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13MMRE/0505

Mr John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
SYDNEY SOUTH NSW 1235

Dear Mr Pierce

A handwritten signature in black ink, appearing to read "John", written over the typed name "John" in the salutation.

Proposed Rule Change – Bidding in Good Faith

The South Australian Government proposes a Rule change under Section 91 of the *National Electricity Law* (NEL) relating to the Bidding in Good Faith provisions of the National Electricity Rules (the Rules). This proposal would effect a change to components of Chapter 3 of the Rules.

On the 30 August 2011, the Federal Court of Australia handed down a decision that the South Australian Government believes provides precedent for the future interpretation and operation of the bidding in good faith provisions contained in Section 3.8.22A of the Rules.

There is concern that the decision will result in generators operating in a manner that originally led to the good faith amendments to the bidding provisions. At that time, generators used the bidding provisions to undertake late strategic reductions in capacity (or offer price) when other participants were unable to effectively respond. This practice gives rise to inefficiencies, which leads to high prices, or in some instances negative prices, in the National Electricity Market (NEM).

In response to this behaviour, in July 2002, NEM Ministers indicated as a matter of policy that they opposed generator bidding and rebidding strategies that were inconsistent with an efficient, competitive and reliable market, such as those not made in good faith, the blatant economic withdrawal of generation and the gaming of technical constraints.

Following the Federal Court decision in August 2011, South Australia became concerned that the decision undermined the existing good faith provisions which seek to ensure that Market Participants are provided with accurate market information ahead of time, which is a fundamental element to the successful operation of the NEM.

The South Australian Government considers that the Federal Court decision has introduced uncertainty around the operation of the bidding in good faith provisions and highlighted issues in relation to the implementation of the policy intent.

The attached Rule change proposal aims to strengthen the current regulatory framework through providing greater clarity to generators and market participants regarding the meaning of bidding and rebidding in good faith to ensure generator bidding and rebidding practices are consistent with an efficient, competitive and reliable market.

Should you have any questions in relation to this proposal, please contact Ms Rebecca Knights, Director – Energy Markets, Energy Markets and Programs Division on (08) 8266 5500.

Yours sincerely



Hon Tom Koutsantonis MP
Minister for Mineral Resources and Energy

13 November 2013

Encl Rule Change Request – Bidding in Good Faith Provisions

Rule Change Request

Bidding in Good Faith Provisions

November 2013

Background and Context

From the commencement of the National Electricity Market (NEM) it has been recognised that rebidding is an essential element of the NEM design. Generators have physical characteristics relevant to the NEM design, including start-up time limitations and, for many fossil-fuel generators, minimum load requirements. There is also a risk of a generator having a technical fault which results in plant no longer being available. Accordingly, generators require the flexibility to adjust their positions to accommodate unexpected changes in demand patterns and plant availability. It is for this reason that the NEM design included provision for a generator to rebid.

However, whilst the NEM design needs to clearly provide for the flexibility to rebid, another key element of the NEM design is the need for pre-dispatch forecasts which can be relied upon by market participants including generators, transmission network service providers and customers. As generators are required to self-commit and have the physical characteristics discussed above, pre-dispatch forecasts are essential for generators to determine whether to be online.

NEM customers also rely on pre-dispatch forecasts to manage their pricing risk. Pre-dispatch forecasts assist customers to determine whether they need to consider forward contracting or to prepare for demand side response. The market operator also relies on pre-dispatch forecasts for its reliability forecasts. If rebids alter the availability of generation, it directly impacts the reliability forecasts that the market operator produces. The market operator may be required to intervene in the market to recall transmission lines or generation for system reliability and security. These actions have an associated cost.

The importance of reliable pre-dispatch information and the need to respond to others' behaviour gives rise to an important feature of the bidding provisions, the requirement for bids and rebids to be made in good faith.

This requirement attempts to provide market participants that rely on pre-dispatch forecasts with some assurance that generators intend to honour their bids. The concept of good faith was intended to improve the reliability of pre-dispatch forecast prices.

At the time the proposed addition of good faith was being considered, there was considerable discussion surrounding whether the term needed to be precisely defined. In its 2002 draft determination which considered the good faith proposal, the Australian Competition and Consumer Commission (ACCC) encouraged the then National Electricity Code Administrator (NECA) to develop a clear definition as to what behaviour constitutes bidding in good faith to avoid problems of uncertainty.

Accordingly, the rebidding provisions include a definition of the term good faith as the market participant's genuine intentions. It was considered that genuine intentions more effectively and precisely described the conduct sought to be prohibited and therefore reduced uncertainty.

The purpose of the bidding in good faith provisions are therefore:

- to provide generators with the flexibility necessary to adjust their positions to accommodate unexpected changes in the market, including network constraints, changes in demand and changes in plant availability; and
- to provide market participants that rely on pre-dispatch forecasts, including generators, customers, transmission network service providers and the Australian Energy Market Operator (AEMO), with some assurance that generators intend to honour their bids.

Dissatisfaction of either of these impedes on the functionality and efficiency of the competitive market, and any inappropriate generator rebidding behaviour has negative implications on the second purpose.

The bidding in good faith provisions are recognised as significant provisions in the National Electricity Rules (the Rules) and, in recognition that a generator could achieve significant financial gain from non-compliance with the bidding in good faith provisions, these provisions attract the 'D' class penalty, which is a penalty not exceeding \$1 million and \$50,000 each day the breach continues.

