

Government's Review of the Gas Industry

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Overview of Presentation

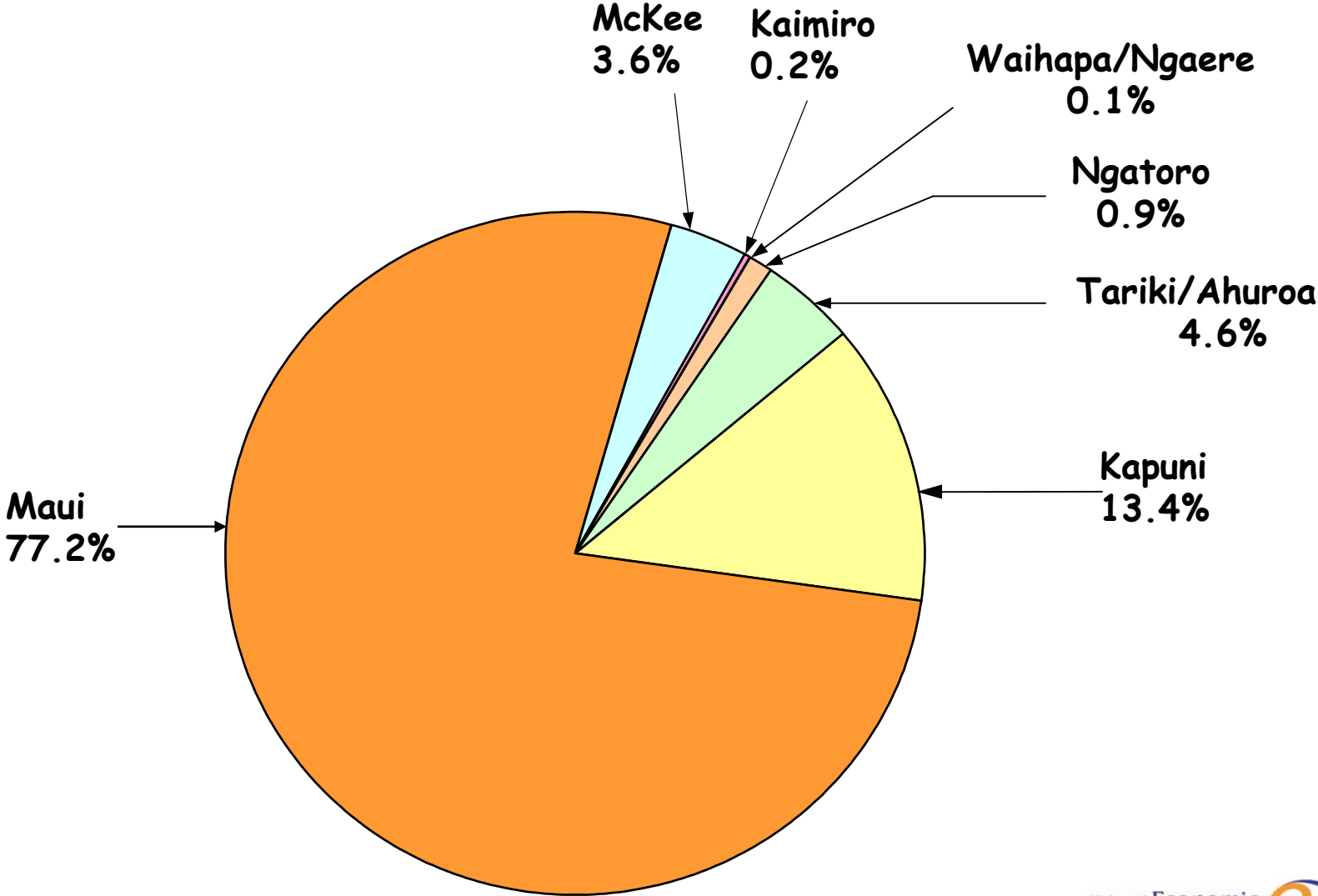
- Significance of the gas sector
- Why review the gas sector?
- Review process to date
- ACIL's efficiency criteria
- Key issues in ACIL report
 - ◆ Transition to post-Maui environment
 - ◆ Efficiency in distribution and retailing
 - ◆ Possible way forward
- Current processes

