Gas Industry Co

QUARTERLY REPORT

Quarter ended 30 September 2012

FROM THE CHIEF EXECUTIVE

Gas Industry Co seeks to play a leading role in 'stitching together the New Zealand Gas Story'. Our overarching view remains that the three key issues currently facing the industry are ensuring:

- robust gas supplies
- efficient use of existing transmission capacity and aligning the pathway for future transmission investment
- a clear customer proposition for small gas consumers

Developments during the quarter, including substantive independent reports progressed by Gas Industry Co and others, throw significant light in each of these three areas.

In relation to gas supply, significant reports by Edison Investment Research and the Ministry of Business Innovation and Employment confirm that the ongoing upstream investment in exploration and production leads to a robust supply story, and open up economic growth prospects for regions beyond Taranaki.

In relation to transmission capacity, Gas Industry Co has commissioned New Zealand's first gas supply-demand study. Submissions on the draft report are currently being analysed and the final report will be released in the near future. Indicatively, the existing pipeline system seems to have sufficient capacity to accommodate the higher-demand scenarios, except for Vector's north pipeline system (from central Waikato northwards), which has reached its capacity limit during peak weeks. With greater use of interruptibility (demand side management), this pipeline may also meet the higher demand scenarios. This area is the focus of Gas Industry Co's ongoing Gas Transmission Investment Programme (GTIP).

Thirdly, we continue to work on the 'customer' proposition for the 250,000 small gas consumers. While customer connections and network kilometres are increasing, the position varies across regions and small consumer gas volumes overall are falling.

We have previously expressed a concern that energy market settings have resulted in a greater focus on small electricity consumers, somewhat clouding the position for gas. Gas Industry Co will shortly be releasing a report on *Consumer Energy Options*, which updates our 2009 report on 'Direct Use of Gas'. In summary, this report finds that gas remains a superior or competitive option for home water heating and space heating in particular in the context of the challenge from heat pumps; and for industrial process heat. Traditional concerns about supply are addressed - we have good gas reserves and direct gas use continues to offer benefits in terms of efficiency and lowering our carbon footprint.

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All reports, submissions and other documents referred to in this Quarterly Report are available on our website at www.gasindustry.co.nz

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Additionally in the consumer space, Gas Industry will shortly publish the third annual assessment under our Retail Gas Contracts Oversight Scheme (Retail Scheme), which shows excellent progress by gas retailers in aligning their retail contracts to industry benchmarks.

Accordingly, we continue to see the New Zealand Gas Story as positive, and key industry issues are being addressed. New discoveries and the ongoing development of existing fields provide the foundations for a solid path into the medium- to long-term future. This in turn supports strong supply scenarios that see gas making a continuing valuable contribution to New Zealand's energy mix. For our part, Gas Industry Co's focus remains on ensuring the market structures and arrangements enable gas, and those who find, develop, transport, sell and use it, to optimise that contribution.

Steve Bielby
Chief Executive

Industry Performance Highlights

This Quarterly Report includes Gas Industry Co's regular report (**page 9**) on the industry's performance against the Switching Rules, the Reconciliation Rules, and the Critical Contingency Management Regulations in the three months ended 30 September 2012. Highlights include:

- Since January 2011, monthly balancing gas volumes have averaged less than 31,000 GJ, a decrease of over 92% from the 403,000 GJ monthly average experienced from 2006-2008.
- Customer switches remain at about 3,200 per month, with an annual switching rate of about 15 percent. The time required to process switches on average is less than six days.
- Unaccounted-for gas (UFG) volumes account for about 1 percent of allocated gas volumes on a rolling annual basis, compared with an average of 2.5 percent prior to the introduction of the Reconciliation Rules.
- Retailer market shares, as measured by customer numbers, are largely unchanged. Genesis Energy continues to hold the largest customer market share with about 42 percent, followed by Contact (24 percent) and Mercury (16 percent).
- By volume, Nova and OnGas are the largest retailers, with 29 percent and 26 percent, respectively, of allocated gas volumes over the past 12 months.
- Consistent with the trend over the past 18 months, over 96% of gas customers are connected to a network where at least six retailers trade.

Critical Contingency Management review progress: Proposed changes to ESP and MLC guidelines

Gas Industry Co's review of critical contingency management (CCM) arrangements, including the Gas Governance (Critical Contingency Management) Regulations 2008 ('CCM Regulations'), is aimed at capturing issues and improvements arising from the five-day Maui pipeline outage in October 2011. As previously reported in our June Quarterly Report a Concept Consulting discussion paper Review of Gas Critical Management: Post Maui Pipeline Outage issued in June 2012, attracted eight submissions, which are analysed here.

Gas Industry Co will shortly publish a Statement of Proposal (SoP) recommending changes to the CCM Regulations (and consequential changes to the Gas Governance (Compliance) Regulations 2008 (the Regulations).

Gas Industry Co will also shortly publish revised *Guidelines for Essential Service Providers (ESPs) and Minimal Load Consumers (MLCs)*. Details of the proposed revisions and submissions received are available here.

While the broader review and the SoP may lead to changes in processes for identifying and designating ESPs and MLCs, the proposed changes to the Essential Service and Minimal Load Guidelines relate to ESPs only and as they operate under the current CCM Regulations. Given the potential timeframes for effecting regulatory changes, the proposed revision of the Guidelines introduced in 2009 reflects a desire by industry participants for a more immediate, interim measure to improve clarity and consistency around the ESP designation process.

Concerns about the ESP designation process were highlighted during the Maui pipeline outage, when numerous applications were received from businesses, via their retailers, seeking urgent ESP classification. In summary, Gas Industry Co's analysis shows that the current volume of gas utilised by approved ESPs is much greater than expected, and may compromise the CCO's ability to effectively manage CCM events. The proposed Guideline revisions and SoP proposals accordingly both seek to tighten up the ESP category. This is expected to see a reduction in ESP approvals/volumes, and countervailing incentives on consumers to manage their gas outage (and other supply) risks.

Proposed Compliance Regulations changes

Gas Industry Co has received submissions on proposed changes to the Compliance Regulations, which set out processes for the efficient determination and settlement of alleged breaches of the Gas (Switching Arrangements) Rules 2008, Gas (Downstream Reconciliation) Rules 2008, the CCM Regulations, and the Gas (Processing Facilities Information Disclosure) Rules 2008

The Compliance Regulations have generally worked well in their first four years of operation, and the proposed changes are relatively minor. In addition to correcting some inefficiencies, there is a proposal aimed at reducing compliance costs for participants by introducing a threshold regime for mandatory reporting by the gas registry operator and allocation agent of alleged breaches of the rules and regulations.

Details of the proposed changes and the submissions can be found here. Gas Industry Co will shortly publish further details of the threshold regime for consultation.

Work on CCM Regulations improvements is also expected to result in changes to the Compliance Regulations, which will be included in the Statement of Proposal referred to above. Careful consideration is therefore being given to the coordination of Compliance Regulations changes arising from these two workstreams, and to the efficient development and timing of consequential recommendations to the Minister of Energy and Resources.

Bridge Commitments update

The Bridge Commitments are a series of commitments made by the majority of shippers aimed at addressing short term concerns about competition on the North Pipeline. They have been in place for a year.

In its fourth Progress Report, Gas Industry Co notes that the Gas Transmission Capacity Trading site has been developed and put into operation. In the period, there have been 12 offers of capacity and two capacity transfers under Commitment 1 (capacity offers by incumbent Shippers). As well, there has been good progress on the other Commitments and on the suite of market projects and information projects instituted under Gas Industry Co's wider Gas Transmission Investment Programme (GTIP).

Market circumstances regarding transmission capacity on the North pipeline have also been changing, and recent reporting has helped to clarify some issues. Whereas a year ago, there was a feeling among some in the gas market that the solution to the capacity shortages lay in investment in a new pipeline, now there is a better understanding that the physical capacity of the pipeline is rarely fully utilised.

Gas Industry Co is also aware that contract capacity reservations in the new gas year commencing 1 October 2012 are lower than the previous year. In particular, Gas Industry Co is aware that the amount of firm capacity reserved by one of the thermal generators has decreased from previous years. In addition, Vector transmission has advised that there was no congestion during the winter 2012 period. Nevertheless, the focus of the GTIP, and especially the work of the Panel of Expert Advisers, remains on the efficient use of existing capacity, including measures for managing future congestion.

At the same time, Gas Industry Co is aware of remaining concerns that the Bridge Commitments, in particular Commitment 1, could be more effective in relation to competitive tender processes on the North Pipeline.

Gas Industry Co continues to encourage signatories and other market participants to obtain the best benefits for consumers from the Bridge Commitments while we progress longer-term solutions through the GTIP.

GTIP: Experts panel considers next steps

The Panel of Expert Advisers (PEA) is considering the nature and direction of its next steps following an analysis of submissions on its initial advice to Gas Industry Co from its gas transmission access and pricing work.

The PEA's deliberations are directed at options to improve current transmission capacity arrangements and are being undertaking as part of Gas Industry Co's Gas Transmission Investment Programme (GTIP). Overall, this programme is aimed at achieving more efficient use of existing gas transmission capacity and laying a pathway for efficient future investment in new capacity.

As reported in the June Quarterly Report, the PEA in its initial advice recommends an 'evolution, not revolution' approach to improving current transmission arrangements and presents a strawman proposal to:

- introduce capacity auctioning when capacity demand exceeds supply.
- introduce a nominations regime.
- water down existing grandfathered rights to capacity.
- improve transparency around interruptible arrangements.
- adjust transmission charges, by lowering throughput fees to variable cost, and raising capacity reservation fees to cover all fixed costs.
- confirm bulletin board and tradability of capacity reserved for power stations.
- discuss investment uncertainty and scarcity pricing with the Commerce Commission and MBIE.

In contrast with the PEA's evolutionary/incremental approach, a number of submissions urged a more revolutionary approach, including a move towards the Victoria (Australia) market model; changes such as adopting a common carriage, rather than contract carriage regime; consideration of short-term trading markets; and changes to property rights. Submitters expressed concerns with the PEA's problem definition and a desire to see more options beyond the strawman presented to them, including wider market design alternatives. Gas Industry Co also provided feedback to the PEA in its role as Project Sponsor, requesting clarification of a number of aspects of the strawman proposal.

The PEA is currently reviewing submissions, and consequential changes to its work programme. In summary, this includes consideration of shorter term steps to address the current potential for North Pipeline congestion and possible longer term market design options. PEA materials can be accessed here.

Gas Industry Co welcomes two new PEA members – Stuart Dickson, General Manager Gas, Powerco; and Roger Johnston, Commercial Manager Fuels, Genesis Energy. Both bring a wealth of energy industry experience to the PEA and we look forward to working with them.

Submissions confirm nature of insolvency 'market failure'

Submissions on a report by Castalia Strategic Advisers on gas retailer insolvency arrangements have generally agreed that orphaned customers is the 'market failure' that may result from a retailer's insolvency. An 'orphaned customer' is one physically connected to a network and able to draw gas but with no responsible retailer to pay funds to for the use of that gas.

Five submissions were received on Castalia's 'Discussion Paper on Gas Retailer Insolvency – Report to Gas Industry Company' commissioned by Gas Industry Co, on whether there is a need for a regulatory backstop in the event of a gas retailer becoming insolvent. Submissions closed on 30 July, and an Analysis of Submissions was issued by Gas Industry Co in August.

While there was general consensus that some form of regulatory intervention is required to manage this type of market failure—including the urgent regulation-making powers under the Gas Act 1992 used in the E-Gas liquidation in late 2010—views differed on the form such intervention should take.

As Castalia was not asked to consider regulatory intervention options, Gas Industry Co will consider submitters' preferred regulatory solutions in the next phase of determining appropriate measures to manage a retailer insolvency event. A further paper will be issued for industry comment by the end of 2012.

Castalia was asked to advise Gas Industry Co on whether 'market failures' are present during normal insolvency processes when a gas retailer becomes insolvent. Its report was the first step in a process initiated in March 2011, when Gas Industry Co issued a Statement of Proposal seeking (retrospective) submissions on the Gas Governance (Insolvent Retailers) Regulations 2010, introduced with urgency when gas retailer E-Gas went into voluntary liquidation (the E-Gas customer base was subsequently sold to Nova Energy).

As a result of the consultation process, Gas Industry Co recommended to then Acting Minister of Energy and Resources in May 2011 that the Regulations should be allowed to expire, and Gas Industry Co would establish a workstream to consider whether a generic regulatory solution is required to address retailer insolvency and, if a regulatory solution is deemed to be necessary, the form of that regulatory solution.

In its report, Castalia finds that unexpected insolvencies of gas retailers in New Zealand are rare and unlikely. It identifies some unique features of the New Zealand gas industry that may create problems when a gas retailer becomes insolvent and finds that outcomes resulting in 'orphaned customers' represent a market failure because such customers impose third party costs on other gas market participants.

