ECONOMICS AND INDUSTRY STANDING COMMITTEE

Sixth Report — "Inquiry into Domestic Gas Prices" — Tabling

DR M.D. NAHAN (Riverton) [10.31 am]: I present for tabling the sixth report of the Economics and Industry Standing Committee entitled "Inquiry into Domestic Gas Prices".

[See paper 3232.]

Dr M.D. NAHAN: Western Australia's economic future is inexorably tied to the development and use of the state's large reserves of natural gas. Since gas first flowed from the North West Shelf project more than 25 years ago, this state has become highly reliant on the use of gas as a fuel source in industry, electricity generation and households. The overall intensity of gas use in Western Australia is double the level of other states and is higher than in the United Kingdom and in the United States. Importantly, we rely on gas to fuel more than 55 per cent of our electricity generation. Moreover, our reliance on gas will grow as we and the rest of the world attempt to limit greenhouse gas emissions. Aside from plentiful supplies of gas, gas use in this state has been encouraged by competitive domestic prices. The state's large gas reserves have also provided the basis for the development of a large and now rapidly expanding liquefied natural gas industry.

In spite of the large expansion in gas reserves, there have been reports of a growing difficulty of local consumers to obtain adequate supplies of gas and evidence of rapidly increasing prices. In response to these concerns, the Legislative Assembly, with the support of all parties, instructed the Economics and Industry Standing Committee to inquire into domestic gas prices. It was a difficult task. The committee had to undertake original research and to obtain price data. The price data available from published sources were inadequate and lumpy. Nevertheless, the committee performed its task.

The committee's general findings are that the average price of wholesale domestic gas in 2009–10 was around $3.78 a gigajoule, which represents an increase of 28 per cent over the past two years. But the average prices understate the real rapid rise in prices because average prices are held down by large low-price legacy contracts from the North West Shelf joint venture partners. Prices in new wholesale contracts are reported to range between $5.55 and $9.24 a gigajoule—that is, between 50 per cent and 250 per cent higher than the average price in recent years. More importantly, the legacy contracts are coming up for renewal and the prices and conditions of those contracts are tightening. There has been a substantial increase in the effective cost of gas overall. In terms of national and international comparisons, the committee found that prices in new wholesale domestic contracts will be at least double those in the eastern states. Prices in some domgas contracts could be as high as, or perhaps exceed, the LNG netback equivalent prices. In short, gas prices in Western Australia are now high by national and international standards, approaching, and being linked with, the prices in the high-cost Asian markets. If these price levels were to continue, it would have a profoundly negative impact on the competitiveness of the state's economy, its businesses and put huge cost pressures on households.

Aside from rising prices, the committee found that the terms and conditions of contracts are becoming less flexible resulting in a significant increase in the effective cost to gas purchasers. We heard evidence that some domestic contracts are being linked to changes in international oil prices, as are prices in LNG contracts generally. It is the committee's view that neither LNG netback prices nor world oil markets are an appropriate benchmark for prices in the Western Australian domestic gas market.

The committee found that the rising domestic gas prices emanate from a combination of, first, a lack of adequate capacity in domestic processing and transmission facilities; secondly, a sharp increase in high-value demand from the miners; and, thirdly, major deficiencies in the operation and structure of the domestic gas market. Since 1997 there has been little increase in domestic processing capacity. As demand grew, particularly since 2005, spare capacity has been eroded to a critically low level. The lack of spare capacity has resulted in an inability to meet demand and has given producers the upper hand in price setting. Since 2005, the demand for gas from the mining sector has grown sharply. Moreover, miners have had the capacity and willingness to pay top dollar. The alternative fuel for most miners is diesel, which has a gas equivalent cost of around $20 a gigajoule, thus LNG netback prices constitute a good price for the miners. Another major factor driving domgas prices higher is the dysfunctional nature of the domestic gas market. The domestic market is highly concentrated with two producers currently accounting for 97 per cent of local gas production. Indeed, one of the major flaws in the existing domestic market is the lack of gas competition. The market is also highly concentrated on the consumer side, with five consumers accounting for 90 per cent of gas use. Prices and quantities are not set in the open market, but via contracts that are generally confidential. As a result, there is little information on prices, quantity, escalation factors, future demand and contract conditions. There is no formal secondary market and no storage capacity. We received reports that at least some older contracts prohibit the on-selling of gas. The domestic market is heavily reliant on one pipeline, which has limited to no spare capacity and is regulated in a manner that imposes significant restrictions and costs on new entrants, particularly smaller users. This structure has led to an inefficient and poorly performing market.

The outlook for the domgas market, however, is not all gloom. The development of new domestic gas processing facilities at Gorgon, Macedon and Devil Creek, which are currently underway, will significantly expand the available facilities and increase the supply of domestic gas. The Department of Mines and Petroleum's 2010 gas supply and demand outlook, which was the basis for many of the concerns that led to this inquiry, was unduly pessimistic, and indeed it has been changed. Gas demand is likely to grow at a lesser rate than predicted by the DMP; moreover, the DMP's low-supply scenario that assumed North West Shelf joint venture partners would sharply reduce their gas sales to the domestic market over the next few years is unduly pessimistic. The committee received evidence that the North West Shelf partners, subject to reserves, are likely to continue to fully utilise their domgas facilities and renew their contracts. Accordingly, the committee concluded that pressure on domgas prices and supply should ease over the next few years. Nonetheless, the committee was strongly of the view that it would be short-sighted to do nothing more than to go with the flow.

