



## Investigation Report

Incorrect STTM Allocation Data:  
Epic Energy's compliance with National Gas Rule 369

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## Summary

Epic Energy (**Epic**) submitted incorrect Short Term Trading Market (**STTM**) allocation data to the Australian Energy Market Operator (**AEMO**) for the Moomba to Adelaide Pipeline (**MAP**) on 90 occasions between November 2010 and October 2011. An error in Epic's formula to calculate gas deliveries led to the incorrect data.

The Australian Energy Regulator (**AER**) investigated Epic's conduct against the National Gas Rules (**Gas Rules**). Rule 369 requires information or data (including allocation data) be provided to AEMO in accordance with good gas industry practice. Rule 369 is a civil penalty provision, meaning the AER may serve an infringement notice.

Following its investigation, the AER has reason to believe that Epic breached rule 369 in respect of the preparation and submission of an allocation notice for the 24 October 2011 gas day which contained inaccurate data. The AER arrived at this view after determining that the formula error, which caused the provision of inaccurate data to AEMO, resulted from failures in Epic's IT governance, and review and testing processes.

The infringement notice was served on 1 June 2012. Epic paid the associated \$20,000 penalty on 18 June 2012. Payment is not an admission by Epic that it breached the rule.

# 1 Introduction

Section 27 of the National Gas Law (**Gas Law**) sets out functions and powers of the AER. These functions include:

- monitoring compliance with the Gas Law, the Regulations, and the Gas Rules
- investigating breaches or possible breaches of the Gas Law, the Regulations and the Gas Rules
- instituting and conducting proceedings in relation to breaches of provisions of the Gas Law, the Regulations, and the Gas Rules.

Further, section 277 of the Gas Law states the AER may serve an infringement notice on a person that the AER has reason to believe has breached a civil penalty provision.

STTMs are wholesale gas markets subject to Part 20 of the Gas Rules. They operate as “hubs” between transmission pipelines and distribution networks where gas can be sold and bought. The Adelaide STTM hub is located where gas on the MAP to the north of Adelaide and SEAGas pipeline to the east of Adelaide meets. Gas is sold and bought in Adelaide by Trading Participants who make offers and bids. Market prices and payments are determined on the basis of these offers and bids as well as on the basis of allocations of how much gas each participant flowed on a gas day.

As an allocation agent for the MAP, Epic is required each day to submit to AEMO an allocation notice in accordance with Gas Rule 419. The allocation notice must set out the amount of gas delivered by trading participants against registered facility services on the previous gas day. The delivery amounts are derived from daily meter measurements and from apportioning or allocating gas flows between trading participant offers and nominations of gas flows to and from the Adelaide hub. AEMO uses this allocation data to calculate prices and payments in the STTM, which trading participants are then subject to.

This report relates to the AER’s investigation into Epic’s preparation and submission of incorrect allocation data for MAP to AEMO. These events occurred on 90 gas days between November 2010 and October 2011.

This report:

- describes the matter (section 2)
- outlines the AER's compliance assessment (section 3)
- outlines the AER's enforcement response (section 4)

## 2 Description of the matter

On 28 October 2011, Epic notified the AER it had submitted incorrect STTM allocation data to AEMO for the MAP on 90 occasions between November 2010 and October 2011. The incorrect data was a result of an error in Epic's formula to calculate forward haul gas deliveries. Epic originally identified an issue in September 2011 as a result of concerns about missing line-pack. It confirmed the cause of the problem in October.

The formula error meant quantities of gas backhauled out of the Adelaide hub were not taken into account when calculating the quantities of gas delivered to the hub. This led to market outcomes on gas days where backhaul services were used being incorrect. The following example provided by Epic illustrates the nature of the formula error:

On a day, 100GJ is scheduled to flow to the hub (forward haul), and 10GJ is scheduled to flow from the hub (backhaul). After the day, 95GJ of gas is metered as having been physically delivered to the hub. The allocation for that day should be 105GJ of forward haul (being the 95 GJ which was metered, plus 10GJ of backhaul), and 10GJ of backhaul. However, Epic Energy's allocation formula for forward haul does not take the backhaul into account, therefore the allocation is 95GJ of forward haul (being the metered quantity only), and 10GJ of backhaul.

Reflecting this example and other information provided by Epic, the AER has found that:

- Epic understated actual deliveries to the Adelaide hub on 90 gas days. In the example above, ex post prices in the Adelaide hub should have been set on the basis of 105 GJ delivered to the hub (against 10 GJ of backhaul). The error meant prices were set on the basis of 95 GJ delivered to the hub.
- Epic's error on forward haulage calculation had an equivalent impact on Market Operator Service (**MOS**) quantities on the 90 gas days<sup>1</sup>. In the above example,

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<sup>1</sup> MOS is the difference between what was scheduled by the pipeline operator (to or from the hub) for a gas day and what gas was actually delivered on that gas day as measured by a physical meter. Since actual consumption in the hub will differ from forecast, there will usually be a difference

because of the forward haulage miscalculation, the MOS calculation was also incorrect by 10 GJ.

