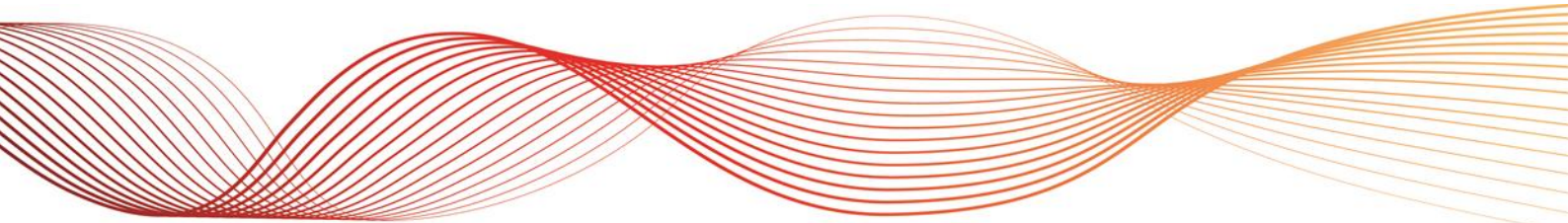




GAS MARKET PARAMETER REVIEW 2018

DRAFT REPORT

Published: **March 2018**





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NOTICE OF CONSULTATION ON DRAFT REPORT

GAS MARKET PARAMETER REVIEW 2018

Date of Notice: 9 March 2018

This notice informs all Registered Participants, registered Intending participants and interested parties (Consulted Persons) that AEMO is conducting the Gas Market Parameter Review 2018. The review covers the Declared Wholesale Gas Market (DWGM) and the Short Term Trading Market (STTM).

This review is being conducted under rule 492 of the National Gas Rules (NGR) for the STTM market parameters, in accordance with the extended consultative procedure requirements detailed in rule 9A of the NGR.

There is no rule requirement for the review of the DWGM market parameters, but AEMO has decided to review them in conjunction with the STTM market parameter review.

Matter under Consultation

This paper presents AEMO's draft determinations for market parameters in the DWGM and STTM. AEMO welcomes stakeholder views on any aspect of the draft report.

Further details are provided in the Draft Report published with this notice.

The Consultation Process

The consultation process is outlined below:

- Publication of Draft Report and Determination Fri 9 March 2018
- Closing date for submissions in response to the Draft Report Mon 26 March 2018
- Publication of Final Report and Determination Mon 30 April 2018

Invitation to Make Submissions

AEMO invites written submissions on any aspect of the draft report.

Please identify any parts of your submission that you wish to remain confidential, and explain why. AEMO may still publish that information if it does not consider it to be confidential, but will consult with you before doing so.

Please note that material identified as confidential may be given less weight in the decision-making process than material that is published.

Closing Date and Time

Submissions in response to this Notice of Consultation should be sent by email to gwcf_correspondence@aemo.com.au, to reach AEMO by 5.00pm (Melbourne time) on 26 March 2018.

Submissions received after the closing date and time will not be valid, and AEMO is not obliged to consider them. Any late submissions should explain the reason for lateness and the detriment to you if AEMO does not consider your submission.

Publication

All submissions (other than confidential content) will be published on AEMO's website.



EXECUTIVE SUMMARY

Rule 492 of the National Gas Rules (NGR) requires AEMO to conduct a review of market parameter settings in the Short Term Trading Market (STTM). While there is no mandated review of the market parameters in the Declared Wholesale Gas Market (DWGM), AEMO is taking the opportunity to also review the DWGM market parameters in conjunction with the STTM parameter review.

AEMO is required to review the STTM market parameters in accordance with the extended consultative procedure set out in rule 9A of the NGR and produce a final report setting out the outcomes of its review by 30 April 2018.

Parameters covered by the review

Market parameters should remain in force for long enough for market participants to establish their forward contracting strategy, but should change when they could be more effective in some aspect, or when they are subject to changes in cost structure.

AEMO has split this review into modelled parameters (where the parameter could be more effective, or could be subject to changes in cost structure) and reviewed parameters (where the parameter is unlikely to become more effective, or are not subject to significant changes in cost structure).

