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A few words.

12 February 2016

John Pierce
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Submitted online via www.aemc.gov.au

Reference GPR0003

Dear Mr Pierce

East Coast Wholesale Gas Market and Victorian Declared Wholesale Gas Market Reviews

AGL welcomes the opportunity to comment on the Australian Energy Market Commission's (AEMC) East Coast Wholesale Gas Market and Pipeline Frameworks Review (Stage 2 Draft Report) and Review of the Victorian Declared Wholesale Gas Market (DWGM) (Draft Report).

AGL is one of Australia's leading integrated energy companies and largest ASX listed owner, operator and developer of renewable generation. Our diverse power generation portfolio includes base, peaking and intermediate generation plants, spread across traditional generation fuel sources as well as renewable sources. AGL is also a significant retailer of energy, providing energy solutions to over 3.7 million customers throughout eastern Australia.

AGL has a long history of involvement in Eastern Australian gas markets and aside from delivering gas to its numerous customers, AGL also utilises gas in power generation, is a gas 'shipper' and owns gas facilities. AGL has also actively participated in the various gas market reviews including the ACCC East Coast Gas Market Review. The views expressed in this submission leverage on AGL's considerable market experience and previous contributions to the policy debate.

AGL wholly supports the Council of Australian Government Energy Council's 'Vision' of a liquid wholesale gas market – including the ability to readily move gas between trading locations. Accordingly, AGL sees merit in addressing the shortcomings identified by the AEMC in the current gas systems.

However, AGL considers that further detail on the proposed reforms must now be developed with further inclusion of industry. This will allow a more comprehensive understanding of the effects of the proposed reforms. Including potential impacts of the measures, outcomes intended to be achieved and, importantly, the completion of a cost-benefit analysis. For example, the interaction between the proposed capacity trading/auction market and the gas trading markets must be worked through with greater clarity, such that participants understand the interactions and market operation with greater confidence. The provision of such detail may also encourage more comprehensive feedback on the proposed reforms.

The following sets out AGL's considered position on the proposed reforms.

Southern Hub for Wholesale Trading: Including entry and exit rights

AGL is not convinced that the introduction of a voluntary exchange based trading platform in the DWGM would improve liquidity. AGL considers that the formalisation of trading with the DWGM has actually led to transparency. A voluntary platform may actually diminish utilisation thereby diluting transparency and adversely impacting efficiency. AGL suggests that further consideration is given as to how participants would be encouraged to trade in the exchange to avoid diminishing the existing levels of transparency in the DWGM.

Other market elements, such as the value of the imbalance charge and the role of hub operator, also require further thought. AGL appreciates that one of the aims of the imbalance charge is to encourage participants to ensure that their position remains in balance. However, a prohibitive imbalance charge may act as a barrier to entry. Further, AGL considers that AEMO should retain the function of hub operator with responsibility for balancing the market. This will ensure the stable provision of this service, and is in line with their existing remit and experience as an energy market operator.

Finally, whilst eventually there may be merit in not having a fixed balancing period, in the short term while liquidity is still growing, there is likely to be merit in its continuation. AGL would, however, be open to a study to look into altering the existing DWGM trading periods, for example to 6am-2pm-6pm in order to simplify the balancing process.

Entry and Exit Capacity Rights Model

AGL is more cautious with regards to replacing the existing open access capacity model in the DWGM, with an entry and exit capacity rights model. AGL does not consider that it has been clearly demonstrated in the Draft Report that there is a definitive problem with pipeline investment in the DWGM to actually warrant the change. AGL considers that there may be other avenues to consider in the first instance – such as clearer pricing signals and adjustments to market constraint procedures within the DWGM, than changing the market design.

The proposed changes will also require the trading of numerous entry and exit capacity rights – in addition to the trading of gas on a separate exchange – this will significantly increase transaction costs, market complexity and could be counterproductive in achieving the COAG EC 'Vision' – by creating a barrier to new entrants.

Should the entry/exit model be pursued, and ultimately implemented, framing of will need to ensure that participants can manage long term pipeline capacity that aligns with supply contracts. The inability to do so would create significant risk for participants when entering into these contracts.

Further consideration is also required in relation to the issue of the allocation of appropriate levels of firm and interruptible.

Finally, AGL supports the grandfathering of existing Authorised Maximum Daily Quantity (AMDQ) rights and credits into any new model for pipeline capacity access, in order to ensure a smoother transition and to appropriately recognise historic investments.

Northern Hub for Wholesale Trading

AGL supports the recommendation to concentrate trading in the Northern region of the East Coast gas market at the Wallumbilla Gas Supply Hub. AGL also notes the ongoing AEMO work program in this space, including the design and implementation of the Moomba Hub.

With regards to the implementation of additional gas supply hubs (GSH), AGL agrees with the AEMC's statement that additional GSH locations are not necessarily 'a long term solution for promoting the Energy Council's Vision'[1].

AGL also has reservations regarding the recommendation to proceed with the Optional Hub Services at Wallumbilla. The limited providers of hub services in the region may not result in increased liquidity at the hub. If the hub services model is introduced, this function should be independently operated and, if necessary, regulated. AGL also supports increasing commonality of the Short Term Trading Markets (STTMs) and implementing changes that complement wider energy market changes (such as balancing markets).

