



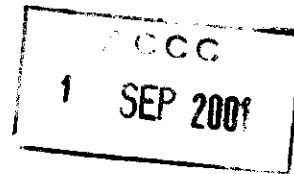
**NATIONAL ELECTRICITY CODE  
ADMINISTRATOR LIMITED**

ACN 073 942 775

Level 5, 41 Currie Street  
Adelaide SA 5000  
Telephone (08) 8213 6322  
Facsimile (08) 8213 6300

12 September 2001

Mr M Rawstron  
General Manager, Regulatory Affairs - Electricity  
ACCC  
PO Box 1199  
DICKSON ACT 2602



*Dear Mike,*

**GENERATORS' BIDDING AND REBIDDING STRATEGIES AND THEIR EFFECT ON PRICES**

We launched an investigation into generators' bidding and rebidding strategies and their effect on prices in May. The issues paper we published on 24 May, and the other material we made available to accompany it, taken together represent the most detailed and comprehensive information and analysis of bidding and rebidding and its effects available in the market. I enclose the Code Change Panel's report on the issues. The report follows extensive consultation on our May issues paper and on draft proposals for change that we published in July. It recommends changes to the market rules aimed at:

- ◆ tackling directly the inefficiencies that have led to the very short-term price spikes experienced in the market that have no basis in its underlying dynamics;
- ◆ requiring generators' bids and rebids to be made in good faith; and
- ◆ specifically addressing those aspects of generators' bidding and rebidding strategies that give cause for concern by imposing a prohibition on bids or rebids that materially prejudice the efficient, competitive or reliable operation of the market. This is intended to outlaw bids or rebids that withhold or withdraw capacity in order artificially to increase prices, establish circumstances where high-priced 'sleeper' bids are despatched, exploit network constraints or reductions in capacity, or manipulate other aspects of the market design.

We should also welcome separate discussions with you about the need to be satisfied that bidding and rebidding is appropriately subject to the relevant provisions of the Trade Practices Act governing the abuse of market power.

These revised proposals demonstrate that we have listened carefully to the valid arguments put to us, not just by generators, about the workability and the likely unintended consequences in particular of our original proposal for a prohibition on rebidding three hours ahead of despatch. Our revised proposals will preserve the essential flexibility rebidding provides to respond to changes in physical, and legitimate commercial, circumstances. They



will ensure that the market preserves the crucial signals for much-needed new investment and demand-side response that genuinely efficient and economic prices represent. Crucially, however, they will meet the objective we set ourselves as part of our original proposals to give the market rules real teeth to tackle those specific and targeted aspects of generators' bidding and rebidding strategies that have given cause for concern. Our proposal to outlaw those strategies is based closely on similar proposals developed, also following extensive consultation, by the Office of Gas and Electricity Markets (OFGEM) in England and Wales.

We are simultaneously publishing draft guidelines on how we intend to interpret the proposed prohibition on such strategies in practice. I enclose a copy. Those guidelines will be subject to further extensive and wide-ranging consultation. We should welcome the opportunity to liaise closely with the Commission in finalising those guidelines. As part of the consultation process, we shall seek also comments on the draft guidelines from the expert market advisory group we have established to help strengthen our surveillance, monitoring and enforcement capability.

Yours,

**Stephen Kelly**  
**Managing Director**

FORM A

COMMONWEALTH OF AUSTRALIA

*Trade Practices Act 1974 - Sub-section 88(1)*

EXCLUSIONARY PROVISIONS:

APPLICATIONS FOR AUTHORISATION

To the Australian Competition and Consumer Commission:

Application is hereby made under sub-section 88(1) of the *Trade Practices Act 1974* for an authorisation under that sub-section:

- to make a contract or arrangement, or arrive at an understanding, where a provision of the proposed contract, arrangement or understanding would be, or might be, an exclusionary provision within the meaning of section 45 of that Act; and
- to give effect to a provision of a contract, arrangement or understanding where the provision is, or may be, an exclusionary provision within the meaning of section 45 of that Act.

- 
1. (a) **Name of applicant (See Direction 2)** National Electricity Code Administrator Limited (ACN 073 942 775) (NECA)
- (b) **Short description of business carried on by applicant** Administration of the National Electricity Code ("the Code").
- (c) **Address in Australia for service of documents on the applicant** Mr Stephen Kelly  
Managing Director  
National Electricity Code Administrator Limited  
Level 5  
41 Currie Street  
ADELAIDE SA 5000  
Phone: (08) 8213 6307  
Fax: (08) 8213 6300
2. (a) **Description of contract, arrangement or understanding and, where already made, its date** The contract, arrangement or understanding with respect of which this application is made are those entered into by participants in the National Electricity Market, pursuant to the Code as amended in accordance with the Code Change Panel report submitted with this Form A (and the accompanying Forms B & E). These amendments

relate to generators' bidding and rebidding strategies and their effect on prices.

For the avoidance of doubt, this application relates only to generators' bidding and rebidding strategies and their effect on prices Code changes and not to the Code as a whole.

- (b) **Brief description of those provisions of the contract, arrangement or understanding that are, or would or might be, exclusionary provisions**  
*(See Direction 4)*
- (c) **Names and addresses of other parties or proposed parties to contract, arrangement or understanding**
3. **Names and addresses (where known) of parties and other persons on whose behalf application is made**
4. (a) **Grounds for grant of authorisation**
- See the Code Change Panel report submitted with this Form A (and the accompanying Forms B & E).
- Code Participants, being the National Electricity Market Management Company Limited (ACN 072 010 327) ("NEMMCO") and every person registered with NEMMCO as a Code Participant as at the date of this application and whose names and addresses are listed in Appendix A to this Form A and any other persons who subsequently register with NEMMCO under the Code as a Code Participant.
- This application is made on behalf of all code participants, being NEMMCO and every person registered with NEMMCO as a Code participant as of the date of this application and whose names and addresses are listed at Appendix A to this Form A.
- In addition this authorisation application is made on behalf of and in relation to all persons who become parties to the proposed contract or arrangement after it is made, or become a party to the proposed understanding at a time after it is arrived at, within the meaning of section 88(10) of the Act.
- Authorisation is sought on grounds set out in the Code Change Panel report, in accordance with clause 8.3 of the Code, submitted with this Form A.

- (b) **Facts and contentions relied upon in support of those grounds (See Notice 1)** These facts and contentions are set out in the Code Change Panel report.

5. **This application for authorisation may be expressed to be made also in relation to other contracts, arrangements or understandings or proposed contracts, arrangements or understanding, that are or will be in similar terms to the abovementioned contract, arrangement or understanding.**

(a) **Is this application to be so expressed?**

Yes, this application is made with respect to each other similar contract, arrangement or understanding or proposed contract arrangement or understanding for the purposes of section 88(13), (14) and (15) of the Act.

(b) **If so, the following information is to be furnished:**

(i) **the names of the parties to each other contract, arrangement or understanding**

The applicant and all Code Participants (being NEMMCO and every person registered with NEMMCO as a Code Participant as at the date of this application and whose names and addresses are listed in Appendix A to this Form A within the meaning of section 88(10) of the Act)

(ii) **the names of the parties to each other proposed contract, arrangement or understanding which names are known at the date of this application (See Direction 5 and Notice 2)**

The applicant and all Code Participants (being NEMMCO and every person registered with NEMMCO as a Code Participant as at the date of this application and whose names and addresses are listed in Appendix A to this Form A within the meaning of section 88(10) of the Act) and any other persons who subsequently register with NEMMCO under the Code as a Code Participant. The names of those persons who will register with NEMMCO as a Code Participant are not known at this time.

6. (a) Does this application deal with a matter relating to a joint venture (See section 4J of the *Trade Practices Act 1974*)? No
- (b) If so, are any other applications being made simultaneously with this application in relation to that joint venture? Not applicable
- (c) If so, by whom or on whose behalf are those other application being made? Not applicable
7. Name and address of person authorised by the applicant to provide additional information in relation to this application. Mr Stephen Kelly  
Managing Director  
National Electricity Code Administrator Limited  
Level 5  
41 Currie Street  
ADELAIDE SA 5000  
Phone: (08) 8213 6307  
Fax: (08) 8213 6300

Date: 12 September 2001

Signed on behalf of NECA

.....  
(Signature) Stephen Kelly .....

Mr Stephen Kelly  
Managing Director  
National Electricity Code Administrator Limited

\* **Note:** References in this application to the Act are references to the *Trade Practices Act 1974* and also include the Competition Codes of New South Wales, Victoria and the Australian Capital Territory as defined in the Competition Reform legislation in force in each jurisdiction.

FORM B

COMMONWEALTH OF AUSTRALIA

*Trade Practices Act 1974 - Sub-section 88(1)*

AGREEMENTS AFFECTING COMPETITION:

APPLICATIONS FOR AUTHORISATION

To the Australian Competition and Consumer Commission:

Application is hereby made under sub-section 88(1) of the *Trade Practices Act 1974* for an authorisation under that sub-section:

- to make a contract or arrangement, or arrive at an understanding, a provision of which would have the purpose, or would have or might have the effect, of substantially lessening competition within the meaning of section 45 of that Act; and
- to give effect to a provision of a contract, arrangement or understanding which provision has the purpose, or has or may have the effect, of substantially lessening competition within the meaning of section 45 of that Act.

- 
- |  |   |
|--|---|
| 1. (a) Name of applicant ( <i>See Direction 2</i> )  | National Electricity Code Administrator Limited (ACN 073 942 775) (NECA)  |
| (b) Short description of business carried on by applicant                                      | Administration of the National Electricity Code.  |
| (c) Address in Australia for service of documents on the applicant                             | Mr Stephen Kelly<br>Managing Director<br>National Electricity Code Administrator Limited<br>Level 5<br>41 Currie Street<br>ADELAIDE SA 5000<br>Phone: (08) 8213 6307<br>Fax: (08) 8213 6300             |
| 2. (a) Description of contract, arrangement or understanding and, where already made, its date | The contract arrangement or understanding in respect of which the application is made is set out in the Code Change Panel report submitted with this Form B, being amendments to the Code in respect of |

generators' bidding and rebidding strategies and their effect on prices.

For the avoidance of doubt, this application relates only to generators' bidding and rebidding strategies and their effect on prices Code changes and not to the Code as a whole.

- (b) **Names and addresses of other parties or proposed parties to contract, arrangement or understanding**
- Code Participants, being the National Electricity Market Management Company Limited (ACN 072 010 327) ("NEMMCO") and every person registered with NEMMCO as a Code Participant as at the date of this application and whose names and addresses are listed in Appendix A to this Form B and any other persons who subsequently register with NEMMCO under the Code as a Code Participant.
3. **Names and addresses (where known) of parties and other persons on whose behalf application is made**
- This application is made on behalf of all Code participants, being NEMMCO and every person registered with NEMMCO as a Code participant as of the date of this application and whose names and addresses are listed at Appendix A to this Form B.
- In addition this authorisation application is made on behalf of and in relation to all persons who become parties to the proposed contract or arrangement after it is made, or become a party to the proposed understanding at a time after it is arrived at, within the meaning of section 88(10) of the Act.
4. (a) **Grounds for grant of authorisation**
- Authorisation is sought on the grounds set out in the Code Change Panel report, submitted with this form B and the accompanying Forms A and E.
- (b) **Facts and contentions relied upon in support of those grounds (See Notice 1)**
- The facts and contentions relied upon are set out in the Code Change Panel report.
5. **This application for authorisation may be expressed to be made also in relation to other contracts, arrangements or understandings or proposed**



**contracts, arrangements or understanding, that are or will be in similar terms to the abovementioned contract, arrangement or understanding.**

**(a) Is this application to be so expressed?** Yes, this application is made with respect to all similar other contracts, arrangements or understandings, or proposed other contracts arrangements or understandings, for the purposes of sections 88(13), (14) and (15) of the Act. The terms of such other contracts are comprised in the Code as amended by the Code changes.

**(b) If so, the following information is to be furnished:**

**(i) the names of the parties to each other contract, arrangement or understanding** The applicant and all Code Participants (being NEMMCO and every person registered with NEMMCO as a Code Participant as at the date of this application and whose names and addresses are listed in Appendix A to this Form B within the meaning of section 88(10) of the Act).

**(ii) the names of the parties to each other proposed contract, arrangement or understanding which names are known at the date of this application (See Direction 5 and Notice 2)** The applicant and all Code Participants (being NEMMCO and every person registered with NEMMCO as a Code Participant as at the date of this application and whose names and addresses are listed in Appendix A to this Form B within the meaning of section 88(10) of the Act) and any other persons who subsequently register with NEMMCO under the Code as a Code Participant. The names of those persons who will register with NEMMCO as a Code Participant are not known at this time.

**6. (a) Does this application deal with a matter relating to a joint venture (See section 4J of the Trade Practices Act 1974)?** No.

**(b) If so, are any other applications being made simultaneously with this application in relation to** Not applicable.

**that joint venture?**

**(c) If so, by whom or on whose behalf are those other application being made?**

Not applicable.

**7. Name and address of person authorised by the applicant to provide additional information in relation to this application.**

The person nominated in item 1(c) of this form.

Date: 12 September 2001

Signed on behalf of NECA

..... Stephen Kelly .....

(Signature)

Mr Stephen Kelly  
Managing Director  
National Electricity Code Administrator Limited

**\* Note:** References in this application to the Act are references to the *Trade Practices Act 1974* and also include the Competition Codes of New South Wales, Victoria and the Australian Capital Territory as defined in the Competition Reform legislation in force in each jurisdiction.

FORM E

COMMONWEALTH OF AUSTRALIA

*Trade Practices Act 1974 - Sub-section 88( 8)*

EXCLUSIVE DEALING:

APPLICATIONS FOR AUTHORISATION

To the Australian Competition and Consumer Commission:

Application is hereby made under sub-section 88(1) of the *Trade Practices Act 1974* for an authorisation under that sub-section to engage in conduct that constitutes or may constitute the practice of exclusive dealing.

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1. (a) **Name of applicant** (*See National Electricity Code Administrator Direction 2*) Limited (ACN 073 942 775) (NECA)
- (b) **Short description of business carried on by applicant** Administration of the National Electricity Code.
- (c) **Address in Australia for service of documents on the applicant** Mr Stephen Kelly  
Managing Director  
National Electricity Code Administrator  
Limited  
Level 5  
41 Currie Street  
ADELAIDE SA 5000  
Phone: (08) 8213 6321  
Fax: (08) 8213 6300
2. (a) **Description of the goods or services in relation to the supply or acquisition of which this application relates** The goods or services in relation to the supply or acquisition of which this application relates is electricity sold into the National Electricity market, as affected by the amendments set out in the Code Change Panel report submitted with this Form E.

For the avoidance of doubt, this application relates only to generators' bidding and

rebidding strategies and their effect on prices Code changes and not to the Code as a whole.

**(b) Description of the conduct that would or may constitute the practice of exclusive dealing (See Direction 4)** The supply of electricity or provision of network services on condition that both the acquisition and resale is in accordance with the Code.

The acquisition of electricity or network services on the condition that the supply is in accordance with the Code.

Refusing to supply or acquire electricity or network services because the supplier/acquirer has failed to comply with the Code.

Aiding, abetting, procuring, counselling or inducing any corporation to engage in any of the above-mentioned conduct.

**3. (a) Class or classes or persons to which the conduct relates**

The classes of persons are:

- (i) the applicant;
- (ii) Code Participants, being the National Electricity Market Management Company Limited (ACN 072 010 327) ("NEMMCO") and every person registered with NEMMCO as a Code Participant and whose names and addresses are listed in Appendix A to this Form E; and
- (iii) any other subsequent parties to the Code, being all parties who register with NEMMCO under the Code as a Code Participant.

This application is made on behalf of each person identified in Appendix A to this Form E. In addition:

- (a) the authorisation being applied for by this application is, in accordance with section 88(8AA) of the Act, to

be expressed so as to apply to the applicant and every person who is registered with NEMMCO as a Code Participant as at the date of this application (being the persons identified in Appendix A to this Form E), and in relation to each other person who becomes a party to the Code by registering with NEMMCO as a Code Participant; and

- (b) this application is expressed to be made also in relation to other proposed contracts, industry codes of practice, arrangements or understandings that will be in similar terms to the Code within the meaning of sections 88(13), 88(14) and 88(15) of the Act, being each of the proposed contracts, industry codes of practice, arrangements or understandings to be made between a person who registers with NEMMCO under the Code as a Code Participant, the applicant, and each existing participant under the Code at that time.

The names of the parties to each other proposed contract, industry code of practice, arrangement or understanding which are known at the date of this application are the applicant and Code Participants (being NEMMCO and each person who is registered with NEMMCO as a Code Participant as at the date of this application and identified in Appendix A to this Form E). Other than to state that the other parties to each proposed contract, industry code of practice, arrangement or understanding for the purposes of section 88(13), (14) and (15) of the Act will be persons who register with NEMMCO under the Code as a Code Participant and each existing Participant

under the Code at that time, the names of those other parties are not known as at the date of this application.

- |  |  |    |
|--|--|----|
| <b>(b) Number of those persons</b>   | <b>(i) At present time</b>   |    |
|  | NECA   | 1  |
|  | NEMMCO   | 1  |
|  | Generators   | 41 |
|  | Customers  | 31 |
|  | Network Service Providers  | 25 |
|  | Special Participants   | 19 |
|  | Intending Participants   | 6  |
|  | Traders  | 8  |
|  | <b>(ii) Estimated within the next year</b>   |    |
|  | Unknown  |    |
| <b>(c) Where number of persons stated in item 3(b)(i) is less than 50, their names and addresses</b>                                 | Not applicable   |    |
| <b>4. (a) Grounds for grant of authorisation</b>   | Authorisation is sought on the grounds set out in the Code Change Panel report, copies of which are submitted with this Form E (and the accompanying Forms A and B). |    |
| <b>(b) Facts and contentions relied upon in support of those grounds (See Notice)</b>  | The facts and contentions relied upon in respect of the Code changes are set out in the Code Change Panel report.  |    |
| <b>5. (a) Does this application deal with a matter relating to a joint venture (See section 4J of the Trade Practices Act 1974)?</b> | No.  |    |
| <b>(b) If so, are any other applications being made simultaneously with this application in relation to that joint venture?</b>      | Not applicable.  |    |
| <b>(c) If so, by whom or on whose behalf are those other applications being</b>  | Not applicable   |    |

made?

6. **Name and address of person authorised by the applicant to provide additional information in relation to this application.** Mr Stephen Kelly  
Managing Director  
National Electricity Code Administrator  
Limited  
Level 5  
41 Currie Street  
ADELAIDE SA 5000  
Phone: (08) 8213 6307  
Fax: (08) 8213 6300

Date: 12 September 2001

Signed on behalf of NECA

..... Stephen Kelly .....  
(Signature)

Mr Stephen Kelly  
Managing Director  
National Electricity Code Administrator Limited

**\* Note:** References in this application to the Act are references to the *Trade Practices Act 1974* and also include the Competition Codes of New South Wales, Victoria and the Australian Capital Territory as defined in the Competition Reform legislation in force in each jurisdiction.

# **Appendix A**

**to**

**Form A Application for Authorisation in respect of  
Exclusionary Provisions**

**Form B Application for Authorisation in respect of  
Agreements Affecting Competition**

**Form E Application for Authorisation in respect of  
Exclusive Dealing**

**List of Code participants**





**List of Code participants as at 12 September 2001**

<b>Company Aliases</b>	<b>Street Address</b>	<b>City</b>	<b>State</b>	<b>Postcode</b>
ActewAGL Distribution	221-223 London Circuit	CANBERRA	ACT	2601
AES Transpower Holding Pty Ltd	Level 5, 416 Collins Street	MELBOURNE	VIC	3000
AGL Electricity Ltd	Level 2, 333 Collins Street	MELBOURNE	VIC	3000
AGL Electricity Ltd	AGL Centre, 111 Pacific Highway	NORTH SYDNEY	NSW	2060
AGL (South Australia)	Level 1, 122 Frome Street	ADELAIDE	SA	5000
AGL South Australia Pty Ltd	1 Anzac Highway	KESWICK	SA	5035
Aurora Energy Pty Ltd	GPO Box 191	HOBART	TAS	7000
Australian Energy Services Pty Ltd	38 Gilby Road	MT WAVERLEY	VIC	3149
Australian Inland Energy	Administrative Building, 160-162 Beryl Street	BROKEN HILL	NSW	2880
BIEP Pty Ltd	PO Box 4	PINKENBA	QLD	4008
Callide Power Trading Pty Ltd	Central Plaza 2, 21st Floor, 66 Eagle Street	BRISBANE	QLD	4000
Citipower Pty	Level 15, Citipower House, 628 Bourke Street	MELBOURNE	VIC	3000
Country Energy	PO Box 172	BATHURST	NSW	2795
CS Energy Ltd	Level 21, 66 Eagle Street	BRISBANE	QLD	4000
CSR Limited	Pioneer Mill	BRANDON	QLD	4808
Delta Electricity	Level 12, Darling Park, 201 Sussex Street	SYDNEY	NSW	2000
Duke Energy Australia Trading & Marketing Pty Ltd	Level 17, 1 Castlereagh Street	SYDNEY	NSW	2000

Company Aliases	Street Address	City	State	Postcode
Duke Energy Bairnsdale Operations Pty Ltd	PO Box 7863	BRISBANE	QLD	4000
Edison Mission Energy Australia Ltd	Level 20, HWT Tower Southgate	SOUTH MELBOURNE	VIC	3205
EDGE Cap	Level 8, IBM Building, 60 City Road	SOUTH BANK	VIC	3006
EDL Plant Services Pty Ltd	Level 2, 199 Toorak Road	SOUTH YARRA	VIC	3141
ElectraNet SA	PO Box 7096	ADELAIDE	SA	5000
Electricity Supply Industry Planning Council	GPO BOX 2010	ADELAIDE	SA	5001
EMMLINK Pty Ltd	Level 24, AMP Place, 10 Eagle Street	BRISBANE	QLD	4000
Energex Ltd	150 Charlotte Street	BRISBANE	QLD	4000
Energex Retail Pty Ltd	Level 6, Anzac Square Building, Commercial Towers	BRISBANE	QLD	4006
Energy Australia	Level 22, 570 George Street	SYDNEY	NSW	2000
Energy Brix Australia Corporation Pty Ltd	Hazelwood Drive	MORWELL	VIC	3840
Enron Australia Energy Pty Ltd	Level 21, 9 – 11 Castlereagh Street	SYDNEY	NSW	2000
Enron Australia Finance Pty Ltd	Level 21, 9 Castlereagh Street	SYDNEY	NSW	2000
Eraring Energy (formerly Pacific Power)	GPO Box 5257	SYDNEY	NSW	2000
Ergon Energy Corporation Ltd (network)	Level 4, 126 Margaret St 30 Marble Street	Brisbane	QLD	4002
Ergon Energy Pty Ltd (Retail)	Ground floor, 61 Mary Street	BRISBANE	QLD	4001
Ergon Energy (Victoria) Pty Ltd	Level 2, 150 Albert Road	SOUTH MELBOURNE	VIC	3205
Ferrier Hodgson Electricity Pty Ltd	Level 17, 2 Market Street	SYDNEY	NSW	2000
Hazelwood Power	Brodribb Road	MORWELL	VIC	3840
Hong Kong Electric International Ltd	Level 28, Rialto, 525 Collins Street	MELBOURNE	VIC	3000

Company Aliases	Street Address	City	State	Postcode
HQI Australia Limited Partnership	Level 24, AMP Place, 10 Eagle Street	BRISBANE	QLD	4000
Integral Energy Australia	51 Huntingwood Drive	HUNTINGWOOD	NSW	2148
Loy Yang Power Management Ltd	Bartons Lane	TRARALGON SOUTH	VIC	3844
Macquarie Bank Ltd	GPO Box 4294	SYDNEY	NSW	1164
Macquarie Generation	34 Griffiths road	LAMBTON	NSW	2299
Meridian Energy Australia Pty Ltd	Level 12, 37 Bligh Street	SYDNEY	NSW	2000
Millmerran Energy Trader Pty Ltd	Level 18, Comalco Place 12 Creek Street	BRISBANE	QLD	4000
Morgan Stanley Dean Witter Australia Finance Ltd	1585 Broadway, 4 <sup>th</sup> Floor,	NEW YORK	10036 -8293	USA
National Power South Australia Investments Ltd	Level 2, 122 Frome Street	ADELAIDE	SA	5000
National Power Synergen Pty Ltd	168 Greenhill Road	PARKSIDE	SA	5063
National Power Synergen Pty Ltd	Level 26, Australia Square, 264-278 George Street	SYDNEY	NSW	2000
NRG Flinders Operating Services Pty Ltd	168 Greenhill Road	PARKSIDE	SA	5063
National Electricity Market Management Company Limited	Level 16, 461 Bourke Street	MELBOURNE	VIC	3000
NSW Electricity Transmission Authority (TransGrid)	Cnr Park and Elizabeth Streets	SYDNEY	NSW	2000
Origin Energy Electricity Ltd	Level 39, AMP Centre, 50 Bridge Street	SYDNEY	NSW	2000
Powercor Australia Ltd	Level 8, 40 Market Street	MELBOURNE	VIC	3000
Pulse Energy Pty Ltd	Shell House, 1 Spring Street	MELBOURNE	VIC	3000
Queensland Electricity Transmission Corporation Ltd (Powerlink Queensland)	33 Harold Street	VIRGINIA	QLD	4104

<b>Company Aliases</b>	<b>Street Address</b>	<b>City</b>	<b>State</b>	<b>Postcode</b>
Queensland Power Trading Corporation trading as Enertrade)	15th Floor, 61 Mary Street	BRISBANE	QLD	4000
Redbank Project Pty Ltd	112 Longpoint Road-West	WALKWORTH via Singleton	NSW	2330
RMB Australia Ltd	Level 5, 37-49 Pitt Street	SYDNEY	NSW	2000
SG Australia	Level 21, 400 George St	SYDNEY	NSW	2000
Sithe Australia Power Services Pty Ltd	Level 12, The Chifley Tower, 2 Chifley Square	SYDNEY	NSW	2000
Snowy Hydro Trading Pty Ltd	Level 17, Bligh House, 4 Bligh Street	SYDNEY	NSW	2000
Snowy Mountains Hydro-Electric Authority	Monaro Highway	COOMA	NSW	2630
Southern Hydro Partnership	Level 13, 500 Collins Street	MELBOURNE	VIC	3000
SPI PowerNet Pty Ltd	25 Flinders Lane, Milton House	MELBOURNE	VIC	3000
Stanwell Corporation Ltd	GPO Box 773	BRISBANE	QLD	4001
State Electricity Commission of Victoria	Level 5, 452 Flinders Street	MELBOURNE	VIC	3000
Tarong Energy Corporation Ltd	Level 10, AMP Place, 10 Eagle Street	BRISBANE	QLD	4000
TXU (South Australia) Pty Ltd	Level 18, 452 Flinders Street	MELBOURNE	VIC	3000
TXU Electricity Ltd	168 Greenhill Road	PARKSIDE	SA	5063
United Energy Ltd	Level 13, 101 Collins Street	MELBOURNE	VIC	3000
Utilities Management Pty Ltd	Level 6, 1 Anzac Highway	KESWICK	SA	5035
VENCORP	PO Box 1721	COLLINGWOOD	VIC	3066
Yallourn Energy Pty Ltd	Eastern Road	MOE	VIC	3825
Yamasa Seafood Australia Pty Ltd	20 Gilbertson Road	LAVERTON NORTH	VIC	3026

### Known intending participants

Auspine Green Energy Pty Ltd	PO Box 79	MOUNT GAMBIER	SA	5290
Beak Industries Pty Ltd	Applicant only at this stage – no address details			
CEPA (Kogan Creek) Holding	GPO BOX 2256	BRISBANE	QLD	4001
Herschel Electricity Partners Pty Ltd	Applicant only at this stage – no address details			
Hydro-Electric Corporation	GPO Box 335	Hobart	TAS	7001
Murraylink Transmission Co Pty Ltd	GPO Box 7077, Riverside Centre	BRISBANE	QLD	4001
National Grid International Ltd.	Level 52, Rialto South Tower, 525 Collins Street	MELBOURNE	VIC	3000
Origin Energy Electricity Limited	Applicant only at this stage – no address details			
Pacific Hydro Limited	Applicant only at this stage – no address details			
Sleiman Trading Pty Ltd	PO Box 334	POTTS POINT	NSW	2001
Snowylink 1 Pty Ltd	Applicant only at this stage – no address details			
Southerlink Transmission Company Pty Ltd	GPO Box 7707 Riverside Centre	BRISBANE	QLD	4001
Transend Networks Pty Limited	1 Bowen Road	Moonah	TAS	7009
Wambo Power Ventures Pty Ltd	Level 1, Princeton Court Three, 13 Princeton Street	KENMORE	QLD	4069



## **DRAFT GUIDELINES**

**Ensuring the efficient, economic and reliable  
operation of the national electricity market**

**September 2001**



**Ensuring the efficient, economic and reliable operation of the national electricity market  
Draft guidelines**

Clause 3.8.22B of the National Electricity Code provides that a market participant must not submit a despatch bid, network despatch offer, despatch offer or rebid if it has the purpose, or has or is likely to have the effect, of materially prejudicing the efficient, competitive or reliable operation of the market, unless the market participant has reasonable cause for the despatch bid, network despatch offer, despatch offer or rebid.

