



Australian Energy Market Commission

RULE DETERMINATION

National Gas Amendment (Calculation of Interest for Gas Markets) Rule 2010

Rule Proponent(s)

AEMO

Commissioners

Pierce
Henderson
Spalding

4 November 2010

JOHN PIERCE

Chairman

For and on behalf of the Australian Energy Market Commission

**RULE
CHANGE**

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About the AEMC

The Council of Australian Governments, through its Ministerial Council on Energy (MCE), established the Australian Energy Market Commission (AEMC) in July 2005 to be the rule maker for national energy markets. The AEMC is currently responsible for rules and providing advice to the MCE on matters relevant to the national energy markets. We are an independent, national body. Our key responsibilities are to consider rule change proposals, conduct energy market reviews and provide policy advice to the Ministerial Council as requested, or on AEMC initiative.

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Summary

The Commission's determination

The Australian Energy Market Commission (AEMC or Commission) makes this final Rule determination and attached Rule on Australian Energy Market Operator Limited's (AEMO's or Rule Proponent's) Rule Change Request regarding the calculation of interest for gas markets. The Commission's determination is to make the Rule proposed by the Rule Proponent, with amendments which better reflect the description of the proposed Rule in the Rule Change Request.

Summary of the Rule Change Request

On 30 August 2010, AEMO submitted a Rule Change Request to the AEMC in relation to the methodology to be applied in calculating interest in the National Gas Rules (NGR or Rules), particularly the Declared Wholesale Gas Market (DWGM) Rules, the Short Term Trading Market (STTM) Rules and the Natural Gas Services Bulletin Board (BB) Rules. The Rule Change Request sought to apply a consistent simple interest methodology for the calculation of interest in the NGR. The Rule Change Request also sought to update and centralise the definitions of "interest rate" and "default interest rate" in the NGR.

Reasons for the Commission's decision

The Commission's reasons for making this Rule are:

- it provides regulatory certainty for gas market participants by removing any ambiguity and improving transparency in the methodology to be applied in calculating interest in the NGR;
- it provides operational and system efficiencies for the Rule Proponent by ensuring the same methodology can be used to calculate interest and by applying one definition of "interest rate" under the NGR which is, in practice, the same rate as that applied by the Rule Proponent in the electricity market so that the Rule Proponent will not need to duplicate near identical processes in each market; and
- it avoids costs for gas market participants, and ultimately natural gas consumers (through increased prices), as the estimated costs of implementing changes to the Rule Proponent's settlement systems to calculate interest on a compound interest basis (which appear to exceed the expected benefits to participants if interest was calculated on such a basis) will not be incurred.

Consultation on the Rule Change Request

On 23 September 2010, the Commission gave notice under sections 303 and 304 of the National Gas Law (NGL) to initiate the Rule Change Request under the expedited Rule change process as a request for a non-controversial Rule. No objections to this process were received, so the Commission has assessed the Rule Change Request under the expedited process provided in section 304 of the NGL.

The consultation period for submissions on the content of the Rule Change Request closed on 21 October 2010. One submission was received. A summary of the issues outlined in that submission is provided in Appendix A.

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1 AEMO's Rule Change Request

1.1 The Rule Change Request

On 30 August 2010, Australian Energy Market Operator Limited (AEMO or Rule Proponent) submitted a Rule Change Request to the Australian Energy Market Commission (AEMC or Commission).¹ The Rule Change Request concerned the methodology to be applied in calculating interest in the National Gas Rules (NGR or Rules), particularly the Declared Wholesale Gas Market (DWGM) Rules², the Short Term Trading Market (STTM) Rules³ and the Natural Gas Services Bulletin Board (BB) Rules⁴.

1.2 Rule Change Request Rationale

The Rule Change Request sought to amend the NGR to apply a consistent simple interest methodology for the calculation of interest. Currently under the Rules, there is an inconsistent approach to the calculation of interest.

The DWGM Rules currently require the Rule Proponent to calculate interest using a compound interest methodology. This is inconsistent with the Rule Proponent's current practices for calculating interest, which are based on its systems and the agreed methodology for calculating interest under the Victorian Gas Industry Market and System Operations Rules (MSOR). The STTM Rules and BB Rules also require interest to be calculated in certain circumstances, but are silent on the methodology to be applied.

In addition, as the definition of "interest rate" varies between the DWGM Rules, STTM Rules and BB Rules and the definition of "default interest rate" is not used consistently, the Rule Proponent also sought to apply one definition of "interest rate" and "default interest rate" to these Rules, to be centrally located in the NGR.