As a number of retailers sell electricity as well as gas, Gas Industry Co is liaising with the Electricity Authority, which is also currently considering retailer insolvency from a policy perspective.

Distribution Contracts Oversight Scheme endorsed

The Minister of Energy and Resources has endorsed the new Gas Distribution Contracts Oversight Scheme (Oversight Scheme), and preparations are underway for the first assessment to be conducted in February 2013.

Under the Oversight Scheme, contracts between distribution network owners and retailers will be assessed against a set of Principles. It is a non-regulatory mechanism promoting core terms and conditions in distribution contracts that are clear and reasonable, promote market efficiency, and ultimately enhance consumer outcomes.

Results from the first assessment will be reported on a consolidated basis, but individual distributors' results from subsequent assessments will be published on Gas Industry Co's website. Results from the first assessment, conducted by an independent assessor, are expected to be published in June 2013.
In his letter of endorsement, the Minister, Hon Phil Heatley, considers the Oversight Scheme will improve current distribution contracts and that they align with the objectives of the Gas Act 1992 and the Government Policy Statement on Gas 2008.

The Oversight Scheme complements the Retail Gas Contracts Oversight Scheme (Retail Scheme), which assesses gas supply arrangements between retailers and small consumers against a set of more prescriptive outcome-based Benchmark terms. The third assessment under the Retail Scheme commenced in July 2012. The results for the first time will include the outcome for individual retailers and will be published shortly.

Update paper on gas quality

An update paper on Gas Industry Co's investigations into gas quality issues concludes there is no reason to doubt that gas quality is being managed by parties in the supply chain in a rigorous and professional manner. However, it notes that the 'small possibility that a gas quality incident could cause serious economic and reputational harm, coupled with the common pool features of pipelines, puts a particularly heavy onus on the industry to ensure a high degree of transparency'.

Gas Governance Issues in Quality: Investigation Update was issued on 1 August, and resulted in eight submissions by the closing date of 31 August.

Gas Industry Co's review of gas quality management commenced with the publication of, and consultation on, an issues paper in 2010. That work identified concerns about the complex and obscure nature of gas quality management arrangements, as they are incorporated in largely confidential provisions of bilateral contracts.

The Gas (Safety and Measurement) Regulations 2010 (Safety Regulations) clarify the responsibility of wholesalers, retailers, and others, for gas quality, and Gas Industry Co considers that greater transparency is required to demonstrate compliance with this responsibility.

However, gas wholesalers and retailers do not directly control gas quality, and they are proposing a 'Gas Information Exchange Protocol' - involving the gathering of gas quality information from other parties within the physical supply chain - to verify compliance with the Safety Regulations.

Gas Industry Co believes the protocol has the potential to improve transparency of compliance with the Safety Regulations, non-specification gas incidents and any variations to gas quality monitoring requirements agreed between suppliers.

An analysis of submissions on the Investigation Update is underway, and Gas Industry Co is monitoring developments with the protocol. If the protocol is not agreed between participants, or does not provide the necessary transparency, Gas Industry Co will consider other options.

Downstream Reconciliation exemptions and rule 37 determination

During the September quarter, Gas Industry Co consulted on two issues relating to the Gas (Downstream Reconciliation) Rules 2008 (Reconciliation Rules) – the proposed extension of exemptions due to expire on 30 September, and the annual determination of the accuracy threshold in rule 37, also required to be made by 30 September. The Reconciliation Rules prescribe the process for volumes of gas leaving the high pressure transmission system to be reconciled with volumes consumed by end users and appropriately attributed to the retailers responsible for them.

The exemptions have been further extended pending the outcome of the current Reconciliation Rules review, which may supersede them. Gas Industry Co has determined that the rule 37 threshold will remain unchanged at ± 10 percent of the consumption information provided for initial allocation.

Following publication of a Statement of Proposal dated 26 July 2012 on a review of the Reconciliation Rules, Gas Industry Co received seven submissions by the closing date of 3 September 2012. A submissions analysis is being prepared and will be followed by the development of a recommendation to the Minister of Energy and Resources.

Gas Industry Co is being assisted in its review of the Reconciliation Rules by an Advisory Group comprising six industry participant representatives selected for their operational understanding of the downstream reconciliation process. The Group was established following the analysis of submissions on an Options Paper which was released for consultation in December 2011.

The work from the Options Paper has been split into two streams. The July 2012 Statement of Proposal is a key milestone in the first stream of work; the second stream focuses on more complex issues associated with improving the accuracy of initial allocations and is being progressed in a separate Statement of Proposal which is expected to be issued by June 2013.

VTC change appeal

Gas Industry Co issued a draft recommendation supporting a Vector Transmission Code (VTC) change request appeal seeking an alteration to arrangements relating to prudential security and disputed invoices.

The changes, proposed by Vector, did not receive the 75 percent support from Shippers necessary for it to be approved, and was referred by Vector to Gas Industry Co as the VTC appeals body on 31 July 2012.

Gas Industry Co arrived at its draft recommendation to allow Vector's change request after taking account of the four submissions received on the appeal and additional information provided by Vector.

Submissions on the draft recommendation will be taken into consideration by Gas Industry Co in reaching its final recommendation.

Details relating to this VTC change request appeal and submissions can be found here.

November	December
2nd – PEA meeting Statement of Proposal – Critical Contingency Management Regulations review Publication of revised Essential Service and Minimal Load Guidelines(and associated Submissions Analysis) Publication of results from third Retail Gas Contracts assessment Further consultation paper – Compliance Regulations amendments Submissions Analysis –Gas quality investigation update Recommendation to Minister – changes to Reconciliation Rules 20th - Gas Industry Co Annual Meeting of Shareholders. 22nd – Co-Regulatory Forum, including presentation of proposed FY2014 work programme. Release of Concept Consulting final gas supply/demand study report. Release of update report on consumer options/benefits of direct gas use.	Further discussion paper- insolvent retailer arrangements Final recommendation – VTC change request appeal

Performance Measures Quarterly Report for the period ending 30 September 2012

1 Summary

This Report provides an update on the performance measures that Gas Industry Co monitors on a regular basis. The purpose of these measures is to track the performance of the Gas (Switching Arrangements) Rules 2008 (the Switching Rules), the Gas (Downstream Reconciliation) Rules 2009 (the Reconciliation Rules), and the Gas Governance (Critical Contingency Management) Regulations 2008 (CCM Regulations), both in terms of activity related to these statutes and the competitive outcomes that they foster. The Report also tracks transmission balancing actions, as a means of informing Gas Industry Co's work on this issue. .

Highlights of the Report:

- Secondary balancing gas volumes are a fraction of what they were prior to 2009. In the 21 months since January 2011, monthly balancing gas volumes have averaged less than 31,000 GJ, a decrease of over 92% from the 403,000 GJ monthly average experienced from 2006-2008.

- There are about 3,200 switches per month, and the annual rate of switching is about 15%. The time required to process switches on average is less than 6 days, a fraction of the weeks that switching used to take before the inception of the switching rules.

- Volumes of unaccounted for gas (UFG) continue to decline; recent data show that UFG accounts for about 1% of allocated gas volumes on a rolling annual basis. Prior to the introduction of the Reconciliation Rules, the annual percentage of UFG averaged 2.5%.

- There have been no major movements in customer market shares over the past quarter. Genesis Energy continues hold the largest customer market share: about 42% of customer ICPs. Contact is next, with 24%; followed by Mercury, with 16%.

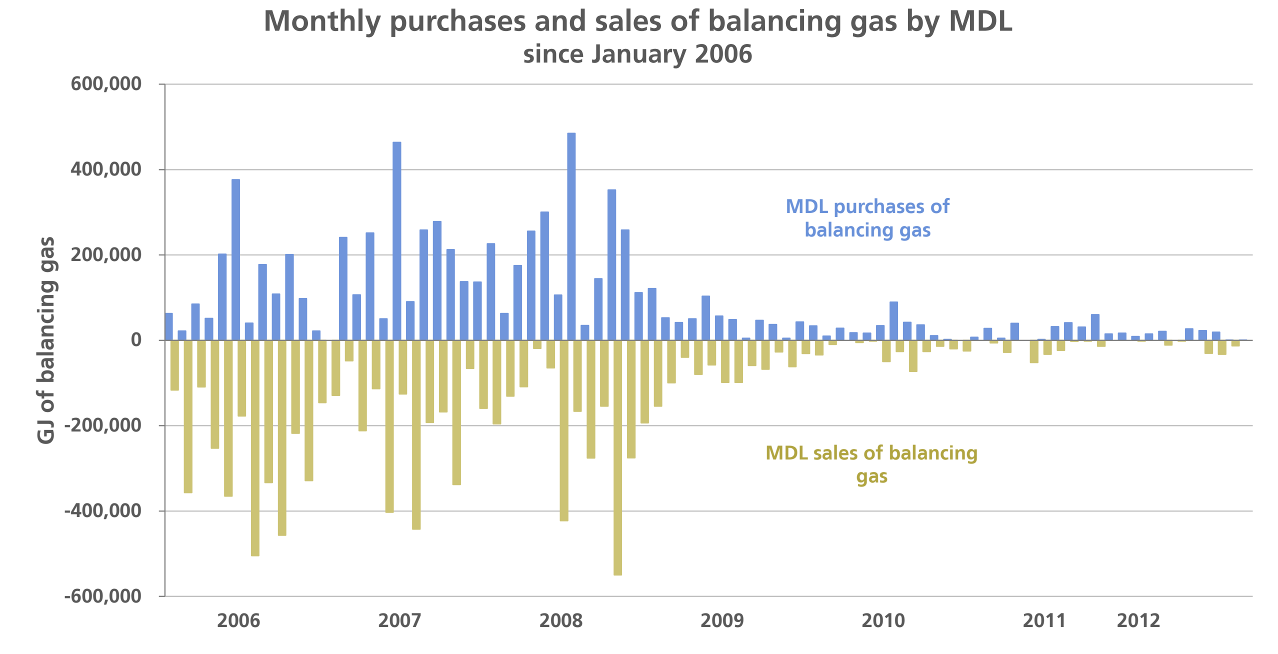
- In terms of market share by gas volumes, Nova and OnGas are the largest retailers, with 29% and 26%, respectively, of allocated gas volumes over the previous 12 months. This reflects their focus on the industrial and commercial sectors of the gas market (although Nova also has a presence in the mass market segment).

- Consistent with the trend over the past 18 months, the majority of gas customers are connected to a gate where least six retailers trade: over 96%, as of September 2012.

2 Balancing gas volumes

The volume of gas in a pipeline relates to the gas pressure in the pipeline and needs to be maintained below the safe operating pressure limit for the pipeline and above the minimum required to maintain the supply of gas to consumers. On the Maui pipeline, pressures will rise or fall as parties who inject gas into the pipeline over- or under-inject and as parties who receive gas from the pipeline under- or over-take relative to their respective scheduled volumes. When a transmission owner, or operator, manages the gas inventory in a pipeline, it is referred to as *secondary* or *residual balancing*. MDL buys and sells balancing gas in order to manage gas volumes and thus maintain gas pressure within safety and operational limits.

Prior to 2008, secondary balancing services were essentially free to holders of legacy Maui gas contracts, but changes implemented at the end of 2008 to the Maui Pipeline Operating Code, together with the arrangements in the Vector Transmission Code, mean that pipeline users are now responsible for imbalances that they create. In 2009, MDL instituted the Balancing Gas Exchange, an online platform that displays pipeline balance conditions and enables parties physically interconnected to the Maui pipeline to post offers to buy and sell balancing gas. These two changes appear to have provided gas transmission customers with an incentive to self-balance and greater information on which to base their balancing decisions.



