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22 July 2013

Mr Blair Comley
Chair, SCER Officials
c/o SCER Secretariat
Department of Resources, Energy and Tourism
GPO Box 1564
Canberra ACT 2601

Dear Mr Comley

**APA response to Gas Transmission Pipeline Capacity Trading Consultation
Regulation Impact Statement**

APA Group (APA) appreciates the opportunity to comment on the Standing Council on Energy and Resources (SCER) Gas Transmission Pipeline Capacity Trading Consultation Regulation Impact Statement.

APA is a major ASX-listed gas transportation business with interests in energy infrastructure across Australia, including over 14,000 kilometres of natural gas pipelines, gas storage facilities and a wind farm. APA is Australia's largest transporter of natural gas, delivering about half of Australia's annual gas use through its infrastructure. APA owns and operates a diverse portfolio of energy infrastructure assets across Australia, with a value of approximately \$12 billion. These assets also include investments in two interstate electricity interconnectors which operate in the National Electricity Market.

As set out in detail in the accompanying submission, APA considers that due to the current structure and maturity of the domestic gas market, there is likely to be limited demand for pipeline capacity trading in the near to medium term. As a result, APA considers that there is not yet a policy case for the establishment of a government-facilitated capacity trading mechanism. The costs of such an approach are likely to exceed the benefits, and in doing so may impose costs on the market that may inhibit instead of support its further growth.

APA considers that there remains scope, however, for the market to provide niche products and solutions to address specific issues associated with capacity trading at a much lower cost than any government/regulatory model. In this vein, APA is currently implementing a project to scope the requirements of both existing shippers and potential users of traded capacity to determine whether there are efficient and effective secondary capacity trading solutions that it could offer to the market. APA is concerned that a move by governments to intervene in the market by establishing facilitated capacity trading at this stage is very likely to foreclose options for a market-led solution, and lead to additional and unnecessary costs being imposed on the gas market.

Please contact Alexandra Curran on 02 9275 0020 if you would like to discuss any aspect of this submission.

Yours sincerely

Peter Bolding
General Manager Regulatory & Strategy



Gas Transmission Pipeline Capacity Trading

APA response to Regulation Impact Statement

1 Introduction

APA Group (APA) appreciates the opportunity to lodge the following submission in response to the Standing Council on Energy and Resources (SCER) Gas Transmission Pipeline Capacity Trading Consultation Regulation Impact Statement.

1.1 About APA

APA is a major ASX-listed gas transportation business with interests in energy infrastructure across Australia, including over 14,000 km of natural gas pipelines, gas storage facilities and a wind farm. APA plays a pivotal role in Australia's energy sector. APA is Australia's largest transporter of natural gas, delivering about half of Australia's annual gas use through its infrastructure. APA owns and operates a diverse portfolio of energy infrastructure assets across Australia, with a value of approximately \$12 billion.

1.2 About this submission

This submission provides APA's views on the need for further intervention in the downstream gas market, and on the policy case for capacity trading in particular.

APA is also a member of the Australian Pipeline Industry Association (APIA), and contributed to the development of APIA's submission to this consultation process. APA refers SCER Officials to the APIA submission in respect of providing a detailed discussion of the issues and questions raised in the consultation RIS.

