

# ACCC RECOMMENDS INCREASING SOURCES OF SUPPLY AND IMPROVING TRANSPARENCY

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Legal Briefings - By **Matthew Bull**, **David Vallance** and **Joshua McGeechan**

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The Australian Competition and Consumer Commission (**ACCC**) found that the future east coast gas supply outlook was uncertain and made a number of recommendations to facilitate new gas supply (such as no blanket moratoria) and improve transparency in relation to reserves, resources and pricing (such as consistent reporting).

ACCC recommends increasing sources of supply and improving transparency. Also, in one of its most significant recommendations, the ACCC indicated that it will be investigating the joint marketing arrangements of the Gippsland Basin Joint Venture (**GBJV**).

## FINDINGS

### **The future supply outlook is uncertain**

The ACCC found that sufficient [gas](#) is currently forecast to be produced to meet domestic demand and export commitments until 2025, although these forecasts are dependent on the development of undeveloped fields, and sufficient investment in an uncertain economic environment.

The ACCC stated that the reliability of future gas supply is affected by significant demand from the LNG projects, low oil prices (which reduce the ability and incentive of producers to explore and develop) and moratoria / other regulatory restrictions prohibiting new gas supply.

In particular, the ACCC found that moratoria and other regulatory restrictions on gas exploration in New South Wales, Victoria and Tasmania hinder the development of new onshore gas reserves which have the potential to exert downward pressure on prices. The ACCC also found that exploration in the Northern Territory has been scaled back due to the potential for future restrictions to be put in place. In the ACCC's view these restrictions may mean that industrial users in southern states will become more reliant on gas supply from basins located farther away, which increases costs and uncertainty.

The ACCC also found that differences in the gas specification required by LNG projects compared to the specification required by other gas users could further complicate the supply outlook. The ACCC was concerned that these differences could lead to the separation of Queensland from the rest of the east coast due to additional costs of accessing processing facilities to ensure gas meets LNG specifications. The additional processing costs could impede the free flow of gas across the market and reduce liquidity and opportunities for gas trading and arbitrage.

### **More sources of gas are needed to compete with GBJV**

The ACCC found that there is a need for more sources of gas supply. It considered that increasing the level and diversity of supply will improve competitive dynamics and lead to better price outcomes for domestic users.

Historically, domestic users and retailers in the southern states purchased gas from suppliers in off-shore Victoria, the Cooper, Surat, Otway or Bass Basins which created competitive tension but, more recently, gas production has been in decline and gas is increasingly being dedicated to supplying the LNG projects.

The ACCC considers that these circumstances have led to the strengthening of the market position held by the GBJV, which now holds 'significant market power'.

### **Lack of transparency**

The ACCC found that a lack of transparency and information about the level of reserves, and commodity prices is hindering efficient market responses.

The ACCC noted that gas reserves and resources are 'not absolute' and therefore not able to be measured directly, but it did identify transparency issues arising from:

- inconsistencies in company reporting – listed companies report to the ASX on gas reserves at different times and at different levels of geographical aggregation. Unlisted companies or companies listed overseas often did not report at all,
- inconsistencies at State / Federal level – the States, Territories and the Commonwealth

collect geological information and reserve and resource data but their approaches are inconsistent and the release of information varies widely,

- difficulties in interpretation – the assumptions underlying reported reserves and resources information are often not disclosed, making it difficult to interpret the reserves and resources which actually are disclosed, and
- the ‘partial, provisional and mostly private’ nature of gas pricing information – confidential bilateral contracts continue to dominate, which gives participants limited insight into pricing levels.

### **Risk management is becoming increasingly important**

The ACCC found that uncertainty was making flexibility more important for buyers, whereas the same uncertainty was affecting the willingness of suppliers to offer such flexibility.

The ACCC noted that storage and short-term trading options in particular are becoming important for users.

The ACCC found that access to storage options is not currently a significant barrier to entry. However, it noted that demand for storage options may become more important if domestic supply increases, particularly in the southern states where storage options are currently limited. The ACCC also noted that appropriate storage options may also be an important factor in the development of gas trading.

In the ACCC’s view liquidity in trading markets is currently limited. As a result, there are insufficient volumes for users to rely on to satisfy their gas requirements and trading fails to provide adequate price signals to the market. The ACCC found that improved liquidity and participation in trading markets would improve price transparency by shifting supply away from long term gas supply arrangements and into shorter term markets. It was also noted that improved liquidity would allow for better management of volume fluctuations and help to alleviate uncertainty.

