



Victorian Declared Wholesale Gas Market Review

Submissions open on Discussion Paper

The Australian Energy Market Commission has today published a discussion paper to provide stakeholders with an opportunity to contribute to the development of the next layer of detail on the Southern Hub model.

Having regard to the unique physical characteristics of the Victorian Declared Transmission System (DTS), this discussion paper is based around four key themes and focuses on the key design issues relevant to the Southern Hub model which need to be addressed ahead of the Final Report. Specifically, this paper therefore focuses on the following:

- **Managing capacity at the Southern Hub:** The new functions which would be created by the Southern Hub are identified and the allocation of these roles between APA GasNet and the Australian Energy Market Operator (AEMO) is discussed, having regard to a number of trade-offs which need to be considered. The paper also discusses the importance of the process for calculating baseline (and above-baseline) transmission capacity in considering the allocation of roles at the Southern Hub.
- **Capacity allocation mechanisms:** The various mechanisms available for allocating existing baseline capacity at the Southern Hub, and for triggering incremental capacity investments, are considered. The paper outlines the general principles behind each allocation mechanisms, along with the characteristics of existing entry and exit points to the DTS. It then presents the Commission's preliminary view on the most appropriate mechanism for allocating transmission capacity at entry and exit points within the Southern Hub. A discussion on transitioning AMDQ and AMDQ cc concludes this section.
- **Capacity pricing and revenue:** How gas pipeline services provided under the entry-exit system could fit within the existing regulatory framework for gas pipelines is briefly discussed and the general process followed when setting regulated capacity tariffs in entry-exit systems is outlined. The paper highlights the factors that need to be considered when designing tariffs for entry and exit points and considers how this could be done at the Southern Hub.
- **Balancing:** Gas balancing at the Southern Hub is considered, including the principles for the balancing arrangements and the characteristics of the DTS. The trade-offs that need to be considered in respect of the balancing period, financial incentives and procurement of balancing gas are also discussed. Two models based on different European approaches are considered: continuous market-based balancing and fixed period market based balancing.

Feedback from stakeholders will be used to inform the Commission's final recommendations for the Victorian DWGM Review which will be presented to the COAG Energy Council in mid-2016. We welcome responses on any of the matters outlined in the discussion paper. However, in light of the tight timeframes for consultation, the discussion paper sets out a few questions intended to help focus submissions.

Submissions are due by **29 March 2016**.

Background

The AEMC developed a package of reform for the Victorian DWGM and associated market carriage arrangements which govern access to the DTS. These reforms were set out in the Draft Report for the Review of the Victorian Declared Wholesale Gas Market, presented to the Council of Australian Governments (COAG) Energy Council on 4 December 2015. The package of reform involves:

- transitioning from the DWGM where trading and balancing occurs on a mandatory, operator led-basis, to the new 'Southern Hub' model where trading and balancing would occur on a voluntary, continuous basis and where the hub operator plays only a residual role; and
- supporting this new form of trading with a system of entry and exit rights which, collectively, contribute to gas being able to be traded independently of its location in the system.

The proposed changes are anticipated to fundamentally improve the outcomes of the Victorian gas market by providing participants with greater flexibility to physically trade gas in the market, and establishing the preconditions required for financial risk management products to develop. The changes will also create market-driven signals for investment in the pipeline system, a feature currently absent from the Victorian DWGM.

Importantly, the proposed reforms will not undermine elements of the Victorian market that have been beneficial both in terms of stimulating a competitive retail gas market and safeguarding the security of gas supply for Victorian customer.

Trading at the "virtual hub" formed by the DTS will provide new entrant retailers and large industrial users with greater flexibility in how they buy and sell gas than the current mandatory gross pool arrangements in the DWGM. Retailers and large users will be able to enter into trades with any other party, irrespective of their location on the DTS, for any period of time. This trading can occur either bilaterally or through the exchange, which will represent a low cost, anonymous and transparent trading mechanism with no counter-party risk.

The recommended new market design would provide more options to new entrants to hedge price risks through either physical or financial trades at the virtual hub, with a wider range of counter-parties. This optionality lowers barriers to entry and promotes competition, creating benefits for consumers.

Further, residual balancing arrangements would mean that if a party was not fully contracted, the system operator would obtain gas on its behalf and charge the party for this. This will ensure that network pressures are maintained within safe operational limits and that gas continues to flow to consumers, as well as providing a fall-back option for participants to purchase gas.

Broader reforms

The proposed reforms to the Victorian gas market form part of the AEMC's broader roadmap for the development of the East Coast Gas Market. A Final Report for the Victoria DWGM Review and for the East Coast Wholesale Gas Market and Pipeline Frameworks Review (East Coast Review) will be delivered to the COAG Energy Council in May. Both reports will provide further detail on the broader East Coast Gas Market reform package, including on the recommendations for a new Southern Hub in Victoria.

As part of the stakeholder consultation process, the AEMC is also consulting on a number of issues relevant to the broader East Coast Gas Market reforms, with particular focus on the pipeline capacity market recommendations. These matters are considered in a separate discussion paper also published today and available on the AEMC website.

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