RULE CHANGE

Australian Energy Market Commission

RULE DETERMINATION

National Gas Amendment (STTM Settlement Surplus and Shortfall) Rule 2014

Rule Proponent

Australian Energy Market Operator

3 April 2014

For and on behalf of the Australian Energy Market Commission

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About the AEMC

The Council of Australian Governments (COAG), through its then Ministerial Council on Energy (MCE), established the Australian Energy Market Commission (AEMC) in July 2005. In June 2011, COAG established the Standing Council on Energy and Resources (SCER) to replace the MCE. The AEMC has two main functions. We make and amend the national electricity, gas and energy retail rules, and we conduct independent reviews of the energy markets for the SCER.

Summary

The Australian Energy Market Commission (AEMC or Commission) has determined to make a rule (a more preferable rule), that sets out a principle for the allocation of any settlement surplus or shortfall to Trading Participants in the Short Term Trading Market (STTM) for gas. The principle in the rule as made, acknowledges that settlement surpluses and shortfalls can arise from circumstances that are either:

- within Trading Participants' reasonable control and for which they are responsible (such as, deviations); or
- beyond Trading Participants' reasonable control (such as, counteracting Market Operator Service (MOS) and contingency gas).

By allowing for the efficient allocation of risk associated with STTM settlements, the rule as made will promote the economically efficient operation of the STTM. These provisions will be effective from 1 November 2014.

AEMO requested a rule change to amend the National Gas Rules (NGR) to rectify unintended potential financial consequences for Trading Participants arising from a rule made in June 2013.[1] This rule (rule 464(2A)) sets out the principle that guides the allocation of any settlement surplus or shortfall to STTM Trading Participants. AEMO sought amendments to this rule that would allow for, what AEMO terms, as the equitable allocation of settlement surplus payments and shortfall charges, while still supporting the original policy objective of the June 2013 rule change[2] (that is, promotion of the "causer pays" principle).[3] AEMO also proposed transitional provisions that would delay the effective date of the June 2013 rule change,[4] and the proposed rule change (if made), until 1 November 2014.

AEMO also requested that the rule change request be considered as an urgent rule change.

The Commission has determined to make a more preferable rule to that proposed by AEMO. The Commission considers that the more preferable rule provides for a clearer approach to efficiently allocating risk associated with STTM settlements, as it:

- explicitly includes the "causer pays" principle as a basis for allocating the settlement surplus and shortfall (arising from deviations);

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1 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

2 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

3 The term "causer pays" refers to the economic principle that describes an approach to allocating costs. Under the causer pays principle, costs are allocated to parties that caused the cost in the first instance. This approach is considered to result in an efficient and equitable allocation of costs, and therefore, efficient market outcomes.

4 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

- acknowledges that the settlement surplus and shortfall may arise from circumstances that are beyond the reasonable control of Trading Participants (arising from counteracting MOS and contingency gas), in which case they should be recovered proportionally from all market participants;
- makes provision for the incorporation of a settlement surplus cap in the STTM Procedures, if required, to maintain incentives for Trading Participants to act in a manner that is consistent with their allocated gas market schedules;

and so better achieves the National Gas Objective.

Including the "causer pays" principle as a basis for allocating the settlement surplus and shortfall is consistent with the Commission’s intended outcomes for the rule made in June 2013.[5]

The rule as made also avoids the need for transitional provisions because it “undoes” the rule made in June 2013,[6] then “re-makes” the majority of that rule with the addition of the new rule 464(2A). That is, the part of the made rule that “undoes” the June 2013 rule change[7] commences on 1 May 2014, whereas the part of the rule made that “re-makes” the majority of the June 2013 rule change[8] with the addition of the new rule 464(2A) commences on 1 November 2014.

5 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

6 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

7 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

8 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

Contents

1 AEMO's rule change request

1.1 The rule change request

On 1 November 2013, the Australian Energy Operator (AEMO, or the proponent) made a request to the Australian Energy Market Commission (AEMC, or Commission) to make a rule in relation to the Short Term Trading Market (STTM) for gas (rule change request). Specifically, AEMO requested an amendment to the National Gas Rules (NGR) which sets out a principle for the allocation of any settlement surplus or shortfall to STTM Trading Participants.[9]

The proponent also requested that the rule change request be considered as an urgent rule under section 304 of the National Gas Law (NGL).[10]

1.2 Rationale for the rule change request

In this rule change request, the proponent seeks to rectify unintended potential financial consequences for STTM Trading Participants arising from a rule made in June 2013[11] (namely, rule 464(2A)), prior to that rule starting on 1 May 2014.[12]

The previously made rule introduced a principle (that is, the "causer pays" principle) to guide the allocation of any settlement surplus or shortfall between STTM Trading Participants.

