

15 November 2010

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

FROM THE OFFICE OF THE
CHIEF EXECUTIVE OFFICER

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By online submission

John,
Dear Mr Pierce

Rule Change Request – STTM Participant Compensation Fund contribution

We request the Australian Energy Market Commission (AEMC) make an amendment to the National Gas Rules (NGR) with regard to the calculation of contributions the participant compensation fund (PCF) in the Short Term Trading Market (STTM).

The rule change proposal seeks to amend rule 452 to clarify that a trading participant's contributions to the PCF are not affected or adjusted by market operator services (MOS) or overrun MOS. This will ensure that the PCF contributions are correctly based upon trading participants' withdrawals from the market rather than being adjusted for the provision of balancing services.

Noting the above, feedback from the Australian Energy Market Operator's (AEMO) consultation on this issue, and the immaterial effect the proposed rule change will have on the market, we ask that the AEMC treat the rule change as non-controversial under section 304 of the National Gas Law.

A description and drafting of the proposed rule, a statement of the issues concerning the existing NGR requirement, and how the proposed rule contributes to the achievement of the National Gas Objective is provided at Attachment A.

AEMO would be pleased if you could have these matters considered by the AEMC. For further details, please do not hesitate to contact Terry Grimwade, Executive General Manager - Market Performance, on (03) 9609 8520.

Yours sincerely



Matt Zema
Managing Director and Chief Executive Officer

Attachment A: Rule change proposal

Attachment A: Rule Change Proposal

1. Background

1.1 Current rule requirements

Under the National Gas Rules (NGR 452), the Australian Energy Market Operator (AEMO) is required to establish and collect funds for the participant compensation fund (PCF). The PCF is collected from trading participants to provide a fund from which compensation can be paid in the event of a market scheduling error.

The NGR requires that the participant payment towards the fund is based on withdrawals from a hub. In the STTM, this covers both STTM shippers who are taking gas from an STTM hub and STTM users who are withdrawing gas at an STTM hub.

In accordance with rule 452(6), AEMO is to use STTM facility allocations and STTM distribution system allocations to determine an STTM shipper's and STTM user's PCF contribution respectively.

The NGR defines STTM facility allocations to include market operator services (MOS) and overrun MOS allocations. Rules 419(2)(a)(ii) and 419(2)(a)(iii), state that the quantity of MOS gas allocated to a registered facility service (RFS) is included in the STTM facility allocation, and that the quantity of overrun MOS is to be included in the quantity of MOS gas.

Specifically, the NGR defines STTM facility allocations for a RFS as:

“the total quantity of natural gas that is taken to be supplied to or withdrawn from the relevant hub on a gas day using that registered facility service, as validly given to, or determined by, AEMO under rule 419”.

NGR 419(2) states:

“(2) An allocation notice must contain, for the relevant gas day:

(a) for each registered facility service provided by means of that STTM facility:

(i) the STTM facility allocation for that registered facility service, which must not be less than zero; and

Note: An STTM facility allocation must be provided for each registered facility service in respect of the relevant STTM facility, even if that allocation is zero.

(ii) the quantity of MOS gas allocated to that registered facility service in accordance with rule 421 (such quantity being included in the STTM facility allocation); and

(iii) the quantity of overrun MOS allocated to that registered facility service in accordance with rule 421 (such quantity being included in the quantity of MOS gas); and

Note: The quantity of MOS gas or overrun MOS may be zero.”

Therefore, under rule 452(6), MOS and overrun MOS is included in STTM facility allocations for the purpose of determining the PCF amount. For STTM users, the distribution system allocations do not include MOS and overrun MOS, as STTM users cannot be MOS providers.

Therefore, as the rules are currently drafted, STTM shippers who withdraw gas from an STTM hub are to be charged PCF based on their total allocations, which includes their withdrawals from the STTM hub, MOS and overrun MOS allocations, whereas STTM users are to be charged the PCF contribution based only on their withdrawals. In addition, the rules require that an STTM shipper who is allocated decrease MOS or decrease overrun MOS is to be charged PCF based on the allocation quantity.

AEMO’s market systems calculate the contribution STTM participants must make to the PCF. The market systems are designed and built to calculate the PCF contribution based on gas withdrawn from the STTM, excluding MOS and overrun MOS.

The STTM settlement systems have been built consistent with the design intent. The issue was discussed and confirmed by the STTM Consultative Forum (STTM-CF) at its meeting of 24 August 2010, noting that the parties who participate in the STTM-CF include those who were part of the industry-led approach for the design and establishment of the STTM.

