

The background of the cover features a large, stylized graphic on the left side. It consists of several overlapping, curved bands in shades of teal and light blue, creating a sense of motion and depth. The top half of the cover is a solid dark blue color, which serves as a backdrop for the main title text.

Submission to the AEMC  
East Coast Wholesale Gas  
Market and Pipeline  
Frameworks Review's Stage  
2 Draft Report

**AEMC Reference: GPR0003**

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## Introduction

The Australian Pipelines and Gas Association (APGA) has been an active participant in the Commission's Review of Wholesale Gas Markets and Pipeline Frameworks. The Stage 2 Draft Report is the culmination of detailed deliberation by the Commission and gas market stakeholders, providing high-level recommendations that can enable a more liquid, transparent gas market for the East Coast. APGA has a number of comments on the direction of the recommendations and issues that will need to be accounted for as details are fleshed out and processes established to implement the recommendations adopted by the CoAG Energy Council.

## Key points

- The Commission has recommended a set of actions that represent a substantial change to current arrangements. It is not clear that the benefits accruing from some of these changes are justified by their costs. In particular, APGA considers the introduction of a virtual hub over Victoria will be a very costly exercise.
- APGA supports the rationale for Pipeline Capacity Recommendations 1 and 2.
- APGA does not support the rationale for Pipeline Capacity Recommendation 3.
- The proposed timeline is ambitious, particularly for implementation of the recommendations for pipeline capacity markets. Government and industry processes will be required to achieve implementation within the timeframe. Government processes will need to move more quickly than has occurred in the past.
- There is a potential to allow industry to implement the recommendations voluntarily, negating the need for some Government processes. APGA estimates that voluntary implementation of the capacity auction and trading platform recommendations could be achieved by October 2017.
- Harmonisation of nomination times is an issue that extends to facilitated markets and gas sales agreements. This is an issue affecting all market participants and is an ideal candidate for a government process.
- Industry processes should lead implementation of capacity auctions, trading platforms and
- The proposed changes would take time to have an influence on market participant behaviour. The time taken for more active utilisation of the STTMs as a genuine source of supply for small users (over 5 years) is a useful guide. Reviews should not be held within 2 or 3 years of implementation.
- Further steps should be contemplated during such reviews, rather than being flagged now. There are a number of factors that could contribute to the utility of new hubs and platforms. These should be considered in due course.

Specific key points on each recommendation are highlighted throughout the submission.



## Pipeline Capacity Markets

### Implementation of recommendations

The path for implementation set out by the Commission is an option that requires legislative and regulatory change. APGA is concerned with the perception that can arise from amending the NGL and NGR to implement the recommendations regarding pipelines. Whilst the Commission is making a set of recommendations that seek to improve gas markets and as such are related to market regulation, there may be a perception, especially amongst financiers and international pipeline investors, that the pipeline access regime is being altered or circumvented (to the detriment of pipeline independence and commercial arrangements) to achieve these market outcomes.

Given that implementing the Commission's recommendations will require many industry-led processes, ***APGA recommends that industry be given an opportunity to implement these recommendations before detailed legislative change is considered necessary.*** Implicit in such an opportunity is the threat that legislation and regulation can be used to impose equivalent outcomes on the gas market if industry does not achieve the required implementation time. The prospect of prescription and higher costs of rapid legislative change following a failure of industry to voluntarily implement reforms is sufficient incentive to ensure satisfactory outcomes.

Removing the need for detailed legislative change frees up resources across industry and government to focus on other areas of implementation.

Naturally, full consultation will be required and government participation would enable effective observation and ensure all parties work towards common outcomes.

APGA understands that FERC has allowed industry processes, under threat of regulatory intervention, to achieve desired outcomes in the past. FERC is currently applying this 'threat of regulation' technique to achieve cyber security outcomes in the electricity and gas sectors.

If legislative change is deemed appropriate, APGA recommends it be fit-for-purpose, non-prescriptive and as flexible as possible. A requirement for registered pipelines to conduct a capacity auction may be sufficient. It is apparent each pipeline operator will have to implement a number of asset specific changes to achieve the standardisation necessary to support capacity auctions and improved trading platforms. It is essential that legislative and regulatory requirements focus on outcomes and not the mechanisms to achieve the desired outcomes.