**Purpose of the guidelines**

These guidelines, prepared in accordance with clause 3.8.22B(b) of the Code, are intended to assist market participants to understand:

- ◆ how NECA will exercise its powers to enforce this provision, by providing general examples of conduct that may be investigated; and
- ◆ the procedures NECA will follow when investigating possible breaches of the provision.

The guidelines contain a non-exhaustive list of the sort of conduct that may be investigated. They are indicative only. They are not legally binding on NECA and do not affect the legal scope of the provision. NECA intends, however, to act in accordance with the guidelines and will give its reasons if it departs from them.

**Actions that may prejudice the efficient, competitive or reliable operation of the market**

High prices or price spikes that reflect the underlying dynamics of supply and demand, or are the result of the normal operation of a competitive market, would not of themselves breach the provision. This includes legitimate, very high, prices for the final increment of capacity. NECA will therefore investigate the circumstances of any potential or alleged breach of the provision very carefully, and will provide relevant market participants with adequate and appropriate opportunities to explain their actions, before deciding whether to exercise its discretion to take an alleged breach of the provision to the National Electricity Tribunal.

The sorts of actions that, in NECA's view, may have the effect of materially prejudicing the efficient, competitive or reliable operation of the market include:

- ◆ withholding capacity from the market in order artificially to increase prices;
- ◆ establishing the circumstances where high-priced 'sleeper' bids or rebids are despatched;
- ◆ exploiting network constraints or rebidding following reductions in generating or network capacity or increases in demand, in a manner that is wholly disproportionate to changes in actual or opportunity costs; and
- ◆ manipulating dynamic capability.

**Withholding capacity.** Withholding capacity has the potential materially to prejudice the market through, amongst other things:

- ◆ artificially increasing prices;
- ◆ increasing risks to the reliability and security of supply; or
- ◆ bringing the market into disrepute, eg because prices would no longer be seen to reflect the underlying fundamentals of supply and demand.

Prima facie evidence of questionable withholding would exist if the amount of capacity a participant presented for despatch in a region was materially less than its registered capacity at a time when market forecasts had indicated potential shortfalls of capacity in that region sufficiently far in advance for the participant reasonably to have increased the amount of capacity offered. NECA would measure a shortfall or potential shortfall for this purpose as a condition which prompted NEMMCO to issue a low reserve notice. NECA recognises that participants must rely on information provided in PASA and, close to despatch, the pre-despatch forecasts. These processes are, by design, iterative. NECA would expect a faster response close to despatch. It would recognise, however, that it will be difficult, if not impossible, for a participant to interrupt a lengthy maintenance programme once it has commenced.

**Sleeper bids.** The practice of bidding significant proportions of high capacity factor plant at very high levels, whilst ensuring that the capacity is available to the market and therefore that reserve levels remain appropriate, exposes the market to the risk of inefficient and uneconomic outcomes.

**Exploiting network constraints, reductions in capacity or increases in demand.** Rebids, especially very close to despatch, that follow interconnector constraints or unplanned reductions in the amount of generating or network capacity, or increases in demand, can have the effect of changing the market price in a manner wholly disproportionate to changes in actual or opportunity costs. High prices in such circumstances can, and will,



often appropriately reflect the dynamics of the market and therefore represent genuine price signals. The emphasis in determining whether or not the behaviour that led to those prices breached clause 3.8.22B will therefore be on the proportionality of the response, and the extent to which it represented a genuine, efficient and competitive market response. Thus, for example, high prices indicative of shortfall would generally be expected under peak conditions where it is important to provide incentives to very low capacity factor generation and demand-side response. NECA also recognises the importance, in assessing opportunity costs especially for energy-constrained plant, for the assessment to take a sufficiently long-term perspective. High prices set by high capacity factor resources under conditions where peak plant was not despatched would, however, be a matter for investigation, not on the basis of high prices alone but to determine whether the responses were proportionate or significantly out of line with what might be expected in a competitive market.

**Manipulating dynamic capability.** Dynamic capability such as ramp rates demonstrably below good industry practice for the type of unit can artificially force despatch of high-priced capacity. It would be of particular concern if the flexibility to rebid ramp rates resulted in inefficient and uneconomic increased or decreased responsiveness.

#### **Investigation of potential or alleged breaches**

NECA will investigate potential or alleged breaches of clause 3.8.22B using its powers to require information under clause 8.5.1 of the Code and in accordance with the existing guidelines on the use of those powers. NECA would, however, expect to use those powers only:

- ◆ in relation to a specific alleged breach of the Code and where NECA is satisfied that there is sufficient prima facie evidence of the alleged breach to warrant use of the powers;
- ◆ where, following discussion with the relevant Code participant(s) and others, the Code participant(s) refuses to provide the information voluntarily;
- ◆ after NECA has provided the relevant Code participant(s) with a formal opportunity to explain why the information should not be requested;
- ◆ where the information is not cost effectively available from any other source; and
- ◆ with the express approval of the monitoring and surveillance committee of the NECA board.

Where NECA does make use of its powers under clause 8.5.1, it will:

- ◆ restrict the information required to that which is reasonably necessary to investigate the alleged breach of the Code;

- ◆ specify in writing the specific information required; and
- ◆ consult with the relevant Code participant(s) to determine a reasonable time in which to provide the information.

NECA will use its powers under clause 8.5.1(b) to appoint a person to investigate a matter on its behalf only as a last resort, and where the relevant Code participant(s) has failed to comply with a formal request for the information and has been provided with a formal opportunity to explain why it has failed to comply with that request and that explanation has failed reasonably to satisfy NECA.

### **Revision and review of guidelines**

These guidelines may need to be amended in the light of experience. Any amendments will, however, only be made in accordance with the Code consultation procedures. NECA will also formally review the guidelines, again in accordance with the Code consultation procedures, by 31 December 2003.

**National Electricity Code Administrator  
September 2001**



## **CODE CHANGE PANEL**

# **Generators' bidding and rebidding strategies and their effect on prices**

## **Volume 1 Report**

**September 2001**



**Code Change Panel**  
**Generators' bidding and rebidding strategies and their effect on prices**  
**Report**

**Executive summary**

NECA has consistently made clear that rebidding in its view represents an essential flexibility to enable generators to respond to changes in physical and legitimate commercial, circumstances. It is imperative for the effective operation of the market. Efficient prices represent crucial signals for much-needed new investment and for demand-side responses. Regulatory responses that have the effect of artificially constraining prices that properly reflect the underlying dynamics of the market will distort those crucial signals and jeopardise the new investment already committed or planned, and future prospective investments, in the market. NECA has therefore been at pains to avoid such responses.

Many of the very short-term price spikes that have been experienced in the market, however, and aspects of generators' bidding and rebidding strategies, have nonetheless given cause for concern. Those very short-term spikes often do not represent genuine price signals. Nor, by definition, would the effects of inappropriate bidding and rebidding behaviour. They have no basis in the underlying dynamics of the market. They are only made possible by the current incomplete state of development of the market and the lack, therefore, of a fully competitive outcome. It is only once such an outcome is achieved that the market will deliver genuinely efficient prices. Such an outcome depends, however, on increased investment, and full and unfettered competition. The current absence of a fully competitive outcome is especially a cause for concern in the electricity market. The instantaneous nature of the market means that it is particularly important to ensure that genuine opportunities for competitive responses, and appropriate checks and balances, exist. The introduction of new and more effective rules also needs to be accompanied by stringent monitoring, surveillance and enforcement of those rules.

NECA and the Code Change Panel therefore propose changes to the Code to:

- ◆ work with NEMMCO and the market to begin to tackle, in particular, the treatment of short-term loading constraints and the handling of non-market ancillary services. The changes are intended as part of a broader programme of

work to address those and other current inefficiencies in the operation of the market; and

- ◆ require generators' bids and rebids to be made in good faith. This includes the obligation for those bids and rebids to represent their genuine intentions at the time they are made. NECA and the Panel propose that this requirement should be accompanied by a shift in the onus of proof so that, in any proceeding, a generator would be required to satisfy the National Electricity Tribunal its bid or rebid was genuinely made in good faith.

NECA had originally proposed a prohibition on rebidding, subject to appropriate but tightly defined exemptions, three hours ahead of despatch. NECA and the Panel are, however, persuaded of the practical and other disadvantages of such a prohibition. We are seeking instead to identify and prohibit the specific sorts of bidding and rebidding behaviour that are objectionable. This includes, in particular, exploiting transmission constraints and engineering the calling of inappropriately high-priced bids. We propose to tackle such behaviour through a prohibition on bids or rebids that have the purpose, or have or are likely to have the effect, of materially prejudicing the efficient, competitive or reliable operation of the market. This will bring the Australian market into line with other major markets worldwide in addressing market behaviour directly within the market rules. The proposed prohibition will be supported by guidelines, on which NECA intends to consult extensively, on how it would enforce that prohibition.

## **Background**

NECA's report of 31 July on generators' bidding and rebidding strategies and their effect on prices recommended changes to the market rules and the way those rules operate in practice in order to:

- ◆ tackle the current inefficiencies in the operation of the market in particular in relation to transfer limits across interconnectors, short-term loading constraints, the efficiency of despatch and network services;
- ◆ require generators' initial bids and rebids to represent their genuine intentions at the time they are made;
- ◆ further strengthen the information disclosure obligations surrounding rebidding to ensure that the reasons for rebids are authorised at an appropriate level; and
- ◆ prohibit rebidding within three hours of despatch, with only very limited and closely-defined exceptions connected to the physical operation of the plant.

At the same time as NECA published its report, the Code Change Panel published a consultation paper on the draft changes to the Code necessary to give effect to the report's conclusions and recommendations. We received 26 written comments on those draft changes from CS Energy, Delta Electricity, Edison Mission Energy Australia,

Energex, Energy Australia, Enertrade, Enron Australia, Eraring Energy, Ergon Energy, Hydro Tasmania, InterGen Australia, Loy Yang Power, Macquarie Generation, NEMMCO, National Generators' Forum, NRG Asia-Pacific, Origin, Snowy Hydro Trading, the South Australian Department of Treasury and Finance, Southern Hydro, Stanwell, Synergen Power, Tarong Energy, TransÉnergie Australia, TXU and Yallourn Energy. Copies of those written comments are contained in volume 2 of this report. The Panel also held a public forum on 14 August to discuss the draft changes. In addition, NECA and the Panel have held a number of formal and informal discussions with Code participants and others.

### **Tackling short-term price spikes**

NECA's report drew attention to a number of very short-term price spikes either directly as a result of inefficiencies in the market rules or the way those rules are applied in practice; or as a result of individual generators taking advantage of those inefficiencies to drive up prices. It concluded that some very short-term price spikes often have no basis in the underlying dynamics of the market. They do not represent a genuine price signal to either the supply side, in terms of the need for new investment, or the demand side of the market. Moreover, because by their nature they arise so suddenly and are so very short-term, no competitive response is possible.

NECA's evidence to the South Australian electricity taskforce drew attention to four specific examples of market inefficiencies and to the need to take urgent action to improve the operation of the market in order to remove the opportunities they create for generators to exploit them:

- ◆ **transfer limits across interconnectors.** The over-conservative application of transfer limits on the Victoria to South Australia interconnector has led directly to sustained periods of prices above \$100/MWh. There is no trade-off in the decision-making process, however, between the application of those restrictions and their effect on prices;
- ◆ **short-term loading constraints.** The Code currently requires the restoration of the system to a secure operating state following a credible contingency or a significant change in power system conditions "as soon as it is practicable to do so and, in any event, within 30 minutes." NEMMCO currently interprets this to mean, wherever possible, within a single (five-minute) despatch interval. This interpretation leads to inefficient and expensive short-term despatch of unnecessary additional plant. It is stricter than applied before the launch of the market when firmer tie-line control was used in conjunction with predictive scheduling. This allowed the delays in the start-up of gas turbine plant to be taken into account in deciding whether or not to accept a short-term overload;
- ◆ **efficiency of despatch.** The draft report of NECA's review of the scope for integrating the energy market and network services pointed to the tendency for constraint equations to be written relatively to favour local generation. This is

the case, for example, in relation to Ladbroke Grove in South Australia and generators in south-east Queensland. It arguably breaches one of the fundamental objectives of the market, that intrastate trading should not be treated more or less favourably than interstate trading. It can, and does, lead to relatively more expensive plant being despatched even where cheaper sources would have been available for import across an interconnector. NECA has elaborated on these points in material it has presented to NEMMCO's constraints working group, of which it is a member; and

- ◆ **network services.** NECA's report argued that there is scope within the existing arrangements for NEMMCO to make more use of, for example, load shedding, real and reactive support and scheduling, and unit commitment contracts. Network services, including real-time ancillary services, could also in NECA's view be developed to help to cope with the consequences of interconnector constraints.

There was significant support for NECA's call for the most urgent possible action to address these inefficiencies. Work is already in hand in relation to transfer limits across interconnectors and improving the efficiency of despatch. NECA's report drew attention to the action taken by ElectraNet SA to relax the restrictions on transfers across the Victorian-South Australian interconnector by reducing the zone of influence of lightning and by reducing the duration of the restrictions after lightning has ceased. NECA also pointed, however, to the scope to go further consistent with maintaining proper management of system security. The MSORC review, which is due to be completed by the end of the year, is likely to include recommendations aimed at achieving consistent operating practices in relation to the management of network assets across the entire market. NECA's report also welcomed NEMMCO's recent establishment of a reference group to address despatch efficiencies. NECA is arguing in that group that its focus should be on ensuring the essential integrity of the fundamental anti-discriminatory principle of the Code and the objective of maximising the benefits of trade.

NECA's report proposed, however, a change to the Code in relation to short-term loading constraints to remove the reference to restoring a secure operating state "as soon as practicable" in order to put beyond doubt that NEMMCO can adopt a more flexible and pragmatic approach but still consistent with maintaining system security and in particular within the overall half hour constraint. NECA also proposed changes to the Code's provisions on the specification and despatch of non-market ancillary services so that they could be used to maximise the value of spot market trading.

Those changes were supported by Energy Australia, Enron and Edison Mission. They were also supported in principle by the NGF and TXU. NEMMCO, in its comments, made clear that it is not philosophically opposed to such changes. It argued, however, that both are premature. It argued that the change in relation to short-term loading constraints should only be introduced as part of a comprehensive package including changes to the despatch algorithm and revised guidelines by the Reliability Panel. NECA and the Panel acknowledge that the proposed change can only be a contribution

towards resolving the issues rather than a complete solution in itself. It would not alter the existing secure operating limits and would not therefore jeopardise the security of the system. It would, however, as NECA believes was always the intent of the Code, allow a better alignment to be achieved between price and despatch within the existing safety margin around those limits. Valuable steps forward could therefore be achieved, without the need for any further changes, as soon as the necessary refinements to the despatch algorithm and associated operating procedures could be made. NECA believes that these refinements should be made as soon as possible. NECA agrees with NEMMCO, however, that any change to the safety margin or to the 30-minute maximum recovery time would require further consultation and the need for revised guidelines from the Reliability Panel. It will invite the Panel to consider the case for such revised guidelines. NECA does not believe, however, that it is necessary or sensible to delay the first stage of these improvements until those guidelines are developed.

NEMMCO argued that the proposed change in relation to non-market ancillary services went further than its avowed intent and placed an obligation on NEMMCO to co-optimize the enabling of NCAS contracts with the despatch of energy in the same way that FCAS contracts are currently co-optimized. NECA has confirmed that this is indeed not the intention and has amended the draft changes to limit them to the more realistic requirement to acquire and despatch non-market ancillary services in order to enhance the value of spot market trading. This clearer and more limited obligation will allow NEMMCO progressively to expand the range of non-market services deployed in this way as the other practical issues it raised, eg in relation to NEMMCO's and TNSPs' relative responsibilities, are resolved.

### **The need for action on bidding and rebidding**

The issues paper published by NECA on 24 May brought together the information provided in its weekly and quarterly reports and analysed rebidding, on an aggregate and region-by-region basis, by type; by time before despatch; by reason and by settlement weeks. The issues paper also analysed the number of significant variations between forecast and actual prices, by region, directly as a result of rebidding. The analysis of rebidding in the issues paper, and in NECA's weekly and quarterly reports and the reports of its investigations into events in the market, taken together represents the most detailed and comprehensive information and analysis of bidding and rebidding and its effect on prices publicly available in the market.

NECA's issues paper also discussed those specific aspects of generators' bidding and rebidding strategies that it believes give cause for concern. They include significant rebids very close to despatch when there is no opportunity for an effective competitive or demand-side response. NECA expressed particular concern about such rebids when they were in response to information or events about which the relevant participant had been aware significantly earlier. The issues paper also drew attention to the very steep supply curves established in New South Wales and Victoria as a result of a mix of generators' initial bids and rebids. NECA has pointed on a number of occasions to the resulting greater price volatility in response to relatively small changes in demand. Those



strategies have also led directly to significant price spikes, including most recently on 27 August when prices reached over \$4,700/MWh in New South Wales and almost \$4,000/MWh in Victoria. The events of 27 August are discussed in detail in NECA's weekly market analysis for 26 August-1 September.

Finally in relation to bidding and rebidding strategies, NECA's issues paper drew attention to occasions when rebidding had led directly to higher prices and even jeopardised the security of the system. The sorts of behaviour NECA has drawn attention to in this context have included gaming of interconnector constraints and inappropriate use of the 'must run' provisions of the market rules. Those strategies too have relied on imperfect competition and the inability of the market, especially in its current state of development, to provide a competitive response.

The analysis in the issues paper, and in NECA's weekly and quarterly reports and the reports of its investigations into events in the market, are all available on its website ([www.neca.com.au/Market Surveillance](http://www.neca.com.au/Market%20Surveillance)).

The number of bids and rebids that give cause for genuine concern is currently comparatively very small. As the analysis in NECA's issues paper also demonstrated, most rebids are benign. The impact of that tiny minority of bids and rebids that does give cause for concern is, however, wholly disproportionate. They do not represent genuine price signals to either the supply side, in terms of the need for new investment, or the demand side of the market. They reflect, eg through the absence of counter-bids to reduce inappropriately high prices, the current lack of a fully competitive market. Taken together, however, they have a significant effect on prices. They also add significantly and inappropriately to trading risks. Moreover, inappropriate bids and rebids affect the reputation of the market and risk bringing it into disrepute. We are satisfied that this warrants a clearer framework of accountability within the market rules.

Hydro Tasmania argued in its written comments in response to NECA's issues paper that the Trade Practices Act, not the market rules, is properly the place to provide such a framework. The issues should therefore be left entirely to the ACCC, with NECA providing solely a monitoring and surveillance rôle. This sentiment was echoed in a number of responses to both the issues paper and our consultation paper. NECA has always recognised the sole responsibility of the ACCC in relation to enforcing the Trade Practices Act. The relevant provisions of the Act governing the abuse of market power, however, relate to the abuse of market power to damage competitors, or to prevent or deter competitive conduct in a market. They do not address the concerns NECA has identified. Ergon Energy, in its comments on NECA's issues paper, concluded that "not only is an investigation into generators' practices necessary but ... those practices have shown that action is needed further to regulate generators' behaviour to prevent the recurrence of past abuses".

A recent paper by ABARE on Californian electricity market reform: an Australian perspective also highlighted the need for appropriate monitoring and mitigation of generators' market power. It concluded that electricity markets are particularly

susceptible to the exercise of market power by suppliers. It pointed to evidence of the exercise of market power in many markets including the UK, PJM and New York as well as Australia. It also pointed to the rules that exist within the PJM and New York markets for assessing and penalising the exercise of market power, although it pointed to the difficulty of enforcing such rules.

The Department of Trade and Industry and the Office of Gas and Electricity Markets (OFGEM) have published revised draft licence conditions, and draft guidelines on the operation of those conditions, aimed at prohibiting action that would prejudice the safe, economic and efficient operation or the economic and efficient balancing of the market in England and Wales; and an obligation prohibiting the limiting, without reasonable cause, of generation or capacity availability if it would prejudice the interests of consumers. OFGEM's initiative would leave only the Australian national electricity market amongst those listed by ABARE with no provisions governing generators' bidding and rebidding strategies in its market rules.

### **Bids to be made in good faith**

NECA's report pointed out that, although the Code requires that the prices provided in generators' initial bids must be 'firm', the flexibility to rebid available capacity and the way this flexibility has been used in practice has rendered that requirement meaningless. It therefore recommended that the rules should be amended to require initial bids and rebids to represent generators' genuine intentions at the time they are made. It represents no more nor less than fair and honest dealing. It is essential to accurate and reliable pre-despatch. This is central to the market design and is in turn essential to informed competitive and demand-side responses. The importance of accurate and reliable pre-despatch was illustrated on 17 August when an error in its initial bids by Snowy Hydro caused by a problem in the implementation of its new bidding system (combined with a planned network outage in Victoria which was subsequently cancelled because of severe weather), resulted in initial pre-despatch price forecasts of \$3,000/MWh in South Australia and \$4,000/MWh in New South Wales for that morning. Snowy Hydro subsequently corrected the error but not before TXU had committed additional units at Torrens Island.

The proposal to require bids and rebids to represent generators' genuine intentions was supported by Energy Australia and Edison Mission. Synergen and TXU concurred with the intent of the proposal. Synergen pointed, however, to the rapid analysis and judgement that is often needed to determine genuine intent. Origin Energy argued that it was unclear how, under the proposed requirement, generators are supposed to proceed in circumstances where they are aware that something may happen in the future that would cause them to rebid. Tarong Energy made a similar point and went further by arguing that the proposal would prevent a generator from bidding unless it could predict that there would definitely not be any events that would require rebidding. This is certainly not the intent, and NECA does not believe that this would be the effect, of the proposal. Nonetheless, it has amended the draft change to put the issue beyond doubt by requiring bids and rebids to be made in good faith.

In order to make this proposed provision effective, the draft Code changes put forward by NECA also proposed to shift the onus of proof so that, in any proceeding, a generator would be required to satisfy the National Electricity Tribunal that its bid or rebid was indeed genuine. It was this proposal that was most clearly and strongly opposed by generators. Such a shift in the onus of proof is, however, preceded in section 51A(2) of the Trade Practices Act in relation to misleading and deceptive conduct. Section 51A(2) provides that:

for the purposes of the application of subsection (1) in relation to a proceeding concerning a representation made by a corporation with respect to any future matter, the corporation shall, unless it adduces evidence to the contrary, be deemed not to have had reasonable grounds for making the representation.

The NGF argued that section 51A does not represent a genuine precedent since it relates to a representation about a future matter, but that whether a representation is in fact about a future matter is a question for the courts in the circumstances of each use. NECA is not, however, seeking to argue a direct equivalence between section 51A and its proposal. It is seeking to argue only that there is a precedent for shifting the onus of proof. Whether it is appropriate to do so in this context is a matter of judgement.

The Panel is satisfied that a requirement that generators' bids and rebids should be made in good faith is appropriate. It also recommends a shift in the onus of proof in relation to that requirement. The Panel is satisfied that it is both appropriate and reasonable. The onus should rest with a generator, in any proceeding before the National Electricity Tribunal, to establish that its bid or rebid was made in good faith; not on NECA to establish that the bid or rebid was made in bad faith. The Panel notes that only in any proceeding for a breach of the clause does the onus shift to the market participant to establish that it acted in good faith. In deciding whether or not to initiate a proceeding for a breach of this proposed clause NECA would first need to be satisfied that the market participant had prima facie acted in bad faith in submitting its bid or rebid. The Panel does not consider that good faith should be defined in the Code. It is a commonly used term in legislation and contractual arrangements and therefore there is a significant body of precedent as to its meaning. The Panel considers that any attempt to define good faith would significantly detract from the effectiveness and scope of the proposal.

### **Ensuring the efficient, competitive and reliable operation of the market**

NECA's proposed prohibition on rebidding, subject to appropriate but tightly-defined exemptions, was aimed at establishing a counterbalance to mitigate the adverse effects of inappropriate rebids and at providing a period of clear water in order to allow a demand-side response. NECA always recognised, however, the need to minimise the inevitable adverse impact of such a prohibition, even if it could be made effective in achieving its stated objectives, on generators' ability legitimately to respond to changing physical and commercial circumstances in the market. A number of generators pointed to this

essential flexibility as being at the core of the market design. Delta Electricity, for example, quoted Larry Ruff and others that:

“If the real time prices faced by generators reflect actual real time network effects, each generator can be allowed wide latitude to decide for itself when to stop or start its units based on its own forecast of real time prices on its contracts. System prices can then be determined based on what actually happens in real time. Such a market simplifies and minimises the rôle of the system operator who does not project, optimise or assume risks over multiple hours. The system operator is left with the relatively simple task of clearing the short term spot market and managing events within each despatch interval of five minutes.”

Delta and a large number of other generators also drew attention to specific circumstances where in their view rebidding would be legitimate but where it would be prohibited even under the proposed expanded exemptions. Snowy Hydro, for example, argued that the proposed exemptions failed either entirely or adequately to deal with legitimate rebids to cope with water management, financial contracts, transmission constraints and ancillary services co-optimisation.

NECA had believed that it would be possible to minimise, although it had always recognised it would be impossible entirely to obviate, these and other adverse effects of its proposed prohibition. NECA and the Panel are persuaded, however, that those effects would be substantive. We are also persuaded that, by effectively locking-in the results of inappropriate rebids rather than allowing the resulting prices to be bid down by a competitive response, a prohibition on rebidding would risk enhancing and exaggerating those effects. Importantly, we are also persuaded that any prohibition, however carefully drafted, would itself have potential to be gamed.

Australian National Power, amongst others, encouraged us instead to specify the precise behaviour about which we are concerned, and then identify and prohibit that behaviour. This same essential point was also made, in one way or another, by Ergon Energy, Yallourn Energy and Macquarie Generation. The latest proposals published by OFGEM in the context of the England and Wales market adopt that targeted approach and, indeed, are aimed at addressing very similar concerns to those identified here. Examples of the sorts of behaviour to which OFGEM points as justifying the need for its proposed licence conditions include some of the sorts of behaviour that NECA pointed to in its issues paper as causing concern in the Australian context.

The different design of the Australian market means that it would not be appropriate simply to carry across the OFGEM proposals directly into the national electricity market. NECA has, however, amended its proposed change in the light of consultation and of OFGEM's proposals to seek to prohibit bids or rebids that have the purpose, or have or are likely to have the effect, of materially prejudicing the efficient, competitive or reliable operation of the market. The Panel is satisfied that this approach has a number of important advantages over a blanket prohibition on rebidding. It is targeted directly at

outlawing specific abuses of bidding and rebidding. It reinforces, rather than risks detracting from, the need for the efficient, competitive and reliable operation of the market. Those three objectives are firmly fixed in the aims of the market. They are expressly stated as the purpose of the market rules in §3.1.2 of the Code.

NECA proposes an obligation on it to use the Code consultation procedures to develop guidelines about how it would enforce the proposed prohibition. It is separately publishing a first draft of those guidelines to coincide with publication of this report. Consultation on those guidelines will begin immediately, in parallel with the ACCC's consultation on the proposed changes to the market rules. This will allow the opportunity for further widespread and extensive consultation about the operation of the provision. NECA will liaise closely with the ACCC in finalising the guidelines. It also intends to invite advice on the draft guidelines from the expert market advisory group it has established as part of the broader strengthening of its market surveillance and monitoring capability.

### **Summary of recommendations**

The Panel recommends revised changes to the Code to:

- ◆ work with NEMMCO and the market to begin to tackle inefficiencies in particular in relation to the treatment of short-term loading constraints and the handling of non-market ancillary services. The changes are intended as part of a broader programme of work to address those and other current inefficiencies in the operation of the market;
- ◆ require generators' bids and rebids to be made in good faith and therefore represent their genuine intentions at the time they are made. The Panel is satisfied that this requirement should be accompanied by a shift in the onus of proof so that in any proceeding a generator would be required to satisfy the National Electricity Tribunal that its bid or rebid was genuinely made in good faith; and
- ◆ prohibit bids or rebids that have the purpose, or have or are likely to have the effect, of materially prejudicing the efficient, competitive or reliable operation of the market.

**Irene Lee**  
**Member**

**Stephen Kelly**  
**Chairman**

**Alan Moran**  
**Member**

**12 September 2001**

## PROPOSED REBIDDING CODE CHANGES

### 3.8.22 Rebidding

- (a) Prices for each *price band* that are submitted in *dispatch bids*, *dispatch offers* and *market ancillary service offers* are firm and no changes to the price for any *price band* are to be accepted under any circumstances.
- (b) ~~Subject to clauses 3.8.22(c), 3.8.22A and 3.8.22B, a A Market Participant may vary its available capacity, daily energy constraints, dispatch inflexibilities and ramp rates of generating units, scheduled network services and scheduled loads and the response breakpoints, enablement limits and response limits of market ancillary services, subject to the requirements set out in this clause 3.8.22.~~
- (c) A *Market Participant* must provide:
- (1) all rebids to *NEMMCO* electronically unless otherwise approved by *NEMMCO*;
  - (2) to *NEMMCO*, at the same time as the *rebid* is made:
    - (i) a brief, verifiable and specific reason for the *rebid*; and
    - (ii) the time at which the event(s) or other occurrence(s) adduced by the *Market Participant* as the reason for the *rebid* occurred;
  - (3) to *NECA*, upon written request, in accordance with guidelines *published* by *NECA* from time to time under this clause 3.8.22 in accordance with the *Code consultation procedures*, such additional information to substantiate and verify the reason for a *rebid* as *NECA* may require from time to time. *NECA* must provide information provided to it in accordance with this clause 3.8.22(c)(3) to any *Market Participant* that requests such information, except to the extent that the information can be reasonably claimed to be *confidential information*. The guidelines developed by *NECA* under this clause 3.8.22(c)(3) must include:
    - (i) the amount of detail to be included in the information provided to *NEMMCO* under clause 3.8.22(c)(2); and
    - (ii) procedures for handling claims by *Market Participants* in accordance with clause 3.8.22(c)(3) or 3.8.19(b)(2) that information provided to *NECA* by such *Market Participants* under those clauses is *confidential information*.

