11 September 2015

Mr John Pierce
Chair, Australian Energy Market Commission
Level 6, 201 Elizabeth Street
Sydney NSW 2000

By online submission: AEMC website

Dear Mr Pierce

RE: Wholesale Gas Markets Discussion Paper

ERM Power Limited (ERM Power) welcomes the opportunity to provide comments on the Wholesale Gas Markets discussion paper released by the AEMC.

About ERM Power Limited

ERM Power is an Australian energy company that operates electricity generation and electricity sales businesses. Trading as ERM Business Energy and founded in 1980, we have grown to become the 4th largest electricity retailer in Australia, with operations in every state and the Australian Capital Territory. We are also licensed to sell electricity in several markets in the United States. In addition, we have recently commenced retailing gas to industrial and commercial customers. We have equity interests in 497 megawatts of low emission, gas-fired peaking power stations in Western Australia and Queensland, both of which we operate.

ERM Power is an active gas market participant in the Declared Wholesale Gas Market (DWGM), the Brisbane Short Term Trading Market (STTM) and the Wallumbilla Gas Supply Hub.

Enhancement of existing arrangements should be an option considered

ERM Power has concerns that the three high level market design concepts put forward by discussion by the AEMC all involve a significant overhaul of the existing trading arrangements on the east coast, including the dismantling of the current facilitated trading markets at major demand centres. ERM Power believes that such a move would significantly reduce competition within Australia's east coast gas market.

In exploring the future direction of Australia's gas market, we believe a fourth option should be considered. The fourth option should build upon the current arrangements and investigate areas for enhancement. Significant investment has been made by industry, AEMO, government and regulatory authorities to develop and implement the existing trading markets. Some of them such as the STTM and Gas Supply Hub are also relatively young, STTM being in operation for less than five years and the Gas Supply Hub for less than two years. It would be sensible to consider an option that involves improvements to the existing market frameworks before concluding that a completely different model is required to achieve the Energy Council's objectives.

Facilitated trading markets at demand centres should not be dismantled

"Focusing trade at a point that best serves the needs of participants" is part of the COAG Energy Council's vision for Australia's future gas market. While recognising that there are certainly areas where the STTM and DWGM could be improved, ERM Power believes that the STTM and DWGM largely contribute towards this objective by enabling trade to occur at key demand centres.

Since the STTM was implemented in late 2010, we have seen new entrant retailers and large direct gas users enter the market, in particular in Sydney and Adelaide.[1] The STTM has been successful in supporting market entry, by enabling participants who have load located within the Hub, to purchase gas without necessarily having to enter into traditional gas supply and transportation arrangements to meet part or all of their demand requirements. This can be particularly helpful for a new entrant with a small initial load, who may face difficulties in securing small parcels of gas on sufficiently competitive and flexible terms. The option of a spot market also helps to provide competitive tension in buyers' gas purchase negotiations with suppliers. In addition, the STTM enables market participants to manage and optimise their short term position by providing a market based mechanism for allocating overs and unders. ERM Power, which owns and operates Oakey Power Station in Queensland, utilises the Brisbane STTM for this purpose.

The DWGM has been around for more than fifteen years and has the largest number of active market participants. ERM Power is a relatively new entrant market participant retailer in the DWGM. While there are issues with the DWGM that we outlined in a previous submission to the AEMC, in general we consider the DWGM to be effective at enabling the trade of short term gas and facilitating the entry of new players.[2] With respect to our concerns with the DWGM, we do not repeat our comments here, but refer the AEMC to our earlier submission dated 26/03/15.

We would not support a removal of the DWGM or STTM, or any change to these markets to make them voluntary and/or solely balancing regimes. Such a move will erode a significant benefit of the current arrangements and adversely impact competition by eliminating a key means of accessing competitively priced short term gas supply. It would impose barriers to entry by making contracted supply and transportation capacity a pre-requisite for participation. This would be detrimental to retail competition and revert the market to pre-STTM days.

Also, given the industry structure at each of the demand hubs, where one or two players dominate (for instance, AGL is a dominant gas retailer in NSW, Origin in SA and Origin and AGL in Queensland), there is a risk that balancing gas regimes end up favouring the larger players and result in disproportionate costs and unmanageable risks imposed on smaller participants.

---

[1] Since the commencement of the STTM in Adelaide and Sydney in October 2010, new participants have entered the market including M2 Energy, Qenos, Go Energy, Red Energy, Visy Paper and CovaU.

