Explanatory Material on the Draft *National Gas (South Australia) (Gas Trading Exchanges) Amendment Bill 2013* and Draft *National Gas (Gas Trading Exchanges) Rules*

**Introduction**

To facilitate the establishment of Gas Trading Exchanges (GTEs) for natural gas, the Standing Council on Energy and Resources (SCER) Senior Committee of Officials (SCO) has prepared an exposure draft of amendments to National Gas Law (NGL) and National Gas Rules (NGR).

The NGL amendments are designed to give high level legal support to the GTE while significant rights and obligations of the operator and market participants are included in the NGR and the details of market operation are in the Gas Trading Exchange Agreement (Exchange Agreement).

The Exchange Agreement is currently being prepared by the Australian Energy Market Operator (AEMO) in consultation with industry participants as part of the Gas Supply Hub Reference Group (GSHRG). It is anticipated that a provisional draft will be released for public consultation in July 2013.

During the research and design phases of this project the GTE was referred to as a Gas Supply Hub. The name GTE has been adopted in the draft legislation to differentiate the exchange from other gas markets and more accurately describe its purpose. The GTE can still be referred to operationally as a Gas Supply Hub.

The proposed NGL and NGR amendments to establish the GTE have not yet been agreed by SCER or SCO.

**Background**

The east coast gas market is facing a period of rapid growth with increasing domestic demand and the development of coal seam gas to liquefied natural gas export projects. The pressure on the supply and demand balance has made it desirable to improve transparency and flexibility in upstream gas transactions.

In 2011, the Queensland Government considered implementing a GTE by 2015 as part of its Annual Gas Market Review 2011. On 9 December 2011, SCER agreed to request that AEMO prepare a full project scoping and cost report on the development of a GTE model.

At its June 2012 meeting, SCER considered AEMO’s scoping report and agreed to task AEMO with the development of a detailed design and implementation plan for the voluntary ‘Brokerage’ hub model – for initial application in Wallumbilla, Queensland. The detailed design and implementation plan is available on the SCER website at: [www.scer.gov.au](http://www.scer.gov.au).
Objectives

The GTE will help facilitate the development of economically efficient gas markets through:
- Allowing large gas users and producers to better manage their positions around long term contracts, by flexibly responding to changes in demand and production.
- Increased gas trading through the standardisation of trading contracts.
- Improved price transparency in upstream gas markets.
- Making the trading of pipeline capacity more accessible.

Market Design

The ‘Brokerage’ hub model will establish an exchange to match and clear trades using existing physical infrastructure. Interested buyers and sellers voluntarily place orders to buy or sell a particular quantity of gas being delivered to the relevant hub location. If a buy and a sell order match on price, the trade is cleared by the market operator. Sellers and Buyers are then responsible for arranging transportation of the gas to, or away from, the hub location.

The core trading products to be established for the GTE are day-ahead, balance-of-day and week-ahead products, with the potential to develop additional forward dated products that would create a forward price curve. This could further assist in risk management and balancing portfolios around long term contracts.

Consistent with the SCER request, a voluntary shipper-to-shipper capacity trading mechanism is also being developed to complement the GTE. This will operate as a listing service for shippers to make contact with market participants if they have an interest in buying or selling capacity at certain supply points.

Post 2015, SCER has agreed to review the model and if necessary consider the introduction of hub services, particularly financial ‘redirection’ services, to assist trading gas between nodes.

Legal Framework

Jurisdictions have prepared the necessary draft legislation to implement the GTE. This includes amendments to the NGL for introduction into the South Australian Parliament later this year and amendments to the NGR which will be made by the South Australian Minister following passage of the legislation. The Exchange Agreement will be made by AEMO after consultation with industry participants, which is anticipated for July this year.