The committee recommends two strategic approaches for the government. It must ensure that the domgas market is not linked, or does not become linked, to LNG netback prices or to oil markets, and it needs to improve, indeed transform, the operation of the domgas market. The committee is very supportive of the continuation of the current reservation policy and considers it an essential instrument for ensuring that an appropriate level of gas is supplied to the local market to achieve reasonable prices. Indeed, a reservation policy is vital to the de-linking of the domestic market from the high-priced premium fuel markets of Asia. The policy was formally announced in 2006 when the government of the day announced that all future LNG project proponents had to reserve up to 15 per cent of LNG production for supply to the domestic market. The policy allows for case-by-case flexibility, allowing producers to negotiate with government on the amount of gas and the manner in which it is supplied. The Liberal–National government has continued this policy. The committee supports its continuation, with some tightening and a few additions.

The committee found that, in the absence of a gas reservation policy, it was unlikely that LNG producers would develop adequate domestic gas processing facilities now and into the future. The committee found no evidence to suggest that the state's current gas reservation obligation has deterred LNG producers from pursuing development opportunities in Western Australia. That is not surprising, given the high price of gas currently obtained in the domestic market. However, the reservation policy must be implemented with care. It is a long-term policy; that is, it comes into effect long after being implemented. It is crude; it is hard to be finely determined.

One of the major findings of the committee is that the world energy market is highly uncertain. Even while the committee's study was underway, there were major transformations of the world energy market. The reservation policy is no magic wand. There are limits on the ability of state governments to enforce such policies. The LNG projects are all located in commonwealth waters. The commonwealth government has indicated its disagreement with the reservation policy and has the ability to inhibit it. In some cases LNG project proponents have avoided, and can avoid, reservation requirements—for example, by building floating platforms and building pipelines to other states and territories. The committee suggests some changes to try to ensure those projects are brought into the reservation policy. The more onerous the cost of the policy, the more likely the commonwealth is to step in or proponents try to avoid the policy. Moreover, there are limits on the ability or willingness of government to force losses on large, highly valuable LNG projects. That said, the reservation policy is essential.

The reservation policy must be implemented in a flexible and transparent manner on the basis of the best future outcomes or positions of the market. It should be based on a thorough understanding of future gas demand and supply and with due consideration of the cost impact on producers. To this end, the committee recommends the establishment of an independent gas market monitor to oversee the operation of the domestic gas market, including publishing annual assessments of the domestic gas market, identifying and addressing market inefficiencies and providing advice to the minister on prospective reservation obligations. This is a policy derived from Queensland, which had a similar issue in the growth of its gas industry.

The reservation policy needs to be supported with a raft of initiatives designed to inform decision makers and improve the function of the domestic market. To this end, the report presents a wide-ranging set of recommendations. To enhance gas-on-gas competition, the committee recommends that the government seek the elimination of joint marketing arrangements currently applied to the North West Shelf joint ventures and the Gorgon joint ventures when these are up for renewal in 2015. To facilitate the use of gas reserves for domestic purposes, the committee recommends that retention lease arrangements be tightened and the supply of gas to the domestic market be given priority when considering renewing or issuing retention leases. To expand liquidity and transparency and to create market prices, the state should follow the lead of the eastern states and develop a short-term gas trading market. To improve transparency, a gas market bulletin board that discloses current production, demand and capacity on an ongoing basis should be developed. To aid planning and transparency, a statement of gas investment opportunities along the lines of what has been in place nationally for electricity should be developed and updated on a regular basis. To aid the operation of the market, gas storage facilities should be developed. That is underway. To improve the operation of the system, pipeline regulations should be reformed to enable quicker and more open access, particularly for smaller users.

I believe it is vital that the state does not rely solely on LNG projects for domgas. The situation we witnessed in Japan over the past few weeks illustrates that things do happen. Most of the gas now comes from the North West Shelf. It is highly reliant. For security purposes, we should look to diversify our sources of gas.

One of the major lessons of the report was that unconventional gas—shale gas and coal seam methane—has transformed the gas markets of the eastern states of North America from high priced to low-priced markets—from markets with shortages to markets with surpluses. Three years ago the US was looking at becoming a massive importer of gas through LNG; now it is considering exporting it. These new unconventional gas reserves are based on new technology and are being developed and rolled out around the world. There has been, to date, limited exploration, some development and exploration for unconventional gas, particularly shale gas, in Western Australia. The indications to the committee are that we have substantial potential reserves. Much of those reserves are located close to the domestic market; that is, in the Perth Basin. In implementing policies, particularly the reservation policies, we should take into consideration the need to provide adequate market incentives for the exploration and development of these unconventional resources into the future, particularly shale gas.