Table 1 Market Parameters to be reviewed

Parameter	STTM	DWGM
Market Price Cap (STTM) VoLL (DWGM)	\$400/GJ	\$800/GJ
Administered Price Cap	\$40/GJ	\$40/GJ
Cumulative Price Threshold	\$440/GJ (110 percent of the MPC)	\$1,800/GJ
CPT horizon (STTM) Cumulative price period (DWGM)	7 consecutive gas days	35 consecutive scheduling intervals (7 gas days)
Minimum Market Price (MMP)	\$0/GJ	\$0/GJ

Modelling approach

The parameters that have been modelled are the market price caps, the administered price caps, and the cumulative price threshold. The main driver for modelling is that there has been sustained increases to underlying market prices in both the STTM and the DWGM.

AEMO appointed Market Reform Pty Ltd to carry out the modelling work for this review. Their modelling approach is a scenario based analysis of each market's economic efficiency for a range of scenarios, market parameter values and market participant types. The scenarios cover extreme events in each market, and input data is modified for different years within the study period. Each scenario includes a sensitivity analysis to check the outcome for variations in input data.

The modelling will allow identification of sets of well performing and robust market parameters which will inform the need for change and provide the basis for any recommendations for change.

Review approach

The parameters that have been reviewed but not modelled are the cumulative price horizon/period and the minimum market price. These parameters are well established, and are unlikely to require change.

AEMO is seeking submissions from interested parties to confirm that these parameters are unlikely to become more effective in any way or are not subject to significant changes in cost structure in any way.



AEMO's draft determinations

AEMO's draft determination for gas market parameters are:

Parameter	STTM	DWGM
Market Price Cap (STTM) VoLL (DWGM)	Unchanged \$400/GJ	Unchanged \$800/GJ
Administered Price Cap	Unchanged \$40/GJ	Unchanged \$40/GJ
Cumulative Price Threshold	Unchanged \$440/GJ (110 percent of the MPC)	Changed \$1,400/GJ
CPT horizon (STTM) Cumulative price period (DWGM)	Unchanged 7 consecutive gas days	Unchanged 35 consecutive scheduling intervals (7 gas days)
Minimum Market Price (MMP)	Unchanged \$0/GJ	Unchanged \$0/GJ

The tightening supply and demand conditions over the studied period mean that the current DWGM CPT fails to provide adequate risk protection to market participants buying gas. The proposed reduction in the CPT value allows the revised parameter to provide adequate protection while minimising the impact on market efficiency.

Further details are included in sections 4 and 5 below.

Consultation to date

AEMO briefed the Gas Wholesale Consultative Forum (GWCF) in June 2017 on the impact of high prices on market parameters and AEMO's proposed approach to the review. A GWCF workshop in November 2017 provided interested parties with more details of the modelling approach.

A consultation paper published in December 2017 sought submissions on the approach to the gas Market Parameter Review 2018. Two submissions were received from interested parties, and are available on the review's page on AEMO's website¹.

A GWCF workshop in February 2018 presented more detail on the modelling methodology and preliminary modelling outputs.

Next Steps

This draft report will be open for submissions until **COB on Monday 26 March 2018**.

The final report will be published by 30 April 2018.

If AEMO recommends changing any market parameter, further regulatory approval is needed to implement any changes with effect from 1 July 2020.

¹ <http://www.aemo.com.au/Stakeholder-Consultation/Consultations/Gas-Market-Parameter-Review-2018>



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1. INTRODUCTION

The Short Term Trading Market (STTM) and Declared Wholesale Gas Market (DWGM) feature a number of price cap parameters that manage participant risk, and convey economic price signals. These parameters have previously been derived based on extensive modelling and review. The STTM parameters were first set in 2009, based on modelling performed by McLennan Magasanik Associates (MMA) and a peer review by Creative Energy Consulting. The DWGM parameters were first set over 1997 and 1998, and were reviewed in 2008 based on modelling performed by MMA, with peer review by Market Reform. No changes resulted from this review. The DWGM cumulative price threshold was reviewed in 2013 and changed from \$3,700 per GJ to \$1,800 per GJ with effect from 1 April 2014.

Rule 492 of the National Gas Rules (NGR) requires AEMO to undertake a review of the STTM market parameters by 30 April 2018. AEMO is also taking the opportunity to review the DWGM market parameters in conjunction with the STTM parameter review.

This document outlines the approach to the review together with AEMO's initial analysis and considerations for stakeholder feedback.

2. PARAMETERS COVERED BY THE REVIEW

2.1 STTM market parameters

The following STTM market parameters are mandated for review under clause 492 of the NGR.