On the 30 August 2011, the Hon Justice Dowsett of the Federal Court of Australia handed down a decision that provides precedent for the future interpretation and operation of the bidding in good faith provisions contained in Section 3.8.22A of the Rules.

The South Australian Government considers that the Federal Court decision has introduced uncertainty around the operation of the bidding in good faith provisions and highlighted issues in relation to the implementation of the policy intent. This Rule Change proposal seeks to address implementation issues regarding the bidding in good faith provisions.

There is concern that the Federal Court's decision will result in generators operating in a manner that originally led to the good faith amendments to the bidding provisions. At that time, generators used the bidding provisions to undertake late strategic reductions in capacity (or offer price) when other participants were unable to effectively respond. This practice gives rise to inefficiencies, which leads to high prices, or in some instances negative prices, in the NEM.

In response to this behaviour, in July 2002, NEM Ministers indicated as a matter of policy that they opposed generator bidding and rebidding strategies that were inconsistent with an efficient, competitive and reliable market, such as those not made in good faith, the blatant economic withdrawal of generation and the gaming of technical constraints.

Following the Federal Court decision in August 2011, South Australia became concerned that the decision undermined the existing good faith provisions which seek to ensure that Market Participants are provided with accurate market information ahead of time, which is a fundamental element to the successful operation of the NEM. The Federal Court decision may provide a precedent for the future interpretation and operation of the bidding provisions. The key findings in relation to section 3.8.22A of the Rules were as follows:

- The AER would need to prove that a trader did not have the subjective intention that a rebid be honoured at the time it was made to establish an absence of good faith;
- A trader turning their mind to the possibility of making a rebid if their objectives are not achieved does not show an absence of good faith;
- A subsequent rebid for the same Trading Interval, or part therefore, does not lead to the conclusion that the relevant trader did not intend to honour a bid;
- An examination of the totality of relevant conditions and circumstances upon which a rebid is based is required rather than focusing on individual elements.
- A change in the dispatch price (even if that change is caused by the generator's own bidding) and a constant dispatch price could be considered a change in circumstances;
- A rebid might, itself, have constituted a change in the conditions and circumstances in which it was made, or upon which it was based.
- The court did not consider extrinsic material, emphasising the desirability of persons being able to rely on the ordinary meaning of a clause and not having to review extrinsic material to determine its meaning.

Finally, to emphasise the importance these generator practices have on prices, we refer to two reports – a special report by the AER on *“The impact of congestion on bidding and inter-regional trade in the NEM”* released in December 2012, and a December 2001 report commissioned by the ACCC titled *“A Review of Generators’ Bidding and Rebidding Practices in the National Electricity Market”*. The purpose of this review was to assist the ACCC in evaluating changes to the market Rules proposed by NECA.

The AER special report provides examples of how generators have responded during periods of congestion on the transmission network. The analysis shows that the prevalence of congestion can be increased through generator rebidding (disorderly bidding). This response by generators has led to inefficiencies, price volatility and has reduced the ability for market participants to manage risks between regions. The AER states that they have observed an increase in the prevalence of disorderly bidding associated with network congestion in the past three years.¹ The report focusses on recent congestion events in New South Wales, Queensland and Victoria.

When a constraint binds, the National Electricity Market Dispatch Engine (NEMDE) dispatches constrained generators out of merit order, therefore dispatch may not be economic as some high priced capacity may be dispatched in preference to low priced capacity. AEMO's published information enables generators to identify the likely impact of forecast constraints on their plant. Generators that are forecast to be constrained have an incentive to rebid their capacity in order to limit the impact of a binding constraint on their dispatch outcomes.

¹ AER, *The impact of congestion on bidding and inter-regional trade in the NEM – Special Report*, December 2012, p 21.

Disorderly bidding in these instances can initially lead to spot prices significantly higher than forecast, with some peaking generators having insufficient time to react to ensure they are dispatched to cover their contractual obligations, and then the price can fall significantly.² The AER report gives recent examples of disorderly bidding as a result of network congestion that have resulted in significant counter-price flows between Victoria and New South Wales on 20 occasions since December 2009. Examples are also provided of 24 events since September 2011 in the Gladstone region where congestion and disorderly bidding led to more than \$150,000 in negative settlement residues into New South Wales.³

The ACCC review focused on 34 events in the NEM regions where bidding and rebidding appeared to be major contributors to high prices and found that the bidding and rebidding behaviour of generators was always a factor in generating high prices – even though a physical event was the initiating cause. The report concluded that while physical withholding of capacity still occurred in South Australia, Queensland and New South Wales at that time, “economic withholding of capacity (by bidding part capacity at very high prices) has become the most common form of capacity withholding to create artificial price spikes unrelated to market dynamics or underlying cost structures”. In addition, the review concluded that while in some of the events analysed there was a change to market conditions such as generator or interconnector failure or limitations which initiated the rebidding behaviour, the major cause of the price spikes was largely attributable to generator bidding and rebidding practices.⁴

The South Australian Government requests that the Australian Energy Market Commission (AEMC) progress the Rule Change proposal in accordance with the Rule making process under the National Electricity Law (NEL). South Australia recognises that in considering the Rule change proposal the AEMC must consult widely and may decide to modify the proposed Rules to more efficiently and effectively meet the National Electricity Objective (NEO).

The following information is provided in support of the Rule change request.

² AER, *The impact of congestion on bidding and inter-regional trade in the NEM*, p 6/7.