2 Development of gas market over last decade

2.1 Transmission sector investment

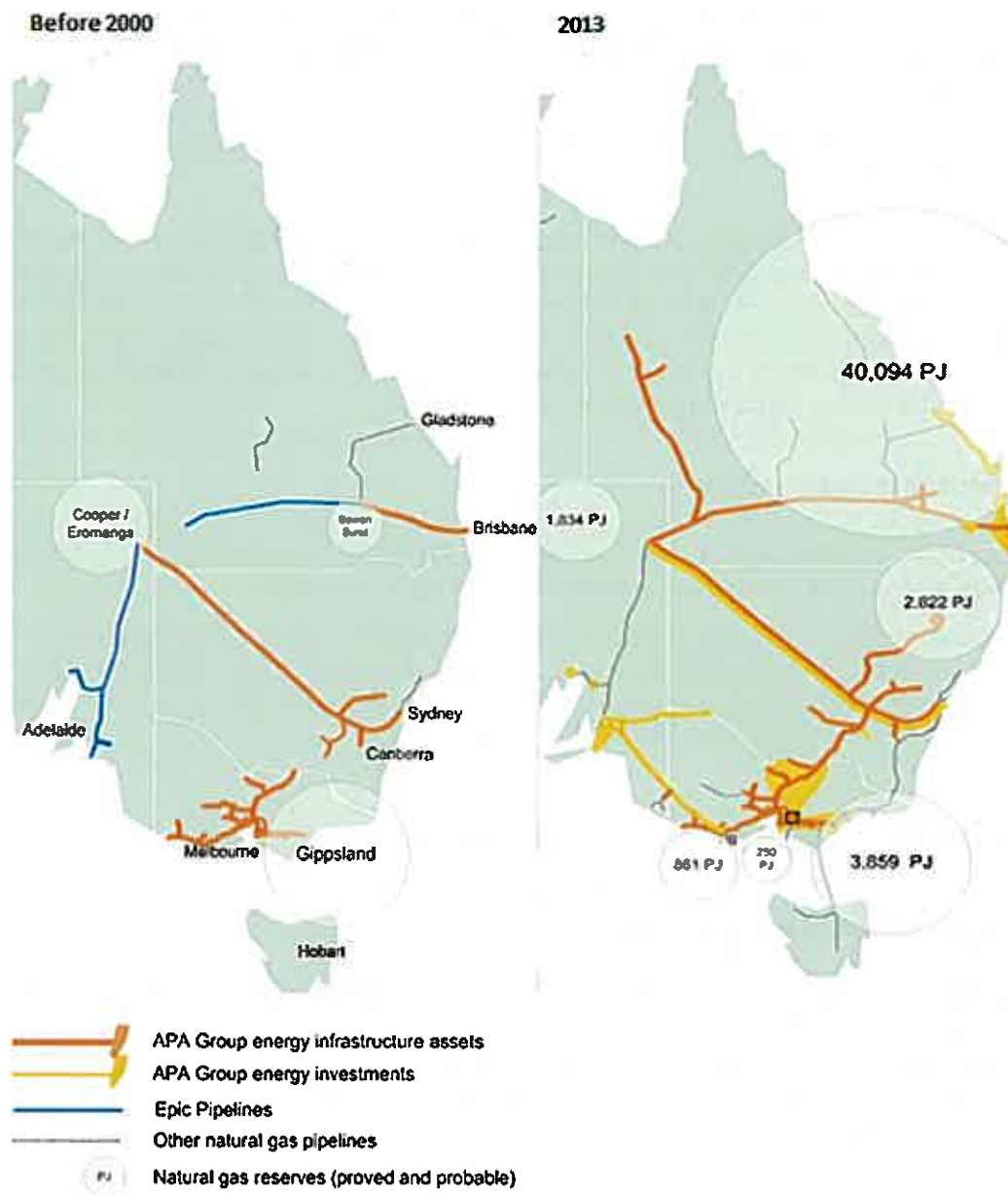
The Australian gas market has experienced significant development in the last decade. Starting from a fragmented market characterised by point-to-point (single basin to demand centre) gas supply, the south east Australian market is now highly interconnected with most major centres served by more than one pipeline, and gas able to be sourced from multiple basins to meet demand.

This development is shown in Figure 1 below, which compares the interconnectedness of the south east Australian gas market prior to 2000 to that now. Of particular note, the construction of the Eastern Gas Pipeline and the Interconnect Pipeline have directly linked the Melbourne and Sydney markets, the SEAGas Pipeline has linked the Melbourne and Adelaide markets, and the BassGas and South West Queensland pipelines have respectively linked the Tasmanian and the Queensland markets to the south eastern gas market.



The interconnectivity of pipeline infrastructure has created the platform upon which basin-on-basin competition could be delivered, and enables users to diversify their gas portfolios as existing long term contracts expire. In addition, new major gas production regions have emerged through the development of coal seam methane reserves in Queensland, and potential for similar development in New South Wales, further enhancing diversity in the south eastern gas grid.

Figure 1 – Gas pipelines and reserves before 2000 compared with 2013





2.2 Developments in the upstream sector

APA notes that there is currently considerable debate about the medium term outlook for eastern Australian gas supply and demand, and therefore gas pricing. This is as a result of the very large changes to the gas market structure currently occurring. These changes are being driven by the development of LNG export facilities in the east coast of Australia, with reserves previously earmarked for domestic supply being directed to the more lucrative gas contracts being offered by LNG proponents.

Market reforms to date (discussed further in the next section) have focused on improving competition and regulation in the downstream sector. During this time, however, the upstream sector (namely, gas exploration and production) has seen considerable aggregation and consolidation, leading to reduced competition between players. This has impacted the availability of gas for the domestic market, as reserves are being allocated to the export contracts of the larger players.

In the past, smaller gas producers have been willing to enter into long term contracts with domestic shippers as their gas reserves were not internationally marketable. Aggregation and joint marketing arrangements now mean that fewer of these smaller reserves are being offered to the domestic market, leading to higher prices.

The lack of upstream competition from smaller producers means that smaller parcels of gas are not being made available for domestic contracts. APA understands that third party access to upstream processing facilities on appropriate terms is a key issue for smaller producers to facilitate the development of small fields and provide access to the market. Instead, in the absence of greater transparency, larger producers appear to be holding back reserves (or not spending the capital to develop resources to reserves classification) until they achieve marketable quantities for international trade.

