



EnergyAustralia

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Dear Commissioners

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East Coast Wholesale Gas Market and Pipeline Frameworks Review

EnergyAustralia welcomes the opportunity to make a submission on the 'east coast gas market and pipeline frameworks review' (*the review*).

We support the COAG gas market vision to encourage competitive supply (stream 1), enhance transparency and price discovery (stream 2), improve risk management (stream 3), and remove unnecessary regulatory barriers (stream 4). We also welcome and support the Victorian Government's request to review the Victorian market to improve risk management, ensure efficient transmission investment, facilitate trade and promote competition.

The review needs to move beyond high level principles and provide concrete reform proposals to improve the efficiency and integration of the downstream gas markets. A competitive market requires a diversity of suppliers. Encouraging new and competitive supplies of gas is the single most important action that can be taken to progress the COAG gas market vision, however we acknowledge that supply issues are outside the scope of this review.

EnergyAustralia is one of the country's leading retailers, providing gas and electricity to more than 2.6 million customers. We own and operate a range of generation and storage facilities, including coal, gas and wind assets, in NSW, Victoria and South Australia.

Current arrangements are not appropriate to meet the future challenges

The East Coast gas market is undergoing fundamental change. The LNG industry in Queensland will soon require twice as much gas as all other domestic users combined. Domestic consumers will become price takers in a global market. The ownership of existing gas supply is highly concentrated and development of new resources is restricted by social, environmental and economic factors.

The scale of demand concentrated at the LNG facilities will draw gas from across the east coast and increase the physical, contractual and financial integration between the historically separate gas markets in each State. The full ramifications of these changes cannot be known in advance, however all reviews point to higher and more volatile prices, driven by increased production costs and linkage to global markets, and more complex swings in demand and production between regions and across the year.

The current market arrangements are not appropriate to meet the challenges of the future.

- There are three fundamentally different types of facilitated markets for trading gas: the Victorian Declared Wholesale Gas Market (DWGM), the three Short Term Trading Markets (STTMs) and the Wallumbilla Gas Supply Hub (GSH). Each is complex, and was designed independently of the others.
- Gas transportation is dominated by opaque and bespoke contract carriage arrangements. The market carriage model in Victoria is the exception, with its own complex arrangements that interface poorly with other pipelines.
- There is no transparent forward market and the ability for participants to effectively manage market risk is limited.

It is difficult to trade between markets and there are high transaction costs to trade transmission access between different participants or delivery points. The current arrangements generally developed independently in each jurisdiction to support local supply and demand, with limited interconnection between regions. The gas supply hub by contrast were specifically designed to support trading and the emerging LNG industry, however further reform and an additional hub at Moomba is required to realise the full potential benefits.

Reform should focus on delivering benefits to domestic end use customers

The move to an export-dominated gas market will impact end users of gas. This is unavoidable. This review should aim to ensure the downstream gas markets and transportation arrangements are as efficient as possible, and that users are able to engage with the market to purchase gas at a competitive price.

We support the use of the National Gas Objective (NGO) to underpin the assessment framework. The NGO seeks to promote economic efficiency in the long term interests of gas consumers.

The interests of domestic end-use gas consumers should be paramount in the interpretation of the NGO. LNG facilities are producers within the global gas supply chain.

A coordinated gas market development strategy is required

A strategic gas market development strategy is needed to guide the development of the facilitated markets and transportation system. Reforms should simplify and align the facilitated markets, and facilitate efficient investment and trade in pipeline capacity.

Market reform must deliver on four key priorities.

- 1) Improve the accuracy, timeliness, and transparency of market information about physical supply and demand;
- 2) Encourage trade in pipeline capacity, and harmonise market designs and interfaces, to encourage trade between locations;
- 3) Facilitate price discovery and transparency in spot markets; and
- 4) Support the development of liquid and transparent forward markets.

EnergyAustralia has endorsed the 'Industry Statement to support the Council of Australian Government's Energy Council Gas Market Development Vision'. This statement includes five

principles that address the need for a clear policy and forward development strategy to improve information transparency, access to efficiently priced transport capacity and more effective facilitated markets. This statement will be submitted separately.

