REPORT OF PROCEEDINGS BEFORE

COMMITTEE ON THE SUPPLY AND COST OF GAS AND LIQUID FUELS IN NEW SOUTH WALES

INQUIRY INTO THE SUPPLY AND COST OF GAS AND LIQUID FUELS IN NEW SOUTH WALES

At Sydney on Monday 2 February 2015

CORRECTED

The Committee met at 9.30 a.m.

PRESENT

The Hon. R. Borsak (Chair)

Mr J. Buckingham (Deputy Chair)
The Hon. N. Blair
Mr S. MacDonald
The Hon. P. Phelps
The Hon. A. Searle
The Hon. M. Veitch

CHAIR: Welcome to the second hearing of the Select Committee into the Supply and Cost of Gas and Liquid Fuels in New South Wales. The inquiry is examining gas and liquid fuels supply, cost and availability in New South Wales. Before I commence, I acknowledge the Gadigal people who are the traditional custodians of this land. I also pay respect to the elders past and present of the Eora nation and extend that respect to other Aboriginals present.

Today is the second and final hearing day we plan to hold for this inquiry. We will hear today from the NSW Business Chamber, the Australian Workers Union, CSR Limited, the Australian Pipeline Industry Association, the Public Interest Advocacy Centre, the Energy Supply Association of Australia and the Australian Petroleum Production and Exploration Association.

I will make some brief comments about the procedures of today's hearing. In accordance with the broadcasting guidelines, while members of the media may film or record Committee members and witnesses, people in the public gallery should not be the primary focus of any filming or photography. I remind media representatives that you must take responsibility for what you publish about the Committee's proceedings. It is important to remember that parliamentary privilege does not apply to what witnesses may say outside their evidence at the hearing.

I urge witnesses to be careful about any comments they may make to the media or to others after they complete their evidence as such comments would not be protected by parliamentary privilege if another person decided to take action for defamation. The guidelines for broadcast of proceedings are available from the secretariat. There may be some questions that witnesses can only answer if they had more time or with certain documents to hand. In those circumstances, witnesses are advised that they may take a question on notice.

Given the short time frame for this inquiry, we are asking witnesses to provide answers within seven days. We would appreciate your help in assisting us to meet our reporting deadline. Witnesses are advised that any messages should be delivered to the Committee members through Committee staff. I ask everyone to please turn off their mobile phones for the duration of the hearing.

PAUL ORTON, Director, Policy and Advocacy, NSW Business Chamber, sworn and examined:

LARISSA CASSIDY, Policy Adviser, NSW Business Chamber, affirmed and examined:

CHAIR: Would you like to start by making a short statement?

Mr ORTON: Yes. The NSW Business Chamber is concerned about this issue because it represents roughly 17,000 businesses across New South Wales, businesses of all shapes and sizes in all locations, north, south, east and west. We are concerned that industry could be facing gas price increases beyond those that might be expected from exposure to international markets and further, that supply shortages are in prospect. Both of these risks would be reduced as soon as New South Wales gas reserves come into production.

Both supply and pricing uncertainty add to the cost of operating in New South Wales, with little capacity to recover them. They contribute to additional uncertainty about the operating environment. These, in turn, lead to reduced business confidence, reduced expansion plans and, at worst, reduced employment. In support of that observation, the Chamber has just released its quarterly Business Conditions Survey today which does show, while there is an increase in sales revenue or an increase in the number of firms reporting increased sales revenue, there is also increased concern about costs and increased concern about profits. So profits are down; costs are up. And there is also, I guess, some concern about the overall economic outlook. Gas prices in New South Wales are increasing partly because the costs of extraction and transport are increasing but also because the eastern Australian gas market is, as we all know, increasingly being exposed to international prices.

Supply is constrained in New South Wales because existing sources of gas are running out. New South Wales has not developed its indigenous gas resources, although new gas resources in Queensland are being developed for export markets. Estimates by the Australian Energy Market Operator and others suggest that supply shortages could occur in New South Wales any time between 2016 and 2018.

All this adds up to employment and growth constraints if New South Wales does not quickly develop its own gas resources. This means getting on with the Government's Gas Plan and acting consistently with the findings of the Chief Scientist's report, to enable the fair and safe development of New South Wales' gas reserves. The genie is out of the bottle in that exposure to the international gas market cannot be reversed. Reservation policy, we believe, is impractical as New South Wales gas is still in the ground and the other States that supply us are not going to voluntarily accept a hit to their revenues implied by a domestic reservation policy. Apart from this, there is enough evidence in Western Australia, for example, to support severe reservations about reservations policies actually working because prices have gone up and really, in our estimation they are likely to have the opposite effect to that intended.

Our key point is that the looming gas shortage and price pressures are adding to uncertainty and cost increases for manufacturing and other industry at a time when confidence is demonstrably fragile. This will impact employment and investment in new capacity and new business. That is why we are concerned to see a gas plan implemented and new sources of supply brought on stream as quickly as possible, consistent with safe standards of extraction. Thank you.

The Hon. MICK VEITCH: I think that was a prepared statement. Is it possible to have that statement tabled?

CHAIR: Yes.

Document tabled.

The Hon. MICK VEITCH: In your submission, in item C, you talk about the domestic gas market and the need for continuing reform. In particular, you talk about the contracts and issues around price discovery. It has been suggested to the Committee that we should recommend legislation for full transparency around gas supply contracts. Could you give the Chamber's view on that?

Mr ORTON: We need to recognise that the gas market is different to the electricity market and it has historically been a case of gas producers negotiating directly with one or maybe two retailers and/or major consumers. So it is not like electricity, where it is easier to pool both suppliers and those who demand it. But it is true that more transparency around that issue would be good. I might ask my colleague to reflect on some of the feedback we have had from members we have been talking to about these issues.

Ms CASSIDY: Certainly many have raised the issue of contracts and the problems they face. Many have perceived little competition among the contracts that they have been offered by retailers and many cite that they provide them with insufficient flexibility for their business operations, so they say take-or-pay provisions are often in their contracts with retailers. I think the Federal Government has done a bit of work on looking at issues around transparency and we fully support ongoing work in this area to see what the most appropriate way to increase transparency is.

Mr ORTON: In summary, we do see it as an issue but we are not convinced yet that legislation is required to deal with it.

The Hon. MICK VEITCH: How do you see it working?

Mr ORTON: We need to review the action that the Federal Government has under way to review some of these issues and we do not want to do something that constrains the gas producers' desire and motivation to explore and extract new gas reserves. I think we do agree that price discovery is a key issue.

The Hon. MICK VEITCH: In a nutshell, you are saying yes, there should be greater transparency around the contracts but you are reserving your position just yet on how that would work.

Mr ORTON: Yes, correct.

The Hon. ADAM SEARLE: You mentioned that gas prices were increasing due to extraction costs rising. That is before these historic long-term contracts expire. How do we know that the increases that are being projected are not the result of the other factors you have mentioned, such as exposure to the international market, as opposed to just rent-seeking by producers, because there is a lack of competition in both production, distribution and also in retailing gas?

Mr ORTON: I think we have to be reassured to some extent that one of the benefits of exposure to international markets should mean that there is pressure on producers to deliver gas at efficient prices. And I think the overall level of knowledge and research about the sector and indeed, knowledge on the part of consumers about the sector, definitely needs to be improved. I think one of the things we did pick up from the members that we have been talking to is that they know a lot less about the gas market than they do about electricity markets and I think there is a fair bit of education required to help make gas consumers more demanding consumers than might currently be the case.

The Hon. ADAM SEARLE: You mentioned producers being encouraged to produce efficiently but the evidence we have received and just from general reading, Australia has had historically relatively low gas prices for consumers, whether industrial or domestic. That is now going up, even before the Queensland trains are exposed to the international market. You say one of the benefits of exposure to international market forces is efficiency but, in fact, we have had historic low prices which now seem to be over and exposure to these international markets seems to be working against prices going down. In fact, at least on some of your evidence, it is one of the causes of prices going up.

Mr ORTON: I think the inevitable nature of the world is that costs continually go up and I think the producers have provided evidence of both transport, labour and capital costs increasing and I think there is not much that can be done about that.

The Hon. ADAM SEARLE: Except some of the prices—I think IPART allowed AGL to increase its prices by something like 17 per cent, is that right, the last IPART review?

Mr JEREMY BUCKINGHAM: Yes.

The Hon. ADAM SEARLE: But wages have not gone up by 17 per cent.

Mr ORTON: I think one of the reasons for being somewhat more enthused than others might be about exploiting New South Wales' gas reserves in a safe manner is that the more supply we have entering the market, the more downwards pressure there is on costs and pricing. And really, we would be expecting increased supply to produce downward pressure on pricing.

The Hon. ADAM SEARLE: Just exploring that, how does that work? At the moment, there seems to be more supply than ever before in Australia as a whole and yet prices are going up. Even if there was sufficiently expanded production, how do we know that that new resource would not just be sold to the highest bidder, including offshore?

Mr ORTON: I think you have also heard evidence that that is not easily achievable in the short-term. There are limitations to the LNG gas trains that would require more demand than is available domestically to justify it. I do not think we can assume that there is an absolute immediate flow-through from domestic extraction to global markets. More supply should mean more pressure on domestic prices and that is why, certainly if we do not do anything about that, things are not going to get any better.

The Hon. ADAM SEARLE: I know that is the economic theory but let us look at what the Australian Energy Market operator says. It describes decreasing demand in the last few years and it projects further decreases in demand for both industrial and residential users. Basic economics usually says, if there is less demand for a good, prices should go down and yet prices inexorably are going up. How can we have any assurance that increased supply would lead to downward pressure on prices?

Mr ORTON: We do not subscribe to the downward spiral, never-ending decrease in demand scenario.

The Hon. ADAM SEARLE: That is not what I said. I was talking about the AEMO projections which are for modest continuing declines.

Mr ORTON: The question was?

The Hon. ADAM SEARLE: Usually when there is more demand for a good, prices go up; and when there is less demand for a good or service, prices go down. In the last few years there have been decreases in demand for gas for both industrial and domestic users and the Australian Energy Market Operator predicts further decreases in demand and yet prices are inexorably going up and are projected to go up further. How can we have any confidence that more supply will have any impact on prices, given the real-world track record of experience?

Mr ORTON: I think we can be confident that in the presence of greater supply the likelihood of prices going up will be less than it would be if we do nothing.

The Hon. MICK VEITCH: In your submission you talk about long-term contracts continuing as the main operating tool. We heard evidence last week that there is a move towards shorter term contracts. I am interested in your views around the pros and cons of the shorter term contract scenario as opposed to the current long-term contracts.

Ms CASSIDY: I think it was the Australian Energy Market Commission that said it still expects that long-term contracts will still be very much a function of the market but notwithstanding there might be some move to more short-term contracts. In terms of our members' points of view, one of the key comments that pretty much everyone has agreed on is that a long-term known price path is very important for their business modelling and their operations. Obviously, the long-term contracts provide a much more certain price path whereas the short-term contracts take away some of this price certainty going forward. In terms of the biggest pros and cons, that is one of them.

The Hon. MICK VEITCH: Short-term contracts would lend themselves to price volatility?

Ms CASSIDY: Absolutely, yes.

The Hon. MICK VEITCH: But if the market is moving towards shorter term contracts does that not lend itself to a need to be a bit more transparent about the contracts so that people have more of an understanding of pricing?

Mr ORTON: It does. That was one of our recommendations in our submission. The concern is that as the eastern gas market transitions to an export focus there will be in that transitional period greater volatility and therefore a need for greater transparency and a need to be educating gas consumers about the market, how it works and what others are paying.

The Hon. MICK VEITCH: At the last hearing we heard from the Minister that there is in fact a great degree of difficulty determining at any given time how much gas is in the system. Do you have views around how we could rectify that issue or at least make the gas information available to consumers? I am happy for you to take that on notice.

Mr ORTON: We will take it on notice.

Mr JEREMY BUCKINGHAM: Mr Orton, you said that your organisation expected gas prices to go beyond those you would expect from exposure to international pricing. Why is that and how could it be that we would be paying more for gas than you would expect on the international market? Are the major wholesalers and retailers using the potential export to gouge Australian and New South Wales businesses and gas users?

Mr ORTON: What I was alluding to was the point I made before. That is that in the transition to exposure to international forces there is much more uncertainty about the likely price path for gas. There is also uncertainty about the level of gas supply. Putting those together does raise the possibility of there being spikes in prices as the market adjusts. We are not suggesting there is likely to be a long-term outcome along those lines but we are in a transitional phase that both suppliers and users have not faced before. The issue of transparency and level of capacity to deal with both retailers and wholesalers really does come to the fore.

Mr JEREMY BUCKINGHAM: You said "as we make the transition". Haven't we already made the transition? Isn't that transition already in effect and your organisation, New South Wales businesses and government are playing catch-up to deal with this issue?

Mr ORTON: The development of New South Wales resources we would see as part of the transition to being exposed to the global market. Quite simply, if we do not develop our resources in New South Wales we are placing jobs and business in jeopardy. That genie is out of the bottle, we cannot reverse it and therefore we really do need to develop New South Wales gas resources to put a bit more certainty back into the market.

Mr JEREMY BUCKINGHAM: The decision to become a major exporter of gas out of the east coast was made at a Federal and State level nearly 10 years ago. Why is it that it is only now that the chamber is raising these issues? Why is it that we are only realising that the bottle has been uncorked? Why was this not raised at a strategic and policy level 10 years ago? Have you and New South Wales business been blindsided by these increases in gas?

Mr ORTON: I think it is a good question about the extent to which there has been public policy focus on these issues over that 10-year period. I think it is arguable possibly—as also has been the case in electricity—that there has been not nearly enough focus on what these changes might mean in reality. To a certain extent there is a bit of catch-up in recognising what these implications are.

Mr JEREMY BUCKINGHAM: You said that New South Wales should develop its indigenous reserves of gas to help alleviate price pressures. The largest gas reserves in New South Wales are in the Sydney Basin. Do you believe that the Sydney Basin should be developed for coal seam gas?

Mr ORTON: No, we do not have a view on particular areas that should be developed. I think that is why the Government's gas plan is one that should be implemented. It is really at the moment a case of getting the two projects that are on foot underway as soon as is reasonably possible.

Mr JEREMY BUCKINGHAM: From the testimony of the proponents, AGL and Santos, and according to your submission those projects are unlikely to be on line before the end of the decade. How is the development of an indigenous gas supply going to make any difference to businesses and gas users in New South Wales over the next five years? It is not, is it?

Mr ORTON: I think one of the vagaries in this whole debate is understanding these time lines. I have heard 2017-2018 in terms of when at least one of them comes on stream. I do not think we should get hung up on a year or two's difference. What really matters is whether these are developed or not. We need them developed as quickly as possible.

Mr JEREMY BUCKINGHAM: Your submission says 2018. I think we should get hung up on whether they are developed and the time line for them. Eastern Star Gas and Santos had plans for 1,100 wells in the Pilliga. That was supposed to come on line with a Government memorandum of understanding and be approved for development on 26 January. That has not happened. In the absence of a domestic coal seam gas [CSG] industry what policy alternatives are there?

Mr ORTON: I do not think we would agree that the absence of a domestic CSG policy is a sensible way to go forward. We have the reserves. They can be developed safely; the Chief Scientist has demonstrated that. Potentially they have the capacity to revitalise industry and business in New South Wales, particularly manufacturing, in the same way as has happened in the United States. It is an opportunity for employment that we cannot refrain from developing.

Mr JEREMY BUCKINGHAM: According to the Minister in his testimony the New South Wales Government's modelling that it commissioned said that a domestic or indigenous CSG supply in New South Wales would reduce prices by up to 3 per cent. Compare that with the fact that wholesale prices in New South Wales are going up by 100 to 200 per cent. What difference is that going to make at all to New South Wales businesses?

Mr ORTON: Like the old Sydney Water adage, every drop counts. I do not think we should be dismissing any percentage point potential reduction in prices. For our manufacturing members, every percentage point counts and it is on top of all the other cost base that they have to deal with. I think we have got to be realistic about that.

Mr JEREMY BUCKINGHAM: You think that a 3 per cent reduction to a 200 per cent increase is significant. What impact will New South Wales gas production have on international prices?

Mr ORTON: I am not too sure about that. The evidence seems to be that New South Wales gas is not easily diverted into the global LNG gas trains, but it does contribute to the overall level of gas supply that we have available for both domestic and international use.

Mr JEREMY BUCKINGHAM: Are you aware that there are already on the table pipeline proposals from north-eastern and north-western New South Wales to pipe gas into Queensland and the export LNG trains? Would that concern you? If a CSG industry was developed and the gas was diverted to export would you oppose that?

Mr ORTON: No, not in the face of a sensible New South Wales policy that developed our gas resources to their fullest and safe extent.

CHAIR: Turn your mind to the international situation at the moment. One of the key issues around why gas prices are going up is that we are being internationally exposed now through the LNG gas trains going to Gladstone. Do you see any medium to longer term effect of the decrease in oil prices and therefore energy in general on what is going to happen in New South Wales?

Mr ORTON: Obviously, it does have an impact on gas prices. The issue really though is to what extent will the current reduction in oil prices prove to be sustained. There is certainly a price war underway between OPEC and other producers. One of them is going to blink. Maybe one of them has blinked somewhat already. I think we need to be careful about assuming that the current reduction in prices is there for the long term.

CHAIR: If they are getting down to a pretty low price it is going to take a while for them to build up, especially with Europe slowing down. A lot of the shale oil capacity in the United States is not economic. Query whether coal seam gas in the end may be economic in New South Wales based on your own assumptions.

Mr ORTON: That obviously is a consideration. I guess it is one that the potential producers will need to take into account.

CHAIR: We have seen evidence of this perpetually spiralling price of gas but the economic situation regarding the price of oil and energy in general is starting to look the other way at the moment.

Mr ORTON: Yes.

CHAIR: No-one that we have heard from so far has started to factor that into their modelling. You talk about the need for the Government to plan to address gas shortages in New South Wales. Where in your view should we be drilling?

Mr ORTON: We do not have particular views about where we should be exploiting gas. That is something that should come from the deliberations that the State Government will be undertaking through its gas plan and taking into account its commitment to fully implement the recommendations of the Chief Scientist.

CHAIR: You are not wedded to any part of the State, except the Sydney Basin?

Mr ORTON: We are not particularly wedded to any sector of the State other than that we do need to do as much as we can as quickly as we can and as safely as we can to make use of our abundant gas resources.

CHAIR: If we develop a domestically feasible gas production industry why is gas reservation not a good thing?

Mr ORTON: Quite clearly, with New South Wales only providing 3 to 5 per cent of its own supply a gas reservation policy currently would effectively mean other States agreeing to it.

CHAIR: No, I said if we developed an industry. In other words, if you look at what AGL potentially could do at Gloucester and what could be done in the Pilliga and other parts of the State we could produce more than 100 per cent of our requirements. If we did that why would it not be a good idea for us to reserve that for New South Wales, even though we had commitments from AGL and, I think, Santos off their own bats to only supply New South Wales?

Mr ORTON: In the face of those commitments the evidence from Western Australia and other places—

CHAIR: Western Australia has a domestic gas reservation policy.

Mr ORTON: But prices have gone up.

CHAIR: But have they gone up as much as they would have gone up?

Mr ORTON: Arguably the reservation policy has constrained exploration and made it less attractive for those who are interested in finding and extracting gas resources. Why not wait and see whether or not we really need it and then with the commitments to companies that you mentioned, the difficulty in sending New South Wales resources through current LNG gas trains, the fact that a much greater resource than New South Wales would be required to justify it, to us there does not seem to be a need to do it. The last thing we need to do is to constrain exploration and extraction in New South Wales.

Mr SCOT MacDONALD: I think in your submission somewhere you said that it was difficult to get feedback from the small business sector; you talk to the larger users but small business was a bit harder to get a handle on. Can you give me, even if it is anecdotal, what would be the impact of the policy moratorium, which is a Greens and Labor policy, on the small business sector?

Mr ORTON: I think we need to recognise that gas users, manufacturing gas users, while Western Sydney I guess is the manufacturing heartland, the Hunter and Illawarra, there is also an extensive regional manufacturing sector from Tamworth, Dubbo, Wagga, Albury—

Mr SCOT MacDONALD: Griffith.

Mr ORTON: —Griffith, that also relies on gas supplies and which do form the backbone of employment in regional areas. I might ask my colleague to reflect on that one as well.

Ms CASSIDY: And also small businesses, as we refer in our submission, include people like drycleaners and fish and chip shop owners. So I think that ultimately, as we have discussed, the lack of a New South Wales supply should lead to prices higher than they would have been, and obviously this will be passed on.

Mr SCOT MacDONALD: For that small business sector?

Ms CASSIDY: This will be passed on through to the small business sector, as it would with households as well.

Mr SCOT MacDONALD: In your submission you talk about price discovery. I get the point you are making but why should the Government insert itself into a supplier/user relationship there?

Mr ORTON: Only as an absolute last resort, and I think one of the things we have been grappling with, as a small business representative body, is that small businesses frankly just do not have the time to spend in analysing energy markets in detail. That applies also to electricity. So there is an education and an assistance role here, I think, required of both us as an industry group—and we do have a number of projects underway in that area—but potentially also a government.

Mr SCOT MacDONALD: Is the supply side of it receptive to that? Are they coming to the table on those sorts of things? I think NSW Farmers is doing something similar, if my memory serves me right. Are the suppliers keen or not?

Mr ORTON: Absolutely. We have not discovered any reticence on their part in working with us. Whether they are keen or not, I am not so sure.

Mr SCOT MacDONALD: Towards the end of your submission you talk about targeted energy efficiency information tools, so it is a bit more than what you were just speaking about. Are there any recommendations you can make to us with a little bit more meat on the bone there?

Mr ORTON: The Government already has an energy efficiency program targeting small businesses. It also has a program through its sustainability advantage program targeting businesses' capacity to conserve energy. Those programs are currently being redeveloped, I understand. So I guess we would urge that the existing successful vehicles be built upon and developed further in conjunction with organisations like us and farmers and the others. In fact, we have been in discussion with Environment and Heritage with a view to doing a lot more in the education and, to a certain extent, hand holding.

Mr SCOT MacDONALD: Is it ease of use or is it time? What were the barriers or how could it be improved a little bit?

Mr ORTON: The improvement is that it needs to be introduced into existing discussions with small businesses; not somebody dreaming up some exciting energy efficiency gas market program, but rather integrating messages about how it works and how to use it in existing conversations that organisations like us already have with small businesses through local chambers of commerce right around the State.

The Hon. Dr PETER PHELPS: One of the arguments that have been put by opponents of CSG is that there is going to be a shortfall anyway over the next couple of years so we should not do anything because the shortfall is inevitable. Is that not simply kicking the can further down the road and that instead of having a short-term shortfall what you will have by not producing is a perpetual shortfall?

Mr ORTON: I think that is a pretty good description of the risk we face if we do not do something to use the reserves that New South Wales is blessed with. Just because we have got some issues at the moment we should not be assuming that that is an immutable pathway that cannot be changed. We only have the US example to see with its revival in manufacturing arising from its improved access to both gas and oil reserves. We used to be the Chamber of Manufactures in New South Wales; a big proportion of our members are manufacturers. New South Wales does have a manufacturing future and we should not be consigning that sector or its employees to the rubbish heap.

The Hon. Dr PETER PHELPS: I want to go through a little bit of micro economic theory now. If you assume that a company has to buy widgets which are then a wholesale price of $15 per widget, the average cost per widget for that company is $15, is it not?

Mr ORTON: Sorry, I missed the first part of your question there.

The Hon. Dr PETER PHELPS: If a supplier receives from a single source widgets at a cost of $15 per widget, the average cost is $15?

Mr ORTON: Yes.

The Hon. Dr PETER PHELPS: If it receives it from two sources, and let us say the cost per widget is $15 from one source and $5 from another sources, if you go 50/50 that is an average cost of $10 per widget, is it not?

Mr ORTON: Correct.

The Hon. Dr PETER PHELPS: So even though there is no guarantee that the retail price that that firm charges will be $10, $11 or $12, it is certainly going to be less than the minimum average cost that it requires if it is entirely a situation where you have to only buy at $15 per widget, is it not?

Mr ORTON: True.

The Hon. Dr PETER PHELPS: So bringing that analogy to New South Wales, if New South Wales gas retailers are absolutely constrained and can only buy on an international pricing market which is three times the domestic wholesale cost that it could produce for itself, that is going to have a very much deleterious effect on the retail price than it would if it could, for example, substitute 50 per cent of that input cost with the domestic rate, which is a third or less lower than the international price market. Is that true?

Mr ORTON: I think that is the way markets operate.

The Hon. Dr PETER PHELPS: So while there is no guarantee that they will retail at a significantly lower amount, it is absolutely true that the price pressure will be lower if you have a significant amount of local production which is able to be produced and sold at a wholesale cost lower than the international wholesale cost. Is that correct?

Mr ORTON: Correct, and that is why we need to exploit our gas reserves.

Mr JEREMY BUCKINGHAM: Why would they sell it cheaper?

The Hon. Dr PETER PHELPS: If you had been here you could have asked AGL that. But we did ask AGL that and it is part of their business model—they want to be a domestic supplier and that is their world view.

The Hon. NIALL BLAIR: Do you have any view around the infrastructure that is available in New South Wales? Obviously we are importing a lot of the gas through pipelines and, to a large degree, where that infrastructure is dictates where the manufacturers and where the major customers are. If you look at the town of Deniliquin, for example, in the Riverina, they would love to be able to have access to gas particularly coming up from Victoria or somewhere because they have a lot of industry down there that would be able to tap into it. Do you have any other views around that infrastructure that is in New South Wales and the potential for other people to access the gas?

