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Australian Energy Market Commission
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Dear Australian Energy Market Commission

GRC0049-National Gas Amendment (DWGM Simpler Wholesale Price) Rule 2019

Meridian Energy Australia Pty Ltd and Powershop Australia Pty Ltd (MEA Group or Powershop) thanks the Australian Energy Market Commission (AEMC) for the opportunity to provide comments on the National Gas Amendment (DWGM Simpler Wholesale Price) Rule 2019 consultation paper (the Paper).

The MEA Group is a vertically integrated generator and retailer focused entirely on renewable generation. We opened our portfolio of generation assets with the Mt Mercer and Mt Millar wind farms. Subsequently, in early 2018 we acquired the Hume, Burrinjuck and Keepit hydroelectric power stations, further expanding our modes of generation. We have also supplemented our asset portfolio by entering into a number of power purchase agreements with other renewable generators, and through this investment in new generation we have continued to support Australia's transition to renewable energy. Powershop has also been active in supporting community energy initiatives, including providing operational and market services for the community-owned Hepburn Wind Farm, supporting the Warburton hydro project, and funding a large range of community and social enterprise energy projects through our Your Community Energy program.

In 2018, Powershop Australia Pty Ltd entered into the Victorian residential gas market to further promote competition and contribute towards a fair and effective retail market. Powershop is particularly cautious of any rule changes which do not promote customer interests or acknowledge fully the wholesale environment in which energy retailers participate.

Simpler Wholesale Price

The AEMC has invited industry to comment on two rule change requests:

- The Victorian Government rule change - The Victorian Minister for Energy, Environment and Climate Change submitted a rule change request that "seeks to improve risk management options in the Victorian Declared Wholesale Gas Market (DWGM) by 'socialising' or 'smearing' the recovery of congestion uplift payments across market participants, instead of the current approach that aims to recover congestion uplift payments from those that caused the congestion"; and

- The Energy Australia rule change - The Energy Australia rule change request seeks to amend the National Gas Rules (NGR) to enable AEMO to include constraints within the Declared Transmission System (DTS) in the pricing schedule for the Victorian DWGM.

Despite the best intentions of the AEMC to address these two rules together in the Paper, the MEA Group does not believe that these two rules changes address similar issues. We believe their merits should be assessed and considered in isolation. Whilst the combining of rule changes may act to increase the efficiency and timeliness of the rule change process, the MEA Group believes more effective assessment can be conducted without having to infer the inter-connected nature of the Victorian wholesale gas market.

The MEA Group has addressed responses to each rule change below.

The Victorian Government rule change

This rule change considers that congestion uplift is outdated and now serves no purpose in today's dynamic East-Coast Market. The two key reasons why congestion uplift should be replaced as outlined in the Paper are:

- It's difficult to hedge and there are limited risk management options; and
- There was \$3.1m of congestion uplift costs in 2016 and there might be more in future years.

The DWGM is a gross pool market and utilises a market carriage arrangement to access transmission rights. The markets' original design was to allow participants to manage imbalances and ensure sufficient transmission rights are contracted for participants to deliver gas to market. There are some important features of the DWGM to understand before entering risk management solutions in financial derivatives or otherwise.

The DWGM is a balance of day market where the market price at each schedule represents the cost of supplying that gas should supply and demand conditions remain unchanged. This is an important feature of the DWGM and along with the deviation settlement and uplift mechanisms; the mechanics of the market are as follows:

- if a participant is scheduled gas at the beginning of the day, they get paid for the gas that is scheduled to be delivered for the balance of the day;
- if participants do not inject or withdraw gas as per their market schedule then they are exposed to deviation payments (difference between scheduled injections and withdrawals vs actual injections and withdrawals) and;
- in the case where AEMO needs to schedule gas out of bid merit order, ancillary payments are generated and allocated according to the various uplift payment types.