Source: MDL and bgx.co.nz

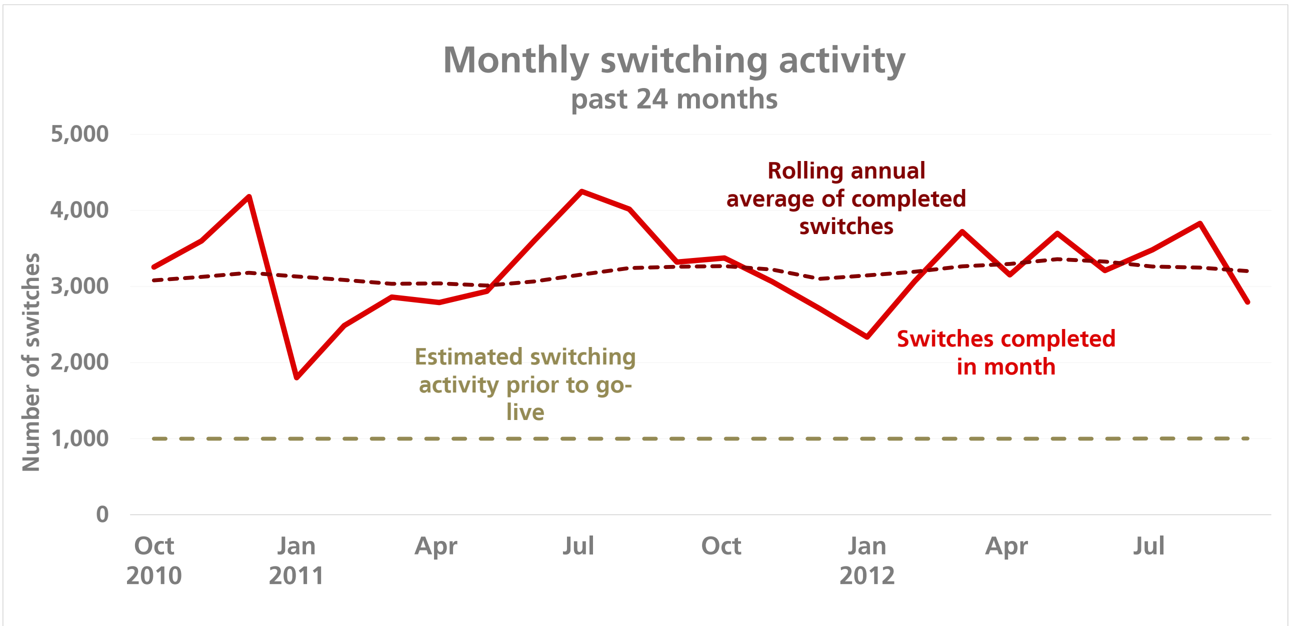
The outcome is the significantly reduced volumes of gas needed to be purchased or sold by MDL to balance the Maui pipeline, as can be seen in the chart above. In each of the calendar years 2006, 2007, and 2008, over 4,600,000 GJ of balancing gas were bought and sold by MDL. In 2009, balancing gas volumes totalled less than 1,500,000; and in 2010, balancing gas volumes were just over 600,000GJ – a decrease of 87% from 2008 volumes. In calendar 2011, balancing volumes declined again, to less than 440,000 GJ. In calendar 2012, about 208,000 GJ of balancing gas have been bought and sold by MDL in the nine months to the end of September.

3 Switching performance measures

Monthly switching activity

There are about 3,200 switches per month, and the annual rate of switching is about 15%. As a comparison, the annual electricity switching rate is about 19.5%.

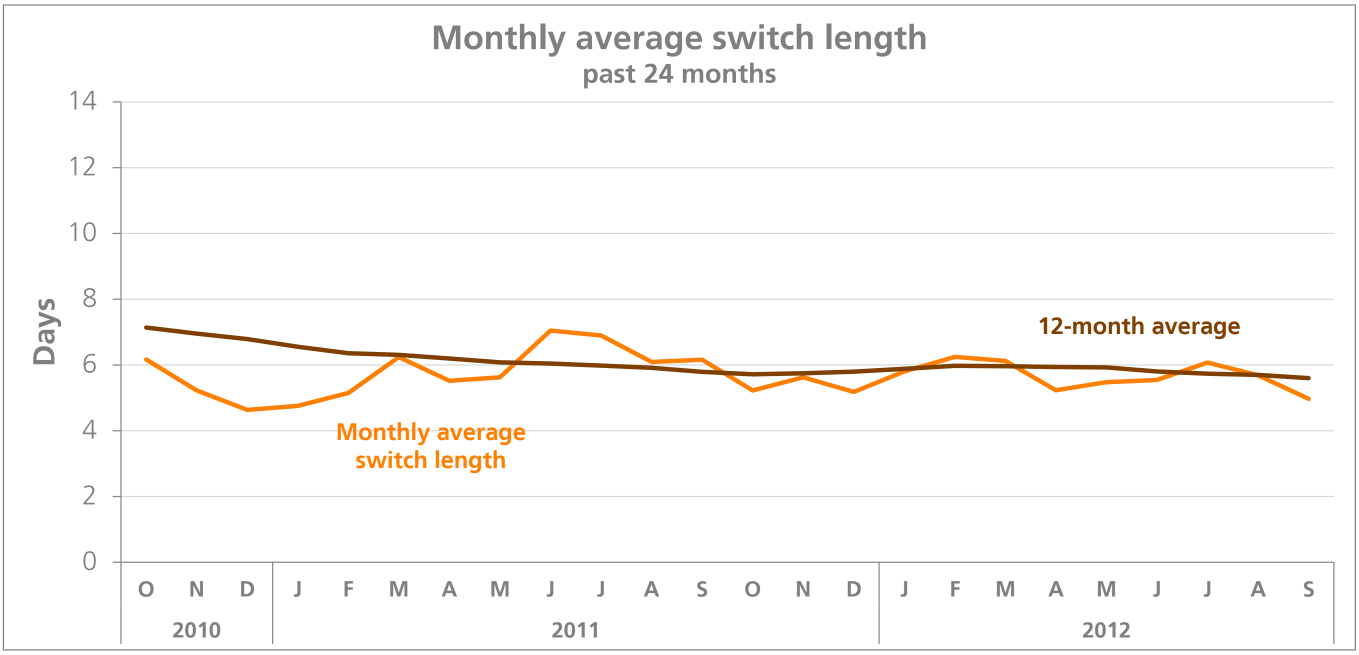
Prior to the gas registry going live in March 2009, approximately 1,000 switches were processed on a monthly basis, and the annual churn rate was approximately 4.8%.



Note that this chart includes only switches that occurred on open-access distribution networks; switches from open-access to bypass networks (or vice versa) would not be recorded as a switch in the Gas Registry.

Time to process switches

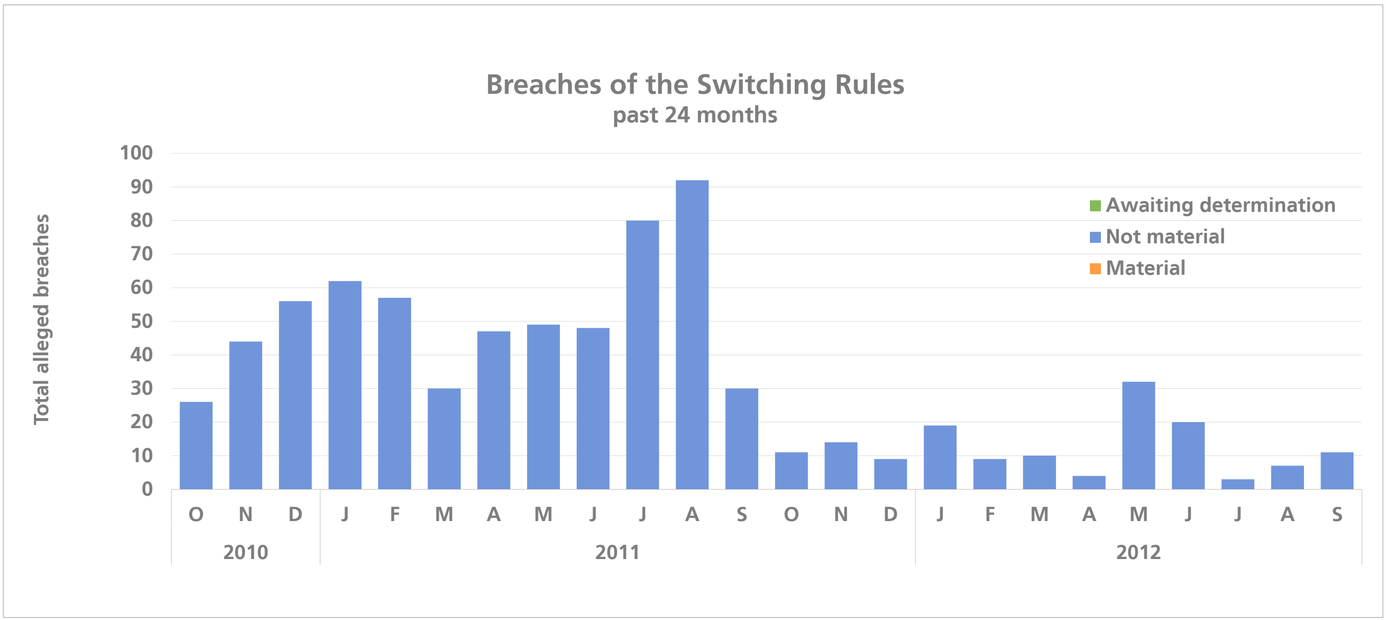
The chart below shows the average length of time it has taken to process the switch requests that have been received in a month. The average time to process a switch has consistently fallen in the past two years. The twelve-month rolling average switching time has been just under six days since July of last year. In comparison, switches could take weeks or even months to process prior to the inception of the switching registry.



Note that the chart above excludes the transfers from E-Gas to Nova and from Auckland Gas to Nova, all of which went through in less than a day.

Number and severity of breaches of the Switching Rules

In the first year after the inception of the Switching Rules, nearly 5,500 switching breaches were alleged. Many of these breaches can be attributed to unfamiliarity with the Rules. Since that first year, the numbers of switching breaches have fallen significantly. The average number of alleged breaches per month has fallen from 450 in the first 12 months to less than 20 in the past 12 months.



4 Allocation and reconciliation performance measures

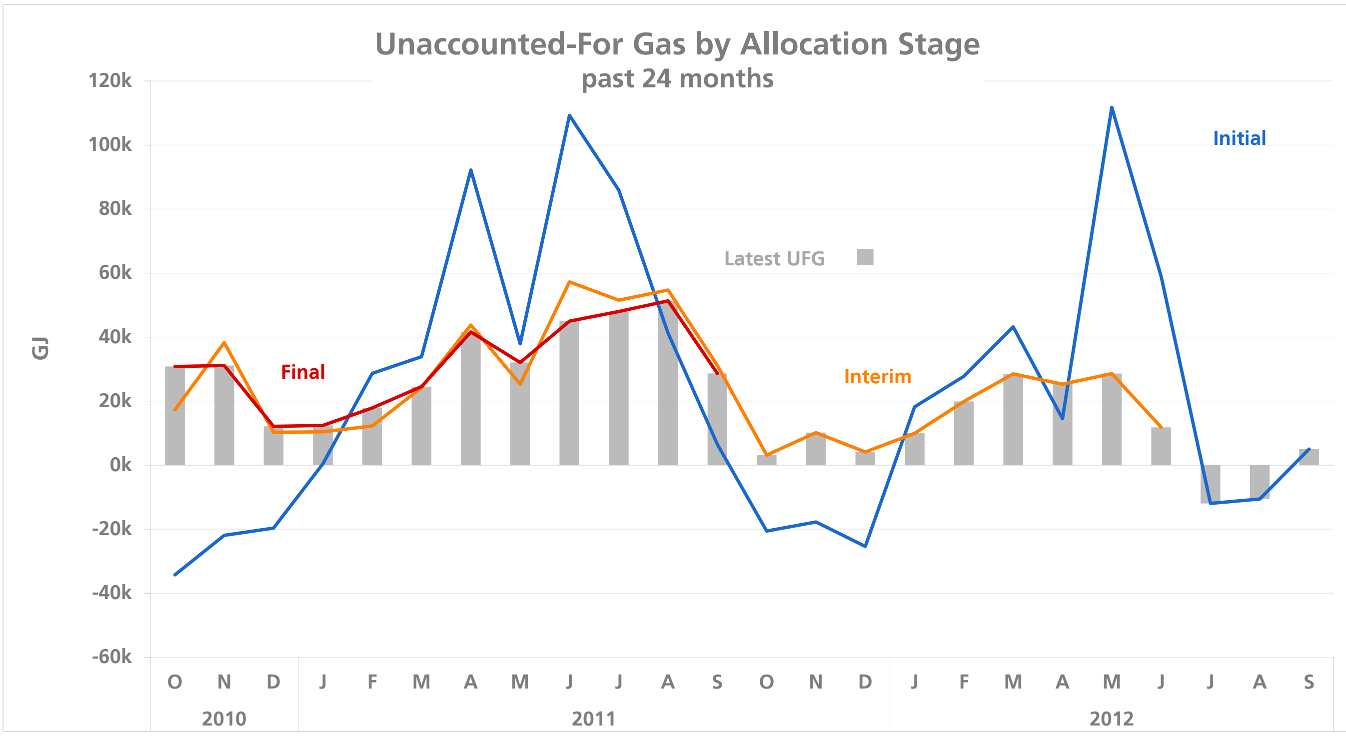
Volumes of Unaccounted-for Gas

Under the Reconciliation Rules, the amounts of gas that retailers estimate their customers have used are subtracted from the amounts of gas leaving the transmission system. The difference is UFG, which arises from technical losses on the system, metering inaccuracies, and retailer estimation errors. UFG imposes a cost on the market: it is gas that retailers are allocated and must pay for, but cannot sell. Tracking UFG is a way of monitoring these costs and the efficiency of the retail market. This transparency should assist the industry to take steps to reduce UFG where it is efficient to do so.