Mr ORTON: Quite obviously we would like more people to have access to it, but I am not too sure to what extent the economics support that. But certainly transport costs are a key part of the overall pricing picture.

Mr SCOT MacDONALD: You mention the take or pay and the long-term contracts. Is the take or pay going to be more problematic in the new environment we are looking at? Take or pay might have been good when, let's say, it was a domestic industry, a domestic supply. Is take or pay going to be problematic in the future?

Mr ORTON: Potentially, but I guess that is really an artefact of the structure of the gas market in single extractors or wholesalers and very large customers.

Ms CASSIDY: I would just add that these are the sorts of things that we would like to see the Federal Government looking at.

Mr SCOT MacDONALD: We do not intervene in take or pay with coal loaders or wheat or anything like that. I was interested when you raised it as to why that is looming to be a problem.

Ms CASSIDY: I do not know that it is so much looming to be a problem; I just think it locks in manufacturers. If, for whatever other reason they do not need that gas they still have to pay for it.

Mr SCOT MacDONALD: Can I take away from that that you want more liquidity in the market?

Ms CASSIDY: I think as the gas market continues to mature, potentially these provisions may not be as necessary.

Mr JEREMY BUCKINGHAM: The submission says that in terms of industrial users in New South Wales "the Energy Users Association of Australia assessed different gas price scenarios, measuring their impact across high gas-using members, accounting for about 20 per cent of total gas used in the industrial sector in Australia" and that "by 2020 the industrial sector would see a loss of 3,300 jobs, foregone capital expenditure of 1.9 billion and a decrease in sales revenue of $2 billion". In your earlier testimony you said that it is very difficult to assess the impact on small businesses. But small businesses—laundromats, kitchens, restaurants, hotels, pubs, everyone—uses some form of gas. Do you think the State Government should urgently model the impact of higher gas prices on the small business sector in New South Wales?

Mr ORTON: It is true that because the use of gas is so pervasive, determining who is using what is somewhat difficult to do. But I am not too sure that it would add that much more to what we already know: that prices are going up and we need to do everything we can to moderate price increases given that energy in the form of electricity has already increased significantly. So I am not too sure what more that would tell us.

Mr JEREMY BUCKINGHAM: It will not tell us what businesses in New South Wales are viable with a 300 per cent increase in gas prices. Should we not know that? Should the Government not know, of the 17,000 businesses you represent and that are operating in New South Wales, how many of them are viable with a 300 per cent increase in gas prices? Should we not know that as well as how many jobs may be affected? The Australian Workers Union [AWU] is talking about hundreds of thousands of jobs. Ten jobs, 100 jobs, 1,000 jobs is a lot. Should we not know how many businesses in New South Wales are viable under a higher gas price scenario?

Mr ORTON: I think the key issue is that we need to be developing our resources as quickly as we can to boost supply. I think we can—

Mr JEREMY BUCKINGHAM: But that is a different question.

Mr ORTON: I think we can—

Mr JEREMY BUCKINGHAM: With all respect, that is a totally different question.

Mr ORTON: No, but I mean—

The Hon. Dr PETER PHELPS: Only for someone who does not believe the supply has an effect on price.

Mr SCOT MacDONALD: Point of order: Chair, I ask you to direct the member to let the witness answer the question reasonably.

Mr JEREMY BUCKINGHAM: If the witness would answer the question. The question is not about supply. It is about whether or not the Government should be doing modelling and have some understanding of what the impact of higher gas prices will be New South Wales business.

Mr ORTON: The point I was getting to is that we should avoid paralysis by analysis. I think it is pretty clear cut that energy prices are going up. We need to boost supply to put downwards pressure on them. I do not think we need to—

The Hon. ADAM SEARLE: Even in the face of decreasing demand?

Mr ORTON: I do not think we need to dissect this to the nth degree. It is a pretty straightforward issue.

Mr JEREMY BUCKINGHAM: What do you mean by "it is a straightforward issue"?

Mr ORTON: I mean that prices are going up, and in the face of constrained supply that can only add to the price pressure. We need to be moderating price pressure by increasing supply.

CHAIR: Order! We have come to the end of our time. Thank you very much for attending today. Given the short time frame for this inquiry, the Committee has resolved that answers to questions on notice be returned within seven days. We would appreciate your help in assisting us to meet our reporting deadline. The secretariat will contact you in relation to the questions you have taken on notice. Thank you very much for coming today.

(The witnesses withdrew)

MICHAEL ZELINSKY, National Vice-President, Australian Workers Union, affirmed and examined:

CHAIR: We welcome our next witness from the Australian Workers Union. Could you please state your name?

Mr ZELINSKY: My name is Michael Zelinsky. Colloquially it is Misha, but legally for the record it is Michael Zelinsky.

CHAIR: Would you like to make a short statement?

Mr ZELINSKY: To be honest, I can keep it very brief. I think the totality of our argument is presented in our submission and in the supporting paper prepared by BIS Shrapnel. I would just make the point, I suppose, that from the point of view of this inquiry it is very important to consider Australia's gas market from a national standpoint, notwithstanding that I understand this is a State inquiry, particularly considering the impacts of the east coast market and that for the first time ever the gas market in the east coast is being linked with the export market, which is having a significant impact on the New South Wales gas market. You cannot really view one in isolation from the other. The point that we are making in our campaign, which is "Reserve Our Gas", is that we do not have a supply-side problem; we are actually producing and extracting more gas than ever before, yet our price continues to go up and up. So what has changed?

What has changed of course is the fact that for the first time technological advances have allowed us to export gas from Queensland. The Queensland Government has made certain policy decisions which are impacting on New South Wales as a net importer of gas in this State, so it is really important to look at not just what we can do in New South Wales but what can be done from other States' perspectives—I suppose, from a Federal point of view—to make sure that this problem is dealt with at its source, if you can put it in those terms. The real question here is what can New South Wales do to influence not just Queensland policy but Federal policy to make sure that the undue impacts of escalating prices of gas are not felt by New South Wales residents and businesses.

There are some of the quick figures I will draw attention to now. Unfortunately these figures look disaggregated, but we are talking about nationwide one in five heavy manufacturers closing, 235,000 jobs on a worst-case scenario being lost and $101 billion in investment. Unfortunately, I cannot disaggregate those figures but New South Wales—being a State that is more heavily reliant on manufacturing than are other States, particularly the western States, and a bigger State generally—you can assume a vast majority of those jobs will unfortunately be lost here in a situation where nothing is done about a gas price escalation.

The other one that I can break down a little bit more are the cost of living impacts which are projected by BIS Shrapnel to be $275 a year, which is not an insignificant amount of money particularly for low income earners, for families and for pensioners. We are already seeing that New South Wales is little better placed than is Victoria due to our climate, but we are already seeing the first signs of energy and security emerging as a result of gas increases in cold months, which is something we should also be very concerned about. I leave my statement there. Obviously I am happy to take questions as we go through. I certainly do not want to waste the Committee's time on a long statement.

The Hon. ADAM SEARLE: You talked about a domestic gas reservation policy. By that you mean a policy that would operate nationwide?

Mr ZELINSKY: Yes, that is right. The only way, really, to deal with this issue is through gas reservation, and that is the policy position that is put forward by BIS Shrapnel and it is the one that the AWU is campaigning on in concert with a vast number of businesses, community and interest groups across the country. At the end of the day Australia is the only country in the world that does nothing when it comes to its gas reserves in respect to export. Other countries have different ways of doing it but, effectively, every country in the world has some kind of check and balance in place to ensure that domestic prices are not adversely affected by the incidence of gas exports.

Unfortunately, in Australia, particularly in Queensland, we have allowed a huge amount of gas exports. We just started this year at Gladstone. That is now commenced without any controls in place. We are now seeing that price escalation flowing through in retail price but also the wholesale price. Unfortunately we are already seeing a lot of manufacturers unable to lock in competitive price contracts. If you take the example of an aluminium smelter, they all have different metrics but typically they operate on a third, a third and a third metric; that is, a third of your cost base issue inputs, a third is your labour and a third is your energy. If you have already got a marginal smelter and you are doubling or tripling one-third of your cost base, you can imagine what impact that would have a business like that.

Smelters are perhaps the best example of what can happen to an energy-intensive business because it is colloquially referred to as congealed electricity. The AWU is of the view that the only way to really solve this issue is to have some kind of reservation policy in place. Look, export gas is a great industry but we need to also make sure that we are not cutting our own throats economically in order to do that. We can have our cake and eat it economically when it comes to liquefied natural gas [LNG]. We just need to quarantine a small amount.

The Hon. ADAM SEARLE: Okay. Can you give us some insight into how some other overseas countries approach this issue of domestic gas reservation?

Mr ZELINSKY: Yes.

Mr SCOT MacDONALD: The back page.

Mr ZELINSKY: Yes. I can turn to that, if it is of any use.

The Hon. ADAM SEARLE: I can read, Scotty. I know it is a struggle for some.

Mr ZELINSKY: I suppose there are a number of different approaches. Some countries have a straight reservation. If you take the Israelis, they have a 60 per cent reservation, which is an extraordinarily high amount. It is not a number for which we would advocate, but that is a huge number. You have the case of the Norwegians, which effectively have a nationalised corporatised industry whereby they partner with other—

The Hon. ADAM SEARLE: What are some countries that are more like Australia that might provide a closer example?

Mr ZELINSKY: A closer example perhaps is if you wanted to look at the United States and Canada. They have national interest tests where you have to pass a series of hurdles before you are granted an export licence to make sure that you are not adversely impacting on domestic prices which would then flow into domestic impacts on manufacturing jobs, et cetera. Those countries, particularly the United States, obviously have undergone the shale and oil boom, which has been highly publicised. What of the things that is not necessarily talked about in that boom is the fact that a lot of the gas has not been able to get out because it requires an export contract before it does. They are starting to export gas but they are doing it in a more moderate slow fashion rather than ours, which is having a large amount of gas being slated for export. That is one example.

The way we would do it here, it really comes down to the policy prescriptions of the government of the day. From the standpoint of the AWU, we advocate for some form of reservation, which could come in the form of a national interest test or straight reservation. But the important thing is the outcome. You have a domestic price that is competitive and ensures that we have good fair price access to Australian gas at a domestic price that is lower than the export price. Therefore you are still able to extract export rents and at the same time you are able to moderate any impacts on the domestic market, making sure that pensioners are not impacted, families are not impacted and businesses are not impacted.

The Hon. ADAM SEARLE: Presumably, the objective of these policies is to ensure that there is a sufficient domestic supply. How do those countries achieve the outcome that domestic supply is at a price that is lower than the export price? Do they live it to the market, or is this some kind of regulatory mechanism that strikes a domestic price that is different from the export price?

Mr ZELINSKY: Again, it varies from country to country, but if you took the United States as an example, it is effectively left to the market in a sense, but they create two markets. There is perhaps a more distorted market domestically where, if there is a whole heap of gas internally and it cannot make its way out, it then requires a lower clearing price internally just because there is more internally.

The Hon. ADAM SEARLE: So it creates downward pressure through supply?

Mr ZELINSKY: That is correct. That is right.

The Hon. MICK VEITCH: I want to explore a bit further with you the national interest test you are talking about. In the United States, does it work in a way whereby they know how much gas is in the system and ensure that the domestic market is met, and it would only be the surplus gas that is exported?

Mr ZELINSKY: In effect. They apply a public interest test, which is pretty broad. A licence is applied for and then they apply a series of metrics to it which take into account whether or not it would be in the public interest. The public interest of exporting is weighed against the public interest of not exporting and a lot of the considerations go to price. Obviously, higher prices do create economic consequences, so that is one of the things that is taken into account.

The Hon. MICK VEITCH: Essentially, the United States would know how much gas is in the system at any given time to be able to operate on those lines?

Mr ZELINSKY: I imagine so. You are asking me a question and I am not entirely certain of the answer.

The Hon. MICK VEITCH: That is okay.

Mr ZELINSKY: But one would assume they have very detailed analysis of their energy markets. I would assume so, but I do not want to make that assumption.

The Hon. MICK VEITCH: I can reword the question. For that type of system to work in the national interest or the public interest, you would need to know how much gas is in the system at any given time.

Mr ZELINSKY: Yes.

The Hon. MICK VEITCH: One of the issues that has been raised with us in this inquiry is around transparency for gas contracts.

Mr ZELINSKY: Yes.

The Hon. MICK VEITCH: Does the AWU in "Reserve Our Gas" have a view around the need for transparency of gas contracts?

Mr ZELINSKY: More transparency would certainly help in the marketplace—knowing exactly who has gas, how much, and what it is being sold for. I think that would help a great deal in this. You only have to take the example of Origin Energy, which last year very proudly stated to the market that it was going to withhold gas and wait until the price went up, essentially, before they would then sell it. From the AWU's point of view, when we consider the economic consequences of high gas prices and the fact that those gas assets are held on behalf of the Australian people and extracted, we would submit, on behalf of the Australian people, withholding Australia's gas in order to profiteer is unconscionable.

More transparency around that and more guidelines around exactly who is selling what, for how much, and to whom would be very helpful as well as how much gas each private company holds. That would be most helpful to this debate. It has been discussed: I think the Australia Institute [AI] group is proposing a gas trading hub. That is not something that we would oppose because more knowledge of the market would always be a great outcome. I suppose at the end of the day anything that gets us to a situation where Australia's gas is benefiting the economy and being sold to the Australian people at a competitive price would be something that we would support.

The Hon. MICK VEITCH: For that to work, though, really that is an issue for the Federal Government around that because of the national market.

Mr ZELINSKY: The States have a role to play in the sense that they obviously control tenements and things of that nature. However, we would encourage the States to coordinate and act together in concert with the Federal Government to make sure that this issue is dealt with. As I alluded to in my opening remarks, New South Wales unfortunately cannot solve this by itself. It needs to be operating in concert with the Queenslanders, the Victorians, the Federal Government and Western Australia. Notwithstanding there are no links by pipeline across the country as yet, it is important to get the right policy parameters in place nationally to make sure that this issue is dealt with, and States doing it by piecemeal alone unfortunately will not get us to the optimal result, in our view.

The Hon. MICK VEITCH: In your submission you provide an example in the US where the US Congress is currently debating for them to change their policy. You talk about Mr Fazzino from Incitec Pivot and the example he gave around their ammonia plant. Do you want to elaborate further on that scenario?

Mr ZELINSKY: To pick up on your first comments, unfortunately in the debate in the US Congress it is a live debate about how much gas should be exported, which is fine in a democracy. However, most unfortunately in that debate Australia is used as the what-not-to-do case by those who champion some level of gas reservation or national interest. They say Australia has nothing, why would you go down that path? A real world example of that perhaps is, as you said, the example of Incitec Pivot which was looking at—this is not a New South Wales example—opening an ammonia plant in Brisbane. In the end they ended up taking that to Louisiana essentially on the back of cheap gas that could be guaranteed in that State. So that is a real net loss to Australia's economy.

Our paper talks a lot about job losses that would come as a result of high priced enclosures, et cetera, but we are already seeing investment go offshore. Coogee Chemicals is another example. They are talking about not opening an additional plant in Victoria but they will send to the US again off the back of cheap gas. We are already losing now. Obviously when you have five-year business horizons, if you cannot lock in a competitive price contract, which anecdotally and the companies we have spoken to are unable to get one at a competitive price—when I say competitive I mean more historic prices—they are making decisions to take it offshore where the gas is cheaper. It is a net loss to the Australian economy and it is a great shame.

The Hon. MICK VEITCH: With regard to contracts and the securing of contracts, at the moment, as I understand it, the industry has a number of long-term contracts which provides some stability, but it is moving towards shorter term contracts. How do we manage the shorter term contract impact on price?

Mr ZELINSKY: Anecdotally—obviously the AWU does not negotiate contracts with gas companies so I can only provide you with some anecdotal insight; I would not want to breach commercial confidence of companies that have spoken to us. Essentially it used to be you could get a contract for a longer period and you could make your forward planning around it, which is a normal business case. Aluminium smelters will have long contracts in place because it is important to know that level of capital investment needs certainty around that. It is just commercial reality. Businesses at the moment, gas producers have no impediments on them to seek the highest price and they are offering very short-term contracts, as you have said, to businesses domestically in Australia on a take-it-or-leave-it basis, which makes it difficult to forward plan your business but also makes it very difficult to even manage your cost base and stay competitive or open.

I suppose the contract issue is just a reflection of the macro policy settings, that is, there are no restrictions in place on exports so therefore we are seeing at a micro level businesses unable to secure contracts that typically they would have got in the past, even as recently as five years ago, at a competitive price for a longer period. Gas producing businesses are saying, "We can sell it overseas." You can have it at what they call net back, which is the LNG price you can secure in Asia, for example, less the cost of shipping. Essentially that is the price they are looking to charge, which in their commercial considerations make sense. However, the question becomes: Is that the smart macro policy setting for Australia to be setting on its energy? Our submission is no, which is why we advocate for some form of reservation.

Mr JEREMY BUCKINGHAM: What capacity has New South Wales more generally and Australian manufacturers and heavy industry to get off gas immediately? Can they manage the shock of this price rise by simply investing in new capital or alternative forms of feed stock of energy? Can they just get off gas and avoid this in the short to medium term?

Mr ZELINSKY: I suppose I could deal with that in two ways. The first question is: Can they get off gas? Some businesses simply cannot. If you took the example of petrochemicals, which rely on gas as a feed stock into their business, you need gas. If you do not have a good steady supply of those inputs then you do not have a business. There is a certain set of businesses that simply rely on it— absolutely, categorically will not operate. There are others—foreseeably you could say, "Why don't you just switch?" Okay, sure, I mean a business can always make a capital decision to switch to a different form of electricity. However, there is an assumption that you have the capital to do it, that you have the line of credit to do it, that you have the support.

A lot of these businesses are global businesses. Do you take businesses that operate all over the world and they are making business decisions whether to invest into older plant in Australia? They will decide: is it in our interests?

Unfortunately when you look at Australian manufacturing, it has been hit heavily over the past five years by the currency being increased as a result of the mining boom we went through. Manufacturing has been hit very hard and capital stocks have been run down throughout that period. I am just speaking very loosely and of course there are various examples throughout that. But if you looked at it from a general macro point of view, capital stock has been run down, cash reserves have been run down, debt has been increased, businesses have struggled to export as a result of the high dollar and they have struggled to compete against the influx of imports as a result of the high dollar and the threat of dumping. So theoretically, sure, some businesses could, but given that we are now at the crunch point, which is 2015, in the sense that gas is now being exported, we are already seeing these huge costs being shifted onto gas users, it is unlikely, I would have thought.

Mr JEREMY BUCKINGHAM: To paraphrase you, Australia is already an uncompetitive place to do business because of the dollar and costs and other factors, so businesses are more likely to shut down or move overseas rather than re-tool, as it were, in the face of higher gas prices, in the union's opinion.

Mr ZELINSKY: You only have to take the example that I cited before of Incitec Pivot. That is a classic example. They were like, "Here's a whole heap of money we are looking to invest somewhere in our global business." They chose to put it not in Brisbane but into Louisiana, and that is a great shame. Coogee Chemicals is looking at doing a similar thing. They are two high-profile ones but no doubt there will be countless examples of that throughout the world as businesses look at allocate their capital.

The question becomes: Where do you put it? That example could so easily be south-west Sydney or Botany or anywhere else. They are jobs we want to see being invested here. So it is not just about protecting that 235,000 I cited before; it is also saying that we want to see future investment in modern manufacturing, in new jobs being invested into Australia. I suppose if there is an example there for new money being chosen, where do they allocate it? They have allocated it overseas on the basis of gas. I can only assume that there will be more of that.

Mr JEREMY BUCKINGHAM: The union's submission is very strong and it makes the assertion that the gas industry is very profitable—60 per cent profit ratio—but also goes on to say that the gas market has decided that the market generally is being wilfully subjected to artificially high global prices and that is being actively manipulated. That is a very strong submission—one with which I agree wholeheartedly. Further the submission states that there is evidence of supply side profiteering, that is, major producers, wholesalers of gas, such as in your submission where Origin has said that it will reduce its call on production from its upstream business and back contracted gas this year and call for that gas in the following years when it is more valuable.

Further, there was a report from March last year in which Credit Suisse said that Santos was always as much about raising the domestic gas price and therefore re-rating large parts of its portfolio outside of GLNG as it was about the project. Could you respond to that? Do you think that that is an acceptable circumstance that it appears these companies are operating like a cartel, profiteering on the backs of businesses and jobs in Australia?

Mr ZELINSKY: I would love to reiterate your point but I suppose if I just touch on some of my earlier testimony, these companies are already—this is not speculative in the sense that we are trying to decide whether or not there is a cartel operating; these are on the record comments from large oil and gas producing companies that are almost wearing as a badge of pride that they will withhold Australia's resources and charge a higher price to us. That is unconscionable, in our view. It is absolutely going to have a destructive impact on the economy. This is not just profiteering on behalf of a private company, which you might have a certain view about, but knowing the impacts of that behaviour it becomes more outrageous when you consider that these gas tenements have been issued on behalf of the Australian people or the owner of the resources.

Coming back to your question about distorted gas markets, when you consider that every country in the world does something when it comes to their domestic gas supplies—they are gas producing, gas exporting nations—there can be no true global price. We are not talking about a global commodity that is being freely traded around the world; it is being restricted everywhere. Yet Australia has decided that it will just openly export its gas without any restrictions. So not only is Australia giving up a competitive advantage by giving away its gas without any restriction; it is also subjecting itself to a distorted price which is higher than it otherwise might have been if all gas were available, so to speak. If every country in the world decided to have open season, we know that will never happen. Given Russia's control of gas, given the Norwegian control of gas and a host of other nations, that will never happen. The price is not global. It is not a market price; it is a distorted price. Australia should consider that when it is setting its energy parameters about what price we should subject ourselves to, given our abundant resources. We should, in our submission, be moderate, be sensible, and have an eye to what is really happening in the market as opposed to just taking a more textbook definition of how markets will typically operate.

CHAIR: It is interesting you make that point about what, in your view, has brought us to this total and complete lassez faire open market situation when very few of the international markets that are suppliers of large amounts of gas in fact operate in the same way. How did we get into this bind, just leaving New South Wales out for the moment?

Mr ZELINSKY: If I had to speculate on it, I think Australia has always been a very energy abundant nation. We have always had a lot of coal, a lot of gas. I just do not think a lot of thought went into what would happen when seven LNG facilities came on board in a very short period of time; what the impact of that would be. I did not make the energy policy considerations. I think there was a lot of excitement. It is great news to have hundreds of billions of dollars invested into Australia. As a union we certainly do not oppose the LNG export industry. It is a great industry. But you can have your cake and eat it too, economically.

Unfortunately, we just did not have the parameters in place, as an export and energy rich nation, whereas a country like America, which has over the years become more energy dependent and an importer, I think they have had to be a little bit more judicious with their settings and the settings were in place when the shale and oil gas boom hit. Ours were not. That is all I can really offer in a speculative answer.

CHAIR: We then move from there to the situation in New South Wales. I take it then from what you are saying that you in favour of an indigenous New South Wales gas industry?

Mr ZELINSKY: We support gas being produced in Australia but I would say that we do not support the argument that more supply will fix this problem. The issue here is not Australia's or New South Wales's gas market in isolation. It is the fact that for the first time Australia's gas market has been linked to the distorted global price.

CHAIR: But you have to understand that unless we produce some gas in New South Wales we have nothing to reserve for New South Wales. You cannot advocate for a reservation policy in New South Wales but have no supply to reserve.

Mr ZELINSKY: Which brings me back to my original point, which is that we advocate for a national approach. Unfortunately New South Wales finds itself in a situation where it is at the behest of decisions of other States. The only way to deal with this is at a national level with a coordinated approach from all States. But just to pick up on your point about whether more supply would fix the issue, at the end of the day we can see through the behaviour of the gas producing companies but also the fact that Australia's gas reserves cannot lower the global price.

More gas would only lead to more expensive gas being sold in the global market. This is not a position just advocated by the Australian Workers Union [AWU]. This has been picked up by numerous commentators in the business community such as Ross Gittins or Clancy Yeates. It is a bit of a furphy argument. The AWU is not at all opposed to more gas being brought onto the market, but you need to have the right parameters in place to make sure that any gas that is produced is secured domestically at an appropriate price.

CHAIR: How do you do that in New South Wales?

Mr ZELINSKY: Through coordination with other States and the Federal Government.

CHAIR: Why would other States agree to us preserving their gas?

Mr ZELINSKY: No one State holds the gas on behalf of the Australian people. For every State we have a coordinated national approach to many issues and one approach that we should have is on energy.

CHAIR: We should have an Indigenous industry so we can talk as equals with other States. That is what you are saying?

Mr ZELINSKY: That is not what I am saying.

CHAIR: That is not what you are saying?

Mr ZELINSKY: No, what I am saying is the most important thing is that New South Wales gets together with the other States and sits down with the Federal Government to figure out how we can fix this issue together. There are a number of issues where the State governments and Federal Government work together. Energy should definitely be one of them, given that energy impacts on the entire community, on the entire economy and not in isolation.

CHAIR: You must realise, Mr Zelinsky, there is a sorry history of cooperation between States in relation to not just this matter.

The Hon. Dr PETER PHELPS: Any issue.

CHAIR: Any issue. One of the things that you do not talk about is the level of State-based capitations in respect of taxation revenue that flows from these things. In my view, if you end up with a national reservation policy with New South Wales having no seat at the supply table, then I think New South Wales, regardless of which way it goes, is not going to see an increase in employment and investment in manufacturing industry, it is going to see a decrease. Do you not see that?

