Tenure Matters

A column by Sue Slater, Senior Advisor Petroleum, RLMS

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Welcome back to the second part of my discussion on the domestic gas crisis and the recent announcement by the Federal Government[1] (27April) that they will secure the domestic gas supply with the introduction of export restrictions. Last month[2] I discussed some of the previous work done to address the domestic gas supply crisis following the release in 2015 of a Domestic Gas Strategy[3]. This month I will review the more recent developments.

It has been a busy month in gas news! The government has formally announced the start of gas export regulations which aim to limit how much gas can be exported out of Queensland[4]. These regulations come into force on July 1 and aim to give Australian customers priority access to gas supply before it is exported. The Australian Domestic Gas Security Mechanism (ADGSM) is within a new Division 6 of the *Customs (Prohibited Exports) Regulations 1958 (C'wth)* which was amended by the *Customs (Prohibited Exports) Amendment (Liquefied Natural Gas) Regulations 2017.* The ADGSM will operate for 5 years, and be reviewed in 2020. The mechanism allows the government to restrict LNG exports in domestic shortfall years (based on a calendar year). The stepped process and timeframes for ADGSM can be reviewed here[5]. Between 1 September to 1 November each exporter will be granted either an "unlimited volume permission" or an "allowable volume permission" for the following year. Exporter's may or may not have a 30 day period within which to respond prior to finalisation of the Export Permissions, depending on whether the process has been delayed. Western Australia and Darwin LNG producers are exempt from the potential restrictions and will receive unlimited volume permissions.

Whilst it is easy to see why government thinks this measure will secure gas supply (notwithstanding that there are probably much better ways of achieving that aim); it is not easy to see how it will reduce gas prices which has been a touted outcome. Additionally energy security is a bigger issue

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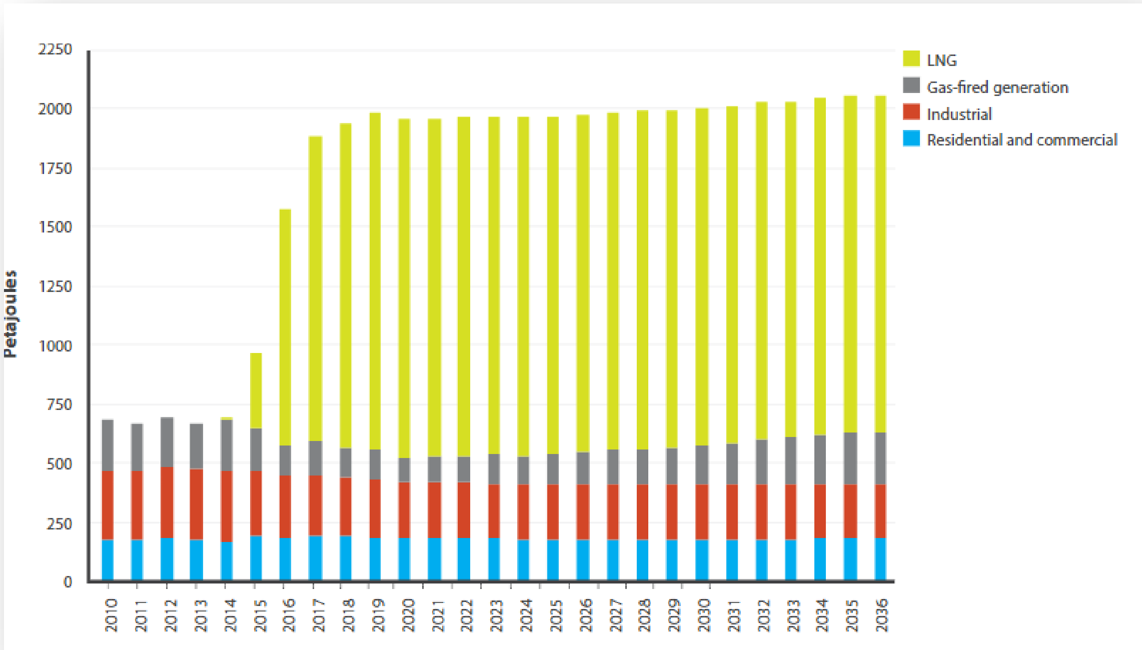
[1] https://www.pm.gov.au/media/2017-04-27/delivering-affordable-gas-all-australians
[2] Issue no 35 https://www.rlms.com.au/wp-content/uploads/2017/06/36-May-17-Tenure-Matters_No35.pdf
[3] https://industry.gov.au/Energy/EnergyMarkets/Documents/Domestic-Gas-Strategy.pdf
[4] http://www.pm.gov.au/media/2017-06-20/securing-our-energy-future
[5] https://industry.gov.au/resource/UpstreamPetroleum/AustralianLiquefiedNaturalGas/Pages/Australian-Domestic-Gas-Security-Mechanism.aspx