2.3 Gas market development

Interventions in the gas market

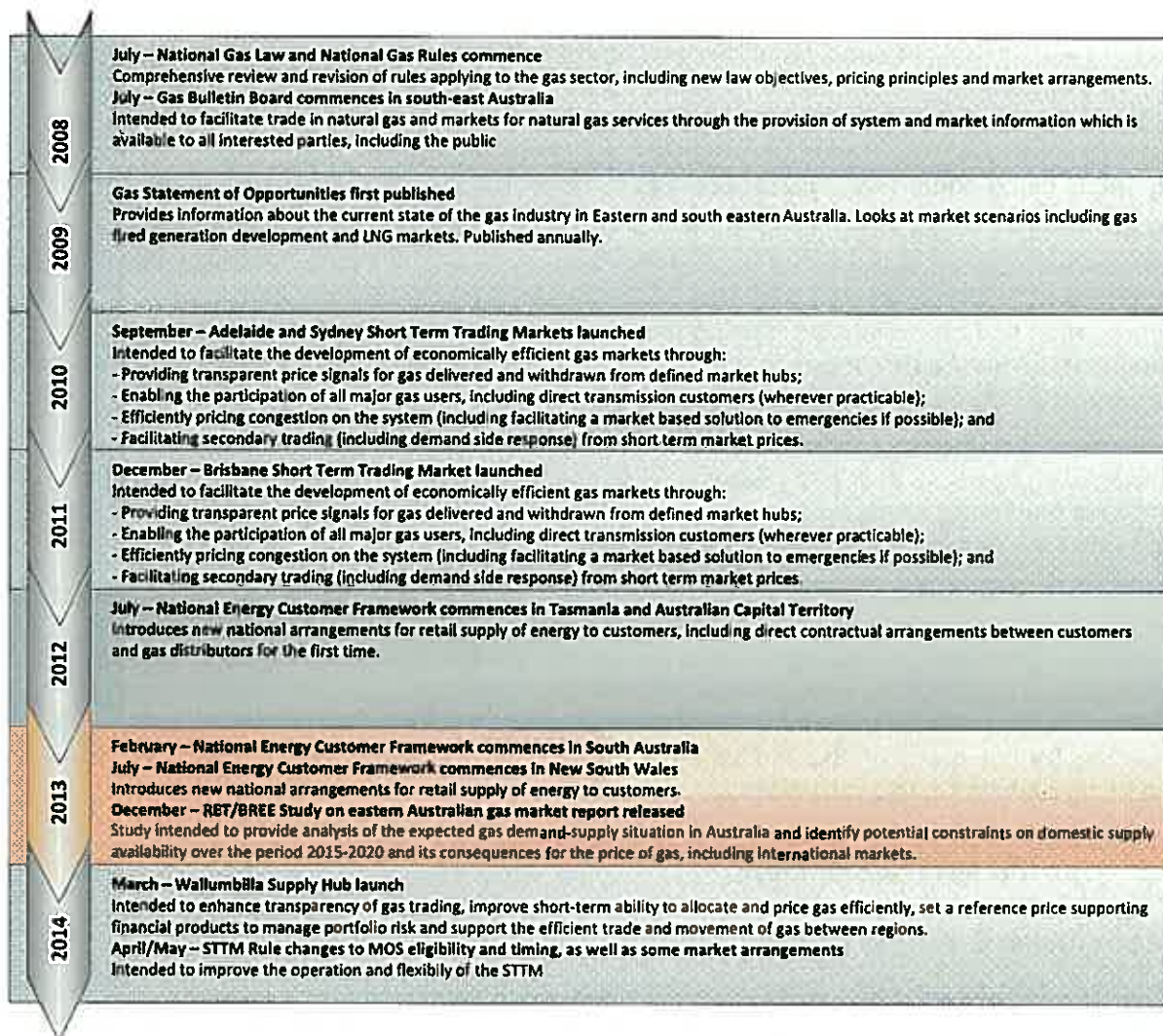
There have been a number of recent interventions in the downstream gas market intended to improve market transparency, asset utilisation, and the ability for smaller users to enter the market. These are set out in the timeline in Figure 2 below.

Of particular note in this timeline is the implementation of the Short Term Trading Markets (STTMs) in Sydney and Adelaide, which commenced on 1 September 2010, and the Brisbane STTM started on 1 December 2011. These reforms were intended (amongst other things) to provide greater opportunities for market participants to trade gas, thereby increasing competition in both the upstream and downstream markets.

Further, the new Wallumbilla gas supply hub, which is based on a different market structure to the STTM, is not expected to start until 20 March 2014. APA also understands that there is a forthcoming rule change proposal from the Australian Energy Market Operator intended to facilitate trading in Authorised Maximum Daily Quantity (AMDQ) holdings between shippers within the Victorian Declared Transmission System. These reforms are intended to further improve opportunities to trade gas amongst participants.



