AEMC

RULE CHANGE

Australian Energy Market Commission

DRAFT RULE DETERMINATION

National Gas Amendment (Portfolio Rights Trading) Rule 2014

Rule Proponent

Australian Energy Market Operator

19 June 2014

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About the AEMC

The AEMC reports to the Council of Australian Governments (COAG) through the COAG Energy Council. We have two functions. We make and amend the national electricity, gas and energy retail rules and conduct independent reviews for the COAG Energy Council.

Summary

The Australian Energy Market Commission (AEMC or Commission) has made this draft rule determination to promote more efficient utilisation of transmission pipeline capacity and thereby defer the need for new pipeline investment in the Victorian declared transmission system (DTS). This is in response to the portfolio rights trading rule change request (rule change request) submitted by the Australian Energy Market Operator (AEMO) on 13 November 2013.

Portfolio rights trading (PRT) would enable market participants to transfer all or part of their portfolio of financial benefits associated with holding authorised MDQ (AMDQ) and AMDQ credit certificates (AMDQ cc) to other market participants operating in the Victorian declared wholesale gas market (DWGM).[1] Physical ownership of AMDQ and AMDQ cc and any associated curtailment rights would remain unchanged by PRT.

Details of the rule change request

The Victorian DTS is the only pipeline operating under a market carriage model in Australia. Under this model, market participants utilising the DTS cannot reserve firm capacity on the pipeline. However, they may hold AMDQ or AMDQ cc which provide certain financial and market benefits, and some limited physical benefits. The financial and market benefits include priority in scheduled injections (injection tie-breaking rights) and reduced uplift payments (uplift hedge protection).

AEMO has identified a number of barriers which it considers currently limit the ability of market participants to acquire AMDQ and AMDQ cc to meet their injection tie-breaking and uplift hedge needs. To address this problem, AEMO proposed a number of amendments to Part 19 of the NGR to introduce PRT in the DWGM. The proposed PRT mechanism is intended to enable market participants to more readily carry out short term trades of the market benefits attached to AMDQ and AMDQ cc.

To support PRT, trades must be given effect in AEMO's scheduling and settlement process. This requires changes to AEMO's market systems. Implementation of PRT would therefore include a new IT interface for registering and confirming bilateral trades between market participants. However, the PRT mechanism would not include contract terms and payments. The terms and conditions, including the financial transactions, related to PRT would be set out in bilateral contracts between the trading parties.

In summary, the draft rule, if implemented, would require AEMO to:

1 AMDQ is a right recognised by the National Gas Rules (NGR) and is normally held by a customer. AMDQ cc is a right created by contract and is normally held by a market participant (but can also be acquired directly by a customer). Broadly, there are two different types of right (or benefits) that are created by holding AMDQ and AMDQ cc. These rights are explained further in Chapter 1.

- transfer the entitlement to the benefits associated with AMDQ and AMDQ cc between market participants;
- adjust trading market participants' AMDQ and AMDQ cc allocations in line with information submitted from PRT (the adjusted figures must then be used to calculate ITR); and
- develop and publish PRT procedures to implement the PRT mechanism.

Details of the draft rule are set out in Appendix D.

Commission's decision

Overall, the Commission considers that the proposed portfolio rights trading mechanism would provide an efficient, flexible and timely mechanism that allows participants to better manage their short term risk exposure and optimise their portfolios. The Commission's draft rule determination is to make a draft rule which is consistent with the proposed rule submitted by AEMO.

The Commission is satisfied that the draft rule will, or is likely to, contribute to the achievement of the national gas objective (NGO) by promoting more efficient use of, and investment in, natural gas pipelines in the long term interests of gas consumers. Specifically, it considers that the draft rule, if implemented, would:

- *Promote competition*: by facilitating access to unused pipeline capacity, the PRT mechanism may increase competition between market participants. This could occur by broadening the tools available for portfolio management, lowering barriers to entry for new market participants (including new retailers) and enhancing participation by end users in the DWGM. Increasing competitive pressure could ultimately result in lower prices to gas consumers.
- *Promote flexibility*: by introducing well-functioning and flexible pipeline trading arrangements, the PRT mechanism may lower transaction costs for market participants seeking access to short-term pipeline services. In addition, by generating interest between buyers and sellers, the PRT mechanism may improve pipeline capacity trading liquidity.
- *Encourage efficient use of gas transmission capacity*: by encouraging the reallocation of unused pipeline capacity between market participants, the PRT mechanism should encourage more efficient use of existing infrastructure, and should contribute to the pipeline being expanded only when it is efficient to do so.

Invitation for submissions

The Commission invites public submissions on this draft rule determination by 31 July 2014.

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1 AEMO's rule change request

1.1 The rule change request

On 14 November 2013, the Australian Energy Market Operator (AEMO or proponent) submitted a rule change request to the Australian Energy Market Commission (AEMC or Commission) to introduce portfolio rights trading (PRT) in the Victorian declared wholesale gas market (DWGM). Under the proposal, PRT would be a new market mechanism to facilitate the transfer the market benefits of authorised MDQ (AMDQ) and AMDQ credit certificates (AMDQ cc) allocated to close proximity points (CPP) between market participants.

1.2 Relevant background

The Victorian declared transmission system (DTS) is the only pipeline operating under a market carriage model in Australia.[2] Under the market carriage model, market participants utilising the DTS cannot reserve firm capacity on a pipeline.[3] While users do not have firm capacity, they may hold AMDQ or AMDQ cc which provides certain market rights and benefits and some limited physical benefits.

AMDQ is a right recognised by the National Gas Rules (NGR) and is normally held by a customer. AMDQ cc is a right created by contract and is normally held by a market participant (but can also be acquired directly by a customer).[4]

Broadly, there are two different types of right (or benefits) that are created by holding AMDQ and AMDQ cc:

- **Limited physical access rights**: The underlying AMDQ and the physical rights associated with AMDQ cc give a customer some protection against curtailment in the event of an emergency. These physical rights are owned by the customer (that is, the end user of gas).
- **Financial rights**: The market benefits associated with AMDQ and AMDQ cc are held by market participants (not necessarily the customer) and include:
  - *Priority in scheduled injections* (injection tie-breaking rights (ITR)): When there are equal-priced injection bids, those bids associated with AMDQ or AMDQ ccs are scheduled first;

2 The types of transportation contracts and services available to a shipper will depend on whether the pipeline operates under a market or a contract carriage capacity management model.

3 In contrast, transportation services provided under a contract carriage model are supplied under bilateral contracts between the pipeline owner and the shipper of gas. These contracts specify a certain amount of firm capacity that will be provided to the shipper.

4 In this context, customer refers to an end-user and market participant refers to the person who is financially responsible to a customer. That is, a retailer.

— *Reduced uplift payments* (uplift hedge (UH) protection): Market participants can use part or all of their AMDQ or AMDQ credits to hedge against congestion uplift charges up to their Authorised Maximum Interval Quantity (AMIQ).

The entitlements to the 'portfolio' of financial rights (that is, to the market benefits associated with AMDQ and AMDQ cc) held by a market participant are the 'rights' that are proposed to be traded under PRT. The underlying AMDQ and AMDQ cc and the curtailment protection associated with it would remain with the customer or market participant who owns them.

Allocating AMDQ

AMDQ was first allocated at market commencement in 1998. The allocation of 990TJ was (and has remained) commensurate with the capacity of the Longford-Melbourne pipeline at the time the sole source of gas supply for the DWGM. Recognising that the DTS was comprised of pre-existing assets that had at least partially been paid for by existing customers of the Victorian Gas and Fuel Corporation, at the start of the market the rights to the existing 990TJ of capacity were allocated to customers in two tranches:

- Tariff D customers (that is, those large customers who had meters measuring daily demand and whose gas tariff included a daily-demand-based component); and
- Tariff V based customers (that is, smaller customers on an energy usage tariff generally based on cumulative gas usage over a two monthly billing cycle).

Tariff D AMDQ was allocated to Tariff D customers individually on the basis of their historic demand.

After allowing for diversity of the individual Tariff D customer allocations of AMDQ, the reminder of the remaining 990TJ of available capacity was allocated to Tariff V customers as a block allocation: that is, not to individual customers. There is no designated permanent owner of Tariff V AMDQ. Instead, gas retailers are allocated the market rights associated with Tariff V AMDQ in proportion to the aggregate of their Tariff V customers' usage. This allocation is adjusted on a daily basis to reflect customer transfers, which continually change the Tariff V allocations between retailers.