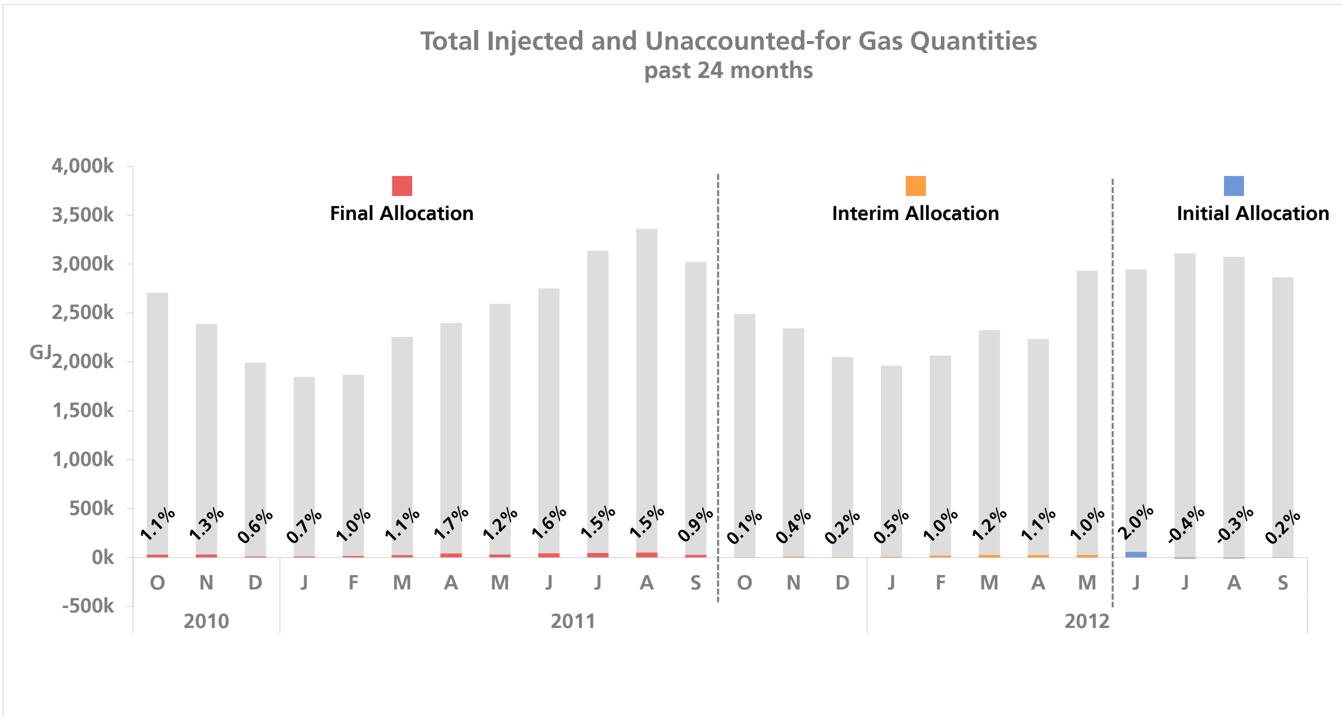
The chart below compares total UFG quantities by consumption month and allocation stage (initial, interim or final). The grey bars show UFG based on the most recent data available.

Changes in UFG from one allocation stage to another are largely due to mass market retailers' consumption submissions becoming more accurate at later allocation stages. The chart below shows that UFG at the initial stage was negative for October, November, and December of both 2010 and 2011, but subsequent allocations for those months resulted in relatively small amounts of positive UFG. This effect is due to retailers tending to overestimate their customers' consumption in that shoulder period between seasons and then correcting the estimations at the interim and final allocations. Similarly, mass market retailers tend to underestimate consumption in winter, as shown by the spikes in UFG at the initial allocation in winter 2011 and 2012.

Generally, UFG volumes diminish considerably from the initial to the interim allocation stages. The final allocation stage reflects further minor adjustments to retailers' data, which can result in slightly more or less UFG, as shown by the orange and red lines in the chart below.

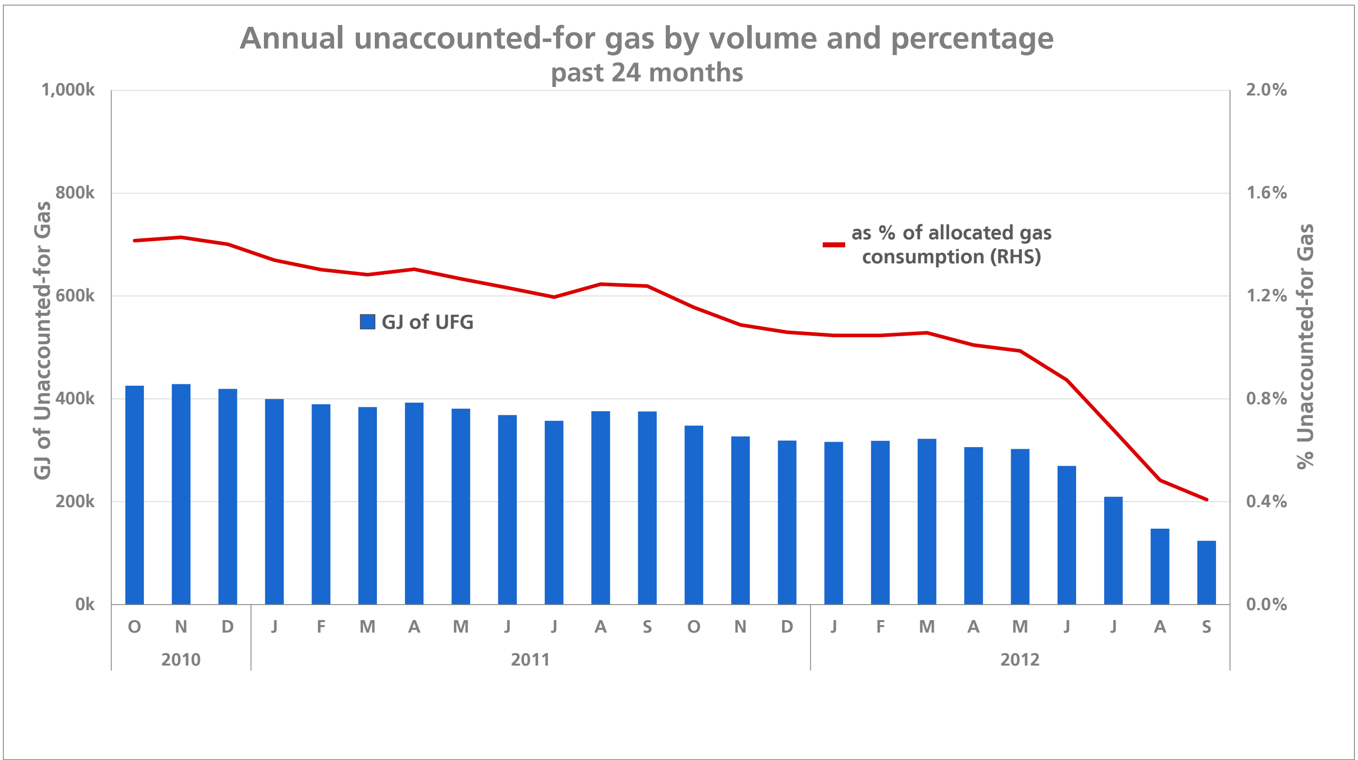


The chart below shows the amount of unaccounted-for gas in comparison to the total amount of allocated gas consumed each month. The grey bars show gas consumption at allocated gas gates, which follows a seasonal pattern: higher in winter and lower in summer. UFG as a percentage of volume follows a similar seasonal pattern.



Another way to think about UFG is the amount recorded over a 12-month period. The chart below shows rolling 12-month UFG figures, both as a GJ total and as a percentage of gas consumed. The information is based on the best data available at the time of publication, so, for example, the September 2012 total is based on three initial allocation results and nine interim results, while the September 2011 total is based on twelve final allocation runs.

For the first year after the Reconciliation Rules came into effect, annual UFG was about 2%. This percentage has dropped to about 1.0% for recent months where interim allocation data are available. (The very low UFG shown for the July, August, and September of this year is likely to be revised upward at the interim allocation stage when more accurate data are available.)

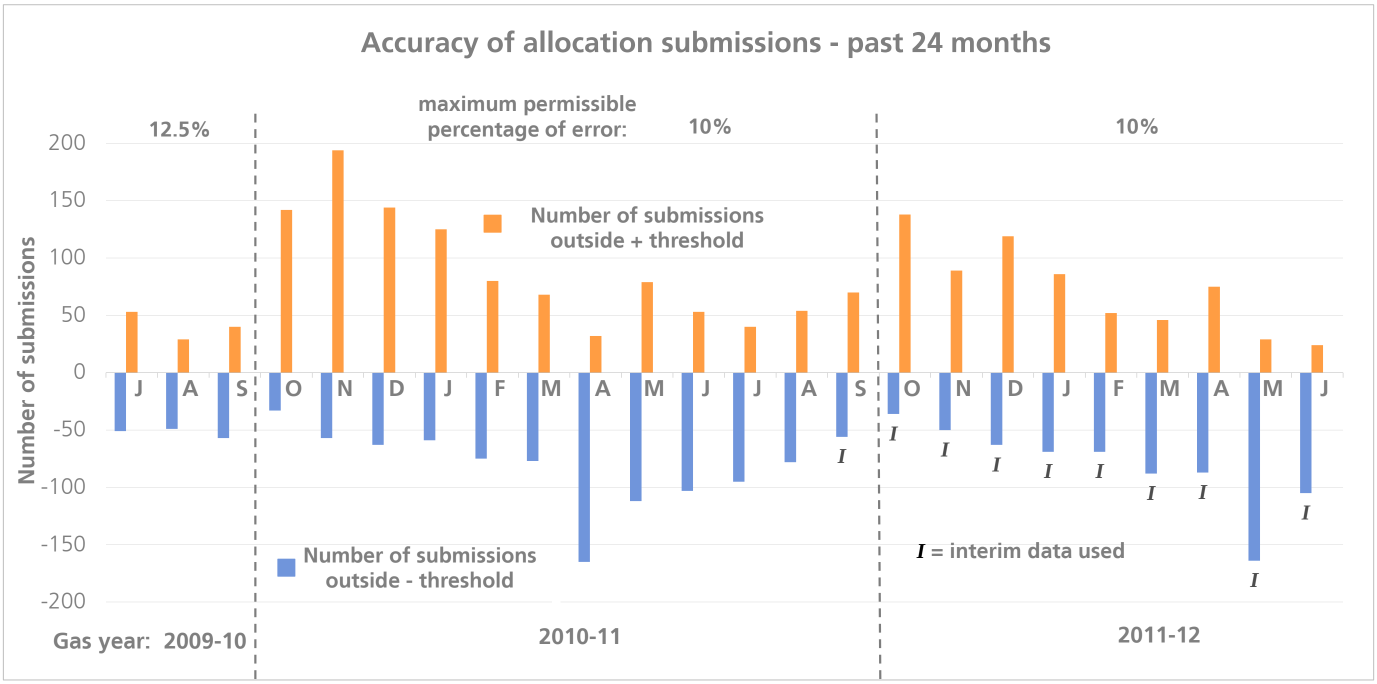


Accuracy of submission data

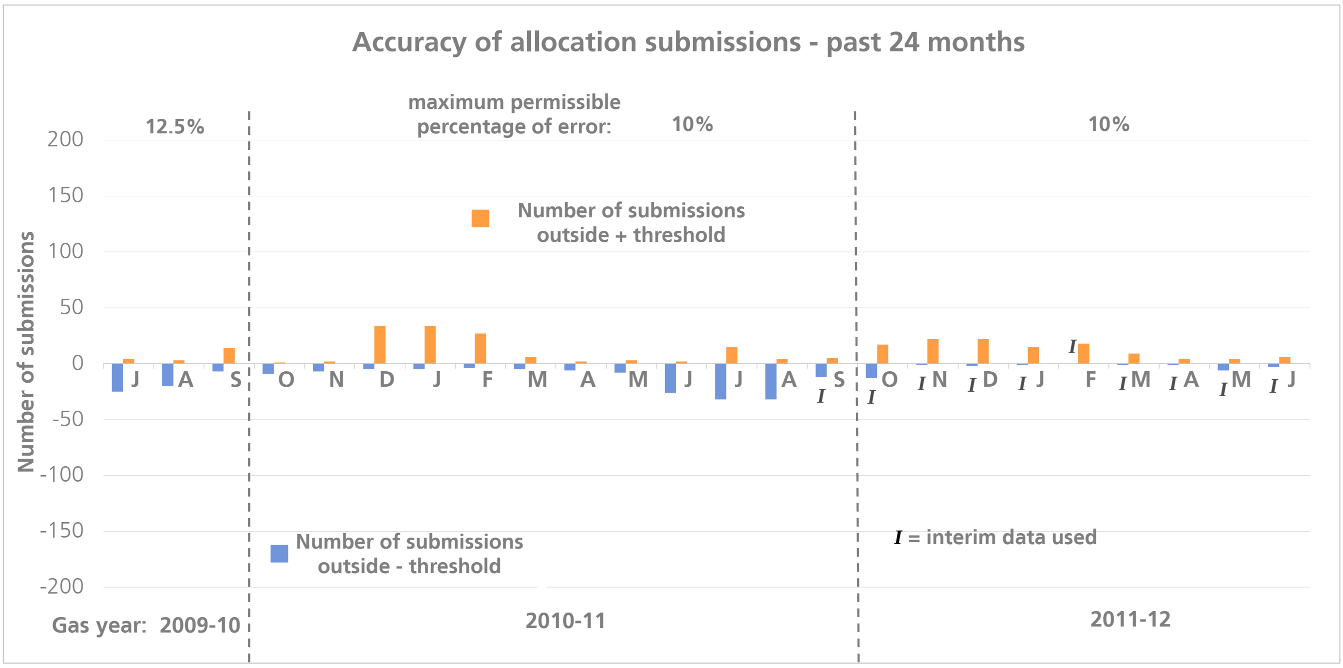
The accuracy of initial submissions is important, as balancing and peaking charges on the Vector transmission system are levied on the basis of initial allocation results and are not subsequently washed up. This means that the UFG created through inaccurate initial consumption submissions falls onto all retailers at the affected gate and affects their exposure to balancing costs. To limit the impact of this effect, the Reconciliation Rules require that initial consumption submissions are within a specified percentage of the final (and most accurate) consumption submissions.

