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Gas Tariffs Review
Office of Energy
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Via email: energymarkets@energy.wa.gov.au

Gas Tariffs Review - Draft Recommendations Report

The Energy Supply Association of Australia (esaa) welcomes the opportunity to comment on the Office of Energy's Draft Recommendations Report for the Gas Tariffs review.

esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of over 40 electricity and downstream natural gas businesses. These businesses own and operate more than \$120 billion in assets, employ 52,000 people and contribute \$16 billion directly to the nation's Gross Domestic Product.

esaa supports the development of open, competitive energy markets free from distortions such as retail price regulation. However, the Association acknowledges that rigidities in wholesale markets can hinder progress towards a fully competitive retail market. Current characteristics of the Western Australian gas wholesale market include:

- Limited sources of supply, in particular significant volumes of domestic gas are dependent on production fields in the North-West Shelf.
- Limited options for the transportation of gas from the main sources of supply, with reliance on the Dampier-Bunbury pipeline to convey gas from the North-West Shelf.
- Reliance on long-term contracts, leading to a lack of price transparency and less flexibility to adjust volumes compared to a situation where there is a spot market on which additional volumes may be bought or sold.
- Reported increases in the price of long-term gas contracts, which could deter entry into the retail market where incumbents are still benefiting from lower prices agreed in previous years.

The Western Australian Government's Strategic Energy Initiative is considering many of these issues. In the longer-term, a secure, reliable and competitive supply of gas

to Western Australia's domestic market would be best promoted through the development and introduction of policies that are targeted at market failures that have contributed to the state's domestic gas shortage and enable competitive market outcomes to prevail.

However, in the short-medium term, there are a range of other measures the Western Australian Government should consider including promoting use-it-or-lose-it contestability in tenured gas resources; implementing a Gas Statement of Opportunities and Gas Bulletin Board; considering the relative costs and benefits of providing a facilitated trading platform for gas and transportation through the Gas Bulletin Board in the short term and through a Short Term Trading Market in the medium term; considering options to promote greater investment in gas transportation; and considering options to promote greater commercial investment in gas storage, along with opportunities to encourage trading of gas storage.

If these reforms are effective in promoting competition in Western Australia's wholesale gas market and allow the unconstrained entry of new energy businesses into the retail gas market it would be expected that requisite market conditions for removing regulated tariffs will prevail.

However, the current process of gas tariff regulation has meant that, while tariffs are adjusted annually by the CPI to ensure real dollar equivalence, increasing energy costs have allowed prices to fall below the costs of supply. This has meant that while competition for small-use customers is possible, there has been no commercial incentive for energy companies to enter the market for small-use customers. Energy prices that do not reflect the cost of resources impede the efficient operation of the market. They create financial pressure for industry participants forced to absorb costs that cannot be passed on. In addition, regulating prices in potentially competitive markets can be self-fulfilling. The 2007 Gas Tariff Regulations Review, also conducted by the Office of Energy, acknowledged that regulated tariffs were likely to be set below efficient costs thereby removing any incentive for energy companies to enter the market and compete for small-use customers.

Suppression of regulated tariffs below cost was observed in the 2008 and 2009 regulated gas tariff increases. Acknowledged failings in gas tariffs regulation have inhibited competition between energy companies, which will continue to provide government with an excuse to maintain inefficient regulation.

esaa considers that the Western Australian Government should remove gas retail price regulation, noting that reforms in the wholesale market are also required. There is no presumption in many east coast jurisdictions that gas retail price regulation is a necessary customer protection (ACT, Victoria, Queensland and Tasmania do not regulate retail prices for households). However, should the Western Australian Government decide to persist with gas retail price regulation then regulated gas tariffs must be set at cost reflective levels (including an appropriate retail margin) by an independent body, such as the Economic Regulation Authority, through a formal, transparent, predictable and consultative process. Either annual or multi-year price reviews are required that allow for adjustment for uncontrollable costs to be passed through (for example transportation costs). In addition, regulated gas tariffs should,

where possible, be harmonised with and reflect decisions on network charges faced by retailers.

However, to ensure that retail price regulation doesn't continue to hamper the development of a competitive retail market, the need for retail price regulation should be reviewed by an independent authority, such as the Australian Energy Market Commission, at a specified date. To this end, the Association considers that a specific methodology should not be prescribed for the period post 2016. Instead, as that date approaches, the AEMC should consult with stakeholders to determine whether there is any justification for regulating retail prices and, if so, what the best methodology may be in light of the prevailing circumstances.

If you require any further information in regard to this submission please contact Kieran Donoghue, kieran.donoghue@esaa.com.au or 03 9670 0188.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Brad Page', with a stylized flourish at the end.

Brad Page
Chief Executive Officer