### Recommendation 1: Auction for contracted but un-nominated capacity

APGA considers an auction for contracted but un-nominated capacity as set out by the Commission can improve the incentives for shippers to make capacity available to the secondary market.

The limiting of the auction to the sale of contracted but un-nominated capacity on a day-ahead basis places capacity sold through the auction in direct competition with 'as available' (AA) capacity sold by pipeline operators and it is appropriate that pipeline operators receive the revenue from the auction.



If revenue from the auction is allocated to shippers then the incentive for shippers to allocate capacity to the secondary market is reduced. The product that shippers can offer to the secondary market is a superior product to that which the auction can provide and should be encouraged. Shippers can sell their unutilised capacity on a firm basis for longer periods – a superior product to day-ahead “as-available” capacity.

### **Rationale for recommendation 1**

APGA supports the rationale for recommendation provided in Section 4.2.1.

### **Recommendation trade-offs**

#### **Investment signals**

APGA cautions the Commission and policy makers that under-playing or dismissing free-rider issues as theoretical does not acknowledge the role such effects, even if they are only perceived, can play in decision making.

There is the possibility that the perception of such effects will lead shippers to contract less than they currently do in an environment where the potential for free rider effects is low. This can lead to smaller investments, with less unutilised capacity available for access through secondary markets and/or a capacity auction.

It is possible to envisage scenarios where the perception of the presence of free rider issues, combined with a desire to increase their own exposure to secondary markets, would lead shippers to reduce their contract requirements. This would have flow-on effects on the liquidity of the secondary capacity markets by leading to smaller, more highly utilised investments.

Whilst there will be different views as to future market participant behaviour, the changes in market design and operation envisaged by the Commission would lead to market participants testing and adopting new contracting and portfolio strategies to better “sculpt” their capacity reservation to their load profiles. These are difficult to anticipate and their effects on capacity markets unknown. It is unlikely many of these strategies would have an increased reliance on long-term contracts. These long-term contracts are the basis for investment and a reduced reliance on them may lead to undersizing of future investment.

#### **Existing nomination and re-nomination rights**

An auction will be impacted by existing nomination and re-nomination procedures. For example, where there are existing contractual re-nomination rights, the capacity purchased through the secondary market auction must be considered as interruptible subject to pre-existing re-nomination rights. Other pipelines may be able to offer a “day-ahead firm” product.<sup>1</sup> *This is best managed on a*

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<sup>1</sup> An Australia-wide standardised auction product may require confiscation of these re-nomination rights, which would require compensation to the holder of those rights.



*pipeline-by-pipeline basis.* Some pipelines will require a more extensive process than others in order to achieve this. For example, there are pipelines that use hourly nomination procedures. Some pipelines will have relatively consistent nomination procedures and others will be outliers in their approach.

APGA considers that each pipeline operator will have to work closely with current shippers on each pipeline to determine the best process to implement an auction for capacity. An industry standard would be a useful mechanism to ensure a consistent approach and outcomes across pipelines and the pipeline industry has a strong history in developing standards. Implementation of the recommendations according to the timeframe set out by the Commission will be a challenge and it is important that industry and government processes can be co-operatively utilised to achieve this.

Consideration of the interplay between GTA nomination times, GSA nomination times, facilitated market nomination times, pipeline operator, producer and shipper requirements will be a complex undertaking and will, as the Commission notes, require care. APGA does caution that it is not actually an issue of auction design, rather it is an industry wide harmonisation effort that can improve the utility of the auction.

From a pipeline perspective, it should be relatively simple to standardise a nomination time that is x hours before the start of gas day. Changing start of gas day is its own undertaking, as identified by the Commission.