In conclusion, I would like to thank my fellow committee members who have worked very constructively and collaboratively on this report, including the member for Cannington as the Deputy Chair. I thank the member for South Perth and the member for Scarborough for their contributions to not only this inquiry, but also past inquiries, noting that they will soon be leaving the committee. Of course, I also thank the member for Collie–Preston. On behalf of the committee, I would like to offer special thanks to Tim Hughes, the committee's principal research officer. Tim performed above and beyond the call of duty. This was not an easy task. I would also like to thank Mrs Kristy Bryden, the committee's research officer, for her contribution and for her self-proclaimed genius! The report would be all the poorer without the assistance of Peter Kolf. I would like to thank the Clerk and the Speaker for providing the committee with adequate funds to undertake professional consulting. This was an extremely difficult task. The data that we required, particularly on prices, was not available, and much of the work of the committee was of an original nature. Peter brought in not only the expertise, but also the diligence to obtain that data. I thank Peter for his contribution.

I urge the government to act on this important report and commend the report to the house.

The DEPUTY SPEAKER: Member, can you confirm that you have tabled the submissions to the inquiry?

Dr M.D. NAHAN: Yes, we have.

[See paper 3233.]

MR W.J. JOHNSTON (Cannington) [10.48 am]: The report of the Economics and Industry Standing Committee is a very technical report. It does not make for light reading. If there is a weakness in the report, clearly, it is that we did not go into enough detail on householders. I think this is a very good report and I want to make some remarks. I want to start by thanking the professional staff of the committee: Tim Hughes, the principal research officer, literally bled for this report; Kristy Bryden, who, as the Chair pointed out, is a genius; Peter Kolf, without whose specialist knowledge and understanding we would not have been able to complete the report; and, of course, the other MPs who make up the committee—the Chair, the member for Riverton, the member for Collie–Preston and our two retiring members, the member for Scarborough and the member for South Perth. I wish them well in their future endeavours and I look forward to seeing their replacements. I hope the replacements meet the same standards that those two members have contributed to the committee. I also thank the member for Rockingham, whose resolution led to this inquiry. I thank all the witnesses, a number of whom had to come before the committee on a number of occasions. These were very technical and complex issues.

I will start my remarks by reading a couple quotes from a different report. The Parer report from 2002 states —

> Nevertheless, Australia's eastern gas markets can still at best be described as emerging. While these recent developments are encouraging, Australia's gas markets remain immature—particularly when compared with the gas markets in the United Kingdom or United States of America. The degree of supply competition in Australia's eastern markets is still weak—particularly compared to Western Australia. This is reflected in lower gas prices in WA.

It goes on to say —

> Compared to the eastern markets, Western Australia has a more diverse gas supply, with at least seven separate joint ventures marketing gas. This has arisen due to a number of factors, including the acreage management regime used to allocate the original exploration permits and is likely to have been influenced by the focus of the North West Shelf producers on export markets.
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> Sustainable competition between a large number of producers is critical if gas consumers are to realise the full benefits of the reforms undertaken in other sectors of the gas market.

I read those two quotes to show how quickly things can change. That rosy view of the gas supply situation in 2002 has completely turned around, if it were ever true. That report failed to properly understand the effect of the legacy contracts entered into with the North West Shelf joint venture by the government of Sir Charles Court. That government took enormous risks in that legacy contract, but the benefit was that after an initial period of a very high price for gas, we went to a very low price. The unwinding of that situation is the problem for us now. The real trick is perhaps not to reduce gas prices but to prevent them from spiking greatly from this point forward. Our report offers ideas on how to unlink the domestic gas market from the LNG market and allow gas-on-gas competition.

I draw the attention of members to a chart showing the price of oil. The chart demonstrates that for much of the period of gas supply in Western Australia, the price of oil has not often gone above $20 a barrel and only occasionally spiked to $40 a barrel. The chart demonstrates that the price of oil reached $140 a barrel in 2008 and, at the end of the chart, which is the beginning of last year, it was $80 a barrel. If we allow gas prices in this state to move towards some link to oil prices, it will mean that the price of gas will not come down but will go up by 100 per cent. We cannot allow that to happen.

The committee has done some important things with this report. We have exposed the real supply situation in Western Australia, we believe we have discovered the causes of the supply situation, we believe we have discovered the real costs of purchasing gas in Western Australia, and we have made what I believe are strong recommendations to try to overcome the high costs of gas. But we have not done everything. I do not believe that we have fully examined, and I do not think we had the ability to fully examine, retail consumer issues. Given that retail consumers are a very small part of the consumption of gas in Western Australia—I understand that about four per cent of the gas supply in this state is burnt in houses—we can see that the committee was dominated by the issues of the 96 per cent of users of gas in this state. Those other gas users are very important to householders, because they include electricity generators. As one witness commented, and as noted in the report, they would not want to be competing with the resources sector for gas supply for electricity generation.