[2] In our submission of 26 March 2015, we outlined our concerns regarding the way in which part of the costs of out of merit order gas, or ancillary payments, are allocated as "congestion uplift". ERM Power considers the cost allocation methodology to be inequitable and overly complex. It also imposes disproportionate risks on smaller participants. The uplift cost allocation methodology should be reviewed and simplified. The AEMC should also investigate whether it would be beneficial to incorporate the cost of ancillary payments into the market price, such that the market price encompasses all price risk.

In addition to price, transparency of market conditions plays a critical role in helping participants manage their risks and make informed trading decisions

Price transparency is another element of the COAG Energy Council's vision for the future gas market. Subject to certain issues associated with DWGM being resolved (refer to footnote 2), ERM considers the STTM and DWGM prices to be reasonably reflective of underlying supply and demand conditions.

In addition to price transparency, ERM Power believes it is very important to ensure transparency of factors which may impact demand and supply conditions. This is extremely critical to enabling market participants make informed trading decisions and manage risks.

A process is required to notify and update the market about potential events, and information should be made available in a single location

Information about physical market conditions should be made available on a much wider and real time basis and captured in a single location. Unplanned pipeline and production facility constraints should be reported as soon as they occur. This is consistent with the NEM, where market participants, network service providers and AEMO are required to notify the market as soon as practicable when events occur that may impact the secure operation of the power system and/or the market price. While the Gas Bulletin Board currently reports a range of useful information, it is not apparent that real time issues affecting key facilities are being adequately reported. A specific example is provided below.

Over 22/07/15 and 23/07/15 there was an incident on the Moomba to Sydney Pipeline that involved a line valve closure near Bulla Park. This incident increased gas flows out of Victoria (via Culcairn and Longford) and impacted Victorian gas prices (the 6 am price reaching $9.75/GJ on 23/07/15). This incident therefore had an impact on participants in Victoria, in addition to Sydney. However when the incident occurred, a notification was sent out by AEMO to Sydney STTM registered participants only (as the incident had been triggered by Jemena Gas Networks as a Sydney STTM Hub Contingency Gas event). Obviously not all participants in the Victorian market operate in Sydney, and hence Victorian-only participants were placed at an information disadvantage, not being alerted to the situation until a later time and not having access to the details.

There should be a public notification process, similar to the Market Notice process in the NEM, by which market participants are notified by AEMO of potential events and all events as they occur. Further, distribution of notices should not be restricted to a particular jurisdiction or market, given the interconnected nature of the east coast gas market.

In addition, information and real time updates should be made available on the Gas Bulletin Board or other single location. During the above mentioned incident, the Bulletin Board linepack adequacy report indicated an "amber" status for the Moomba to Sydney Pipeline, however the information available was limited; there was no information about what steps were being taken or how long it would take to resolve the issue. There was some information provided on the AEMO website, however without being notified of the event in the first place, a participant would not have been prompted to look at this particular section of AEMO's website.[3] A single website

[3] From the home page, a participant would have to then navigate through four further pages to find the information (Home page, Gas, Policies and Procedures, Short Term Trading Markets, Contingency Gas).

that captures all real time market information would be more efficient and reduce complexity for participants (including NEM and gas market participants).

National Gas Bulletin Board improvements are needed

We refer to the comments made in our earlier submission to the AEMC's initial discussion paper, in which we emphasized the importance of making publicly available key LNG related information on the Gas Bulletin Board. As such we welcome AEMO's recent decision to establish a Gladstone Demand Zone which has the effect of capturing the LNG pipelines and making relevant LNG related data publicly available.

Exemption provisions need review

In addition to the comments in our earlier submission, we strongly recommend that the rules and procedures relating to Gas Bulletin Board be reviewed and an assessment made of the appropriateness of current provisions that allow a facility to apply for and be granted an exemption from registration and reporting, and whether such provisions are consistent with the objective of achieving a transparent Australian gas market. For example, we note the recent exemption granted to the Silver Springs Storage facility in Queensland, which has a storage capacity of 35 PJ and hence not insignificant.[4] The exemption was granted on the basis that the facility is not connected to a Bulletin Board pipeline. Given the size of this facility and the fact that it is connected (via pipeline) to the east coast gas market at Wallumbilla, we would have expected this facility to be captured. While not disputing AEMO's interpretation or application of the existing market rules, we believe it is inconsistent with the objective of the Bulletin Board to allow such major facilities to be exempted (the Bulletin Board's purpose, as defined under the National Gas Rules, being to "*facilitate trade in natural gas and markets for natural gas services through the provision of system and market information which is readily available to all interested parties, including the general public*" (Rule 142)). In a transparent gas market, all major facilities (over a reasonable size) that connect to the east coast gas market (whether indirectly or directly) should be captured to provide a complete picture of the market.