1.3 Solution proposed by the Rule Change Request

The Rule Proponent proposed to address the above issues by making a Rule that:

- amends the relevant clauses of the DWGM Rules to calculate interest on compensation payments, adjustments to revised statements and overdue

¹ This Rule Change Request is available on the AEMC website, www.aemc.gov.au. This Rule Change Request replaced an earlier request submitted by AEMO on 31 May 2010. The earlier request only discussed changes to the Declared Wholesale Gas Market Rules and the Short Term Trading Market Rules. The earlier request was not considered by the Commission.

² Rules in Part 19 of the NGR.

³ Rules in Part 20 of the NGR.

⁴ Rules in Part 18 of the NGR.

amounts using a simple interest methodology, rather than a compound interest methodology as currently prescribed in the Rules;

- amends the relevant clauses in the STTM Rules to remove any ambiguity and clarify that interest is to be calculated on a daily basis using a simple interest methodology;
- amends the relevant clauses in the BB Rules to clarify that interest is to be calculated on a daily basis using a simple interest methodology;
- updates the definition of "interest rate" to refer to a 1 month Bank Bill Swap Reference Rate (BBSW) for the DWGM Rules, STTM Rules and BB Rules; and
- centralises the definitions of "interest rate" and "default interest rate" for the DWGM Rules, STTM Rules and BB Rules.

1.4 Relevant background

Given the Rule Proponent's rationale for its Rule Change Request, the current provisions in the NGR that are the subject of this Rule Change Request and a short history of these relevant provisions are set out in Appendix B.

1.5 Commencement of Rule making process

On 23 September 2010, the Commission published a notice under section 303 of the National Gas Law (NGL) advising of its intention to commence the Rule change process and the first round of consultation in respect of the Rule Change Request. A consultation paper prepared by AEMC staff identifying specific issues or questions for consultation was also published with the Rule Change Request. Submissions closed on 21 October 2010.

The Commission received one submission on the Rule Change Request as part of the first round of consultation. It is available on the AEMC website.⁵ A summary of the issues raised in this submission and the Commission's response to each issue is contained in Appendix A.

The Commission accepted that the Rule Change Request was a request for a non-controversial Rule. Accordingly, the Commission decided to expedite the Rule Change Request under section 304 of the NGL, subject to any written requests not to do so. The closing date for receipt of written requests was 7 October 2010.

No written requests not to expedite the Rule Change Request were received. Accordingly, the Rule Change Request was considered under an expedited process under section 304 of the NGL.

⁵ www.aemc.gov.au.

2 Final Rule Determination

2.1 Commission's determination

In accordance with section 311 of the NGL, the Commission has made this final Rule determination in relation to the Rule proposed by the Rule Proponent. In accordance with section 313 of the NGL, the Commission has determined to make, with amendments, the Rule proposed by the Rule Proponent.

The Commission's reasons for making this final Rule determination are set out in section 3.1.

The *National Gas Amendment (Calculation of Interest for Gas Markets) Rule 2010 No. 2* (Rule as Made) is published with this final Rule determination. The Rule as Made commences on 4 November 2010. The Rule as Made is the Rule proposed by the Rule Proponent, with amendments. Its key features are described in section 3.2.

2.2 Commission's considerations

In assessing the Rule Change Request, the Commission considered:

- the Commission's powers under the NGL to make the Rule;
- the Rule Change Request;
- submissions received during consultation;
- the fact that there are no relevant Ministerial Council on Energy (MCE) statements of policy principles in relation to this Rule Change Request;⁶
- MCE communiqués and bulletins relating to the drafting of the DWGM Rules;⁷ and
- the Commission's analysis as to the ways in which the proposed Rule will, or is likely to, contribute to the achievement of the National Gas Objective (NGO).

2.3 Commission's power to make the Rule

The Commission is satisfied that the Rule as Made falls within the subject matter about which the Commission may make Rules.⁸ The Rule as Made falls within the matters set out in section 74 of the NGL as it relates to:

⁶ Under section 73 of the NGL, the AEMC must have regard to any relevant MCE statements of policy principles in making a Rule.

⁷ Specifically, the MCE seventh meeting communiqué, 2 April 2004, and MCE Bulletin No. 146, 24 February 2009.

- regulating AEMO's declared system functions and the operation of a declared wholesale gas market (section 74(1)(a)(v)); and
- regulating AEMO's STTM functions and the operation of the STTM of an adoptive jurisdiction (section 74(1)(a)(v)).

Further, the Rule as Made falls within the matters set out in Schedule 1 to the NGL as it relates to:

- the payment of money (including the payment of interest and the provision of related security) for the settlement of transactions for natural gas or services purchased or supplied through a regulated gas market operated and administered by AEMO (item 55L) because AEMO operates and administers the DWGM and STTM (each of which are "regulated gas markets") and is required to calculate interest in both of these markets; and
- the terms and conditions on which the persons, or classes of persons, mentioned in item 62 of Schedule 1 of the NGL may access the BB (item 63) because AEMO operates and provides access to the BB and is required to calculate interest in certain circumstances.