The rationale for creating a flexible arrangement where Tariff V AMDQ is allocated to market participants in accordance with their customer share, was to not create a barrier to retail competition. If AMDQ were permanently held by retailers, there was a concern that those retailers who won customers from rival retail businesses would then be forced into a position of either trying to negotiate with that rival retailer to sell them AMDQ, or take on additional risk.

Allocating AMDQ cc

Since the commencement of the DWGM, the capacity of the DTS has increased as a result of numerous augmentations.[5] As new pipeline capacity becomes available, AMDQ cc are created to provide similar benefits to those arising from AMDQ on the Longford pipeline. AMDQ cc gives market participants a contractual right to the market benefits of the AMDQ cc.

The increase in pipeline capacity resulting from an extension or expansion project is agreed between APA GasNet (the DTS owner) and AEMO (the operator of the DTS and the DWGM). Once agreement is reached and the new capacity becomes operational, new certificates are created. AEMO allocates the AMDQ cc to market participants for quantities and periods as directed by APA GasNet. The directions from APA GasNet reflect the outcome of a competitive tender process it manages. In this process, interested market participants are able to tender for an amount of AMDQ cc for a specified period.

AMDQ cc is not differentiated by final customer (Tariff V or D) and is not allocated directly to customers. Rather, market participants with AMDQ cc must advise AEMO whether the allocated AMDQ cc are to be nominated to sites or the reference hub.

Obtaining AMDQ and AMDQ cc

There are a number of ways that market participants can acquire AMDQ and AMDQ cc. They can:

- enter into an agreement with existing holders of AMDQ to transfer an agreed quantity from one site to another or to the reference hub;[6]
- enter into an agreement with existing holders of AMDQ cc to transfer an agreed quantity at the reference hub;
- tender for AMDQ cc when new DTS capacity is created;
- fund an expansion of the DTS (although this has not happened to date);
- tender for existing AMDQ cc from the DTS owner when the current term of the AMDQ cc expires; and
- bid for spare AMDQ at an AEMO run auction.

Appendix C sets out the current allocation of AMDQ and AMDQ cc in the DWGM.

5 Changes to the DTS have included the Interconnect, the South West Pipeline, the connection of the former Western Transmission System, the Brooklyn Lara Loop and the BassGas project.

6 The reference hub is a notional site within the DTS established for the purpose of valuing AMDQ and AMDQ cc. When a market participant does not nominate its entire AMDQ to actual sites, it has to nominate its residual AMDQ somewhere.

1.3 Rationale for the rule change request

Section 3 of AEMO's rule change request includes a statement of issues. In summary, AEMO has identified a number of barriers which limit market participants' ability to acquire AMDQ and AMDQ cc to meet their injection tie-breaking and uplift hedge needs. These barriers are explored further in Chapter 3 of this draft rule determination. They relate to the following matters:

- AMDQ allocation is unrelated to market participants' injection capacity at Longford.
- The market in AMDQ and AMDQ cc created by the transfer process is not liquid.
- Opportunities to gain injection tie-breaking rights through means other than holding AMDQ or AMDQ cc are limited.
- Currently, AMDQ cc tends to be released in tranches (often 5 years).
- Future expansion of the Longford-Melbourne pipeline to create new AMDQ cc is unlikely given the pipeline has some spare capacity.

AEMO considers that a mechanism which enables underutilised AMDQ and AMDQ cc to become available to market participants who do not have enough to cover their available gas injections will provide for more efficient utilisation of pipeline capacity in the DWGM. This should ultimately defer the requirements for new pipeline capacity.[7]

1.4 Solution proposed in the rule change request

To address the matters identified above, AEMO has proposed a number of amendments to Part 19 of the NGR to facilitate the introduction of portfolio rights trading in the DWGM. The rule change request includes a proposed rule.

The proposed portfolio rights trading mechanism is intended to allow market participants to more readily carry out short term trades of the benefits attached to AMDQ and AMDQ cc (the holder of the AMDQ and AMDQ cc would remain unchanged). It is anticipated that this, in turn, would encourage more efficient utilisation of the Victorian pipeline system. This is on the basis that if market participants are able to access the benefits of AMDQ and AMDQ cc, then they may be more willing to utilise existing pipelines.

In accordance with the amendments proposed to the rules, AEMO would develop a new market systems interface (the PRT nomination WebExchanger (WEX) and Web service) for registering and confirming trades carried out between market participants. AEMO would also develop a new market systems module for updating market participant's AMDQ and AMDQ cc allocation to take account of the traded quantities.

7 AEMO, rule change request, p.16.

This would enable market participants engaged in PRT to receive the relevant market benefits of the trades.

The PRT mechanism does not include contract terms and payments. Financial transactions related to PRT would take place through bilateral contracts between the trading parties outside of the NGR. It also does not include a listing service. Market participants interested in participating in PRT would need to search for suitable trading partners also outside the NGR.[8]

Importantly, physical ownership of AMDQ and AMDQ cc and any curtailment rights would remain unchanged by PRT.

The amendments proposed to Part 19 of the NGR include a number of changes to existing definitions and rules as well as the inclusion of a number of new definitions and rules. In summary, the proposed rule seeks to:

- create a number of new definitions, for example “Adjusted AMDQ”, “Adjusted AMDQ credits”;
- amend several existing definitions, for example “AMDQ credit”, “AMIQ”, “AMDQ”;
- amend several existing rules related to AMDQ cc tie-breaking and uplift payments; and
- create a new rule which requires AEMO to make PRT procedures to implement the PRT model.

The proposed rule also clarifies the type of rights that are created by AMDQ and the ownership of them. A description of the proposed amendments to the NGR is included in Appendix D.

As noted above, the proposed rule requires AEMO to develop procedures detailing how the PRT model would operate. While not specified in the proposed rule, AEMO notes that the PRT procedures would contain information related to:

- permitted trades;
- the available quantity of transferrable portfolio rights;
- PRT nominations;
- determination of market participants' adjusted AMDQ and AMDQ cc;
- notification to APA GasNet; and
- restrictions on transfer quantities.

8 This issue is discussed further in Chapter 3.

Consultation on the PRT procedures would be expected to commence following publication of a draft rule determination.

1.5 Commencement of rule making process

On 13 March 2014, the Commission published AEMO's rule change request and a consultation paper prepared by AEMC staff identifying specific issues or questions for consultation. Submissions closed on 10 April 2014.

The Commission received six submissions on the rule change request. They are published on the AEMC website (www.aemc.gov.au). A summary of the issues raised in submissions, and the Commission's response to each issue, is contained in Appendix B.

1.6 Consultation on draft rule determination

The Commission invites submissions on this draft rule determination by 31 July 2014.

Any person or body may request that the Commission hold a hearing in relation to the draft rule determination. Any request for a hearing must be made in writing and must be received by the Commission no later than 3 July 2014.[9]

Submissions and requests for a hearing should quote project number "GRC0021" and may be lodged online at www.aemc.gov.au or by mail to:

Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

9 In accordance with s. 310(2) of the National Gas Law (NGL). A public hearing is a formal requirement for the Commission to appear before the applicant to enable the applicant to make a presentation to the Commission.

2 Draft rule determination

2.1 Rule making test

Under s. 291(1) of the National Gas Law (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 national gas objective (NGO). The NGO is set out under s. 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."

2.2 Assessment criteria

To give effect to the NGO, the Commission has considered the following principles in assessing the rule change request:

- *Competition:* Arrangements which facilitate access to unused pipeline capacity may increase competition between market participants. This could occur by broadening the tools available for portfolio management, lowering barriers to entry for new market participants (including new retailers) and enhancing participation by end users in the DWGM. Increasing competitive pressure could result in lower prices to consumers.

- *Flexibility:* Well-functioning and flexible pipeline trading arrangements may lower transaction costs for market participants seeking access to short-term pipeline services. In addition, arrangements which generate interest between buyers and sellers may contribute to pipeline capacity trading liquidity.

- *Efficient use of gas transmission capacity:* Arrangements which encourage the reallocation of unused pipeline capacity will facilitate efficient use of existing infrastructure and should contribute to the pipeline network being expanded in an efficient manner.

In assessing the request against the NGO, the Commission has also considered the likely long term costs and benefits of the proposed rule compared to the counterfactual of not making the proposed change to the NGR. In doing so, the Commission has considered whether the proposed rule is likely to lead to more efficient use of, and investment in, natural gas pipelines, which is in the long term interests of consumers.

As noted in the consultation paper for this rule change request, the Commission has also been mindful of the direction and outcomes (where relevant) of any other streams of work currently taking place which are also exploring issues affecting the development of the eastern Australian gas market.[10]

2.3 Draft rule determination

The Commission's draft determination is to make a rule which implements the proposed rule submitted by AEMO.