~~*NECA* must *publish* the guidelines developed under this clause 3.8.22 within 3 months after this clause 3.8.22(c)(3) commences operation and may amend such guidelines from time to time.~~

- (d) *NEMMCO* must:
- (1) subject to the *Market Participant* complying with clauses 3.8.22(c)(1) and 3.8.22(c)(2)(i) and (ii), accept the *rebid*; and
  - (2) *publish*, in accordance with clause 3.13.4(p), the time the *rebid* was made and the reason provided by the *Market Participant* under clause 3.8.22(c)(2)(i).

### **3.8.22A Variation of offer, bid or rebid**

- (a) *Market Participants* must make *dispatch offers*, *network dispatch offers*, *dispatch bids* and *rebids* in good faith.
- (b) In any proceedings for a breach of clause 3.8.22A(a), a *Market Participant* is deemed to have contravened clause 3.8.22A(a) unless the *Market Participant* satisfies the *Tribunal* that the *dispatch offer*, *network dispatch offer*, *dispatch bid* or *rebid* was made in good faith.

### **3.8.22B Conduct prejudicial to the market**

- (a) A *Market Participant* must not submit a *dispatch bid*, *network dispatch offer*, *dispatch offer* or *rebid*, if such conduct has the purpose, or has or is likely to have the effect, of materially prejudicing the efficient, competitive or reliable operation of the *market* in accordance with the *market objectives* and the purpose of the market rules as set out in clause 3.1.2, unless the *Market Participant* has reasonable cause for the *dispatch bid*, *network dispatch offer*, *dispatch offer* or *rebid*.
- (b) *NECA* must determine, *publish* and maintain, in accordance with *Code consultation procedures*, guidelines to explain how *NECA* shall exercise its powers to enforce clause 3.8.22B(a). Any guidelines issued by *NECA* under this clause 3.8.22B(b) are indicative only, not legally binding upon *NECA* and do not affect the legal scope of clause 3.8.22B(a).
- (c) Any steps taken by *NECA* prior to this clause 3.8.22B taking effect, in respect of the guidelines to be prepared by *NECA* under clauses 3.8.22B(b) as in operation at the commencement of this clause 3.8.22B, which are consistent with the *Code consultation procedures* are deemed to be valid if otherwise invalid due to the relevant provisions of the *Code* having not come into force at the time of the action being taken.

## **Ancillary Code changes**

### **3.11.3 Procedure for determining quantities of non-market Ancillary Services**

- (b) *NEMMCO must develop and publish a procedure for determining the quantity of each kind of non-market ancillary service required for NEMMCO to achieve the power system security and reliability standards and to enhance the value of spot market trading.*

#### 4.2.6 General principles for maintaining power system security

- (b) Following a *credible contingency event* or a significant change in *power system* conditions, it is possible that the *power system* may no longer be in a condition which could be considered secure on the occurrence of a further *contingency event*. Following a contingency event (whether or not a *credible contingency event*) or a significant change in *power system* conditions, *NEMMCO* should take all reasonable actions to adjust, wherever possible, the operating conditions with a view to returning the *power system* to a *secure operating state* as soon as practical to do so, and, in any event, within at most thirty minutes.

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## Glossary

### dispatch interval

A period defined in clause 3.8.218(a1) in which the *dispatch algorithm* is run in accordance with clause 3.8.218(b).

### network control ancillary service or NCAS

Means a service which provides *NEMMCO* with a capability to control the real or reactive power flow into or out of a *transmission network* in order to:

- (i) maintain the *transmission network* within its current, voltage or stability limits following a *credible contingency event*; or  
(ii) enhance the value of *spot market* trading in conjunction with the *central dispatch* process.
-





## **CODE CHANGE PANEL**

# **Generators' bidding and rebidding strategies and their effect on prices**

## **Volume 2 Written comments in response to Panel's consultation document**

**September 2001**



## **Generators' bidding and rebidding strategies and their effect on prices Written comments in response to Panel's consultation document**

NECA publish a report on 31 July on generators' bidding and rebidding strategies and their effect on prices. That report recommended changes to the market rules and the way those rules operate in practice in order to:

- ◆ tackle the current inefficiencies in the operation of the market in particular in relation to transfer limits across interconnectors, short-term loading constraints, the efficiency of despatch and network services;
- ◆ require generators' initial bids and rebids to represent their genuine intentions at the time they are made;
- ◆ further strengthen the information disclosure obligations surrounding rebidding to ensure that the reasons for rebids are authorised at an appropriate level; and
- ◆ prohibit rebidding within three hours of despatch, with only very limited and closely-defined exceptions connected to the physical operation of the plant.

At the same time as NECA published its report, the Code Change Panel published a consultation paper on the draft changes to the Code necessary to give effect to the report's conclusions and recommendations. We received 26 written comments on those draft changes from CS Energy, Delta Electricity, Edison Mission Energy Australia Limited, Energex, Energy Australia, Enertrade, Enron Australia, Eraring Energy, Ergon Energy, Hydro Tasmania, InterGen Australia, Loy Yang Power, Macquarie Generation, NEMMCO, National Generators' Forum, NRG Asia-Pacific, Origin Energy, SA Department of Treasury and Finance, Snowy Hydro Trading, Southern Hydro, Stanwell, Synergen Power, Tarong Energy, TransÉnergie Australia, TXU and Yallourn Energy. Copies of those written comments are attached. The Panel also held a public forum on 14 August to discuss the draft changes. In addition, NECA and the Panel have held a number of formal and informal discussions with Code participants and others.

### **Tackling the current inefficiencies in the operation of the market**

There was significant support for NECA's proposals to address inefficiencies, in particular for a change to the Code in relation to short-term loading constraints to remove the reference to restoring a secure operating state "as soon as practicable" in order to put beyond doubt that NEMMCO can adopt a more flexible and pragmatic approach but still consistent with maintaining system security and in particular within the overall half hour constraint.

- ◆ several generators argued it would be difficult to define all circumstances where rebidding within three hours of despatch might be appropriate;
- ◆ NRG, Snowy Hydro Trading and others noted the demand side and unscheduled generators are free to change consumption or generation without having to state a reason and without notification to the market, which means the proposed restrictions on rebidding within three hours of despatch would place scheduled generators at a comparative disadvantage;
- ◆ several generators, in particular Delta Electricity, Eraring Energy, Hydro Tasmania, Snowy Hydro Trading and Southern Hydro, argued the proposed restrictions made insufficient provision for response by generators to externalities such as environmental regulations, water management obligations and transmission constraints;
- ◆ Tarong Energy and TXU argued that the proposed changes would have an adverse impact on the management of energy limited plant and would also mitigate against its ability to act as a retailer in the South Australian region;
- ◆ Edison Mission Energy Australia Limited, NRG and others warned the proposed restrictions may lead to lower levels of contract cover available in the market, diminished liquidity in contract markets and to a significant loss of transparency in the spot market;
- ◆ Enertrade argued that system security and reliability may be compromised by restrictions on rebidding because peaking plant may be locked into generating in advance of peak demand and may not have fuel available to offer capacity at a later time;
- ◆ Synergen objected that a Code requirement that reasons for rebids be authorised at an appropriate level within organisations constituted an inappropriate intrusion into the administration of risk management strategies;
- ◆ Loy Yang Power, NRG and others noted that the proposed changes do not allow for generators to rebid other parts of their portfolio to compensate for plant coming offline;
- ◆ Origin Energy claimed that the proposed restrictions on rebidding are in conflict with the new ancillary services arrangements; and
- ◆ Tarong Energy queried whether protected provisions of the Code regarding a price competitive spot market for electricity prevented the proposed Code changes proceeding without the unanimous approvals of all participating jurisdictions.

Stanwell expressed opposition to the proposed Code changes. It acknowledged, however, that the problems the proposed changes seek to address might be evident in South Australia but it believed they are likely to be transitory. It proposed, therefore, that the changes be limited to that region and be subject to a sunset clause.

Ref: 379/168/3 - MT198

28 August 2001

Greg Thorpe  
NECA  
Level 5  
41 Currie Street  
ADELAIDE SA 5000

Dear Greg

### **Bidding and Rebidding Strategies and their effect on prices**

Thank you for the opportunity to comment on your report and proposed Code changes for bidding and rebidding strategies and their effect on prices. CS Energy wish to re-iterate that that flexibility in bidding and re-bidding is an essential design feature required for the efficient operation of the National Electricity Market. The proposed restrictions will be distortionary and severely impede efficient market responses.

As stated in our previous submission CS Energy believes that s46 of the Trade Practices Act 1974 (Misuse of market power) should apply to all Participants. NECA's report raises concerns that the Code authorisation limits exposure under s46. Advice made available to the National Generator's Forum (NGF) indicates that this concern is not well founded and CS Energy believes that changes to the Code authorisation should not be contemplated without proper investigation of the consequences for normal participation in the NEM.

The National Electricity Market is an energy only market where decision making is decentralised to participants. This feature provides simplicity in the market design but requires Participants to manage inter-temporal and optimisation issues for their own plant or retail portfolios. Flexibility in bidding and rebidding is essentially the only tool available to Participants to manage these issues. Most issues such as unit commitment and start-up profiles, optimisation of energy limited plant or use of fuel resources, plant physical changes, and exposure in financial markets are well known. However new issues are evolving and will continue to evolve. Examples of new issues include bids representing a combination of instructions from joint venture owners for the same plant or managing exposures arising from the new ancillary services cooptimisation process. External issues include price changes, demand forecast changes, unscheduled demand response, breakdown of competitor plant and binding network constraints not apparent in pre-dispatch. Any restrictions on rebidding will force sub-optimal outcomes due to inability to react to unexpected market outcomes (driven by externalities) or Participant circumstances.

NECA are attempting control what they believe is inappropriate behaviour through changes to rebidding rules. The proposal makes two assumptions. Firstly the distinction between appropriate and in-appropriate rebidding is based on the time of the rebid in relation to dispatch. Secondly for some defined circumstances rebidding is acceptable up to the time of dispatch. CS Energy's view is that these changes will compromise the effective operation of the market because;

Mr Stephen Kelly,  
Managing Director  
NECA,  
Level 5, 41 Currie Street,  
Adelaide SA 5000

Gj\_00138 v:1  
22.08.2001

27 August 2001

Dear Stephen,

**PROPOSED CODE CHANGES - BIDDING AND REBIDDING IN THE  
NATIONAL ELECTRICITY MARKET**

I refer to the open invitation on the NECA web site of 31 July 2001 to provide comments to the Code Change Panel on the National Electricity Code Administrator ("NECA") proposed Code changes affecting offering and rebidding in the NEM. Delta Electricity thanks you for this invitation and is pleased to submit its comments on what it considers to be a matter of significance to the efficient and effective operation of the National Electricity Market ("NEM").

Delta has previously provided a submission to NECA on the earlier issues paper on this matter. Albeit that submission covered a number of proposed options which NECA have not elected to pursue it is nevertheless still relevant to this specific proposal and Delta would like the Code Change Panel to take into consideration the issues raised in that submission.

We would once again like to stress the importance of the offering and rebidding function to the market design and would urge that the Code Change Panel to carefully consider the potential ramifications of the proposed 3 hour embargo rule before seeking its codification.

Given the potential impact of the proposed Code change Delta feels it would be prudent for NECA to disclose its analyses and in particular an evaluation of how the proposal aligns with the market objectives.

From a detailed perspective Delta also has concerns regarding the drafting of the rule changes.

The following detailed comments refer to the proposed code changes:

- The proposed code change appears not to allow portfolio rebidding. Delta believes significant market benefit is derived from portfolio generators having the ability to provide replacement power when one of its generators is restricted.

In addition it is noted that the intention of clause 3.8.22 (b1) (3) is to allow rebidding if a financial contract is exercised. It should be noted almost all contracts in the market place are “financial” and only commit the counterparties to cashflow obligations – there is no contractual requirement to adjust dispatch despite the incentive and practice of hedging a financial position by adjusting physical generation. Therefore the code change needs redrafting to achieve the intended objective that changes to pure financial contracts are sufficient reason to rebid.

While the proposed code changes may have been intended to accept changes in contract position as a valid reason to rebid Delta believes that the mere existence of a contract may give rise to a valid reason to rebid. For example under conditions of widespread loadshedding and negative spot prices generators may face significant payouts (higher payouts if contracted low, lower payouts if contracted higher) – the impact on a generator of circumstances brought about by NEMMCO action on existing contracts is no different to the impact of a counterparty exercising a call to change a contract.

Finally contracts or binding agreements are with counterparties (eg Delta) not specific generating units within portfolios. Therefore if rebidding is allowed due to changed contractual circumstances then by default portfolio rebidding must be allowed – otherwise the proposed code change has no meaning.

- The draft code changes do not recognise restrictions due to environmental limits (eg lake temperature, emission limits etc). Generators do not wait until limits are reached but must act in advance within the time delays of physical systems to ensure EPA limits are not exceeded. Rebidding activity normally occurs to ensure a prudent safety margin is maintained – the proposed code change must allow this activity to continue.
- The time of mechanical and electrical breakdown is not always defined. For example:
  - tube leak occurs at 9.00am
  - fitter investigation by Midday
  - acoustic expert called in by 2.00pm
  - by 2.50pm expert confirms tube leak and a decision taken to reduce capacity to minimise consequential damage
  - spot trader advised 3.00pm
  - unit rebid 3.05pm

When did the mechanical failure occur for the purpose of rebidding at 3.05pm? Delta believes that the time of failure should be the time at which the spot trader has reasonable evidence that a breakdown has occurred. In this case that would be 3.00pm.

Mr Geoff Henstock  
Company Secretary  
NECA  
Level 5, 41 Currie Street  
ADELAIDE SA 5000

GWJ\_00137\_28.06.2001

29 June 2001

Dear Mr Henstock,

## **BIDDING AND REBIDDING IN THE NATIONAL ELECTRICITY MARKET**

I refer to your invitation to provide comments on the National Electricity Code Administrator ("NECA") issues paper on bidding and rebidding strategies<sup>1</sup> ("Issues paper"). Delta Electricity thanks you for this invitation and is pleased to submit its comments on what it considers to be a matter of significance to the efficient and effective operation of the National Electricity Market ("NEM").

### **Introduction**

The NECA issues paper and specifically the 'proposed options for additional safeguards governing bidding and rebidding' has been prepared within the context of express concerns by NECA on 'aspects of generators' bidding and rebidding strategies' Further, NECA states that this concern has previously been articulated by itself in reports on various 'special investigations into specific market events' and 'market analyses'.<sup>2</sup>

The proposed options by NECA for additional safeguards include:

- Introducing a phasing mechanism that would limit the increase in prices between one five minute dispatch interval and the next to (say) \$500;
- Changing the market rules to expose rebidding more clearly to anti-competitive scrutiny and enforcement under the *Trade Practices Act 1974 (Cth)*;
- Introducing a 'bright line' test which limits individual generator's bids to a predetermined multiple of their historical norm;

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<sup>1</sup> National Electricity Code Administrator, *Bidding and rebidding strategies and their effect on prices: Issues paper*, 24 May 2001

<sup>2</sup> Ibid at page 1

The offering regime is fundamental to the effective operation of the NEM. Supply and demand in an electricity market fluctuate constantly and unless mechanisms exist to allow both supply and demand side response to these fluctuations there will be distortions to the market with material impacts on economic efficiency.

The economic efficiencies that were indicated from implementing a National Electricity Market included:

- Allocative – prices were to reflect the costs of supply;
- Productive – costs would be lower in a competitive market; and
- Dynamic – incentives to respond to changes in market conditions and to make sound and timely investment decisions.

The offering regime seeks to maximise each of these three economic efficiencies in the NEM.

Efficient pricing is a central figure of a competitive electricity market. It is essential if the benefits of a competitive market are to flow through to customers and other market participants. Pricing that is inefficient, on the other hand, will fail to signal and encourage appropriate levels of consumption and supply or the appropriate levels and locations of new generation and transmission investment.<sup>4</sup>

The offering regime represented a conscious decision by the designers of the market to move away from a central planning approach to unit dispatch wherein the system operator had to make inter-temporal optimisation decisions for plant merit order dispatch. Such a centralised process would require the system operator to be aware of all the issues which would impact on plant availability, commitment, capacity limits, energy limits and fuel costs etc many of which factors are dynamic.

This approach was considered and dismissed as sub-optimal for the NEM. The approach adopted was a decentralised approach where the market participants had to make their own decisions regarding self commitment of generating units, optimisation of energy limited plant, offer and off loading prices, including the ability to change these offers (rebidding) based on changed circumstances such as plant problems.

Under this decentralised approach a simple scheduling pricing and dispatch algorithm (SPD) would be used by the system operator who would provide information including forecast dispatch schedules, prices and sensitivities, future projections of system availability (PASA) to participants to enable them to make their own decisions regarding their business optimisations.

The theoretical benefits of such a decentralised approach are well reported in the literature:

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<sup>4</sup> William W Hogan, *Electricity market restructuring: reforms of reforms*. May 25 2001 20<sup>th</sup> Annual Conference, Centre for Regulated Industries, Rutgers University, May 23-25 2001 at p13



divestiture would have little, maybe no, impact on the outcome of prices and production. Most importantly, price caps that appear more justifiable in the presence of traditional market power become exactly the wrong approach in dealing with scarcity.<sup>7</sup>

### **ACCC Considerations**

The issue concerning the extent of restrictions which should be placed on rebidding in the NEM is by no means new. This issue was widely canvassed during the development of the National Electricity Code and it was also comprehensively considered by the ACCC as a part of its public deliberations in authorising the Code. As a result of these deliberations the ACCC authorised the Code on the basis of the current five minute rebidding provisions subject only to NECA monitoring and reporting on significant price variations between the NEMMCO forecast prices and actual spot prices.

It is considered relevant, in light of the proposed options for additional safeguards by NECA, to revisit the defining reasons the ACCC relied upon in arriving at this determination. The ACCC considered the competing arguments put forward by the different segments of the market and other interested parties and carefully weighed up their respective merits and impact on the operation of the market. The ACCC considered that the costs to the market of restricting rebidding beyond the five-minute interval would include:

- Higher spot prices;
- Inefficient production outcomes;
- Increased risk management costs to some participants; and
- Possible costs arising from discouraging demand side participation in the market.

On the issue of demand side management it is considered that this factor is essential for the effective operation of the market. The evolving FCAS markets will lead to a more real time market in the NEM and it will be necessary for the demand side to more actively participate in this market. The New Zealand review of their electricity market highlighted the importance of demand side management.<sup>8</sup>

It was because of these potential costs to the market that the 90 minute moratorium on rebidding included in the co-extensive rules of the NSW and Victorian markets prior to NEM commencement were not adopted in the Code. Delta considers that these arguments are just as pertinent today as they were when the ACCC canvassed these issues in their published authorisation for the Code.

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<sup>7</sup> Ibid at page 18

<sup>8</sup> The Board should also explore and consider any other opportunities for stronger demand-side participation in support of the Government's overall objectives. - *Government's Policy Objective for Electricity Statement: Further Development of New Zealand's Electricity Industry* Hon Pete Hodgson Minister of Energy

of Section 46 of the Act nor does it provide immunity for individual participants who engage in other anti competitive behaviours not covered by the limited authorisation by the ACCC. We do not believe that a 'carve out' of section 46 is a practical response to this issue.

Delta believes that the current proposed changes to the surveillance regime and increased reporting requirements, together with the NECA/ACCC memorandum of understanding on this issue within the context of existing laws should be adequate to enforce competition in the NEM.

### **3. A 'bright line' test**

Although this option seems sound in principle and has been applied in United States competitive electricity markets this proposal does not readily lend itself to implementation in the Australian NEM. Firstly, the NEM allows generators to offer in 10 price bands per generating and prices which range from negative to VoLL. Portfolio generators such as Delta use the flexibility of this regime to balance its production across its portfolio and to change prices and offered generation to compensate for transient plant problems and fuel limitations.

The internal merit order within the portfolio can change considerably as a result of changed costs in spot coal purchases and therefore a 'benchmark' of historical prices may discriminate against legitimate changes in costs. As indicated earlier decentralised decision making, including the right to change offer prices to reflect changed decisions within participant organisations is a fundamental design principle of the NEM. To change this right will have an adverse impact on the efficiency of the NEM.

### **4. Blanket restrictions on rebidding**

This proposal has been canvassed on a number of previous occasions and has been dismissed by the ACCC as detracting from the competitive advantages in the NEM. The impact of such a restriction would probably lead to higher prices as even NECA's quantitative analysis has indicated that changes in generator offers have more often than not lead to reductions in prices. Additionally, for the same reasons as discussed above, the imposition of this restriction would be contrary to the decentralised inter-temporal decision making in the NEM.

### **5. A prohibition on rebidding prices**

This proposed option also suffers from the problem of conflicting with the design principle of decentralised inter-temporal decision making and self-commitment. It also will have serious implications for energy constrained plant such as hydro generators who rely on such short notice changes in prices to generate their long run revenue requirements. The flawed Queensland 90 minute rebidding derogation which only permitted reductions in offers in the 90 minutes prior to dispatch has shown the problems with introducing such types of restrictions. Delta is sympathetic to ensuring that the demand side of the market is not 'ambushed' by sudden changes in offers. However, Delta does not consider that there is credible evidence that this behaviour has been prevalent. We consider that NECA surveillance and reporting of such

26<sup>th</sup> August 2001

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## **Edison Mission Energy Australia Limited Comments on Proposed Rebidding Code Changes**

Edison Mission Energy Australia Limited (“EMEAL”) previously wrote to NECA in response to its rebidding issues paper. In that response EMEAL noted a number of high level factors that it believes are necessary to repeat in this submission. This need comes about due to the apparent failure of NECA to consider them in its Report titled “Generator’s bidding and rebidding strategies and their effect on prices” dated July 2001. EMEAL believes that this failure on the part of NECA will lead to:

1. Substantial increases in risk for all wholesale market participants (not just generators),
2. Significant loss of transparency and as a consequence less potential for demand side to participate in the market,
3. Creation of artificial price volatility and an increase in the volatility overall (not decreases as proposed by NECA),
4. Increases in prices to end use customers (not decreases as proposed by NECA).

### **General factors**

EMEAL notes that the NEM design is based on maximising market efficiency (formulated in the Code as maximising the value of trade). This is predicated on the philosophy that an efficient market is one that provides the “best value for money” to the end consumer of electricity. This does not mean the cheapest price regardless but rather the lowest cost electricity over time that meets the consumers desired level of reliability and quality of supply. This trade off between price and reliability is fundamental to the debate that NECA has raised in the issues paper. Yet NECA has failed to address how this fundamental issue will be affected by its “fiddle” with the market rules.

As a general note, the misuse and abuse of market power where it occurs is not effectively contained by changes to rules. If NECA is convinced that market power is

market,

4. Lower levels of reliability as generators will be unable to respond to contingency events. In locking generators out of rebidding within three hours of dispatch, NECA would be requiring demand to respond to any supply shortfall, even though additional supply may otherwise be available through a rebid
5. Creation of artificial price volatility and an increase in the volatility overall as the market will be at the mercy of forecast errors and contingencies,
6. All of the above will result in lower market efficiency and increases in prices to customers

## **Exemptions**

If the Code Change Panel determines that they will present the proposed Code Changes to the ACCC, EMEAL is of the view that open cycle peaking gas turbines must be substantially exempted from clause 3.8.22 (b1) and (b2). These type of plant are designed to operate during peak prices to cover peak demand. They are generally in the "off" mode and are committed from time to time as higher prices and peak demand occur. This end of the market is the most risky and volatile. In general they have a substantial start-up cost penalty. This type of plant is often flagged for dispatch, but to run for a very short time, and the start-up penalty can substantially exceed any benefit from being dispatched. In order to manage the start-up cost penalty in the most volatile end of the market, these units need to be able to rebid very close to dispatch. Hence they should be fully exempted from the proposed clause 3.8.22 (b1) and (b2).

28 August 2001

Mr Greg Thorpe  
Associate Director  
NECA  
Level 5  
41 Currie Street  
Adelaide SA 5000

email: gthorpe@neca.com.au

Attention: Greg Thorpe

Dear Sir

**ENERGEX Comments on NECA Consultation Paper – PROPOSED  
REBIDDING CODE CHANGES**

ENERGEX welcomes the opportunity to provide comment on the "Proposed Rebidding Code Changes". We note that already there has been much discussion regarding Generators' bidding and rebidding strategies.

With respect to the proposed rebidding code changes, we make the following comments:

1. Generators will still wish to achieve the same revenue outcomes and may, as shown in the past, bid a higher price initially than they would otherwise have done. This will tend to artificially inflate prices and defeat part of the purpose of the change. Rebidding often delivers over the longer term lower rather than higher pool prices. Previous research, which you will be aware of, supports this.
2. As to the conditions for rebidding, ENERGEX believes that there must be an ability to audit generators and enforce penalties where generators have been found to withdraw capacity on other than legitimate grounds.

ENERGEX generally supports prices being determined by the market and that the supply/demand equilibrium should determine wholesale and retail market prices. Consequently we are concerned that the proposed code changes could skew market behaviour in favour of particular participants. However accepting that generators do at times have the ability to game the market, we would favour an option whereby each rebid close to real time has a cap on the level of the increase. We suggest this proposal be further examined as it appears to be an appropriate compromise.

We would be please to discuss our comments further.

Yours faithfully

Louise Dwyer  
Regulatory Affairs Manager - Retail  
ENERGEX Regulatory Affairs



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**EnergyAustralia™**

28 August 2001

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Dear Mr Henstock,

**EnergyAustralia's submission to NECA concerning the proposed Code changes to bidding and rebidding.**

EnergyAustralia does not fully support NECA's proposed code changes. In order to provide clarity and context for this submission EnergyAustralia;

- supports the proposition to make bids and rebids that represent genuine intentions.
- supports the proposition to further strengthen information disclosure.
- supports the proposal to initiate flexibility for short term loading constraints, to reduce short-term price spikes.
- does not support the proposal to prohibit rebidding within 3 hours of dispatch. We propose that that rebidding should be prohibited within 30 minutes of dispatch except for genuine physical reasons.

We believe that the proposed code changes are not in the best interest of the market. It appears that short-term agendas are being pursued without regard to the continuing long-term viability of the market.

NECA's proposed code changes limiting rebidding within 3 hours of dispatch except for physical reasons goes too far and adds an additional level of complexity to an already complex market. The weight of initial submissions received by NECA from market participants does not support the extent of NECA's far-reaching proposal. Certainly, short-term price spikes in the market do nothing for market perception from both the public and government regardless of whether they are related to physical issues or not. Such a sweeping reform, while addressing perception issues, will not necessarily address the issues it seeks to in the longer term.

It has to be recognised that the electricity market is not like other markets. Demand for electricity is largely inelastic to price which creates an environment where producers (generators) can drive prices higher without fear of a concerted demand side response. Competition is the only factor that can limit periods of sustained high prices. The proposed code changes do nothing to improve competition and in fact will limit generators' competitive responses to be dispatched.

The approach taken by NECA for these proposed changes seeks to limit price spikes brought about as a result of predatory behavior or "financial optimisation" but allowing rebidding for physical reasons. This approach may in fact lead to higher pool and contract prices.

NECA, so far, has not demonstrated that the proposed changes will lead to a change in generator bidding behavior. It is our contention that generators will be able to achieve higher prices more easily as a result of the proposed changes. These changes remove a generator's competitive ability for self-dispatch closer to the actual dispatch time. Additionally, the proposed changes do not take into account a change in market conditions, such as demand, within the 3-hour limit. This may preclude a peaking plant from rebidding to generate to take advantage of the higher resulting prices, and therefore discourage investment in peaking plant to the detriment of the market in the longer term.

It seems clear that in order to achieve a competitive market that takes into account a range of physical issues, we must allow for near to real time pricing and dispatch. Limiting bidding and rebidding through regulation in the proposed way may create a whole range of unintended outcomes. It may in fact be simpler to recognise and accept that there will be times when price spikes will occur for whatever reason, either because of demand and supply issues or due to financial optimisation. It is imperative that the market be given suitable investment signals for new generation. The most effective means is through price. However, it is clear that high spot prices (and contract prices) are both publicly and politically unpalatable. Consequently, a compromise must be found to address these two diverging views. At the NECA forum held in Melbourne earlier this month, participants were invited to propose alternate solutions to these issues. It is apparent to us that reviewing the level of VoLL may provide one such alternative.

The level of VoLL is set at such a level so as, among other things, to attract investment for new generation. The current level of \$5,000/MWh is due to be raised on 1 April 2002 to \$10,000/MWh. At the time NECA argued that the lower level was insufficient to attract new generation, demand side response and network augmentation. It was therefore decided to increase VoLL to \$20,000 to meet these needs. The ACCC, in its determination, authorised an increase to \$10,000/MWh and reduced the cumulative price threshold from \$300,000 to \$150,000.

Price outcomes in the market now are stepped such that they move to around \$300 in relatively small increments but once this threshold is breached prices escalate to near VoLL levels. There appears to be a binary price outcome in the market, prices are historically either below \$300 (approx.) or close to VoLL. It appears the presence of the price cap is attracting bids at or near that level. It should be noted this point does not argue for the removal of the price cap completely as the financial risks it would create would be too much for the market to bear.

