Australian Paper

a member of the Nippon Paper Group

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Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South
NSW 1235

Dear Mr Pierce,

Re: Australian Paper submission – Stage 1 Draft Report East Coast Wholesale Gas Market and Pipeline Frameworks Review

Thank you for the opportunity to submit a submission on the issues and questions raised by the draft report on Stage 1 of the review into the east coast wholesale gas market and pipeline frameworks.

We are disappointed at the relatively short timeframe in which to make a submission to a 302-page document, especially as there are a number of energy industry reviews being conducted in parallel, all of which require submissions. Industry in general, and Australian Paper in particular, does not have the resources to respond in a short timeframe to the demands of these reviews. Consequently, our comments here are necessarily brief and do not address the full content of the draft review.

We would respectfully draw the Commission's attention to the submissions made by the EUAA, Qenos and CQ Partners. We particularly support the comments made by CQ Partners in respect of the lack of large users' representation in the Advisory Group members and the views of CQ Partners as a body that is actively using and participating in STTM's.

The *Industry Statement to support the Council of Australian Government's Energy Council Gas Market Development Vision*, letter submitted to the AEMC on 30 March, 2015 by a cross section of Producers, Suppliers, Users and Associations also covered a number of issues pertinent to the AEMC's consideration of submission feedback.

Australian Paper

Australian Paper is a subsidiary of the Japanese-based organisation, Nippon Paper Industries (NPI), which has an overseas network of manufacturing subsidiaries and affiliates in Asia, Oceania, Europe, North and South America and Africa, covering production of pulp, paper, timber and chemicals.

Australian Paper, Australia's only fine paper manufacturer, employs approximately 900 people at its Maryvale pulp and paper manufacturing plant in the Latrobe Valley, 191 at its Preston envelopes and stationary manufacturing and office papers distribution business and a further 108 in its sales, marketing and head office in Mount Waverley. This is a total of approximately 1,200 direct employees in Victoria, with wages and salaries totalling $150 million annually. In addition, there are a significant number of on-site operations managed and operated by other companies to provide goods and services to Australian Paper and to process by-products from its operations.

Past economic studies by Western Research Institute in 2006 have demonstrated a flow on of a further 143% to 188% to household incomes in the community.
Total sales of Australian Paper's Victorian manufacturing businesses are just under $800 million, again with a flow on of a further 120 – 152% to the community, much of this in regional Victoria.

With the completion of its recent pulp mill redevelopment, Australian Paper is much less reliant on imported pulp for its paper manufacture and therefore a much larger part of the sales revenue remains in Victoria.

AP has a substantial investment in the Australian economy, including an additional $1 billion outlay over the past 15 years.

Our EITE operations at the Maryvale Mill pulp and paper facility consume some 18PJ of energy annually making us one of the largest, if not the largest, energy users in Victoria. Some 55% of our energy requirements are generated on site from renewable energy and we have the largest bioenergy power plant in Victoria accounting for 42% of the installed bioenergy capacity of the State. Our renewable energy power plant, fuelled by Black Liquor, typically generates in excess of 240 GWh of electricity each year. The balance of our energy demand is purchased through contracts for the supply of electricity and natural gas, typically purchasing 7-8 PJ per annum of natural gas for the mill's requirements.

Overall Scope – Significant Omissions
The scope of the review, and the subsequent draft report, ignores the lack of competitive gas offers to large users and the inability to secure long-term gas supply contracts. Similarly the withholding of gas supply from the domestic market is also being ignored. This failure to consider the gas market in an holistic approach necessarily compromises any recommendations that may eventually flow from the review.

In this respect the AEMC review can be compared to the internally initiated review held by the Productivity Commission. In their review the PC made two basic assumptions:

- The gas market was a fully competitive market with no market power influences; and
- Gas supply would flow to meet gas demand.

Given the inappropriateness of the basic modelling inputs, it was not surprising that the conclusions reached by the modelling were equally flawed. The AEMC review runs the same risk of providing inappropriate and uninformed outcomes by virtue of ignoring what are major impediments to the functioning of a liquid and efficient market.

The failure to include all aspects of the gas market, lack of large consumer representation and the preponderance of gas producers and suppliers, calls into question the ability of this review to adequately address the National Gas Objective – *to promote efficient investment in the, and efficient operation and use of, the natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.*

The draft review suggests that the interests of consumers have been subjugated by consideration of outcomes that would benefit natural gas producers at the expense of consumers. The overriding consideration would appear to be facilitating the LNG gas export producers. We struggle to comprehend the Commission classifying LNG producers as *gas consumers* the businesses are engaged in the <u>production and sale</u> of gas, in this instance sale of gas also includes the liquefaction and exporting of gas.

Facilitating an Efficient and Competitive Gas Market
Australian Paper is dismayed by the negative comments and connotations applied to the STTM and the lack of consideration of large users who utilise the STTM as a sole means of providing an element of competitive behaviour into a parochial market.

