



15 September 2008

The Secretary
Senate Standing Committee on Economics
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Dear Mr Hawkins

INQUIRY INTO MATTERS RELATING TO THE GAS EXPLOSION AT VARANUS ISLAND, WESTERN AUSTRALIA

The Chamber of Minerals and Energy of Western Australia (CME) thanks you for the opportunity to tender a submission to this inquiry.

The Chamber of Minerals and Energy (CME) was present at the emergency meeting called by the Premier on Sunday 8th June 2008. Subsequent to that meeting CME became part of the two committees and one working party that were formed to coordinate a response to the incident:

- Gas Supply Coordination Committee
- Gas Supply Disruption Recovery Group
- The Communications Working Party

Government and Industry worked cooperatively to minimise the impact of the gas outage. Industry and the Chamber were supportive of the State Government's preferred strategy of not invoking emergency powers but of seeking voluntary contributions to a managed outcome.

In relation to security of energy supply, the Chamber has long called for a long-term vision for the State and a robust but flexible State Energy Policy to support this vision.

At this time there is no clearly enunciated State or Federal policy on the matter.

ECONOMIC IMPACT

The foundation of the Western Australian economy has become the mining, mineral processing and oil and gas sectors. These sectors are now major drivers of economic growth and contribute over \$2 billion in royalty payments as well as substantial contributions to other taxation revenues.

The State is a large energy consumer as a consequence of general economic expansion and the growth in mineral processing and extraction, but also has become a substantial energy exporter.

Broadly, the CME strongly supports a preference for market solutions in energy policy, but notes the important role Government plays in setting policy and regulations, and in removing barriers to new investment. This then allows markets to operate freely in the provision of energy to industrial, commercial and residential users.

Extent of losses

The Chamber of Commerce and Industry of Western Australia (CCIWA) estimated the impact of the gas disruption at \$2.4B across June and July 2008. WA State Treasury estimated a 0.5% reduction in growth for 2007/08 or \$1.8B between 2007/08 and 2011/12.

Individual companies may well be exploring compensation options.

Disruption to SW

The State's heavy industrial and manufacturing base in the southwest generates process heat from natural gas. The bulk of this gas is transported from the north of the state to the population centres in the southwest via the Dampier to Bunbury Natural Gas Pipeline (DBNGP) and the Parmelia Pipeline (Dongara to Pinjarra). As a result of the disruption to supply at Varanus Island, supply available to the DBNGP was curtailed.

Disruption due to the incident in the southwest was two-fold; shortage of gas volumes and significantly escalated electricity charges. Many of the commercial users of gas in the southwest are relatively small and are customers of retailers rather than direct buyers of gas from the producers. Many of the smaller industrial consumers had immediate curtailment of supply, were unable to access part of the increased gas production from the Woodside managed NW Shelf Venture during the first month of the incident and as a result of increased price of generated electricity were faced with very significant increases to cost.

Where gas supply could be accessed it was often of variable daily volumes making ramping up and production scheduling very difficult.

The corollary of this was that gas supply to non-essential smaller businesses was diverted to support priority areas. There was not enough gas available to maintain business as usual for all sectors, and certainly heavy industry and mineral processing were also required to reduce use and use alternative fuel for process heat where possible. (This was generally distillate burners where these were still available, as most have been replaced with gas burners in recent years due to cost and environmental implications). Not all major industries were able to use alternative fuels and some major industrial electricity consumers had supply withdrawn to provide electricity back to the grid.

The interests of many small business owners in Western Australia are represented by the Chamber of Commerce and Industry of Western Australia (CCIWA). We are aware that CCIWA will make its own submission to the Committee of the impacts and implications of the gas supply disruption to the small businesses of the southwest of the State.

Contractual Arrangements

The market (and hence the State) relies on private investment in production and distribution capacity. Any policy position that minimizes investment is a threat to capacity expansion. Appropriate electricity and gas tariff structures and regulation must underpin the market and allow the market to operate freely in providing solutions for energy requirements.

During the crisis a number of member companies made arrangements to secure alternative gas supplies where possible. Costs and terms of these short term contracts are commercial-in-confidence and CME is not able to comment on these arrangements, their longevity or current status. The Chamber is aware that the short term alternate contracts were struck at a significant price premium to existing contracts.