Figure 2 – Government interventions in gas market since introduction of National Gas Law in 2008



Success of recent gas market interventions

It should be noted that in the context of a gas market characterised by longer term supply and transmission contracts, the new STTM arrangements have been in place for a relatively short period. It will take time for the gas market to adapt to these changes, and it may be the case that existing contracts and arrangements need to roll off before these market arrangements can be fully utilised by participants. APA considers that it is therefore too early to draw definite conclusions as to the success or otherwise of these market interventions.

Notwithstanding that these market interventions have only been made relatively recently, early indications suggest that they have made limited differences to competition in downstream markets, and have not yet driven greater competition in upstream markets. It is also not clear that they have assisted in delivering lower gas prices.



For example, the average delivered gas price changes at each domestic gas market from the first quarter of 2011 to the first quarter of 2012 were as follows:

- Brisbane STTM Hub: increased 120%
- Sydney STTM Hub: increased 50%
- Adelaide STTM Hub: increased 35%
- Victorian DWGM: increased 33%

Looking more closely at these price changes, there is a very modest increase in transmission tariffs (contributing only 2% of increase at each of the Sydney and Brisbane hubs), compared to very significant increases in the commodity component. Transmission tariffs also make up only a small proportion of the total delivered gas price at each of these hubs: under 20% at the Sydney hub (Moomba to Sydney Pipeline tariff), and just over 10% at the Brisbane hub (Roma to Brisbane Pipeline tariff).

The driver of price increases is the increase in gas supply cost through the trend towards international gas price parity. APA considers that the introduction of domestic gas or capacity trading markets are very unlikely to have any material impact on that trend.

Further, recent interventions in the market have imposed costs on participants. For example, AEMO STTM market fees impose an additional 7.2c per GJ on all gas moving through the hubs (regardless of whether that gas is traded through the hubs). The cost per GJ of actual trades between unrelated parties is likely to be significantly higher. AEMO's fee is up 11% from 2012/13, and AEMO forecasts that it will increase 12% next year as well.¹ In addition, individual market participants have incurred significant costs in building systems and hiring staff to manage their STTM obligations. These costs must be considered against the benefits delivered from existing markets, as well as in the case for making further interventions.

2.4 Need for a review of existing gas market and interventions

APA considers that an assessment of upstream sectoral arrangements is a critical precondition to further gas sector reform. This assessment will be important in determining what further interventions may be appropriate, in particular if it is found (as APA suspects) that issues in the upstream sector are driving outcomes in the domestic gas market as a whole. If upstream issues are found to be inhibiting gas market efficiency, then further intervention in the downstream market, such as that contemplated in the consultation RIS, will not noticeably improve market efficiency, and may instead impose additional costs on the domestic market without an associated benefit.

Such an assessment (as contemplated by the recently announced domestic gas market study to be undertaken by the Department of Energy, Resources and Tourism (DRET) and the Bureau of Resource and Energy Economics (BREE)) is therefore important to ensure that interventions are appropriately targeted to address identified problems in the sector.

Further, given limited gains made from market interventions to date (as well as the pending developments at Wallumbilla), APA considers that it would be prudent to review the success or otherwise of current market interventions in the downstream sector before initiating further changes downstream. APA therefore supports the proposal in the consultation RIS that the

¹ Australian Energy Market Operator 2013, *Short Term Trading Market (STTM) Final Budget and Fees 2013-14*, p 3



status quo be maintained until after the Wallumbilla hub is operational, in order to be able to assess the level of demand for unused capacity.²

APA considers, however, that one year (as suggested in the consultation RIS) is not sufficient time in which to assess the success or otherwise of that intervention. Instead, APA considers that three years would be the minimum amount of time sufficient to allow that market to settle and operate as intended, considering that contractual arrangements (for both supply and transportation) must adapt before potential benefits can be realised.

APA also considers that it is important for governments to at the same time review the degree to which the other recent gas market interventions have achieved their stated policy goals. In this light, APA recommends that the SCER undertake a comprehensive review of the success of the Bulletin Board, STTM hubs in Sydney, Adelaide and Brisbane, and the Wallumbilla supply hub in 2016/17. At this time it would be possible to comprehensively assess the success of market interventions as:

- the Sydney and Adelaide STTM hubs will have been operating for 6 years;
- the Brisbane STTM hub will have been operating for 5 years; and
- the Wallumbilla gas supply hub will have been operating for 3 years.

This approach would support evidence-based policy development that considers the costs and benefits of government interventions in the downstream gas sector.

In summary, the downstream market must be given sufficient time to develop and mature under the existing arrangements before additional external mechanisms are imposed, potentially at significant further cost to market participants and ultimately consumers. APA considers that this approach will allow the downstream market to develop its own solutions and services to ensure efficient pipeline utilisation driven by demand.

By contrast, the threat of early and unwarranted government intervention has the potential to undermine any market-led processes. This is a particular threat in relation to pipeline capacity trading, where the option of pipeline-facilitated trading is under active consideration by APA. The possibility of a government facilitated capacity market that would erode any value from a market participant-led solution undermines this work and the associated business case, most likely leading to less efficient market outcomes being imposed through regulatory intervention.

