energy

Congress prepares to tackle the thorny natural gas issue

‘One man’s meat is another’s poison’

By Rogers Olverson

What is big, hairy, mysterious, gives oilmen ulcers, throws Midwesterners into a rage, and eats politicians for lunch? Easy. The natural gas issue.

But now Ronald Reagan says he’s ready to take on the monster and late last month whipped out his six-gun: a decontrol bill with something for everyone.

For gas producers, there is a return to a free market. For consumers there are new limits to keep any increases in gas prices at or below the rate of inflation. For pipelines there is the repeal of the Fuel Use Act, a barrier to development of new markets, and the removal of the incremental pricing that was constantly jacking up costs.

So, is everybody happy? Nope. One man’s meat is another man’s poison, they say, and in this three-sided banquet, Reagan is serving some of both at each place.

Producers must face lower prices for deep gas and other “incentive prices” which, in some contracts, are as high as $10 per mcf. Consumers must face the vagaries of a completely free market in natural gas by January 1, 1986, and the increase in the cost of ‘old gas,’ which, in some contracts, is as low as 30-cents per mcf. Interstate pipelines must give up their “cushion” of this old, cheap gas and their exclusive access to gas from federal waters.

“It bites everybody differently,” says Lafayette independent producer Paul Hilliard, a member of the Independent Petroleum Association of America executive committee.

Hilliard had a chance to study the President’s proposal shortly after it was sent to Capitol Hill, at an IPAA committee meeting.

“It’s an end to penalties and subsidies,” he says.

Consider a few major points of the bill, based on an early assessment of the bill by IPAA:

—Upon the bill’s enactment, all gas not under contract would be decontrolled. All gas under contract would be subject to contract renegotiation by buyer and seller. All new contracts would be decontrolled, that is, not subject to the current price ceilings of the Natural Gas Policy Act (NGPA).

—Escalator clauses in existing contracts, which track incremental improve under the NGPA, would be limited by a new ceiling or “cap” based on the volume-weighted average of all decontrolled contracts for the previous three months. Prices under existing contracts could be no higher than NGPA prices or the cap, whichever is lower.

—On January 1, 1985, for any old contract that has not been renegotiated, either party may “market out,” or abrogate the contract. If buyer and seller cannot agree on a new contract, then the former buyer is obligated to transport the gas (at some incentive rate) to the new buyer.

—The Fuel Use Act, which forbids use of natural gas by some industrial and utility customers, would be repealed.

—Natural gas produced in the federal offshore domain, now reserved for interstate pipelines, would become available to all buyers.

—Take or pay provisions in existing contracts would be reduced to 70 percent of the deliverable gas. That is, buyers could not be forced either to take or to pay for more than 70 percent of the gas, even though some contracts include 85 to 100 percent of the gas under a take-or-pay provision. If the buyer does reduce his take, however, the seller may abrogate the contract and sell his gas elsewhere.

— Pipelines, which have been allowed automatic pass-through of increased gas purchase costs, could not pass on any increase in gas purchase
costs above the inflation rate. Admittedly the bill is now in the hands of Congress, and will, without a doubt, be folded, spindled and mutilated beyond recognition before the battle is over. But it still bears the President's stamp of approval and warrants a close interpretation.

Clear messages

The various lobbying groups have not yet put out their projections of how this bill would affect the average price of gas in the nation—currently in the neighborhood of $3. But the bill itself carries a few clear messages for those of us in Louisiana.

For Louisiana consumers, the fact that the bill declares open season on OCS gas is nothing but good news. In addition, the dissolution of the low-priced cushion that the interstate pipelines now enjoy, would put the state's ailing intrastate lines on even footing and ready for some head-to-head competition.

The state's biggest consumer, the

NGPA—nooks like the deep gas of the Tuscaloosa Trend—prices will drop as buyers will also be freed from those burdensome contracts.

Paul Hilliard, for one, figures he would be hurt by the President's bill. "Over half of our income is from deep gas, under no-market-out-classes," he notes.

But Hilliard takes a broader view, pointing out that such gas accounts for only five percent of the nation's production. And he points out that high-priced gas has been subsidized by cheap gas in an artificial market created by the NGPA.

"We never should have had $8 gas," he says, "but we never should have had 20-cent gas either."

In the longer run, Hilliard sees a boon to the industry. Thanks to the Fuel Use Act and spiralling gas prices, the market for this clean-burning fuel has been shrinking. Hilliard figures gas producers and distributors have lost 4 percent of the market to coal. They could lose

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The chemical industry, is delighted with the looks of the President's bill.

"We think (gas) prices in Louisiana would fall," says Fred Loy, director of the Louisiana Chemical Association.

But what about Louisiana gas producers, and the service companies that depend on their financial health and eagerness to drill? Producers have been clamoring for deregulation for years, but deregulation in today's slack market can't act as a panacea. Too much gas and too little demand naturally puts downward pressure on prices.

The movement of all gas to a median price would help some, hurt others. For producers with old, cheap gas, the news is good, as they will be freed from those old contracts to negotiate a higher price. For producers who have specialized in the high-priced nooks allowed by the another 15 percent to cheap oil if gas prices don't fall into free market competition.

"I'd rather be looking for a commodity to sell to a healthy economy than looking for a commodity to sell to a shrinking market," he says.

"I'd rather sell gas at $3 than have gas shut in at $5."

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"There would be an incentive to drill for the free market on 1-186. People would be looking for gas now to sell under the rolling cap until then," says Hilliard. "To me that's a lot better than dealing with what we have now."