A draft of the proposed rule is attached to, and published with, this draft rule determination. It's key features are described in Appendix D.

Having regard to the issues raised by AEMO in the rule change request, the Commission is satisfied that the draft rule will, or is likely to, contribute to the NGO for the following reasons:

- *Promoting competition:* by facilitating access to unused pipeline capacity, the PRT mechanism may increase competition between market participants by broadening the tools available for portfolio management, lowering barriers to entry for new market participants (including new retailers) and enhancing participation by end users in the DWGM. Increasing competitive pressure could result in lower prices to consumers.
- *Promoting flexibility:* by introducing well-functioning and flexible pipeline trading arrangements, the PRT mechanism may lower transaction costs for market participants seeking access to short-term pipeline services. In addition, by generating interest between buyers and sellers, the PRT mechanism may contribute to pipeline capacity trading liquidity.
- *Encouraging efficient use of gas transmission capacity:* by encouraging the reallocation of unused pipeline capacity between market participants, the PRT mechanism should encourage more efficient use of existing infrastructure, and should contribute to the pipeline network being expanded in an efficient manner.

2.4 Strategic priority

This rule determination relates to the second of the AEMC's current strategic priorities: promoting the development of efficient gas markets (the gas priority). This rule change would increase opportunities for the trade of unused AMDQ and AMDQ cc and so increase the ability of market participants to manage their short term market risk. This is likely to promote efficient development of the gas market by allowing for more

10 A number of strategic gas market reports have been released by the AEMC, and the Commonwealth and Victorian Governments, exploring issues affecting the development of the eastern Australian gas market. Among other things, these reports have included consideration regarding access to transmission pipeline capacity under contract and market carriage arrangements. See AEMC 2014, Portfolio Rights Trading, Consultation Paper, 13 March 2014, Sydney, p.7.

efficient utilisation of existing capacity and potentially deferring the need for new pipeline investment. Ultimately, this could avoid increased costs for consumers.

3 Commission's assessment

This chapter sets out the Commission's views in relation to the problem identified, and solution proposed, by AEMO in its rule change request. A summary of the stakeholder submissions to the consultation paper is also included.

A discussion of three additional issues identified by the Commission, having had regard to stakeholder submissions and AEMO's rule change request, is provided in Chapter 4.

3.1 AEMO's rule change request

3.1.1 Problem identified by AEMO

In section 3 of its rule change request, AEMO identified a number of issues which it believes are affecting market participants' ability to acquire AMDQ and AMDQ cc to meet their injection tie-breaking and uplift hedge needs. The key issues outlined by AEMO are set out below.

- *Allocation of AMDQ at Longford.* AMDQ associated with Longford is allocated for Tariff V customers between market participants based on their customer base. This may give rise to a situation where a market participant has been allocated more AMDQ than it has injection capacity at Longford.[11] Since AMDQ allocated to Tariff V customers cannot be transferred (see below), it is effectively stranded.

- *The market in AMDQ transfers is not liquid.* The NGR provide for the transfer of AMDQ and AMDQ cc. However, for practical reasons, the AMDQ associated with Tariff V customers (equivalent to two thirds of all AMDQ and AMDQ cc) cannot be transferred in this manner.[12] In addition, AMDQ held by Tariff D customers tends to be widely dispersed and held by those with minimal incentive to trade.

- *Alternatives to AMDQ and AMDQ cc that provide ITR are limited.* It is possible to gain an ITR by selling an agency injection hedge nomination (AIHN) to a market

11 According to AEMO, currently all 990TJ of AMDQ has been fully allocated. The three major retailers are responsible for over 75 per cent of the allocations as a result of them supplying Tariff V customers. However, these retailers now have a more diversified supply portfolio - over time, they have progressively moved away from Gippsland gas supplies to BassGas or Otway gas. As a result, these retailers are holding more AMDQ than they require to support their ITR and UH at the Longford close proximity point (CPP). On the other hand, the Longford CPP remains the major source of gas supplies for some other market participants even though they do not have sufficient AMDQ allocations to cover their current ITR and UH requirements.

12 AMDQ can be transferred: between Tariff D customer sites; from a Tariff D customer site to the reference hub; from the reference hub to a Tariff D customer site; and between parties at the reference hub. Transfers of AMDQ cc may only be undertaken between parties at the reference hub. See AEMO Wholesale Market AMDQ Transfer Procedures (Victoria) v2.0 available at www.aemo.com.au.

participant who has AMDQ or AMDQ cc but no injections at the relevant injection point. An AIHN provides the market participant with physical injection with a tie-breaking right and payment for validating the other market participants' uplift hedge. Importantly, an AIHN does not provide an uplift hedge benefit to the injecting party. In addition, the process is complicated and tends to be used intra-company only.

- *Allocation of AMDQ cc.* AMDQ cc tends to be released in tranches, often for five years in line with APA GasNet's access arrangement period. This means that market participants must forecast their requirements out five years when tendering for AMDQ cc. This is likely to result in over or underestimation. New entrants within the five year period will also be unable to obtain AMDQ cc from APA GasNet if the full allocation has been sold.

- *Creation of new AMDQ cc at Longford.* AEMO considers that expanding the Longford-Melbourne pipeline through either an expansion that is then included in APA GasNet's regulated asset base (RAB) (regulated expansion), or privately funded augmentation is unlikely in the near future.[13] Consequently, obtaining AMDQ cc through an increase in capacity of the Longford-Melbourne pipeline is also unlikely.

To highlight the extent of, specifically, the mismatch between allocated AMDQ and injections at Longford, AEMO provided some analysis in the rule change request. Based on consultation with stakeholders in 2011-2012 and drawing on data from winter 2011, AEMO found that approximately 250TJ of the 990TJ of allocated AMDQ at Longford was not supported by injections at the Longford CPP. That is, 250TJ of capacity on the Longford-Melbourne pipeline was not used.

Using data from winter 2012, AEMO also compared market participants' scheduled injections at the Longford CPP with their allocated AMDQ at Longford. This analysis showed AEMO that while some market participants were allocated up to 142TJ of AMDQ over their scheduled injections, other market participants experienced a shortfall of up to 92TJ of AMDQ relative to their scheduled injections.

In AEMO's view, this analysis indicates that there is potentially up to 92TJ of AMDQ available for trade between market participants who have either a surplus or shortfall of AMDQ at Longford relative to their actual injections at the Longford CPP.

3.1.2 Solution proposed by AEMO

To address these issues, AEMO has proposed changes to the NGR to facilitate the introduction of portfolio rights trading in the DWGM. The proposed PRT mechanism

13 In respect of a regulated expansion, AEMO considers that the current underutilisation of the Longford-Melbourne pipeline would make it difficult for APA GasNet to successfully argue to the Australian Energy Regulator (AER) that an expansion would create an economic benefit and should be included in its RAB. In respect of a privately funded expansion, AEMO considers that ITR benefits alone would be unlikely to incentivise market participants to sign the long term contracts needed to underpin the investment.

is intended to allow market participants to more readily carry out short term trades of the benefits attached to AMDQ and AMDQ cc. The holder of the AMDQ and AMDQ cc would remain unchanged.

To support PRT, trades must be given effect in AEMO's scheduling and settlement process. This requires changes to AEMO's market systems. The PRT mechanism therefore includes a new IT interface for registering and confirming bilateral trades between market participants. However, the mechanism does not include contract terms and payments. Financial transactions related to PRT will take place through bilateral contracts between the trading parties.

In summary, the proposed rule, if implemented, would require AEMO to:

- transfer the entitlement to the benefits associated with AMDQ and AMDQ cc between market participants;
- adjust trading market participants' AMDQ and AMDQ cc allocations in line with information submitted from PRT (the adjusted figures must then be used to calculate ITR); and
- develop and publish PRT procedures to implement the PRT mechanism.

AEMO's rationale for the rule change can be summarised as:

- *Price impact on consumers*. AEMO considers that the proposed changes will, by promoting more efficient utilisation of existing pipeline capacity, defer the need for costly augmentation of the DTS. Deferring increases in the capital base will delay increases in transportation tariffs. In addition, AEMO considers that improving the ability of market participants to manage their risk exposure via ITR and UH will also ultimately deliver lower gas costs to consumers.
- *Competition*. AEMO considers the proposed changes will promote competition in the DWGM by providing larger market participants with the flexibility to manage hedging instruments in the short term, and smaller market participants and new entrants with a mechanism to access AMDQ or AMDQ cc to manage short term exposure.
- *Risk management*. By providing market participants with greater flexibility to optimise scheduled injections and uplift hedge to mitigate the risk of uplift payments, AEMO considers that the proposed changes will increase certainty of supply and result in more efficient allocation of gas.
- *Transparency*. AEMO considers that, by broadening the AMDQ and AMDQ cc transferrable base and allowing a more liquid market for AMDQ and AMDQ cc to develop, the introduction of PRT will improve market transparency.

