

Dr Kerry Schott AO
Energy Security Board

8th March 2019

Submitted via e-mail to: info@esb.org.au

Dear Dr Schott,

ACCC REPI Recommendation 41 Consultation Paper

The Australian Energy Council (the “**Energy Council**”) welcomes the opportunity to make a submission in response to the Energy Security Board’s (“**ESB’s**”) *ACCC Retail Electricity Pricing Inquiry Recommendation 41 Consultation Paper*.

The Energy Council is the industry body representing 23 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia, sell gas and electricity to over ten million homes and businesses, and are major investors in renewable energy generation.

Introduction

Recommendation 41 of the Australian Competition & Consumer Commission’s (“**ACCC’s**”) *Retail Electricity Pricing Inquiry Final Report*¹ (“**REPI**”) was to expand the Australian Energy Regulator’s (“**AER’s**”) wholesale market monitoring functions to include the contract market. This recommendation is a consequence of the ACCC’s review of the Over the Counter (“**OTC**”) market in Section 5.3.

The Section 5.3 review is based on the information compulsorily acquired from 17 retailers, and concluded (in Recommendation 6) that all OTC trades should be reported to a repository administered by the AER, and then disclosed publicly in an anonymised format. The justification for imposing this compliance burden is that “the lack of transparency in the OTC market impedes the transmission of price signals in the market.”²

Since the REPI was prepared in June 2018, there have been a number of developments which have diminished the justification for the recommendation. In particular the proposed development of the Reliability Guarantee may exhibit some similarities with the proposed trade repository, since retailers will be required to lodge their contract positions with the AER. In addition, the *Market Making Arrangements in the NEM* proposed rule change has elements which will address the ACCC’s concerns in relation to the OTC markets.³

What the ACCC is proposing is that willing counterparties will need to disclose their private arrangements, entered into between willing sellers and willing buyers, despite there being publicly reported trades via ASX Energy representing the majority of the total trading market and market development such that the recommendation is no longer pertinent. The Energy Council is therefore not convinced of the utility of imposing this additional obligation.

Discussion

The ESB has been charged with implementing Recommendation 41. The focus of the ESB’s implementation plan will be the AER, and providing it with the tools and authority to complete its new contract market reporting obligations. To do so adequately, the ACCC has assumed that a trade repository will need to be established, and data will need to be gathered from the repository, ASX Energy and compulsorily acquired from market participants.

¹ Australian Competition and Consumer Commission, *Restoring electricity affordability and Australia’s competitive advantage: Retail Electricity Pricing Inquiry – Final Report*, June 2018

² *Ibid.*, p.122

³ Available at <https://www.aemc.gov.au/rule-changes/market-making-arrangements-nem>

As the ESB notes in its Consultation Paper,⁴ a trade repository and mandatory reporting of OTC trades is not justified on transparency grounds alone, given the expenses of establishing and maintaining the repository, as well as the reporting burden on market participants. The Energy Council supports this finding.

The Consultation Paper discusses the nexus between electricity and gas markets, and the Energy Council acknowledges the AER's role in relation to both markets. Nevertheless the ACCC's Recommendation 41 (and Recommendation 6), as well as the discussion immediately before, was specific to electricity and therefore the Energy Council does not believe it is appropriate for the Consultation Paper to contemplate wholesale gas matters as well as wholesale electricity. In addition, the Energy Council disputes the Consultation Paper's statement that, "The links between the markets can also provide opportunities for cross market manipulation".⁵ Companies which are participating in both markets have the opportunity to conduct arbitrage between the gas and electricity markets, and seek to optimise the return on their investments, their inputs and their outputs. This should not be characterised as "manipulation".

AER's compulsory information acquisition powers

Clause 18D(1)(a) of the National Electricity Rules provides for the AER to use publicly available information to conduct its wholesale electricity market monitoring functions. Wholesale electricity market is defined as "any wholesale market for electricity regulated under this Law and the Rules".⁶

Under paragraph (b) of this clause, if the AER has identified any matters under Clause 18C(1), the AER may compel wholesale electricity suppliers to provide it with information. Clause 18C(1) is an effective competition assessment.