The chart below shows the number of retailer submissions that were outside the maximum permissible error threshold in the last 24 months for which data are available. For this analysis, final submissions were compared to initial allocation submissions for the months they were available (July 2010 – August 2011). Other months use interim submissions (in place of final) for the comparison data and are marked with ‘*I*’. The percentage of error relevant to the consumption month has been used to measure accuracy: 12.5% in the 2009-10 gas year and 10% in both 2010-11 and 2011-12.

There is a pattern of retailers oversubmitting in October through January (shown by the orange bars), which corresponds with the negative UFG seen at the initial allocation stage in the preceding charts. Retailers also tend to undersubmit in the months of April through June (as seen in the blue bars), which corresponds with the high levels of UFG experienced in those months.



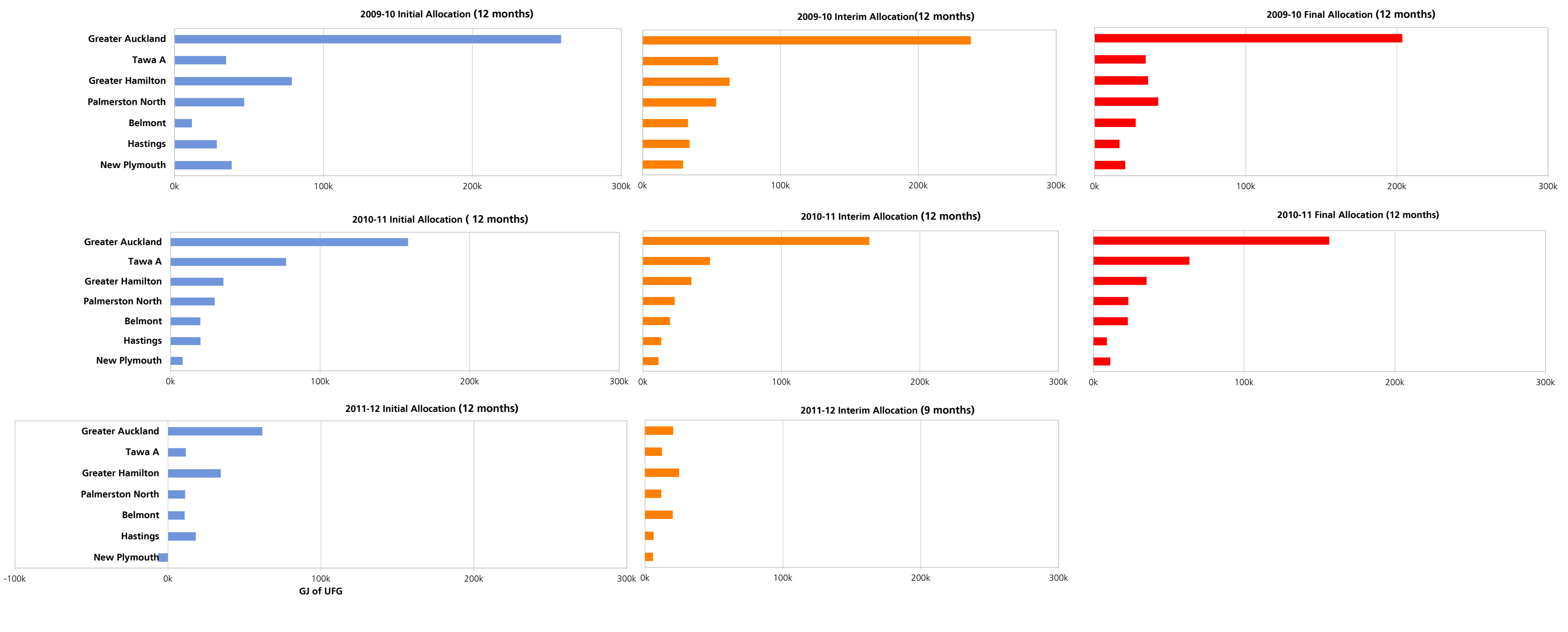
The market administrator uses a volume threshold of 200 GJ as a means of differentiating those breaches that are likely to have had a materially adverse effect on other market participants. The chart below shows the number of accuracy breaches that involve gas quantities larger than 200 GJ. As a comparison of the two charts illustrates, there is a significant proportion of accuracy breaches that have involved less than 200 GJ. Deeming these breaches not material allows industry participants to focus on addressing the harm caused by larger volume estimation errors.



Gas gates where UFG is the highest

Greater Auckland gas gate is consistently the largest contributor of all the gas gates to UFG volumes, followed by Tawa A, Greater Hamilton, Palmerston North, Belmont, and Hastings. These gates are also the largest gates in terms of consumption volumes, so it is not surprising that they are relatively large contributors to UFG. The pattern is roughly consistent over all three allocation cycles and across gas years.

The charts below compare UFG across time and across allocation stages. All allocations have now been performed for the 2009-10 and 2010-11 gas years and are shown in the top two rows. For the 2011-12 gas year, shown in the third row, all twelve initial allocations and interim allocations for October through June 2012 have been performed. As can be seen from the charts, there is a general trend of decreasing UFG both from year to year and across allocation stages. An exception to the trend can be seen with the final allocations for 2010-2011: as shown in the Unaccounted-for Gas by Allocation Stage chart above, in a number of months during the year, the final allocation resulted in slightly greater volumes of UFG.



GAS INDUSTRY COMPANY LIMITED

Audits commissioned

Event audits

There have been no event audits commissioned in the past quarter, reflecting that there have been no unexplained events.

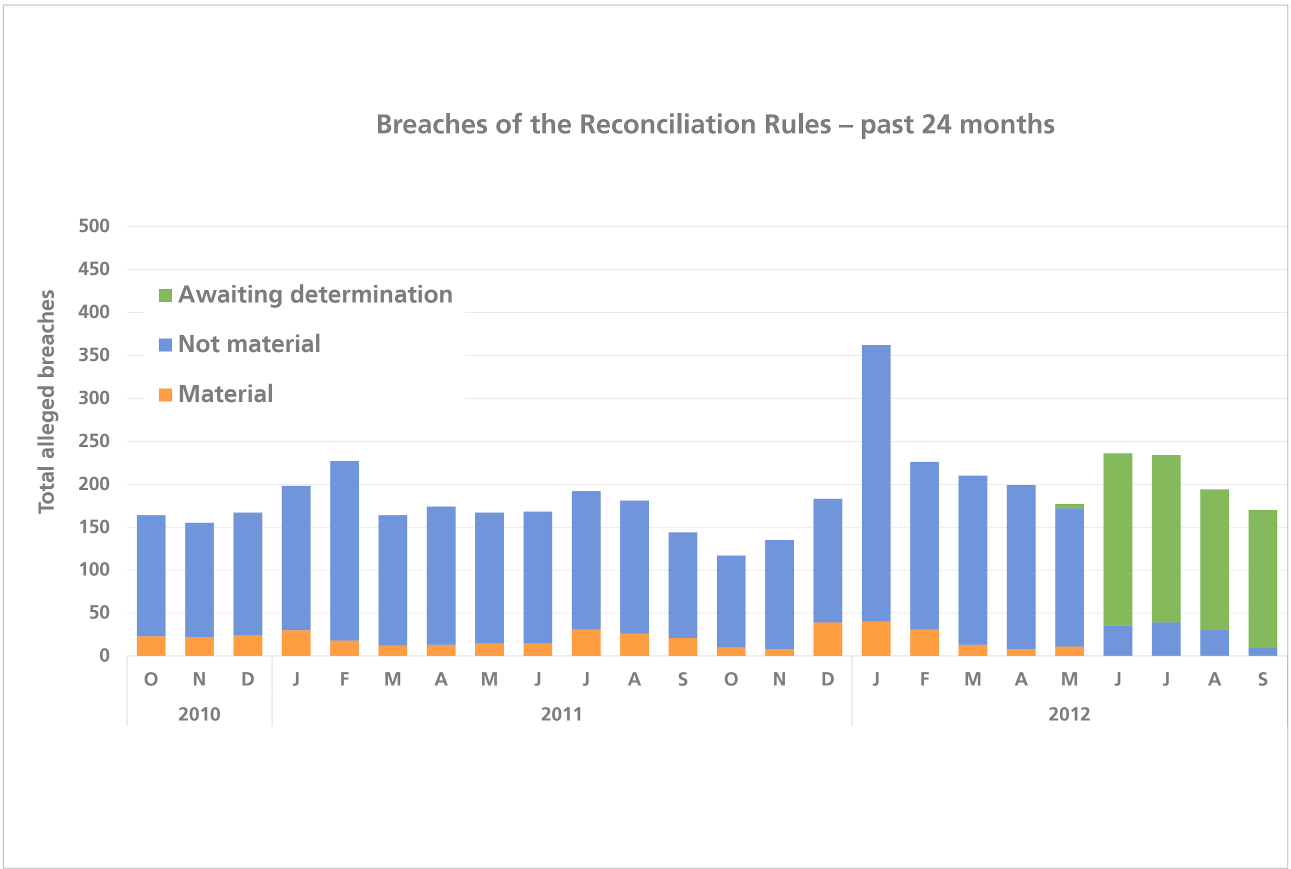
Performance audits

There have been no performance audits commissioned this quarter.

Number and severity of breaches of the Reconciliation Rules

On average, about 85% of breaches alleged under the Reconciliation Rules relate to rule 37, the rule that requires the accuracy of consumption information provided at the initial allocation stage to be within a specified tolerance level of the information provided at the final allocation stage.

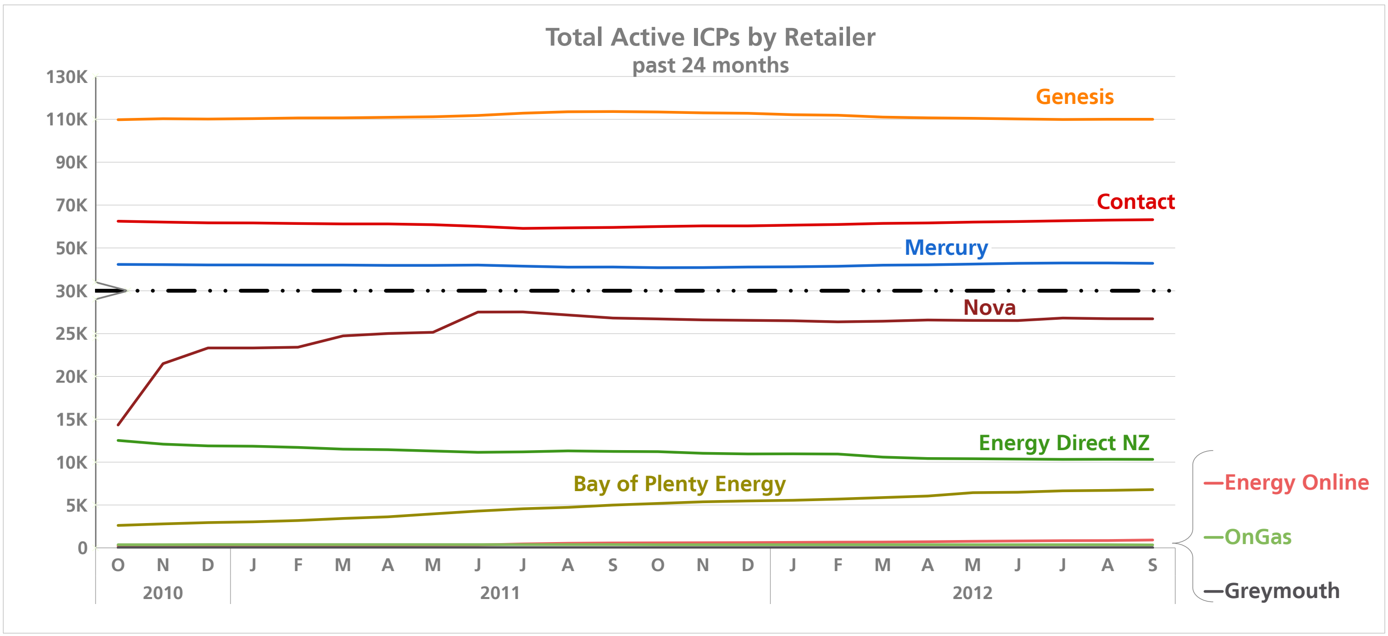
It has proven efficient for the Market Investigator to attempt to reach a settlement on batches of rule 37 breaches. In September, the Rulings Panel approved a settlement of a batch of rule 37 breaches relating to consumption months December 2009 to March 2011 (and alleged February 2011 to May 2012).