AEMO anticipates that the introduction of the PRT mechanism will encourage more efficient utilisation of the Victorian pipeline system on the basis that if market participants are able to access the benefits of AMDQ and AMDQ cc, then they may be more willing to utilise existing pipelines.

AEMO included a high level cost-benefit assessment in its rule change request. The results indicate that the PRT mechanism may return positive net market benefits if the traded quantity of AMDQ and AMDQ cc is above 10TJ for each year over the lifetime of the project (which is assumed to be five years).

In addition, after discussions with market participants, AEMO considers it has identified sufficient opportunities for the take-up of PRT. Assuming each market participant retains a five per cent position buffer to manage risk associated with demand fluctuations, AEMO identified scope for between 5-10TJ of AMDQ that could be transferred at Longford, and a further 10-20TJ of AMDQ cc at Iona.[14]

3.2 Stakeholder views

The Commission received six submissions from stakeholders on the rule change request.[15] An overview of submissions is provided below. A more detailed summary of the key issues raised by stakeholders in their submissions to the consultation paper, including the Commission's response to each issue, is set out in Appendix B.

Broadly, most stakeholders who made submissions on the AEMC's consultation paper were supportive of the proposed rule change.[16]

AGL Energy (AGL) expressed full support for the proposal and noted that freeing up underutilised rights, and creating an opportunity for the buying and selling of those rights, would enhance economic efficiency and thus contribute positively to the NGO. It considered that the ability to trade potentially up to 90TJ of AMDQ would bring about sufficient benefits to warrant the rule change and associated costs.[17]

GDFSAE considered the proposed rule would enhance the DWGM by increasing the ability to trade both AMDQ and AMDQ cc, particularly for market participants who use these hedging instruments for injection prioritisation and insurance against constrained uplift charges. It cited the potential challenges associated with exchanging or trading AMDQ cc, and the lack of liquidity in AMDQ, as the reason why it supported the proposal.[18]

14 There is currently no opportunity for trade of AMDQ cc at Culcairn. This is because the full allocation of AMDQ cc at Culcairn tends to be supported by injections.

15 AGL Energy, Lumo Energy, GDF Suez Australian Energy (GDFSAE) , Hydro Tasmania, APA Group, Alinta Energy.

16 AGL Energy, consultation paper submission, p.1; Lumo Energy, consultation paper, p.1; GDFSAE, consultation paper submission, p.2; Hydro Tasmania, consultation paper submission, p.1; APA Group, consultation paper submission, p.1; Alinta Energy, consultation paper submission, p.1.

17 AGL Energy, consultation paper submission, p.1.

18 GDFSAE, consultation paper submission, p.1.

Both Lumo Energy and Hydro Tasmania considered that permitting the trading of AMDQ would improve the efficiency of the DWGM. Specifically, Lumo Energy considered the proposal would promote more efficient utilisation of existing pipeline capacity which, in turn, would defer new pipeline capacity and lead to lower transportation tariffs in the long run.[19]

APA Group (APA) noted there was an issue with the current market structure of the DWGM in respect of providing market participants with the certainty they required. It considered the proposed rule may partly address this issue. However, it also considered that the PRT mechanism would create significant additional complexity on top of an already complex and technically challenging market structure. Overall, APA considered that a contract carriage based market model would offer superior outcomes for market participants, and ultimately consumers. It recommended that it ought to be considered in the context of the long term development of the Australian gas market.[20]

Alinta Energy (Alinta) welcomed efforts to improve trade in the benefits of AMDQ and considered the proposal may result in more efficient allocation of gas by allowing participants to trade with greater certainty and manage their risk exposure. It may also result in customers facing a more competitive market for supply. However, while it considered the proposal had a number of benefits in line with the NGO, it was not convinced that the proposal would increase transparency in the market, as suggested by AEMO.

In addition, Alinta did not consider that it was clear that the development of an additional instrument or a mandatory system administered by AEMO was the only approach to address the issues identified by AEMO. Alinta suggested that alternatives may be preferable. Specifically, Alinta identified two alternatives to portfolio rights trading which is considered warranted further consideration. These options are considered further in the next chapter.[21]

3.3 Commission's assessment

3.3.1 Problem identified by AEMO

In light of the changing patterns of demand and supply which have resulted from a number of recent key developments in the eastern Australian gas market, the Commission considers there is a role for some mechanism that will help broaden the tools available for market participants to manage their operational and financial risks.

The DWGM operates under a market carriage model which means that market participants cannot reserve firm capacity on the DTS. However, they may hold AMDQ or AMDQ cc which provides them with certain financial and physical benefits. AMDQ and AMDQ cc therefore provide market participants with a means of optimising their

19 Lumo Energy, consultation paper, p.1; Hydro Tasmania, consultation paper submission, p.1

20 APA Group, consultation paper submission, pp.1-2.

21 Alinta Energy, consultation paper submission, pp.1-3.

injections and mitigating the risk of uplift payments. In general, market participants will seek to hold enough AMDQ or AMDQ cc to cover their anticipated injections at the relevant injection point.

As outlined in Chapter 1, there are a number of ways market participants can acquire AMDQ and AMDQ cc. They can: enter into an arrangement with an existing right holder to transfer ownership of the AMDQ or AMDQ cc permanently; apply for AMDQ cc when the DTS' capacity is expanded; fund an expansion of the DTS; acquire existing AMDQ cc from the DTS owner when they expire; and bid for spare AMDQ at auction.

However, as outlined by AEMO, these arrangements create a number of challenges for market participants seeking to acquire AMDQ and AMDQ cc for their short term needs. In particular, the Commission notes the following two key issues with the current arrangements:

- While the AMDQ transfer process allows market participants to transfer ownership of AMDQ and AMDQ cc between themselves, it is only applicable to Tariff D AMDQ, and to AMDQ cc; Tariff V AMDQ is excluded on the basis that there is no designated permanent owner. In addition, Tariff D customers tend to be widely dispersed and have little incentive to trade. Together, this means the base of rights holders able and willing to trade unused AMDQ is relatively small which has implications for liquidity.

- Auctions to obtain expired AMDQ cc are only held every five years, while auctions to obtain spare AMDQ from defunct customer sites are discretionary and often involve small quantities of AMDQ. Therefore, while providing an important means of reallocating permanent ownership of AMDQ and AMDQ cc in the medium to long term, these mechanisms do not cater to market participants day to day risk management needs.

The Commission therefore agrees that there is no efficiently flexible and timely mechanism that allows market participants to effectively manage their short term risk exposure, and optimise their supply portfolios. As suggested by AEMO, this may have implications for the efficient use of, and investment in, pipeline capacity in the DWGM if left unaddressed.

3.3.2 Solution proposed by AEMO

The Commission supports AEMO's efforts to introduce a new mechanism to assist market participants to manage their short term risks in the DWGM.

Having considered AEMO's rule change request, the Commission considers that the proposed portfolio rights trading mechanism would address two key gaps in the current arrangements:

- It would broaden the base of rights holders able to bilaterally trade AMDQ and AMDQ cc. It does so by providing for the transfer of the market benefits associated with AMDQ and AMDQ cc, without changing the holder of the AMDQ and AMDQ cc. This avoids fundamental questions around ownership of Tariff V AMDQ.

- By facilitating bilateral trade of AMDQ and AMDQ cc, market participants would have the flexibility to tailor the terms and conditions of each trade to their individual needs. For example, decisions about the quantity of AMDQ and AMDQ cc available for trade (including whether a quantity is fixed or variable (or as available)), as well as decisions around the duration of a contract (including whether it is short term or long term) and location would be made by market participants, subject to the benefits they would derive.

Consistent with AEMO’s observation, the Commission considers that by broadening the AMDQ and AMDQ cc tradeable base, PRT would allow a more liquid market for AMDQ and AMDQ cc. However, it does not believe that this, in turn, would lead to improved market transparency as suggested by AEMO. Rather, the Commission considers that improvements in liquidity would, by generating interest among market participates in PRT, help to build competition in the Victorian gas market over time.