2.4 Rule making test

Under section 291(1) of the NGL the Commission may only make a Rule if it is satisfied that the Rule will, or is likely to, contribute to the achievement of the NGO. This is the decision making framework that the Commission must apply.

The NGO is set out in section 23 of the NGL as follows:

“The objective of this Law is to promote efficient investment in, and efficient operation and use of, natural gas services for the long term interests of consumers of natural gas with respect to price, quality, safety, reliability and security of supply of natural gas.”

For the Rule Change Request, the Commission considers that the relevant aspect of the NGO is: *"the efficient operation and use of natural gas services for the long term interests of consumers of natural gas with respect to price... of natural gas."*⁹

The Commission is satisfied that the Rule as Made will, or is likely to, contribute to the achievement of the NGO by providing incremental efficiency benefits. The Commission has concluded that the Rule as Made has an incremental efficiency benefit because:

⁸ The Rule as Made does not apply in Western Australia as the Rule as Made does not fall within the subject matters about which the Commission may make Rules under the Western Australian Application Act (the National Gas Access (WA) Act 2009). See section 2.5.

⁹ Under section 291(2) of the NGL, for the purposes of section 291(1) the AEMC may give such weight to any aspect of the NGO as it considers appropriate in all the circumstances, having regard to any relevant MCE statements of policy principles.

- it provides regulatory certainty for gas market participants by removing any ambiguity and improving transparency in the methodology to be applied in calculating interest in the NGR;
- it provides operational and system efficiencies for the Rule Proponent by ensuring the same methodology can be used to calculate interest under the NGR and by applying one definition of "interest rate" under the NGR which is, in practice, the same rate as that applied by the Rule Proponent in the electricity market so that the Rule Proponent will not need to duplicate near identical processes in each market; and
- it avoids costs for gas market participants, and ultimately natural gas consumers (through increased prices), as the estimated costs of implementing changes to the Rule Proponent's settlement systems to calculate interest on a compound interest basis (which appear to exceed the expected benefits to participants if interest was calculated on such a basis) will not be incurred.

The incremental efficiency benefits outlined above should place downward pressure on costs and promote productive efficiency benefits.

Under section 295(4) of the NGL, the Commission may only make a Rule that has effect with respect to an adoptive jurisdiction if satisfied that the proposed Rule is compatible with the proper performance of AEMO's declared system functions. The Rule as Made is compatible with AEMO's declared system functions because it enhances AEMO's ability to administer the declared wholesale gas market through improved clarity of the interest rate to be used in the relevant provisions and enables AEMO to continue calculating interest using a simple interest methodology, as is its current practice.

As the Rule as Made does not affect the allocation of powers, functions and duties between AEMO and a service provider for a declared transmission system, AEMO's consent to the making of the Rule is not required.

2.5 Application of the Rule as Made to Western Australia

The Rule as Made applies in each participating jurisdiction except Western Australia.¹⁰ For the reasons set out below, it does not apply in Western Australia as the Rule as Made does not fall within the subject matters about which the Commission may make Rules for Western Australia.

Under the National Gas Access (WA) Act 2009, Western Australia adopted a modified version of the NGL, known as the National Gas Access (Western Australia) Law and version 1 of the NGR.

¹⁰ Under section 21 of the NGL, the participating jurisdictions are the States, the Commonwealth, the Australian Capital Territory and the Northern Territory.

Under section 74 and Schedule 1 of the National Gas Access (Western Australia) Law, the AEMC has no specific rule making power in respect of the DWGM or the STTM.¹¹

While section 74 and Schedule 1 of the National Gas Access (Western Australia) Law provide for the AEMC to make Rules in respect of the Bulletin Board and the BB Rules have been adopted in WA, these provisions must be read subject to section 20A of the National Gas Access (Western Australia) Law which provides that "To the extent that a provision of this Law relates to the Natural Gas Services Bulletin Board, the provision does not apply before a date is fixed by the Minister." The Western Australian Minister has not fixed such a date. Until such a date is fixed, the Commission considers that it does not have the power to make Rules with respect to the Bulletin Board for Western Australia.

¹¹ The DWGM Rules and STTM Rules have not been adopted in WA.

3 Commission's reasons

The Commission has analysed the Rule Change Request and assessed the issues/propositions arising out of this Rule Change Request. For the reasons set out below, the Commission has determined that a Rule be made. Its analysis of the Rule proposed by the Rule Proponent is also set out below.