than just the gas supply or gas price. The gas industry already supplies gas into the electricity market in response to sudden outages – but the electricity market has been badly exposed by recent closures of coal-fired stations and over-reliance on renewable sources, as demonstrated, for example, by events in South Australia last year[6].

It is simplistic to think that the LNG markets are solely responsible for the east coast "gas crisis" by extracting large volumes of gas from the domestic market and that if that was stopped, all would be well in the world of gas supply and gas price. The CSG LNG market exists because the domestic gas market is relatively small, with limited growth opportunities and therefore no huge incentives to provide further supplies. So it is arguable whether the gas being exported would in fact have been developed without an export market to supply. This is demonstrated by the graph below, extracted from the Finkel review which shows a reasonably consistent gas consumption across the three domestic uses, but especially industrial and domestic uses.

Figure 1 Total annual gas consumption by sector (historical and forecast) (ex- Figure 4.6, page 113 Finkel)



If we look at prices, many of the industrial users who came off long-term contracts at extremely low prices cannot expect those prices to be replicated, irrespective of whether there is an export industry or not. The cost of extracting the gas has increased, as have most costs, including transportation costs. Pipelines take a long time and a lot of money to develop, and foundation suppliers and customers that justify the effort are not that easy to come by. Yes, "*build it and they will (probably) come*" but you can't underpin the sort of expense involved in a pipeline project with that philosophy. And every project has got more difficult with additional regulations, more compliance, more reporting and higher fees – and that includes finding and extracting the gas, transporting the gas and selling the gas. Unless there are going to be subsidies involved, it is difficult to see how gas can be made available domestically for any less than export parity.

[6] Discussed in Tenure Matters Issue 27 August 2016

Meanwhile, the predictions by the Australian Energy Market Operator (AMEO) of a gas shortfall, which arguably sparked off the ADGSD, have been reviewed by two widely divergent groups. The Wilderness Society commissioned a report from the Australian-German Climate and Energy College[7] which argues that the AMEO predictions were wrong and that Australia has a gas price crisis, not a gas supply crisis. They argue that more developments will not result in substantially lower gas prices below the export parity price and are therefore unnecessary[8]. Instead we should embrace renewable energy, such as solar and wind, which are "*now producing power cheaper than gas"* (Really? I would love to see that data!). This is a not unsurprising stance from The Wilderness Society which does not want any more fossil fuel developments. Lock the Gate's stance that export gas controls were needed since they put Australian energy prices and security at risk[9], is another way of limiting more onshore development, and again is a not unsurprising stance for the group to take since they have been fighting on that front for several years.

The Australian Industry Group has reviewed the commissioned report, and although they agree with many of the facts, their take is that Australia is facing a dramatic energy crisis and needs more gas supply[10]. Gas is a critical feedstock for many industries, for which there is no real substitution option, so irrespective of any developments and improvements in renewable energy, gas is still required by certain industries.

AMEO's revised outlook suggests that all regions of the NEM will meet the reliability standard for the next 2 years, thereby obviating any need for LNG export controls. APPEA's position[11] is that the AGDSM will potentially discourage further investment in new gas supply, thereby exacerbating the "problem" it is attempting to solve. The existence of export controls certainly increases sovereign risk which has already taken quite a few hits over the last few years with changes to legislation and policy and ad hoc moratoriums and bans being applied. Science plays no part in many of these decisions, only party policies that pander to the green vote – meaning this is a battle replayed in almost every election.

