Gorgon Gas Project: Application for Joint Selling Authorisation

ACCC Draft Determination: Response by the DomGas Alliance

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C/- DBP, Level 6, 12-14 The Esplanade, Perth WA 6000
Postal Address - PO Box Z5267 St Georges Terrace Perth WA 6831
Telephone: +61 8 9223 4300 Facsimile: +61 8 9223 4301
Website: www.domgas.com.au

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1. Overview

1. The DomGas Alliance is dismayed and disappointed that the ACCC proposes to allow Shell, Chevron and ExxonMobil to combine as a cartel to fix prices for the sale of Gorgon gas to consumers.

2. The Alliance recognises that the ACCC's assessment is being undertaken amidst intense political interest in the Gorgon Project and intense pressure on the part of the applicants.

3. The Alliance had expressed hope that in this highly politicised environment, the ACCC would stand firm against attempts by Shell, Chevron and ExxonMobil to characterise the issues as being anti-Gorgon investment.

4. It is disappointing that the Draft Determination appears to rely almost exclusively on the claims and assertions by Shell, Chevron and ExxonMobil - and their consultants' reports - while dismissing the substantial evidence presented by consumers.

5. The ACCC also appears to have ignored its own commissioned Allen Consulting Group report which dismissed as "misleading" the Gorgon applicants' claims that joint selling was necessary to manage risk or to underpin project investment.

6. That report considered it "difficult to accept the argument put forward by the Applicants that joint marketing is required as a risk mitigation tool" because:

    - Domestic gas represents less than 5 per cent of the Gorgon gas resources;
    - Domestic gas would account for less than 5 per cent of total Gorgon revenue;
    - Shell, Chevron and ExxonMobil are three of the largest companies in the world with combined 2008 income of over $US 120 billion;
    - Chevron and Shell are equity partners in the largest domestic gas seller in Western Australia;
    - The domestic phase post-dates LNG export start-up by three or more years;
    - Domestic gas prices will almost certainly have lower price volatility than LNG exports;
    - Domestic sales will be subject to take-or-pay contract provisions;

- Chevron and Shell management are familiar with the WA gas market through their investment in the NWS project; and

- ExxonMobil is the world's largest and most profitable oil and gas company with over 40 years experience in the Australian gas market.[1]

7. The report concluded that the applicants had failed to demonstrate why joint marketing for domestic should be required following a Final Investment Decision on the Gorgon Project:

   "[I]t could be argued that when the FID is made, the Applicants should then be required to substantiate why joint marketing should occur. This may be particularly relevant because sales contracts may not be negotiated for some time."[2]

8. The Gorgon applicants have failed to do so. There is no justification for the ACCC permitting cartel selling of Gorgon gas to Australian consumers following the Project's FID announcement in September 2009.

9. The Draft Determination's assessment contains serious errors of fact. It does not reflect market reality and the immense power exercised by Shell, Chevron and ExxonMobil – the world's biggest oil and gas producers.

10. The ACCC for instance expresses a mistaken belief that major producers and different Projects would compete with each other on price to expand market share.

11. As the Alliance has pointed out, the WA gas market is experiencing - and will continue to experience - an extremely tight supply situation with producers withholding supply. In such a market, producers are seeking to maximise prices for the limited supplies of gas that they make available. They are not seeking to compete on price to increase market share as the ACCC would believe.

12. Similarly, the Draft Determination appears to accept the spurious claims by the applicants on the risks of an "oversupply" in the WA market. Such claims are patently false, and indeed are contradicted by major producer assessments of the WA gas market.

13. If granted, final authorisation will entrench and extend the current market structure which is already one of the most anti-competitive markets in Australia.

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[1] Allen Consulting Group, 'Gorgon Gas Project Joint Venture Application for Authorisation of Joint Marketing', Final Report to the Australian Competition and Consumer Commission, July 2009.

[2] ACG Report, p.30.

14. Just two producer groups control close to 100 per cent of the market. This is the outcome of the ACCC's actions over many years to protect anti-competitive cartel selling arrangements.

15. The absence of competition and the exercise of market power by major producers have impacted every business and household. As a result, WA consumers are being asked to pay around three times the price of new gas compared to in Victoria.

16. Far from the notional "LNG-netback" prices contemplated by the ACCC, major gas producers are now obtaining a premium price return from Australian consumers – in excess of that from overseas customers. As Apache Energy has publicly stated: "For price, it's the domestic market, for quantity it's the LNG market."[3]

17. As the Allen Consulting Group report points out, authorisation will lead to higher gas prices for Australian consumers.

18. The proposed six year authorisation period would also negate any competitive benefit that might be expected from the Gorgon Project.

