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COAG Energy Council

By email to gas.environment.gov.au

Re: Measures to Improve Transparency in the Gas Market – ERM Power comments

Dear COAG Energy Council

About ERM Power

ERM Power (ERM) is an Australian energy company operating electricity sales, generation and energy solutions businesses. ERM has grown to become the second largest electricity provider to commercial businesses and industrials in Australia by load[1]. A growing range of energy solutions products and services are being delivered, including lighting and energy efficiency software and data analytics, to the company's existing and new customer base. The company operates 662 megawatts of low emission, gas-fired peaking power stations in Western Australia and Queensland. ERM operates across the east coast gas market in the states of Victoria, NSW and Queensland and is a market participant in the Victoria DWGM, the Sydney and Brisbane STTMs, the Gas Supply Hubs and the recently introduced capacity trading markets.

Comments on the RIS

ERM Power welcomes the COAG Energy Council's consideration of policy options to improve the transparency of the gas markets. In general, ERM Power supports arrangements that aim to promote a level playing field with respect to access to information about material factors that impact demand, supply and the price of gas. However, any requirement to disclose commercially sensitive information needs to be carefully considered to ensure that the benefits outweigh the commercial risks and other costs associated with that information disclosure.

ERM Power supports the recommendations contained in Option 3 of the Regulation Impact Statement (RIS), except for the proposal to publish details of short term bilateral gas trades. We believe that the risks associated with this proposal significantly outweigh any potential benefits.

Disclosure of commercially sensitive information may adversely impact trading and innovation

ERM believes that there is a risk that the proposal to require the reporting of short term bilateral trade details will result in the disclosure of commercially sensitive information. Even if data is aggregated before being published, we believe it will be possible in many instances to deduce the identities of parties to a trade, given the relatively small number of players (identities of whom are generally known) operating at each trading location or within a region.

If identities are able to be deduced, commercially sensitive information about a participant's trading position and its strategies will be revealed to its competitors. This can erode the ability of a participant to effectively execute its trading or optimisation strategies (especially if the information about a transaction is to be published before the transaction supply period has ended), and could lead to a reduction in short term trading. Incentives for participants to innovate or develop new ways to optimise their position, may also be diminished.

For example, assume that a participant decides to purchase some short term gas in Queensland over next year's winter period, with the intention to secure a locational swap and sell the gas to its southern state customers. The release of information about the gas transaction in the public domain may make it difficult for this participant to

[1] Based on ERM Power analysis of latest published financial information.

negotiate optimal commercial terms for the locational swap, given that sellers of such products (who are also this participant's competitors) may have formed views about the participant's intentions and maximum willingness to pay, based on the information the participant was required disclose. There is a risk that the participant will not be able to bring its trading strategy to execution or earn a margin commensurate with the risk it has taken. Disclosure of short term GSA information may therefore hinder the ability to close transactions and diminish trading activity.

Administrative costs associated with the reporting requirement may deter trading

The requirement to report details of short term transactions will also impose significant administrative costs on market participants. This may discourage short term trading. While the RIS indicates that an ACCC study found that only about 70 off-market trades were undertaken in Queensland during 2018, we believe that this figure underestimates the actual number of bilateral trades over this period, noting that over 2018, the number of short term off market trades undertaken by ERM alone was significantly higher than this number.[2]

ERM believes that low margin transactions undertaken to promote deal flow are less likely to occur with an added cost of regulatory reporting. Administrative costs may also discourage trading by smaller participants, commercial and industrial customers, or transactions managed by small consultants on behalf of end users, who may not have resources readily available to establish processes to comply with the reporting requirements.

ERM has also experienced situations where producers have indicated they are not interested in selling small quantities of gas due to the "paperwork" involved. A reporting requirement would only increase the administrative burden and could make it more difficult for users to secure short term gas.

Disclosure of GSA key terms is unlikely to result in material market benefits

ERM is unconvinced that the publication of short term GSA pricing and key terms will materially benefit the market.

At present there is a range of information available in the public domain to assist with short term price discovery. This includes the STTM, DWGM and GSH spot prices, ASX gas futures prices, JKM and Brent prices and price curves from brokers. The other gas transparency measures being contemplated under Option 3 of the RIS, such as the publication of information relating to gas production costs, LNG netback prices, and the pricing of transmission, compression and storage services, will also support price discovery.

ERM observes that since the commencement of the Queensland LNG export industry, liquidity in the short term trading markets has grown year on year. We have seen an increase in trading activity on the GSH, new virtual trade points established on major transmission pipelines facilitating physical spot trades, and more recently we have seen growth in the level of trading in ASX Victorian gas futures. The recent capacity trading reforms have also led to increased short term trading across the east coast gas grid. ERM is concerned that there is a risk that imposing a trade reporting requirement on market participants may unwind the liquidity that has been developed to date rather than enable the market's further development.

We are also concerned that a trade reporting requirement may encourage participants to transact and/or develop alternative product structures to avoid being covered by the reporting requirements. This would result in inefficiencies and create complexities.

It would be more beneficial to focus the reforms on other areas

In our experience, impediments to short term trading relate not to price discovery issues, but more to factors such as the following-

[2] Measures to Improve Transparency in the Gas Market – COAG Regulation Impact Statement - page 56

- Excessive pipeline transportation costs for variable use services (such as interruptible or as-available, or typically any other service with a term < 1 year), which at the rack rate charged by the pipelines tends to make any short term trade across locations uneconomic.

- Lack of competition on the supply side and unwillingness of producers to commit to forward sales when prices (e.g. Wallumbilla LNG netback) are low.

- Information asymmetry with respect to changes to the operational capacity of key facilities (production, transmission and LNG export facilities) that connect to the east coast gas grid.

[Paragraph removed – confidential]

Thank you for considering our comments.

Yours sincerely

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