



Statement of Proposal on FY2013 Strategy, Work programme & Levy

Date issued: 21 December 2011
Submissions close: 10 February 2012





About Gas Industry Co.

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

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

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

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

Submissions close: 10 February 2012

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Executive summary

The Government and the gas industry have implemented a unique co-regulatory model in which a specially established 'industry body' facilitates the nexus between Government and industry to deliver improved governance arrangements for participants and consumers in gas markets. Gas Industry Co was established in 2004 to perform the role of the 'industry body' as set out in Part 4A of the Gas Act 1992 and, in consultation with the industry, sets an annual strategic work programme and associated levy funding requirements.

Gas Industry Co is required to have regard to the objectives and outcomes in the April 2008 Government Policy Statement on Gas Governance (the GPS). Accordingly, under the Act and GPS, the industry body pursues objectives and outcomes that seek:

- efficiency and reliability in the delivery of gas to consumers;
- improved competition in the gas industry; and
- reporting on the current state and performance of the gas industry.

This paper sets out the key elements of Gas Industry Co's strategic plan, work programme and associated levy for the year ended 30 June 2013 (FY2013) and seeks stakeholder submissions on this proposal.

The Company's corporate strategic goal is to optimise the contribution of gas to New Zealand and its purpose is to provide leadership for the Gas Industry and the New Zealand Gas Story. The following strategic objectives are then developed in the proposed FY2013 work programme:

- Build efficient, competitive, and confident gas markets.
- Facilitate efficient use of, and timely investment in, infrastructure.
- Deliver effectively on Gas Industry Co's accountabilities as the industry body (which includes the communication of the NZ Gas Story).

The detailed work programme proposed in this paper includes meeting statutory requirements, such as the administration of existing gas governance regulations, and also seeks to address government and industry priorities through the completion of deliverables of key projects. For the current financial year, this particularly includes the recent development of the Gas Transmission Investment Programme aimed at providing long term solutions to transmission capacity and access issues.

With the competing demands of a finite budget and the Government's desire to reduce costs imposed on levy payers, it is necessary to prioritise the projects that comprise the work programme. Priority is

driven by a matrix of necessity (for example, statutory obligations), maintaining momentum on existing and committed projects, and attending to new work that is seen as a priority by a broad section of stakeholders. The paper provides a framework for assessing priorities and costs, both between and within project areas.

This paper has been prepared after taking into consideration feedback received through written submissions on and attendance at the Co-regulatory Forum held at Gas Industry Co's offices on the 18th November.

Considering the expected end-point of workstreams during FY2012, including unplanned (and therefore unbudgeted) work on transmission issues, we have developed a work programme for FY2013 that continues to meet the above objectives and priorities.

As a result, the estimated FY2013 Work Programme costs of \$6,357,307 are expected to be similar to sum of forecast costs for FY2012 (\$6,089,841) and expected increases arising from the unbudgeted transmission work.

The cost of operations will be met by market fees, raised under specific gas governance regulations, and by the levy proposed in this paper. The proposed levy rates for FY2013 are: a retail levy of \$6.23 per ICP, and a wholesale levy of 1.79 cents per GJ of gas. This is an increase from the current levy rates of \$5.76/ICP and 1.66c/GJ, which is due in part to the increase in forecast costs and in part to the decrease in costs met by market fees.

A more detailed breakdown of proposed cost of operations and levy requirements is set out in section 3 of this paper, and in Appendix C.

Submissions

Submissions on the proposals in this discussion paper should be provided by **5.00pm on Friday, 10 February 2012**. Submissions can be made by registering on Gas Industry Co's website and uploading your submission, preferably in the form of the submissions template attached to this consultation document (Appendix A). All submissions will be published on this website after the closing date. Submissions may be amended up to closure date. Full details of the submissions process can be found in Appendix B.

Contents

1	Legislative and Strategic Context	9
1.1	The Role of Gas Industry Co	9
1.2	Gas Industry Co Strategic Direction	10
1.3	Strategic Plan and Levy Setting Process	10
1.4	Submissions sought on this Statement of Proposal	11
<hr/>		
2	Indicative Work Programme	12
2.1	Prioritisation	12
2.2	Strategic Goal: Build efficient, competitive, and confident gas markets	14
2.3	Strategic Goal: Facilitate efficient use of and timely investment in infrastructure	16
2.4	Strategic Goal: Deliver effectively on Gas Industry Co's accountabilities as industry body	20
2.5	Delivering value for money	25
<hr/>		
3	Funding of Operations	26
3.1	Sources of funding	26
3.2	FY2013 levy evaluation	26
3.3	Levy breakdown	27
3.4	Comparison with prior years	29
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4	Proposed regulation amendments	31
Appendix A	Recommended Format for Submissions	32
Appendix B	Submissions Process	33

1

Legislative and Strategic Context

The Government and the gas industry have implemented a unique co-regulatory model in which a specially established 'industry body' facilitates the nexus between Government and industry to deliver improved governance arrangements for participants and consumers in gas markets. Gas Industry Company Limited was established in 2004 to perform the role of the 'industry body' as set out in Part 4A of the Gas Act 1992 and, together with industry, sets an annual strategic work programme and consults on the associated funding requirements.

This paper presents the Company's strategy, links it to the setting of work priorities in FY2013, and proposes the level of levy required to fund this work.

1.1 The Role of Gas Industry Co

The overall purpose of Part 4A of the Act is to 'provide for the governance of the gas industry'. Gas Industry Co seeks to achieve this through developing gas governance arrangements¹ that meet the objectives of the Gas Act and of the Government Policy Statement on Gas Governance (issued April 2008, the 'GPS').

The statutory objective of any formal gas governance arrangement is to ensure that gas is delivered to existing and new customers in a safe, efficient, and reliable manner. Other objectives set down in the Gas Act are:

- The facilitation and promotion of the ongoing supply of gas to meet New Zealand's energy needs, by providing access to essential infrastructure and competitive market arrangements
- Barriers to competition in the gas industry are minimised
- Incentives for investment in gas processing facilities, transmission, and distribution are maintained or enhanced
- Delivered gas costs and prices are subject to sustained downward pressure.