In the STTM, settlement surpluses and shortfalls may arise from circumstances that are either:

- within Trading Participants' reasonable control and for which they are responsible (such as, deviations); or
- beyond Trading Participants' reasonable control (such as, counteracting MOS and contingency gas).[13]

AEMO considers the rule in its current form is likely to lead to the disproportionate distribution of settlement shortfall charges to STTM Trading Participants where costs are not attributable to identifiable causes (such as those that may arise from counteracting MOS and contingency gas).[14]

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9 A STTM Trading Participant is a party with a financial role in the STTM, which can either be an STTM shipper or STTM user (AEMO, STTM Glossary of Terms v3.0, 1 December 2011, p.11).

10 AEMO, rule change request cover letter, 31 October 2013, p.1.

11 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

12 AEMO, rule change request cover letter, 31 October 2013, p.1.

13 Counteracting MOS and contingency gas are explained further at Appendix A.

14 AEMO, rule change request, 31 October 2013, p.4.

1.3 Solution proposed in the rule change request

The rule proponent, AEMO, proposes to resolve the issues referred to above by requesting a rule that seeks to amend the NGR, specifically:

- rule 464(2A), to provide a principle which will enable, what AEMO terms, the equitable allocation of settlement surplus payments and shortfall charges; and
- to include transitional provisions that delay the effective dates of the June 2013 rule change,[15] and the proposed rule change (if made), until 1 November 2014. This is for the purpose of avoiding adverse market outcomes and improving the administrative efficiency of the STTM.[16]

The proponent's rule change request seeks to amend one component of the June 2013 rule change.[17] This would allow AEMO to develop and consult on proposed STTM Procedures that permit the allocation of settlement surpluses and shortfalls under all circumstances, while still supporting the "causer pays" principle.

1.4 Commencement of the rule making process

On 20 February 2014, the Commission published a notice under sections 303 and 304 of the National Gas Law (NGL) advising of its intention to commence the rule making process, and to expedite the proposed rule as an urgent rule (subject to any written requests not to do so), respectively. No objections to the rule being considered as an urgent rule were received by the due date of 6 March 2014.

At the same time that the rule change request was published, an AEMC consultation paper was published, identifying specific issues or questions for public consultation. Submissions closed on 20 March 2014. The Commission received four submissions from stakeholders on the rule change request, all of which are available on the AEMC website.[18] A summary of the issues raised in submissions, and the Commission's response to each of those issues raised, is contained in Appendix B.

15 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

16 AEMO, rule change request, 31 October 2013, p.9.

17 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

18 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 AEMO. In accordance with section 313 of the NGL, the Commission has determined not to make the rule proposed by the proponent, and to make a more preferable rule.[19] The Commission's reasons for making this final rule determination are set out in chapter 3.

The *National Gas Amendment (STTM Settlement Surplus and Shortfall) Rule 2014 No. 2* (rule as made) is published with this final rule determination. The part of the rule as made that "undoes" the June 2013 rule change[20] commences on 1 May 2014, whereas the part of the rule as made that "re-makes" the majority of the June 2013 rule change[21] with the addition of the new rule 464(2A) commences on 1 November 2014. The key features of the rule as made are described in section 3.4.

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;
- stakeholder submissions received during consultation;
- the final rule determination relating to the National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4; 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).

There is no relevant Ministerial Council on Energy (MCE) Statement of Policy Principles relating to this rule change request.[22]

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19 See section 2.5 of this final rule determination for the meaning of a more preferable rule.

20 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

21 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

22 Under section 73 of the NGL, the AEMC must have regard to any relevant MCE Statement of Policy Principles in making a rule.

