



Australian Energy Market Commission

CONSULTATION PAPER

National Gas Amendment (Various Hedging Instruments in the Declared Wholesale Gas Market) Rule 2011

Rule Proponent

Australian Energy Market Operator

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RULE
CHANGE

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About the AEMC

The Council of Australian Governments, through its Ministerial Council on Energy (MCE), established the Australian Energy Market Commission (AEMC) in July 2005. The AEMC has two principal functions. To make and amend the national electricity and gas rules – and to conduct independent reviews of the energy markets for the MCE.

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1 Introduction

On 18 November 2010, the Australian Energy Market Operator (AEMO or Proponent) submitted a Rule change request to the Australian Energy Market Commission (AEMC or Commission) in relation to market hedging instruments in the Declared Wholesale Gas Market (DWGM).

This Consultation Paper has been prepared by the staff of the AEMC to facilitate public consultation on the Rule change proposal and does not necessarily represent the views of the AEMC or any individual Commissioner of the AEMC.

This paper:

- sets out a summary of, and a background to, the Rule change request proposed by the Proponent;
- identifies a number of questions and issues to facilitate the consultation on this Rule change request; and
- outlines the process for making submissions.

2 Background

What the Rule change request is about

This Rule change request seeks to increase the flexibility with which participants in the DWGM can use market hedging instruments. In particular, it seeks to improve the flexibility with which Market Participants (MPs) can use Authorised Maximum Daily Quantity (Authorised MDQ or AMDQ), AMDQ Credits and Authorised Maximum Interval Quantity (AMIQ) profiles.

AEMO consulted on the significant elements of this Rule change request with its Gas Wholesale Consultative Forum (GWCF) and the public before submitting the Rule change request to the AEMC.

Declared Wholesale Gas Market

The DWGM is a wholesale gas market in Victoria regulated by the National Gas Rules and operated by AEMO. Parties bid gas into the market at System Injection Points (SIPs) – points on the Declared Transmission System (DTS) which is the transmission network for the DWGM. AEMO schedules injections and withdrawals to meet the projected demand for gas at least cost while ensuring the gas transmission network remains safe and secure.

Market instruments for managing financial risk

Authorised MDQ, AMDQ Credits, and AMIQ profiles are market instruments which participants can use to help manage their financial risks in the market. These instruments and the benefits they provide to MPs are described below.

System Injection Points and Close Proximity Injection Points

Gas is injected into the market at SIPs. There are eight SIPs in the DTS: Longford, VicHub, BassGas, Dandenong LNG Storage Facility, Culcairn, Iona Gas Storage Plant, SEA Gas and Otway Gas Plant.

Under the Rules¹, AEMO can treat two or more SIPs as a single SIP for some purposes – such SIPs are called Close Proximity Injection Points (CPPs). CPPs are SIPs as determined by AEMO that can be regarded as the same SIP for the purposes of scheduling and determining an MP's AMIQ.

Authorised MDQ and AMDQ Credits

Authorised MDQ and AMDQ Credits can provide financial and scheduling benefits to their holders in the DWGM. 990 TJ of Authorised MDQ was created in 1998² and primarily allocated to consumers and their retailers. It remains primarily allocated to consumers and their retailers.

1 Rule 200.

2 The peak capacity of the system from Longford in 1998 was 990 TJ per day.

AMDQ Credits have been created following capacity expansions in the DTS since 1998. Projects leading to the expansion of the DTS include the South West Pipeline, the connection of the Western Transmission System, the NSW-Victoria interconnect and BassGas. It is currently understood that there is a total of 460 TJ of AMDQ Credits.³

Authorised MDQ and AMDQ Credits (collectively referred to as AMDQ) can provide financial and physical benefits to their holders:

- tie-breaking rights for scheduling injections and controllable withdrawals at injection and withdrawal points to which the Authorised MDQ or AMDQ Credits are allocated;
- the potential to create hedges against congestion uplift charges; and
- prioritisation in not being load shed.

Authorised Maximum Interval Quantity profiles

DWGM participants holding AMDQ may be able to hedge against congestion uplift charges by submitting an AMIQ profile to AEMO before the start of the gas day and being scheduled to inject gas into the market.

Congestion uplift charges are levied on DWGM participants and the DTS service provider to partially fund ancillary payments.⁴ Ancillary payments are additional payments made to DWGM participants who have been scheduled to inject or withdraw gas out of merit order as those participants are to pay or be paid their bid price instead of the market (imbalance) price for that scheduling interval.

