

Australian Energy Market Commission

# RULE CHANGE

## FINAL RULE DETERMINATION

### National Gas Amendment (STTM Data Validation and Price Setting Process) Rule 2011

**Rule Proponent(s)**

AEMO

**Commissioners**

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5 May 2011

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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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## Summary

On 9 February 2011, the Australian Energy Market Operator (AEMO) submitted the STTM (Short Term Trading Market) Data Validation and Price Setting Process Rule change request. In response to two high price events that occurred in the Sydney hub of the STTM towards the end of 2010, this Rule change request proposes to provide a validation process in the National Gas Rules (Rules) that is intended to reduce the risk of erroneous information being used in the determination of prices and schedules in the STTM.

On 24 March 2011, the Australian Energy Market Commission (Commission) gave notice under the National Gas Law (NGL) of its decision to initiate and assess this Rule change request under an expedited Rule change process on the basis that the Rule change request was a request for an urgent Rule. The Commission received no objections to the expedited process and received two submissions.

On 5 May 2011, the Commission gave notice under the NGL of its decision to publish the final Rule determination and the Rule as Made. The Commission determined that the provision of a validation process in the Rules would reduce the risk of erroneous STTM facility information (either STTM facility operational capacity information or STTM facility allocation information) being used in the setting of schedules and prices in the STTM. Separate validation processes would apply to STTM facility operational capacity information and STTM facility allocation information. The Commission considers that by providing for a validation process in the Rules, this would:

- help to ensure that prices reflect actual market conditions and thus enhances the quality of information available to market participants;
- reduce the risk of manifestly incorrect STTM facility information being used for the setting of schedules and prices; and
- reduce the risk of market participant failure due to pricing events resulting from erroneous STTM facility information.

The Commission considers that the Rule as Made would promote efficient investment in, and use of, natural gas services in the long term interests of consumers. Consequently, the Commission is satisfied that the Rule as Made will or is likely to contribute to the achievement of the National Gas Objective (NGO).

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# 1 AEMO's Rule change request

## 1.1 The Rule change request

On 9 February 2011, AEMO (Rule Proponent) made a request to the Commission to make a rule to address the risk of erroneous information being used in the setting of schedules and prices in the STTM (Rule change request).

## 1.2 Rationale for the Rule change request

In the Rule change request, AEMO sought to address the risk of erroneous STTM facility information (that is, either STTM facility operational capacity information or STTM facility allocation information) affecting the setting of schedules and prices in the STTM. AEMO submitted the Rule change request as a response to two high price events occurring in the STTM as a result of the use of erroneous STTM facility information. Specifically, the two high price events were:

- On gas day 8 October 2010, the ex post imbalance price was set at \$390/GJ leading to \$2.67 million in deviation charges due to erroneous STTM facility allocation information submitted by APA for the Moomba to Sydney Pipeline (MSP);<sup>1</sup> and
- On gas day 1 November 2010, the ex ante market price and capacity price were set at \$150/GJ respectively and the ex post imbalance price was set at \$400/GJ resulting in ex ante charges and payments of \$34 million, deviation charges of \$335 247, deviation payments of \$4.3 million and Market Operator Services (MOS) commodity payments of \$2 million. This was largely due to erroneous STTM facility operational capacity information submitted by APA for the MSP.<sup>2</sup>

## 1.3 Solution proposed in the Rule change request

AEMO proposes to reduce the risk of erroneous information being used for the setting of schedules and prices in the STTM by proposing a Rule that would:

- bring forward the deadline for the submission of STTM facility operational capacity information to AEMO from 11:00am to 9:30am. This is intended to give AEMO more time to validate the information and if the information fails validation or is not submitted in the first place, then AEMO may request that STTM facility operators confirm or resubmit this information. AEMO will then use this information as an input in the setting of the provisional and ex ante market schedules;

