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Objective

Gas Industry Co has convened a workshop of industry practitioners to discuss issues related to investment in, and access to, gas infrastructure. The objective of the workshop is to identify and develop some initial strategic industry positions on these issues. In particular, to consider whether, how and when investment in additional North Pipeline capacity should occur, and what associated commercial access arrangements should be. The outcomes of the workshop may then be discussed at a later meeting of industry CEOs or senior managers to develop some consensus on an industry strategy and work programme. In this context, it would be very helpful if those attending this workshop could be acquainted with their companies' views on these issues and authorised to discuss them.

Background

A key element of Gas Industry Co's work in recent years has been about industry arrangements for access to gas transmission infrastructure. In May last year, we published a consultation paper, Options for Vector Transmission Capacity (the Options Paper), in which we analysed and presented some options for changing the Vector access arrangements. The aim of the options paper was to present and evaluate alternative ways in which Vector may develop its access arrangements. We paid particular attention to the difficulties arising from the North Pipeline capacity constraint, and the significant links between the capacity regime and the price-quality and investment aspects of the regulations being developed by the Commerce Commission.

A common theme in submissions on the Options Paper was that the issues for the industry were much bigger than those described by Gas Industry Co. In particular, the constraint on the North Pipeline raises questions about assessment of current and future gas demand and about requirements for future investment. Ultimately, these issues are about the future role of gas in Auckland and in New Zealand as a whole.

Gas Industry Co shares the industry's concerns that these bigger picture issues need to be tackled, and agrees transmission constraints should naturally trigger discussion about new investment. We suggest

the industry would benefit from more discussion about how to assess the need for new investment and how to implement any new investment in timely fashion. We think the gas industry would benefit if investors were able to access more of the data that informs investments decisions. Related industries such as electricity transmission publish such information in 'statements of opportunities'.

Issues about capacity investment also require the industry to consider:

- Government policy on upstream investment and infrastructure investment.
- Economic and other regulation and in particular the role and effect of the Commerce Commission's price-quality regime work on gas transmission and distribution.
- Investment models.

The industry was founded on government investment but now relies mainly on private sector investment. We need to examine whether current market conditions, including policy and regulatory settings, will lead to timely investment. If not, other investment models may need to be considered.

The scope of the investment issue means the whole industry must work together to resolve it. Currently, each relevant industry body (including Gas Industry Co) has been dealing with that part of the problem that falls under its jurisdiction. No single body has been charged with looking at the 'big picture' to determine what arrangements would facilitate investment. However, Gas Industry Co has a general responsibility under the Gas Act to promote an effective and efficient gas industry. We believe that this responsibility places an onus on us to help the industry put the investment issue in context and, if impediments to investment are identified, consider options for overcoming such problems.

Questions for discussion

The workshop will attempt to answer the following questions, which are explained in more detail below.

1. Do we need investment in new transmission capacity? Where and when?
2. Do we need additional information or tools to identify opportunities for efficient and timely investment?
3. What commercial incentives are needed to ensure that efficient investment is actually undertaken?
4. If capacity remains scarce, even under a reformed investment regime, what changes are needed to promote effective and on-going retail competition?

Do we need investment?

We will discuss investment need from practical and theoretical perspectives.

Practically, we will try to understand what “space” we are in. Is investment definitely required? Or definitely not required? Or are we in a grey area where more information and analysis is required?

Theoretically, investment is required if some users would be prepared to pay (directly or indirectly) the efficient cost of investment to obtain additional capacity. But the expression of this willingness to pay, and who ends up paying, depends upon the access regime: specifically, whether it is a form of contract carriage or common carriage.

Under contract carriage, for investment to proceed there must be a ‘queue’ of users wanting new capacity and willing to pay for the cost.

Under common carriage, since there is no barrier to entry of new users even when capacity is scarce, a need for investment is signalled by supply reliability falling below the level that users require. All users share the investment cost - and the benefit of improved reliability.

Do we need additional information or tools?

We will look at the tools and methods used for investment planning in similar markets (for example, electricity transmission in New Zealand and gas transmission in Australia) and discuss whether they are relevant and appropriate for the New Zealand gas transmission market. Tools include comprehensive analysis of supply-demand scenarios (the ‘statement of opportunities’), and investment ‘tests’ to verify that a proposed expansion project is needed. Issues in developing similar tools for New Zealand gas will be discussed.

What commercial incentives are needed?

We will discuss how the design of economic regulation and access arrangements affects the incentives on a company to invest in pipeline capacity. Incentives can be in the form of the ‘carrot’ of a profitable return on investment or the ‘stick’ of regulatory penalties. We will discuss how the details of the new economic regulation might affect investment behaviour and how to design it to ensure that efficient investment – and only efficient investment - occurs. For that to occur, economic regulation must somehow distinguish between “good” and “bad” investment, to ensure that only the former gets rewarded.

We will also consider the scenario of a company other than Vector investing and the implications for regulation, access and competition.

What if capacity remains scarce?

If, even under a reformed investment regime, capacity remains scarce, the competition issue must still be addressed. There are two options.

Firstly, change the access arrangements to promote competition. Possible ways of doing this were presented by Gas Industry Co at workshops and in reports last year and will also be discussed in the morning retail competition workshop.

Secondly, adapt the investment regime to promote “over-investment” that supports competition by ensuring there is always some spare capacity.

This discussion can then bring together the investment and access aspects of the competition issue and discuss how effective and on-going competition is best promoted.