3.1 Assessment of issues

The Commission considers that there is merit in having a single approach to the calculation of interest and having consistent definitions of "interest rate" and "default interest rate" under the NGR. Currently, the Rules in this regard lack clarity in that they provide for a methodology for calculating interest that is not, in fact, applied by the Rule Proponent or they do not specify what the calculation methodology will be. A single approach to the calculation of interest would also result in operational and system efficiencies. Confirming that the methodology for calculating interest is on a simple interest basis would also avoid costs for participants (and ultimately consumers) in implementing changes to systems to provide for the calculation of interest on a compound interest basis.

To address these issues, a Rule is required to confirm and clarify the methodology to be applied under the DWGM Rules, STTM Rules and BB Rules. A Rule is also required to apply one consistent definition of "interest rate" and "default interest rate" throughout the NGR.

3.2 Rule as Made

The Rule as Made amends the following rules:

- in Part 1 (Preliminary) - rule 3;
- in Part 18 (the BB Rules) - rules 141, 194 and 195;
- in Part 19 (the DWGM Rules) - rules 200, 203, 238, 249 and 253; and
- in Part 20 (the STTM Rules) - rules 364, 466, 473 and 476.

The Rule as Made reflects the Rule Proponent's description of the proposed Rule in its Rule Change Request. In considering the Rule Change Request, the AEMC identified some inconsistencies between the Rule Proponent's description of the proposed Rule and the drafting of the proposed Rule.

The Rule as Made provides for the calculation of interest in the NGR based on a simple interest methodology. It also updates the definitions of "interest rate" and "default interest rate" to clearly identify the appropriate interest rate to be applied. The following amendments to the proposed Rule are consistent with the Rule Proponent's description of the proposed Rule in its Rule Change Request:

- for revised statements in the STTM Rules¹², interest is to be calculated as simple interest on a daily basis - the Rule Proponent has confirmed that its drafting of this clause in its proposed Rule incorrectly referred to "interest compounding monthly on the last day of each month";
- the definition of "interest rate" is further clarified to refer to the "1 month Bank Bill Swap Reference mid rate" - which is consistent with the Rule Proponent's current processes, as described in its Rule Change Request¹³, and clearly identifies for AEMO and all participants in the DWGM, STTM and BB the appropriate interest rate to be applied; and
- the location of the definitions of "interest rate" and "default interest rate" are provided in rule 3 and the definitions of these terms within Parts 18, 19 and 20 of the NGR will reference the definitions in rule 3 - the proposed Rule located these definitions in rule 3 as well as in the respective Parts of the NGR, and this amendment clarifies that these definitions will be defined in one location within the NGR.

In addition, amendments have been made to the proposed Rule to ensure consistency of language in the Rule as Made.

3.3 Civil Penalties

Civil penalty provisions are Rules or provisions of the NGL for which a fine is payable in respect of a breach. Rule 476(1) is prescribed as a civil penalty provision.¹⁴ The amendment to this rule is only to clarify the provision and does not place any additional requirements on a Trading Participant. The Commission does not intend to recommend to the MCE or Victorian Minister (in respect of the DWGM Rules) that rule 476(1) be no longer prescribed as a civil penalty provision or that any of the other rules as amended by the Rule as Made be prescribed as civil penalty provisions.

3.4 Conduct Provisions

Conduct provisions are Rules or provisions of the NGL for which any person (including the Australian Energy Regulator (AER)) may institute civil proceedings in respect of a breach.¹⁵ A person (other than the AER) who suffers loss or damage by conduct of another person in breach of a conduct provision may recover their loss or damage by action against the other person in a court.¹⁶

¹² Rule 473 of the NGR.

¹³ AEMO, Rule Change Request, p.5.

¹⁴ The civil penalty provisions are prescribed in the National Gas (Victoria) (Declared Systems Provisions) Regulations 2009 and the National Gas (South Australia) Regulations.

¹⁵ Under section 229(3) of the NGL.

¹⁶ Under section 233 of the NGL.

The Rule as Made amends Rule 476(1), which is prescribed as a conduct provision. The amendment to this rule is only to clarify the provision and does not place any additional requirements on a Trading Participant. The Commission does not intend to recommend to the MCE or Victorian Minister (in respect of the DWGM Rules) that rule 476(1) be no longer prescribed as a conduct provision or that any of the other rules as amended by the Rule as Made be prescribed as conduct provisions.

4 Commission's assessment approach

This chapter describes the Commission's approach to assessing the Rule Change Request in accordance with the requirements set out in the NGL (and explained in chapter 2).

In assessing this Rule Change Request, the Commission has considered the following issues:

- whether the impact of the proposed Rule would promote regulatory certainty for gas market participants within the NGR;
- whether the impact of the proposed Rule would improve system and operational efficiencies for the Rule Proponent; and
- the costs for gas market participants and consumers of natural gas if interest was calculated on a compound interest basis.