### **Regulatory burden**

Direct costs of developing and implementing the auction will need to be considered prior to an implementation system. As with all market development reforms, initiatives have the greatest potential to provide net benefit if they are implemented in ways that minimise costs. APGA considers costs of the implementation of capacity auctions would be minimised if:

- Auction mechanisms are designed to account for the specific operational and system requirements of each pipeline. This will require each pipeline operator to determine the best systems approach for its assets.
- Auction mechanisms are implemented by pipeline operators with results being reported to AEMO. The auction will need to be conducted as soon as possible after nomination cut-off and its results processed as quickly as possible. This can be achieved at lowest cost if the requirements for external communications and interactions (which would require more sophisticated systems with additional redundancy) are limited. The implementation and operation of an auction mechanism will be similar to the MOS processes implemented and operated by pipeline operators to support the STTM. Just as it is more efficient for pipeline operators to manage MOS processes, it will be more efficient for pipeline operators to manage auction processes.
- The mechanism to establish a floor price is not very complex. Regulatory determinations regarding cost can vary in complexity and cost from the extensive to minor. A full access arrangement process undertaken by covered pipelines is at the extensive end of the spectrum. The auditing process used to approve STTM pipeline facilities MOS costs is at the minor end. A less complicated mechanism would deliver significant savings to regulators and pipeline



operators. These savings would then be reflected in the floor price. This is discussed more fully below.

## Design Considerations

### Setting the reserve price

The setting of a reserve price for a capacity auction could be highly contentious.

As the Commission notes, the short run marginal cost is likely to differ on a variety of circumstances. The cost of developing, implementing and running the auction will also need to be considered. A complex regulatory process to establish the reserve price will lead to greater costs that will be reflected in the reserve price.

It is widely accepted that the short run marginal cost of transporting an additional unit of capacity on a given day on a pipeline is very low.

It is not costless, additional capacity throughput will be achieved by running compressors. The more compressors run, the more fuel they burn.

*APGA considers fuel costs should be managed consistent with current practice.* This can differ for each pipeline, but typically requires shippers to provide compressor fuel to the pipeline operator. This is usually pro-rated to each shipper on a daily throughput basis. The current fuel gas practice will form part of the terms and conditions that each party seeking to acquire capacity on a pipeline would be required to agree to prior to participating in any auctions.

Aside from fuel costs, and the costs of establishing the auction, *APGA considers that the short run marginal cost of additional capacity is sufficiently low that a complex regulatory process to establish an appropriate reserve price could have such high costs that it would materially alter the short run marginal cost.*

Further, it is likely the auction settling price would often be at least slightly above the reserve price. This further decreases the benefit of establishing an accurate short run marginal cost.

It is appropriate that the costs of developing and implementing systems to run the auction are recoverable. These costs should be factored in to the reserve price of an auction. Setup costs can be verified through a simple mechanism such as a process mirroring the recovery of MOS costs for STTM pipelines, whereby pipeline operators submit costs to the AER for approval. These costs could then be used to set the reserve price based on assumed auction activity.

Such a process establishes an auction reserve price that should recover auction costs without imposing significant regulatory burden on industry and the AER to establish an accurate short run marginal cost.

*In summary, APGA considers that the reserve price should be established to recover the costs of establishing and operating the auction market mechanism, and shippers should provide fuel in accordance with existing practice applicable to existing shippers.*



### **Determining the amount of capacity to be auctioned**

At its most basic level, the amount of capacity to be auctioned should be equivalent to the contracted firm capacity (known on a daily basis to all parties through publication on the Bulletin Board as per the recent enhanced information rule change) less the nominations received.

There will be operational considerations for a pipeline. Market participants will have good visibility on this through the seven day capacity forecast published on the Bulletin Board.

There will be further operational matters to consider due to matters introduced by the auction, trading platforms and the required standardisation. These include:

- The need to indicate capacity availability by zone (or alternative mechanism of introducing flexibility to receipt and delivery points). The spread of nominations across a pipeline is likely to mean that there will be varying levels of capacity available to auction for each zone.
- The interactions of deliverability across zones. A high level of demand in one zone may impact on deliverability in other zones. For example a high level of demand in a zone at the downstream end of the pipeline may mean less capacity is available for delivery to zones further upstream. Alternatively, a high level of demand in an upstream zone may deplete linepack to the point downstream deliverability is affected. Particularly where auctioned products are to be standardised, the capacity available for auction may be less than the capacity not nominated on a particular day. Pipeline operators will have to manage and prioritise incoming bids (presumably on their value) for capacity accordingly.