¹ The Gas Act provides for the making of regulations or rules; however, Gas Industry Co is required to consider all reasonably practicable options for achieving the objectives of any regulations it might consider. As such, we generally refer to 'gas governance arrangements', which includes rules, regulations, and any voluntary arrangements developed with the industry.

The GPS expands the principal objective to include consideration of fairness and environmental sustainability. It also sets out specific tasks or outcomes that the Government wants achieved for the gas industry. The GPS can be found on the Company's website².

1.2 Gas Industry Co Strategic Direction

Consistent with the above legislative and policy framework, the Board of Gas Industry Co has set a corporate strategic direction for the Company that recognises its unique role and establishes goals that will enable it to achieve its important role in the coregulatory model.

Strategic Goal: Optimise the Contribution of Gas to New Zealand

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

Purpose: Provide leadership for the Gas Industry and the New Zealand Gas Story

Of its nature, the gas industry is complex and ever-changing. It is dependent on a range of players, from upstream explorers and producers through to customers, and on competitive markets and ongoing investment of all stages. Gas Industry Co will be a leader, building on its statutory role as industry body, in making the next phase in the New Zealand Gas Story a success.

Objectives:

- Build efficient, competitive, and confident gas markets
- Facilitate efficient use of and timely investment in gas infrastructure
- Deliver effectively on Gas Industry Co's accountabilities as the gas industry body
- Build and communicate the NZ Gas Story (includes review of industry performance)

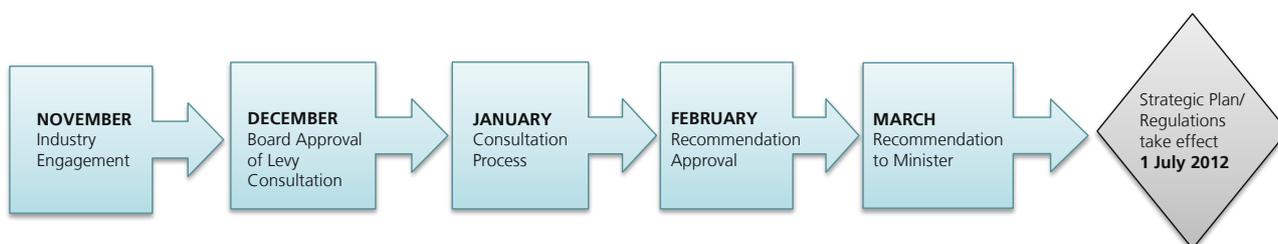
1.3 Strategic Plan and Levy Setting Process

The Company must then consider the work programme necessary to achieve the goals set for it. The Company's strategy and work programme for FY2013, and an indication of further activity in FY2014 and FY2015, will be published before the start of the next financial year (1 July 2012) as the Company's Strategic Plan. This is a document that the Gas Act requires the Company to produce and

² http://gasindustry.co.nz/sites/default/files/publications/Government_Policy_Statement_on_Gas_Governance_-_April_2008.pdf

submit to the Minister. Prior to the publication of this Plan, the Company must also recommend to the Minister regulations for a levy on industry participants to fund its work in the FY2013 financial year.

The diagram below outlines the process undertaken to put in place the levy. As noted above, it operates in parallel with the development of the Company's Strategic Plan.



1.4 Submissions sought on this Statement of Proposal

An industry workshop will be held at Gas Industry Co's office in Wellington from 1.30pm to 3.30pm on Thursday 2nd February 2012. Formal written submissions on the levy will then be due by 5.00pm on Friday, 10 February 2012.

Following analysis of these submissions, Gas Industry Co will finalise its draft Strategic Plan, work programme, and Recommendation for levy regulations for approval by the Board and Minister. Several statutory steps are then required to ensure the Levy Regulations for FY2013 are in place before 1 July 2012.

2

Indicative Work Programme

The indicative work programme set out in this section provides an outline of Gas Industry Co's proposed operations for FY2013 within a framework principally determined by statutory accountabilities, committed deliverables in existing workstreams, and continued work on the Gas Transmission Investment Programme. As indicated at the recent Co-regulatory Forum, it has taken into account feedback received on the proposed programme.

2.1 Prioritisation

With the competing demands of a finite budget and the Government's desire to restrain costs imposed on levy payers, it is necessary to prioritise the projects that comprise the work programme. Priority is driven by a matrix of necessity (for example, statutory obligations), maintaining momentum on existing and committed projects, and attending to new work that is seen as a priority by a broad church of stakeholders. Outlined below is a framework for assessing priorities and costs between and within project areas.

Statutory accountability

Gas Industry Co has a number of statutory accountabilities that arise from:

- obligations under the various rules and regulations that Gas Industry Co previously recommended and now administers; and
- specific tasks defined by the Gas Act and GPS.

Given that these are statutory obligations they must be given a high priority in the work programme. Funding for the first of these is from a combination of market fees and levy, and for second, funding is from the levy.

Committed and/or ongoing projects

There are projects that Gas Industry Co has previously committed to and which are regarded as important by at least a subset of stakeholders or have been requested by the Associate Minister for Energy and Resources. Examples of these are:

- annual benchmarking of small consumer retail contracts;
- developing benchmarks for network use of system agreements (UoSA) and benchmarking UoSAs against those benchmarks; and
- undertaking reviews of existing gas governance arrangements to ensure they continue to be fit for purpose and recommending changes where improvements can be made efficiently.

In order to ensure meaningful progress is made with such projects it is essential to programme them into the budget as a means of establishing or maintaining some momentum.

New work requested by stakeholders

In FY2011 major end users and other industry stakeholders requested a focussed project be led by Gas Industry Co to address the transmission capacity issues, particularly in respect of the North Pipeline owned and operated by Vector. That work is in addition to the existing work programme and is a major undertaking.

The work commands a high priority for stakeholders from the gas industry, end users, and Government. Moreover, a number of those stakeholders are supporting that programme of work by committing their own resources.

In addition, Gas Industry Co consulted (retrospectively) on the emergency regulations that were put in place in late calendar 2010 to address the possible need to address stranding if the E-Gas liquidator had been unable to sell the customer base. Numerous submissions sought a more permanent form of regulation to address future situations. There were also submissions that presented cogent arguments for leaving such situations in the hands of the receiver/liquidator and the market. The strength of the submissions from both camps suggests this is also a priority matter to be advanced. Given that this was not budgeted for in the current year (FY2012) it is likely that only limited progress will be made by FY2013. Accordingly, this is also a priority project for FY2013.