3 Pipeline capacity trading

3.1 Policy rationale

The Consultation RIS sets out a potential policy rationale for further intervention in the downstream gas market through the introduction of some form of facilitated pipeline capacity trading. In particular, the consultation RIS discusses the need for increased transparency and flexibility in the domestic gas market in order to achieve greater efficiency, and then tests the case as to whether these outcomes can be achieved through facilitated pipeline capacity trading.³

² Standing Council on Energy and Resources Officials 2013, *Gas Transmission Pipeline Capacity Trading Regulation Impact Statement Consultation Paper*, 15 May, p 4

³ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, p 10



APA notes that while the consultation RIS looks at the case for pipeline capacity trading, it does not assess the validity of its base assumptions around the desirability of increasing transparency and flexibility in the gas market. These are effectively taken 'as read'.

APA agrees that transparency and flexibility are important for any effective market, including the domestic gas market. APA considers, however, that the case for government intervention to facilitate increased transparency and flexibility must be tested, first, by looking at the current levels of transparency and flexibility and asking whether they are in need of improvement, and secondly, if the first is confirmed, by asking whether, in light of the current maturity of the gas market, increasing transparency and flexibility will improve the efficiency of the market. APA considers each of these matters below.

Transparency

Unlike in the United States, the Australian gas market is characterised by a small number of participants. These participants are, however, large and highly informed. Due to the transactions involved, smaller (second tier) retailers and intending participants must also be of a sufficient size, with access to significant business and financial resources, as evidenced by the prudential requirements in place for all operating gas (and electricity) markets.

In respect of market transparency, these participants have access to or are able to access all the information they require to operate in the market. Existing public resources include the gas market bulletin board, the pipeline register of spare capacity for covered pipelines, access arrangements and posted prices (for the availability of capacity and the price of gas transportation) and the STTM and Declared Wholesale Gas Market (DWGM) for the short-term price of gas. Users and potential users can also approach producers, retailers and transmission companies to uncover further detail as to available gas and capacity.

The transparency of the market must therefore be assessed against the availability and accessibility of information for existing and intending market participants. It is not necessary for there to be broad public knowledge of expected gas and transportation costs for the gas market to be considered transparent – it is only necessary that market participants have knowledge of expected gas and transportation costs, or be able to readily uncover those costs through enquiries.

APA considers that the gas transportation market performs well in this regard, with information readily available on the cost of gas transportation through a number of means, including but not limited to prices determined in full access arrangements.

APA considers that improvements could be made to the transparency of gas supply, and anticipates that the DRET/BREE domestic gas market study will assist in this regard.

Flexibility

APA understands that shippers and end users are currently facing difficulties in securing longer term gas supply contracts at prices in line with historic trends. Gas supply contracts, where offered, also lack the flexibility often included in past contracts. This lack of flexibility at the producer level is being reflected in shippers only entering into transportation contracts to match their contracted supply.

As a result, shorter transportation contracts have been replacing existing longer term point-to-point transportation contracts for a number of years. It is therefore not accurate to assert that gas transmission companies will not enter into shorter term arrangements.⁴

⁴ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, pp 17-18



APA's experience, however, is that where longer term gas supply contracts are available, shippers also prefer longer term transportation contracts. Under these contracts (both long and short term), flexibility is available through mechanisms for bare transfers that facilitate capacity trading where the shipper wishes. APA therefore considers that current concerns over flexibility are largely driven by upstream market arrangements.

Will improved transparency and flexibility increase market efficiency?

Notwithstanding that APA considers that downstream market arrangements display a level of transparency and flexibility that is commensurate with the maturity of the gas market, it is important to consider whether further improving transparency and flexibility in the downstream sector will aid efficiency in the domestic gas market. The consultation RIS suggests that actions to reduce transaction costs associated with capacity trading and to assist willing trading partners to identify each other will increase the depth and liquidity of the market.⁵

APA is concerned that this line of argument may be confusing the drivers of increased market transparency and liquidity with their outcomes. For example, a commonly made argument in respect of the pipeline sector is that long term contracts detract from efficiency. In fact, where a market is not deep and liquid, long term contracts are likely to aid efficiency by effectively managing participant risk regarding investment and access to the market.

In a deep and liquid market, long term contracts are unlikely to be as necessary for either the shipper or the investor, however, the market needs to be deep and liquid first to reduce the risks in order to drive this change. Merely increasing market transparency will not reduce risks – it is important for the market to also be mature with a broad and diverse customer base.

Recent trends in both the upstream and downstream gas sectors (in particular the aggregation of gas producers and the vertical integration of retail and production/generation) may be contrary to the development of deep and liquid gas markets. It therefore stands to reason that policy efforts to improve the efficiency of the gas market by increasing market transparency alone may not be effective. Indeed, the limited successes of market interventions to date provide an indication of this.

