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Australia's Domestic Gas Security Mechanism Consultation
Department of Industry, Science and Resources
GPO Box 2013
ACT 2600

RE: CONSULTATION PAPER: *CONSULTATION ON REFORMING AUSTRALIA'S DOMESTIC GAS SECURITY MECHANISM*

Please find below the Australian Petroleum Production & Exploration Association's (APPEA) comments and recommendations on the proposed changes to the Australian Domestic Gas Security Mechanism (ADGSM) Guidelines.

Australia has established itself as a trusted energy and economic partner in the region and a reliable, stable investment destination. The role of gas is widely acknowledged by governments in our region as being critical to ensuring energy security and in the region's transition to a net-zero emissions future with Australian liquefied natural gas (LNG) representing a key pillar of regional energy supply. The importers of Australian natural gas are key investors in the gas sector and in the LNG projects themselves, as well as in Australia's economy more broadly. In many cases, these countries are also our key diplomatic and national security partners in the region.

The proposed revisions to the ADGSM Guidelines risk undermining Australia's role in the region. The government's proposed 30-day minimum notice period for breaking critical energy supply contracts and broad ministerial discretion to limit LNG exports may result in allied countries in our region being left without the gas they need to power their homes and industries and will encourage them to seek alternative energy supply from more secure sources. The Guidelines undermine the certainty of long-term export contracts and will make investment in Australia's market less attractive. Regional partners, including the government of Japan, have already raised concerns with the proposed changes.

The Guidelines do nothing to address the root causes of forecast domestic gas shortfalls and instead export energy uncertainty to the region. The Australian Competition and Consumer Commission (ACCC) in its January 2023 *Gas Inquiry Interim Report* identifies investment in new gas supply as the solution to shortfalls in the domestic gas market. However, instead of addressing the structural factors driving potential shortfalls and supporting new domestic gas supply, the proposed Guidelines effectively export Australia's domestic gas market uncertainty to the region.

To address forecast shortfalls in the domestic gas market, increase the transparency of the ADGSM and moderate its impacts, APPEA recommends:

- **The government should prioritise increasing domestic gas supply, rather than compromising international contracts, investments and partnerships.**
- **The assessment and determination of a shortfall must be objective and transparent.**
- **The procedures for triggering the ADGSM must be more robust and objective – minimising ministerial discretion and maximising the notice provided to LNG producers and customers.**
- **The Guidelines cannot be considered or revised in isolation and must align with the ongoing Heads of Agreement and Code of Conduct discussions and processes.**

APPEA and its members remain committed to providing a secure, reliable and affordable supply of natural gas for households and businesses, in Australia and the region, and to working with government to find an effective, transparent, workable, and sustainable way forward.

COMMENTS AND RECOMMENDATIONS

The government should prioritise increasing domestic gas supply, rather than compromising international contracts, investments and partnerships. In its January 2023 *Gas Inquiry Interim Report*, the ACCC anticipates gas shortfalls from 2027. In the report, the ACCC concludes that "*avoiding long-term supply shortfalls will require development of new supply*". In contrast, recent interventions, including the December 2022 Price Order and proposed Mandatory Code of Conduct, are undermining investor confidence, placing investment in new domestic supply in jeopardy, and exacerbating the risk of future shortfalls rather than moderating them. This can already be seen with the $1 billion Senex Atlas project expansion – backed by the South Korean POSCO Group – being put on hold following the recent interventions. The proposed changes to the ADGSM Guidelines decrease the transparency of the mechanism, by affording very broad discretion to the Minister, and decrease the notice period for LNG exporters and importers of interruptions to gas contracts. This does nothing to address the root cause of potential shortfalls but instead streamlines the breaking of international contracts to make up for domestic market failures. Rather, the government should be looking to provide clear and stable policies as well as well designed, stable and predictable regulation to provide industry with the confidence to invest in new domestic gas supplies. Further the government should be encouraging southern states to remove barriers to new oil and gas developments, to ensure gas can be available where it is needed most.