5 Market competition performance measures

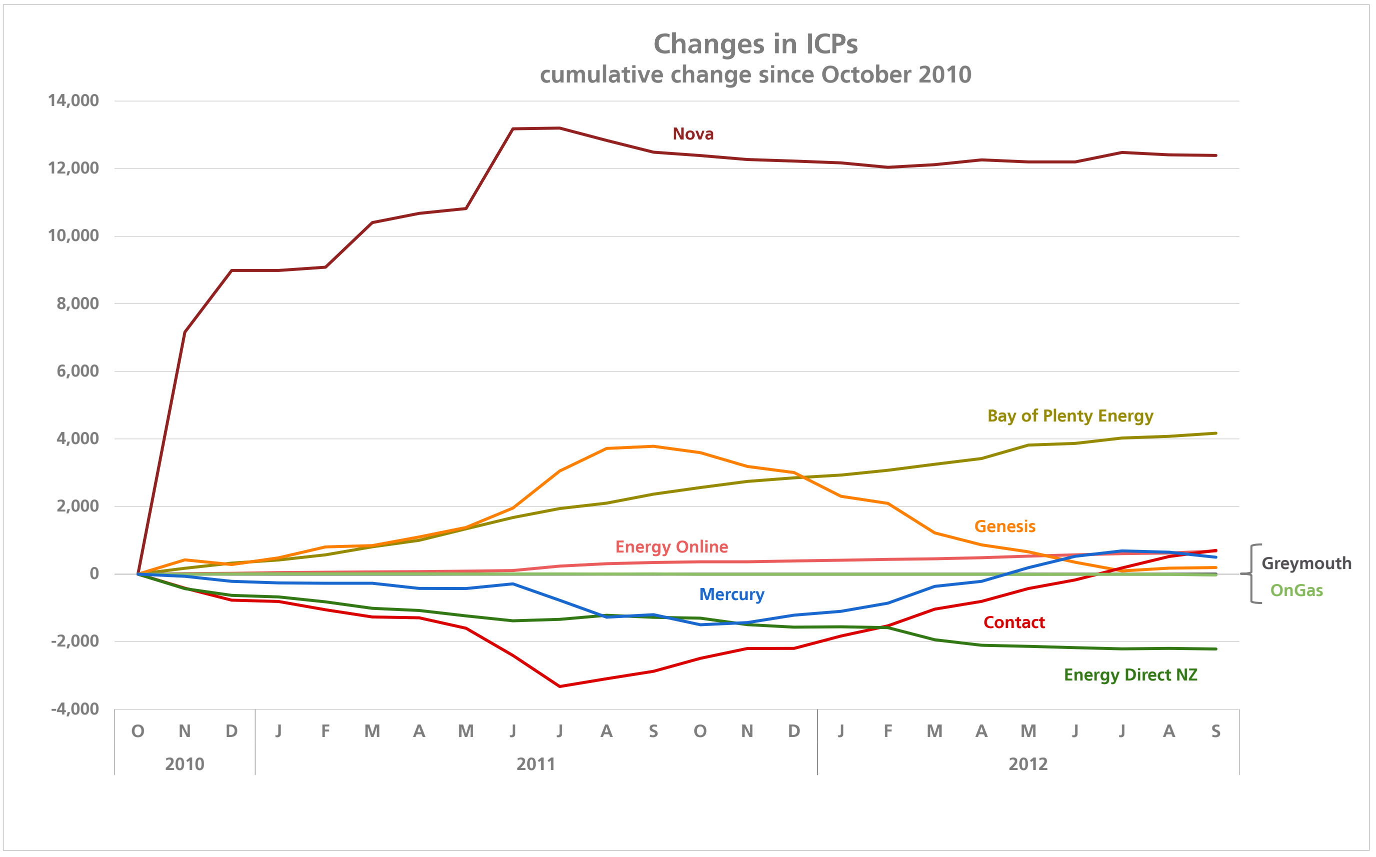
Market share of ICPs by retailer

Market share of ICPs has again been relatively constant for most retailers over the past year, as illustrated by the chart below. A notable exception is Bay of Plenty Energy, which has added more than 2,000 customers in the past 12 months – an increase of over 40%. The increase in Nova customers reflects the acquisition of E-Gas customers in October 2010 and the amalgamation of the Nova and Auckland Gas brands in November 2010 and June 2011.



The two charts below are drawn from the same data set. The first chart shows the change in numbers of ICPs, and the second chart shows the percentage change in ICPs, relative to October 2010.

Most retailers have gained ICPs over the past two years. Contact and Mercury have more than regained the customer losses experienced mid-last year. Genesis Energy's customer numbers reflect the opposite pattern, but its customer numbers are still greater now than two years ago. Bay of Plenty Energy continues to gain customers. Nova has lost some customers since the amalgamation of Auckland Gas and E-Gas, but still shows an increase of more than 12,000 customers in the past two years. The exception is Energy Direct, which has lost more than 2,000 customers in the same time period.



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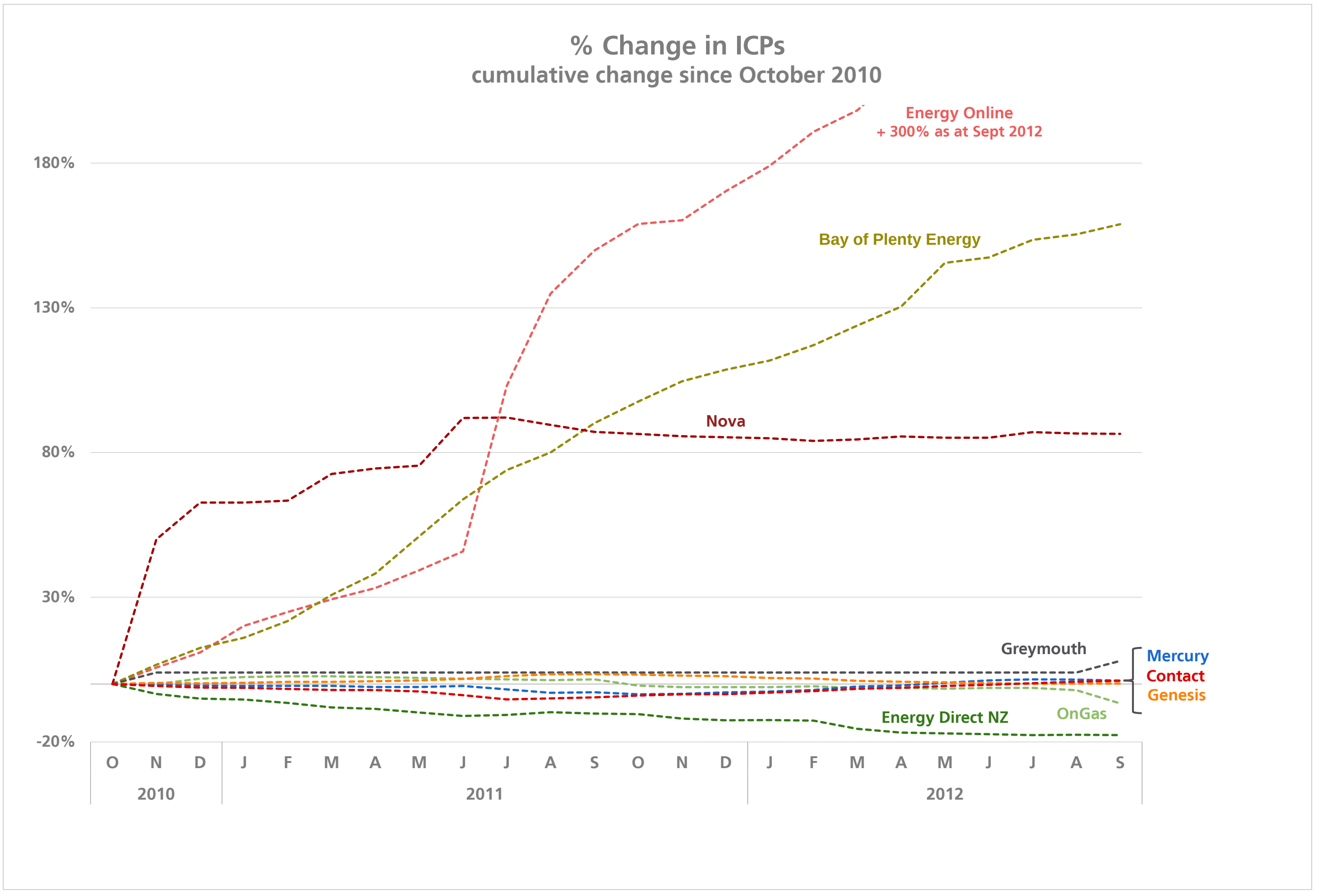
In percentage terms, Energy Online, a retail brand of Genesis Energy, has grown by 300% in the past two years, adding nearly 700 ICPs to its customer base. Bay of Plenty Energy has grown160% with the addition of over 4,100 ICPs.



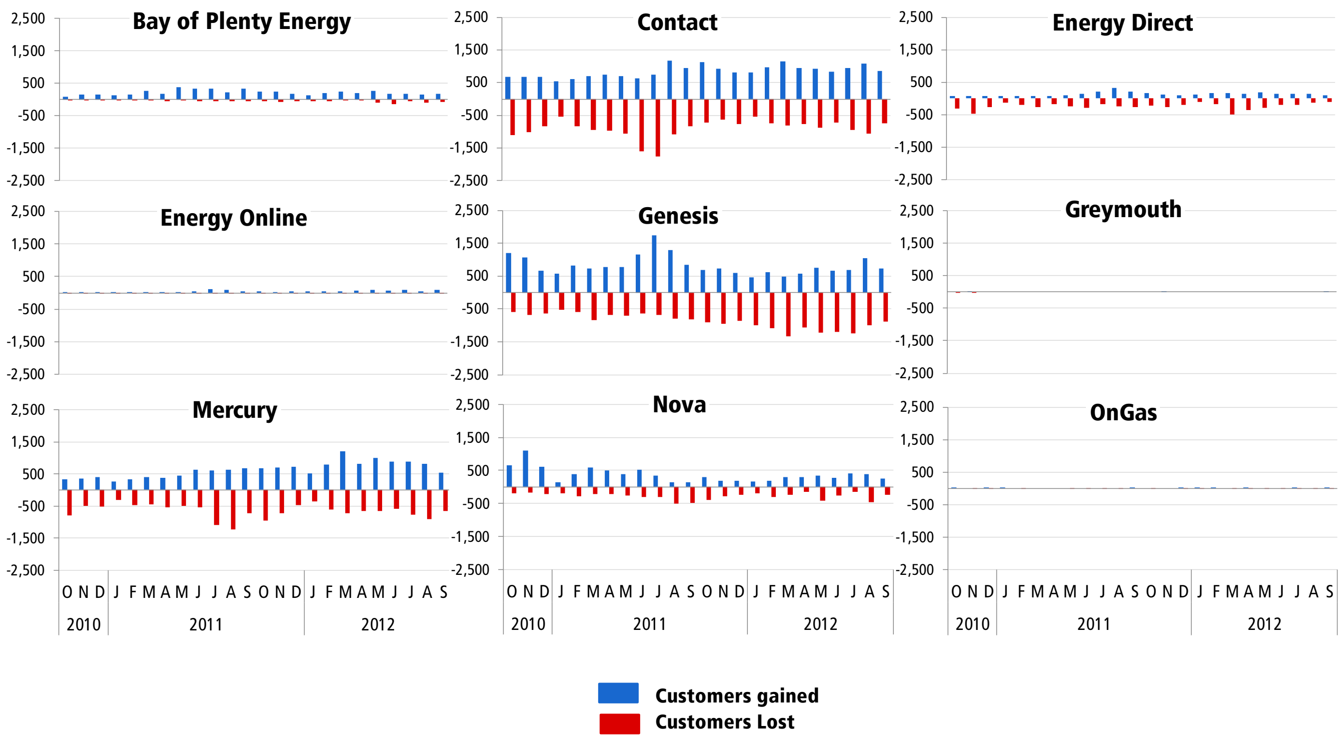
Note that all three of the ICP share charts above include data from ICPs on open-access distribution networks only; information about ICPs on bypass networks is not available in the Gas Registry.