Mr ZELINSKY: Again, I think we are operating at false distinctions between States. This is a national issue and it needs to be dealt with.

CHAIR: I agree with you, it is a national issue, but I am looking at the practicalities of our very imperfect Commonwealth.

Mr ZELINSKY: Absolutely, and Western Australia will scream very loudly for more share of the GST, so New South Wales perhaps should scream more loudly for more share of gas.

CHAIR: I do not know how you do that. There is no overriding national taxation sharing arrangement for gas royalties. If you could give us one way of doing it, go for it.

Mr JEREMY BUCKINGHAM: There is, GST. He just gave you a good example, GST.

The Hon. NIALL BLAIR: What is the rate of GST?

CHAIR: GST may be a great example, but it is not something—

The Hon. MICK VEITCH: Do you really want to talk about the Queensland election, Niall?

The Hon. NIALL BLAIR: I am happy to talk about it; The Nationals did all right.

The Hon. MICK VEITCH: I notice you are not sitting so close to your Liberal Party colleagues today.

The Hon. NIALL BLAIR: The Nationals held most of their seats.

CHAIR: The Queensland election is outside the purview of this Committee. We are talking about gas in New South Wales.

The Hon. NIALL BLAIR: How many did you guys get?

The Hon. ADAM SEARLE: We did okay.

The Hon. NIALL BLAIR: How did the Greens go?

Mr JEREMY BUCKINGHAM: We did very well.

The Hon. Dr PETER PHELPS: To make it clear, as AGL and Santos has indicated, they want to create an indigenous gas production industry in New South Wales, which will effectively, for their own corporate interest, be reserved for New South Wales consumers. Would the AWU consider that to be a good thing?

Mr ZELINSKY: The AWU is not opposed to more gas; it never has been throughout this debate. However, it is concerned about the argument being used by gas companies to say that this is a supply issue. This is not a supply issue. This is a demand issue; i.e. where is it going? Australia is producing more gas than it ever has and yet the price is higher than it ever was. It tells you something has changed. What has changed is a linkage to the export market. If we have a situation where we are going to extract more gas and be charged netback, we do not support that position because that would be a situation where more gas that belongs to the Australian people is being extracted by private interests that are not serving the interests of the Australian people.

It is a dangerous argument that is being pushed—and a convenient argument—by the gas companies that more gas will solve this issue. The assumption is that more gas can reduce the global price, which we know cannot happen. It simply cannot; there is not enough gas in Australia to do that. To be clear, we do not oppose gas being produced in New South Wales, but we are absolutely opposed to that being the solution to the price crisis because it is being driven by demand and export settings, not by how much gas we are producing.

The Hon. Dr PETER PHELPS: AGL does not export, and if it produces a vertically integrated process which only uses gas that is produced indigenously in New South Wales at their effective wholesale rate to themselves, that certainly is going to produce price pressures at the retail level, is it not?

Mr ZELINSKY: Again, this is an assumption that New South Wales is operating, if I can call it that, in a bubble. We know the east coast market is integrated. We know already the Queensland operations—the four plants in Gladstone—are behind schedule. They are not producing as much gas and they are calling for gas from other places, such as the Cooper Basin and other States. If New South Wales is relying on the operation of the east coast market, then it is going to be totally at the behest of what happens in the export settings. That may have an impact; I am not an expert on the energy market. At the end of the day we know the companies that are exporting gas want to charge a higher international price less the cost of shipping—netback, if you want to call it that technically. The answer is the most important thing is to make sure we have our export settings correct before we worry about getting more gas out of the ground.

The Hon. Dr PETER PHELPS: When you say it is integrated, it is only integrated so far as New South Wales is concerned to the extent that AGL has to buy on a broader market what it cannot produce indigenously. That is correct, is it not? It is only integrated to that extent because AGL is not an exporter.

Mr ZELINSKY: I am not familiar with AGL's business model. I certainly do not want to get into a technical argument with you about their business model. That may or may not be the case. However, I rely on analysts who have said that no matter where gas comes from, New South Wales, Victoria or Queensland—it does not matter how much we get out of the ground, if we do not get it right where it is going then we do not assume transparency in the market, making sure that Australia is not held to ransom, so to speak, by the LNG netback price.

The Hon. Dr PETER PHELPS: You indicated you had some concerns with Origin's accumulation of gas at current prices. Why would it not be sensible for Origin to accumulate a large amount of gas at $5 a petajoule and ease in any price increase that it has to go to with purchasing on an international market rate? Why would it not be sensible for them to aggregate a large amount at $5 a petajoule rather than to have a price shock at $15 petajoule later on? Why is that a bad business model?

Mr ZELINSKY: I am not suggesting it is a bad business model. I do not know whether or not it is conscionable conduct from a company that is extracting Australia's resources on behalf of the Australian people. If you are suggesting they are doing it for some sort of altruistic view of the world, I would only rely on the quote from the managing director, who said:

> Origin will reduce its call on production from its Upstream business and bank contracted gas this year and call for that gas in the following years when it is more valuable.

It is clear that the value is the consideration not whether or not there is a price shock.

The Hon. Dr PETER PHELPS: That is two sides of the same coin. The value comes from the price shock.

Mr ZELINSKY: Which they want to benefit from, right?

The Hon. Dr PETER PHELPS: There is always the possibility of substitution. If you have a price shock of tripling of the price overnight, you will have a natural tendency towards consumers, especially those which can substitute relatively easily to move towards a different energy source, whether it be coal-fired electricity, or whatever.

Mr JEREMY BUCKINGHAM: Say "solar".

Mr SCOT MacDONALD: Run the aluminium plant on that one.

Mr JEREMY BUCKINGHAM: Say the "s" word.

Mr ZELINSKY: That is a separate consideration. Substitution will likely happen as the price goes up. What we certainly do not want to see, and this is the concern we have in our submission, in the paper prepared by BIS Shrapnel—what we would hate to see in New South Wales particularly is a demand crunch; i.e. price goes up and a heap of businesses shut their doors and we go, "Beautiful, New South Wales does not need as much gas anymore." That would be a disastrous outcome in the sense it will destroy jobs and employment. We would hate to see that.

We certainly do not want to see companies such as Origin, which are extracting Australia's gas, holding onto it in order to make more value for themselves down the track. As a commercial interest that makes sense from their point of view. Our point is that the smartest and most judicious usage of Australia's resources is that they are leased and rented on behalf of the Australian people. That is the crux of our submission.

The Hon. Dr PETER PHELPS: If these contracts are ending in the next 24 months or so, why would you not buy up as much as you can as cheaply as possible and then ease it into the inevitable price shock that you are going to face in 2016, 2017?

Mr ZELINSKY: I agree with everything you are saying in the sense that you would do that if you have control of gas supplies. I do not think they are looking at easing it in. They are looking at holding it back so they know it is worth more. If I had the choice of selling you something today for $5 or sell it to you next week for $10, I make a commercial consideration to hold it and sell it to you for $10. The only difference—

The Hon. Dr PETER PHELPS: Unless, of course, I have the option of buying the same thing for $7.50, which is exactly the situation the gas retailers face in relation to electricity.

Mr ZELINSKY: Without getting into a back and forth—

The Hon. Dr PETER PHELPS: We do not know, but I am saying that there are not sinister guys in top hats and fob watches and pin-striped suits with cigars, sitting around saying, "Let's screw the consumers"—

The Hon. MICK VEITCH: No, they are sitting at the table across from us.

The Hon. ADAM SEARLE: That is you.

Mr JEREMY BUCKINGHAM: That is right.

CHAIR: Order!

The Hon. Dr PETER PHELPS: It may well be the case that Origin is making a business decision to try to buy as much at a lower price—

The Hon. ADAM SEARLE: Point of order: This forum—call me old-fashioned—is designed for the formulation and posing of questions, not—

The Hon. Dr PETER PHELPS: I am just suggesting an alternative explanation.

Mr SCOT MacDONALD: You indulged in that.

The Hon. ADAM SEARLE: If they could be put as questions that would be of more assistance to the Committee as a whole.

Mr SCOT MacDONALD: Point of order: That is really—

CHAIR: I do not accept your point of order. Let me rule on this one. The members should be asking questions and not putting positions as often.

The Hon. Dr PETER PHELPS: You said that the LNG export market is unfortunate. Are there any other export markets in Australia that you consider unfortunate?

Mr ZELINSKY: Sorry, I think throughout my evidence I made it very clear that we support the LNG industry. It is a great industry; it has been fantastic for Australia. What is unfortunate about that is that we did, not like other nations, have the appropriate parameters in place to make sure that we get the maximum benefit domestically by making sure that Australia still maintains a good competitive supply of its own gas and we still then make the export premium and the export rents externally. To be clear, the AWU is very much in favour of the LNG export industry but it is also in favour of domestic manufacturing, and we can have both.

The Hon. Dr PETER PHELPS: You mentioned the United States had export controls on its LNG exports, is that correct?

Mr ZELINSKY: They issue licences based on a public interest test, yes.

The Hon. Dr PETER PHELPS: Except to non-free trade agreement [FTA] countries.

The Hon. ADAM SEARLE: I think you mean not inside the FTA.

The Hon. Dr PETER PHELPS: In your submission it says, "Gas exports to non-FTA countries require government approval."

The Hon. ADAM SEARLE: That is right.

Mr ZELINSKY: Yes.

The Hon. Dr PETER PHELPS: If we applied that same principle, do we not have a free trade agreement with both Japan and China?

The Hon. ADAM SEARLE: I think that means the North American Free Trade Agreement.

The Hon. Dr PETER PHELPS: If we use the American model, we would be exporting to China?

The Hon. MICK VEITCH: It is the North American Free Trade Agreement [NAFTA], is it not?

The Hon. ADAM SEARLE: I think it is the NAFTA.

Mr ZELINSKY: Firstly, these contracts were signed well before the free trade agreements were designated. It is speculative how it would have played out and it is also within our control what we choose to do. The Americans have a certain model. They still, at this point, export a vastly less amount of gas and have controls in place before they do it.

The Hon. Dr PETER PHELPS: But the majority of examples you site are basically nationalised industries are they not? Surely we are not suggesting a nationalisation of the gas industry in Australia?

Mr ZELINSKY: No.

The Hon. Dr PETER PHELPS: Thank heavens. A socialist objective finally can be removed from the Labor Party constitution.

Mr SCOT MacDONALD: You might have heard the previous witnesses. The issues you are pointing out and others are pointing out, in a large part, transition. We have difficulties now with contracts coming from very stable, low, to a world commodity, I guess. Can you make any comments on that? Are we at risk of overshooting, if you like, some of these regulations you are talking about, reserve and all that sort of thing? I think most of the submissions say that in three or four years time the supply and demand balance will probably restabilise, if you like.

Mr ZELINSKY: That may or may not be the case. The issue is that a lot of these businesses are marginal now and they cannot sustain a tripling of their energy price input. Even if it is transitionary shock, there is definitely an even stronger case to do something to ensure that these businesses do not fall over during, if has been suggested, a relatively narrow window. Again, I do not know whether that will be the case. However, let us assume that it is. We would still have a demand crunch and businesses falling over during that period. That would be even more tragic because they may have survived in the longer term had they survived in the medium term.

Mr SCOT MacDONALD: I think we are in furious agreement about most of what you are talking about. Last week suppliers told the Committee that they were very cognisant of that; they did not want to see demand destruction and they wanted to ensure that their customers were there for the long haul. I hear everything you say, but what will reservation do to fix that when there is a very strong awareness of the risks of demand destruction?

Mr ZELINSKY: You already have a problem now. There is an issue. It is one thing for them to say that they are very concerned, but Origin talks about stockpiling when it is more valuable. The real experience is that we are not seeing these competitive contracts being offered. If they are so concerned about it, I submit that it is only crocodile tears because we are not seeing the rubber on the road in terms of offering contracts at an historically competitive price to ensure these businesses stay open. You are concerned and we are concerned, but we are not necessarily seeing concern on the part of energy suppliers because at the end of the day they are going to get overseas rents that they will not get in the domestic market. They make a commercial decision, which is not surprising if you pick up on the points made earlier. It is not surprising that they are making those decisions. The question is whether it is smart for us—and by that I mean the community, governments and the public at large—to accept that as the outcome.

CHAIR: Thank for appearing before the Committee today and for your submission

Mr ZELINSKY: Thank you for your time.

(The witness withdrew)

MARION JOHNSTONE, Group Treasurer, CSR Limited, affirmed and examined:

CHAIR: Do you wish to make a short opening statement?

Ms JOHNSTONE: Good morning Chairman and members of the Committee. Thank you for the invitation to be here today. CSR is extremely concerned about the availability of gas in New South Wales and eastern Australia generally from 2016 onwards, not only because of the high volume of gas already earmarked for export but also because the high fixed-cost nature of gas export facilities will see a strong drive towards ensuring that they operate at full capacity and therefore consume every available molecule of gas. This causes us to be very concerned about the structure of the domestic gas industry and market. The structure is essentially the same as it was 40 years ago, when there were no exports and producing natural gas was considered pioneering.

In our view the Government has a significant role to play in facilitating an active and flourishing market in all points of the value chain for product, transport, distribution and risk managment services. In the medium term the right structure will overcome the shortage of gas in New South Wales and on the East Coast while ensuring a fair price is paid and received for product and services. That will help to drive confidence for manufacturers to invest and to support jobs in New South Wales, and in Western Sydney in particular. However, this will require a multi-year, multi-government program and some interim steps to substitute for the absence of a vibrant market in New South Wales. Our submission outlines some of the steps that we believe are required of government to achieve this. I am pleased to answer questions.

The Hon. MICK VEITCH: Thank you for your submission and your attendance today. I refer to page 8 of your submission and transitional measures. You talk about the need for export licensing for both gas resources and LNG plants. Please explain what you mean by "export licensing" so that we are clear?

Ms JOHNSTONE: I would distinguish export licensing from reservation. I would propose a system similar to that operating in the United States. The United States system was put in place when its free trade agreements were with only Mexico and Canada.

The Hon. MICK VEITCH: That is referred to as NAFTA, or the North American Free Trade Agreement.

Ms JOHNSTONE: That is right. We can look at the United States for a range of things because it has a very vibrant and open market with a great deal of investment in gas, many suppliers, highly contested elements of the value chain, contested pricing for pipelines, contested pricing for gas, and contested pricing for risk management and distribution services. It is a very vibrant and flourishing market in all respects, and government was important in making that a reality. Export licensing does not mean a prohibition on exports; it means there is some consideration of the domestic market before it takes place. That is, it is an open and flourishing market and gas is available. As members probably know, the United States has a very deep energy security policy, so there is context there as well.

The Hon. MICK VEITCH: You also refer to Chinese walls.

Ms JOHNSTONE: They are very much transitional measures. We would like the value chain to be broken up and for there to be markets in each aspect of that chain. Chinese walls would be simply an interim measure while those markets were set in train.

The Hon. MICK VEITCH: Does that mean you have issues with the current ownership of the infrastructure—the pipeline?

Ms JOHNSTONE: At the moment the problem is that there is no active and open market in all aspects of the value chain. I will define what I consider to be a market. It means that I can go to my market terminals and get my price for 2018, 2019, 2020 and so on. I cannot do that; in fact, I cannot even get a price. That is another issue. That is not only in respect of gas; it is also true for the other components.

The Hon. MICK VEITCH: It has been suggested that the Committee consider some sort of transparency arrangements whereby the contracts are made public and are known. What is CSR's view of that?

Ms JOHNSTONE: The most effective market is one that operates on hub pricing—it is transparent to everybody. There will be additional costs. You do not buy only at the hub and it gives you the opportunity to manage price risks over the longer term. You know your pricing and you can have confidence when investing. Hub pricing means it is there for all to see—my molecule is as good as anyone else's.

The Hon. MICK VEITCH: You also talk about reporting and disclosure.

Ms JOHNSTONE: Yes.

The Hon. MICK VEITCH: What sort of disclosure regime do you see being put in place, and not only as a transitional measure?

Ms JOHNSTONE: We need some long-term reporting and disclosure. To have confidence in investing in this country we need to understand how much gas we have available. At the moment we cannot be confident about that. We need to know how much gas there is, who has it and where it is.

The Hon. ADAM SEARLE: What are the barriers to having that information? Are the producers keeping it from the public?

Ms JOHNSTONE: It is not readily available. We can only infer because there is no requirement to make information available and it is not.

The Hon. ADAM SEARLE: What steps could New South Wales take to require that that information be made available?

Ms JOHNSTONE: The New South Wales Government controls large areas that are relevant to gas. It would be in order to require statements of reserves, use of reserves and information about where gas is in pipelines and in storage facilities.

The Hon. ADAM SEARLE: And your organisation would welcome that increased transparency?

Ms JOHNSTONE: Absolutely. That is essential in a commodity industry. We operate in commodity industries ourselves, or have done in the past—for example, in aluminium. There is a lot of information available through the London Metal Exchange [LME] warehousing system about what commodities are where at any one time. I can check how much aluminium is in the LME warehouse, whether it be in Detroit, Europe or Japan. We know that, we know what our capacity is, when it will be on the ship and so on.

The Hon. ADAM SEARLE: On page 4 of your submission you mention that only a handful of economic interests control almost three-quarters of current reserves while about 90 per cent of Australian gas production is also similarly controlled by limited sources. What steps could New South Wales take and what steps do other governments need to take to break that down to make it more competitive?

Ms JOHNSTONE: As a commodity it needs to be very realistic in its approach to knowing that commodities need to be available and from a variety of sources. If you have only one or two sources that are supplying all of the commodity, by definition you have monopoly or an oligopoly. I would like to see New South Wales and other States say, "You have enough reserves. It is time to bring on others and to enable other producers to come on board." Basically we need a larger number of entities with control over the raw material. The New South Wales Government has control of all the licensing, so it has a lot of tools at its disposal.

The Hon. ADAM SEARLE: Your submission deals with market structure using a series of bullet points. How could governments restrict the capacity of any one entity, joint venture or partnership to dominate the reserves?

Ms JOHNSTONE: Obviously States play a critical role in controlling reserves and who has access to exploration licences, production permits and so forth. We have a competition commission and one would have thought there would be a significant role for such a body in recognising the need for larger number of players when it comes to a commodity. It will be multifaceted and multi-tiered in respect of government. Nevertheless, States, and New South Wales in particular, can play a critical role in breaking up value chains.

The Hon. ADAM SEARLE: What form of regulation of the pipelines do you envisage as being necessary?

Ms JOHNSTONE: The pipelines are the lifeblood of all consumers. They are a critical piece of infrastructure. There are many pipelines, some of which are more regulated and some are lightly regulated. The problem with the pipelines in this country is that they tend to be dominated by long-term contracts, which means that access is very limited. We have no information about the cost of transport or other elements. We cannot trade in parcels of transport. I think AGL referred in its submission to difficulty with charging and so forth. It is a piece of infrastructure that needs to be priced and open in that context.

The Hon. ADAM SEARLE: On page 8 of your submission you talk about requiring the registration of book volume by destination in the market. Who how would that work and what would it mean?

Ms JOHNSTONE: It is in the context of transparent information.

The Hon. ADAM SEARLE: Price discovery.

Ms JOHNSTONE: Yes. I hesitate to call it a market, but at this stage in terms of tentative steps towards a market it is about facilitating that.

The Hon. ADAM SEARLE: In your submission you seem to support the export licensing for both gas and LNG, is that correct?

Ms JOHNSTONE: That would be correct, yes.

The Hon. ADAM SEARLE: Why do you think that is desirable?

Ms JOHNSTONE: Because I think we have seen already the building of facilities which—on the research that we have privately commissioned—have more capacity than there is gas available.

The Hon. ADAM SEARLE: Talk us through the implications of that.

Ms JOHNSTONE: If we have facilities with more capacity than there is gas available and in addition you have the same parties that control the facilities also controlling, let me say, a very large, very dominating share of Australia's reserves, they have got incredibly high fixed costs at the export facilities—incredibly high fixed costs—their expectations on being able to secure extra gas for themselves have not been met. And, I should add, according to, let me say, the anecdotes and the information that is being passed on to me by others very close to them, that the penalty clauses in those export contracts are extremely high. So you can add it up and say, "I have got an extremely high-cost facility and if I do not meet all my contracts, I am going to pay, not just the cost of the gas price in the Japan market, but potentially double that or more, the penalties are so high". So that is anecdotal, I have to emphasise that. But that means there is no price they will not pay.

The Hon. ADAM SEARLE: Does that mean that they could also potentially take gas that was intended for the domestic market in order to meet those foreign contracts and produce the gas supply problem?

Ms JOHNSTONE: What I would say to that is, what gas is intended for the domestic market? We have never had a notion that gas is intended for the domestic market. What we had was a market that lived in splendid isolation—that is true. But there is no notion of gas intended for the domestic market.

The Hon. ADAM SEARLE: So you are in favour of, through export licensing, that could leave the door open to some form of domestic reservation?

Ms JOHNSTONE: I think it is about being pragmatic about where we are today and we would be very concerned to see any more going towards the export market until there is a functioning and vibrant domestic market.

Mr JEREMY BUCKINGHAM: That is an interesting line of inquiry that Mr Searle has been exploring. The assertion from the gas industry in Australia was that the ramp-up to LNG would mean that everyone would be looked after, that there would be more supply than we actually needed, in terms of export and domestic. Is that the case in the initial years?

Ms JOHNSTONE: Our experience in seeking contracts gives us no confidence and does not support that.

Mr JEREMY BUCKINGHAM: But that was the expectation—

Ms JOHNSTONE: I do not know whose expectation.

Mr JEREMY BUCKINGHAM: If you look at the Bureau of Resources and Energy Economics and the like. But clearly in CSR's case that has not come to fruition, there is actually a shortfall in terms of the amount of gas available domestically. There is not the availability there?

Ms JOHNSTONE: The research that we have privately commissioned suggests that that is the case.

Mr JEREMY BUCKINGHAM: You have said there are penalty clauses potentially?

Ms JOHNSTONE: That is an anecdote that I have but yes, my understanding is that penalty clauses are very significant. And why that is important is because it drives the economics towards export.

Mr JEREMY BUCKINGHAM: Absolutely, because of the penalty clauses. And I have heard anecdotally that the potential for those contracts to be voided if they are unable to supply, especially in an environment where there is a low oil price in other places, that that is a possibility as well. I am interested in your submission that you have said there that gas supply contracts are no guarantee of actual supply. How can that be? Why would you have a gas supply contract that does not guarantee—how is that market actually operating?

Ms JOHNSTONE: In wholesale gas contracts they typically have clauses which allow for non-supply for 20 to 30 days. But in addition to that, if there is no gas available in the system, you then end up with an allocation mechanism. I think AGL covered that in their submission.

Mr JEREMY BUCKINGHAM: How does that mechanism work?

Ms JOHNSTONE: I have never been through that experience myself but my understanding is that it is based on levels of emergency. You end up with a rationing situation.

Mr JEREMY BUCKINGHAM: Are we in that situation at the moment?

Ms JOHNSTONE: At the present time we are not in that situation but we do not have confidence that we will not get into that situation. We are extremely concerned about it, especially in later years.

Mr JEREMY BUCKINGHAM: When you say "later years", are we talking 2020?

Ms JOHNSTONE: 2016, 2017, 2018, 2019.

Mr JEREMY BUCKINGHAM: What would be the impact on your business?

Ms JOHNSTONE: It is profound, especially for a glass facility—it has to keep operating.

Mr JEREMY BUCKINGHAM: Would it mean a shutdown?

Ms JOHNSTONE: A shutdown. We are in the process of considering how we can get back up for short term but, yes, for a glass facility, if a glass furnace closes it closes forever. It does not reopen in Australia.

Mr JEREMY BUCKINGHAM: In your submission, you say:

> Until the dramatic fall in oil prices very recently, there has been little interest from suppliers in engaging in even preliminary discussions for supply of gas beyond 2015.

So it is very, very short-term contracts. Could you elaborate on that? Are you writing, seeking meetings? Is the experience that you are not even getting a hearing with gas suppliers?

Ms JOHNSTONE: Especially for later years, our experience during 2014 has been very much that requests go deferred, unanswered and so on.

Mr JEREMY BUCKINGHAM: So there is not even a willingness—it was very strong testimony, I must say, to describe it as an oligopoly and also a cartel.

Ms JOHNSTONE: I do not think I used the word "cartel". Someone used it previously, but I did hear that and smiled.

Mr JEREMY BUCKINGHAM: You say there needs to be a major change in the market structure and in particular, you say:

> Unbundle the value chain from resource ownership/control and production through to consumption to ensure ownership is diverse, competitive, and separated at each point of the value chain.

That is a significant reform. You are calling for a major intervention.

Ms JOHNSTONE: Major reform, correct.

Mr JEREMY BUCKINGHAM: A disintegration, a break-up of the gas production, distribution, wholesale, retail industry in Australia?

Ms JOHNSTONE: Yes, and I would evidence the market that operates in the United States as being evidence of its success—that kind of policy, that style of policy.

Mr JEREMY BUCKINGHAM: Based on the Henry Hub type of—

Ms JOHNSTONE: Right. In other words, we do not want somebody who can control every molecule from the point it leaves the ground to the point it arrives at whatever your facility is, or the point it arrives in your home. And control, I should also say, not only is necessarily ownership because, by definition, they do not own the molecules anyway, but control is long-term contracts which are structured such that they provide effective control.

CHAIR: At the outset you mentioned in your testimony a while ago that CSR had commissioned private research. Could you supply a copy of that to the Committee, even on a confidential basis? Could you take that on notice?

Ms JOHNSTONE: If you would like I will request the people, I can do that. I will ask them and see.

CHAIR: I am sure they would like to give it to us.

