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Mr John Pierce
Mr Neville Henderson
Dr Brian Spalding
Australian Energy Market Commission

Dear Commissioners

Lodged electronically: www.aemc.gov.au (GPR0002)

AEMC 2016, Review of the Victorian Declared Wholesale Gas Market, Discussion Paper, 3 March 2016

EnergyAustralia welcomes the opportunity to respond to the Review of the Victorian Declared Wholesale Gas Market Discussion Paper (the Discussion Paper). We are one of Australia's largest energy companies with over 2.5 million electricity and gas accounts in NSW, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate a multi-billion dollar energy generation portfolio across Australia, including coal, gas, and wind assets with control of over 4,500MW of generation in the National Electricity Market.

It's useful to review gas markets from time-to-time, particularly to ensure they are effective at times when prices are rising prices and other significant market changes are occurring. The proposed Victorian model appears more suited to the new dynamic and integrates well with the overall east coast design; opening trading opportunities between north and south.

We have commented on three key areas arising from the Australian Energy Market Commission's (the Commission's) recommended model for the Victorian gas market:

- Increased support of market-led investment
- Simplifying congestion cost-to-cause allocation
- Moving to a continuous market-based balancing regime

While we see advantages in all three areas, we do have concerns and questions that we would like to continue to work on with the Commission and industry. The Commission has outlined a model which has the potential to meet the National Gas Objective however we would like to see this assessed at a detailed level before any commitment is made to proceed to implementation.

If you would like to discuss this submission, please contact me on (03) 8628 1242 or Ben Hayward on (03) 8628 4518.

Regards

Melinda Green

Industry Regulation Leader

1. Managing capacity at the Southern Hub

1.1. Institutional roles

We largely support the separation of duties outlined by the Commission. The only change we suggest is to have AEMO facilitate the sale of the baseline as well as the additional capacity. We see that this options has potential benefits such as continuity between systems for baseline and additional capacity. The Commission has recently made a rule concerning AMDQ allocation.[1] AEMO will auction off AMDQcc where the costs for the capacity are included in the Declared Transmission System (DTS) service provider's opening capital base or approved expenditure. This determination is consistent with a model where AEMO allocates the baseline capacity.

1.2. Mechanisms for allocating capacity at the Southern Hub

The Commission's recommendations place more emphasis on market-led investment, meaning that participants will have additional incentives to fund expansions but also face additional risks. This better allows retailers and gas-fired generators to make their own decisions and trade-offs concerning their required capacity.

There are recent examples in the DTS which aid the case for market-led investment. These include timely capacity augmentations where market participants have identified a need and funded the expansion outside the access arrangements. There have also been failures of the regulatory model where it has not been successful in delivering needed capacity.

However, we have also seen evidence to the contrary: a reluctance of market participants to invest in gas supply (plus transportation) due to the significant risks involved in long-term commitment where gas price is increasing and demand and other factors are uncertain. An equivalent issue can be seen in the market for Large-scale Renewable Energy Certificates where investment has been lacking due to forward uncertainty. The balance of risk between consumers and participants and the period over which capacity can be purchased is critical and may need to remain flexible in-order to meet changing circumstances.

The timeframes for capacity allocation should be consistent with sources of supply. Obtaining commodity and capacity for similar periods is important for a retailer to have certainty. Our preference is for auctions 12-18 months in advance of a period which aligns with the access arrangement for the DTS (i.e. five years).

We agree that in allocating capacity, a distinction must be made between controllable injections/withdrawals, distribution exit points, and large, direct connected customers. We also support distribution exit rights being automatically allocated to retailers based on proportion of retail customer load. For this to work, we note that bilateral planning between APA and the customer and distribution networks will be required. However, questions remain with respect to regulator involvement, the commitment period, and cost recovery approach.

Given the development of capacity trading markets on contract carriage pipelines, it is appropriate to also allow a mechanism to trade DTS entry and exit rights. The systems which are implemented for the former can be leveraged to provide trading of Victorian rights at little

[1] http://www.aemc.gov.au/Rule-Changes/DWGM-AMDQ-allocation

marginal cost for significant benefits – particularly given the opportunity costs associated with an underutilised pipeline.

2. Balancing at the Southern Hub

2.1. Balancing regime

As noted in EnergyAustralia's submission[2] to the Stage 2 Draft report, continuous balancing has the potential to be the most efficient option. Short and long balancing periods both have disadvantages and the most efficient fixed time interval may vary seasonally. The implementation costs and the benefits gained from continuous balancing, above say a 4-hour balancing period, may be able to be quantified through historical analysis.

While we are open to the idea of continuous balancing, it is very different to the current approach and we're unsure how it would work in practise and if it offers clear benefits over the current approach. Some of the aspects we have considered are:

- There may be greater emphasis on primary balancing due to the uncertainty for participants in knowing when they are at risk of imbalance charges and in being able to take corrective action to avoid these charges. The market may operate less efficiently if participants are more focussed on remaining in balance for more of the time.

- Currently the responsibility for balancing the system lies with the system operator alone. There is a possible coordination issue with the new design that arises where both a participant and market operator act to balance the market at similar times. What real-time information will shippers have if they or the system are balanced? Solutions to this should be investigated in the detailed design.

- Matched injections and withdrawals made at the same time may create a locational-based linepack requirement while not exposing shippers to any charge. In the current system, AEMO is able to manage linepack to limit these effects due to importance placed on accurate forecasts. If AMDQ has not been assigned to an injection point, as an injection hedge, the participant is exposed to these prices.

- Under a continuous balancing arrangement, the time element of the price is impacted and assessing whether to inject or not becomes more difficult.

- Additional resources are likely to be required for shippers to continually monitor and balance their gas position. We agree with the other sources of potential cost introduced under a continuous market-based balancing regime.[3]

2.2. Procurement of balancing gas

Given that participants must balance in real-time based on estimated (baseline) usage, we consider that resettlement on a neutral gas price (e.g. volume weighted average price of gas delivered on that gas day) may be appropriate. The Commission has included comments[4] from Gasunie, the operators of the Dutch Gas Transmission System, to this effect. We note

[2] http://www.aemc.gov.au/getattachment/101a6067-2bd8-4b5d-bdd1-6393ac9a7969/Energy-Australia.aspx
[3] Discussion Paper, pg 69-70
[4] AEMC 2016, Review of the Victorian Declared Wholesale Gas Market, Discussion Paper, 3 March 2016, Sydney pg 59

that this is a departure from the current arrangements where resettlement uses the same price as on-the-day deviations.

The intra-day products outlined in the Discussion Paper include the balance-of-day and 1-hour products. These seem appropriate in the DTS where the products would largely align to a change in forecast demand and short-term congestion management. Profiling of these injections may be required to ensure gas that is injected is timed to relieve the constraint efficiently.