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Gas Market Consultation
Department of Climate Change, Energy, the Environment and Water

**Mandatory Code of Conduct for the East Coast Gas Market – Chemistry Australia submission**

## Preamble

1. Chemistry Australia welcomes the opportunity to provide this submission on the consultation paper – Mandatory Code of Conduct for the East Coast Gas Market (the Code).

2. Broadly Chemistry Australia agrees with the policy objectives outlined in the paper enabling a fundamental re-set of the domestic gas market for the long-term benefit of consumers and the long-term security of the national economy at a time of significant geo-political change. The draft mandatory code represents a welcome step-change in domestic gas and energy policy long needed and long identified as a key part of structural manufacturing reform. This includes re-balancing market power between gas suppliers and users, enabling reasonable domestic market price and supply outcomes to be governed by domestic factors, and improving depth, liquidity and transparency to the benefit of both gas suppliers and users. These are key elements required to restore a confident, stable domestic market in the longer term. This includes the role of gas as a transition fuel also supporting increased electrification via peaking plants with the retirement of coal-fired generation assets.

3. However, for a Mandatory Code of Conduct to enable and help deliver these objectives it requires several design areas to be further strengthened so that the market conduct areas of concern are, in fact, mandatory. The design of the draft Code contains inherent loopholes and other areas of weakness that ongoing market power concentration by producers, retailers and aggregators will continue, unabated, to exploit to the disadvantage of all gas users and the broader economic, social and environmental reforms the Government is seeking to achieve. For example:
   a. At $12 /GJ feedstock users contracting with gas producers are unlikely to have a long-term future in Australia. Given the multiple opportunities built into the Code for producers to avoid the price cap, a $12 anchor price will inherently default to a price floor. This is in contrast to the important aspirational objective of the Code to deliver the required depth and liquidity intended to reduce price. Producers should be producing and providing gas for the domestic market to ensure this occurs, including bringing existing holdings to market by enforcement of use it or lose it powers.

   b. At $20 - $40 /GJ other gas users contracting with retailers and aggregators will be similarly challenged in terms of viability. A Code that does not include retailers and aggregators, and deal with the market concentration and power they possess, will disadvantage smaller users with no other options available to them.

4. A truly functioning and competitive domestic market, and therefore suitable objectives for the Code to incorporate, include:
    a. Buyers receiving multiple offers for required contract lengths
    b. Supply exceeding demand
    c. 2P Reserves replacement outstripping Reserves depletion
    d. Increase in the number of active producers in the market that decreases market concentration, and
    e. Increased prevalence of longer term (3+ years) GSA's being struck.

5. Ultimately a successful outcome would be domestic gas prices similar to those in other countries that have large gas producing jurisdictions such as the USA, Middle East, Thailand and similar economies.

6. The Code's role is therefore vital given the ongoing challenges of endemic domestic market dysfunction experienced over recent years, resulting in a domestic gas crisis and highlighted by successive ACCC Interim Gas Market Reports. The Russian invasion of Ukraine has added additional dynamics and complexities, disrupted global energy markets and further contributed to sharp increases in both gas and electricity prices. It is both reasonable and foreseeable that these global supply dynamics and their volatility will be in place for the next decade with the potential to impact domestic market operations and further erode Australia's manufacturing base.

7. Chemistry Australia members use gas in two ways. Firstly, as a non-substitutable feedstock to produce gas-based commodities essential for secure domestic supply chains and able to contribute to decarbonisation and circularity objectives. Secondly, as non-substitutable energy sources to drive chemical processes in addition to heat, steam and other process needs. Long-term gas contracts are required to match and underpin the known 3 to 5- year re-investment 'turnaround' cycles of large-scale petrochemical facilities, costing approximately $50M.

8. Chemistry Australia members purchase gas in two ways. Large gas users purchase gas via contracts direct with gas producers. Smaller gas users, and the vast number of Chemistry Australia's value-chain partners, purchase gas via retailers and aggregators. Retailers and aggregators are arguably one of the largest block buyers of gas on the East Coast, with their own significant market power.

**Recommendations to further strengthen the Mandatory Code of Conduct**

Chemistry Australia recommends:

9. The Government holds fast to its policy intent of market reforms via balanced intervention in order to restore a functioning east coast domestic market. Reasonable price, supply and terms are critical to restoring a confident gas-based manufacturing investment environment needed to ensure sovereign manufacturing, secure domestic supply chains, de-carbonisation and circular economy objectives.