The Commission also considers that providing market participants with a flexible tool to help mitigate against the risk of uplift hedge should lead to the more efficient allocation of gas by assisting market participants in optimising their injections. This should encourage more efficient use of existing pipeline capacity and, in turn, potentially defer or remove the need for augmentations of the DTS.

With that said, the proposed amendments to the NGR focus specifically on ensuring that market participants engaged in PRT receive the relevant market benefits of a trade. For this to occur, trades must be given effect in AEMO’s scheduling and settlement processes which, in turn, necessitate changes to AEMO’s market systems. In this sense, AEMO’s proposed amendments are facilitative: they would provide for all market participants, including holders of Tariff V AMDQ, to receive the benefit from participation in portfolio rights trading. However, the success of PRT; in particular its ability to lead to more efficient utilisation of the DTS, would largely be driven by several additional factors.

First, PRT would not provide value to market participants if there is no market for AMDQ and AMDQ cc. That is, there must be willing buyers and sellers. As noted in section 3.2.1, AEMO suggests that there is the potential for trade of between 5-10TJ of AMDQ at Longford, and 10-20TJ of AMDQ cc at Iona. This view of the potential opportunities for trade appeared to be supported by some stakeholders in their submissions to the consultation paper. Lumo Energy considered that AEMO's analysis of the potential trading quantities was conservative and that volumes were realistically likely to be closer to 30TJ in any given year.[22] AGL Energy also observed that the ability to trade potentially up to 90TJ in AMDQ would bring about sufficient benefits to warrant the rule change.[23]

22 Lumo Energy, consultation paper submission, p.2.

23 AGL Energy, consultation paper submission, p.1.

Recognising that it is difficult to identify with certainty the likely volumes of AMDQ and AMDQ cc to be traded through the PRT mechanism, the Commission is comfortable that sufficient quantities exist to make the PRT provisions potentially worthwhile.

Second, PRT would only be viable if market participants seeking AMDQ or AMDQ cc are able to find willing counter-parties. At discussions held at the Gas Wholesale Consultative Forum (GWCF) during development of the PRT mechanism, AEMO indicated its intention to create a new Market Information Bulletin Board (MIBB) report detailing market participants' AMDQ and AMDQ cc positions. The MIBB report would be market participant specific and only accessible by authorised users nominated by the market participant (that is, by invitation only).

Stakeholders did not comment directly on the matter of transparency of surpluses and shortfalls in AMDQ and AMDQ cc in their submissions to the consultation paper. However, given the implications this has on the viability of the PRT mechanism, the Commission has included further discussion on this matter in Chapter 4.

3.3.3 Conclusion

Overall, the Commission considers that the proposed PRT mechanism would provide an efficiently flexible and timely mechanism that allows market participants to better manage their short term risk exposure and optimise their supply portfolios. The Commission therefore proposes to make a draft rule which implements the proposed rule submitted by AEMO.

4 Additional issues

This chapter provides a discussion of three additional issues identified by the Commission, having had regard to stakeholder submissions and AEMO's rule change request.

4.1 Alternatives to portfolio rights trading

In its submission to the consultation paper, Alinta suggested that the AEMC consider further two alternative options for addressing the issues raised by AEMO in its rule change request. A discussion of the alternatives is provided below.

Bilateral exchange

Alinta suggested that a change could be made to current arrangements to allow the sale of all existing AMDQ and AMDQ cc through bilateral contract. This would mean the existing limitations on AMDQ trade for Tariff V customers would be lifted and allocation of AMDQ would be primarily derived from exchange on the market.

As mentioned previously, the existing limitation on trade of Tariff V AMDQ is a consequence of there being no designated permanent owner of the AMDQ. When first allocated in 1998, a proportion of available AMDQ was allocated directly to Tariff V customers as a block allocation: that is, not to individual customers or to market participants.

The rationale for allocating AMDQ to Tariff V customers rather than to market participants, retailers or shippers was to avoid a barrier to retail competition and creating an advantage to incumbents. If AMDQ were held by retailers, there was a concern that those who won customers from rival retail businesses would then be forced into a position of either trying to negotiate with that rival retailer to sell them AMDQ, or take on additional risk.

Allowing the sale of all existing AMDQ and AMDQ cc through bilateral contract, as suggested by Alinta, would require complex issues about ownership of Tariff V AMDQ to be addressed. For example:

- assigning customers or end-users ownership of Tariff V AMDQ would not guarantee they had an interest, ability or market incentive to trade in AMDQ; and

- assigning retailers ownership of Tariff V AMDQ may have implications for competition amongst new and incumbent retailers; and

In addition, it may be difficult to gain support for this option from end-users, as it would likely require some of them to release their right to Tariff D AMDQ.;

Perhaps most importantly, however, this approach is very similar to the portfolio rights trading mechanism. In effect, PRT would provide for the bilateral trade by market participants of the benefits of Tariff D and V AMDQ and AMDQ cc. The advantage of PRT is that it would avoid the issue that Tariff V AMDQ is not permanently owned either by the customer or market participant.

For this reason, this option as suggested by Alinta would require fundamental change to the market and may be better considered in the context of longer term development of the DWGM.

Regular auction

Alinta also suggested that, as an alternative to PRT, changes could be made to allow for the regular auctioning of a greater proportion of AMDQ. These auctions would cover fixed periods into the future for the purposes of encouraging more active use (and purchase) of AMDQ. Once AMDQ had been purchased, and where a market participant did not utilise that AMDQ, it would have a greater incentive to trade in order to recover its costs.

Currently, market participants are able to acquire spare AMDQ and AMDQ cc via two auctions:

- *Auction of AMDQ*: AEMO, at its discretion, conducts periodic auctions of unclaimed AMDQ resulting from Tariff D site closures and which have been surrendered to AEMO.
- *Auction of AMDQ cc*: Market participants can tender for existing AMDQ cc from APA GasNet when the current term of AMDQ cc expires. As directed by APA GasNet, AEMO allocates the AMDQ cc to market participants as specified quantities for set periods (typically five years) at certain locations.

In theory, the block allocation of Tariff V AMDQ could be auctioned rather than allocated. However, issues associated with ownership of Tariff V AMDQ and requiring customers to release their right to Tariff D AMDQ may also need to be resolved.

In addition, this option would not address the issue of 'within period' trade of AMDQ and AMDQ cc. That is, unless an auction was conducted daily (a potentially complex and costly exercise), a mechanism to allow secondary and/or short term trading of AMDQ and AMDQ cc would still be necessary. This would require similar changes to AEMO's systems as PRT, in order for market participants to manage the day to day variations in their requirements for AMDQ as customers are won and lost.

Again, while feasible, this auction approach is unlikely to provide a better solution in the short term to the issues identified by AEMO, compared to the proposed PRT mechanism. As above, this auction option may also be best considered in the context of longer term development of the DWGM.

4.2 Ancillary payments

In its submission to the consultation paper, Alinta expressed concern about the potential for the PRT proposal to expose market participants without AMDQ or AMDQ cc to increased ancillary payments.[24]

Ancillary payments are compensatory payments made to market participants affected by events (such as congestion) which require gas that is more expensive than the market price to be scheduled. These payments are recovered from those market participants considered to have caused the events through uplift charges. There are three categories of uplift charges:

- *Congestion uplift*: recovered from market participants who have exceeded their AMIQ (that is, uplift hedge);
- *Surprise uplift*: recovered from market participants who have failed to follow their schedule and which have caused an 'event' or 'surprise' to the system; and
- *Common uplift*: a catch-all for any uplift generated by the market which cannot be allocated to any particular market participant. Common uplift is recovered from all market participants in proportion to their withdrawals.

Market participants who hold AMDQ and AMDQ cc are able to hedge against congestion uplift charges to the limit of their AMIQ. In effect, AMDQ and AMDQ cc provide a form of authorisation allowing market participants the right to withdraw gas up to their AMIQ. On days when the system is congested, market participants who have exceeded their AMIQ may face congestion uplift charges for excess or unauthorised use of the system for that amount above their authorised quantity.

In its rule change request, AEMO observed that if more market participants were able to access AMDQ and AMDQ cc through PRT, then on days when ancillary payments occur, a greater proportion of those payments would be recovered from all market participants through common uplift charges, as opposed to individual market participants through congestion uplift charges. However, AEMO considered this to be a secondary issue. In its view, if a market participant considered its risk of increased exposure to uplift charges was greater than the cost of acquiring AMDQ or AMDQ cc, it would have the option of participating in PRT to help manage that risk.

