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26 April 2019

Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Submitted online

Dear Sir/Madam,

Consultation on DWGM Improvement to AMDQ Regime

Lochard Energy, owner/operator of the Iona Underground Gas Storage in Western Victoria, wishes to provide its views on the potential effects of changes to the AMDQ Regime suggested in the Commission's Consultation Paper on: DWGM Improvement to AMDQ Regime. Lochard Energy thanks the Commission for this opportunity.

Lochard Energy supports initiatives that increase its customers' operational flexibility and reduce their risk in the DWGM. The AMDQ regime is part of DWGM risk management and is complex and hard to grasp fully. Lochard Energy considers that the proposed structural changes to AMDQ, namely the introduction of entry and exit AMDQ in place of current AMDQ and AMDQ cc, will benefit its customers. Introduction of varying tenures for AMDQ and AMDQ trading will further enhance flexibility, especially coupled with the calculation of AMDQ on shorter-term basis leading to more AMDQ rights being available.

Lochard Energy considers the short-term changes proposed by the AEMC could improve the efficient use of pipeline capacity and interconnecting facilities, however Lochard is unsure of whether the changes would lead to efficient levels of investment – a situation Lochard and its customers face with the capacity of Southwest Pipeline. In our view, a clear capacity price signal is the best means and leading indicator to investment.

If you wish to discuss any aspect of this submission in further detail, please contact Ee Siew Ong, Commercial Analyst, at eesiew.ong@lochardenergy.com.au or on 03 8646 0507.

Yours Sincerely,

Becky Nguyen
Commercial Manager

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1. Introduction

1.1 AEMC Consultation

On 14 March 2019 the Australian Energy Market Commission (AEMC) released a series of consultation papers requesting submissions on proposed changes to the Declared Wholesale Gas Market (DWGM) in Victoria. The proposed changes were submitted by the Victorian Government following the AEMC's 2017 review of the DWGM (the Review).

The Review recommended the adoption of a target model which would unbundle the three roles currently undertaken through the DWGM:

1) gas commodity trading
2) balancing responsibility
3) pipeline capacity allocation.

The Review recognised that implementation of this model would take time and suggested a staged approach in which incremental changes consistent with the above be implemented in the short-term. The incremental changes, requested by the Victorian Government, are:

1) **providing a cleaner wholesale market price** by including the costs currently intended to be recovered by common and congestion uplift in the market price, while retaining separate pricing of temporal constraints
2) **establishing a forward trading exchange over the DTS (Declared Transmission System)** while retaining the existing daily DWGM
3) **improving pipeline capacity allocation and introducing capacity rights trading** by:
    a) introducing separate, tradable entry AMDQ rights and exit AMDQ rights
    b) introducing an exchange to improve secondary trading of AMDQ rights (permanent transfer) and benefits (temporary transfer)
    c) making AMDQ available for a range of different tenures.

This submission, which focuses primarily on the changes to AMDQ, has been prepared in response to the AEMC's request.

1.2 The Iona Underground Storage Facilities

Lochard Energy is the owner/operator of the Iona Gas Plant, a facility near Port Campbell in Western Victoria which comprises a gas processing plant and underground gas storage reservoirs, referred to as Iona Underground Storage (Iona). Iona is the only underground storage in Eastern Australia that provides access to third parties.

Iona interconnects with the SEAGas Pipeline, the Mortlake Pipeline, and the Victorian Transmission System (VTS) at the Southwest Pipeline. The VTS connection creates the interface between firm capacity contracts at Iona, the Victorian "Market Carriage" system and the AMDQ regime.

1.3 The Role of Iona in the Eastern Australian Gas Market

Iona provides customers (market participants) with capacity to balance supply and demand additional to that provided by gas production and gas demand management, by diverting gas supply from the market to storage and later withdrawing it from storage to the market.

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The current Iona withdrawal capacity of 480 TJ/day can meet up to 20% of south eastern Australian co-incident peak day demand (circa 2200 TJ) or 36% of Victorian peak day demand (circa 1200 TJ).

Projected declines in peak gas production in the south east[1] suggest that further storage capacity may be required in the near term, and Iona is in a position to provide this in competition with other storage options and sources of additional peak supply. To do so however it will be dependent on commensurate increases in the flow capacity in the SWP pipeline in both easterly (injections into SWP) and westerly (withdrawals from SWP) directions.