Ms JOHNSTONE: I would not be surprised if they would.

CHAIR: Is it fair to characterise your submission as seeking regulation of the gas supply industry, much along the lines of the electricity industry? In other words, organising it as opposed to the free-for-all we have there now?

Ms JOHNSTONE: To be honest, it is not really aimed at organising, so much as breaking up the value chain but ensuring that there are competitors at each part of the value chain. And to the extent it needs to be organised, then I think the role of government is to facilitate entry of new competitors at each part of the value chain and that the services that are part of it are actually readily available and there is a vibrant—

CHAIR: As a large manufacturing or retail consumer of gas, it is obviously in the interests of CSR, as far as its profitability and its ability to employ people, to get the lowest possible price it can.

Ms JOHNSTONE: Certainly and to be confident as well.

CHAIR: Yes, confidence in long-term contracts for gas and also to reduce the volatility in the marketplace.

Ms JOHNSTONE: I think this is where there is particularly a role for New South Wales in that I see financial institutions that usually base trading operations here in Sydney would form a major part of facilitating risk management services for long-term pricing for gas. So an open market would enable us to hedge out for a considerable period and make decisions.

CHAIR: CSR is a large company, it has overseas operations. The building supply side of things is oriented to the domestic market. If you are going to make bottles, for example, you are going to make them for the local market and if the price was right you may export some. But CSR, like any other multinational company, has the ability over the medium term to relocate its capital off shore.

Ms JOHNSTONE: We are very Australian focused with manufacturing and it is important to us that our manufacturing facilities in Australia, and in western Sydney in particular, remain competitive.

CHAIR: It is important to us that they remain in New South Wales.

Ms JOHNSTONE: Obviously, with the price of gas effectively doubling and more, it is a serious impediment to investment in Australia.

CHAIR: In your submission, you recommend transitional arrangements to bring order to the national gas market. How do you see this applying in New South Wales specifically?

Ms JOHNSTONE: I think New South Wales has a big role in licensing and permitting. I see that right from the control over the resource itself, all the way through to regulation and access to pipelines and distribution facilities. In addition, I think New South Wales can play a large role in facilitating more retail competition. For the home consumer, there is a choice of two. And I think for the business consumer, especially the multi-state business consumer, there is realistically one provider for the distribution and for the gas, there is a choice of one.

CHAIR: Would that necessarily mean that that opinion extends to the point where you would support increased production of gas in New South Wales?

Ms JOHNSTONE: I think I can unequivocally say that we need more gas. I think we would certainly like to see supplies increase and we would like to see more suppliers.

CHAIR: That was my next question.

The Hon. Dr PETER PHELPS: You said you would like to see entry facilitated for new developers, new producers. Would not that mean that a pro-deregulation environment would be advantageous?

Ms JOHNSTONE: I think we do not have an environment at the moment that takes that into account. So I do not think it neatly is described as deregulated or regulated because markets do not operate in a vacuum, do they? They need facilitation.

The Hon. Dr PETER PHELPS: But generally speaking, would you say that increased Government regulation which places a cost burden on producers is beneficial for bringing new players into the market?

Ms JOHNSTONE: I do not think this is about cost burden; this is about bringing on more competitors. My point is about bringing on more competitors.

The Hon. Dr PETER PHELPS: Why would a competitor enter a highly regulated New South Wales market when they could invest their money in Louisiana at a lower regulatory burden?

Ms JOHNSTONE: We are talking here about the source of gas. There are actually quite a lot of small explorers and would-be producers out there who would like to participate in the domestic market but who find the current structure very difficult.

The Hon. Dr PETER PHELPS: Does CSR still have interests in the Tomago smelter?

Ms JOHNSTONE: Yes.

The Hon. Dr PETER PHELPS: Is it 100 per cent?

Ms JOHNSTONE: No, its effective interest is about 27 per cent.

The Hon. Dr PETER PHELPS: Has that reduced over recent years?

Ms JOHNSTONE: No.

The Hon. Dr PETER PHELPS: Is Tomago still operating?

Ms JOHNSTONE: Yes.

The Hon. Dr PETER PHELPS: Is it likely to continue operating in the future if it could achieve energy input costs at the current level?

Ms JOHNSTONE: I am probably not the right person to ask that question but certainly from where I sit that would be my expectation. But it is an electricity consumer largely, not a gas consumer.

The Hon. Dr PETER PHELPS: My next question was going to be wasn't the concern about Tomago in relation to the expected cost that might have accrued if there had been a broadly based increase in electricity costs brought about through an indiscriminate carbon tax arrangement?

Ms JOHNSTONE: I am really not close to the Tomago situation because the joint venture operates separately.

The Hon. Dr PETER PHELPS: If, as they have indicated, AGL wishes to increase production in New South Wales not for export but purely to provide them with an upstream supply source at a lower rate than world market gas for New South Wales and Australian Capital Territory consumers is that something that CSR would support?

Ms JOHNSTONE: I have to say that the context is a complex one because what I would say before that is that we need more suppliers and more choice of suppliers in New South Wales. That would have to be the first step. The other thing that you have to bear in mind about gas is that simply having more gas produced in New South Wales may not be enough because gas that is already produced here can go elsewhere. Nothing can be done unless it is a holistic consideration of the matter. In isolation, it is difficult to say.

The Hon. Dr PETER PHELPS: Except that AGL has indicated they have no interest in an export market whatsoever?

Ms JOHNSTONE: No, they do not but gas is a fungible commodity. If it frees up other contracts then that means there is more gas available for supply. We would come to our point, which is: More gas in its own right, even if it is a retailer, is not by itself the ingredient to resolve our gas crisis.

The Hon. Dr PETER PHELPS: You believe that greater competition and greater supply in the New South Wales market would offer an advantage to particularly manufacturing industries in New South Wales?

Ms JOHNSTONE: Yes, I do. But I also would come back to the point that it is a multifaceted thing and the issues do not stop. It is difficult to put a border around all of the issues. It is one ingredient of many.

The Hon. Dr PETER PHELPS: Do you agree with the principle that there are some industries in which economies of scale allow for cheaper production costs that can then work their way through to lower retail prices?

Ms JOHNSTONE: By itself it is not an automatic impact because otherwise Australia would have monopolies in everything. Would we all be better off? I think that would be very much case by case on the product.

The Hon. Dr PETER PHELPS: Were you working with CSR in 2010?

Ms JOHNSTONE: Yes, in my current role.

The Hon. Dr PETER PHELPS: In 2010 Sucrogen had 60 per cent of the Australian sugar market. Is that necessarily bad for consumers?

Ms JOHNSTONE: I would say that CSR does not own Sucrogen anymore.

The Hon. Dr PETER PHELPS: But in 2010 CSR owned Sucrogen. One single supplier held 60 per cent of the Australian market. Is that necessarily bad for consumers?

Ms JOHNSTONE: I am sure the consumers made up their own minds about it.

Mr SCOT MacDONALD: In your submission you say that you employ 750 full-time equivalents. Can you give me a rough idea where they are located?

Ms JOHNSTONE: I do not have the State numbers with me.

Mr SCOT MacDONALD: That is 750 in New South Wales.

Ms JOHNSTONE: The New South Wales staff would be all over New South Wales. The manufacturing for CSR building products is in Western Sydney. The bulk of employment is in Sydney but there are distribution centres throughout the State.

Mr SCOT MacDONALD: On page 2 you talk about the possibility of outages of about 10 days but you do not nominate a possible year that might happen.

Ms JOHNSTONE: I need to also say that our research is ongoing. The 10 days was based on some of the research but when I look at the contracts, if we went down the path of trying to get a wholesale contract and then arrange all the other services if we were able to, they provide for 20 days. One is on the basis of supply shortfalls; the other one is based on contract issues.

Mr SCOT MacDONALD: On page 3 you make the point, "Transitional measures such as prioritising the most advanced projects in NSW to reduce dependence ..." When you hear people putting a position of moratoriums and the like what does that do to CSR in terms of confidence, possible investment plans and employment decisions?

Ms JOHNSTONE: The whole question needs to be answered through good process. That is the same for supply, how it happens and the number of suppliers.

Mr SCOT MacDONALD: But if there is a slow down or a brake on prioritising those projects—that is Pilliga and Gloucester I assume you are talking about—can you comment on your confidence?

Ms JOHNSTONE: We are certainly very frustrated through, I would say, the whole process. That would be evidence of one part of the process but through the whole process. We are agnostic as to where gas comes from, we just want gas.

Mr SCOT MacDONALD: Is that leading to impacts on your decisions about investment?

Ms JOHNSTONE: What is important to recognise is some processes cannot be run without gas because the company cannot switch. Certainly if you have already made the investment and that investment uses gas then the issue about confidence is would you today invest substantial amounts of money to convert a manufacturing facility to electricity if it could use electricity. You would need to think very hard about it.

Mr SCOT MacDONALD: Are we at risk of some CSR operations migrating interstate or even overseas if we cannot get this market security sorted out?

Ms JOHNSTONE: At the moment what I would say is that we really lack confidence in the market. If we were making new decisions today that could have a significant impact. As to the existing operations, we would be constantly reviewing our competitiveness in those businesses and, naturally, we will be thinking about the competitiveness of the businesses based on energy prices going forward.

Mr SCOT MacDONALD: Victoria has a moratorium. Some people sitting around this table believe a moratorium is the way to go. When you hear that discussion round the board table what does that trigger in your minds?

Ms JOHNSTONE: At the end of the day Australia generally has a lot of gas. We would just like to see it developed.

Mr SCOT MacDONALD: Has CSR thought about using a strategy like Incitec Pivot, which is striking a deal with Beach Energy and accessing gas directly out of Moomba themselves and cutting out quite a lot of the middle?

Ms JOHNSTONE: We are reviewing all our options. We have to.

Mr SCOT MacDONALD: Most of your submission goes to the market, its transparency, its liquidity and security but there is not a lot of discussion about the price per se. I hear what you say about security and contracts and all the rest of it but price does not seem to be as important.

Ms JOHNSTONE: Price is extremely important and it is always going to be important. The price has doubled, so obviously that is going to be important. We are functioning on the basis that if you have a functioning market, price may begin to be resolved. But of course you have to have multiple choices of supplier and you have to be able to freely access all the services in between them to actually see that resolution.

Mr SCOT MacDONALD: You are saying that the market is too thin at the moment and not transparent; it is not a functioning market?

Ms JOHNSTONE: I do not believe it is a functioning market.

The Hon. NIALL BLAIR: You have made recommendations that Moomba is potentially a better place to be looking for the hub. Would you talk about that?

Ms JOHNSTONE: A hub will be successful because it is logical and successful, not because somebody says it should be so. The hub needs to be central to pipelines and resource. A hub that is close to the export essentially means back hauling of gas. How can that be logical? It has to be where most gas comes from. There might be more than one hub. It may be that Australia will not sustain liquidity in more than one hub but—

CHAIR: You talk in your submission about virtual hubbing, provided you can get the transparency of data.

Ms JOHNSTONE: Yes but it is always going to have at a place at a point in time. I do not know enough about the European system to be as unequivocal about virtual hubbing. They do use virtual hubbing but they do not appear from afar to have the same vibrancy of market.

The Hon. NIALL BLAIR: Has CSR spoken to the South Australian Government or made representations to the Federal Government on that issue?

Ms JOHNSTONE: We are making the same representations to everybody who will listen.

The Hon. MICK VEITCH: The pipeline control centre is at Young. Is there any reason why that could not be the market hub?

Ms JOHNSTONE: If a hub is to develop it will develop in the most logical place. In the absence of other studies we would more advocate and put out there Moomba but I think it really needs very serious and deep consideration. As I think I did say, the Henry Hub was actually nominated by the New York Mercantile Exchange [NYMEX], whose interest was in developing a vibrant and flourishing market. Long-term pricing—in the United States you can get pricing to December 2027 so you know exactly what your gas price will be out to 2027. That was the reason why they selected Henry Hub, and it has worked because they did not choose it to suit themselves as a supplier or a producer. It works because it worked for the market.

The Hon. NIALL BLAIR: That research you spoke about, which I think you have agreed to consider supplying on those, does that address the issue of the hub and where it should be located?

Ms JOHNSTONE: No, it does not. It was only about the quantity of gas. The research on the hub, there is some research that is available publicly from the International Energy Agency [IEA] and I would commend the research on developing an Asian hub and Asian hub pricing. Sitting where I do as a treasurer, I think that there are significant opportunities for New South Wales in financial markets. The potential to develop an Asian hub is here, but there are many ingredients to make that happen. I would commend the IEA report on Asian hubs.

CHAIR: Thank you very much; we will finish there, Ms Johnstone. You have taken some issues on notice for us. Given the short time frame of this inquiry, the Committee has resolved that answers to questions on notice be returned within seven days. We would appreciate it if you could assist us to meet that reporting deadline. The secretariat will be in contact in relation to questions you have taken on notice. Thank you very much for coming.

(The witness withdrew)

STEVE DAVIES, National Policy Manager, Australian Pipeline Industry Association, affirmed and examined:

CHAIR: Would you like to make a short opening statement?

Mr DAVIES: Yes, I would. I would like to start by saying that the pipeline industry has a long history of providing transportation services to New South Wales gas users, starting with the Moomba to Sydney pipeline in the mid 1970s and then with the supplies of gas coming in through Victoria in 1999 and 2000 through the New South Wales-Victorian Interconnect and the Eastern Gas Pipeline. Over time the capacity of those pipelines has developed through competition between South Australia and Victoria to the point where we have a combined total pipeline capacity into New South Wales of 800 terajoules a day—approximately 400 terajoules a day from each of South Australia and Victoria.

Mr SCOT MacDONALD: Could I just check, did you say petajoules or terajoules?

Mr DAVIES: Terajoules—that is 1,000 less than petajoules. Current peak capacity in New South Wales is about 600 terajoules; so its current pipeline capacity is more than efficient to meet New South Wales' gas demand from interstate if the gas is available to be transported from either South Australia or Victoria. The prices that that transportation service has been provided has been reasonably static over the last decade, riding roughly in line with the CPI. Both the Moomba to Sydney pipeline and the Eastern Gas Pipeline publish tariffs on their owners' websites; so those tariffs can be tracked and are around $1 a gigajoule for transportation from either Victoria or South Australia.

In response to some of the gas supply tightness that is being experienced in the gas market at the moment, the pipeline is looking at ways it can provide new services to gas users in New South Wales and across the eastern coast—primarily, pipeline capacity trading, facilitated capacity trading, operational capacity transfers have been introduced on some pipelines and will be introduced on others shortly—and also then improve storage options. We have also seen this year for the first time pipelines offer open seasons on new capacity for expansion—that is making it widely publicly known that they are looking for opportunities to expand pipelines and calling for expressions of interest to try and get as many consumers of gas that is involved in those expansions as possible to allow them to be as big as possible and, therefore, ultimately as cheap as possible.

In terms of gas supply, APIA considers that the answer to the gas supply tightness in eastern Australia at the moment is to increase gas supply through a variety of means. There are lots of options on the table, which include more unconventional gas for New South Wales and Victoria, improving gas supply composition in the upstream market and trying whatever is necessary to grow the gas market in Australia so it can be as healthy, vibrant and competitive as possible.

The Hon. MICK VEITCH: In your submission you talk at length about how pipeline infrastructure is constructed and expanded. Can you go through some of the issues that may arise from, say, long-term contracts to short-term contracting?

Mr DAVIES: We are seeing definitely a move away from long-term contracts in gas supply. What that will mean in terms of pipeline investment is that pipeline investment will become riskier. Currently pipeline investment tends to attract very low costs of debt because it is underpinned by long-term contracts and pipeline companies are able to make investment decisions that will allow them to recover the cost of their pipeline over decades, not over years. With short-term contracts that are prevailing, they are currently in the market and are expected to continue when expansions of pipelines do occur. They are riskier; pipelines will have to start taking more risks and make assessments on whether they think the gas will continue to flow for decades in those directions. The increased riskiness will mean that there are higher costs of debt that pipelines will have to pay to get the money to build the pipelines and the expansions and that will translate into higher tariffs.

The Hon. MICK VEITCH: This Committee has heard some evidence that relates to pipeline infrastructure, particularly the difficulty in getting access to existing infrastructure. Does your association have any views on how those concerns could be eased?

Mr DAVIES: When it comes to access to pipeline capacity, what almost every gas user wants is guaranteed access and there is only so much guaranteed access that any pipeline can provide. Capacity trading will improve your availability of non-firm access—so, unguaranteed access. Every single pipeline in Australia offers non-firm access for sale, which is, we cannot guarantee that you will have it on any given day but you can look at our history of utilisation and determine for yourself whether or not there will be capacity available on any given day, and, to be honest, there is very little interest from any gas user in acquiring capacity on those terms.

Capacity trading will allow existing customers who have their firm capacity to better trade that when they are not using it, but the reality is that most of the time on days of peak demand they are probably not going to be interested in trading their capacity and that will be when the interest in that trading capacity is highest. Currently, any shipper that does have firm capacity on a pipeline is free to trade it to whoever they want under whatever terms they want. Pipelines are starting to offer services to make it easier to trade but shippers do not have to use those services, they can continue to use existing arrangements to trade capacity to whoever they please.

The Hon. MICK VEITCH: I am interested in the issue around how much gas is in the system at any given time. Am I correct in drawing from your comments that your association can say exactly how much gas is in the system at any given time? If we could go into a website somewhere right now, it would be publicly available information?

Mr DAVIES: The National Gas Bulletin Board does show the gas flows on any given day across eastern Australia. That is as good an indication of the gas in the system as you can get.

The Hon. MICK VEITCH: That is interesting because last week the Minister said that it was difficult to determine how much gas was in the system at any given time.

Mr DAVIES: The Gas Bulletin Board has just been revised; it shows how much gas is flowing on each major pipeline in eastern Australia, how much gas is being processed at each major gas processing facility in Australia every day.

The Hon. ADAM SEARLE: Is that in real time?

Mr DAVIES: It is on a daily basis.

The Hon. MICK VEITCH: Not in real time?

Mr DAVIES: No, not in real time.

The Hon. ADAM SEARLE: What is the time lag?

Mr DAVIES: It is one day. It is published in the morning for the day. I guess that it is a big difference between gas and electricity markets—

Mr SCOT MacDONALD: Five minutes.

Mr DAVIES: Five minutes—it is instantaneous. Electricity moves at the speed of light around the electricity network and the network has to be maintained in constant balance. If you inject gas at Moomba it arrives in Sydney three or four days later. So we are moving at a walking pace. People order their gas days in advance and it arrives at the other end of the pipeline days later.

The Hon. MICK VEITCH: I am interested in your comments in the submission about the availability of pricing. This Committee has heard evidence—people have recommended to us that the contracts around gas be made public so people have a greater understanding or a greater awareness as more information is available and there is a more transparent market in place for gas supply. What are your association's views about whether that should or should not be the case?

Mr DAVIES: I do not think our association supports publicly available information of every single contract. There are very few markets where that would be required; I cannot think of one. The vast majority of electricity is bought and sold under contracts that no-one knows anything about. I think there is benefit in knowing about total quantities in aggregate in terms of pipelines, so if there is available capacity for contract the association has proposed that that could be something useful to be published on the Bulletin Board so that there is one place where every gas market observer could see what capacity is available for contract. But in terms of either gas supply contracts or gas transportation contracts being made publicly available that does seem unnecessarily intrusive.

The Hon. ADAM SEARLE: In relation to your observation when you say that the quantum of gas demand in Australia is relatively low, has that been fairly static or has it declined?

Mr DAVIES: Gas demand right now is very static. It had been growing strongly up until three or four years ago and now it has been very static. But in terms of eastern Australia, I think one of the reasons we are experiencing the gas supply tightness that we are is a single LNG facility has as much gas demand as almost the entire east coast of Australia. That is what we mean by a relatively low gas demand in comparison to an international market.

The Hon. ADAM SEARLE: But the Australian Energy market operator has put forward that there has been a decline in gas demand for New South Wales over the last three or four years and it is projecting future diminutions in demand for both industrial and residential users going forward.

Mr DAVIES: I would say gas forecasting has been problematic over the last five or six years. Five or six years ago they were forecasting 10 per cent growth a year for 10 years.

The Hon. ADAM SEARLE: And that has proved not to be anything like the case.

Mr DAVIES: That is exactly right. Until we know what is going to happen with the gas price we are not going to know anything about how gas demand does eventuate. But on current projections gas demand will decline in New South Wales in particular but across the eastern seaboard.

The Hon. ADAM SEARLE: This is in advance of a shelf in Queensland opening up towards the foreign market?

Mr DAVIES: That is right, yes.

The Hon. MICK VEITCH: The problems around gas forecasting, what are some of the issues that has caused this to vary from what was forecast and the actual?

Mr DAVIES: I guess the gas price is the primary driver. It was widely anticipated that there would be a lot of new gas available as a result of the Queensland CSG developments and export linking and then that would fuel a wide availability of gas that would have increased gas use for electricity generation in particular, and a bigger switch from electricity to gas as a result of the strong carbon price, which also did not eventuate. Those two things are the two big drivers of the change of objectives.

The Hon. MICK VEITCH: Are there any other reasons? The forecasting is the issue. As the Hon. Adam Searle said, the projections just have not been met and it makes it difficult when people start talking about a supply shortage based on projections that so far has been more inaccurate than the weather forecasts.

Mr DAVIES: That is right. All we can go on is what people are experiencing in the market right now. It would appear that right now they cannot get gas supply contracts for the next few years**,** which means the producers—

The Hon. ADAM SEARLE: They cannot get long term.

Mr DAVIES: So you would expect that the producers are not confident they can meet both their export requirements and further domestic contracts.

The Hon. ADAM SEARLE: Or, alternatively, that they are holding back, wanting shorter-term contracts so that they can charge higher prices when people are convinced that there is a gas shortage that drives prices up—rent seeking, in other words.

Mr DAVIES: That is an alternative interpretation.

Mr JEREMY BUCKINGHAM: Mr Davies, in what sort of nick is the Sydney to Moomba gas pipeline that was built in 1975? Does it need replacing? What sort of condition is it in?

Mr DAVIES: It is in very good condition. The pipeline industry is constantly renewing its infrastructure. Usually the design life for a pipeline is initially 40 years when the Moomba to Sydney pipeline was built. Modern design life is 60 years, but the Moomba to Sydney pipeline has been maintained constantly and has, in the last few years, been confirmed that it has another 40 years of operational life left.

Mr JEREMY BUCKINGHAM: You say it has the capacity to supply 400 terajoules a day.

Mr DAVIES: Yes.

Mr JEREMY BUCKINGHAM: That is two-thirds of New South Wales' supply per day. What is the association's view of that into the future? Will the gas still be coming down that pipeline in the next year or 18 months going forward? What is the industry's view on whether or not there will be gas flowing from the Cooper Basin to Sydney in the short term?

Mr DAVIES: I will start by saying that the Moomba to Sydney pipeline has not really operated at full capacity since the eastern gas pipeline was built in the year 2000, so it is probably averaging around 50 per cent utilisation over the last decade—obviously not in peak times—but probably as an average. I can come back to you with the exact average. It has not been fully utilised for a long time. The expectations currently are from the public signals we see that with each utilisation it will stay flat at best, and could well decline. As well, a lot of Cooper Basin gas seems to be being contracted into Queensland and to export markets.

Mr JEREMY BUCKINGHAM: What do you mean by "could well decline"? Could you elaborate on that?

Mr DAVIES: Yes. If more gas is contracted from the Cooper Basin to Queensland and the existing production capability stays the same, that will mean that less gas is coming south out of the Cooper Basin.

Mr JEREMY BUCKINGHAM: Is it foreseeable that there will be no gas coming south?

Mr DAVIES: I think that would be the highly unlikely, but anything is possible.

Mr JEREMY BUCKINGHAM: Jemena in its submission states that even with the tightening supply conditions, they are well placed to maintain a continuous supply of gas to all residential and commercial customers. They also note that some of the largest industrial customers have entered voluntary agreements in exchange for discounted tariffs that will allow gas supply to be curtailed to them when the market gets tight. Could you speak to that? Is that, in effect, a gas rationing that is already occurring?

Mr DAVIES: I think that is customers who can change their requirements to suit their purposes and who can secure some cheaper gas now on a non-firm basis. They are offering, "We don't need it absolutely every day. On the days when demand is highest, we won't take any and, in return, we will be paying less every other day." That is the commercial market working to deal with the gas supply tightness that is being experienced.

Mr JEREMY BUCKINGHAM: But, in effect, it is rationing.

Mr DAVIES: "Rationing" to me implies an involuntary allocation of gas, and this is companies volunteering to curtail their gas use on days of high demand.

Mr JEREMY BUCKINGHAM: All of those companies are doing it because it is in their commercial interests rather than for any other reason.

Mr DAVIES: Presumably so.

Mr JEREMY BUCKINGHAM: What is the status of the Hunter to Wallumbilla gas pipeline proposal? It has been approved under New South Wales planning law linking the Newcastle-Hunter Valley north-west of the State with the Wallumbilla gas hub. Is it the association's view that this will go ahead into the future? Does this pipeline rely on the development of the coal seam gas industry—the unconventional gas industry—in the Hunter-New England region?

The Hon. NIALL BLAIR: Why do you not do them one at a time?

Mr JEREMY BUCKINGHAM: Because he is a smart man. He can deal with lots of things at once, mate, unlike you.

Mr DAVIES: The Queensland to Hunter Valley pipeline has been on the drawing board for over a decade, originally to bring gas south from Queensland to New South Wales. That was approved on that basis. More recently conversation has turned to "it could help develop New South Wales coal seam gas fields and transport gas into Queensland for export." It could also, probably if it did get built, end up being bidirectional and being able to bring gas from the Wallumbilla hub into New South Wales and take gas north, if it was approved it to do so. At the moment it really remains on the drawing board. We do not consider it to be likely to be built in the next five years.