It is very important that people understand that there is no world price for gas. There is a price in Alberta, a price at Henry Hub, a European Union price and a Japan and Korea LNG price. These are all very different. The other issue that needs to be understood is that the reason gas is very, very cheap in the Middle East is that it is associated gas. In other words—I learnt this—it is cheap because the gas comes out when they are trying to get oil. They would otherwise just burn that gas. Obviously, if they can get $1 or $2 a gigajoule for the gas, that is better than burning it and not using it for anything. We also have to think about the effective giveaway price to China, which of course was a contract signed just before world oil prices started to rise. That is demonstrated in figure 20 of the report. We often read the comment that the value of gas can be doubled or tripled by using it in an ammonium nitrate plant and all those sorts of things. The highest value use of gas is to burn it in a peaking plant for electricity in Japan. People there pay the highest value for gas. I have some sympathy for the LNG exporters. They want to maximise the return for their shareholders. If selling it to the Japanese market is the way to maximise their returns, I understand their motivation, but I am a Western Australian member of Parliament and my first priority is the Western Australian community. Western Australia's energy system is totally reliant on gas. We have the largest gas intensity in electricity supply. Major employers in Western Australia such as Alcoa use gas as a critical part of their business operations. We cannot allow the Western Australian price to rise to LNG prices or to be in some way linked to oil prices, because that would not suit the Western Australian community.

In conclusion, I want to make it very clear that I reject the position of the Chamber of Commerce and Industry of Western Australia. I cannot understand why the Chamber of Commerce and Industry would put in a submission that suggests an approach that would inevitably lead to significant increases in the cost of gas and electricity in this state. It beggars belief that an organisation that is supposed to represent small businesses in this state would put in a submission that does not support a lower price for gas in this state.

My final point is that the LNG industry around the world is highly regulated by government. For example, in the United States, LNG can be exported only to the same extent that LNG is imported into the US. If a shipment of LNG arrives in the United States, an equivalent amount can be exported, but no more than that. In many places production sharing agreements are in place under which the gas is simply given to the country in which the LNG facility is set up. In Norway, Statoil, the Norwegian-owned government instrumentality that is involved in oil and gas exploration in that country, is required to be involved in all projects. Western Australia is the only place in the world that exports LNG and effectively allows free market operation by the operators of the projects. BP's Io field is an example of that. Io gas will be exported from Australia without any reservation because it will be processed on BP's behalf by the Gorgon partners. Australia is the only place that allows a free market operation for LNG. I do not have a problem with that, so long as there is gas-on-gas competition in our domestic market that leads to prices at a very reasonable level and that are not linked to either the price of oil or the most expensive gas in the world, which is LNG into north Asia.

MRS L.M. HARVEY (Scarborough — Parliamentary Secretary) [10.58 am]: It is my pleasure to speak on this report into domestic gas prices. I particularly thank the Chair, the member for Riverton, Dr Mike Nahan, and also my fellow committee members, the members for Cannington, Collie–Preston and South Perth. I also express my thanks to the committee secretariat. I endorse the comments of the members for Riverton and Cannington; Tim Hughes, Kristy Bryden, Mr Peter Kolf and Dr Loraine Abernethie worked very hard with us on this report. This inquiry has involved complicated analysis of the issues. Also, a fairly deft touch was needed with contributors to the inquiry to secure submissions and agreement to testify at hearings. Most of the witnesses' evidence was given full or partial in-camera protection due to the commercial sensitivity and confidentiality of the material. I thank the secretariat most sincerely for their professionalism, support and advice throughout this inquiry. The need for in-camera protection for witnesses is particularly acute when inquiring into a gas market as concentrated as the WA market; 97 per cent of the state's domestic gas supply comes from three joint venture projects and over 90 per cent of the demand for domestic gas is represented by five major consumers.

Our state is heavily reliant on gas for our power generation needs, as gas represents 56 per cent of our primary energy fuel source. This differentiates WA from other states and from international markets, where the reliance on gas varies by comparison to 20 per cent in Victoria, 26 per cent in the United States and reaching 40 per cent in the United Kingdom. Indeed, aside from the electricity sector, the remainder of WA's main domestic consumers are also heavily reliant on natural gas for various uses, from power generation through to manufacturing. Our 600 000 residential customers are serviced by one retailer, Alinta, and 46 per cent of these customers use gas as their main form of heating. Although our domestic residential market is a small proportion of the industry overall, it is the sector of the industry that is of the greatest concern and, I dare say, of the highest importance to those in this house. The most dominant supplier of gas to the domestic market in WA is Woodside Pty Ltd. Woodside's North West Shelf joint venture partners supply two-thirds, or 66.2 per cent, of the local market. Apache Energy Ltd operates the other two joint ventures, which supply 31.3 percent of the market. The remaining 2.5 per cent of supply comes from a range of smaller projects.