In being scheduled to inject gas, an MP holding AMDQ can create a daily uplift hedge (in units of energy). An MP can divide its uplift hedge amongst the five scheduling intervals⁵ in that gas day⁶ by submitting an AMIQ profile to AEMO before the start of the gas day.⁷ This AMIQ profile is expressed as a percentage for each scheduling interval and the uplift hedge is divided amongst the scheduling intervals according to its AMIQ profile.

For each scheduling interval, an MP will only be charged for congestion uplift to the extent its actual withdrawals exceed its uplift hedge allocated to that scheduling interval.

³ AEMO, *AEMO Public Register of Spare Capacity for the Gas Transmission System*.

⁴ The remaining cost recovery for Ancillary payments occurs through levying Surprise Uplift and Common Uplift charges. See AEMO, *Wholesale Market Uplift Payment Procedures (Victoria)*, January 2011.

⁵ The five scheduling intervals are the periods of time commencing at 6am, 10am, 2pm, 6pm and 10pm each gas day. Scheduling intervals do not overlap.

⁶ A gas day is the 24 hour period starting at 6am each day.

⁷ There are limitations on the way in which an MP can allocate its uplift hedge amongst the five scheduling intervals for a gas day.

An MP can only nominate an AMIQ profile to AEMO before the start of the gas day. An MP cannot renominate its AMIQ profile during the gas day.

Injection Hedge Nominations and Agency Injection Hedge Nominations

DWGM participants must submit an Injection Hedge Nomination (IHN) to AEMO in relation to each SIP to obtain an uplift hedge from that SIP. The IHN is the amount of an MP's scheduled injections that it nominates to AEMO to apply in the determination of its AMIQ.

Participants can also make arrangements with another participant to allocate part of their scheduled injections towards the uplift hedge of that other participant by submitting an Agency Injection Hedge Nomination (AIHN) to AEMO. The scheduled injections of an MP are firstly allocated towards meeting the MP's IHN. Scheduled injections can be allocated to an AIHN if they exceed the MP's IHN.

DWGM participants may only submit IHNs to SIPs and are unable to renominate their IHNs during a gas day.

3 Details of the Rule change request

The Rule change request from the Proponent proposes to:

- permit MPs to update their nominations of AMDQ during the gas day, including moving AMDQ between SIPs that are CPPs. However, AMDQ could only be moved from a SIP to the extent that gas injections have not been scheduled at that SIP⁸;
- allow DWGM participants to update their AMIQ profiles for future scheduling intervals within the gas day;
- allow AEMO to classify a collection of SIPs to be CPPs if those SIPs can be regarded as a single SIP for the purposes of calculating an MP's uplift hedge. Currently a collection of SIPs can only be classified as CPPs if they can also be regarded as a single SIP for the purposes of scheduling; and
- allow MPs to have the option of submitting IHNs, AIHNs and AMIQ profiles to AEMO up to one hour before a gas day starts. Currently MPs have the option of submitting this information to AEMO up to 11:00am on the day that is two days before the day on which a gas day commences.⁹

In its Rule change request the Proponent provides its rationale for the Rule change. A number of key points raised in the Rule change request are summarised as follows:

- MPs are currently unable to reallocate their AMDQ amongst SIPs at CPPs within a gas day for injection tie-breaking purposes. This increases risks to participants if a SIP fails and they are unable to inject gas into the DTS.
- MPs are unable to optimise the use of their uplift hedge during a gas day as they are unable to modify their AMIQ profile within the gas day.
- It is not possible for a collection of SIPs to be regarded as a single SIP for the purposes of scheduling as physical flow constraints differ between SIPs and these affect scheduling.
- It will provide more flexibility to MPs in how they use IHNs, AIHNs and AMDQ, allowing these products to be used more effectively and efficiently.

The proponent's Rule change request includes a proposed Rule.

⁸ For example, if a participant had been scheduled to inject 10 TJ at a SIP to the end of the current scheduling interval, 10 TJ AMDQ must remain nominated to that SIP until the end of that gas day. However, it could be renominated to another SIP for the next gas day.

⁹ Rule 211.

4 Assessment Framework

The Commission's assessment of this Rule change request must consider whether the proposed Rule promotes the National Gas Objective (NGO) as set out under section 23 of the National Gas Law (NGL).