19. The Allen Consulting Group report warns that if joint selling arrangements enable the Gorgon supply to be locked away, the Project cannot contribute to "competitive tension" in the market place with respect to other gas developments.[4]

20. Furthermore, the six year authorisation period is excessive and likely to be overtaken by ongoing developments in the WA gas market.

21. Following the successful deployment and operation of a Gas Bulletin Board during the 2008 Varanus Island outage, the WA Government is progressing work to establish a permanent arrangement.

22. According to the WA Independent Market Operator, a Gas Bulletin Board could be successfully implemented in Western Australia and within a short period of time.

23. Should the ACCC decide to grant final authorisation, the period of authorisation should be limited to 2 years or until the establishment of a WA Gas Bulletin Board or comparable arrangement – whichever is the earlier.

24. A decision to grant final authorisation will have profound implications for industry, small businesses and households. It is vital that consumers have confidence in the ACCC's authorisation process

[3] Reuters, 'Apache decision on Australian gas by October', 4 June 2009, available at: http://www.reuters.com/article/GlobalEnergy09/idUSTRE5535LZ20090604
[4] ACG Report, p.30.

25. The Alliance urges that an independent panel be appointed to undertake a detailed review of the evidence presented by the applicants and interested parties, and the findings of the Allen Consulting Group report.

26. This review would assist the ACCC in making a final determination, and provide confidence to Australian consumers in the authorisation process.

2. The ACCC's findings on an "immature" WA gas market are based on serious errors of fact

27. The Alliance's response to the Draft Determination does not propose to critique every finding by the ACCC and will instead highlight some of the most serious errors of fact.

28. The Draft Determination considers that separate marketing is not practical given what it considers to be: "lumpy" demand profile and a small number of large customers with long term contracts; the lack of liquidity; and very limited gas storage options in the WA gas market.

29. These findings are based on serious errors of fact. They do not reflect the current market reality which has shown significant transformation over the past 10 years.

2.1 Gas storage and balancing

30. Gas infrastructure operators, gas aggregators and retailers, and major gas users provided detailed evidence about the operation of gas storage and balancing arrangements in the current WA market.

31. DBP's submission for example highlighted the recent and substantial changes in the role that the duplicated DBNGP can play in load profile management and storage:

- The capacity of the DBNGP is being expanded with expansion expected to be completed in early 2010;

- Following expansion, the pipeline will be approximately 85 per cent looped with approximately 441 km of additional looping installed as part of Stage 5B;

- Firm full haul capacity of the pipeline will be increased to approximately 840 TJ/day;

- The DBNGP provides shippers with an unconditional Accumulated Imbalance Limit of +/- 8 per cent of Contracted Capacity and a conditional limit of +/- 20 per cent – which are among the most generous in the world;

- Given that the current Contracted Capacity across all firm services on the DBNGP exceeds 800 TJ/day, this equates to over 160 TJ/day – which is more than the proposed initial production target for the Gorgon Project;

- In addition, DBP offers Park & Loan Storage services on the DBNGP and has entered into Operational Balancing Limits with the operators of production facilities and interconnected pipelines;

- Producers and gas customers therefore have a high degree of flexibility to balance daily, monthly and even yearly variances between contracted sales and actual gas volumes.[5]

32. DBP is in active discussions with gas shippers on engineering options to further increase the storage capability of the pipeline. This could significantly expand storage by around 150-200 TJ/d.

33. In addition, the APA Group already operates a gas storage facility at Mondarra in the Perth Basin, which is used by Western Power. A report by the WA Office of Energy during the Varanus Island outage notes:

    "[T]he APA Group's Mondarra Storage facility, which is located adjacent to both the Parmelia and DBNGP pipelines south of Dongara, has been running at full production for the entire duration of the outage, presently contributing a useful 12 TJ/d to the overall WA gas market."[6]

34. This volume alone *exceeds* the additional 10 TJ/d in domestic gas supply that the Gorgon participants claim would be delivered under joint selling as opposed to separate selling, and which the ACCC assesses to be a potential benefit from authorisation.

35. The Alliance understands that APA has proposed further expanding this storage capacity through the installation of additional gas compressors.

36. The Draft Determination's findings do not therefore reflect recent and ongoing developments in the WA gas market.

37. It is compelling that a report commissioned by APPEA, and presumably prepared in close consultation with major gas producers, recognises the existing role of pipeline infrastructure. The report does not consider any lack of gas storage options as a significant gas market barrier:

    "Australia's need for storage facilities is mitigated by the fact that gas production facilities are generally located close to the main demand

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[5] DBP submission to the ACCC, 4 June 2009.
[6] Office of Energy, 'Information Update', 18 June 2008, available at: http://www.energy.wa.gov.au/cproot/1179/10284/Gas%20Update%20OOE%20Web%2020%20Jun%2008.pdf

centres. Gas production matches demand and Australia relies on spare pipeline capacity to deal with the supply / demand mismatch. *This spare capacity acts effectively as gas storage*."