A process is needed to ensure compliance with the rules

There needs to be an improved process for ensuring that facilities are aware of their obligations and reporting as required under the rules. For example, we note that production facilities do not appear to be providing Medium Term Capacity Outlooks as required by the "National Gas Bulletin Board Capacity Outlooks" rule changes that have been effective since 8 January 2015. These rules require pipeline operators and production facilities to report information about any planned maintenance (scheduled to occur beyond the next 7 days) and submit to the Bulletin Board the same notices that they provide to shippers who are their customers. While the pipeline operators appear to be furnishing such information, since the start of the year we have only seen one production facility (Camden – which we understand has since been exempted) provide this report.

Additional physical supply hubs and capacity trading

ERM Power has been an active trading participant in the Wallumbilla Gas Supply Hub for nearly a year and supports the investigation into the pros and cons of introducing new supply hubs at

[4] As reported by Core Energy Group in its report to AEMO, "Gas Storage Facilities, 2015" which forms part the 2015 GSOO Supporting Information.

different locations such as Moomba. However as discussed earlier, we do not support the dismantling of the existing facilitated trading markets at the demand centres.

To maximise the benefit of supply hubs, and more generally to enable gas to flow to where it is most valued within the interconnected east coast gas market, a transparent mechanism is required to enable the trading of short-term pipeline transportation capacity. In respect of the Gas Supply Hub, any capacity trading mechanism should be designed to support commodity trading on the exchange. This will encourage an increase in the volume of trades by enabling more buyers and sellers to come to market. Under the current Gas Supply Hub arrangements, a participant can only trade if it has pre-contracted transportation capacity rights to flow gas to or from the Hub.

Ideally, any pipeline capacity (including capacity that has been contracted to a shipper) that is not being utilised would be made available on a market for purchase. A mechanism that enables the release and trading of unutilised capacity, would reduce current inefficiencies, alleviate barriers to trading gas and minimise the cost of delivering gas to energy consumers.

We recommend that the AEMC should investigate possible arrangements that would allow unutilised capacity to be released and traded on a short term basis.

Virtual Hub models - important elements need to be defined

ERM Power recognises that the AEMC's conceptual models are intended to be high level. However we find it difficult to comment without certain elements being defined. The following factors need to be explored before we can meaningfully comment on any Virtual Hub concept.

- **Market price**: How will the reference or market price determined? E.g. based on bids and offers such as the STTM/DWGM, or more similarly to the GSH approach of determining a volume average weighted price based on trades undertaken in a day?
- **Hub services**: What other services (e.g. transportation, balancing, redirection, compression) would be required to move gas within the defined Hub? How would they work? How would such costs be allocated? In the AEMC's example under Concept 3 where a participant injects gas at Moomba and withdraws at Hobart, how would the gas be transported, who would provide the transport service, and how are costs accounted for?
- **Physical local differences**: How do the models cater to the physical differences in each location (e.g. Victoria's "meshed" transmission system versus the point to point pipelines in NSW and Queensland).
- **Access to entry and exit points and terms for access**: How would the exit and entry points be defined? How would participants secure access and at what cost?
- **System security**: Who would be responsible for system security?
- **Risks and risk management:** What are the key trading risks? Are risks manageable?
- **Who participates**: Are the markets mandatory or voluntary?
- **Investment incentives**: What are the incentives to invest in pipeline infrastructure?
- **Regulatory arrangements and industry structure**: In considering the appropriateness of any Virtual Hub model and the provision of Hub Services, the current industry structure, where there is obvious dominance with respect to ownership and operation of gas

transmission pipelines, needs to be taken into account when determining what regulatory arrangements may be required.

- **Costs and benefits**: Ultimately any move away from the current arrangements would need to be justified by a cost-benefit assessment.

As stated earlier, due consideration would need to be given to the alternatives, including the option of building upon the existing arrangements and addressing known issues before moving to a completely different framework.

Alignment with other gas market development work streams

Clarification is needed as to how the AEMC east coast gas market review, DWGM review, AEMO's work in developing the Wallumbilla Gas Supply Hub and the ACCC East Coast Gas inquiry will tie together. There appears to be overlap in areas and we are unclear about how any inconsistent findings will be addressed.

Thank you again for the opportunity to provide input into this important review. Please feel free to contact me if you would like to discuss any of the points raised in our submission.

Yours sincerely

[signed]

Sarah Kok
Commercial Manager - Gas
02 8243 9109 - skok@ermpower.com.au