

7 June 2012

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Dear Mr Pierce

Rule Change Request – STTM Market Schedule Variation Transactions

We request the Australian Energy Market Commission (AEMC) make an amendment to the National Gas Rules (NGR) with regard to the originating participant for market schedule variation (MSV) transactions in the Short Term Trading Market (STTM).

The existing rules limit MSV transactions to being initiated by STTM shippers and do not allow STTM users to transact MSVs directly with other STTM users. Presently, user to user transactions are effected by having a shipper (acting as an intermediary) undertake two transactions, one with each user. The proposed Rule change seeks to amend rule 423 to enable users to undertake an MSV transaction directly with other users. The change is to enable STTM users to manage MSV transactions more efficiently.

Other than providing for more efficient implementation of transactions that can already take place within the market, the proposal would have no impact on operation of the market or market outcomes.

Shippers, who currently are required to act as the intermediary for such transactions, have indicated their support for the proposed change. Therefore, AEMO requests that the AEMC consider this rule change request as non-controversial under section 304 of the National Gas Law (NGL).

If made, AEMO would seek to incorporate this rule change in the March 2013 release of the market systems. Therefore publication of the Notice of Proposed Rule under section 303 of the NGL by the end of July would enable us to meet this goal.

A description and drafting of the proposed Rule, a statement of the issues concerning the existing NGR, and how the proposed Rule contributes to the achievement of the National Gas Objective is provided at Attachment A.

AEMO would be pleased if you could have these matters considered by the AEMC. For further details, please do not hesitate to contact Terry Grimwade, Executive General Manager, Market Performance on 03 9609 8520.

Yours sincerely



Matt Zema
Managing Director and Chief Executive Officer

Attachment A: Rule Change Proposal

120607 AEMC SUBMISSION - MSV USER TRANSACTIONS

Attachment A: Rule Change Proposal

This Rule Change Proposal is structured as follows:

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1. Summary

At present only an STTM Shipper can initiate a Market Schedule Variation (MSV) transaction with another STTM Shipper or STTM User. STTM Users undertaking an MSV with other STTM Users currently have two transactions initiated and managed by an STTM Shipper. That is, the STTM Shipper has to undertake an MSV transaction with User 1, then initiate a reversing transaction with User 2, in order to match the deviation quantities of the STTM Users.

AEMO is proposing that the rules be modified so that an STTM User may initiate an MSV with another STTM User directly, without having an STTM Shipper act as intermediary and managing the process.

2. Background

The Short Term Trading Market (STTM) is a day-ahead market for natural gas at defined hubs. The STTM currently operates in Adelaide, Brisbane and Sydney. Offers to supply gas are submitted by STTM Shippers to the market and bids to withdraw gas are submitted by STTM Users for that hub on the day before the relevant gas day (i.e. ex-ante). AEMO then determines the market price and initial market schedule for that gas day the day before the relevant gas day. This schedule is published approximately 18 hours ahead of the gas day so that shippers can use this information to input into their shipping nominations to the relevant facility operators, a process which occurs outside the STTM.

The day after the gas day, allocation agents appointed by STTM facility operators submit allocation data to AEMO. This allocation data is used to calculate participants' deviations from their scheduled quantities. This is known as their deviation quantity. Deviations incur penalties compared to the ex ante market price.



Figure 1 - Simple Timeline of STTM activities

Market Schedule Variations (MSVs) are a mechanism in the STTM which was designed to allow STTM Shippers to renominate expected changes in gas supply and consumption to the facility operator either ahead of or during the gas day in response to changes in conditions that may have occurred since the ex ante schedule was run. MSVs incur lower penalties than deviations to encourage expected changes to be communicated to the market and facility operators.

Under the current rules, an MSV requires two parties to undertake the transaction; an originating shipper and a receiving party, who may either be a shipper or a user. The agreed variation quantity submitted and confirmed in the MSV transaction results in a reduction in each party's deviation quantities.

