

The Australian Government tightens control on the east coast gas market

The Government has announced a number of measures which are likely to have significant ramifications for participants in the east coast gas market. On 19 April 2017 the Treasurer directed the Australian Competition and Consumer Commission ("ACCC") to hold a new inquiry ("2017 Inquiry") to improve transparency and monitor gas supply in Australia. On 27 April 2017 the Government announced that it would introduce a new Australian Domestic Gas Security Mechanism ("ADGSM") that would give the Government the power to impose export controls on companies when there was a shortfall of gas supply in the domestic market. These measures may result in a period of uncertainty for participants in the east coast gas market, particularly those who are heavily reliant on export activities as part of their business operations.

Engaging the ACCC's help once again

2017 Inquiry

Following the ACCC's east coast gas market inquiry in 2015 ("2015 Inquiry") the Treasurer has engaged the ACCC's help once again and directed it to hold a new 2017 Inquiry into domestic gas supply.

The 2017 Inquiry is designed to inform the Government's implementation of the ADGMS going forward as well as report on particular features of the industry and possible ways of addressing the anticipated east coast gas supply crisis.

In particular, the 2017 Inquiry will look to:

- develop measures to improve the transparency of gas supply arrangements in Australia;
- examine components of the gas supply chain other than the production of gas, including the storage, transportation and processing of gas, to ensure that actions taken by industry players are not adversely affecting domestic supply; and
- identify impediments to efficient supply, and where the use of market power may exist, propose solutions to address any issues found.

The 2017 Inquiry commenced on 19 April 2017.

Parameters of the 2017 Inquiry

Compared to ACCC's 2015 Inquiry which was completed over a period of

Key issues

- The ACCC has been directed to use its inquiry powers to monitor and scrutinise conduct across the entire domestic gas supply chain over the next 3 years.
- The ADGSM is expected to come into effect from 1 July 2017 giving the Minister for Resources the power to impose export controls on companies when there is a shortfall of gas in the domestic market.
- Sellers and buyers should review their sale and purchase agreements to determine the potential consequences of these new measures.

one year and focused on the competitiveness of wholesale gas prices and the potential misuse of market power in particular segments of the industry such as the pipeline sector, the 2017 Inquiry will focus on the availability and terms of domestic gas supply, building on the ACCC's previous findings.

Matters to be monitored and taken into consideration in the 2017 Inquiry include:

- the pricing and availability of offers to supply gas;
- the volumes of gas supplied or available for current or future supply including natural gas extracted or produced in Australia or imported into Australia;
- the pricing, volume and availability of gas for domestic supply compared to the pricing, volume and availability of gas for export; and
- the pricing, volume and availability of other goods or services, such as goods or services for drilling for, storing or processing gas, that enable, assist or facilitate the supply of gas or gas transportation services in Australia.

The ACCC's role of monitoring and scrutinising conduct across the gas supply chain over the next three years may help the Government hold gas suppliers to account with respect to their commitments to make more gas available to the domestic market and LNG exporters with respect to their commitment to be net domestic gas contributors and will likely be used by the Government to facilitate its powers under the proposed ADGSM (described below).

According to the Treasurer, the ACCC will also work with industry experts and relevant agencies to refine longer term transparency measures which will cover the full gas supply chain.

Investigative powers of the ACCC

The 2017 Inquiry will be undertaken using the ACCC's investigative powers under Part VIIA of the *Competition and Consumer Act 2010* (Cth).

The ACCC will be able to demand the disclosure of information in a number of ways including by:

- summoning witnesses to answer questions before the ACCC; and
- issuing s95ZK notices to compel the production of documents and information.

For further details on the 2015 Inquiry please refer to our briefing which summarises the ACCC's key findings – [click here](#).

ACCC reporting

The ACCC will be required to submit interim reports to the Treasurer no less frequently than every 6 months and provide information to the market "as appropriate".

The 2017 Inquiry is to be completed and a final report submitted to the Treasurer by 30 April 2020.