2. Iona Capacity Expansion and the AMDQ Regime

Iona and its customers experience difficulties with the current AMDQ regime at both the strategic planning and operational levels.

2.1 Strategic Capacity Planning

Under the current regime, AMDQ (or AMDQ cc) provides a weak investment signal for DTS pipeline capacity expansion. This, combined with the 5-year access arrangement period and the fact that DWGM otherwise lacks clear capacity price signals, results in delay in investment in DTS and creates uncertainty for investment and contracting in facilities interconnecting with DTS.

Currently, it is difficult for Iona customers to align their requirements in quantity and duration for injection and withdrawal capacity at Port Campbell with the injection and withdrawal capacities of the SWP. The situation is acute for new and smaller customers who acquire Iona capacity at the time when all AMDQ is fully contracted and unavailable for the 5-year period.

Despite the slight increase in the AMDQ cc price over the years, this, in itself, has not led to material SWP capacity expansion. In the current Access Arrangement (2018-2022) period, the Iona customers identified significant incremental injection capacity requirements into the SWP at Port Campbell. In response to customer requirements, Lochard Energy is committed to invest in additional capacity, which will enable Iona injection capacity increase to 520 TJ/day by 2021. This compares to current SWP injection capacity of 413TJ/day, which is scheduled to increase to 449 TJ/day in 2022 after construction of the Western Outer Ring Main (WORM)[2].

This discrepancy creates a systemic capacity mismatch between Iona and SWP, potentially limits the ability of customers to use their positions in Iona effectively, and strategically impacts further Iona capacity expansion to 570TJ/d, planned for 2022 onwards.

Timing of resolution of the strategic issues is becoming urgent. Both the VGPR and the Gas Statement of Opportunities (GSOO) have identified tightening gas supply from known resources, with gas shortfalls possible by the mid-2020s. New supply from that date must be committed several years earlier to allow for construction, probably no later than 2022, hence the decision making processes, including market changes, must be in place to support that timeframe.

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[1] 2019 Victorian Gas Planning Report, AEMO, March 2019

[2] 2019 Victorian Gas Planning Report, AEMO, March 2019

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2.2 Separate Entry and Exit AMDQ Rights

The proposed separation of AMDQ rights into entry and exit captures the current rights more precisely. This is a good step in simplifying the existing arrangements and should therefore result in more efficient usage of those rights. The demand for and price of the entry and exit rights are likely to provide better information on which flow direction capacity is required and enable market-led investment in DTS by redefining the rights as between the DTS and specific injection/withdrawal points.

The value of AMDQ rights in providing hedge against congestion uplift or curtailment is an important feature that needs to be retained. This feature affirms the AMDQ holders' right to flow gas at the connection point in an otherwise market-carriage system. Until a clearer and more effective capacity price signal is available, the price of AMDQ rights, together with the congestion uplift, are both indicators of demand for capacity.

2.3 Calculation of the amount of AMDQ

In absence of further investment in SWP to enable capacity matching with Iona and other injection/withdrawal points in SWP, Lochard considers there could be significant benefits in the proposed calculation of the amount of AMDQ on a shorter term, i.e. annually, seasonally, or quarterly. This would release the capacity existing in the system to the customers who need it on a short-term basis and at the time it is needed. This approach has the potential of optimising the existing operating capacity in the DTS and, in theory, could alleviate some pressure on immediate investment in further capacity.

Additionally, this approach also makes it possible for Iona to release and utilise seasonal capacity in the storage facility, a win-win outcome for both systems.

2.4 AMDQ contract duration

Currently, AMDQ is released for long periods of time (five years or in perpetuity), which most likely mismatches with users' duration or quantity requirements and acts as barrier for shorter-term and small users.

Lochard proposes AEMC to consider, in consultation with the market participants, separate tranches of AMDQ being released for different terms, i.e. seasonal, 1 year, 3 years and 5 years. The efficiency of various contract tenures should also be enhanced by secondary trading. This, combined with a simple and low-cost process to facilitate the buying, selling, and trading of AMDQ rights, could provide the ease of seeking out AMDQ buyers and sellers anonymously and lower the search cost.

However, the contract duration and tradability of AMDQ rights are unlikely in themselves to resolve the fundamental issue of capacity mismatch at some DTS interconnection points, until sufficient investment is made through the regulatory or a market-led process.