*Impact of error*

AEMO has received corrected allocation data from Epic so as to resettle gas volumes for billing periods affected by the error. It is continuing an administrative process of revising monthly billing period statements to account for revised volumes in accordance with the 9 month post settlement revision processes.<sup>2</sup> However, not all incorrect financial outcomes can be corrected through this revision. Ex post price effects on 40 gas days cannot be corrected because that price cannot be revised under the Gas Rules. Fortunately, ex post price errors are of relatively small financial impact (tens of thousands of dollars), compared to the more significant MOS errors.

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between what was scheduled and what was physically delivered. In the above example provided by Epic this amount is 5 GJ, being the difference between net scheduled (90 GJ) and physical delivery (95GJ)—in this example, demand in the hub must have been higher than forecast. Notably, because Epic misallocated flow to the hub by 10 GJ it follows that it would have submitted -5GJ of MOS to AEMO instead of +5 GJ of MOS—an error of 10 GJ magnitude.

<sup>2</sup> Gas Rule 473.



### 3 Compliance assessment

Rule 369 provides:

A person required by a provision of this Part or the STTM Procedures to give information or data to AEMO must:

- (a) prepare and submit that information or data; and
- (b) if applicable, maintain any equipment from which that information or data is derived,

in accordance with good gas industry practice

Rule 419(1) concerns the submission of information or data. It requires allocation agents for STTM facilities to give AEMO an allocation notice no later than 4.5 hours after the start of each gas day for the immediately preceding gas day:

No later than 4.5 hours after the start of each gas day, the allocation agent for an STTM facility must give AEMO an allocation notice for the immediately preceding gas day that meets the requirements in subrule (2).

Epic is an allocation agent for the MAP (an STTM facility). Accordingly, it must submit an allocation notice (allocation data) each gas day and is subject to rule 369 GGIP requirement in relation to preparing and submitting the data.

GGIP is unique to Part 20 of the STTM rules and provides a standard in respect of information-providing obligations. GGIP is defined in rule 364 as:

the practices, methods and acts that would be reasonably expected from experienced and competent persons engaged in the business of providing natural gas services in Australia, acting with all due skill, diligence, prudence and foresight and in compliance with all applicable legislation (including these rules), authorisations and industry codes of practice.

#### 3.1 The AER's framework for assessing good practice

The AER's approach to assessing GGIP in monitoring businesses' compliance with the requirements of Part 20 is based around principles of Good Energy Industry Practice (**GEIP**). The AER considers the following factors in assessing whether GGIP has been satisfied:

- **Governance**—participants’ internal arrangements covering reporting lines and supporting systems; and the overall compliance culture, including levels of involvement and commitment of senior managers and committees.
- **Expertise**—the human resources dedicated to technical compliance, including the allocation of responsibilities; underlying knowledge systems; and the nature and extent of the technical understanding of applicable obligations.
- **Implementation**—the practical means by which participants drive and promote compliance through internal procedures and processes, encompassing staff training, technical testing, internal reviews and audits, and reporting of compliance matters.
- **Performance**—the overall compliance status of a participant in regard to the effectiveness of compliance programs and arrangements, including ongoing evaluation and updating of programs, and arrangements to reflect lessons learnt.

These GEIP factors have been presented in several AER quarterly compliance reports (QCR)<sup>3</sup>.

## 3.2 Epic’s conduct

To assist its investigation, the AER analysed Epic’s conduct in the context of the above GEIP factors. During this process Epic provided extensive information in response to the AER’s requests.

### **Governance**

In February 2012 Epic informed the AER that it assembled a large ‘STTM project implementation team’ during its STTM preparation and testing between May 2009 and September 2010. Epic outlined the various staff involved in the team and their respective roles. Working alongside the STTM project implementation team was a separate team focussed on implementing changes to the Customer Reporting System (CRS) to accommodate the STTM. The method for calculating facility allocations

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<sup>3</sup> AER, QCR (Oct-Dec 2010, Jan-Mar 2011, July-Sep 2011), <http://www.aer.gov.au/node/454>

was initially communicated from the STTM project implementation team to the CRS team. Communication between both teams was facilitated by a single staff member in each team.

In regard to the facility allocation process, where the formula error occurred, Epic indicated internal communications involved only one person from each of the STTM and CRS teams, both of whom had left the organisation. In March 2012, the AER requested further information about the change management process at the time the error occurred. Epic confirmed the error was coded in systems in May 2010, prior to the commencement of the STTM trial and before new governance arrangements began in December 2011.