³ AER, *The impact of congestion on bidding and inter-regional trade in the NEM*, p 12 and 17.

⁴ *Amendments to the National Electricity Code - Changes to bidding and rebidding rules*, 3 July 2002, p 78.

Rule change request

1. Proponent of the Rule change

The Hon Tom Koutsantonis MP
South Australian Minister for Energy
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ADELAIDE SA 5000

2. Description of Proposed Rule

The proposed Rule changes seek to address the current implementation issues regarding the bidding in good faith provisions.

The South Australian Government considers that the proposed Rule change will provide market participants with greater confidence in relation to the reliability and accuracy of pre-dispatch forecasts, thereby aiding competitive demand and supply side response. This is achieved by providing greater clarification around when a dispatch offer, dispatch bid or rebid will be considered to be made in good faith, in particular requiring:

- all existing material circumstances to be taken into account when a dispatch offer, dispatch bid or rebid is made; and
- participants to honour their dispatch offer, dispatch bid or rebid if these material circumstance remain substantially unchanged.

The proposed Rule changes will strengthen the current regulatory framework and promote generator bidding and rebidding practices that are consistent with an efficient, competitive and reliable market. The proposed changes will enhance economically efficient outcomes by ensuring both customers and generators can make appropriate decisions based upon accurate forecasts.

The South Australia Government considers that improved price transparency in the wholesale electricity spot market will promote certainty for market participants and competition in the energy retail market, improve liquidity in the futures market and provide economically efficient signals for investment in electricity generation. These proposed Rule changes will therefore ensure that the long term interests of consumers are protected with respect to price, reliability and security of electricity supply.

We consider the best way to mitigate market participants acting in a manner which may be described as “bidding in bad faith” is to proscribe the relevant conduct in additional clauses added to 3.8.22A of the Rules, as well as through other amendments to the existing 3.8.22A clauses. Minor changes are also proposed to clause 3.8.22. The key principles behind the proposed Rule change are:

- an initial dispatch offer or dispatch bid should reflect the participant’s best intentions based on available information;
- participants should make a dispatch offer, dispatch bid or rebid based on all known material circumstances at the time and honour that dispatch offer, dispatch bid or rebid if there is not a material change to those circumstances;

- a rebid should be made within a reasonable time of a material change in the circumstances on which the previous dispatch offer, dispatch bid or rebid was based;
- a Generator or Market Participant should provide, on request from the AER, accurate and complete information and data regarding the material circumstances on which a dispatch offer, dispatch bid or rebid was based and provide full and clear reasons regarding why each dispatch offer, dispatch bid or rebid, in the context of the participant's entire registered portfolio, is a reasonable response to the relevant change in material circumstances.
- a participant should not vary a dispatch offer, dispatch bid or rebid unless it is in response to a significant and quantifiable change in circumstances.

The proposal will allow the Australian Energy Regulator (AER) to consider all of the bids or rebids by all of the generator's units when determining if the participant has breached the good faith provisions. The existing provisions relate to generating units, rather than an entire power station or larger generation portfolio, and so when reviewing compliance with the rebidding provisions the participant's behaviour is only allowed to be assessed on a unit by unit basis. Bids and rebids are therefore assessed and compared to the previous offer of the relevant unit, but this is not consistent with how a participant would bid in practice.

Specifically, the Rule changes propose the following:

- To clarify what is meant by good faith for the purposes of the Rules, and specifically to state when a dispatch offer, dispatch bid or rebid would not be considered to have been made in good faith.
- To provide that a dispatch offer, dispatch bid or rebid can only be taken to be made in good faith if the participant has a genuine intention to honour that bid if the material circumstances upon which it was based remain substantially unchanged until the relevant dispatch interval.
- To provide that a variation to a dispatch offer, dispatch bid or rebid must not be made unless it is in response to a significant and quantifiable change in price, demand or other data published by AEMO in respect of that trading interval. The variation must also occur as soon as is practicable after the change comes to the participant's attention.
- To provide a clear requirement for participants to provide the AER with accurate and complete data and information on request to substantiate compliance with the bidding in good faith provision.
- To allow the AER to assess the intention of the participant by having regard to all of the dispatch offers, dispatch bids and rebids that a participant has had substantial control or influence over, as well as information provided by the participant or published by AEMO.

3. Nature and scope of the issues that are proposed to be addressed

Reliable and accurate information is key to determining meaningful pre-dispatch forecasts and allowing competitive demand and supply side responses. The accuracy and reliability of these forecasts can be undermined by rebidding.

These forecasts are becoming even more important as the market continues to evolve. Recent developments will result in more types of market participants becoming reliant on accurate forecast information.

At its December 2012 meeting, the Standing Council on Energy and Resources (SCER) endorsed the development of a demand side wholesale market mechanism based on recommendations made in the AEMC's Power of Choice review. In the review, the AEMC considered that a new option for demand side resources to participate in the NEM wholesale market would enhance participation by some consumers by allowing them to see the value of reducing their consumption in response to spot market prices. A demand response mechanism was therefore proposed that would give incentives for demand side response based on price signals in the wholesale market.

The option could reduce the costs of wholesale market participation by allowing specialist third parties to trade in the market on behalf of consumers with demand response capabilities. Consumers who see sufficient value in the option could also participate on their own behalf. The AEMC considered larger electricity users in the commercial and industrial sector would be most likely to take advantage of this option in the first instance.

