

Tender - Natural Gas Large Market Accounts

File No: S084740

Summary

The City has driven down our emissions by 76 per cent compared to 2006 baselines, resulting in the City achieving our 2030 carbon emissions target nine years ahead of schedule in the 2020/21 period.

The City has committed to the electrification of its portfolio by including it as an objective in the 10-year capital plan. The electrification will entail switching from gas assets to electric and transitioning certain pools that reached the end of life to electric water heating. Retrofitting existing buildings is more complicated and higher cost and the optimal time to do this is when a building is undergoing a major refurbishment or otherwise equipment is due for replacement.

The City's properties that require a Natural Gas Large Market account contract are Town Hall House, Cook & Philip Aquatic Centre, Gunyama Aquatic Centre, Prince Alfred Aquatic Centre and Ian Thorpe Aquatic Centre. Collectively these five sites used 75 terajoules (TJ) of natural gas in 2020/21, accounting for 86 per cent of the City's total natural gas demand. The primary use for natural gas at Town Hall House is for operating the tri-generation system, and at aquatic centres is for pool heating, space heating and cogeneration systems.

When the City installed trigeneration to Town Hall House it reduced emissions compared to the electricity grid. However, this changed in July 2020 when the City started using emissions-free renewable electricity.

The City's aquatic centres use a mix of cogeneration, electric heat pumps, gas boilers and heat recovery for pool heating. At present no single technology can replace gas for pool heating. Electrification also often requires more space for equipment using currently available technologies, but this is expected to change over time.

The natural gas market has experienced unprecedented volatility due to increased international demand, and a shortage of gas supply as some energy generators have increased gas-powered electricity generation.

Due to this market volatility, the City's previous natural gas retailer (Weston Energy Pty Limited) was suspended from retail natural gas operations on 23 May 2022. Consequently, as of 24 May 2022, the Australian Energy Retailer (AER) triggered the "Retailer of Last Resort" (ROLR) placing the City's natural gas accounts on default natural gas rates and terms. The physical supply of natural gas to the City's facilities was not affected by the suspension. The natural gas-related operations continue to operate as per business as usual.

For the large market accounts, the Southern Sydney Regional Organisation of Councils (SSROC) conducted a procurement activity for five affected councils. This activity requested pricing for various contract terms ranging from six months to three years. The market did not offer pricing for a six-month term. Based on the submissions received, SSROC recommended a one-year term, expiring on 30 June 2023.

Councillors were briefed about the situation on 20 June 2022 and the presentation is provided in Confidential Attachment C.

The Chief Executive Officer on 27 June 2022 approved contracts with Origin Energy LPG Limited for the provision of retail natural gas supply for the City's large market accounts for a period of one year, noting that the current market conditions meant that these contracts were required to be entered into on an emergency basis under section 55(3)(k) of the Local Government Act 1993.

The current projections of the natural gas market, by the Australian Competition and Consumer Commission (ACCC) and industry bodies, are anticipating a shortfall in 2023 and 2024. The shortfall would lead to elevated prices for any gas procured closer to that period. It is important that the City goes to market for the new supply of retail Natural Gas at the right time, as the market prices can fluctuate extensively in the current environment.

The natural gas procurement exercise also needs to accommodate the short validity period for market pricing offers which typically are valid for approximately one week. Short validity periods are a result of the dynamic nature of the natural gas wholesale market where local and international factors can influence the pricing in a matter of weeks.

It is therefore recommended that the City continue to review market conditions and call tenders at the estimated optimal timing between now and early 2023 for a new Large Market Gas Supply Contract, noting the financial information and natural gas market forecast as outlined in Confidential Attachment A and Attachment B. Given the short validity period offered in this industry at present, it is recommended that Council delegate authority to the Chief Executive Officer to accept the tender and negotiate, execute and administer such contract.

Recommendation

It is resolved that:

- (A) Council note that a tender will be issued by May 2023 for a new Large Market Natural Gas Supply Contract, noting the financial implications and natural gas market forecast as outlined in Confidential Attachments A and B to the subject report;
- (B) Council note that the timing of tender release will be based on a staff assessment of optimal market conditions to achieve the best outcome for Council;
- (C) authority be delegated to the Chief Executive Officer to:
 - (a) approve the acceptance of the tender for Large Market Natural Gas Supply with the prior consultation of the Chief Financial Officer, following a tender process in accordance with the Local Government Act 1993 and relevant regulations; and
 - (b) negotiate, execute and administer the Large Market Natural Gas Supply Contract; and
- (D) Council note that it will be provided with a CEO Update following the award of the Large Market Natural Gas Supply Contract.

