ECONOMICS AND INDUSTRY STANDING COMMITTEE

INQUIRY INTO DOMESTIC GAS PRICES

TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
WEDNESDAY, 20 OCTOBER 2010

SESSION TWO

Members

Dr M.D. Nahan (Chairman)
Mr W.J. Johnston (Deputy Chairman)
Mr M.P. Murray
Mrs L.M. Harvey
Mr J.E. McGrath

Hearing commenced at 10.36 am

MITCHELL, MR JAMES KEVIN
Managing Director, Synergy, examined:

McDOUGALL, MR ALLAN JAMES
Manager, Synergy, examined:

ADAMS, MR SIMON ROYCE
Acting Head of Wholesale, Synergy, examined:

The CHAIRMAN: Thank you for coming; I will read an opening statement. This committee hearing is a proceeding of the Parliament and warrants the same respect that proceedings in the house itself demand. Even though you are not required to give evidence on oath, any deliberate misleading of the committee may be regarded as a contempt of Parliament. In the lead-up to today's hearing, you indicated to the secretary that you will request restrictions on some of the questions and answers that may be posed by the committee. In accordance with this request, we will close the latter part of the hearing to the public to discuss these questions in a manner in which you may be comfortable in answering them. For now, there are a couple of procedure questions that I need to ask: have you completed the "Details of Witness" form?

Mr Mitchell: I have.

The CHAIRMAN: Do you understand the notes at the bottom of the form?

Mr Mitchell: I do.

The CHAIRMAN: Did you receive and read the "Information for Witnesses" briefing sheet regarding giving evidence before a parliamentary committee?

Mr Mitchell: I did.

The CHAIRMAN: Do you have any questions relating to your appearance before the hearing today?

Mr Mitchell: No.

The CHAIRMAN: The committee has received your submissions; thank you for your contribution. Do you wish to propose any amendments to your submission?

Mr Mitchell: No.

The CHAIRMAN: Do you wish to make an opening statement before we get into questions?

Mr Mitchell: Yes, we do.

The CHAIRMAN: Please proceed.

Mr Mitchell: Thank you, Mr Chairman and committee members. I would like to thank the committee for providing Synergy with an opportunity to speak at the hearing. Synergy is Western Australia's largest electricity retailer, and now the second-largest gas retailer in the state. We have over one million customers in industrial and commercial, small and medium enterprise; franchise electricity customers, but not franchise gas customers.

With respect to gas, Synergy entered the gas market in 2003, and, as I said, we have just become the second-largest gas retailer. Synergy's operations are limited to the SWIS—the south west interconnected system—so Kalbarri, Kalgoorlie, and Albany up. We currently estimate that we have 60 per cent, by volume, of the medium and large gas business customers connected to the

SWIS distribution system. We also have another role with respect to electricity generation. We have significant gas machines hanging off those wells, so we also toll gas under arrangements with generators to supplement Synergy's wholesale electricity portfolio.

Synergy has procured, and continues to procure, electricity through competitive tenders and other processes. Over the past four years we have built the largest wholesale electricity supply portfolio in Western Australia, and have written over $20 billion worth of long-term power purchase arrangements for gas, coal, wind, renewables, and so on. We are very experienced in negotiating and managing and understand the risks in long-term contracts.

Our procurement incorporates alternative fuel sources, including gas, to address the issue of security, price and sustainability. Gas is an important fuel for the diversity of Synergy's electricity portfolio. In order to service its industrial and commercial customers and to have gas for tolling, Synergy has developed a diverse and flexible gas supply portfolio and complementary transport arrangements. Synergy purchases gas from the Carnarvon and Perth basins, and has gas transport arrangements on the Dampier to Bunbury natural gas pipeline, the Parmelia pipeline, and the Goldfields gas pipeline. We are also exploring various gas storage options. Gas storage is important to ensure the stability of supply and smoothing of peak loads for both gas users and also electricity, particularly during emergencies. It assists in contract management of terms being imposed by gas producers, such as take-or-pay requirements. Natural gas now supplies around 60 per cent of the state's electricity generation.