There will need to be procedures in place to ensure that shippers do not nominate a high initial capacity before an auction in order to limit the availability of capacity to auction then subsequently lower nominations after the auction has been held.

### **Pipelines that are not fully contracted**

The Commission correctly notes that there is an issue in applying a capacity auction to pipelines that are not fully contracted.

An auction of contracted but unutilised capacity is a common form of short term Use-It-Or-Lose-It (UIOLI) arrangement. These arrangements have generally put in place where access to pipeline capacity is restricted due to perceived hoarding behaviour by incumbent shippers, addressing the issue of 'contractual congestion'.

*Where a pipeline is not fully contracted, 'contractual congestion' does not exist.* Hoarding behaviour cannot restrict access to the pipeline, and therefore a UIOLI mechanism to discourage hoarding behaviour is not required.

APGA therefore considers that the auction of reserved but unutilised capacity should not be applicable to pipelines that are not fully contracted.

Whilst the Commission is concerned that limiting the application of the auction to fully contracted pipelines will incentivise pipeline operators to only contract a proportion of their capacity in order to



avoid the auction, APGA considers it more likely that shipper behaviour in response to the auction will lead to a decrease in contracting on pipelines.

As APGA presents above, the presence of a capacity auction may lead to a situation where fewer pipelines are fully contracted. Market participants will develop new strategies to best utilise an enhanced secondary capacity market and a capacity auction. It is highly unlikely these will maintain the current reliance on long-term contracts. Combined with a forecast lack of growth in many domestic markets, the potential for this behaviour to lead to an increase in pipelines with uncontracted capacity, must be considered when determining the design of the auction.

It is appropriate that some rules are developed to determine the applicability of the auction to a pipeline. At some level of contracted capacity, the presence of a compulsory auction is an impediment to a pipeline operator selling capacity on the primary market and recovering its long-term costs.

This level of contracted capacity is likely to be high.

Pipelines are generally considered low-risk, low-return investments. Long-term contracts provide financiers with certainty and provide shippers with favourable tariffs. As such, pipelines need to be fully contracted in order to deliver expected returns to investors. If to the level of contracted capacity falls, pipeline profitability drops rapidly. A drop in contracting level of a few per cent will result in a much greater drop in profitability, possibly an order of magnitude greater.

***The auctioning of contracted but unutilised capacity may lead to pipeline operators having difficulty maintaining current contracting levels. This outcome cannot be ruled out.***

Where pipelines have spare capacity and are actively marketing it, it is unnecessary, and inappropriate, to mandate an auction to ensure access to the pipeline.

Some pipelines that are not fully contracted may choose to utilise an auction mechanism to increase utilisation. They should not be forced to, to do so impacts the ability to sell primary capacity. This could be seen as an imposition on property rights, being forced to sell one form of capacity before another

***APGA considers that capacity auctions should only be applied to pipelines that are fully, or nearly fully, contracted.***

An auction reserve price could be developed that accounts for the level of contracting on a pipeline, but this would lead to a more complex approach that would increase the costs associated with the auction mechanism across the board.

### **Auction Design**

The issues raised in this section of the Stage 2 Draft Report are largely related to an increased flexibility in receipt and delivery points. APGA will address this in its comments on standardised capacity products.



### **Terms and conditions of capacity and service standards**

APGA considers that the terms and conditions for capacity sold through an auction would not have to be set with regulatory oversight. It should be a relatively simple matter for pipeline operators, in discussion with market participants, to extend their published standard terms and conditions to auctioned capacity.

One issue that will need to be resolved is the nature of capacity acquired through auction, i.e. will it be firm or interruptible. ***To ensure existing renomination rights are not removed, it is likely capacity acquired through auction will need to be interruptible.***

Importantly, APGA envisages that market participants will have to enter prior arrangements with a pipeline operator to meaningfully participate in a capacity auction. Just as any market participant desiring to use the operational capacity transfer service must have a pre-existing arrangement with a pipeline operator, any market participant seeking capacity through an auction will have to satisfy a pipeline operator it meets the prudential requirements necessary and that responsibilities and obligations are fully understood and complied with.

