longer a shareholder. The payment to NGC Holdings will occur during the 2008 financial year. No liability to repay the loans (in part or in full) exists unless Gas Industry Co would meet the solvency test immediately after making the repayment.

### 4. Share capital

	2007 Actual \$	2006 Actual \$
<b>Issued and paid up capital</b>		
<b>Redeemable shares</b>		
Share issued	10	10
Shares redeemed	(1)	-
<b>Balance at end of period</b>	<b>9</b>	<b>10</b>

NGC Holdings Limited redeemed its share on 30 June 2007.

As at 30 June 2007, there were nine redeemable shares on issue. The shares are redeemable at any time for the consideration of \$1 payable by Gas Industry Co on redemption. The redeemable shares confer on the shareholders the rights set out in section 36(1) of the Companies Act 1993.

## 5. Accumulated earnings/(losses)

	2007 Actual \$	2006 Actual \$	2007 Budget \$
Opening balance	(331,796)	(1,095,313)	(331,796)
Net surplus for the period	711,550	763,517	316,880
<b>Balance at end of period</b>	<b>379,754</b>	<b>(331,796)</b>	<b>(14,916)</b>

## 6. Income tax

	2007 Actual \$	2006 Actual \$	2007 Budget \$
Operating deficit before tax	732,415	783,626	316,880
<b>Permanent differences</b>			
Non taxable (surplus)/deficit	(669,189)	(722,689)	(298,246)
Income subject to tax	63,226	60,937	18,634
Tax at 33%	20,865	20,109	-
<b>Income tax recognised in the statement of financial performance</b>	<b>20,865</b>	<b>20,109</b>	<b>-</b>

## 7. Payables and accruals

	2007 Actual \$	2006 Actual \$	2007 Budget \$
<b>Unsecured</b>			
GST payable	8,735	-	-
Accounts payable	272,466	475,396	236,828
Finance lease	2,634	4,105	4,105
Accruals	110,725	44,651	-
<b>Total payables and accruals</b>	<b>394,560</b>	<b>524,152</b>	<b>240,933</b>

## 8. Employee entitlements

	2007 Actual \$	2006 Actual \$	2007 Budget \$
Annual leave	23,020	19,253	19,253
<b>Total employee entitlements</b>	<b>23,020</b>	<b>19,253</b>	<b>19,253</b>

## 9. Property, plant and equipment

2007					
	Cost \$	Opening book value \$	Additions \$	Depreciation \$	Book value \$
Office equipment	37,392	23,503	9,064	(6,820)	25,747
Leasehold improvements	134,598	110,318	-	(33,016)	77,302
Furniture and fittings	87,071	70,208	7,879	(13,773)	64,314
Computer equipment	62,457	42,253	12,144	(13,747)	40,650
<b>Total</b>	<b>321,518</b>	<b>246,282</b>	<b>29,087</b>	<b>(67,356)</b>	<b>208,013</b>

2007 Accumulated depreciation			
	Opening accumulated depreciation \$	Depreciation \$	Closing accumulated depreciation \$
Office equipment	(4,824)	(6,820)	(11,644)
Leasehold improvements	(24,281)	(33,016)	(57,297)
Furniture and fittings	(8,984)	(13,773)	(22,757)
Computer equipment	(8,060)	(13,747)	(21,807)
<b>Total</b>	<b>(46,149)</b>	<b>(67,356)</b>	<b>(113,505)</b>

2006					
	Cost \$	Opening book value \$	Additions \$	Depreciation \$	Book value \$
Office equipment	28,327	4,104	24,177	(4,778)	23,503
Leasehold improvements	134,598	12,076	122,523	(24,281)	110,318
Furniture and fittings	79,193	-	79,192	(8,984)	70,208
Computer equipment	50,313	-	50,313	(8,060)	42,253
<b>Total</b>	<b>292,431</b>	<b>16,180</b>	<b>276,205</b>	<b>(46,103)</b>	<b>246,282</b>