"Unlike other countries, most of Australia is not exposed to strong seasonal swings in demand. However, Victoria, Tasmania and the ACT experience seasonality in winter demand and the storage facilities do not always solve the problem as they have limited capacity. *Whilst it would be ideal to have additional storage facilities in key locations, an option to increase pipeline capacity will also increase flexibility in the markets*."[7]

38. The Draft Determination's findings are based on serious errors of fact and should be reviewed in light of the substantial factual evidence on recent and ongoing WA market developments.

2.2 Short term trading and Gas Bulletin Board

39. The Draft Determination has made serious errors of fact by failing to reflect the significant expansion in short term gas trading that is already underway in Western Australia.

40. As DBP's submission points out, a gas trading exchange (gasTrading) already facilitates trades of both gas and pipeline capacity, with trades accounting for up to 10 per cent of the gas delivered into the DBNGP on some days.

41. Extensive work is also being undertaken by the State Government and gas market participants to improve transparency and expand short term trading through the establishment of a Gas Bulletin Board.

42. A Gas Bulletin Board was rapidly developed and deployed by the WA Independent Market Operator in response to the 2008 Varanus Island outage. It operated for over three months between July – October 2008. The Independent Market Operator reports:

"The GBB was designed and implemented in a short period of time to facilitate the trading in natural gas during the disruption in supplies as a result of the explosion on Varanus Island.

The GBB provide transparent trade data, including pricing information, which allowed Western Australian gas users to evaluate the cost of securing gas supplies. This information was published to the public on the IMO website.

[7] Asia-Pacific Partnership and PriceWaterhouseCoopers, *Asia-Pacific Gas Market Growth*, June 2009, p.31.

The IMO received a great deal of cooperation from the gas traders, gas pipeline owners and the Office of Energy during the design and implementation of the GBB.

Despite the limited time the GBB operated, with 27 registered traders, 14 active traders, and trading volumes of 47.8 TJs, this initiative could only be viewed as a success.

The GBB demonstrated that a formal regulated gas market could be successfully implemented in Western Australia."[8]

43. The WA Office of Energy and the State's Gas Supply and Emergency Management Review Committee are currently building on the Varanus Island experience for a permanent Gas Bulletin Board.

44. An initiative by a privately owned West Australian based company, backed by a number of well established WA gas market participants, is likely to see an industry driven, independent and WA focused trading mechanism being launched during 2010. In addition to short to medium term trades, this initiative also aims at providing its members with market and pricing information presented in an aggregate manner.

45. Gas consumers are supportive of efforts to improve transparency and short term trading arrangements.

46. As the Independent Market Operator points out, such arrangements could be successfully implemented in Western Australia and within a short period of time. The proposed six year authorisation period is therefore excessive and likely to be overtaken by gas market developments.

47. Should the ACCC decide to grant final authorisation, the period of authorisation should be limited to 2 years or until the establishment of a WA Gas Bulletin Board or comparable arrangement – whichever is the earlier

2.3 The same market features have not prevented Shell, Chevron and ExxonMobil from selling separately to overseas customers

48. The Draft Determination refers to a small number of large customers, long term contracts and a lack of liquidity as features of the WA gas market preventing separate marketing.

49. However it does not adequately explain why *those very same features* have not prevented Shell, Chevron and Exxon from separately selling Gorgon gas to overseas customers.

[8] Independent Market Operator, 'Gas Bulletin Board Report', presentation to the WA Gas Supply and Emergency Management Review, available at: http://www.energy.wa.gov.au/3/3270/64/presentations.pm

50. The fact remains that Shell, Chevron and ExxonMobil have been *separately* entering into $19 billion, $50 billion and $70 billion in gas contracts:

- to supply a very small number of very large customers – "lumpy customer demand";
- covering 20 year terms;
- at a time when – according to producers' own statements - the spot market "has almost disappeared".[9]

51. As the Allen Consulting Group report points out, to the extent there are commercial risks attached to gas marketing, these lie heavily in relation to the international marketing of LNG as opposed to domestic gas:

"[T]he relative impact of differing modes of Gorgon domestic marketing on price outcomes is almost certainly less than the price volatility which LNG sales will encounter. While each of the Applicants are attempting to secure term contracts for some or all of their expected LNG entitlements from Gorgon, pricing will be heavily exposed to oil price volatility and probably spread across less than four customers. Domestic pricing is likely to be linked to less volatile indices and to multiple customer contracts."[10]

52. Domestic sales will also be subject to take-or-pay contract provisions which would transfer much of the risk associated with domestic supply to customers.[11]

53. There is no basis for concluding that a small number of large customers, long term contracts and a lack of liquidity prevent separate marketing in the Australian market. Separate marketing is practical and feasible and should be required of the Gorgon applicants.