The prospect of the Minister deciding not to permit LNG exports to cover a shortfall is likely to create serious uncertainty for the LNG exporters and their shareholders and ultimately overseas customers. The Guidelines propose breaking critical energy supply contracts with as little as 30-days' notice, risking gas shortfalls for households and business in important partner countries in the region. Overseas customers require reliable and secure gas supply and will look to other jurisdictions if supply from Australia becomes uncertain. Australian LNG exporters will also have less incentive to invest in more supply because there is no guarantee of an appropriate rate of return if the Minister decides the gas needs to be supplied domestically at a fixed price.

Cascading government intervention in the gas market puts Australia's reputation as a stable and reliable energy and trading partner at risk. The importers of Australian natural gas are also key investors in the gas sector and in the LNG projects themselves, as well as in Australia's economy more broadly.[1] Combined, the key LNG importers of Japan, China, Korea and Taiwan alone have invested over $400 billion in the Australian economy, with Japan representing the fourth largest national investor in Australia (See Annex 2). However, investors are watching these developments in the gas market with great concern. Capital is mobile and if Australia loses its reputation as a safe, dependable investment destination, it will have significant repercussions across the economy and on the cost of living for all Australians. This is especially the case given the investment we need to grow the economy and maintain secure affordable energy supply, while we transition to net zero.

These trading partners are also countries with whom Australia holds close diplomatic and security relationships with. Australia's commitment to bolstering energy, food and national security with these important partners must not be undermined. APPEA agrees with the Prime Minister, who recently said at the Press Club that, "*Energy security is a pressing global challenge. We can make it a national economic strength if we get it right*." However, the Guidelines work in opposition to this, undermining energy and national security amongst our regional allies and impacting the rebuilding of trade ties with China, which is a key investor in and importer of Australian LNG.

1. The assessment and determination of a shortfall must be objective and transparent. The implementation of the ADGSM is predicated on a forecast gas shortfall in the domestic market. Section

[1] See Annex 2 for a table of Australia's major LNG export and investment partners and the scale of their overall economic contribution to Australia.

8(9) affords the Minister complete discretion in determining whether there is a shortfall, without any input from LNG producers, domestic gas producers or industry experts. A shortfall does not exist where domestic supply commitments from the LNG exporters are sufficient to cover any gap between forecast gas demand and all other sources of supply in a given quarter. The headline of the ACCC *Gas Inquiry Interim Report* is a projected 30 PJ shortfall in 2023, but the report caveats this stating the shortfall only exists "*if the Queensland LNG producers export all of their uncontracted gas*". The ACCC then identifies, based on engagement with LNG producers, 58 PJ of uncontracted gas from LNG producers, suggesting no shortfall at all. The wide-reaching government discretion and lack of transparency in the determination of a shortfall means that a shortfall quarter could be announced even when in practice there is sufficient supply, with the current structure potentially leading to avoidable and premature shortfall notifications. In-turn, this broad discretion leads to poor public policy outcomes, creating uncertainty and risk, chilling investment and resulting in less gas supply in the long-term.

LNG exporters should be consulted in advance of a shortfall determination. To further add to the robustness and objectivity of the shortfall assessment, the "*Consultation with LNG projects"* process outlined between section 8 (5) and (9) should occur prior to the *"Minister's notification"* process outlined in section 8 (3) and (4), rather than after it. Early consultation with the industry prior to the issuing of the Minister's notification will provide the government with access to up-to-date data on predicted supply compared with relying on out-of-date forecasts envisaged by the Guidelines. This will prevent the premature and/or erroneous triggering of the ADGSM.

2. The procedures for triggering and implementing the ADGSM must be more robust and objective – minimising ministerial discretion and maximising the notice provided to LNG producers and customers. The broad ministerial discretion and lack of transparency built into the Guidelines on when the ADGSM may be triggered creates significant uncertainty in the market in general and amongst gas importers in particular. Additionally, there is limited certainty and transparency around the processing of export permits. Broad ministerial discretion and the absence of an export permit approval criteria make the process highly subjective. The Minister is also permitted to depart from the Guidelines, raising issues of procedural fairness (see section 5(3)). This gives the Minister an enormous amount of discretion to determine gas supply issues in the market going forward.