As the Paper has acknowledged, congestion uplift can be managed by contracting the Authorised Daily Maximum Quantity (AMDQ) and ensuring AMDQ is validated by injecting gas at a close proximity point. The ability of a market participant to manage congestion uplift risk therefore is subject to the participant being able to contract AMDQ (transportation rights) and gas supply. This should be viewed as a reasonable component of a market in which a retailer buys goods and transports them to market.

The MEA Group therefore considers that the key factors that drive the efficiency of this market are the ability to contract competitively priced gas supply and AMDQ.

The Paper suggests that the effectiveness of risk management options is limited as the market price for gas does not reflect the wholesale cost of gas. The Paper states that the wholesale cost of gas is a combination of the spot price and the congestion uplift cost so this limits the effectiveness of financial derivative hedges.

The MEA Group does not consider socialising congestion uplift will result in a 'simpler' market price and does not believe this will promote the use of risk management solutions such as financial derivatives.

All ASX traded Victorian gas financial contracts are struck against the 6am beginning of day price (BOD). No congestion uplift has ever been applied in the 6am price.

Socialising congestion uplift only shifts cost to other parts of the market. While it may be a simpler product for the financial buyer it might not be simpler for the financial sellers to manage, any increase in risk would be built into the price of the contract.

The ASX Victorian gas contract is actively trading, and as at 17 April 2019 aggregate open interest between the Jun-19 to Dec-20 quarters was 505 lots. On most days for 2019 there has been a market (bids and offers) on the ASX for Victorian gas futures quarterly contracts.

Constitution and appropriateness of congestion uplift payments

To effectively address any issues with market operations associated with congestion, the way in which different participants may view congestion must be ascertained. The Paper, in reference to a particular event, states:

“The amount allocated to market customers as congestion uplift payments was according to the rules, although the nature of the congestion, being caused by an unplanned outage of a major facility, does not accord well with many stakeholders’ understanding of what ordinarily constitutes congestion on gas pipelines.”

The MEA Group takes a different view from this. The DWGM is a balance-of-day market and at each market schedule gas is scheduled for the balance of the day. On 1 October 2016 market participants were scheduled at BOD to inject a volume of gas over the following 24 hours. When a market participant fails to inject gas in accordance with their scheduled quantities for any reason, unplanned outage or otherwise, there is a requirement for the market to replace this gas.

On 1 October 2016 a supply interruption occurred and gas was required to be scheduled out of bid merit order. The participants who failed to meet their scheduled injections from Longford created the requirement for more gas to be injected from other supply sources and through other pipelines. Failure to follow scheduling instructions can create congestion in other parts of the market.

This was experienced on the 1 October as a greater amount of pipeline capacity was required from other parts of the market to replace the originally scheduled Longford gas. The market allocated costs correctly such that the market participants who failed to follow scheduling instructions and failed to validate their AMDQ, were allocated congestion uplift.

Conclusion

The MEA Group believes that socialising congestion uplift is inconsistent with the National Gas Objective and will inhibit efficient investment or operation of the gas market. A market that allocates on a ‘cost-to-cause’ basis supports effective procurement from reliable sources and acts to increase system security and integrity.

Naturally, it would be expected that participants would contract less reliable or lower priority gas to achieve cost reductions, in the knowledge that other participants will be similarly accountable for any losses resulting from poor performance of such contracts. This would act to diminish system integrity and may contribute towards greater volatility and costs associated with serving customers. Uncertainty over cost structure in this market arrangement may also indirectly limit the likelihood of new entrants joining the market in the long term.

Energy Australia rule change

The MEA Group believes that constraints internal to the DTS should be included in the pricing schedule in order to avoid adverse outcomes as described in the Paper. We support the rule change proposal for rule 221(4) of the NGR to be amended so that:

- where a system constraint would act to physically limit scheduled withdrawals from the DTS, AEMO will apply a constraint to represent this in the pricing schedule; and
- a differential between the pricing schedule and operating schedule will remain in cases where constrained on injections are required.

If you have any queries or would like to discuss any aspect of this submission please do not hesitate to contact me.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'J. Mulder'.

Justin Mulder
Head of Energy Markets
Meridian Energy Australia
Powershop Australia