Currently, Western Australian domestic gas customers pay considerably more than consumers in other states, despite there being substantially greater volumes of gas in federal waters off the WA coastline. Just two joint venturers supply over 95 per cent of gas to the Western Australian domestic gas market. In the absence of market forces, gas purchasers such as Synergy have no alternative other than to accept the pricing and terms and conditions offered if they wish to stay in business, unless we can pass those prices on to customers. In contrast, gas consumers are prevented from jointly purchasing gas, and therefore miss out on the benefits such as lower prices.

It is becoming increasingly difficult for new and existing gas fuel generators to source sufficient long-term—namely, 15-plus years—gas at commercially competitive prices. Generators have been turning to Synergy to solve these fuel issues. We have gone out to the market every year for the last four years, and we have potential generators who are saying, "We can build, run, operate and maintain the gas-fired generator, but you'll have to supply the gas because we cannot get it." The effect is likely to be an increasing reliance on coal generation, together with a significant increase in the cost of gas-generated electricity, with resulting upward pressure on domestic electricity prices.

The existing retention lease approval process protects the current holders. The current closed nature of the approval process contrasts sharply with the procedure employed for environmental approvals within the state, in which detailed information is publicly disclosed.

The LNG business started many years ago and better prices are currently being achieved for LNG exports here in WA, and that is causing the upward trend in domestic gas prices in Western Australia.

We believe there are a number of measures that could be employed to reduce the price of domestic gas. Firstly, the transition to separate marketing by joint venture partners should be considered. Indeed, the ACCC's recent determination on Gorgon noted that it would expect that separate marketing by gas producers would result in a more competitive market. It is also important to note that the ACCC only granted that exemption until 2015.

Secondly, more transparent retention lease approvals should be considered, ensuring the public disclosure of cost assumptions and the parameters used to test the commerciality of the project. Thirdly, ensuring the right balance between LNG export and the long-term energy needs of the local community will put downward pressure on the prices of domestic gas. Fourthly, providing the right incentives could promote smaller domestic gas developments or LNG projects with a domestic gas component. We currently have a significant amount of gas in federal waters offshore—there is the inshore and there is the onshore. The onshore is particularly prospective if you can provide the right amount of incentives in that area.

Lastly, improving information transparency through the gas supply chain would facilitate and ensure a more competitive market. Synergy supports the recommendations made last year by the Gas Supply and Emergency Management Committee that would see the establishment of a permanent gas bulletin board and the implementation of a gas statement of opportunity. We would actually see one more recommendation that we would like to propose, which is the establishment of a visible long-term contract gas market, in addition to the short-term gas market that they propose.

Without prompt action, the Western Australian domestic gas market will continue to experience a tight demand–supply balance, and demand is likely to remain high and to further increase as new customers seek substantial supply. Synergy is finding it difficult to acquire sufficient tranches of gas from the Carnarvon basin at sustainable prices to enable it to supply its current customer base well into the future. It is now critical for an increased commitment of gas reserves to the domestic market to ensure sufficient supply to meet not only current demand requirements but also additional growth as existing reserves deplete.

Mr Chairman, we were given some insight into the potential questions and we have prepared answers to those, but we would seek that further discussion on those questions could be done in camera because we can disclose information that we would not otherwise be publicly available or will prejudice us in a competitive market.

The CHAIRMAN: What questions were they? We will explore some general ones for the public, and then if you think the questions should be in camera let us know and we will postpone those to the in-camera session.

Mr Mitchell: Thank you.

The CHAIRMAN: As you know, the origin of this inquiry is the concern that I think you have expressed in your preliminary statements and in your submission that there is not only a potential growing lack of overall supply of gas—potential—but also very rapid price rises. You stated in your preamble that you have been going to the market and coming up with difficulty in acquiring additional gas and also additional sources of gas. Is that the case?

Mr Mitchell: That is correct.

The CHAIRMAN: Okay. Even though there have been some new sources, particularly with Apache or Macedon and the Reindeer projects that have come onto the market, Gorgon, is—we understand—starting to talk about, or think about, domestic gas aspects for the project. Is that easing the supply and price pressures that you are facing?

Mr Mitchell: I think it is fair to say that most gas tenders that have come out are completely overbid on. There is more demand for gas than there is supply; clearly, additional supply provides some amelioration of the demand need, and also as it comes into different parts of the Dampier to Bunbury pipeline it increases security of supply. But we continue to find that there is significant demand for gas well and truly above that which is available.

