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Domestic Gas Reservation Scheme
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Chemistry Australia submission to the Domestic Gas Reservation Scheme Draft Design Framework

1. Executive Summary

Chemistry Australia supports the introduction of the Commonwealth Government's domestic gas market reforms with a Domestic Gas Reservation Scheme (DGRS) and Domestic Supply Obligation (DSO). The reforms acknowledge a fundamental reality: Australian households and chemical manufacturers should benefit from Australia's abundant natural gas resources, and domestic gas supply security.

The reforms provide the opportunity to rebalance domestic needs with export needs and obtain the maximum benefit from the abundance of gas in Australia. This includes being a reliable supplier coupled with affordable gas pricing to its Australian domestic markets for critical chemicals and sovereign manufacturing, and also meeting export needs of international markets for energy.

The Government approach creates a functioning domestic gas market through increasing domestic gas availability, strengthening market liquidity, supporting long term (5 -7-10 year) supply arrangements, and placing downward pressure on prices to achieve a sub $10 domestic gas price.

Chemistry Australia requires that gas is sold into the domestic market as opposed to the gas being merely "offered". This ensures the domestic market is not a secondary market to the export market, where surplus gas can be offered at prices that are not affordable and then exported on spot.

Providing affordable gas creates an environment for new investment in gas-based chemical manufacturing at existing facilities, as well as plants that have been mothballed being able to be re-started. Long-term contracts for chemical manufacturing provide investment certainty for producers and consumers.

2. Gas is Fundamental to Australia's Critical Chemicals and Sovereign Chemical Manufacturing Capability

Gas policy must be viewed not simply as an energy policy issue, but as a national economic security, productivity and sovereign capability issue for the country. The issue is of critical importance to the future of the Australian chemicals manufacturing sector in particular.

Natural gas is an essential feedstock and energy source for many industries that cannot presently substitute away from gas in the short to medium term. It is critical for the manufacture of fertilisers, industrial chemicals, explosives, mining reagents, plastics, crop protection, packaging materials, cleaning and hygiene products, personal care products, food processing inputs and numerous other critical products used throughout the Australian economy.

The chemistry sector demonstrates the exceptional value generated from domestic gas utilisation. According to analysis referenced by Chemistry Australia[1], the chemistry industry contributes approximately $286 million in economic output and supports over 1,600 full-time jobs for every petajoule (PJ) of gas consumed. By comparison, LNG exports contribute approximately $8.7 million and around 20 jobs per PJ consumed.

Australia's economic resilience increasingly depends upon maintaining local industrial chemical manufacturing capability in strategically important sectors. Recent geopolitical instability, supply chain disruption, and emerging national security challenges have reinforced the need for reliable domestic chemical manufacturing and production capacity to produce fertilisers, explosives, polymers and industrial gases.

Affordable gas via five to ten year long-term contracts underpins ongoing chemical manufacturing.

Many of the large industrial chemical manufacturers produce not only primary products such as ammonium nitrate, urea and hydrogen peroxide but also create by-product, derivative chemicals that are critical to everyday operations in medicine, housing and transport across regional and urban Australia. Natural gas is an enabler of a range of critical chemicals that underpin the economy now and into the future.

Natural gas creates value from heavy industrial and chemical manufacturing plants, ranging from small family operations to world-scale facilities and supports the following industries:

- Agricultural - fertilizer production, crop protection
- Mining and mineral processing - explosives and processing reagents
- Food security - packaging and processing inputs
- Defence - industrial chemical manufacturing
- Energy - advanced materials and manufacturing
- Medical – oxygen, disinfectants and sterilisation
- Highly skilled jobs - regional employment and investment.

A functioning domestic gas reservation framework supported by gas producers and chemical

[1] Chemical Industry Economic Analysis, Acil Allen, 2019

manufacturers is critical for securing and building this sovereign industrial and chemical manufacturing capability, providing a more resilient economy.

3. A DGRS for chemical manufacturing and future gas supply investment

A DGRS underpinned by long term contracts provides the foundation for much-needed investment certainty in upstream gas market development and downstream gas-based chemical manufacturing.

Investment opportunities are available at existing manufacturing facilities, and at plants that have been mothballed and can be re-started. These provide mutual benefit for gas suppliers, chemical manufacturers, employment, and the domestic economy.

There are Australian and international chemical manufacturers that will consider restarting and investing in onshore chemical manufacturing with an affordable domestic gas price on long term contracts.

4. Chemistry Australia supports the following

a. The Domestic Gas Reservation Scheme via an annual, licensed Domestic Supply Obligation (DSO) process set at 20% of export amounts, which recognises the current West Coast market arrangements and provides clarity for West Coast users.

b. The DGRS increases market liquidity and places downward pressure on prices

c. The DGRS includes increased market reforms within the Gas Market Code, including the requirement that gas is sold, not just offered

d. The DGRS will be regulated by the Australian Energy Regulator (AER) under new Federal legislation and subordinate regulations.

5. Chemistry Australia recommends six key actions

There are six fundamental actions now required to deliver a DGRS and DSO and meet the needs of chemical manufacturers and other large industrial users.

1. **Inclusion of an explicit price marker to reflect globally competitive domestic pricing, for a five year period as the east coast domestic gas market is established. The current reforms seek to create downward pressure on prices.**

Affordable price underpins affordable investment in gas-based manufacturing. Downward pressure on pricing reflecting sub $10 per PJ remains a critical outcome to ensure both investment and supply chain resilience.

