

DEREGULATION FROM THE GAS UTILITY'S PERSPECTIVE

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Abstract

The paper covers the process of energy sector reform as it relates to the New Zealand Gas Industry. The reform processes are aimed at deregulating the gas industry, encouraging competition within the energy sector, and providing only light-handed controls in the areas of transmission and distribution where competition is unlikely. The paper concentrates on the technical aspects and views the process from the utility point of view.

The first section looks at the specific elements of the energy sector reform legislation and identifies the changes that were brought about through the new Gas Act, the Gas Regulations and associated law amendments. The changes range from the removal of the exclusive franchises and price controls through to the development of a new regime to control gasfitting and gas appliances.

The second section reviews the relevant aspects of the broader changes of the deregulation process which have impacted on all New Zealand industries as the country moves through the 90s. These changes range from new legislation to manage resources through to changes in the health and safety area.

The final section covers the activities and initiatives of the Gas Industry to optimise the opportunities that the deregulation process provides. These changes range from the preparation of access agreements for transportation of gas through to new training structures to ensure that adequate skills are available to maintain the industry's excellent safety and reliability record.

Introduction

In 1988 the then Labour Government announced its intention to deregulate the gas and electricity industries in line with the general thrust to free up and restructure various aspects of the New Zealand economy. The aim was, through increased competition and efficiencies in the energy sector, to provide consumers with greater choice and hence better prices and services.

The legislation to bring about reform of the energy sector finally completed its progress through the Parliamentary process and passed into law in December 1992, with most provisions coming into effect on 1 April 1993.

This paper looks firstly at the consultative process to introduce the reforms specifically for the gas industry (and electricity industry) and then at other changes affecting all industries, and concludes by indicating the activities that are occurring within the industry after nearly twelve months of operating in the deregulated environment.

The Objective of the Changes

The four years between the Government's initial announcement to deregulate and the actual passing of the legislation into law saw little change in principle or objective from that originally announced. This was despite a general election and a change in Government midway through the process.

Some of the specific details were different from those originally envisaged, and some aspects were fiercely debated, particularly in relation to line and energy charges, but overall the objective remained the same.

That objective was to increase competition in all possible areas and through competition leave market forces to

encourage efficient, innovative solutions and produce for consumers the best possible prices and services.

Where competition was unlikely and/or would be contrary to the country's best interest, such as in duplication of transportation systems, reliance was to be placed on a minimum of constraints and publication of specific financial and statistical data through a disclosure regime to identify any instance of monopoly abuse. The threat of re-introduction of price control was to be held in the wings for those who might be tempted to exploit the opportunity unfairly.

Developing the Legislation

Throughout the process of developing the legislation the Government remained committed to ensuring that both the gas industry and the electricity industry were to be subject to similar rules and constraints. This resulted in the electricity industry seeming to be much more involved in consultation with officials, setting the pace of progress, and gaining advantage in the market place. This was perhaps not surprising because of the multitude of players in that industry, the complexity of ownership issues, the high customer numbers, and the impact on tariffs etc as cross subsidies were to be removed. It was however very frustrating for those in the gas industry.

As we attempted to move through the process of finalising legislation we were frequently advised that details were still being "worked through with the Electricity Industry", or we have "not thought about the impact in the Gas sector". Such remarks did not improve relationships and yet the Gas Industry remained committed to and supportive of the change throughout.

Although the deregulation formulation process dragged on, the end results from the Gas Utilities perspective were not

unsatisfactory. In many instances the level of consultation was good, and we felt committed to the process, and more importantly we wound up with reasonable and workable solutions.

Competition

Intra-fuel competition, that is competition within fuel types as opposed to competition between fuels, appeared to be the principal concern of Government throughout the entire reform process, with little perceived attention given to the implications for inter-fuel competition. Yet in many markets and particularly for new consumers the choice between fuels and the benefits provided by each fuel are important considerations in the process of deciding on the fuel to be used.

The term "level playing field" became widely used, as details of the deregulation process were debated. However, on the line and energy charge issue, that is, the proportion of costs recovered from consumers through standing charges, the Gas Utilities believed that the field had a considerable unfavourable tilt to it. By the end of the process we even had officials wanting to tilt the playing field to encourage new entrants. The degree of innovation and lack of clear thinking are apparent in the final solution but if we had attempted to further refine the requirements the additional delays would have been unacceptable and many of the benefits would have been in danger of never being achieved.

