Energy Ministers Secretariat

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25 August 2022

To whom it may concern,

Amending the Australian Energy Regulator Wholesale Market Monitoring and Reporting Framework – Consultation Paper

ENGIE Australia & New Zealand (ENGIE) appreciates the opportunity to respond to the Energy Senior Officials ("the Officials") in response to the Amending the Australian Energy Regulator (AER) Wholesale Market Monitoring and Reporting Framework -Consultation Paper (the "Paper").

The ENGIE Group is a global energy operator in the businesses of electricity, natural gas and energy services. In Australia, ENGIE has interests in generation, renewable energy development, and energy services. ENGIE also owns Simply Energy which provides electricity and gas to more than 740,000 retail customer accounts across Victoria, South Australia, New South Wales, Queensland, and Western Australia.

The proposed reforms are far-reaching and thus require stronger justification

The reforms represent a highly significant shift in the information-gathering powers of the AER. The effect of abolishing Section 18D is to give the AER almost unfettered power to require information from market participants, across gas and electricity wholesale markets and their associated contract markets.

Reference to governments "needing more information" is unfortunate. The subject of the Paper is the increase in information powers of the AER which is not a government. AER provides *advice* to government based on the information it collects, but this is not the same as passing large volumes of highly commercially sensitive information to them. ENGIE trusts that this is simply a slip of the keyboard rather than reflecting the true intent of the reforms.

The examples given of why the powers are required do not provide a strong rationale for the proposed reforms. The paper opens with a summary of major drivers of the recent high energy price environment. ENGIE does not take issue with this analysis but notes that the drivers fall into two categories. Some of the drivers represent trends and information that are broadly already in the public domain, including persistent high international commodity prices (European gas demands have been affecting international gas prices

for over a year); the connection between gas and electricity markets (reforms to reflect this were first mooted over a decade ago) and the challenges in ensuring investment in infrastructure (multiple reform processes have been set up to facilitate new transmission and underpin new generation in recent years). Therefore, more information gathering powers were not required to discern these. Other drivers cited, such as unseasonable weather and unanticipated generation outages were not foreseeable and so the AER could not reliably forecast these even if it had greater information-gathering powers.

The more specific examples cited of retailer failures are also not sufficient justification alone for the major increase in powers sought. Retailer failure is a known risk in the NEM (and the gas markets) and the main concern is to avoid systemic failure rather than individual failure. The Paper would have benefited from an explanation of the plausible counterfactual and why it would have served the public interest for the AER to have information that these retailers were at risk of failure. ENGIE notes that avoidance or management of individual retailer failure is not one of the goals of the WMM clause in the NEL, nor is it mentioned in the AER's Statement of Approach to its WMM requirement.

More analytical rigour is necessary to understand the logic of the proposal to repeal Section 18D in full. The various provisions of 18D are not interdependent, that is, the section would still make sense if one or more elements were removed. So, it would be preferable to consider in turn each element and for the Paper to explain why it unduly constrained the AER in fulfilling its role.

The Paper largely focuses on the first element, the requirement to identify a concern based on public information. ENGIE understands that this requirement will serve as some sort of constraint, but it is not clear from the Paper how significant a constraint it is. It would be useful to know how far the AER has tried to push the public information requirement in carrying out its wholesale market monitoring (WMM) functions before determining that it is a material impediment in practice.

The second element is that the AER should not use confidential information for any purpose other than the performance of the AER WMM functions. This seems an eminently reasonable clause to retain. In combination these first two requirements are presumably in place in order to preclude the AER "going on a fishing expedition". No rationale has been given for why this clause hinders the AER from carrying out its functions.

The third element is that the AER must not disclose confidential supplier information unless it is for the purposes of the AER WMM functions. Again, no rationale has been given for why it would be in the public interest for disclosures to made under other circumstances.

A similar point can be made about the clause that obliges the AER to return a document it obtained from a supplier within 12 months or as soon as reasonably practical after the 12 months.

If section 18D is repealed, ENGIE requests that the officials consider an alternative form of wording that could act as some basic constraint on the AER's exercise of its powers. Appropriate wording could be of the form that the AER should request [confidential] information from participants for the purposes of its WMM functions only to the extent necessary for the AER carrying out its WMM functions.

The logic of the proposals implies a further extension of powers is likely in future

It is unlikely that this is the last time that this area of the law will be reviewed. For example, a key rationale for extending the AER's wholesale market monitoring powers to gas is that gas is an important fuel for electricity and there is limited transparency. However, currently, coal is a far more important fuel by volume, and coal plant is still sometimes the price-setter in the NEM. There are no facilitated markets for coal and so there is even less transparency than in gas markets. Accordingly, it seems a short step from gas to the AER seeking information from coal providers and rail infrastructure providers (to the extent they are involved in moving coal from mines to power plants). Other areas of interest could follow, maintenance contracts, more information about inverter software settings, etc.