Improvements to the Facilitated Markets (STTMs, DWGM, GSH)

The recent development of the GSH at Wallumbilla has improved price discovery and the ability to trade. Creation of a supply hub at Moomba is likely to deliver further benefits, including facilitating development of a forward market. We support the development of the gas supply hub at Moomba as a strategic location for a trading hub to support trade between Qld, NSW, SA and Victoria. Lessons from the development of the supply hubs should be considered in reviewing the design of the STTMs and DWGM.

There may be a role for AEMO, or other hub operator, to facilitate coordination to reduce the transaction costs that inhibit short term and intra-day flexibility. The review should focus on opportunities to align producer nomination times and market schedules, options to enhance intra-day flexibility, and the interaction between gas and electricity markets.

Each of the facilitated markets manages deviations and imbalances in a different manner, increasing the complexity and costs of participating in the market. This need not imply that a single approach is required, and we acknowledge that some differences reflect the inherent differences in the underlying physical networks. Market development needs to focus on improvements targeted to individual markets but guided by a coherent strategy.

Linking the domestic gas market with international markets will increase the need for effective gas hedging markets. It will also increase the complexity as producers seek to price gas with reference to oil in US dollars. Hedging the risks associated with gas contracts will therefore require the hedging currency and oil price risk.

There will be costs to develop the markets. These costs need to be considered against the long term benefits of improved market efficiency.

Transmission investment, access and trading

Efficient investment in, and access to, pipeline capacity is essential. Gas transmission is highly capital intensive and its development needs to be underwritten by consumers either via long term supply contracts in the 'contract carriage' model, or by economic regulation in the 'market carriage' model in the Victorian Declared Transmission System (DTS).

Both models have their advantages and disadvantages. It is likely that both approaches will continue to coexist in the Australian gas market and it is therefore important that the two systems interact effectively.

For contract carriage pipelines, the review should concentrate on identifying opportunities to improve short term trading and capacity utilisation through standardisation of contracts, simplified processes to change delivery points, and reducing the search and transaction costs for short term trades. The holders of existing capacity have strong commercial incentives and reform should focus on removing barriers to mutually beneficial trades occurring.

For the market carriage Victorian system, the review should focus on ensuring efficient and timely investment in new capacity, improving participants' ability to manage risk, and the interaction with contract carriage pipelines at the boundary.

Priorities for the phase one report

The development of a draft gas market development strategy to support an integrated, transparent and efficient market should be the first priority for the review. The strategy should set clear priorities and be informed by a detailed gap analysis between the objectives of the COAG gas market vision and the current market and transportation arrangements.

The gap analysis needs to be done at a detailed level and consider the physical and financial markets. A high level study is unlikely to be effective in identifying significant opportunities. A coherent forward strategy will be essential to ensure incremental reforms and rule changes are consistent with progress towards the COAG gas market vision.

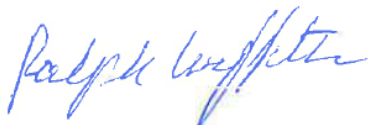
The terms of reference require the phase one report to identify immediate actions and rule changes for consideration by COAG. Australia's gas markets are complicated and have been subject to multiple previous reviews and ongoing incremental improvement. The review is unlikely to quickly identify major improvements ready for immediate consideration and should concentrate on defining the strategy and opportunities to progress material reforms over time.

AEMO's current development work is well targeted and timely. This work should continue and inform the Commission's recommendations. In particular

- Improving transparency and access to information through further development of the Gas Bulletin Board. The AEMC Phase one report should outline specific information that will be required by the market going forward.
- Facilitating trade through ongoing development of the gas supply hubs at Wallumbilla and Moomba. Lessons from these markets should be incorporated the Commission's analysis of opportunities for a strategic gas market development plan.

For any questions regarding this submission, please contact me on (03) 86281034.

Regards



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