Deregulation

Despite the arguments over a number of issues the legislation eventually wound its way to top of the heap and appeared first as the voluminous Energy Sector Reform Bill with 253 pages and 353 clauses. This was subsequently separated into various parts as it proceeded through the public consultation stages and returned for its final readings. Midway through 1992 the Energy Companies Act emerged to resolve ownership issues and then the Gas Act 1992 (and its equivalent Electricity Act) finally passed into law on 17 December 1992. Two other pieces of legislation, the Plumbers, Gasfitters and Drainlayers Amendment Act 1992, and the Building Amendment Act 1992 were also passed on the same day and these Acts together provided most of the changes necessary for the reform programme.

With these Acts came new regulations which contained much of the detail. The two major aspects covered were those relating to information disclosure and those relating to safety and measurement issues. At the time of writing the Information Disclosure Regulations are still not finally promulgated although they are close. A full review of the Safety and Measurement Regulations is in progress to tidy up errors, and omissions and to capture those aspects which were still outstanding when the first edition was promulgated.

A number of other peripheral matters covered by Regulations still remain to be tidied, but overall we have enough detail to be able to say that the legislative changes are complete and we can operate fully to the new regime.

The Changes

The key changes introduced by the reform process were:

- Removal of exclusive franchises to supply and replacement by an open access system with operators being licensed to provide distribution and retailing services throughout New Zealand.

- Removal of price control though the Commerce Commission on Wholesale and Retail Tariffs and replacement by a light-handed information disclosure regime relating to publication of tariffs, accounts and performance measures.
- Removal of the requirement to provide a gas supply as of right, allowing normal commercial conditions to apply to network developments.
- Introduction of a process to permit Codes of Practice for a whole variety of industry activities to be formally adopted and given the force of law.
- Removal of the requirement for gas suppliers to inspect and certify all gas installation work, and introduction of a self certification system for gasfitting. In addition the range of persons who can carry out gasfitting has been extended considerably.
- Amendment to the regulatory requirements for gas appliances, replacing the one-off type approval system with a compliance process which puts much more direct responsibility on manufacturers and importers to provide consistent quality products. Penalties and recalls will now be as defined in the Fair Trading Act.

Many of the changes overturn traditional thinking in the gas industry around the world and, with its total package of reforms, New Zealand has shown a lead in introducing new concepts which remove the extensive regulatory controls which characterise the industry in other parts of the globe.

Other Reforms which affect the Energy Sector

Before discussing the activities by Gas Utilities to fully implement the reforms it is important to appreciate the other changes that are occurring and to remember that Energy Sector reform was just one piece of the overall New Zealand economy restructuring process.

In late 1991 the Resource Management Act (RMA) came into force. This massive piece of legislation, coupled with the Crown Minerals Act repealed or amended a whole raft of legislation which impacted in a variety of ways on the Gas Industry. Generations of laws relating to air, water and soil quality and use, and to planning procedures were replaced with a system of controls to promote sustainable management of natural and physical resources. The RMA sets out to revise attitudes towards the use, development and protection of resources, and to minimise adverse environmental effects. It also brought moves away from central control and placed accountabilities on individual companies and at regional and local district levels.

At the same time labour relations were being overhauled and also health and safety attitudes revised. The Health and Safety in Employment Act introduced in 1992 moved the emphasis away from prescriptive listing of requirements for safe working and in its place put the onus on individuals as employers and employees to set and improve workplace conditions.

Although a stick remains firmly in the Government's hand, albeit behind the back, the opportunity is provided for individuals to take control and develop systems that meet the health and safety needs in the most appropriate, and hence, most cost-effective way. Linked with this are the changes to the ACC levies which again are aimed at encouraging industries to operate safely and be able to reap the benefits of so doing.

In the provision of skills the same principles have been used. The Industry Training Act, which is part of the education system reforms, encourages the formation of industry training organisations allowing groups with similar needs to define and take responsibility for the training requirements to meet those needs. It dismantled many of the previously very formal structures, and when linked with the new eight-level qualifications framework provides flexibility for employers to formulate training programmes which again meet the real needs.

For the gas industry particularly where the potential hazards could be significant, and safety and training are vital, these changes provide the opportunity for a proactive approach to maintaining an excellent safety record.

To complete the picture, in the commercial field the influence comes from the Commerce Act, the Fair Trading Act and more recently from the Consumer Guarantees Act.

The Commerce Act is aimed at promoting competition in New Zealand markets, and prohibiting anti-competitive agreements, use of dominant levels of market power, and business acquisition which would result in creation or strengthening of dominance in any market. The Fair Trading Act defines responsibilities of suppliers and puts an obligation on advertisers and promoters not to mislead or deceive consumers. Finally the Consumer Guarantees Act provides protection for consumers where goods or services are supplied for personal or domestic use.

Preparation for Open Access

As individual companies, and collectively through the Gas Association, the Gas Utilities are progressing with plans to operate the transportation systems in a full open-access mode.