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. The rule as made falls within the matters set out in section 74 of the NGL. More specifically, it relates to:

- the operation of a STTM of an adoptive jurisdiction (section 74(1)(a)(va) of the NGL); and
- the activities of Registered Participants, users, end users and other persons in a regulated gas market (section 74(1)(a)(vi) of the NGL).

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."

The Commission considers that the relevant aspect of the NGO for this rule change request is the efficient operation of, and efficient investment in, natural gas services for the long term interests of consumers of natural gas with respect to price.[23]

The Commission is satisfied that the rule as made will, or is likely to, contribute to the achievement of the NGO by:

- Reducing the financial risks of participating in the STTM.
  - This is achieved by recovering settlement shortfalls and distributing settlement surpluses based on total deviations (that is, applying the "causer pays" principle), and the socialisation of costs and risks that are outside the reasonable control of Trading Participants in a proportionate manner. Allocating costs/risks and surpluses in this way contributes to the efficient operation of natural gas services; particularly for surplus allocation as it promotes more efficient behaviour by Trading Participants in the way they manage their deviations.
- Not creating, or avoiding any further, barriers to entry to the STTM.

23 Under section 291(2), 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 Statement of Policy Principles.

— The proportionate allocation of financial risk potentially limits unnecessary hedging costs incurred by Trading Participants, thereby not creating, or avoiding any further, barriers to entry to the STTM for potential Trading Participants. This promotes efficient investment in gas services.

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 network functions. The rule as made is compatible with AEMO's declared network functions because it has no impact on them.

2.5 More preferable rule

Under section 296 of the NGL, the AEMC may make a rule that is different (including materially different) from a market initiated proposed rule (a more preferable rule) if the AEMC is satisfied that, having regard to the issue or issues that were raised by the market initiated proposed rule (to which the more preferable rule relates), the more preferable rule will, or is likely to, better contribute to the achievement of the NGO.

Having regard to the issues raised by the proposed rule, the Commission is satisfied that the rule as made will, or is likely to, better contribute to the NGO.

It promotes the efficient operation of the STTM, and efficient investment in natural gas services, by allocating any settlement surpluses or shortfalls that may arise from Trading Participants' deviations, or from circumstances that are beyond the reasonable control of Trading Participants, in a more efficient manner than the proposed rule.

The proposed rule would amend rule 464(2A) to provide that the STTM Procedures must specify the basis and method for calculating the settlement surplus payment and settlement shortfall charge in accordance with the principle that, to the extent practicable, any settlement surplus or shortfall be allocated "efficiently" to Trading Participants.

The rule as made requires the STTM Procedures to allocate settlement surpluses and settlement shortfalls by efficiently allocating the proportion of any settlement surplus or settlement shortfall arising from:

- a deviation quantity, to the Trading Participants on the basis of their total deviation quantity, subject to any settlement surplus cap; and
- MOS related services or circumstances that are beyond the reasonable control of the Trading Participants (other than deviation quantities), to all Trading Participants.

By doing so, Trading Participants may be able to better manage any financial risk arising from circumstances that are beyond their reasonable control (such as, counteracting MOS and contingency gas). In addition, where deviations are caused by Trading Participants' actions in the market, then settlement surplus payments or shortfall charges can be allocated appropriately to those participants who are responsible (that is, in accordance with the "causer pays" principle).

The rule as made also avoids the need for transitional provisions because it “undoes" the rule made in June 2013,[24] then “re-makes” the majority of that rule with the addition of the new rule 464(2A). The effect of this is that, the part of the made rule that “undoes” the June 2013 rule change[25] commences on 1 May 2014, whereas the part of the rule made that “re-makes” the majority of the June 2013 rule change[26] with the addition of the new rule 464(2A) commences on 1 November 2014.

24 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

25 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

26 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

3 Commission's reasons

The Commission's analysis and assessment of this rule change request, and the rule proposed by the proponent, is set out below.

