East Coast Gas Inquiry key findings

Gas supply

1. Domestic purchasers of gas, particularly industrial users, experienced an unprecedented change in their ability to obtain gas, especially in the period from about 2012 to the end of 2014 for gas to be supplied in 2016 and beyond. When seeking gas they received few, if any, real offers. Offers received were high priced, with limited volumes over shorter periods of time, had more restrictive terms and conditions and some were on 'take it or leave it' terms.
2. More gas supply offers are now available, but at higher prices, for shorter durations and with more restrictive non-price terms and conditions. Domestic industrial users may have seen margin reductions of 0.6–6.0 percentage points, depending on the industry and the wholesale gas price increases. Household gas bills may increase by 5 per cent in New South Wales and 11 per cent in Victoria with wholesale gas price increases of, for example, $2/GJ.
3. The reliability of future gas supply is affected by three significant factors coinciding:
   - Significant demand from the LNG projects, which has diverted gas from traditional sources of domestic supply.
   - Low oil prices reducing the ability and incentive of producers across the entire east coast gas market to explore for and develop gas.
   - Moratoria on onshore gas exploration and development and other regulatory restrictions in New South Wales, Victoria and Tasmania, and potentially the Northern Territory, prohibiting new gas supply.
4. The future supply outlook is uncertain. Future domestic and LNG demand will require extensive development of undeveloped gas reserves. Sufficient gas is currently forecast to be produced in the east coast gas market to meet domestic demand and existing LNG contract commitments until at least 2025, but there is uncertainty over the timing of some developments, particularly due to low oil prices.
5. There is a need for more sources of gas supply, particularly in the southern states. The gas users in these states are becoming overly dependent on the jointly marketed GBJV gas. If their alternative to dealing with the GBJV is to transport gas from Queensland, southern users may have to pay considerably more for gas than they are otherwise likely to pay in a competitive market. This is exacerbated by the high cost of transportation. Increasing the level and diversity of supply, located close to southern demand centres, will improve the competitive dynamics in the south and is likely to lead to better pricing outcomes for domestic users.

Gas transportation

6. Pipeline operators have responded to the changes underway in the market. There is, however, evidence that a large number of pipeline operators have been engaging in monopoly pricing. This gives rise to higher delivered gas prices and is having an adverse effect on the economic efficiency of the east coast gas market and upstream and downstream markets, the costs of which will ultimately be borne by consumers. There is also evidence that the ability and incentive of existing pipeline operators to engage in this behaviour is not being effectively constrained by competition from other pipelines, competition from alternative energy sources, the risk of stranding, the countervailing power of shippers, regulation or the threat of regulation.
7. The current gas access regime is not imposing an effective constraint on the behaviour of a number of unregulated pipelines. The current test for regulation under the National Gas Law (NGL) (the coverage criteria) is not designed to address the market failure that has been observed in this Inquiry, that is, monopoly pricing that results in economic inefficiencies with little or no effect on the level of competition in dependent markets. Other gaps in the regulatory framework are also allowing pipelines that are subject to regulation to continue to engage in monopoly pricing. Information asymmetries are limiting the ability of shippers to identify any exercise of market power and to negotiate effectively with pipeline operators.

8. Less than 20 per cent of the transmission pipelines on the east coast are currently subject to regulation under the NGL and National Gas Rules (NGR). This is in direct contrast to other comparable jurisdictions, such as the United States, the European Union and New Zealand, where the vast majority of transmission pipelines are regulated. It is well recognised in these jurisdictions that pipelines can wield substantial market power even where producers and users have a number of transportation options.

Market operation and the level of market transparency

9. The gas specification required by the LNG projects is different to the specification required by other gas users. This difference has the potential to impede the free flow of gas across the east coast gas market and impose additional costs on some market participants, potentially bifurcating the market, and reducing liquidity and opportunities for trading and arbitrage.
10. Lack of transparency and information about the level of reserves, and commodity and transport prices are hindering efficient market responses to the changing conditions and are not signalling expected supply problems effectively.
11. Trading of longer-term capacity held by shippers is occurring across the east coast. Shorter-term capacity trades are also occurring but not on all pipelines. There is no evidence of withholding of capacity by shippers on major east coast pipelines.
12. However, there is evidence that capacity is being withheld by incumbents on some regional pipelines, which is restricting competition for supply from other retailers.
13. APA has taken steps, in conjunction with AEMO, to improve transparency around gas flows into the Wallumbilla compound which services the Wallumbilla GSH. Some concerns remain as to the transparency of actual hub services being delivered and the pricing of those services.
14. Risk management mechanisms are becoming more important for buyers, and especially industrial users, as the terms and conditions of supply are tightened by suppliers. These include storage and gas trading mechanisms such as the STTMs. The liquidity of gas trading mechanisms is currently limited. In the long-run, liquidity will be best supported by an increase in the diversity of gas market participants and the volume of gas supply in the market overall. At present, there is no evidence that access to storage capacity on reasonable terms is a significant barrier to entry by smaller retailers in the east coast gas market. This may become a more significant issue in the future if the volume of gas available for supply into the market increases.