Cost efficiencies

In line with a request from the Minister to all public and levy-raising entities, Gas Industry Co aims to deliver value in both its operational workstreams and in the provision of corporate services to the Company as a whole. There is a specific focus on delivering efficiency and value for money, including by putting downward pressure on corporate costs.

In the remainder of this chapter we outline the components of the work programme and indicate the required resources for completing these elements.

2.2 Strategic Goal: Build efficient, competitive, and confident gas markets

Gas quality

This workstream has developed in response to industry concerns about the responsibility and liability for gas quality in New Zealand. Some participants believe responsibilities are unclear, or not well aligned with liabilities. Gas Industry Co will report to the Minister on this issue by June 2012. In FY2013, we will assess any issues that remain on gas quality. By that time we expect to have greater clarity on what will be addressed by the retailers' Information Exchange Protocol (IEP) and to be in a position to identify any gaps.

Forecast Activities FY2013

- Identify which issues are addressed by retailers' IEP.
- Consider options for addressing any remaining gas quality issues.
- Consult on any substantive issues.

Resources

A modest amount has been provided for in the budget to engage external advisers to assist with any remaining gas quality issues. For budgeting purposes, this work stream is assumed to require 0.2 FTE.

Retail Rule Changes

FY2013 will see the completion of the process Gas Industry Co has begun to amend the Gas (Downstream Reconciliation) Rules 2008. Those rules are in the process of being reviewed in light of several years' experience with them. In FY2013, we plan to refine proposals for rule amendments and develop measures for transitioning to the amended rules.

Gas Industry Co is also progressing amendments to the Gas (Switching Arrangements) Rules 2008 and the Gas Governance (Compliance) Regulations 2008 in FY2012 and plans to address any remaining issues in FY2013.

Forecast Activities FY2013

- Convene and work with an implementation group to address transition issues in downstream reconciliation rule changes.
- Finalise downstream reconciliation rule amendments, provide recommendation to Minister.
- Remaining switching and/or compliance work, including, if necessary, convening and working with a switching changes implementation group.

Resources

This workstream will require a significant amount of internal resource of 0.75 FTE in FY2013 to work with industry implementation groups; to liaise with the allocation agent and registry operator; and to finalise the necessary rules changes. There is also a modest budget for external advice relating to alternative algorithms for calculating the initial allocation.

Retailer Insolvency

Following a request from the Minister, this workstream was formed to consider the market issues created when a gas retailer becomes insolvent and to determine whether permanent regulations are required to manage any future instances of insolvency. Significant interest was expressed in this area through the submissions to the retrospective consultation on the regulations made under urgency in calendar 2010. Gas Industry Co plans to release an issues and options paper in the second half of FY2012. Work in FY2013 will concentrate on the development of a Statement of Proposal, if the earlier work determines that a regulatory solution is needed. The Electricity Authority is also undertaking work relating to retailer insolvency and Gas Industry Co will keep abreast of those developments. Nevertheless, given the structural differences in the two markets it cannot be assumed that the same solution will apply to both gas and electricity.

Forecast activities FY2013

- Dependent on feedback received in FY2012, may range from a regulated option to a market-based solution.

Resources

This will be a significant workstream in FY2013 given the spectrum of views on this issue and the need to liaise with the EA work in this area. There is a modest budget for external advice and that assumes the availability of internal resource of 0.5 FTE dedicated to this workstream.

Distribution Principles

Gas Industry Co has recommended to the Minister that gas distributors' contracts be assessed annually against a common set of distribution principles. The assessment would measure progress made by distributors in reflecting the distribution principles in their own contracts with retailers. In FY2013, Gas Industry Co plans to develop, consult on, and implement a methodology by which adherence to the distribution principles can be evaluated.

Forecast activities FY2013

- Design evaluation process & consult
- Evaluate UoSAs against principles and report

Resources

Given the previous work on designing the evaluation process for model contracts, sufficient expertise resides in-house to undertake that work, estimated at 0.25 FTE. The evaluations themselves will likely be contracted out using the same model as for retail contracts.

Retail Contracts Oversight Scheme

In 2010, Gas Industry Co established a series of benchmarks consistent with satisfactory customer expectations and outcomes. Expected position as at end of FY2012: review of Benchmarks following transitional assessment; consult with retailers on any amendments; meet with the retailers to discuss next annual assessment

Forecast activities FY2013

- Undertake annual assessments of retailer contracts in July 2012.
- Publication of individual assessments.

Resources

This work will require 0.2 FTE to oversee the assessment work and to liaise with retailers on possible amendments and future assessments. A modest external budget is provided for the external assessors.

2.3 Strategic Goal: Facilitate efficient use of and timely investment in infrastructure

Gas Transmission Investment Programme

The Gas Transmission Investment Programme (GTIP) arose from industry concerns over the long-term outlook for gas transmission capacity availability in the Auckland region. The GTIP encompasses a number of interlinked projects relating to the efficient use of and timely investment in infrastructure.

Bridge Commitments

The Bridge Commitments are a package of seven measures that Vector and gas shippers have agreed to undertake to address the short-term issues large end users on the constrained North Pipeline are facing. In FY2013, Gas Industry Co plans to monitor the effectiveness of these commitments in enhancing retail competition on the North Pipeline.

Forecast activities FY2013

- Monitor tenders
- Monitor capacity trading activity

- Operate the capacity trading bulletin board (Gas Transmission Exchange, GTX)

Resources

It is expected that only limited time should be required to monitor or facilitate the Bridge Commitments in FY2013, especially given that the Commitments and associated work is being led by the shippers who made them. By then they will have been in operation for almost a year and it would be expected that participants will have factored those commitments into their processes and procedures. However, there may be a need to report on outcomes to confirm that the Bridge Commitments are delivering the expected benefits, that work will be undertaken externally. Provision has been made for 0.1 FTE.

Gas demand outlook

As part of the GTIP work, Gas Industry Co is commissioning a gas supply and demand model that will be used to examine possible gas supply and demand scenarios. The model will be used to assess the likely need for, and timing of, additional investment in transmission capacity or its alternatives. The model will likely be complete by the end of FY2012, and it will then be used as a means of developing and testing various scenarios for investment in transmission capacity and alternatives.