If the level of VoLL were to be reviewed downwards, the issue of public confidence in the market, as well as recognition that the ability to bid and rebid close to dispatch is a central plank to the market are addressed. However, an alternative mechanism would need to be developed to ensure an appropriate mix of plant types. Our suggestion offers a compromise between the two diverging opinions, without removing the economic pricing signals and eliminating the need for the proposed code changes to occur due to the reduced market influence of the generators.

NECA is currently reviewing the current and proposed levels of VoLL at the request of the Energy Ministers Forum formed following the recent COAG meeting. We recommend the VoLL issue is reviewed in parallel with the bidding and rebidding issues.

As stated in our original submission on this issue "EA supports any proposal that makes generators liable for any misuse of market power". It was clear at the NECA forum that this is an extremely contentious issue. It was said at this forum in that "exploitation of market power is not unlawful, abuse of market power is unlawful". NECA will need to provide the market with any legal advice it has received in relation to the proposed code changes with respect to the Trade Practices Act to enable participants to make informed comment.

In EA's previous submission it was stated that "whatever the rules in relation to bidding and rebidding are invoked, it is necessary to ensure they are applied uniformly to both energy and ancillary services markets". This issue has not been dealt with under NECA's proposed code changes. In fact, it appears to have been completely ignored thus creating a situation where one market is traded under a separate set of rules to the other where both are inextricably linked. This will potentially lead to gaming in one market or the other. Because generators will be unable to rebid capacity through the energy market during the 3 hours prior to dispatch, they may be in a position to rebid it through the ancillary services market on a 5 minute basis. This may lead to highly volatile ancillary service prices and therefore will not solve the issues that NECA has sought to address.

### **Conclusion**

EnergyAustralia does not fully support the proposed code changes in relation to bidding and rebidding. NECA has not demonstrated that the proposed changes will address the issues in the desired manner. It is NECA's responsibility to provide greater information to all participants before instituting any changes to the National Electricity Code as it currently stands.

We further believe that seeking the proposed code changes are motivated by short term concerns and are being pursued without regard to the continuing long-term viability of the market. NECA must act to protect the market from such short-term agendas and protect its ongoing viability.

EnergyAustralia urges NECA to investigate our proposal to review the level of VoLL in parallel with the bidding and rebidding issue. We believe that VoLL mechanism is a means that can be employed to address these issues whilst delivering the required market investment incentives.

Should you have any questions concerning this submission please contact either myself (02 9269 2920) or Andrew Young (02 9269 7273).

Yours sincerely



Tim O'Grady  
General Manager – Energy Risk Management



28 August 2001

Ref. 479/75/24

Attention: Mr Greg Thorpe

NECA  
Level 5, 41 Currie Street  
Adelaide SA 5000

Dear Mr Thorpe

### Proposed Rebidding Code Changes

I refer to the Code Change Panel Consultation Paper containing draft Code changes on rebidding. This letter contains Enertrade's response to the draft Code changes. It also provides limited comment upon the NECA paper entitled "Generators' bidding and rebidding strategies and their effect on prices: Report: July 2001", released with the draft Code changes. Enertrade appreciates that NECA did not solicit comments upon the Report. However, aspects of it are so inextricably linked to the draft Code changes that Enertrade cannot make clear its position on the latter without also discussing the former.

For reasons already outlined in its related submission dated 6 July 2001, Enertrade remains convinced that the current rebidding arrangements in the Code should not be altered. Enertrade also retains its previously expressed concerns that NECA has failed to explain:

- the harm caused by any rebidding,
- why such harm – if identified – should be dealt with in the market rules, given that they are designed to facilitate and not regulate competition,
- why any rebidding behaviour is inconsistent with the law or the policy objectives and design of the market, or
- how restrictions upon rebidding would provide a net economic benefit over the current arrangements.

Participants' confidence in the market's regulatory regime has diminished because these matters were not addressed before changes to the regulatory regime were recommended. It is also doubtful that Participants have been accorded procedural fairness because NECA has not always adequately and precisely disclosed its intentions to recommend changes. For instance, NECA did not disclose its intention to remove the rebidding rule from the authorisation of the Code,<sup>1</sup> or the grounds that allegedly make it necessary to insert into the Code a modified version of sec 51A and 52 of the *Trade Practices Act*. Enertrade is concerned that such failures may have materially affected Participants' ability to comment to their advantage upon proposed changes.

### 3 hour rule and limited exceptions

The draft Code changes propose a restriction on rebidding within three hours of dispatch, with very limited exceptions connected to the physical operation of plant. Enertrade opposes this change because it would harm investors and the public without demonstrably providing a countervailing net economic benefit.

Any rebidding restriction can be expected to have the following adverse impacts upon the NEM:

- spot prices may increase because:

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- a generator may not be dispatched even though it would have been willing to provide energy at a lower cost than the final unit dispatched. This creates an economically inefficient market outcome, particularly where unplanned events (eg transmission problems, demand forecast errors) occur and generators cannot respond to them; and
- generators may elect to raise prices before the cut-off, to ensure they generate only at prices they consider economic. This option would be particularly attractive to generators that are not heavily contracted.
- the price of hedge contracts would rise if the spot price rises, because the latter influences the former.
- hedge contract availability could drop. Many generators would be reluctant to sell hedge contracts if they could not rebid to cover them. Decreased contract market liquidity would increase price volatility for generators and retailers alike.
- market signals would be distorted because the restriction would artificially limit suppliers' ability to send the price signals that would attract further essential infrastructure investment. Although it may be politically unpalatable to some, profit maximisation generally is a valuable economic signal of potential deficiencies in supply. It should not be arbitrarily repressed.
- system security and reliability could be compromised because operational flexibility would be reduced. For instance, energy limited plant would be 'locked in' to generate at sub-optimal times where it relies on demand forecasts that prove to be inaccurate. In these circumstances, the plant could have used up its fuel supply and be unable to generate by the time demand actually peaks. This could cause blackouts in regions where security of supply depends upon the plant.

#### ***Specific objections***

The new rule is also objectionable because it adversely affects some types of plant more than others. This may offend the market objective of technological neutrality. For instance:

- where an exception to the new rule allows a generator to rebid after the cut-off, NECA intends that the generator may rebid only the *unit* that suffers the relevant problem, and not *other units* as well.<sup>11</sup> This would disadvantage portfolio generators compared to generators with aggregated units because only the latter would be allowed to adjust the output of several units (within an aggregated unit) to compensate for the one suffering the problem. This could offend clause 3.8.3(d), which requires all Code rules to apply equally to generating units and aggregated generating units.
- Exception 2 does not allow a change in a generator's fuel *price* to justify a rebid after the cut-off, but it should. Generators with gas fired plant are likely to be buying gas in a highly volatile market. They therefore need to be able to respond quickly in the electricity market to changes in the price of their input (ie gas). If they cannot, the legitimate expectation on which they based their investment decisions would be fundamentally and unfairly damaged.

The rule is so ambiguous that it imposes unmanageable regulatory risks on generators. For instance:

- Exception 4 is apparently intended to allow fast start plant to bid itself available before the cut-off, then bid itself unavailable after the cut-off if likely to get an uneconomic run. However, the exception is so unclear that this intention is invisible. Fast start plant must be able to rebid to avoid being constrained on for a short period when pool price is low. If not, it would have to bid itself unavailable (and therefore useless) before the cut-off.
- Exception 3 is apparently intended to permit a generator to rebid when an agreement requires it to generate in certain circumstances but those circumstances were not foreseeable before the cut-off. However, the exception might not actually permit this. Enertrade doubts the correctness of the suggestion that the exception would allow a rebid where a generator has sold a callable cap but could not have known before the cut-off that the cap would be called upon. This sort of cap probably would *not* fall within the exception



because the cap would not "require" a generator to generate. It would merely require a generator to pay difference payments in certain circumstances.

- where an exception permits a rebid after the cut-off, it is not clear how much volume could be rebid, or whether the generator could rebid just *once* or more often. If a generator could only rebid *once* to withdraw itself from the market if its unit suffers a problem, it would not be able to rebid again to get back into the market if the problem was fixed before dispatch. This would damage the generator's commercial position and the pool price.

For all these reasons, Enertrade contends that the new rebidding rule should not be adopted. Enertrade also objects to the proposed changes relating to the *Trade Practices Act 1974* ("TPA"), for reasons outlined below.

### **Code changes relating to the Trade Practices Act**

#### ***Codifying parts of the TPA***

NECA has not disclosed its basis for including draft clause 3.8.22A. This draft clause effectively forbids a generator from making an offer or rebid unless the generator can prove it had reasonable grounds for believing, at the time it makes the offer or rebid, that the offer or rebid will not be subsequently varied. However, NECA verbally claimed that the draft clause:

- merely codifies sections 52 and 51A of the TPA, and
- is necessary to overcome the fact that these sections may not apply to generator rebidding due to "technical legal reasons".<sup>iii</sup>

In Enertrade's opinion, this clause imposes unreasonable administrative costs upon generators and significantly raises their legal risk. A generator may well have had grounds for believing its initial offer, or a rebid, would not be subsequently varied but these grounds may have been comprised of a number of relatively intangible factors. Proving that these grounds existed and were reasonable will therefore be extremely difficult, if not impossible. The creation and maintenance of a paper trail to justify every offer and rebid can be regarded only as a wholly impracticable task, but it is conceptually the only means of providing a defence under the draft Code changes.

Enertrade also cannot see adequate justification for this regulatory measure. Section 52 of the TPA already forbids misleading or deceptive commercial conduct, and section 51A already deems a representation about a "future matter" to be misleading if the representor does not have reasonable grounds for making it. These sections are sufficient to regulate industry behaviour alleged to be misleading or unfair, unless they do not apply. NECA has not shown that they do not apply.

Clause 3.8.22A is also objectionable because it far exceeds the regulatory scheme laid down by sections 52 and 51A of the TPA. For instance, clause 3.8.22A:

- imposes a far more stringent behavioural norm than section 52 of the TPA. Section 52 of the TPA merely prohibits misleading conduct, whereas clause 3.8.22A(a) prohibits offering a product for sale where there are reasonable grounds for believing the price of the product will be subsequently varied;
- effectively deems all generator offers and rebids to be representations about future matters. This conflicts with the TPA scheme. Under that scheme it is not permissible to make 'ambit claims' that all statements by certain persons are about future matters.<sup>iv</sup> Why then should the Code be permitted to effectively make an ambit claim that all generator offers and rebids are statements about future matters? There is a real legal question about this issue. This legal question should be decided by the Courts in an action under the TPA, rather than by NECA via a Code change.



Even if clause 3.8.22A was truly reflective of sections 52 and 51A of the TPA, it would still not be appropriate to insert it into the Code and allow the National Electricity Tribunal ("NET") to adjudicate alleged breaches of it. The NET is an administrative body not obliged to follow established legal procedure.<sup>v</sup> It should not determine legal questions when a Court could do so instead.

#### ***Removing authorisation of rebidding rule***

NECA has verbally expressed the intention to remove the rebidding rule from the authorisation of the Code, in order to destroy a 'loophole' allegedly created by section 46(6) of the TPA. Section 46(6) provides a corporation with immunity from suit for misuse of market power under section 46 where conduct alleged to amount to a misuse of market power would *also* amount to an anti-competitive agreement, price fix, exclusionary provision or exclusive dealing, but for an authorisation.

Enertrade is concerned that destroying the 'loophole' might create unforeseen detriments that will far outweigh the scant benefits likely to be achieved.

#### ***Benefits***

Removing the section 46(6) 'loophole' may achieve few benefits because the 'loophole' appears to have negligible value. This is demonstrated by the dearth of cases in which respondents have relied on it to avoid liability for a misuse of market power. The 'loophole's' value is very limited because the circumstances in which it is activated are very limited. For instance:

- conduct that amounts to a misuse of market power must also amount to an anti-competitive agreement, price fix, exclusionary provision or exclusive dealing before the 'loophole' can operate. In practice, it seldom does<sup>vi</sup>; and
- where generators engage in anti-competitive agreements, price fixes, exclusionary provisions or exclusive dealing, they will often be liable for these offences *even though* the Code is authorised.<sup>vii</sup> If this unlawful conduct also amounts to a misuse of market power, the section 46(6) 'loophole' will not operate. It will only operate where the conduct in question is actually protected by an authorisation.

#### ***Detriments***

Removing the rebidding authorisation in order to destroy the 'loophole' might render generators immediately liable for anti-competitive conduct where they simply comply with the rebidding rule. For example, generators might be accused of price fixing. Because the new rebidding rule will effectively prevent them from reducing their prices within three hours of dispatch, they might arguably – as competitors – be giving effect to an arrangement that has the purpose or likely effect of controlling the price of wholesale electricity.<sup>viii</sup>

Generators certainly should not be subjected to a rebidding rule that might only be complied with by potentially breaching the TPA. This is just one potential adverse consequence of revoking the authorisation of the rebidding rule. There may be more. Enertrade is very concerned that there has been no visible consideration of these consequences, and that generators may not be able to protect themselves against them.

Enertrade therefore cannot support either the draft Code changes or revocation of authorisation of the rebidding rule. In Enertrade's view, the ramifications of both have not been adequately analysed and may be severely detrimental to generators, the NEM, and ultimately consumers.



Should NECA or the Panel wish to further discuss any aspects of this submission, Enertrade would be happy to assist.

Yours sincerely

Malcolm Whalley  
**ENERGY RISK MANAGER**

Enquiries: Jodi Buckle  
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<sup>i</sup> This intention was not adequately stated in relevant NECA documentation. It was only verbally expressed at the rebidding Forum on 14 August 2001.

<sup>ii</sup> Enertrade notes that this is not clear from the drafting of the rule.

<sup>iii</sup> Claim made by NECA's lawyers at the Forum.

<sup>iv</sup> *Hunt Contracting Co Pty Ltd v Roebuck Resources NL & Ors* (1992) ATPR ¶41-193.

<sup>v</sup> Section 32 of the National Electricity Law.

<sup>vi</sup> Anti-competitive agreements, price fixes and exclusionary provisions are quite different offences to a misuse of market power. The former offences involve several corporations acting in concert, while the latter involves unilateral conduct by a single powerful corporation. It is hard to see, logically, how the same conduct could amount to an offence of both types. If a corporation is sufficiently powerful to misuse its market power, it will not need to collude with competitors to achieve anti-competitive aims.

An exclusive dealing arrangement could more easily also amount to a misuse of market power (eg where a powerful firm supplies goods to a competitor in a downstream market on terms unfavourable to the competitor, in order to protect its own subsidiary or related company operating in that downstream market). However the incidence of such conduct occurring in this industry should be low, given that electricity market reforms have substantially disaggregated generators from their downstream interests.

<sup>vii</sup> This could occur, for instance, where generator conduct exceeds the terms of the Code or where the Code is silent about the validity of that conduct.

<sup>viii</sup> While the new rule leaves generators free to individually set prices prior to the three hour cut-off, it prevents them from discounting during that period. Controlling a discount can amount to price fixing.



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24 August 2001

Mr Greg Thorpe  
National Electricity Code Administrator  
Level 5  
41 Currie Street  
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Dear Mr Thorpe,

**RE: Generators' bidding and rebidding strategies and their effect on prices**

Enron Australia (Enron) welcomes the opportunity to provide comments to NECA and the Code Change Panel on the draft Code changes with respect to bidding and rebidding in the National Electricity Market (NEM).

**Summary**

Enron concurs with NECA's premise that rebidding is essential to the efficient operation of a competitive NEM. As such we are opposed to any move that attempts to limit the ability of any market participant to rebid, and do not support the Code changes proposed by the Code Change Panel. We are particularly opposed to the introduction of Code changes that have the potential to treat market participants in an inequitable manner.

Having attended the forum on rebidding, we are aware of NECA's acknowledgement of the many shortcomings in the proposed Code changes, and support both NECA and other Market Participants in requesting an open review of Philips Fox's advice to NECA, and publication of data to support the financial impact of "misuse" of market power within the NEM prior to any proposed Code changes being implemented. As these Code changes are likely to have a significant detrimental affect on the competitive efficiency of the market, we strongly urge NECA to relax the proposed timetable and allocate more resources to an equitable and appropriate solution.

**Proposed restrictions of rebidding**

Proposed changes to fundamental features of the NEM such as bidding and rebidding should only be made after proper supporting analysis has been completed and made public. Historical evidence from markets that have placed restrictions on rebidding (including Queensland when subject to a derogation) clearly illustrate the potential downside to bidding and rebidding restrictions.

We do not believe the current Code changes will operate effectively to prevent "undesirable" or "inefficient" rebids without at the same time restricting legitimate, or desirable and efficient, rebids. This is because an action by one participant that is deemed efficient can be deemed a misuse of market power and inefficient, if taken by another participant in an otherwise similar position. For example, a generator rebidding in response to an interconnector outage often represents a legitimate reallocation of resources for a generator with fuel supply or contract obligations, yet a generator doing just this was described as "inappropriate" in the issues paper published in May 2001.

Enron is concerned by the potential for inequitable treatment of market participants under the proposed section 3.8.22(b1). As currently drafted, it is structured to provide exemptions to certain types of operating restrictions such as mechanical breakdowns and fuel supply limits. Even with redrafting, it is highly likely that a participant with a legitimate operating restriction will not be covered. As noted above, we believe that all rebidding action could be subject to an exemption. The drafting of section 3.8.22(b1)3 also appears to limit the rebidding of generation subject to binding agreements to those units that are not subject to dispatch. Generators that are scheduled to generate, but are then subject to a change in their contract position, appear to be excluded. If this is the intended result, it is likely that generators will increase the prices in their initial bids so as to maintain rebidding flexibility. The economic and political consequences of the resultant higher pool prices are likely to be far greater than the claimed inefficiency associated with current rebidding practices.

#### **Proposed exemption from the Trade Practices Act**

Like all other pricing activity, bidding within the NEM should be subject to the Trade Practices Act. We agree with NECA that this issue needs to be put beyond doubt, and that appropriate changes need to be made to legislation and/or the Code.

At this time, Enron Australia is concerned that the potential exists for legitimate bidding behaviour to be considered market manipulation under the proposed clause 3.8.22A. Market participants may then be forced to defend frivolous claims. We will be in a position to comment further on the appropriateness of clause 3.8.22A after NECA has published the relevant legal opinion from Philips Fox.

#### **Other Market Initiatives**

Enron views rebidding and its effects to-date as symptoms of the wider issue of the market's design, interpretation and implementation. Rebidding, network standards, interconnector loading constraints and frequency control rules represent a "basket" of correlated issues that may permit the "misuse of market power". Enron is concerned that the proposed Code changes may appear an effective short-term solution but will ultimately be detrimental to the long-term competitiveness of the NEM. As such, Enron supports a further review of these changes with reference to coincident developments in the area of network standards, loading constraints and frequency control in order to allow for a more co-ordinated approach to the development of the Code.

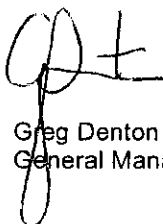
In this regard, Enron is a member of the NEMMCO Network Constraints Review Reference Group, and is fully supportive of the efforts to improve the efficiency of dispatch. While the issues in this area are complex, we agree that improvements are possible and should be pursued.

#### **Conclusion**

To address the claimed inefficiency and inappropriateness of some bidding behaviour, Enron supports NECA's moves to put beyond doubt the application of the Trade Practices Act and its endorsement of efforts being made to improve the efficiency of dispatch. However, Enron believes that the proposed draft changes will detrimentally affect the long term competitiveness of the market and do not support such restrictions on bidding behaviour.

Please feel free to contact me at 02 922 2402 to discuss any of these and other issues.

Yours faithfully,



Greg Denton  
General Manager - Commercial Development

28 August 2001

Mr Greg Thorpe  
Assistant Director  
National Electricity Code Administrator  
Level 5  
41 Currie Street  
Adelaide SA 5000

Dear Mr Thorpe

### **ERARING ENERGY'S COMMENTS ON REBIDDING IN THE NATIONAL ELECTRICITY MARKET**

I refer to NECA's proposal on generator bidding and rebidding in the National Electricity Market and their effect on prices published in a report dated 31 July 2001.

Eraring Energy remains unconvinced that there is a genuine issue that requires resolution. Furthermore, the proposals put forward are complex and may not necessarily lead to the desired outcomes.

Our general position is that any rebidding arrangements should attempt to maximise the efficiency of the market.

#### **The Role of Interconnection and System Security**

Our fundamental position is that the efficient operation of the market is best served through the construction of sufficient interconnection between the States to enable low cost producers to serve customers in regions where there is a shortage of capacity. The present process for the review of new transmission capacity through the SNOVIC proposal, Murraylink and SNI is likely to result in a more robust interregional network.

Until these important parts of national electricity market infrastructure are put in place, the existing system needs to be operated in such a manner that the full capacity of the interregional interconnectors is maximised. This will require over summer that adequate ancillary services are purchased in order to manage both the thermal and reactive power constraints associated with the Snowy/Victoria interconnection.

We have noted your concerns that NEMMCO may be operating the power system in a very conservative manner. Under Clause 4.2.6 of the Code it is required to restore



the system to a secure operating state "as soon as it is practicable to do so and, in any event, within 30 minutes". We note that work is currently being undertaken by the Reliability Panel to review revised power system frequency standards. We also note that the so-called "gatekeeper" arrangements are also being reviewed. If both of these arrangements could be "fast-tracked" and interim solutions put in place prior to next summer, then it is likely that many of the issues that concern NECA could be addressed.

### **Rebidding and the ACCC**

At the time of market start, the ACCC authorised the Code on the basis that rebidding would provide net public benefits and that the Commission would review this issue in the light of market developments.

At that time, it should be noted that the Commission made the following statement in its authorisation of the National Electricity Code.

*"The Commission must assess whether the efficiency benefits of allowing rebidding outweigh the potential for this feature of the market design to be used to manipulate spot market price outcomes. While such behaviour may not contravene the TPA, it could significantly detract from the potential public benefits of the market arrangements".*

It is our view that this was a correct position and in any subsequent review by the ACCC, Eraring Energy would wish to make further detailed comments to the Commission at that time on the application of the TPA to participate covered by the authorisation.

### **Rebidding Prohibition Within Three Hours of Dispatch**

Eraring Energy notes the questions associated with rebidding prior to dispatch.

It is our view that:

- The current arrangements provide for the most economically efficient outcome in the market, with both generators and demand-side participants being able to rebid in real time in response to price signals.
- Any change in the rebidding arrangements could introduce additional volatility in the market with bids being locked in three hours in advance and with demand variations and demand-side responses being able to substantially influence prices.
- The fact that one side of the market, namely the demand-side, would be provided with a "free-option" under these arrangements to alter price is of concern. We remain concerned that large loads can effectively opt-out of the market through the dispatch process but may well have the capability to influence price.
- Variations in predispach forecasts are also likely to be a major source of a need to rebid capacity into the market. It would be very difficult to assess what rebid is appropriate for an assumed error in pre-dispatch demand and the associated rebidding that would be required to compensate for this error. Different participants would have different forecasts as to likely error in demand forecasts and consequently this would imply a differing capability to rebid. In a more general context, it is likely that participants would "game the rules" and that in this

context there would be strong incentives on participants to develop new contractual arrangements which allowed participants to meet the letter but not the spirit of the proposed rule changes.

- Locking-in of bids three hours in advance would increase the compliance costs of establishing whether an exemption to the rebidding rules was appropriate in each case. For example, additional procedures would need to be written and implemented to provide guidance to energy trading staff and station operators.
- From NECA's perspective, the provision of an extensive list of exemptions from the rebidding rules, mainly restricted to a range of plant-related reasons, demand forecasting variations or the need to comply with contractual arrangements would be difficult to administer and would require NECA to substantially upgrade its surveillance capability.
- Earing Energy already is subject to the operation of the Electricity Tariff Equalisation Fund. This is in effect a whole-of meter obligation, which needs to be managed in the context of continual rebidding. Earing Energy's obligations are not known in advance but are estimated as a proportion of system demand. Any rebidding arrangements would need to take this issue into account.
- The rebidding rules would also need to take into account the short-notice callable contracts - such as generator co-insurance arrangements or other short-term contract arrangements.
- There is no certainty that the proposed changes would do any more than lock in high priced events without the opportunity for rebidding to reduce the impact of these prices.
- Prohibition of rebidding except for physical reasons becomes major risk management issue as available capacity within a portfolio cannot be utilised in the case of a forced capacity restriction. For example in case of trip of one of the Earing units, spare capacity available in the other Earing units cannot be rebid to cover financial exposure. This will, of course, lead to higher spot prices.
- Earing Energy has pumped-storage capacity at the Shoalhaven scheme. In the context of the rebidding proposals, this would have the following implications:
  - Due to the need to bring its full capacity to the market, Shoalhaven will need to be offered to the market for at least twenty minutes prior to full output being achieved;
  - Due to energy limitations, rebidding will be required for to maintain water levels in order to preserve the commercial viability of the plant;
  - Pumping will need to be undertaken on a real-time basis in order to ensure that water management options is optimised and that there is no conflict between generation and pumping requirements; and,
  - At times of pumping, if a sudden price increase occurs, we may need to rebid Earing units to cover high prices and continue pumping. Under the new rules, it will not be possible to manage high price risks during pumping.

In summary, Earing Energy believes the current rebidding arrangements work sufficiently. For the above reasons, Earing is therefore unable to support NECA's rebidding proposal in its current form.

Yours sincerely

GERRY GROVE-WHITE  
MANAGING DIRECTOR

ERGON ENERGY



**SUBMISSION ON  
CONSULTATION PAPER:  
GENERATORS' BIDDING AND  
REBIDDING STRATEGIES AND  
THEIR EFFECT ON PRICES**

31 August 2001



Mr Greg Thorpe  
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Our ref: R-01-224

E-mail: gthorpe@neca.com.au

Dear Mr Thorpe

**CODE CHANGE PANEL CONSULTATION PAPER – GENERATORS’ BIDDING  
AND REBIDDING: STRATEGIES**

We refer to the consultation paper issued by the Code Change Panel on generators’ bidding and rebidding strategies and their effect on prices (“the Paper”) released by the National Electricity Code Administrator Limited and thank you for providing an extension of time in which to lodge this submission until 31 August 2001.

We thank you for the opportunity to provide comments on the Paper and ask that you accept this letter and the attached document as our submission on the issues raised.

We would welcome the opportunity to discuss the Paper and our comments with you at your convenience and also to participate in any subsequent consultation process.

Should you have any queries, please feel free to contact Sandra Heymer on (07) 3228 8259.

Yours sincerely

**Darren Barlow**  
**Manager Regulation**  
**Strategic Business Development Group**

## 1. INTRODUCTION

We refer to the consultation paper issued by the Code Change Panel on generators' bidding and rebidding strategies and their effect on prices ("the Paper") released by the National Electricity Code Administrator Limited ("NECA") for comment.

We appreciate the opportunity to provide comment on the Paper and ask that you accept this document as our submission on the issues raised. Where possible, Ergon Energy has sought to respond in the context of the specific issues raised by NECA for comment throughout the Paper.

Ergon Energy will, of course, give consideration to further comment as part of any subsequent consultation process.

## 2. GENERAL COMMENTS

As a general comment, Ergon Energy is concerned that the proposed Code changes fail to address the issue of abuse of market power as exhibited through generator rebidding. We submit that the Code changes would simply alter generator gaming behaviour without addressing the underlying issues leading to the behaviour. In addition, the changes would prevent the efficient operation of peaking and intermediate plants to the detriment of the market overall. Ergon Energy believes that if implemented these changes would actually exacerbate existing market flaws and result in inappropriate increased long run average prices for all generators.

## 3. EFFECTIVENESS OF THE CURRENT REBIDDING REGIME

We are concerned that the proposed rebidding restrictions are being implemented without a thorough and comprehensive examination of the effectiveness of the current rebidding regulations. We would submit that, because of past reluctance to effectively regulate generator's rebidding activities, it is impossible to ascertain whether the current rebidding rules are ineffective and in fact whether they need amending at all. History does illuminate that the enforcement of rebidding has been ineffective.

We note that NECA's report accompanying the Paper states that the changes are necessary because of the "*absence of effective checks and balances governing bidding and rebidding*". While we do support increased regulatory requirements to address and prevent inappropriate rebidding, we do not agree with the assumption that inappropriate rebidding occurs at present because there are currently no "*effective checks and balances*" available to NECA. Rather, we consider that it is irrelevant what checks and balances exist at present because those existing tools are not being used, and as such there is no way of evaluating their effectiveness. We question the efficiency of implementing further safeguards and regulatory measures if NECA, in keeping with its' historical behaviour, does not use those tools to regulate anti-competitive behaviour.

We submit that the proposed amendments are necessarily flawed in that they were developed without a comprehensive understanding and analysis of market power. As rebidding is merely one aspect of the exercise of market power, we do not consider that rebidding can be considered or addressed in a vacuum.

The only way in which generator's rebidding can be effectively reviewed and addressed is as part of a all encompassing review of market power, which would involve an examination of all forms of market power, the development of appropriate definitions and regulatory tools and increased monitoring, enforcement and surveillance.

We are concerned that without this review the proposed Code changes may in fact have a detrimental impact on the efficient operation of the market. In addition, implementing the changes will create the perception that the issue of rebidding and abuse of market power is being adequately addressed when by its' very nature, an incomplete, isolated review cannot effectively address the issue.