The Commission has focussed on these issues because they relate to the principles of good regulatory design and practice. The Commission seeks to apply the principles of good regulatory design and practice as it considers that the NGL has implications for the means by which the regulatory arrangements operate (in addition to their ends). In applying these principles, the Commission seeks to have regard to the need, where practicable, to:

- promote stability and predictability - Rules should be stable, or changes to them predictable, so that participants can plan and make informed decisions; and
- promote transparency - to the extent that intervention in the market is required, it should be based on, and applied according to, transparent criteria.

5 Regulatory certainty for participants

This chapter sets out the Commission's considerations regarding certainty for participants on the approach for calculating interest under the NGR.

5.1 Rule Change proponent's view

According to the Rule Proponent, in transitioning the MSOR to the DWGM Rules, amendments were made to the calculation of interest provisions to specify that interest is to be calculated on a compound interest basis. Under the MSOR, the calculation of interest provisions did not explicitly state that the interest should be calculated on a simple interest basis; however, this was the interpretation of the wording at the time the Rule Proponent's metering management system (MMS) was designed and implemented.¹⁷ The Rule Proponent also advised that all relevant interest payments have been calculated and paid on a simple interest basis since the Victorian wholesale gas market commenced in March 1999.¹⁸

In its Rule Change Request, the Rule Proponent referred to various examples of the lack of clarity around how interest is to be calculated under the NGR. For example:

- in clause 476(1) of the NGR (STTM Rules), interest is to be "...calculated on a daily basis..." - the Rule Proponent indicated that the clause is silent as to whether this is to be on a simple interest basis or a compound interest basis; and
- in clause 195(3) of the NGR (BB Rules), interest is "...accruing on a daily basis..." - the Rule Proponent advised that the clause may be interpreted as either interest compounding (and accruing) daily or as simple interest accruing daily.

The Rule Proponent considers that its amendments to the NGR promote regulatory certainty by increasing the clarity of the NGR and aligning the NGR to its current practices.¹⁹

In its Rule Change Request, the Rule Proponent also identified that the definitions of "interest rate" were inconsistent between Parts 18, 19 and 20 of the NGR, and some definitions referred to interest rates that no longer existed as specified. The Rule Proponent considered updating the definitions of "interest rate" and "default interest rate" in a consistent manner across the three Parts of the NGR would promote clarity, simplify the NGR, and ensure that the Rules are transparent and accurate. The Rule Proponent proposed a single definition of interest rate as follows:

¹⁷ The MMS calculates the interest payments for compensation amounts, revised statements and overdue amounts in the DWGM.

¹⁸ AEMO, Rule Change Request, p.2.

¹⁹ AEMO, Rule Change Request, p.16.

1. "Is a reference to the 1 month Bank Bill Swap Reference Rate identified by AEMO on its website most recently determined by the Australian Financial Markets Association.
2. If the above rate ceases to exist, or that rate becomes, in AEMO's reasonable opinion, inappropriate, the interest rate is a rate determined and published by AEMO."²⁰

The Rule Proponent proposed that the definition of "default interest rate" remain as "an interest rate of 2% above the interest rate".²¹

5.2 Stakeholder views

In its submission, TRUenergy supported the Rule Proponent's Rule Change Request.²² TRUenergy stated that it:

- "agrees with AEMO that the current wording of the interest rate facility in the National Gas Rules (as this facility applies to the DWGM) is in error as a result of the translation process from the original Market and System Operational Rules"²³;
- concurs with "AEMO that there is value in aligning this market element with similar provisions in the Rules for the Short Term Trading Market (STTM) and the National Gas Services Bulletin Board (BB)"²⁴; and
- accepts "AEMO's proposal to update the now obsolete interest rate reference source in the current DWGM, STTM and the BB."²⁵

5.3 Other relevant considerations

MCE Bulletin No. 146 indicates that:

- the exposure drafts of the DWGM Rules were "prepared on a minimal change basis, with the intention being to move the gas market rules to the national framework largely unchanged, except where necessary to apply the national governance framework"²⁶; and

²⁰ AEMO, Rule Change Request, p.11.

²¹ NGR rules 203 and 364.

²² TRUenergy submission, 1 October 2010, p.1.

²³ Ibid.

²⁴ Ibid.

²⁵ Ibid.

²⁶ MCE Bulletin No. 146, 24 February 2009, p.1.