Table 2 STTM Market Parameters

Parameter	Description	Documented In	Value
Market Price Cap (MPC)	The maximum market price to apply for a gas day. The MPC provides an upper limit on market clearing prices while not suppressing or distorting economic incentives for capacity investment, and providing market compensation for involuntary curtailment.	National Gas Rules	\$400/GJ
Administered Price Cap (APC)	The cap applicable when an administered price cap state is in place. The APC mitigates the risk of high prices in circumstances where exposure to extreme pricing is unlikely to promote a reasonable market response or market outcome.	National Gas Rules	\$40/GJ
Cumulative Price Threshold (CPT)	The threshold for automatic imposition of an administered price cap state. The CPT mitigates the risk of extended periods of high prices.	National Gas Rules	\$440/GJ (110 percent of the MPC)
CPT horizon (CPTH)	The period over which hub prices are summed to determine whether the cumulative price threshold has been exceeded.	National Gas Rules	7 consecutive gas days
Minimum Market Price (MMP)	The minimum market price to apply for a gas day.	National Gas Rules	\$0/GJ

There are two other parameters that currently operate in the STTM:

- Market operator service (MOS) Cost Cap—currently set at \$50/GJ, the MOS cost cap is the maximum price for MOS increase and decrease offers covering the MOS service component of market settlements. The MOS cost cap must be sufficient to cover the cost of holding capacity, while limiting MOS costs on the market.

- Settlement Surplus Cap—currently set at \$0.14/GJ, the settlement surplus cap is the maximum settlement surplus payment rate to be allocated based on deviations.

Neither the MOS cost cap nor the settlement surplus cap are within the scope of this review. Both were considered in the STTM operational review completed on 30 March 2012².

2.2 DWGM market parameters

The following DWGM parameters were included in the 2008 review:

Table 3 DWGM Market Parameters

Parameter	Description	Documented In	Value
Value of Lost Load (VoLL)	The maximum market price. VoLL provides an upper limit on market clearing prices while not suppressing or distorting economic incentives for capacity investment, and providing market compensation for involuntary curtailment.	National Gas Rules	\$800/GJ
Administered Price Cap (APC)	The cap applicable when an administered price cap state is in place. The APC mitigates the risk of high prices in circumstances where exposure to extreme pricing is unlikely to promote a reasonable market response or market outcome.	Wholesale Market Administered Pricing Procedures (Victoria)	\$40/GJ
Cumulative Price Threshold (CPT)	The threshold for imposition of an administered price period. The CPT mitigates the risk of extended periods of high prices.	Wholesale Market Administered Pricing Procedures (Victoria)	\$1,800/GJ
Cumulative Price Period (CPP)	The period over which marginal clearing prices are summed to determine whether the cumulative price threshold has been exceeded.	Wholesale Market Administered Pricing Procedures (Victoria)	35 consecutive scheduling intervals (7 gas days)
Minimum bid price (MBP)	The minimum price for a bid	National Gas Rules	\$0/GJ

The Value of Customer Reliability (VCR) is not within the scope of this review.

3. REVIEW APPROACH AND TIMETABLE

3.1 Review approach

Once set, market parameters should remain in force for long enough for market participants to establish their forward contracting strategy, but should change when they could be more effective in some aspect, or when they are subject to changes in cost structures. Accordingly, AEMO has split the market parameters being into two review categories:

- **Modelled parameters** – where the parameters may be more effective or could be subject to changes in cost structure; and
- **Reviewed parameters** – where the parameters are unlikely to become more effective or are not subject to significant changes in cost structure.

Each is discussed in more detail below.

² STTM Operational Review and Demand Hubs Review—Final Report, AEMO, 30 March 2012.



Modelled Parameters

Modelled Parameters were:

- Market Price Cap (MPC) / VoLL
- Administered Price Cap (APC)
- Cumulative Price Threshold (CPT)

AEMO retained consultants Market Reform Pty Ltd to develop a modelling approach, model the parameters and make recommendations for the values of market parameters to be applied from 1 July 2020.

Reviewed Parameters

Where parameters are unlikely to become more effective or subject to significant changes in cost structure, AEMO will be consulting with interested parties to confirm that these parameters should remain unchanged. Parameters included in this category are:

- CPT Horizon (CPTH) / Cumulative price period (CPP)
- Minimum Market Price (MMP) / Minimum bid price (MBP)

These market parameters are reviewed in section 4 below.