The Commission acknowledges that the introduction of portfolio rights trading may result in a situation where, on days when the system is congested, a greater proportion of ancillary payments may be recovered via common uplift charges (and spread across all withdrawing market participants) as more market participants are hedged against congestion uplift charges. However, given that no stakeholder other than Alinta raised this as a concern, the Commission considers any risks associated with this issue are likely to be minor. Consistent with AEMO's view, the Commission considers that any

24 Alinta Energy, consultation paper submission, p.2.

risk may encourage greater participation in portfolio rights trading which should improve efficiency in the DWGM.

4.3 Search for suitable trading partners

As noted above, the ability of PRT to achieve the desired outcomes requires that market participants willing and able to trade AMDQ and AMDQ cc are able to locate one another.

During development of PRT, AEMO proposed that a public MIBB report also be created detailing market participants' AMDQ and AMDQ cc surplus and shortfalls. In effect, this would provide a type of listing service with the aim was to assist market participants in the search for potential trading partners. However, there was some concern expressed by market participants over the confidential nature of some of the information proposed for publication (that is, Tariff V AMDQ is allocated according to market share which market participants regard as confidential). They requested that AEMO develop an alternative report with the slightly different aim of assisting market participants to assess their own capacity for PRT. AEMO subsequently created a market participant specific MIBB report. This report would only be accessible by authorised users nominated by the market participant (that is, by invitation only).

The Commission sought the views of a number of stakeholders on this matter. One market participant considered the DWGM was small enough for potential buyers and sellers to locate each other without the need for a listing service. In contrast, another market participant expressed some support for a simple and cheap listing service which did not reveal the identities of potential trading participants to the market. This market participant considered that a listing service could potentially prevent larger retailers from refusing to trade bilateral with new market entrants, or pricing new market entrants out of the market.

There have been a number of recent developments in the gas market that relate to the issue of trading in pipeline capacity and which have included consideration of a capacity listing service. As part of the development of the gas supply hub at Wallumbilla, AEMO introduced a bulletin board style of web page that enables market participants in the supply hub to register their interest in either buying or selling pipeline capacity. It is intended that parties contact each other outside this web page and, using a standard contract, trade pipeline capacity.

Although AEMO developed this platform for the supply hub, APA Group also developed its own trading system for shippers to trade firm forward haul capacity on the South West Queensland Pipeline (SWQP) and the Roma to Brisbane Pipeline (RBP) (the pipelines it owns and operates).[25] APA recently provided a new public webpage that provides information on trades that have occurred as well as on available capacities as a listing service. Participants are able to carry out a trade bilaterally and

25 The pipelines connected to the Wallumbilla gas supply hub are two APA pipelines: SWQP and the RBP; and the Queensland Gas Pipeline (QGP) owned by Jemena.

register it with APA Group, provided they have a new transportation contract with APA in place.

These two developments highlight that listing services can be provided, and do exist, in gas markets outside of the DWGM.

There are a number of ways transparency could be improved without raising issues around the release of information which is confidential or commercially sensitive (or which could be deciphered by competing businesses to reveal such information). Three examples are provided below:

- *Ranked MIBB report*: The report would not detail the absolute quantity of market participants' surpluses and shortfalls. Rather, it would rank market participants based on quantity bands. This option would detail all market participants' positions, albeit anonymously. Unless required by the rules, the GWCF members would need to agree to publication. A procedure change may also be required.
- *Utilise gas supply hub (GSH) exchange*: Available AMDQ and AMDQ cc could be listed on the GSH exchange as a product for trade. This option would facilitate price transparency. However, given that the exchange is not public, market participants interested in viewing the listing service would need to register as a viewing participant and pay the relevant licence fee.[26] This option would be voluntary and therefore only useful to the extent that potential trading parties chose to participate.
- *Utilise the Bulletin Board (BB)*: The bulletin board already provides a platform for market participants to post their interest in buying or selling AMDQ or AMDQ cc. This option would also be voluntary and therefore also only useful to the extent that potential trading parties chose to participate.[27] In addition, it is separate from AEMO's DWGM IT systems.

The Commission accepts that market participants currently operating in the DWGM are likely to have a fairly good idea of who to contact to request, or offer for trade, unused AMDQ and AMDQ cc. However, this may not be the case for new entrants or less established participants who do not have established contacts with incumbents.

The Commission therefore believes that the development of some form of listing service to complement the PRT mechanism is likely to be beneficial. As illustrated by the work recently carried out by AEMO and APA Group at the gas supply hub, there seems to be appetite from the market for mechanisms which increase transparency around unused pipeline capacity and make the search for trading partners easier. In the context of the DWGM, the Commission notes that any of the three options outlined above could be progressed by AEMO now, with minimal effort and cost and without requiring an amendment to the NGR. AEMO is therefore encouraged to consider this

26 Viewing participants are required to pay an annual fixed fee of $5,500.

27 This BB platform is available for use by market participants now but is not used.

matter further with market participants, to ensure that the full benefits of PRT can be released.

Abbreviations

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
AGL	AGL Energy
AIHN	agency injection hedge nomination
Alinta	Alinta Energy
AMDQ	authorised MDQ
AMDQ cc	AMDQ credit certificates
AMIQ	Authorised Maximum Interval Quantity
APA	APA Group
BB	Bulletin Board
Commission	See AEMC
CPP	close proximity points
DTS	declared transmission system
DWGM	declared wholesale gas market
GDFSAE	GDF Suez Australian Energy
GWCF	Gas Wholesale Consultative Forum
ITR	injection tie-breaking rights
MCE	Ministerial Council on Energy
MIBB	Market Information Bulletin Board
NGL	National Gas Law
NGO	national gas objective
NGR	National Gas Rules

PRT	portfolio rights trading
QGP	Queensland Gas Pipeline
RAB	regulated asset base
RBP	Roma to Brisbane Pipeline
SWQP	South West Queensland Pipeline
UH	uplift hedge
WEX	WebExchanger

A Legal requirements under the NGL

This appendix sets out the relevant legal requirements under the National Gas Law for the AEMC in making this draft rule determination.

A.1 Draft rule determination

In accordance with s. 308 of the NGL, the Commission has made this draft rule determination in relation to the rule proposed by AEMO.

A.2 Power to make the rule

The Commission is satisfied that the draft rule falls within the subject matter about which the Commission may make rules.

The draft rule falls within s. 74 of the NGL. More specifically, it relates to AEMO's declared system functions and the operation of a declared wholesale gas market (s. 74(1)(a)(v)).

Further, the draft rule falls within the matters set out in schedule 1 to the NGL as it relates to clause 55B because it relates to the operation and administration of a regulated gas market.

A.3 Commission's considerations

In assessing the rule change request, the Commission has considered:

- the Commission’s powers under the NGL to make the rule;
- the rule change request;
- stakeholder submissions received during first round consultation;
- the fact that there is no relevant Ministerial Council on Energy (MCE) statement of policy principles;[28] and
- the Commission’s analysis as to the ways in which the draft rule will or is likely to, contribute to the NGO.

28 Under s. 73 of the NGL, the AEMC must have regard to any relevant MCE statement of policy principles in making a rule.

A.4 Other

A.4.1 Compatibility with AEMO's declared system functions

Under s. 295(4) of the NGL, the Commission may only make a rule that has effect with respect to an adoptive jurisdiction if it is satisfied that the proposed rule is compatible with the proper performance of AEMO's declared system functions.[29]

The draft rule will impact on AEMO's declared system functions of operating and administering the DWGM. The Commission considers that the draft rule is compatible with the proper performance of AEMO's declared system functions because AEMO would, following changes to its systems to incorporate the amended rules, continue to be able to operate and administer the DWGM.

A.4.2 AEMO's allocated powers, functions and duties

Under s. 295(5) of the NGL, the Commission may only make a rule that affects the allocation of powers, functions and duties between AEMO and a service provider for a declared transmission system if AEMO consents to the making of a rule of the rule is requested by the Minister of the relevant adoptable jurisdiction.[30]

In relation to this rule change request, there is no requirement under s. 295(5) of the NGL for AEMO to consent to the AEMC making this draft rule. This is because the draft rule does not affect the allocation of powers, functions and duties between AEMO and a service provider for a declared transmission system. This draft rule only impacts the nature of the nominations market participants can make to AEMO regarding their AMDQ and AMIQ profiles.

A.4.3 Participating jurisdictions

Although the draft rule applies to each participating jurisdiction except Western Australia, it amends Part 109 of the NGR which currently only relates to the operation of the wholesale gas market, transmission system and distribution systems in Victoria as declared under the *National Gas (Victoria) Act 2008*.[31]

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29 AEMO's declared system functions are specified in section 91BA of the NGL.

