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ENA response to the Eastern Australian Domestic Gas Market Study

The Energy Networks Association (ENA) welcomes the opportunity to make a submission on the Eastern Australian Domestic Gas Market Study (the Study).

By way of background, the ENA is the peak national body representing gas and electricity transmission and distribution businesses throughout Australia. ENA's gas distribution members provide the vital link between gas producers and consumers. Gas distributors are responsible for the quality and reliability of the natural gas that is utilised by more than 4 million households and businesses across Australia.

The delivery of natural gas to homes and businesses is conducted through an 85 000 kilometre network of distribution pipelines, valued at over \$8 billion.

Of specific interest to the ENA is the extent to which forecasts of demand, particularly residential and commercial gas demand, contained in the Study reflect potential impacts of changing wholesale gas prices on small customer demand. The study suggests relatively constant demand volumes despite significant changes to wholesale gas prices.

Australia is currently experiencing unprecedented development in liquefied natural gas (LNG) projects. While this is of significant value to the national economy, there is considerable uncertainty about the outlook for supply and demand in the domestic gas market. As the cost of wholesale gas supply increases, there is the potential to significantly affect residential and commercial gas customers through higher retail gas prices, and through driving up the cost of electricity sourced from gas fired power generation.

Section 3.4 of the Study discusses residential and commercial gas demand and states that 'a significant demand response to higher wholesale gas prices in this sector is unlikely in the near - and medium - terms' because 'consumers are relatively slow in switching from gas to electricity appliances' and the models used later in the Study suggest a relatively flat residential and commercial gas demand. The ENA notes however that the Western Australian Inquiry into Domestic Gas Prices¹ noted that *...wholesale price of gas has had a significant impact on the regulated gas tariffs facing householders.*

The Inquiry also cited media reports that during a cold snap in Perth on 7 July 2010 *household power costs (gas and electricity) had risen by 40 per cent since April 2009, that amounts outstanding on bills*

¹ Page 12 Western Australia Legislative Assembly Economics and Industry Standing Committee Inquiry into Domestic Gas Prices 2011.
http://www.domgas.com.au/pdf/Other_reports/Domestic%20Gas%20Prices%20Inquiry%20Report%202011.pdf

increased from \$1 to \$9 million over the past year, that pensioners and low income earners were foregoing heating their homes due to the expense of their power bills and that there was a doubling in the number of Synergy customers who received assistance via the Hardship Utility Grants Scheme with similar experiences for other energy providers.

The 2013 final report of the Victorian Government's Gas Market Taskforce states that:

Gas prices are expected to rise for retail customers in the eastern market. The Grattan Institute estimates that Victorian customers are likely to experience the largest price rises with the average annual bill increasing by around \$170 by 2020. Modelling commissioned by the Victorian Government estimates that, if all the LNG projects that are currently under construction commence production and export as planned, the annual average residential gas bill in Victoria could increase by almost 20 per cent over the period from 2013 to 2020, rising by \$180 by 2020, after peaking in 2015 at 30 per cent higher than current rates²

The ENA notes that this statement is in disagreement with the Study's suggestion on page 74 that Melbourne will be isolated from gas price rises due to the availability of supply from Bass Strait, demonstrating considerable uncertainty in modelling of the effect of gas prices generally.

A reduction in the use of gas also has the potential to drive gas prices higher because infrastructure costs would have to be recouped over a smaller customer base.

The ENA's submission addresses certain aspects of the Study relevant to ENA's member organisations and provides recommendations. The ENA believes however that there are other aspects relating to the development of a robust gas market that are not explored by the Study which are outlined below the specific questions raised by the Study.

What should the key objectives and priorities be for the eastern gas market reform agenda in the short, medium and long term?

The ENA consider the key objective for Eastern Australian gas market reform is to support market development and a level playing field for gas, through removal of unnecessary barriers to new gas supply, developing measures to promote greater transparency in the gas market and to ensure that energy schemes designed to reduce emissions are fuel neutral.

What are the appropriate principles to underpin that reform?

The ENA suggests that the appropriate principles to support the development of an efficient market are;

- the ability to supply long and short term information and with minimal transaction and compliance costs;
- consistent rules and oversight across jurisdictions with limited Government intervention;
- a transparent and rigorous process for rule changes; and
- effective emergency management processes.