In the later stages of this work, identified investment possibilities will be assessed against known technical, environmental, legal, and policy constraints.

Forecast activities FY2013

- Use model to assist with developing testing investment options for transmission or non-transmission alternatives.
- Investigate options for implementing new transmission capacity where that is required.
- Work closely with Commerce Commission and other stakeholders.
- Analyse feasibility of potential investment options.

Resources

Assuming the model is completed in FY2012, it is likely that this workstream focus on developing and testing investment options for transmission. This will require 0.7 FTE and moderate external resource.

Transmission access and pricing

The work on transmission access and pricing that was commenced in FY2012 is expected to develop a preferred approach for allocating transmission access and determining an efficient price for the transmission services. The preferred approach will be further refined and developed in FY2013: if it is a non-regulatory solution, then it is likely that a change to the Vector Transmission Code will be needed;

if a regulatory solution is preferred, then it will need to be developed into a Statement of Proposal in FY2013.

Forecast activities FY2013

- If regulatory solution preferred, prepare and consult on a Statement of Proposal
- If non-regulatory, facilitate VTC change request process

Resources

It is envisaged that this would continue to be a resource-intensive process with 1.5 FTE dedicated to the workstream and considerable need for external advice (be that economic, technical and/or legal).

Panel of Expert Advisors and Panel of Strategic Advisors

The Panel of Expert Advisors (PEA) is the industry group tasked with identifying options for ensuring that existing transmission capacity is used as efficiently as possible and opportunities for future investment in gas transmission capacity or its alternatives.

The Panel of Strategic Advisors provides strategic advice on matters referred to it by the programme sponsor. This would likely be in situations where the PEA has provided advice that indicates a split view (either in preferred option or implementation methodology).

Forecast activities FY2013

- Provide secretariat services
- Engage external advisers as required
- Prepare meeting papers as required
- Arrange meetings as required

Resources

Undertaking the secretariat function is reasonably resource-intensive, particularly if the PEA continues to meet at monthly intervals. As a result we are planning on the basis of one FTE being required. Similarly, the PEA will require economic and technical experts to assist it to provide the necessary advice to Gas Industry Co and provision has been made for such advice.

Information Gathering Project

The objective of this workstream is to establish a framework by which Gas Industry Co can access the information it needs to settle particular issues that arise in the gas industry. A statement of proposal is shortly to be released on this issue. At this stage, Gas Industry Co expects that the preferred option

will be a set of regulations that enable us to specify and require information from industry participants. By the end of FY2012, we expect that work will be advanced on a set of draft regulations; work in FY2013 will focus on the recommendation to the Minister and implementing the regulations.

Forecast activities FY2013

- Recommendation to the Minister.
- Work with PCO to finalise regulations.
- Backstop information regulations in place.

Resources

Given that the bulk of the work is expected to be done during FY2012 it is anticipated that there should be minimal need for external advice in the latter stages of this workstream. Experience has shown that, with regulations, there is a good degree of liaison with MED and PCO in finalising the regulations and having them approved. We have allowed for 0.5 FTE in the budget.

Transmission Pipeline Balancing

Expected position as at end of FY2012: MPOC change request outcome known; review status of balancing issues; report progress to Minister.

Forecast Activities FY2013

- Depends on outcome of MPOC change and feedback from Minister/MED
- If further action needed, likely to be subsumed by or at least delayed until outcomes of GTIP access and pricing work.

Resources

Because this work is likely to become part of the GTIP, no specific allocation of resources has been made for the workstream. That said, to the extent that code changes/appeals arise, they will continue to be processed as usual.

Interconnection

Gas Industry Co has an established set of guidelines that set out our expectations with regard to transmission system owners' policies and procedures for connecting to their pipelines. As agreed with the Minister, as interconnections occur, we assess new transmission interconnection processes against these guidelines, with a view to determining whether interconnection policies present undue barriers to entry.

Forecast activities FY2013

- New interconnections reviewed following commissioning.

Resources

There is no specific provision for this work as there is no forward information on the rate of new connections. However, given the sporadic nature of interconnections and the low level nature of the work required to review them it is considered that this can be fitted within the available resources.

Code changes and appeals

Under memoranda of understanding with MDL and Vector, Gas Industry Co processes Maui Pipeline Operating Code change requests and Vector Transmission Code change request appeals.

Forecast activities FY2013

- Process MPOC change requests and VTC appeals as required.

Resources

Although somewhat variable, experience shows that the rate of code changes and/or appeals requires approximately 0.25 FTE per annum. In addition there are sometimes legal issues to consider and a modest amount has been provisioned for external legal advice.

2.4 Strategic Goal: Deliver effectively on Gas Industry Co's accountabilities as industry body

Access to gas processing facilities

The Gas (Processing Facilities Information Disclosure) Rules 2008 gather information on gas processing facilities with a view to settling the issue of whether access to such facilities should be regulated. Under these rules, Gas Industry Co receives and publishes information on the capability of, and availability of capacity at, gas processing facilities; it also monitors responses to requests for third party access to gas processing facilities.

Prior to the expiry of the Rules in 2014, Gas Industry Co will need to consult with gas processing facility owners and the wider industry on experience with the Rules and whether further regulation or other action is required.

Forecast activities for FY2013

- Receive and publish returns from processing facility owners.
- Receive reports from access-seekers (if any).

- Survey facility owners and consult on expiration of Rules.