Importance of the Gas Sector

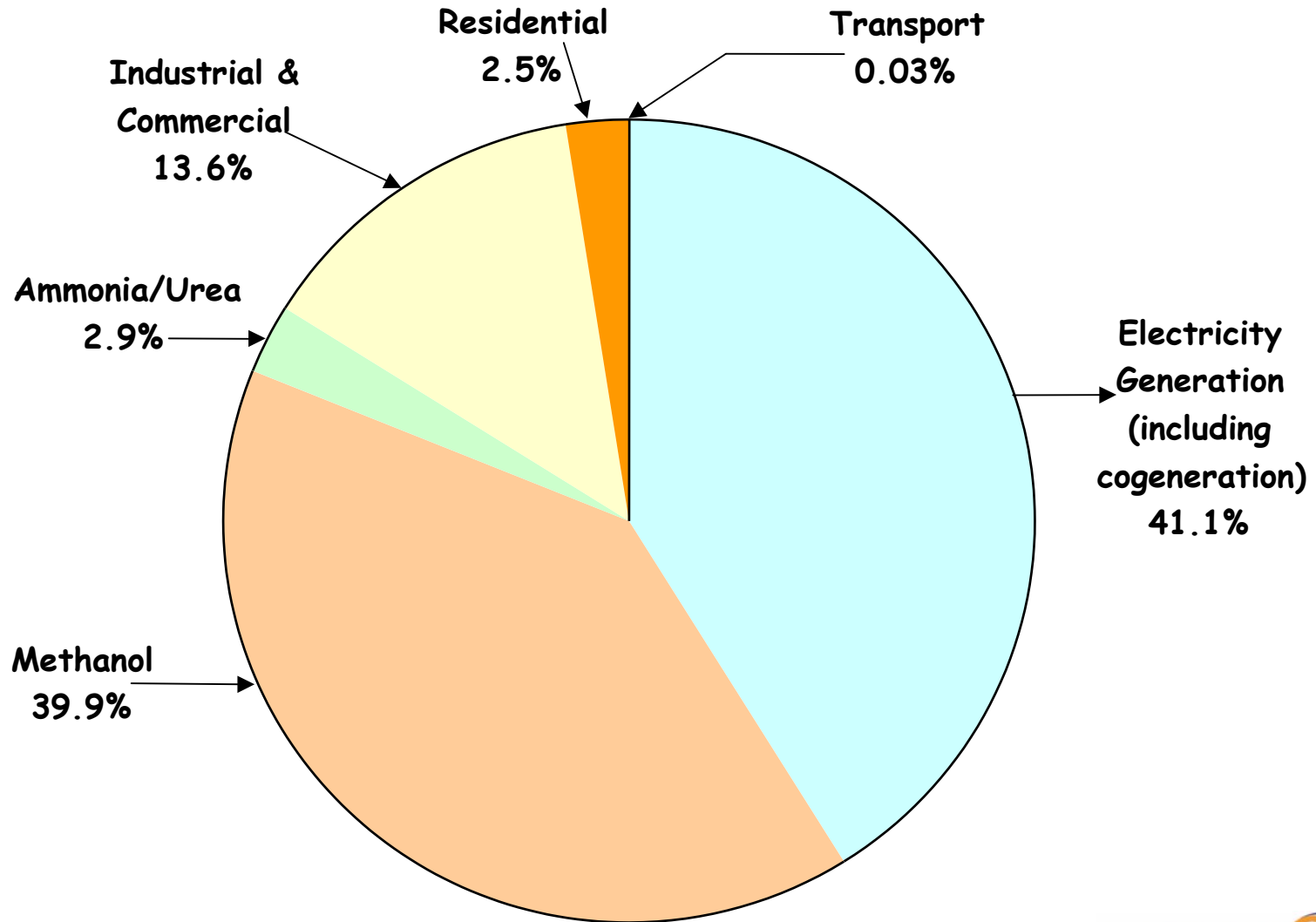
- 30% of New Zealand's primary energy
- High quality, high value fuel for:
 - Gas fired generation (30% of electricity capacity)
 - Petrochemical use (Methanol exports - \$500 - 600m pa)
 - Industry - process & space heating
 - Domestic fuel - space heating & cooking

Sources of Gas - 2001

255 PJ



Uses of Gas - 2001 230 PJ



Why review the Gas Sector?

- Government's overall energy policy objective:
 - "to ensure that energy is delivered in an efficient, fair, reliable and sustainable manner to existing and potential users"*
- Government has reviewed the electricity industry and is implementing reforms
 - ◆ Ministerial Inquiry - David Caygill reported June 2000
 - ◆ Self-governance, backed by regulation power
 - ◆ Commerce Commission oversight of natural monopoly lines
- Attention now turning to gas

Process for the Gas Review

- Announced 15 March 2001
 - ◆ Comprehensive amendments to Information Disclosure Regulations put on hold
- Competitive tender for consultants to prepare a detailed public discussion paper
 - ◆ ACIL commissioned late April
 - ◆ Consultants approached industry participants
- Discussion paper released November 2001
 - ◆ Submissions due 31 January. 17 received. Posted on MED's web-site
 - ◆ 5 cross-submissions received 22 February, also posted
- Officials' analysis
 - ◆ Submission summary available on MED's website
 - ◆ Advice to Cabinet