Switching activity by retailer

This chart shows the numbers of ICPs gained and lost by retailers over the past two years. The blue bars show the number of customers gained by the retailer each month, and the red bars show the numbers of customers lost.

As shown by these charts, although the net changes in number of customer ICPs may not change significantly from month to month for some retailers, there is a lot of underlying switching activity, particularly for the mass market retailers Contact, Genesis, and Mercury. Note that these charts exclude the bulk transfer of 6,348 ICPs from E-Gas to Nova in November 2010; they also exclude the transfer from Auckland Gas to Nova of 1,478 ICPs in December 2010 and 2,243 ICPs in June 2011.

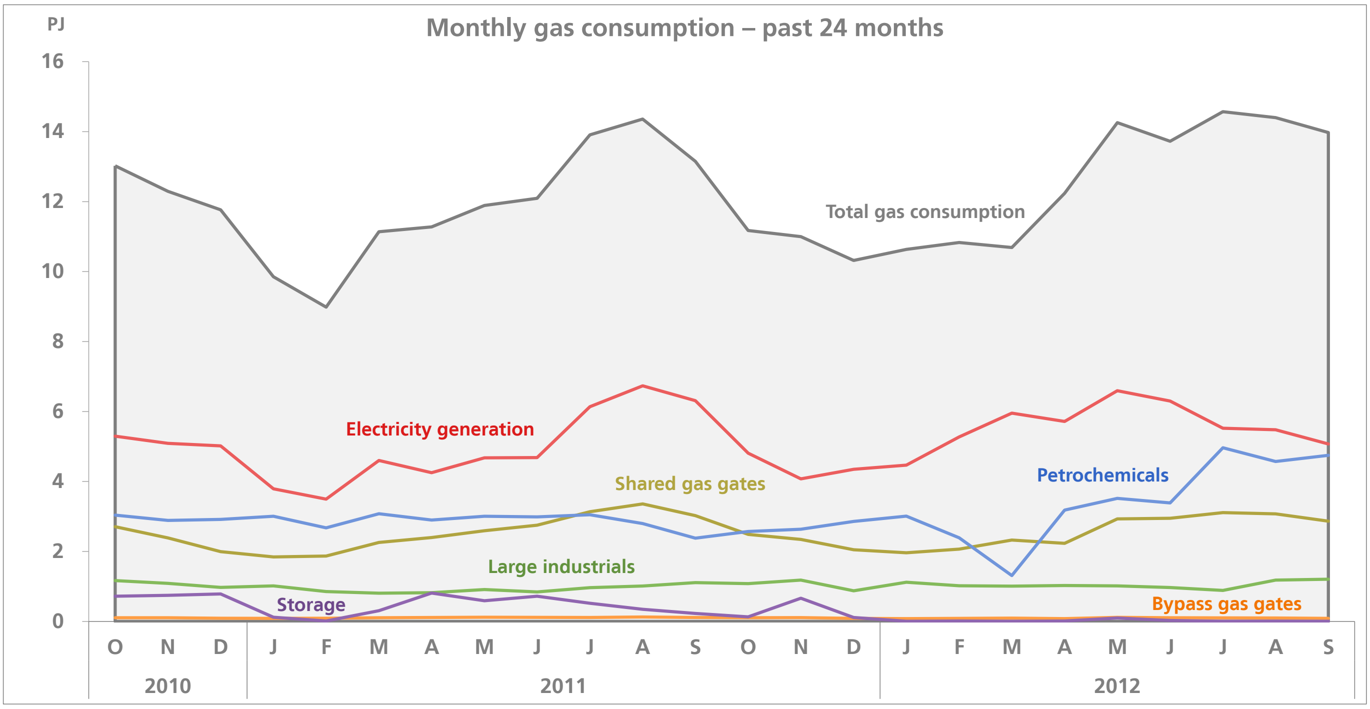
Switching activity by retailer



Total gas volumes

The chart below shows the total amount of gas consumed over the past two years by all gas users. The top grey line shows total consumption; the coloured lines provide a breakdown by type of use.

- The red line shows the seasonal peaks and troughs in gas used for thermal electricity generation.
- Consumption for petrochemicals, in blue, was relatively flat until March of this year. The dip in petrochemical gas consumption in March was caused by scheduled and unscheduled outages of the Pohokura production station during the month. Since July, consumption has increased under the widely reported gas sale agreement between Methanex and Todd Energy.
- The green line represents volumes of gas used by large industrials, including steel, wood products, dairy processing, and oil refining.
- The purple line shows the volumes of gas going to storage.
- The orange line represents gas used by consumers connected to the private pipelines owned by Nova.
- The tan line shows the amount of gas used by customers connected to shared gas gates. This represents the majority of commercial and residential customers. There is a seasonality trend to the consumption, higher in winter and lower in summer. These allocated gas volumes are broken down by retailer in the next section.



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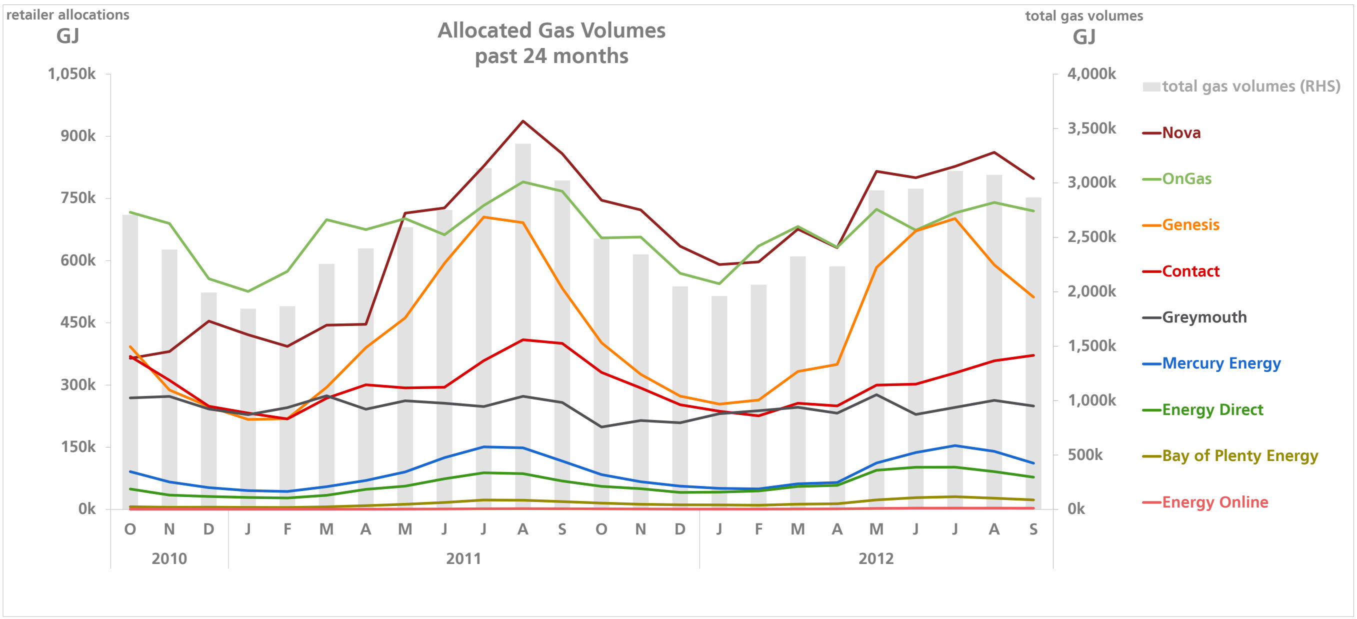
Allocated gas volumes

This chart shows the gas volumes allocated to retailers at shared gas gates over the past two years. This is gas consumed by industrial, commercial, and residential customers, but it excludes gas volumes from direct connect gas gates; that is, from gas gates that supply a single customer directly from the transmission system. For this reason, gas volumes supplied through direct connect gas gates to such industrial sites as thermal power stations, oil refinery, and paper and chemical factories are not included in the chart below.

In May last year, Nova Energy overtook OnGas in terms of the largest share of allocated gas. This increase reflects the increase in Nova's customer base, through its acquisition of E-Gas, amalgamation of Auckland Gas, and organic growth. Genesis, the third largest retailer by volume, has a load profile that peaks in winter and troughs during the summer. Contact, Mercury, and Energy Direct all show similar – but less pronounced – winter peaking patterns. Greymouth's share of allocated gas, in contrast, is relatively steady throughout the year, reflecting its position as largely a supplier to industrial loads.

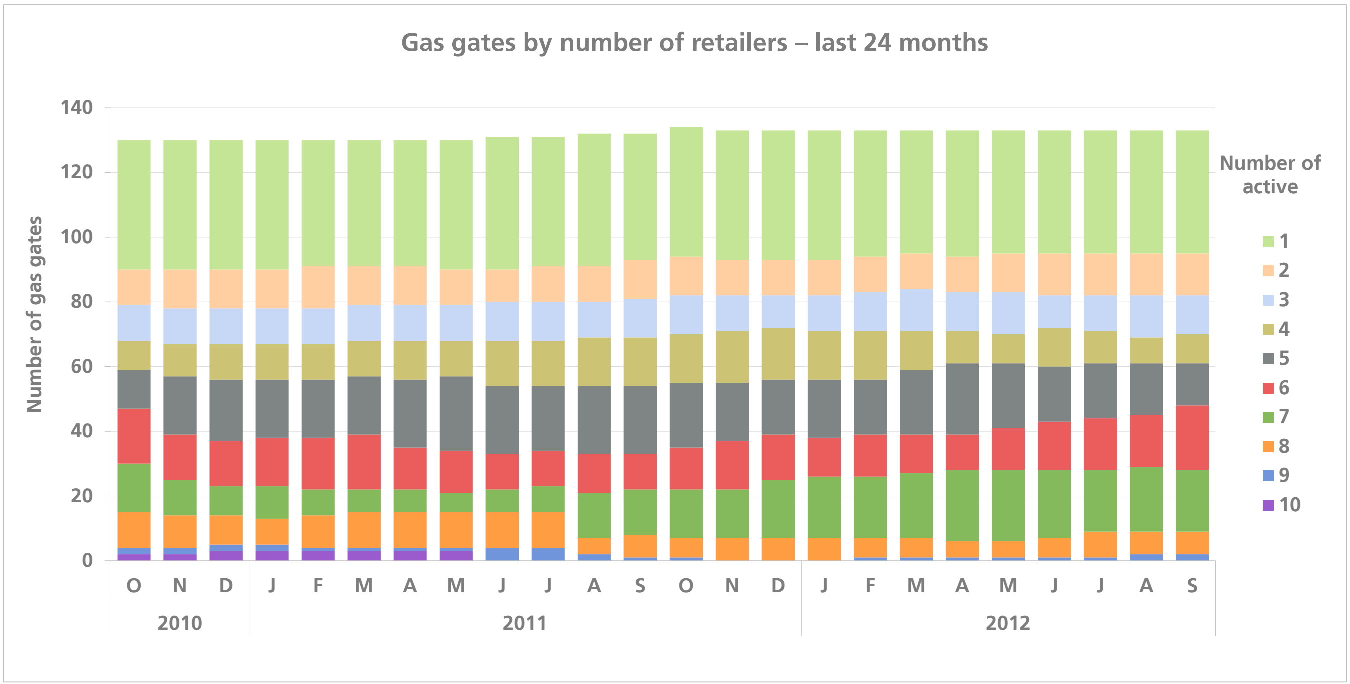


The data are from a mix of allocation stages: Final through September 2011; Interim for October 2011 through June 2012; and Initial for July through September 2012.

Gas gates by number of retailers

This chart shows, by month, numbers of gas gates by the number of active retailers. The greater the number of retailers that trade at a gas gate, the greater is the potential competition for customers.