On 17 September 2010, AEMO notified the Australian Energy Regulator (AER) of this discrepancy. In response, on 6 October 2010, the AER issued a letter of “no action” for non-compliance with rule 452(6), subject to AEMO submitting a NGR change proposal to the Australian Energy Market Commission (AEMC). Copies of these letters can be provided upon request.

1.2 Allocations, MOS and Overrun MOS

1.2.1 Facility and distribution allocations

The STTM is an ex ante market where the market is run the day before the relevant gas day setting an ex ante market price and schedule for each STTM hub for each gas day. The market schedule is determined using supply offers, demand bids, and the capacity of the pipeline.

On the gas day, the pipeline operator delivers gas to the hub, and users withdraw gas at the hub. However, the quantities delivered to or withdrawn from the hub may not, and generally will not, match with the ex ante market schedules. And during the day, as gas requirements become better known, and if permitted by their contract, shippers may renominate, through intraday nominations, with their pipeline operators.

Each gas day is settled based on allocation information provided after the gas day about activities on the gas day. Allocations define the actual quantities flowed to and from the hub on the gas day.

Allocations to individual STTM shippers are provided by the pipeline operators (facility operators), or a nominated allocation agent. For STTM shippers, pipeline operators measure the flow on the facility daily at various meter stations and custody transfer points. There are three types of allocation data used in the STTM for STTM shippers: STTM facility allocations, MOS step allocations and RFS allocations.¹

Allocations for STTM users, STTM distribution system allocations, are made by AEMO as the retail market operator using metered data provided by distributors and aligned with the pipeline allocations.

¹ STTM facility allocation—these allocations are made by facility operators for each registered facility service (RFS) on each facility. The STTM facility allocations represent the total quantity flowed on an RFS on a gas day and includes quantities of MOS and overrun MOS allocated against the RFS. The STTM facility allocations will include the flows on the RFS for the contract holder and include the total flows on all the trading rights attached to the RFS.

MOS step allocations—these allocations are also made by pipeline operators and allocate MOS to MOS providers using the MOS stacks prepared by AEMO.

RFS allocations—these allocations are made by STTM shippers, or their nominated allocation agent, which shows the quantities flowed for other shippers on a RFS through trading rights.

1.2.2 Market operator services

Deviations by shippers and users are physically balanced by pipeline operators maintaining pressures at the distribution gates within agreed operating ranges. The STTM settles this balancing gas under MOS arrangements.

MOS is an on-the-day service that balances the difference between scheduled pipeline flows and what is actually delivered at the hub. AEMO procures the MOS gas from MOS providers who have capability to absorb these daily fluctuations, by either increasing or decreasing flows on a gas day.

Where a pipeline deviation occurs on a gas day, this is allocated by the pipeline operator to MOS providers using the MOS stacks prepared by AEMO. If the capacity of the MOS stack is exhausted, the overflow is allocated as overrun MOS to shippers on a basis agreed between the pipeline operator and shippers on the pipeline.

As MOS is a balancing service provided by a MOS provider to the market, the MOS provider is paid a service component according to their MOS offer price, and any resulting deviations incurred by the MOS provider for MOS gas is exempt from deviation payments and charges. AEMO pays or charges MOS providers, MOS commodity cost, for restoring MOS gas. Shippers who are allocated overrun MOS will also be settled for the service provided to the market, and overrun MOS is also exempt from deviation payments and charges.

2. Statement of Issues

2.1 Treatment of MOS in PCF calculation

As noted above, an inconsistency has been identified between AEMO's settlement systems and the NGR relating to the treatment of MOS and overrun MOS in determining the PCF contribution for STTM shippers.

The intended allocation of contributions to the PCF was to be based on withdrawals from the hub exclusive of MOS and overrun MOS. However, the current rule requirement means that:

- A STTM shipper who takes gas away from the STTM and is allocated MOS increase or overrun MOS increase against a RFS will pay less in PCF contributions than intended.
- A STTM shipper who takes gas away from the STTM and is allocated MOS decrease or overrun MOS decrease against a RFS will pay more in PCF contributions than intended.

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- A MOS provider who is allocated MOS decrease or overrun MOS decrease will be charged a PCF contribution which was not intended to be the case.

For example, if an STTM shipper who is also a MOS provider withdraws 10 TJs of gas from the STTM and is allocated a further 5 TJs of decrease MOS, then under the current rules they will have a facility allocation of 15 TJ, and their PCF would be based on a quantity of 15 TJs. The market design intent was for PCF contributions, in this case, to be based solely on the 10TJ withdrawal quantity.

