

27th October 2015

Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

Submission lodged online at: www.aemc.gov.au

Project Number: ERC0166

Dear Mr Pierce

Bidding in Good Faith Rule 2015 – Second Draft Rule Determination

Snowy Hydro appreciates the opportunity to comment on the Second Draft Rule Determination.

Through-out the consultation process it has been acknowledged that rebidding is required to optimise the economic benefit of market operations. It is clear through the AEMC's own analysis that rebidding supports efficient price discovery. By discouraging rebidding, price discovery will be adversely affected and disproportionately impact flexible scheduled generators. This is perverse as flexible load following plant should be rewarded and incentivised to operate as flexibly as possible in a macro environment where the NEM will experience more variability in supply and demand due to a range of exogenous factors including wind/solar/demand response/climate change policies.

The AEMC recognises that structural issues in one NEM region could be the root cause for re-examining the good faith bidding provisions in 3.8.22A. It remains our view that amending the Rules would be an inefficient and inappropriate means to address a localised structural issue.

Any changes that limit rebidding would undermine the efficiency of the central dispatch mechanism. We are therefore very concerned that the second draft determination still has a significant degree of uncertainty for Market Participants. The uncertainty created from the interpretation of the second draft rule is not good regulatory practice and undermines confidence in operating in the NEM. Uncertainty in the application of Rules also creates a risk premium which will be passed on to consumers.

The AEMC is contemplating introducing a requirement for Market Participants to make a contemporaneous record of circumstances in relation to a rebid during the late rebid period. We believe these late rebid reports would place an onerous compliance burden on Participants ultimately increasing costs with no commensurate benefit and ultimately does not advance the National Electricity Objective.

Issues with the behavioural statement

The current provisions only require a generator to act in good faith at the time of making a bid/rebid. 3.8.22A(d) places an obligation on a generator to change their bid “as soon as practicable” after the Market Participant becomes aware of the change in material conditions and circumstances on the basis of which it decides to vary its dispatch offer. This would prohibit a generator deliberately sitting on a rebid.

In addition to 3.8.22A(d), sub-section (e) states:

“...in determining whether the Generator or Market Participant made a rebid as soon as practicable, a court must have regard to:

(1) the market design principle set out in clause 3.1.4(a)(2); and

*(2) whether the rebid was made in **sufficient time to allow reasonable opportunity for other Market Participants to respond** (including by making responsive rebids, by bringing one or more generating units into operation or increasing or decreasing the loading level of any generating units, or by adjusting the loading level of any load) prior to:”*

Snowy Hydro argues that sub-section (e)(2) is not required once a generator has an obligation under sub-section (d) to rebid as soon as practicable. In fact sub-section (e) creates a **conflicting obligation** where a scheduled Market Participant contravenes 3.8.22A(d) by not making a rebid as soon as practicable because of concern with breaching 3.8.22A(e)(2). That is, how would a generator respond if they have formed a view a rebid is necessary, but one or more Market Participants would not be able to respond if a rebid was lodged. Further to this an internal assessment of a competitors respond capability would be highly uncertain and therefore a decision not to rebid would be made on very subjective grounds. We advocate deleting 3.8.22A(e)(2).

Additional regulation of late rebidding

In deciding whether additional regulation is required on rebids that occur close to dispatch, the AEMC characterises this issue as a consideration of the trade-off between¹:

- *the promotion of an iterative process of price discovery and the flexibility of the market to respond to changing market conditions; and*
- *limiting the ability of participant rebids to disproportionately influence price outcomes close to dispatch.*

Snowy Hydro disagrees that these are two competing drivers of market efficiency on the basis that:

- The ability to rebid is an essential part of an efficient NEM as it promotes the process of price discovery. This is supported by academia experts such as Professor George Yarrow and is evidenced in analysis on rebidding by Roam Consulting and AEMO.
- There is no robust analysis on rebids disproportionately influencing price outcomes close to dispatch. We believe the Ernst & Young analysis has many acknowledged limitations² such as

¹ AEMC Second Draft Determination, page 54

² Ernst & Young, Impact of late rebidding on the contract market, page 9

“price movements may reflect a **variety of factors related to the expectation** of future wholesale outcomes. This may therefore cloud the analysis of the impact of late rebidding on contract prices.”

Hence, this “trade-off” should be firmly biased towards the promotion of an iterative process of price discovery and the flexibility of the market to respond to changing market conditions. In an iterative price discovery process it is natural for there to be more rebids closer to dispatch as more ‘firm’ information becomes available and the fulfilment or non-fulfilment of subjective expectations are confirmed.

Contemporaneous records of rebids during the late rebidding period is not required

Snowy Hydro does not support the requirement to make a contemporaneous record in relation to a rebid made during or with less than 15 minutes before the commencement of the trading interval. We disagree with the AEMC’s view that³:

“..., this may be less onerous than reporting to the AER on all late rebids.”