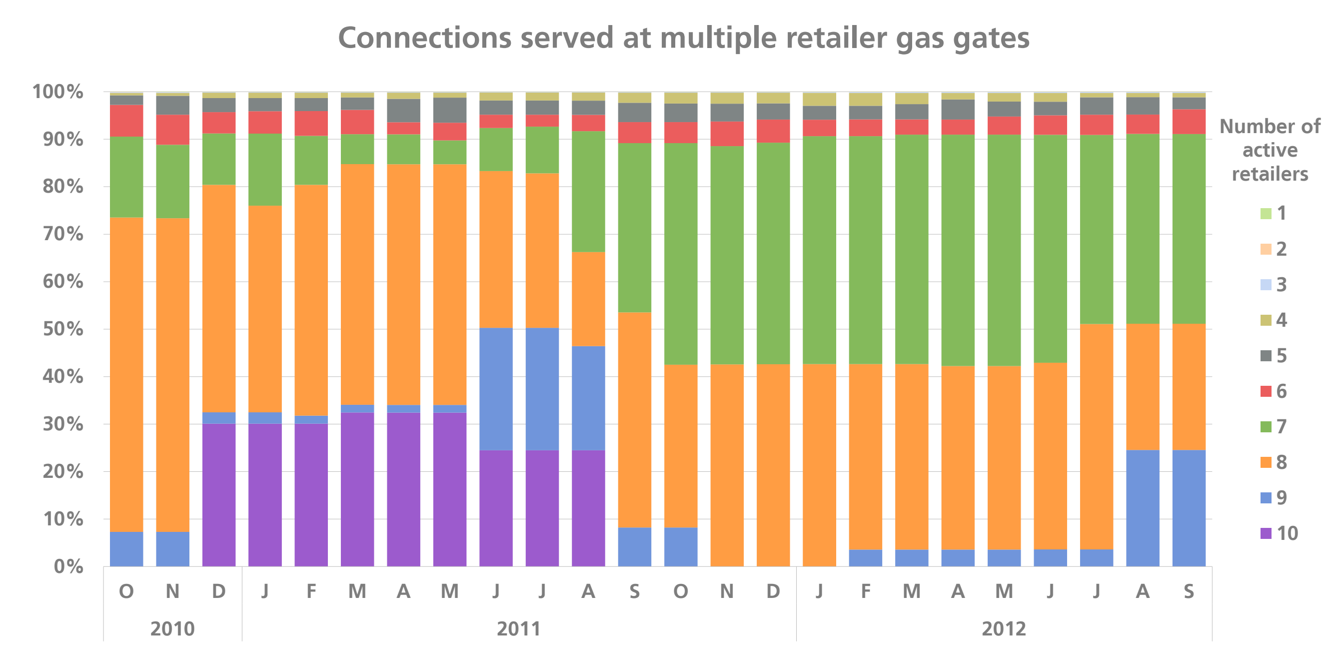
The chart shows that there has been a slight increase in retailers' activity at gas gates, following the amalgamation of Auckland Gas into the Nova Gas brand in 2011 and the exit from the market of E-Gas in 2010. The number of gas gates with six or more retailers (the red band and below in the chart) has steadily increased over the past year: in September 2011 there were 33 such gates; now there are 48.



Connections served by multiple retailers

This chart plots the proportion of gas customers who are served from the gas gates in the chart above; that is, customers served at gas gates where multiple retailers trade. As with the previous chart, the acquisition of E-Gas and the amalgamation of Auckland Gas have produced step changes in the data.

There are now two gas gates at which nine retailers trade, both in the Auckland region. Consistent with the trend over the past 18 months, the majority of gas customers are connected to a gate where least six retailers trade: over 96%, as of September 2012.



Note that the above chart includes data from ICPs on open-access distribution networks only; information about ICPs on bypass networks is not available in the Gas Registry.

6 Critical Contingency Management performance measures

There were no critical contingencies in the previous quarter.

Strategic Progress: Quarterly Report July-September 2012

This report provides an update of progress towards Gas Industry Co's strategic goals. These reflect the Government's objectives and outcomes for the gas industry, as set out in the Gas Act 1992 and the April 2008 Government Policy Statement on Gas Governance, as implemented through the Company's FY2012-2014 Strategic Plan.

Project	Rationale	Activity	Status
Strategic Goal: Efficient Use of, and timely investment in infrastructure			
Transmission Pipeline Balancing	• Improved industry arrangements. Gas industry participants and new entrants are able to access transmission pipelines under reasonable terms and conditions.	• Assess balancing market developments. • Provide advice to Minister on balancing market developments by February 2012.	• Advice to Minister on 2 March reports significant industry initiatives to improve balancing arrangements, including through a Maui Pipeline Operating Code (MPOC) change request relating to transmission balancing to take effect on 1 June 2013. Assisting industry to implement complementary balancing improvements also by 1 June 2013.
Interconnection	• Improved industry outcomes. Gas industry participants and new entrants are able to access transmission pipelines under reasonable terms and conditions.	• Monitor two new interconnection arrangements on each open access transmission pipeline (Vector, MDL). • Review transmission pipeline interconnections and consult on any issues by the end of 2013. • Investigate the extent, if any, of issues relating to access to private pipelines.	• Only one new pipeline connection (Sidewinder field) has occurred since Ministerial request. This has been reviewed and no issues have been identified.
Access to Processing Facilities	• Statutory Role under Gas (Processing Facilities Information Disclosure) Rules 2008.	• Collect, monitor, and publish disclosed information. • Recommend to Minister by 27 June 2013 as to continuance, amendment, or expiry of these Rules.	• All disclosures for current year received and published on Gas Industry Co website.

Project	Rationale	Activity	Status
Strategic Goal: Build efficient, competitive, and confident gas markets			
Rule Changes	• Improved industry governance through regular review of existing arrangements and recommending changes where appropriate.	• Maintain rule change registers. • Review industry feedback on options paper on Reconciliation Rules review. • Consult on Statement(s) of Proposal for changes to Reconciliation Rules. • Review effectiveness of the Gas Governance (Critical Contingency Management) Regulations 2008 following any events/exercises. • Consult on proposed changes to the Compliance Regulations.	• Advisory Group has continued to assist with the development of a recommendation for amendments to the Reconciliation Rules • Preparation of Statement of Proposal for amendments to the CCM Regulations well advanced. Will be issued in November. • Publication of revised Essential Services and Minimal Load Guidelines expected shortly. • Statement of Proposal issued 31 May 2012 on proposed changes to the Compliance Regulations and submissions received. A further consultation paper is being prepared detailing the proposed structure of the threshold regime contained in the amendments.
Gas Quality	• Maintain an acceptable standard of gas quality. • Ensure costs of gas quality incident are met efficiently. • Achieve improved transparency on gas quality incidents.	• Ongoing review of industry arrangements for managing gas quality. • Consider options for improving gas quality arrangements. • Report review findings to Minister by June 2012.	• Survey of gas quality monitoring completed. • Retailers establishing information exchange protocol to demonstrate compliance with gas quality requirements.
Insolvent Retailer Arrangements	• Following recommendation to revoke 2010 temporary Insolvent Retailer Regulations, consider whether generic regulatory solution is required to address retailer insolvency.	• Prepare Issues and options paper for industry consultation.	• Proceed to consider options to address possible market failure – paper to be released by year-end.

Project	Rationale	Activity	Status
Gas Distribution Principles	• Improved industry outcomes. Gas industry participants and new entrants are able to access distribution pipelines on reasonable terms and conditions. • Ensure consistency in distribution services arrangements.	• Monitor and report annually to Minister on status of distribution arrangements. • Develop and publish distribution contract Principles. • Encourage publication of network services agreements.	• Minister has endorsed the Oversight Scheme and preparations underway for first assessment in February 2013.
Transmission Change Requests	• Contractual role pursuant to MoUs with MDL and Vector. • Ensure ongoing relevance and efficiency of multilateral terms of access to transmission pipelines.	• Process MPOC change requests and VTC change request appeals in accordance with respective Memorandum of Understanding (MoU).	• Change requests and appeals processed as received. • VTC change request appeal (dated 31 July 2012) draft recommendation in support of the appeal. Submissions received and analysed, final recommendation to be released shortly.
Compliance	• Statutory role under the Compliance Regulations. • Improved industry operations through provision of a compliance and dispute resolution process for industry participants.	• Oversight of Gas Governance (Compliance) Regulations 2008.	• Gas Industry Co continues to fulfil its role as Market Administrator under the Compliance Regulations. • [45] breach notices received from the CCO relating to apparent non-compliance with retailer curtailment directions in October 2011 Maui outage. Notices will be sent to parties allegedly in breach.
Customer Issues	• Enhanced consumer benefits through complaints process for small gas customers.	• Liaise with the Electricity & Gas Complaints Commission (the approved complaints scheme), and other relevant regulators to remain aware of consumer complaint issues.	• Regular liaison with Electricity & Gas Complaints Commission, and bi-monthly meetings with Electricity & Gas Complaints Commission and other relevant regulators. Gas-related inquiries and complaints statistics included in Gas Industry Co 2011 Annual Report.

Project	Rationale	Activity	Status
Retail Contracts	• Enhanced consumer outcomes by providing clarity around the respective roles and obligations of consumers and industry participants involved in the supply of gas to small users.	• Administer the Retail Gas Contracts Oversight Scheme. • Annual assessment of alignment of retail contracts with contract Benchmarks. • Report to Minister on the results of the 2012 assessment.	• Transitional assessment of retailers' progress towards alignment with the Benchmarks completed and report provided to Minister. • Third assessment commenced in July 2012. Results to be published November 2012.
Transmission Pipeline Capacity	• Improved consumer outcomes by addressing short and long-term competition issues arising from the North Pipeline capacity constraint. • Enhanced industry/consumer outcomes by improved level, and quality, of information on which to base business/energy use decisions.	• Address by regulatory and/or non-regulatory options any lessening of competition due to transmission constraints. • Implement the Gas Transmission Investment Programme (GTIP). • Improve the quality and availability of pipeline security standards and supply/demand information. • Promote changes to commercial and regulatory arrangements so the GTIP objectives can be met.	• Continued monitoring of information provided by signatories to the "Bridge Commitments", designed to address short-term issues. • Gas Transmission Exchange (GTX) - one of the 7 Bridge Commitments - live and capacity offers have been posted and accepted. • New work programme, Gas Transmission Investment Programme (GTIP), initiated to address long-term solutions to capacity issues on North Pipeline. • Panel of Expert Advisers issues first advice report to Gas Industry Co (July 2012). Report issued for industry comment. • PEA considering submissions and determining next steps and revised work programme.

Project	Rationale	Activity	Status
Strategic Goal: Deliver effectively on accountabilities			
Downstream Reconciliation	• Statutory role under Reconciliation Rules. • Improved industry arrangements and consumer outcomes through the objective of fairly allocating, and reducing, unaccounted-for-gas (UFG) and its associated costs.	• Oversight of Gas (Downstream Reconciliation) Rules 2008.	• Gas reconciliations being performed each month • Long-term UFG has flattened out at ~1%.
Switching and Registry	• Statutory Role under Switching Rules 2008. • Efficient retail market and improved consumer outcomes by facilitating market contestability through customer switching between retailers.	• Oversight of Gas (Switching Arrangements) Rules 2008.	• Customer switching at steady-state level of ~3200 switches per month.
Performance Measures	• Improved industry and consumer outcomes through the provision of public information on industry performance. • Monitor the effectiveness of governance arrangements.	• Determine and publish information on each gas governance arrangement that has been implemented.	• Performance measures computed and reported quarterly.

Policy Development and Information Gathering	• Ensure Gas Industry Co has all information required to properly analyse issues in arriving at conclusions. • Industry and consumer benefits from improved level, and quality, of information on which to make business and/or energy use decisions.	• Proposal initiated following the publication in June 2011 of the FY2012-2014 Strategic Plan - to develop a process enabling Gas Industry Co to request and, if necessary, require the supply of specific information from participants to assist the timely development of market solutions.	• Statement of Proposal issued for industry comment December 2011. Submissions due by 17 February. • Following submissions analysis, developing information requests protocol and continuing to develop regulatory framework.
Industry Facilitation	• Facilitate nexus between industry and Government. • Maintain informed industry participants and other stakeholders.	• Facilitate, influence and communicate with the industry and Government. • Liaise with other regulatory bodies, agencies and associations with responsibilities and interests encompassing the gas industry.	• CEO presentations to industry conferences (Downstream, 'Wind Energy, LPG).
Critical Contingency Management	• Statutory role under Gas Governance (Critical Contingency Management) Regulations 2008. • Improved industry outcomes through increased market confidence in industry's ability to manage critical events.	• Manage Critical Contingency Operator (CCO) via service provider agreement. • Review effectiveness of the Regulations following any events/exercises. • Operate critical contingency pool following an event.	• Annual exercises held. • CCO activities monitored and reviewed quarterly. • Reviewed CCO Incident and Performance Reports on the Maui Pipeline outage on 25-30 October 2011 • Reviewed CCO Incident and Performance reports on critical contingency event arising from a Pohokura production station outage on 3 March 2012.