#### **4. THE PROPOSED CODE AMENDMENTS**

##### **4.1 EFFECT OF THREE HOUR REBID RESTRICTION**

We do not consider the proposed restriction on rebidding after the sixth trading interval prior to dispatch is a realistic deterrent to uncompetitive rebidding. We consider that this three hour limit is arbitrary and will simply lead to generator's gaming the market and rebidding three and a half hours or some other time frame prior to dispatch. We do not consider that this three hour period has any significance or justification and does not appear to have been chosen based on any evidence about the operation of the market.

##### **4.2 IMPACT ON BASE LOAD GENERATING PLANTS**

We do not support the three hour prior to dispatch restriction for base load generators. By their very nature, base load generators are constantly operated for significant continuous periods. We do not consider that the three hour restriction period is appropriate, and contend that as the plants produce constant loads the rebidding restriction period should be at least 24 hours (with similar exemptions for legitimate technical reasons provided NECA adequately monitors the use of these exemptions). Despite the above comment however we do not believe that an informed decision can be made unless the comprehensive review mentioned above is carried out.

##### **4.3 IMPACT ON PEAKING AND INTERMEDIATE PLANTS**

We are also concerned about the effect of the proposed Code changes on the efficient operation of intermediate and peaking plants. The proposed rebidding restriction would remove the flexibility needed for the operation of these types of plant, thereby impeding the efficient operation of the market.

The restriction on rebidding after the sixth trading interval prior to dispatch is unduly restrictive and is too long a period to allow peaking plants to rapidly commence or alter operation according to market conditions.

#### **5. CONCLUSION**

In summary, Ergon Energy believes that the proposed Code changes are fundamentally flawed because NECA has tried to address rebidding activity in isolation from an analysis of abuse of market power generally. Although we agree that generator

rebidding is a problem and needs to be addressed, we do not agree that it can be resolved by adopting this isolationist view and for this reason the proposed Code amendments may in fact exacerbate the problem and increase inefficiency in the market.

We submit that rebidding abuse can only be used as part of a wide ranging review that will address market power generally, provide appropriate definitions and review monitoring, surveillance and enforcement activities.

In relation to the proposed Code changes specifically, we consider that the proposed general 3 hour rebidding period restriction cannot be justified on any technical grounds. The proposed period is too short for base load generators and too long a period for peak and intermediate generating plants, thereby leading to significantly increased inefficiency in the market.

We would be happy to discuss our comments with you in further detail should you require and thank you for the opportunity to comment on the Paper.



**Hydro Tasmania**  
*the renewable energy business*

28 August 2001

Mr Geoff Henstock  
Company Secretary  
NECA  
Level 5, 41 Currie St  
ADELAIDE 5000.  
By email [ghenstock@neca.com.au](mailto:ghenstock@neca.com.au)

Dear Geoff

### **NECA PROPOSAL ON REBIDDING**

Hydro Tasmania is very concerned at some of the proposed code changes which NECA has published and makes the following comments:

#### **Proposed TPA Changes**

As witnessed at the Forum which NECA held on rebidding, this approach has not been thought through. The proposed change will have no effect since generators are already behaving as though the TPA does apply to their rebidding behaviour. In addition, the proposed changes introduce additional risks to generators which NECA has made no attempt to assess.

#### **Propose prohibition on rebidding within 3 hours**

In our view, this approach is poorly conceived for the following three major reasons:

- Counters the long term market direction
- No demonstration of a problem from rebidding
- Rebidding is status quo so needs a strong argument to make changes

#### *Counters the long term market direction*

Development of NEM has been a general movement to more market based solutions as the confidence of stakeholders has grown. There were naturally many safeguards in the initial market structure to ensure that reliability was maintained.



Since market start, several innovations have come about which have moved NEM towards the vision of a market in which market mechanisms dominate. Such innovations include the introduction of MNSP's and an FCAS spot market. Those still underway are the review of the dispatch and pricing timing disparity and a potential relaxation of technical requirements for generators under the Technical Review so that technical requirements can be met through appropriate market solutions.

*No demonstration of a problem from rebidding*

The papers, which NECA have produced on rebidding, have failed to provide any analytical basis of what the problem is and to document the size of any perceived problem. It would be very helpful in attempting to find a solution if NECA could document 10-20 cases where "unacceptable" rebidding behaviour has occurred.

Whilst it may be hard to develop a new rule which eliminates this behaviour, the market is really at a loss to understand which behaviour NECA considers unacceptable. Its own report says rebidding has increased but it also notes that the net effect of rebidding has been to reduce prices. Does this mean that restricting rebidding will raise prices?

In terms of developing a market, there should then be some analytical work undertaken to assess the impact of proposed changes. This appears to be completely lacking. One of the real dangers of any change is the unintended consequences. Without some serious analytical work, it is very difficult to assess the potential for these to occur.

*Rebidding is status quo so needs a strong argument to make changes.*

NECA adopted a very sound approach in its approach to network pricing two years ago. It proposed that the current arrangements for network pricing which are in the code should stand unless a sound argument could be made for change.

Hydro Tasmania proposes that this same approach should be adopted in relation to rebidding. Notwithstanding that there was discussion at market start in relation to the benefits of rebidding, the status quo now allows rebidding. We propose that there should only be a departure from the current arrangement when a strong case for change exists. The burden of proof must be on the proposer of the change.

NECA have patently failed to make a case for change.

## **Other Issues**

The primary motive for change appears to be to protect South Australia from price spikes in summer. These very same price spikes are the ones which have been driving new generation investment in South Australia. Indeed, there is a real danger that the NECA proposal, by introducing regulatory uncertainty, may delay investment and thus worsen the position it purports to fix.

In conclusion, Hydro Tasmania made a detailed submission in response to the issues paper. We do not believe that the arguments made in that submission were sufficiently recognised in NECA's subsequent papers. The principal conclusions of our submission, which we still hold to, are:

- Rebidding is an essential feature of an efficient market
- No further re-bidding restrictions are necessary or desirable.
- The proposed restrictions on rebidding identified by NECA would be detrimental to the development of the market.
- The most appropriate way to address any concerns stakeholders have about rebidding is through the existing rebidding disclosure requirements and the new market surveillance, monitoring and enforcement regime that NECA has already implemented.
- The Code is an inappropriate instrument with which to deal with market behaviour issues associated with re-bidding.
- The Trade Practices Act is the appropriate instrument to deal with any re-bidding which involves a misuse of market power.

We urge NECA to reconsider this retrogressive change.

Yours sincerely



Albert de Geest  
General Manager Marketing and Trading



**INTERGEN**

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28 August 2001

Mr. Stephen Kelly  
National Electricity Code Administrator Limited  
Level 5, 41 Currie Street  
**ADELAIDE SA 5000**

Dear Stephen,

**Re: Code Change Panel: "Bidding and rebidding strategies and their effect on prices"**

**Introduction**

InterGen (Australia) welcomes the opportunity to comment on NECA's Report "Generators' bidding and rebidding strategies and their effect on prices" and the associated Code Change Panel draft Code changes.

NECA has recommended to the Code Change Panel the following changes to the Code to:

1. require generators' initial bids and rebids to represent their genuine intentions at the time they are made;
2. further strengthen the information disclosure obligations surrounding rebidding to ensure that the reasons for rebids are authorised at an appropriately senior level;
3. increase flexibility in the treatment of short-term loading constraints consistent with maintaining system security, and allow NEMMCO to contract for a wider range of network ancillary services, in order to remove short-term price spikes; and
4. prohibit rebidding, except for essential physical reasons connected with the operation of the plant, within three hours of dispatch.

InterGen (Australia) finds it regrettable that NECA has recommended these poorly conceived Code changes to the Code Change Panel as it has failed to demonstrate, as a result of its consultation, any evidence of the spot market not functioning in the way it was intended in its original design or provided any economic justification for the Code changes.

Further, InterGen (Australia) is extremely concerned that NECA has exceeded its mandate into the areas of price levels and market power and that in doing so NECA has introduced unnecessary and unwarranted regulatory risk into the NEM. In relation to price levels in the NEM, we are not aware of any requirement for NECA to consider the quantum of prices, keep prices low, or indeed to determine the most appropriate level of price outcomes. In relation to market power, it is our understanding of the intention of the market design, that the NEM Code was never intended to be the tool to address



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this issue. Market power is a structural issue that cannot be contained by market rules and in any event under Australian Law, the ACCC, not NECA, has explicit jurisdiction in this area.

### Summary of Position

InterGen (Australia) recommends that the Code changes recommended by NECA be withdrawn as NECA has not demonstrated that a problem in the NEM actually exists. NECA has not completed any analysis or modeled the current operation of the NEM in relation to bidding and rebidding, has not evaluated alternative solutions and has not demonstrated the case for change.

The behaviours cited by NECA in its consultation are behaviours that InterGen (Australia) would contend are transitory and are better addressed by the action of the market in its normal iterative bidding activity and in the form of increased investment as a result of the price signals from the market. We see no analysis to support the Code change, only a cursory examination of a small number of high price outcomes within the market. As proponent, the burden of proof lies clearly with NECA that the Code changes will address the problem and benefit the market, and unfortunately NECA has failed to do so.

### NECA's Code changes:

- are arbitrary and based on selective observation and opinion;
- are retrograde, as they will create major operational problems for participants and result in NEMMCO having to adopt a higher level of intervention;
- will compromise and reduce market efficiency in a market that is currently operating as designed;
- will produce distorted market outcomes that introduce significant sovereign risk, reduce investment and expose customers to market distortions; and
- will not address market power issues, if these are the reason for the proposed Code changes by NECA.

In its previous submission, InterGen (Australia) commented that short-term trends of increasing price and/or volatility are part of the intended market dynamics that provide fundamental and appropriate signals for supply side and demand side investment. We are concerned that inappropriate and unwarranted regulatory intervention that attempts to deal with transitory, non-systemic behaviour in the form of NECA's recommended Code changes will have quite considerable long-term dis-benefit to the market in the form of reduced investment.

**A market should be allowed to respond first. Regulatory intervention should be the last resort and should be specifically and clearly aimed at a systemic problem of either abuse of market power or a fundamental flaw that prevents the market from responding.**

### Discussion

Various submissions from market participants in the consultation process have highlighted many of the technical flaws and potential implementation issues associated with NECA's proposed Code changes. It is obvious from participants' submissions that the proposed Code changes are hasty, ill-



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conceived and drafted with little input from experienced market participants. InterGen (Australia) is concerned that if the proposed Code changes are implemented they will create the necessity for a series of "quick fixes" to respond to identified operational flaws and yet unforeseen side-effects or problems. This will create further uncertainty and degradation of market integrity.

InterGen (Australia) is further concerned that the implementation of Code changes that are so arbitrary in nature they create an environment that threatens two other key Code principles:

- minimising the requirement for NEMMCO decision-making in market operation; and
- neutral treatment of technologies.

InterGen (Australia) has serious reservations in relation to the recommended Code changes, particularly recommendations 1 and 4. Our comments on each of the proposed Code changes are set out below.

**Code Change 1** - require generators' initial bids and rebids to represent their genuine intentions at the time they are made

InterGen (Australia) does not accept that generator bidding behaviour is subject an authorisation from the ACCC exempting behaviour from the provisions of the Trade Practices Act (TPA), particularly Section 46.6. Our understanding is that generators do not have immunity from rebidding conduct in breach of Section 46 as suggested by NECA but even if this was technically correct it would do so in such limited circumstances as to be practically non-existent. The proposed Code changes import some TPA like provisions, especially into proposed Code Section 3.8.22A. InterGen (Australia) asserts that the statute specifically designed for market power and pricing issues is the TPA and its provisions should be used to regulate conduct alleged to be misleading or deceptive, not the Code. The proposed Code changes also introduce a reversal of the onus of proof, that is an assumption that the bidder is "guilty until proven innocent". We question whether NECA as an administrator, has the resources or appropriate skill set within its organisation to decide if a bidder has reasonable grounds for making a bid or otherwise.

**Code Change 2** - further strengthen the information disclosure obligations surrounding rebidding to ensure that the reasons for rebids are authorised at an appropriately senior level.

InterGen (Australia) notes that information disclosure provisions of the Code were recently strengthened. We accept that market transparency is enhanced by the reasons for rebids being subject to market disclosure but consider overly intrusive the requirement for senior management authorisation. The participants' internal processes and delegated authorities for bidding and rebidding are not be relevant to the Code administrator.

**Code Change 3** - increase flexibility in the treatment of short-term loading constraints consistent with maintaining system security, and allow NEMMCO to contract for a wider range of network ancillary services, in order to remove short-term price spikes

InterGen (Australia) considers that the changes proposed should properly be proposed by NEMMCO in their market development role. We question why NECA would single these issues out from matters



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that holistically should be considered by NEMMCO and propose these provisions in isolation, only to remove short term price spikes that would otherwise be considered by the market as investment signals.

**Code Change 4** - prohibit rebidding, except for essential physical reasons connected with the operation of the plant, within three hours of dispatch

This proposed Code change, in the form of an arbitrary constraint on rebidding within 3 hours of dispatch, represents a significant and retrograde change in market arrangements. Participants are required to internally optimise the economic effects of:

- demand forecast errors, irrespective of cause;
- network constraints;
- price forecast errors;
- competitive conditions;
- sales position;
- plant input cost variation;
- inter-relationships with other markets – e.g. ancillary services, regions;
- internal financial position;
- plant condition – e.g. Gross capability (major failures), intermediate estimates of capability i.e. reducing loading on suspect plant like mills to reduce the short term prospect of failure and short term decisions by operators and engineers on issues like cycling; and
- energy constrained plant which requires minimization of opportunity costs, particularly for low capacity factor generation. An example is hydro plant.

NECA is proposing to reduce rebidding timeframes to covering only the last two causations, in a market where the risks of all of the above issues increase as the dispatch interval nears.

InterGen (Australia) is extremely concerned that this proposed constraint represents significant regulatory risk for current and potential investors. NECA should be aware that the introduction of an arbitrary constraint introduces inflexibility and therefore risk that will be priced into the spot market. This will have a direct and unintended effect in the forward market, reducing forward market liquidity and potentially increasing average prices.

The Queensland experience on restrictions on rebidding close to dispatch (i.e. the “90 minute rule”) is a salient and practical example of a similar and likewise arbitrary restriction that failed absolutely and this derogation was withdrawn with the blessing of all participants and the jurisdictional regulator. One of the main criticisms of the practical implications of the prohibition was that it was consistently alleged that the rule resulted in high prices being bid and the forced the withdrawal of capacity.

## Conclusion

Rebidding is an essential and robust feature of the design of the National Electricity Market that leads to efficient market outcomes. This point was acknowledged by NECA itself in the introduction to this consultation and in its Code change summary paper, by the ACCC in its current NEM market authorisation and by direct observation of behaviour in the NEM by market participants. InterGen (Australia) is concerned that whilst the benefits of rebidding are clear and well understood in the NEM,



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NECA have concluded that Code changes to introduce an arbitrary constraint in rebidding is required without any analysis, modeling or demonstration of the benefit of the Code changes to the NEM.

The proposed 3 hour rebidding constraint will in our view have the effect of compromising the NEM market design, reducing economic efficiency and creating further regulatory risk. All of which, in concert, will undermine the investment signals being created by market prices.

Price levels and variability of prices are an important investment signal and prices signals need to be preserved at all cost to ensure appropriate investment in the NEM. Changes in market rules, especially those that influence price signals to the market, have the immediate and long-term effect of reducing investment and should only be considered by regulators where clear evidence of market failure has occurred.

Unfortunately the rebidding constraints proposed by NECA are unlikely to achieve the stated intentions but will damage investment signals and introduce inefficiencies into a market that is already highly efficient, transparent and competitive. InterGen (Australia) suggests NECA allow the market to respond naturally, without arbitrary and unjustified interference. NECA should withdraw its proposed Code changes.

Yours sincerely

James M. Driscoll  
Managing Director



Tuesday, August 28, 2001

Greg Thorpe  
NECA  
Level 5, 41 Currie St  
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Delivered by email to [gthorpe@neca.com.au](mailto:gthorpe@neca.com.au)

**RE: NECA Code Change Panel – generators' bidding and rebidding strategies and their effect on prices**

Dear Greg,

The following submission is presented on behalf of Loy Yang Power (LYP) in regard to the above topic and is presented as an adjunct to our previous submissions on the topic which are also attached for your information. LYP also supports the National Generator Forum response, in particular the aspects relating to the TPA (*s46* and the *codification of s51A and s52*), the *3-Hour Prohibition* on rebidding and the *Consequences* of the proposed changes.

In addition to the points raised previously and those mentioned in the NGF submission, LYP wishes to highlight additional concerns it has with the proposed changes.

**Rebidding of Portfolio's and the inherent risks**

As mentioned in our submission in early July and raised at the Public Forum on the 14<sup>th</sup> July, LYP is concerned that a generator could not rebid other parts of its portfolio to compensate for plant coming offline. Under the NECA proposal it appears that a generator would not be able to rebid its other units as there is no technical reason for doing so. Therefore, not only will the market price be higher than it need might have been if other units could be rebid, the generator may also suffer a greater outflow than is desired due to its possible contract commitments. This impact will create additional risk to the market.

If this additional risk is to be managed, a potential outcome is that a generator would need to reconsider its contractual position, as it may need to 'self-insure' against units coming offline. Given the current perceptions concerning contract liquidity, this restrictive rebidding environment will not serve to lessen this perception.

Similarly, with respect to short term contracting, the proposed restriction on re-bidding will reduce the ability of generators to offer immediate intra-day contracts and generation positions can not be altered to provide such cover. As a consequence, counter-parties with exposures within the rebidding restriction period will be less able to source hedging cover over this time.

**Trade Practices Act**

LYP supports the points of view raised in the NGF submission to do with TPA compliance. As outlined in our previous submissions, LYP has continually supported further surveillance and monitoring by NECA and has always recognised the potential exposure participants have to the TPA.

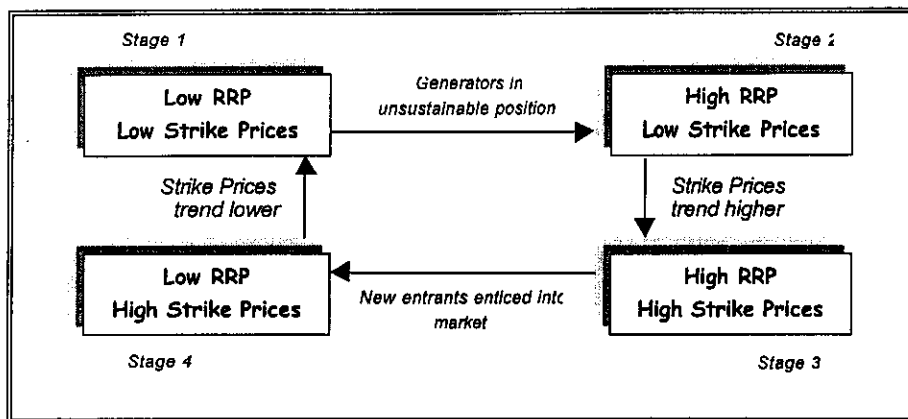
The concept of 'codifying' various elements of other legislation in the National Electricity Code seems nonsensical to us, and completely goes against NEC cl 1.4 (b) (1), "*to provide a regime of "light-handed" regulation of the market to achieve the market objectives"*.



### Bigger Picture Development

It has become apparent to us that the rebidding issue is part of a bigger picture that is looking at why the NEM has experienced high prices. The NECA investigations into high prices (and only high prices for that matter), the various public media releases from governments, comments by electricity industry participants and critics alike, have all tried to explain, justify and perhaps criticise the NEM. LYP would encourage a broader perspective.

Competitive markets will go through cycles and our market is no different. The illustration below highlights (in a very basic manner) the various stages.



At market commencement in December 1998, the environment could have been described as per Stage 1. Through Summer '00/'01, the RRP increased through tightening demand (Stage 2), leading to higher contract prices (Stage 3). As has been observed in the market, new entrants enter the market with the view to capturing some of the benefits of these higher prices, leading of course to Stage 4 (Low RRP but Strike Prices still high). Stage 4 leads to Stage 1 and the cycle continues.

It would be LYP's contention that the market is currently in between Stage 3 & 4, with signs of moving to Stage 1 as well. There are many signs that our market is working under the current rules.

- The new capacity scheduled for development in Victoria and South Australia (over 1000 MW's by mid 2002<sup>1</sup>).
- The document recently released by the Interconnector Process Working Group shows promise to improve the policy framework with which interconnections are processed, hence speed up the process for new interconnection, hence increased competition within the regions.
- The recent downward trend seen in the forward contracts market.

To implement structural changes and blanket restrictions to the degree that is proposed, in an attempt to deal with specific situations and events, seems somewhat heavy-handed and potentially creating a range of new problems yet to be fully understood. The lack of modelling of the proposed changes and the fact that no one can completely determine what the net result of the changes is extremely disappointing. It also appears that the actual implementation of such a regime may also not be completely understood. For example, let us propose that a generator bids a unit up (or down) for plant reasons, yet the bid is 'not accepted' by NEMMCO as a genuine plant reason (for whatever reason).

<sup>1</sup> NEMMCO, "SOO 2001 Addendum", 28 June 2001



There are a whole host of issues that are raised with this example that need careful consideration before adopting this path.

When all of the above is coupled with the arguments in this paper on increased risk, potential detriment to both long and short term contracts, and the general observance that NECA itself made, "*comparisons of forecast prices based on initial bids suggests that rebidding leads overall to lower prices than would otherwise have been the case*", more detailed analysis must be conducted before such a change can be conducted. Rebidding has been identified too many times as an appropriate market mechanism (e.g. ACCC and the 90-minute rebidding restriction in Queensland), for the options proposed here to be accepted. If the issue is higher prices, it is not clear that this proposal will actually reduce price levels or volatility. The national electricity market is still in its infancy and the pricing cycle is yet to be completed – as an industry we need to have faith in the current market architecture and demonstrate courage in market leadership to allow the time for the development of a mature outcome.

If you have any further enquiries please do not hesitate to contact me.

Yours faithfully

Ken Thompson  
General Manager, Marketing  
Loy Yang Power Management Pty. Ltd.  
(03) 5173 3300



**Attachment 1:**  
**Previous LYP submissions on Rebidding**



6<sup>th</sup> July, 2001

Mr Geoff Henstock  
NECA  
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ADELAIDE 5000

By email: [ghenstock@neca.com.au](mailto:ghenstock@neca.com.au)

**RE: NECA Issues paper – Bidding and Rebidding strategies and their effect on prices**

Dear Geoff,

Loy Yang Power (LYP) supports the arguments in relation to market design and market efficiency put forward in the National Generators Forum (NGF) response on this topic. However, LYP would like to present its own comments on several of the issues discussed in the NECA paper. In addition, there is significant concern that in attempting to deal with this issue that new problems will be created. In our view this is certainly the case with the solutions discussed your paper and some of this demonstrated in this submission to you.

The analysis we have carried out supports NECA's finding as detailed in the NECA paper :-

“ ... subject to appropriate disclosure, the ability for generators to rebid is essential for the efficient and effective operation of the market”.. and “...comparisons of forecast prices based on initial bids suggests that rebidding leads overall to lower prices than would otherwise have been the case.. “

Thus we are of the view that there is little evidence to support radical changes to the bidding and rebidding structure, especially given the relatively recent code changes requiring bids and rebids to be 'explicit and verifiable'.

Stephen Kelly is quoted in the NECA paper as having said “ The case for further safeguards against potential abuses of bidding and rebidding is increasingly becoming overwhelming....”

Whilst this view does seem to have gathered public popularity, nobody has yet brought a verifiable case and even the data that NECA presents in this paper does not suggest any endemic price manipulation on the behalf of generators.

If indeed there is a valid claim of price manipulation, then surely it must fall to the demand side who are able to suddenly reduce demand by hundreds of MW's without any notification or reason whatsoever. Even NEMMCO, the party responsible for attempting to keep the system in balance under these conditions is not informed of these changes. If a generator were carrying out this sort of action on the supply side without notification and rebidding, there would be a hue and cry.

Bidding and rebidding behaviours and actions are subject to Trade Practices legislation. If NECA or any other party feel that a participant is breaching this act, they are able to refer the case to the ACCC for investigation. Why should generators, in what is supposed to be a freely competitive and open market, be more restricted than participants in other markets over which the ACCC has jurisdiction?

There is no requirement on NECA, or for that matter NEMMCO or the ACCC, to keep prices in the NEM low. In fact, sound economic argument can and has been put by various parties from all parts of the industry, as to why sustained low prices might not be beneficial for the industry or ultimately the consumer in the medium to longer term. One only has to look to California to see the impact of price capping and heavy handed regulatory interference.

Whilst a limit on the rate of price increase may well exist in what you call 'other futures market', the price you are looking to manipulate here is **not a futures price**. It is a **physical market-clearing price**. The futures prices in our market refer to the bi-lateral contracts which exist between counterparties in the marketplace. We are not aware of, and would certainly not support NECA contemplating playing a role in the setting of the strike prices in bilateral contracts.

Given that recent NECA initiated code changes now require bidding and rebidding reasons to be specific and verifiable, blanket restrictions on rebidding within a specified time of dispatch are inappropriate as they do not allow the flexibility that our market is designed to provide.

The imposition of a blanket or partial restriction may have the undesirable impact of reducing the amount of volume available in the contracts market. This situation would arise as a generator would be unable to change its physical position at short notice due to sudden changes in supply or demand. Contracting under this restrictive rebidding environment would place greater risk on the generator and may drive it to reduce its contractual commitment as it will need to 'insure' against its units coming offline and still being able to generate to meet its contract cover if the prices go high. This further reduction in contract liquidity will only exacerbate the current perceptions about the issues of contract availability – particularly at times of increased volatility.

If the generator can only rebid for technical reasons, then presumably a generator could not rebid other parts of its portfolio to compensate for a plant coming offline. For example, let us consider a generator who has multiple units in its portfolio. The generator may be contracted to say 80% of its portfolio capacity. Under the NECA proposition, if one or more of its units trips offline due to a plant problem, that generator is able to rebid the tripped unit(s), as this is a technical reason. However, the generator may then not be able to cover his contracted load without rebidding the MW's on its remaining units into lower price bands. Under the NECA proposal the generator would not be able to rebid its other units as there is no technical reason for doing so. Thus, not only is the market price likely to be higher than it would otherwise have been, but the generator concerned is liable to suffer a greater outflow of difference payments than would otherwise have been the case.

Restrictions on rebidding may also have a detrimental impact on contract availability and liquidity in the short-term contract market. Sudden changes in demand or price often result in an increased demand for short-term contract coverage. If rebidding for other than technical reasons were not possible, the generators would very likely not be able to offer these intra-day contracts, as they would not be able to rebid their plant to physically cover them.

It is interesting to note that significant demand side response is still happening at spot time (in fact, it is being encouraged by various jurisdictions). Applying NECA's reasoning evenly and equitably to both sides of the market, demand side response would not be allowed either as there is a reduced opportunity for competitive market response.

The introduction of a 'bright line test' is inappropriate for a market such as ours, which has a substantial level of contracting and natural demand driven volatility over a day. A limit on bids based on historical norms would be inappropriate and may not provide the incentive for peaking generation to run at times that it is most needed, resulting in supply shortfalls or investment in the right type of plant at the various stages of market cycle .

LYP would also like to comment on the example given in the NECA paper of Loy Yang Power's bidding behaviour over the recent summer period. Generally our bidding behaviour was such that we gave at least 24 hours notice of our base position. This position was altered closer to spot time (usually more than 2 hours prior) as a result of re-forecast RRP's or demand. Some of the changes were also



due to contract cover being provided to other participants. It is interesting to note, that if the NECA proposed changes were applicable at this time, we would very likely not have been able to offer these intra-day contracts, as we would not have been able to rebid our plant to physically cover them.

LYP also believes that the NECA phrasing is inappropriate and misleading as it talks of capacity changes. At all times, LYP bid its full capacity as available into the market and any rebids were a movement of MW into/out of various price bands. Further, the NECA comment that actual revenue does [not] take into account Loy Yang Power's income from contracts, is again misleading as it implies an additional sum to the spot earnings. As NECA should well know, the flow of difference payments can be either to or from a generator depending on the contractual arrangements at the time. It is mischievous to publicly infer any level of income to LYP without explaining all the possible outcomes. It is quite possible that the station was fully or even over contracted at the level of generation that NECA reported and if this were the case, the level of revenue that was reported would be substantially erroneous and irrelevant to the argument being made.

The market by its design will experience volatility and high prices. Generally it is this volatility and price fluctuation that is one of the drivers for much needed new investment as identified by NEMMCO demand forecasts, and industry observers. New capacity looking to enter a market must see that it is able to gain the return it requires and that the fundamental principles of market design are reasonably static and without political interference. Imposition of non commercially based restrictive market measures will either reduce the appetite of new investment, or will drive the price required by this new investment higher, as they will need to balance their risk/reward against the effects of increased regulatory impediments.

It is LYP's view that increased surveillance and investigative powers (which is already happening to some extent ) would seem a more appropriate form of control and regulation than imposing onerous rebidding restrictions and would result in less distortion to the market.

If you have any further enquiries please contact me.