The proposed demand response mechanism encourages price responsive demand side participation in the wholesale market, in addition to any demand side actions coordinated through the bilateral contracts between a retailer and consumer. In this regard, the review states that demand forecasting will likely play an increasingly important role in understanding the level of activity of demand side participation in the market, and also assisting in efficient decision making on behalf of consumers providing a demand response.

For example, the AEMC review states that prior to entering into a demand response interval under the proposed mechanism or any existing demand response arrangements, a consumer will need to make an economic decision that is based on the potential value of providing a demand response according to plant operating levels. For consumers, the risks involved in making such decisions are minimised when pre-dispatch price signals closely reflect actual dispatch. Pre-dispatch timeframes are particularly important as price responsive demand side resources use this information to ascertain the potential value of providing a demand response.⁵

SCER has requested that AEMO undertake the work necessary to develop and submit rule change proposals which would give effect to the AEMC's recommendations. The targeted implementation date of the demand response mechanism is the first quarter of 2015.

AEMO have also been asked to consider whether a new 'sub-category' of market participant (most likely under the category of market generator) would be required to facilitate participation of consumers in the demand response mechanism, following submissions to the AEMC's recommendations in the Power of Choice review.⁶ This follows another recent rule change that introduced a new category of market

⁵ AEMC, *Power of choice review - giving consumers options in the way they use electricity – Final Report*, 30 November 2012, p 142.

⁶ AEMC, *Power of Choice review*, p 139.

participant. On 29 November 2012, the AEMC published the Small Generation Aggregator Framework final determination and final rule. The rule sought to lessen potential barriers to fully participating in the market faced by small generators.

AEMO, the initial proponent of the rule change considered that, for generators that would otherwise be exempt from market registration requirements, the process of becoming a Market Generator to sell output at the spot price represented an inefficient cost. To address this AEMO proposed that small generating units be able to aggregate and sell their generation through a third party.

A new category of Market Participant has now been added to the Rules. This Market Small Generation Aggregator will be able to receive the spot price on behalf of a portfolio of generators that are exempt from registration requirements due to their small size. This new type of market participant would also be reliant on accurate forecast information in order to make informed decisions when selling their output.

The reliability and accuracy of the information used to determine meaningful pre-dispatch forecasts is therefore becoming increasingly important as more participants rely on this information to make competitive demand and supply side responses. The need for bids and rebids to be made in good faith therefore continues to increase in importance, as does the need for certainty around the operation of the bidding in good faith provisions of the Rules. We believe this certainty has been eroded following the 2011 Federal Court decision.

A key component of the Federal Court decision was not to consider extrinsic material, emphasising the desirability of persons being able to rely on the ordinary meaning of a clause. It is therefore important that the ordinary meaning of the bidding clause is equivalent to the intended purpose of the rebidding provisions. Accordingly, if there is any doubt or concern that the intended purpose is not clear in the ordinary meaning, even if it is not possible to determine how market participants will behave in a rebidding circumstance post the Federal Court decision, the rebidding provisions should be amended.

Subjective Expectations

A trader's subjective expectation of the effect of a rebid was treated by the Federal Court as part of the material conditions and circumstances on which the rebid was based, and therefore the nonfulfillment of that expectation would be lawful justification for another rebid.

Further, it suggests that even if the dispatch price was unchanged, this may represent a change in material conditions and circumstances. Accordingly, the Federal Court decision suggests a very wide interpretation of what is a material condition and circumstance. Therefore, as it is currently drafted, Rule 3.8.22A cannot prevent or hinder repeated attempts by a trader to cause price spikes by shifting capacity into higher price bands.

Genuine Intentions

There is uncertainty regarding how the AER can establish genuine intentions, including what conduct could be assessed to infer an absence of genuine intentions.

The Federal Court decision suggests that to prove a breach of the Rules, the AER must prove that the relevant trader was placing bids that were never intended to be honoured.

The decision imposed on the AER the requirement to prove that at the time of making the rebid, the participant positively intended to resile from the rebid, even if the material conditions and circumstances stayed the same. It would be very difficult for the AER to prove that the participant intended to resile from the rebid at the time it was made, and therefore difficult to prove that the bid was made without good faith.

Determining the subjective intention of an individual is difficult at the best of times. However, the judge also placed particular weight on the trader's testimony in court, which was not consistent with previous information provided to the AER.

Accordingly, the decision implies that for the AER to monitor compliance with the rebidding provision, they need information regarding an individual trader's state of mind.

The AER currently uses the powers set out in section 28 of the National Electricity Law (NEL) in relation to the conduct of investigations. The ability of the Federal Court to place weight on new information (the trader's testimony) suggests that these powers do not ensure that the AER is provided with accurate and complete information, with which to assess compliance.

The key issue with the bidding in good in faith provisions in this area is therefore that the information provided to the AER, which is used to assess compliance, may not be complete and accurate.

In addition to the issues encountered in and arising from the Federal Court case in 2011, analysis of the AER's reports on "*Spot prices greater than \$5,000/MWh*" (AER's reports) revealed that other implementation issues exist. While the AER reports highlighted that in many cases the bidding and rebidding activities of generators were used for their intended purpose, that is, to allow the necessary flexibility to respond to market changes noting the need for accurate day-ahead forecast market data for market participants, there were a number of examples that raised issues in relation to the implementation of the bidding in good faith provisions. These included the following issues.

Known conditions and circumstances

The AER reports highlighted that rebidding occurs in response to known conditions and circumstances that should have been taken into account when the original bid is made.