2.4 Features of a mature market

54. It is incorrect, as the Draft Determination does, to consider that all of the features of a mature market need to be present for separate marketing to be feasible.

55. As the Parer Report pointed out as early as 2002:

"[N]ot all the features of a mature market need to be present for separate marketing from joint facilities to be feasible. If they were, separate marketing itself would probably only be of academic interest, as a high degree of competition would already be achieved. The

[9] Alliance submission of 27 August 2009, para. 51-64.
[10] ACG Report, p.24.
[11] ACG Report, p.24. Such provisions are also typically contained in LNG contracts.

existence of secondary markets with associated financial products are outcomes of a mature market, rather than prerequisites for separate marketing. For each gas producing joint venture, some market features will be more important than others in considering the feasibility of separate marketing."

"Moving toward separate marketing would be considered as part of the overall package to improve the competitive nature of the natural gas market. *Separate marketing itself should be regarded as one of the ingredients that in the appropriate circumstances helps create competition and thereby a more mature market*."[12]

56. To the extent the WA market has not matured to the extent possible, this could only be the outcome of decisions by the ACCC over many years to protect anti-competitive cartel selling arrangements.

57. The Draft Determination provides little consideration as to how such arrangements and the existing market structure of just two supply groups have suppressed, and will continue to suppress, development of those same market features identified by the ACCC.

2.5 Shell, Chevron and ExxonMobil have been compelled by competition authorities to sell separately in other countries

58. The Alliance does not agree with the Draft Determination's conclusions that the New Zealand experience is not comparable.

59. Furthermore, the Draft Determination has not adequately explained why Shell, Chevron and ExxonMobil have been able to sell separately in Norway and Denmark as required by EC competition authorities.

60. These same companies have been compelled by competition authorities to sell separately in other countries.

61. A decision by the ACCC to grant final authorisation will lead to an absurd regulatory outcome – whereby the biggest companies in China, India and Japan will enjoy the benefits of competition for Gorgon gas, while this competition is denied to Australian consumers by the ACCC.

3. Potential benefits vs. public detriment

62. The Draft Determination assesses the public benefits as including:

- "avoiding delays in bringing additional gas to market";[13]
- More domgas supply than would be the case under separate marketing – the ACCC refers to the applicants' consultants report

[12] 2002 COAG Energy Market Review Report ("the Parer Report"), pp.199-200.
[13] Draft Determination, para. 6.129.

which claims that under separate marketing 10 TJ/day less domgas will be supplied than would be the case under joint marketing;[14] and

- "lower prices".[15]

63. These assessed public benefits are based on serious errors of fact and do not reflect actual market reality as experienced by gas consumers.

3.1 Delays in domgas supply

64. It is remarkable that in accepting the claims made by the applicants about potential delays in domgas supply, the ACCC provides no quantification as to what these "delays" might be.

65. To the extent there could be any delay in relation to domgas supply, this is directly attributable to the actions of the Gorgon participants to delay domgas supply and volumes to derive maximum benefit from an extremely tight domestic market.

66. The Gorgon applicants have indicated that domgas will be delayed until end 2015. Even then, volumes will only be "up to" 150 TJ/d. They do not envisage meeting the State Agreement commitment of 300 TJ/d until 2021, i.e. some 12 years after the Project's Final Investment Decision!

67. The applicants have sought to justify this delay on the spurious claim about the need to avoid an "oversupply" (!) of gas. As outlined below, such a claim is patently false.

68. The Alliance is dismayed that the ACCC as the independent regulator has endorsed what is clearly an opportunistic abuse of market power on the part of the world's biggest oil and gas companies at the expense of consumers. It has done so without challenging the applicants' assertions on the basis of factual evidence.

3.2 Additional domgas supply

69. In assessing that more domgas supply would be expected under separate marketing, the ACCC refers to the applicants' consultants report. That report claimed that under separate marketing 10 TJ/day less domgas will be supplied than would be the case under joint marketing.

70. It should be pointed out that 10 TJ/d equates to just over *6 per cent* of the 150 TJ/d domestic supply that the Gorgon applicants expect to deliver.

[14] Draft Determination, para. 6.130.
[15] Draft Determination, para. 6.166.