The Consultation Paper questions whether the AER should have to identify a question of effective competition in the wholesale electricity market before it can use its compulsory information gathering powers.

In the Energy Council's view, the wholesale electricity market is the National Electricity Market ("**NEM**") operated by the Australian Energy Market Operator. To manage the risks associated with participation in the NEM, market participants may choose to enter into other arrangements, such as derivatives, but also including bespoke agreements such as power purchase agreements. Counterparties to these transactions may or may not be registered participants within the NEM, and financial dealings of this nature are already regulated by the Australian Securities & Investments Commission ("**ASIC**"), and in relation to the conduct of exchange-traded instruments, the Australian Securities Exchange ("**ASX**"). The AER, as a regulator of physical energy activities, is not the appropriate agency to make enquiries which are outside its skill set and already overseen by more relevant regulators.

Should the AER's powers be expanded to allow information gathering in anticipation of possible competition issues, the compliance burden on industry and possibly other parties will be substantially expanded, for little benefit. The Energy Council cannot foresee a circumstance where the AER's general market monitoring functions would not alert it to issues which require further investigation, and the AER and ASIC have arrangements that allow them to collaborate. Therefore there is no need for expansion of the AER's information gathering powers into financial markets.

The information provided by market participants in good faith is to assist the AER's market monitoring functions. While every care is taken with compiling the information, it is possible that insignificant errors may be present in the data. Should the purposes of the data be expanded to enforcement or compliance monitoring functions, or dissemination to another body such as ASIC or the ACCC, the increased risk of a penalty as a result of an inadvertent error will cause each company to increase the scrutiny associated with such reporting, with a consequential increase in compliance costs. Ultimately the increase in costs will be borne by consumers. On that basis the Energy Council opposes widening the uses to which data provided to the AER for its wholesale market monitoring purposes can be put.

⁴ Consultation Paper, p.3

⁵ Ibid., p.5

⁶ National Electricity Law, Clause 2

Options for expanding the AER's Wholesale Market Monitoring Functions

The Energy Council acknowledges the ESB's task to expand the AER's wholesale market monitoring functions, but does not support establishing a trade repository for the following reasons:

- reduced liquidity – traders will assess the value of trades against the compliance burden of reporting them and may choose not to proceed with a trade rather than be required to report it;
- reduced innovation – new products will not be developed since they will be unable to be reported to the repository;
- increased compliance costs in having Risk departments collate the necessary data and report it.

Without going to the individual trade level with its business intrusion and significant compliance overhead, broker reports, subscription trade services, and the Australian Financial Markets Association Electricity (“AFMA”) Derivative Turnover Report,⁷ which has been recently re-established, are all suitable indicators for OTC trading. By having this information available, with minimal compliance burden on market participants, the AER will have a better understanding of OTC market and be able to use its information gathering powers in a more targeted way, reducing its investigation costs, and not unduly imposing upon market participants.

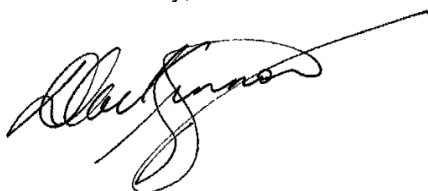
The Energy Council notes that there is an industry working group currently investigating improvements to the AFMA Derivative Turnover Report, and this is reflective of industry's willingness to address the foundation for the ACCC's concerns.

Conclusion

In conclusion, the Energy Council does not support broadening the AER's powers to demand information in anticipation of competition issues which may or may not develop. As energy markets have developed since the ACCC's recommendation was made nearly a year ago, the need has diminished, and there are other avenues for the AER to conduct its wholesale market monitoring functions. The AER has proven this by the publication of its *Wholesale Electricity Market Performance Report*, which was compiled without the need to compulsorily acquire data.⁸

Any questions about this submission should be addressed to the writer, by e-mail to Duncan.MacKinnon@energycouncil.com.au or by telephone on (03) 9205 3103.

Yours sincerely,



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⁷ Available at <https://afma.com.au/data>

⁸ Australian Energy Regulator, *Wholesale electricity market performance report*, December 2018