For example, if a user’s demand increases by 5 TJ, they would request an STTM Shipper to deliver an additional 5 TJ of gas to meet this demand. The STTM Shipper will make an intraday nomination to the STTM facility operator to deliver an additional 5 TJ of gas to the hub. At the end of the gas day, the additional gas delivered to the hub by the STTM Shipper is seen by the STTM as a deviation and the additional gas consumed at the hub by the STTM User is also seen as a deviation. However, as this change was expected and the additional gas was ordered, the STTM Shipper may submit an MSV for 5 TJ. The user confirms that they requested this increase in delivery. Both parties’ deviations are decreased by 5 TJ as a result.

In practice, MSVs are used as much to trade deviations between two parties after the gas day as they are to reflect intraday renominations. In this aspect they are used as a risk mitigation tool in the STTM to reduce parties’ exposure to deviation charges and settlement shortfall charges. As the rules currently limit the originating party to being an STTM Shipper, if two STTM Users wish to trade their deviation quantities they require a third party shipper to act as an intermediary to conduct the transaction. This requires two opposing MSV transactions to be submitted by this shipper and relies on the two users to accept the transactions.

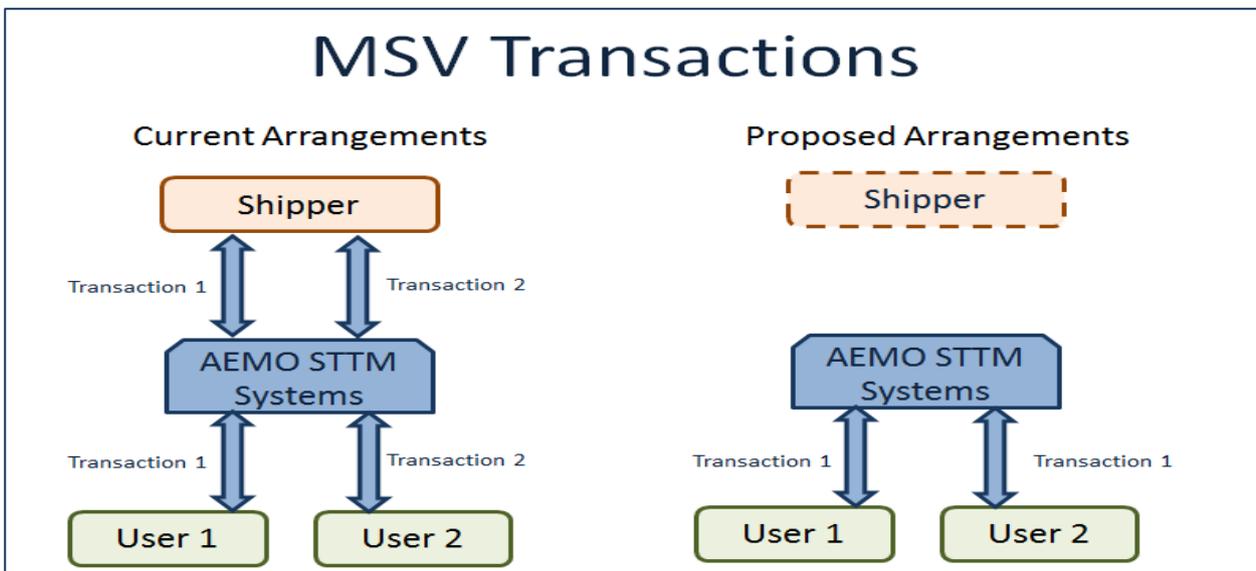


Figure 2 - Simplified MSV Transaction and proposal

In order to improve efficiency in the market, AEMO proposes to allow a user to submit an MSV where the counterparty is also a user, thereby enabling a direct user to user MSV in a single transaction.

3. Statement of Issues

3.1 Current NGR requirements

Rule 423 of the National Gas Rules (NGR) sets out the framework governing MSVs, including who can submit and receive an MSV, the type of information that is to be contained in an MSV and the timing for an MSV transaction. The STTM Procedures (clause 7.3) outlines the detailed requirements relating to MSVs.

In particular, this Rule 423 specifies that an MSV must be initiated by an STTM Shipper. This means that MSVs must always have an STTM Shipper participating in any MSV transaction. This does not allow for STTM Users to transact MSVs directly with other STTM Users.