3.1 AEMO's rule change request

AEMO proposed an amendment to the principle that guides the allocation of any settlement surplus or shortfall between STTM Trading Participants. AEMO considered that the proposed rule change was required to rectify unintended potential financial consequences for STTM Trading Participants it has identified with the implementation of the rule made in June 2013.[27]

AEMO considers that implementation of the principle in the current rule 464(2A) may result in, what AEMO terms, the inequitable allocation of settlement surpluses and shortfalls between STTM Trading Participants.[28] AEMO is particularly concerned that the rule is likely to lead to the disproportionate distribution of settlement shortfall charges to STTM Trading Participants where costs are not attributable to identifiable causes (such as those that may arise from counteracting MOS and contingency gas).[29]

AEMO submitted that, without its proposed changes to rule 464(2A), there could be a transfer of risk (resulting from excessive MOS or over-scheduling of contingency gas) from larger to smaller STTM Trading Participants. It has estimated that this risk transfer may be valued at up to $200,000 in a single month.[30]

AEMO considered its proposed amendments to rule 464(2A) would allow it to develop and consult on possible changes to the STTM Procedures that:

- permit the allocation of settlement surpluses and shortfalls in a way that is, what AEMO terms, equitable under all circumstances, while still supporting AEMO's policy objective of promoting the "causer pays" principle in STTM settlements.[31]
- allow financial risks caused by factors outside the control of Trading Participants (such as, counteracting MOS and contingency gas) to be allocated appropriately, such that no parties are faced with a disproportionate risk.

AEMO considered that its proposed rule change would not increase, or decrease, total costs in the STTM. Rather, the proposed rule change would improve the method for allocating costs.[32] AEMO submitted that the administrative costs for implementing the

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27 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

28 AEMO, rule change request cover letter, 31 October 2013, p.1.

29 AEMO, rule change request, 31 October 2013, p.4.

30 AEMO, rule change request, 31 October 2013, p.11.

31 AEMO, rule change request, 31 October 2013, pp.4&10.

32 AEMO, rule change request, 31 October 2013, p.10.

proposed rule (if made) have already been captured in the costs to implement the rule made in June 2013.[33]

3.2 Stakeholders' views

The Commission received four submissions from stakeholders on the rule change request. Submissions were received from AGL Energy (AGL), Origin Energy (Origin), Lumo Energy (Lumo) and AEMO. Stakeholders were supportive of the STTM cost allocation principles advanced by the proposed rule change.[34]

AGL supported the reasons advanced by AEMO for favouring the distribution of settlement shortfalls on the basis of withdrawals, rather than on deviations. AGL noted that settlement shortfalls arise from a number of events and design features of the market, and it is not always the case that cost can be attributed to a cause or causer. AGL submitted that this is particularly true of counteracting MOS that occurs from time to time at the Sydney and Adelaide STTM hubs. For this reason, AGL considered that allocation of settlement shortfalls based on withdrawals was the least objectionable and least discriminatory approach to adopt.[35] AGL also submitted that it preferred AEMO's drafting of rule 464(2A) over the alternative indicative rule drafting, but it did not provide a reason for its position.[36]

Origin was supportive of the proposed rule change because it considered that it is a step towards further, more beneficial STTM market reforms. In this regard, Origin submitted that it will continue to engage with AEMO and other market participants to establish the appropriate methodology to allocate the settlement surplus and shortfall.[37]

Lumo considered that, as there may be a transfer of risk of up to $200,000 in a single month (according to AEMO's estimate) from larger to smaller Trading Participants under the current rule 464(2A), this was inconsistent with the NGO.[38] For this reason, Lumo supported the proposed rule change on the basis that it will enable financial risks caused by factors outside the control of Trading Participants to be allocated appropriately; and reduce the barriers to entry in the STTM for potential new Trading Participants, especially smaller participants.[39]

AEMO was supportive of the alternative drafting for rule 464(2A) that was included in the AEMC consultation paper, subject to minor amendment. AEMO considered that

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33 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule No. 4, 2013; and AEMO, rule change request, 31 October 2013, p.11.

34 AEMO, submission, 19 March 2014, p.1, AGL, submission, 20 March 2014, p.1, Lumo Energy (Lumo), submission, 20 March 2014, p.1 and Origin Energy (Origin), submission, 20 March 2014, p.1.

