

Reforming Australia's Domestic Gas Security Mechanism

23 February 2023

Introduction

The Australian Chamber of Commerce and Industry welcomes the opportunity to contribute to the proposed guidelines of Australia's Domestic Gas Security Mechanism (ADGSM).

Since its introduction on July 1, 2017, the ADGSM has been ineffectual and needs reform. It has yet to be triggered by the responsible minister despite operating in an extremely tight gas market, and major disruptions to gas supply and surging prices in 2019 and 2022. The ADGSM has failed in its aim to ensure that there is sufficient supply of natural gas to meet the forecasted needs of Australian gas consumers.

In its current state, the east coast gas market is dysfunctional. ACCI has always regarded the ADGSM as a temporary measure to be applied only while broader, more comprehensive reform of the gas market is being developed. The government's recent legislated \$12/GJ price cap and proposed mandatory code of conduct should not be viewed as an alternative to more effective, long-term strategies. Increased supply and greater competition are needed to put downward pressure on the price of gas in the east coast market and should be the hallmark of more comprehensive reforms.

ACCI continues to call for the development of a national gas strategy. The strategy would aim to achieve a functioning gas market, by removing supply constraints, freeing up the market to competition and bringing down domestic gas prices, rather than adding further regulation. An energy roadmap also needs to be established, supporting the transition to renewable energy, optimising gas power generation and removing undue pressure on the gas market.

Activation

ACCI is pleased to see our previous recommendation on more regular monitoring of the supply-demand balance, at intervals of three months rather than 12 months, has been adopted in the draft guidelines. We are also pleased to see the change in focus of the draft guidelines, with the ADGSM being seen as a preventative rather than a reactive tool.

Under the previous activation timeframe, the minister was unable to trigger the ADGSM to respond to the May 2022 east coast gas crisis. This was despite the Australian Energy Market Operator (AEMO) taking the unprecedented step to intervene and impose a cap on spot market gas prices in Queensland, NSW and Victoria.

These shorter intervals allow the Minister to regularly monitor the supply-demand balance and activate the ADGSM in a timely manner. Further, the requirement for the minister to consult with liquefied natural gas (LNG) projects in determining a domestic shortfall quarter, and notify intent to do so at least three months prior to commencement of the quarter, ensures that the ADGSM is a proactive measure that

accurately addresses the changing market conditions. This adequately solves the previous limitation of the ADGSM being a reactive tool that activates too late following slow consultative processes.

Protecting International Contracts

ACCI is concerned that the draft ADGSM guidelines do not appropriately weight the importance of the long-term contracts LNG producers have with Australia's key trading partners. The draft guidelines, enabling LNG producers to apply to increase their allowable export volume permission if it is less than the long-term contracted gas, does little to provide certainty to LNG producers that they can meet their contractual obligations. It also creates significant tensions with nations reliant on Australia's LNG exports, notably Japan and South Korea. The need to protect these long-term contracts is three-fold: support the industry providing a significant boost to the Australian economy; maintain strong international relationships and trade reputation; and restore international confidence and investment in the gas sector.

LNG exports make a substantial contribution to Australia's GDP. Since the opening of the three export facilities in Gladstone in 2015-16, LNG exports have grown to become Queensland's second largest merchandise export after coal and is estimated to be valued at \$49 billion in 2021-22. In the September 2022 quarter alone, Australia's LNG exports returned \$25 billion to the economy.¹ With European gas in a state of disarray due to Russia's war in Ukraine, the value of Australia's LNG exports is expected to rise even higher. The Australian Government's *Resource and Energy Quarterly* report expects LNG export values to reach \$90 billion in 2022-23 FY, an increase of nearly \$20 billion from 2021-22 FY.² With economic growth in Australia forecast to slow considerably over the next two years, it is important that the LNG exports are not unnecessarily hindered in the near- and long-term.