Similarly an STTM shipper who withdraws 10 TJs of gas and is allocated 5 TJs of increase MOS will have a facility allocation of 5TJs. Again, the design intent was for the PCF contribution for this shipper to be based on the 10TJ withdrawal quantity.

In both instances, the inclusion of MOS modifies the quantity of gas that would be used as a basis for the calculation for PCF contributions.

Furthermore, a STTM shipper who makes no withdrawals from the hub at all but, as a MOS provider, is allocated 5 TJs of decrease MOS, will have a facility allocation of 5 TJs and, under the current rules would effectively be charged a PCF contribution for providing a service to the market.

Contrary to the current rule 452(6), AEMO's market systems calculate the PCF contributions based on the gas withdrawn from the hub, unmodified by MOS, consistent with the market design intent.

2.2 Consistent provisions for the STTM

AEMO considers that it would be prudent to amend rule 452(6) to ensure that the charging of the PCF contribution is consistently applied to STTM shipper and STTM user participants within the STTM.

Under the existing rule, STTM shippers who take gas from the hub and are allocated MOS are required to be charged either a higher or lower PCF amount, depending on whether the MOS allocation increases or decreases their total facility allocations. The current rules treat parties who withdraw gas from the STTM hub differently, as STTM shippers' quantities may be modified by MOS quantities, whereas STTM users' quantities are not modified by MOS allocations.

The current rule also means that a MOS provider providing MOS decrease offers are exposed to an additional charge (i.e. PCF contribution) which MOS providers providing MOS increase offers are not exposed to. This creates asymmetry in the treatment, and provision, of MOS increase and decrease offers to support the market balancing arrangement.

The current rule is also inconsistent with the way in which deviations and imbalance payments/charges are settled. MOS and overrun MOS are currently excluded from the determination of a participants' deviation volumes because MOS providers are providing and being paid for a balancing service to the market and should not face additional charges as a result.

The current rule requirements also means that STTM shippers' contribution to the PCF is inconsistent with the way participant fees are determined for these parties. In determining STTM shippers' participant fee contribution, AEMO uses gas withdrawn amounts, unmodified for MOS or overrun MOS for the reasons outlined above, and MOS decrease providers are not required to pay participant fees for the decrease allocation amount because they are providing a balancing service to the market.

2.3 Materiality of MOS in PCF calculation

2.3.1 STTM shipper and MOS provider

Since the market commenced on 1 September 2010, there has been and continues to be one company who is registered as an STTM shipper and withdraws gas from the STTM on a backhaul contract. That company is currently not a MOS provider.

Therefore, at this point there are no circumstances in the STTM where a STTM shipper withdrawing gas from the STTM is also registered to be a MOS provider. Therefore, despite the potential for it to occur under the current rules, there have been no practical instances where allocation quantities have been modified by MOS or overrun MOS for the purposes of determining the PCF contributions.

2.3.2 MOS decrease providers

Consistent with the design intent, AEMO's settlement systems do not calculate any PCF contributions for participants in relation to MOS services provided at the hub. AEMO has however, calculated the PCF contribution for each MOS decrease provider, using MOS allocations for September 2010 and October 2010, if this were to be done in accordance with the current rules²:

Table 1 shows that had the STTM settlement systems calculated the PCF amount consistent with the current NGR requirements, MOS providers who were allocated decrease MOS would have been charged \$951 and \$258 at the Sydney and Adelaide hub respectively over the September and October period.

² Analysis of the effect on individual MOS decrease providers has been supplied confidentially to the AEMC.

Table 1: Comparison of PCF charge for MOS provider – rule requirement against STTM system calculation

Month	Decrease MOS provider – PCF contribution as per rule	Decrease MOS provider – PCF contribution as per rule	Decrease MOS provider – PCF as per systems
	Adelaide hub	Sydney hub	
September 2010	\$90.59	\$395.28	0
October 2010	\$166.89	\$555.75	0
Total	\$257.48	\$951.03	0

2.3.3 Cost to amend STTM settlement systems

In order to comply with the current rule requirements, AEMO would need to incur costs of approximately \$48,000 to change the STTM settlement system. Instead, AEMO proposes that the NGR should be amended so that the market does not incur costs associated with system changes to produce outcomes that are contrary to the policy intent and have no material impact on market outcomes.

