3 October 2022

Anna Collyer
Chair
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Submitted online: www.aemc.gov.au

Dear Ms Collyer

DWGM interim LNG storage measures – Consultation Paper

Origin Energy Limited (Origin) welcomes the opportunity to provide comments on the Australian Energy Market Commission's (AEMC) Declared Wholesale Gas Market (DWGM) interim LNG storage measures Consultation Paper.

Origin agrees AEMO should have the relevant tools to effectively manage the market. However, we do not consider the proposed rule is necessary or appropriate. This is because it is unclear what deficit in the current framework the proposed rule would address, and the rule would likely have the perverse effect of reducing incentives for market-led procurement of storage capacity, exacerbating the issue it is expected to resolve. Should the rule proceed, it would be crucial to design the framework with a view to minimising the potential for market distortion. We consider this would be best achieved by: explicitly linking the target level of capacity procured to an assessment of security / reliability of supply risk; recovering costs from causers; operationalising AEMO's injection of contracted capacity through directions rather than bidding capacity into the Declared Wholesale Gas Market (DWGM) directly; and ensuring the mechanism is only in place for a temporary period.

1. There is no clear deficiency with the existing framework

Market participants have strong incentives to ensure they can cover their peak demand to avoid exposure to purchasing spot gas at potentially high prices. Access to alternate sources of supply provides participants with a range of options as to how to achieve this and efficiently manage their gas portfolios. The Iona underground storage facility has a critical role to play in this respect, as it allows for storage of large volumes of gas (approximately 23.5 PJ) to support peak winter withdrawals. In comparison, the Dandenong LNG storage facility stores a relatively small volume of gas (approximately 680TJ) and is therefore typically used to address short-term demand peaks, maintain system security and for emergency management.

Having regard to the above, it is important to note the Iona underground storage facility is close to fully contracted over the period from 2021 to March 2025, with the level of contracted capacity increasing by more than 2,500 TJ relative to June 2020 levels.[1] In contrast, the level of contracted capacity at the Dandenong LNG facility has reduced by only 300-400 TJ over the same period.[2] We therefore do not agree that lower contracting at the Dandenong LNG facility is indicative of an underlying market failure

[1] ACCC, 'Gas inquiry 2017-2025 – Interim report', July 2022, pg. 89.
[2] Ibid, pg. 91.

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that would warrant the introduction of a procurer of last resort function, particularly for reliability purposes. Rather, it is more likely a reflection of the cost-effectiveness of the service relative to alternate supply options.

The size of the facility also means it would only likely play a limited role in supporting reliability of supply in practice and is therefore better suited for security type services. To that end, National Gas Rule (NGR) 343 already provides AEMO with a range of intervention tools for managing security of supply, including directing participants to inject gas and also utilising the LNG facility. It is under this framework that AEMO procured 60 TJ of capacity at the Dandenong LNG facility on 19 January 2022 to help mitigate an identified threat to system security during winter 2022.

2. Establishing a formal procurer of last resort function would be distortionary

As noted in the Consultation Paper, the ACCC has observed the decline in LNG stock and contracted capacity at Dandenong coincided with a change in the facilities contracting model.[3] The ACCC further noted this change resulted in a 44-46 per cent increase in prices payable for storage at the facility.[4] Where the cost-competitiveness of the service (relative to other supply sources) is the primary driver for reduced contracting, the proposed rule would likely exacerbate the perceived underutilisation by market participants and lead to less efficient utilisation of the facility. This is because the operator would have reduced incentive to improve the cost competitiveness of the service if AEMO is willing to buy all uncontracted capacity. Under a generalised cost recovery approach (e.g. through market fees), participants with contracted DLNG capacity would also be exposed to additional charges associated with AEMO's procurement, undermining the overall benefits of proactively contracting the capacity.

Concerns around the efficiency of AEMO-led procurement were a key reason for the removal of AEMO's broad storage contracting powers in a separate 2010 rule change process. At the time, the AEMC concluded that liberalising the use of the Dandenong LNG storage facility was likely to promote the efficient operation and use of that facility and may ultimately result in price benefits for end-use customers.[5] The proposed rule seeks to mitigate against the risk that AEMO-led procurement would crowd out other market participants by allowing AEMO to relinquish capacity to the LNG storage provider if a market participant seeks to acquire that capacity. However, this design feature would not address the underlying disincentive for market participants to procure Dandenong LNG capacity created by the rule.

The proposed rule would also result in AEMO becoming a trading market participant, given it would need to procure gas from the spot market to fill its storage capacity and subsequently bid volumes into the DWGM at the market price cap (MPC) for scheduling. It would be important for the AEMC to consider the appropriateness of AEMO participating in a market it is responsible for operating, given AEMO would effectively be competing with market participants in procuring gas from the DWGM and there may be a level of information asymmetry between those parties that could distort efficient market outcomes.

3. The design of the proposed rule would need to be revised if progressed

Given the above concerns, we do not consider it necessary or appropriate to implement the proposed rule. Where progressed, we have provided comments on specific design elements of the propsoal with a view to mitigating the likely level of market distortion.

- Target level of capacity: We recognise there is no formal gas-reliability standard and consideration is being given to the development of such a metric as part of a separate reform package currently

[3] Ibid, pg. 89.
[4] Ibid.
[5] AEMC, 'Dandenong Liquefied Natural Gas Storage Facility – Rule Determination', 16 December 2010, Pg. 13.

being considered by the Commonwealth Government. However, we do not consider it appropriate to provide AEMO with the ability to procure *any* level of uncontracted capacity regardless of need. The target level of capacity should be explicitly linked to an assessment of security / reliability of supply risk and transparently reported by AEMO prior to it commencing capacity procurement.

- AEMO trading: We agree AEMO / APA's schedule for withdrawing gas from the spot market to fill storage capacity should be transparently conveyed to market participants. Injection of AEMO's contracted LNG capacity should also be treated as an intervention and operationalised through directions as a last resort measure, and not through participation in dispatch processes. This would minimise the impact of the injections on market outcomes and is consistent with the view outlined by AEMO in its March 2022 Declared Wholesale Gas Market – Intervention Report which noted that '*… it is appropriate that when AEMO injects gas into the market it is through an intervention and not as an injection bid*.'[6] Bidding contracted capacity at the MPC is also unlikely to materially impact reliability, given voluntary load curtailment is likely to occur at that price in any case.

- Cost recovery: We recommend the AEMC considers allocating costs to net withdrawers during the winter period. This would be a similar approach to allocating procurer of last resort (PoLR) costs under the Retailer Reliability Obligation (RRO) and ensure costs are only recovered from those participants that are notionally creating the need for the reserve procurement. Alternately, consideration could be given to an approach that allocates a lower portion of costs to parties that have contracted capacity at the facility.

- Duration of the rule: We agree any rule should only be applied on a temporary basis and not extend beyond winter 2025.

Where the rule is to be expedited, the AEMC should seek to follow an equivalent process to that applied under the APC rule change, whereby a Directions Paper is released prior to a Final Report. This would provide market participants with an opportunity to consider the AEMC's initial analysis on key aspects of the proposed rule. This includes the approach to cost recovery and how the capacity would be used, as well as the likely impact of the rule on market efficiency, noting there is little detail on these matters in the initial Consultation Paper.

If you wish to discuss any aspect of this submission further, please contact Shaun Cole at shaun.cole@originenergy.com.au or on 03 8665 7366.

Yours Sincerely,

Steve Reid
General Manager, Regulatory Policy

[6] AEMO, 'Declared Wholesale Gas Market – Intervention Report – Notice of threat to system security', March 2022, pg. 10.