This state has built much of its economic prosperity on cheap gas-generated power. Much of this development was underpinned by low cost, take-or-pay legacy–type contracts. Some of these contracts were under review at the time that this inquiry was called. Today's environment is very different from the environment in which the contracts were first struck many years ago, back in 1977, when the offshore hydrocarbon resources were being developed by Sir Charles Court. He negotiated contracts for the state government–owned State Energy Commission of Western Australia to underwrite these developments. Over time, one could say that the state became somewhat complacent in its approach to regulating and managing its domestic gas supply, until the Varanus Island processing plant explosion in June 2008. In a state such as WA, which is so heavily reliant on its gas supply, that plant explosion caused a crisis in the industry and highlighted several weaknesses and failings, and triggered a belated but necessary focus on the domestic gas market. I base my assertion of complacency on several findings of the committee relating to the regulatory agencies involved in the industry. In trying to get a snapshot of the domestic gas industry, I found it both surprising and disturbing to discover the wild variations in available data. Indeed, many players in the industry, government and private, use different reporting frames, formulas and methodologies. Not surprisingly, this has resulted in widely varying forecasts for demand and supply, which then affects the government's ability to determine the volume of gas required for domestic consumption and to ensure we have the capacity to service it. Recommendation 4, which covers the establishment of a gas market monitor, would go some way towards facilitating market transparency and also more accurately informing government of the state of the market.

One of the committee's tasks was to compare the WA domestic gas market with the domestic gas markets of other states, such as Victoria. We quickly determined that it is not really valid to compare the markets of the east coast with our own market. Indeed, in 2002 Western Australia was held up as an example of a well-functioning and effective market. This appears to be based on the outcomes of low-cost gas in plentiful supply and more supply being proposed through legacy contracts. These legacy contracts hid a dysfunction in our market; in fact, the low-cost gas served as an inhibitor to the development of new resources and to creating the capacity required to ensure adequate continuous supplies of appropriately priced domestic gas.

There are key differences between WA and the east coast, not the least being the tyranny of distance. In the main, our gas resources are located very distant to our market and, therefore, require expensive extraction techniques and incur significant costs in transportation from producers to consumers. Along the east coast multiple gas sources and suppliers are located close to pipeline infrastructure and near to the major population centres and, therefore, consumers. The network of gas pipeline infrastructure is interconnected and well developed. The pipelines link four states and effectively allow competition between those states. Also, the weather is colder, especially in Victoria. Hence there are more residential customers using gas for longer periods of time for heating, which makes the residential market more competitive. In Victoria, a reticulated residential gas network delivers to the majority of residential consumers. In addition to this, a storage facility was developed in response to the Esso Longford explosion in 1998, which allowed another layer of competition in the market. Gas storage effectively gives consumers greater flexibility to store, sell or redraw excess gas from supply contracts.

While there are many aspects of the east coast markets that cannot be replicated in Western Australia, we can draw from their successes. For instance, we could pursue the development of official secondary trading markets. There is a possibility of developing some onshore unconventional gas deposits to encourage gas-on-gas competition amongst our suppliers. We can also develop storage facilities. Other issues with the WA domestic gas market can be addressed through other mechanisms. One of these is the domestic gas reservation policy. Although industry has objected to the imposition of the requirement to supply gas to the domestic market, finding 20 in the report is that it is unlikely that any LNG producers would develop adequate domestic gas processing facilities without this policy in place. The tests of commercial viability need to be clarified and assessed independently. It seems that similar rigour should also be applied to the renewal of retention leases.

I feel that I must address some of the lost opportunities along the way. I think it is most unfortunate that the state lost the Inpex Corporation development to Darwin. The company employs 300 people in Perth and is estimated to have spent $900 million to date in WA. I refer to my earlier assertions regarding the complacency of the government, which was likely linked to the flourishing economic environment at the time of the development of the Inpex project. After taking evidence in this inquiry, I can only lament the loss of a significant domestic gas supply opportunity should the government of the day have found a place somewhere in WA for the processing facility required to bring the gas onshore. Inpex said that it was prepared to meet the 15 per cent domestic gas reservation policy from its 12 trillion cubic feet field. Further to this, figure 12 of the report shows that while capacity had outstripped demand until about 2003, capacity constraints were becoming apparent at that time. If the state had successfully bedded down the Inpex project, it is quite likely that, with the implementation of the domestic gas reservation policy, our gas supply needs would have been well and truly met into the future. There is no point lamenting this loss, but I draw members' attention to it to highlight the danger of complacency.

In light of recent world events such as the tragic disaster in Japan, the turmoil in the Middle East and the oil spill off the Florida coastline last year, we can be sure that there will be further demand-driven cost pressures on our domestic gas supply as other countries start to look toward gas for their power generation requirements. In this context, we need to ensure energy security by developing other sources of gas and storage facilities. I hope that the government will give due regard to the findings and implement the recommendations of the report. While the report does not offer much in the way of immediate relief for residential consumers who are coming to grips with increases in the price of gas, it does offer recommendations that will help to better manage fluctuations in domestic gas pricing in the long term.

The recommendations of this report, if implemented, will address the gaps in data, which have led to a lack of transparency in the domestic gas market. I urge the government to take on recommendation 13 regarding working with the federal government toward the elimination of the joint marketing authority currently enjoyed by the North West Shelf and Gorgon joint ventures. The application for renewal is a few short years away and we cannot afford to be complacent.

In closing, I urge the government to continue with the very successful hardship utility grant scheme, which has provided relief to those vulnerable consumers who have had relatively rapid rises in electricity and gas prices. The WA domestic gas industry is a complicated space; this report serves to explain why we are where we are with gas pricing in this state.