And in one of the best examples of hypocrisy seen in this whole debate, the Victorian government who have banned all onshore gas exploration, including conventional resources, wants even tougher export restrictions to protect its industrial and domestic users BUT will apparently happily take the gas produced in other States including unconventional gas – a classic "not in my backyard" response from the Victorian government. Whatever happened to "*as you sow, so shall you reap*"??

Add to the mix recent suggestions by the Federal Treasurer that GST[12] may be used to 'threaten' the states and territories who are limiting gas exploration (only South Australia and Queensland do not have some form of limit on fraccing or gas exploration); and APPEA's suggestion that all royalties for onshore and offshore gas, whether conventional or unconventional, be excluded from the calculation of revenues for GST distribution purposes. The aim is to incentivise the development of each state's or territory's resources, but the suggestions have been met with the expected furore from Lock the Gate and Greenpeace.

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[7] http://climate-energy-college.org/

[8] http://www.energynewsbulletin.net/energynewsbulletin/news/1142586/gas-fears-overblown-report

[9] http://www.energynewsbulletin.net/energynewsbulletin/news/1143233/appea-claims-aemo-vindication

[10] http://www.energynewsbulletin.net/energynewsbulletin/news/1142664/gas-crisis-real-ai

[11] https://www.appea.com.au/media_release/no-need-for-gas-export-controls/

[12] http://www.energynewsbulletin.net/energynewsbulletin/news/1143553/morrison-weaponises-gst

And in the midst of all this, the Finkel review (*Independent Review into the Future Security of the National Electricity Market*) was released on 9 June 2017. The report outlines three pillars to achieve four key benefits (future reliability, increased security, rewarding consumers and lower emissions) for the electricity system:

1. **Orderly transition measures**, including a Clean Energy Target to reduce emissions while supporting security and reliability, notices of closure from existing large electricity generators, obligations on new generators to provide essential services to maintain voltage and frequency;
2. **System planning**, recommends a system-wide grid plan to inform network investment decisions and ensure security;
3. **Stronger governance** calls for a new Energy Security Board to drive implementation of the blueprint and deliver an annual health check.

The Finkel review has suggested that gas and renewables are the fuels of the future- with gas having the ability to provide reliable low-emission substitute for coal-fired generation with a security of supply that cannot currently be met by the intermittent renewable generation. *"Access to a reliable and affordable gas supply is in the interest of all Australians for its direct use for heating, as a feedstock chemical for industrial processes and as a fuel for electricity generation. In the NEM, gas-fired generation can provide a reliable, low emissions substitute for ageing coal-fired generation, and can provide essential security services to complement variable renewable electricity (VRE) generation.[13]"*

The review states that government policy and regulatory settings should facilitate new investment and enable the development of Australia's gas resources and address community concern about the environmental and social impacts associated with unconventional gas. That includes freeing up the resources currently ring-fenced by moratoriums and bans. No-one is going to invest in gas-fired generation with gas moratoriums or bans in place. And let's stop subsidising renewables – a practice which impacts on the economics of low-emission thermal energy such as gas or clean coal.

Our "gas crisis" hasn't been caused by LNG exports – at least not directly – but by poor policy decisions aimed to appease vested interests and win short-term political advantage. However, the scale of CSG-LNG did attract the attention of the likes of Lock the Gate, with their well-orchestrated anti-gas campaign from which there has been significant fall-out.

I am happy to hear suggestions about topics you would like covered. Feel free to email me at sue.slater@rlms.com.au with the subject heading Tenure Matters.

In the meantime, remember "Tenures make the Project; the Project doesn't make the Tenures".

RLMS covers the project spectrum from planning through to State and Federal government approvals, including land access, compensation, environmental impact statements and work schedules for clients ranging from entrepreneurs to major corporations, from start-ups to government agencies, and state significant projects such as Queensland's LNG giants. Contact RLMS at:

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[13] http://www.environment.gov.au/system/files/resources/1d6b0464-6162-4223-ac08-3395a6b1c7fa/files/electricity-market-review-final-report.pdf

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