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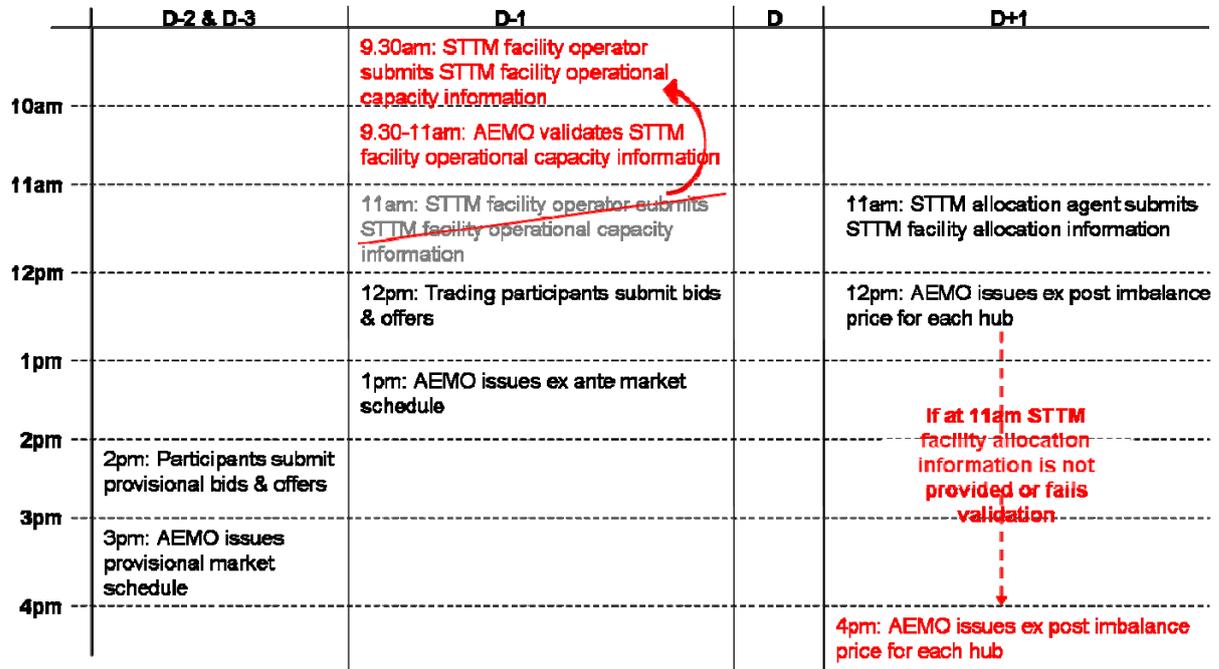
<sup>1</sup> AEMO 2011, Rule change request, p.1.

<sup>2</sup> AEMO 2011, Rule change request, p.1.

- delay the deadline for AEMO to publish the ex post imbalance price from 12:00 noon to 4:00pm in circumstances where AEMO finds that STTM facility allocation information does not meet validation requirements or no STTM facility allocation information have been submitted in time by a STTM allocation agent. Where STTM facility allocation information does not meet validation requirements or no STTM facility allocation information have been submitted by a STTM allocation agent, this gives STTM allocation agents the opportunity to confirm this information and/or resubmit this information to AEMO for substitution;
- require AEMO to validate and substitute STTM facility operational capacity information and STTM facility allocation information in accordance with the STTM Procedures; and
- require STTM facility operators and STTM allocation agents to provide information as required by the STTM Procedures to enable AEMO to validate and substitute STTM operational capacity information and STTM facility allocation information.

Figure 1.1 below depicts the timetable for AEMO's proposed validation process as described in its Rule change request:

**Figure 1.1**



#### 1.4 Commencement of the Rule making process

On 24 March 2011, the Commission published a notice under section 303 of the NGL advising of its intention to commence the Rule making process and consultation in respect of the Rule change request. A consultation paper prepared by Commission staff

identifying specific issues or questions for consultation was also published with the Rule change request. Submissions closed on 21 April 2011.

The Commission received two submissions on the Rule change request following consultation. They are available on the Commission's website<sup>3</sup>. A summary of the issues raised in submissions and the Commission's response to each issue is contained in Appendix A.

The Commission considered that the Rule change request was a request for an urgent Rule. Accordingly, the Commission published its intention to expedite the Rule change request under section 304 of the NGL, subject to any written requests not to do so. The closing date for receipt of written requests was 7 April 2011 and no requests were received. Consequently, the Rule change request was considered under an expedited process in accordance with section 304 of the NGL.

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3 [www.aemc.gov.au](http://www.aemc.gov.au)

## **2 Final Rule Determination**

### **2.1 Commission's determination**

In accordance with section 311 of the NGL, the Commission has made this final Rule determination in relation to the Rule proposed by AEMO. In accordance with section 313 of the NGL the Commission has determined to make a Rule that is substantially similar to that proposed by the Rule proponent.

The Commission's reasons for making this final Rule determination are set out in section 3.1.

The *National Gas Amendment (STTM Data Validation and Price Setting Process) Rule 2011 No 2* (Rule as Made) is published with this final Rule determination. The Rule as Made commences on 16 June 2011. The commencement date for the Rule as Made was set to coincide with the implementation of AEMO's revised systems and procedures.

The Rule as Made is substantially similar to the Rule proposed by the Rule Proponent. The Commission has improved the legal drafting of the Rule and has added a requirement to notify the market if the publication of the ex post imbalance price for a hub is delayed. The key features of the Rule as Made are described in section 3.2.

### **2.2 Commission's considerations**

In assessing the Rule change request the Commission considered:

- the Commission's powers under the NGL to make the Rule;
- the Rule change request;
- the fact that there is no relevant Ministerial Council on Energy (MCE) Statement of Policy Principles;<sup>4</sup>
- submissions received during consultation; and
- the Commission's analysis as to the ways in which the proposed Rule will or is likely to, contribute to the achievement of the NGO.

### **2.3 Commission's power to make the Rule**

The Commission is satisfied that the Rule as Made falls within the subject matter about which the Commission may make Rules. The Rule as Made falls within the matters set out in section 74 of the NGL as it relates to:

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<sup>4</sup> Under section 73 of the NGL the Commission must have regard to any relevant MCE Statement of Policy Principles in making a Rule.

