stanwell

15 February 2013

Mr Steven Graham
Chief Executive Officer
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Dear Mr Graham

Stanwell Corporation Limited (Stanwell) welcomes the opportunity to comment on the rule change request proposed by the Australian Energy Market Operator (AEMO) which seeks to increase the participant compensation fund (PCF) for the short term trading market (STTM) Brisbane hub.

As background, Stanwell is a Queensland Government owned generator, with the capacity to supply more than 45% of the State's peak power needs. We are a diversified energy company, with an energy portfolio comprising coal, gas, diesel and hydro power generation facilities geographically dispersed across Queensland.

Stanwell is an active participant in the STTM, specifically in the Brisbane hub. Our generation assets include Swanbank E Power Station, a Combined Cycle Gas Turbine power station. Gas for Swanbank E is obtained from multiple sources including coal seam methane fields in south west Queensland via the Roma to Brisbane Pipeline.

In responding to the paper, further to commenting on AEMO's proposed increase, Stanwell recommends that consideration be given to introducing a mechanism to regularly review the PCF to ensure it reflects changing market conditions, which are particularly relevant in Queensland. We also consider thought should be given to reviewing the allocation methodology to ensure it is delivering the most efficient and equitable outcome for the market, and pose a possible option for further consideration. Each of these issues is discussed below.

1. AEMO's proposed increase to the PCF

Stanwell is supportive of the PCF as it provides compensation to participants for direct losses incurred as a result of scheduling errors by AEMO. Stanwell also considers that the amount of money available in the fund should take into account the size of potential gas withdrawals in the particular hub (i.e. total capacity at the hub). It is imperative the PCF appropriately balances the trade-off between the risk of incurring losses as a result of a scheduling error and the cost of a 'co-insurance' scheme for participants.

It is acknowledged that the PCF for the Brisbane hub was originally set at $100,000, based on forecast withdrawals of the distribution network connected users. Stanwell considers it appropriate that the quantum of the PCF be revisited given the significant increase in demand at the hub following the inclusion of transmission connected users.

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Stanwell has no objection to an increase in the PCF from $100,000 to $450,000, given the relatively small increase in participant fees required to achieve a substantially higher compensation fund should scheduling errors occur in the future.

Notwithstanding our support for an increase to the PCF, we consider there to be an opportunity to consider alternative calculation methodologies for implementation at a future date that would enhance the overall integrity of the market. Further, Stanwell is concerned that the level of the PCF for Brisbane is determined by comparison to the Sydney hub. This presumes that the level of the PCF for the Sydney hub is inherently appropriate. While this may be the case, there does not appear to be any evidence to confirm this position. We note that the Queensland market is likely to experience change with the development of the LNG industry.

2. A mechanism to review future changes to the PCF

Stanwell recommends consideration is given to a methodology that enables both the quantum of the fund itself and participant contributions to appropriately reflect the financial implications of potential scheduling errors. In relation to the size of the fund, Stanwell recommends moving to an approach that incorporates ongoing monitoring of the size of the fund, with reference to total capacity at the hub. For example, AEMO undertakes an annual review of the size of the fund and, if it is deemed insufficient, adjusts accordingly. Note that this approach would only be feasible if suitable consultation provisions were in place prior to AEMO adjusting the fund and therefore participant contributions. It is important that total capacity is the relevant market driver, not actual usage, given the size of the risk is as large as the ability of participants to use their capacity at any given time.

3. Alternative methodologies to allocate participant funding

In addition to examining the fund itself, the annual review process could also be used to determine whether the level of contributions of respective participants remains appropriate relative to their level of capacity at the hub. One option could potentially involve moving to a 'bond' type arrangement, whereby market participants contribute to the PCF based on their proportion of the total available capacity at the hub. Under this alternative methodology, existing participants would contribute an amount that reflects their proportion of the total capacity. This would provide an opportunity to readjust should new participants enter the market. Conversely, if a participant were to cease participating in the hub, there would be an opportunity for their component to be refunded (in part) given they are no longer trading at the hub, and therefore the risk has been reduced by their withdrawal of capacity at the hub.

Given the potential increase in gas trading in Queensland associated with the introduction of liquefied natural gas exports in the coming years, it is important that a review mechanism is in place to ensure the fund continues to adequately reflect the possible risk to participants associated with scheduling errors. A failure to maintain adequate balances in the fund moving forward will discourage both new entrants and existing market participants to trade at the hub. Further, the contributions made to the fund by participants should be commensurate with the level of risk they could potentially be exposed to at the hub.

Under the current methodology, a new participant could enter the Brisbane hub, taking a sizeable proportion of the available capacity, and only contribute as and when they use that capacity. It is conceivable that it would be a long time (if at all) before that participant's contribution to the fund is commensurate with their proportion of the risk associated with the hub. Alternatively, an existing participant who has contributed significantly due to historical levels of usage receives no recompense if they were to materially reduce their capacity in the future, despite this reducing their contribution to the risk exposure at the hub.

The option highlighted above is only at a conceptual stage and we would strongly recommend the AEMC consider undertaking more detailed analysis of the impacts for the market and participants.

Stanwell considers that the above outcomes demonstrate the need to investigate alternative methodologies that more effectively meet the National Gas Objective. The alternative option canvassed above is likely to provide a more reflective allocation of funding and participant risk exposure, reducing potential for 'free riding'. This in turn enhances the overall integrity of the market. We welcome the opportunity to discuss possible approaches with you in more detail.

If you wish to discuss any of these issues further please do not hesitate to contact me on (07) 3228 4352 or Mr Peter Tolhurst, Market Regulation Advisor, on (07) 3228 4163.

Yours sincerely,

T. Mills

Tanya Mills
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