I commend this report to the house.

MR J.E. McGRATH (South Perth) [11.08 am]: Similar to previous speakers, it gives me great pleasure, as a member of the Economics and Industry Standing Committee, to make a contribution to the debate on the report titled "Inquiry into Domestic Gas Prices". I have to say at the outset that most Western Australians are concerned about the upward trend in gas prices in recent years. Even the Premier has conceded to having concerns about the domestic gas market. In a speech to the James A. Baker III Institute for Public Policy in Houston in April 2010, the Premier described the policy as a bit of a "'jigsaw' in ensuring that gas is available for Western Australia at a competitive price".

This committee report that has been tabled today records that the Premier has even suggested that the price of domestic gas should be the cost of the gas as it enters the liquefied natural gas processing plant, plus a fair profit margin. However, the Premier also observed that domestic gas prices were 30 per cent to 50 per cent above today's world price. That observation was made last year. Although conceding that there were some mitigating factors, the Premier added that that could not persist for the long term. I believe those were comments of a Premier who is genuinely concerned about the upward trend in domestic gas prices, as we as Western Australians are concerned. As a result of those concerns, this house voted to refer a task to the Economics and Industry Standing Committee; namely, to look into domestic gas prices in Western Australia. From the outset, this inquiry has been a most interesting and challenging exercise. As other members have alluded to, the structure of long-term gas contracts between producers and buyers is highly complex.

At this point, I acknowledge the input of our committee chair, the member for Riverton, who has a very sound knowledge of the industry. In fact, he is one of the few people I know who gets quite excited at the mention of the word gas! I also pay tribute to the members for Cannington, Scarborough and Collie–Preston. I acknowledge the work of the principal research officer, Tim Hughes, and research officer Kristy Bryden, and also for a brief period at the start of the inquiry, Dr Loraine Abernethie. It has been mentioned before that the committee would not have been able to achieve the result it did in handing down the report if not for the contribution of specialist research officer Peter Kolf. His industry expertise was invaluable in putting together this report.

What did the committee find? It found that the price of domestic gas has gone up quite considerably. Finding 17 reads —

> It is now highly likely that the recent rise in local gas prices has created an environment where—for certain contracts—domestic prices will trade at or above LNG netback equivalent levels.

That is a real concern for the domestic market. The committee also found that the price of new domgas contracts in WA is at least double those in the eastern states. During the inquiry, the point was made that when comparing Western Australia to Victoria, at times the price of domestic gas in Western Australia has been three times that of the price in Victoria. As other committee members have said, it is difficult to compare apples with apples. Victoria does not have an LNG industry. It is a much smaller state in geographical size, the gas fields are relatively close by, there is plenty of pipeline accessibility, there is also strong competition in the gas market, and many more households use gas in Victoria—something like 800 000.

Some sectors of the WA domgas industry believe that the price rises experienced in Western Australia in the last few years are due to a marketing cartel among the major offshore gas producers. Although the committee does not discount this belief, it finds that such concentration raises legitimate concerns about the level of competition and the effectiveness of this market. However, the committee also believes other factors are involved; for instance, there is no doubt that the huge demand placed on the supply of domestic gas by the big iron ore operators is pushing up the price. New pressures could also be on the gas supply horizon. The terrible tsunami in Japan knocked out many power generators such that Japan's need for our LNG is likely to go through the roof. I am sure that this will place even greater pressure on our gas supplies until new projects such as Gorgon, Macedon and Devil Creek come on stream. This is another reason for people to be grateful that the government introduced the domestic gas reservation policy in 2006. As other members have mentioned, there was some opposition at the time—certainly at a federal level. The reservation policy requires new producers to retain 15 per cent of gas for the local market. The committee believes—the chair made this point earlier—that this is an essential policy instrument for ensuring that an appropriate level of gas is supplied to the local market to achieve reasonable price outcomes. Until a few years ago, there had been no problems with gas. It was plentiful and was being provided at a relatively cheap rate to the domestic market under the legacy contracts that have already been spoken about. What has happened? Those legacy contracts have begun to expire. New contracts have been drawn up. The committee heard that in some cases countries such as Japan and China were getting Western Australian–supplied LNG gas cheaper than that provided to domestic customers. That is what has caused Western Australians most concern—and rightfully so.

What can be done? The committee has looked at the overall gas marketing picture and concluded that LNG and domgas need, in the words of the chairman, to be de-linked. How do we do that? I do not know. In a perfect world, if there were sufficient supply of unconventional gas in onshore basins to supply the domestic market at a price acceptable to both the producer and the buyer, all the offshore gas could be exported as LNG, thereby providing an even bigger boost to our economy. We are told that there is plenty of unconventional gas out there, but I do not think that this will happen in the short term.

Therefore, the committee has made a number of recommendations to government that it believes will improve liquidity, transparency and competition in the WA domgas market. Central to those is a recommendation that the government establish an independent gas market monitor to oversee the operation of the local wholesale gas market. I believe that this position will have a key role in monitoring the reservation policy. It would be modelled on that of the Queensland Gas Commissioner who, with that state now going into the business of exporting LNG, plays an instrumental role in making sure that the demands of the local market are met.