For auction participants with existing gas transportation arrangements in place, the prudential requirement satisfaction could be referred from the existing contracts. For those without a pre-existing gas transportation arrangement, prudential requirements would have to be met in order to gain access to the auction system.

These arrangements include matters such as:

- Gas quality obligations.
- Meeting prudential requirements.
- Ensuring a capacity acquirer has the systems in place to communicate with the pipeline operator's systems for matters such as nominations, emergency communications and invoicing.
- Fuel gas obligations
- Treatment of overruns

***There must be formal agreement to these arrangements before any party can transport gas on a pipeline.***

The pipeline industry has addressed many of these matters during the development of the operational capacity transfer service. There is no need to reconsider these issues.

APGA anticipates that a standard set of terms and conditions for parties seeking capacity through an auction will be developed and published by each pipeline operator. A requirement for regulatory oversight would add to the cost of such a standard and is unlikely to bring additional benefits.

It is already apparent that most pipeline operators publish non-discriminatory, standard terms and conditions of service on each asset. In the first instance, these can readily be extended to capacity acquired through auction. It is also appropriate that all pipelines publish standard terms and conditions for both primary capacity and capacity acquired through trade or auction. Over time, it is reasonable



to expect that standard terms and conditions on each asset will evolve to a common standard across most, and possibly all, assets.

When the standard terms and conditions on each asset are better understood, it may be apparent that they have more in common than in difference.

### **Covered pipelines**

APGA considers that the recommendations developed by the Commission are more appropriately considered matters of market regulation than access regulation. Coverage is concerned with the application of access regulation to a pipeline.

*APGA remains concerned about the application of regulatory involvement to uncovered pipelines. In this regard, APGA considers that a voluntary, industry-led auction process avoids the need to tread on the Coverage criteria.*

### **Pipelines serving a single facility**

APGA agrees that it seems unnecessary for pipelines serving single facilities to conduct an auction.

### **Other considerations**

There is a range of detail that APGA and its members have begun to consider that needs to be addressed:

- It is likely that parties participating in the auction will need to specify the receipt and deliver points they intend to use. This information should not be made public, but can be used by the pipeline to ensure all parties receive capacity they can use.
- Following this, if there are too many bids for a single delivery point a pipeline operator cannot accept them all. Presumably, the lowest bids will be removed first. These bids may be higher than successful bids at other delivery points.
- Whilst an auction to allocate capacity should aim to provide it to those parties that value it most highly, there will be a need to consider efficiency and utilisation – a pipeline may be able to deliver more GJ of gas if it prioritises midstream delivery points over downstream delivery points. There must be scope for a pipeline operator to consider overall deliverability when allocating capacity through an auction.
- There may need to be a throughput threshold for the implantation of the auction and trading platform mechanisms. It is difficult to see value in requiring very small pipelines (<20TJ/day) to implement these mechanisms. It may be appropriate to limit these mechanisms to pipelines connecting to facilitated markets.



## **Recommendation 2: Secondary trading platform with information reporting requirements and standardised capacity products**

APGA considers that a secondary trading platform with information reporting requirements and standardised capacity products is a necessary mechanism to achieving an effective, liquid secondary capacity market. Many of the elements in this recommendation have been flagged in the past as appropriate for industry-led reform. Indeed, recent industry initiatives have seen capacity posting services implemented and the recommendation sets out further improvements, some of which have been under active consideration.

*APGA considers a simple, anonymous trading platform can be implemented at relatively low cost.*

An ability to anonymously post capacity bids and offers is simple to build into existing systems. If trades are offered at set prices, a counter-party can simply contact a pipeline operator to indicate it wishes to trade. If trades (either bids for or offers of capacity) are offered to the market for open season or through auction, a pipeline operator can accept bids until a pre-arranged cut-off time and then accept the highest bid. In neither circumstance is a sophisticated system required to manage such a process. If the level of activity is high, such that an investment in automated systems can be justified, they can be rolled out in time.

As discussed above, standardised capacity products may result in less-than-nameplate capacity being available, depending on the physical characteristic of the capacity released and the capacity purchased.

### **Rationale for recommendation 2**

APGA accepts the rationale for the recommendation.

### **Recommendation 2 tradeoffs**

#### **Anonymity, confidentiality and information provision requirements**

Anonymity of trades appears to be important in order to minimise discrimination.