AER's reports demonstrated that in some cases a change in market conditions, which was stated as the reason for the rebid, was known ahead of time. Despite notification of a network constraint or high demand, market participants were seen to rebid just before dispatch and the rebid appeared to be reasoned on the basis of the previously known conditions. It would therefore be expected that if the bidding provisions were achieving their purpose, market participants would account for known circumstances

at the time of their bid (or shortly after becoming aware of the material circumstances), thereby allowing other market participants to respond.

As discussed above, the reason the NEM design includes provisions for rebidding is because generators require the flexibility to adjust their positions to accommodate unexpected changes in demand patterns and plant availability. However, another key element of the NEM design is the need for pre-dispatch forecasts which can be relied upon by market participants. As generators are required to self-commit, pre-dispatch forecasts are essential for generators to determine whether to be online.

As generators take on risk when entering forward contract arrangements, they must set up the capability to observe forecasts and respond as flexibly as possible. Rebidding close to dispatch may allow generators to manipulate spot prices in a time frame within which other competing generators (and market customers) cannot respond. It is generally the case that the closer the rebid is to the time of dispatch fewer generators can physically alter their total capacity available to the market. If the ability for generators to respond is reduced, it is likely to expose them to further risks.

Two key issues with the bidding in good faith provisions in this area are therefore that:

- the provisions fail to stop a market participant, in a subsequent rebid, from relying on material conditions and circumstances which were known at the time of the preceding dispatch offer, dispatch bid or rebid; and
- the provisions fail to require a market participant to take any action arising from changes in material conditions and circumstances within a reasonable period of the participant becoming aware of them.

Materiality

We believe there is ambiguity around the term “material” which is used to limit when a variation of a bid or rebid occurs. In the current bidding in good faith provisions, a dispatch offer, dispatch bid or rebid is taken to be made in good faith if the participant has a genuine intention to honour it if the material conditions and circumstances upon which it was based remain unchanged. Accordingly, if a wide interpretation of material conditions and circumstances is taken, there will be a large number of circumstances upon which the participant may rebid. This is due to the drafting of the provision linking materiality to the conditions and circumstances. AER’s reports highlighted this, with rebids being observed in circumstances where demand and capacity were at close to forecast levels.

The key issues with the bidding in good faith provisions in this area are therefore that:

- they provide market participants with insufficient clarity regarding what is a material condition and circumstance.

4. Proposed solution

The South Australian Government has assessed the operation of the generator bidding and rebidding provisions of the Rules and identified issues with the operation of these provisions, as outlined in section 3. It is recommended that amendments be made to the Rules to address the issues identified with the current provisions.

The Rules should be redrafted to mitigate bidding in “bad faith” and also to provide market participants with sufficient guidance as to what would constitute a contravention of the bidding in good faith Rule clauses.

Proposed changes to the Rules are provided in Attachment A. An outline of these changes and their objective is provided below:

What constitutes bidding in good faith

Changes to clause 3.8.22A(b) are proposed to address, in part, the final two issues discussed in section 3. The proposed amendments aim to overcome the issue identified in the Federal Court’s ruling where clause 3.8.22A(b) was not considered to provide a thorough list as to what constitutes acting in good faith. One approach would be to make it clear that the requirements regarding what constituted good faith were exhaustive. However, it is considered that indicating that a trader would be considered to have acted in good faith if certain requirements are met could be potentially be insufficient, as there may be other alternative factors that might demonstrate good faith that are not listed.

As such, we propose casting this provision in the negative by stating that a dispatch offer, dispatch bid or rebid is taken not to be in good faith unless, at the time of making the bid, the participant has a genuine intention to honour that bid if material circumstances remain unchanged. There is additional benefit in casting the provision in this way.

In 2011, the Federal Court considered that the participant, at the time it made its original bids, had an honest intention to honour those bids. Although the traders knew that it would be possible to make another rebid, that did not of itself mean that the original bid was made without good faith. The Judge considered that the mere possibility that they could make a rebid did not mean that they had no genuine intention to honour the first bid if nothing changed. No such inference could be drawn merely because there had been a rebid in circumstances where nothing had changed.

Recasting clause 3.8.22A(b) in the negative is also intended to assist with this problem. If a trader makes a rebid when nothing has changed from the earlier bid, the new wording more clearly allows an inference to be drawn that the original bid was not made in good faith.

Related to this, we propose a note be included in clause 3.8.22A(e) to clarify that where a trader expects a change to occur following its own rebid but that change does not eventuate, that is not a change in “material circumstances”. The proposed drafting attempts to clarify that the non-fulfilment of a trader’s expectation of the result of a rebid is not a change that justifies another rebid.

We also think that the use of the expression “material conditions and circumstances” could potentially be unclear on whether changes subjectively held by a trader are to be treated as changes under Rule 3.8.22A. We think this could perhaps be overcome by using the expression “material circumstances” instead.

Finally, rebids should be made as soon as practicable after the change in material circumstances comes to a participant’s attention. As mentioned above, the concept of

rebidding in good faith is integral to efficient dispatch and transparent market outcomes, it is therefore imperative that other participants have time to react to changes in the market. We consider that the current lack of restriction regarding timing of rebids has allowed participants the ability to rebid close to dispatch, which provides other participants with little or no time to respond. It was noted that in some previous cases of rebidding, the change in market conditions, which was stated as the reason for the rebid, was known ahead of time.