Yours faithfully

Terry Killen  
Manager Regulation and Pool Operations  
Loy Yang Power Management Pty. Ltd.  
0351 73 2533



Tuesday, May 22 2001

Peter Adams  
Project Leader  
NECA  
Level 5, 41 Currie St  
ADELAIDE SA 5000

Delivered by email to [padams@neca.com.au](mailto:padams@neca.com.au)

RE: Rebidding - draft guidelines

Dear Peter,

Whilst we appreciate that some reason for rebids is necessary and fully support NECA being able to request additional and more detailed data relating to rebidding, we do not agree with the detail and complexity NECA has outlined in its discussion paper.

Requiring detailed plant reasons to be given implies that NECA or NEMMCO have the detailed plant knowledge to determine the veracity of the rebid. As market operators and regulators, remote from the plant, it would seem foolish for NECA or NEMMCO to claim such expertise or to be able to fully glean the circumstances that surround a rebid

Ultimately all rebidding is driven by commercial outcomes (even where plant issues are concerned), however the categories of rebid could quite easily be put into three classifications:

- Plant,
- Commercial or
- Change in Market conditions (this latter reason would cover changes in demand and NEMMCO supplied information, reaction to unexplained events or market circumstances)

To go to an initial level of detail below this would seem to be an unnecessary and non productive use of time and resource.

The NECA paper suggests that the reason code can be embedded with a drop down list in order to make the task of rebidding easier. Whilst this pick list idea is valid (LYP currently employs this method), it is virtually impossible to have a pick list large enough to cover every eventuality that may occur in our plant. Shift operations personnel carryout the bulk of the rebidding out of hours. At times of plant failure, they are normally very busy trying to get the plant back online. It may be counterproductive not only to the participant, but also ultimately to the market itself if they are spending inordinate amounts of time trying to work out what reason to lodge for a rebid.

If the aim of the rebidding reasons is to verify why the change has occurred and identify the key driver for a change in bid, then the above abbreviated reason codes ( along with the participant having verifiable evidence/documentation to support his rebid reason) should be all that is necessary. Publishing the specific cause of a plant fault or the plant affected would seem to offer little value. Should the behaviour of the participant be such that the timing or



veracity of the rebid is in question, or the participant's behaviour is seen to be in breach of the National Electricity Code or TPA, then NECA have full investigation powers anyway.

NECA have suggested that the rebid reason should also include the unit that is affected. This is not necessary as the unit ID is identified in the rebid data, as is the timing of the rebid.

Further, LYP is unlikely to be using the reason of contract change or similar, as this information when analysed may give the rest of the market information on the contract profile and through deduction, the likely value of those contracts.

Over the last few months, particularly over the summer period, it has become obvious that substantial Demand Side Management has been used in the market. It seems a very inequitable proposition that retailers and some larger customers are able to exercise this DSM at no notice to the market and also without any reason, let alone a detailed one. The fact is, that the exercise of this DSM can have significant impact on the RRP and therefore the financial position of any market participant – Generator, Retailer, customer and/ or Trading organisation.

Therefore, in the interests of market transparency and equity, whatever the outcome of this consultation, similar requirements and restrictions should be placed on both sides of the market. If this is not practically possible, then the additional requirements should be delayed until both sides can comply, or at the very least demand side actions should be identified by quantity and participant after the event.

LYP believe that the better approach for NECA to take is to issue reasonably broad guidelines and then evaluate the response and information received on rebids, rather than be needlessly prescriptive resulting in additional cost and resource allocation on the part of participants.

Should you have any questions regarding this consultation, please do not hesitate to contact me.

Yours faithfully,

Terry Killen  
Manager, Regulation and Pool Operations  
Loy Yang Power  
Email: [Terry.Killen@loyyangpower.com.au](mailto:Terry.Killen@loyyangpower.com.au)  
Phone: 03 5173 2533





Wednesday, November 24, 1999

Greg Thorpe  
NECA  
Level 5, 41 Currie St  
ADELAIDE SA 5000

Delivered by email to [gthorpe@neca.com.au](mailto:gthorpe@neca.com.au).

RE: Loy Yang Powers Response to Rebidding

Dear Greg,

Loy Yang Power disagrees with the proposed changes on the grounds of its impracticability, its inapplicability to our market design and the fact that the market behaviour, which it is trying to discourage, is well covered by existing Trade Practices legislation.

As pointed out by NECA, the ACCC in its final determination on the Code, acknowledged that imposing restrictions on rebidding "risk[ed] introducing distortions into the market, imposing costs on the market, introducing inequities in the treatment of generating plant and introducing perverse incentives for demand-side participation"<sup>1</sup>

The nature of our market (reportedly one of the most competitive in the world) dictates that participants must be able to rebid/ offer up to spot time in response to market events or commercial drivers. The existing Trade Practices legislation is more than sufficient to ensure that participants do not exercise market power, or otherwise take unfair advantage of their market position. Market participants and NEMMCO only need to know of a participant's Bid/Offer change and its market impact, not the detail.

The rebidding changes as suggested in the code change are simply not required and add no value to the market. The proposals for rebidding are impractical both from a NEMMCO and participant point of view. For example, on the 23/11/99, there were approximately 2100 rebids lodged across the NEM. Under this proposal, each of the rebids would have specific detailed reasons attached to them. Unless NEMMCO intends to employ additional people to actually read all of these reasons and cross check their validity, I cannot see any value being added by more detailed reasons.

What is more likely to be the case is that NEMMCO will look at the reasons only if any inquiry is raised as to why a participant rebid at a particular time. In this event, I am sure that NEMMCO would ring the participant to discuss the issue and not rely solely on an electronically lodged reason.

The NECA document, "Options for Change" makes mention of the events of 4 August. From our analysis, the NECA report on the event and given that no prosecutions were made, there would appear to be nothing illegal or untoward about the activities surrounding the event. This being the case, I do not believe that the circumstances would have been any different had detailed rebid reasons been lodged at the time. If the event is deemed unusual or warrants investigation, the parties in question will be spoken to in any case, and adequate reasons provided in confidence to the investigating party.

NECA seems to have, as a driving motivation, the eradication of price spikes and believes that a restriction on rebidding will achieve this. When we are actually seeing in the vicinity of 2000 rebids per day with the current pricing outcomes, even a cadet market analyst would be able to draw the

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<sup>1</sup> NECA: Options for Change, released 15/10/99



conclusion that the majority of rebidding is actually depressing price. I would not be surprised to see the rebidding as suggested in the NECA paper actually lead to a pool price increase over time. Consequently, Loy Yang Power does not support any of the options on conditions for rebidding as detailed in the NECA paper.

At the time of the rebids taking place, plant is normally going offline or requiring attention. Loy Yang Power, and I believe other participants, rely on shift personnel to rebid out of hours on these occasions. The Shift Manager doing the rebidding will be very busy with plant issues and will not have time to write out detail as to why he has just lost a unit or had to rebid. Hence, the rebids will be unlikely to be lodged promptly and so make dispatch for NEMMCO more difficult and delay the true market position from being published. This in turn will impact on market efficiencies and outcomes.

Again, at Loy Yang Power we have a bid proforma with set reasons that can be chosen for the rebid, ie. plant failure, plant outage, commercial reasons etc. It is much more efficient in stressful situations (which is usually the case when a rebid is conducted) to select and submit predetermined reasons. Detailed rebids for any reason are always kept, as part of internal audit procedures and also to allow verification by external parties (NECA, NEMMCO, ACCC).

In a competitive market, why do reasons for rebidding need to be given at all? I know of no other competitive market where the manufacturer is required to give public reasons for changing their plant capacity or pricing!

Loy Yang Power fully support NECA's contention that participants should be required to maintain substantial records and justifications for rebidding which are capable of undergoing scrutiny. Offending participants may be prosecuted under Trade Practices Act should they be found to have misled the market or exercised market power or otherwise breached Trade Practices legislation. Loy Yang Power does not see that in a competitive market any value is added by making these reasons public, especially when there are so many produced per day and therefore does not support the NECA code change recommendations.

If you have any queries on any of the above comments, please do not hesitate to contact me.

Yours faithfully,

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Greg Thorpe  
Associate Director  
National Electricity Code of Australia  
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Dear Greg

## **GENERATORS' BIDDING AND REBIDDING STRATEGIES AND THEIR EFFECT ON PRICES**

Macquarie Generation appreciates the opportunity to comment on NECA's report "Generators' bidding and rebidding strategies and their effect on prices" and the associated Code changes.

However, we will argue that on the basis of the evidence provided we believe the proposed changes are unjustified and premature. In our view, NECA has not established a clear case that generators' bidding behaviour has led to excessive spot prices. Even if such a link could be established, it is not clear to Macquarie Generation that implementing ad hoc and arbitrary behavioural rules would address the perceived problem. In fact we submit that this would have serious consequences for the allocative and dynamic efficiency of the market, and question NECA's role in driving such changes in the absence of rigorous analysis. These ideas will be expanded more fully below.

### **NECA's Role**

Prima facie NECA's role is Code administrator and also to conduct specific reviews under the Code. However, it has no role in initiating Code changes outside its review role. Prices that are not in accordance with political expectations in certain constituencies should not itself justify politically expedient price regulation to assuage those constituencies. NECA's role does not encompass price regulation.

Moreover, while Macquarie Generation accepts that COAG has a legitimate role in asking NECA to examine rebidding, we do not believe that this justifies NECA in assuming a problem without doing the appropriate analysis. Clearly without an adequate formulation of the problem regulatory intervention can only serve to compromise the efficiency of the market as a whole, while at the same time enhancing future regulatory risk.

### **Is there a problem**

Macquarie Generation does not believe, on the basis of the analysis provided, that a problem is apparent. NECA provides nothing more than a few anecdotal instances of high spot prices for which 'financial optimisation' are the given reasons and while this is where NECA appears to identify the problem it does so without clearly articulating in what sense 'financial optimisation' is inappropriate or inefficient. Clearly a generator, like any other firm, must focus on maximising its profits, or otherwise it will be competed out of the market by those who do. That is how markets work.

A problem may arise when such attempts to maximise profit lead to inefficiently high spot prices. But NECA has not clearly defined what 'inefficient' in this sense actually means. As stated in the *Independent Commission of Inquiry* report into National Competition Policy "What appears a 'high price' may reflect no more than competitive rate of return, given the risk factors and payback periods involved" (Hilmer, Rayner, Taperell 1993 p 270). Prices that are not high enough in this context will "deter new investment, constrain productivity growth and dull the signal to new firms to enter the market" (Ibid, p 271)

However, while profit maximisation is a legitimate business goal, it can be artificially inflated and sustained if the appropriate market structure is not in place. An inadequate market structure, in turn, reduces the level of demand and supply elasticities present within the market or, in other words, the level of competition. In this context prices would likely substantially exceed those consistent with underlying demand and supply characteristics.

While it is recognised that the elasticity of demand is very low in the electricity industry, little work has been done by NECA on examining supply side elasticity. NECA is right to note that the potential for high spot price is increased if generators are constrained from responding to others' supply bids, yet provides no analysis to determine the extent to which this is a material issue.

In fact Macquarie Generation has observed that, as often as not, attempts by generators to optimise volume/price tradeoffs through rebidding have led to significant losses in market share and revenues as residual supply has responded strongly. As long as adequate residual supply elasticity is present in the market than the capacity to extract excessive and sustained profits is severely constrained, and the notion of excessive prices caused by generators becomes irrelevant.

In light of these factors we therefore reiterate that more analysis needs to be done in order to justify any costly regulatory intervention. Nevertheless, even given the existence of material link between generators' bidding behaviour and price spikes, we believe NECA's proposed solution to this would likely do more harm than good.

### **NECA's solution to the problem**

If a case can be made that strong inefficiencies are generated from opportunistic rebids, than this may need to be addressed. However, Macquarie Generation believes the solutions advanced by NECA would be counterproductive. A three-hour restriction on rebidding greatly reduces the flexibility of the real-time adjustment processes of the NEM, while failing to address the problem of excessive prices in a number of ways, including:

First, if rebidding reflects the exercise of market power or inappropriate behaviour then imposing numerous complex behavioural rules, as demonstrated in the UK market, will only result in circumvention of those rules. For instance, it is unlikely that market power would be reduced as a result of the three hour moratorium on rebidding, it would simply be brought forward by three hours, or manifest itself in other ways, such as for example through 'manufactured' technical reasons for rebids.

Second, increasing the complexity of such rules imposes significant additional administration costs. In fact NECA, in its issues paper, alluded to the potential administrative costs associated with the difficult process of distinguishing legitimate from non-legitimate reasons for rebids and imposing appropriate enforceable sanctions.

Third, NECA's restriction on rebidding would arguably inflate spot prices, not reduce them. Generators would clearly require an additional risk premium for the reduced flexibility in bringing their energy to market. Moreover, NECA's restrictive legal obligation that requires generators to prove the 'genuineness' of their rebids will only add to this risk. Inevitably such additions to generators' risk profiles will be passed on in the form of higher wholesale prices.

Fourth, the types of plant most affected by the rule, fast start and peaking plant, are precisely those providing the predominant source of new investment in the NEM. Substantially reducing the operational opportunities of such plant will likely deter new entry resulting in reduced competition and supply elasticity, as well as a lower reliability of supply. Again this can only serve to push up wholesale prices in the long run.

Finally, the costs that ad hoc and arbitrary behavioural rules impose on the market necessitates a clear justification for their introduction, particularly if such intervention is likely to exacerbate the problems it is attempting to solve. Moreover, Macquarie Generation would argue that the problems of excessive prices and/or market power do not stem from participants' behaviour, but rather, from the underlying structure of the market.

### **Enhanced surveillance, monitoring and disclosure**

Given the potentially significant detrimental consequences outlined above Macquarie Generation strongly urges NECA to discard the Code changes currently under review. We advocate instead a continued focus on an enhanced disclosure,

surveillance and market-monitoring regime and consider this the most effective and efficient way of curbing the opportunistic behaviour of market participants. We also advocate for NECA to more specifically proscribe any behaviour which it deems inappropriate, rather than pursue what currently amounts to a double negative approach.

However, to the extent that the proposed changes to the Code attempt to impose a special competition regime applying to one segment of the Australian economy, they are inconsistent with the recommendations of the *Independent Commission of Inquiry*, which entail the 'universal' and 'uniform' application of the TPA. Introducing different rules for different sectors and industries compromises the efficiency of the market as a whole and unfairly privileges some sectors and industries at the expense of others (Ibid 1993).

### **Reversal of onus of proof**

We also consider NECA's proposed changes to 3.8.22A of the Code misguided. The following argument draws heavily on recently received legal advice.

The proposed clause 3.8.22A(b) would require generators to prove they had reasonable grounds to believe that each bid was the "last" bid, in order to avoid the penalty provisions of the Code and the Law. This would reverse the usual onus of proof and place an unreasonable burden on market participants, particularly since breach of the new provisions would give rise to substantial civil penalties.

It is an established principle of law that the level of proof required to satisfy a tribunal of an issue should depend on the severity of the consequences of the tribunal's determination for the party involved. Given the severe consequences of a breach of the Code or the Law for any market participant, these breaches should not be deemed but should require proof to the relevant standard.

The proposed clause appears to reflect section 51A of the Trade Practices Act 1974 and its equivalent section 12BB in the Australian Securities and Investments Commission Act 1989. These sections reverse the usual burden of proof in determining whether a corporation has reasonable grounds for making a statement as to the future. However, as a practical matter these sections only apply to conduct giving rise to damages, and not to civil penalties. In addition, a finding that the corporation does not have reasonable grounds is simply a factor in determining whether the corporation has engaged in misleading or deceptive conduct, and does not conclude the matter.

By contrast, if a generator fails to adduce satisfactory evidence that it has reasonable grounds to believe its bid to be the "last" bid, it is automatically deemed to have breached section 3.8.22A(a) without more, and becomes liable for civil penalties. The consequences of the deemed breach are therefore much more serious than is the case under similar provisions in other legislation.

Macquarie Generation also notes that the equivalent provision in the Corporations Law, reversing the onus of proof for reasonable grounds for making statements as to the future, was removed by the CLERP reforms in 1999.

For these reasons, Macquarie Generation submits that proposed clause 3.8.22A(b) should not be added to the Code and that the ordinary burden of proof should instead be maintained, consistent with established legal principles and existing laws.

### Conclusion

Macquarie Generation believes NECA has not adequately demonstrated the existence of a problem demanding regulatory intervention. Given the high costs of such intervention there needs to be a clear and material link established between the bidding behaviour of generators and 'inefficient' spot prices. Moreover, we believe it will be ineffectual to impose arbitrary and ad hoc behavioural solutions to what are effectively market structure issues. In fact Macquarie Generation submits that NECA's Code changes would exacerbate the problems it is attempting to solve, leading to higher market clearing prices in the long run. Consequently, we support NECA's enhanced monitoring, disclosure and surveillance framework as the most effective and least cost way to control inappropriate market behaviour, but argue strongly against imposing stronger legal and regulatory obligations than exist elsewhere in the business community.

If you have any further questions please do not hesitate to call us on (02) 4968 7457

Yours sincerely



30/08/01

LUKE WELFARE  
REGULATIONS OFFICER

*References: Hilmer, G., M. Rayner, G. Taperell, 1993, National Competition Policy Review, Report by the Independent Committee of Inquiry. Commonwealth Government Printer, Canberra*

23 August 2001

Mr Stephen Kelly  
Managing Director  
NECA  
PO Box 2575  
ADELAIDE SA 5000

Dear Stephen

**Comments on NECA Report "Generator bidding and rebidding strategies and their effect on prices" and associated proposed Code Changes**

The following is NEMMCO's response to your consultation on "Generator bidding and rebidding strategies and their effect on prices" and associated Code changes.

**1) Proposed Changes to Clause 3.8.22 Rebidding**

From a general perspective, NEMMCO is concerned that the restrictions to rebidding proposed by NECA appear to have been proposed without a full evaluation of the issue they are attempting to address. If the issue is one of potential market manipulation, then options to address that issue directly do not appear to have been canvassed. The ACCC, in its final determination on the VoLL Code changes, imposed a condition of authorisation that NECA report by April 2003, on a number of aspects of market monitoring including the establishment of examples of market behaviour that would trigger investigation. NEMMCO suggests that work in this area would most likely address concerns at their root rather than treating the symptoms.

Also of broad concern is the potential for limitations on rebidding to impact on the operation of the NEM well beyond the price spike issues raised by NECA. The NEM has been designed on the principle that rebidding is an essential part of the inter-temporal optimisation process, an area outside of the scope of the dispatch algorithm. One of the core principles here was to provide participants with adequate information and appropriate incentives to allow them to make decentralised decisions in the market context. Any change that significantly restricts the capability of rebidding therefore needs careful evaluation, otherwise such changes may create more problems than they solve.

From a more specific perspective, NEMMCO is uncertain whether the intention of these Code Changes was to restrict rebidding of Market FCAS within the proposed restrictions. If this is not the case then NEMMCO believes that this needs to be clarified in the draft Code Changes. NEMMCO is concerned that exceptions allowed under Clause 3.8.22(b1) do not address a number of circumstances under rebidding within three hours of dispatch that would be both legitimate and necessary for the efficient operation of the Market. These include but should not be limited to:



- Circumstances requiring Ancillary Service and Power System Security Directions are in most cases likely to arise with less than three hours notice. NEMMCO's procedure is where possible to request Participants to respond to address the issue prior to issuing a direction. Such a response is likely to require rebidding. Unless an exception is granted to rebids in response to a request from NEMMCO in such circumstances there may be an increased incidence of directions.
- In cases of Low Reserve Conditions, NEMMCO's procedure is to first seek a market response that would require rebidding by some Market Participants. Unless an exception is provided to allow rebidding in response to a request from NEMMCO due to actual or forecast Low Reserve Conditions then NEMMCO may have to make a decision on intervention three hours earlier than is presently the case. This is likely to increase the incidence of interventions.
- NEMMCO has concerns that some exceptions need to be made for fast start generators and MNSPs. These types of Participants can be affected by "five minute/thirty minute" anomalies in the Market. At present rebidding is the only mechanism available to these Participants to attempt to minimise any undesirable effects of such anomalies. To assist such parties in managing these types of problems NEMMCO has developed a 5 minute pre-dispatch system looking ahead for 60 minutes. Unless some form of exception is granted in these cases such forecasting will be of little value in this situation. NEMMCO believes the exception that is allowed under proposed Clause 3.8.22(b1)(5) for "stranded" units should be extended to "trapped" units. NEMMCO fails to see why the two cases should be treated differently.
- NEMMCO believes that the exception that is allowed under proposed clause 3.8.22(b1)(6) for rebidding in order to comply with a direction should be extended to rebidding at request of NEMMCO to comply with Reserve Contracts or Mandatory Restriction Offers. If this is not done then restrictions on rebidding could impact significantly on efficient market operation in these two areas by not allowing participant actions to be reflected in the dispatch process.
- NEMMCO also believes that some latitude needs to be provided in cases of plant undergoing testing or commissioning. The behaviour of plant in these circumstances is less predictable than normal and it is not unreasonable that even with best efforts testing and commissioning plans will need to be revised within the three hour window.

NEMMCO believes that the proposed exceptions would be clearly defined and verifiable and so would not provide avenues for abuse.

In addition NEMMCO has general concerns regarding the application of rebidding restrictions on the new FCAS markets whilst they are still in their infancy. This is because Participants may not have had an opportunity to gain sufficient expertise to adequately structure their FCAS and energy bids three hours ahead to be able to satisfactorily respond to changes in the new markets and the resulting impact across different markets due to the co-optimisation mechanism.

NEMMCO is also seriously concerned by NECA's proposal as outlined in its report to remove the rebidding clause from the scope of the ACCC authorisation of the Code. NEMMCO fears that this could well have very significant unintended consequences and may have risks to NEMMCO by operating under a clause that is no longer authorised by the ACCC.

## 2) **Proposed Changes to Clause 4.2.6 General Principles for Maintaining PSS**

Despite the comments in the NECA Report "Generator's bidding and rebidding strategies and their effect on prices" NEMMCO believes that the current wording of Clause 4.2.6(b) places an obligation on NEMMCO to return the power system to a secure operating state "as soon as practical to do so" without consideration on its impact on prices in the market. The proposed code change would place an obligation on NEMMCO only to restore to a secure operating state within 30 minutes. The NECA report clearly infers that the intent of this code change would be to place an obligation on NEMMCO to restore to a secure operating state in as gradual a means as allowable so to minimise the level of any price spikes.

Although NEMMCO is not philosophically opposed to such a change, it needs to be stressed that such a policy approach inevitably decreases the security of the power system. All parties involved in such a policy decision need to have this point very clear in their minds before it is proceeded with. In any case a change to Clause 4.2.6 represents only a small part of an overall package which would need to be put in place to effectively achieve this change. Some of the major tasks required are detailed in the following paragraphs.

Such a revised approach effectively means an explicit trade-off between risk and market pricing. Any delay in returning the power system to a secure operating state means that the risk of a major system disturbance is increased as the power system remains in a vulnerable state for a longer period. Whilst it is arguable that such an increased risk may represent an acceptable trade-off for reduced spot prices, NEMMCO is firmly of the opinion that such a decision should not be left to NEMMCO alone. NEMMCO believes that any decision regarding such a trade off needs to be made in explicit terms by the Reliability Panel in a similar manner to its current review of the Frequency Operating Standard.

The proposed code change still places a requirement upon NEMMCO to return the power system to a secure operating state "within at most thirty minutes". To achieve this NEMMCO will in many occasions need to take action well before the end of the 30-minute period. This is because the speed of response of the power system is limited by the available rate of change of synchronised generating units and the start up times for unsynchronised fast start generators. For instance if the secure limit on the Vic to SA interconnector is violated due to a major contingency in the SA Region, such as loss of a 260 MW unit, then NEMMCO may at times have to initiate action within 5 to 10 minutes after the contingency to achieve restoration of a secure operating state within 30 minutes. In such cases the effect of the proposed Code Change on reducing the resulting price spike could be minimal.

The decision making process to determine the latest time that such action would have to be taken would be required to be built into the dispatch algorithm. Otherwise, NEMMCO would be required to issue Power System Security directions every time a major contingency occurred. This would not be a simple process, as the dispatch algorithm would need to have some form of look ahead capability over the next thirty-minute period. The algorithm would then, based upon such forecasts, need to determine the point at which constraints on dispatch need to be imposed and in some manner or other adjust the severity of these constraints to the minimum judged necessary to restore to a secure operating state within 30 minutes. The five-minute pre-dispatch forecasts, which are being introduced shortly, represent a starting point. However the transition from a forecasting system to a closed loop control system would not be trivial, and would need to be carefully specified to ensure that such a process would work reliably following major contingency events.

NEMMCO would also caution against inflated expectations as to what the proposed code change could achieve for the following reasons:

- The proposed Code Change will only allow NEMMCO to cease to maintain a secure operating state following a "credible contingency event or a significant change in power system operating conditions". In all other conditions NEMMCO would be required to act continuously to maintain a secure operating state. Thus, on many occasions price spikes will still occur. For instance NEMMCO has reviewed the month of March 2001 for the SA Region to identify price spikes and their causes. For the purpose of this review NEMMCO defined a spike as where the spot price exceeded by one-third the average of spot prices for the trading interval immediately prior to and the trading interval immediately following the one in question. On this basis NEMMCO identified 21 trading intervals which were subject to price spikes. Out of these only six could be linked to credible contingency events or significant changes to conditions. Of the remainder, nine were associated with increases in load outside of the SA Region mainly due to hot water switching. A further four instances were apparently related either to delays in planned commitment of units or units coming out of service earlier than expected during planned de-commitment.
- As indicated above following major contingencies, particularly in the South Australian Region, NEMMCO would still have to act very soon after the contingency to achieve restoration to a secure operating state. Thus the potential for such new arrangements to eliminate price spikes in these cases would be strictly limited. This is particularly pertinent as large price spikes in the SA Region are predominantly due to such events.

NEMMCO believes that NECA's proposed Code change to Clause 4.2.6 will not address the real concerns regarding price spikes and their effects on the financial markets. More fundamental issues regarding the very nature of energy pricing may need to be addressed. NEMMCO's position is that the proposed Code change to Clause 4.2.6 should only be introduced as part of a comprehensive package of changes. Until such a comprehensive package is developed NEMMCO opposes this Code change.

### **3) Proposed Changes to Clause 3.8.1 Central Dispatch and 3.11.3 Procedures for determining quantities of non-Market Ancillary Services**

The NECA report "Generator's bidding and rebidding strategies and their effect on prices" indicates that the intent of these changes is to give clearer and wider powers for NEMMCO to enter into Network Control Ancillary Services. However NEMMCO believes the wording of these proposed amendments goes far beyond this to place an obligation on NEMMCO to co-optimize enabling of NCAS Contracts with dispatch of energy in the same manner that FCAS contracts are currently co-optimised.

Whilst NEMMCO is not philosophically opposed to development of such an approach where feasible in the longer term to enhance the value of spot market trading, it has serious concerns about these amendments. If the actual intent is to require co-optimisation of NCAS, then these amendments could be viewed as changes to the ancillary services arrangements that would run counter to the recent moratorium on spot market based NCAS developments imposed by the ACCC as a Condition of Authorisation of the Ancillary Service Code Changes.

Even if the Code Change proposal could be interpreted in a narrower fashion, significant issues would remain, including:

- Where does the responsibility of NEMMCO stop and the responsibility of the TNSPs start in this area? Final resolution of this needs to be achieved through the MSORC process, or possibly a future review of the matter as outlined in the recent ancillary service Code changes, before there can be any real progress in this area;

- The NECA report suggests a whole raft of possible services that are apparently available. There remain however a few practical issues that need to be considered as follows:
  - Post contingency load shedding schemes are really only suitable in cases where the limit is set by short term thermal ratings, such schemes would be of little use in cases where the limits are determined by rapid voltage collapse or stability limits. The availability of suitable loads of large enough size to make a difference would certainly be open to question in at least the South Australian region;
  - As regards reactive support, NEMMCO already has contracts in place with many of the major synchronous condensers, and it would be questionable as to what other sources of reactive support would be available that is not already provided to the power system through AS contracts or via the TNSP.
  - As regards real power support, to enhance interconnector transfer levels the Network Constraints Working Group set up by NEMMCO is already looking at this issue. However implementation would require Code Changes well beyond the minimal level proposed by NECA. Pre-empting the conclusions of the industry-based process currently being conducted by NEMMCO is inappropriate, however if NECA has proposals to make they are welcome to subject them to analysis in the working group. Although NECA is a member of the working group, no detailed proposals have been forthcoming to date.
  - As regards generator commitment contracts, except in one isolated case, it is difficult to see what these would do to substantially increase interconnector transfer levels. Even if such contracts were found to be of use, there are a number of issues that would need to be answered if NEMMCO were to enter into such contracts as regards interaction with energy pricing:
    - ❖ If units were to be committed under such contracts, could they then freely participate in the energy market or should they be restricted only to operation at minimum load?
    - ❖ When such units were committed, should what-if pricing apply ?

NEMMCO believes such fundamental issues would need to be addressed in the Code. In any case, the Code already has a mechanism where similar services can be provided via Network Support contracts with the relevant NSP (refer Clause 5.6.2(m)). This option has been exercised on a number of occasions. The need for a parallel mechanism to be put in place by NEMMCO therefore needs further justification.

The NECA report justifies the need for such an immediate initiative on the basis of reducing the incidence of short-term price spikes. However studies have questioned a systematic (or any) link between an increase in interconnector capacity and reduced incidence of price spikes, particularly in the context of the South Australian Region. For instance the SAIIR Information Paper No 3 - Impacts of Interconnections on South Australian Electricity Supply - October 2000 states in Section 5.1 that:

"In SA there are also significant high price spikes with constrained operation of the current interconnection when variations in SA generation requirements within a 5 minute dispatch period must be satisfied by SA generators. These adverse impacts, which are discussed in 3.4.2, may be increased by increases in interconnection capacity that are insufficient to reduce the significance of constrained imports.