- AEMO's STTM functions and the operation of a short term trading market of an adoptive jurisdiction (section 74(1)(a)(va); and
- the activities of Registered participants, users, end users and other persons in a regulated gas market (section 74(1)(a)(vi)).<sup>5</sup>

Further, the Rule as Made falls within the matters set out in Schedule 1 to the NGL as it relates to the following items:

- 55B - The operation and administration of a regulated gas market;
- 55C - The declared system functions or STTM functions;
- 55D - AEMO's functions, powers and duties, and the duties and obligations of Registered participants, exempted participants and others, in regard to the operation of a declared transmission system or a regulated gas market; and
- 55E - The setting of prices (including maximum and minimum prices) for natural gas and services purchased through the declared wholesale gas market or short term trading market operated and administered by AEMO.

## 2.4 Rule making test

Under section 291(1) of the NGL the Commission may only make a Rule if it is satisfied that the Rule will, or is likely to, contribute to the achievement of the NGO. This is the decision making framework that the Commission must apply.

The NGO is set out in section 23 of the NGL as follows:

“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.”

For the Rule change request, having regard to any relevant MCE Statement of Policy Principles, the Commission considers that the relevant aspect of the NGO is efficient investment and use of natural gas services for the long term interests of consumers of natural gas with respect to the price of natural gas.<sup>6</sup>

The Commission is satisfied that the Rule as Made will, or is likely to, contribute to the achievement of the NGO because providing for a validation process in the Rules would:

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<sup>5</sup> The STTM is a regulated gas market.

<sup>6</sup> Under section 291(2) of the NGL, for the purposes of section 291(1) the Commission may give such weight to any aspect of the NGO as it considers appropriate in all the circumstances, having regard to any relevant MCE statement of policy principles.

- reduce the risk of erroneous STTM facility information being used for the setting of schedules and prices in the STTM. This would help to ensure that prices are more reflective of actual market conditions and result in accurate pricing signals to trading participants. By providing more accurate pricing signals, this would facilitate efficient investment in, and use of, natural gas services in the long term interests of consumers with respect to the price of natural gas. Also, more accurate prices would promote price certainty and foster market participants' confidence in the efficient investment in, and use of, natural gas services in the long term interests of consumers; and
- reduce the occurrence of manifestly incorrect STTM facility information affecting the setting of schedules and prices in the STTM. This would reduce the risk of market participant failure, particularly for smaller market participants to meet its prudential requirements, and would thus contribute to efficient investment in natural gas services and would be in the long term interests of consumers with respect to the price of natural gas.

## **2.5 Other requirements under the NEL**

### **MCE Statement of Policy Principles**

In applying the Rule making test in section 291 of the NGL, the Commission has also had regard to any relevant MCE Statements of Policy Principles as required under section 73 of the NGL. There are no MCE Statement of Policy Principles relevant to this Rule change request.<sup>7</sup>

### **Expedited Rule making process**

If the Commission considers that a request for a Rule is a request for an urgent Rule, the Commission may make the relevant Rule in accordance with an expedited process under section 304 of the NGL.

An urgent Rule is defined in section 290 of the NGL as: 'a Rule relating to any matter or thing that, if not made as a matter of urgency, will result in that matter or thing imminently prejudicing or threatening: (a) the effective operation or administration of a regulated gas market operated and administered by AEMO; or (b) the supply of gas'.

Under an expedited Rule making process, the Commission has six weeks from the publication of the notice under section 303 of the NGL to publish a final Rule determination. No draft Rule determination is published under an expedited Rule making process. Stakeholders have two weeks from the publication of the notice under section 303 of the NGL to submit written requests not to expedite the Rule making process. Stakeholders have four weeks from the publication of the notice under section 303 of the NGL to provide written submissions on the content of the Rule change request.

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<sup>7</sup> Under section 73 of the NGL the Commission must have regard to any relevant MCE statement of policy principles in making a Rule.

## Urgent Rule

AEMO requested that this Rule change request be assessed as an urgent Rule because:<sup>8</sup>

- The Rule change request addresses a material risk to the effective operation of the STTM. Namely, it prevents or reduces the risk of erroneous STTM facility information being used in the setting of STTM prices and thus promotes investor confidence, prevents inefficient wealth transfers and adverse financial impacts on trading participants, particularly market participant failure; and
- The Rule change request would address the risk of another high price event by ensuring that some protections are in place particularly before the onset of the first winter period in which the STTM will operate.

The Commission considers that the Rule change request is a request for an urgent Rule on the basis that it is a Rule which relates to a matter (lack of validation of information used in the setting of schedules and prices in the STTM) which, if not made as a matter of urgency, would result in that matter threatening the effective operation or administration of the STTM. On this basis, the Commission decided to expedite the Rule change request (subject to written requests not to expedite the Rule making process) under section 304 of the NGL. No requests not to expedite the Rule making process were received.

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<sup>8</sup> AEMO 2011, Rule change request, p. 11.

### **3 Commission's reasons**

The Commission has analysed the Rule change request and assessed the issues arising out of this Rule change request. For the reasons set out below, the Commission has determined that a Rule be made. Its analysis of the Rule proposed by the Rule Proponent is also set out below.

