



Proposed National Gas Amendment (Portfolio Rights Trading) Rule 2014

Request for submissions on a specific issue Explanatory note

23 October 2014

Request for submissions

The Australian Energy Market Commission (Commission) invites written submissions and comments from interested parties on a specific issue raised by the Australian Energy Market Operator (AEMO) with respect to the portfolio rights trading (PRT) rule change request. Details on the issue are set out below. Submissions should address this matter only and must be received by **6 November 2014**.

Submissions should quote project number "GRC0021" and may be lodged online at www.aemc.gov.au or by mail to:

Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Background

Background to the rule change request

The PRT rule change request was submitted to the AEMC on 14 November 2013. It was developed by AEMO in close consultation with the Gas Wholesale Consultative Forum.

The PRT mechanism was proposed to address concerns held by AEMO and the industry that there are a number of barriers which limit market participants' ability to acquire authorised MDQ (AMDQ) and AMDQ credit certificates (AMDQ cc) to meet their injection tie-breaking and uplift hedge needs. To address this problem, AEMO proposed a number of amendments to Part 19 of the National Gas Rules (NGR) to introduce PRT in the Victorian Delcared Wholesale Gas Market (DWGM). The intention was to enable market participants to more readily carry out short term trades of the market benefits attached to AMDQ and AMDQ cc.

AEMO included a high level cost-benefit assessment in its rule change request. It calculated the total system implementation cost of PRT to be \$500,400. With a proposed implementation date in April 2015, the results of the analysis showed that the PRT mechanism could return positive net market benefits if the traded quantity of AMDQ and AMDQ cc was above 10TJ for each year over the lifetime of the project (assumed to be five years).

Further, after discussions with market participants, AEMO considered it had identified sufficient interest in the take-up of PRT. Assuming each market participant retained a five per cent position buffer to manage risk associated with demand fluctuations, AEMO identified scope for between 5-10TJ of AMDQ that could be transferred at Longford, and a further 10-20TJ of AMDQ cc at Iona. That is, enough for the PRT mechanism to return a positive net market benefit, if it were implemented.

The rule change process was initiated by the AEMC on 13 March 2014 with the publication of a consultation paper. A draft rule determination and draft rule were published on 19 June 2014. The Commission's draft rule determination was to make the proposed rule submitted by AEMO. Two stakeholder submissions were received. Both supported the Commission's draft rule determination.

In preparing the final rule determination and final rule, the Commission sought clarification from AEMO on an appropriate commencement date for the final rule, should it be made by the Commission. AEMO was unable to provide a certain timeframe for implementation, but confirmed that the any changes to its IT systems to implement PRT would not be included in its April 2015 IT release as originally proposed. AEMO also informed the Commission that there may be some changes to the estimated costs associated with implementing the proposed rule .

Both of these matters are relevant to the Commission's assessment of the PRT rule change request and need to be addressed in the final rule determination. However, at the time, AEMO was not in a position to be able to advise the Commission on these matters, and stated that it would not be able to do so with any certainty for a few weeks. On 29 August 2014, AEMO requested that the AEMC delay its final rule determination to allow further investigation of changed circumstances, potentially affecting the projected benefits of the proposal.

On 9 September 2014, the Commission made a decision to extend the period of time for making the final rule determination and final rule to 30 October 2014. This was to provide AEMO sufficient time to determine, and to consult with participants on, the re-estimated costs and implementation timeframes, and to then advise the AEMC.

Background to the specific issue

The need for an extension to the timeframe for making the final rule determination has arisen from new information provided by AEMO on the implementation of the proposed rule. This new information results from an internal review by AEMO on the approach taken to estimating the costs and implementation timeframes for PRT.

This review was driven by the recent issues experienced by AEMO in implementing the system changes required to effect the short term trading market (STTM) market operator service (MOS) rule change where an unidentified critical system defect resulted in AEMO administering the market for three days.

AEMO subsequently engaged PriceWaterhouse Coopers (PwC) to conduct a review of the STTM MOS IT change project. In its August 2014 report, PwC made a number of recommendations from which AEMO has developed an action plan. This action plan has had a direct impact on the estimated costs and timeframes for implementing the proposed PRT rule.