²Page 41, Victorian Government Gas Market Taskforce, Final Report and Recommendations, 2013
http://www.energyandresources.vic.gov.au/data/assets/pdf_file/0008/205469/Victorian-Gas-Market-Taskforce-Final-Report-October-2013.pdf

What are the key barriers or impediments to bringing on gas reserves? How would you prioritise government action for removing unnecessary impediments or facilitating specific projects? How could regulatory frameworks be improved to avoid unnecessary delays in gas supply development?

ENA considers that two factors are critical to the development of new sources of gas supply. Firstly capacity by government and project proponents to address community concerns regarding the development of natural gas reserves and secondly removing unnecessary restrictions or duplication in approval processes for exploration, development, production, transmission and distribution without compromising evidence-based environmental regulation.

The Victorian Government Gas Market Taskforce, Final Report and recommendations notes that:

“There are over fifty pieces of Victorian legislation, regulations, policies and administrative arrangements relevant to adopting leading practices for coal seam gas operations. The complexity in regulatory arrangements creates uncertainty in the regulatory environment and adds to the cost for industry. The diversity of the legislation as well as the number of agencies involved creates uncertainty, delays and confusion. Without compromising environmental or safety standards, the Victorian Government should take action to improve certainty, consistency and reduce regulatory costs.”³

Many of the environmental approvals processes under State and Commonwealth laws apply not just to the extraction of gas but also to the development of production, transmission and distribution facilities.

Federal and State Government approval processes can impose a significant cost of approvals for new sources of supply. International investors and institutions routinely place great weight on factors of regulatory stability and predictability in investment assessments that affect the availability and terms of capital for Australian networks. Regulatory risk is factored into the real cost of capital. When coupled with political considerations, approvals processes can add to uncertainty, leading to higher rates for lending due to increased risk, thus changes to regulatory risk or the burden of high levels of regulation that do not complement or duplicate each other, result in higher network prices for consumers than would otherwise occur.

Do you see there is a need to improve on current markets and what would you propose as the mechanism for progressing any reforms? Are there mechanisms for improving the gas market governance framework, including the role and responsibilities of SCER and institutions?

The regulation of gas distribution networks under the NGL by the AER already ensures that there is a high degree of transparency concerning gas network tariffs and charges. In addition, the operation of Eastern Australian gas markets are overseen by AEMO which operates the retail and wholesale gas markets in South-East Australia, and the Victorian Gas Declared Transmission System, including operating the gas Short Term Trading Market (STTM), a wholesale market system designed to facilitate short term gas trading driven by daily prices.

³ Victorian Government Gas Market Taskforce, Final Report and Recommendations, 2013, p.30

ENA suggests that the current SCER market reform program has been focused on downstream reforms and that industry-led initiatives currently underway that will facilitate further transparency need to be given time to work. Government consultation on upstream reforms would be welcomed.

The ENA believes SCER is the appropriate body to pursue improvements to upstream transparency in the gas market and that the AEMC should be enabled to conduct reviews into upstream issues that would increase upstream market transparency throughout the remainder of the supply chain.

Should non-market interventions like reservation policy or export controls be ruled out?

The ENA is concerned about the impact of wholesale gas price volatility on domestic gas markets and considers this is an issue which must be addressed meaningfully in the Government's Eastern Australian Gas Supply Strategy to 2020 and the Energy White Paper. Such consideration should include evaluating the role of a National Interest Test on future large-scale export gas developments, as has been adopted in other international jurisdictions. While the ENA does not support direct government intervention in markets unless this can be justified from a public policy perspective, the government should remain open to intervening in the gas market in the event that the evolution to an export based gas industry creates transitional issues in Australia that undermine the long term productive capacity of the domestic gas sector. If intervention is required, it should be technologically neutral.

What would be useful processes to facilitate stakeholder engagement and improve accountabilities?

The relationship between the Study, the proposed Eastern Australian Gas Supply Strategy to 2020 (the Gas Strategy) and the current call for submissions to the Energy White Paper Issues Paper is not clear. In particular it is not clear how the Gas Strategy will be developed in time to inform the Energy Green Paper to be released for consultation in May 2014, and the Energy White Paper in September 2014 and the timing on any consultation processes. It is also not clear how Western Australian and Northern Territory gas issues will be included in the Energy White Paper if not included in the Gas Strategy.

Issues not covered by the study

The impact of incentives schemes

The ENA is concerned that higher gas wholesale prices may drive customers to switch to appliances that are less energy-efficient and emit higher levels of greenhouse gas emissions. Gas has a significant role to play in promoting clean energy efficiency. The ENA believes an increased use of natural gas within the Australian domestic energy market provides a genuine opportunity to reduce the carbon intensity of energy consumed by Australian businesses.