The CHAIRMAN: If you look at world gas prices—Henry Hub or whatever—just like with oil, there was a huge peak in 2007–08, and then it comes way down, not to where they were in 2003, but they have come way down. Is your problem that you are finding prices and quantity of gas caused by that peak, or is it a world phenomenon, or is it just, do you think, a domestic issue?

Mr Mitchell: I think it is a combination of both international and domestic. The west coast of Australia is linked into the world LNG market, and therefore we are in the world energy business—

it is not the same on the east coast of Australia. In time it actually may well be the case, and one could only presume that groups like British Gas have come in on that basis.

The second thing is, we basically go out to the market and seek prices. If we cannot see anything south of $8, then it indicates that the market has completely moved from where it was a few years ago, and the only thing we can do is to seek opportunities to, basically, get sources of supply from different areas. There are, basically, two different types of gas fields: those that will always be LNG, massive cost, massive everything, and they need the scale of LNG; then you have others, like the stuff that Santos and Apache have done, which was basically more for domestic markets. To the extent that you are not actively in the LNG market, that provides an opportunity to, basically, get gas into the domestic market, where it will never be an export LNG facility and you will not put in that massive amount of capital that is needed and so on. So to the extent that the state can support both onshore and inshore investment in finding more gas, incentives provide the opportunity for more domestically targeted gas than would otherwise be the case.

Mr M.P. MURRAY: Do you think that maybe you were lulled into a false sense of security on price due to the take-or-pay and long-term contracts that were sort of underpinning the early part of the development of the gas fields themselves, and if you really took it to the nth degree, the take or pay, which is a subsidy in some ways, price was really false and if you did not use them, you were paying anyway, even though it had been bought.

Mr Mitchell: I do not see any difference between what happened in the 20-year take-or-pay arrangements, or whatever they were—15-year take-or-pay arrangements—domestically, with what every other major entity is doing overseas; the Japanese, the Koreans, the Chinese. They are seeking to find gas at an acceptable price and to lock it in for quite a period of time. Our challenge is that we have a very small market; whereas the Japanese can buy it from Australia, Indonesia, Qatar—wherever—we have a rather small market here. We have the same issues in power basically; we have a very small market and these projects are just lumpy—significantly lumpy—so prices have been held flat. In hindsight, I have always argued that there should be a glide path to get to cost-reflective tariffs, otherwise, one day, you will come to a cliff face and all of a sudden you will have a number of significant issues.

Mr M.P. MURRAY: Probably the point I am making is, if you had to take double the amount for that week, the price is no longer cheaper, is it? If it is a take or pay and if you do not use it, you have paid anyway so you are paying double the price. That is the point I am trying to make.

Mr Mitchell: It depends on the nature of the contract. Within contracts you basically get an upper and lower boundary, so, on average, you take this, but you can go up and you can go down. If you have a significant number of contracts, you can basically flex a lot up and down. When plant goes out, we just reduce our take components without breaching our pay component; you look for flexibility in take-or-pay arrangements. There comes a point in time where you will be paying without taking, but we have not reached that point at all.

Mr W.J. JOHNSTON: Can I just ask, reflecting on the question from Mick, for the big LNG export contracts often the counterparty—not every time, particularly not in Japan, but in most other places—in Korea it is KOGAS that is the purchaser, in China it is a government-backed entity and it is in Singapore, and I understand that in Fiji there is a government-backed aggregator, and of course if you go back to 1979 it was the Western Australian state government, through SECWA at the time, that took the big take or pay to underpin the North West Shelf. Do you have any comment about whether it is worthwhile, the government taking that type of take-or-pay contract over 20 or 30 years and then selling on to other parties?

Mr Mitchell: In the in-camera session we will be happy to show you our gas supply portfolio; we are actually performing that role right now in, basically, the industrial and commercial market and the tolling generation market there. One of the absolute benefits of the gas aggregator is, instead of just being locked into one particular contract—it is either there or not there—you have a number of different contracts all with their unique circumstances. Because you have a major off-take element, you can basically do things that others cannot. Basically, that is exactly the role that Synergy performs in the energy market; we have written over $20 billion of power purchase arrangements that go on for five, 10, 15, sometimes 20 years. We basically blend all those portfolios together to come up with an efficient portfolio of supply, and we have done exactly the same thing with gas. We have quite a number of different sources of gas coming down different pipelines, and it is up to the skill of people like Allan to, basically, stay on top of it, and, basically, maximise the value of the portfolio that we have. If you can find a natural off-taker, you can find a natural aggregator.

