Options to improve gas pipeline regulation

COAG Energy Council – consultation RIS

SHELL AUSTRALIA RESPONSE

17 January 2020

Shell is a global group of energy companies, with its headquarters in The Hague, the Netherlands. Shell operates in over 70 countries around the world and has been investing in Australia since 1901. Australia continues to be a priority market for Shell's investment as Australia trends towards greater electrification in line with consumer needs for a lower-emissions energy system.

On the east-coast, Shell has a majority interest in and operates the QGC-LNG project in Queensland. Through this project we have a strong presence in the east-coast gas market, supplying both domestic and LNG customers. The energy trading venture – Shell Energy Australia – has expanded our gas trading portfolio into the southern domestic gas market, introducing competition. We also operate the 144MW Condamine Power Station in the National Electricity Market (NEM). The recent acquisition of ERM as a wholly-owned subsidiary of Shell Energy Australia, further unlocks growth opportunities to support the NEM as it transitions to more renewable flexible generation and storage.

Long-term success of both the Australian economy and companies such as ours will be highly dependent on our ability to anticipate the types of energy and technology needed to support a reliable, flexible and cost-effective electricity grid. As investment in renewable generation continues to grow, natural gas will have an important role as a fuel source for gas-fired generators to provide firming and security services to the grid. A stable, efficient and effective pipeline regulatory framework is therefore critical to support the energy market transition in the long-term interests of consumers.

Shell Australia welcomes the opportunity to provide a submission to the COAG Energy Council's consultation regulation impact statement on options to improve gas pipeline regulation (RIS).

GENERAL COMMENTS

Shell Australia supports the purpose of the RIS 'to identify and evaluate options to deliver a more efficient, effective and well-integrated regulatory framework for gas pipelines'.[1] A clear and stable pipeline regulatory framework is needed to support a liquid gas market, a transitioning energy market and deliver benefits for consumers. We consider the recent pipeline reform processes (i.e. arbitration, information disclosure, day-ahead auction and short-term capacity trading) have gone some way in ensuring the development of a more liquid east-coast domestic gas market.

We believe the market is still adapting to the recent reforms and time is required to determine how effective these reforms have been in supporting competitive outcomes. Also, given the recent significant level of reform in this area, Shell Australia does not view changes such as those proposed in the RIS as a regulatory priority.

[1] http://www.coagenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/EC%20-%20Gas%20Pipeline%20RIS%20Terms%20of%20Reference%20-%2020181221.pdf

As such, Shell Australia recommends that any further changes to the pipeline regulatory framework be put on hold until sufficient time has been given to determine the effectiveness of the recent pipeline reforms.

Specifically (i) whether these prior reforms are sufficient in addressing the underlying concerns driving this review (i.e. those identified by the Australian Energy Market Commission (AEMC) and by some industry players (including Shell Australia) over recent times) and (ii) enable industry the time to properly consider whether a complex proposal to regulate pipelines is in the overall interest of the market and the appropriate policy response.

Furthermore, Shell Australia encourages the COAG Energy Council to consider a broader package of measures to support efficient regulation of gas pipelines. We consider this would better achieve the National Gas Objective and the COAG Energy Council's Vision for the Australian Gas Market.

PROPOSED POLICY OPTIONS

Shell Australia agrees that there is still more to be done to ensure an effective and efficient pipeline regulatory framework. However, Shell Australia does not consider that the perceived problems around when a pipeline should be regulated, how it should be regulated, information disclosure and dispute process, are material issues for the industry at this stage. In addition, Shell Australia has not used Part 23 to date and is unable to comment on its effectiveness as part of this consultation.

While, we acknowledge the potential for pipeliners to exercise market power, we do not necessarily agree that the proposed options will address this or promote increased competition. Rather, Shell Australia is concerned that the options, as proposed, are overly complexed and unnecessarily confusing for market participants. It is also not clear how the options would work in practice and as a result could lead to unintended consequences. In 2016, Dr Michael Vertigan examined the coverage test.[2] Shell Australia considers the findings are still relevant and encourages the COAG Energy Council to give more weighting to the report.

There are more prominent issues that the COAG Energy Council should focus on to deliver its Gas Market Vision – including actual pipeliner behaviour. We have seen market behaviour that restricts shipper's ability to gain access on reasonable terms. Regulatory solutions or changes to the coverage test is unlikely to provide the right incentive for pipeliners to change this behaviour. Shell Australia considers a holistic discussion of pipeline regulation would be more prudent at this time to deliver a more efficient and effective regulatory framework which benefits consumers and supports the energy market transition.

HOLISTIC APPROACH IS REQUIRED

Shell Australia recommends that a holistic discussion on a package of reforms is initiated, with industry input, to ensure the optimal and efficient movement of supply at a price which reflects a competitive market. While economic pipeline regulation is a feature of other mature gas markets in which Shell operates globally, most of these markets have introduced a package of measures that work together (e.g. capacity expansion obligations,

[2] http://www.coagenergycouncil.gov.au/sites/prod.energycouncil/files/publications/documents/Examination%20of%20the%20current%20test%20for%20the%20regulation%20of%20gas%20pipelines%20-%20Final%20Report.pdf

national expansion planning). Implementing the proposed options outlined in the RIS without consideration of these other aspects, in our view would still leave gaps (when compared internationally).

Equal consideration should be given to the following.

1. **Long-term pipeline development plan**: There is no long-term infrastructure planning for gas in Australia as there is for electricity. This is a feature in overseas gas markets and supports the timely investment in infrastructure that links major demand and supply centres. Furthermore, investment in gas infrastructure will be needed to support the NEM as it transitions. Shell Australia considers this is a key piece missing in Australia's east-coast gas market. While the Gas Statement of Opportunities provides an annual supply demand forecast, this doesn't necessarily translate into identified needs for future pipeline investment to support a transitioning energy market. Shell Australia recommends the COAG Energy Council task AEMO, working with market participants, to scope out the elements of an annual report.
2. **Long-term capacity by existing shippers**: There is no direct incentive/requirement/mechanism for shippers to offer unused long-term contracted capacity back to the market which would be beneficial to the market. COAG Energy Council should investigate requirements that if capacity is unused over a specified period, it must be surrendered back to the pipeline for release by the pipeline as part of a long-term capacity release program.
3. **Incentive based economic regulatory framework**: Currently there is a lack of willingness of pipeliners to expose themselves to market risk and offer risk-based transportation products, even where a pipeline has been fully depreciated. COAG Energy Council should investigate a semi-regulatory framework that offers pipeliners incentives (and/or) penalties to take on more market risk and offer more risk-based products to shippers.
4. **Effectiveness and quality of current information provisions:** Making information provision data more easily digestible and less resource intensive for shippers to interpret would make Part 23 more effective. Given the AER's experience in network regulation there potentially is a role for the AER to publish the information in a more useful manner.
5. **Market power review:** To occur 2 years post the commencement of capacity trading as sufficient time would have passed to determine the effectiveness of these reforms. A terms of reference should be developed with industry consultation and published in advance as a signal to the market. The review should consider: Rate of Return comparison (pipelines vs other regulated sectors and the rest of the market); breath of product offering; price comparison to overseas pipelines; future areas for further competition. This review would then inform whether changes to the regulatory framework (full/partial) and coverage test is warranted. In the interim, the ACCC should monitor pipeliner behaviour as part of its ongoing gas Inquiry.

Shell Australia welcomes the opportunity for further discussion on pipeline regulatory reform.

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