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Wholesale Gas Market Design

1 December 2005

Framework

- Gas Act
- Government Policy Statement
- Size and scope of NZ Gas Market

Conceptual Design

- Issues and progress

Where to from here?

- Gas Industry Co processes
- Timeframe

Gas Act Requirements

S. 43F(2)(a) allows for [rules/regs] to be made...

- *“providing for the establishment and operation of wholesale markets for gas”*

S.43J(1)(b): Minister may only recommend [rules/regs] if the recommendation...

- *“implements the effect of a recommendation of the [Gas Industry Co]; and*
- *Does not differ ... in any material way...”*

GPS Objectives and Outcomes

Overall policy objective:

- *“To ensure that gas is delivered to existing and new customers in a safe, **efficient, fair**, reliable, and environmentally sustainable manner.”*

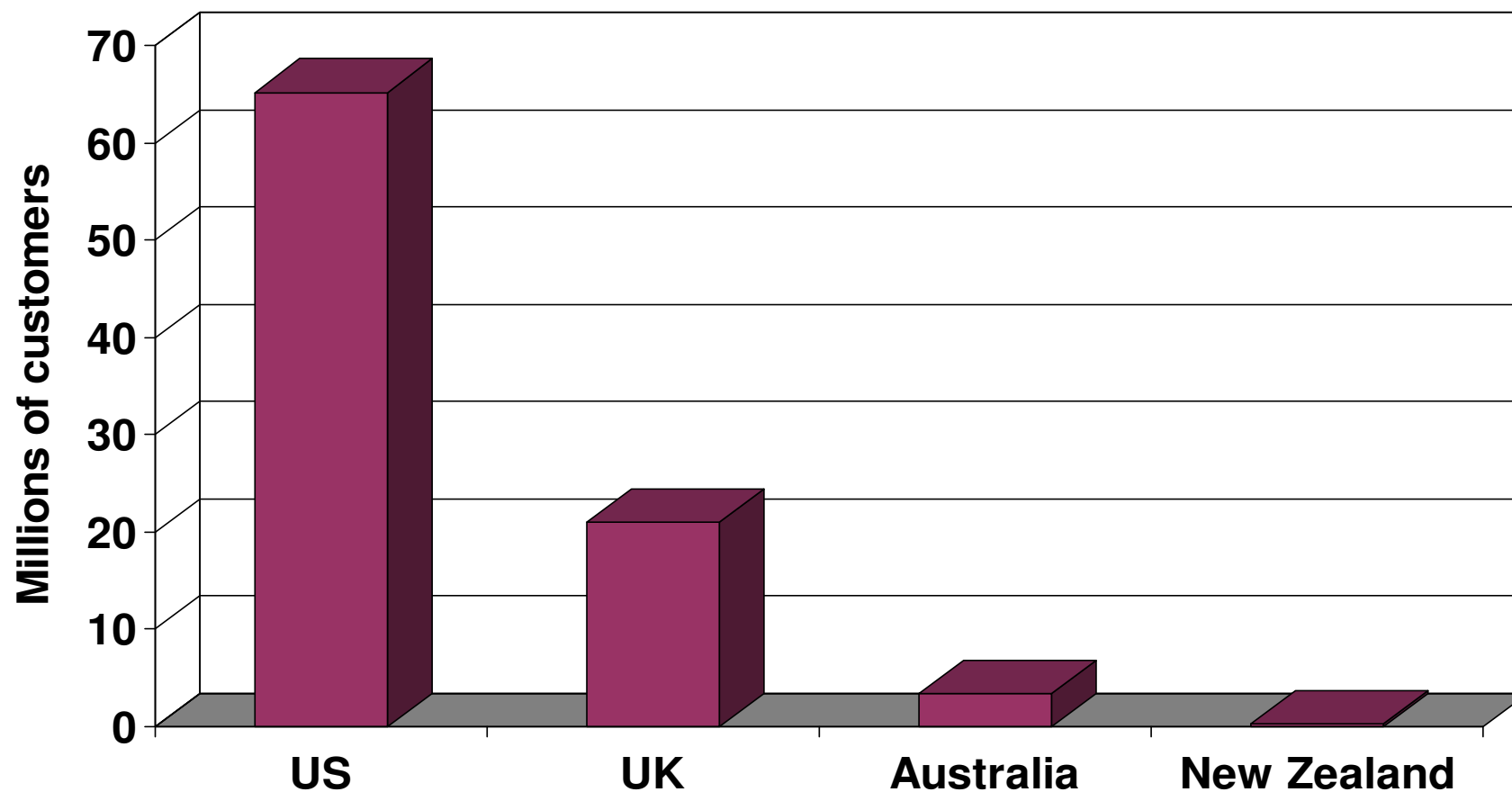
Specific outcomes sought:

- *“The facilitation and promotion of the ongoing supply of gas ... by providing ... **competitive market arrangements**”*
- *“Energy and other **resources are used efficiently**”*

Specific outcomes sought:

- *“Barriers to competition in the gas industry are minimised to the long-term benefit of end-users”*
- *“The development of protocols and standards applying to wholesale gas trading ...”*
- *“The development of a secondary market for the trading of excess and shortfall quantities of gas”*

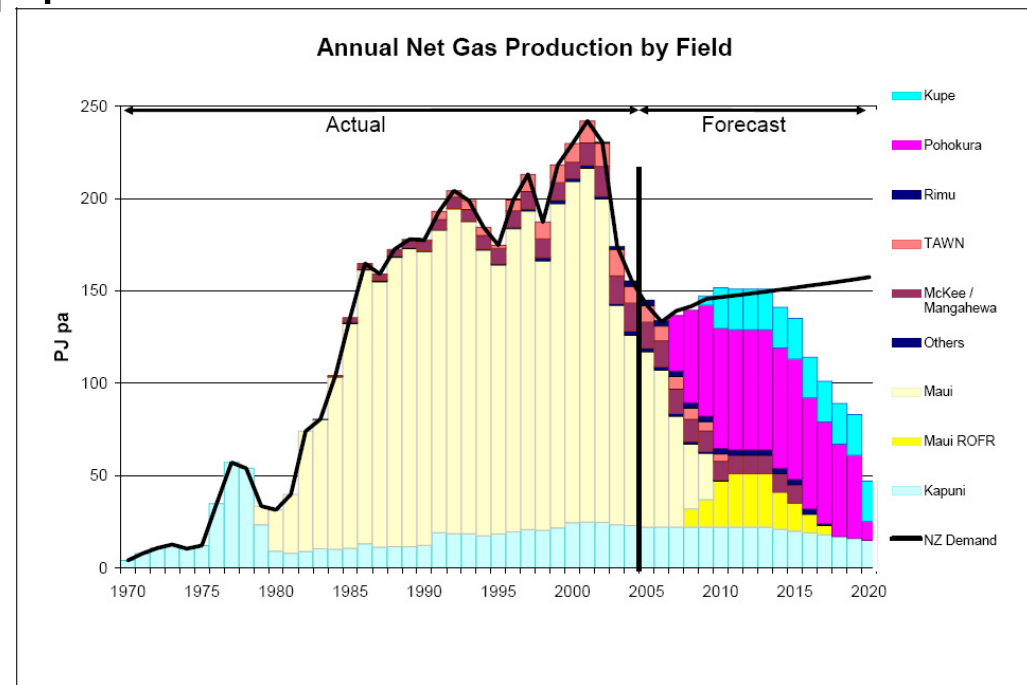
Context - Size of NZ Market



Context – Market Structure

Transition from Maui-dominated market to:

- Multiple producers
- Generally, smaller fields
- Open-access to MDL pipeline
- Uncertainties:
 - Long-term supply/demand balance
 - LNG?



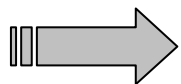
Conceptual Design – Initial Findings

Overall work stream objective:

“To develop workable, efficient arrangements for the trading of gas (including regulations and rules where appropriate) that satisfy both government and industry”

Market characteristics

- Concentrated supply
- Concentrated demand
- Substantial investment by supply- and demand-side
- Contract inflexibility
- Logistics of production and transmission
- Small economy caps market size
- Metering and information availability



Need for market, and constraints on mechanism

International markets – some lessons

- Bilateral market – US: large market, many participants
- Pool market – UK/Victoria: dense network, multiple supply sources, high information availability
- NZ: small market (illiquid), limited information available to third parties (barrier to entry), supply constraint (sellers' market)

International markets – lessons (2)

- In many overseas markets trading points spontaneously developed
- Information can be provided in various ways (eg formal markets, billboards)
- Some markets (US) have voluntary reporting of trades
- Risk allocation: given market is not large (c.f. US), standardisation of contracts could be considered (UK)
- All markets exhibited formal balancing mechanisms, daily correction most common with penalties outside a tolerance – limited linepack important consideration

