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Bidding in good faith – Second Draft Determination

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Australian Energy Market Commission (AEMC) on the Bidding in good faith rule change.

The esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of 37 electricity and downstream natural gas businesses. These businesses own and operate some $120 billion in assets, employ more than 59,000 people and contribute $24.1 billion directly to the nation's Gross Domestic Product.

Materiality

Based on the information provided it is still not clear that late rebidding presents a material problem to the National Electricity Market (NEM). We note the AEMC has held out the work undertaken by Ernst & Young (EY) as representing the materiality of the issue. While all modelling requires assumptions to simplify an issue, in the industry's view EY have made assumptions that render the figures meaningless.

As has consistently been affirmed by all parties, volatility in the spot price is an inherent and necessary feature of a market with the characteristics of the NEM. Flexibility is essential for maintaining a reliable system given the range of factors that impact on the dynamics of both demand and supply of electricity. As such, any piece of analysis that assumes all of the volatility is caused by undesirable bidding practices does not offer any insights.

To be of any use a more sophisticated piece of analysis would be required that makes an attempt to account for legitimate reasons for late rebidding, such as late changes in demand and late changes in available supply. The first method used to estimate the impact of late strategic rebidding was to assume the higher level of volatility in the 5th and 6th dispatch intervals is solely attributable to strategic late rebidding. This assumption is baseless. While EY claims to account for this by comparing volatility in first four dispatch intervals to the fifth and sixth in earlier time periods, this approach again attributes all the changes to last two intervals, regardless of the cause. For example, a fall in volatility in the first four dispatch intervals creates a relatively higher level of late rebidding in the fifth and sixth interval, even though there has not been a change in absolute terms.

The industry is disappointed the AEMC has held out these figures as being representative of the materiality of the issue. In doing so, it has:

- created an unrealistic expectation about potential future changes in contract prices once this rule comes into effect;
- created the false impression that rebidding shortly before a dispatch interval is an unwelcome element of the market design, and;
- conversely, ignored the potential for material market efficiency costs from generators adopting a more conservative approach to offering their generation and ancillary services due to a more draconian regulatory regime.

Drafting

The esaa agrees with the Commission that deliberately withholding a rebid is not desirable behaviour and should be prevented. As such, the industry is comfortable with the idea of making explicit in the rules that a generator's offers to the market need to reflect their current intentions, but we have concerns with some of the current drafting.

As noted above, the industry accepts the proposition that a generator's offers should reflect their actual intentions, subject to the timing of lodging a rebid once a decision is taken. The current draft determination seems to suggest this continuous obligation could in part be enforced through 3.8.22A(a), as an earlier bid would become misleading or false once a generator changes its intentions. We have concerns with using subsection (a) to retrospectively make bids false or misleading. Subsection (a) should only apply at the time the bid or rebid is made. The continuous obligation should only arise from subsection (d). Subsection (d) requires a generator to rebid as soon as practicable, once they have made a decision. This provision clearly creates the obligation for a generator to ensure their current bid/rebid represents their intentions, as they are required to rebid once they take the decision.

We have identified several uncertainties with the current drafting. Clause 3.8.22A(a1) could be interpreted as imposing a strict liability that is independent of clause (a). If this is interpreted as a strict liability, this is a fundamental change and presents greater risks to the energy industry. A deeming provision such as clause (a1) may be useful in clarifying how to interpret clause (a), but the current drafting of (a1) goes beyond this, and creates a strict liability of its own. The esaa would welcome whether clarification from the AEMC as to whether the purpose of 3.8.22A(a1) is in fact to impose a strict liability independent of clause 3.8.22A(a).

Clause 3.8.22A(b) starts with the words "without limiting paragraph (a)…". This suggests that (a) is intended to cover circumstances beyond those contemplated by (b). It is unclear what additional liabilities are intended by 3.8.22A(a) that are not addressed by 3.8.22A(b). A discussion of the reasoning behind the drafting of 3.8.22A(b) could help the industry better understand what issues the AEMC is hoping to address through this provision.

The current draft rule would also be helped by greater clarity as to the intent of subsection 3.8.22A(b)(2). In other contexts, courts have interpreted 'reasonable grounds' as requiring the person to have an intention and an ability to perform the representation. This would suggest the proposed subsection (b)(2) would operate in a nearly identical manner to

subsection (b)(1). But its existence as a separate clause implies a view that it means something significantly different from subsection (b)(1). This creates ambiguity until the point at which a court applies statutory interpretation principles to give subsection (b)(2) its own distinct meaning.

In the current draft determination the AEMC has made explicit that subsection 3.8.22A(e) does not create an obligation on generators to take account of whether any other generator is able to subsequently rebid. The need for the court to consider this is still not clear. Subsection (d) frames a generator's obligation internally, to act once they have formed a judgement. This approach requires the generator to act on information completely within its control. Subsection (e) is framed with reference to other market participants. Leaving aside the issue of determining who should be allowed to respond, it is not clear how referencing other market participants allows one to assess if a generator acted as soon as practicable, i.e. the time they took to implement a decision once it was taken.

While the esaa appreciates the AEMC's decision to opt for a recording regime rather than a reporting obligation in the second draft rule, it remains the industry view that the proposed "contemporaneous" record of late rebids is not required. As we stated in our submissions on the first draft determination, the AER's existing information collection powers are extensive and it is not clear there are any benefits from an additional reporting or contemporaneous record requirement, but there will be additional costs. Some of these compliance costs are identified in Oakley Greenwood's assessment for the AEMC.

Additional uncertainty arises in clause 3.8.22A(d) as a result of the phrase "as soon as practicable…". The draft rule change sets out that rebids must be made as soon as practicable after becoming aware of the change in material conditions. This does not reflect the reality that there may be time gaps between when a generator becomes aware of a change in conditions and decides whether or not to act on these changes before submitting a rebid. The time it takes for a generator to reach a decision is an important consideration, yet the current drafting ignores this.

Finally, the esaa has identified that there are possible unintended consequences as a result of the proposed rule change. Error bids or IT bids (e.g. to test systems) which are then changed would technically be in breach of the proposed rule change even though the intent is not to mislead other market participants. The Association would welcome clarification from the AEMC that fixing errors or testing IT systems would not be classified as a breach.

Any questions about our submission should be addressed to Ben Pryor by email to ben.pryor@esaa.com.au or by telephone on (03) 9205 3103.

Yours sincerely

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