Mr JEREMY BUCKINGHAM: What do you mean by recent discussions suggesting that it could be used to deliver gas into Queensland?

Mr DAVIES: On the back of New South Wales coal seam gas development, if a sufficient industry was developed, presumably one scenario is that that gas is made available into the Wallumbilla hub, equally as it is to New South Wales.

Mr JEREMY BUCKINGHAM: Gas from the New England north-west could be delivered to Queensland and the export market.

Mr DAVIES: Possibly.

Mr JEREMY BUCKINGHAM: That is very, very interesting. If Santos, say, were to not deliver the gas out of the Moomba pipeline, are the pipelines and storage potential in the East Coast Pipeline adequate to supply New South Wales gas demand, even at peak periods?

Mr DAVIES: You are saying in the scenario where there is no gas?

Mr JEREMY BUCKINGHAM: There is zero out of Cooper Basin.

Mr DAVIES: The current pipelines from Victoria are not big enough to meet all of New South Wales' gas demand.

Mr JEREMY BUCKINGHAM: How far short are they?

Mr DAVIES: There is about 400 terajoules available from Victoria under current arrangements. APA has committed to expansion of the New South Wales and Victoria interconnect and Jemena is actively pursuing expansion opportunities on the eastern gas pipeline, but there current combined capacity is about 400 terajoules a day, which is sufficient for average demand in New South Wales but is quite a bit short of peak demand in New South Wales.

The Hon. Dr PETER PHELPS: How much short? What sort of volume?

Mr DAVIES: Peak demand is 600 terajoules a day.

The Hon. Dr PETER PHELPS: So it is a full 50 per cent short.

Mr DAVIES: Thirty per cent short, 400 to 600.

Mr SCOT MacDONALD: Six hundred total.

Mr DAVIES: That is right.

CHAIR: That leads me to my question. I was going to ask about the potential expansion of the eastern interconnect and also the eastern pipelines coming from South Australia and Victoria. You have just mentioned that there are plans to increase the capacity in those.

Mr DAVIES: There is a committed expansion to the New South Wales-Victoria interconnect and there is active investigation of the eastern gas pipeline being expanded. But in terms of pipeline investment, pipeline investors do not build a pipeline and hope the gas will flow through them. Gas supply contracts and arrangements are finalised first and then you can commit to expanding the pipeline.

CHAIR: You say in your submission that pipelines are built on a just-in-time basis.

Mr DAVIES: Yes.

CHAIR: That is really what you are saying.

Mr DAVIES: Yes.

CHAIR: You have to have the demand there before you will commit, obviously.

Mr DAVIES: That is right.

CHAIR: You do not want infrastructure sitting there empty and being unused. Do you have a feel for what the extra capacity may be built into the interconnect and the eastern?

Mr DAVIES: No. There are a number of factors that will come into play. First and foremost it is how much extra processing facility is put on in Victoria to provide gas to Victoria or to the entirety of south-east Australia. There are probably a few commitments that need to be made in terms of expanding the processing facilities in Victoria. That will give an indication of how big the gas supply would be, but I think it would be unlikely that the pipelines from Victoria would expand to such an extent as to meet all of New South Wales' gas demand. I think some gas will continue to always come from South Australia.

CHAIR: Okay. By inference, the expansion would not be sufficient to replace what may be lost coming down from the Moomba field.

Mr DAVIES: I think that is the most likely scenario, yes.

Mr JEREMY BUCKINGHAM: Recently there was a lot of noise made by the New South Wales Chief Minister about the possibility of a pipeline from the Northern Territory.

CHAIR: Chief Minister?

The Hon. Dr PETER PHELPS: The Northern Territory Chief Minister.

Mr JEREMY BUCKINGHAM: What did I say?

Mr SCOT MacDONALD: New South Wales.

Mr JEREMY BUCKINGHAM: I am sorry, the Northern Territory Chief Minister it is. He spoke about a pipeline to New South Wales.

Mr DAVIES: Yes.

Mr JEREMY BUCKINGHAM: Potentially via the Cooper Basin and the like. What is the prospect of that? If we have falling demand for gas in New South Wales—we have had overoptimistic forecasts from AEMO and others for electricity and gas for a long time when there is actually falling demand and we have not even seen the flow-through of prices—is that a viable prospect in the short-to-medium term?

Mr DAVIES: I think in the medium term it definitely is a viable prospect. It depends. There are a lot of factors that will contribute to that, but it does present a really good opportunity to expand the eastern Australian gas market. APIA certainly views that the bigger the gas market is, the more competitive, viable, flexible and liquid it will be. There is certainly potential for that pipeline to be built.

Mr JEREMY BUCKINGHAM: Is that potential based on supplying New South Wales or, more likely, supplying a shortfall of gas to the east coast gas traders?

Mr DAVIES: If the pipeline gets built, it will probably be built on the basis that it is supplying the entirety of south-east Australia, not just New South Wales. Some gas could certainly flow into South Australia as well or to Adelaide, and some gas would probably go into Queensland as well. But I think just meeting the New South Wales demand shortfall may be a stretch to make a business case for that pipeline.

Mr JEREMY BUCKINGHAM: Would you describe it as a panic pipeline—a pipeline that we are dealing with right now because the Queensland export industry is short on gas?

Mr DAVIES: I would not describe it as a panic pipeline but I would say that maybe some of the enthusiasm about that pipeline is seen as a short-term solution to a much bigger issue.

The Hon. Dr PETER PHELPS: Firstly, Mr Davies, I thank you for pointing out what a number of witnesses have not pointed out, which is that supply increases result in an increase in supply. It is an important concept to state and something that do not think The Greens fully understand.

Mr JEREMY BUCKINGHAM: Not necessarily. It depends if you have availability. It is complex, mate.

The Hon. Dr PETER PHELPS: How many pipeline companies are there in Australia?

Mr DAVIES: In Australia?

The Hon. Dr PETER PHELPS: Yes.

Mr DAVIES: In terms of pipelines, companies that are specifically there to provide transportation services to others and are not really transporting their own gas, there are five major gas transmission companies.

The Hon. Dr PETER PHELPS: Would any of those have a market share greater than, say, 40 per cent?

Mr DAVIES: There is one company that has a market share greater than 40 per cent.

The Hon. Dr PETER PHELPS: Which is that?

Mr DAVIES: That is the APA Group.

The Hon. Dr PETER PHELPS: There has been some discussion about oligopolistic behaviour within the broader gas market. Retailers blame producers, produces blame pipeline owners.

Mr DAVIES: Yes.

The Hon. Dr PETER PHELPS: From your point of view, is there any evidence of that being the case—of supernormal profits?

Mr DAVIES: Look, certainly not in the pipeline industry. There are a lot of claims made by all parties against all other parties and they are claims which, when questioned, evidence most often seems to fail to materialise. But in terms of the pipeline industry, the pipeline industry does have access regulation under the national gas law. Pipelines that are deemed monopoly pipelines are fully regulated by the Australian Energy Regulator. Pipelines that are deemed to be in competition with other pipelines are not automatically regulated, but if there are concerns about market abuse, they can be applied for coverage by full regulation.

The Hon. Dr PETER PHELPS: Would it be fair to say that the fact that there are five companies is more due to the size of the market or the potential market for pipeline work, or is there some other factor at play?

Mr DAVIES: I think it is more the potential market. The reality of Australian gas demand is that every major gas demand centre in Australia can be serviced by one or two pipelines. There is just not a market that is going to foster multiple pipelines being built to a single destination, in which case you are going to see a small number of companies owning most of the pipelines when there is not actually business case to build very many major pipelines at all.

The Hon. Dr PETER PHELPS: One of the suggestions that has been put forward is that New South Wales does not have to develop an indigenous coal seam gas industry because we can just get all or the overwhelming majority of a gas from Victoria. What would happen if Longford caught fire again in that situation?

Mr DAVIES: If Longford caught fire again, then Victoria, New South Wales and South Australia would all be experiencing gas shortages.

The Hon. Dr PETER PHELPS: By rejecting an indigenous gas supply and relying essentially on a single supplier, you are putting all your eggs in one basket with the attendant security risks which would flow from that?

Mr DAVIES: Yes.

The Hon. Dr PETER PHELPS: You mentioned the city Moomba. There has been talk that there will be so much demand on that from overseas exports that there will literally be no gas flowing into New South Wales. Why do you believe that that will not be the case?

Mr DAVIES: I am not very good on international gas markets and how those prices are determined, but the reality is there will always be some gas users in New South Wales who are willing to pay international market prices for gas from Moomba.

The Hon. Dr PETER PHELPS: And that would also mean that a company like AGL, which if it is denied its ability to vertically integrate and produce its own upstream gas will still have to rely on those markets for its retail base, will it not?

Mr DAVIES: That is right, yes.

The Hon. NIALL BLAIR: Other witnesses have told us how much it costs to build pipelines per kilometre, for example. I would like to hear from the actual industry the costs associated with either expanding or building pipelines?

Mr DAVIES: To some extent it is how long is a piece of string because every pipeline is very different.

The Hon. Dr PETER PHELPS: How long is a piece of pipeline?

Mr DAVIES: To New South Wales, usually about 1,000 kilometres. Expanding an existing pipeline is almost always a cheaper proposition than building a new pipeline.

The Hon. Dr PETER PHELPS: Sorry, do you mean duplicating or just—

Mr DAVIES: Both. Usually you would duplicate. I am not aware that you would dig up an existing pipeline and replace it with a larger diameter.

The Hon. MICK VEITCH: That is along the same corridor, is it not?

Mr DAVIES: That is right. You put it next to it. Basically, if you put two pipes next to each other and connect them along the way you have effectively just made a single larger diameter pipeline. The costs are highly variable and are not usually measured in terms of how much capacity you deliver. I think for a major pipeline project some of the numbers that we have heard are about right. We are talking many hundreds of millions of dollars, if not close to a billion dollars, to build a 1,000 kilometre long pipeline.

The Hon. NIALL BLAIR: Most of the pipelines that are being built are being done through private organisations?

Mr DAVIES: All of them are.

The Hon. NIALL BLAIR: I have had representations from some communities, particularly in the southern Riverina—Deniliquin for example—where the nearest pipe to them is Griffith or Culcairn, I think. It is a community that is looking for other ways to attract jobs and industry growth to the area. At the moment the economics would not stack up for a private operator to come in and say, "We'll extend the pipeline either down from Griffith or across from Culcairn."

Mr DAVIES: No, that is right.

The Hon. NIALL BLAIR: So there are no cases where as part of regional development—

Mr DAVIES: In Victoria there has been Gas for the Regions funding that has funded gas connections to smaller towns. There is the kind of large industrial customer that would usually underpin pipeline investment. That has occurred.

The Hon. Dr PETER PHELPS: If you build it they will come.

The Hon. NIALL BLAIR: Yes.

Mr DAVIES: That is correct, yes. And the Government has chosen to subsidise the cost of that infrastructure.

The Hon. NIALL BLAIR: What sort of return time frame have they been built on? Are you aware of the specifics around that?

Mr DAVIES: I could get you some information on that. I know we do have some but I am not familiar with how it works.

The Hon. NIALL BLAIR: The straight out economics, you can see where a Committee like this is, like the concept, build it and they will come. They have an abundance of land, they have plenty of people who want the work and they are looking to attract other industries. So it may be thinking outside the square because no private company will turn around and put money into that at the moment.

Mr DAVIES: No, that is right.

The Hon. Dr PETER PHELPS: From the industry perspective is there a significant regulatory or environmental burden on greenfield pipeline development specifically in New South Wales? We cannot talk about other States.

Mr DAVIES: Not specifically in New South Wales but there has not been a major greenfield pipeline in New South Wales in some time.

Mr SCOT MacDONALD: Except Gloucester.

Mr DAVIES: I am not familiar with the Gloucester pipeline. I guess in the scheme of things it probably does not count as a major greenfield pipeline.

Mr SCOT MacDONALD: We have heard assertions that gas will be taken out of Gloucester, the northern rivers, New England or the north west for the export market. Particularly with those sites like Gloucester, is there any discussion at all about the pipeline industry shifting that anywhere else but into the Newcastle and Sydney markets?

Mr DAVIES: Not that I am aware of, and right now pipelines typically flow in one direction. There are one or two pipelines in Australia that are bi-directional pipelines but right now there is no pipeline capacity to take the gas out of New South Wales.

Mr SCOT MacDONALD: What you have just said is very important. Can you give me some insight into the pipeline industry, how its confidence levels are when you hear policy discussions and suggestions of moratoriums around an indigenous gas industry?

Mr DAVIES: The pipeline industry is uneasy and it is a trying time to be in the gas industry in any regard except as an exporter.

Mr SCOT MacDONALD: When you expand on that can you talk about what investment decisions might mean for price and jobs?

Mr DAVIES: In terms of transportation price it will not mean a lot. A moratorium in New South Wales also presents opportunity to the pipeline industry because there is a business case for pipelines from Victoria and South Australia to continue or, in the case of Victoria, to expand even more.

Mr SCOT MacDONALD: So become more reliant on our southern suppliers.

Mr DAVIES: That is right. I am not sure if you can become more reliant on interstate suppliers.

Mr SCOT MacDONALD: With associated transmission costs, say, pulling out of Bass Strait and Gippsland, presumably that has an impact on cost?

Mr DAVIES: It does but it is already factored into the cost of gas in New South Wales. I am not sure of the exact percentage but it is probably close to 50 per cent of your gas is already coming from Victoria with transportation costs. Another 45 per cent is coming from South Australia with transportation costs. So those transportation costs are already being paid.

Mr SCOT MacDONALD: If you inject an indigenous gas industry into that equation with lower transmission costs, what sort of impact are we are looking at? Pulling out of Gloucester? Pulling out of the Pilliga? Pulling out of Camden?

Mr DAVIES: As a rough estimation—

The Hon. MICK VEITCH: Narrabri.

Mr SCOT MacDONALD: Pulling out of Narrabri?

Mr DAVIES: They would all have different costs but they would all be lower than the long distance transportation costs that are currently paid.

Mr SCOT MacDONALD: Can you give us a rough estimate, a broad figure, per gigajoule?

Mr DAVIES: Per gigajoule, potentially half the price; 50¢ a gigajoule instead of $1.00 a gigajoule.

Mr SCOT MacDONALD: And that flows onto wholesale, it flows onto the retail price.

Mr DAVIES: In a competitive market it would.

Mr SCOT MacDONALD: Cost for our manufacturers.

The Hon. NIALL BLAIR: I go back to the concept of trading, for example. At the moment that is not being regulated; that is just being done by the wholesaler to their customers basically. Is that the concept?

Mr DAVIES: Are you talking about capacity trading facility?

The Hon. NIALL BLAIR: Capacity trading, yes.

Mr DAVIES: Capacity trading specifically is now done on a shipper to shipper basis. Anyone who has a contract on a pipeline can trade their contracted capacity to other shippers. The reality is that the Australian gas market is quite small both in terms of volume and in the number of participants. Most pipelines have under 10 customers; almost all pipelines have well under 10 customers. Customers tend to know who the other customers on a pipeline are and pick up the phone and arrange trades.

The Hon. NIALL BLAIR: Is a comparison of that happening across other markets or other pipelines, do you know?

Mr DAVIES: No. I am not aware of any comparisons.

The Hon. NIALL BLAIR: And that is not happening at the retail level; these are larger retail.

Mr DAVIES: I think larger retailers trade between themselves usually on short-term arrangements to facilitate small imbalances that might be occurring, but you would have to ask a gas retailer about that. I cannot really comment reliably.

The Hon. Dr PETER PHELPS: Why would shippers not have a better estimation of their likely demand for capacity? Why would they need to effectively spot price sale that extra cost?

Mr DAVIES: In the current environment it tends to be short-term fluctuations in terms of we ordered gas—

The Hon. Dr PETER PHELPS: Of production or of demand?

Mr DAVIES: It is mostly demand in terms of the weather forecast, three days out, can get things wrong by a couple of degrees and in winter that can have a big impact on gas demand.

The Hon. MICK VEITCH: You were talking about the costs of construction for pipelines. Is there a huge variance internationally? For instance, in the US where there is a large market, is the cost of construction significantly lower?

Mr DAVIES: Not that I am aware of. I have never really heard any comparison of construction costs. I guess every country has its own unique circumstances for construction costs and its probably the health and safety environment that contributes to the biggest variation—

The Hon. MICK VEITCH: There are also local vagaries such as geography?

Mr DAVIES: That can occur within a country as well, yes, but I have not heard any comparisons one way or the other so presumably they are fairly similar.

The Hon. MICK VEITCH: I am fascinated about capacity trading and how it works. I understand the explanation you provided such as temperature impact. How often does that occur? How often does capacity trading occur?

Mr DAVIES: I think it is fair to say that it does not occur a great deal.

CHAIR: Thank you for your attendance. I do not think you have taken any questions on notice.

The Hon. NIALL BLAIR: Yes, there was the follow-up on the Victorian Gas for the Regions.

CHAIR: Given the short time frame for this inquiry, the Committee has resolved that answers to questions on notice be returned within seven days. We would appreciate your help in assisting us to meet our reporting deadline. The secretariat will contact you in relation to questions you have taken on notice.

Mr SCOT MacDONALD: Is the Victorian thing continuing?

Mr DAVIES: I think most gas policy in Victoria is up for debate at the moment but I believe that the task force run by Peter Reith—

Mr SCOT MacDONALD: Thank you.

(The witness withdrew)

(Luncheon adjournment)

GABRIELLE KUIPER, Senior Policy Officer, Public Interest Advocacy Centre, and

OLIVER DERUM, Senior Policy Officer, Public Interest Advocacy Centre, affirmed and examined:

CHAIR: Welcome. Would you care to make a short statement?

Dr KUIPER: We would be delighted. Thank you very much for the opportunity to speak with the Committee this afternoon. Regardless of the issue of supply, the Public Interest Advocacy Centre's [PIAC] primary concern about the issue of gas is in respect of equity. As you may know, the Public Interest Advocacy Centre is a community legal and policy centre. It works across a wide range of areas—everything from running a homeless persons' legal service to Indigenous justice. For the past 15 years, PIAC has been funded by the New South Wales Government to run an energy and water consumer advocacy program. We are actually funded by the New South Wales Government to advocate on behalf of all residential consumers in New South Wales, but we have a particular interest in low income and vulnerable consumers. The evidence we will be speaking to today will be from that perspective.

We have a number of ways in which we can engage with the gas market and gas market issues. My colleague, Oliver Derum, sits on the consumer consultative groups for Jemena gas networks and also for AGL. A year ago we ran a gas master class for all of our fellow consumer advocates from around the country to get them up to speed in this rapidly changing policy area. We obviously engage with the New South Wales Government on a regular basis, so we have a wide range of engagement on gas issues.

Obviously we are here because we are very concerned about the gas price rises. We are concerned not only about the prospective rises, but also about the fact that they come on top of previous rises to date and obviously all households that have gas in New South Wales have electricity as well, and we have seen dramatic price rises in electricity primarily because of the price rises due to increases in network revenue.

Combined electricity and gas have gone from being relatively affordable for Australian consumers 10, 15 years ago to being relatively unaffordable, particularly for low income households. Obviously we are very concerned about that because electricity and gas provide essential services and particularly because of what that means for the remainder of expenditure for households if they have to spend a higher proportion on electricity and gas bills. However, we do not yet know enough about what the consequences are of the past or projected future gas price rises because the analysis has not been done. The Alternative Technology Association [ATA] has done an excellent report, which we commend to you, called "Are we still cooking with gas?" It looks at the consequences of gas price rises by household type and by location throughout Australia. We have tried to find out more. Particularly, Mr Derum wrote to the New South Wales Department of Housing to try to find out what proportion of public housing units have a gas connection and for what purposes. We put that inquiry in more than three months ago and are yet to hear anything back. It seems to us there is not enough information available about what proportion of public housing has gas connected and for what services, what proportion of other social or community housing has gas and, in general, in the private housing market for low income rentals, what proportion of those households have both electricity and gas? We think that a distributional analysis is needed and it is really important that that is done, so then we can get a better understanding of what are the consequences.

More broadly, PIAC's position on concessions is that they need to be increased and they need to be proportional to people's bills. Obviously it is more complicated to set up a proportional concessions regime. It is easier to give a fixed $100, $200, $300, but that is not equitable and it does not take into account family size or the amount of gas that people may use for a whole variety of reasons, or the amount of electricity they may use. Obviously there are fundamental changes needed that we will talk about in respect of energy efficiency in homes and the like but, for starters, the concessions regime needs to be examined and looked at in respect of how can a proportional concession be set up?

Also, consumer protections is an area where New South Wales lags Victoria. There can be debate about Victoria's refusal to sign up to the National Energy Consumer Framework [NECF], but the fact that there are significant protections in Victoria like a lack of exit fees, we think, needs to be looked at because it seems inequitable that there are consumers in New South Wales who are forced to pay exit fees when they are not in Victoria, and obviously provisions like that are likely to affect low income households more than the general public.

So concessions, consumer protections and then we would like to recognise the good work that the New South Wales Government has done with the Home Power Saving Program, which was a low income energy efficiency program that the Committee is likely to be aware of. We understand the New South Wales Government has been looking at what are the next steps in respect of low income energy efficiency programs and we would absolutely support this as a vital area for Government investment. Obviously not only do energy efficiency programs lower people's bills, especially if they tackle the household fabric, it has the opportunity to improve people's comfort in their homes, but it also potentially has health benefits. So we would like to see more done in that area.

One area where there has not been work done to date, so far as we are aware, is the potential to assist low income households—people who own their own home—to install solar systems. Mentioning Government involvement in solar can be controversial. However, we would like to draw the Committee's attention to the program that is being run by Darebin Council, using the same method as environmental upgrade agreements, which is in the New South Wales legislation as well. What they have done is paid the up-front costs for pensioners to install solar photo-voltaic systems on their roofs and for that cost to be repaid through people's rates. That way, people's bills are reduced, but they do not have to come up with the up-front capital cost. Obviously policies that support rollout of distributed generation like that will, in the end, with the right regulatory regime, reduce network costs as well through having more distributed generation.

Mr JEREMY BUCKINGHAM: Hear, hear!

Dr KUIPER: Our final point would be, please, we understand there has been some consideration of subsidising the rollout of gas networks to rural and regional areas. PIAC would not support that as a policy. Obviously there is a lot of uncertainty—in fact, we believe there is too much uncertainty around the price rises to go ahead with a policy like that. We know from the ATA's analysis that if you are building a new home it is not cost effective to connect to gas now when you are putting in efficient electric appliances in houses, and we would hate to see a policy of subsidising the rollout of gas infrastructure basically locking people in to higher than necessary bills. That is a range of our interests and our position on various consumer matters relating to the gas network. We welcome your questions.

The Hon. MICK VEITCH: You mentioned a council in your opening remarks, which council is that and where is it?

Dr KUIPER: This is Darebin Council in Victoria. I should have been clearer that it is in Victoria.

The Hon. MICK VEITCH: You may not have this information and you may wish to take it on notice, but are you aware of the current level of energy poverty in New South Wales?

Mr DERUM: There is not even agreement about what energy poverty is. The most solid definition is from the United Kingdom where it is 10 per cent of income, but it has not been looked at in Australia. The Independent Pricing and Regulatory Tribunal [IPART], certainly when they had a bigger role in monitoring New South Wales energy markets, would break it down by decile of income and how much people in those groups spent on energy.

Dr KUIPER: We would have to confirm this on notice, but the last IPART figure, if I remember correctly, suggested that it was up to 14 per cent of people's household income in the lowest decile that they were spending on energy bills, so it is quite significant. I think what is so significant is that it has risen so quickly, the combined rise of electricity and gas.

The Hon. ADAM SEARLE: I am interested in the financing of the Darebin Council experience in Victoria. If you have any further information on that, can you provide that to the Committee on notice?

Dr KUIPER: Absolutely, happy to provide it to the Committee. Are you aware of how environmental upgrade agreements work in general?

The Hon. ADAM SEARLE: No.

Dr KUIPER: This is a financing mechanism that is called PACE, Property Assessed Clean Energy, from the United States, so it started there. I think I have got that acronym right; I will confirm that for you. It was started first in Australia through the City of Melbourne. The legislation was passed through the Victorian

Parliament to allow for environmental upgrade agreements [EUA], whereby a building owner could decide that they were, for example, going to put in a new more efficient air-conditioning system and this was focused on commercial office buildings in the central business district, but equally applicable to residential. The mechanism is that there is public or private sector finance, but that the costs of that are recouped by the council in the same way that the rates are. So that solves the problem of the potential split incentive for an owner to install equipment and then sell a building without having recouped the cost. Effectively the cost of the upgrade sits with the building in the same way that a rates requirement does.

The Hon. ADAM SEARLE: Who finances the upgrade?

Dr KUIPER: That could be anyone. I do not think there are any restrictions on that. In the case of Darebin, I believe the council tapped into their own funds to do it because it was only 100 households, but there is no reason it could not be third party financing.

The Hon. ADAM SEARLE: It would depend whether the third party financier was prepared to have the rate of pay back that could be generated, so it is constrained by that?

Mr DERUM: Yes.

Dr KUIPER: Yes.

The Hon. ADAM SEARLE: Any information you have about that would be greatly received.

Dr KUIPER: Sure.

The Hon. ADAM SEARLE: You talk about the need to revise the concessions regime to make it a proportionate rebate. Is that what happens in Victoria?

Mr DERUM: Yes, it is. It is 17.5 per cent.