35 AGL, submission, 20 March 2014, p.1.

36 AGL, submission, 20 March 2014, pp.1-2.

37 Origin Energy (Origin), submission, 20 March 2014, p.1.

38 Lumo Energy (Lumo), submission, 20 March 2014, pp.1-2.

39 Lumo Energy (Lumo), submission, 20 March 2014, p.2.

the alternative drafting meets AEMO's policy objective in regard to the allocation of the settlement surplus and shortfall, while maintaining the "causer pays" principle. AEMO suggested that, for the avoidance of doubt, the AEMC's rule drafting should be amended to specifically exclude deviations quantities from clause (b)(ii) of the rule, as deviation quantities can be caused by factors that are beyond the reasonable control of Trading Participants.[40]

3.3 Commission’s analysis of the issues

AEMO is seeking to rectify unintended potential financial consequences for STTM Trading Participants it has identified with implementation of the rule made in June 2013.[41]

Stakeholders’ submissions were supportive of the STTM cost allocation principles advanced by AEMO in its proposed rule change.[42]

The Commission has considered the views of AEMO and other stakeholders who made submissions on the rule change request.

When making the final rule determination in June 2013, the Commission intended to develop a deviation pricing framework that is supported by principles that efficiently allocate the risks associated with Trading Participants deviating from their daily gas market schedules and the consequences for the STTM.[43] Having considered the possible implications of the current rule 464(2A) when implemented, the Commission agrees that these would be inconsistent with its June 2013 final rule determination. This is because the current rule 464(2A) does not specify that the STTM Procedures allocate any settlement surpluses or shortfalls to Trading Participants arising from circumstances that are, on the one hand, within their reasonable control and for which they are responsible, and on the other hand, beyond their reasonable control (such as, counteracting MOS and contingency gas). Accordingly, the Commission agrees that an amendment to the current rule 464(2A) should be made.

3.4 Commission’s analysis of the proposed rule and conclusion

The proposed rule does not resolve the problem identified. It does not provide for a clear principle for differentiating the allocation of any settlement surpluses or shortfalls to STTM Trading Participants arising from circumstances that are: within their reasonable control and for which they are responsible; and beyond their reasonable

40 AEMO, submission, 19 March 2014, p.1.

41 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No. 4.

42 AEMO, submission, 19 March 2014, p.1, AGL, submission, 20 March 2014, p.1, Lumo Energy (Lumo), submission, 20 March 2014, p.1 and Origin Energy (Origin), submission, 20 March 2014, p.1.

43 See aemc.gov.au, *STTM Deviations and the Settlement Surplus and Shortfall*, final rule determination, GRC0014, published 20 June 2013.

control. Rather, it would simply require any settlement surplus or shortfall to be allocated “efficiently” to Trading Participants.

An alternative approach to the drafting of rule 464(2A) was included in the AEMC's consultation paper for the purpose of attaining stakeholder feedback.

The Commission considers that a rule which provides for a clearer approach to efficiently allocating risk associated with STTM settlements, is preferable as it would:

- explicitly include the "causer pays" principle as a basis for allocating the settlement surplus and shortfall (arising from deviations);
- acknowledge that the settlement surplus and shortfall may arise from circumstances that are beyond the reasonable control of Trading Participants (arising from counteracting MOS and contingency gas), in which case they should be recovered proportionally from all market participants;
- makes provision for the incorporation of a settlement surplus cap in the STTM Procedures, if required, to maintain incentives for Trading Participants to act in a manner that is consistent with their allocated gas market schedules;[44]

and so better achieves the NGO.

Including the "causer pays" principle for deviations, and as a basis for allocating the settlement surplus and shortfall, is consistent with the Commission’s intended outcomes for the rule made in June 2013.[45]

The costs associated with implementing such a rule to the market as a whole would be negligible. It would have an impact on how the settlement surplus and shortfall is allocated to individual Trading Participants, but would not adversely impact the operation of the market as a whole.

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44 The need for this provision arose from informal discussions between AEMO and the AEMC prior to the inclusion of the provision in the alternative indicative rule drafting in the AEMC consultation paper. These discussions identified that such a provision was required in order for the rule to maintain incentives for Trading Participants to meet their allocated gas market schedules, and for the rule to be workable over time.

45 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No.4.

Abbreviations

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
Commission	See AEMC
MOS	market operator service
MSV	market schedule variation
NGL	National Gas Law
NGO	National Gas Objective
NGR	National Gas Rules
Proponent	See AEMO
Rule	See NGR
STTM	Short Term Trading Market

A Background

For the purpose of assisting stakeholders' understanding of this rule change, this appendix provides descriptions of the STTM, and payments and charges related to the balancing the STTM.