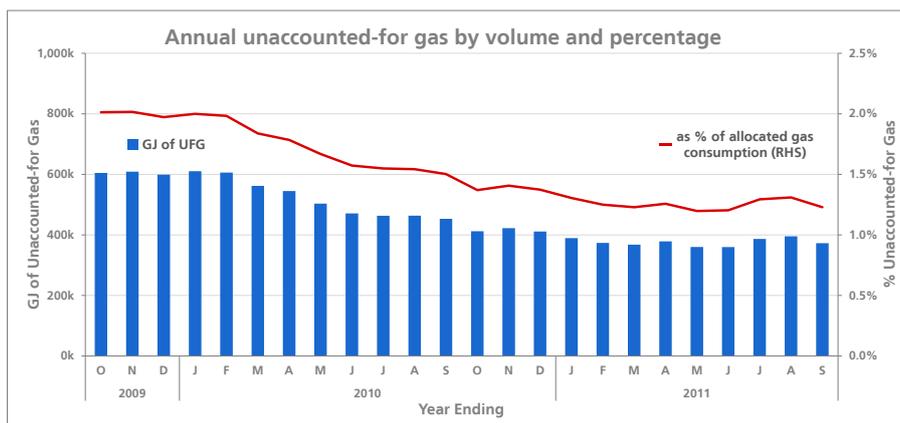
Resources

The resource requirements for this work are quite modest at 0.1 FTE and this work is funded entirely from the levy. Internal resources are engaged in reminding facility owners that returns are due, receiving and publishing those returns, and following up with any overdue returns should that ever happen. In this year's budget there is also a modest amount of external budget for a consultant to undertake a survey of facility owners and any identified access-seekers. That survey is the first step towards determining any further work that might be required for a recommendation to the Minister in FY2014.

Downstream Reconciliation

The purpose of the Gas (Downstream Reconciliation) Rules 2008 is to establish a set of uniform processes that will enable the fair, efficient, and reliable downstream allocation and reconciliation of downstream gas quantities. Under these rules, Gas Industry Co has ongoing obligations to oversee the operation of the allocation agent and other rule provisions. Gas Industry Co also monitors allocation results so as to identify, at an early stage, any issues so that they may be addressed in a timely fashion. This work complements that of a number of industry participants who also undertake monitoring and, from time to time, identify issues to Gas Industry Co or the allocation agent.

These rules have been instrumental in bringing down the level of UFG (at the final allocation stage) and this is largely due to the efforts of industry participants, the increased transparency of the processes for reconciliation, the application of the global methodology, compliance activities, and issues identified and resolved through the performance and event audits undertaken to date. Collectively, this represents an ongoing stream of cost savings in excess of \$2.5 million per annum.



Forecast activities FY2013

- Monitor allocation agent.
- Assess ongoing performance of the rules.

- Monitor allocation results.
- Commission performance and event audits as required.

Resources

Significant resources are required for this work stream. These take the form of approximately 0.5 FTE within Gas Industry Co plus the service provider arrangements with the allocation agent. The first of these is funded from the levy while the second is funded by way of market fees.

Compliance

The Gas Governance (Compliance) Regulations 2008 are an overarching set of regulations that provide for monitoring and enforcement of the other gas governance rules and regulations. The compliance arrangements are designed as a low-cost means of settling rules breaches that raise material issues. Where parties are unable to settle breaches, the last resort is a hearing before a one-person Rulings Panel, a quasi-judicial body. The Rulings Panel can issue fines, make orders for compensation, and make orders directing compliance and/or suspending or terminating participants.

As new rules have been introduced these have typically been associated with an increased level of compliance activity as participants adjust to the new arrangements. The breach statistics reported in Gas Industry Co's quarterly performance reports³ demonstrate that 'teething troubles' with new rules/regulations are short-lived and compliance activity typically sits at a fairly low level.

Forecast activities FY2013

- Perform the Market Administrator role.
- Assist the Investigator and Rulings Panel as requested.
- Monitor regulations for effectiveness.

Resources

Each of the Investigator and Rulings Panel is engaged as prescribed by the Compliance Regulations. Those costs, and any associated expenses, are funded by market fees as provided for in the Compliance Regulations. The Market Administrator role is undertaken by Gas Industry Co and that accounts for 0.75 FTE. Once matters are referred for investigation or referred to the Rulings Panel, then the input from Gas Industry Co will increase, and that increase may be substantial in significant and complex cases. Accordingly, the resources required in this area are almost entirely demand-driven. The assumption for the FY2013 budget is that there will be a relatively low level of compliance and enforcement activity that requires 0.2 FTE of internal resource.

³ These reports can be found on the Gas Industry Co website: <http://gasindustry.co.nz/work-programme/performance-measures/performance-measures-quarterly-reports>

Switching

The Gas (Switching Arrangements) Rules 2008 have the purpose of enabling 'consumers to choose, and alternate, efficiently and satisfactorily between competing retailers'. The Switching Rules provide for a centralised database, the gas registry, that stores key parameters about every customer installation and that monitors each switch from initiation through to completion.

Forecast activities FY2013

- Monitor gas registry service provider.
- Assess ongoing performance of the rules.
- Monitor switching statistics.
- Make determinations under the rules as required.

Resources

Although this used to be quite resource-intensive, particularly in the first year of operation, administering the switching rules is now a relatively low-level activity. Gas Industry Co has allowed for 0.25 FTE internally, thus the levy-funded resources are minimal. The service provider is funded from market fees.

Critical contingency management

The purpose of the Gas Governance (Critical Contingency Management) Regulations 2008 is to '*achieve the effective management of critical gas outages and other security of supply contingencies without compromising long-term security of supply*'. These regulations provide for the appointment of a Critical Contingency Operator (CCO) and that role is responsible for determining, managing, and terminating critical contingencies as well as associated activities such as training and running exercises.

Forecast activities for FY2013

- Monitor the CCO under the Service Provider Agreement.
- Appoint/monitor service providers as required.
- Monitor exercises and events as required.
- Administer contingency pool as required.
- Carry out any remaining work from 2011 Maui Pipeline outage.

Resources

Since 'go live' this has generally been a low-resource work stream. However, the October 2011 critical contingency has indicated a number of matters that need to be addressed, by measures such as training/education or fine-tuning the regulations. It is hoped that good progress can be made during FY2012, but the number of unfunded workstreams already being addressed suggests that it will be unlikely Gas Industry Co will be able to bring this to a conclusion before FY2013. As a result this is likely to require 0.25 FTE for FY2013.

Strategic Plan and Annual Report

The Gas Act requires that the industry body provide its Annual Report to the Minister of Energy within three months of the end of the financial year (the Minister then tables it in the House of Representatives). Similarly, the Strategic Plan is required to be approved by the Minister prior to being finalised and published. As evidenced by this paper, both documents are developed in close consultation with industry participants and other stakeholders.