For this reason APA considers that it is critically important to assess the current performance of the gas market as a whole, including the upstream sector, before embarking on future gas market interventions. It is not sufficient to simply look at the market for transmission capacity in isolation, as this is likely to disregard barriers to efficiency that may undermine the success of such interventions.

3.2 Expected policy outcomes from increased capacity trading

The consultation RIS states that capacity trading will become increasingly important to:

- efficiently re-allocate unused capacity and gas to higher-value uses;
- maximise the efficiency of capital stock;
- incentivise pipeline investment;
- create opportunities for gas trading, particularly at the Gas Supply Hub;
- support gas market growth; and

⁵ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, p 28



- assist with bringing additional gas to market.⁶

APA discusses each of these expected policy outcomes in the following sections.

Re-allocation of unused capacity and gas to higher-value uses

This outcome relies on two conditions: first, that there are 'higher value' gas uses that are currently unmet by the market, and which cannot be met without a facilitated trading platform; and secondly, that there is 'unused' capacity available at the same time that a higher value use may want it. APA considers that there is insufficient evidence to support either of these conditions.

In respect of the existence of higher value uses that are unmet by the market, the consultation RIS states:

Although it is not clear how strong the demand for unutilised capacity is, it is unlikely that the current market for gas transportation is preventing wide-scale unmet demand for transportation capacity being filled.⁷

APA supports this conclusion as it reflects its own experience in the market.

APA is in the business of providing pipeline capacity. As such it is in its interest to seek out and develop opportunities for new pipelines, and extensions/expansions to existing pipelines. These activities grow the business and improve revenue. Further, APA is incentivised to improve the utilisation of its existing pipelines as this increases revenue. Given APA's position in the market, it is unlikely that there is unmet demand of which APA is unaware.

Notwithstanding that APA has 'as available' capacity available on most of its pipelines, the concept of a 'higher value' use also suggests that such a user may be in the position to underpin investment in additional capacity to meet that need.

Nevertheless, it is important to identify what that theoretical higher value use might be before intervening in the market to facilitate its market position – otherwise the ultimate market design may not meet the needs of that user. This may occur, for example, if that user needs longer term firm capacity as opposed to the types of short term capacity potentially available under a capacity trading mechanism.

In respect of the second condition, the consultation RIS notes that existing contractual arrangements reflect the peak needs of users, and therefore 'unused' capacity is only likely to be available outside of the peak.⁸ A key reason that shippers prefer firm transportation contracts is that they ensure capacity is available at peak times to meet their needs or their customer's needs, and to match gas supply contracts that often lack flexibility as to gas delivery (that is, gas supply cannot be stopped just because the shipper does not have pipeline capacity available). Given these issues, it is unlikely that there is significant unmet demand for capacity only at off-peak times. In any case, it is at these times that other shippers with firm capacity contracts, as well as the pipeliner through as available contracts, would be able (and incentivised) to offer this capacity to the market.

Maximise efficiency of capital stock

Pipeline businesses are incentivised to offer any available capacity (either firm or as available) to the market.

⁶ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, p 4

⁷ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, p 31

⁸ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, p 14



As a non-vertically integrated infrastructure provider, APA has clear incentive to provide access to its existing facilities. APA faces high sunk costs in its network of assets and has a clear incentive to maximise throughput so as to earn higher revenues. Further, APA is incentivised to facilitate new entry by customers as well as gas producers as, not only will this increase throughput, but a broader portfolio of customers will more effectively manage APA's counter-party credit and countervailing power risk. That is, APA has no incentive to hinder access and every incentive to facilitate access and grow its business through increased utilisation of its assets.

Given this, and with APA's experience with its contractual arrangements, APA does not agree with the assertion in the consultation RIS that pipeliners are less interested in negotiating short term or as available contracts as they represent lower value transactions.⁹ While it is the case the vast bulk of APA's pipeline revenue is derived through firm contractual arrangements, this reflects the preferences of its shippers. As available contracts provide scope for additional revenue for APA and therefore add value to the business.

Incentivise pipeline investment

It is not clear that additional capacity trading will incentivise pipeline investment. To the extent that pipeline capacity trading increases utilisation on pipelines that do not have firm capacity available, the consultation RIS notes that trading is likely to discourage, delay or avoid the construction of new capacity.¹⁰ Of course, this outcome is dependent on there being current unmet demand for capacity outside of peak times that would otherwise have been met by pipeline expansion. As noted above, APA does not consider that there is evidence to support this position.

Create opportunities for gas trading

This condition would only be met if there were current (or expected future) opportunities for gas trading that are or would be stymied by the lack of available pipeline capacity. Given the current conditions in the upstream gas sector, APA considers it unlikely that there is significant gas available for trade at the moment, or expected in the foreseeable future.