A.1 The Short Term Trading Market

The STTM is a "day ahead" market, whereby gas is traded a day before the actual "gas day" (that is, the day the gas is scheduled to flow). This means that relevant activities take place before (ex-ante), on (intra) and after (ex-post) each individual gas day.

The day before any gas day, pipeline operators submit pipeline capacity information to AEMO, who publishes this data to the market on its website.

STTM users (e.g., gas retailers) and shippers (e.g., gas wholesalers) can then place "bids" to buy quantities of gas at the STTM hub,[46] and STTM shippers can place "offers" to sell quantities of gas to the hub.

On the basis of the above information, AEMO matches offers and bids, determines the ex-ante market price and draws up the initial market schedule for the flow of gas to and from the hub on the gas day. All the gas that is supplied and withdrawn, according to the market schedule, is settled at the ex-ante market price.

The market schedule is published by AEMO approximately 18 hours ahead of the gas day, so that shippers can use this information to nominate the quantity of gas they require to be transported by each pipeline operator (note, a process which occurs outside of the STTM). Pipeline operators then prepare pipeline allocation schedules, detailing the quantities of gas to be delivered to each shipper on each pipeline on the gas day.

On the gas day, shippers supply gas to the hub, and users withdraw gas from the hub. Shippers and users are able to re-nominate expected changes to their gas forecasts to pipeline operators during the gas day. The STTM has a market schedule variation (MSV) mechanism which allows these re-nominations to be recognised in the market. The variation must be matched by an opposite variation from either another shipper or user.[47]

46 A notional gateway in the gas supply system defined by custody transfer points between pipelines and distribution systems at which the STTM schedules gas deliveries and withdrawals (AEMO, STTM Glossary of Terms v3.0, 1 December 2011, p.5).

47 AEMO, rule change request, 31 October 2013, p.2; and AEMO, Overview of the Short Term Trading Market v4.2, 14 December 2011, p.12.

A.2 Payments and charges related to balancing the STTM

A.2.1 Settlement surplus and shortfall

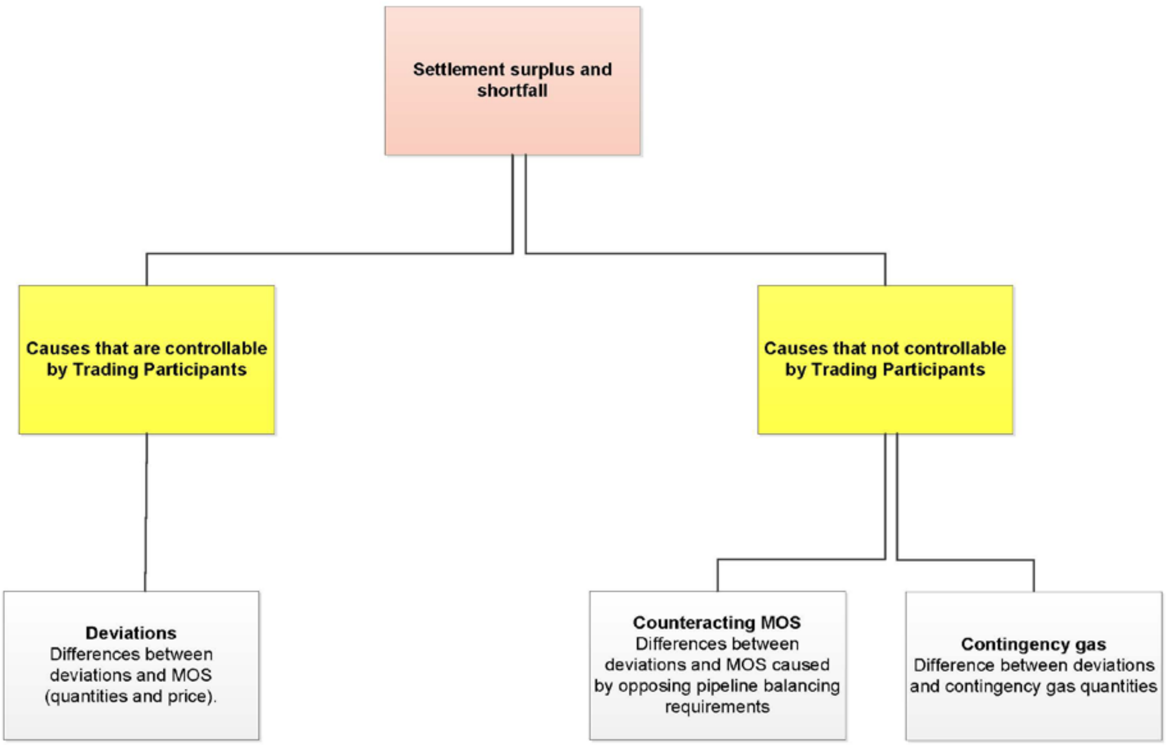
Settlement surplus payments and settlement shortfall charges are funds that accrue over a STTM monthly billing period, which result from differences between STTM market income and market outgoings.