Specific issue

On 13 October 2014, following its internal review of the cost and timeframe associated with implementing PRT, AEMO notified the Commission in writing of the following changes:

- The estimated timeframe for implementation of PRT had moved from April 2015 to December 2015.
- The estimate of the total system implementation cost of PRT had increased to \$687,500 from \$500,400 (a 37 per cent increase).
- Under a reduced IT functionality model,¹ the estimate of the total system implementation cost of PRT would be \$559,500 (a 12 per cent increase).

Using the re-estimated timeframe and costs, AEMO revisited its original cost-benefit assessment and found that positive net market benefits would only be achieved if the total traded quantity of AMDQ and AMDQ cc was greater than 13TJ each year over five years. This is greater than the original estimate of 9.5TJ.² AEMO's revised cost-benefit assessment is included as Attachment A.

AEMO also sought feedback from market participants to understand the implications of the revised implementation costs and timeframe (that is, December 2015) on the interest in take-up of PRT if the proposed rule was made. Of the six responses AEMO received:

- two market participants continued to support the implementation of PRT;
- three market participants considered PRT should be put on hold given the AEMC's anticipated Victorian gas market review (see next section); and
- one market participant did not have a clear view but noted that the benefits of PRT remain marginal.

Additional information

In October 2013, the Victorian Government published a report by the Victorian Gas Market Taskforce (Reith Report) which recommended (among other things) that the AEMC undertake a review of pipeline capacity, investment, planning and risk management mechanisms in the Victorian DWGM. The objective of the review would be to ensure the arrangements for access to pipeline capacity promote competition, risk management and provide appropriate investment signals and incentives.

In its note to the Commission advising of the recent changes, AEMO acknowledged that any recommendations for change to the Victorian DWGM resulting from an AEMC led review could affect AMDQ and AMDQ cc. Assuming that any recommendations would have a target implementation date for within a five year horizon, AEMO considered that (taking a conservative approach) this could place an upper time limit on the cost-benefit assessment for PRT.

Update on specific issue

On 20 October 2014, AEMO notified the Commission of a further change to the estimated timeframe for implementation of PRT. In the instance the Commission decided to make a rule to introduce PRT in the DWGM, the expected date for deployment of the IT system

¹ AEMO also considered options for reduced functionality. It found that not providing full Web-Services functionality for PRT would result in savings of approximately 14 per cent of total project costs. In addition, allowing only for pro-rata allocation for PRT would result in a further saving of six per cent of total project costs.

² Under a reduced IT functionality option, net positive benefits can be achieved if the total traded quantity of AMDQ and AMDQ cc is greater than 10.7TJ each year over five years.

changes is now expected to be **late March-early April 2016**. AEMO has indicated that this new timeframe is not expected to change the revised implementation costs. That is, the current estimate of implementation costs remains in the order of \$687,500.

The reason for the change to the expected implementation timeframe from December 2015 to April 2016 is set out in the letter sent from AEMO to the Commission. This is included as Attachment B.

In addition, on 13 October 2014, the Victorian Government released an Energy Statement setting out its plan to secure continued access for Victorian consumers to least cost electricity and gas over the long term. Among other things, the statement announced that in 2014 the Victorian Government will fund the AEMC to undertake a thorough review of capacity and risk management mechanisms in the Victorian gas market, in consultation with AEMO. As indicated by AEMO, any recommendations arising from the review may have additional implications for implementation and use of PRT. However, precisely what impact the pending review will have is largely unknown at this time.

Questions for consultation

Having regard to the above, the Commission requests submissions and comments from stakeholders on the implications of the changes to the implementation costs and timeframe for PRT on the potential uptake - and hence the benefits - of PRT.

Stakeholders may wish to consider the following questions in preparing their submissions:

1. Do you consider that AEMO's revised analysis of the implementation timeframe of April 2016 and total system implementation cost of PRT continues to demonstrate a case for the introduction of PRT in the Victorian DWGM?
2. Would you participate in PRT as a buyer and/or seller of AMDQ and/or AMDQ cc? Please explain your view.
3. As a potential participant (buyer and/or seller), what are the costs and benefits to you from participating? Where possible, please quantify these costs and benefits.

Participant Briefing Note – Portfolio Rights Trading Project

23 September 2014

1. PURPOSE

To update participants on the status of the Portfolio Rights Trading (PRT) project in relation to its value proposition and to seek feedback on whether the project should proceed.