Pipeline Capacity Markets

AGL is broadly supportive of the proposed reforms for pipeline capacity trading outside of the DWGM, however AGL notes that risks associated with making the pipeline capacity market more liquid should not just borne by gas retailers, but by the pipeline owners as well.

In addition, AGL has concerns with regards to the daily auction for contracted but un-nominated capacity without greater consideration of the balancing period. AGL considers that this proposal may have limited take up and may adversely impact re-nomination rights. Renomination rights are contractually defined and assist those who hold them in dealing with any short term changes in their gas needs – they are an effective risk management tool. Removing, or hindering, re-nomination rights would simply create extra risk for market participants in managing their gas needs.

It is also unclear to AGL as to the extent of the market for the un-nominated capacity, particularly during low gas demand periods – at such times there is likely to be limited demand for pipeline capacity. Conversely, in peak demand periods, the full contracted capacity may be nominated by the shipper, which will mean there will be limited un-nominated capacity to auction.

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[1] AEMC 2015, *East Coast Wholesale Market and Pipeline Frameworks Review, Stage 2 Draft Report*, 4 December 2015, Sydney, p. 90.

AGL considers further that the AEMC should be open to the seller of contracted un-nominated capacity being the holder of the capacity, for the purposes of the auction, rather than the pipeline owner – as currently proposed. This would ensure appropriate compensation is paid directly to the shipper, resulting from changes to access rights, without unnecessarily increasing transaction costs.

There also exists the perception that shippers 'hoard' pipeline capacity in order to limit competition. However, AGL considers that this view does not actually recognise that contracting capacity is a prudent risk management strategy in the face of highly variable gas demand (a retailer must purchase sufficient gas and capacity to service their supply contracts of their peak demand) and that such a strategy has an opportunity cost – any capacity withheld where demand for such capacity exists equates to revenue foregone.

AGL supports the further development of the online exchange for secondary capacity rights. AGL is also supportive of the idea of creating secondary delivery points, as this will greatly aid the fungibility and liquidity of capacity trading. If secondary delivery and receipt points are available on gas transport agreements, then segmentation of pipeline capacity may not be necessary.

Finally, the proposed test to ascertain whether reform has resulted in sufficient liquidity in accessing capacity must also be re-considered. It is not realistic to expect a nascent market, such as the secondary gas market, to satisfy the measures of liquidity set out in the criteria and it is doubtful whether many established markets – including electricity – satisfy them[2]. Further, the consequence for not meeting the criteria is the introduction of 'Use it or Lose it' for capacity rights – which AGL considers unnecessary and heavy-handed.

Information and the Bulletin Board

AGL is generally supportive of the additional information that the AEMC recommends be published on the Bulletin Board, including information on compressor outages and upstream information such as proven and probable reserves.

In terms of new pipelines, there should be a capacity threshold test to determine whether a new pipeline should be included on the Bulletin Board. However, AGL does not agree with extending information requirements to include consumption by users, as this is commercially sensitive information. For example, it could reveal commercial positions in either energy markets and likely serves no real benefit to the market overall.

AGL also supports the initiative to make data more up to date including placing greater responsibility on AEMO to ensure information is up to date. AGL also sees merit in conducting a trial of a real time or intra-day reporting model.

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[2] It is questionable whether even a liquid market such as the electricity forward market can satisfy the equivalent of two out of the four liquidity criteria, namely 1. That there needs to be greater than 15 trades per day per product per region so that the price signal can be considered trustworthy and 2.That the amount of the product offered/requested for on a hub is greater than 10,000GJ, *AEMC East Coast Wholesale Gas Market and Pipeline Frameworks Review- Stage 2 Draft Report*, p.98.

In relation to outage information, AGL agrees with the recommendation to require any material changes to a facility's capacity during a gas day to be reported as soon as practicable on that day. Additionally, it would greatly benefit the market to have more detailed information on outages and for it to be published in a standardised way–similar to the Projected Assessment of System Adequacy (PASA) in the wholesale electricity market and for it to be presented in a manner that enables participants to use it i.e. to create alert systems

Finally, AGL also supports the introduction of a reporting standard that is based on the same 'good gas industry practice' standard that applies in the STTM, which would include for example an obligation for parties to undertake reasonable endeavours to honour information that it posts on the Bulletin Board. However, AGL notes that these measures must be balanced against the costs of introducing them.

Conclusion

In conclusion, AGL considers that many of the proposed reforms tabled by the AEMC have merit and would contribute to delivering the Energy Council's gas market Vision. However, further detail on the package of reforms must now be produced, in order to ensure that intended benefits can be delivered and a thorough cost/benefit analysis undertaken – in order to critically assess the reforms. It is also worth noting that any conclusions that come from the ACCC East Coast Gas Market review in relation to upstream gas activities will impact the East Coast market and the AEMC's proposed reforms.

If you have any queries about the submission or require further information, please contact Josynta Singh at jsingh@agl.com.au or on 03 8633 6628.

Yours sincerely,

Simon Camroux
Manager Wholesale Markets Regulation