

Review of the Victorian Declared Wholesale Gas Market Working Group

Meeting 3

Date: 10 August 2016
Time: 10.30am to 3.00pm
Location: Novotel Hotel, Melbourne

1 Agenda

- i. Welcome
- ii. Detailed discussion
 - Virtual hub vs. reality
 - Cost to cause vs. complexity
 - Balancing proposal
 - Timing of monitoring
 - Capacity follow up:
 - Short-term capacity release
 - Examples

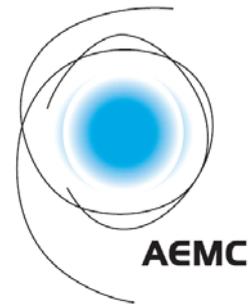
2 Attendee organisations

Organisation	Organisation
AEMC	ExxonMobil
AEMO	Gas Trading Australia
AER	Jemena
AGL Energy	Lochard Energy
APA Group	Major Energy Users
EnergyAustralia	Origin Energy
ENGIE	Public Interest Advocacy Centre
ERM Power	Vocus (ex-M2)

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3 Presentations and discussion

- The AEMC provided an introduction to the balancing topic, elaborating on the trade-offs between assigning cost to cause and complexity and highlighted that where possible, market design should tend to simplicity in order to encourage trading activity by allowing participants to fully understand their risk.
- The AEMC subsequently presented the key elements of the proposed **balancing mechanism** in more detail, focusing on the following issues:
 - **Continuous balancing:** market participants (MPs) will need to manage their own balancing by obtaining sufficient gas to achieve a reasonable balance with withdrawals over a gas day. A full suite of information will be provided to MPs on a regular basis in order to facilitate balancing decisions and action.
 - **Residual balancing:** the system operator would be required to take actions to maintain the balance of the system and to manage congestion. Key issues include when the system operator should take action and the extent to which costs should be targeted at those MPs causing the action.
- As a follow-up on the prior working group meeting, the AEMC also presented four examples on how capacity could be re-allocated on a day-ahead/intraday basis to allow MPs to manage their portfolios. The examples illustrated strategies that could be used by participants in response to different scenarios.
- Discussions throughout the meeting included broader questions such as the justification for the proposed reforms, as well as more specific issues relating to the detailed presentations. These discussions are summarised below:

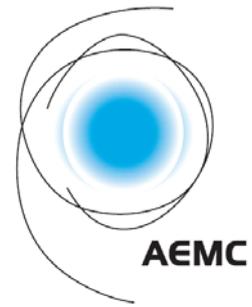
3.1 Support for proposed reforms

- One participant indicated that it did not support the proposed market reform, while another suggested that it does not address the matters outlined by the Victorian Government. A number of attendees questioned whether the case for change had been made.
- The AEMC reiterated the drivers for reform, highlighting how these relate to the COAG Energy Council's Vision, and highlighted that reform options were discussed and consulted on last year. Consequently, the focus of the AEMC's work is now to further develop the chosen option. A number of attendees suggested that, in hindsight, they had been insufficiently engaged during the consultation on options, but noted the significant number of initiatives underway at that time.
- One participant suggested that it had been coordinating other industry stakeholders in identifying alternative design options for the DWGM, including potential incremental

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improvements. This participant committed to bring any agreed alternative design options to the attention of the AEMC in due course.

- The AEMC noted that it is pleased to see that discussion is taking place, however it highlighted that any proposals would need to be new, concrete and address the key reform priorities.
- Over the course of the meeting, as in the first two meetings, a few stakeholders suggested that nodal pricing may be a more appropriate solution than the virtual hub model being explored by the AEMC.
- One participant mentioned that the National Electricity Market has five regional prices (five nodes) because of system constraints and that the DWGM faces similar constraint issues.

3.2 Continuous balancing

- A number of attendees raised concerns around (the possible lack of) visibility of MPs' positions and one questioned if market participants would be best placed to manage their positions. The AEMC reiterated its view that, with the appropriate market signals and information, MPs can and will respond.
- A number of attendees noted that they potentially saw benefits in balancing actions being taken on an hourly basis, and suggested that such a mechanism could be one of the incremental changes to the current DWGM model.
- Another attendee questioned whether MPs would need to be in balance across multiple geographic zones. The AEMC responded that, while the system operator will need to have tools to manage congestion, most likely MPs will only need to be in balance in the overall system. This issue interacts with the allocation of capacity and requires further consideration during the detailed design phase.

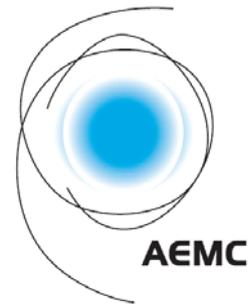
3.3 Short-term capacity allocation and examples

- At the previous working group meeting, a number of questions were raised around how capacity could be re-allocated on a day-ahead/intraday basis to assist participants in managing their portfolios.
- After that working group meeting, the AEMC had a number of conversations with stakeholders to understand in greater detail different scenarios to test the proposed market model against.
- The AEMC presented four examples with illustrated strategies that could be used by participants in response to different scenarios in terms of altering injections and withdrawals. Some of the examples also addressed the coordination between commodity and capacity markets. To explain the examples, the AEMC went through a potential 'hierarchy' of capacity sales, including a release mechanism for sold but not nominated capacity.

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- Questions were asked about the operation of the capacity release mechanism for sold but not nominated capacity, for instance what would happen to capacity procured through the mechanism but then, itself, not nominated. There was also some discussion of the appropriate pricing of overruns during times of plentiful capacity and at times of capacity scarcity. One attendee suggested that pricing of overruns would need to be mindful of the risk of undermining demand for capacity rights.
- Some attendees commented that they continue to view the separation of capacity and commodity as adding a new layer of complexity for participants. The AEMC noted that separation of capacity and commodity trading is normal in most gas markets and made suggestions as to how the process could be automated, not requiring separate actions from MPs.

3.4 Next steps

- A fourth working group meeting is likely to be scheduled for 31 August 2016 to discuss options around transition to the potential new market design.
- The AEMC will subsequently publish a Draft Final Report on 14 October 2016 for consultation.
- The consultation period and process for finalising the report and recommendations have not been specified by the Victorian government, and the AEMC intends to give an update on these matters at the next meeting.