The Paper appears to suggest normal commercial behaviour is a problem that needs addressing via regulatory intervention

The Paper raises a number of issues and scenarios to which the AER may not have full visibility of the participants' behaviour and explains that these are examples of why the AER needs the additional powers. Some examples include:

> "The AER cannot assess which generators may be opportunistically bidding and making 'super' profits" (p3).
>
> "Participants including gentailers that operate gas powered generators have reduced their total supply to gas markets and opted to sell a higher proportion of gas at market price caps" (p3)
>
> "failed retailers on-selling financial contracts for a profit while transferring customers to a retailer of last resort." (p4)

What is troubling is that on the face of it these are normal commercial behaviours. Gas and electricity markets were set up in the full knowledge that participants would typically be commercial, profit-maximising businesses (noting there remain several government-owned participants too) whose directors and managers have clear fiduciary duties to their shareholders. Numerous provisions in the Laws and Rules already exist to protect energy consumers from adverse consequences that may arise.

In considering the Potential Generator Market Power in the NEM rule change some years ago, the AEMC determined that it was entirely consistent with the operation of an energy only market that there be periods of transitory market power. Logically this is the only way that the marginal generator in the system could ever hope to earn back its capital. So periodic episodes where some generators make larger profits are part of the normal working of the markets. Of course, extended periods of high prices may indicate a market inefficiency, but if this should occur, it presumably constitutes publicly available information which means the AER's investigations are not constrained by Section 18D.

It is consistent with a market economy that resources are allocated to the highest value. Thus, if a participant finds it more profitable to sell gas into the gas market than use it to generate electricity then that is effective resource allocation. To the extent that this creates supply issues in the electricity market then that is indicative of an underlying long-term supply side issue, rather than due to the commercial imperatives on an individual participant.

Similarly, even a failing retailer has a fiduciary duty to its shareholders which may be best discharged by departing the market and unwinding its contracts.

The Paper indicates scope creep in the WMM requirement

The Paper makes numerous references to a forward-looking approach; with phrases such as "anticipate and avoid" (p2), "proactively anticipate" (p8), "visibility of a potential failure" (p8). This represents a substantial shift in policy as to what the AER's role is in respect of WMM. Such language does not exist either in the enabling clause in the Law or the AER's Statement of Approach. It would be appropriate to consult on the merits of expanding the role of the AER in this way, and for that consultation to contain some discussion as to how in practice the AER could use information to achieve a better outcome, before getting to the details as to whether and how this requires drafting changes to the Laws.

Significant new powers require consequential obligations on the AER

It's implied that the intent of the reforms is that the AER still uses them in a targeted manner rather than simply asking for continuous disclosure of all OTC contract information, for example. However, the proposed drafting affords almost total discretion to the AER in the volume and scale of its information requests. Arguably, one could make a case that to understand price outcomes, one needs to know the positions of all participants in the market as market settlement is the outcome of all bids in the market. Hence the importance of some countervailing wording in the NEL (and the NGL assuming the gas market is brought in scope as proposed) to ensure that information requests remain proportionate to the specific task of market monitoring.

The consequence of the AER's new powers is that it will find itself in possession of a large volume of commercially sensitive information, and it must take all necessary precautions to avoid this information being disclosed, either inadvertently or as the result of a cyberattack.

AER staff who have access to this information and are analysing it in order to carrying out the WMM function will have an unprecedentedly comprehensive view of the energy markets and individual participants' positions within these markets. This information will go well beyond the scope of confidential information that staff may acquire as part of an investigation into an individual company, and so will be especially commercially valuable. Consideration should be given to restrictions such as compulsory "gardening leave" for relevant staff who take a job with a market participant.

In respect of the proposed gas market information powers, the Paper notes "where information is already available to the AER as a result of obligations arising under new transparency requirements, it would be expected that the AER would not collect the same information in the exercise of its gas WMM function". This should not be merely an expectation but an obligation on the AER to avoid duplication of information requests in order to minimise the regulatory burden on participants.

If the reforms proceed, officials should also review opportunities to reduce the regulatory burden

ENGIE considers that despite the concerns raised in this submission, the reforms are likely to go ahead. There is an opportunity to deliver additional benefits by way of considering whether the AER's enhanced

surveillance capability means that existing regulatory burdens could be repealed or “sunsetted”. Some of these exist at least in part because commercial positions are not fully transparent.

For example, if the AER has a comprehensive view of all participants’ hedging positions and the ability to proactively identify risks in the market, then there could potentially be a case for reduced prudential requirements for fully hedged participants.

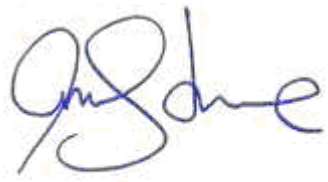
It could also reduce the need for the Retailer Reliability Obligation, which in practice is designed more to review participants’ hedging levels than to elicit new generation.

With these powers, the monitoring activities of the AER would be somewhat duplicative of the ongoing enquiries by the ACCC (of which the AER is a branch) into gas and electricity markets. These inquiries could be wound down early.

While this standard letter format has allowed us to make some broader points about the rationale for and potential consequences of the reform, we have also completed the submission template as requested, and this is included as an attachment to this letter.

Should you have any queries in relation to this submission please do not hesitate to contact me via email on jamie.lowe@engei.com.

Yours sincerely,



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