- "the provisions relating to the Declared Wholesale Gas Market Rules are being reviewed to ensure they preserve existing arrangements fully".²⁷

The Commission notes that the published final consultation draft of the DWGM Rules, dated 2 February 2009, did not provide for interest calculated under the DWGM Rules to use a compound interest methodology. The relevant calculation of interest clauses in the published final consultation draft of the DWGM Rules were consistent with the similar MSOR clauses.²⁸

5.4 Commission's analysis and conclusion

Based on the MCE Bulletin and the published final consultation draft of the DWGM Rules, there appears not to have been an intention to amend the methodology for calculating interest at the time the MSOR was transitioned to Part 19 of the NGR. Rather, the intention was to clarify the methodology. As stated by the Rule Proponent, however, that clarification is inconsistent with the methodology actually applied in the Rule Proponent's MMS. It is also inconsistent with the approach the Rule Proponent was proposing to take for calculating interest under the STTM Rules and the BB Rules, both of which are silent on the methodology for calculating interest.

Similarly, the current definitions of "interest rate" used in the DWGM Rules, STTM Rules and BB Rules are inconsistent. In the case of the DWGM Rules and STTM Rules, the definitions refer to a source that is no longer available as specified.

The Commission also notes that the Rule Proponent consulted with relevant stakeholders in the DWGM, STTM and BB prior to submitting its Rule Change Request, and received no objections to its proposal. In addition, the only submission received on the Rule Change Request supported it.

The Commission concludes that applying one methodology for calculating interest in the NGR provides consistency and regulatory certainty to the Rule Proponent and participants, and that a simple interest methodology is appropriate, as it is currently applied.

The Commission accepts that the proposed definition of "interest rate" is consistent with the Rule Proponent's current practices. The Commission also considers it appropriate to amend this definition to further clarify that it refers to the mid rate quoted on the Australian Financial Markets Association (AFMA) website, as currently applied by the Rule Proponent.

²⁷ MCE Bulletin No. 146, 24 February 2009, p.2.

²⁸ Available on the MCE website, <http://www.ret.gov.au/documents/mce/default.html>.

6 Operational and system efficiencies

This chapter sets out the Commission's considerations regarding operational and system efficiencies achieved by adopting a consistent methodology to the calculation of interest under the NGR.

6.1 Rule Change proponent's view

The Rule Proponent claimed that a consistent single approach to calculating interest under the NGR would provide operational and system efficiencies.²⁹ Currently, the Rule Proponent's MMS calculates interest using a simple interest methodology for the DWGM and STTM. The Rule Proponent considered that the calculation of interest in the BB should also use a simple interest methodology.³⁰ The Rule Proponent also claimed that one consistent interest rate calculation methodology would allow for future efficiency improvements in the settlement processes across the DWGM, STTM and BB.³¹ Similarly, a single definition for "interest rate" and "default interest rate" under the NGR will allow efficiency gains to be realised as the Rule Proponent streamlines its market and operating systems.³²

The Rule Proponent also proposed that the definition of "interest rate" in the NGR be consistent with the definition of interest rate under the National Electricity Rules (NER). This will allow the Rule Proponent to reduce its costs across the gas and electricity markets as it would only need to source the one rate, rather than spending time sourcing various rates for the two energy markets.³³

6.2 Stakeholder views

TRUenergy did not comment on this issue in its submission.

6.3 Commission's analysis and conclusion

The Commission notes that the Rule Proponent's MMS was designed to calculate the interest payments for compensation amounts, revised statements and overdue amounts in the MSOR using a simple interest methodology, and the MMS continues to calculate the interest provisions in the DWGM using the same methodology.³⁴

²⁹ AEMO, Rule Change Request, p.15.

³⁰ AEMO, Rule Change Request, p.8.

³¹ AEMO, Rule Change Request, p.16.

³² AEMO, Rule Change Request, p.11.

³³ AEMO, Rule Change Request, p.16.

³⁴ The Commission also notes that the AER has been notified that the Rule Proponent is not currently complying with its obligations under the DWGM Rules in relation to the calculation of interest on a compound interest basis. AEMO, Rule Change Request, pp.6-7.

The Commission accepts that as the Rule Proponent operates the DWGM and the STTM, and administers the BB, there are likely to be operational and system efficiencies in ensuring the relevant interest rate provisions use the same methodology to calculate interest, when required. Similarly, defining "interest rate" in the NGR to be consistent with the rate applied by the Rule Proponent under the NER (i.e. a one month tenor), in practice, may provide operational efficiencies for the Rule Proponent, as it will not need to duplicate near identical processes to identify the relevant rates to be applied in each market.

The Commission also accepts that such consistency in the Rule Proponent's processes, procedures and systems will allow improvements in the Rule Proponent's systems, over time, to be efficiently implemented to the benefit of all gas market participants.

7 Costs for participants and consumers

This chapter sets out the Commission's considerations regarding the costs that would be incurred by participants (and consumers) if interest was calculated on a compound interest basis.