30 The declared transmission system is the transmission pipeline for the DWGM.

31 Under s. 21 of the NGL, the participating jurisdictions are the States, Commonwealth, the Australian Capital Territory and the Northern Territory. The draft rule does not apply in Western Australia as it does not fall within the subject matters about which the Commission may make Rules under the Western Australia Application Act.

B Summary of issues raised in submissions

The table below provides a summary of the policy issues raised by stakeholders in their submissions to the consultation paper. The table sets out the Commission's response to each issue.

The submissions received are available on the AEMC website at www.aemc.gov.au.

Stakeholder	Issue	AEMC Response
APA Group	APA supports initiatives that seek to improve the operation of the DWGM by addressing known shortcomings in the Victorian market. It notes that a key shortcoming is the inability of market participants to manage their risk exposure when they do not have adequate AMDQ or AMDQ cc. It considers this risk exposure arises because the design of the DWGM is based on market carriage, and is also a legacy of the initial allocation of AMDQ. (p.1)	Noted.
APA Group	APA notes that the rule change attempts to create additional opportunities for market participants to access instruments designed to provide some elements of the firmness available on contract carriage pipelines. It considers there is an issue with the market structure of the DWGM in respect of providing market participants with the certainty they need. However, it considers that the rule change will only partially address the issue. (p.1)	Noted.
APA Group	APA considers that the PRT mechanism will create significant additional complexity on top of an already complex and technically challenging market structure. It notes that other market models offer opportunities for improving market liquidity without giving rise to issues in respect of firm capacity rights, and that these models operate without the complexity or cost of	While the Commission agrees that the introduction of a new mechanism may add a degree of additional complexity to the market which may come at some cost, it considers the benefits of providing market participants with additional flexibility while avoiding the need for fundamental change to the current market

Stakeholder	Issue	AEMC Response
	the DWGM. (p.1)	design, will outweigh that cost.
APA Group	APA considers that contract carriage market models offer superior outcomes for market participants and ultimately customers, and ought to be considered in the context of the long term development of the Australian gas market. (p.2)	This matter is outside the scope of this rule change and would, as suggested, be better considered in the context of longer term development of the DWGM and, more broadly, the eastern Australian gas market.
AGL Energy	AGL suggests that rule change is timely given the oft-stated need that is cited in recent gas market reviews to make secondary transportation capacity available on a voluntary basis. It considers the PRT rule and procedure change package should be seen within the context of broader work by SCER and APA Group in relation to secondary capacity trading. (p.2)	In considering this rule change request, the Commission has been mindful of the direction and outcomes of the various other streams of work currently taking place in relation to issues affecting the development of the eastern Australian gas market.
AGL Energy	AGL noted that is was fully supportive of the rule and procedure change package as it represents faithfully the outcomes and resolutions of Transmission Capacity Working Group (TCWG).[32] It believes that the facility to trade potentially up to 90TJ in AMDQ will bring about sufficient benefits to warrant not only the rule change, but the costs AEMO would need to incur to modify its systems. In addition, by freeing up underutilised rights and creating an opportunity for the buying and selling of portfolio rights, AGL considers the proposal must be seen as enhancing economic efficiency and thereby contributing positively to the NGO. (p.1)	Noted.
Lumo Energy	Overall, Lumo Energy considers that, by allowing market participants to make use of existing financial rights associated with AMDQ and AMDQ cc, the proposal should defer augmentations in the long run, leading to lower gas prices for	Noted.

32 The concept of PRT was first considered by the TCWG in 2011. In August of that year, the TCWG was formed by the GWCF to investigate issues affecting the development of the DWGM, in particular, issues related to transmission capacity.

Stakeholder	Issue	AEMC Response
	consumers. For this reason, it considers the proposal is consistent with the NGO. (p.1)	
Lumo Energy	Lumo Energy considers AEMO's analysis of potential trading quantities is quite conservative and that trading quantities in any given year are realistically likely to be close to 30TJ. It strongly agrees that PRT will deliver a net benefit to the market over its life (which is assumed to be 5 years). (p.2)	Noted
Hydro Tasmania	Hydro Tasmania supports the proposed rule and believes it will improve the efficiency of the DWGM. It considers that permitting AMDQ trading will significantly increase supply, releasing AMDQ that has become stranded as retailers have diversified supply away from Gippsland. (p.1)	Noted.
Alinta Energy	Alinta supports additional trading of AMDQ. However, it notes that it is not clear that the development of an additional instrument or a mandatory system administered by AEMO is the only approach to the issues raised and that alternatives may be preferable. Alinta notes that a number of matters require further consideration and the value of alternative proposals should be investigated before it can fully support the rule. (pp.1,3)	A discussion of the two alternatives identified by Alinta is provided in Chapter 4.
Alinta Energy	Alinta can see a number of potential benefits in line with the NGO. It notes that the proposal may increase its ability to acquire and trade hedging instruments in the short term and therefore may facilitate greater levels of trade and competition. It may also improve its ability to manage market risk and mitigate potential charges in the market resulting from uncertain supply. However, in contrast with the view of AEMO, Alinta is less clear that the proposed rule will increase transparency significantly, if at all. (p.1)	The Commission agrees with Alinta that the ability of the PRT mechanism to improve market transparency, as suggested by AEMO, is unclear. As discussed in section 3.3.2, the Commission considers that by broadening the tradeable base of AMDQ and AMDQ cc, the proposal will generate more interest among market participates in PRT and in doing so, will help to build competition and liquidity in the Victorian gas market over time.

Stakeholder	Issue	AEMC Response
Alinta Energy	Alinta notes that while the proposal relies on bilateral contracts, it is unclear how this will guarantee a transparent or liquid market. It considers that while the differences may be marginal, the existence of multiple forms of instrument may not be ideal. (p.2)	As above. In addition, while the introduction of a new mechanism may add a degree of additional complexity to the market which may come at some cost, the Commission considers the benefits of providing market participants with additional flexibility while avoiding the need for fundamental change to the current market design, will outweigh that cost.
Alinta Energy	It is not clear to Alinta why the decision to restrict the ability of tariff V customers to trade AMDQ cannot be revisited. It considers that if all AMDQ was able to be freely traded, there would be less need for the proposed approach. While this may reduce AEMO's role in allocating AMDQ, outside of regular auctions, thought should be given to whether this approach is more desirable. (p.2)	An advantage of PRT is that it would provide for the transfer of the *market entitlements* associated with AMDQ and AMDQ cc, without changing the holder of the AMDQ and AMDQ cc. This avoids fundamental questions around ownership of Tariff V AMDQ. This avoids the need to make a fundamental change to the market which would likely be required if the proposal to free up all AMDQ (Tariff V and D) for trade was progressed.
Alinta Energy	Alinta is unclear how the proposal may impact scheduling, for example AMIQ. While it is not proposing that limits be imposed on the terms of trading under PRT, it notes that it is not necessarily the case that market impacts will be understood or immediately appreciated by participants. (p.2)	The introduction of PRT would impact scheduling only when the system is constrained and market participants have equal-priced injection bids. This is because it more market participants may have access to ITR as a result of participating in PRT. However, the rules and procedures for scheduling and AMIQ would be unchanged by implementation of the draft rule.
Alinta Energy	Alinta considers the potential to be exposed to increased ancillary payments for market participants who do not hold AMDQ or portfolio rights is of concern and does not contribute to transparency. (p.2)	A discussion of the impact of PRT on ancillary payments is provided in Chapter 4.
Alinta Energy	Alinta is supportive of the trading of AMDQ where the costs of implementation are proportionate, and a net benefit can be demonstrated. Given the implementation costs for AEMO are significant at around $500,000, it considers there needs to be certainty that the proposal is the least costly of all option available. (p.2)	Noted.

Stakeholder	**Issue**	**AEMC Response**
Alinta	Alinta considers a number of alternatives to PRT warrant further consideration, including: • Allowing for the sale of all existing AMDQ through bi-lateral contract. This would mean the exiting limitations on AMDQ trade for tariff V customers would be lifted and allocation of AMDQ would be primarily derived from exchange on the market. Alinta suggests that the AEMC consider the potential merits of a more preferable rule for the purpose of freeing up the ability to trade existing AMDQ including that held by tariff V customers. • Regular auctioning of a greater proportion of AMDQ. These auctions would cover fixed periods into the future for the purposes of encouraging more active use of AMDQ. This would allow increased opportunities to purchase AMDQ. Once AMDQ has been purchased and where a participant does not utilise that AMDQ, it will have a greater incentive to trade to cover paid costs. (p.3)	A discussion of the two alternatives identified by Alinta is provided in Chapter 4.