71. It represents just *3 per cent* of the 300 TJ/d supply volume contained in the State Agreement.

72. In terms of the current market, 10 TJ/d equates to *less than 1 per cent* of WA gas consumption consumption.

73. It is astounding that the ACCC could assess the potential benefit of just 3 per cent of Gorgon domestic gas or 1 per cent of current WA gas consumption as outweighing the impact of higher gas and electricity prices for every business and household.

74. The Alliance recalls that similar claims were made by Shell, Chevron and their partners as part of their justification for seeking authorisation for NWSJV joint selling in 1997.

75. They claimed that joint selling would underpin an expansion in the capacity of the domestic gas processing plant to 1,100 TJ/d through the construction of an additional domestic gas processing train:

> "A discussed with Dr John Tamblyn, a representative of the Australian Competition and Consumer Commission (the ACCC) on 27 November 1995, the Joint Venture Participants are contemplating expanding the capacity of the Project. **The proposed expansion will increase the production of gas for sale in Western Australia**. This will result in the current capacity of the Domestic Gas Joint Venture (the Domgas Venture) being exceeded. **The Joint Venture Participants, for reasons of certainty, have decided to seek additional authorisation** to that issued on 15 February 1977 (the 1977 Authorisation) by the Trade Practices Commission (the TPC) to the then participants of the Project."[16]

> "To be able to compete for the supply to industrial projects forecast to be undertaken in the short to medium term, and in some cases to render a project, the Joint Venture Participants are contemplating an **expansion of capacity of 550 TJ/day to enable them to accept obligations for the supply on a firm basis of approximately 1,100 TJ/day**. Sellers are currently negotiating with existing and prospective customers for supply to various new and expanded facilities and projects. The industrial tranches of gas necessary to meet these customers' demand is in excess of what any individual participants would be able to meet from their respective shares. **Therefore these discussions must involve all the Joint Venture Participants**." [17]

> "The proposed expansion by the Joint Venture Participants therefore extends to creating additional capacity for existing customers, as well as capacity for new customers and projects. The national importance

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[16] North West Shelf Project, *Submission to the ACCC in Support of an Application for Authorisation*, 5 September 1997, para. 1.2.
[17] North West Shelf Project, *Submission to the ACCC in Support of an Application for Authorisation*, 5 September 1997, para. 9.7.

of these developments in terms of increased exports and import replacement, as well as the direct benefits enjoyed by the businesses and communities concerned, are likely to be significant. However, such an expansion decision must necessarily involve all the Joint Venture Participants, including MIMI, because it will result in supply of natural gas by the Incremental Venture … **It must also be predicated on the ability of the Joint Venture Participants to co-ordinate the marketing of any expanded capacity**."[18]

"The proposed expansion which also includes potential investment in LNG expansion entails the construction of:

(a) a second pipeline from North Rankin A platform to the onshore processing facilities on the Burrup Peninsula; and

(b) a third pipeline gas processing train and additional fractionation and stabiliser facilities (which would be installed alongside the existing processing facilities on the Burrup Peninsula)."[19]

76. This commitment to expand domestic gas capacity and to construct a third domgas processing train was never met despite:

- clear demand for domestic gas; and
- Shell, Chevron and their NWSJV partners continuing to sell jointly.

77. It is disappointing that the ACCC would once again accept these same claims by Shell and Chevron in the face of actual evidence to the contrary.

3.3 Domestic gas prices

78. The Draft Determination considers that "the price of domgas in WA is likely to be more significantly influenced by the overall volume of gas supply rather than whether that gas is jointly or separately marketed".[20]

79. It also concludes that: "To the extent joint marketing would result in lower prices, this would constitute a public benefit".[21]

80. The ACCC's contention that limiting competition and the number of independent sellers in a market could result in *lower prices* appears at odds with established economic practice and competition policy.

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[18] North West Shelf Project, *Submission to the ACCC in Support of an Application for Authorisation*, 5 September 1997, para. 9.8.
[19] North West Shelf Project, *Submission to the ACCC in Support of an Application for Authorisation*, 5 September 1997, para. 9.9.
[20] Draft Determination, para. 6.150.
[21] Draft Determination, para. 6.166.

81. As the Allen Consulting Group report found, authorisation for joint selling would lead to higher gas prices for Australian consumers, whereas separate selling would lead to lower prices.

82. The decision now opens the way for every major producer in Australia to combine together to form monopoly selling arrangements of gas. This will have profound implications for every industry and household in Australia – not just Western Australia.

83. The Draft Determination's findings do not reflect current market experience in WA. The absence of competition and the exercise of market power by major producers have resulted in a situation where WA consumers are being asked to pay around three times the price of new gas compared to in Victoria.