The Hon. ADAM SEARLE: Is there an upper limit?

Mr DERUM: There is, but from discussions with welfare agencies in Victoria we understand that once people reach the upper limit—I will have to check what it is—they go through a further check with the department. However, they generally say that they still meet the requirement.

The Hon. ADAM SEARLE: What is the cost of running that scheme on a proportionate basis? If you do not know, you can take the question on notice.

Mr DERUM: Yes.

The Hon. ADAM SEARLE: I think the low-income household rebate in New South Wales is a flat amount.

Dr KUIPER: All the concessions in New South Wales are flat amounts. Obviously we would not want to see a proportional rebate that reduced the amount households are getting. However, provision could be made for a floor if there were changes. We are aware that it is not as easy to administer and there are complexities. Obviously it is more equitable and the retailers are supportive.

The Hon. ADAM SEARLE: I would appreciate it if you could take on notice whether there are any constraints on scheme participation.

Mr DERUM: It is the same as New South Wales; that is, it relates to Centrelink entitlements or the age pension.

The Hon. MICK VEITCH: I refer to the disincentives for someone to convert from gas to another power source, which were raised last week by the Melbourne University Energy Institute. What are some of the disincentives and how can they be corrected?

Dr KUIPER: Obviously the biggest barriers exist for those people who do not own their home. We understand there are some housing units that have two gas hot-water systems—one for the kitchen and one for the bathroom. If both are inefficient, the gas price rise will have an exacerbated effect. There is obviously a massive split incentive when you have a landlord/tenant residential relationship, and that is largest disincentive. For low-income households, simply having access to the capital to upgrade those facilities where they own their home is significant. Of course, there are also information barriers and the like. There is a great deal of confusion about whether they should convert from gas. It has been relatively recent that electrical appliances have become highly efficient. People are not necessarily aware that there are efficient air conditioning options and that they can use air conditioning units for heating as well as cooling. There are many awareness issues as well.

The Hon. MICK VEITCH: The Committee has heard evidence that more transparency in gas pricing would help consumers.

Mr DERUM: It would definitely help groups like ours in the work we do as a full-time job. I do not think there would be that many household consumers who would be following the rise and fall in gas prices. We find that in any of these complex areas as soon as they are subjected to external scrutiny it becomes clear that all sorts of things could be improved. We would definitely welcome more transparency.

The Hon. MICK VEITCH: I refer back to my question about energy poverty, and I acknowledge that the definition is flexible around the world. Is there not an issue around people's capacity to pay, particularly in winter months?

Mr DERUM: It is a huge problem. The number of people who have had their electricity disconnected—I will have to check the figures for gas—has doubled in five years. Gas is now increasing similarly. When you cannot pay your bill, you go onto a payment plan and the conditions of that plan are outlined in the law. The plan is meant to be calculated having regard to your debt, your capacity to pay and your likely future consumption. The problem is that given what prices have done those circles do not overlap anywhere for people with low fixed incomes. They cannot stay connected and pay off their debt, and that is why we are seeing disconnections going through the roof.

The Hon. ADAM SEARLE: That is one of the problems with the proposal to have prepaid meters. It would remove the visibility of those kinds of disconnections caused by poverty or low income.

Mr DERUM: If prepaid meters were implemented in the way it has been done in nightmare cases in the United Kingdom we would have a problem.

The Hon. MICK VEITCH: Has anyone mapped disconnections across the State to establish where they are more prevalent?

Dr KUIPER: We can take that question on notice. The Energy and Water Ombudsman collects that data and that office would be the best source of that information.

Mr DERUM: But reporting of the number of disconnections has just moved from the Independent Pricing and Regulatory Tribunal to the Australian Energy Regulator [AER] and I am not sure what detail goes into it.

Mr JEREMY BUCKINGHAM: To be honest, you have answered all my questions both here and in your submission. You say that the repeal of the carbon tax is relatively insignificant in the face of rising wholesale prices. Would you agree that if gas prices doubled, coal seam gas production were allowed and prices reduced by 3 per cent—as the New South Wales Government has suggested they will—that that would also be relatively insignificant?

Dr KUIPER: If you are talking about doubling—

Mr JEREMY BUCKINGHAM: If the wholesale price doubles or triples and an Indigenous coal seam gas industry is developed in New South Wales, the State Government's modelling suggests that that would lower prices by 3 per cent as opposed to there being a 200 per cent or 300 per cent increase.

Dr KUIPER: I am not sure we are in a position to answer such a speculative question. There are many ifs and buts. It all depends on what happens to network prices, concessions and the like. I do not know that we know enough to say that the development of a coal seam gas industry in New South Wales would reduce prices. There seems to be a lot of debate about how much this is a supply problem and how much it is a price issue.

Mr JEREMY BUCKINGHAM: I agree.

Mr DERUM: We can agree that three is less than 10 when speaking about numbers generally though.

Mr JEREMY BUCKINGHAM: And less than 300. How easy is it for renters to transition away from gas? What are some of the issues? Will renters be disproportionately impacted by rising prices?

Mr DERUM: It is very hard. Only if someone is renting a really good property and they plan to be there for a long time would they bother to have a stake in the fixed appliances. If an appliance broke down and the renter was well informed, he or she could request that it be replaced with an electrical appliance rather than a gas appliance. People on low incomes are overwhelmingly renters, so they will feel the impact more strongly.

Dr KUIPER: If I recall correctly, the ill-fated green loan scheme was available to landlords, but there was negligible take-up, and that was with government incentives. Obviously, there are always cases where landlords will seek to increase the value of their property through upgrades. However, where there is such a significant split incentive whereby the tenant is paying the energy bills—whether it be electricity or gas—it will not be in the landlord's interests to upgrade the appliances and services whether they be electric or gas heating, hot-water services or air conditioning.

Mr JEREMY BUCKINGHAM: I understand. I refer to environmental upgrade agreements. I assume that the liability for repaying them over 10, 20 or 30 years rests with the owner if the house is sold?

Dr KUIPER: Yes.

Mr JEREMY BUCKINGHAM: The liability is attached to the contract of sale stating that the solar panels or the wind turbine are fixed to the property going forward?

Dr KUIPER: It is similar to a rates liability with the local council; it sits with the property. I should have clarified that the first legislation in Australia was passed in Victoria with regard to the City of Melbourne. However, that legislation was subsequently also passed by the New South Wales Government and is applicable across the State.

Mr JEREMY BUCKINGHAM: What legislation is that?

Dr KUIPER: I will have to take that question on notice. It is essentially the same legislation as was passed in Victoria with regard to environmental upgrade agreements.

Mr JEREMY BUCKINGHAM: I would appreciate that. Do you have any information about how successful it is? What was the uptake, who entered into agreements and who benefited?

Dr KUIPER: As I understand it, it has been used only in the City of Sydney local government area to date for commercial building upgrades. The Darebin case was the first time I have seen it used for residential buildings. It was certainly the first time it has been used to provide solar photovoltaic systems for low-income households. I will take on notice the question about the number of agreements entered into in New South Wales.

Mr JEREMY BUCKINGHAM: And Victoria if you could.

Dr KUIPER: Yes.

Mr SCOT MacDONALD: I refer to recommendation No. 4 in your submission dealing with energy efficiency. I am thinking of public or social housing. Surely one way to increase efficiency would be to move people out of draughty houses into better houses? Do you have anything to say about the housing stock?

Dr KUIPER: Yes. It is one thing to upgrade hot-water systems in public housing, but if the building is old and draughty and has poor insulation and glazing it will be of limited value. We should have either comprehensive upgrades or move people into new and super-efficient housing.

Mr SCOT MacDONALD: It sounds as though you are talking about Millers Point.

The Hon. Dr PETER PHELPS: Did you say the council scheme was limited to 100 houses?

Dr KUIPER: Yes, to date. It was rolled out as an initial scheme late last year.

The Hon. Dr PETER PHELPS: Was there any reason it was limited to 100, or was it simply because of the council's financial ability to carry that debt?

Dr KUIPER: I am not clear about the exact rationale; that is, to what extent it was debt related or that it was a novel and innovative program.

The Hon. Dr PETER PHELPS: What public benefit accrues? Why is the council providing its money for what will ultimately be a private benefit for the individuals in those houses?

Dr KUIPER: There are benefits at a number of different levels. In respective of the supply chain for electricity at the wholesale level, we have a free wholesale market in generation. To a significant extent demand/supply operates in the national electricity markets. If you have a lower level of demand from the centralised generators connected to the grid then the price will fall. As with the renewable target, when there is support for decentralised generation, in this case with solar, then the wholesale price will fall. You may be aware that the modelling that was done for the Federal Government's RET review showed that the renewable energy target—to try and paraphrase it—paid for itself because the wholesale price would fall to such a large extent over time. So there is a public benefit on the generation side.

Then if you take transmission, which are the largest poles and wires that go from the power stations to the outskirts of cities, there is roughly of the order of 10 per cent of losses along those transmission lines. So you avoid those losses by generating on-site and then, with the next stage of the supply chain, with the distribution, the smaller poles and wires and substations from the outskirts of cities to the houses, as you would be aware, that is now half of all bills in New South Wales, which it should not be. But because of the large investment, those assets have been built to a higher level than required, especially when solar has been increasing. But if the regulatory system works well and recognises the distributed generation in the system, then we should need a much lower level of investment in the distribution networks.

Then obviously, on the fourth part of the supply chain is retailers. And obviously, every private individual who puts solar on their house is reducing the retail costs effectively for everyone else because the retailers are supplying fewer electrons through the NEM. People are supplying it from their own houses. So, at every stage on that supply chain, from the generator in a centralised coal-fire generator to the household, you are getting public benefit through people putting PV on their homes.

The Hon. Dr PETER PHELPS: I am not sure your definition of "public benefit" and mine are the same, because those last three instances are all instances where the generator has received a benefit or the consumers of that, other consumers receive a benefit in terms of reduced pricing through supply and demand. But that is by the by.

Dr KUIPER: There would be also one other fifth benefit, if you like, particularly because these were pensioner households, people who, in almost all cases, would be in receipt of some kind of Commonwealth benefit and State concessions, that there would be a public benefit because you would need a smaller dollar value of State concessions because these households have PV on the roofs.

Mr JEREMY BUCKINGHAM: Good point.

Dr KUIPER: You would have a lot more people living in energy poverty, with all the consequences of that.

The Hon. Dr PETER PHELPS: You talked about supply and demand curves. If there is an increase in supply in a closed market, won't that also decrease price, the equilibrium price?

Dr KUIPER: Closed market—in what sense?

The Hon. Dr PETER PHELPS: For example, if AGL has decided that it wants to increase supply of its domestic production purely for the New South Wales market and not tap into the international market, won't that increased supply for that closed market also reduce price or have a greater tendency to reduce price?

Dr KUIPER: Are you saying that the New South Wales gas market is a closed market?

The Hon. Dr PETER PHELPS: I am saying AGL's wholesale and retail base is a closed market, yes.

Dr KUIPER: For gas?

Mr DERUM: If AGL had a lot of gas and said, "We are only going to sell this to New South Wales households at a lower price" yes, that would lower the price. But the issue of reservation of gas and specific allocations we would say has no impact on price, only potentially on availability. So, for households that are at the end of the order of curtailment—

The Hon. Dr PETER PHELPS: Hold on—Dr Kuiper said that demand changes have changes in price but are you saying supply changes have no change in price?

Dr KUIPER: To clarify, I was talking about how the wholesale electricity market works, which operates slightly differently in regard to putting solar PV on roofs. In terms of gas, just to give an overarching answer, what the challenge here is the debate about to what extent this is a supply problem and to what extent it is a cost problem, in light of the internationalisation of gas prices.

The Hon. Dr PETER PHELPS: But the supply problem has to do with the fact that, if you have to buy at a world market price, it is likely to be a higher retail price, is it not?

Mr DERUM: Yes.

The Hon. Dr PETER PHELPS: If AGL—as it has—has announced that it wants to vertically integrate and produce its own gas so that it can sell at a cheaper rate without having to buy at the international gas market rate, will that not necessarily reduce or have the potential to reduce the costs of the retail gas prices in New South Wales?

Mr DERUM: It would if AGL said: We are going to sell this gas to ourselves at a price that is lower than the net back price, the price in Japan less the cost of transportation. Have they said that?

The Hon. Dr PETER PHELPS: Yes.

Mr DERUM: That the price at which they are going to sell it will be lower?

The Hon. Dr PETER PHELPS: Yes, otherwise why would they bother? Why wouldn't they simply buy at the international market rate?

Mr JEREMY BUCKINGHAM: Because they cannot get it; that is the point. It is not the price, it is that they cannot get it at all.

The Hon. Dr PETER PHELPS: That is not what we heard. For AGL and its own corporate requirements, would it not be better for consumers to have a greater degree of supply which was not tied to international market rates?

Dr KUIPER: It is beyond our scope to talk about the issue of supply separate from—the issue of supply, full stop. Our concern is the price which people are paying. And it is the internationalisation of the price that is the key concern and being aware that, even if the sale price is net back less the transportation costs, that will still be higher than what it has been to date. And we know that gas and electricity are now both relatively unaffordable, compared to what they were 10 years ago. So the current price is a problem for those on the lowest income and the most vulnerable consumers in New South Wales, regardless of any future scenarios.

CHAIR: You have answered all the questions. Thank you for attending the hearing. You took a question on notice. Given the short time frame for this inquiry, the Committee has resolved that answers to questions on notice be returned within seven days. We would appreciate your help in assisting us to meet our reporting deadline. The Secretariat will be in contact with you in relation to the questions you have taken on notice. Thank you for attending.

(The witnesses withdrew)

KIERAN DONOGHUE, General Manager Policy, Energy Supply Association of Australia; and

SHAUN COLE, Policy Advisor, Energy Supply Association of Australia, affirmed and examined:

CHAIR: Would you like to start by making a short statement?

Mr DONOGHUE: Yes, we have a short opening statement. I thank you for the opportunity to give evidence today to the New South Wales Legislative Council's Inquiry into the Supply and Cost of Gas and Liquid Fuels in New South Wales. The Energy Supply Association of Australia [ESAA] is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the chief executives of 37 electricity and downstream national gas businesses. These businesses own and operate some $120 billion in assets, employ more than 59,000 people and contribute $24 billion directly to the nation's GDP. Our members transport gas, retail gas and use it as a feedstock in electricity generation, both in New South Wales and in the other states and territories. A few also have upstream interests in gas. As such, our interest is in the availability of gas in New South Wales and a well-functioning market. An important element of the latter is the number of buyers and sellers.

Appropriate exploitation of New South Wales' own gas resources will support a well-functioning gas market by adding to the range of potential sellers of gas. The New South Wales Government's recent declaration that it is committed to growing a local gas supply is a welcome development in this regard but achieving this will require a better balance of the social, environmental and economic costs and benefits of resource development than has previously been achieved. This includes giving adequate consideration to the concerns of local communities, as well as the broader benefits for New South Wales, including economic growth, employment opportunities and a royalty stream.

The Hon. MICK VEITCH: Can you forward your statement to the secretariat?

Mr DONOGHUE: Yes.

Document tabled.

The Hon. MICK VEITCH: I ask some questions around the transparency of the market. If you have read the submissions and possibly the transcript of last week, you will see we have had put to us by some of the submission holders and the participants from last week that there is a need for full transparency of all the supply contracts so that people have a much greater idea about the actual pricing within the gas industry. I am keen to hear your comments about that but also what other measures you see could be undertaken by governments—State and Federal—to increase the transparency of the market.

Mr DONOGHUE: I am sure you have had, probably several times, comparisons drawn between the gas and electricity markets in this regard. It is important to note that they have very different histories and have come from different places. So the electricity market was a very deliberate creation of governments, as part of a broader package of microeconomic reforms, it was deliberately looking to break open what at the time were largely State-based vertically integrated monopolies and to enable competition, both between States and territories and within them, in most cases by breaking up the monopoly. In doing so, it was natural to look at the ways that a facilitated compulsory market might drive that.

By contrast, the gas market has developed differently, and although there has been Government ownership in the past, at this present time there is much less of that amongst the participants in the market. There is a functioning market, compared to other markets. I will retract that. It is not that unusual in Australia for markets for commodities, products and services, to have a relatively small number of buyers and sellers such as we see in the gas market.

It is also not unusual for those markets to be characterised by bilateral contracts, the terms of which are commercial and confidential in nature. But where the informed buyers and sellers that make up much of the market are able to make fairly informed judgments about the nature of other contracts than those to which they are party they can make fairly informed judgments about the tightness of demand and supply and what is the going rate for the given commodity, product or service. In fact, the electricity market is really the exception rather than the rule and that is something to be borne in mind when governments consider what actions they might take in respect of the gas market.

It is the view of our members broadly speaking that it would be preferable that transparency be increased by market participants willingly entering into arrangements that improve the transparency of the market. That may include participating in voluntary hubs such as the Wallumbilla hub, which was set up last year. Also potentially over the next few years we expect to see the development of indexes by private players who look to market that as an information service and potentially in turn to forward contract products. I should also add that APA Group, who is the major transmission pipeline owner across Australia, has been working on capacity trading products recently.

There you have a number of initiatives. Particularly in the case of the Wallumbilla hub because the Australian Energy Market Operator [AMEO] is part-owned by government as well as by industry there has obviously been some government involvement there, but in general they represent developments that have occurred or are occurring because that is what the buyers and sellers in the market want. That is our preference for how transparency should be increased in the market. We have a deep concern about the regulatory impost that would be entailed by governments seeking to impose transparency on the market by way of requiring participants to reveal details of supply contracts or, as in the case of the short-term trading markets, requiring parties to effectively sell and then buy back their own gas through markets in which a relatively small proportion of the gas changes hands.

We made an estimate a couple of years ago. It is probably something we will look to refresh but certainly at the time that we looked at it if you actually looked at the cost of the short-term trading markets, the transaction costs, in terms of the amount of gas that changed hands—in practice it is charged on every single gigajoule of gas but most of that is just being passed from the same party back to itself—you get a figure of up to $1 a gigajoule, which we think is pretty significant

The Hon. MICK VEITCH: That is the cost of trading?

Mr DONOGHUE: Yes, that is the cost of the market fee that has to be paid on every gigajoule but because only around 5 or 10 per cent at any given time on average is changing hands, i.e. going to a different seller from the buyer, the effective cost for each gigajoule of gas that gets traded is approximately $1. If there were proven to be significant benefits flowing from the existence of that market that may justify the transaction cost but if not that is a pretty high transaction cost to be obliged to pay to participate in that market.

The Hon. MICK VEITCH: What you are saying is that you are not in favour of those supply contracts being even partially made public?

Mr DONOGHUE: No. We have concerns about that sort of heavy-handed government intervention.

The Hon. MICK VEITCH: How does the capacity trading proposal work in essence in your mind?

Mr DONOGHUE: It probably works better in my colleague's mind.

Mr COLE: With respect to the industry-led initiatives specifically, my understanding is it is essentially a listing service whereby capacity might be offered and bidders can then decide whether or not they are willing to pay for access to that particular capacity at a point in time on one of APA's pipelines.

The Hon. MICK VEITCH: That is currently operating?

Mr COLE: Yes, and there is also some capacity trading functionality around the Wallumbilla hub to try to free up access in and around that site with a view to improving liquidity there. I would need to double check my figures but I do not know that there have been high take-up rates for that spare capacity at this stage.

The Hon. MICK VEITCH: We were advised this morning that export licensing is a model that is used in the United States. I am keen to gather your association's views around the need or otherwise for export licensing.

Mr DONOGHUE: I think it might depend precisely on the conditions of the export licence. An export project is obviously a very large piece of physical infrastructure, so we understand that they have to go through a very significant range of approvals as is. I assume you are referring to a licence based on some assessment of the economic impact?

The Hon. MICK VEITCH: That is correct.

Mr DONOGHUE: It is not something we have specifically discussed with our members. I can say that we are not in favour of a situation where export licences are only granted with a specific requirement to sell a portion of the gas into the domestic market. If in fact it was being used as a proxy reservation policy then we would not be supportive of that.

Mr JEREMY BUCKINGHAM: I am interested to get the association's views broadly on the issues of demand and a reduction in demand. In your submission you say:

> Tight supply and rising wholesale gas prices are expected to have an impact on domestic gas demand on the east coast. According to the Australian Energy Market Operator's (AEMO) latest forecasts, total demand will decline at a rate of 5.2 per cent per annum over the 2014-19 period. This low growth rate is largely attributable to a decline in demand for gas-fired electricity generation ...

I know that New South Wales does not have a large gas-fired electricity generator sector but what has the impact been on gas-fired electricity generation in New South Wales since prices started to go up and where does the association see that going?

Mr DONOGHUE: The electricity wholesale market not just in New South Wales but right across the east coast is currently characterised by a very large level of oversupply. There have been a few factors affecting this. One has been the fall in demand for electricity, which in turn has a number of causes. The other is that the Large-scale Renewable Energy Target requires that more generation be added to the mix across the system regardless of whether there is any signal that more supply directly is required. That is not meant to be a comment on the appropriateness of that policy or not but that is in our working of that policy.

As a consequence we are seeing effectively historical lows for average prices across the National Energy Market [NEM]. There is a slight exception in Queensland because there is a significant upturn in demand caused by the demand from the gas projects in the Surat Basin and the LNG plant at Gladstone, but in general the market is very depressed. We have had the price signal attributable to carbon emissions removed recently. That was only in place for two years. Given that our industry builds assets to last 30 to 40 years it had not had much time to have a really material impact or a long-term impact on emissions.

That puts us in a situation that is being faced in a number of other countries around the world, which is that gas is being somewhat squeezed both by the fact that it is more expensive particularly on a short-run basis to run than a coal-fired plant typically. On the other hand renewables as well as having zero marginal cost—certainly wind and solar tend to—also get a particular form of support or extra income outside the market via the Renewable Energy Target. So gas is the one that is being squeezed in the middle. We would certainly agree that generally the prognosis for gas-fired generation is pretty poor over the short to medium term.

Mr JEREMY BUCKINGHAM: How are you seeing that manifest in New South Wales? What is happening with the gas-fired power stations in New South Wales—are they mothballed?

Mr DONOGHUE: At present I do not believe any of the gas-fired power stations in New South Wales are mothballed. We have seen mothballing of gas in South Australia and also in Queensland. In Tasmania it is not technically mothballed but in practice they have not run Tamar Valley for some time. That is partly a consequence of the fact that in New South Wales the gas plants are generally designed to be peaking or mid-merit plants, so they are not designed to run all year round and compete directly with coal. On that basis they are there to come on when there are spikes in demand. They have the advantage, a spike being more expensive, of being more flexible in terms of turning on and off than other plant. But given that that signal is price driven and in an oversupplied market there are fewer high price events there has been less market signal for them to run as often, so they run less.

Mr JEREMY BUCKINGHAM: An interesting part of your submission says:

> To the extent there is a decline in mass market consumption, a reduction in distribution network throughput could lead to higher network charges as network businesses seek to recover costs from fewer units, thus driving prices higher and gas usage lower.

Is that a comment generally about the electricity market in New South Wales or Australia?

Mr DONOGHUE: Yes. In terms of the way that gas and electricity networks are regulated there is a somewhat different outcome depending on whether they have a revenue cap set, which is the total million or billion dollars they are allowed to recover over the five-year period of each determination, or whether they have a price cap set, in which case what is determined by the regulator is an average price for each year of the five years.

In electricity the trend is towards setting revenue caps. If throughput is declining that means that you have to charge more for each unit of electricity just to recover the same amount of revenue. Even if revenue is set flat by the regulator you could see unit charges go up year on year as a result of that. That is reflective of a mismatch between the cost drivers of networks and the way we charge for them. That is something that the industry and the AEMC and governments are working on in concert and in consultation with stakeholder groups to find ways to charge more effectively for electricity and still recover the same total amount.

In the case of gas and in particular in the case of Jemena Gas Network, which is the main gas network in New South Wales, they are on a price cap. The Australian Energy Regulator is in the process of determining their allowed average price cap for the period 2015 to 2020. There are two things to note about that. Although the final decision has not been handed down the draft decision has been. I am sure Jemena will be submitting further information in this regard but the best information we have available is the draft determination. It would see the cost to an average household user of gas fall by around $112 in the first year and then increase by $2. That will be a nominal increase but below the rate of inflation for the next few years. That will quite likely have the impact of offsetting totally the increases in wholesale cost for an average user.

The other thing is that because it is a price cap, if demand for the gas that Jemena supplies goes down over the period 2015 to 2020, they will not be able to increase unit charges to recover that, they will simply have to wear the lower revenue due to those lower volumes. I think this is probably worth mentioning because when I was looking at the analysis coder by the Melbourne Energy Institute, which I think has been presented to you, my view was that they had not taken account of those factors in their expectations about prices going forward for households.

Mr JEREMY BUCKINGHAM: That is significant. Can you explain to me once more why it is that you are expecting a reduction in the price to consumers of, did you say, $120 per annum?

Mr DONOGHUE: It is $112, and I can take it on notice to confirm that.

Mr JEREMY BUCKINGHAM: Because of the ruling of the Australian Energy Market Operator?

Mr DONOGHUE: Technically it is the Australian Energy Regulator. They set the network portion of the charges and then the retailer obviously takes that, adds in the wholesale charge and then adds in their own retail costs on top of that to get to the final price. So it will very much flow through to final retail prices. The big driver of that, and it is similar to the trends we are seeing in electricity networks, is that the previous determination that was set was around the time of the global financial crisis when expectations on interest rates were much higher, so the company was allowed a higher cost to capital than is likely to be allowed this time and, because these are very capital-intensive businesses, that has a big impact on the overall level of charges they are allowed to set.