2006 Accumulated depreciation			
	Opening accumulated depreciation \$	Depreciation \$	Closing accumulated depreciation \$
Office equipment	(46)	(4,778)	(4,824)
Leasehold improvements	-	(24,281)	(24,281)
Furniture and fittings	-	(8,984)	(8,984)
Computer equipment	-	(8,060)	(8,060)
<b>Total</b>	<b>(46)</b>	<b>(46,103)</b>	<b>(46,149)</b>

## 10. Commitments

	2007 Actual \$	2006 Actual \$
<b>Operating leases</b>		
Within one year	82,680	82,680
One to two years	75,955	82,680
Two to five years	-	75,955
<b>Total operating lease commitments</b>	<b>158,635</b>	<b>241,315</b>
<b>Other commitments</b>		
Within one year	24,471	21,268
One to two years	4,662	19,366
Two to five years	400	2,906
<b>Total other commitments</b>	<b>29,533</b>	<b>43,540</b>

Gas Industry Co leases premises. The lease expires on 30 May 2009 and does not provide the company with a right of renewal.

## 11. Accounts receivable

	2007 Actual \$	2006 Actual \$
Levy debtors	10,053	7,462
Goods and services tax (GST) receivable	-	11,766
Prepayments	706	388
Provision for taxation	8	1,990
Other receivables	607	88
<b>Current receivables</b>	<b>11,374</b>	<b>21,694</b>

Levy debtors represent unpaid levies as at 30 June 2007. Levies are invoiced and due each month for the liability arising in that month.

## 12. Financial instruments

Gas Industry Co is subject to a number of financial instrument arrangements as part of its everyday operations. These financial instruments include bank accounts, accounts receivable, and accounts payable. As at balance date, Gas Industry Co's bank balances were held in an interest bearing current account.

### Interest rate risk

Interest rate risk is the risk that Gas Industry Co's return on any funds it has invested and the cost of borrowed funds will fluctuate due to changes in market interest rates. The shareholder loans provide for interest to be paid on those loans if requested by the lender. The interest rate applicable is determined by reference to the deposit rates of registered banks for a deposit equivalent to the value of the loan amount and for an 18-month duration. As at 30 June 2007, no shareholder requested interest be paid on their loan to Gas Industry Co and consequently no interest expense has been recognised.

### Credit risk

Credit risk is the risk that a third party will default on its obligations to Gas Industry Co causing Gas Industry Co to incur a loss. In the normal course of business, Gas Industry Co incurs credit risk from financial institutions. Gas Industry Co does not require collateral or other security to support financial instruments with credit risk, as Gas Industry Co deals with financial institutions that have high credit ratings. Gas Industry Co does not have any significant concentrations of credit risk.

### Fair values

The fair value of all financial instruments is equivalent to the carrying amount disclosed in the statement of financial position.

### Currency risk

Currency risk is the risk that debtors and creditors due in foreign currency will fluctuate because of changes in foreign exchange rates. Gas Industry Co is exposed to currency risk on its dealings with consultants in Australia.

### 13. Contingent gains and losses

As at 30 June 2007, Gas Industry Co had no contingent liabilities (2006: nil). There is an arrangement with Westpac Banking Corporation Limited whereby Gas Industry Co has a liability current to the bank for the Westpac Business MasterCard facility (limit \$100,000) and a payroll Letter of Credit facility (limit \$100,000).

### 14. Related party information

The shareholder loans detailed in Note 3 are related party transactions. Various shareholders have, from time to time, provided administrative assistance to Gas Industry Co at no cost. Levy payments are made by industry participants who, in many cases, are also shareholders of Gas Industry Co.

### 15. Remuneration

Salary band	2007 Actual \$	2006 Actual \$
\$110,001–\$120,000	1	–
\$120,001–\$130,000	–	1
\$140,001–\$150,000	–	1
\$150,001–\$160,000	1	–
\$190,001–\$200,000	1	–
\$200,001–\$210,000	1	–
\$290,001–\$300,000	–	1
\$350,001–\$360,000	1	–

### 16. Post balance date events

No significant events, which would materially affect the financial statements, have occurred between 30 June 2007 and the date of signing the financial statements.