The development of an anonymous trading service should be relatively low cost and address confidentiality concerns. At its simplest, such a service would be very similar to the existing posting service, with parties names removed. A pipeline operator could facilitate the transaction without either party identifying the other. Appropriate standardised products should limit, if not remove, the ability for receipt and delivery points to reveal trading party information.

#### **Cost of developing capacity trading platform and standardisation**

The costs of developing capacity trading platforms does not need to be excessive. Costs can be minimised by allowing pipeline operators to leverage existing systems and provide appropriate services. It is appropriate that the costs of developing and operating the platforms are recoverable. APGA notes that AEMO recovers the costs of facilitated markets on a c/GJ basis. It is likely that a



similar approach is appropriate for trading platforms, with the AER approving pipeline costs on a similar basis to the current STTM MOS cost recovery arrangements and allocating these on a per GJ basis.

*Standardisation of products for trade should not be a complicated process.*

Standardisation of capacity rights will be more complicated. However, it is necessary to do so for both the auction mechanism and enhanced trading. As discussed above, standardised capacity products may result in less-than-nameplate capacity being available, depending on the physical characteristic of the capacity released and the capacity purchased.

### **Standardisation**

APGA considers the products available for capacity trade should be in line with the products available at the Wallumbilla Supply Hub.

Standardisation of capacity rights will be a complex process and the Commission is right to recognise this.

Flexibility in receipt and delivery points will be essential in achieving standardised capacity rights. APGA considers that regulated segmentation will not be required in order to achieve this. Industry has been considering the issue and should be able to develop zones covering multiple delivery points and rules to allow capacity to cross zones and provide the increased flexibility required to enhance the secondary capacity market.

### **Design considerations**

#### **Compulsory trading through the platform**

The implementation of a capacity auction should provide sufficient incentive to ensure shippers wish to trade. Once shippers have this incentive, the likelihood that they will discriminate between trading parties to the detriment of some seems low, particularly when an anonymous capacity trading service will be available.

*Shippers should be free to trade their capacity in the manner they wish.* Trades should be free to occur outside the platform, providing they are published along with trades through the platform. It should be noted in this respect that bilateral trades can offer a superior product to standardised trading through a platform, in that a bilateral capacity trade can be tailored to meet the exact requirement of the counterparties.

Further, trading platforms are costly. There will undoubtedly be charges associated with trading through platforms. These charges should not be forced on market participants. If market participants are not satisfied with charges they should have the ability to arrange trades outside the platform.



Finally, a requirement for all trades to occur through the platform removes the ability for market participants to bundle capacity trades with other market transactions, such as gas swaps.

### **Segmentation and flexibility in receipt and delivery points**

Segmentation might not be the appropriate mechanism to achieve flexibility in receipt and delivery points.

*An approach that groups receipt and delivery points into zones may be more appropriate for Australia pipelines, which have a low level of interconnection and a tendency for delivery points to be clustered.* Trading capacity within a zone would be simple. Rules to trade capacity across zones could be established.

The use of zones rather than segments should enable shippers to acquire end-to-end capacity through auctions and trades without needing to 'string' segments together.

APGA considers the defining of zones will depend on more than just physical location. Also, the characteristics of delivery points and the shippers that use each will be highly relevant. For example, a cluster of gas fired power generators will have different characteristics than a single large user facility.

### **Counterparty risk**

Counterparty risk will need to be considered and should be addressed through prudential requirements to access the trading platform.

### **Longer-term use it or lose it mechanism**

*APGA does not support the Commission's recommendation that a long-term UIOLI mechanism be reconsidered in the event that recommendations 1 and 2 fail to develop sufficient levels of trade.* In the event trade does not develop, a thorough review will be required. APGA continues to hold the position that the market characteristics of the East Coast gas market might not be conducive to liquidity, particularly the number and size of participants, and regulatory intervention will not change this.



### **Recommendation 3: Information regarding primary capacity trades to be made transparent**

To date, the recommendation to publish information regarding primary capacity trades has not been widely considered during the Review. As referenced by the Commission, only one submitter (not a market participant) has raised the issue.

