

Pipeline Regulation and Capacity Trading Discussion Paper published

Submissions open on Pipeline Regulation and Capacity Trading Discussion Paper

The efficient use of pipelines supports liquid wholesale markets

The Australian Energy Market Commission (AEMC) has today released a discussion paper on pipeline regulation and capacity trading as part of Stage 2 of its East Coast Wholesale Gas Market and Pipeline Frameworks Review.

This objective of the discussion paper is to stimulate discussion around the arrangements for pipeline regulation and capacity trading in the context of the Council of Australian Governments' Energy Council Vision for the establishment of a liquid wholesale gas market.

The ability of gas to flow easily across the pipeline system to where it is most highly valued is a critical enabler of a liquid gas market. If there are obstacles to participants being able to access pipeline capacity, this will inhibit their ability to trade gas. Consequently, efficiency in the use of pipeline capacity will be of fundamental importance in allowing the Vision to be achieved.

Efficiency in the usage of pipelines can be facilitated by capacity trading, which is likely to be increasingly important as structural changes in the gas sector lead to more volatile gas transportation requirements for shippers. Given the inconsistency between the potentially dynamic nature of shippers' transportation requirements and the long-term allocation of capacity typical under the contract carriage model to date, there may be a need to reconsider regulatory frameworks to facilitate greater liquidity in the trading of capacity.

The paper discusses three potential impediments to the efficient use of capacity:

1. high search and transaction costs in the market for transmission capacity;
2. a lack of incentives to provide access by shippers that hold capacity; and
3. a lack of incentives to facilitate access by pipeline owners.

The Commission is working with the Australian Competition and Consumer Commission which is currently undertaking an inquiry into the east coast gas market to get a better understanding of the extent to which capacity trading occurs in practice, and the materiality of these potential impediments.

Approaches to address issues

The discussion paper introduces three broad approaches to how changes in the market might be implemented to address the potential impediments identified.

Facilitate trading between parties

This approach addresses search and transaction costs by facilitating trade between parties, on the assumption that shippers and pipeline owners have incentives to trade capacity and that these costs are the primary barrier to trades occurring. Individual elements within the approach include improved information provision and capacity rights standardisation.

Improve the incentives of capacity holders in the provision of capacity

Under certain circumstances, capacity holders may have an incentive to "hoard" capacity in order to preclude competitors from upstream or downstream markets, despite not using the capacity to transport gas. This can result in capacity going unused despite being of value to a shipper, in an outcome known as contractual congestion.

The paper presents a number of possible mechanisms to improve the incentives of capacity holders to provide capacity, or require them to do so through compulsory capacity reallocation.

The paper introduces three broad approaches to how changes in the market might be implemented

Improve the incentives of pipeline owners in facilitating access to capacity

The current gas transmission regulatory regime under the National Gas Law is based on the National Access Regime under Part IIIA of the *Competition and Consumer Act 2010* (Cth), which applies to a range of infrastructure sectors. The focus of the National Access Regime is to facilitate access to infrastructure where the facility owner also competes in upstream or downstream markets. This market structure is not applicable to the gas industry, with pipeline owners generally not competing to produce or retail gas.

The gas regulatory regime may therefore not be directly targeted at addressing the potential sources of market failure that might arise specifically in the gas transmission sector. This may be resulting in inappropriate level of regulation for transmission pipelines.

Unconstrained by competition or regulation, pipeline owners may be able to price capacity at a level higher, or offer a level of service lower, than that which would be expected to prevail in a workably competitive market. Amongst other things, this could have a detrimental effect on competition in the wholesale market, if high prices result in the inefficient under-utilisation of pipelines.

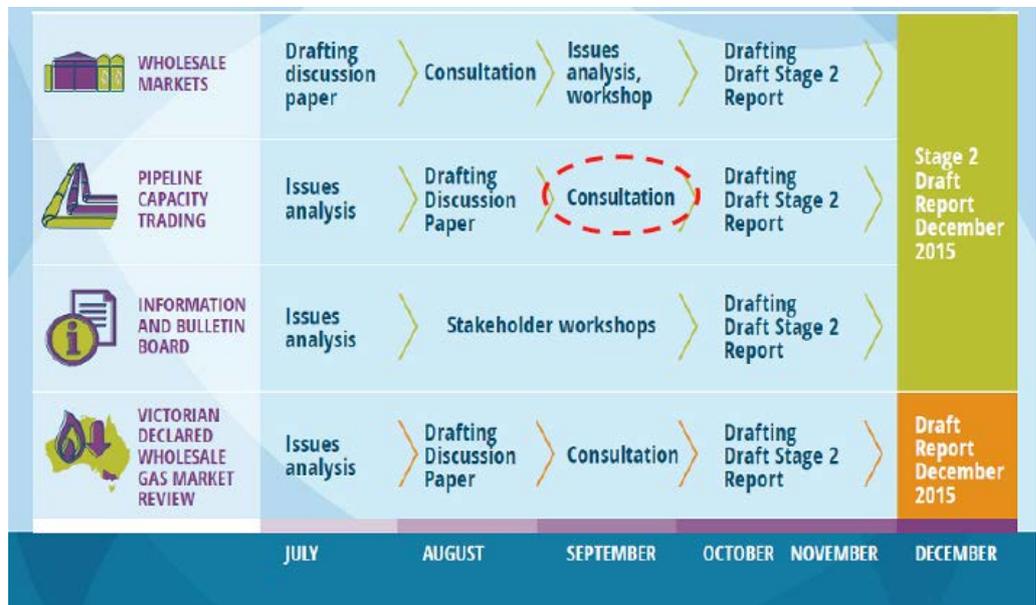
The paper presents a number of possible ways to improve the incentives of pipeline owners to facilitate access to capacity, including changes to the regulatory regime so that it more directly considers potential sources of market failure in the gas transmission sector.

Next steps

The Commission is holding a public forum on the East Coast Wholesale Gas Market and Pipeline Frameworks Review on 30 September 2015, 2pm – 5pm at Pullman Sydney Hyde Park. If you wish to attend the public forum, please register online by Friday 25 September 2015.

Submissions to the Pipeline Regulation and Capacity Trading Discussion Paper close on 16 October 2015. Feedback from stakeholders through the consultation process will inform the Commission's recommendations in the Stage 2 Draft Report, which will be presented to the COAG Energy Council for its December 2015 meeting.

As outlined in the Stage 1 Final Report, there are four workstreams being progressed as part of Stage 2 of the review. These are illustrated in the diagram below. This discussion paper relates to the Pipeline Capacity Trading workstream.



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