Forecast activities FY2013

- Prepare/publish Strategic Plan to meet statutory timeframes. Requires Ministerial approval
- Prepare/publish Annual Report, provide to the Minister together with copies for tabling in the House

Resources

This work is predominantly carried out internally utilising staff resources from across the Company. External printing costs and some design work is required, although these are increasingly reduced by using email and website communication.

NZ Gas Story

Gas Industry Co is required by the Gas Act to report on the present state and performance of the gas industry. As reflected in the Company's corporate strategy, there is a role for Gas Industry Co to take a wider look at the industry and to stitch together – through analysis and debate – the wider NZ Gas Story.

Work is accordingly progressing on our State and Performance of the Gas Industry Review (which we also refer to as the 'New Zealand Gas Story') in the expectation that it will be largely completed by the end of 30 June 2012 (FY2012). Apart from fulfilling the statutory reporting requirement, this work is intended to help the industry shape its own future in a more strategic sense.

Forecast activities FY2013

Publication and release of the Review may occur in the early part of FY2013, depending on the timing of any material developments in the meantime, including the supply/demand study and outcomes of

the Gas Transmission Investment programme. The New Zealand Gas Story is intended to be a living document, to be regularly and routinely updated in order that Gas Industry Co maintains a suite of current information and statistics relevant to the gas industry. Other FY2013 activity will include receiving and responding to industry feedback, which will help inform future State and Performance Reviews for the Minister.

Resources

This work is predominantly carried out internally utilising staff mainly within the Chief Executive's team and the Corporate Services Group. Other staff resources from across the Company may be called upon from time to time. External printing costs and some design work is required.

2.5 Delivering value for money

The Acting Minister has written to Gas Industry Co, as an entity that is funded by a levy on industry, to convey the Government's expectations for providing 'value for money' and 'reducing business and household costs'. The letter set out three objectives:

- **Clear priorities** – focusing on things that matter, including providing high quality, cost effective and customer-focused frontline services.
- **High quality services** – ensuring that services are modern, responsive, business like, and provide good value for money,
- **Reducing waste** – ensuring that administration is as efficient, streamlined, and as well organised as it can be

The work programme has been designed to address those issues of most pressing concern to the industry, and the principal Gas Act objective for the Company is focused on the safe, efficient, and reliable delivery of gas to end-users. The Gas Industry Co team comprises experienced and professional people who are committed to operating a fit-for-purpose, best-practice organisation. Furthermore, the Company receives guidance from a Board with lengthy public and private sector experience, and includes industry representatives to cement the link between industry and Government. The Company's operations are supported by an administrative team that consistently seeks to provide high quality support in the most cost-effective way possible. The Company's overhead costs have reduced significantly over the last three years; from in excess of \$2 million in FY2009/10, to the forecast \$1.6M for FY2013.

Q1: Do you consider there to be any other items that should be included in the Company's intended work programme for FY2013?

Q2: Do you consider there to be any items that should be excluded from the Company's intended work programme for FY2013?

3

Funding of Operations

3.1 Sources of funding

The Company has two main sources of funding for the total cost of operations:

Market Fees

Market fees are those monies directly required to administer the various gas governance arrangements currently in place. The fees cover the costs of any service providers (such as the Allocation Agent, or the Registry Operator) and any other expected direct costs related to the monitoring and improvement of those arrangements.

Levy

The levy covers all other costs of the industry body's operations, including the direct costs of workstreams (consultants, salaries, etc), and the corporate overheads for the business (rent, administrative support, legal costs, etc).

3.2 FY2013 levy evaluation

The Company is committed in this current year to delivering on an expanded strategy and work programme, which now includes the unbudgeted Gas Transmission Investment Program. This demanding work will continue into FY2013.

A description of this increased work programme, and the corresponding indicative increase in levy, was presented to industry and stakeholders at the Coregulatory Forum. Gas Industry Co considers it to be a very cost-effective plan to tackle a substantive redesign of transmission arrangements; there was no opposition voiced with respect to any of the work items, and little discussion of the cost.

Considering the expected end-point of workstreams during FY2012, including unplanned (and therefore unbudgeted) work on transmission issues, we have developed a work programme for FY2013 that continues to meet all of the stated objectives and priorities. As a result, estimated Work Programme costs are expected to be similar to the upward revised estimate of expenditure for FY2012.

As a result, the estimated FY2013 Work Programme costs of \$6,357.307 are expected to be similar to sum of forecast costs for FY2012 (\$6,089,841) and expected increases arising from the unbudgeted transmission work.

The cost of operations will be met by market fees, raised under specific gas governance regulations, and by the levy proposed in this paper. The proposed levy rates for FY2013 are: a retail levy of \$6.23 per ICP, and a wholesale levy of 1.79 cents per GJ of gas. This is an increase from the current levy rates of \$5.76/ICP and 1.66c/GJ, which is due in part to the increase in forecast costs and in part to the decrease in costs met by market fees.

3.3 Levy breakdown

As described in Section 2, the work programme for FY2013 is aimed at achieving three key strategic goals. The cost of each goal is set out below, and the consequent levy rates are provided. A full breakdown of the costs of operation is in Appendix C.

Table 1 FY2013 Costs of Operations

FY2013 Budget breakdown			
1: Build efficient, competitive, and confident gas markets			538,919
2: Facilitate efficient use of, and timely investment in, infrastructure			2,362,365
3: Deliver effectively on industry body's accountabilities			3,456,023
	Total Work Programme		6,357,307
	Less: Market Fees		(1,693,925)
	Total Levy Funding Requirement ⁴		4,299,578
		Wholesale	Retail
	Levy Funding Requirement	2,691,253	1,608,325
	GJ / ICP	150,000,000	258,000
	Levy Rate	1.79 cents	\$6.23

Note: Figures include direct costs and overhead.