In general sufficient supplies of distillate were available to those operations that were able to use it, although at additional cost and generally not in sufficient volumes for normal production levels. Transport arrangements for the volume of liquid fuels required for some larger industrial customers were problematic.

GOVERNMENT RESPONSE

Adequacy of Crisis Mgt

Work within the Gas Supply Coordination Committee was undertaken by a dedicated group from the WA public sector and in the main from the Office of Energy. CME does not doubt the focus of the people involved in managing the incident. CME does, however, make the observation that resources appeared very limited, with staff appearing to work very long hours with limited provision for redundancy coverage.

The committee was supplemented with very knowledgeable professionals from the energy generators and transmitters. This knowledge and information was invaluable.

Reliance on One Source Supplies of Gas for Domestic Market

WA currently has several sources of domestic gas, two of which use the Varanus Island hub for primary processing before entry into the market. These two sources, (the John Brookes and Harriet fields), along with the North Rankin fields of the North West Shelf Venture, feed gas into the Dampier to Bunbury Pipeline, the major delivery pipeline for the South West of the State.

The loss of the Varanus Island processing facility reduced gas availability in the State by about 35%. Some of the lost capacity was able to be diverted to the southwest from the other major pipeline in the State (the Goldfields Gas Transmission Pipeline), with many affected users in the Goldfields able to use alternative diesel generation in many cases (albeit at an increased cost). For some the additional expense of diesel transport, storage and electricity generation made continued mineral production uneconomic.

Fuel diversity must be a key consideration for the State Energy Policy. Diversity of fuels in terms of fuel-on-fuel and inter-fuel competition will be a key driver of a competitive market and secure, stable and competitively priced electricity for consumers. Future gas sources are likely to have differing specifications and are also likely to be technically more challenging to develop than existing reserves.

Diversity of technology will allow broadening of the generation base and geographic distribution of generation sources. Renewable energy sources will require pricing of electricity that reflects the cost of bringing these supplies to the market, such as those of backup and balancing. Whilst distributed renewable generation has implications for network stability, it also limits transmission losses.

Alternative Sources

Some of the electricity production loss in the Southwest was able to be made up by quickly returning mothballed coal-fired capacity to service, but this was not able to meet the total energy demand, and in any case was not able to substitute for off-grid operations that required gas as a heat source or chemical feedstock rather than as an electricity generation input. The formerly mothballed coal-fired capacity had been withdrawn from service due to environmental concerns associated with the age of the plant and equipment. Planned maintenance shutdowns of generating units meant that some mothballed units would have been returned to service as part of the maintenance cycle. These returns to service were expedited where possible, however safety and availability issues prevented the rapid bringing-on of several units.

Potential for Emergency Storage

Because of the heavy reliance on gas by industrial users in the State's southwest, emergency storage of a sufficient volume to be meaningful (i.e. beyond a few days) is both technically and environmentally challenging and may not be economically feasible. Investment in alternative supply and redundancy in delivery systems may provide longer term security.

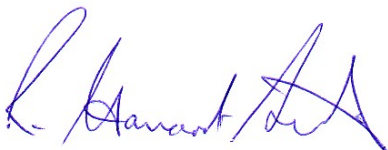
The State Energy Policy must ensure that energy infrastructure is adequate to meet future energy demand at both regional and local level. This includes maintenance of the South West Interconnected System in the long term. The State can best facilitate this by ensuring a clear and consistent long-term investment climate including reduced costs of entry to the market, and tariffs that provide appropriate pricing signals. The State must ensure any owner/operator of the SWIS provides for the State's future growth by facilitating economic and industry development.

CME Action

CME member companies have been invited to make their own submissions and we would draw your attention to the greater detail provided therein.

We recognise this brief communication can only flag some of the issues. We would welcome the opportunity to continue dialogue with your committee should you feel it would add value to the discussion. Please contact myself or Paul Hynch, Executive Officer Industry Policy (p.hynch@cmewa.com or phone 08 9220 8514), to arrange further discussion of these and other issues.

Yours sincerely



Reg Howard-Smith
Chief Executive