Current Government incentives schemes such as the Small-scale Renewable Energy Scheme (SRES) distort markets by further driving the residential and commercial customer base away from least cost low emissions gas technologies. The Million Solar Roofs program, if not implemented in a fuel-neutral manner to achieve emissions abatement objectives, has the potential to increase these market distortions, disadvantaging gas as a competitive supply source, without benefit to consumers.

The ENA does not support direct government intervention in markets, including the implementation of a gas reservation policy or incentives programs that do not provide a technologically neutral solution to emissions reduction, such as the Small-scale Renewable Energy Scheme. The ENA notes

that the or the proposed Million Solar Roofs program must be carefully designed to avoid exacerbating current hot water appliance market distortions, without benefit to consumers.

The ENA supports incentives programs that provide a technologically neutral solution to emissions reduction. A number of energy schemes designed to encourage lower emissions energy consumption are not fuel neutral and thus represent a distortion in the market. The ENA believes that this is particularly the case in residential hot water heating appliances, where there are market distortions such as SRES that discriminate against gas hot water systems. The impact of energy market distortions created by Government programs such as SRES was not considered by the Study.

Alternative transport options

The increased use of natural gas within the national vehicle fleet could be a significant opportunity to reduce GHG emissions and improve liquid transport fuels security as well as provide an incentive for the development of a more robust domestic gas market. However, the adoption of natural gas within the national vehicle fleet has been slow. CNG is used within some government bus fleets and a small amount of LNG is used within the road freight sector. The use of CNG within the passenger car fleet is almost non-existent, apart from a handful of natural gas conversions of petrol-powered vehicles.

The underlying causes for the slow uptake of natural gas in Australia relate primarily to the lack of natural gas refuelling infrastructure and the limited availability of new natural gas vehicles, particularly natural gas passenger cars.

The barriers to the provision of natural gas refuelling infrastructure are complex and are generally cost related. This includes the cost of compliance with regulations at multiple levels of government for the development of the infrastructure. A further barrier is expected in the form of increasing costs of wholesale natural gas in the near future.

There is an increasing range of home-based natural gas refuelling systems available for the refuelling of natural gas vehicles via a residential gas connection – in much the same way that home-based recharging systems are potentially available for electric vehicles.

Under current policy and regulatory settings, it appears that in the near to medium term the Australia market is unlikely to overcome the limited availability of new natural gas vehicles and the barriers to the development of refuelling infrastructure. Realisation of the opportunity to reduce greenhouse gas emissions and improve transport fuel security through the increased use of natural gas within the national vehicle fleet could be assisted by the following measures.

- The streamlining of regulation that allows for further incentives for the establishment of home-based and public refueling infrastructure for natural gas vehicles.
- Examination of financial options such as allowing for the accelerated depreciation for taxation purposes for investment in public refueling infrastructure.
- The consideration of gas transport infrastructure and vehicles when undertaking transport planning.
- A discussion around the removal or reduction of gas fuel excise

Recommendations

Recommendation 1

Support market development and a level playing field for gas, through removal of unnecessary barriers to new gas supply, developing measures to promote greater transparency in the gas market and to ensure that energy schemes designed to reduce emissions are fuel neutral.

Recommendation 2

Remove unnecessary restrictions or duplication in approval processes for exploration, development, production, transmission and distribution without compromising evidence-based environmental regulation

Recommendation 3

Enhance SCER's role in developing transparent upstream markets and undertake Government consultation on upstream reforms.

Recommendation 4

The AEMC should be enabled to conduct reviews into upstream issues that would increase market transparency.

Recommendation 5

While direct government intervention in markets should not occur unless it can be justified from a public policy perspective, the Energy White Paper should evaluate the role of a National Interest Test on future large-scale export gas developments, as has been adopted in other international jurisdictions.

Recommendation 6

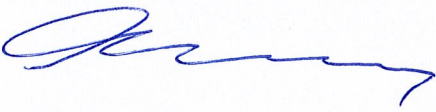
ENA recommends that the Government clarify the timeframes for the development Eastern Australian Gas Supply Strategy to 2020.

Recommendation 7

Reject incentives programs that do not provide a technologically neutral solution to emissions reduction

Any questions about our submission should be addressed to ENA's Director of Energy Infrastructure and Gas Markets, Dougal Torrance, by email to dtorrance@ena.asn.au or by telephone on (02) 6272 1511.

Yours sincerely



John Bradley

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