

Explanatory Material on the Draft Short Term Trading Market Rules

Introduction

To facilitate the establishment of a Short Term Trading Market (STTM) for natural gas, the Gas Market Leaders Group (GMLG) and the Ministerial Council on Energy's Standing Committee of Officials (SCO) have prepared an exposure draft of the proposed amendments to the National Gas Rules (NGR). These amendments, which are supported by the amendments to the National Gas Law (NGL) released on 27 May 2009, contain the majority of the detail of the regulation of the operation and administration of the STTM. Further technical and administrative detail will be included in the STTM Procedures. The Australian Energy Market Operator (AEMO) will make the initial STTM Procedures in accordance with the STTM amendments to the NGL, and will prepare those Procedures in consultation with industry.

The content of the NGR amendments are based on the GMLG's STTM Detailed Market Design which was approved by the Ministerial Council on Energy (MCE) at its 10 July meeting.

Background

The MCE agreed in April 2004 to expand the gas market element of the energy market reform program to accelerate the development of a reliable, competitive and secure gas market and to further increase the penetration of natural gas. In December 2004, MCE approved a set of Principles for Gas Market Development as a basis for developing the Australian gas wholesale market and later established the GMLG to develop a Gas Market Development Plan.

The GMLG's Gas Market Development Plan, finalised in June 2006, presented MCE with seven recommendations, including three initiatives focussed on improving information disclosure and market transparency:

- the National Gas Market Bulletin Board;
- an annual national gas supply/demand statement (Gas Statement of Opportunities); and
- the development of the detailed design of a STTM.

Related to these measures was a separate initiative to create a single National Gas Market Operator that would administer the Bulletin Board and STTM and produce the annual national gas statement.

The Market Operator proposal subsequently evolved into the AEMO, which assumed responsibility for both the gas and electricity markets from 1 July 2009.

In April 2008, the MCE accepted the GMLG's recommendation to proceed with the detailed design and implementation of a STTM and asked the GMLG to oversee the STTM project until AEMO is established. AEMO has chosen to retain GMLG as an advisory group for the STTM Establishment Project.

Objectives

The STTM will help facilitate the development of economically efficient gas markets through:

- Providing transparent price signals for gas delivered and withdrawn from defined market hubs;
- Enabling the participation of all major gas users, including direct transmission customers (wherever practicable);
- Efficiently pricing congestion on the system (including facilitating a market based solution to emergencies if possible); and
- Facilitating secondary trading (including demand side response) from short term market prices.

Market Design

The GMLG completed its detailed market design in April 2009 with key features being that the STTM will:

- be a city gate or 'hub'-based market operating initially in Sydney and Adelaide (separate markets but governed by the same rules);
- be administered by the AEMO;
- operate in parallel with existing gas transportation contracts/access arrangements, gas supply agreements and retail market rules (other than balancing arrangements);
- establish a single daily market clearing hub price before each gas day (i.e. an ex ante market price), by matching supply and demand through 'offers' and 'bids' to deliver gas to, and take gas from, each hub;
- rely on allocations performed by pipeline operators (or allocation agents), and by AEMO in its retail market operator role, to determine the quantity of gas delivered to, or taken from, the hub by each shipper and network user; and
- replace existing balancing services under the relevant gas retail markets by empowering AEMO to procure a Market Operator Service (MOS) to balance physical deviations on a pipeline, being the difference between the actual gas flows on a day (as allocated by pipeline operators and distributors) and the pipeline operator's schedule of gas flows for that day.

Legal Framework

Jurisdictions and the GMLG have prepared exposure drafts of amendments to the NGL and NGR to implement the STTM. The NGL amendments are intended to be introduced into the South Australian Parliament later this year. The legal package also includes amendments to the NGR which will be made by the South Australian Minister following passage of the legislation, and a set of STTM Procedures which will be made by AEMO. It is anticipated that an exposure draft of the Procedures will be available later this year.

Under the conceptual framework for the STTM legislation the NGL will deal with a limited number of high level features of the regime, the NGR will contain the detail of

the market operation and the STTM Procedures will include the more detailed process requirements involved in NGR obligations and address lower level technical and administrative matters. The table below illustrates this approach.

Instrument	Responsibility	Subject Matter
National Gas Law	Enacted by SA Parliament, as the lead legislator. Application Acts govern the extent to which the national gas legislation applies in the relevant jurisdiction.	The STTM will be authorised under the NGL, which will make high level provisions for: <ul style="list-style-type: none"> • STTM establishment; • the functions of AEMO in relation to the STTM; and • liabilities of AEMO and other participants (where appropriate) in relation to the STTM.
National Gas Rules	Made initially by the South Australian Minister, subject to MCE endorsement. Future amendments to be made by the Australian Energy Market Commission, in accordance with the rule change procedures outlined in the NGL.	The rules for the STTM will be incorporated in the NGR and will deal with issues such as registration, market operations, balancing arrangements via MOS, contingency gas and settlements.
STTM Procedures	Made by AEMO, in accordance with the NGL/NGR.	STTM Procedures will cover more detailed technical and administrative matters. The initial STTM Procedures will be developed and made by AEMO under the NGL. AEMO will then be able to amend STTM Procedures in accordance with the consultation process in the NGR.

The NGR Amendments

The exposure draft of the NGR contains the majority of the detail about the operation and administration of the STTM. The draft has been developed by the GMLG and SCO.

The STTM rules provisions will predominantly be located in a new Part 20 of the NGR. However, use is made of existing rules wherever possible, for example in relation to registration, dispute resolution and participant fees. Existing Part 15B, which deals with the Retail Gas Market Procedures, Wholesale Gas Market Procedures and the Bulletin Board Procedures, will also contain the heads of power for the STTM Procedures. An indicative list of heads of power for the STTM Procedures has been included in the exposure draft.