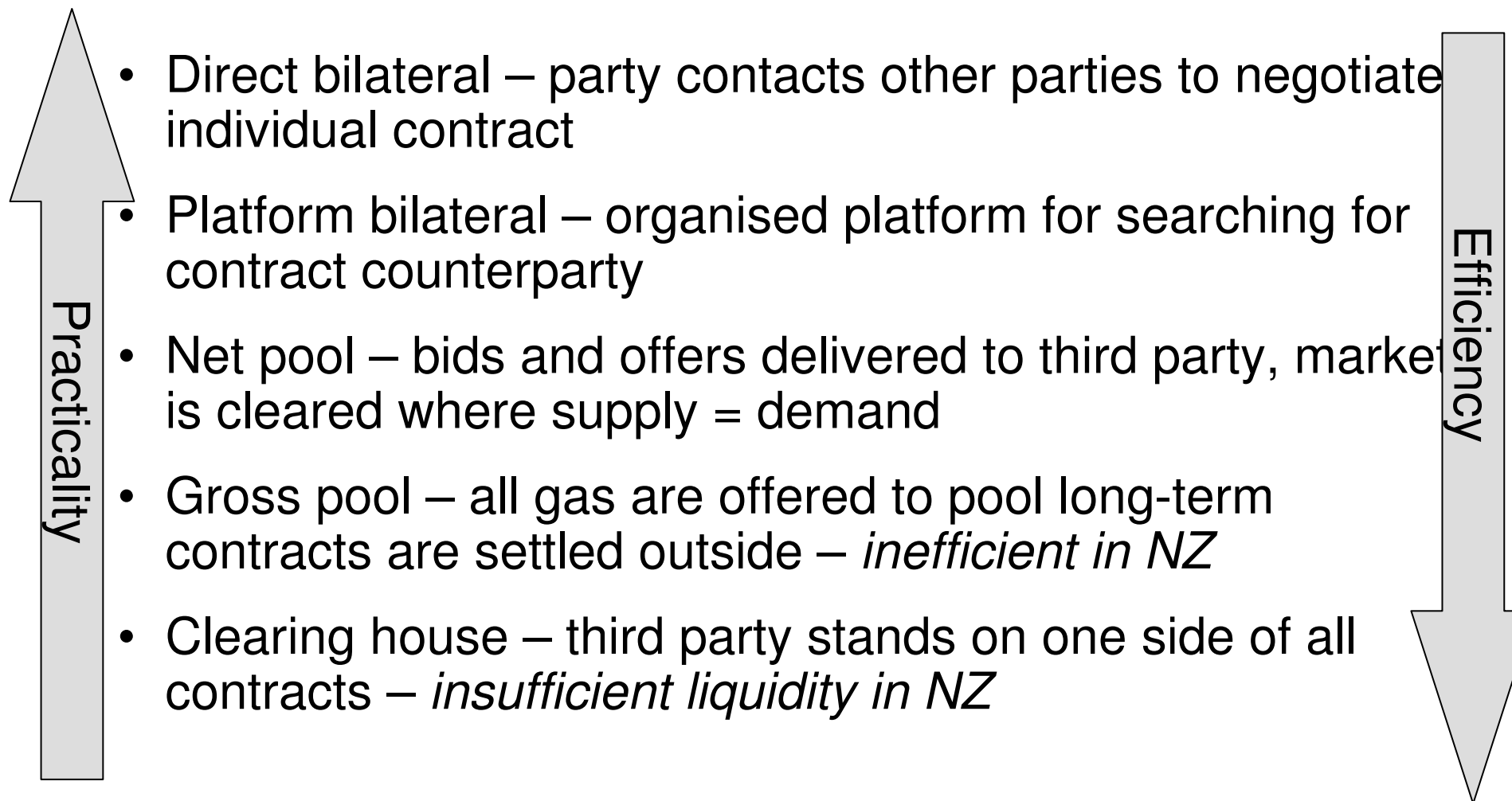
Available features and contract terms

- Compulsory v voluntary – liquidity v efficiency in trading mechanisms and practicality
- Anonymous v known counterparty – managing risk v discrimination
- Prudential requirements – net trading limits

Available features and contract terms (2)