3.2 Issue with current NGR requirements

The initial concept was that an MSV would be used by a shipper to recognise changes in the quantity of gas shipped to the hub to meet changes in demand required by a user. Consequently, the current rules were drafted on the basis of MSV transactions being initiated by STTM Shippers.

Experience in the market has shown that the diversity of user demand and forecasting also provides users with opposite deviations which provide an opportunity for STTM Users to undertake MSVs with other STTM Users, not just matching changes in deliveries with changes in consumption.

Hence, while Rule 423 of the NGR only allows STTM Shippers to initiate MSV transactions, MSV transactions between users can only be effected with an STTM Shipper acting as an intermediary with back to back transactions with the two users.

STTM Shippers and STTM Users have advised AEMO that this is inefficient and have asked that the direct user to user transaction be implemented. AEMO supports this position and therefore proposes that the rule be modified so that the originating participant party who can submit an MSV be broadened to include STTM Users.

4. Proposed solution and Rule

4.1 Description of the Proposed Rule

The proposed amendment to the NGR (Rule 423) which would remove the limitation of the party submitting the MSV from being an STTM Shipper to being either an STTM Shipper or STTM User.

The proposed rule, if made, would also require a number of STTM Procedure and IT system changes. Therefore AEMO is also proposing a transitional rule which would allow the NGR amendments to come into effect when the STTM Procedures are made.

AEMO's proposed change to rule 423 is provided at Appendix I.

4.2 If the Rule is made, what will be included in the STTM Procedures?

AEMO proposes to amend the STTM Procedures to allow STTM Users to submit an MSV and to detail the processing of that MSV.

4.3 Other requirements under the NGL

Compatibility with AEMO's declared system functions under s295(5) of the National Gas Law –

This rule only impacts market participants in the Short Term Trading Market, where AEMO has no declared system functions in gas; therefore this change is not incompatible with the proper performance of AEMO's declared system functions.

4.4 Request for non-controversial rule

AEMO requests that the AEMC considers this Rule change proposal as non-controversial under section 304 of the National Gas Law (NGL). Section 290 of the NGL defines a non-controversial Rule as:

“...a Rule that is unlikely to have a significant effect on a market for gas or the regulation of pipeline services;”

AEMO considers that section 304 applies for the following reasons:

- Users are able, under the current rules, to complete an MSV transaction between themselves, but in an inefficient manner, with a shipper acting as an intermediary; The proposed rule simply improves the efficiency with which these transactions can be undertaken.
- This proposal has industry support as indicated in the feedback to the STTM Review and the STTM Consultative Forum. Further, STTM Shippers have not objected to the proposed change as they have received no benefit from acting as an intermediary; and
- AEMO considers the proposed rule change will not have a material effect on the STTM market outcomes, trading participants or other market observers for the above reasons.

4.5 Stakeholder consultation

Under the National Gas Rules (NGR), the Australian Energy Market Operator (AEMO) is required to conduct a number of market reviews for the Short Term Trading Market (STTM).

The first review commenced in August 2011 and was completed in March 2012 and covered a variety of areas ranging from the operation of Market Operator Service to improvements in the operation of the STTM.

The review has involved public consultation and public workshops. The notes and information for the consultation paper and workshops have been published on AEMO's website on the STTM Reviews page¹.

In the course of this review in considering operational improvements which could be implemented in the STTM, Participants raised the issue of the initiation of MSV transactions. Participants identified that operational improvements could be achieved by allowing two STTM Users, not just STTM Shippers, to initiate an MSV transaction.

There was support from industry through the consultation to improving the MSV process, with the final report recommending:

From an efficiency perspective and with a view to reducing barriers to inter-company market schedule variations (MSV) trading, AEMO considers that the MSV framework should be amended to recognise user-to-user transactions.

¹ <http://www.aemo.com.au/en/Gas/Wholesale-Gas-Markets/Short-Term-Trading-Market/Review-of-Short-Term-Trading-Market>

Appendix II provides a summary of the submissions from participants who supported the proposal to extend the initiation of MSV transactions to Users on the basis of improved market efficiency. No objections were raised to the proposed change.