Chemistry Australia recommend

a. that a transparent domestic gas prices series is created on gas production cost estimates, coupled with the AER developing a clear guideline for domestic gas pricing. This pricing approach must align with the DSO requirements.

b. The government should therefore consider a price marker that retains and defines 'reasonableness'.

2. Stronger focus, and process certainty, on enabling long-term contracts of five to ten years required by chemical manufacturers.

Manufacturing investment requires certainty over five to ten-year periods. However, the proposed DSO framework operates through annual processes which do not align with industrial chemical manufacturing investment cycles.

Gas exporters have long-term gas contracts to provide certainty for international customers and enable investment in gas field development to underpin contracts.

Chemistry Australia recommend

a. the same approach is undertaken by Australian gas producers having long-term contracts with Australian industrial chemical manufacturers, to support future Australian gas developments.

The benefit to the Australian economy is through large industrial manufacturers being able to reinvest in their plants and importantly support the chemicals sectors with by-products such as oxygen, CO2 and Ad Blue that under pin the resilience of the medical, food and transport industries.

Chemistry Australia recommend

a. a Gas Supply Agreement Register for large industrial / chemical manufacturers / users, managed by the AER, to align plant turnaround demand with longer term supply requirements. These 20 – 30 industrial and chemical manufacturing plants consume consistent annual volumes, with turnarounds at regular, rolling intervals, based on safety and reliability.

b. Any access by producers for gas through the release valve mechanism must be specifically tied to the commitment of long-term contracts for industrial chemical manufacturers and other industrial users.

3. Ensuring a clear disconnect of the domestic market supply from export markets.

The DGRS currently only includes the DSO having a Minimum Liquidity requirement to support a modest oversupply.

The reforms improve domestic supply but stop short of fully decoupling domestic and LNG export markets. Domestic markets should not be residual to export markets.

Chemistry Australia recommend

a. The proposed release-valve mechanism allowing domestic surplus gas to be exported risks maintaining current market tightness and preserving pricing outcomes linked to export markets and must be excluded from legislation.

b. The DGRS proposes the ACCC maintaining LNG netback series for five years using Brent Crude. This LNG series is irrelevant and must be removed, as it continues to maintain a link between domestic and LNG pricing structures.

4. Locking in the key scheme design features

The DGRS design features will underpin gas feedstock manufacturing investment. Investment certainty will be strengthened by ensuring key features are locked in, excluding any exemptions or other variations that dilute the intended outcomes.

Chemistry Australia recommend

a) The 20% DSO is maintained in the scheme design, not reduced
b) The obligation to supply, not just offer, enshrined within the scheme design and its mechanisms
c) No compliance exemptions for supply obligation permitted under the scheme
d) Formalised inclusion of a customer advisory panel is required to support the development of the legislation, in an ongoing capacity, to ensure the DGRS is functioning properly, and meeting the requirements of customers. This should also cover a formal right to provide input on any and all individual DSO variation and release valve applications.

The DGRS applies nationally with state and territory government consultations to ensure policy objectives are achieved, and existing regulatory arrangements, such as domestic supply obligations under state-based schemes, are recognised. Greater certainty is required for West Coast users, given the different features of West Coast and East Coast markets.

Chemistry Australia recommend

a) The DGRS recognise the structural separation of East Coast and West Coast markets and differing market characteristics
b) That consultation with major industrial users is included as part of framework design.

5. Use it or lose it

Concerns remain regarding the ability of producers to strategically manage Domestic Supply Obligations.

Chemistry Australia recommend

Where the resistance exists to bring required gas volumes to market and meet forward supply obligations, the Government should clarify its ability to apply 'Use it or Lose it' provisions.

6. Targeted support for sovereign chemical manufacturing Industries

The Review recognises that some strategically important high energy / feedstock chemical manufacturers may still require targeted measures if DGRS alone cannot deliver.

The preference is to develop a properly functioning domestic gas market. The DGRS framework needs to address how long-term contracts can support gas feedstock / chemical manufacturers who are critical to the chemical sector with many of their derivative chemicals.

Should the Government's DGRS and DSO not deliver affordable gas and long-term contracts,

then other options will need to be considered.

Closure of Australian critical chemical manufacturing facilities is not in the long-term interests of economic resilience due to unaffordable gas supplies and short-term contracts.

Chemistry Australia notes the increasing volumes of gas required by data centres for electricity supply, and that existing gas-based manufacturing needs to be secured into the future, prior to new demand requirements.

Conclusion

The Domestic Gas Reservation Scheme acknowledges that domestic gas users require secure access to Australia's gas resources at affordable prices at sub $10/PJ and that structural reforms are required to ensure industrial chemical manufacturing continues to support the resilience of Australia to deliver the essential products for our major export industries of mining, agriculture, and food, as well as the continued daily operation of medical, fast moving consumer goods and transport related activities.

The success of the reservation framework should ultimately be measured not only by volumes reserved and sold, but by whether Australia retains and invests in the chemical manufacturing sector to transform gas into high-value manufacturing, employment, innovation and national resilience. This includes securing Australia's existing critical chemicals capability as a foundation for strengthening supply chain resilience in key products that underpin the economy.

Australia has the gas resources. The opportunity now is to ensure those resources deliver enduring national benefit through a stronger, more competitive and sustainable domestic chemical manufacturing sector.

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