Over the monthly billing period, AEMO accumulates the daily settlement surplus and shortfall at a STTM hub. AEMO then distributes the net settlement surplus (over-collection) or shortfall (under-collection) to Trading Participants at the end of the month. This is to ensure that over each month, the total market revenue balances the total market expenses.

Settlement surplus and shortfall is caused by differences in the way market operator service (MOS), deviations and contingency gas (defined in the following sections) are priced and balanced.[48] These differences result from circumstances that are either controllable by Trading Participants (such as, deviations), or are not controllable by Trading Participants (such as, counteracting MOS and contingency gas).

Figure A.1 shows the various factors that can lead to a settlement surplus or shortfall.

Figure A.1 Causes of settlement surplus and shortfall



48 AEMO, rule change request, 31 October 2013, pp.2&4.

A.2.2 Factors that are controlled by Trading Participants

The primary cause of the settlement surplus or settlement shortfall is deviations. Deviations are a direct result of Trading Participants' activities in the marketplace.

Deviations

Deviations are the difference between quantities of gas allocated to Trading Participants and the market schedule (after adjustments for any MSVs). Deviations from the nominated schedules generally incur a financial penalty. This is to incentivise trading participants to forecast as accurately as possible and meet their gas schedules, and to recognise the costs caused by deviations.[49]

Market operator service (MOS)

If there is a deviation on a pipeline, the gas that is necessary to balance that deviation is provided (or withdrawn) by MOS. MOS is provided by Trading Participants who have contracts with a pipeline operator that enables them to vary the quantity of gas supplied from the pipeline or stored on the pipeline. MOS is managed by AEMO and is dispatched with reference to separate MOS stacks for "increase MOS" (where additional gas needs to be delivered to the hub) and "decrease MOS" (where excess gas needs to be withdrawn from the hub).

Differences in the way deviations are priced, and how MOS is priced, can result in either a settlement surplus or shortfall, as there is not a single clearing price for balancing gas (the difference between scheduled and actual flows) after the gas day.[50]

As deviations are a direct result of Trading Participants' activities in the marketplace, any settlement surplus or shortfall resulting from deviations can be allocated to Trading Participants on the basis of their total deviations for the month – that is, applying the "causer pays" principle.[51] The "causer pays" principle was the policy intent of the June 2013 rule change[52] with respect to providing a guiding principle for the allocation of settlement surplus and shortfall.

A.2.3 Factors that are not controlled by Trading Participants

The settlement surplus or settlement shortfall may also be caused by factors that are outside the control of Trading Participants. These factors, such as counteracting MOS and contingency gas, can result in costs which AEMO, in its rule change request,

49 AEMO, rule change request, 31 October 2013, pp.2&4.

50 AEMO, rule change request, 31 October 2013, p.2.

51 The term "causer pays" refers to the economic principle that describes an approach to allocating costs. Under the causer pays principle, costs are allocated to parties that caused the cost in the first instance. This approach is considered to result in an efficient and equitable allocation of costs, and therefore, efficient market outcomes.

