
Natural Gas Control Inquiry



Conference on the Draft Report, 22 to 28 July 2004

Assessment of benefits of control too narrow

- **Inquiry is into control of gas pipeline services not control of delivered gas**
 - Commission's focus on delivered gas blurs issues and obscures cross subsidisation issues
- **Commission's determination of benefits limited to examination of pricing behaviour**
 - does not consider service quality
- **Commission assumes that open access is available with or without control and that control will not impact on quality of open access**
- **Commission should also consider:**
 - terms of open access including price of services
 - whether pipeline owner required to offer open access
 - requirement to unbundle services
- **The full benefits of control cannot be determined without that wider consideration**
- **Inclusion of foreign ownership is simplistic and will discourage foreign investment**

Service “quality” depends on terms of access

	<u>Common Carriage</u>	<u>Contract Carriage</u>
Tradable rights	none	yes
Investment climate	unfavourable	favourable
Access certainty	none	yes - contractual right
Consistency with local practice	inconsistent	consistent
Consistency with overseas practice	inconsistent	consistent
Economic efficiency	poor	improved allocative and dynamic efficiency
Dominance of vertical integration	increased	Firm contractual rights limit opportunity

Economic efficiency also depends on access terms

	<u>Characteristic</u>	<u>Common Carriage</u>	<u>Contract Carriage</u>
Allocative	Reflects customer preferences?	No	Yes
	Capacity rationing	Volume	Price
	Capacity goes to highest value use?	No	Yes
Dynamic	Upstream and downstream investments and market entry facilitated by secure access?	No	Yes

- Dynamic efficiency a real concern:
 - Pipeline could become constrained within 5 to 10 years
 - But decisions on long-lived assets (new power stations, LNG terminal, upstream production facilities) required within next 2 years
 - Resulting uncertainty regarding pipeline access will adversely affect investment decisions

Other terms of access impact on benefit of control

- **Balancing arrangements, particularly availability of balancing gas and price of balancing gas**
- **Cost of penalties for exceeding rights**
- **Management of gas flows and access to information on gas flows**
- **Management of gas quality**
- **Access to developable capacity**
- **Access to new receipt and delivery points**
- **Credit worthiness of other users**
- **Rights to compensation**
- **Method for resolving disputes**

Open access should be available on all pipelines

- Commission's presumption that there will be open access on all pipelines, is not necessarily true
- Bypass pipelines have different cost structures and provide different services, open access to those services can increase competition and efficiency
- Most overseas gas markets now offer regulated open access on all pipelines, including bypass

Evidence of bypass justifies control

- Both constructed bypass pipelines and revised terms of access implemented from threat of bypass justify control
- Opportunities for bypass reveals evidence of excessive charging by pipeline owners
- The Commerce Commission has not included the costs associated with development of bypass proposals in the benefit of control

Service unbundling provides benefits

- **Unbundling services increases transparency and effective competition:**
 - **Pipeline**
 - transport
 - access to linepack
 - metering
 - reconciliation
 - gas flow information
 - **Energy supply**
- **Unbundling pipeline services enables competition services and more efficient outcomes**
- **Most open access regimes require legal separation of energy supply and pipeline services**
- **An integrated supplier of gas and pipeline services has information advantages and can cross subsidise supply of gas**

Summary

- Control should only be a last resort if competition ineffective and evidence of excess profits or poor service quality
- Contact supports control on the basis that the Commission concludes that control will deliver benefits
- Commission may have understated benefits of control because it has not considered matters such as service quality and service unbundling
- Control should cover all gas pipelines
- Control should be consistent across assets – i.e. electricity and gas
- Control should cover pricing but extend to requirement to provide open access, quality of that access, and unbundling of services