Gas for the domestic market through export controls

ADGSM

The Government introduced the ADGSM on 27 April 2017, the operation of which will in part rely on the ACCC advising the Government on whether there is likely to be a domestic gas shortage or a distortion of domestic gas prices due to a shortfall in supply pursuant to its 2017 Inquiry remit.

The ADGSM is intended to give the Minister for Resources, in consultation with relevant ministers, the power to impose export controls based on advice from the ACCC and the Australian Energy Market Operator.

If an exporter draws more from the domestic gas market than they put in, they will be required to explain how they will fill the shortfall of domestic gas as part of their overall production and exports. The Government intends to give exporters the flexibility to determine how they may fill the shortfall of domestic gas that has been identified including by selling gas on the spot market such as the Wullumbilla Hub.

LNG exporters who are drawing from the domestic gas market may be ordered to limit exports of LNG to ensure there is sufficient gas available for domestic supply.

If an exporter does not draw more from the domestic gas market than they put in, they will be licensed to export according to their production forecasts.

Potential ramifications

These export controls are likely to have significant ramifications for the east coast gas market including on existing (and often long term) commitments to buy and sell gas and LNG.

Depending on the manner in which the ADGSM is rolled out by the Government (the details of which are not yet available) sellers and buyers may need to revisit the terms of their existing gas and LNG sales and purchase agreements in the context of (amongst other things) their take or pay obligations and entitlements to claim relief as a result of force majeure and change of law.

By way of example, sellers may seek to pass on these risks to buyers by claiming that the ADGSM is a relief event under the sale and purchase agreement which relieves the seller from its supply obligations or requires the parties to renegotiate the terms of the sale and purchase agreement. Buyers may wish to be prepared for these discussions and have an internal position settled on their response ahead of the proposed commencement of these new regulations (see below).

Key dates to be aware of

The new regulations that will give effect to the ADGSM are due to be released by the Government in June and take effect by 1 July 2017.

Industry Reactions

Caution against overregulation

There have been repeated calls by various industry participants for Australian States such as Victoria, Tasmania and the Northern Territory

to lift their moratoria on gas development, in line with the ACCC's recommendation in the 2015 Inquiry that Australian states move to a system of case-by-case assessment of projects.

Concerned parties, including the Business Council of Australia, have urged the Government to design and implement the ADGSM carefully to ensure that there is no undue pressure on gas companies who have existing contractual commitments to meet certain export targets.

Call for stronger Government action

In contrast, other industry bodies such as the Australian Industry Group, have advocated for the Government to pursue stronger actions to free up local gas supply and bring gas prices into equilibrium with international pricing.

One such proposed measure is for LNG exporters to fulfil some of their supply contracts with gas sourced from Asia via gas swap contracts.

However, the east coast gas squeeze is arguably a broader, industry-wide problem, the resolution of which requires a combined effort across the whole supply chain.

One example that was brought to the ACCC's attention in its 2015 Inquiry is the high cost of pipeline transportation that makes it uneconomical to develop the Northern Territory gas industry as a solution to the East coast gas predicament. This suggests that the gas shortage problem is multi-faceted and cannot be resolved simply by regulating one or more major industry players such as Santos.

Current outlook

Other solutions

The Australian Deputy Prime Minister has expressed a view that part of the solution to the east coast gas crisis comes down to 'commercial principles', including paying landowners 'the right amount of money' for access to their land.

The Government has also indicated that it is currently considering two big new pipelines that would be 'nation-building' projects, one line running from the Northern Territory to South Australia, and the other being a potential line from Western Australia to Eastern Australia, as part of the package of measures aimed at addressing the gas squeeze.

Conclusions

It remains to be seen whether the 2017 Inquiry can uncover information that was not already obtained by the ACCC as part of its 2015 Inquiry or to what extent its findings will encourage the Government to impose export restrictions on other companies pursuant to the ADGSM.

Whilst it is hoped that the 2017 Inquiry may lead to the development of better, more robust and informed policy, the lead time for the 2017 Inquiry is concerning. This is because, in the meantime, the uncertainty and signs of increased regulation and Government intervention may further dampen any appetite to invest in gas exploration and production projects at a time when it is critical that these activities continue to ensure a long term sustainable and reliable supply of gas to the Australian domestic market.

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