The present bundled gas supply and transmission contracts are being replaced by two agreements, one for the wholesale supply of gas and one for transportation services up to the city gate stations. These contracts incorporate the access and carrying conditions as well as the tariff information.

At the distribution system level after initially sharing thoughts on access terms and conditions, each distributor is now separately preparing documentation and establishing tariffs. Specific contract details are currently less urgent at the distribution level because no other distributors or traders are operating yet, but this may soon change.

Guidelines have been agreed with the Ministry of Commerce for allocation of costs and establishment of tariffs between the existing distribution and retailing activities. These guidelines relate tariffs initially to consumer meter capacities, but other aspects, such as load factor, may be of sufficient significance to warrant consideration in tariff formulation. If the guidelines are fully complied with, the information disclosure regime requires only for the results (the tariffs) to be declared, but if load factor or other bases are used the methodology as well as the outcomes have to be released.

To take note of the new supply arrangements and the other legal changes most Utilities have now revised and reissued their Conditions of Supply to customers. In many cases, as well as making the changes necessary to reflect the new legal framework the opportunity has been taken to use plain language.

Installations

A unified approach has been taken on the various changes in the gasfitting and installation processes.

The introduction of self certification of gasfitting work, replacing the utility-driven inspection process, has worked well. The initial feedback after nine months through the selective audit programme operated by the Plumbers, Gasfitters and Drainlayers Board has been positive. Contrary to some fears standards have not dropped, and the tradesmen have grasped the new opportunity.

The move into DIY gasfitting has been cautious, as was expected, but improved codes of practice and consumer education should see this gain momentum. The other move to provide more competition in the installation business, the introduction of employer licences, has also been slow, or more correctly, non-existent. The very tough conditions set under the legislation for acquisition of employer licences has deterred many and yet the system offers significant opportunities to improve installation services. The conditions may need review to make them more achievable.

The appliance type approval scheme has now been dismantled and replaced with basic safety related requirements for each and every appliance that enters the market place. A New Zealand standard setting out these requirements, backed by the Gas Regulations and the Fair Trading Act provides a good example of how the market can operate. While we in the New Zealand industry are comfortable with the system, the change in appliance controls are very sceptically regarded by some of our overseas industry colleagues.

The major negative influence in the drive to improve service to our customers has come through the Building Act where the introduction of a Territorial Authority consent and compliance system has added costs and time delays, and brought no benefit for the consumer wanting a gas-fired water heater installed. Attempts through the Gas Association to modify the restraints are proving to be very frustrating.

Other Combined Activities

In other areas, particularly in training, the Utilities are co-operating effectively. In the next few months the Gas Industry Training Organisation should be formally established and we can begin to build skill blocks into the qualification frameworks. Whenever possible expertise is being shared on dealing with RMA issues, but inevitably the local personal touch is important to ensure that permitted activity status is obtained for distribution systems and for most gas installations.

Major revisions of a number of Codes of Practice, prepared as New Zealand Standards, are progressing. Some of the changes are driven by the new legislative requirements while others are technology driven. The aim as far as possible is to define the high level standards that must be complied with to ensure safety, and to provide detailed solutions as one means of compliance leaving opportunity for innovative solutions where appropriate.

The review of the Safety and Measurement Regulations is also being tackled by the Association on behalf of the Utilities. The basics are correct we believe, but some fine tuning is necessary to complete the process.

Conclusion

After nearly twelve months of operating in the deregulated environment the Gas Utilities are active in all areas to ensure that the opportunities are taken and that where it is appropriate competition is fostered and efficiencies are achieved. The Utilities individually and through the Gas Association put a

lot of time and effort into liaising with Government to develop a workable framework for the Industry, and we are keen to make sure that it works and our customers reap the benefit. Our future depends on our customers being satisfied that they are receiving a safe and efficient service from their gas supplier.

Author

TONY HAMMOND is the President of the Gas Association of NZ (Inc). Tony was born and educated in England and worked for British Gas for 20 years prior to coming to New Zealand in 1976. With BG he was involved initially in gas production and later with the development of transmission and distribution systems as natural gas replaced manufactured gas. In 1976 he joined Hutt Valley Energy Board as Chief Gas Engineer and in 1987 joined the Natural Gas Corporation of NZ as Manager Technical Services. During the six years with NGC he has been involved in various engineering roles and is currently General Manager, Engineering Support, based in the Head Office in Wellington. Tony has been involved with the Gas Association for 12 years principally in technical areas such as development codes and standards, training and safety. He was elected President for a two-year term in February 1993. His qualifications include Chartered Engineer (UK), BSc in Chemical Engineering, Member of Institution of Gas Engineers (UK), Member of Institution of Professional Engineers of NZ, and Fellow of New Zealand Institution of Gas Engineers.