East Coast Gas Inquiry recommendations

Gas supply

1. Governments should consider adopting regulatory regimes to manage the risks of individual gas supply projects on a case by case basis rather than using blanket moratoria. Governments should take into consideration the significant effects that moratoria and other restrictions on gas development may have on gas users.
2. Gas reservation policies should not be introduced, given their likely detrimental effect on already uncertain supply.

Gas transportation

3. The COAG Energy Council should agree to replace the current test for the regulation of gas pipelines (the coverage criteria) in the NGL with a new test. This test would be triggered if the relevant Minister, having regard to the National Competition Council's recommendation, is satisfied that:
   - the pipeline in question has substantial market power
   - it is likely that the pipeline will continueto have substantial market power in the medium term, and
   - coverage will or is likely to contribute to the achievement of the National Gas Objective.

   The COAG Energy Council should also ask the AEMC to carry out further consultation on the specific matters that should be considered when applying this test and how it should be implemented and to advise the COAG Energy Council of the amendments that would need to be made to the NGL and the NGR to give effect to this new test.
4. The COAG Energy Council should ask the AEMC to review Parts 8–12 of the NGR and to make any amendments that may be required to address the concern that pipelines subject to full regulation may still be able to exercise market power to the detriment of consumers and economic efficiency. In carrying out this review, the AEMC should also consider whether any changes can be made to the dispute resolution mechanism in the NGL and NGR to make it more accessible to shippers, so that it provides a more effective constraint on the behaviour of pipeline operators.
5. The COAG Energy Council should ask the AEMC to explore how the scope of the information disclosure requirements in the NGL should be expanded to require all pipelines operating on an open access basis (that is, regulated and unregulated pipelines) to publish financial information that shippers can use to determine whether or not the prices they are offered by pipeline operators are cost reflective. The publication of this information would enable shippers to negotiate more effectively with pipeline operators and to identify any exercise of market power more readily.

Market operation and the level of market transparency

6. All explorers and producers, including non-ASX listed companies, should report consistent reserve and resource information across the east coast gas market. Reporting should be based on common price assumptions in the calculation of reserves and resources. Gas reserve and resource information should be displayed on the Gas Market Bulletin Board consistent with the COAG Energy Council Gas Market Development Plan to enhance the market information available to Bulletin Board users.
7. The COAG Energy Council should ensure that the geological and reserve/resource information collected by the states and territories and the Commonwealth, is consistent, non-duplicative and shared. Where this information is made public, the Energy Council should ensure that it is in a consistent format.
8. AEMO should develop and publish a monthly LNG netback price to Wallumbilla, with a clear explanatory framework and inputs.

9. The AEMC should consult with gas users about the potential benefits of requiring AEMO or the AER to publish a periodic price series of actual commodity gas prices paid to producers, either for the east coast generally or for Victoria and Queensland. Any price series should be weighted by volume and be based on commonly observed take or pay percentages and load factors.
10. The AEMC should consider how to monitor changes in the level of trading flexibility available to gas buyers over time, and how the trading and other risks of having to purchase gas and transportation services on a day-ahead basis can best be managed.
11. The COAG Energy Council should monitor the emerging issue of separate gas specifications in the east coast gas market. This issue has the potential to impede the free flow of gas across the east coast gas market and impose additional costs on some market participants. The COAG Energy Council should ensure that any costs associated with a non-standard gas specification are borne by the market participants that require that alternative specification.
12. The AEMC should consider requiring the introduction of a centralised capacity trading platform to facilitate secondary capacity trading and day-ahead auctioning of unutilised capacity.
13. The AEMC should consider the benefits of a short-term auction process for hub services if it decides to implement the day-ahead auction for pipeline services.

ACCC future work

1. The ACCC will consider the competitive effect of joint marketing arrangements of the GBJV in light of current market dynamics, for the purposes of s. 45 of the CCA.
2. The ACCC will consider whether the availability or pricing of capacity on regional pipelines raises any concerns as a breach of the misuse of market power provisions or the exclusive dealing provisions of the CCA.