The CHAIRMAN: I have a couple of issues. One of the problems with our gas market is that it is not very competitive because there are a few producers—only one until recently; two now, but one major one—and two pipelines, both regulated, and a few major consumers. This does not allow markets to work very well, and also they are locked into very long-term contracts offshore for LNG. Do you see ways to move towards more competitive markets; that is, more competitors on each one of the segments of the gas supply chain?

Mr Mitchell: I think you first have to appreciate that we are a very small market domestically, and this is where the issue comes from. Gas is important both for industrial use but also power use—60 per cent of the state is powered by gas. We are the smallest wholesale market in the world except for Iceland, and with that comes significant challenges. You do not get another TJ down a 1 500-kilometre pipeline if it is at capacity without spending billions of dollars. We have a very small and a very lumpy market. We made some comments in my opening remarks about how you could get a more competitive market, and, basically, looking at how one might look at the joint selling arrangements and replicate that with, potentially, joint purchasing arrangements. I also note that Santos and Apache do not need joint marketing arrangements; they are able to do it successfully.

The CHAIRMAN: BHP and Apache have the Macedon project. Are they separately marketing onshore? BHP is part of the North West Shelf and they are jointly marketing.

Mr Mitchell: Correct. The joint marketing has been re-extended, but only to 2015.

The CHAIRMAN: That is for Gorgon, not North West Shelf.

Mr Mitchell: No, North West Shelf as well.

The CHAIRMAN: Until 2015?

Mr Mitchell: I think it is; it is 15ish—something like that. That was the determination that came out a few weeks ago. Once again, the ACCC acknowledges that. The opportunity that that presents, if you can get away from the joint selling, is, ultimately, aggregation and storage. They then become opportunities and participants can step into that position. Basically, I understand that with North West Shelf they have issues of balancing, so if they have all sold it and you have not, what do I do with mine? Well, there is a balancing issue there. That will generate other entities coming into the market to actually provide the balancing and potentially storage. Gas is this wonderful commodity where you have an ability to store; the challenge that we have with electricity is that you cannot store it, and, in that, comes so much complexity. Gas is the only one where you have, actually, a significant opportunity to do something about it.

The CHAIRMAN: And other markets draw a lot of gas.

Mr Mitchell: Correct.

The CHAIRMAN: A lot of markets do.

There has been a very rapid growth in the mining sector demand for gas, but you only supply the SWIS. Do you want to provide gas to Rio Tinto, or do they have their own contracts, for instance for their power stations up in the Pilbara? You are not party to any of those, are you?

Mr Mitchell: No, we are not. We are involved in discussions with respect to the Mid West. From my perspective, we would much rather miners take electricity over transmission lines than gas, because their other version of power generation is through on-site generation—normally distillate units and so on. The cost-benefit analysis there is—I do not know where it is today, but during Varanus it was, like, $35 a gigajoule, back to gas equivalent; now it is back to something like $20 a gigajoule. I would strongly prefer not to be competing against the miners for gas. In my perfect world you would build large baseload power stations, getting all the economies of scale, you put transmission lines in, and then you can delve out the power that is needed, or supplied from that power station, to the respective mining site. That way, not everyone has to do their own thing. You get significant economies of scale, and instead of building five 50 megawatts, you could build one 250 megawatts or whatever the magical number is. The basic premise is that they have a different cost base to us. We seek to buy long term, and, going back to Mick's question some time ago, our generators supply us our $20 billion worth of power purchase arrangements—we have locked in fixed-price contracts—but on the east coast the price determination is not on what your cost is, it is actually what your new entrant price is that provides that glide path. Instead of it being 20 years now and just going like that again, it is the new entrant price that gets factored into the price determinations and not your current historic cost.

[11.00 am]

The CHAIRMAN: That is what is happening here, essentially, as new demands come onto the market, which includes the alternative of distillate. They are willing to pay a higher price than they have been used to paying for the glide path, and they are paying it. Often they are purchasing large volumes; Pacific has a 500-megawatt combined cycle power station. That is a lot of gas.

Mr Mitchell: Absolutely.

The CHAIRMAN: You are competing with the very high end and with an industry that is in a hurry.