The significance of protecting international LNG contracts goes beyond the exporting of LNG. Government intervention that prevents LNG producers from meeting their contractual obligations places Australia's trade relations and reputation in jeopardy, harming negotiations and exports of other Australian commodities. Japan and South Korea rely heavily upon Australia's LNG, so much so they are second and third in Australia's greatest export earning of LNG.³ If Australia is judged to be an unreliable trading partner, then Japan and South Korea will look for alternative sources of LNG, broadening their supply chains and decreasing their activity with our LNG producers. The damage incurred on these relationships will spill over into the trading of other commodities with nations becoming increasing wary of doing business with Australia.

ACCI views the ADGSM as a stop-gap measure, to be available only until a comprehensive long-term gas strategy can be developed. The focus must be on increasing supply to address the domestic gas supply shortfalls and lower domestic gas prices, while continuing to support LNG export contracts. Already we are seeing the \$12 per GJ price cap and proposed mandatory code of conduct impact on international investment in gas exploration and development. Senex Energy, whose majority owner is the South Korean steel producer Posco, has put their \$1 billion expansion project of the Atlas and Roma North natural gas developments in Queensland's Surat Basin partially on hold due to gas market government intervention.⁴ The government needs to consider the ADGSM as a back-up plan that, when triggered, still ensures long-term gas contracts are upheld by LNG producers, restoring confidence and investment in our gas market.

¹ Department of Industry, Science and Resources, *Resources and Energy Quarterly*, December 2022 [pg.71-80]

² Ibid

³ Ibid

⁴ Senex, *Federal Government gas intervention puts \$1 billion Atlas expansion in Queensland at risk*, News, December 2022

Activated by Region

The ADGSM views the Australian gas market as a whole, with the decision to activate it based solely on the balance of supply and demand across all of Australia. Yet, the three separate gas markets (Northern, Western and Eastern) operate largely independently and the deficits in supply typically occur at the local or regional level. Viewing the Australian gas market as a whole and triggering the ADGSM only when there is a forecasted deficit in supply nationally overlooks the supply deficits at the regional level.

The ADGSM should disaggregate the three gas markets, acknowledging the difference in each of the gas markets. The ACCC, in their *Gas Inquiry 2017-2030 Interim Report* (January 2023) forecasts the east coast gas market to have a 30PJ shortfall in supply in 2023. This is, however, entirely projected in the southern states (Victoria, NSW, South Australia and the ACT), which face a shortfall of 52PJ. Even if the ADGSM were triggered and LNG exports were redirected to consumers in the southern states, transport pipeline capacity limitations still constrain supply. Gas transmission pipelines from north to south are already operating at close to capacity. Whilst not the role of the ADGSM to bolster the transmission capability of the gas network, it is important that this is factored into the minister's decision.

Incentives Domestic Supply and Remove Regulatory Barriers

An effective method proposed by the ACCC of addressing the shortfall predicted in the southern states of the east coast gas market is boosting domestic supply in these regions.⁵ Recognising the substantial timeframe and investment required, it is essential the government commence work on a national strategy to increase gas supply. Extensive regulatory barriers are currently limiting investment in gas exploration and new gas field developments.

The Victorian government has a moratorium on any new gas field development despite dwindling supply from the Otway basin and the unpredictability of the Gippsland basin. The Narrabri gas field development in NSW has been subject to extremely arduous, multi-layered environmental assessment processes since it was first proposed in 2016, significantly delaying this crucial supply of gas to the network. The ACCC has proposed additional supply in the southern states to meet their demand could come from the development of new reserves and/or supply from basins already connected to the east coast market, including the Bowen, Surat, Cooper, Gippsland, Otway, Bass and Amadeus basins.⁶

Commercial and industry gas users in Victoria and NSW that need gas as a feedstock such as plastics, fertiliser and chemical manufacturers have become increasingly reliant on gas transported from northern Australia. This a far more ineffective and expensive method. NSW imports 98 per cent of its gas requirements from other states. Improving the regulation to fast-track gas field development would increase supply to the market and contribute to affordable gas prices.

Acknowledging this is largely determined at a state government level, ACCI notes the federal government has an important co-ordinating role in influencing the states to lift restrictions of gas exploration and extraction. Increasing supply is the key to addressing the current dysfunction in the gas market and bring gas prices down. Correspondingly, it is important that regulatory barriers are removed and the ADGSM does not deter international engagement and exploration in the Australian market and further delay the required increase in gas developments.