- Hub v all welded/delivery points – liquidity, transparency, participants' capacity to process information v transmission constraints, ability to participate
- Dispute resolution process
- Information availability – participants and non-participants
- Standardised contracts – spectrum of possibility

Options



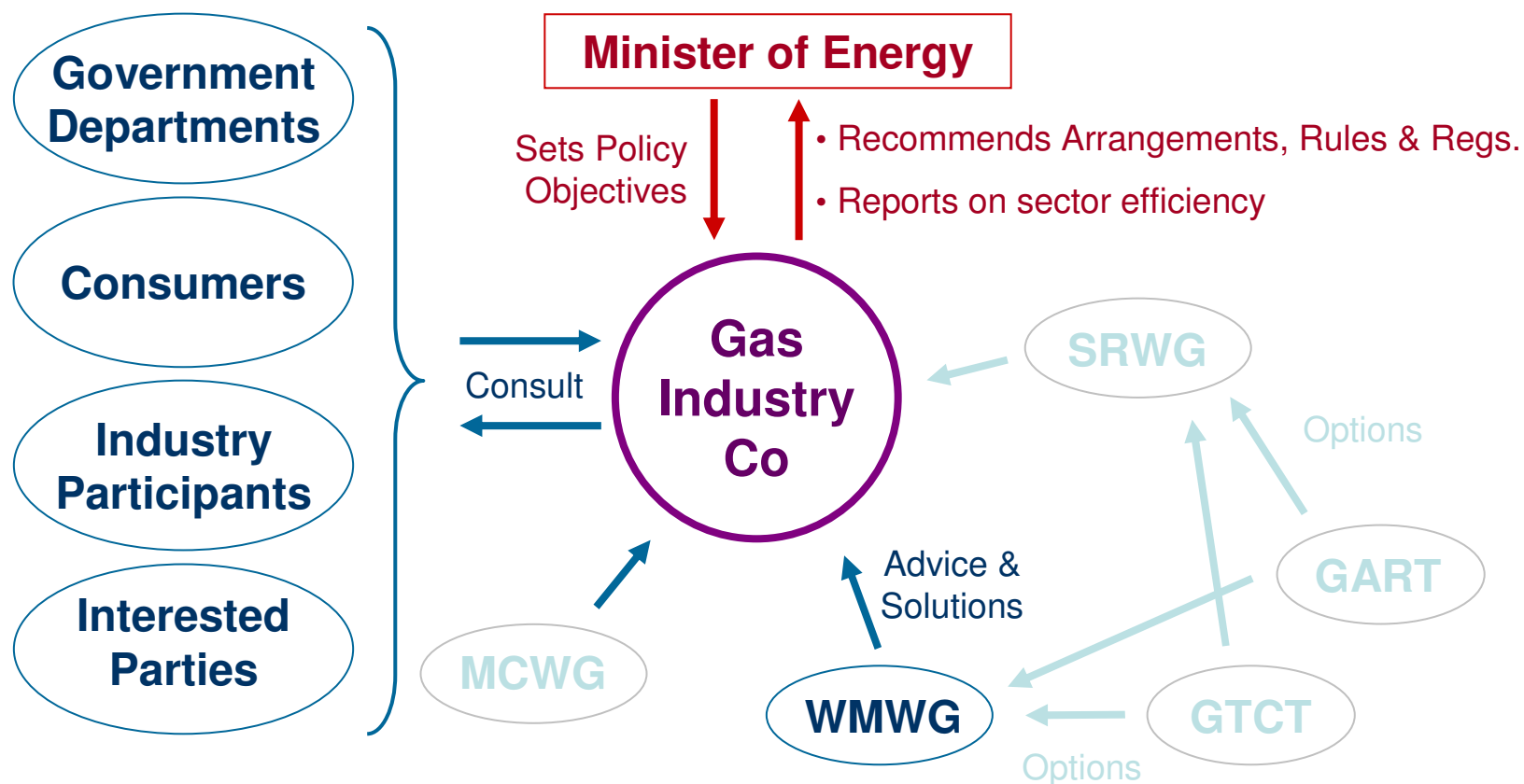
Evaluation criteria

- Efficiency
- Information availability
- Contract availability and competitive effects
- Regulatory certainty
- Administrative and compliance costs
- Practicality
- Equity
- Scalability