We believe practically there is no difference in the extra administrative burden on all Market Participants who rebid within the late rebidding period under the Draft and Second Draft Determinations. The fact is Spot Traders would need to consider the trade-off between the necessity of the rebid and the requirement to prepare a contemporaneous record setting out the material conditions and circumstances giving rise to the rebid. We expect this compliance burden will result in more conservative rebidding and limit the ability of generators to respond to dynamic and changing market conditions. This would be inconsistent with the National Electricity Objective.

The compliance burden of making a contemporaneous record during the late rebid period will be very high. Table 1 shows that the new recording requirement would result, on average, in 81 records being produced every day.

Rebidding within 15 minutes	Total		Daily Average	
	2014	2015	2014	2015
Snowy Hydro	1,479	494	4	5
All Generators	24,122	8,601	66	81

Table 1.

On a volatile day such as 21/02/2014 there were 392 instances of rebidding during the late rebid period for all Dispatchable Unit IDs (DUIDs) during the day. This illustrates the larger compliance burden for Market Participants compared to the requirements in the current Rules.

We expect this compliance burden will result in more conservative rebidding as Spot Traders limit rebidding during the late rebid period even though the rebid would have been more efficient for the NEM.

The AEMC has assumed the only cost of implementing the Second Draft Rule is in compliance costs, which would include systems costs for generators. In total the Commission estimate the cost will be \$4 to \$6 million and consider this proportionate to the problem. Snowy Hydro disagrees with this assessment of costs associated with the second draft rule.

³ AEMC Second Draft Determination, page 60

There is no accounting for unintended consequences, such as restricting rebidding close to dispatch which would not have been false or misleading, but was not undertaken for fear of penalties. This could reduce the efficiency of the price discovery process. If we consider the Draft Determination to be a filter of misdemeanours, the AEMC is expecting it to be 100% successful in filtering out the misdemeanours. This expectation is simple unrealistic.

By more heavily regulating the changing of offers, the Rule is likely to reduce the number of efficient rebids. It appears the AEMC discounts the benefit of the quantity of rebidding, especially close to dispatch, assisting in price discovery and efficient signals. This restriction while difficult to quantify would be worth hundreds of millions per annum given that the available evidence to date concludes that unrestricted rebidding enhances market efficiency.

In summary, proposed rule clause 3.8.22 (ca) should be removed. The requirement to make a contemporaneous record for late rebids will effectively restrict responsiveness of flexible scheduled generators and loads to provide load following services by increasing costs and risks of punitive action. This appears to be a conscious attempt to impose a “brake” on responding to dynamic market conditions. Costs will increase (from administrative burden and less efficient outcomes) which will to some extent be passed to consumers.

The AER already have powers under the existing Rules, clause 3.8.22(c)(3) to request “...such additional information .. for a rebid .. from time to time”. Under the AER’s existing information collection powers they can specifically target rebids which are peculiar.

Good regulatory practice

In section 4.5.3 Rebidding as soon as practicable, the AEMC have made a number of statements which are concerning. For instance:

and that it is ultimately a matter for the court to determine whether or not the time taken to make a rebid was reasonable. (page 52)

and

The Commission notes the extent to which the behavioural statement is enforceable and effective in deterring adverse behaviour will be determined largely by a court’s interpretation of the participant’s actions. (page 52)

These statements highlight to Market Participants the ambiguity and uncertainty in the proposed draft Rule changes. We believe it is not good regulatory practice for the AEMC as the energy market legislator to enact Rules which lack sufficient clarity such that the Court’s interpretation would ultimately be required to determine compliance with the Rule. It would be disappointing if the AEMC abdicates its responsibility to develop clear and concise Rules. This lack of clarity on the draft Rules only serves to increase Market Participant’s risk profile in rebids, will impede the current efficient iterative price discovery process, and hence does not advance the National Electricity Objective.

Summary

On balance available evidence suggests unfettered bidding results in efficient outcomes (ROAM's analysis to the Draft Rule Determination and AEMO's analysis where the actual data from the last two dispatch intervals was replaced with the average of the first four dispatch intervals).

The existing Rule assumes an offer was in good faith unless proven not so (by inference from data, evidence). To remove this presumption and to increase the propensity for a court to infer an offer was false, misleading or likely to mislead, would suggest that the AEMC believes it efficient to restrict, in volume terms, the changing of offers close to dispatch. Additionally the requirement for a contemporaneous record of rebids made during the late rebid period would have the effect of further restricting the changing of offers close to dispatch. Without unambiguous evidence that change is required we firmly believe that the second draft rule would not advance the National Electricity Objective and hence needs significant moderation to limit any adverse impact on the NEM.

Snowy Hydro appreciates the opportunity to respond to this Second Draft Determination. Should you have any enquires to this submission contact Kevin Ly, Head of Wholesale Regulation on kevin.ly@snowyhydro.com.au or on (02) 9278 1888.

Yours sincerely,



Roger Whitby

Executive Officer, Trading