7.1 Rule Change proponent's view

The Rule Proponent claimed that in order for it to comply with the current drafting in the DWGM Rules, it "would need to incur costs of more than \$105 000 to change the MMS, with the likely annual impacts on financial outcomes being a small fraction of this amount."³⁵ If incurred, the Rule Proponent advised that these costs would be passed through to registered participants in the DWGM through higher gas fees and would ultimately be borne by consumers of natural gas.³⁶

The Rule Proponent also provided some analysis of the difference between the simple interest payments that have occurred and the estimated compound interest payments that would have occurred, over a six month period in which the Rule Proponent did not comply with the DWGM Rules in respect of interest calculations. This analysis was to illustrate the potential benefits some participants may have received if interest had been calculated for this six month period using a compound interest methodology. The Rule Proponent found that of the revised settlement statements that have been issued:

- the net payments between Market Participants would have been approximately \$210 higher for the six month period if compound interest was calculated;
- the difference between compound and simple interest for individual Market Participants was no greater than \$10 in magnitude for an average of three out of the nineteen Market Participants (for which interest was calculated) for each month; and
- the largest differences calculated for the three peak gas demand months were \$21.31, \$27.78 and \$39.06.³⁷

The Rule Proponent also considered that because of the small amounts involved between calculating interest using a simple interest methodology compared to a compound interest methodology, there would be no impact on market incentives or behaviours and no material impact on financial outcomes as a result of a different basis for interest calculation.³⁸

The Rule Proponent does not expect any compliance costs would result from clarifying the STTM Rules or the BB Rules. Similarly, in clarifying the reference interest rate

³⁵ AEMO, Rule Change Request, p.7.

³⁶ AEMO, Rule Change Request, p.15.

³⁷ AEMO, Rule Change Request, p.16.

³⁸ AEMO, Rule Change Request, p.15.

definitions, the Rule Proponent does not expect any compliance costs as the amendments will ensure the definitions are consistent with its current practices.³⁹

7.2 Stakeholder views

TRUenergy did not comment on this issue in its submission.

7.3 Commission's analysis and conclusion

The Commission has considered the Rule Proponent's comparison of the difference between the calculation methodologies for the revised settlement statements issued from July to December 2009 in the DWGM, if the Rule Proponent had calculated the interest using a compound interest methodology. The Commission undertook further analysis of the figures provided by the Rule Proponent, and acknowledges that there appears to be a small difference between the interest payments calculated, using either a compound interest or simple interest methodology - up to an additional \$50 between participants for each month, if using a compound interest methodology. Based on the information provided by the Rule Proponent, these differences in interest payment methodologies appear to be approximately one per cent of the total interest paid for each month. The value of the adjustments to the revised settlement statements also appear to be less than six per cent of the final settlement statements for each month.⁴⁰

The Commission also notes that if interest was calculated on a compound interest basis, the difference in interest payments essentially balances out between the participants, with the exception of AEMO market fees - that is, some participants would pay more in interest and others would receive more interest.

Taking into account the Rule Proponent's estimated costs of implementing changes to its MMS to calculate interest on a compound interest basis, and the potential benefits to participants if interest was calculated on a compound interest basis, the Commission accepts that the costs of implementing changes to the Rule Proponent's MMS to calculate interest on a compound interest basis appear to outweigh any benefits to participants.

In addition, the Rule Proponent has consulted with relevant stakeholders in the DWGM, STTM and BB on the potential costs and benefits to participants if it is required to calculate interest on a compound interest basis. As no objections were raised by these stakeholders, the Commission does not consider that requiring the Rule Proponent to calculate interest on a compound interest basis is warranted.

³⁹ AEMO, Rule Change Request, p.17.

⁴⁰ A final settlement statement is issued to participants for each month, based on estimated data. Following a period of time as prescribed in the NGR, a revised settlement statement is issued to participants. This revised settlement statement is based on more accurate data from meter readings as well as any other corrections in settlement information from the time the final statement was issued. Interest is calculated on the adjusted amount for the period.

Abbreviations

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator Limited
AER	Australian Energy Regulator
AFMA	Australian Financial Markets Association
BB	Natural Gas Services Bulletin Board
BBSW	Bank Bill Swap Reference Rate
Commission	See AEMC
DWGM	Declared Wholesale Gas Market
GMLG	Gas Market Leaders Group
MCE	Ministerial Council on Energy
MMS	metering management system
MSOR	Victorian Gas Industry Market and System Operations Rules
NER	National Electricity Rules
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
Rule Proponent	See AEMO
Rules	See NGR
STTM	Short Term Trading Market