### 17. Major budget variances

#### Wholesale levy revenue

Wholesale levy revenue was \$427,008 higher than budget due to higher-than-expected wholesale gas volumes. It was assumed in the budget that the wholesale gas volume would be 124 PJ. The actual wholesale gas volume for the year ended 30 June 2007 was 148 PJ.

## Abbreviations

**Act** Gas Act 1992

**EGCC** Electricity & Gas Complaints Commission

**Gas Industry Co** Gas Industry Company Limited

**GJ** gigajoule

**GPS** *Government Policy Statement on Gas Governance* October 2004

**GST** goods and services tax

**ICP** installation control point

**MED** Ministry of Economic Development

**Minister** Minister of Energy

**NGOCP** National gas outage contingency plan

**NZES** *Draft New Zealand Energy Strategy to 2050*

**NZ IFRS** *New Zealand equivalents to International Financial Reporting Standards*

**PJ** petajoule

**RFP** request for proposal

**UFG** unaccounted for gas

# Directory

## Gas Industry Company Limited

Level 9, State Insurance Tower  
1 Willis Street, PO Box 10 646,  
Wellington 6143, New Zealand  
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**Facsimile** +64 4 472 1801  
**Email** info@gasindustry.co.nz  
**Website** www.gasindustry.co.nz

## Directors

**Rt Hon James B Bolger**, ONZ, Chair, independent director

**Robin Hill**, BComm, FCA, Deputy Chair, independent director

**Keith Davis**, independent director

**Mark Verbiest**, LLB, independent director

**Ajit Bansal**, PhD, BSc (Hons), DipM, non-independent director  
(resigned 15 June 2007)

**David Baldwin**, MBA, BE (Chemical),  
non-independent director (effective 1 July 2007)

**Mark Franklin**, BE (Electrical), non-independent director

**Murray E Jackson**, MBA, BEc, FTSE, FIEAust,  
non-independent director

## Executive

**Christine Southey**, BA (Hons), LLB, Chief Executive

**Helen Brown**, CA, Senior Adviser, Finance

**Kate Conaglen**, BA, Team Secretary/Receptionist

**Ian Dempster**, BE (Electrical) (Hons), MCom (Hons),  
Senior Adviser, Wholesale Markets

**Lucy Elwood**, BSc, LLB (Hons), Strategy and Policy

**Jay Jefferies**, BJuris, Office Administrator/Team Secretary

**Nicki Lau Young**, BA, LLB, Senior Adviser, Legal

**Nicole MacFarlane**, BA, LLB (Hons), General Counsel

**Mark Soper**, BA (Hons), MIntSt, Adviser, Strategy and Corporate

**Gael Webster**, BSc, LLB, Human Resources

**Ian Wilson**, BSc (Structural Engineering) (Hons), BBS  
(Economics), Senior Adviser, Pipelines

## Auditors

Grant Thornton, Wellington

## Bankers

Westpac Banking Corporation Limited

## Shareholders

Contact Energy Limited

Genesis Power Limited

Mighty River Power Limited

OMV New Zealand Limited

Powerco Limited

Shell (Petroleum Mining) Company Limited

Swift Energy New Zealand Limited

Vector Limited

Wanganui Gas Limited

## External consultants

Aretê Consulting Limited

Concept Consulting Group Limited

Creative Energy Consulting Pty Limited

Energy Acumen Limited

Farrier Swier Consulting Pty Limited

Global Business Consulting

Harding Katz Pty Limited

Maunsell Limited

New Zealand Institute of Economic Research

PricewaterhouseCoopers

R P Treder

Simpson Grierson

Strata Engineering Consultancy

Tetenberg & Associates Limited

The Allen Consulting Group

