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7 April 2010

Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Ref: GRC0001

Dear Sirs,

APA Group submits its comments on the recent draft decision of the Commission on the National Gas Rules (NGR) change proposal to allow priority in withdrawals at controlled withdrawal points on the Victorian Declared Transmission System (DTS) for those withdrawals associated with AMDQ.

APA group is especially mindful that this is the first Rule change proposal relating to the NGR that has been reviewed by the Commission and APA Group's comments include a discussion of the precedents that will be set by this decision and how they might affect future reviews.

This submission is provided to the Commission in both electronic and hard copy form.

If you have any queries regarding this submission please contact the undersigned on (03) 9797 5204.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Paul Callander', is written above the printed name.

Paul Callander
Manager Regulatory & Gas Market

Encl.

**APA Group Submission
NGR Rule Change Draft Decision
Priority of Withdrawal AMDQ**

APA Group submits its comments on the recent draft decision of the Commission on the National Gas Rules (NGR) change proposal to allow priority in withdrawals at controlled withdrawal points on the Victorian Declared Transmission System (DTS) for those withdrawals associated with AMDQ.

Background

The NGR incorporates the previous Market and System Operations Rules (MSOR) on the operation of the Victorian DTS. These rules allow for priority in scheduling of injection bids into the DTS where there are tied bids at an injection point. However, they do not provide for priority of withdrawal bids under equivalent circumstances although they do provide priority for withdrawals in a curtailment situation.

Currently if two parties submitted withdrawal bids at the same price, the existing rules would prorate the nomination to each party respectively.

The rule change proposal is to provide for priority for withdrawals associated with AMDQ in a tie break situation.

The Commission has made a draft decision not to allow the rule change. This decision appears to be on the basis that it is not apparent that the change would make any significant positive contribution to the attainment of the National Gas Objective (NGO) and that some aspects of the outcome could be detrimental to that attainment.

This submission addresses the positive outcomes, which are stronger than the Commission considered, and the negative outcomes, which were based on a misunderstanding? of the dynamics of the Victorian Declared Wholesale Gas Market (DWGM) and its future relationship with the gas Short Term Trading Market (STTM).

National Gas Objective

“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.”

The decision addressed the potential impacts of the proposal on elements of the NGO and concludes that these impacts are not likely to be significantly positive.

Impact on efficient network investment

While accepting that the impact of the proposal would not be negative in informing investment decisions in the DTS, the Commission does not see any positive impacts. Their reasoning is summed up in the dot points in 3.1.2 of the decision.

- AEMO does not take AMDQ into account in planning True
 - APA Group notes that AEMO is identifying potential enhancements required on the DTS. It is not concerned with the mechanisms by which the identified enhancements may be financed.
- Limited trading of AMDQ True

- APA Group notes that it is not clear why an active market in existing AMDQ would provide useful input into future demand beyond that arising from the auctioning of AMDQ by APA GasNet.
- Will affect demand for AMDQ rights at Culcairn only. True
 - APA Group notes that the fact that the change would affect AMDQ rights at Culcairn only is not a reason to refuse the proposed change.
- AMDQ has limited role in DWGM True
 - APA Group notes that while the role is limited it is not negligible and use of AMDQ rights can increase certainty of gas flows. Greater certainty means that Shippers are more likely to be willing to fund enhancements.

The Commission notes that AMDQ rights are not fully firm transportation rights as recognised on contract carriage pipelines but discounts the degree of firmness that AMDQ can provide. A tie break right means that a Shipper can guarantee that it will get access to gas at the relevant withdrawal point up to its AMDQ limit in priority to all other Shippers. This contrasts with the current situation where such a Shipper ranks equally with all other Shippers who have bid at the same price.

The Commission has also questioned whether, if the investment impact were material, the Rule change should only apply “on a forward looking basis”. It is not clear how this could be implemented as there is no differentiation between current and possible future AMDQ rights in the AEMO market systems. It is also not clear how such a dichotomy of treatment would advance the achievement of the NGO as it would involve significant complications and probably uncertainties into the operation of the DWGM.