3.2 Modelling Approach

Based on a Scope of Work developed in consultation with the Gas Wholesale Consultative Forum (GWCF), AEMO sought proposals from consultants to carry out the modelling work. Three submissions were received. After evaluation of the proposals, AEMO appointed Market Reform Pty Ltd as the modelling consultant.

Summary of Market Reform's modelling approach

Market Reform's approach was to model the market's economic efficiency for a range of market parameter values across a number of scenarios. Each scenario included base and extreme event cases, so that the loss of economic efficiency for the modelled market parameter values can be determined for the scenario. The market outcomes for the scenario are then applied to a number of typical market participants to assess their varying degree of risk exposures resulting from the scenario.

The market context for scenarios reflected either the DWGM or the STTM, with the supply and demand modified to reflect conditions for a particular year within the study period and extreme events relevant to the particular market. Each scenario included an extreme pricing event and subsequent days during which the CPT may be reached, triggering APC. This allows assessment of each market's economic performance for the modelled market parameter values.

A scenario designed to reflect interactions between markets will include sets of STTM data and DWGM data suited to the scenario, but the market modelling for each was run separately. Each simulation included a sensitivity analysis to test the robustness of the market parameters for outcomes resulting from changes to the uncontrollable demand and offer prices used in the scenario. Where a scenario and set of data inputs would result in curtailment, the outputs were ignored³.

The modelling produced sets of results for combinations of gas market parameters, extreme events (in different market contexts) and for different sensitivity factor settings. From these, a set of well performing and robust parameters were identified. This set of parameters was used to inform the need for change for a market parameter, and to inform the recommendation of more appropriate market parameter values.

³ General curtailment in the STTM or the DWGM will lead to an APC regardless of other market prices, so the scenario is ineffective.



For more details of Market Reform’s approach, please refer to Attachment 1 – Gas Market Parameter Review 2018 – Draft Report - Market Reform Pty Ltd.

3.3 Review timetable

AEMO is required to review the STTM market parameters in accordance with the extended consultative procedure as per section 9A of the NGR. AEMO is required to complete this review by producing a final report setting out its final recommendations by 30 April 2018.

The review of the DWGM market parameters will adhere to this timetable.

Table 4 Review timetable

Process	Date
<i>Industry workshop to discuss review approach and scope</i>	<i>3 November 2017 (Completed)</i>
Consultation Paper – Open for Consultation	<i>8 December 2017 (Completed)</i>
Consultation Paper – Closing date for submissions	<i>24 January 2018 (Completed)</i>
Gas Wholesale Consultative Forum – Presentation of modelling and consultation outcomes	<i>13 February 2018 (Completed)</i>
Draft Report – Open for consultation	9 March 2018
Draft Report – Closing date for submissions	26 March 2018
AEMO releases final report	30 April 2018

4. MODELLED PARAMETERS

Market Reform Draft Final Report

Market Reform’s draft final report is included in Attachment 1, and is structured as set out in Table 5 below.

Table 5 Market Reform Report Structure

Section	Description
Section 1	Introduction
Section 2	Roles and bounds on the gas market parameters.
Section 3	Methodology and approach.
Section 4	Consultation and other feedback received
Section 5	Data and key assumptions
Section 6	Study findings
Section 7	Market Reform recommendations
Appendix.	Abbreviations
Appendix B	Scenarios
Appendix C	Summary data on market outcomes
Appendix D	Risk exposure levels for the different hypothetical participants



AEMO's draft determinations

AEMO has accepted Market Reform's recommendations for the modelled market parameters and has made draft determinations as follows:

Draft determination 1 – No change to market price cap / VoLL

The market price cap in the STTM \$400 per GJ

The value of VoLL in the DWGM \$800 per GJ

Draft determination 2 – No change to the Administered Price Cap

The administered price cap in the STTM \$40 per GJ

The administered price cap in the DWGM \$40 per GJ

Draft determination 3.1 – No change to Cumulative Price Threshold in STTM

The cumulative price threshold in the STTM 110% of marker price cap (\$440 per GJ)

Draft determination 3.2 – Change to Cumulative Price Threshold in DWGM

The cumulative price threshold in the DWGM changed from \$1,800 per GJ to \$1,400 per GJ