In considering the information provided by Epic, the AER found:

- Epic did not supply documentation to support that an adequate change management control process existed at the date the formula error was introduced into systems (May 2010)
- documentation to show incorporation of STTM requirements post May 2010 is difficult to follow and does not identify the specific process required for forward haul calculation. It also does not refer to the relevant STTM rule requirements.
- the status of certain change management documentation is unclear

Epic informed the AER on 30 March 2012 that its new change process (effective from December 2011) involves:

- a formal change management procedure, including documented roles and responsibilities
- a physical register of forms, to assist with tracking
- a requirement to complete a close out process
- the reinstatement of the CRS working group to allow a forum for review.

The AER is of the view that the governance process Epic had in place at the time of the formula error lacked the prudence or diligence expected of experienced and competent persons in accordance with the GGIP definition. If more staff had reviewed the implementation of STTM changes, which may have been facilitated through better documentation, this would have increased the chance of someone detecting the formula error. Epic appears to have recognised these deficiencies by implementing a new change management process.

### **Expertise**

Epic outlined the staff involved in establishing and maintaining the relevant formulas for its STTM systems, noting their experience and qualifications. Key staff members had at least 10 years experience in their respective roles, and were aware of the obligations under the Gas Rules.

The AER is of the view that Epic's staff were appropriately trained and had the necessary technical skills to perform their roles competently.

### **Implementation**

Epic explained that during its STTM preparation and testing phase prior to September 2010, only forward haul services were provided to the Adelaide hub. Contracts for backhaul services were completed after the commencement of the STTM, which Epic claimed limited the ability of Epic to test its systems with backhaul, resulting in the formula error not being identified earlier.

The AER considers that Epic did not take steps to ascertain the correctness of the formula at relevant stages post market start. For example, it may have done so when it first allocated backhaul gas in November 2010 and also when it formally documented STTM processes in April 2011. These occasions presented opportunities for Epic to discover the error.

The AER considers Epic's conduct in preparing and submitting erroneous data does not demonstrate satisfactory implementation practice. An experienced and competent provider would be expected to more rigorously and exhaustively test its formulas and IT systems prior to a substantial new responsibility commencing. The AER would

have expected Epic to review its operations and outcomes closely when it began providing a backhaul service and when it documented its STTM processes.

## **Performance**

As discussed, the GEIP factor of ‘performance’ relates in part to the overall compliance status of a participant with regard to the effectiveness of its compliance programs and arrangements.

The AER considers Epic’s submission of incorrect allocation data on 90 gas days is a significant and adverse indicator of the standard of Epic’s performance.

While the formula error was identified by Epic and has since been rectified, the error occurred on 90 gas days over an 11 month period. The AER considers the delay in identifying the error also reflects a level of performance not in accordance with good gas industry practice.

## **AER assessment**

The submission of incorrect allocation data does not in itself establish that Epic’s conduct is of less than good gas industry practice. Even the best and most competent organisations can make mistakes.

That is not to say the occurrence of errors has no part in determining whether Epic’s conduct was in accordance with good gas industry practice. Rather, the occurrence of errors should be considered alongside other relevant factors.

It was necessary for the AER to look at the cause of the errors and the reason they were undetected to determine whether Epic’s conduct was in accordance with good gas industry practice.

## 4 The AER's enforcement response

Following its assessment, the AER had reason to believe Epic's conduct was not in accordance with GGIP. The factors AER has regard to when deciding whether to take formal enforcement action are set out in its *Compliance and Enforcement – Statement of Approach*.<sup>4</sup> These factors include:

- the nature and extent of the conduct that forms the breach
- the amount of loss or damage caused
- the circumstances in which the breach took place
- whether the breach was deliberate, and the period over which it extended
- whether the breach arose out of the conduct of senior management or at a lower level
- whether the participant has a corporate culture conducive to compliance
- whether the participant has cooperated with the AER in relation to the breach
- whether the breach forms part of a sustained pattern of non-compliance

As noted, Gas Rule 369 is a civil penalty provision. Section 277 of the Gas Law states the AER may serve an infringement notice on a person the AER has reason to believe has breached a civil penalty provision.

Having regard to all of the above factors, the AER decided to serve an infringement notice for the incorrect allocation data submitted to AEMO for the 24 October 2011 gas day.

The infringement notice was served on 1 June 2012. Epic paid the associated \$20,000 penalty on 18 June 2012.

In accordance with section 285 of the Gas Law, the payment of the infringement notice is not an admission by Epic of the breach or an admission of liability. Pursuant

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<sup>4</sup> AER, *Compliance and Enforcement Statement of Approach*, <http://www.aer.gov.au/node/454>

to section 284 of the Gas Law, the AER will not commence proceedings against Epic in respect of the conduct to which the infringement notice relates, now that Epic has paid the \$20,000 penalty.