In closing, the committee found that this is a real challenge for the government. I believe that the committee's recommendations are very sound. Hopefully, the respective ministers will take a very good look at those recommendations. Some meaningful change in the competitiveness, transparency and liquidity of the domestic gas market is needed because much of Western Australian industry relies on gas, as does the growth of our state. The growth of cities in the north west will rely on the supply of reasonably priced gas. Domestic gas customers throughout the state will rely on the product that most Western Australians assume is a Western Australian–owned asset being reasonably priced. I do not think that consumers from outside Australia can get our gas at a cheaper price than can Western Australian consumers.

MR M.P. MURRAY (Collie–Preston) [11.17 am]: I, too, rise in support of the Economics and Industry Standing Committee report into domestic gas prices. First, I wish to thank the staff Tim Hughes and Kristy Bryden—who promoted herself quite well in the bottom of the draft document!—and Loraine Abernethie, who worked with the committee at the start of the inquiry, and special research officer Mr Peter Kolf. Their work was excellent and much appreciated by all.

I wish to make special mention of my committee colleagues, and especially the member for Riverton, the chair of the committee, and the member for Cannington, the deputy chair, who got stuck into this inquiry boots and all and up to their necks. Due diligence can sometimes go missing when the pressure is on, and I wish to offer a quick apology for the meetings that I missed due to travel time between the city and my electorate. I appreciate their help and that of the members for Scarborough and South Perth. I believe the committee has produced a fair and very well researched report.

Although the domestic reservation policy was a strong topic in the report, it was disappointing to learn that some companies work hard, in my view, to dodge the 15 per cent required by the domestic reservation policy. The chair of the committee mentioned that some of these companies have worked the system or, I believe, used the system to pressure the government to allow them to have their own way by saying that they will not bring the gas onshore, but will take it directly onboard ships or pipe it to another state. That goes against the business ethics of the Western Australian gas industry. That issue needs to be addressed very quickly by both the state and commonwealth governments. It is essential that we look at how we reserve some of our gas. It is no good saying that because it is outside the dotted line, we do not have a say. That issue is very important. It is one of the major issues that should be addressed almost immediately.

As other members have said, the report also touches on price comparisons with other states and countries. These comparisons are always very difficult and dangerous to try to line up, because there are many different aspects in our state and historical reasons for the variations. Oilfields produce gas as a by-product, and it is then shipped to shore for a lower price because a return can be made instead of it just flaring off. In our case, issues such as distance, infrastructure, population, the onset of new industries and no major manufacturing industries have an impact on competition, the way our system works and the way that gas is brought down through a very vulnerable one-pipeline system. It is easy to say that the price of gas on the east coast is half the price of gas on the west coast, but it is certainly not that simple.

Another thing that will probably disappoint a few people on the domestic gas front is that I am not talking about household gas prices. We have to get the structure right before the price is reflected in the price for householders. We have made the recommendation that we need to get the structure right to encourage competition, which will then start to put pressure on the domestic market—that is, for households. I think the word "domestic" has possibly caused some problems because people thought we were talking about the price for households, but the word "domestic" was used in reference to Western Australia.

The inquiry's main focus was on access to the gas reservation policy, competition, accessibility and pricing transparency, which, again, is a market driver. It is hoped that by addressing these issues, a transparent price system will encourage competition, which will then allow the price of onshore gas to come down. In some cases, the current system is a winner-takes-all system. I went to China with Clive Brown when he was Minister for State Development. The pressure that China put on to get the lowest price in the early contracts was extraordinary. I can recall arguing over 0.4 of a cent at four o'clock in the morning. The federal government was trying to help out. That was in the early days, when China got really low prices because we were trying to build an industry. It was very important to have those prices so that we could start the industry off. Nowadays, people say that that was a bit of a stupid price. But history indicates that it was a major starting point with one of our biggest customers. I am sure that the Chinese think that they did a pretty good job themselves to get the lowest price. That has also happened with Burrup Fertilisers Pty Ltd. Again, we needed people to get the industry started. These people were on the front foot and were able to get very low prices. We know that some of those contracts are running out. When I say "domestic", I mean our local generation areas. We will find in the next round that the prices will go up again and will certainly impact on the price of electricity.

I was also disappointed in the speeches of my colleagues when they did not refer to the competition between external energy providers such as coal-fired energy providers. I have raised this issue many times. How could I have missed that? I do not think I could have. But there is a relationship between gas and coal prices; it is not only oil. There is competition in the market. Some of the prices are confidential, but we do know that the price of coal is far lower than the price of gas. We need external energy providers, such as wind power and renewable energy providers, so that we have a mix and match in the energy market in Western Australia. We need our electricity market. Although I spoke tongue in cheek a little earlier about the price of coal, it is of concern that we have only one gas pipeline from the north west to the south west. We saw what happened when there was a problem on Varanus Island. There have also been cyclones recently. We saw what happened in the Gulf of Mexico when those oil wells broke down. We need more than one source of energy. I am concerned that some of the focus has been only on gas. The production rate of electricity has turned around from about 50–50 when I came to Parliament to about 35 per cent now from coal. We have seen the market become distorted. We must take into account all factors in the energy market; otherwise, we could be in a lot of trouble further down the road. I am sure that my constituents would have been very disappointed if I had not raised that issue.