⁵ ACCC, *Gas inquiry 2017-2030 Interim report*. January 2023 [pg.18-19]

⁶ ACCC, *Gas inquiry 2017-2030 Interim report*. January 2023 [pg.19]

National Gas Strategy

ACCI continues to advocate for the development of a national gas strategy which aims to achieve a functioning competitive gas market. This must focus on improving its efficiency and effectiveness, increasing competition and removing regulatory constraints.

To be consistent with the National Gas Objective, the strategy must be consumer focused, catering for the needs of commercial and industrial (C&I) gas users and residential customers. This, however, needs to be balanced with support to the LNG export sector, which is a major contributor to Australia's trade balance and GDP, and limit any disruption to this trade.

In developing the national gas strategy, ACCI recommends the government work with its state and territory counterparts through the Energy National Cabinet Reform Committee and Energy Ministers' Meetings to ensure consistency of policy and regulation. With a national gas strategy comes greater clarity, direction and confidence for investment and development in the gas market, this is particularly important considering the disruption caused by the price cap and proposed mandated code of conduct.

Energy Roadmap

Alongside the national gas strategy, ACCI recommends the government produce an energy transition roadmap. The government has committed Australia to a substantial transition task but has set no guidelines for the private or public sector to follow. This ambiguity disincentivises investment, slows the transition, and continues to leave the National Electricity Market (NEM), and consequently the gas market, vulnerable.

The increasing reliance on gas power generation (GPG) to support the transition of electricity supply to renewable sources was acknowledged by the ACCC as a risk to the supply and demand outlook for the gas market.⁷ Similarly, the Australian Energy Market Operator (AEMO), in their integrated system plan (ISP) for the electricity market to 2050, show that GPG will continue to play an important role in electricity generation over the next 30 years as Australia transitions to renewable energy generation, with the goal of achieving net zero by 2050. The ISP shows the reliance on GPG will increase, up 50 per cent, over the next 30 years to 2050. The accelerated transition to renewables and early closure of coal-fired power plants will increase the strain on gas supply, emphasising the need to establish an energy roadmap, so the NEM can operate effectively.

To ensure there is sufficient gas available to meet this increasing demand, it essential that work begins now to develop a comprehensive long-term national gas strategy with an overall goal of ensuring secure, reliable and affordable gas supply.

Using the resources of Treasury, the Commonwealth should conduct its own analysis and modelling of the significant transition to renewable energy. From this analysis, the production of a roadmap will serve as a pathway and checklist to make the abatement task transparent and accountable and provide confidence for private investors.

The Budget has allocated \$1.9 billion to a Powering the Regions fund to assist with the transition to net zero emissions. The AEMO's Electricity Statement of Opportunities notes that any delays in new renewable energy projects risk the ability of the NEM effectively replace retiring coal generation. This increases the reliance on gas to stabilise in the NEM and ensure security of electricity supply. The

⁷ ACCC, *Gas inquiry 2017-2030 Interim report*. January 2023 [pg.32]

creation of an energy roadmap would help ensure that the transition to a renewables grid follows the abatement task closely.

Recommendations

Recommendation 1: To ensure contractual obligations with key trading partners are met and Australia's reputation as a reliable trading partner is upheld, exemptions need to be granted in LNG exporters allowable volumes permits

Recommendation 2: The ADGSM should not view the Australian gas market as one, rather it needs to disaggregate the three largely independent gas markets (Northern, Western and Eastern) and triggered at a more local level

Recommendation 3: The ADGSM should be seen as a stop-gap measure, used whilst more comprehensive forms are developed

Recommendation 4: Increase domestic supply at a federal and state level by removing restrictions on gas exploration and fast-tracking the approval process for new gas field developments

Recommendation 5: Develop a national gas strategy to increase competition, and create a more interconnected network and improve the efficiency and effectiveness of the gas market

Recommendation 6: Develop an energy roadmap to guide investment, support the National Energy Market's (NEM) transition to net-zero, and reduce reliance on gas-fired generation and take undue pressure off the gas market

About the Australian Chamber of Commerce and Industry

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