#### **3.1 Assessment of issues**

This Rule change request addresses the issue of erroneous STTM facility information (either STTM facility operational capacity information or STTM facility allocation information) being used in the setting of schedules and prices in the STTM. In order to address this issue, AEMO has proposed that a validation process, whereby AEMO is required to validate information in accordance with the STTM Procedures, be stipulated in the Rules. This validation process would apply to STTM facility operational capacity information that is used in the setting of the provisional and ex ante market schedule. Also, a validation process would apply to STTM facility allocation information that is used in the setting of the ex post imbalance price.

The Commission considers that the Rules should provide for a validation process because this would reduce the risk of erroneous STTM facility information being used in the setting of schedules and prices in the STTM. This requires a Rule to be made. The Rule as Made reflects the Commission's position. In particular, the Rule as Made would:

- help to ensure that prices reflect actual market conditions and thus enhances the quality of information available to market participants;
- reduce the risk of manifestly incorrect STTM facility information being used for the setting of schedules and prices; and
- reduce the risk of market participant failure due to pricing events resulting from erroneous STTM facility information.

#### **3.2 Assessment of Rule**

The Rule as Made provides for a validation process to apply to STTM facility information that is intended to reduce the risk of erroneous STTM facility information being used in the setting of prices and schedules in the STTM. In particular, the Rule as Made:

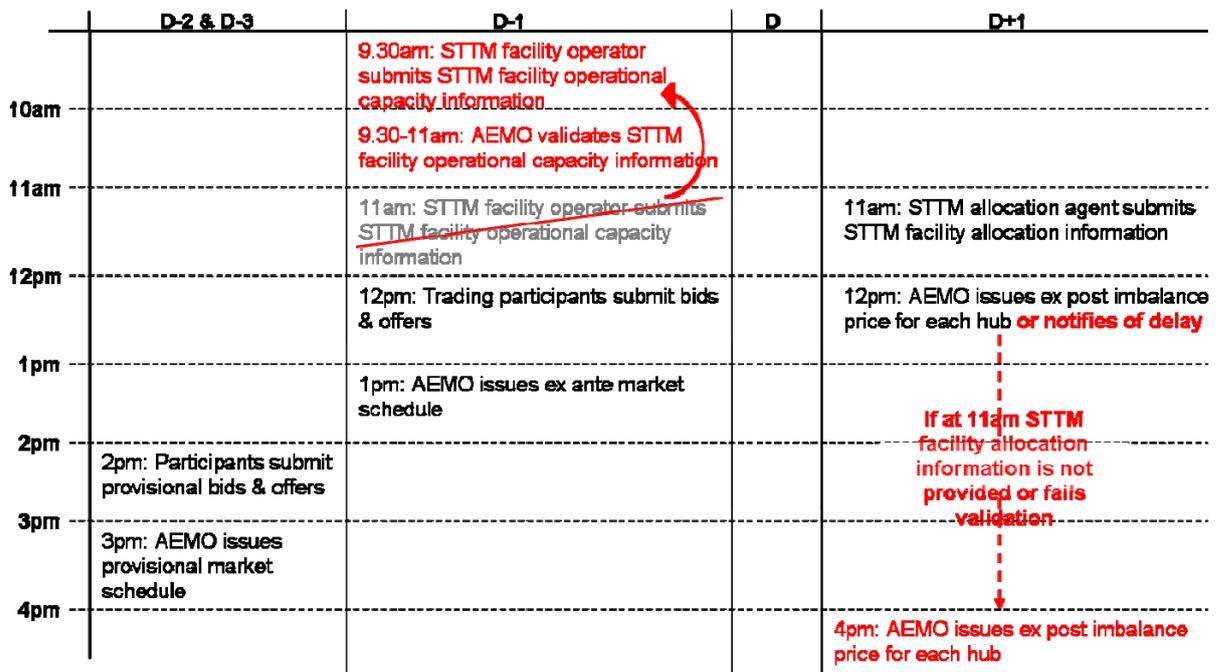
- brings forward the deadline for the submission of STTM facility operational capacity information to AEMO from 11:00am to 9:30am. This is intended to give AEMO more time to validate the information and if the information fails validation or is not submitted in the first place, then AEMO may request that STTM facility operators confirm or resubmit this information in accordance with

the STTM Procedures. AEMO will then use this information as an input in the setting of the provisional and ex ante market schedules;

- delays the deadline for AEMO to publish the ex post imbalance price from 12:00 noon to 4:00pm in circumstances where AEMO finds that the STTM facility allocation information does not meet validation requirements or no information is provided. Where STTM facility allocation information does not meet validation requirements or no information is provided, this gives STTM allocation agents the opportunity to confirm and resubmit this information back to AEMO for substitution in accordance with the STTM Procedures. If the publication of the ex post imbalance price is delayed from 12 noon to 4pm for the relevant hub, then AEMO must notify trading participants of this delay;
- requires AEMO to validate and substitute STTM facility operational capacity information and STTM facility allocation information in accordance with the STTM Procedures; and
- requires STTM facility operators and STTM allocation agents to provide information as required by the STTM Procedures to enable AEMO to validate and substitute STTM operational capacity information and STTM facility allocation information.