CHAIR: I see in your submission that you make mention of domestic gas pricing in relation to the CSG industry, or no CSG industry, as it were, in New South Wales. What is your view on what would happen to the domestic price of gas if we do not develop a CSG industry in New South Wales?

Mr DONOGHUE: Relative to the case where there is development I think there are two factors in play. We tend to talk about a gas price and sometimes about a netback or a link to international prices and in a broad sense that is true. Any gas producer when looking to negotiate a contract will consider the opportunity cost of selling to that buyer and selling to another buyer. A key buyer going forward or a number of buyers are going to potentially be the LNG components with their trains up in Queensland, although there are probably going to be fewer of those than we might have thought a few years ago with Shell and PetroChina announcing today that they are not looking to develop an independent LNG train for their Arrow project.

But while there is broadly likely to be a link to what we call the netback of international prices, which I can go into but I suspect you have had that presented to you several times already, because the gas market is dependent on bilateral contracts and because different buyers and sellers are seeking different terms in respect of the tenor of the contract in respect of the location of where the gas is from and where it is to be delivered and in respect of other terms such as where the balance of risk lies between the parties, while that international netback will be a reference point it will come down to the negotiating between the two parties and, other things being equal, if projects are allowed to go ahead in New South Wales there will be two more parties with gas or parties already in there will have additional sources of gas that they will be looking to market. Other things being equal, that will be in the buyer's favour.

Mr SCOT MacDONALD: It is a downward pressure on pricing.

Mr DONOGHUE: Yes, at the margins. I would not be in a position to put a hard figure on it.

CHAIR: Your submission says by 2030 it could be as much as 23 per cent cheaper than the international price for gas.

Mr COLE: Work was commissioned by the Australian Petroleum Production & Exploration Association. They basically looked at a case where CSG developed—and I think that included Narrabri and Gloucester projects—and compared that to a case where no CSG developed. I think there was a 25 to 32 per cent price differential.

Mr DONOGHUE: The other factor is that, regardless of views on that dynamic, the local projects are clearer nearer to the main demand sources of Sydney and Newcastle and so on, so the transportation costs to get it there will be lower—you would probably save a dollar or so versus Victoria.

CHAIR: The Independent Pricing and Regulatory Tribunal seems to be happy with the retail end of competition now. What are your views on if these gas resources in New South Wales were to be developed they would be reflective of further integration of the existing gas producers or gas retailers in New South Wales?

Mr DONOGHUE: AGL obviously is both one of the main proponents of CSG in the State and is also probably the largest retailer by some distance. Santos, I am not 100 per cent sure but I do not think they market to household customers, so to the extent that they had gas available for sale, that would either be supplied to large industrial customers or it would be available for sale to the retailers that are there. I think we said in our submission that there are around 21 licensed retailers for gas. There is certainly a good diversity of retailers, so there is competition at the small-scale side of the market, but obviously that needs ongoing supply to keep it healthy.

CHAIR: What is your view on the potential for reservation policy if New South Wales does develop a viable CSG gas industry?

Mr DONOGHUE: Given that the resources are the property of the State of New South Wales, that is obviously a decision for the State, for the Government, and the community. We are, in general, in favour of free and open markets where possible so we would not prefer to see those kinds of conditions imposed. It would be preferable if the alternative was not to have development at all, but I think naturally the gas would flow domestically given the location.

CHAIR: Would it be true to say that you are not happy with the current situation? You do not think it is a good thing that we have, effectively, a moratorium on the development of coal seam gas?

Mr DONOGHUE: That is correct. We are aware that there are obviously environmental and community concerns that need to be addressed and we encourage the Government and the industry to work with affected stakeholders to find a balanced resolution of those issues. New South Wales has been home to resource extraction of various types for 200 years.

Mr JEREMY BUCKINGHAM: Bile oil, asbestos, uranium.

CHAIR: Order!

Mr DONOGHUE: I am not disputing the appropriateness of environmental safeguards, I am merely noting that in the past the State has found a way through these issues and I do not see why one particular industry should be held to a different standard from the rest. There may be conditions specific to the nature of the resource and the extraction method but we would expect it to be treated in a broad sense like other resources.

Mr SCOT MacDONALD: It is called political opportunism.

Mr DONOGHUE: I could not comment.

Mr SCOT MacDONALD: The previous question touched on what I was going to ask: moratorium. Your 34 members, what is that doing for their confidence, what is that doing for their investment decisions and possible work in the future?

Mr DONOGHUE: One of our members is AGL, so they are obviously extremely directly affected. You have already heard, I believe, directly from them so I will not attempt to speak for them beyond that. More broadly, as I say, we have several members that are engaged in retailing gas to large and small users, who transport gas within the State and who seek—although, as I noted, decreasingly so—to use it in gas generation. All of those users are all businesses that carry out one or more of those activities and have an ongoing interest in seeing a diverse range of supply within the State.

Mr SCOT MacDONALD: Through your submission you mention a couple of times the uncertainty. Does the moratorium feed into that uncertainty?

Mr DONOGHUE: Yes, to the extent that any—

Mr SCOT MacDONALD: Proposed moratorium, I should say.

Mr DONOGHUE: Anyone that is looking to do anything that would require a new contract—and that might include replacing an old contract as well as expansion of business either via very aggressive entry or expansion in the retail market—if anyone did want to build a new gas-fired power station, although I think that is some way off at the current point in time, then they would obviously think, "How do I get my hands on a reliable source of supply?" and I think that is a question they would find very difficult to answer.

Mr SCOT MacDONALD: Can you give me any sense of what that is doing to how people are thinking about contracts? If a moratorium is producing that sort of uncertainty and questions around confidence, people who are supplying the contracts, people who are looking for the contracts, what are your members' views on that—length of contract, certainty?

Mr DONOGHUE: My assessment of the market—although many of our members are participants we, in a sense, are an outsider to it—is that the market on the east coast has gone through a very significant dislocation with the introduction of the LNG industry. That is not necessarily a reason that we should regret it having happened, because it has delivered a great deal of investments to the areas in which it is taking place and income to landowners and job opportunities and so forth. But—again you will have heard the statistics from several others—it is tripling east coast gas demand in a few years. The nature of the coal seam gas resource is also that it takes a bit of time to prove up exactly how much gas you are going to get from each well and then the depletion rates, because the wells deplete quicker than conventional gas. So it has introduced a good deal of uncertainty and I think that, combined with the fact that there is no single transparent price reference point, has made it difficult for buyers and sellers to find mutually agreeable terms.

Mr SCOT MacDONALD: So there is a risk element built in there, if I understand you?

Mr DONOGHUE: Yes and I think that stems from the uncertainty, and that uncertainty will be lowered once the trains are up and running. I am not saying that will bring the price down to where it was; that will have an impact on the price but I think some of the uncertainty will recede. But I think the other aspect of the uncertainty is when and to what extent unconventional resources in New South Wales and also in Victoria—which does currently have a moratorium on exploration—will be developed. I think that is an important dynamic. If you did not have those resources here at all, if you absolutely had to import all your gas, then anyone looking to get up a pipeline and underpin that with a supply contract would know that they would be the only game in town or there might be one from the north and one from the south.

Mr SCOT MacDONALD: You would structure your raw material sourcing that way then, would you not—feedstock or—

Mr DONOGHUE: I am not sure I quite follow.

Mr SCOT MacDONALD: If there was no prospect of indigenous gas you would look to Victoria or elsewhere and lock in there, but at the moment we have got this uncertainty.

Mr DONOGHUE: Yes. So I think from the supplier's point somebody will think, "If I go ahead and assume it is not going to get developed here what will happen to the value of my contract if it does turn up and that potentially can undercut me by virtue of being near allocation-wise?" and somebody on the buyer's side will say, "Do I suck it up and pay a much higher price than I am used to because that may be the only price available or is it worth me hanging on to see if the indigenous resource is developed?"

Mr SCOT MacDONALD: Can I encapsulate that? Moratorium equals risk equals higher cost.

Mr DONOGHUE: I think that is a fair summary.

The Hon. Dr PETER PHELPS: Thank you very much for coming in. A few years ago there was a lot of talk about gas-fired electricity generation as being the way of the future. Why was that seen as a preferable mode of electricity generation?

Mr DONOGHUE: At the time I think we were used, particularly in eastern Australia, to historically very low gas prices and very low gas prices by reference to the rest of the world because we did not have that link. It was also the case that there was an expectation that there would be enduring carbon constraint brought in at some point and that would advantage gas relative to coal.

The Hon. Dr PETER PHELPS: In other words, gas was seen as a more economic option if a long-term regime of punitive taxation on coal-fired generation, which is effectively what any scheme would have been, would have come into play.

Mr DONOGHUE: I would not characterise it in those words myself but I see what you are getting at. From our perspective, we do not completely repudiate the idea of recognising the social cost of emissions. We are in a situation where, when we decide to build something, we are building it to look to last for 40 years so we need to know; we need a clear signal from the community via governments of what value, if any, they put on those emissions or, conversely, on the reduction of those emissions. That enables us to make reasonable choices, noting that there is always some risk entailed in what might happen when you build long-term assets.

The Hon. Dr PETER PHELPS: In other words, if government had not entered the market to deliberately distort it against coal-fired generation, the demand expectations would likely not have been as great as what they were.

Mr DONOGHUE: I am sorry, I am just thinking through your question.

The Hon. Dr PETER PHELPS: If no government at any time had mooted a tax—effectively a tax—on coal-fired electricity generation, then the demand expectations for gas-fired generation would not have been as high as what they were.

Mr DONOGHUE: Yes. That is true.

The Hon. Dr PETER PHELPS: All this talk about reduced demand, in effect, comes about because government decided not to pick winners in the market, ultimately.

Mr DONOGHUE: Well, the other thing that is affecting gas, however, is that there is support given to renewables and it is given on the basis that they help reduce emissions. Now, relative to coal, gas also reduces emissions but that is not currently recognised. Again, I leave it to the Committee to decide which is the worst distortion. I think I will also leave it to the Committee to decide—

The Hon. Dr PETER PHELPS: Could we say that they are both bad distortions?

Mr DONOGHUE: I can certainly say they are both, to an extent, distortions. We can work within the constraints imposed on us by the community as long as they are done in a consistent and enduring manner. That is the fundamental issue that we have been grappling with for the last three years.

The Hon. Dr PETER PHELPS: But the optimal situation would be if governments did not interfere in the free flow of energy markets.

Mr DONOGHUE: Subject to it being credible that there would be no driver to reduce carbon emissions and given developments across the world, both in terms of the state of the science and in terms of statements by governments and government agencies, mostly in developed countries but also in some developing countries, the totality of that is seen as a glass half empty or a glass of full by different parties. But I would wonder whether it was credible that no such intervention could be expected in the longer term.

The Hon. Dr PETER PHELPS: In relation to your position as the Energy Supply Association of Australia [ESAA], you have both electricity and gas, which ultimately to some extent are competing technologies—

Mr DONOGHUE: Correct.

The Hon. Dr PETER PHELPS: —for the same not only domestic but also commercial arrangements. Is there any tension, in your submission, between those two? Anything that has a deleterious effect on gas obviously is going to work towards electricity.

Mr DONOGHUE: Given that most of our members have, if you like, a foot in both camps, we would not see that. I mean, we strive to be fuel and technology neutral as far as possible and that includes both in terms of electricity generation technologies but also in terms of choices between gas and electricity as a source of energy for users.

The Hon. Dr PETER PHELPS: If that is your mode of optimal operation, why should not the Government be exactly the same and not to pick winners and losers and say, "We preference one form of energy over another"?

Mr DONOGHUE: That would be our preferred situation. I say "we", we prefer not to have governments picking winners and losers but on the other hand we look to work with governments as far as possible.

The Hon. Dr PETER PHELPS: Who decide to do that anyway?

Mr DONOGHUE: It is not so long ago that the potential for putting an emissions trading scheme or some other constraint on carbon was held by both major parties. It is not so long ago that the increased renewable energy target was agreed to by both parties. In that situation we accepted that as a legitimate expression of the community's preferences. Those preferences have not endured as long as we need them to, in order to be able to make efficient investment decisions.

The Hon. Dr PETER PHELPS: But that sort of sanguinity is simply one of, "Well, they're going to chop off one of my legs. I know that they are going to chop off one of my legs …" is preferable to, "Well, I'm not sure whether they're going to chop off all of my limbs." Would it not be better just to say that we do not need any chopping off whatsoever and that governments should stay out of the markets, which are operating freely and effectively?

Mr DONOGHUE: We have debated that long and hard within our membership.

The Hon. Dr PETER PHELPS: I am surprised that there would be any debate to that concept.

Mr DONOGHUE: Within the context of a community decision to reflect the social cost of carbon, there is a market mechanism that does that. That is still within the market through an emissions trading scheme, for example.

Mr SCOT MacDONALD: I have a very quick question. Can I get your very quick response—your visceral response, if you like—to a quote in a submission from Santos, which is quoting a politician who said: "Australia is an expensive place to do business. My job is to make it more expensive and that's what I hope to do." What is the impact?

Mr DONOGHUE: I would be very surprised if any politician would think that that was their role.

CHAIR: Just in relation to free markets, if the free market without interference is working so well for us, why are we staring down the gun barrel of 200 per cent and 300 per cent price increases?

The Hon. Dr PETER PHELPS: But it is not a free market at the moment.

Mr SCOT MacDONALD: It is gold plating that was.

The Hon. Dr PETER PHELPS: That is the problem.

CHAIR: There is no interference in the market in New South Wales.

The Hon. Dr PETER PHELPS: Except that you are not allowed to mine for coal seam gas. That is kind of an impediment.

The Hon. NIALL BLAIR: Is this a deliberative?

The Hon. ADAM SEARLE: No. I think two of our members are having a conversation with their own navels.

CHAIR: Thank you very much indeed.

Mr DONOGHUE: Thank you for your time.

Mr SCOT MacDONALD: You have had some impact.

The Hon. Dr PETER PHELPS: The lights are going out as a Greens utopia.

Mr JEREMY BUCKINGHAM: No. It is a free market failing. That is what it is—a free market in total collapse. I am sorry, it is a closed market.

CHAIR: Order! We have not finished yet.

Mr DONOGHUE: I am sorry, Chair: can I clarify whether you believe we have a question taken on notice?

CHAIR: I think you do. Given the short time frame for this inquiry, the Committee has resolved that answers to questions on notice be returned within seven days. We would appreciate your help in assisting us to meet this reporting requirement. The secretariat will contact you in relation to the questions you have taken on notice. Think very much for attending.

(The witnesses withdrew)

(Short adjournment)

PAUL FENNELLY, Chief Operating Officer, Eastern Region, Australian Petroleum Production & Exploration Association, and

DAMIAN DWYER, Director, Economics, Australian Petroleum Production & Exploration Association, sworn and examined:

CHAIR: Would you like to start by making a short statement?

Mr FENNELLY: Yes. I want to focus in the opening comments on four themes. Firstly, the increased indigenous supply will put downward pressure on prices. Increased gas supply will result in economic growth for New South Wales. We are opposed to a reservation policy and we support a competitive market. Finally, there is a critical need for regulatory certainty for the development of the CSG industry in New South Wales. Firstly, by way of introduction, the Australian Petroleum Production & Exploration Association [APPEA], as you are probably aware, is the peak national body representing Australia's oil and gas industry. Our membership account for an estimated 98 per cent of the nation's petroleum production.

In terms of the submission, I am sure you all have it. As I said before, I will focus on some of the key points. Downward pressure on prices is where I want to focus now. New South Wales possesses Australia's second largest onshore natural gas field, providing considerable potential to supply the State with the energy it critically needs. The Australian Energy Market Operator [AEMO] estimates that New South Wales has 85,000 petajoules of undeveloped gas resources. The State's current demand is just over 150 petajoules per year. We are aware of course that there are a range of views about the development of the onshore gas industry in New South Wales, but one thing is consistent and one thing is real. Despite possessing these substantial gas reserves, New South Wales currently imports, as you have probably heard many times, 95 per cent of its supply from South Australia and Victoria at a time when regulated gas prices are rising.

In 2004 IPART raised regulated gas prices by over 10 per cent, impacting on households, small business and manufacturers across the State. The availability and cost of gas has become a critical issue for New South Wales. APPEA has long argued that downward pressure cannot be applied to rising gas prices if restrictions on developing natural gas from coal seams in New South Wales are allowed to continue. One of the key means by which to place downward pressure on gas prices is to develop an indigenous gas supply. On the issue of reservation, we submit that the answer to New South Wales energy security challenge does not lie in market interventions or in new protection or subsidies for gas users or as advocated by others.

It is in Australia's best interests to maintain access to open and competitive markets in all sectors of the economy, not just oil and gas. Australia's gas industry is a source of comparative advantage that should be harnessed, not hindered. In this light we, like the government of every eastern gas market jurisdiction, continue to reject the calls for inefficient, inappropriate and ineffective regulatory interventions such as domestic reservation policy. The focus instead should be on market-based energy policies. Efficient and competitive markets where prices are determined by demand and supply forces and negotiations between willing buyers and willing sellers is where our focus should lie.

Extracting the maximum value for natural gas resources will benefit the whole Australian economy. A rapid and efficient supply response to meet domestic needs depends largely on clear market signals and efficient government regulation is required to address any gas supply issues in New South Wales. A freely operating and competitive market is the best way to allow gas resources to be developed. The idea of domestic gas reservation policy has almost universally been rejected globally throughout the free market economic for a very good reason. Gas reservation can actually worsen the very situation it is supposed to fix. Rather than generating more gas and driving down prices, reservation policy reduces investment needed to bring on new and cheaper supplies. In our submission we refer to a recent review by the regulator in Western Australia.

Finally, on the issue of reservation, it is not just the jurisdictions as I mentioned; it is also manufacturers and the major industry groups. I understand you had NSW Business Chamber here this morning. The Australian Industry Group, the Australian Food and Grocery Council, the Energy Users Association, the Australian Aluminium Council, the Australian Steel Institute, the Plastics and Chemicals Association—all bodies that represent big natural gas users do not support reservation calls. The final point is regulatory burden. Australia's upstream oil and gas industry, including in New South Wales, has the potential to deliver substantial economy-wide benefits in terms of investment, jobs and regional development. In order to achieve this we must further explore. New production depends on successful exploration activity.

Without new exploration and production in New South Wales, it will be very difficult to put downward pressure on New South Wales gas prices. Over the last several years the industry has experienced a range of policy and regulatory restrictions which have undermined the industry's confidence in New South Wales as a viable market for investment. New South Wales requires policy and regulatory stability in order to attract investment for gas exploration and production. The natural gas industry in New South Wales can be a world-class industry. It already has a solid track record in exploration underpinned by science. The NSW Chief Scientist and Engineer found in a recent review of the CSG exploration in New South Wales that technical challenges and risks posed by the natural gas industry can be managed, and praised the industry's high standards of engineering and professionalism.

In closing my opening address I would like to support or affirm what I believe are two important comments made to this Committee by Mr James Balderstone of Santos and Minister Roberts. Firstly, Mr Balderstone said, at page 27, that the New South Wales Government has the ability to mitigate future gas price rises. Energy users in this State, like all States in Australia, require government to put in place regulations that protect the environment, enable co-existence with traditional land use while supporting the safe and timely development of natural gas projects. This has been done in every State in Australia and I am sure New South Wales will be able to rise to this challenge. Finally, and importantly, the Minister said that energy security is not something that should be subject to political point scoring or a deliberate stoking of emotive debate. Quite frankly, it is too important for that. Thank you. I am happy to take questions.

The Hon. MICK VEITCH: Thank you for your submission and for your attendance today. My first question relates to page 5 of your submission where you talk about maintaining flexibility in farmer compensation agreements. I take it you are not keen on benchmarked farmer compensation agreements?

Mr FENNELLY: The point we allude to there is that there is some suggestion that—you have seen in the NSW Gas Plan there is some consideration of IPART determining compensation or at least benchmarking compensation. What we have experienced, particularly in Queensland and in other States but in Queensland for example, we are now approaching some 5,300 agreements between farming families, farmers, and the gas companies, and they all vary dramatically. It depends on the terrain, the crop, the characteristic of the land. What we were highlighting there is to have a template approach to compensation is problematic. We have found from experience that it is probably not the best way to proceed. What the Government is doing in the Gas Plan is enshrining, if you like, the importance of compensation for access to land for exploration and production purposes.

The Hon. MICK VEITCH: So you support that last aspect to your statement? Are you saying that you support the Gas Plan's requirements?

Mr FENNELLY: No. We have met with the Minister recently and we have indicated that while it is easy to put that type of concept or approach in a gas plan, we are saying it is problematic and difficult to have a template approach to compensation of farmers because of broad acre cropping to a dairy farmer, different terrain, different types of issues.

The Hon. ADAM SEARLE: This is not rocket science. Surely some kind of benchmarks, principles or other differing formulas could be reduced to writing without too much difficulty, except to your members who might have to pay it.

Mr FENNELLY: The gas companies have different formulas when dealing with landholders but there are issues about the way the gas industry operates. Farmers are provided with legal representation. They are advised by their legal representation. Then there is a negotiation. It surrounds a range of compensation. It could be fencing, it could be roads, as well as remuneration and compensation. All I am saying in that statement is that to apply a template for every farm that it must receive this. That is probably not going to be well received by the farmers groups as well. All we are saying is that it is a complex issue and we are adding caution about that issue.

The Hon. MICK VEITCH: Obviously you have read the transcript from last week and some of the submissions so you would know that we have received testimony recommending to the Committee that we seek full transparency on all gas supply contracts so that the New South Wales Government has full knowledge of all commercial transactions relating to gas supply—I am quoting from one of the submissions. I gather you do not support that? I do not want to put words in your mouth. I am happy to hear your views.

Mr FENNELLY: Gas supply contracts are different to farmer compensation.

The Hon. MICK VEITCH: No. I have moved onto another area.

Mr FENNELLY: If I could just stress one thing, I think the farmers will tell you this. A lot of the confidentiality around those agreements in Queensland is at the request of the legal representation of the farmer. In some respects our life would be easier if there was greater transparency in some of the compensation arrangements in Queensland, just by example.

The Hon. MICK VEITCH: I had moved on.

Mr DWYER: Sure and I guess in relation to the transparency issue you will have heard testimony from witnesses, particularly Santos and AGL, last week and their views on this issue, views that we support as well. It is important to understand the context within which this sort of debate takes place. You will have had explained to you in some respect the fact that since 2006, when an industry led group provided a report to what was then the ministerial council on energy, we have had the gas market statement of opportunities, the gas bulletin board and a number of short-term trading markets developed across the eastern part of the country and there are similar things underway in the west. We have gone from a situation where there was none of those mechanisms available to the situation we are in now where those mechanisms are available. So the gas bulletin board provides information on the amount of gas flowing through the pipelines in New South Wales, in Victoria, in Queensland, in South Australia and in Tasmania on any given day. We can go on the website and check that.

The short-term trading market makes available, as the name suggests, short-term trades for gas and the gas statement of opportunity provides each year a solid rigorous overview by an AEMO about the state of gas market demand and supply. So that is the situation we are in now. As I think Minister Roberts set out last week, the December COAG energy council meeting mapped out further developments in that space. From an industry perspective we stand ready to work with governments in terms of what can be done and what needs to be done in that space. What we have suggested is that in many places most of this information or a vast amount of information is available. It may not all be in one spot and available to everyone at any given time but just because you are not aware of it does not mean it does not exist. We have suggested to jurisdictions that a useful first step would be a stocktake of the information that is available and that can allow us to identify whether there are gaps, and if there are gaps, if the information that currently exists is not meeting the sorts of outcomes that Ministers like Minister Roberts are after, then we can talk further about what can be done in that space. So I would characterise us as being part way through a very solid—

The Hon. MICK VEITCH: So you do not oppose having it all in one place. You are saying the information is there but at the moment it is presented in a fragmented way. To have it consolidated into one portal, one place where everyone can access it, you do not oppose that?

Mr DWYER: What we have is a useful step. Before we talk about what additional information might or might not be required—what do you consider a transparent gas market as opposed to what others might consider a transparent gas market—let us take a sensible first step, which is stocktake of the information that exists, and from there we have an information base that we can locate. We have the information we need; no, we do not have the information we need and more is required. Then we can have a conversation.

The Hon. MICK VEITCH: Can I infer from your statements that you in some way refuting what has been said by some others, not all others, to this inquiry that the information is not there? They do not know what is going on at a given time. You are saying the information is there albeit it may well be in a myriad of places.

Mr DWYER: What we are saying is that jurisdictions should get together and see what is and what is not available before we get into that conversation about the need for more transparency. The final point I guess I would make is that it is the case that since the end of 2012 there have been at least 22 that are on the public record—there may be more but 22 are on the public record—commercial agreements, gas supply agreements, commercial deals that have been done. What that suggests to us is that for willing buyers and willing sellers wanting to come together to make a deal there is information out there and they can come together and do that.

The Hon. MICK VEITCH: Also in your comments before you mentioned that if you were to seek how much gas is in the system at any given time or on any given day you can do that at the moment on the bulletin?

Mr DWYER: The gas bulletin board, which is an AEMO operated website, will show you the processing capacity of processing plants and the gas flows through the pipelines. So there is a range of information on what is physically happening in the gas network or in the gas pipeline system, the gas processing part of the supply chain at any given time. That is an active website that has been in place since 2008.

The Hon. MICK VEITCH: My last question relates to contracts. We are hearing that this industry has had long-term contracts as part of its operation model but is now moving towards short-term contracts. What do you see is the impact on pricing of the short-term contract environment?