## **RECOMMENDATIONS AND ACCC ACTION**

### **Improving gas supply - no moratoria or gas reservation**

The ACCC recommended that Governments should assess gas supply projects on a case-by-case basis rather than imposing a ‘blanket moratoria’ . While the ACCC recognised that there are ‘serious concerns’ in the community regarding unconventional gas exploration, it recommended that Governments should take into consideration the significant effects that moratoria and other regulatory restrictions are likely to have on domestic gas users when considering the cost-benefit assessment of environmental regulatory regimes.

The ACCC also recommended that gas reservation policies should not be introduced. The ACCC did not identify any market failure that would justify gas reservation policies and instead found that, rather than increasing supply, a reservation policy would be likely to 'artificially depress prices in the short term' and discourage investment in new supply.

In reaching this view, the ACCC drew on the 2014 report of the Western Australian Economic Regulatory Authority (**ERA**), which concluded that reservation policies had a number of negative consequences including increased reliance on subsidised gas prices leading to over compensation and reduced incentives for investment in the gas industry.

### **Improving reserves and resources transparency**

To address the issues of fragmented and inconsistent reporting of gas reserves, the ACCC recommended that:

- all explorers and producers should report consistent reserve and resources information, based on common price assumptions. This should be provided to the Gas Market Bulletin Board; and
- the COAG Energy Council should ensure that information collected by the States, Territories and the Commonwealth is 'consistent, non-duplicative and shared'. This information should be published in a consistent format.

The ACCC considered that standardised reporting of reserves and resources would provide greater certainty to all stakeholders and would allow for better forward planning and investment decision.

### **Improving price transparency - LNG netback and invoice pricing**

To address the issue about public pricing information being 'partial, provisional and mostly private', the ACCC recommended that the Australian Energy Market Operator (**AEMO**) publish a monthly LNG netback price to Wallumbilla (e.g. the price derived from subtracting the cost of shipping, liquefaction and transmission from the LNG price). The ACCC considered that publishing an LNG netback price to Wallumbilla would indicate the conceptual maximum amount that an LNG exporter would pay for gas and would provide a reference point for domestic Gas Supply Agreement (**GSA**) negotiations.

The ACCC also recommended that the Australian Energy Market Commission (**AEMC**) consult with market participants about the benefit of establishing an invoice-based pricing series given potential issues with its introduction. The ACCC noted that an invoice based price series could provide a number of benefits, including:

- greater visibility of producer gas prices, including information about take or pay percentages and load factors, and
- providing a reference point for negotiations between producers and retailers.

However, the ACCC recognised that there are also a number of potential issues with the introduction of such a price series. For example, it would require the collection of information on GSAs (which are private bilateral contracts between producers and users) and the publication of a price series may increase the 'potential for tacit price collusion' or price signalling by producers.

### **Recommendations for further monitoring**

To address the issues in relation to flexibility and diverging gas specifications, the ACCC recommended that:

- the AEMC should monitor changes in the level of flexibility available to gas buyers over time, and
- the COAG Energy Council should monitor the emerging issue of divergent gas specifications in the east coast gas market.

### **Further action - GBJV investigation**

In light of its finding that the GBJV has 'significant market power', the ACCC will further consider the 'competitive effect of joint marketing arrangements of the GBJV'.

The ACCC conducted a preliminary review of the GBJV joint marketing arrangements in 2010. However, the ACCC now considers that the strengthening of the competitive position of the GBJV 'compels' the ACCC to re-consider the joint marketing arrangements of the GBJV as those arrangements may have a 'more detrimental impact on competition than in the past.'

In particular, the ACCC has indicated that it will consider whether the gas market is sufficiently mature to support separate marketing by the GBJV participants. However, the ACCC also stressed that its assessment will include consideration of the 'likely effect of separate marketing on future investment' so that any potential improvements from increased competition are not 'offset by the reduction of gas supply' from the Gippsland Basin.

This article is one of a [series](#) that Herbert Smith Freehills is publishing on the ACCC's East Coast Gas Enquiry.

## KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



**LIZA CARVER**  
PARTNER, SYDNEY

+61 2 9225 5574  
Liza.Carver@hsf.com

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