Restricting bidding close to dispatch would be one mechanism to overcome this problem, however this would not recognise that there may be changes in market circumstances close to dispatch, where it would be acceptable to respond by rebidding. The inclusion of the requirement for a participant to rebid as soon as practicable after the change comes to its attention is designed to ensure the rebid is made in a timely manner and should therefore be an important characteristic of bidding in good faith. Proposed additions to Rule 3.8.22A would bring this change in to effect.

Sources of inference

Clause 3.8.22A(c) of the Rules is a facilitative provision designed to assist in proving contravention of clause 3.8.22A(a). The existing clause lists the sources of inference from which the intention of the participant is ascertainable from. We have proposed various modifications to improve this existing clause. It is however, important that the modifications avoid suggesting anything that could be regarded as a condition or restriction on the way the courts would approach a contravention proceeding.

The changes expand the list of matters that can be assessed in determining the intention of the participant. We have also made reference to "knowledge" and "belief" being inferable under this provision, not only "intention".

The additional sources of inference are proposed to include information that the Generator or Market Participant submits pursuant to clause 3.8.22A(d) (the addition of new information provisions are discussed further below). We believe the information provided by the participant should be placed first on the list of sources of inference. This is to emphasise the importance of this information being complete and accurate.

Secondly, we have proposed extending the existing reference to "conduct" of any other person being a potential source of inference, to the "conduct, knowledge, belief or intention" of any person. Information published by AEMO for the relevant participant should also be added as a potential source of inference.

Finally, we propose including other bids that have been made by the participant or other bids that the relevant participant has substantial control or influence over to the list of sources of inference. This amendment will ensure that the intention of the generator or market participant is ascertainable by inference from all of the dispatch offers, bids and rebids made that a generator (or market participant) has had substantial control or influence. This is intended to capture the participant's entire registered portfolio, allowing the AER to consider all of the bids or rebids by all of the generator's units (more than one) when determining if the participant has breached the good faith provisions.

Currently, existing provisions relate to generating units, rather than an entire power station or multiple power stations, and so when reviewing compliance with the rebidding provisions the participant's behaviour is only allowed to be assessed on a unit by unit basis. Bids and rebids are therefore assessed and compared to the previous offer of that unit. An amendment should therefore be made to allow the AER to take into account the generator's behaviour in relation to their whole portfolio when assessing compliance with the good faith provisions.

In view of the possibility that we may see more strategic bidding by loads into the future, we have proposed the broader reference to Market Participants.

The same facilitative provisions have been carried forward into the proposed clause 3.8.22A(f).

Information provision

We propose the addition of a Rule to introduce a requirement for generators to provide accurate and complete data and information that substantiates that the dispatch offer, dispatch bid or rebid has complied with the good faith provisions, if requested to do so by the AER. When assessing compliance against these provisions, the AER should be assured that in response to their questions, the participant is providing full and complete information regarding their bid and rebid. This seeks to address concerns regarding the accuracy and fullness of information provided to the AER prior to court proceedings. Introducing such a provision in Rule 3.8.22A ensures that the rebidding civil penalty provision applies.

Requirements for rebids

As mentioned above, we propose the inclusion of new clauses to proscribe detrimental conduct with regard to participants rebidding practices. By introducing these clauses under the existing clause 3.8.22A it maintains the existing rebidding civil penalty provision.

While clause 3.8.22A(b) aims to clarify the circumstances when dispatch offers, dispatch bids and rebids are constituted to have been made in good faith, these further amendments are proposed to set additional requirements for when rebids are considered to have been made in good faith.

The proposed clauses 3.8.22A(e) and (f) describe the circumstances under which a trader is permitted to rebid to shift capacity across price bands. The clause should prevent a participant from varying its bids unless it does so in response to a significant and quantifiable change in price, demand or other data published by AEMO in respect of that trading interval, or change in other material circumstances.

This change would allow a participant to rebid in response to any significant change in price or demand that can be quantified. This clause would therefore still provide generators with the flexibility necessary to adjust their positions to accommodate unexpected changes in the market, including network constraints, changes in demand and changes in plant availability. However, by limiting the ability to rebid to events that are significant and quantifiable it provides market participants that rely on pre-

dispatch forecasts with some assurance that generators intend to honour their bids. This is therefore consistent with the purpose of the good faith provisions.

A significant change in the data published by AEMO is proposed to be included as a justifiable reason for a rebid to occur. This is considered appropriate as it provides clear guidance that the non-occurrence of (AEMO's) forecast changes might justify a rebid. This is contrasted with the notion of the non-occurrence of a merely subjectively expected change not occurring (that should not justify a rebid).

The phrases “significant and quantifiable” and “material circumstances” are integral to this clause. Any rebid based on a minor change in circumstances should not result in a change in the generators bid. The same should apply for changes in circumstances that are not quantifiable.

As discussed above, clause 3.8.22A(e) importantly should include a requirement for rebids to be made “as soon as practicable after the change in material circumstances comes to its attention”. A note is also proposed to be included under this clause to clarify that where a trader expects a change to occur following its own rebid but that change does not eventuate, that is not a change in “material circumstances”.

Finally, we have also included the previously discussed facilitative provisions under the proposed clause 3.8.22A(f) to assist in proving a contravention of clause 3.8.22A(e).

5. How the proposed Rule changes contribute to the National Electricity Objective

Section 88 of the NEL requires that the AEMC may only make a Rule if it is satisfied that the Rule will, or is likely, to contribute to the achievement of the NEO.

