



## Bidding in good faith

### Options paper released for consultation

**The Australian Energy Market Commission has prepared an options paper to facilitate consultation on a rule change request proposing changes to the provisions in the National Electricity Rules that govern the manner in which generators may offer electricity to the wholesale market.**

#### The options paper

The purpose of the options paper is to discuss the outcomes of analysis undertaken for the Commission, to test stakeholders' views on a number of potential options identified to address the rule change request, and to continue the assessment of the proposed rule.

The rules that relate to the generator bidding process are fundamental to the operation of the National Electricity Market (NEM) and the promotion of efficient price outcomes in the interests of consumers, and changes to these rules have the potential to significantly affect participants. As a consequence, the Commission considers that there is value in adding an extra stage of consultation with stakeholders to the normal rule change process prior to the publication of the draft determination.

#### The rule change request

Participation in the NEM requires that generators submit bids to the Australian Energy Market Operator (AEMO) specifying the minimum price they are willing to receive for the generation volume offered. Following the submission of initial bids, generators may submit rebids to shift volume to different prices to allow for changing market conditions.

The National Electricity Rules (NER) require that generators make all bids and rebids in good faith. At the time of making the bid, the generator must have a genuine intention to honour that bid if the material conditions and circumstances upon which the bid is based remain unchanged.

The rule change request was submitted by the South Australian Minister for Mineral Resources and Energy following the Federal Court decision handed down in August 2011 between the AER and Stanwell Corporation. The rule change proponent considers that the current good faith provisions face practical enforcement limitations and has proposed changes intended to provide greater clarity on the meaning of bidding in good faith in the NEM.

#### Defining the issues raised in the rule change request

The ability to rebid provides generators with necessary flexibility to adjust their position to accommodate changes in market conditions and to respond to the offers of other generators. In this way, rebidding drives competitive outcomes that reveal prices reflective of underlying demand and supply conditions, leading to efficient operation and investment in the long-term interests of consumers.

However, the rebidding process can also compromise the ability of the market to arrive at an efficient outcome when rebids are made close to real time. This is because other market participants may still have an incentive to respond but do not have sufficient time to undertake the necessary rebid prior to generation occurring.

Late rebidding has the potential to result in inefficient price outcomes if high price plant is dispatched ahead of lower price plant that does not have sufficient time to respond by changing output to meet its generation targets. The efficacy of the rebidding process may be further impacted over time if late rebidding is part of a strategy of behaviour that is aimed at misleading competitors and promoting false expectations.

## Materiality of the issues identified

While the NEM has maintained the same broad market design since commencement, an assessment undertaken for the AEMC suggests that the more widespread occurrence of late rebidding has been a recent phenomenon, occurring within the last two years and predominantly in Queensland and to some extent in South Australia.

Although late rebidding quite often has a role to play in responding to price spikes in pre-dispatch forecasts and reducing anticipated market volatility, the recent late bidding behaviour in Queensland has resulted in price spikes, specifically towards the end of 30-minute trading intervals.

The recent prevalence of late rebidding may have contributed to a reduction in the amount of demand and supply-side response that is available by making it difficult to predict or foresee with an acceptable level of accuracy when a period of sufficiently high price to warrant a response is likely to occur.

## Potential options for consideration

While the Commission notes that the issues raised by the rule change request have manifested themselves recently and only in particular regions of the NEM, the design of the market framework should set reasonable boundaries on the ability of participants to influence price outcomes that are to the detriment of other participants and that are not reflective of an efficient functioning market.

The fundamental importance of this issue to the functioning of the market has led the Commission to conclude that there would be merit in considering a broad range of options that have the potential to contribute to the achievement of the National Electricity Objective (NEO), in addition to the proposed changes to the good faith bidding provisions.

The Commission is consequently considering two broad sets of options that may form the basis of an appropriate regulatory response to these issues. These are:

- the design of a behavioural statement of conduct, similar to the good faith bidding provisions; and
- the design of the market and the bidding process, including potential restrictions on rebidding close to real time.

Behavioural statements of conduct focus on the intentions of the rebidding generator and act as a guide to appropriate market behaviour. In addition to the proposed rule, the Commission has identified a number of alternative options for a behavioural statement of conduct, including changing the design of the good faith provisions, or developing a different behavioural statement of conduct to address the bidding and rebidding strategies that have been identified to be of some concern. While potentially challenging to design, the exact structure of a statement of conduct would play a key role in the enforceability of the provisions in preventing the specific adverse behaviour.

Placing restrictions on rebidding close to real time recognises that inefficient market outcomes may arise regardless of generator intentions. Providing certainty in this way would assist in mitigating the issues of non-responsiveness that result from the current deadline immediately before generation occurs by allowing both demand and supply-side participants time to adjust their physical positions.

Rebidding restrictions are a common feature of electricity markets in a number of overseas jurisdictions. The design of such regulations may be used to inform the development of similar regulations in the NEM.

The Commission considers that these two sets of options are not mutually exclusive and the appropriate solution to the issues raised by the rule change request may involve elements of both. The Commission welcomes submissions by 12 February 2015.

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