10. That for the avoidance of doubt, and to support the practical application of the Code in the market, that the definition of Regulated Gas in Part 1, Section 4 be applied including (b) consists of naturally occurring hydrocarbons, or a naturally occurring mixture of hydrocarbons and non-hydrocarbons, the principal constituent of which is methane.

11. The review process be ongoing and be alert to changing market dynamics in addition to the current set of issues the Code seeks to remedy. A $12 gas price still provides significant challenges for Australian industry to be globally competitive. The review process should factor in the need for both users and suppliers to obtain a reasonable rate of return, consistent with the National Gas Objective. Experience teaches that Government referenced prices quickly become market price floors. However, $12 operating as a true price cap has potential to signal to suppliers that depth, liquidity, competition, transparency and governance influence future market pricing, but only if there are no loopholes, exemptions or other mechanisms available to be exploited.

12. Further strengthening of the 6 monthly published reporting of uncontracted gas that will be available. This should include:
    a. How long the gas has been held in tenements to support action on use-it or lose it factors constraining supply
    b. Information that will assist the ACCC and other regulators to understand the costs of bringing the gas to market and the reasonableness of the pricing offered
    c. The term availability of the gas to better facilitate longer-term contracts (ie rather than 6 month increments)
    d. Any data or other materiality alignment required with the quarterly reporting of sufficiency for ADGSM reviews.

13. That the Code enables identification of gas for long-term contracts. Long-term contracts have been challenging to achieve given the market dynamics of recent years. At best 2 years of gas has been made available, well short of the 3-to-5-year plant turnaround re-investment cycles typical across the industry. One mechanism that may help achieve this objective is for the Code to enable the potential allocation of gas for term contracts from unallocated volumes as part of the 6 monthly reporting.

14. That the Mandatory Code also covers retailers and aggregators, given the large amounts of gas traded and the large amount of market power they hold, with the ability to exercise that power over smaller users with little or no alternatives. Smaller buyers in the 1-3 PJ market are generally unable to participate in the bilateral negotiating space for a range of reasons and need to default to retailers and aggregators. The Governments' policy objectives are unlikely to be fully met without specifically ensuring this portion of the market is under the influence of the Code.

    A suitable price cap, governance and transparency arrangements applied on retailers and aggregators would operate in the same way these reform elements should operate for wholesalers. Currently we understand this significant part of the market is operating with pricing in the range of $20-$40 / GJ - a disproportionally large mark-up. The alternative is that retail customers continue to be subject to unreasonable pricing and supply with no certainty that this is resolved, other than the consultation paper's aspiration of improved domestic supply lowering retail pricing. Experience clearly demonstrates that low East Coast prices don't automatically follow increased volume without proportional regulatory support.

    This could be achieved in a number of ways including:
    a. a staged approach where the first year of Code operation consolidates functionality in relation to gas producers, including identifying lessons that would be used to automatically bring in the retail sector in the second year of operation. In this way, all

gas users would have the benefit of market certainty from proportional regulatory support to underpin reasonable gas supply and price

   b. a mechanism whereby evidence that retailers / aggregators are exercising market power triggers a regulatory response. This might include a suitably time-bound arbitration model or suitable penalty
   c. The capability to introduce collective industry bargaining to design in greater market power balance and disincentivize retailers / aggregators exercising market power.

15. That no automatic exemption be provided to small producers, or those not exporting. Experience demonstrates these players are likely to align pricing with LNG export pricing in the first instance, rather than the $12 price cap. Further compounding the price and supply risks to users, these players, as noted in the consultation paper, often sell to retailers, who then sell to industrial and other users. These cumulative factors compound to increase pricing well beyond $12.

16. The Government review the exemptions provisions to ensure they don't provide conduct loopholes able to derail the policy intent and market requirements. If and when exemptions do occur there should be full and rigorous public transparency throughout each process stage for each specific exemption.

17. That bilateral and buyer led EOIs are allowed that encourage producers to respond in direct negotiations outside a producer EOI process. It is reasonable to expect that good faith terms on producers also extend to them responding to Buyer EOIs and requests for offers.

18. That for gas to be offered in good faith that it needs to be offered at major trade points, such as Wallumbilla high pressure trade point, Moomba, Sydney STTM and the like.

19. That uncontracted gas from producers should commence from 1 July 2023, to enable any new GSAs to be developed for calendar year 2024.

20. That anti-avoidance provisions monitor the level of spot market sales and transactions less than 12 months durations, which are not yet covered by the Code.

21. That the ACCC and other regulatory agencies be suitably resourced to ensure they are able to deliver the Government's policy intent.

Please let me know if you require any additional information or clarification.

Your sincerely,

Peter Bury
Director – Strategy, Energy and Research