The NEO, as set out in section 7 of the NEL, is as follows:

“The objective of this Law to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to –

(a) price, quality, safety, reliability and security of supply of electricity; and

(b) the reliability, safety and security of the national electricity system.”

The proposed Rule change recognises that it is in the long term interests of consumers for rebidding to occur in certain circumstances. For example, rebidding allows generators to respond to physical problems such as unexpected outages. Accordingly, the proposed Rule changes retain the ability of a market participant to vary certain parameters (listed in clause 3.8.22(b) of the Rules) through rebidding.

However, the South Australian Government considers that the proposed Rule change will provide market participants with greater confidence in relation to the reliability and accuracy of pre-dispatch forecasts, thereby aiding competitive demand and supply side response. This is achieved by providing greater clarification around when a

dispatch offer, dispatch bid or rebid will be considered to be made in good faith, in particular requiring:

- all existing material circumstances to be taken into account when a dispatch offer, dispatch bid or rebid is made; and
- participants to honour their dispatch offer, dispatch bid or rebid if these material circumstance remain substantially unchanged.

A requirement that attempts to provide the participants of the market that rely on pre-dispatch forecasts with some assurance that generators intend to honour their bids should be an important feature of the electricity market. Indeed, the concept of requiring parties to honour the offers they have made is not one that is unique to the electricity market. For example, if an offer is made by a retailer of whitegoods for the sale of their products, then consumers can be sure that this offer will be honoured by the retailer, otherwise the retailer would be in breach of Australian Consumer Law which prohibits parties from making false or misleading representations in connection with the supply, possible supply or promotion of goods or services (s29). These legislative provisions therefore aim to ensure that retail customers can rely on the advertised prices of retail goods. In much the same way, the concept of good faith was intended to improve the reliability of pre-dispatch forecast prices for all market participants.

The proposed Rule change also seeks to ensure that participants are provided with timely information with which to make demand and supply side response decisions. The South Australian Government considers that due to the current lack of restriction regarding the timing of rebids, participants have the ability to rebid close to dispatch, which provides other participants with little or no time to respond.

Whilst this issue could be overcome by having a restriction on rebidding close to dispatch, this type of artificial mechanism does not recognise that there may be changes in market conditions and circumstances close to dispatch, where it is appropriate to respond through rebidding. Accordingly, the proposed Rule changes seek to link timeliness of response to when the generator or market participant had knowledge of the change in market circumstances.

Demand side response has the potential to provide benefits to individual consumers and consumers as a whole. For example, the NEM currently has a number of market customers that respond to pre-dispatch forecasts to manage their electricity costs. Their response to high price signals can also reduce short term supply costs and reduce peak capacity requirements in the longer term thus providing savings for all consumers. The addition of the proposed demand response mechanism in the Power of Choice review will further encourage price responsive demand side participation in the wholesale market. Meaningful pre-dispatch forecasts therefore become increasingly important as more participants rely on this information to make competitive demand and supply side responses. The need for bids and rebids to be made in good faith consequently continues to increase in importance. The proposed amendments to the bidding in good faith provisions of the Rules will enhance economically efficient outcomes by ensuring both customers and generators can make appropriate decisions based upon accurate forecasts.

Consumers also benefit from efficient dispatch of generation and the provision of correct market signals in relation to investment in new capacity. Where these things are not achieved, the result may be higher wholesale prices that are likely to flow through to retail prices and increase consumer costs, and uncertainty in relation to investment decisions which could impact reliability of supply.

The South Australia Government considers that the proposed Rule changes would contribute to meeting the NEO by strengthening the current regulatory framework and promoting generator bidding and rebidding practices that are consistent with an efficient, competitive and reliable market. Accordingly, the proposed Rule changes are likely to enhance the ability of the Rules to better meet the requirements of the NEO.

6. Expected benefits and costs of the proposed Rule changes and the potential impacts on those affected

Benefits

As discussed above, the proposed Rule changes will promote the achievement of the NEO by strengthening the current regulatory framework and promoting generator bidding and rebidding practices that are consistent with an efficient, competitive and reliable market. The proposed changes will enhance economically efficient outcomes during periods of high demand by limiting the ability of a generator to engage in strategic withdrawal of generation capacity when other parties are unable to respond, thereby removing the risk of capacity not being dispatched, and facilitating a more considered analysis of market behaviours.

The South Australia Government considers that improved price transparency in the wholesale electricity spot market will promote certainty for market participants and competition in the energy retail market, improve liquidity in the futures market and provide economically efficient signals for investment in electricity generation. These proposed Rule changes will therefore ensure that the long term interests of consumers are protected with respect to price, reliability and security of electricity supply.

It is important to note that in July 2002, the MCE agreed that they oppose generator bidding and rebidding strategies that are inconsistent with an efficient, competitive and reliable market, such as those not made in good faith. We believe this proposed Rule change will restore the policy intent of the MCE policy position.

Costs

While the proposed Rule changes will require generators to keep information to substantiate that their dispatch offer, dispatch bid or rebid practices have complied with the good faith provisions, it is envisaged that this requirement would not require a significant change to existing practices. The South Australian Government therefore does not consider that any significant costs would be imposed on generators.