The ADGSM should only be triggered to address a likely shortfall in the next quarter, rather than in subsequent quarters. Section 8(12) gives the Minister the ability to implement the Mechanism, even if there is no shortfall forecast, to deal with a potential shortfall for a subsequent quarter. In the lead up to the development of the Heads of Agreement there was concern about how peak periods were factored into annual forecast shortfall determinations. As the Guidelines move to quarterly assessments, a thorough and transparent process of how this issue is addressed should be considered by government.

The proposed Guidelines appear to undermine the operation of Australian Customs Regulations as they are not subject to parliamentary oversight or scrutiny. According to Section 13GF of the *Customs (Prohibited Exports) Regulations 1958*[2] (the Customs Regulations), the Minister for Resources has the capacity to publish guidelines relevant to the Customs Regulations. Section 13GE of the Customs Regulations defines what would constitute a domestic shortfall year. This regulation remains in force, and it may be amended or disallowed through the parliament. However, under the proposed ADGSM Guidelines, note:

[2] Customs (Prohibited Exports) Regulations 1958, https://www.legislation.gov.au/Details/F2017C00597.

- Section 5(2): *These Guidelines are subject to, and do not replace or amend the requirements of, the Regulations and the 'Customs Act 1901', which should be read in conjunction with these Guidelines,* and
- Section 5(3): *These Guidelines are not a legislative instrument. The Minister may depart from the Guidelines where justified by the circumstances.*

Sections 5(2) and 5(3) of the Guidelines appears to undermine the operation of Section 13GE of the Customs Regulations as they are not subject to parliamentary oversight or scrutiny. Furthermore, Section 13GE of the Customs Regulations defines the settings for the Minister for Resources to declare a domestic shortfall year, whereas the Guidelines provide the Minister with the framework to declare a domestic shortfall quarter. The shift from an annual to a quarterly shortfall period in the Guidelines may also be inconsistent with the ongoing operation of Section 13GE of the Regulations.

3. The Guidelines cannot be considered or revised in isolation and must align with the ongoing Heads of Agreement and Code of Conduct discussions and processes. The ADGSM does not exist in isolation, rather it must be considered in the context of the ongoing Heads of Agreement discussions and the proposed Mandatory Code of Conduct, all of which relate to the supply of gas to the domestic market and to the operations of LNG producers. Given the interdependence of these complex market agreements and interventions, all these elements need to be considered together by both the government and Australian gas producers, including gas exporters and domestic-focussed suppliers.

The industry is committed to maintaining the delivery of affordable and reliable gas to households, manufacturers, and power generators, in Australia and the region. Providing an attractive investment environment to encourage more investment in natural gas on the east coast is the best and most enduring way to ensure energy security and competitive price outcomes.

APPEA would be pleased to discuss these issues further with the Department and to provide any additional information that may be useful.

Yours sincerely

S McCulloch

Samantha McCulloch
Chief Executive

ANNEX 1: THE AUSTRALIAN UPSTREAM OIL AND GAS INDUSTRY

The Australian oil and gas industry has invested well over $400 billion in the Australian economy undertaking exploration and developing natural gas production, transport, liquefaction and export facilities over the last decade. A further $27 billion commitment has been made in the past 18 months.

This investment will deliver returns for Australia for decades to come, through increased gas supply for Australian customers, export revenue, jobs, and in payments to governments in royalties and taxes – nearly $65 billion[3] in payments have been made to government over the last decade.

LNG is now Australia's second largest export commodity after iron ore, with export revenue of more than $70 billion in 2021-22, expected to rise to over $90 billion in 2022-23.[4] As well as providing a significant return to the Australian economy, this LNG export industry is also a key enabler of domestic gas supply.