The following summary highlights some of the key aspects of the rules.

Hubs and STTM Distribution Systems

Division 2 of Part 20 describes where the STTM is to operate by reference to the Adelaide and Sydney hubs. A hub is defined in relation to the relevant STTM distribution system and the custody transfer points connected to that distribution system. The rules provide support for the STTM Procedures to list the specific custody transfer points.

Registered Participants

Rules relating to the registration of STTM participants will be included in the general part of the NGR dealing with registration, Part 15A. A new rule, 135ABA, outlines the registrable capacities in the STTM as being an STTM Shipper and an STTM User (together STTM Trading Participants). In order to be registered in the STTM, participants must have existing transmission or distribution haulage contracts or subcontracts. (Information relating to those contracts must be provided to AEMO in accordance with Division 5.) Division 3 of Part 20 contains additional STTM-specific requirements relating to participant registration.

STTM facility operators (transmission pipeline operators, storage facility operators and specified production facility operators) and STTM distributors will not be required to register under the general registration provisions, but will have obligations under the STTM rules, including the requirement to provide information to AEMO in accordance with Division 4 (with such information to be registered by AEMO).

MOS (Market Operator Service)

Division 6 contains rules concerning MOS (the market operator service). MOS is a service offered to AEMO by STTM shippers to increase or decrease the quantity of gas they flow on a day in order to balance pipeline deviations on an STTM pipeline during a 'MOS period'. The rules allow STTM Shippers to make MOS increase offers and MOS decrease offers, and require AEMO to produce MOS stacks for each STTM pipeline.

If there is an ongoing shortage of MOS (in other words AEMO is not receiving enough MOS offers to cover anticipated pipeline deviations), the rules allow AEMO to procure or facilitate the provision of MOS (after compliance with certain processes in the rules).

Market Operations

Division 7 deals with the day to day operation of the STTM. It specifies how AEMO is to operate the market and how buyers and sellers of gas will participate in the STTM. Notably the Division prescribes the requirements in relation to the timing of bids and offers, and the scheduling of those bids and offers by AEMO. Further technical detail about the operation of the STTM will be contained in the STTM Procedures.

Market Parameters

The rules will specify values for the following market parameters:

- Market Price Cap (formerly VoLL);
- Cumulative Price Threshold;
- Administered Price Cap;
- Minimum Market Price; and
- MOS Cost Cap.

Proposed values for these parameters, other than the MOS Cost Cap have been endorsed by the GMLG (see the Synopsis of 21st GMLG meeting, available on the MCE website – www.mce.gov.au). As the final values have not been approved by MCE, they are not included in the exposure draft.

Title to Gas and Gas Quality

Subdivision 3 of Division 7 covers the issues of ownership, risk and responsibility for gas. The rules authorise AEMO to transfer title to gas at each hub from STTM Shippers to STTM Users. This rule is necessary as buying gas from the market breaks the chain of back to back contracts currently in place. The rules also place an obligation on an STTM Shipper to ensure that the gas delivered to the hub complies with the relevant jurisdictional gas quality specification (outlined in the definitions).

Contingency Gas

Division 8 sets out the processes surrounding the requirement for, and supply of, contingency gas. Contingency gas may be necessary to meet an operational requirement associated with actual or forecast adverse operating conditions at a hub. A requirement for contingency gas will be determined on a short term basis - for the current or next gas day - where it is considered unlikely that the operational requirement will be met through normal STTM operation. The rules deem certain events to be 'contingency gas trigger events' (for example, pressure conditions being above or below acceptable operating conditions). The occurrence of such an event will require AEMO to commence a consultation process to determine whether to call for the provision of contingency gas at that hub (but will not necessarily lead to AEMO scheduling contingency gas).

The rules then provide for offers from STTM Shippers and STTM Users to increase or decrease the amount of natural gas injected into, or withdrawn from, the hub. The STTM Procedures will provide for the detailed scheduling process for contingency gas.

Scheduling Errors and the Participant Compensation Fund

Under Division 9, AEMO must establish a participant compensation fund for the STTM for the purpose of paying compensation to Trading Participants for losses incurred due to scheduling errors. The draft rules provide for a separate fund for each hub. The rules will prescribe the funding requirements, the process for determining whether a scheduling error has occurred, when an entitlement to compensation arises, and the amount of compensation payable.

Market Settlement and Prudential Requirements

Division 10 provides for the requirement for AEMO to manage the billing and settlement of transactions between Trading Participants. AEMO must determine various amounts for each gas day as set out in the rules, with detailed calculations of those amounts to be set out in the Procedures. The rules place an obligation on Trading Participants to pay to AEMO the settlement amount as shown in their final statement. They also provide for adjustments to be made via revised statements at a time when market data (including metering information) has been finalised. AEMO will require Trading Participants to provide security at a level relative to their estimated exposure to the market.

Market Review and Audits

AEMO must conduct various reviews of the STTM as prescribed by Division 11. For example, in relation to the effective operation of MOS; whether the STTM could include additional hubs; and whether the market parameters (contained in the rules) are set at appropriate levels. It should be noted that these provisions do not preclude the rules being changed independently of an AEMO review through the normal rule change process.

Division 12 provides that there must be an annual audit of the STTM by an independent auditor, and that trading activity in the STTM must be monitored by the Australian Energy Regulator.

Transitional provisions

The final NGR amendments will also contain transitional rules which will ensure a smooth transition from current arrangements to commencement of the STTM.