3. Proposed Rule

3.1 Description of the proposed rule

The proposed rule would amend clause 452(6) to make clear that MOS and MOS overrun is excluded from the calculation of the PCF.

AEMO's proposed change to this rule is contained in Appendix A.

3.2 Request for a non-controversial rule

AEMO requests that the AEMC reviews this rule change proposal under section 304 of the National Gas Law (NGL). Section 304 applies if the AEMC considers that a request for a rule is a request for a non-controversial rule. A non-controversial rule means a rule that is unlikely to have a significant effect on a market for gas or the regulation of pipeline services.

AEMO considers that section 304 applies for the following reasons:

- Making the rule aligns with the policy intent of ensuring that MOS providers are not penalised for participating in the provision of MOS – for example, under the current

design, STTM shippers who are allocated MOS or overrun MOS will not incur deviation charges or payments for the MOS allocation quantity. Making the rule will also ensure consistent treatment of STTM shippers withdrawing gas from the STTM with the treatment of STTM users.

- The analysis presented in section 2.3 shows that the proposed rule amendment would not have a material impact on market participants, as the rule seeks to align the rule requirement with the policy intent as implemented in the AEMO settlement system. Because currently there is one STTM shipper withdrawing gas from the STTM and that STTM shipper is not a MOS provider, the participant's PCF contribution is currently not being adjusted for MOS or overrun MOS. Given the market commenced on 1 September 2010, it is too early to determine whether there will be more participants who register as an STTM shipper and become both a shipper who withdraws from the STTM and also a MOS provider.
- The analysis presented in section 2.3.2 also shows that the impact on market participants' monthly settlement amounts had MOS decrease providers been charged a PCF contribution by the AEMO settlement system is not material, especially when compared to the cost of changing the STTM settlement systems to align with the current rule requirement. Going forward, it is difficult to estimate which market participants would be affected by this given it will depend on whether decrease MOS is allocated on a pipeline facility and which parties seek to be MOS providers as part of the MOS tendering process from December 2010 onwards.
- As noted at section 3.3 of this rule submission, AEMO consulted and discussed the rule change proposal at the STTM-CF meeting of 24 August 2010, meeting attendees unanimously supported AEMO submitting the rule change proposal as non-controversial.

3.3 Stakeholder consultation

AEMO has consulted the STTM-CF, discussing and seeking views on this matter at the STTM-CF meeting on 24 August 2010.

The STTM-CF unanimously supported AEMO's position on this matter and agreed that the PCF contributions should be made on the basis of withdrawals and should not be modified for MOS and overrun MOS.

The minutes of the STTM-CF for 24 August 2010 are available on the AEMO website and are provided at Appendix 2 for completeness.

4. How the Proposed Rule Contributes to the National Gas Objective

Before the AEMC can make a rule change it must apply the rule making test set out in the NGL, which requires it to assess whether the proposed rule will or is likely to contribute to the National Gas Objective (NGO). Section 23 of the NGL states the NGO 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.”

AEMO considers that the proposed amendments regarding the calculation of the PCF contribution for the STTM are likely to contribute to the NGO as the proposed rule change will ensure consistency and predictability in the calculation of the PCF contribution as it is applied to the different categories of STTM participants (STTM shippers and STTM users, and MOS providers) as well as ensuring consistency between the inputs and methodology for determining the PCF contribution with STTM participant fees.

AEMO also considers that not making this rule may lead to inefficient pricing of gas purchased by STTM shippers who may include PCF fees in bid amounts. This may potentially distort the price bid by STTM shippers and therefore lead to a distortion in the market costing. This would lead to inefficiencies in the operation of the STTM market and would not be in the interests of consumers of natural gas.

5. Expected Benefits and Costs of the Proposed Rule

AEMO considers that the persons likely to be affected by the proposed rule included registered participants, including intending participants.

AEMO expects that the proposed rule would benefit participants, and hence consumers, by providing consistency in the methodology used by AEMO in the calculation of the PCF for STTM shippers and STTM users, and does not impose additional costs for MOS decrease providers, which are not incurred by MOS increase providers. This rule change proposal seeks to align the rule with the AEMO systems. As this is the basis on which the AEMO market systems already calculate the PCF contribution, there is no cost in making this rule. AEMO does not expect that the rule change would impose costs on the market or market participants.

AEMO considers not making the rule could lead to inefficiencies in terms of the pricing and operation of natural gas services. For example, the inconsistency in the calculation of PCF contributions may lead to some distortionary impacts on MOS decrease and increase offers. Without certainty of the basis for the calculation of the PCF contribution, AEMO may have to change its market systems to align them with the rule as it currently stands.