APGA considers that the practice or perception of price discrimination should not be considered material:

- The cost of gas transmission has traditionally be around 20-25% of the delivered gas price for wholesale customers and 3-8% for retail customers.<sup>2</sup> These proportions are for historical gas prices, as wholesale gas prices increase the proportion of delivered gas price made up by transmission tariffs will decrease significantly. If the wholesale gas price is to double, the proportion of delivered gas made up by transmission tariffs would drop to 11-15% for wholesale customers and 2-6% for retail customers. Taking action to address concerns regarding price discrimination only in this segment of the supply chain is unlikely to address the largest contributors to any perceptions of price discrimination. Such perceptions are likely to be strongest in those segments of the market where vertical integration is more prevalent.
- All covered pipelines and many uncovered pipelines publish standard tariffs, services and terms and conditions. These pipelines include all APA and Jemena pipelines, the two main owners on the East Coast. The publishing of indicative tariffs for capacity should be acting to limiting perceptions of price discrimination.
- Price variations occur for good reasons, including the cost of new capacity and contract duration.
- Transparent secondary capacity markets, such as those seeking to be achieved by recommendations 1 and 2, serve to prevent price discrimination and limit the perception of its occurrence by:
  - Offering a viable alternative to acquiring primary capacity, limiting the potential for price discrimination in primary capacity transactions.
  - Providing increased data on price, limiting the perception of price discrimination.

***For these reasons, APGA does not accept the rationale for recommendation 3 and sees little value in the standalone publishing of pipeline primary capacity transaction.***

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<sup>2</sup> State of the Energy Market 2014 - Australian Energy Regulator



## Wholesale gas trading markets

### Southern Hub for trading gas

The recommendation to implement a virtual hub over the Victorian DTS represents a major change from existing practice and would be highly costly. *APGA can see no improvements in outcomes, compared to current arrangements, that would justify the high cost of change.* Maintaining two distinct markets over Eastern Australia will enable the existing tensions between market structures to continue.

Under the current DWGM, network access is allocated along with successful bids to the commodity auction. The key element of the Commission's recommendation in this regard is to separate the trading of gas (the commodity) from network access. This could allow non-physical participants (ie those that have no intention to either inject or deliver gas) to enter the market, which may ultimately increase headline liquidity and allow for the creation of financial hedging instruments.

While this submission does not comment directly on the concurrent DWGM review, APGA notes that the Commission has declared that transitioning the VTS to a contract carriage arrangement is too complex. APGA's preliminary analysis suggests that the transition to an entry-exit model is no less so.

### Northern Hub for trading gas

APGA supports the recommendation for the Wallumbilla Gas Supply Hub to act as the focal point for a physical northern hub. Supported by a liquid secondary capacity market, the Northern Hub represents a logical progression from existing arrangements and is likely to provide additional benefits for minimal cost.

APGA considers that the development of a supply hub at Moomba is less than ideal as it will increase complexity and dilute trading concentration.

### STTMs

APGA supports the proposed evolution of the STTMS as trading hubs and capacity markets evolve.

### Monitoring growth in market liquidity

APGA supports the establishment of metrics to measure growth in liquidity



## **Information and the Bulletin Board**

APGA supports the Commission's proposals on information and the Bulletin Board but does question the utility in dropping the BB reporting threshold for facilities to 10TJ/day. In combination with the requirement for large users to have reporting obligations, the 10TJ/day threshold will cause many market participants to have new obligations.

## **Implementation and next steps**

APGA considers the proposed timetable, with reforms to pipeline capacity markets to be implemented by 2018 to be highly ambitious. To achieve such a timeline would require well organised co-operation between government and industry participants and a much faster process than has been observed in CoAG Energy Council activity.

As acknowledged by the Commission, achieving the timeline will require industry processes to address appropriate components, such as capacity product standardisation and standardised nomination cut-off times.

APGA considers the process will be further served by requiring pipeline operators to design and implement auction mechanisms and trading platforms over their own existing systems. Clearly each pipeline operator will be required to provide equivalent services, but the need to ensure rapid and seamless transfers of capacity is best met through platforms designed to meet the specific system characteristics of each pipeline operator.