Initial arguments for gas trading were premised around, amongst other things, the idea that there would be significant 'ramp up' gas in the lead up to the completion of LNG export facilities that would be made available in the domestic market. In reality, LNG producers appear to be facing a possible shortfall of gas in the early stages of their projects, and are instead looking for options to store or otherwise procure additional gas from alternative gas sources in order to meet contractual obligations. This has been a key driver of increased gas prices ahead of actual gas export.

Support gas market growth

This would be a key condition for any gas market intervention.

It is not clear to APA that capacity trading will support gas market growth. As noted above, APA does not believe that there is significant unmet demand for pipeline capacity in the domestic gas market. Similarly, APA does not observe that there is significant scope for gas trading (at least, scope sufficient to support a government-facilitated market structure) due to current tightness of gas supply. Capacity trading is also unlikely to incentivise pipeline investment. Further, while trading may deliver some gas arbitrage opportunities, these opportunities are more likely to lead to transfers rather than net growth in the gas market.

⁹ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, p 17

¹⁰ SCER Officials 2013, *Pipeline Capacity Trading RIS Consultation Paper*, p 28



In the end, gas market growth will be driven by economic growth that leads to new commercial, industrial or power generation demand. It is unlikely that capacity trading will deliver this type of growth.

Assist with bringing additional gas to market

As noted above, it is not clear that there is currently significant additional gas available for domestic supply. To the contrary, there appears to be a net shortfall of gas for export LNG projects, such that smaller producers and supplies are being purchased by LNG project proponents to bolster supply in the short to medium term. While in the past these smaller producers may have offered their smaller gas quantities to the domestic market, these supplies are now destined for international markets.

Conclusion

APA considers that under the current gas market arrangements, it is unlikely that increased capacity trading will deliver the policy outcomes sought by governments. It seems apparent that current gas market conditions related to LNG exports are driving market outcomes at this time, and further interventions in the downstream market will not address perceived market failures.

3.3 Consideration of capacity trading options

The consultation RIS sets out a number of options for facilitating capacity trading, as discussed below. In many cases, these options are only described at a very high level. Because of this, it is difficult to fully engage with the options and discuss their various strengths and weaknesses. This is particularly the case where some options leave open the question as to whether they would be government or market hosted/driven.

APA considers that this is a key question that will drive the success or otherwise of capacity trading, and one that must be clarified before market participants can meaningfully engage with the options set out in the consultation RIS. Notwithstanding this, APA provides some high level comments on these options in the following sections.

Option 1 – Status quo

The status quo involves no change to the current arrangements, but does include the continuation of current plans for a gas trading platform as part of the Wallumbilla Hub.

APA supports this option, subject to APA's earlier comments on the need for a robust assessment of the costs and benefits of current (and pending) market interventions. Importantly, it should be noted that this option does not represent a 'no capacity trading' option.

Shippers currently have the ability to trade pipeline capacity on a bilateral basis, and there is evidence that this type of trading does occur, though it is limited. Shippers also engage in the trade of bundled gas and capacity through the STTM, where the buyer of gas is able to utilise capacity owned by the seller of gas.

Given the economic incentives that shippers that hold unused firm capacity would have to trade that capacity, APA considers that it is reasonable to assume that shippers would seek to trade this capacity if it were genuinely 'unused', and if there were a market for it. As the domestic gas market is a reasonably small market, APA does not consider that there are material barriers to shippers identifying potential counterparties to such trades.



In addition, pipeliners are able to offer as available contracts on most pipelines. Even in the absence of shipper trading of capacity, as available contracts effectively offer unutilised contracted capacity to the market.

A status quo option also provides scope for further market-led solutions and products to emerge (discussed further in section 3.4). It is likely that a government facilitated trading platform will foreclose opportunities for market-led solutions that are tailored to the needs of the market.

Option 2 – Improved information provision and the standardisation of contractual terms and conditions

APA does not support this option. There is already considerable information available on the gas market bulletin board regarding available pipeline capacity (that is, the difference between the pipeline capacity and daily nominations). Ex ante information is available on a daily basis, and in a three day outlook. Ex poste data is also published. It is not clear that further pipeline capacity information disclosure would materially assist the market from the current arrangements.

APA also notes that the consultation RIS leaves open whether this information would be posted on the gas market bulletin board or on pipeliners' websites. APA considers that there is a considerable difference between these two options, not the least of which being the need for detailed rules, systems and data transfer protocols associated with a bulletin board option compared to a pipeliner-based option. Further consideration must be given to the associated costs and regulatory burden of 'centralised' data options compared to options at the participant level before proceeding. APA considers that as the market has relatively limited participants that are easily identified, the case for a centralised information exchange is limited.

Option 2 also includes the standardisation of contractual terms and conditions. No further detail is provided on this issue, and it is not discussed elsewhere in the consultation RIS. In the absence of detail, APA is not able to comment on this option except to note that if standardisation of terms and conditions were important to the market, then there is already opportunity for this to happen.