Mr Mitchell: If it comes to the battle of the cheque books —

The CHAIRMAN: You do not want to compete with Rio.

Mr Mitchell: That is basically it.

Mr M.P. MURRAY: Just to step back a little to storage, does Synergy have any joint ventures, or is it doing any work by itself on the issue of storage because of the previous problems at Varanus and those sorts of things? Again, the break could happen anywhere on the line. Are you doing any work in that region?

Mr Mitchell: Yes, we are. We are in discussions with potential parties who can provide storage opportunities here in WA, I think one of which you canvassed well with Verve before.

The CHAIRMAN: We can discuss the details about that in camera if you wish.

Mr Mitchell: Sure. There are other parties as well.

The CHAIRMAN: What about unconventional gas? That has been mooted as a potential in Western Australia. Are you looking at it? Some people, we hear, are looking at it.

Mr Mitchell: Mr Chairman, we go out for tenders nearly every year and we invite the private sector and Verve to bid for our needs. Where does it start? It starts with customer demand. You get your demand and work out what you need. Do you need baseload, intermediate peaking, renewables, thermal or whatever? The skill sets we have are not in the development of coal and gas generation and that sort of thing; our skills are in contracting long term to acquire power from those entities. We rely on the private sector and Verve to bring their best offers and opportunities to us so that we can sort through them and provide the best mix of portfolio off-takes that benefit our customers. We have been particularly successful in that over the last four years. We can show that we have saved almost $2 billion to our customers by basically going out to that competitive market. There are only a few players and every tender we do has to be successful because we want them to come back and play tomorrow. If they are not successful and they do not come back to play, there becomes too few players. We have been instrumental in NewGen Kwinana—the 320-megawatt combined cycle gas turbine; the Neerabup gas plant, which is an OCGT 330-megawatt power station; the Collgar wind farm, a 40-megawatt biomass project; and a humble little three-turbine wind turbine plant at Mt Barker. That is in our skill set. We expect the developers to bring that skill set with them. We have identified a source of fuel, and that is great. We have a need for your load. That is the place that we play in the value chain. We acquire long term and we sell to our customers, basically. It is diversity of supply not only with respect to gas, but also renewables. We would kill for baseload renewables. We are supporting Carnegie Corporation and the New World Energy on wave and geothermal projects. We wish them every success and hope that they get commercial quickly because there is a real need for that renewable off-take in the market. If you are talking about generation in this state, the next word that comes out of your mouth has to be “fuel” and where we can get it from.

The CHAIRMAN: At the Office of Energy conference a few weeks ago, you confirmed that household energy prices have increased by 49.6 per cent over the last 15 months.

Mr Mitchell: Correct.

The CHAIRMAN: How much of that increase is attributed to the cost-reflective tariffs and how much is attributed to gas price contracts, or increases in gas prices?

Mr Mitchell: The increase that we have seen is to get us to cost-reflective tariffs, and we are not there yet. Part of the analysis I showed you was that the electricity tariff had not gone up since 1991, except for a humble increase of 3.75 per cent in 1997, but the humble tariff also had to wear the 10 per cent GST in 2001. Basically, real prices went down another 10 per cent. The tariffs have been held very low for a long time here and now an adjustment has to be made. We need to get to cost-reflective tariffs, but it is a matter of balance because we must make sure that we support those people who will do it tough in that environment at the same time. Is it gas? During the in camera session I can show you where we know generation costs will go to at today’s gas price. We can show you what our historic cost of gas generation is to date and, with the assumptions we will show you, we will show you what tomorrow’s gas price will be. That is important because for every $100 that someone gives to Synergy, $50 goes to generation, $40 goes to the network and $10 goes to retail. Of that $50, if that is to go up, there will be a significant impact on the cost of supply.

The CHAIRMAN: During the first period of the decade 2000–10—before that, your cost of fuel was not going up very much. Oil prices were pretty stagnant in the latter part of the 1990s. I do not know what the coal prices were because I do not know what the contract prices were like. Fuel prices started rising in the first part of this century. Did your prices also rise during that time? Were they going above CPI? Was your underlying cost of fuel going up, needing rises in underlying prices?