We need across-government agreement. Politics played a role when the 15 per cent gas reservation policy was brought to this house in earlier times. I believe it was only role playing. I think we have gone past that now. We must secure our future, and we must secure it at a reasonable price. It is no good saying that we have reserved 15 per cent if the price is too high. The focus of our inquiry was to ensure that we have competition and that we have an onshore gas market. It does not all have to be offshore. We must develop and work on that market. It does not really matter whether it is through conventional or non-conventional ways; we must secure our gas supply. With everything that is happening in the world, whether it be cyclones or wars, we must secure our energy supplies. We must make sure that we are looked after as well as anyone else in the world. With those comments, I again thank the staff of the committee and commend the report to the house.

MR M. McGOWAN (Rockingham) [11.27 am]: Under standing order 279, I seek leave, as the mover of the original motion, to make a few brief remarks on this report.

Leave granted.

Mr M. McGOWAN: I have had a look at the report and I have listened to the speeches of members of the Economics and Industry Standing Committee. I acknowledge the committee and thank members for their work, particularly the chair of the committee, the member for Riverton. All committee members made good contributions. I can tell that they have done a lot of work in getting this report to this stage. It is a substantial piece of work. Some of the financial analysis involved would have been difficult to put together, so I thank all members of the committee for that work.

I think that a number of members were trying to say that we are Western Australian members of Parliament. In a perfect world—perhaps as an executive or a shareholder of a major company—our main focus would be on the maximum price that could be achieved. If the maximum price could be achieved by sending it to a peaking power station—someone said in Japan—that would be our view. But our view is much broader than that. Our view is much broader than that of an executive of a company. Our view concerns what is best for Western Australia. Gas is essential to our state's industry. It is essential to lots of businesses in this state and to people who work in this state, so we have to take the broader view of what we can do to make sure that the people in those industries have jobs in the future and that those companies are not priced out of business because of energy prices. We also have to take the view of householders who use the gas. As small a component as that might be, the reticulated gas supply to people's kitchens and hot-water systems should be a major concern for every one of us in this place. The price that ordinary mums and dads pay for gas should be our major concern. I am pleased to see that the members of the Economics and Industry Standing Committee have taken the view that we are Western Australians first.

The "Inquiry into Domestic Gas Prices" report will be closely examined by a lot of people. I have spoken to some corporate people who have been following this committee with great trepidation. I do not believe that they have a great deal to worry about what is contained in the report; it seems to be eminently reasonable and sensible. The reservation policy was a good policy and Alan Carpenter deserves credit for it. In 2006 he brought that in in the teeth of great opposition by some elements in the industry and also the then federal Minister for Industry, Tourism and Resources, Ian Macfarlane, who publicly attacked the then Premier at a forum on this issue that was held in Western Australia. As with a lot of controversial policies, over time they are accepted and people wonder why it was even a debatable issue. It is a good policy that is now in place. What is lacking in that policy is a way of making sure that the 15 per cent reserve for the domestic gas supply is competitively priced and is priced differently from the gas that is sold overseas. I will say a few things about that. The member for

Riverton talked about the establishment of offshore floating liquefied natural gas facilities. As a state we need to fight those for all they are worth because they are located in federal waters that are outside our control. We need to tell the commonwealth government that we do not support floating offshore facilities. We need to let the federal government know that neither side of politics wants to see facilities to exploit our gas resources established off the coast of Western Australia. We want the gas brought onshore.

The joint marketing arrangements have been an issue of contention for some time. I believe that the Australian Competition and Consumer Commission made a mistake. We should support greater competition. The ACCC said that the supply would dry up. We know that the supply will not dry up because of the reservation policy. We need to support competition in the provision of gas that comes down the pipeline. Again, we need to tell the ACCC on a bipartisan basis that the state supports competition. Recommendation 4 is about the establishment of a gas monitor. I am unsure what power the gas monitor will have. Obviously, that is a transparency mechanism, which is good. I do not believe that we need to take a heavy-handed approach initially. However, that will take a long time to establish. Perhaps sooner rather than later we need to look at putting in place a mechanism that expands the powers of the Economic Regulation Authority, or something of that nature. If it is likely to take another two or three years to establish that, perhaps we will need to consider using a different body so that it can be done more quickly. Recommendations 14 and 15 concern the short-term market and bulletin board. I understand they have been on the drawing board for a long time—ever since Varanus. Obviously that has not happened. The gas market bulletin board and short-term trading market should have happened by now. I do not know why the people responsible for that have been so slow to put it into practice. That should be in place in Western Australia today.

They appear to be the key recommendations. We cannot allow more time to pass while the long-term contracts ensure that the people from overseas who purchase our gas are purchasing it a great deal more cheaply than are domestic customers. We need to ensure that the price of gas in Western Australia is affordable for Western Australian industry and for mums and dads. The recommendations in this report need to be either implemented or put into an alternative mode of operation as soon as possible.