Figure 3.1 below depicts the timetable for the validation process as described in the Rule as Made:

**Figure 3.1**



### **3.3 Difference between the Rule as Made and the proposed Rule**

The Rule as Made is substantially similar to the Rule proposed by the Rule proponent. However, the Rule as Made differs from the proposed Rule insofar as the Rule as Made contains an additional obligation on AEMO to notify trading participants if the ex post imbalance price cannot be published by 12 noon with respect to the relevant hub. In addition, legal drafting improvements have been made.

### **3.4 Civil Penalties**

The Rule as Made amends a provision (rule 414(1)) that is currently classified as a civil penalty provision under the *National Gas (South Australia) Regulations*. The Commission considers that rule 414(1) should remain classified as a civil penalty provision.

The Rule as Made makes new provisions in the Rules. The Commission will not recommend that any of these new provisions be classified as civil penalty provisions. AEMO considers that the equivalent of rule 414(2B) be classified as a civil penalty provision. This rule requires STTM facility operators to provide information, in accordance with the STTM Procedures, to enable AEMO to validate and substitute information in accordance with rule 414(1). The Commission will not recommend to the MCE that rule 414(2B) be classified as a civil penalty provision. This is because this rule effectively requires compliance with the STTM Procedures (as the STTM Procedures will detail the information that must be provided in order to comply with the rule and the manner in which it must be provided). Section 91BRJ of the NGL (Compliance with the STTM Procedures) sets out the consequences of non-compliance with the STTM Procedures and the Commission considers that it would be potentially inconsistent with section 91BRJ of the NGL if, in addition, rule 414(2B) was classified as a civil penalty provision.

### **3.5 Conduct Provisions**

The Rule as Made does not amend any Rules that are currently classified as conduct provisions under the *National Gas (South Australia) Regulations*.

The Rule as Made makes new provisions in the Rules. The Commission will not recommend that any of these new provisions be classified as conduct provisions.

## 4 Commission's assessment approach

This Chapter describes the analytical framework that the Commission has applied to assess the Rule change request in accordance with the requirements set out in the NGL (and explained in Chapter 2).

The Commission's assessment of this Rule change request must consider whether the proposed Rule will, or is likely to, contribute to the achievement of the NGO as set out under section 23 of the NGL. The proposed Rule will be assessed against the relevant counterfactual arrangements, which in this case are the existing provisions in the Rule.

In assessing the Rule change request against the NGO the Commission has considered the extent to which the Rule change request promotes efficient investment in, and use of, natural gas services.

In assessing this Rule change request, the Commission has considered the following issues:

- the validation process for STTM facility operational capacity information used in the setting of the provisional and ex ante market schedule; and
- the validation process for STTM facility allocation information used in the setting of the ex post imbalance price.

The Commission focused on these set of issues because these were the key proposals outlined in the Rule change request.

Furthermore, the Commission considers that this Rule change request raises broader questions on how to comprehensively address the problem of erroneous STTM facility information. Detailed consideration of these matters would affect the requisite scope of this Rule change request.

However, given that this Rule change request is a request for an urgent Rule and the Commission acknowledges the need to put in place appropriate measures before the onset of the first winter period in which the STTM will operate, the Commission considers that the scope of this Rule change request should be confined to an assessment of the solution specifically proposed by AEMO. That is, the Commission's assessment will focus on whether the measures proposed by AEMO contribute to the achievement of the NGO.

With respect to broader questions on how to address the problem of erroneous STTM facility information, the Commission considers that these questions should be considered by AEMO when it conducts its reviews regarding the identification of any improvements in the operation of the STTM. AEMO must complete its review of the operation of the STTM by 31 March 2012.<sup>9</sup>

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<sup>9</sup> Rule 489.

## **5 Validation process for the setting of the provisional and ex ante market schedule**

This Chapter discusses the proposal to provide a validation process in the Rules that applies to STTM facility operational capacity information, which is used to set the STTM provisional schedules and ex ante market schedule.

### **5.1 Rule Proponent's view**

AEMO considers that the current arrangements in the Rules do not provide sufficient measures to address the risk of erroneous STTM facility operational capacity information affecting the setting of the provisional and ex ante market schedule.

AEMO's concerns in relation to the quality of STTM facility operational capacity information arose out of events occurring on 1 November 2010. On this gas day, the ex ante market price and capacity price were set at \$150/GJ respectively and the ex post imbalance price was set at \$400/GJ resulting in ex ante charges and payments of \$34 million, deviation charges of \$335 247, deviation payments of \$4.3 million and Market Operator Services (MOS) commodity payments of \$2 million.<sup>10</sup> This high price event was largely due to erroneous STTM facility operational capacity information submitted by APA on the Moomba to Sydney Pipeline.<sup>11</sup>

Under AEMO's proposed Rule, the deadline for the submission of STTM facility operational capacity information for the day preceding the relevant gas day would be shifted from 11am to 9.30am.<sup>12</sup> Requiring STTM facility operational capacity information to be submitted earlier would provide AEMO with time to validate submitted STTM facility operational capacity information.

Under AEMO's proposed Rule, AEMO would be required to validate and, if necessary, substitute STTM facility operational capacity information. There would be an obligation on STTM facility operators to provide AEMO with information to enable AEMO to validate and, if necessary, substitute STTM facility operational capacity information. The STTM Procedures would provide the details of this validation and substitution process.