Characteristics of an Efficient Gas Sector

ACIL: An efficient New Zealand gas sector would have the following characteristics:

- Full competition in production, wholesaling and retailing
- Interconnected transmission and distribution system with clear rules for access
- Where natural monopoly exists, information disclosure and legal remedies to apply
- Absence of cross-subsidisation in vertically integrated companies
- Market signals encourage efficient allocation of resources along the gas supply chain
- Freedom of choice by all consumers
- Clearly defined safety and reliability requirements
- Environmental costs incorporated into prices

Transition to Post-Maui Environment

- Is competition between producers robust?
 - ◆ ACIL: Not a source of inefficiency
 - ◆ Producers: Agree
 - ◆ Downstream parties: Concern re ownership concentration (NGC, Contact, Genesis)

- Should Maui, as well as NGC pipelines, be "open access"?
 - ◆ ACIL: Need open access across Maui and NGCT - this requires renegotiation of Maui contracts
 - ◆ Wide agreement
 - producers: promote new field access (eg Shell, Preussag, MDL, NZOG)
 - downstream participants: caveat - need to protect existing rights under Maui contracts (eg Contact)
 - ◆ Crown has dual role (ownership and gas market efficiency)
 - Crown has rights and obligations

- Should transmission be a separate corporate entity?
 - ◆ ACIL: Government could explore with NGC the possibility of corporate separation
 - ◆ NGCT should be separate (Powerco, Todds, MEUG)
 - ◆ Further consideration required (NGC)
 - ◆ Similar consideration required re separation of Maui pipeline (NGC)

- Does transmission pricing need revision?
 - ◆ ACIL: transmission pricing meets efficiency tests given limited injection points, but may need updating
 - ◆ Agree (Contact, Todds and others)
 - ◆ NGC considers arrangements are evolving satisfactorily

- Do wholesale market arrangements need improvement?
 - ◆ ACIL: present arrangements are workable in market dominated by Maui, but improvements now required
 - ◆ Broad agreement (Shell, NGC, Contact, United, Todds and others)

Efficiency in Distribution and Retailing

- How much regulation is needed?
 - ◆ ACIL: light regulation only required at this stage; review after 3 -4 years
 - ◆ Distribution efficiency is a concern (Contact, MEUG, Simon Terry Associates)
 - ◆ Favour information disclosure (Powerco, Contact, GANZ)
 - ◆ Profits need to encourage investment, consistent energy-wide approach required (Powerco, United)

- Should pipelines be “ring-fenced” (corporate separation)?
 - ◆ ACIL: Government should encourage ring-fencing to promote retail competition
 - ◆ Agree: Contact, Genesis

- Do multi-utilities introduce efficiency risks?
 - ◆ ACIL: Trend to multi-utilities should not be impeded, but tighter accounting rules required
 - ◆ Multi-utilities are efficient (Powerco, WEL)
 - ◆ Multi-utilities protect electricity, gas not marketed effectively (Genesis, United, Gas Appliance Retailers)
 - ◆ Vertically integrated gas companies do not compete effectively in electricity (WEL)
 - ◆ Entry of energy retailers impeded by difficulty in sourcing electricity (United)
 - ◆ Agree need tight accounting rules (Genesis)

- How should pipeline assets be valued?
 - ◆ ACIL: Values between historic cost and ODV are OK, monitoring and independent review of ODVs suggested
 - ◆ ODV regulation required (MEUG, Powerco, NGC, Contact, Genesis, Wanganui, WEL)
 - ◆ ODVs have led to excessive profits (Simon Terry Associates, Todds)
 - ◆ Values too high. Bypass may remedy this, but too risky (Todds)

- Should retail churn statistics be disclosed?
 - ◆ ACIL: Disclosure would highlight areas where competition impeded
 - ◆ Agree (MEUG, NGC, Genesis)
 - ◆ Not helpful (Contact)
 - ◆ Improved switching protocols required (Genesis, Contact, Powerco)

Possible Way Forward

- Is self-regulation viable?
 - ◆ ACIL: Government should encourage “voluntary decision making body” and establish clear objectives
 - ◆ Support self-regulation (Powerco, NGC)
 - ◆ GANZ initiatives noted (NGC, Contact)
 - ◆ Support issue of Government policy statement (Contact, Genesis, MEUG: “with consumer involvement”)

Current Processes

- Officials' advice to Government
- Government decisions/announcements to come
- Gas industry has:
 - ◆ demonstrated an ability to develop codes and protocols on pipeline access and reconciliation
 - ◆ actively reviewed how best to advance ACIL's objectives