4.6 Application of Proposed Rule

In submitting the proposed rule change AEMO believes:

- that the proposed rule change does not impose or impact the substantive rights, obligations or duties of STTM participants. MSV transactions are voluntary bilateral transactions, not mandatory transactions. Further, the proposed rule acknowledges the existing arrangements which allow users to make MSV transactions with other users using a shipper as an intermediary.
- this proposal has only positive benefits for market participants as it reduces the number of transactions required to be undertaken by a participant to achieve a user to user transaction.
- trading participants using automated MSV transactions may have to amend their IT systems to accommodate the additional class of Users within the transaction, however, they can still submit these transactions directly with the market systems until those changes are made.
- this proposal has no substantive financial implications for the operation of the STTM in that the market outcome of a user to user MSV transaction already occurs.

5. How the Proposed Rule contributes to the National Gas Objective

Before the AEMC can make a rule change it must apply the rule making test set out in the National Gas Law (NGL), which requires it to assess whether the proposed Rule will or is likely to contribute to the National Gas Objective (NGO).

The NGO 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.”

AEMO considers that the proposed Rule is likely to contribute to the NGO for the following reasons:

- *Allowing User to User MSV transactions* – the proposal Rule change improves the efficient operation of MSV transactions between two users by removing one transaction which is not necessary. This proposal does not change the market outcome as the result is already achievable.
- *Cost of making the changes* – the proposed Rule change would improve operational efficiency of STTM participants by allowing the users to conduct user to user MSVs in a single transaction, rather than through two transactions.

- *Cost of delaying the changes* – User to User transactions will continue to require a second MSV transaction until the rule and procedures are changed.
- *Regulatory Certainty* – the proposed rule change does not substantively change the NGR. The MSV framework continues with only a minor modification being made to it.

Overall, this rule change will provide for more efficient operation of natural gas services for STTM Users and STTM Shippers, as a direct transaction will enable parties to eliminate unnecessary negotiation, reconciliation and management of transactions.

6. Expected benefits and costs of the Proposed Rule

The proposed rule would affect existing and intending STTM Shippers and STTM Users.

As highlighted in previous sections, AEMO expects that the proposed rule would benefit STTM participants, and hence consumers, by removing an unnecessary transaction during the provision of the user to user MSV.

At present there are an average of over 30 user to user MSVs occurring each month in Sydney and Adelaide, each requiring two transactions. Therefore, the removal of the unnecessary transaction improves the efficiency of all of these transactions by removing one of the two transactions from these outcomes.

Further, by removing the unnecessary transaction, the additional transaction management and transaction reconciliation that STTM Shippers presently undertake will be eliminated, leading to more efficient operation.

The benefits to industry, and hence consumers of natural gas, is that removing the unnecessary transaction increases efficiency for STTM Shippers and STTM Users and hence reduces operating costs for STTM participants.

There are minimal costs associated with the Rule change. Some STTM participants who are utilising automated MSV transactions may have to amend their systems to accommodate the change.

From AEMO's perspective, the rule change would require AEMO to undertake a procedure change process, which is considered non-material. The proposed rule would also require changes to the STTM market system, which has been estimated at \$30,000. AEMO, considers this a reasonable cost to change the transaction requirements.

Appendix I: Draft Rule

This appendix outlines the proposed changes to the NGR covered by the Rule change proposal.

Strikethroughs represent proposed deletions and underlined text represents proposed additions.

This draft is based on version 12 of the NGR.

National Gas Rules – Part 20

423 Market schedule variations

- (1) An STTM Shipper ~~(the originating STTM Shipper)~~ or an STTM User (the originating Participant) may submit a proposed market schedule variation in respect of a hub and a gas day to AEMO within the time period specified in the STTM Procedures.
- (2) A proposed market schedule variation submitted to AEMO under subrule (1) must contain the information set out in the STTM Procedures about:
 - (a) the nature and quantity of the proposed market schedule variation; and
 - (b) the originating ~~STTM Shipper~~ Participant whose modified market schedule quantity is to reflect the proposed market schedule variation; and
 - (c) the STTM Shipper or STTM User whose modified market schedule quantity will reflect the same proposed market schedule variation (the **receiving Participant**).

Note:

The originating Participant ~~STTM Shipper~~ and receiving Participant may be the same Trading Participant.