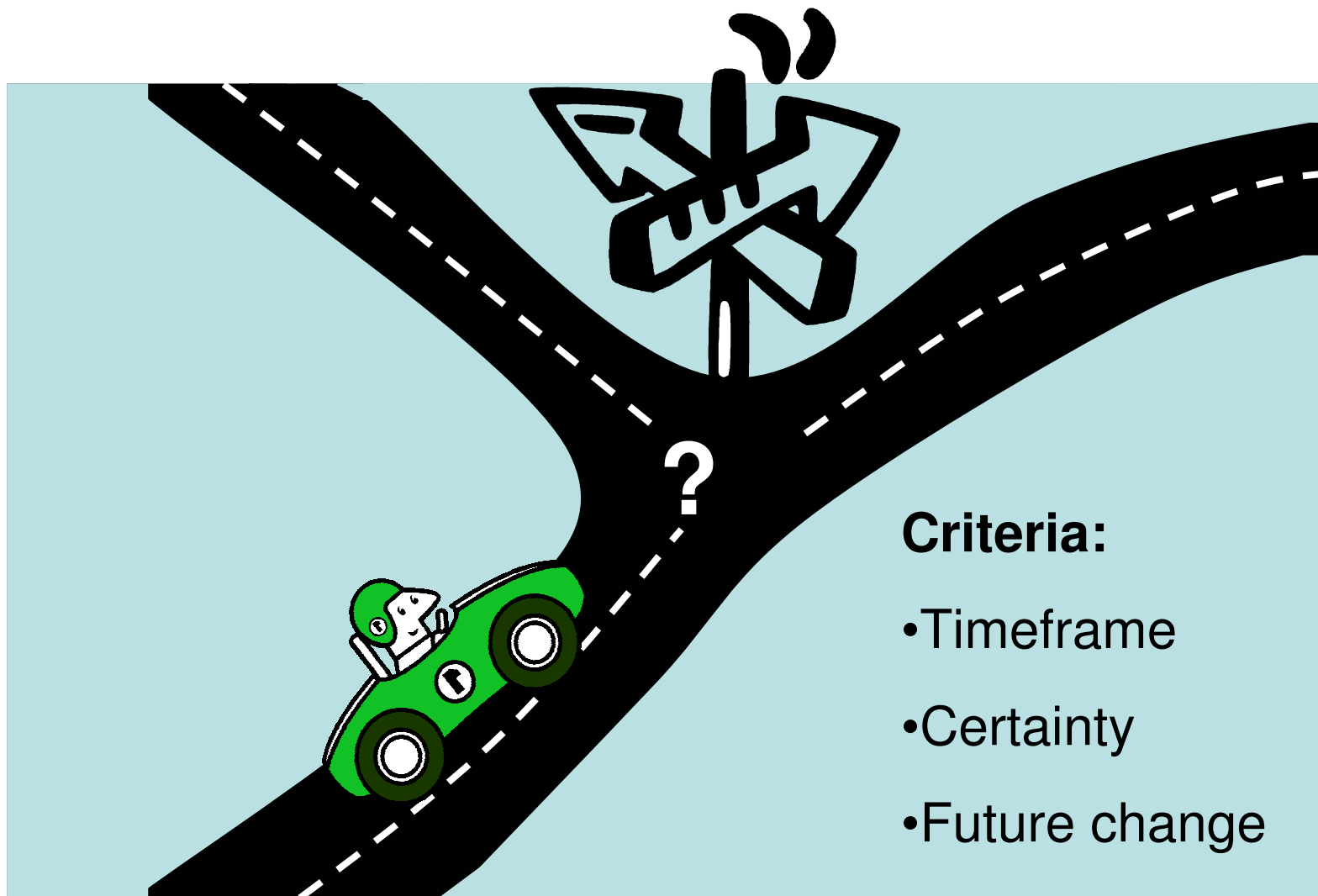
Prior to recommending regulations, we are required to:

- Identify all reasonably practical options
- Assess those options:
 - Costs and benefits of each
 - Extent to which each achieves the objective(s); and
 - Any other relevant considerations
- Can objective(s) be achieved by means other than rules/regulations?
- Undertake consultation

Dramatis personae



Industry Arrangement vs. Rules



Timeframe – Conceptual Design

Evaluation of short-term options	December 2005
Consideration and feedback from WMWG	December 2005
Evaluation of options for long-term market	January 2006
WMWG input	
Finalise report	February 2006
Gas Industry Co Board	March 2006
Consultation document released	March 2006

Overall Timetable