Mr Mitchell: They did, but to the extent the generators—I joined Synergy in 2006, and during the first half of the decade, it would have been vertically integrated with Western Power. To the extent that they had bought fuel for a fixed term at fixed prices, like North West Shelf gas with its escalation increases, and coal from Wesfarmers, Griffin and so on, those price increases would have been flowing through. Any new generation coming in would be at today’s or tomorrow’s new entrant cost because not only has fuel gone up, but also everything else has gone up, including steel, electronics and that sort of thing.

The CHAIRMAN: What share of your gas, or the gas marketed in the SWIS, goes to households in terms of gas itself?

Mr McDougall: None. We are prevented from selling domestic gas to residential customers.

The CHAIRMAN: Is that totally Alinta?

Mr McDougall: No; it is a totally deregulated market but there is a moratorium against Synergy retailing to residential customers.

Mr Mitchell: Alinta is the only party supplying gas, although the rules are that anyone can supply gas to household customers.

Mrs L.M. HARVEY: Except Synergy.

Mr Mitchell: Correct.

The CHAIRMAN: Is that to stop excessive market power?

Mr McDougall: It is more aligned with the electricity deregulation.

Mr Mitchell: The way you stop excessive market power in those sorts of environments is through regulation.

The CHAIRMAN: That is more regulation.

Mr Mitchell: I was going to say that it was tried and tested, but it is a tried mechanism.

The CHAIRMAN: How much of the increases in gas—I know that you are not delivering it—is falling on domestic users when the ordinary punter out there is worried about —

Mr Mitchell: You would have to ask Alinta that. The question you would have to ask them is: what prices are there in the market today, as opposed to yesterday, for domestic gas? It is the same for us: what gas is there for our tolling operations and so on? It just depends on their business model, and I cannot comment on that.

The CHAIRMAN: In your submission, you have argued that short-term and long-term trading in the secondary market is common, despite there being no official market to implement these trades. How active is Synergy in this unofficial secondary market?

Mr Mitchell: I will let Allan talk about that.

Mr McDougall: We would receive calls every month to participate in that market for buying and selling.

The CHAIRMAN: How does it operate? Does someone call you up and say that they have too much gas?

Mr McDougall: That is exactly how it works. There are some major players in the downstream market. Everyone knows who everybody is and we call each other up to complete a transaction.

The CHAIRMAN: Would it be beneficial to formalise that through a short-term trading market like they have on the eastern seaboard?

Mr McDougall: Potentially, it would open it up to a broader group of people.

The CHAIRMAN: How long are the contracts? Are they generally quite short term, such as for a day?

Mr McDougall: They vary from a day to a month.

Mr Mitchell: You must recognise that there are two different markets: the short-term market, which is what you are talking about now, and the long-term contract market. Long-term power purchase arrangements, fuel supply and generators are all done in that long-term market, so you can see the spot price going up and down on supply and demand and whether a pipeline is out today or is operating at double capacity or an industrial facility has closed down. You get supply and demand. That is the short-term market. The more important one is the long-term contract market. My perfect world is if you can buy—this is similar to the metals market—you basically go in and do what is called a “frame contract” where you agree on everything including quality, delivery, premium and all those sorts of things, except the price. The price is determined by a different mechanism. In the LME market it is determined by an average of metal prices at the London Metal Exchange over the last 35 business days. If we can get a long-term contract price, such as a five-year price, you can then basically start ensuring that you can pass price increases through in an environment where you do not have to go to the High Court every time to try to get a determination of where the market is. We know that Alinta went through this in its gas price determination. Every gas supplier and consumer in the state was basically subpoenaed. It must have cost a fortune. But if you can get a visible five-year contract market, a whole lot of other things can actually follow. You can then go to the regulators and say, "This is the five-year market and this is the price. Please pass any price increases through to customers". An industrial customer can say, "How do you know I am not paying too much?" If you have a visible market, you can get reliance. The day when we can move from a short-term market into a five-year market, a whole lot of other opportunities will open themselves up and a whole lot of pass through of costs and visibility of prices and discussions and disagreements about where the market is and is not will get solved.

The CHAIRMAN: You could say that that might be happening in the sense that you have a lot of gas sold through LNG. LNG is increasingly tied to oil prices of some sort. You could say that you could relate domestic sales to netback LNG or to oil prices. There could be some percentage of oil prices, and that could be the marker and you could then negotiate around the very valuable service aspects of the contract.