84. Far from the notional "LNG-netback" prices contemplated by the ACCC, major gas producers are now extracting a premium price return from Australian consumers – in excess of that from overseas customers.

85. Apache Energy has publicly announced: "For price, it's the domestic market, for quantity it's the LNG market."[22]

86. These public statements require detailed investigation by the ACCC. According to EnergyQuest, Australia's average LNG sales price for the last quarter was A$ 6.24 / GJ.[23] This would equate to "LNG netback" prices of around A$ 3 - $4 per gigajoule, i.e. *less than half* the prices currently being sought by major producers from Australian consumers.

87. Any assessment of competitive impacts by the ACCC cannot therefore be made in the absence of a comparison between:

- the "netback" prices being entered into by Shell, Chevron and ExxonMobil in their recently announced Gorgon LNG contracts; and
- the upwards of $8 - $8.50 / GJ domgas prices currently being sought by major producers.

88. It is vital that the Draft Determination provides a comparison of recent LNG contract prices concluded by the Gorgon participants, their "netback" equivalents and the prices currently being sought by major producers for domestic gas.

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[22] Reuters, 'Apache decision on Australian gas by October', 4 June 2009, available at: http://www.reuters.com/article/GlobalEnergy09/idUSTRE5535LZ20090604

[23] The Australian, 'Gorgon revenue doubt as LNG price slumps', 2 September 2009.

4. WA supply and demand outlook

89. The Draft Determination considers: "While the ACCC notes that the WA market is currently experiencing latent demand, there is no guarantee that this will be the case in 6 years. Several new domgas fields are expected to come into production before or after 2015."[24]

90. The ACCC appears again to accept as uncontested fact the assertions made by the Gorgon participants about an "oversupply" in the WA gas market.

91. The Draft Determination provides no analysis about expected gas demand for Western Australia to 2020.

92. Nor does it assess the level of supply that could be expected from these "several new domgas fields".

93. Claims about a potential oversupply of gas are patently false. The fact is that WA has been experiencing a serious domestic gas supply shortage since at least 2004 and will continue to do so for many years:

- A 2008 study by Economics Consulting Services concluded WA will require over 1100 TJ/day in new and replacement gas by 2014-2015.
- The WA Government's 2006 Reservation Policy Consultation Paper concluded that 2 trillion cubic feet of gas is needed from existing and proposed gas projects to meet WA's gas requirements to 2020. Of this, the Gorgon Project would need to supply 1.85 Tcf [*this assumes that almost the entire 2000 PJ Gorgon reservation volume is delivered by 2020!*]

94. It appears that producers' public claims about an "oversupply" of gas are not matched by producer assessments.

95. A presentation by BHP Billiton, a fellow participant in the North West Shelf Joint Venture, cites 2025 gas outlook projections by Core Collaborative. BHP Billiton concludes:

- "WA gas supply is currently predominantly sourced via two hubs: NWS (~ 65%) and Varanus Island (~30%)."
- *"These hubs are running at their practical capacity and the fields currently supplying them are mature and are expected to decline*."
- "Existing natural gas supply capacity is fully utilised."

[24] Draft Determination, para. 6.85.

- “Forecast growth and the decline of existing sources means that *1000 Tj/d of capacity and reserves backing must be added by 2020*.”

- “Replacement of existing supply and supply to meet forecast growth *must come from new sources*.”

- “Only one domestically focused project that will provide additional near term supply is currently under construction (late 2011 & 110 TJ/day).”

96. Thus according to BHP Billiton – Chevron and Shell’s partner in the North West Shelf Joint Venture – 1000 TJ/d of capacity and reserves backing must be added by 2020 to meet forecast growth and the decline of existing sources. This supply must come from *new sources*.

97. Prospective developments in WA are however unlikely to meet this requirement – *leaving a potential gas shortfall of around 500 TJ/d*. This shortfall is equivalent to half the size of the current WA gas market.

Prospective domestic gas projects

Project	**Gas Supply**	**Start-up**
Reindeer	Up to 120 TJ/d	From 2011
Macedon	Up to 200 TJ/d	From late 2012
Gorgon	Up to 150 TJ/d “if commercial”	From end 2015, rising to 300 TJ/d by 2021
Julimar	? - may be processed into LNG through Pluto	?
Pluto	? - 5 years after LNG “if commercial”	?
Total New Gas Needed	1000-1100 TJ/d	
Total New Gas Supply	470 TJ/d	
Potential Shortfall	**500 TJ/d**	

98. Notwithstanding this expected shortfall, the Gorgon participants have indicated they will significantly delay domestic supply and volume - until end 2015 for first gas, and 2021 for the 300 TJ/d commitment.

99. This can only reflect a deliberate strategy on their part to withhold supply from an extremely tight gas market in order to drive up prices.