52 The National Gas Amendment (STTM Deviations and the Settlement Surplus and Shortfall) Rule 2013 No.4.

regards as general market operational costs, and therefore should be "socialised" among Trading Participants according to their withdrawals.[53]

Counteracting MOS

Counteracting MOS occurs where there are two pipelines supplying a STTM hub (for example, Sydney and Adelaide). Circumstances may arise as a result of each pipeline's opposing balancing requirements, such that the MOS that is acquired is in excess of the hub's balancing requirements. In such circumstances, as there will be more MOS to be paid for than there are deviations in the market, the market will accrue a settlement shortfall. AEMO's view, in its rule change request, is that counteracting MOS appears to be caused by factors related to the physical characteristics of the pipeline, rather than particular actions taken by individual Trading Participants.[54]

Contingency gas

Contingency gas is called upon when MOS arrangements are unlikely to meet the balancing requirements of the market.[55] That is, AEMO can call on additional gas supplies, or withdrawals, to balance the market and safeguard the continuity of supply.

Where deviation quantities are greater than the amount of contingency gas scheduled for a particular gas day, then a settlement surplus may result. Conversely, where deviation quantities are less than the amount of contingency gas scheduled, then a settlement shortfall may result.[56]

53 AEMO, rule change request, 31 October 2013, pp.3–5.

54 AEMO, rule change request, 31 October 2013, pp.3&5.

55 Contingency gas is defined as the increase or decrease in the quantity of gas, which is supplied or withdrawn from a hub by a Trading Participant in accordance with the rules, to address a contingency gas requirement (rule 364 of the NGR).

56 AEMO, rule change request, 31 October 2013, p.5.

B Summary of issues raised in submissions

Stakeholder	Issue	AEMC response
Australian Energy Market Operator (AEMO), AGL Energy (AGL) and Origin Energy (Origin)	*Achievement of the proponent's policy objective?* AEMO was supportive of the alternative indicative drafting for rule 464(2A), subject to minor amendment. It considered that the alternative drafting meets AEMO's policy objective of providing for the equitable allocation of settlement surplus and shortfall in circumstances where costs and risks may be beyond the control of Trading Participants, while still supporting the "causer pays" principle. AEMO suggested a minor amendment to clause (b)(ii) of the alternative drafting of rule 464(2A). AGL was supportive of the proposed rule change and favoured it over the alternative drafting of the rule, but did not provide reasons for its position. AGL supported the reasons advanced by AEMO for favouring the distribution of settlement shortfalls on the basis of withdrawals rather than on deviations. It noted that settlement shortfalls arise from a number of events and design features of the market, and it is not always the case that cost can be attributed to a cause or causer. AGL submitted that this is particularly true of counteracting MOS that occurs from time to time at the Sydney and Adelaide STTM hubs. For this reason, AGL considered that allocation of settlement shortfalls based on withdrawals is the least objectionable and least discriminatory approach to adopt. Origin was supportive of the proposed rule change because it considered that it is a step towards further, more	The Commission considers that AEMO's suggested change to the alternative drafting of rule 464(2A) improves the clarity of the rule. The Commission considers that the benefit of the rule as made is that it will better promote the NGO by allocating settlement surplus and shortfall between Trading Participants in a more efficient manner. This is because, the rule as made will allow AEMO to develop and consult on STTM Procedures to allocate settlement surplus and shortfall appropriately in all circumstances, including those circumstances that are beyond the reasonable control of Trading Participants. By doing so, Trading Participants may be able to better manage any financial risk arising from circumstances that are beyond their reasonable control (such as, counteracting MOS and contingency gas). However, where deviations are caused by Trading Participants' actions in the market, then settlement surplus payments or shortfall charges can be allocated appropriately to those participants who are responsible (that is, in accordance with the "causer pays" principle).

Stakeholder	Issue	AEMC response
	beneficial STTM market reforms. In this regard, Origin submitted that it will continue to engage with AEMO and other market participants to establish the appropriate methodology to allocate settlement surplus and shortfall.	
Lumo Energy (Lumo)	*Efficient allocation of risk between Trading Participants* Lumo considered that, as there may be transfer of risk of up to $200,000 in a single month (according to AEMO's estimate) from larger to smaller Trading Participants under the current rule 464(2A), this was inconsistent with the NGO. For this reason, Lumo supported the proposed rule change on the basis that it will: • enable financial risks caused by factors outside the control of Trading Participants to be allocated appropriately; and • reduce the barriers to entry in the STTM for potential new Trading Participants, especially smaller participants.	 As per the Commission's comments above.