STTM's provide an important market reference point and assist large users in managing their gas portfolios and minimising gas costs. Building upon and resolving identified issues with existing trading hubs is considered to be a necessary pre-condition to the development of an integrated eastern Australia gas market.

We would refer the Commission to the submissions made by Qenos and QC Partners in support of STTM's for the views of those who actively participate in the STTM system. It is telling that the STTM has, in its short period of operation, attracted sixteen participants who are either registered, or have applied for registration, to participate in the STTM process. Contrast this with the National Electricity Market (NEM) which has been in existence for many years but only has five direct participants, four of whom are smelters.

STTM's at Sydney and Adelaide are providing a competitive gas supply for large users, often complimenting a more traditional bilateral contract, and providing users with a foil for the *take it or leave it* offers from more traditional gas suppliers. It is surprising therefore, to read the AEMC's bias towards the least successful hub – Wallumbilla. This hub is remote from the majority of the domestic gas load but it is close to the LNG export facilities. As such it is the most likely of the hubs to be influenced by LNG net-back pricing and provide a market signal closer to what the gas producers would wish to see.

Development of an STTM at Moomba would address the concerns raised in the draft report in relation to hubs being remote from the production areas. Moomba would also be in closer proximity to the domestic gas load and less likely to be unduly influenced by LNG net-back pricing. This would be of benefit to consumers.

Given the benefit that STTM's bring to gas consumers we would oppose any moves to restrict or remove STTM's prior to an identified alternative being introduced and established. To do otherwise would be removing a competitive plank from a market that is not currently performing as a competitive and efficient market.

From a consumer's perspective the most efficient and competitive aspects of the current gas market are the Adelaide and Sydney STTM's and the DWGM system operating in Victoria. It is with concern that we read the Commissions' views that these market mechanisms are not providing the market options to complement the trade of natural gas. As a large user with operations in various eastern States it is our contention that the DWGM is the most efficient and cost-effective method of transporting gas molecules. The impediments to obtaining capacity for gas transport outside the DWGM are significant and, in some instances, have served to reduce market competition by rendering it impossible or uneconomic to transport gas from an otherwise competitive supply point to an end use point.

Reliability and security of supply is paramount for many large gas consumers and it is for this reason that a *Voluntary* market does not serve the interests of gas consumers. It would however, further the interests of gas producers by removing a competitive alternative supply option and push consumers back to more traditional gas contracting options. For this reason it is not considered feasible to entertain the concept of a voluntary STTM option.

Harmonising the gas day start times across the east coast gas market is a welcome step to promoting an efficient and competitive market. The current misalignment of market time detract from competitive behaviour as it is possible for some sections of the market to know the ex-ante price of gas supply prior to nominating their own price.

Lack of transparency in the gas market impedes the ability of a consumer to engage with gas producers and suppliers on a level field. Large users historically entered the market at infrequent intervals and contracted long. In the current market long contracts are not being offered to consumers, although it is noted that long term contracts are being executed between various producers. There is clearly a desire, on the behalf of consumers, to have more price discovery available. However, the draft report contemplates establishing the Gas Bulletin Board as a *one stop shop* for gas market data. In our opinion it would be advisable to consider a number of options for the provision of gas market information and be driven by a cost-effective solution. A *one stop shop* may not be the most efficient option.

Conclusion
Australian Paper supports further development of the east coast gas market to address current challenges and uncertainties. Proposed changes should support overall productivity and efficiency improvements and further the NGO, i.e. the emphasis should be on long term benefits to the gas consumer.

Industry and government both have roles to play in promoting market development and identifying reform priorities and market impacts. Reform should facilitate timely development of the market whilst appreciating the need for continued market engagement and management of any identified transformation. The need to maintain a functioning market during the transition phase should be paramount.

Given that information asymmetries are impediments to fully functioning markets, we support the view that the market would be better served by a centralised and holistic reporting framework. However, this should be provided in a cost-effective and supporting manner rather than opting to utilise an existing reporting format.

The development of STTM's to provide an alternative competitive option to users should be encouraged. A review of the current costs incurred by AEMO in operating the STTM's should be implemented to identify processes that could improve efficiency and reduce costs. The option of establishing a STTM at Moomba should be on the list of actions being considered by the AEMC.

It is our belief that the AEMC Review has not complied with the National Gas Objective and does not benefit the long term interest of gas consumers. Gas producers, gas suppliers and pipeline owners are the predominant members of the Advisory Group with gas consumers being notably conspicuous by their absence. The Draft Report favours the interest of producers and pipeliners' to the detriment of gas users.

We are concerned that the most effective market mechanisms for consumers, the Adelaide and Sydney STTM's and the DWGM, are being questioned by the AEMC whilst the least efficient and most costly alternatives, Wallumbilla and Market Carriage, are being promoted.

We thank you for considering Australian Paper's submission and would be pleased to discuss our comments at length should the occasion arise. If you have any questions concerning this submission, please do not hesitate to contact the undersigned.

Yours sincerely,

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