In this regard, APA has developed standard terms and conditions for all its gas transportation agreements which form the starting point for negotiations with shippers. APA's experience has been that shippers do seek modification of those terms to meet their specific needs for transportation and risk allocation. Given this, APA considers that standardisation of terms and conditions would not be a straightforward process, and may indeed hinder the development of the market and the tailoring of products to shippers' needs.

APA also notes that any move to standardised terms and conditions is likely to involve increased obligations on most shippers as terms and conditions must be designed to accommodate the entire market. This is particularly relevant in areas such as credit support, where provisions will need to be sufficient for the least credit worthy of potential shippers, thereby imposing costs on other shippers that they otherwise might have avoided under normal commercial arrangements.

Further, the majority of pipelines that might be involved in a government-facilitated capacity trading are not regulated for price and service. A move to enforce standard terms, conditions and services on such pipelines would be contrary to the scope of current access regulation, and ought to be carefully considered before being initiated due to the potential for regulation to significantly impact market efficiency.



Option 3 – Voluntary trading platform and an incentive for incumbents to release capacity

APA does not support this option and finds it the least detailed of all options presented in the consultation RIS. For example, this option does not specify:

- Whether platform would be operated by a government body, a pipeliner/pipeline or another party/parties;
- Whether, if the platform is hosted by a pipeliner or another party, it is market or government initiated/led;
- What type of incentives may be considered;
 - If incentives are financial, who might be paying them;
 - Incentives are regulatory, who might be enforcing them;
- The differential cost of options; and
- What 'standard contract terms' might encompass.

APA considers that a government initiated/led option is likely to impose considerable costs on the gas market that, given the expectation of limited demand for capacity trading, are likely to far exceed the benefits. This level of intervention would foreclose any scope for a market-led solution for capacity trading.

APA considers that a market-led solution ought to be preferred by policy makers as it is likely to be more efficient than a government-led option, and will ensure that only the beneficiaries of the market pay for its costs. These issues are discussed further in section 3.4.

Option 4 – Mandatory trading obligations requiring incumbents to release unutilised capacity to all market participants on either an 'as available' or firm basis

APA does not support this option.

As noted in the consultation RIS, there does not appear to be an adequate policy or market case for pursuing this option. This option is likely to be highly costly, and will increase uncertainty and volatility in the gas market. It is also likely to considerably undermine pipeline investment by removing certainty from shippers on the availability and accessibility of firm capacity.

APA already acts as an incentive to offer as available capacity on its pipelines to the extent that this is economically efficient (that is, that it does not undermine the demand for other pipeline services). It does not appear necessary to compel pipeline (or other market participants) to act in their economic interest by compelling the trade in spare capacity.

3.4 Opportunity for a market led capacity trading solution

The Australian domestic gas market is not a deep and mature market by international standards; it has only a limited number of participants and the volumes of gas traded are relatively small. As an immature market, there is a strong case for allowing the market to respond to issues and develop its own solutions. Intervention can only be supported if there is a clear case of market failure, and in that circumstance, by very carefully crafted responses.

The key risk faced by governments is that intervention seeks to move the market beyond its current level of maturity, and in doing so imposes costs on the market that may inhibit instead of support its further growth.



Given the expected limited market for pipeline capacity trading in the near to medium term, it seems unlikely that there will be sufficient demand to support a government-facilitated capacity trading market model. APA considers that there remains scope, however, for the market to provide niche products and solutions to address specific issues associated with capacity trading at a much lower cost than any government/regulatory model.

APA considers that a market-led response to capacity trading is likely to deliver the most efficient market outcome, particularly as demand for capacity trading is likely to be limited. There does not seem to be sufficient demand to support the development of centralised systems for capacity trading which, like other facilitated markets in place, would impose transaction and administrative costs on all gas market participants, regardless of whether they directly participate or benefit from the new market (as is the case, for example, with the STTM). A market-led solution would see transaction costs paid only by those that participate (and presumably benefit) from that market.

As mentioned earlier in this submission, APA is currently implementing a project to scope the requirements of both existing shippers and potential users of traded capacity to determine whether there are efficient and effective secondary capacity trading solutions that it could offer to the market. This involves detailed consultation with existing shippers and potential users of traded capacity of potential products and services.

This process will involve consideration of a number of alternatives for delivering the capability, and may involve a staged approach to implementation which delivers the appropriate scale of solution to meet demand for capacity trading services. This work is being supported by an external review of international markets, and will utilise the learnings from this process to influence any trading capability or platform that is developed.

A market-led response such as that currently under investigation by APA, will also be tailored to the needs of the market, and can be tailored to the needs of individual participants. To this end, APA is consulting with current and potential shippers on potential products and services that it may offer.

In contrast, a premature move by governments to intervene in the market by establishing facilitated capacity trading is very likely to foreclose options for a market-led solution, and lead to additional and unnecessary costs being imposed on the gas market, thereby inhibiting rather than supporting its growth.