100. It is disappointing that the ACCC proposes to assist this clear abuse of market power by protecting their anti-competitive cartel selling arrangements.

5. Domestic gas reservation policy

101. The Draft Determination opines that: "In the longer term, [the domestic reservation policy] may have the effect of discouraging exploration for and development of gas fields off WA."[25]

102. In repeating the same untested claims by major gas producers, the ACCC provides no supporting evidence to support its conclusion.

103. Claims by major producers that the WA reservation policy will "increase sovereign risk" and "drive away exploration and development" have proven to be empty rhetoric.

104. The gas reservation policy has not prevented Woodside from flagging the potential for an extra six LNG processing trains and 77 million tonnes of additional LNG capacity within the next 15 years.

105. Nor has it prevented Woodside from outlining plans to expand Pluto with at least two more LNG trains to increase production from 4 million tonnes per annum to 12 mtpa.

106. It is telling that in a recent speech to an APPEA conference, Woodside CEO Don Voelte highlights advantages which Australian LNG has over international competitors:

> "In addition to world class gas reserves, Australia has existing LNG infrastructure, experience in LNG production, established and diversified LNG marketing experience, political and fiscal stability and an open economy that allows private enterprise to pursue commercial LNG negotiations."[26]

107. No mention was made of the WA gas reservation policy as constituting a barrier to gas exploration or development despite Mr Voelte previously describing the State's reservation policy as "crazy".

[25] Draft Determination, para. 6.149.
[26] Woodside CEO Don Voelte, Presentation to APPEA Conference, 2 June 2009.

Table: The rhetoric vs. the reality

The Rhetoric	The Reality
"The economics of Pluto … are so fine that an LNG development would not be viable if 15 per cent of field reserves were unavailable for LNG production."[27]	Woodside flags the potential for an extra six LNG processing trains and 77 million tonnes of additional LNG capacity within the next few years.
"The Pluto project would not go ahead if the gas reservation policy was applied." [28]	Woodside outlines ambition to expand Pluto with at least two more LNG trains to increase production from 4 million tonnes per annum to 12 mtpa.
"Two companies who are considering and in fact well into the development of LNG options in Western Australia told me in the last 24 hours that those projects would not go ahead if a reservation scheme of the type being proposed was enforced on them."[29]	Exploration expenditure significantly increases from June 2006 Alcoa and ARC Energy enter an agreement to expand ARC's Canning Basin exploration program.
"Our reputation as one of the world's best LNG exporters and our ability to guarantee no sovereign risk is under real threat." [30]	"With first gas for Pluto next year as well as the Gorgon, Browse and Sunrise opportunities in the years ahead, there is no doubt the timing for Australian LNG is now." [32]
"… we think it's counter productive in the long-term and will not help to promote investments in the long-term large LNG projects." (ExxonMobil)[31]	

108. Contrary to the ACCC's opinion, exploration and development activity in WA has significantly increased *in spite of* the State's reservation policy. This is demonstrated by public data available from the Australian Bureau of Statistics.

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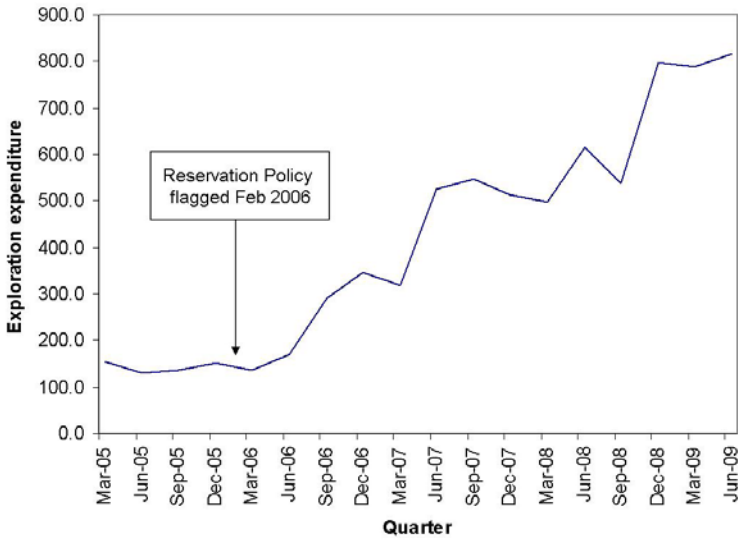
[27] The Australian, 'Woodside, WA sort out deal on Pluto', 9 October 2006, reporting comments by Woodside CEO Don Voelte.
[28] The Australian, 'Woodside, WA sort out deal on Pluto', 9 October 2006, reporting comments by Woodside CEO Don Voelte.
[29] The West Australian, 'Opponents go head-to-head in very public stoush', 1 September 2006, quoting former Federal Minister Ian Macfarlane.
[30] The West Australian, 'Opponents go head-to-head in very public stoush', 1 September 2006, quoting former Federal Minister Ian Macfarlane.
[31] ABC News Online, 'ExxonMobil complements Carpenter over gas policy handling', 12 October 2006, quoting ExxonMobil.
[32] Woodside CEO Don Voelte, Presentation to APPEA Conference, 2 June 2009.