2. BACKGROUND

The current AMDQ transfer process allows for transfers of tariff D AMDQ and AMDQ Credit Certificates on a customer site-to-site or to hub basis which also transfers the physical curtailment right. Such transfers are performed manually by written application and would require agreement of any customer involved. These manual transfers practically cannot be completed more frequently than weekly. Tariff V AMDQ currently cannot be transferred.

PRT would allow transfers of tariff D and V AMDQ and AMDQ Credit Certificates between parties for the benefits of uplift hedges and injection tie-breaking rights without affecting the ownership of the underlying physical (curtailment) rights.

PRT includes a market systems interface which allows for transfers to be transacted electronically by participants on a daily basis if needed.

PRT does not apply to withdrawals (ie. withdrawal tie-breaking rights are unaffected by PRT).

3. RULE CHANGE SUBMISSION TO AEMC

As a result of initial findings on increased scope, schedule and costs, and concerns raised over projected benefits, AEMO requested that AEMC delay its final decision on the PRT rule change proposal to provide time to re-estimate the costs and timeline and consult with participants on changes. AEMC subsequently extended the date for final rule determination to 30 October 2014.

4. WHAT HAS CHANGED SINCE THE AEMC DRAFT DECISION?

A number of matters have arisen which has resulted in AEMO reviewing the value proposition of the PRT project that was part of the rule change submission. These are discussed below.

4.1. Reassessment of implementation requirements

The scope and plans for implementation of PRT have been reassessed following completion of the detailed design and incorporating lessons learnt from the STTM MOS project. As a result:

- Cost of implementation has increased to \$687,500 (up from \$500,400 as per rule change proposal).
- Project completion has moved to 1 December 2015 (from April 2015).
- These changes are necessary due to previous underestimation of development requirements (effort to build), improvement of project management to manage previously underestimated risks inherent in the complexity of the change, and expanded testing to provide the required level of assurance and incorporate an external industry testing stage.

Options for reduced functionality were also considered:

- Not providing full Web-Services¹ functionality for PRT would result in savings of approximately 14% of total project costs.
- If the design was further simplified to only allow for pro-rata allocation² (and not preference), then costs would reduce by approximately a further 6%.

¹ Web-Services functionality allows for participant automated submissions. Only Origin has indicated that it will use Web-Services and still wants csv file upload via the Web-Exchanger as a back-up. However, it has acknowledged that the frequency of its own use is likely to be relatively low.

² Current design has both pro-rata and preference allocation methods as user options. The nominated allocation method only applies if the total nominated quantities exceed the pre-transfer available AMDQ.

- Project costs would then reduce to \$559,500.

4.2. Victorian Gas Market Taskforce report

The Victorian Government may request the AEMC conduct a review³ of access to pipeline capacity (amongst other things) in the Victorian Declared Wholesale Gas Market (DWGM). Any resultant recommendations for change could affect AMDQ and AMDQ credit certificates and would likely have a target implementation date within a 5 year horizon which, taking a conservative approach, places an upper time limit for the cost-benefits assessment of the PRT project.

5. REVISED COST – BENEFIT ASSESSMENT

5.1. Cost-benefits re-assessment

Using the revised costs, the cost – benefit assessment indicates a positive 5 year NPV for full functionality implementation if total traded quantities are more than 13 TJ per annum over 5 years (up from 9.5 TJ).

Under the reduced functionality option, net positive benefits would be achieved if the total trade quantities are greater than 10.7 TJ per annum.

5.2. Benefits re-assessment

The core benefits originally envisaged to support this change were:

- Levels of usage (trading levels) were projected to be 15-20 TJ per annum over 5 years.
- PRT would defer need for pipeline investment by enabling greater utilisation of existing capacity. The cost of system augmentation was assumed to equal the price paid for an Iona credit certificate or 15.58\$/GJ/year (based on a 2011 tender of Iona AMDQ CC).

Feedback sought –

Do you consider the anticipated benefits to continue to remain appropriate in today's context?

Is the proposal to reduce the functionality appropriate, or would this diminish the value of this change?

What quantum of trades do you anticipate?

Do you consider that PRT would defer the need for pipeline augmentation?

Is the assumed cost of system augmentation of 15.58 \$/GJ/year a valid assumption to use for benefits assessment?