The inefficiencies in investment come from the AEMO costs to modify the market systems (preliminary estimates place this cost at \$48 000) and would therefore be an additional cost to participants, and hence consumers, of natural gas services. There are also inefficiencies in operation which arise from AEMO diverting resources to modify the market systems and undertake additional settlement revisions.

GLOSSARY

Term or Abbreviation	Explanation
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
MOS	Market Operator Services
NGL	National Gas Law
NGO	The National Gas Objective as stated in section 23 of the NGL
NGR	National Gas Rules
PCF	Participant Compensation Fund
RFS	Register Facility Service
STTM	Short Term Trading Market
STTM-CF	STTM Consultative Forum

Appendix 1: Draft Rule

This proposed rule change is based on version 5 of the National Gas Rules.

Part 20, Division 9:

Rule 452

(6) Each Trading Participant for a hub must pay to AEMO, as part of the settlement amount payable by that Trading Participant in respect of each billing period, an amount calculated by multiplying the contribution rate by the aggregate quantity of natural gas withdrawn from that hub by that Trading Participant during the relevant billing period, in accordance with its STTM facility allocation, excluding MOS and Overrun MOS, or STTM distribution system allocation.

Appendix 2: Extract STTM CF minutes of 24 August 2010 meeting

MINUTES – STTM CONSULTATIVE FORUM

MEETING No: 3
DATE: Tuesday 24 August 2010
TIME: 2:00 pm – 4:00 pm
LOCATION: Melbourne L 22, 530 Collins St **LOCATION:** Melbourne L 22, 530 Collins St
INVITEES: STTM CF Distribution List

1 ATTENDEES

Organisation	Representative	Organisation	Representative
Chair (AEMO)	Terry Grimwade	Delta Electricity	Simon Lipert
Secretary (AEMO)	Mark Riley	Envestra	Rick Abbott
AEMO	Peter Ferretto	Epic	John Perfrement
AEMO	Paddy Costigan	Esso	Brendan Champness
AEMO	Sarah McKelvie	Energy Australia	Sarah Kok
AEMO	Roger Shaw	International Power	Haseeb Sherer
AEMO	Craig Price	Jemena – EGP	Gabrielle Sycamore
AEMO	Noel Murray	Jemena - EGP	Sumit Garg
AEMO	Chin Chan	Jemena Networks	Alvin Lau
AGL	George Foley	Jemena Networks	Scott Martin
APA	Brad Evans	Origin Energy	Dave Grove
APG	Shelley Reed	SEAGas	Jeff Cooke
BP	Tam Pham	SGM Solutions	Brendan Dillon
Delta Electricity	Dat Vuong	TRUenergy	Don Vigilante
AEMO	Canh Diep		

4.3 Rule Change - PCF

STTM 10-15-01: Amendment to Rule 452 - PCF Calculation

M. Riley (AEMO) spoke to this proposal for a Rule change to remove ambiguity in the current drafting of the provisions with regard to the allocation of Participant Compensation Fund (PCF) contributions. AEMO indicated that its understanding of how PCF would be collected was to be based on withdrawals in the market and that it had built its market systems on this basis.

However, the wording in rule 452(6) refers to the STTM Facility Allocation. For STTM Shippers withdrawing gas from a hub, this could be read to mean that the quantity used to calculate the PCF contribution is a Participant's withdrawal modified by MOS allocations.

AEMO stated that it considered such an interpretation would be inconsistent with the discussions held with industry during the development of the STTM Market and the approach for collecting fees, which was to be consistent with the Victorian gas market.

AEMO sought confirmation from the meeting attendees of its interpretation of the intent of the rule provisions for the calculation of PCF contributions, namely that the allocation should be based on withdrawals, exclusive of MOS quantities.

AEMO indicated that if this was not the case, then it would have to re-code part of the settlement systems, which would cost in the order of \$30, 000.

Meeting attendees sought clarification on minor matters but agreed with AEMO's interpretation.

Meeting attendees noted the proposal and unanimously supported the approach to clarify the NGR that PCF should be collected on the basis of withdrawals, exclusive of MOS.

The meeting also indicated unanimous support for a request that the rule change be considered by the AEMC as a non-controversial change on the basis of it being a point of clarification and having no impact on market operation.

AEMO advised the meeting attendees that it may advise the AER of the meeting outcomes on this matter and how AEMO would comply with the current Rules.