Impacts on efficient use of natural gas services

The Commission has come to the tentative conclusion that the proposed Rule change could lead to inefficient use of natural gas services. In making its decision, the Commission has developed a scenario that it judges to be the most likely (albeit still highly unlikely) to result in the use of AMDQ rights at Culcairn (Appendix B). This scenario relates the use of AMDQ rights at Culcairn to supply problems in the NSW market. The pricing assumed by the Commission is not what would occur but the outcome that the proposed rule change would change the allocation of gas exported to NSW at Culcairn is correct.

What would occur is that, under the current rules, a Shipper requiring gas in NSW as a result of problems in alternative supply (ex Moomba or Longford via EGP) can bid gas for export at Culcairn. To be sure of at least some supply, the Shipper must bid withdrawals at the Victorian VOLL. The NSW price cap is irrelevant. All DTS Shippers are equal and all bids at VOLL are pro rated to the available Culcairn capacity. The proposed rule change would change only the allocation of gas for export to provide priority to AMDQ holders in a tie break situation.

However, the Commission has not analysed what is a common scenario where there is demand for exports at Culcairn above the available capacity. This happens with reasonable frequency especially during the winter period as the capacity at Culcairn is limited. This scenario is shown below.

Realistic Scenario

Shipper A has demand in the Riverina region of NSW that it wishes to supply with Longford sourced gas of 10 TJ on the day.

Shipper B has a regular demand in Southern NSW and a supply contract at Longford with a bid for 5 TJ on the day.

Shipper C is facing a supply shortfall in Sydney due to problems at Moomba and needs 10 TJ on the day.

Shippers A, B have purchased 12 and 3 TJ of AMDQ respectively. Shipper C does not have AMDQ.

Culcairn capacity on the day 17 TJ

All 3 Shippers have rights to flow gas on the MSP system north from Culcairn.

Current situation

Each Shipper bids what it needs.

Unless bids are equal gas is dispatched in bid order (highest bid first) until capacity is reached.

If bids are equal then all gas bid is prorated down to available capacity.

Shipper	Bid	Allocated
		(TJ)
A	10	6.8
B	5	3.4
C	<u>10</u>	<u>6.8</u>
	<u>25</u>	<u>17</u>

The only case where a Shipper can guarantee getting at least some of its bid accepted is a bid at Victorian VOLL. The actual price of gas in Victoria or NSW is irrelevant.

Proposed situation

Each Shipper bids what it needs.

Unless bids are equal gas is dispatched in bid order (highest bid first) until capacity is reached.

If bids are equal, gas with AMDQ is dispatched ahead of gas without AMDQ.

After AMDQ bids satisfied in full, gas bid without AMDQ at the equal bid price is pro rated to remaining capacity.

Shipper	Bid	AMDQ Held	AMDQ Allocated	Balance	Total Allocated
			(TJ)		
A	10	12	10	0	10
B	5	3	3	0.667	3.667
C	<u>10</u>	<u>0</u>	<u>0</u>	<u>3.333</u>	<u>3.333</u>

The only case where a Shipper can guarantee getting at least some of its bid accepted is a bid with AMDQ at Victorian VOLL. The actual price of gas in Victoria or NSW is irrelevant.

Shippers with AMDQ can get all of their gas up to their AMDQ entitlements.

It is important to note that all capacity is available for shipping every day. AMDQ not used does not prevent other Shippers from using that capacity.

Currently AMDQ can be utilised by shippers to provide protection for withdrawals from the DTS to distribution networks or consumption sites. Under the proposal these rights to curtailment protection would be extended to shippers selling gas into other transmission systems. This means that they can protect their supply into NSW, which may be for an ongoing demand with significant costs to interruption, against opportunistic pre-emption.

The proposed changes provide shippers holding AMDQ with certainty of bidding outcomes thus ensuring reliable gas supply, one of the elements of the NGO. It should also be noted that the lack of certainty surrounding the shipping of gas from the Victorian to NSW systems, provides an impediment to the development of interstate trade in gas and to expansion of the NSW system.