Should this project proceed?

³ One of the recommendations made by the Gas Market Taskforce in its final report dated October 2013, was that the Victorian Government request the AEMC undertake a review of pipeline capacity, investment, planning and risk management mechanisms in the Victorian Declared Wholesale Gas Market (DWGM) with the objective of ensuring arrangements for access to the pipeline capacity promote competition, risk management by market participants and provide appropriate investment signals and incentives. The report is available at (link) [Gas Market Taskforce report](#).



20 October 2014

Ms. Anne Pearson
Senior Director
Australia Energy Market Commission
PO Box A2449
Sydney South NSW 1235

By email: anne.pearson@aemc.gov.au

總辦事處地址

Level 22
530 Collins Street
Melbourne VIC 3000

Postal Address:
GPO Box 2008
Melbourne VIC 3001

T 1300 858724
F 03 9609 8080

Dear Anne,

Rule Change Request – Portfolio Rights Trading – update on costs and timing

This letter provides an update of costs and timings associated with the deployment of the Portfolio Rights Trading (PRT) rule change proposal under consideration by the Australian Energy Market Commission (AEMC).

Issues arising with deployment of changes to the STTM systems, in June 2014, led AEMO to undertake a critical review of its market IT system development and testing processes. In turn, this led to a reassessment of the development scope and effort required for implementation of PRT.

AEMO's reassessment has identified significant additional complexity, with greater development and testing requirements than provided for previously. Consequently, we are estimating significantly higher implementation costs, in the order of \$687,500 (compared to \$500,400 as stated in the original rule change request), and a deployment date of March-April 2016 (approximately 12 months later than that initially indicated).

The impact of the higher implementation costs of \$687,500 is that total traded quantities of more than 13 TJ per annum would be required each year, over 5 years, to provide a positive net present value (up from 9.5 TJ as stated in AEMO's rule change proposal).

Initial identification of these issues led AEMO to make a request to AEMC, in late August 2014, to defer its final determination on the PRT rule change request, which was then due on 11 September 2014, to allow further review of the cost/benefit analysis for the proposal. At that time AEMO indicated that the implementation date would likely be deferred from April to December 2015, based on an initial assessment of the additional development and testing effort that would be required.

However, in September 2014, AEMO suspended all IT development effort on the PRT project, to focus on the review of the cost/benefit analysis, including further consultation with industry on the likely take up and benefits of PRT. As a result of this and taking into account the following factors, AEMO has in recent days updated its estimated date for implementation as end-March to early-April 2016:

1. Allowance for 10-11 weeks of lost development time since early September due to the suspension of the implementation project to re-assess the business case. It is not planned to recommence this activity until a final determination on the rule change proposal.
2. Allowance for some delays in the re-start of the implementation project, including the time needed to allow an orderly exit of IT teams from other projects to which they were

reallocated in the meantime, re-setting of environments, and bringing newly allocated teams up to speed with detailed design for PRT.

3. As implementation will now straddle an additional Christmas/January period in 2015/6, allowance for some delay in the coordination and progress of testing activities during this period.

AEMO has consulted individually with DWGM market participants throughout September and October, advising them of the increased estimated implementation costs and delayed implementation dates (with discussions at that time based on an implementation date of December 2015), to explore updated participant views on the potential uptake and benefits of the PRT proposal.

Participant feedback to AEMO, a summary of which has been separately provided to the AEMC, remained generally supportive of PRT in concept. However, in light of the increased costs, delayed deployment, the likelihood that benefits would be less than originally thought, and the announced Victorian Government funding of an AEMC review of the Victorian Declared Wholesale Gas Market (DWGM) capacity and risk management mechanisms, some participants expressed reservations with proceeding with implementation of PRT at this time.

AEMO plans to release to participants, within the next week, a summary of the outcomes from the recent consultation on the cost/benefits of the PRT proposal, including our latest revised estimate of the deployment date.

AEMO supports the AEMC undertaking further consultation based on the updated information now available, prior to reaching a final determination on the proposed rule change. AEMO understands this means that a final determination is not now expected until late November 2014, which would remain consistent with the revised implementation date of March-April 2016.

If you have any questions on any of the above, please do not hesitate to contact me on (03) 9609 8520.

Yours sincerely



Terry Grimwade
**Group Manager – Wholesale
Markets**