Under the conceptual framework for the GTE legislation: the NGL will deal with a limited number of high level features of the regime; the NGR will contain the most significant rights and obligations of the operator and market participants; and the Exchange Agreement will address the detail of market operation and the remainder of the rights and responsibilities. The table below illustrates this approach.
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<th>Instrument</th>
<th>Responsibility</th>
<th>Subject Matter</th>
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| National Gas Law  | Made by SA Parliament, as the lead legislator. Application Acts will allow the establishment of GTEs in jurisdictions. | - Include the GTE among AEMO’s statutory functions  
- Authorise the SA Minister to make initial rules relating to AEMO’s GTE functions |
| National Gas Rules| Made initially by the South Australian Minister, subject to SCER endorsement. Future amendments to be made by the Australian Energy Market Commission, in accordance with the rule change procedures in the NGL. | - Establish the roles of AEMO and the AER (in relation to the GTE)  
- Include minimum scope for the content of the Exchange Agreement and the process for amending it  
- Provide for AEMO to set and recover fees for operating the GTE  
- Authorise AEMO to determine and recover payments  
- Provide for membership of the GTE, including suspension of access and termination of membership  
- Establish requirements regarding market conduct for the GTE |
| Exchange Agreement| Made by AEMO, in accordance with the NGL/NGR. The initial Exchange Agreement will be made by the AEMO Board. The Exchange Agreement will become enforceable as a contract between the operator and each GTE participant by executing Membership Agreements. | - Sets out the detailed provisions governing participation, trading and settlement for the GTE  
- Provides for trading and non-trading participants  
- Details regarding the trading products (including terms applicable to transactions), operational requirements, and processes to support transaction delivery, settlement and billing  
- Enables the Operator to impose prudential requirements for trading participants  
- Sets out events of default and other circumstances leading to suspension of access to the GTE or termination of membership |

The GTE is the first project of this kind and represents an incremental step in the development of liquidity in upstream gas markets. The ability of the GTE design to maximise participation has been an important consideration, considering its voluntary nature, and it has been designed to complement existing bilateral contract arrangements. As such, the Exchange Agreement will be a multi-lateral contract between AEMO and market participants who elect to become members of the GTE.

The proposed split of terms between NGR and Exchange Agreement is a measured balance between the need for a flexible and ‘light-handed’ approach, to encourage
participation and responsive development of the GTE, and an appropriate framework to safeguard and enforce key rights and responsibilities.

The NGL Amendments

The exposure draft of the NGL contains a small number of high level provisions to support the establishment of the GTE. The draft has been developed by jurisdictions.

AEMO’s Statutory Functions

The existing powers conferred on AEMO in the NGL to operate markets for natural gas were not designed for the GTE, which is different to existing markets. The amendments will provide AEMO with statutory authority to establish and operate the GTE. Section 91A(1) will include ‘gas trading exchange functions’ in AEMO’s statutory functions and a new section 91BRK will establish the content of those trading exchange functions.

National Gas Rules

The NGL specifies the broad content for the NGR. In order for the NGR to include provisions on the GTE, a new section 294D will be inserted to allow the South Australian Energy Minister to make Rules on the GTE and section 74(1) and Schedule 1 will be amended to include the GTE.

The NGR Amendments

The exposure draft of the NGR contains the key rights and obligations that are expected to impact GTE participants. The draft has been developed by AEMO.

The GTE rules provisions will predominantly be located in a new Part 22 of the NGR. The draft amendments have been designed to define the nature of the market (as hub model), include the minimum requirements for the content and amendment of the Exchange Agreement, and address other matters that are by nature more appropriate for rules than a contractual document.

These include provisions relating to:
- Participation fees;
- Membership;
- Determining payment amounts on a common basis in certain circumstances; and
- Conduct rules to be monitored and enforced by the AER.

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

Division 1 – Preliminary

This section defines relevant concepts for the GTE.
Division 2 – Operator

This section provides for AEMO to:
- charge and recover market fees;
- appoint another person to operate a gas trading hub if AEMO is satisfied that person has the appropriate qualifications, approvals and experience to do so; and
- determine payments on a common basis in certain circumstances (in the ordinary course payments in the GTE would be determined by matching orders).

Division 3 – Membership and Participation

This section provides for AEMO to:
- via Membership Agreements, enter into the Exchange Agreement with an applicant to be a GTE Member;
- allow a GTE Member to withdraw from participation at its request, subject to meeting all its obligations under the Exchange Agreement;
- suspend access to the GTE by a GTE member or terminate its membership in certain circumstances.

Division 4 – Exchange Agreement

This section sets out the following:
- allows for AEMO to make the Exchange Agreement and any procedures referred to in that agreement, and amend them from time to time;
- provide that changes to the Exchange Agreement may be proposed by AEMO and GTE Members and provide for:
  - the circumstances in which AEMO can decline to evaluate a proposed change;
  - the minimum requirements for AEMO to evaluate and consult on proposed changes, including minimum consultation periods;
  - the circumstances in which a modified (shorter) consultation procedure may be used); and
  - the Exchange Agreement to include additional requirements not inconsistent with the NGR.
- information to be published in accordance with the Exchange Agreement;
- provide for AEMO to make the Exchange Agreement available to market participants and to any other person who requests a copy (via a website).
- minimum requirements for content within the Exchange Agreement.

Division 5 – Conduct Rules

This section sets out the market conduct rules. The AER will be responsible for monitoring and enforcing compliance with these rules, through the compliance and enforcement framework already established in the NGL.