The oil and gas industry supports 80,000 jobs directly and indirectly in Australia and hundreds of thousands more in manufacturing.

Investment in new gas supply for the east coast market is critical to the ongoing functioning of a stable, reliable electricity market and affordable domestic gas supply. These conditions are vital as the broader energy market transitions through the closure of coal-fired power generators, the construction and grid connection of new renewable projects and the implementation of storage or peaking capacity to firm renewables.[5]

The industry is pivotal to reaching net zero, supporting the transition away from coal, providing the firm dispatchable energy required to unlock our renewable energy potential, and powering Australian industries across the economy. The industry is also central to delivering step-change technologies including carbon capture, utilisation and storage, and low-carbon hydrogen.

APPEA is the peak national body representing Australia's oil and gas exploration and production industry, accounting for around 95 per cent of the nation's petroleum production.

APPEA has around 60 full member companies representing oil and gas explorers and producers active in Australia, as well as around 140 associate member companies that provide a wide range of goods and services to the upstream oil and gas industry.

APPEA has for many years supported a national climate change policy that delivers greenhouse gas emissions reductions, consistent with the objectives of the Paris Agreement, and applies a broad-based price signal on emissions to facilitate investment decisions at the lowest cost to the economy. APPEA is committed to working with the Government as it develops policy responses to climate change.

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[3] See Media Release: Oil and gas industry helps bankroll public services despite pandemic challenge | APPEA and Historical-Summary-2019-20.pdf (appea.com.au) for more information. Over and above this, Australia's LNG exporters are set to almost triple their financial contribution to the public this financial year, forecasted to pay an extra $9 billion to federal and state governments. New preliminary forecasts released in October 2022 revealed the gas export sector is estimated to pay around $13 billion during 2022-23 – up from $4.8 billion forecast for last financial year (see Media Release: LNG exporters forecast to pay extra $9 billion to governments as tax and royalty collections almost triple | APPEA for more information).

[4] See Office of the Chief Economist - Resources and Energy Quarterly - September 2022 (industry.gov.au) for more information.

[5] For example, the Australian Energy Market Operator's (AEMO) recent *2022 Integrated System Plan* (available at AEMO | 2022 Integrated System Plan (ISP)) confirmed the long and enduring value of natural gas partnering with renewables with the report finding (page 57): *"Peaking gas-fired generators will play a crucial role as significant coal-fired generation retires, as an on-demand fuel source during extended periods of low VRE output, and to provide power system services for grid security and stability and High renewable output and high demand – gas is needed to meet the demand peaks just after sunset, and to keep going through the night to cover wind variability."* See Media Release: 'Crucial' role for gas powering electricity grid for decades: AEMO report | APPEA for more information.

ANNEX 2: MAJOR REGIONAL LNG EXPORTERS AND INVESTORS[6]

Country	Two-way trading relationship with Australia	Export market	Key export sectors	Total investment in Australia	Key investment sectors
Japan	Third-largest partner A$66.3 billion	Second-largest market A$46.4 billion	**LNG** Coal Iron ore Beef Copper Aluminum	A$265 billion	Coal Iron ore **LNG**
South Korea	Fourth-largest partner A$34.9 billion	Fourth-largest market A$25.3 billion	Iron ore Coal **LNG** Beef	A$32.7 billion	**LNG** Iron ore Coal Rare earths
Taiwan	Seventh-largest partner (merchandise) A$32.6 billion	Fifth-largest market (merchandise) A$23.1 billion	Coal **LNG** Iron ore Aluminum Copper	A$14.4 billion	Minerals **LNG**
China	Largest partner A$267 billion	Largest market A$178 billion	Iron ore Coal **LNG** Beef Wool Education Tourism	A$91.8 billion	Real estate Manufacturing **LNG** Mineral exploration

[6] Data refers to the year 2020, as the latest available data on the Department of Foreign Affairs and Trade's country briefs: https://www.dfat.gov.au/geo/countries-economies-and-regions.