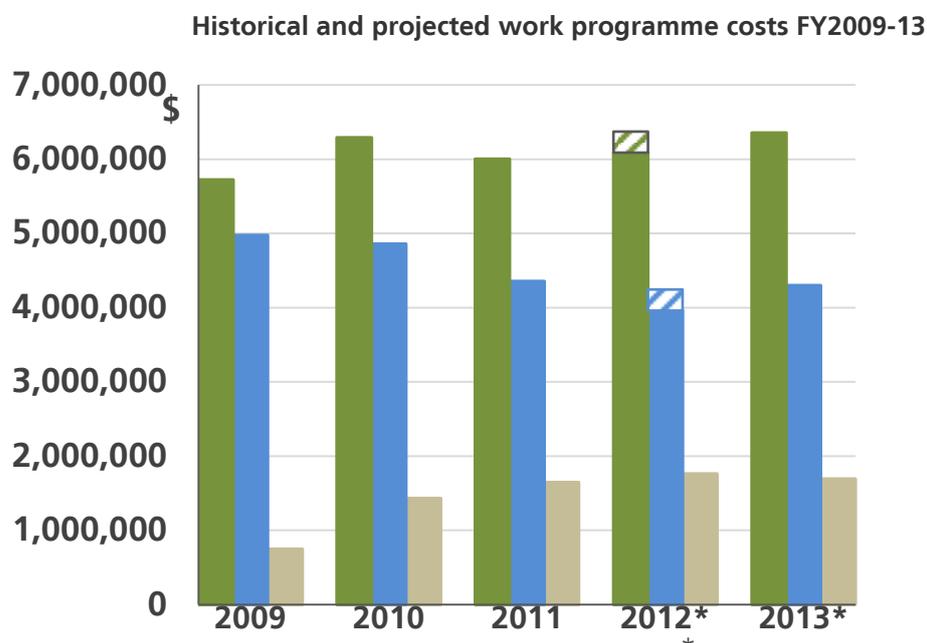
Allocation of indirect costs

Corporate costs broadly comprise the indirect costs of Gas Industry Co, that of governance, administrative support services, and office infrastructure. Work that is generally related to gas governance, rather than to one of the two aggregated work streams (wholesale or retail), is also classified as indirect.

⁴ This figure excludes amortisation costs of \$363,804, which are met by a reserve fund already set aside for this purpose.

Gas Industry Co apportions its indirect costs on the basis of the total direct costs of each work stream. This approach is used as it is simple to apply. It also better represents indirect costs that are unrelated to staff salaries, such as Board costs and work on general aspects of gas governance. As well, it reflects the dominance of consultant costs in the non-salary component of direct costs, which have historically been incurred as a substitute for sufficient permanent staff.

3.4 Comparison with prior years



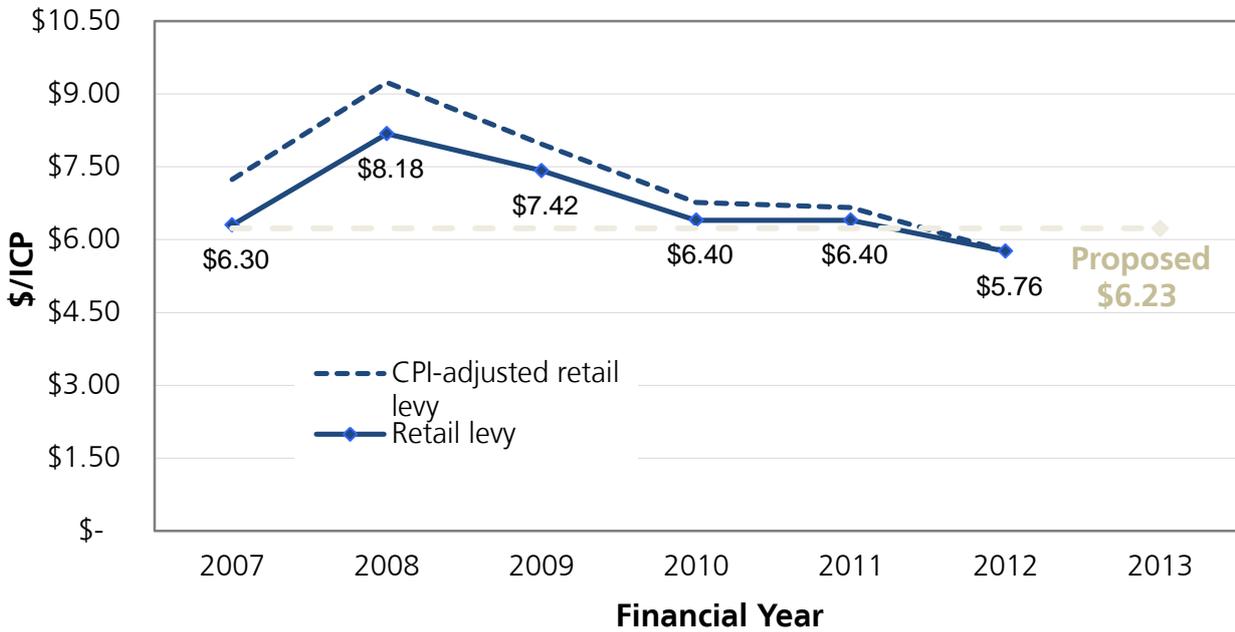
This chart shows total historic work programme costs for FY2009-11, and projected costs for FY2012 and 13 (green bars).

In FY2012, the hatched area indicates the expected increase in expenditure due to unbudgeted costs related to gas transmission issues. The blue and grey bars show the proportion of costs met by the levy (blue) and market fees (grey).