C Allocation of AMDQ and AMDQ cc

Figure C.1 illustrates the current allocation of AMDQ and AMDQ cc in the DWGM.

Figure C.1 Current allocation of AMDQ and AMDQ cc

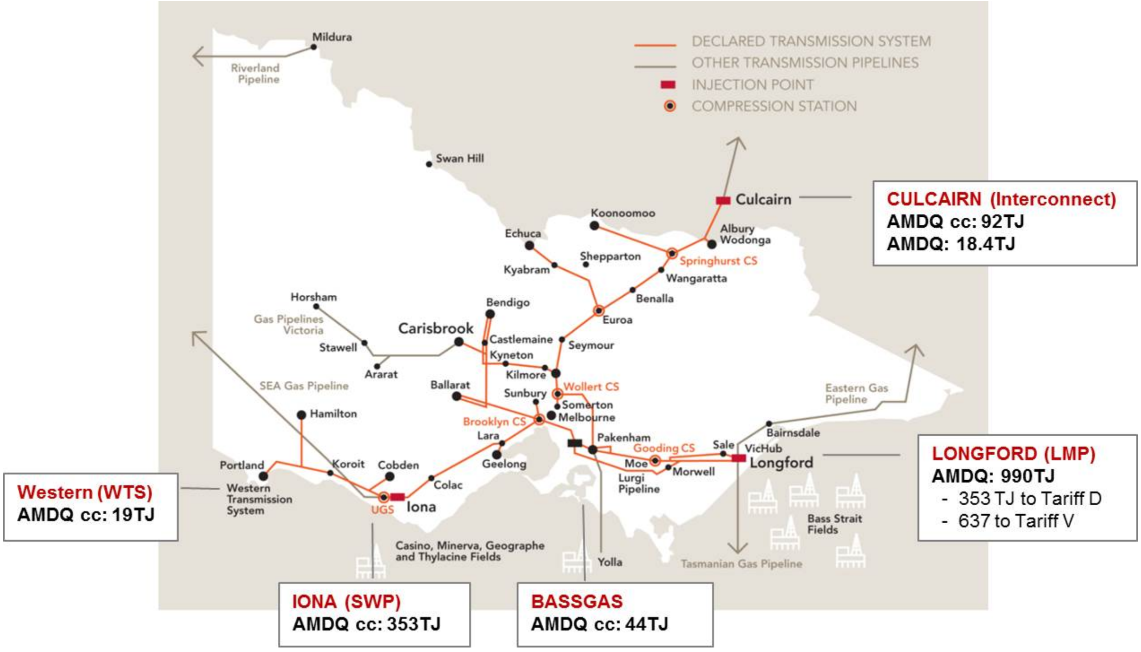
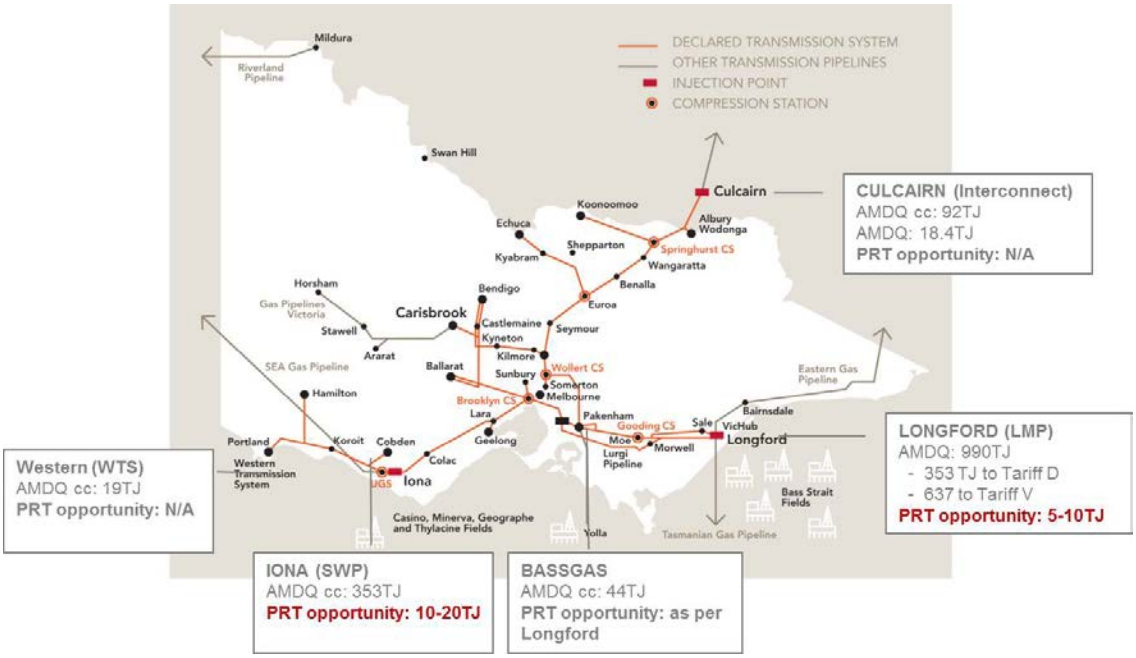


Figure C.2 illustrates the potential opportunities for the trade of AMDQ and AMDQ cc in the DWGM, as identified by the AEMO in its rule change request.

Figure C.2 Opportunities for PRT



D Proposed amendments to the NGR

Table D.1 sets out the changes proposed by AEMO in its rule change request.

Table D.1 Proposed amendments to the NGR

NGR reference	Section title	Description
New definitions		
Rule 200	"Adjusted AMDQ"	Market participants' AMDQ entitlements adjusted as set out under new rule 327A(1) to take account of the AMDQ entitlements it has transferred with other market participants for that gas day in accordance with the PRT procedures and any associated diversity factors.
Rule 200	"Adjusted AMDQ Credits"	Market participants' AMDQ credit adjusted to take account of the AMDQ credit entitlements it has transferred with other market participants for that gas day in accordance with the PRT procedures and any associated diversity factors.
Rule 200	"Diversity factor"	A factor determined by AEMO by reference to the expected gas consumption at that system point.
Rule 200	"Portfolio Rights Trading Procedures"	The proposed new PRT procedures required under new rule 331A.
Amended definitions		
Rule 200	"AMDQ credit"	Amended to clarify the distinction between AMDQ credit and AMDQ cc.
Rule 200	"Authorised Maximum Interval Quantity"	Amended to reflect AMIQ only has a role in determining uplift payments and not ancillary payments. Amendment also clarifies that AMIQ is based on the adjusted quantities of the AMDQ credit not the total AMDQ cc.
Rule 200	"AMDQ"	Amended to simplify the definition.
Amended rules		

NGR reference	Section title	Description
Existing rule 214(e)	Priority of bids in the scheduling process	Amended to clarify that it is the adjusted quantities for the AMDQ credit and not AMDQ cc that is used for tie-breaking.
Existing rule 240	Uplift payments	Amended to clarify that AEMO must use the adjusted AMDQ or adjusted AMDQ credits when calculating a market participants' exposure to uplift payments.
Existing rule 240(3)(c)	Uplift payments	Amendment moves the reference to the different types of loads allocated adjusted AMDQ to under new rule 327A.
Existing rule 331(2)	Transfer of AMDQ or AMDQ ccs	Amendment moves the clause (related to the AMDQ transfer mechanism) to new rule 327A.
New rules		
Proposed rule 327A	Rights associated with AMDQ and AMDQ ccs	New rule clarifies the rights and entitlements of market participants in relation to AMDQ and AMDQ cc (note that these matters are not directly addressed in the existing rules). It does so by first clarifying that market participants who: are responsible for settling Tariff D sites with AMDQ; have AMDQ allocated to them in relation to Tariff V customers; or otherwise hold AMDQ or AMDQ cc, are entitled to the benefits arising from ITR and UH associated with the AMDQ and AMDQ cc. The new rule then clarifies that a market participant may transfer to another market participant an entitlement to the benefits from ITR and UH associated with a quantity of AMDQ or AMDQ cc (without transferring the AMDQ or AMDQ cc themselves) in accordance with the PRT procedures.
Proposed rule 331A	Portfolio Rights Trading procedures	New rule requires AEMO to make procedures for the transfer of entitlements to the benefits associated with a quantity of AMDQ and AMDQ credit between market participants.
Consequential amendments		
Existing rule 211(2A)	Timing of submissions by market participants	Amended as consequence of definition change.
Existing rule 239	Ancillary payments	Amended as consequence of definition change.