



Hon Lily D'Ambrosio MP

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Mr John Pierce
Chairman
Australian Energy Market Commission
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Dear Mr Pierce

THE VICTORIAN GOVERNMENT'S RESPONSE TO THE DRAFT REVIEW OF THE VICTORIAN DECLARED WHOLESALE GAS MARKET

The Victorian Government welcomes the Australian Energy Market Commission's (AEMC) *Draft Report – Review of the Victorian Declared Wholesale Gas Market* (Draft Report).

On 4 March 2015, the Victorian Government requested the AEMC to undertake, in consultation with the Australian Energy Market Operator (AEMO), a review of pipeline capacity, investment, planning and risk management mechanisms in the Victorian Declared Wholesale Gas Market (DWGM).

In accordance with the Terms of Reference for the review, following is the Victorian Government response to the AEMC's Draft Report.

Firstly, the Victorian Government would like to thank the AEMC for the work completed to date and would like to recognise the efforts of the staff involved in this review.

The Victorian Government notes that the AEMC's draft recommendations on developing a new Southern Hub have the potential to drive benefits including the establishment of a wholesale gas reference price that would facilitate competition and provide the tools needed by Victorian retailers and wholesale customers to manage exposure to gas prices in an export linked market.

However, for the Victorian Government to assess the draft recommendations, the following is required of the AEMC:

1. **An assessment of costs and benefits:** This will need to focus on benefits and costs to Victorian gas consumers, as well as have due consideration for impacts on smaller players and potential new entrants. It will also be critical to outline the implications and risks of not undertaking reform to the Victorian DWGM and maintaining the status quo.

2. Assess the potential implications for reform to the Victorian DWGM in the unlikely event that broader east coast gas market reform stalls.
3. Respond to questions raised by stakeholders, including requests for further design details, and the following:
 - i. How can the proposed system of entry and exit rights and the balancing market generate the necessary level of liquidity to support a well-functioning derivatives market given that there are few gas producers in Victoria?
 - ii. Given that the National Electricity Market has produced a derivatives market, why has this not occurred in the Victorian DWGM?
 - iii. How reliably can imbalance costs be allocated differentially to market participants (to create the expected incentives on market participants to balance their positions)?
 - iv. How can gas pipeline capacity hoarding be prevented in the proposed system of entry and exit rights?
 - v. How will issues of market power be addressed where there are limited players at individual entry and exit points?
 - vi. Will the proposed system of entry and exit rights create barriers to entry and how does the proposed model compare with the existing DWGM in terms of barriers to entry?
 - vii. Do existing entry-exit trading systems that are applied in other jurisdictions feature participation by small retailers?
 - viii. Are there any trade-offs between economic efficiency and system security?
 - ix. How will the Southern Hub improve gas procurement options for gas users and small retailers?

The Victorian Government recognises that the above actions will require additional consultation with stakeholders and further analysis. Accordingly, the AEMC is granted an extension to complete the review with a Draft Final Report due by 14 October 2016. Following this, the Victorian Government requests that a stakeholder consultation is held on the Draft Final Report before a Final Report is issued.

As noted by the AEMC, there is further work to finalise design and transitional issues. The Victorian Government would like the AEMC to outline how it plans to resolve key design issues and other matters relating to information requirements, transitional arrangements for existing market participants and technical and systems requirements. Articulating a clear process for addressing design and implementation issues will provide confidence to participants that resolving outstanding issues will occur in a consultative manner.

It is paramount that AEMO is fully consulted on potential security of supply issues for Victorian business and households. Furthermore, given that the Victorian DWGM is currently operated by AEMO, it will also be important for AEMO to continue to assist with the development of the proposed recommendations and associated design issues, as they

are likely to have new roles and responsibilities under the proposed recommendations. It will also be important to consult closely with the AER.

Victoria is strongly committed to pursuing reforms in the Victorian DWGM that can ensure it continues to be effective, competitive and transparent for market participants and that price and service benefits are delivered to Victorian business and households.

If you require further information, please contact Mark Feather, Executive Director, Energy Policy and Programs Branch, of the Department of Economic Development, Jobs, Transport and Resources on telephone (03) 9092 1880.

Yours sincerely



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