5. REVIEWED PARAMETERS

5.1 Minimum market price / Minimum bid price

Purpose of Minimum market price

Key principles in setting minimum market price are:

- no shipper should want to supply the spot market at a price less than MMP⁴
- MMP set sufficiently low as to not constrain the schedule

Previous reviews

The initial review of the STTM market parameters during the STTM Establishment Project concluded that:

“...a commercial or operational requirement for a negative minimum market price may not exist. Without a demonstrated need to bid below \$0/GJ there appears little justification for setting a minimum market price below this level.”⁵

Although not specifically modelled in previous reviews of the DWGM, the circumstances applying to the STTM are directly applicable to the DWGM.

⁴ STTM MARKET SETTINGS ANALYSIS, June 2009, Report to VENCORP by McLennan Magasanik Associates

⁵ STTM MARKET SETTINGS ANALYSIS, June 2009, Report to VENCORP by McLennan Magasanik Associates



Treatment of minimum market price in the NEM

The National Electricity Market (NEM) includes a negative minimum market price to allow negatively priced offers to give greater certainty of dispatch, thus avoiding stopping and starting generators for short periods.

Because injections of gas are treated as being uniform for the balance of the gas day in the DWGM, and for a full gas day in the STTM, the scheduling period in gas is significantly longer than the five minute NEM dispatch interval. It is therefore unlikely that the incentive for generators to offer short periods at negative prices in the NEM is replicated in gas markets.

Are current minimum market prices effective?

From 2013 until the end of Q3 in 2017, there have been 14 instances where the ex-ante market price has cleared at zero dollars per GJ (see Table 6 below for details).

Table 6 Ex Ante market prices of zero dollars per GJ

	DWGM	STTM
2013	1 (10am)	1 (Adelaide)
2014	-	1 (Brisbane)
2015	-	-
2016	2 (10am) 3 (6pm) 6 (10pm)	-
2017	1 (10pm)	-

While it is likely there will be tie breaking at zero dollars due to system point constraints in the DWGM (eg during maintenance), setting a negative MMP is likely to shift the tie breaking to the lower MMP with no change to the ex-ante market price.

Submissions on suitability of current minimum market prices

AEMO's initial assessment was that the setting for an MMP set at zero dollars per GJ is effective.

AEMO sought seeking submissions from interested parties as to whether the setting for MMP in the DWGM and STTM at \$0 per GJ could be more effective in any way.

No submissions were received, and AEMO's draft determination is that there will be no changes to the minimum market price in the STTM or the minimum bid price in the DWGM.

Draft determination 4 – No change to minimum market price / minimum bid price

The minimum market price in STTM and minimum bid price in DWGM remain at \$0 per GJ.

5.2 CPT horizon / Cumulative price period

Purpose of the CPT horizon / Cumulative price period

The primary purpose of the CPT is to cap price risks over a period of time. The CPTH / CPP sets the period of time for which prices are accumulated. It is aligned across the DWGM and STTM at seven gas days (35 consecutive scheduling intervals), which corresponds with the 336 intervals used in the NEM.



Treatment of the CPT horizon in current Reliability Panel review

The Reliability Panel has determined that the current review of reliability standard and settings will not examine the form of the CPT, and will only assess the level of the CPT⁶.

Submissions on suitability of the current CPT horizon

AEMO's initial assessment is that having the settings for CPTH / CPP are effective at seven consecutive gas days in the STTM and 35 consecutive scheduling intervals in the DWGM.

AEMO sought submissions from interested parties as to whether the setting for CPTH at seven consecutive gas days in the STTM and CPP at 35 consecutive scheduling intervals in the DWGM could be more effective in any way.

No submissions were received, and AEMO's draft determination is that there will be no changes to the CPT horizon in the STTM or the cumulative price period in the DWGM.

Draft determination 5 – No change to CPT horizon / cumulative price period

The CPT Horizon in the STTM should remain at 7 days.

The cumulative price period in the DWGM should remain at 35 scheduling intervals.

6. CONSULTATION TO DATE

6.1 GWCF briefing

The GWCF was briefed on the impact of higher prices on market parameters and AEMO's proposed approach to the parameter review, and were given the opportunity to provide input to the scope of work for modelling of market parameters.

Papers for past GWCF meetings are available on AEMO's website.