If industry-led processes are leveraged, APGA considers the design and implementation of capacity auction mechanisms and trading platforms will be relatively uncomplicated. The Commission should give serious consideration to allowing these initiatives to be implemented on a voluntary basis, under the threat of legislative and regulatory intervention if they are not delivered in the required timeframe. This would negate the need to amend the National Gas Law and the National Gas Rules or develop new AER Guidelines for various matters. This will rapidly speed implementation.

## **Indicative processes to implement recommendations**

### **Capacity Auctions**

Pipeline operators have recent relevant experience consulting with customers and stakeholders during regulatory determination processes, as required by the 2012 Economic Regulation of Network Service Providers reforms. This experience suggest a combination of private and public discussions achieve the best outcomes, as some stakeholders are more comfortable raising particular issues in private. These issues can, where appropriate, be considered by broader groups in public forums in a more effective manner.

Combined with the fact that each pipeline operators will have unique system requirements, it is appropriate that specific processes to implement capacity auctions should be run by each pipeline operator for each pipeline. There will be need the direct, individual consultation with each shipper on each pipeline to identify and manage issues relating to contracts. There will also be the need for



separate consultations with shippers as a whole and the broader group of market participants throughout the process.

Areas of commonality across all pipelines, such as the principles for conducting an auction (timing, payment, notification and publishing of results, tie break provisions etc), user interface for submitting bids, information presentation and other matters can be dealt with through an open process. There is the potential for many of these to be resolved in the remainder of the AEMC's process. Where they not, it is most efficient in pipeline operators work together to develop a draft proposal for market participant and policy make input. This serves to provide a basis for discussion and is more efficient than convening a working group and seeking to identify and solve issues through a committee with diverse participants. APGA is also willing to develop an industry standard addressing these issues. APGA offers its publication, Guidelines for the provision of operational capacity transfer services by pipeline operators (attached), as an example of an industry guideline that has been developed and used to ensure the consistent offering of a new service across pipeline operators

As APGA has noted, the management of operational issues that may arise from auctioned or traded capacity, such as overruns, renominations and balancing arrangements, have been dealt with on a pipeline specific basis during the development of the operational capacity transfer service. These do not need to be revisited.

### **Harmonisation of nomination times**

This issue is highly complex and involves all market participants, the market operator and policy makers. The interaction between the nomination times in GSAs, GTAs and facilitated markets will take time to map out, understand and identify routes to harmonisation.

The pipeline capacity recommendations can be implemented independent of harmonisation of nomination times, but are likely to be most effective if or when harmonisation is achieved.

For these reasons; the implications for all market participants and the ability to implement auctions and trading platforms independent of this reform; APGA consider this process is one that is well suited to being conducted by Government.

### **Trading Platforms**

Pipeline operators have already demonstrated their ability to implement trading platforms through industry-led processes. The recommendation in the Stage 2 Draft Report embodies a logical evolution of current platforms that industry supports.

As for capacity auctions, the process for implementing capacity trading platforms is one that should be conducted by pipeline operators and specific to each pipeline.

Issues of commonality across trading platforms will be similar to those of auctions and can be achieved through open processes and industry standards.



## **Standardisation**

### **Products**

The standardisation of products should be a relatively simple matter. With a starting point of alignment with the products offered at the Wallumbilla Supply Hub, consultation to agree on products for capacity trade should be straight forward. Some pipelines may have unique characteristics that warrant specific consideration.

### **Terms and conditions**

Each pipeline already offers standard terms and conditions. These can be analysed, in conjunction with consultation with market participants, to identify any impediments to the transport of gas across multiple pipelines. If there are any, these will need to be addressed as a matter of priority. Over time, standard terms and conditions on each pipeline can evolve to greater harmonisation on non-critical issues.

### **Flexibility in receipt and delivery points**

This is another process which needs to be managed through processes specific to each pipeline. Once high level agreement on a zone (or alternative) approach is agreed, pipeline operators will have to work with shippers to identify and propose suitable zones. These can be confirmed and refined through consultation and then incorporated into existing arrangements.

### **Implementation date**

*APGA has consulted with members and considers the above processes could achieve implementation of capacity auctions and trading platforms across all pipelines by October 2017.*