WA petroleum exploration expenditure ($)



Source: ABS

109. In October 2009, the Federal Government awarded ten offshore exploration permits in Western Australia and the Northern Territory for new investment worth $158 million. Claims that the WA reservation policy discourages exploration stand contrary to actual facts. Of the ten offshore permits awarded, *eight relate to Western Australia*.[33]

110. As the Federal Minister for Resources and Energy comments:

“Despite the global economic downturn, the awarding of these ten new exploration permits indicates that *Australia remains a highly attractive and secure destination for offshore petroleum exploration*.”[34]

111. The WA reservation policy is consistent with policies being enacted by governments in other countries. A report by Curtin University concluded that governments around the world are acting to secure energy reserves.[35] WA’s 15 per cent policy is modest by world standards.

112. Egypt for example has a national reservation policy that reserves one-third of natural gas for exports, one-third for domestic use and one-third “to save for our children” – a 68 per cent reservation policy.

113. This reservation policy has not prevented Egypt from accounting for Apache Energy’s largest acreage position and 22 per cent of production revenue. Apache continues to have an active drilling

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[33] Minister for Resources and Energy, ‘$158 million investment in offshore exploration’, 2 October 2009.
[34] Minister for Resources and Energy, ‘$158 million investment in offshore exploration’, 2 October 2009.
[35] Leonard, Manuhutu and West, *Domestic Energy Reservation Policies: An International Comparison*, Curtin University, June 2008.

program, completing 215 of 238 wells and conducting 701 workovers and recompletions.[36]

114. A domestic reservation policy is also currently being considered by Queensland. An up to 20 per cent reservation policy has been proposed by the Queensland Government as one of two options to ensure the State's long term gas security.[37]

115. The Curtin University report also notes that over 90 per cent of world natural gas reserves are controlled by national governments and national oil companies. Only 8 per cent of world reserves are available to international oil companies like Shell, Chevron and ExxonMobil on an open access basis.

116. Western Australia with just under 2 per cent of the world's reserves therefore accounts for *a quarter of the total global opportunity* available to international oil companies on an open access basis.

117. Claims by producers that a 15 per cent reservation policy would drive away investment and discourage exploration therefore have no basis in fact.

118. It is very disappointing that the ACCC has once again shown a willingness to accept, as proven fact, assertions by major producers in the absence of any supporting evidence – indeed, in the face of actual evidence to the contrary.

6. Authorisation period

119. The proposed six year period for authorisation does not reflect the recent and ongoing development of the WA domestic gas market such as the recent and substantial changes in the role of the DGNBP in providing gas storage and load management.

120. Nor does it reflect the extensive work underway by the State Government and gas market participants on establishing a Gas Market Bulletin Board.

121. As the operation of the Varanus Island Gas Bulletin Board demonstrated, such arrangements could be successfully implemented in Western Australia and within a short period of time.

122. Any authorisation period should therefore be limited to 2 years or until the establishment of a Gas Bulletin Board or comparable arrangement – whichever is the earlier. A 6 year authorisation period is excessive and would likely be overtaken by current developments in the WA gas market.

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[36] Apache Energy website, http://www.apachecorp.com/Operations/Egypt/index.aspx.
[37] Queensland Government, *Domestic Gas Market Security of Supply*, Consultation Paper, September 2009.

7. Independent review sought

123. A decision to grant final authorisation will have profound implications for industry, small businesses and households for many years with respect to energy availability and pricing.

124. The Alliance urges that an independent panel be appointed to undertake a detailed review of the evidence presented by the applicants and interested parties, and the findings of the Allen Consulting Group report.

125. This review would assist the ACCC in making a final determination, and provide confidence to Australian consumers in the authorisation process.

List of Attachments

1. Reuters, ‘Apache decision on Australian gas by October’, 4 June 2009.

2. BHP Billiton, ‘Macedon Domestic Gas Project’ presentation, abstract.

3. The Australian, ‘Gorgon revenue doubt as LNG price slumps’, 2 September 2009.

4. Independent Market Operator, ‘Gas Bulletin Board Report’, presentation to the WA Gas Supply and Emergency Management Review.