Attachments

- Attachment A.** Financial Implications (Confidential)
- Attachment B.** Natural Gas Market Forecast (Confidential)
- Attachment C.** 20 June 2022 Councillor Briefing (Confidential)

Background

1. The natural gas market has experienced unprecedented volatility due to increased international demand, and a shortage of gas supply as some energy generators have increased gas-powered electricity generation due to supply shortages.
2. Due to this market volatility, the City's previous natural gas retailer (Weston Energy Pty Limited) was suspended from retail natural gas operations on 23 May 2022. Consequently, as of 24 May 2022, the Australian Energy Retailer (AER) triggered the Retailer of Last Resort (ROLR) placing the City's natural gas accounts on default natural gas rates and terms. The physical supply of natural gas to the City's facilities was not affected by the suspension. The natural gas-related operations continue to operate as per business as usual.
3. For the large market accounts, the Southern Sydney Regional Organisation of Councils (SSROC) conducted a procurement activity for five affected councils. This activity requested pricing for various contract terms ranging from six months to three years. The market did not offer pricing for a six-month term. Based on the submissions received, SSROC recommended a one-year term, expiring on 30 June 2023.
4. An update on the natural gas market forecast is provided in Confidential Attachment B with predictions on future prices based on industry feedback. Councillors were briefed on the situation on 20 June 2022 and that presentation is provided in Confidential Attachment C.
5. The Chief Executive Officer on 27 June 2022 approved contracts with Origin Energy LPG Limited for the provision of retail natural gas supply for the City's large market accounts for a period of one year, noting that the current market conditions meant that these contracts were required to be entered into on an emergency basis under section 55(3)(k) of the Local Government Act 1993.
6. Natural gas pricing was at a historical low and stable from 2018 to early 2021. This was primarily because of excess supply within domestic and international markets. However, since late 2021, the gas market has become volatile due to pressures within the electricity market and increased demand from international markets.
7. The current projections of the natural gas market, by the Australian Competition and Consumer Commission (ACCC) and industry bodies, are anticipating a shortfall in the years 2023 and 2024. The shortfall could lead to further elevated prices for any gas procured closer to that period. It is important that the City goes to market for the new supply of Natural Gas at the right time, as the market prices can fluctuate extensively in the current environment.
8. The City's current agreement for the supply of Retail Natural Gas that covers the Large Market accounts within the City's portfolio is set to expire on 30 June 2023.
9. A large market account typically consumes greater than 10,000 GJ per annum. However, while this is the industry benchmark, gas retailers are currently forcing customers on Large Market accounts for annual consumption as low as 5,000 GJ. The large market accounts cover approximately 90 per cent of the City's natural gas demand.
10. The City's properties that require a Large Market account contract are Town Hall House, Cook & Philip Aquatic Centre, Gunyama Aquatic Centre, Prince Alfred Aquatic Centre and Ian Thorpe Aquatic Centre.

Carbon Emissions Profile

11. The City has driven down our emissions by 76 per cent compared to 2006 baselines, resulting in the City achieving our 2030 carbon emissions target nine years ahead of schedule in the 2020/21 period.
12. This significant overall reduction has been implemented through electricity initiatives such as:
 - (a) the offsite renewable contract;
 - (b) rooftop solar and building efficiencies at multiple City sites including office buildings, childcare centres, libraries, community centres and sporting fields; and
 - (c) LED streetlighting.
13. The City has committed to the electrification of its portfolio by including it as an objective in the 10-year capital plan. The electrification will entail switching from gas assets to electric and transitioning certain pools that reached the end of life to electric water heating. Retrofitting existing buildings is more complicated and higher cost and the optimal time to do this is when a building is undergoing a major refurbishment or otherwise equipment is due for replacement.
14. Future initiatives include:
 - (a) renewable gas to further minimise natural gas related emissions; and
 - (b) the electrification program to further enable the move away from fossil fuels.