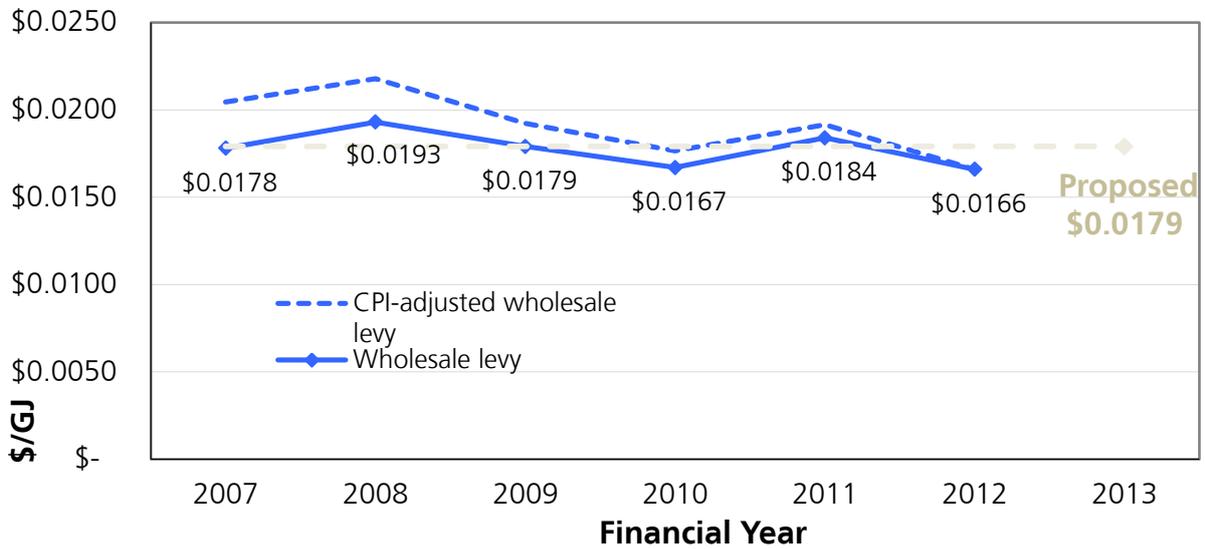
The chart shows that, over the last five years, costs have tended to come in at or around the \$6,000,000 level. The step between FY2012 and FY2013 is consistent with this trend when the increased FY2012 work programme is considered. In budget terms, the effect on the levy of the increased costs and a reduction in market fees is an increase; however, this is mitigated somewhat by the planned use of reserves to cover the expected deficit for this year (which might otherwise have been recouped through a future levy).

The following two charts show how the different levy components (retail and wholesale) have tracked over the last five years.

Retail levy comparison



Wholesale levy comparison



Q3: Do you have any comment on the proposed levy for FY2013?

4

Proposed regulation amendments

When consulting on the levy arrangements for FY2012, the Company raised a concern about the auditing of information on levy returns. Following instances of industry participants discovering and rectifying under-reporting of gas volumes, Gas Industry Co identified that there was no mechanism in the levy regulations to verify the information supplied with respect to wholesale gas purchases.

It was determined that this issue required an amendment to the Gas Act. Gas Industry Co has advised the Ministry of Economic Development (MED) of the need for this amendment, and MED has included it in the Statutes Amendment Bill (No 3) 349-1 (2011), which has been introduced to Parliament and is awaiting progression through the various reading stages.

The proposed amendment to the Gas Act would enable the Company to seek clarity and verify information provided with respect to levy payments.

Should the Statutes Amendment Bill pass prior to the development of the levy regulations for FY2013, it is intended to include in those regulations a mechanism for verifying levy return information.

Q4: Do you have any comment on regulatory amendment described in section 4?

Appendix A Recommended Format for Submissions

To assist Gas Industry Co in the orderly and efficient consideration of stakeholders' responses, a suggested format for submissions has been prepared. Respondents are also free to include other material in their responses.

Submission prepared by: (company name and contact)

QUESTION	COMMENT
Q1: Do you consider there to be any other items that should be included in the Company's intended work programme for FY2013?	
Q2: Do you consider there to be any items that should be excluded from the Company's intended work programme for FY2013?	
Q3: Do you have any comment on the proposed levy for FY2013?	
Q4: Do you have any comment on regulatory amendment described in section 4?	

Appendix B Submissions Process

Submissions

Gas Industry Co invites submissions on the proposed FY2013 levy and the associated issues set out in this paper. Specific matters on which submissions are sought are set out in each section of the paper, and a suggested format for submissions is set out in the template in Appendix A.

Submissions can be made by registering on Gas Industry Co's website www.gasindustry.co.nz and uploading your submission, preferably in the form of the submissions template attached to the consultation document. All submissions will be published on this website after the closing date. Submissions may be amended up to closure date.

Gas Industry Co will acknowledge receipt of all submissions electronically. Please contact Jay Jefferies (Ph: +64 4 472 1800 or email: jay.jefferies@gasindustry.co.nz) if you do not receive electronic acknowledgment of your submission within two business days.

The closing time for submissions is **5pm on Friday 10 February 2012**. Please note that submissions received after this date may not be able to be considered.

Gas Industry Co values openness and transparency and therefore submissions will be made available to the public on Gas Industry Co's website. Submitters should discuss any intended provision of confidential information with Gas Industry Co prior to submitting the information.

Levy workshop

To assist industry participants with submissions and to provide a prior indication of matters that will require consideration by Gas Industry Co, an industry workshop will be held at Gas Industry Co's office in Wellington, from **1.30pm to 3.30pm on Thursday 2nd February 2012**. If you plan to attend the workshop, please register on Gas Industry Co's website by **5pm on Friday 27th January 2012**.

Levy Principles

Gas Industry Co now has seven years' experience of setting an annual levy. During this time we have consulted extensively, receiving a number of submissions on both the structure of the levy and our methodology. Drawing on this experience, a robust set of general levy principles, covering levy setting, were codified into a formal Statement of Levy Principles and published in September 2009.

The Statement of Levy Principles describes the legislative authority, levy principles, and levy structure Gas Industry Co uses when developing its levy recommendation for funding each year under the levy provisions of the Act. These have been used in the preparation of the FY2012 levy proposal.

The Statement of Levy Principles is available on the Gas Industry Co website.

Appendix C Cost of Operations

Strategic Goal 1: Build efficient, competitive, and confident gas markets	\$000's	
Gas Quality	110	
RC Retail	260	
Insolvent Retailers	80	
Distribution	90	
Retail Contracts Oversight	65	605
Strategic Goal 2: Facilitate efficient use of, and timely investment in, infrastructure		
GTIP - Bridge Commitments	150	
GTIP - Gas Demand	910	
GTIP - Transmission Access/Pricing	580	
GTIP - PEA/PSA	420	
Transmission Balancing	30	
Interconnection	100	
Code changes and appeals	100	
		2,290
Strategic Goal 3: Deliver effectively on industry body's accountabilities		
Performance Measurement	50	
Gas Processing	50	
Downstream Reconciliation	*1,140	
Compliance	510	
Switching	*690	
Critical Contingency Management	605	
Strategic Plan/Annual Report	150	
NZ Gas Story	250	3,445

Notes:

1. All numbers rounded to nearest \$5,000.
2. The table above includes service provider costs and other items that may be met through market fees. Costs represent external consultants, staff time, and overheads.

* Includes provision for amortisation of system assets