If the proportion of generation provided by local generators is reduced, the availability of relatively cheap 5 minute response in SA may also reduce and the incidence of high pool price spikes increase."

Thus any causal link between relatively small increases in interconnector capacity and reduction in the incidence of price spikes as assumed in the NECA report is open to question.

#### 4) **Issues Raised by NECA on Constraint Formulation**

In relation to NECA's assertions on page 6 of the rebidding report regarding the formulation of network constraints at Ladbroke Grove and South East Queensland (under the heading "efficiency of dispatch"), NECA is a member of NEMMCO's Network Constraints Reference Group, which has been convened to address issues of constraint formulation. It is noted that NECA has not, to date, chosen to bring up such matters for resolution in the working group process, even though the process has been operating with an established Terms of Reference for some four months now, and NEMMCO has actively encouraged input of this type. NECA's representative on the working group has now been requested to bring the concerns, together with supporting and background material, to the next meeting of the group, so that the issues can be openly and fully analysed, and the conclusions integrated into the findings of the Group. NECA's commentary on that process in the context of a rebidding report is perplexing.

#### 5) **Network Services**

In respect of NECA's references to the potential use of various contract arrangements to "help to cope with the consequences of interconnector constraints", NEMMCO is concerned as to whether NECA is pre-empting the outcomes of the current "gatekeeper" review being run by NEMMCO. Any proposals NECA has would be most welcome in that working group, where they can be fully examined by industry representatives, and firm recommendations can emerge. In the meantime however, proposals for Code change in this area must be considered premature, lacking in detail at present, and lacking in co-ordination with the other work being carried out by the industry. NEMMCO therefore does not support the changes at this time.

#### **Conclusion**

NEMMCO remains of the view that NECA's proposed Code changes to Clauses 3.8.1, 3.11.3 and 4.2.6 will not address the real concerns regarding price spikes and their effects on the financial markets. More fundamental issues regarding the very nature of energy pricing need to be considered and addressed. NEMMCO therefore considers the proposals to be underdeveloped. They should not proceed in their current form, or indeed in any form without further discussion, unless their implications are fully and properly developed so that the benefit to the market can be assessed

As regards the proposed change to Code Clause 3.8.22, NEMMCO strongly urges that additional exemptions be granted as detailed above. If this was the intention of the proposed Code Changes, NEMMCO has general concerns regarding the effect of rebidding restrictions on the FCAS Markets whilst these are in their infancy. Also NEMMCO would urge that very careful consideration be given to the possible consequences, both intended and unintended, of a significant change to a major mechanism on which the design of the Market has been based.

In order to assist the Code Change Panel in complying with Code Clause 8.3.5(f), so that it can take into account any comments from NEMMCO, we request the opportunity to meet with the Code Change Panel to discuss our comments.

Yours sincerely

**Brian Spalding**  
**General Manager Power Exchange**



28 August 2001

Mr Geoff Henstock  
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ADELAIDE 5000.

By email [ghenstock@neca.com.au](mailto:ghenstock@neca.com.au)

Dear Geoff

### **NECA PROPOSAL ON REBIDDING**

The National Generators Forum (NGF) welcomes the opportunity to provide input on NECA's proposed changes to a number of aspects of the NEM Code, including those on the generator bidding structures in the code.

The NGF supports the principle of several of the changes proposed by NECA, specifically rectification of over conservative application of physical system limits and continuous improvement in the surveillance, monitoring and enforcement provisions of the Code.

The NGF however wishes to express severe and deep reservation with two aspects of the Code changes proposed. These are proposals relating to the application of sections of the Trade Practices Act, and the ill considered proposal to apply restrictions on the repricing of generation within an arbitrary (3 hour) period before dispatch.

### **The Trade Practices Act ("TPA") - s46**

NECA has expressed a view that the authorisation of the Code has a consequential effect that behaviour that would under normal circumstances be "caught" under s46 (Misuse of Market Power) is protected, as it were, through the operation of s46.6

Internal advice provided to the NGF, advice provided to Macquarie Generation by Gilbert Tobin and published during the consultation (page 110), and extensive discussion at the forum on 14 August disputed this advice. While s46.6 might *technically* provide immunity from suit under s46, it will do so in such limited circumstances that its value as 'immunity' is effectively nil. Generators are therefore

very unlikely to "in practice be immune from action under s46 as a result of the operation of s46.6".

Removing the s46.6 'immunity' by revoking authorisation of the rebidding rule will therefore produce infinitesimal benefits, but may produce very significant detriment. For instance, it might expose generators to liability for price fixing where they merely abide by the new rule. After all, the new rule does appear to be an arrangement that prevents competitors from pricing within three hours of dispatch. This might amount to an anti-competitive control on price or an anti-competitive agreement.

The NGF is also very concerned that NECA did not adequately identify the fact that it intended to 'carve out' rebidding from the existing Code authorisation. Its relevant Papers failed to explicitly state this. The NGF is also disturbed that NECA has not adequately justified the need to alter the existing authorisation or adequately assessed the impact of doing so. The NGF doubts it has benefited from good, or even standard, regulatory practice because NECA has not:

- justified the need to remove the s46.6 'immunity' before recommending its removal by such radical means. Provision of actual examples of the way in which s46.6 might operate to protect generators from suit under s46 would have assisted in this regard,
- pointed to other regulatory regimes with limited scope or partial authorisations; and
- provided some analysis of the legal and practical ramifications of revoking authorisation of the rebidding rule.

The course proposed by NECA

- Is not one that should be followed without the explicit request of the ACCC,
- Is beyond the jurisdiction of NECA in the operation of the Code
- Has substantial unintended consequences associated with the removal of s45 and s47 authorisation of the rebidding procedures. This would affect **all** rebids, for any reason, after the initial bid required under the Code 11am on the day prior.

The latter point was not examined by NECA in its discussion of the Code changes. It is a deep concern to the NGF that NECA could propose removal of the authorisation from one part of the Code without

- Publishing its brief and the advice received
- Examining the effect of its proposal on the operation of the Code, the participants and NEMMCO
- Disclosing other options examined and the rationale for the adoption of the preferred option

It is the view of the NGF that excising the rebid provisions from the authorisations may have the effect of preventing any rebids, for any reason, from being legally protected from the price fixing prohibitions of the TPA.

### **The Trade Practices Act ("TPA") - s52 and 51A**

The rationale for the existence of the cl 3.8.22A proposal is in our view not clear in the NECA document. In response to a question to that end at the forum, NECA claimed that a clause replicating ss52 and 51A of the TPA is necessary because these sections may not apply to generator rebidding conduct for 'technical legal reasons'.

It is not appropriate to codify ss52 and 51A of the TPA via draft clause 3.8.22A without supporting the claim that the relevant TPA sections do not apply. In the NGF's opinion, it is better to regulate conduct alleged to be unfair or misleading via the statute specifically designed by Parliament for that purpose.

Even if the TPA sections cannot be enforced against generators and some sort of codification of them is (perhaps) justifiable, cl 3.8.22A goes far beyond replicating the TPA sections. Clause 3.8.22A effectively forbids generators to offer energy for sale if they think they will later alter its price. Section 52 of the TPA merely forbids commercial conduct that is misleading or deceptive. There is a big difference.

NECA also appears to have made some inappropriate and questionable legal assumptions in the process of 'importing' s51A of the TPA into the Code. Section 51A of the TPA deems a representation about a 'future matter' to be misleading if the representor cannot prove it had reasonable grounds for making it. But whether a representation is in fact about a 'future matter', and therefore attracts a reversed onus of proof, is always a question for the Courts. NECA seems to have simply assumed that all generator offers and rebids are representations about 'future matters', and therefore should be subjected to the same kind of reversed onus of proof found in s51A. However, it is not appropriate for NECA to decide such legal questions. It is a matter for the Courts to decide under the TPA.

In summary, the NGF does not believe that the Code needs to import other legislation and specifically not these sections, and the drafting significantly alters the operation of the imported sections in inappropriate ways.

### **3 Hour Prohibition**

The NEM is an energy only market. Participants are required to internally optimise the economic effects of

- Demand forecast errors, irrespective of cause
- Network constraints
- Price forecast errors
- Competitive conditions



- Sales position, (i.e. a significant number of retailers use generation plant as cost optimisation)
- Plant input cost variation (i.e. cost and availability of gas, oil and coal) (wind?)
- Inter-relationships with other markets (ancillary services, MNSP position, regions)
- Internal financial position, and
- Plant condition (Gross capability (major failures), intermediate estimates of capability i.e. reducing loading on suspect plant like mills to reduce the short term prospect of failure and short term decisions by operators and engineers on issues like cycling)

This optimisation has significant economic benefits to the Australian Energy Market. NECA is proposing to reduce rebidding to covering only the last causation, in an economic environment where the risks of all of the above issues increase as the dispatch interval nears.

To suggest, as NECA has, that these optimisations can be curtailed at some arbitrary time horizon defies commercial common sense. The forum was an illustration, where NECA had expanded the original range of 6 "exceptions" to 13 prior to the forum, and where 15 minutes of conversation provided a number of fatal examples and queries to the defined exception list. The effect of a number of the exceptions is to violate the market objective of technological neutrality, enshrined in clause 1.3(b)(5).

The core of many of these optimisations is time. To restrict time flexibility is to create the potential to fatally damage the principle.

In its issues paper, NECA has suggested that there are a very small number of situations where it believes participant rebidding was not appropriate. At the forum NECA did not reply to the issue raised by a number of those participants that they had been named by NECA and their rationale hypothesized without NECA approaching their organisation. This raises issues as to the accuracy NECA's hypotheses on motivation and causation of these "events".

Importantly, in its written material, NECA does not

- Examine the effect of its proposed prohibition on the particular events of concern to NECA
- Examine the effect of its proposed prohibition on other market events.

NECA's own issues paper analyses the effect of rebidding as reducing November 2000 to April 2001 Queensland price by 40% (corresponding period Sth. Australia 14%, NSW 10% and Victoria 6%), the summer effects 55%, 46%, 29% and 42% respectively. *(at page 11 of Issues Paper)*

Historical review suggests that the effect of rebids within 3 hour of dispatch reduced January 2001 to March 2001 Victorian Pool price by 28%.

NECA has offered no analysis of the effect of prohibiting 60-68% of NEM rebids, for an issue relating to several half hours, over a couple of years, assuming a problem exists.

- Relate the 3 hour time period chosen to supply side dynamics, demand response, NEMMCO's demand forecast accuracy, predispatch volatility, ramp rate constraints or temperature rate of change data.
- Model the impact of reduced flexibility on energy constrained plant.
- Review the effect of increased dispatch risk on the hedge market, that is, the impact of increased risk premiums for contracted capacity on the market for hedge, cap or other products. Increased risk in the underlying market will lead to premiums in the hedge market and reduced liquidity.
- Examine the impact on the ancillary service costs sourced by NEMMCO and paid by customers given the reduced self dispatch flexibility of the energy market.
- Examine the impact on other market developments such as the 5 minute 30 minute anomaly, five minute pre-dispatch, and Ancillary Service causer-pays

In short, NECA has suggested but failed to prove a problem, and put forward a solution, without testing the solution solves or exacerbates the problem. (See our comments below on price levels as a problem) The NGF restates, that we do not believe that the problem is one of rebidding, once the constraint equation and dispatch working groups have eradicated SPD errors uncovered over the last 12 months.

## Price

Is the problem price?

If the "problem" is one of a perception of misuse of market power, it is a matter of law and economic common sense that market rules will not eliminate its effect. Structural change to the market is the proper mechanism for rectification of market power imbalance. NECA does not have a remit to examine or control price. The ACCC has statutory power to review and prosecute misuse of market power.

The NGF is not satisfied that NECA has not acted *ultra vires* in proposing Code changes whose initiation appears to have been based on a desire to regulate price outcomes.

Any affected person can take action under s46 of the TPA and the NGF is not aware of any current actions under s46 that would illustrate a potential problem with market power in the electricity industry, or failed actions that would illustrate the need for rectification to the authorisations as proposed by NECA as above.

The NGF is not aware of comment by the ACCC expressing concern as to market outcomes, indeed, the ACCC has commented to the contrary in recent times. The NGF is of the view that the market has been appropriately signaling the requirement

for investment in a number of regions and seasons, in the type of generation called for in the statement of opportunities over the last 3-5 years.

The NGF does not believe that this proposal is in the interest of its members' customers, particularly given the very real prospect of increased prices and increased volatility resulting from the proposal. If the prohibition leads to increase in risk and or pool price, what is the next step?

### **Improvement in the Pricing Efficiency of the NEM**

The NGF is of the view that pricing efficiency could be improved in the NEM.

1. It is our view that the disparity between 5 minute dispatch and 30 minute pricing leads to inefficiencies of the pricing process. The 5/30 Working Group, currently in place, is reviewing this process with a view to improving its effectiveness. This work could be accelerated.
2. The Network Constraints Working Group is examining issues fundamental to alignment of SPD and the physical system. The NGF supports the most accurate reflection of the physical system in the NEMMCO constraint equations and operating protocols. This work could also be accelerated.
3. The continued delay in a market for ancillary services reduces the competitive efficiency of our market, reducing an important economic signal to a annual tender and non-transparent dispatch constraints. NEMMCO are obviously working to commence the ancillary services market in September. NECA should work assiduously to prevent another extension of time on this much delayed and important reform.

### **Consequence**

The move away from self-committed self-optimised generation economics is the first retrograde step in the history of the market. In addition to reducing the viability of peak generation it alters the underlying economics of baseload plant. The NGF, under these conditions will have to reconsider its approach to several prior proposals, specifically the lack of transparency of the dispatch-able demand side load and the need for demand side and retailer demand commitments.

On the first of these, if the evolution of the Australian market will be toward artificial restrictions on the flexibility of the supply side, then economic efficiency will require the symmetric removal of the current flexibility of the demand side of the industry in respect of switchable load essentially as an extension of the Hazelwood Code change rejected by the Code Change Panel last year on the grounds of a self committed supply side.

In addition, the information asymmetry implied by the need for supply to bid accurately and explicitly 3 hours in advance, may need to be matched by obligations for retailers to forecast and manage their commitments of load into the pool.

This is not a direction the NGF sees as of long term value to the Australian Electricity Industry, but would become necessary to avoid allocative and other inefficiencies between demand and supply sides of the industry.

## **Conclusion**

NECA is seeking to apply an artificial constraint to the operation of an energy only self commitment real time market, to remove pieces of the Code from the authorization, and alter the burden of proof for parts of participant's information provision. The burden of proof associated with such a fundamental change to the economics of the Generation and Retail businesses, and the analysis of effects on our customers, has not been discharged by NECA.

The code change should be forwarded by NECA to the ACCC without these aspects.

The NGF further wishes to advise that following its meeting with NECA Chief Executive Stephen Kelly on Monday 27 August, that it is very willing to pursue jointly with NECA measures that would ensure that bidding and rebidding practices might not act in any way to jeopardise the security of the system. Unfortunately our meeting with Mr. Kelly was scheduled such that the NGF has had insufficient time to assess whether some alternative measures might be jointly developed, however we do point to the possible market improvements highlighted in this report and reiterate our willingness to further develop these, and other measures, into a comprehensive package with NECA.

Yours sincerely



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27 August 2001

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Dear Geoff

## NECA PROPOSED REBIDDING CODE CHANGES

NRG Asia-Pacific and NRG Flinders (NRG) takes this opportunity to provide comments to NECA in relation to the proposed rebidding code change. We have a number of concerns with the code change proposal as a "solution" to the perceived price volatility problem.

NRG would like to note that this code change proposal is being introduced into the market for consultation at a time when high prices have had a significant positive impact on investment within South Australia. Higher and sometimes volatile prices in South Australia have provided investment signals imperative for the future of the South Australia region. South Australia has seen new investment predominantly in the form of Pelican Point, but more importantly has had a number of committed projects including the upgrade of Playford Power Station and Murraylink.

The market is dynamic and is changing. In fact South Australia has experience low and stable pool prices since March 2001 and for the month of August 2001 (as at the 28<sup>th</sup> August), SA experienced a regional reference price of \$2.77 less than Victoria and \$6.00 less than New South Wales. This is the result of new investment and greater competition amongst supply side participants. This rebidding code change proposal will dampen this price signal. NRG considers that this code change proposal cannot be in the best interest of the NEM.

### 1. Trade Practices Act<sup>1</sup>

#### Section 46

NECA's Report ("*Generators' bidding and rebidding strategies and their effect on prices*") appears to proceed under a misapprehension about the application of section

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<sup>1</sup> Trade Practices Act advice provided by Johnson Winter Slattery – Adelaide Office

46 of the Trade Practices Act (TPA) to rebidding activity, and hence the width or utility of the “immunity” provided by the ACCC authorisation in conjunction with section 46(6) of the TPA.

Section 46 is aimed at actions with a purpose of hindering or preventing competitive activity or damaging a competitor. To the extent that rebidding is used in contravention of this section, then it is unlawful, notwithstanding the limited immunity under section 46.6.

This means that the “immunity” from section 46 is illusory, because the conduct authorised under section 90 for the purpose of sections 45 and 47 would not include use of the rebidding procedures to give effect to a collateral abuse of market power.

Section 46.6 would only operate where the rebidding rules are applied as currently provided in the NEC without the additional purpose of taking advantage of market power to damage competition. In our submission therefore it is unnecessary for NECA to introduce new bidding rules to limit generator bidding behaviour as it is already dealt with in the TPA.

In essence, we think that NECA (and certain market participants) may have confused the ambit of section 46, by assuming it would apply to rebidding but for the authorisation and section 46(6), and therefore assumed that section 46(6) would in practice exempt rebidding from scrutiny under section 46. These assumptions are incorrect, and consequently NECA’s discussion on page 7 of the Report, along with its intended invitation to ACCC to vary the terms of the authorisation is misguided. We urge NECA to reconsider its position.

All that said, the underlying issue of concern is “price volatility” caused by or associated with rebidding. The underlying cause of these price spikes is a lack of generation capacity, and the price spikes send important investment signals to participants and potential new entrants about the opportunities for profit from installation of additional generation capacity. The perceived deleterious effects of rebidding would be removed if additional capacity became available. Amendments that interfere with the operation of the price signals of the market must therefore be avoided.

We therefore believe that NECA must leave TPA decisions to be initiated and undertaken by the ACCC.

It is very concerning to NRG that NECA has not fully identified the “carve out” of rebidding from the existing Code authorisation. NECA has not provided any indication of the legal or operational impact that this may create for participants within the NEM.

## **2. Proposed 3.8.22A**

We strongly object to proposed clause 3.8.22A.

Paragraph (a) is objectionable because it is drafted in the negative – that there must be reasonable grounds for believing that the bid will not be varied.

Paragraph (a) would not permit a bid to be made if there is a possibility or contingency that a varied bid may need to be submitted. That is, if the generator has

reason to believe that a bid might need to be varied (but is not certain one way or the other), paragraph (a) would mean that it cannot submit a bid.

This is highly impractical, because in practice bids must be submitted on a best estimate basis - based on the circumstances known and expected – but uncertainty and unpredictability are inherent in a dynamic energy only market.

We think NECA is seeking to apply concepts developed in other contexts (that is under the TPA for consumer protection in relation to marketing type representations) in areas for which they are inappropriate.

Paragraph (b) is more objectionable.

This would in effect reverse the onus of proof, meaning that a generator would be deemed not to have reasonable grounds for its belief that a bid would not be varied unless it adduces evidence to the contrary. In effect, generators are deemed or presumed to be in breach of paragraph (a) unless they can prove to the contrary. This is unfair, unusual and onerous, given the potential penalties that can be applied. It is worth noting that breach of section 52 of the TPA is not an offence, does not carry a penalty, and exposes a defendant to civil damages.

Once again NECA is seeking to adapt an inappropriate regime. In the TPA, section 51A is to similar effect to paragraph (b), but it relates to statements as to future matters. Interestingly, this reversal of the onus of proof in relation to future matters has been removed under the Corporations Act in relation to dealings in securities, where the unworkability of the concept has been recognised.

In any event, under the TPA it applies in situations where there is a choice as to whether to make a statement as to the future. Hence, if a person does not have reasonable grounds, they can choose not to make a statement to which section 51A might apply. Generators do not effectively have that choice. Given the operation of the market, generators do not have choice as whether they submit bids (other than by withdrawing supply, which would not be consistent with the policy objectives of NEC). In our view, it is inappropriate to impose such a draconian measure.

In practice compliance with paragraph (b) would require onerous and impractical record keeping because the generator would have to positively prove a negative proposition – that it has reasonable grounds for believing the bid will not be varied – that is, every conceivable reason that could give rise to a variation will need to be considered, excluded and that exclusion documented in relation to every bid. A failure to do so would cause a generator to be in breach of paragraph (a).

With respect, this would be an onerous and unfair obligation to impose on generators, quite apart from the fact that a reversal of the onus of proof in relation to a provision carrying a penalty itself is unfair and onerous.

The inability of NECA to produce a positive set of code change proposals aimed at a positive rebidding regime with explicit areas of breach is unfortunate, effectively isolating those participants that are affected by the proposal.

### 3. Prohibition of rebidding within 6 trading intervals prior to dispatch

NECA and ACCC have both accepted that the flexibility to rebid is fundamental to the efficient and effective operation of the market and further NECA has determined that rebidding in fact has the effect of reducing average pool prices. NECA in its paper on Generators' bidding and rebidding strategies and their effect on prices in fact stated, "Rebidding represents an essential flexibility to enable generators to respond to changes in physical and legitimate commercial circumstances. It is imperative for the effective operation of the market. Efficient prices represent crucial signals for much needed new investment and for demand side responses".

This code change directly contradicts both NECA and the ACCC's assertions as stated above.

This proposal does not allow generation participants to internally optimise their physical and economic position. It takes away the ability to react to market anomalies such as demand forecast errors, network constraints, competitive conditions, plant start up and input costs and contract position.

The clause 3.8.22 (b1) effectively does not allow a participant to vary its available capacity at any time after the sixth trading interval to that trading interval unless:

- The rebid is a result of a mechanical breakdown, electrical breakdown or failure of equipment that occurs after the sixth trading interval prior to dispatch and which consequently changes the capacity of the generation unit .....
- The rebid is required as a direct result of a reduction in or change in the nature of fuel to the generating unit....
- The rebid is of any part of capacity of a scheduled unit not scheduled for dispatch, which is required to be dispatched pursuant to the terms of binding agreements...
- The rebid is required to ensure the scheduled unit is operated in accordance with good electricity practice at the time of the rebid that otherwise would not occur if the scheduled unit was operated in accordance with the current pre dispatch schedule and other market information....

This clause of the code change proposal is very unclear in relation to a number of areas, namely:

- i. The reference to generating unit infers that a participant cannot rebid any of its generating units to cover a unit that has been affected by one of the four exceptions above. A generator is therefore not capable of providing any self-insurance capability and would find it difficult to get contract insurance because other generators would not be capable of covering a unit failure within the 3-hour period.
- ii. How are generating units that are aggregated treated in relation to this clause?
- iii. How many times can a participant rebid within the 3 hours, if affected by one of the excepted reasons above? (i.e. can it rebid to come off then on again within the 3 hours?)





- iv. The code change effectively allows some generators to optimize their position due to fuel related constraints. This is directly in conflict with the NEC market objectives 1.3(b)(5) "a particular energy source or technology should not be treated more favorably or less favorably than another energy source or technology".
- v. The code change also contradicts the NEC market objective 1.3(b)(1) which states that the market should be competitive. This 3-hour prohibition in effect removes competitive pricing close to dispatch.
- vi. We are uncertain how NECA would monitor rebids "under terms of binding agreements". For the most part, contracts are very confidential and secondly counter parties may contract to each other for certain volumes.

A limit on rebidding 90 minutes prior to dispatch in the Queensland market was implemented, failed and was removed. Recent outcomes in the Queensland market demonstrate that its removal resulted in a significant reduction in pool prices from those artificially created by the rebidding restriction. Similarly the market operator in NEM1 recommended that the restrictions imposed on rebidding be relaxed to allow more efficient operation of the NEM1 market.

Rebidding to account for changes in financial position is an essential component for liquidity in the financial markets. The short term insurance or hedging market will become illiquid if the sellers in this market are unable to match their physical and contract positions as new contracts are written. This liquid short-term market is a valuable risk management option for all market participants.

#### **4. Demand side participation**

NECA has paid weight to demand side arguments that price volatility is damaging to the NEM. This is an ironic argument, because demand side participants will not have to abide by these code changes, more so they benefit from not having to hedge their position because these code changes helps mitigate their risk position.

Demand side participation is very much required in the NEM, but it must be transparent. There is little point having demand side participants having the ability to switch off during high prices when the rest of the market is blind to their actions and are unable to react to it.

We believe that there would be less demand side support for these proposed code changes if loads over say 30MW were required to bid into the market.

The code change proposal is therefore not symmetrical in its effect or treatment.

#### **5. NEM improvements to help reduce volatility**

NECA has not implicitly reviewed any alternatives to reduce inefficient market outcomes, which may impact on the volatility of pool prices. NRG believes that there are a number of areas that should be addressed before implementing the rebidding code change proposals, including:

- i. The use of five minute ex ante dispatch and 30 minute ex post settlement results in a significant distortion of the market signals for both generators and customers, which creates difficulties in hedging short-term price volatility. NECA must encourage the resolution of this price distortion via the current NEMMCO review.
- ii. Alignment of SPD and the physical system via the Network Constraints Working Group.
- iii. Timely implementation of the ancillary services market, which is aimed at improving the efficiency and reliability of the system.
- iv. Further investigate and provide an optimum solution to the market regarding the de rating of the Vic-SA interconnector.
- v. Improve demand side participation as well as transparency into the market.
- vi. Allow the previous code change on rebidding to take effect i.e. the requirement to disclose adequate and verifiable reasons for rebidding.

## Conclusion

NRG believes that the rebidding code change proposals have the potential of seriously effecting the operation of the market on both a physical and financial level. NECA has not demonstrated that a change of this magnitude is required. There has been no real analytical evidence to support the need for a code change nor has there been analytical data to support the option considered by NECA.

We believe that NECA's interpretation of the TPA is flawed and even more fundamentally do not believe that NECA has the authority to make these changes.

We request that NECA reconsider its approach in relation to rebidding and firstly look at alternative solutions to improving the current inefficiencies in the market, which may be impacting on price volatility. NRG points to the past few months in the NEM (since March 2001), which has experienced stable competitive pool prices.

The current low and stable pool prices experienced in SA are primarily a result of previous price signals having the right market result, i.e. increased investment. South Australia is a classic example of how efficient price signals have resulted in new investment in both generation and entrepreneurial interconnection. NECA's code change proposal will squash this price signal, exacerbating a problem that it is attempting to solve.

The code change proposal cannot be supported by NRG.

If you have any questions please contact me on (08) 8372 8726.

Yours faithfully

Reza Evans  
Manager Regulation and Market Development

20 August 2001

Mr Greg Thorpe  
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Attention: Greg Thorpe

Dear Greg

**CODE CHANGE PANEL: PROPOSED REBIDDING CODE CHANGES**

**Executive Summary**

Origin Energy welcomes the opportunity to offer its views on the rebidding code changes proposed by NECA. Origin is a vertically integrated market participant with an incumbent retail position in Victoria and a growing retail position throughout the NEM. Therefore we are concerned about any market changes that may influence our ability to manage this retail position and result in increasing the costs of supply for our customers.

In Origin's opinion NECA has overreacted to poorly informed public criticism and media reports on the NEM performance. Contrary to media reports and views of some lobby groups, generator rebidding is not a significant cause of increased electricity prices or supply problems. Increased prices are market signals calling for increased peak capacity and have resulted in substantial new additional generation capacity. It is important that proper supply and demand signals be allowed to continue to operate to bring forward the additional capacity essential to satisfy peak summer demand.

By limiting rebidding to 3 hours before dispatch NECA is proposing radical code changes to what is of necessity a 5-minute dispatch market. Peaking generators will be unable to competitively respond real time to demand changes when the system is stressed and customers will pay the cost. These proposed code changes will play into the hands of the very market participants NECA perceives to have the market power to lift prices. NECA has incorrectly identified the problem it endeavours to correct and has failed to adequately analyse the proposed solution. The proposed code changes will therefore be counterproductive.

Central to these code changes are proposals that would:

1. Limit the rebidding of registered generating units to three hours from the despatch trading interval
2. Deem generators not to have had cause to rebid unless they can prove otherwise.
3. Relax the requirements of NEMMCO to return the electrical system to a secure operating state as soon as possible and force NEMMCO to make an economical

decision between prices and system security, a role, which will remove the impartiality that is essential for NEMMCO to maintain as the market operator.

It is understood that these code changes were motivated by a belief within NECA that on some occasions some market participants have exerted undue market power, despite legally operating within the ACCC authorised rules of the National Electricity Code and without notice from the ACCC that they have breached the Trade Practices Act.

The role of NECA (as industry regulator) is to "administer the ongoing development of, and changes to, this Code to achieve the *market objectives*". And to ensure that jurisdictional policy is met by the operation of the code and that market participants adhere to the code. The ACCC has not expressed a concern about the behaviour of market participants in relation to breaches of the TPA and thus it is inappropriate for NECA to do so.