The amendments should in no way prevent participants from rebidding where there is a genuine need to do so. It would still provide participants with the flexibility necessary to adjust their positions to accommodate unexpected changes in the market, including network constraints, changes in demand and changes in plant availability. We therefore consider that the benefits to promoting the NEO substantially outweigh the costs imposed.

Potential impacts on parties likely to be affected

The proposed Rule changes will impact generators by requiring them to provide accurate and complete data and information that substantiates their compliance with the bidding in good faith provisions, if requested to do so by the AER. However, those impacts are not expected to be substantial as those changes would not require a significant change to existing practices.

7. Stakeholder Engagement

The South Australian Government has engaged with officers from the AER in the development of this Rule change proposal.

Attachment A

Proposed amendment to the National Electricity Rules

[1] Clause 3.8.22 Rebidding

Amend clause 3.8.22(c) as follows:

- (2) to *AEMO*, at the same time as the *rebid* is made:
 - (i) a brief, verifiable and specific statement of the reason(s) for the *rebid*; and
 - (ii) the time at which the event(s) or other occurrence(s) adduced by the relevant Generator or Market Participant as the reason(s) for the *rebid*, occurred; and

Note

This clause is classified as a civil penalty provision under the National Electricity (South Australia) Regulations. (See clause 6(1) and Schedule 1 of the National Electricity (South Australia) Regulations.)

- (3) to the *AER*, upon written request, in accordance with guidelines published by the *AER* from time to time under this clause 3.8.22 and in accordance with the *Rules consultation procedures*, such additional information to substantiate and verify the reason(s) for a *rebid* as the *AER* may require from time to time.

Note

This clause is classified as a civil penalty provision under the National Electricity (South Australia) Regulations. (See clause 6(1) and Schedule 1 of the National Electricity (South Australia) Regulations.)

[2] Clause 3.8.22A Variation of offer, bid or rebid

Amend clause 3.8.22A(b) as follows:

- (b) ~~In~~ For the purposes of paragraph (a) a *dispatch offer*, *dispatch bid* or *rebid* is taken not to be made in good faith ~~if~~ unless, at the time of making such an offer, bid or *rebid*, a *Scheduled Generator*, *Semi-Scheduled Generator* or *Market Participant* has a genuine intention to honour that offer, bid or *rebid* if the material ~~conditions and~~ circumstances upon which the offer, bid or *rebid* ~~were~~ was based remain unchanged until the relevant *dispatch interval*.

[3] Clause 3.8.22A Variation of offer, bid or rebid

Amend clause 3.8.22A(c) as follows:

- (c) A *Scheduled Generator, Semi-Scheduled Generator* or *Market Participant* may be taken to have contravened paragraph (a) notwithstanding that, after all the evidence has been considered, the knowledge, belief or intention of the relevant *Generator* or *Market Participant* is ascertainable only by inference from:
- (1) information provided by the relevant *Generator* or *Market Participant* pursuant to clause 3.8.22(d);
 - (2) other dispatch offers, bids, and rebids made by the *Generator* or *Market Participant* or in relation to which the relevant *Generator* or *Market Participant* had substantial control or influence;
 - (3) the other conduct of the relevant *Generator* or *Market Participant*;
 - (4) the conduct, knowledge, belief or intention of any other person;
~~or~~
 - (5) information published by AEMO to the relevant *Generator* or *Market Participant*; or
 - (6) any other ~~the~~ relevant circumstances.

Note

This clause is a rebidding civil penalty provision for the purposes of the National Electricity Law. (See clause 6(2) of the National Electricity (South Australia) Regulations.)

[4] Clause 3.8.22A Variation of offer, bid or rebid

After clause 3.8.22A(c) insert:

- (d) At the request of the *AER*, a *Scheduled Generator, Semi-Scheduled Generator* or *Market Participant* must provide accurate and complete data and information to substantiate that the *dispatch offer, dispatch bid* or *rebid* complied with paragraph (a).
- (e) A *Scheduled Generator, Semi-Scheduled Generator* or *Market Participant* must not vary the available capacity allocated to a price band in a *generation dispatch offer* or *dispatch bid* for a *trading interval* or any *dispatch interval(s)* thereof after the relevant deadline in the *timetable* unless the *Scheduled Generator, Semi-Scheduled Generator* or *Market Participant* does so:
- (1) in response to a significant and quantifiable change in:

- (i) price, demand or other data published by AEMO in respect of the trading interval or dispatch interval(s); or
 - (ii) other material circumstances; and
- (2) as soon as practicable after the change comes to its attention.

Note

Where a Generator or Market Participant expects a change to occur following its own rebid but that change does not eventuate, that is not a change in material circumstances.

- (f) A Scheduled Generator, Semi-Scheduled Generator or Market Participant may be taken to have contravened paragraph (e) notwithstanding that, after all the evidence has been considered, the knowledge, belief or intention of the relevant Generator or Market Participant is ascertainable only by inference from:
 - (1) information provided by the relevant Generator or Market Participant pursuant to clause 3.8.22A(d);
 - (2) other dispatch offers, bids and rebids made by the Generator or Market Participant or in relation to which the relevant Generator or Market Participant had substantial control or influence;
 - (3) the other conduct of the relevant Generator or Market Participant;
 - (4) the conduct, knowledge, belief or intention of any other person;
 - (5) information published by AEMO to the relevant Generator or Market Participant; or
 - (6) any other relevant circumstances.

Note

This clause is a rebidding civil penalty provision for the purposes of the National Electricity Law. (See clause 6(2) of the National Electricity (South Australia) Regulations.)