A Summary of issues raised in submissions

Stakeholder	Issue	AEMC response
<p>TRUenergy Pty Ltd</p>	<p>TRUenergy:</p> <ul style="list-style-type: none"> • agrees with AEMO that the current wording of the interest rate facility in the National Gas Rules (as this facility applies to the DWGM) is in error as a result of the translation process from the original MSOR; • concurs with AEMO that there is value in aligning the DWGM market element with similar provisions in the Rules for the STTM and BB; and • accepts AEMO's proposal to update the now obsolete interest rate reference source in the current DWGM, STTM and BB. <p>In summary, TRUenergy supports the Rule Change Request made by AEMO and requested that the AEMC's determination be made as soon as possible to rectify the current error. (p.1.)</p>	<p>Support for the Rule change has been noted.</p>

B History of the relevant Rules provisions

B.1 Calculation of interest

Currently under the Rules, the Rule Proponent is required to:

- calculate interest "compounding daily" on compensation payments, adjustments to revised settlement statements and overdue amounts in the DWGM Rules;⁴¹
- "calculate interest on a daily basis" on the determination and payment of claims, adjustments to revised settlement statements and overdue amounts in the STTM Rules;⁴² and
- calculate interest "accruing on a daily basis" on a manifest error in invoicing for BB services or following the resolution of a disputed invoice where the BB operator is obliged to repay part or the whole of the disputed amount in the BB Rules.⁴³

B.1.1 History of these relevant provisions

The DWGM Rules commenced on 1 July 2009, and were transitioned from the MSOR. In the MSOR, the interest rate provisions for adjustments to revised statements and overdue amounts were provided in the first version of the MSOR, which commenced on 25 February 1999. The MSOR was amended to include interest rate provisions for compensation payments on 7 April 2005.⁴⁴ In the MSOR, the wording in the calculation of interest clauses for compensation payments and adjustments to revised settlement statements did not specify the methodology to be used, only that interest was to be calculated on a daily basis. For overdue amounts, the relevant clause specified that simple interest was to be calculated on a daily basis.

In April 2004, the MCE agreed to expand the gas market element of the energy market reform program to accelerate the development of a reliable, competitive and secure natural gas market and to further increase the penetration of natural gas.⁴⁵ The MCE established the Gas Market Leaders Group (GMLG)⁴⁶ to develop a gas market development plan to meet these objectives. Establishment of the STTM and BB were among initiatives recommended by the GMLG to focus on improving information disclosure and market transparency. The BB and BB Rules commenced together on 1 July 2008. The STTM Rules commenced on 7 May 2010, and the STTM started operation in the Adelaide and Sydney hubs on 1 September 2010.

⁴¹ NGR clauses 238(4), 238(6), 249(4)(b) and 253(2).

⁴² NGR clauses 466(4), 473(5)(b), 476(1) and 476(2).

⁴³ NGR clauses 194(3)(a), 194(3)(b)(i), 194(4) and 195(3).

⁴⁴ MSOR version 25, operational 7 April 2005.

⁴⁵ MCE, seventh meeting communiqué, 2 April 2004.

⁴⁶ The GMLG comprises representatives from all sectors of the gas industry and users.

B.2 Definition of reference interest rates

Currently under the Rules, the definitions of interest rate and default interest rate, where applicable, vary slightly between the different Parts:

- in the DWGM Rules, interest rate "is a reference to the Bloomberg Bank Bill Swap Reference Rate most recently published in the *Australian Financial Review*" and if this rate "ceases to exist, or that rate becomes, in AEMO's reasonable opinion, inappropriate, the interest rate is a rate determined and published by AEMO", and default interest rate "means an interest rate of 2% above the interest rate";⁴⁷
- in the STTM Rules, interest rate "means, at any time, the Bloomberg Bank Bill Swap Reference Rate identified by AEMO on its website for the purposes of this Part, as most recently published in the *Australian Financial Review*" or "if no such rate is published or, in AEMO's reasonable opinion, appropriate, a replacement rate determined and published by AEMO", and default interest rate "means an interest rate of 2% above the interest rate";⁴⁸ and
- in the BB Rules, applicable interest rate "means the interest rate quoted from time to time by Australia and New Zealand Banking Group Limited as its reference rate or, should there cease to be such a reference rate, the rate at which that bank designates as being an appropriate substitute for the reference rate".⁴⁹

B.2.1 History of these relevant provisions

In the MSOR, interest rate was defined as the "ninety day Bloomberg Bank Bill Swap Reference Rate as published in the *Australian Financial Review* from time to time" and default interest rate was defined as "an interest rate of 2% above the *interest rate*".⁵⁰ There was no predecessor to the STTM Rules or the BB Rules, and hence no earlier definitions of interest rate or default interest rate for these rules.

47 NGR rule 203.

48 NGR rule 364.

49 NGR rule 141.

50 MSOR version 31, operational 1 May 2009, chapter 11.