Mr Mitchell: The Singapore gas price is based on oil. As the price of oil goes up, gas goes up and as oil goes down, gas goes down. But there is a fundamental assumption that the oil and gas markets are similar; we do not accept that assumption. If you have a lack of future oil production coming out and you have significant quantities of gas in the federal waters off the WA coastline sitting there—massive reserves—one does not necessarily follow the other.

The CHAIRMAN: So you have to come up with a relevant market price?

Mr Mitchell: Correct. In Peter's old firm—the ERA—we would have to show him that we have efficiently purchased gas for them to pass that through in a tariff arrangement. How do we show it has been efficiently procured? We would go to the ERA and say that the domestic customers will pay it based on world oil prices going up and down all the time. That is a pretty tough ask. We go out and deliberately seek gas away from the link to the oil market because we cannot pass that on to customers easily. One, we cannot pass it on and, two, it would be a difficult sell to try to explain why your gas tariffs go up and down based on what happens in the international oil market based in Singapore. I know that happens with petrol, but we have a few more challenges to get to cost-reflective tariffs before we get to that point.

The CHAIRMAN: The challenge is getting the relevant market price to link the contracts on.

Mr Mitchell: Correct, but also you need the whole economy to be able to have the flexibility of price pass throughs. When you have held it flat for so long, you do not have that flexibility mechanism to say, "If I increase my price, he will increase his price and another person will increase his price down the value chain." Someone will get badly hurt. In my view, the economy will have to adjust to more flexible prices arrangements than it has to date if that is our future.

The CHAIRMAN: Do you think there is scope for governments to ensure greater transparency of long-term gas contracts? There is a lot of secrecy involved in all those contracts among a very limited number of players.

Mr Mitchell: Welcome to the reality of the small market with major players.

The CHAIRMAN: The reality is that there will be change. The question is whether these contracts have to start being published. I understand that in other jurisdictions many of those contract prices are published.

Mr Mitchell: I cannot comment on that. I am seeking a method to have a visible price signal that everyone accepts because from that simple principle you can easily —

The CHAIRMAN: We do have a very thin market with few contracts, relatively, and there is no spot market. One way to improve transparency is to say that all these contracts are transparent and they are publicly available, not only the prices, but also the aspects of them—all of them. It would have to be all of them. There might be some difficulties in achieving that, but that would be one way to allow a great deal of information on the market as to what the wholesale long-term market price is.

Mr Mitchell: In essence, that is what happens in a regulatory environment. You go out and you get efficiency. Once it gets published, everyone knows where the market is at, and that in itself draws the market together.

The CHAIRMAN: One of our problems is that very few people—in fact almost no-one—knows where the market is at.

Mr Mitchell: Correct.

The CHAIRMAN: We hear a lot of rumours and we have to go in camera to get even an indication of the prices. It is a small group and I am sure that you look at each other's belly buttons a lot to find out what is going on, but this market lacks transparency, to any degree, of long-term prices. One of the aims of this committee is to look at the structure of the market and the disclosure mechanisms of not only the structure, but also the conduct of the market to try to improve competition here. We accept the arguments of the joint marketing issues and other things relating to downstream processing. I am speaking off the top of my head—I do not know whether it is even legally feasible to do or whether we should do it. I am exploring enforcing greater disclosure of contracts.

Mr Mitchell: All I can say is that the natural response to a monopoly power is regulation.

The CHAIRMAN: In many places when you do have a monopoly power that is regulated, the contracts are all disclosed.

Mr Mitchell: We will talk about that later.

The CHAIRMAN: Okay. On page 4 of your submission you make the point that in limited circumstances large consumers can jointly purchase gas. Under what circumstances is joint purchasing permitted?

Mr Adams: I suspect that is a reference to the provisions under the Trade Practices Act where joint venturers can jointly purchase under a joint venture arrangement. The recent amendments to the Trade Practices Act allow a joint buying group for a specific purpose to collectively acquire. They would be the only circumstances that we are aware of that would be legally permissible.

The CHAIRMAN: Okay. Also on page 4 of your submission you have argued that commodity gas costs in WA can be as high as $9 per gigajoule. Is this statement based on your own experience?

Mr Mitchell: Yes, it is. We can show you our price curves in camera.

The CHAIRMAN: Any other questions? We will go to in camera session.

[The committee took evidence in camera]