It is also unclear how the Commission has reached the conclusion that the proposed rule could be characterised as “creates a risk that a party that values the gas more highly relative to the holder of AMDQ/AMDQ rights (sic) is prevented from accessing the gas” (6.3.1).

There are only a few possible situations that can occur at Culcairn:

- If the other Shipper (without AMDQ) bids higher it gets the gas,
- If the other Shipper bids the same as the AMDQ holder and a tie break occurs, the AMDQ holder gets the gas up to his AMDQ limit and the balance (if any) is pro rated as shown above, and
- If the AMDQ holder does not bid then the capacity is available to the other Shipper.

Only in the second situation is the other Shipper prevented from accessing some or all of the gas and in that case it is obvious that the AMDQ holding Shipper values it more as it has committed to the AMDQ cost in Victoria, often having backed this with firm transport rights in NSW, as well as the gas price bid.

The tradeability of AMDQ is irrelevant to this situation. The fact that there may be barriers to trading of AMDQ does not prevent gas from being allocated efficiently.

Market Power

The Market Power argument advanced by the Commission is curious in a number of areas.

- It appears to be based largely on the expected outcomes under the STTM when the market is under stress in NSW.
- It assumes that AMDQ holders could harm other Shippers in some undefined way.
- It ignores that the STTM in NSW applies only to the Sydney (and possibly later Canberra) hub in NSW and specifically excludes the regional markets upstream of Sydney.
- It suggests that refusal to trade AMDQ rights would frustrate the efforts of other Shippers to enter some NSW markets.
- It ignores the advantages security of supply provides in being able to develop markets.

The common theme of all of the arguments used by the Commission in this section of its decision seems to be that, in some way, the holders of AMDQ can unfairly harm the interests of other Shippers. The assumption is that, whether through refusal to trade AMDQ rights or some misuse of those rights, the other Shippers are prevented from flowing gas from the DTS to NSW. As shown above there are a limited number of bidding combinations (between holders of AMDQ and those without) and in only one of the outcomes do the rights of holders of AMDQ cause other Shippers to get less gas than they bid. In that case the Shipper with AMDQ is merely exercising his rights just as the holder of capacity rights on a contract carriage pipeline does. Note that in a similar bidding situation under the current rules the non AMDQ holding Shipper does not get all of the gas it bid for.

Risk Management

The Commission agrees that the proposed rule change would lead to Shippers being able to better manage their risks in the market because they would have more certainty as to the outcome of gas bidding in the DWGM. However, the Commission notes that it is not able to quantify this advantage and thus appears to discount it as a factor in its decision.

Advancement of NGO

The Commission has indicated in its decision that it can only make a rule “if it is satisfied that the Rule will, or is likely to, contribute to the achievement of the NGO.” The Commission, in this decision, appears to have interpreted this test to mean that the proposed Rule change must positively and significantly contribute to the NGO. This interpretation implies that as the current NGR have been shown over approximately 10 years of operation to be reasonably well constructed then it will be difficult for any Rule changes to be approved unless a major flaw is discovered. In the current situation it means that the relatively minor enhancements to the achievement of the NGO likely to accrue from this change seem to be discounted against hypothetical and unlikely problems. It would appear that the Commission is setting an unreasonably high bar for Rule change proposals to clear.

As this is the first Rule change proposal to be considered for the NGR by the Commission a precedent should not be set that will adversely affect future Rule change proposals. The may be particularly relevant for minor non-controversial Rule changes which, by their nature, would have negligible effect on the achievement of the NGO.

Conclusion

This Rule change proposal would appear to make only modest contribution to the achievement of the NGO through a small effect on efficient investment in transmission pipelines and the increase in reliability of supply to gas customers in NSW. However, APA Group regards the arguments put forward by the Commission that there are potential negative effects on achievement of the NGO through inefficient allocation of gas and exercise of market power to be flawed. As a result APA Group considers that the proposed Rule change in balance does advance the achievement of the NGO and thus should be approved.