6.2 Industry workshop

To initiate consultation on the review process, on 3 November 2017, AEMO held an industry workshop. The purpose of the workshop was to seek industry views on the following:

- The review approach and timetable proposed by AEMO.
- The set of parameters requiring review and/or modelling.
- Presentation from Market Reform Pty Ltd including:
 - Markets and Trends
 - Past Reviews
 - Proposed Approach
 - Modelling
 - Data Sources

Presentations to the workshop are available on the Gas Market Parameter Review 2018 web page on AEMO's website (<http://www.aemo.com.au/Stakeholder-Consultation/Consultations/Gas-Market-Parameter-Review-2018>)

⁶ Reliability Panel, Review of reliability standard and settings guidelines, final guidelines, 1 December 2016, Sydney (Section 3.4)



6.3 Gas Market Parameter Review 2018 – Consultation paper

AEMO published a Consultation paper in December 2017, and sought submissions from interested parties as to the proposed modelling approach for market parameters that may be subject to changes in cost structures (market price caps, the administered price caps, and the cumulative price threshold) and review approach for those market parameters thought to be unlikely to become more effective in any way or subject to changes in cost structures (cumulative price horizon/period and the minimum market price).

AEMO received two submission that were generally supportive of approach.

Submissions and AEMO's comments on the submissions are available on the Gas Market Parameter Review 2018 web page (<http://www.aemo.com.au/Stakeholder-Consultation/Consultations/Gas-Market-Parameter-Review-2018>)

6.4 GWCF briefing

AEMO briefed the GWCF on 13 February 2018 on the modelling approach and Market Reform presented and discussed initial model outputs.

AEMO received three submissions after the GWCF briefing.

Presentations and notes from the briefing and submissions received after the briefing are available on the Gas Market Parameter Review 2018 web page on AEMO's website (<http://www.aemo.com.au/Stakeholder-Consultation/Consultations/Gas-Market-Parameter-Review-2018>).



7. NEXT STEPS

7.1 Submission in response to Draft Report

AEMO invites submissions from interested parties in response to any aspect of the draft determinations in this paper and in Attachment 1 Gas Market Parameter Review 2018 – Draft Report - Market Reform Pty Ltd. Interested parties should respond by email to gwcf_correspondence@aemo.com.au, with '[company name] Submission to Draft Report – Gas Market Parameter Review 2018' in the subject to be received no later than **COB on Monday 26 March 2018**.

7.2 AEMO to prepare a Final Report

AEMO will consider submissions received, and will publish the Gas Market Parameter Review 2018 - Final Report by no later than 30 April 2018.

7.3 Regulatory changes to implement recommendations

Following the Final Report, AEMO will commence the regulatory change process to implement the final determinations.

Based on the draft determinations in this Draft Report, changes would need to be made to the Wholesale Market Administered Pricing Procedures (Victoria) only. This change would follow the ordinary process for making Procedures set out in Part 15B of the NGR.

8. ATTACHMENTS

1. Gas Market Parameter Review 2018 – Draft Final Report - Market Reform Pty Ltd.



MEASURES, ABBREVIATIONS AND GLOSSARY

Units of measure

Abbreviation	Unit of measure
GJ	Gigajoule
TJ	Terajoule
PJ	Petajoule

Abbreviations

Abbreviation	Expanded name
AEMO	Australian Energy Market Operator
APC	Administered Price Cap (STTM & DWGM)
CPP	Cumulative Price Period (for CPT in DWGM) – equivalent to CPTH in STTM
CPT	Cumulative Price Threshold (STTM & DWGM)
CPTH	CPT Horizon (for CPT in STTM) – equivalent to CPP in DWGM
DWGM	Declared Wholesale Gas Market - Victoria
MBP	Minimum Bid Price (DWGM) - equivalent to MMP in STTM
MMP	Minimum Market Price (STTM) – equivalent to MBP in DWGM
MPC	Market Price Cap (STTM) – equivalent to VoLL in DWGM
NEM	National Electricity Market
NER	National Electricity Rules
NGL	National Gas Law
NGR	National Gas Rules
STTM	Short Term Trading Market – Sydney, Adelaide and Brisbane hubs
VoLL	Value of Lost Load (DWGM) – equivalent to MPC in STTM

Glossary

This document uses many terms that have meanings defined in the National Electricity Rules (NER) or the National Gas Rules (NGR). The NER / NGR meanings are adopted unless otherwise specified.