### **5.2 Stakeholders' views**

There were two submissions on this issue. Origin Energy submitted that it generally supported the provision of a validation process in the Rules as proposed under AEMO's Rule change request.<sup>13</sup>

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<sup>10</sup> AEMO 2011, Rule change request, p. 4-5.

<sup>11</sup> AEMO 2011, Rule change request, p. 1.

<sup>12</sup> AEMO 2011, Rule change request, p. 5.

<sup>13</sup> Origin Energy 2011, Submission on Rule change request, p.1.

The Australian Pipeline Industry Association (APIA) also expressed its general support on the Rule change request, but sought to raise a specific matter. That is, APIA submitted that where STTM facility operational capacity information has failed AEMO's validation process (flagged/suspect information) and is not subsequently confirmed by the STTM facility operator, then AEMO should use the default STTM facility operational capacity information and not the flagged/suspect information. In these circumstances, APIA considers that using the default STTM facility operational capacity information would further reduce the risk of erroneous pipeline information causing high price events.<sup>14</sup>

The Rule as Made will require AEMO to validate and substitute information in accordance with the STTM Procedures. Therefore, the details of how validation will be conducted and what 'default' information will be used when no information is provided or information provided fails validation will be contained in the STTM Procedures. For this reason, the Commission considers that APIA's concerns would be more appropriately addressed in the Procedure change process relating to the STTM Procedures currently being conducted by AEMO.

### 5.3 Analysis

The ex ante market schedule refers to the schedule of gas offers and bids, and the setting of prices for the day prior to a particular gas day (D-1).

The ex ante market schedule has the following inputs:<sup>15</sup>

- all current valid ex ante offers for a gas day;
- all current valid ex ante bids and price taker bids for a gas day;
- current STTM facility hub capacities;
- capacities and haulage priorities of registered facility services;
- capacities of registered trading rights;
- price limits; and
- scheduling parameters used by AEMO.

These inputs are then run using a scheduling and pricing engine, which then produces the following outputs:<sup>16</sup>

- the quantity of gas to be delivered to or withdrawn from the hub by each shipper;

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<sup>14</sup> Australian Pipeline Industry Association 2011, Submission on Rule change request, p. 2.

<sup>15</sup> Rule 415(1) and refer to AEMO 2010, Technical Guide to the STTM, p. 41.

<sup>16</sup> Rule 415(2) and refer to AEMO 2010, Technical Guide to the STTM, p. 44.

- the quantity of gas to be withdrawn at the hub by each user;
- ex ante market price;
- capacity price for each STTM facility; and
- pipeline flow direction constraint price for each STTM pipeline.

Currently, the timing of this scheduling process is as follows:

- By 11am on D-1 - STTM facility operator submits operational capacity information;<sup>17</sup>
- By 12pm on D-1 - Trading Participants submit last bids and offers;<sup>18</sup> and
- By 1pm on D-1- AEMO issues the ex ante market schedule.<sup>19</sup>

The provisional schedules are determined two and three days prior to a particular gas day (D-2, D-3 respectively). At D-2 and D-3, the following times apply to the setting of the provisional schedule:

- 2pm - submit provisional bids and offers;<sup>20</sup> and
- 3pm - AEMO issues provisional market schedule.<sup>21</sup>

AEMO's concerns focus on the STTM facility operational capacity information that is provided by STTM facility operators to AEMO. STTM facility operational capacity information (or hub capacity information) refers to the STTM facility operator's daily estimate of the quantity of natural gas that the STTM facility operator expects that the STTM facility can deliver to the relevant hub for the following three gas days.<sup>22</sup> The STTM facility operational capacity information limits the quantity of gas that the STTM will schedule for delivery to the hub from that facility on a gas day.<sup>23</sup>

Under the current Rules there is only one hour on D-1 between the time that a STTM facility operator submits the STTM facility operational capacity information and when trading participants submit bids and offers. Further, under the current Rules, there are two hours between the time that STTM facility operational capacity information is submitted and the setting of the ex ante market schedule.

The Commission accepts that there is no process in the Rules currently in place to determine the validity of STTM facility operational capacity information.

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17 Rule 414(1).

18 Rule 410(2)(c).

19 Rule 417(1).

20 Rule 410(2)(a)-(b).

21 Rule 416(1)-(2).

22 Rule 414(1).

23 AEMO 2010, Technical Guide to the STTM, p. 32-3.

Consequently, as the event at the Sydney hub of the STTM on 1 November 2010 demonstrates, there is a material risk that erroneous STTM facility operational capacity information can affect the setting of the ex ante market schedule.

The Commission considers that this risk can be addressed by AEMO's proposal to provide a validation process in the Rules that applies to the STTM facility operational capacity information, which is used to set the ex ante market schedule. The Commission considers that a validation process is a reasonable measure that would reduce the risk of erroneous STTM facility operational capacity information being used in the setting of the ex ante market schedule. More pertinently, a validation process would help ensure that prices reflect actual market conditions (or the true supply-demand balance) and thus result in the transmission of accurate pricing signals to trading participants.