Box 4.1: National Gas Objective

The National Gas Objective 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.

We intend to assess this proposal by focussing on the following issues.

The ability of Market Participants to manage their financial risks

AEMO stated in the Rule change request that the proposal seeks to enable MPs to use hedging instruments more effectively, allowing them to more efficiently manage their trading risks.

We will consider the impact of the proposal on the ability of MPs to manage their financial risks, in particular managing their congestion uplift charges and other charges.

Impact on ancillary payments and uplift charges

The proposal would allow MPs to renominate their AMIQ profiles, potentially impacting the total level of ancillary payments in the DWGM and cost-recovery for those ancillary payments.

We will consider the impact of the proposal on:

- the total level of ancillary payments in the DWGM and the allocation of congestion, surprise and common uplift charges amongst parties; and
- the extent to which the costs of ancillary payments are recovered from the parties whose actions generated the relevant ancillary payments.

Impact on competition

Allowing participants to update their AMDQ nominations during the gas day may impact the level of competition to inject gas at Close Proximity Injection Points, both in relation to parties holding AMDQ and parties not holding AMDQ.

We will consider the impact of the proposal on the level of competition to inject gas into the DTS.

5 Issues for consultation

Taking into consideration the assessment framework and potential requirements to implement the proposed Rule change, we have identified a number of issues for consultation that appear to be relevant to this Rule change request.

These issues outlined below are provided for guidance. Stakeholders are encouraged to comment on these issues as well as any other aspect of the Rule change request or this paper including the proposed framework.

Managing financial risks

Question 1

What would be the likely impact of allowing Market Participants to renominate AMDQ between SIPs during the gas day on their ability to manage congestion uplift and other charges?

Question 2

What would be the likely impact of allowing Market Participants to renominate AMIQ profiles during the gas day on their ability to manage congestion uplift and other charges?

Ancillary payments and uplift charges

Question 3

What would be the likely impact of the proposal on the total ancillary costs and allocation of those costs in the DWGM?

Question 4

What would be the likely impact of the proposal on the extent to which the costs of ancillary payments are recovered from the parties whose actions generated the relevant ancillary payments?

Competition

Question 5

What would be the likely impact of the proposal on the level of competition to inject gas into the DTS?

6 Lodging a submission

The Commission has published a notice under section 303 of the NGL for this Rule change request inviting written submission. Submissions are to be lodged online or by mail by Thursday 24 March 2011 in accordance with the following requirements.

Where practicable, submissions should be prepared in accordance with the Commission's Guidelines for making written submissions on Rule change proposals.¹⁰ The Commission publishes all submissions on its website subject to a claim of confidentiality.

All enquiries on this project should be addressed to Sacha Blumen on (02) 8296 7800.

6.1 Lodging a submission electronically

Electronic submissions must be lodged online via the Commission's website, www.aemc.gov.au, using the "lodge a submission" function and selecting the project reference code GRC0004. The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated.

Upon receipt of the electronic submission, the Commission will issue a confirmation email. If this confirmation email is not received within 3 business days, it is the submitter's responsibility to ensure the submission has been delivered successfully.

6.2 Lodging a submission by mail

The submission must be on letterhead (if submitted on behalf of an organisation), signed and dated. The submission should be sent by mail to:

Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Or by Fax to (02) 8296 7899.

The envelope must be clearly marked with the project reference code: GRC0004.

Except in circumstances where the submission has been received electronically, upon receipt of the hardcopy submission the Commission will issue a confirmation letter.

If this confirmation letter is not received within 3 business days, it is the submitter's responsibility to ensure successful delivery of the submission has occurred.

¹⁰ This Guideline is available on the Commission's website.

Abbreviations

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AIHN	Agency Injection Hedge Nomination
AMDQ	See Authorised MDQ
AMIQ	Authorised Maximum Interval Quantity
Authorised MDQ	Authorised Maximum Daily Quantity
Commission	See AEMC
CPPs	Close Proximity Injection Points
DTS	Declared Transmission System
DWGM	Declared Wholesale Gas Market
GWCF	Gas Wholesale Consultative Forum
IHN	Injection Hedge Nomination
MPs	Market Participants
NGL	National Gas Law
NGO	National Gas Objective
Proponent	See AEMO
SIPs	System Injection Points