Mr DWYER: It is the case that this is an industry that has grown up around long-term bilateral contracts. That is the characteristic of this industry and its development historically. We are moving to a situation where there are short contracts. That is both from a producer and a consumer side in many circumstances. To us, what it reflects is a growth in evolution of the market, an increase in liquidity around the operation of the market. That is part of a natural evolution of a growing market. In respect of prices, what does it mean? It will mean that they are more dynamic than they were previously. There are more opportunities, potentially, for review. That would depend on the review natures and those long-term clauses. Those long-term contracts are not set and forget; they have review clauses in them. What it means is that gas prices can operate in a more dynamic environment. The industry is operating in a more dynamic environment now than it was when those contracts were first struck.

The Hon. ADAM SEARLE: You said that jurisdictions around the world had rejected domestic gas reservation. We have received submissions that indicate there are quite a number of jurisdictions, including North America, United States and Canada, as well as Norway and others, who have a domestic gas reservation policy either explicitly or through the requirement to meet a public interest test when obtaining export licences. Why should we not operate something here to ensure there is not a market failure inducing a lack of supply?

Mr FENNELLY: Again I will refer that to Damian. Damian has done a fair bit of work on this and he can take you through it in a bit more detail. Let us not forgot that a lot of those examples you use are not exporters as well.

Mr DWYER: The situation is somewhat more complicated than what has been expressed in some of the evidence that we have heard. A more rigorous and prudent examination of the issue would see three basic categories of markets around the world. In general respects, interventions in the gas market; fit as are part of a broader policy, energy policy framework, and they tend to follow the nature of the economy itself. Is it a market-based economy? Is it a command and control-based economy? Not surprisingly, the view you take on the gas market tends to follow those structures. We have observed three basic categories of markets. A range of OECD countries—the United Kingdom, Netherlands, very importantly, and Norway—allow wholesale market prices to be set by the operation of the market and they do not have interventions to favour domestic supply.

Then you come to OECD countries that have export review processes and they are the North American countries. Those countries allow market forces to set wholesale gas prices but they have an export review process. What is very important about those export review processes is to understand how they operate. For countries with which the United States has a Free Trade Agreement, exports are deemed to be in the public interest, so it is a formality. For countries with which the United States does not have a Free Trade Agreement, then there is a review process. That review process takes as a starting point that exports are in the public interest, so you have to refute that starting point if you think there is something wrong with exports or that exports are going to be a detriment to the economy; it is up to you to prove that to be the case. So far no export project in the United States has been rejected on that basis. In Canada there is an export review process. It requires an assessment of the level of Canadian gas resources; how much gas is actually available in Canada. Importantly, that is resources. That is the total resource base for the nation.

The Hon. ADAM SEARLE: Which is something we do not know about at the present time in Australia.

Mr DWYER: Well it is Geoscience Australia's job; that is what they do each and every year. They will say there is nearly 800 trillion cubic feet [TCF] of gas across the country. The Canadians also look for opportunities for new supply that will be opened up by an export market and, in a similar way, there has been no Canadian export project rejected on that basis. Finally, and I will cover this very quickly, there are a range of non-OECD countries that have interventions of some form or another. What we have seen from those countries is that typically the industry in those countries is dominated by State owned gas companies and, in many cases, state owned gas using industries. Those entities may serve social political objectives, not just commercial objectives.

What you see from those countries is that the sorts of interventions we are talking about have reduced domestic wholesale gas prices in unsustainable ways, have put downward pressure on investment in those countries, led to shortages, and so you have a number of examples. Places like Egypt, which has a third domestic gas reservation, has subsidised prices. Those energy subsidies are a major contributor to Egypt's significant budget deficit. Indonesia is buying gas from its own LNG plants. Algeria has Sonatrach, which is a very large national oil company and it has had very little interest in taking up exploration acreage in that country because of the presence of such a large national oil company. There are certainly lessons to be drawn from what other countries do in this market, but they are not the lessons that you have had put to you by some. They are lessons that, in fact, it is not a good idea for us to follow.

Mr JEREMY BUCKINGHAM: Mr Fennelly, you live in Brisbane, do you not?

Mr FENNELLY: Yes, I do.

Mr JEREMY BUCKINGHAM: In your role as the chief executive officer [CEO] of the Australian Petroleum Production and Exploration Association [APPEA], have you ever utilised a driver?

Mr SCOT MacDONALD: Point of order: What could this possibly have to do with the terms of reference?

Mr JEREMY BUCKINGHAM: You are about to see.

CHAIR: Order!

The Hon. ADAM SEARLE: To the point of order: It may appear that the question is quite broad but a bit of flexibility and latitude is given to members to ask a couple of questions to at least establish some ground of relevance.

CHAIR: Let me rule on this. If this is leading to something, Mr Buckingham, then yes. If it is just a flight of fantasy, no.

Mr JEREMY BUCKINGHAM: We will see. Have you ever, in your role as the CEO of APPEA, used a driver?

Mr FENNELLY: Used a?

Mr JEREMY BUCKINGHAM: Driver.

Mr SCOT MacDONALD: A golf driver, I think he means.

Mr FENNELLY: A taxidriver?

Mr JEREMY BUCKINGHAM: No, a driver like a—

CHAIR: A chauffeur.

Mr JEREMY BUCKINGHAM: —a chauffeur; a driver?

Mr FENNELLY: No.

Mr JEREMY BUCKINGHAM: You have never had a driver—

Mr FENNELLY: No.

Mr JEREMY BUCKINGHAM: —in your time? Well that is surprising.

Mr JEREMY BUCKINGHAM: Mr Fennelly, in an article—

Mr FENNELLY: Why is that surprising?

Mr JEREMY BUCKINGHAM: Well, it is surprising. Mr Fennelly on 31 January—

Mr SCOT MacDONALD: Welcome to our world.

Mr JEREMY BUCKINGHAM: On 31 January you wrote an article for the *Courier-Mail* in which you attacked the broadcaster Alan Jones for his inner city lifestyle and the fact that he used a chauffeur and you made a couple of innuendos and—

Mr SCOT MacDONALD: I repeat my point of order.

Mr JEREMY BUCKINGHAM: —on the issue of coal seam gas [CSG], you raised his inner city lifestyle.

The Hon. Dr PETER PHELPS: Point of order.

Mr SCOT MacDONALD: Are you prepared to apologise to Mr Jones for your attack?

CHAIR: Order!

Mr SCOT MacDONALD: Surely we have got to be broadly close to the terms of reference.

CHAIR: I think you are well outside the terms of reference.

The Hon. MICK VEITCH: Phelps is defending Jones today, last night he was into him.

CHAIR: There are no terms of reference that I have seen that allows you to ask Mr Fennelly to apologise to Mr Jones.

Mr JEREMY BUCKINGHAM: Mr Fennelly—

CHAIR: Do not go back down that track otherwise I will disallow your questioning.

Mr JEREMY BUCKINGHAM: Mr Fennelly and his organisation are proponents of coal seam gas and have been very—

The Hon. NIALL BLAIR: Are you flouting the ruling? Are you questioning the ruling?

Mr JEREMY BUCKINGHAM: I am not flouting the ruling, I am asking another question. Mr Fennelly, your organisation has been a strong advocate for coal seam gas and has been frustrated in New South Wales, Queensland and Tasmania with the vehement and sustained opposition. In regard to that article and that opposition, is your organisation becoming more dishonest and desperate in your attempts to get the industry in New South Wales and are relying more and more on lies and innuendo?

Mr SCOT MacDONALD: Point of order: Will the Chair rule whether that is an appropriate way to address a witness?

CHAIR: I do not think that is an appropriate way to address the witness. If Mr Buckingham continues along this line, I will disallow all questions.

Mr JEREMY BUCKINGHAM: Mr Fennelly, who said this: "Drilling will, to varying degrees, impact on adjoining aquifers. The extent of impact and whether the impacts can be managed is the question"?

Mr FENNELLY: Could you say it again, please.

Mr JEREMY BUCKINGHAM: Who said the following, "Drilling will, to varying degrees impact on adjoining aquifers. The extent of impact and whether the impact can be managed is the question." Do you remember who said that? It was on the front page of the *Sydney Morning Herald*.

The Hon. NIALL BLAIR: If you have got the article, why do you ask?

Mr JEREMY BUCKINGHAM: That was Ross Dunn, who—I understood—at the time was working for APPEA and may still work for them. Do you stand by those comments, that drilling for coal seam gas will impact on aquifers?

Mr FENNELLY: No, I do not. Quite frankly, Ross Dunn, I understand, left APPEA five years ago. Would that be right? What date are you talking to?

Mr JEREMY BUCKINGHAM: 2011.

Mr FENNELLY: 2011, so what are we now, 2015.

Mr JEREMY BUCKINGHAM: You do not stand by that—

Mr FENNELLY: I have never met Mr Dunn. I cannot comment on what he said and I do not know the context of that article.

Mr JEREMY BUCKINGHAM: It was front page of the *Sydney Morning Herald*; you will have to look it up. What do you believe to be the number one cause—the principal cause—of gas price rises on the east coast of Australia?

Mr FENNELLY: The number one cause, unquestionably, is the changing dynamic, and that is we are now a global exporter. We are starting to export to the world.

The Hon. ADAM SEARLE: Except it has only just started. That does not explain the price rises in the last few years in the face of falling demand.

Mr FENNELLY: The prices are rock bottom.

The Hon. ADAM SEARLE: The prices have risen.

Mr FENNELLY: What were the prices at Christmastime?

Mr DWYER: The short-term trading market prices were in the single cent range.

The Hon. ADAM SEARLE: The prices charged to customers have risen in the past few years, even though demand has fallen and demand is projected to fall further by the Australian Energy Market Operator [AEMO].

Mr FENNELLY: I think there are a number of submissions that have been put to you. The cost of exploration has increased dramatically. I think in our submission we—EnergyQuest, in their gas industry trends say that between 2000 and 2013 exploration development costs for new reserves has increased six-fold.

The Hon. ADAM SEARLE: Yes, but you are just trying to persuade us—

Mr FENNELLY: Piping, infrastructure, labour. There is a combination of issues—

The Hon. ADAM SEARLE: —that the number one cause of price rises was exposure to the international market, which has not happened yet, sir. That was misleading.

Mr FENNELLY: What was misleading?

The Hon. ADAM SEARLE: You were trying to persuade us just then that the number one cause of price rises on the east coast was exposure to the international market. That is only just starting.

Mr FENNELLY: I was trying to understand what Mr Buckingham was actually asking me. He said, "What is the number one driver?"

The Hon. ADAM SEARLE: That is right.

Mr FENNELLY: And it will be the move to—

Mr JEREMY BUCKINGHAM: So the number one driver, just to be clear on—

The Hon. NIALL BLAIR: Point of order: Hansard has absolutely no chance of being able to record a three-way conversation with two members interjecting on the answer. I please ask that members, when they ask a question, allow the witness to answer the question without interjecting.

CHAIR: I support that and rule that we have one question and one answer at a time, otherwise Hansard cannot follow.

Mr JEREMY BUCKINGHAM: APPEA's view is the principal driver of increased prices on the east coast of Australia, in terms of gas, is the move for us to become an exporter of gas. That has been the principal driver of gas price rises.

Mr FENNELLY: I think when I started I said there is a change of dynamic in the gas market, and that will be a key driver. I also referred to a point that I think has been also raised by Santos. The cost of producing gas has increased dramatically in this country and will continue to increase, unless we reduce our production cost.

Mr JEREMY BUCKINGHAM: Do you accept that the long-run marginal cost of Australian gas and specifically CSG is far worse than anywhere else in the world, and that that makes a lot of the CSG projects on the east coast of Australia particularly vulnerable and unviable in comparison to the rest of the world?

Mr FENNELLY: Not at all. We currently have some $200 billion of construction and infrastructure underway in Australia.

Mr JEREMY BUCKINGHAM: And you do not think any of that is vulnerable—

Mr FENNELLY: We have never seen—

Mr JEREMY BUCKINGHAM: —to high oil prices or competition from other places? Do you expect any of the gas trains being constructed at Gladstone to fall over?

Mr FENNELLY: No.

Mr JEREMY BUCKINGHAM: Not one?

Mr FENNELLY: No. They are so well advanced. They are almost finished. At the end of this year, most of the projects—the six trains—will be finished.

Mr JEREMY BUCKINGHAM: Do all those trains have the gas that they need to meet their contracts?

Mr FENNELLY: You will have to talk to the companies about that.

Mr JEREMY BUCKINGHAM: As recently as December last year the head of Total was out here saying they did not have the gas they needed to supply their contract. Does that make them unviable and likely to fall over?

Mr FENNELLY: No, they understand what is required to meet their contracts.

Mr JEREMY BUCKINGHAM: Gas is required, but they do not have it, do they? Do those export LNG companies have the gas they need to meet their contracts?

Mr FENNELLY: You will have to ask the companies; I cannot tell you the status of the gas supply for three different joint ventures. Some 6,000 wells are underway and a drilling program of 1,000 or 1,500 additional—

Mr JEREMY BUCKINGHAM: And you do not know whether they have the gas they need to meet their export contracts?

Mr FENNELLY: A number of public comments have been made by the chief executive officers of the leading companies—Origin, Santos—

Mr JEREMY BUCKINGHAM: And lots of them say they do not have the gas.

Mr FENNELLY: They have been very clear to the markets about their ability to meet their contracts. You will have to talk to the companies. As an industry representative, I am not in a position to answer a question about their capacity to meet their contracts.

Mr JEREMY BUCKINGHAM: That is very surprising. Is the Australian Petroleum Production and Exploration Association embarrassed by the fact that it is unable to establish an industry in New South Wales? You have run big public relations campaigns with slogans saying, "We want CSG—our natural advantage". Are you embarrassed that you have been unable to persuade New South Wales to accept a coal seam gas industry?

Mr FENNELLY: Probably the most embarrassing thing that I have noticed is the lack of political leadership in this Parliament, and particularly from you. You have said that you are hell bent on increasing the cost of production in this State. That is negligent language.

Mr JEREMY BUCKINGHAM: I have never said that I wanted to increase the cost of production; I said that I wanted to make you pay the full cost of production. Are you referring to other members of this Parliament? I do not write policy or legislation. Are you referring to the current Government when you say that?

Mr FENNELLY: To answer the question—

Mr JEREMY BUCKINGHAM: Do you accept that the regulatory regime—

CHAIR: Order! The witness should be allowed to answer the question.

Mr JEREMY BUCKINGHAM: I was just—

CHAIR: You were talking over him.

Mr JEREMY BUCKINGHAM: He had not started talking.

CHAIR: He had.

Mr JEREMY BUCKINGHAM: Are you happy with the regulatory—

CHAIR: You are taking up my time now.

Mr JEREMY BUCKINGHAM: Are you happy with the current coal seam gas regulatory regime in New South Wales?

Mr FENNELLY: We are working with the Government as we speak on the NSW Gas Plan and a range of measures have been announced. We also have the Chief Scientist and Engineer's final report. We are working with the Government on guidelines and regulations that will apply to the industry. We are not after more regulation though we are after certainty. We have to stop moving the goalposts. To get investment in these two projects in particular involving AGL and Santos, we need regulatory certainty. That is what is required. If you are on a board of a major company that is about to invest hundreds of millions of dollars, you want certainty. That is what we need in this State.

Mr JEREMY BUCKINGHAM: Do you have certainty?

Mr FENNELLY: No, we do not at the moment.

Mr JEREMY BUCKINGHAM: Do you think you will get it soon?

Mr FENNELLY: We do not have it at the moment.

Mr JEREMY BUCKINGHAM: Do you think you will have that regulatory certainty soon?

Mr FENNELLY: We are working actively with Minister Roberts to ensure that the NSW Gas Plan reflects best practice. The industry has had solid input into the development of those regulations.

Mr JEREMY BUCKINGHAM: Has it?

Mr FENNELLY: As is indicated in the plan, it will then be regulated by the Environment Protection Authority.

CHAIR: I have 45 seconds of my time left in which to ask questions thanks to Mr Buckingham. Do you feel that you are getting the cooperation you need from the Government to lift the moratorium in a responsible way?

Mr FENNELLY: The greatest challenge is the achievement of a recognition that we have an energy security challenge in this State. That has taken some time. Yes, bricks have been thrown by various parties. The reality is that I think we now have an understanding throughout Parliament, but particularly within the Government, that we have a strategic threat to the New South Wales economy. It is a threat which cannot be ignored and which must be confronted. We can talk about reservation policies or whatever, but unless we develop gas in this State the people of New South Wales will be paying dearly and, of course, manufacturing and other industries will be potentially jeopardised.

CHAIR: Correct me if I am wrong, but fundamentally the Government needs to develop a policy and we need to make recommendations. We are here to try to answer those questions.

Mr FENNELLY: The NSW Gas Plan is a positive step, and we have said so. We are working with the Minister as we speak.

Mr SCOT MacDONALD: I refer to page 2 of your submission, which mentions a "CSG freeze". Are you referring to the moratorium?

Mr DWYER: That is a situation where there is no further development other than the development that is underway at the Camden project.

Mr SCOT MacDONALD: Camden and Gloucester?

Mr DWYER: No. If only Camden continues, that is the scenario.

Mr SCOT MacDONALD: And nothing else. We have not heard much about early exploration. If we are not to run out of gas in 10, 20 or 30 years, what is the timeframe for exploration?

Mr FENNELLY: AGL and Santos have given the Committee a timeframe. They are saying that ideally they would like to bring on production from 2017 to the end of the decade. In a perfect situation, you would look at three to four years to get to production stage; that is, rolling out pipeline.

Mr SCOT MacDONALD: If I understand it correctly, to bring on new gas you need to be looking four or five years ahead. You need to be testing and exploring.

Mr FENNELLY: Very much so.

Mr SCOT MacDONALD: What has happened to that sort of activity? I am not talking about Narrabri and Gloucester; I am talking about people looking at maps and deciding where they can go.

Mr FENNELLY: We have been talking to the Minister about this very important point. Rightly so, there is focus on both Santos and AGL. We cannot lose sight of the fact that we still need to encourage exploration; it is an ongoing activity.

Mr SCOT MacDONALD: For 10 or 20 years.

Mr FENNELLY: Yes. The Minister has indicated that he is the Minister responsible for developing the gas industry. He wants to work with us to understand what are the barriers to entry for explorers. He is concerned that we do not get cowboys coming in—

Mr SCOT MacDONALD: And rightly so.

Mr FENNELLY: —or speculators, for want of a better term. He wants to ensure that they are quality companies, that they have financial standing and a good reputation, and that they have a commitment to the New South Wales economy. That is what he is seeking. I think we can work together to ensure we have a regime that encourages exploration, and I am confident of that.

Mr SCOT MacDONALD: We had a history until four years ago of some of those operators running around the countryside.

Mr FENNELLY: Yes.

Mr SCOT MacDONALD: That is interesting; that is good.

The Hon. Dr PETER PHELPS: First, it is wonderful to hear an industry association talking about free, efficient and competitive markets. It is as pleasing as it is rare to hear that sort of thing. You mentioned that one of the largest gasfields in Australia is located in New South Wales. Which one is it?

Mr FENNELLY: It is sitting right under the Santos reserves.

The Hon. Dr PETER PHELPS: In the Pilliga?

Mr FENNELLY: Yes.

The Hon. Dr PETER PHELPS: Is there an estimate of the size of that reserve? What are the known reserves there?

Mr FENNELLY: I do not have the figures to hand. I will take that question on notice.

The Hon. Dr PETER PHELPS: Would it be fair to say that the New South Wales known reserves are all known at this stage, or at least the substantial gas reserves are known, or is there room for exploration to continue in the future?

Mr FENNELLY: There is certainly room for exploration. As I indicated, there is an email that signals the potential supply opportunities in New South Wales. The most important thing is that we need to prove the reserves. That is often overlooked. One of the important aspects of exploration is that we need to understand the nature of the geography and the reserves. That is why exploration is a critical feature of the development of the gas industry.

The Hon. Dr PETER PHELPS: The known reserves in New South Wales at the moment are extensive. You might need to take this question on notice. At current levels of production and consumption, how long will those reserves last if they are used purely for domestic purposes in New South Wales?

Mr FENNELLY: Based on the Australian Energy Market Operator's figures and on today's demand, which obviously will increase, we are saying that we have of the order of 500 years of supply.

The Hon. Dr PETER PHELPS: That gives a lot of time for solar PV technology to develop, does it not?

Mr FENNELLY: Indeed.

Mr JEREMY BUCKINGHAM: It is ready to go.

The Hon. Dr PETER PHELPS: According to Jeremy it is always sunny somewhere.

Mr JEREMY BUCKINGHAM: Do you still use an abacus?

CHAIR: Order!

The Hon. Dr PETER PHELPS: Approximately how many jobs rest on the development of the coal seam gas industry in New South Wales?

Mr FENNELLY: Ideally, if we have a gas strategy or plan that encourages investment and development of Pilliga and Gloucester and exploration, we are saying that it will generate in the order of 20,000 to 30,000 indirect and direct jobs. There is an ongoing spend and activity as part of exploration and developing production. Part of that would be construction and pipeline activity. However, it would provide a real fillip to regional New South Wales. I can only point to the revitalisation of regional Queensland as a result of the gas industry.

The Hon. Dr PETER PHELPS: On that point, investment funds are not locked into New South Wales are they? If New South Wales decides to take a head-in-the-ground attitude and turns its back on this exciting new prospect, money will go elsewhere, whether within Australia or to other more generous jurisdictions?

Mr FENNELLY: That troubles me greatly and that is why I read the Minister's quote. We have to stop the point-scoring and undermining. The reality is that if we do not we are living in a fool's paradise. This State will suffer and suffer badly. Members of every persuasion would have heard evidence that this State is confronting a real economic challenge.

The Hon. Dr PETER PHELPS: If there had not been this stop/start approach to coal seam gas development in New South Wales do you believe that the potential shortfall that we will face in 2016-17 could have been averted?

Mr FENNELLY: Absolutely. AGL was looking at production in 2016-17, and Santos was anticipating about the same period. They were mobilised, resourced and ready to go.

The Hon. Dr PETER PHELPS: So, the shortfall that may well occur has nothing to do with market failure or inefficiencies of supply and demand; it is purely a government creation?

Mr FENNELLY: I think it is a reflection of the Australian attitude of "She'll be right". It will not be right. The reality is that in the next two years we will confront real challenges, particularly in the manufacturing sector.

The Hon. NIALL BLAIR: I refer to the benchmark compensation agreements. I would like some clarification. I agree with the idea of flexibility and that most farms are different. However, there was a reason that the agreements were drafted, was there not? People did not have good experiences in the past, particularly with regard to farmers receiving some sort of equity. Is that not the reason for the benchmarks? If I am wrong, please tell me. Is that not a good reason to have at least a safety net?

Mr FENNELLY: I am simply cautioning. As I said, in Queensland there are more than 5,000 agreements. Initially some farming groups were concerned about how the process was conducted. There were disputes about well placement. Engineers were belligerent about the site of wells. They now work with the farmers. There is a different approach, a different level of trust and a different attitude. You are talking about whether there are guidelines or some sort of framework. We are happy to work with the Government on that. All we are saying, and as you said, is that it is not a straightforward issue. We have an open mind about that discussion, particularly in New South Wales. If it is an attempt to provide greater certainty and confidence, we will certainly look at it. I said that a one-size-fits-all approach is problematic.

The Hon. NIALL BLAIR: I have acknowledged that flexibility and one-size-fits-all does not work. However, should there not be a safety net, for want of a better term, to ensure that we do not have problems?

You have acknowledged that one of the things that everybody is trying to achieve is not having speculators running around doing the wrong thing.

Mr FENNELLY: Yes.

The Hon. NIALL BLAIR: Wouldn't the benchmark provide another level of protection against some dodgy operators that may end up doing over a landowner in an agreement? Surely the benchmarking provides some protection against that?

Mr FENNELLY: Yes and of course in the NSW Gas Plan, there are two key points:

> The NSW Government will mandate by law that landholders are entitled to receive compensation for petroleum exploration and production ...

Then it goes on: IPART will "benchmark compensation rates annually" and will consider "the economic benefits of exploration and production over the expected life of the wells". Where that goes at the moment is still a long way away but that will be a complex exercise for IPART, I have no doubt about that. What you are saying is enshrined in the NSW Gas Plan—the principle.

The Hon. NIALL BLAIR: I know what I am saying. I was just trying to clarify what your position was because I would hate the flexibility to be at the detriment of what I think would be the reasoning behind the benchmarking, which was, to a degree, a "safety net", rather than a "benchmark", is probably a better word.

Mr FENNELLY: Yes.

CHAIR: "Benchmark" in your sense being "minimum standard"?

The Hon. NIALL BLAIR: Yes. Well, minimum level. We have heard some horror stories from other jurisdictions where there are farmers in particular getting very little compensation for some of the imposts on some of their landholdings and that is the point I was making—or the detriment to other assets—roads, fences et cetera, things you have spoken about.

Mr FENNELLY: I note that you are a National Party member but the thing is that there is a widespread awareness of how the negotiation occurs. As I said before, the industry—

The Hon. NIALL BLAIR: I know I am a National Party member. I was giving you the opportunity to clarify what I thought was a confusing statement in your submission.

Mr FENNELLY: I see what you are saying, yes.

The Hon. ADAM SEARLE: But in fact they do not seem to be in favour of minimum standards.

CHAIR: Thank you for coming, Mr Fennelly and Mr Dwyer. You took a question on notice. Given the short timeframe for this inquiry, the Committee has resolved that answers to questions on notice are to be returned within seven days. We would appreciate your help in assisting us to meet our reporting deadline. The Secretariat will contact you in relation to questions you have taken on notice.

(The witnesses withdrew)

(The Committee adjourned at 4.18 p.m.)