Thus, a validation process would help ensure that more accurate or higher quality information (as expressed through accurate pricing signals) is available and would encourage efficient trading among trading participants in the STTM. Enhancing the efficiency of trading among trading participants in the STTM would promote efficient investment in, and use of natural gas services in the long term interests of consumers with respect to the price of natural gas. The provision of a validation process in the Rules would thus be likely to contribute to the achievement of the NGO.

By providing for a validation process in the Rules to reduce the risk of erroneous STTM facility operational capacity information, this would also address the risk of market participant failure. If a validation process was not in place, then the market may be settled at prices higher than they should be, which would affect the financial position of trading participants. This could result in trading participants exceeding their trading limit and leading to AEMO issuing a margin call and potential leading to the suspension of a trading participant from the STTM. The provision of a validation process in the Rules would reduce the risk of market participant failure due to erroneous STTM facility operational capacity information affecting its financial position. This validation process would thus contribute to the NGO by promoting efficient investment in natural gas services in the long term interests of consumers.

Furthermore, by providing for a validation process for the setting of the provisional schedules and ex ante market schedule and prices, there appears to be no adverse implications for other STTM processes. For example, the time for the submission of trading participants bids and offers would remain unchanged and would not affect the pipeline nomination process.

Importantly, a validation process proposed by AEMO would not involve resetting prices after erroneous STTM facility operational capacity information has been submitted. This would help to ensure that there is sufficient price certainty, which forms the basis for consequential commercial decisions, including the pipeline nomination process. The Commission considers that the validation process proposed by AEMO strikes the right balance of reducing the risk of erroneous STTM facility operational capacity information while retaining price certainty for commercial decisions. By retaining price certainty and accuracy, this fosters market confidence and

facilitates efficient investment in, and use of, natural gas services. This would be in the long term interests of consumers with respect to the price of natural gas and would be likely to contribute to the achievement of the NGO.

#### **5.4 Conclusion**

The Commission determines that providing for a validation process in the Rules that applies to STTM facility operational capacity information would help to address the risk of erroneous information affecting the setting of the provisional schedules and ex ante market schedule. The Commission considers that a validation process in the Rules that applies to STTM facility operational capacity information would help to ensure that the provisional and ex ante market schedule more accurately reflects actual market conditions. By more accurately reflecting actual market conditions, this would help to ensure efficient pricing signals and thus would promote efficient investment in, and use of, natural gas services in the long term interests of consumers. The provision of a validation process in the Rules would thus be likely to contribute to the achievement of the NGO.

## 6 Validation process for the setting of the ex post imbalance price

This Chapter discusses the proposal to provide a validation process in the Rules that applies to STTM facility allocation information, which is used to set the STTM ex post imbalance price.

### 6.1 Rule Proponent's view

AEMO considers that the current arrangements in the Rules do not provide sufficient measures to address the risk of erroneous STTM facility allocation information affecting the setting of the ex post imbalance price.

AEMO's concerns arose out of events occurring on 8 October 2010. On this day, the ex post imbalance price was set at \$390/GJ leading to \$2.67 million in deviation charges. This event was largely due to erroneous STTM facility allocation information submitted by APA on the Moomba to Sydney Pipeline.<sup>24</sup>

AEMO proposes that a validation process be applied to STTM facility allocation information that has been submitted to AEMO from STTM allocation agents. Specifically, AEMO proposes that if a STTM allocation agent submits STTM facility allocation information at 11am on the day after a particular gas day and this information fails AEMO's validation process, then AEMO will send this information back to the STTM allocation agent to confirm or resubmit. AEMO would then defer the setting of the ex post imbalance price from 12pm to 4pm. By deferring the publication of the ex post imbalance price, this gives AEMO the opportunity to verify any STTM facility allocation information, which has been flagged by AEMO due to having failed its validation process, with the STTM allocation agent.

Additionally, if AEMO does not receive STTM facility allocation information by 11am, then the setting of the ex post imbalance price would be deferred until 4pm, and AEMO would request that the STTM allocation agent submit this information to AEMO.

Note that under AEMO's proposal, if the STTM facility allocation information is submitted at 11am and it satisfies AEMO's validation process, then the ex post imbalance price will be published at 12 noon as consistent with current arrangements.

AEMO also proposes that deferring the setting of the ex post imbalance price would not trigger an administered ex post pricing state. An administered ex post pricing state sets the ex post imbalance price equal to the ex ante market price, which may be capped at the administered price cap. AEMO proposes that the administered ex post pricing state would be triggered if:

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<sup>24</sup> AEMO 2011, Rule change request, p. 1.

- The STTM facility allocation information was submitted at 11 am and it passed the validation process, but for other reasons, AEMO was not able to publish the ex post imbalance price by 12pm; or
- The STTM facility allocation information was submitted at 11am and it failed the validation process or no STTM facility allocation information was provided at 11am, but nevertheless, AEMO was not able to publish the ex post imbalance price by 4pm.