- (3) ~~Where a proposed market schedule variation affects two STTM Shippers,~~ The originating Participant ~~STTM Shipper~~ is to be determined in accordance with the STTM Procedures.
- (4) AEMO must reject a proposed market schedule variation if it does not comply with the requirements of subrule (2) or the STTM Procedures.
- (5) Unless AEMO rejects a proposed market schedule variation under subrule (4), AEMO must:
 - (a) if the originating Participant ~~STTM Shipper~~ and receiving Participant are the same Trading Participant – use that market schedule variation in determining the modified market schedule; or
 - (b) if the originating Participant ~~STTM Shipper~~ and receiving Participant are not the same Trading Participant – make the details of the proposed market schedule variation available to the receiving Participant as soon as practicable for confirmation in accordance with the STTM Procedures, and:
 - (i) if the receiving Participant confirms the proposed market schedule variation within the time period specified in the STTM Procedures, AEMO must use that confirmed market schedule variation in determining the modified market schedule; or

- (ii) in any other case, the proposed market schedule variation will expire and must not be used by AEMO in determining the modified market schedule.
- (6) AEMO must make information regarding the status of a proposed market schedule variation available to the originating [Participant](#) ~~STTM Shipper~~ and the receiving Participant within the time period specified in the STTM Procedures.

Transitional Rules

Time period for the provision of proposed market schedule variations

- (1) From the commencement date to the date on which the STTM Procedures are amended to accommodate users submitting market schedule variations:
 - (a) old rules 423(1), 423(2), 423(3), 423(5) and 423(6) continue to apply; and
 - (b) new rules 423(1), 423(2), 423(3), 423(5) and 423(6) have no effect.

Appendix II: Feedback from consultation

The tables below provide a reference to the submissions made by participants in relation to MSV User to User transactions during the Phase 1 review of the STTM.

1.1 Initial Submissions

Table 1 - Submissions on STTM Reviews Phase 1 - Discussion Paper – 16 August 2011

Participant	Submission Date	Page	Feedback
AGL	5 Sep 2011	5	AGL's view is that a further change that should be considered is for the market to permit user-to-user MSVs because what is being modified through this transaction is the ex ante schedule and not pipeline allocations.

1.2 Workshop on STTM Market design – 14 November 2011

Issue of MSV User to User Transactions was discussed and minuted:

MSVs – User to User transactions

Attendees noted that the parties are already able to make user-to-user market schedule variations (MSV) through two transactions and supported allowing such transactions to be made via one transaction. Attendees noted that this provides efficiencies for trading participants.

1.3 Submissions on Draft Report

Table 2 - Submission of STTM Design and demand hubs - Draft Report – 19 December 2011

Australian Power & Gas	2 Feb 2012	4	Australian Power and Gas recognises the importance of MSVs in managing deviations and participants' market risk. It is reasonable to expand this tool for use beyond shippers and allow user to user transactions.
BP	3 Feb 2012	3	Draft recommendations on page 35 10. BP supports User-to-User MSV functionality
Infratil	5 Feb 2012	3	Market Schedule Variations User to User MSVs. IEA supports the addition of User to User MSVs. We see the failure to incorporate User to User MSV's in the initial STTM design as an oversight.
IPPLC	3 feb 2012	6	3.5 Market scheduled variations Participant should be able to enter Market Schedule Variations (MSV's) without restrictions, including related companies. For these reasons, IPRA supports recommendation number 10.

MEU	3 Feb 2012	13-14	The MEU cannot understand why there is a constraint on who a counterparty must be (currently shippers can only be counterparties), and user-to-user trade should be permitted because the outcome still results in a more balanced market.
TRUenergy	3 Feb 2012	14	we support AEMO's attempts to increase options and flexibility in the functionality of MSVs. To this end, we agree with AEMO's recommendation to recognise direct user-to-user transactions.

Glossary

Abbreviation	Explanation
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
MOS	Market Operator Service
MSV	Market Schedule Variation
NGL	National Gas Law
NGO	The National Gas Objective as stated in section 23 of the NGL, being “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”
NGR	National Gas Rules
STTM	Short Term Trading Market
STTM-CF	Short Term Trading Market Consultative Forum