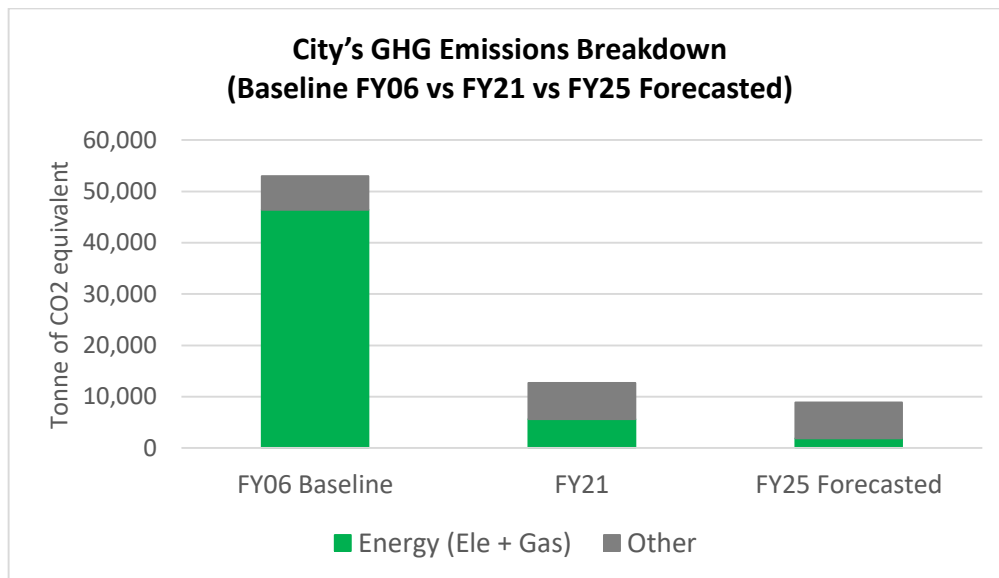


Table 1 - City of Sydney Carbon Emissions

Procurement Process

15. The City will undertake a standard procurement process, however must accommodate the short validity period for any prospective market pricing offers which typically are valid for around a week maximum. Short validity periods are a result of the dynamic nature of the natural gas wholesale market where local and international factors can influence the pricing in a matter of weeks.
16. It is therefore recommended that the City continue to review market conditions and call tenders at the estimated optimal timing between now and March 2023 for a new Large Market Gas Supply Contract, noting the financial information as outlined in Confidential Attachment A.
17. Given the short validity period offered by suppliers in this industry at present, it is also recommended that Council delegate authority to the Chief Executive Officer to accept the tender and negotiate, execute and administer the contract. This delegation is being sought as it is anticipated that the total contract value of this contract will exceed the \$5M limit on the current delegation to the Chief Executive Officer to accept tenders.

Key Implications

Financial Implications

18. The market has indicated that the retail gas price increase of over 300 per cent compared to pre-2022 rates could be maintained for several years.
19. Due to budget timings, the increased cost was not included in 2022/23 budget. Assumptions behind this shortfall are provided in Confidential Attachment A. The City will attempt to absorb any shortfall but may request additional funds from CEO Contingency.
20. The revised pricing will be included in the annual operating cost forecast for Gas and inform the next iteration of the Long Term Financial Plan

Relevant Legislation

21. Local Government Act 1993.
22. Local Government (General) Regulation 2021.
23. Local Government Act 1993 - section 377(1) allows Council to resolve to delegate the award of this tender to the Chief Executive Officer.
24. Local Government Act 1993 - Section 10A provides that a council may close to the public so much of its meeting as comprises the discussion of information that would, if disclosed, confer a commercial advantage on a person with whom the council is conducting (or proposes to conduct) business.

25. Attachments A, B and C contain confidential commercial information which, if disclosed, would:
 - (a) confer a commercial advantage on a person with whom Council is conducting (or proposes to conduct) business; and
 - (b) prejudice the commercial position of the person who supplied it.
26. Discussion of the matter in an open meeting would, on balance, be contrary to the public interest because it would compromise Council's ability to negotiate fairly and commercially to achieve the best outcome for its ratepayers.

Critical Dates / Time Frames

27. The City's current agreement for the supply of Retail Natural Gas that covers the Large Market accounts within the City's portfolio is set to expire on 30 June 2023.
28. The City will continue to review market conditions and call tenders at the estimated optimal timing for a new Large Market Gas Supply Contract.

Options

29. The City has the following options in regard to the Large Market natural gas retail supply contracts:
 - (a) delegate authority to the Chief Executive Officer to award the tender to enable staff to engage with the market when appropriate. This is the recommended option as it is expected to achieve the best value for money outcome for Council.
 - (b) continue without a pre-approval for a predetermined contract amount. This option is not recommended because the City would be unable to execute the contract within an anticipated short validity period of the offer of approximately one week.
 - (c) allow the City to be placed on default rates post from July 2023. This is not recommended as it would expose the City to 20 to 30 per cent greater than procured rates.
 - (d) utilise SSROC to undertake procurement activities on City's behalf. This is not recommended as the City requires active involvement in tender process and discussion with potential retailers regarding site complexities.

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Chief Operating Officer

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