## 6.2 Stakeholders' views

There was one submission on this issue: Origin Energy submitted that it generally supported the provision of a validation process in the Rules as proposed under AEMO's Rule change request.<sup>25</sup>

## 6.3 Analysis

The ex post imbalance price reflects the impact that deviations on the gas day would have had on the ex ante market price if they had been included in the original schedule.<sup>26</sup> The ex post imbalance price is calculated on the day after a particular gas day (D +1).

STTM facility allocation information is an input to the setting of the ex post imbalance price. STTM facility allocation information allocates flows on a gas day to the registered facility services for a particular STTM facility (for example, pipeline, storage and production facilities). STTM facility allocation information are submitted by allocation agents appointed by the operators of a STTM facility.<sup>27</sup>

Under current arrangements, the following timeframe applies on the day after a particular gas day (D+1):

- 11am - allocation agent must submit STTM facility allocation information to AEMO;<sup>28</sup> and
- 12pm- AEMO must publish the ex post imbalance price.<sup>29</sup>

Based on the timeframe given above, AEMO has one hour between receipt of the STTM facility allocation information and publication of the ex post imbalance price. Given that there is no validation process currently in the Rules, there is a material risk, under the current timeframes, that erroneous STTM facility allocation information may affect the setting of the ex post imbalance price.

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<sup>25</sup> Origin Energy 2011, Submission on Rule change request, p.1.

<sup>26</sup> AEMO 2010, Technical Guide to the STTM, p. 69.

<sup>27</sup> AEMO 2010, Technical Guide to the STTM, p. 61.

<sup>28</sup> Rule 419(1).

<sup>29</sup> Rule 426(1).

In this context, the Commission considers that AEMO's proposal to provide a validation process in the Rules to verify the accuracy of the STTM facility allocation information is a reasonable measure to help address the material risks associated with erroneous STTM facility allocation information. The Commission considers that this validation process would help to provide accurate information such that the ex post imbalance price is reflective of actual market conditions. The Commission considers that implementing a validation process would enhance the quality of the information and enhance the accuracy of pricing signals, which are based on this information. By enhancing the accuracy of pricing signals, this would facilitate efficient trading between trading participants. These accurate pricing signals would facilitate efficient investment in, and use of, natural gas services in the long term interests of consumers with respect to the price of natural gas. Therefore, the Commission determines that a validation process to apply to STTM facility allocation information would be likely to contribute to the achievement of the NGO.

Furthermore, providing for a validation process to address the risk of erroneous information would consequentially reduce the risk of market participant failure. This result would follow because a validation process would reduce the risk of erroneous information affecting the financial position of trading participants. This would reduce the likelihood of trading participants exceeding their trading limits and consequently reduce the likelihood of margin calls or even suspension from the market. Therefore, providing for a validation process in the Rules would be likely to contribute to the achievement of the NGO by promoting efficient investment in natural gas services.

In addition, the Commission considered and consulted upon whether delaying the publication of the ex post imbalance price would have adverse impacts on related or consequential STTM processes. The Commission accepts that the proposed deadline of 4pm (where STTM facility allocation information has failed validation or no STTM facility allocation information was initially submitted) is appropriate and would not significantly impinge upon the calculation of the Cumulative Price Threshold and prudential monitoring processes.

Finally, in the Rule as Made, the Commission has enhanced the drafting of the proposed Rule by including an additional obligation on AEMO to notify trading participants if the ex post imbalance price cannot be published by 12 noon with respect to the relevant hub.

## **6.4 Conclusion**

The Commission determines that providing for a validation process in the Rules that applies to STTM facility allocation information received by AEMO from STTM allocation agents would reduce the risk of erroneous information affecting the setting of the ex post imbalance price. The Commission considers that providing for a validation process in the Rules would help to ensure that pricing signals reflect actual market conditions. This would promote efficient trading between trading participants and would facilitate efficient investment in, and use of, natural gas services in the long term interests of consumers. Also, the Commission considers that providing for a

validation process in the Rules would help to reduce the risk of market participant failure and thus promote efficient investment in natural gas services. The provision of a validation process in the Rules that applies to STTM facility allocation information would thus be likely to contribute to the achievement of the NGO.

## Abbreviations

AEMO	Australian Energy Market Operator
APIA	Australian Pipeline Industry Association
Commission	Australian Energy Market Commission
MCE	Ministerial Council on Energy
MOS	Market Operator Services
MSP	Moomba to Sydney Pipeline
NGL	National Gas Law
NGO	National Gas Objective
Rules	National Gas Rules
STTM	Short Term Trading Market

## A Summary of issues raised in submissions

Stakeholder	Issue	AEMC response
Origin Energy	Support for the Rule change request	Noted.
Australian Pipeline Industry Association	If STTM facility operational capacity information fails AEMO's validation process and is not subsequently confirmed in time by the STTM facility operator (flagged/suspect information), then AEMO should use the default STTM facility operational capacity information and not the flagged/suspect information.	The Rule as Made will require AEMO to validate and substitute information in accordance with the STTM Procedures. Therefore, the details of how validation will be conducted and what 'default' information will be used when no information is provided or information provided fails validation will be contained in the STTM Procedures. For this reason, the Commission considers that APIA's concerns would be more appropriately addressed in the Procedure change process relating to the STTM Procedures currently being conducted by AEMO.