Origin believes that NECA has failed to clearly identify the problems being addressed nor to quantify the materiality of these problems and their impacts. The suggestion by NECA that the code change proposals will resolve an undefined problem has also not been proven via any form of rigorous analysis. Nor has NECA analysed and presented the flow on repercussions of its proposals on system capacity and security. For NECA to propose code changes that will have a material impact on the operation of the market without any form of evidence or analysis is both irresponsible and dangerous. We urge the Code Change Panel not to accept any proposal by NECA that is accompanied by anecdotal evidence rather than adequate analysis in support of its proposals. The panel should not entertain any suggestion by NECA that it is not possible to model the likely impacts of their proposals. NECA is the industry regulator and should be in the best position to analyse industry behaviour. If it is not then NECA should not initiate code changes it does not understand.

The NEM is only three years old. Two years ago the concern over summer supply predominately in the southern states was over potential blackouts caused not by the operation of the market but by industrial unrest. Last summer the concern was about price although wholesale supply was maintained throughout. The coming summer sees the NEMMCO SOO 2001 and follow up addendum indicate that reserves will be sufficient for summer. This is reflected in summer peak swaps in Victoria, which are trading around \$129/MWh, substantially lower than the \$180/MWh that traded several months ago. This fall in prices is reflective of the new generation being constructed as a response to appropriate forward price signalling.

The proposals by NECA will pre-empt a normal competitive response and result in a significant change to the operation of the NEM.

NECA suggests when referring to certain generator rebidding behaviour in their July 2001 report that;

*"As well as their direct effect in the spot market, those very short-term price spikes also drive up the cost of financial contracts. They have no basis in the underlying dynamics of the market"*

Such statements show both a lack of understanding by NECA of how the market operates and financial contracts are priced, but more importantly indicate a complete lack of acknowledgement by NECA of the various generation projects that have been developed and the increase in competition that has naturally resulted.

#### Key Issues:

- The NEM is working as demonstrated by the development of over 1,000MW of new generation in Queensland as a response to higher prices and over a 1,000MW of new generation in Victoria and South Australia. NECA has failed to show that there is a market failure, nor have they proven that their unsubstantiated claims of generator rebidding problems will occur into the future as competition increase. The evidence suggests that the market is working properly with the appropriate investments occurring. NECA code change proposals are likely to threaten the very success that the market is currently demonstrating and be counterproductive to long term market viability.
- While short-term price spikes will certainly influence the spot wholesale trading market, long-term investment decisions are made based on the long-term forward price curve and the rules that govern the market. The NECA proposals may inhibit the ability of some generators to generate so as to manage any forward financial sales position and thus such risks will be reflected in higher forward prices. Thus the NECA proposals may result in a far greater increase in forward prices and end use customer prices than occasional price spikes.
- NECA proposals are in direct conflict of the new Ancillary services arrangement.
- The code changes are discriminatory in nature between different types of gas fired generation units.
- The proposals may lead to an inefficient use of resources.
- The end result of the proposals will be higher contract prices and hence end user retail prices. While the proposed code changes will clearly impact the manner in which generators offer capacity into the market the costs of these proposals will be borne by the retailers and the end use customers. Retail competition will only be maximised by not inhibiting the ability of generators to offer financial contracts by restricting their ability to manage these sales.
- The real time ex anti market that operates in the NEM creates a pool price that is reflective of the real time conditions of supply and demand. The NECA code changes will create pool prices that do not reflect the true market circumstances. And it is this outcome which should be of the greatest concern to the jurisdictional, NEM Ministers, COAG, the ACCC and other regulatory bodies whom are relying on private investment responding to price signals to provide supply investments and for end use customers to receive the lowest possible price for a guaranteed supply.

It is our view that the proposed code changes will not address the concerns that NECA has expressed. The code proposals will discriminate specifically against peaking generators, those very investments that the jurisdictions are trying to encourage so as to ensure security of supply. The code changes will rather increase the market power of some participants by disallowing competition to occur in real time, while threatening the supply security of the market and deterring new investment. Therefore, Origin Energy does not support any of the proposed code changes.

## Inaccuracy of NEMMCO demand and price forecast

In offering generation capacity market participants take account of many factors, including both physical plant conditions, underlying contract positions, and demand and price forecasts. Electricity is an instantaneously produced and consumed product that generally cannot be stored. Thus supply needs to follow demand for the vast majority of time. Therefore the accuracy of demand forecasts is crucial in determining the appropriate bids of generation units.

In their quarterly statistical digests NECA analyses the accuracy of price variations in the various regions and offers some data as to the most probable reasons for these variations. Table 1 below presents the data for financial year ending 2000/2001. As can be seen, the vast majority of price variations are due to demand forecast

Period	Reason For Variation	Demand	Availability	Combination	Network	Other
July-September 2000 (Winter)	Queensland	74%	22%	4%		
	NSW	82%	18%	0%		
	Snowy	66%	33%	1%		
	Victoria	69%	33%	1%		
	South Australia	64%	27%	3%	6%	
October-December 2000	Queensland	68%	28%	4%		
	NSW	88%	12%	0%		
	Snowy	52%	47%	1%		
	Victoria	74%	25%	1%		
	South Australia	69%	20%	6%	4%	1%
January-March 2001 (Summer)	Queensland	69%	27%	4%		
	NSW	78%	18%	1%	3%	
	Snowy	N/A	N/A	N/A	N/A	N/A
	Victoria	69%	26%	1%	4%	
	South Australia	62%	25%	3%	5%	5%
April-June 2001	Queensland	83%	16%	1%		
	NSW	90%	9%	1%		
	Snowy	N/A	N/A	N/A	N/A	N/A
	Victoria	80%	20%	0%	0%	
	South Australia	67%	29%	4%	0%	0%

Table 1

NECA Quarterly Statistical Digests, October 2000, January 2001, April 2001, and July 2001: The Most Probable reason for the variations between actual and forecast price in each region.

The information presented above indicates that the key driver for price differences in the market between forecast and actual, in either direction is the inaccuracy of NEMMCO demand forecasts. Demand fluctuates generally without any limitations, and generators are expected to respond to these fluctuations instantaneously. Therefore great reliance is placed on NEMMCO demand forecasts.

In the same quarterly NECA statistical digests, data is presented as to the mean absolute error between the actual and forecast demand in each region. NECA compares the twelve, four and one hour ahead forecast with the actual demand levels. This data was

presented in graphical form, therefore Table 2 below which presents this data are estimates based upon the graphs. While the table does not show the extremes that can occur in forecast errors, however they do show an important trend.

Period	Hours Till Despatch	4	2	1	Variation 4-1
July-September 2000 (Winter)	Queensland	2.00%	1.75%	1.25%	0.75%
	NSW	2.25%	2.00%	1.04%	1.22%
	Victoria	2.50%	2.20%	1.50%	1.00%
	South Australia	3.50%	3.20%	2.35%	1.15%
October-December 2000	Queensland	1.80%	1.65%	1.25%	0.55%
	NSW	2.20%	2.00%	1.40%	0.80%
	Victoria	2.25%	2.00%	1.60%	0.65%
	South Australia	3.50%	3.25%	2.25%	1.25%
January-March 2001 (Summer)	Queensland	2.00%	1.75%	1.25%	0.75%
	NSW	2.25%	2.00%	1.35%	0.90%
	Victoria	2.50%	2.00%	1.65%	0.85%
	South Australia	3.50%	3.25%	2.20%	1.30%
April-June 2001	Queensland	2.00%	1.80%	1.25%	0.75%
	NSW	2.30%	2.00%	1.40%	0.90%
	Victoria	2.50%	2.25%	1.50%	1.00%
	South Australia	3.90%	3.25%	2.25%	1.65%

**Table 2**

NECA Quarterly Statistical Digests, October 2000, January 2001, April 2001, and July 2001: Mean Absolute error between actual and forecast demand.

It can be seen in the above table that the closer the demand forecast to real time the more accurate the forecasts. This is important for generators in deciding upon the timing for maintenance works and unit availability. And therefore, by restricting generation bids to three hours from real time this will result in participants making bids based on less accurate demand and price forecasts than if this was done five minutes prior to its consumption.

There is a high level of inefficiency created by relying on demand and price forecast three hours from real time to make generation bidding decision. The further out the demand and price forecasts, the less reflective it will be of weather changes, unit failures and other changes in conditions as closer to real time forecasts, and this will result in misinformed decisions being made by participants as to generating plant availability and bid pricing to suit the market conditions.

One consequence of a three-hour restriction may be to restrict the availability of a generation unit that is having maintenance work done, but could be available within half an hour if needed. The proposed restrictions would not allow such a unit to be bid into the market if demand grows at a quicker rate than forecast three hours earlier. Alternatively if demand was to fall at a quicker rate than forecast, the restriction on rebidding would stop generators wishing to be dispatched from competing for the lower levels of demand, thus resulting in higher prices than would have occurred under real time bidding conditions.

It is clear that the rebidding restrictions place an undue reliance on the accuracy of demand forecast, which by NECA own admission, is the predominant cause of current differences between forecast and actual prices.

### **Intention of Code Proposals**

Despite NECA personnel being vocal in recent market forums about certain problems that they believe exist in the market, there are no specific references made in these code proposals as to the aim or purpose of the changes. No evidence has been produced to show that any problem exists, nor has any analysis been provided to support these changes. Code changes should not be proposed without relevant background evidence in support of the changes. We would recommend that the Code Change Panel ignore the code change proposals completely until appropriate evidence has been produced showing that a proven problem exists and which shows that the proposed code changes address these problems and will not result in more significant problems.

### **Ancillary Services**

The Frequency Control Ancillary Service (FCAS) market expected to begin sometime in September 2001 requires generation units to better manage their units frequency variation and penalises those units whose output does not match its despatch target by increasing its causers pays factor when this variance matches the variance of the market. This factor is used to determine the charges to be allocated to that generator in the next period for its share of regulation FCAS costs. Therefore, the new arrangements place an obligation on generators to rebid their units as often as required so as to avoid this mismatch and reduce their causer pays factor. Thus there would be a conflict in the market rules if units were prohibited from rebidding for three hours out, as they would not be able to correct their bids to match their unit's output to mitigate FCAS exposures. This is a major issue for gas-fired peakers whose output often changes over short time frames as the temperature changes especially during the summer as temperatures fluctuate over minutes and hours.

There is a further bias here between steam and non-steam gas turbine units. Only steam turbine units will have the flexibility to react to regular load variation requirements for the provision of ancillary services. In the energy market gas turbine units are generally unable to be the marginal generator, as they generally do not have load variation flexibility without the cost of capital modifications that will result in accelerated maintenance and higher operational costs. Thus the proposed rebidding restrictions will require such units to either bid themselves unavailable or at higher levels than under the current bidding rules so as to avoid potential mechanical damage to the turbines. This operational difference will discriminate between steam turbine and gas turbine units under NECA's rebidding prohibitions. NECA must also be mindful that the Code prohibits discrimination in the operation of the rules between alternative forms of generation.

The limitation on rebidding will also require a higher level of enablement for the provision of FCAS. This will result from lower levels of generation flexibility within the energy market where unavailable units will not be able to react to real time events within three hours of dispatch. However enhanced market power will be delivered to those generators that can offer load into the ancillary services markets where five-



minute rebids are possible. In fact, there will be an incentive for some generators to offer their entire load into the energy market at very high levels (i.e. VoLL, so that in effect, this unit will not be generally despatched for the supply of energy), so as to game the ancillary services market and energy markets due to this mismatch between five-minute and 3 hour rebids. Such action by some generators will make a mockery of the co-optimisation formula that attempts to dispatch energy and ancillary services in a manner that creates a least cost solution for the market.

The market power of generators bidding into the less competitive ancillary services market will also be enhanced by the fixed bidding period in the energy market. Generators bidding into the ancillary markets will know that based on current demand the energy pool price should remain unchanged or at least not be any lower, as these generators cannot change their bids. This will give ancillary generators a competitive advantage and enhanced market power and will clearly impact on the co-optimisation formula.

The issue of market power is further accentuated by the fact that not all generators that offer energy in the energy market can offer ancillary services, as they may not have automatic governor control or even governor control which allows the provision of contingency services. Thus a greater requirement of ancillary services will be bid by a fewer number of generators than in the energy market. This will result in a lessening of competition and increased costs for end use customers. This outcome is clearly counterproductive to what NECA is trying to achieve by the energy rebidding restrictions. It is but one example of a failure by NECA to conduct a rigorous analysis of the full consequential impact of its proposals.

There have been many complaints about the liquidity of the financial markets for the provision of energy hedges. In the ancillary services market where there are fewer suppliers than in the energy market. When this market starts this issue will be further exacerbated. The hedging market is non-existent in the ancillary services market and will likely take a long time to develop. NECA's proposals will therefore place a greater level of ancillary exposure on retailers. This will undoubtedly lead to higher end use prices and increased volatility as these un-hedgeable costs will be reflected in retail prices offered to contestable customers and eventually will have to be passed on to franchise customers.

### **Fuel Restrictions and Substitution.**

While the proposed rules allow for a rebid of a unit down when unforeseen fuel problem occur, it will remove the flexibility of a generator to conserve fuel when shortages are forecasts. This will result in higher prices as participant bid their units in a conservative manner so as to avoid being despatched at uneconomical levels.

The best example of this impact relates to when there are potential gas shortages in Victoria and South Australia where gas fired units are relied upon for the provision of peak and in S.A. often base load electricity supply. While the marginal fuel cost for gas may be around \$50/MWh, for fuel oil or diesel the fuel costs vary from \$200-\$300/MWh. This cost variation will present a dilemma for gas-fired units that are able to switch between fuels and those gas-fired units, which have no fuel switching capacity but lesser contractual priority for within day fuel supply. If there is a concern that gas restrictions may occur a generator will need to be conservative and will offer its capacity at the marginal cost of alternative more expensive fuels rather than at the lower marginal cost

of natural gas. To not do so may result in this unit being dispatched at uneconomical levels if a gas shortage occurs and it wants to shift to a more expensive fuel source. However the price impact of this behaviour will be that if a gas shortage does not occur then pool prices may be higher than if the rebidding restrictions were not in place and this generator could vary its bid.

The proposed exception by NECA where fuel source problems occur does not cover instances where fuel shortages are foreshadowed all day, without a defined period when a problem may occur. In such a circumstance because a participant has known about a potential problem prior to the three-hour period he would be restricted from the rebidding exemption where a fuel source problem occurs.

### **NEMMCO Management of Power System Security**

NECA proposal to change the wording in 54.2.6(b) of the code to remove the words "as soon as practical to do so" places an undue risks and decision making process on NEMMCO while placing at risk the system security of the NEM.

The defined operational rating of various inter-connector are principally set so as to manage possible contingency events such as units tripping or unexpected sudden demand increases. Once an initial contingency event occurs the risk to the market security if a second event occurs is increased dramatically. Therefore it is important for system security that any contingency event be resolved promptly. The NECA proposal would increase the risk that a second contingency event would result in supply security problems or blackouts. It is unlikely that any jurisdiction would be happy with a procedure that increases the chances of blackouts so as to decrease some occasions of higher prices that may result from returning the power system to a secure operating state as soon as possible.

NEMMCO is the market operator whose role is to apply the rules of the code and manage the physical operation of the market. It is therefore important that all NEMMCO decisions are based on a known set of rules so as to give both market participants and NEMMCO certainty about the manner in which the market should operate. The NECA code change proposal will force NEMMCO to make a system security versus price trade off. It is not appropriate for NEMMCO to have to make such decision, nor is there any guidelines as to how NEMMCO would apply such a methodology.

It may even be possible that some participants whom have peaking assets in an importing state may be displaced at times when NEMMCO allows the insecure system to last for longer than necessary thus resulting in losses for that generator. Such incidents may create a potential liability for NEMMCO and create a disincentive for new generation investment.

NECA would be better served to focus their attention on the operational standards of the TNSPs. The TNSP must be more accountable for the operation of the various inter-connectors and carry some financial exposure/liability as an incentive towards increased reliability and availability. The TNSP must have incentives to offer firm capacity over inter-connectors at times of high market stress or demand.

### **Trade Practices Act Provisions**

NECA intends to request that the ACCC subject bidding and rebidding conduct to the operation of section 46 of the Trade Practices Act without limitation. It appears as if NECA intends to seek the removal of the protection provided by sections 46(6), so that the effect would be to remove the immunity to participants to actions in breach of s.46 where the ACCC have provided immunity to actions under s45 and s47.

It is our belief the ACCC does not have the power to exclude the operation of section 46(6). The TPA provides that if an activity is authorised, then the immunity in section 46(6) applies for any conduct that would breach section 46 and any one or more of the other sections in Part IV. The ACCC is not given the power, either in this provision or the TPA generally, to exclude that immunity. Accordingly, we cannot see how the ACCC could, in an authorisation, exclude the operation of section 46(6).

We believe that NECA has misunderstood the manner in which section 46 applies. The ACCC's authorisation does not, at first instance, provide an immunity for conduct that breaches section 46 of the TPA. Section 46 prohibits a corporation that has a substantial degree of market power from taking advantage of that power for prescribed anti-competitive purposes, namely:

- Eliminating or substantially damaging a competitor;
- Preventing the entry of a person into any market;
- Deterring or preventing a person from engaging in competitive conduct in any market.

While, at first instance, generators are subject to section 46, the section is not likely to apply to generators who rebid in accordance with the Code. This is because section 46 is limited in its scope. It requires the misuse of market power to be in respect of one of the three prescribed purposes listed above. Rebidding, however, even for the purpose of increasing prices solely for financial gain, is not likely to fall within one of these three prescribed purposes. Section 46 does not in general terms prohibit parties with market power from deriving monopoly rents.

### **Implications of Proposed Clause 3.8.22A**

NECA also proposes to insert a new clause 3.8.22A which will provide that a generator must not make a dispatch bid, unless the generator has reasonable grounds for believing, based on latest information available, including where appropriate the pre-dispatch schedule, that the dispatch offer will not be varied by a subsequent rebid. If proceedings allege that a generator has breached this provision, then the generator is deemed not to have had reasonable grounds for its belief, unless the generator adduces evidence to the contrary.

The effect of the proposed clause 3.8.22A is that if proceedings are brought against a generator, that generator will have the burden of proving that it did not breach this clause. To do so, the generator must "adduce evidence to the contrary" (i.e., give evidence showing that it did have reasonable grounds for its belief that its dispatch bid would not be varied by a rebid). This is problematic because it is unclear what evidence will be sufficient to discharge the generator's onus of proof and the standard to which that evidence must be demonstrated. There is a risk that generators will be

disadvantaged by this clause because it is unclear what is required in order to defend such allegations.

Further, it is unclear how generators are supposed to proceed in circumstances where they are aware that something may happen in the future which would cause them to rebid. If the generator bids on the basis that the event will not happen, then it is not clear to us that the generator has complied with clause 3.8.22A, as the generator had reason to believe that the bid might be varied. Conversely, if the generator bids on the basis that the event will happen, the generator has reason to believe that it may have to vary the bid, since if the event does not happen, the generator will need to rebid.

It is our opinion that the NECA proposal is an untenable code change that will create a high level of confusion amongst participants, deter new investment and place at risk the supply security of the market.

### **Impacts on price and market Power**

NECA has previously expressed concern about the undue market influence that a few participants may have on some occasions. And thus, NECA is of the belief that by restricting rebids to three hours prior to dispatch that this market power will be diminished. However all NECA accomplishes via its proposal is to enhance the market power of those very participants that it seeks to capture. Under the current market rules when a particular market participant attempts to influence the price via a rebid the impact of its action only lasts as long as it takes for other generators to rebid in order to take advantage of a higher price or a varied condition. This may be five minutes for a hydro plant to react or fifteen minutes for a gas fired unit to react. However, under the NECA proposal any rebid by a market participant in the last rebid period prior to the restrictions proposed coming into force, will simply result in a three hour period in which other generators cannot react. This is another example where NECA's proposed rule changes will be counter-productive to efficient market operation.

NECA incorrectly presumes that every generating unit is operating in idle reserves just waiting to ramp up. Generators vary their bids and availability as previously mentioned in line with demand and price forecast. If three hours prior to real time NEMMCO forecast show low demand and prices at which a gas peaker or a hydro plant may not be operating such units will leave their available capacity at high price levels. Thus any last minute rebids by a large generation unit will simply result in a longer period of price influence than is currently experienced.

The recent introduction of a new real time ancillary services market has raised the question of market power in the ancillary service markets. The proposal by NECA will not only increase the market power of some participants in the energy market but it will give some participants greater market power in the ancillary service markets. Thus the increased costs of NECA's rebidding restriction to the national electricity market will be reflected not only in the energy market but also in increased volatility and pricing risk to retailers, (and generators), in the ancillary service markets.

### **Risks Management**

There has been much discussion of late as to the adequacy of the electricity financial markets. Origin Energy believes that the financial markets are healthy and believes that



higher contract prices which reflect a tightening of supply and demand in some regions is not a reflection of market failure, but rather the proper price signalling mechanism that is crucial to new generation capacity investments being made. We are one of the largest financial traders in the market, a status that existed even prior to the purchase of the Powercor retail assets. We believe that retailers have a choice as to how to manage retail sales exposures based upon their appetite for risk and corporate objectives.

Risk management practices is the choice of individual participants and such participants should not feel as if the Code Administrator will change the rules to help manage these risks. To do so, would see some participants whom have been more prudent in their risk management practices be disadvantaged, as other less prudent companies are given a figurative "helping hand" in their risk management. Participant should not believe that the regulator will make changes so as to minimise their chosen level of risk as a result of poor decisions.

### **Physical Capabilities of Units**

Origin Energy is a vocal advocate of transparent market signals in the NEM. We support private investments being encouraged to support demand growth over taxpayer funded solutions, and have backed up this view with the construction of Roma and Ladbroke Grove power stations, and are currently constructing a new 100MW power station at Quarantine in South Australia. We note the development of a range of other privately funded solutions such as AGLs proposed Somerton and Hallet gas units as well as the gas turbines being constructed by others in Victoria.

We see the construction of these units as a positive sign that the market design is working and it is important that the construction of such units be encouraged. However, it is key to note that small gas fired units often avoid being the marginal generator. This is due to the physical capability of these units which often do not have the capability to regularly vary load without accelerating maintenance costs substantially, thus it is preferable to only operated such units fully loaded. It is for this reason that our Roma and Ladbroke grove units' only offer load at negative \$50/MWh when being dispatched, so as to avoid being the marginal generator which may lead to a requirement to vary the units output and risk damage to the units. It must be pointed out that bidding \$-50/MWh has a downward pressure on price. We believe NECA should be supporting gas-fired units offering peaking and fast start capacity when the market needs it. NECA's 3 hour bidding rule will discourage these generators and put upward pressure on price.

The rebidding restrictions will also at times threaten the supply security of the market and lead to higher prices, by not allowing peaking generators to rebid while generating in response to changes in prices and demand forecasts. If a fast start gas fired peaker with an inflexibility profile is dispatched at 1.00pm because the RRP price is \$200, which is above its bid of \$100, then this unit will be despatched for a minimum of one hour. However if the prices are below \$100 at 1.50pm then the T4 step of this unit will be triggered and it will begin reducing load until it comes to a full stop. Some gas-fired peakers require a period of up to an hour or more to cool down before they can be restarted so as not to damage the unit. However, if prices are forecast to be high even at VoLL levels from the half hour ending 2.30pm this unit could not be immediately restarted. The current rebidding rules give the owners of this generator the flexibility to rebid the capacity of this unit to a lower price band so as to ensure that it does not get directed by NEMMCO to shut off. Three hour bidding would not allow this and as a consequencel result in higher prices and at times threaten supply security with no ability for this unit to be turned back on, even if directed to by NEMMCO.

It is clear that the NECA code change proposals are discriminatory against peaking generators, specifically gas turbines.

## **Impacts on Contract and Retail Markets**

Generators rely heavily on offering financial contracts as a means of managing the exposure of being long the market by virtue of owning generation units. Such contracts offer revenue stability, satisfy bankers and also help substantiate new investments. However the proposed code changes will result in generators offering lower levels of financial contracts. If a peaking generator was to offer \$300/MWh financial caps, then in order to manage the exposure of such a financial sale the peaking generator would need to dispatch energy, not simply when the pool price was above the contract strike price on a five minute period, but more importantly, where it was believed that the higher pool prices would be sustained above this strike price for a sustained period, so as to substantiate all the costs involved in turning the unit on. However the proposed code changes would remove this flexibility from such generators as such decisions will need to be made three hours in advance when a price spike may not have even been forecast. Therefore, a peaking generator will be more cautious about offering hedge contracts and will need to build in a risk premium to take account of the inflexibility risk now created by the rebidding restrictions. This new risk will increase general market credit risk that will be a reflection of higher priced contract prices for retailers but more importantly bankers will have a greater concern about a generator's ability to manage the exposure of selling financial contracts.

This inflexibility risk will apply to all generators and will result in a general reduction of available financial contracts in the market. This will flow through to retail prices. In effect, the NECA proposal will not reduce market power of selected generators, but rather increase it, while impacting on the availability of financial contracts, thus increasing the risks of retailers and resulting in end use customers being asked to pay the price for the NECA code changes. We doubt this is the outcome NECA was proposing the changes to achieve.

## **Regulatory Risk**

Both the COAG review and the NEM Ministers forum recognises regulatory certainty as a key issue to ensure private investment in the NEM. While COAG agreed to request that NECA give early attention to NEM bidding and rebidding it appears as if NECA has approached an examination of rebidding as an independent exercise without any regard to the impacts of its proposed code amendments on any other aspect of the market or supply security. NECA has taken a direction from COAG and turned it into mandate to change the code. While the proposals result in reducing competition there is no apparent National Jurisdictional policy direction to restrict competition or rebidding on which NECA can base their actions. Nor are the proposals founded on either an ACCC direction or a proven breach of the Trade Practices Act.

It is also important to note the conflict of interest in that NECA personnel run and chairs the code change panel that is responsible for deciding upon code changes proposed by NECA. Such a conflict is not acceptable on the Inter-regional planing council, on other



government bodies or in the judicial system, and therefore should not be acceptable here.

## **Investment**

The ability to manage risks is a key driver behind the planning of any form of capital investment. The NECA code changes prejudice the development of new peaking generation plant. This consequence will likely result in times of supply shortfalls and higher prices for end users. Fast start generation offers many advantages to the NEM. While it certainly provides quick response supply to demand spikes, it also provides insurance products to base load generators whom face the risk of mechanical failure. However for fast start plant to manage these risks they need the flexibility to dispatch load into the market in real time, not be required to commit to a specific course of action three hours earlier. The code changes, while allowing for units with mechanical problems to rebid, do not allow for other fast start units to rebid on to replace failing units. The consequence of this could be short-term supply restrictions and higher prices.

Generation companies are often required to sell forward financial products ahead of construction so as to satisfy bankers and internal requirements. The proposed code changes will make such forward sales harder, as the ability to manage these sales will be limited. This will add to the features discouraging future investment in new generation in the NEM.

## **Portfolio Management**

Companies often develop generation portfolios, comprising of both peakers and base load plant. In the case of Origin energy we are developing multiple units on our sites such as the four units to be built at Quarantine. There are occasions, when despite there being multiple units at a site that there is insufficient fuel to run all these units. This may be due to supply problems, or onsite gas train restrictions. Thus at Ladbroke Grove for example, there may only be sufficient gas pressure to operate one unit at a time. Therefore under the current rules if the unit running was to experience a mechanical failure we would be able to turn on the other unit, effectively providing self-insurance. However, the proposal by NECA in S.3.8.22 (b1)(1)(i) would prohibit such behaviour within three hours. Therefore, if a unit tripped, while that unit could be rebid off, no other Origin owned unit could be bid on in order to make up the lost capacity.

The proposed code change in S.3.8.22A (a) does not provide the required flexibility for generators when fuel restrictions occur, as this clause would force a conservative bidding behaviour by generators if there was a possibility of fuel restriction such as gas shortages in S.A. during the summer (or winter). While a participant may be aware that gas is short it is not always possible to be completely confident about the fuel situation prior to the three-hour proposed time frame. Therefore units will need to bid more conservatively i.e. at the cost of liquid fuels in case a gas shortage arises and they are prohibited from rebidding under this clause. This issue is further exacerbated when companies take a portfolio approach for all their generation units in various regions, especially when managing internal force majeure risks. As highlighted previously, an inability to manage this risk internally will without doubt lead to higher contract and retail prices.



## NECA Rebidding Guidelines Powers

In S.3.8.22c3 NECA has changed the wording so as to give them the power to amend the rebidding guidelines whenever it wants. This change is completely unacceptable as it imposes no due process or checks on NECA. NECA is not an omnipotent body; it is responsible to both the market participants and the jurisdictions and should act and operate with that in mind. This code proposal should not be approved and alternative wording requiring public consultation should be included.

## Conclusion

The code changes proposed by NECA will increase retailer risks and price volatility leading to higher costs for end users while increasing the market power of some generators who are able to bid into the FCAS market as well as the energy market. Generators are likely to offer load in a more conservative manner reducing the availability of financial contracts thus increasing the risks of retailers while increasing the costs of end use customers.

There is much commentary in the Australian NEM about the events that occurred in the Californian Electricity market over the last few years. Many commentators including NECA and NEMMCO believe that the Australian market is fundamentally better in design and operation than the Californian market. Yet despite this, NECA has proposed market changes that run the risk of creating our own Californian consequence by increasing risks, end use customer prices, and discouraging much needed private investment. NECA has proposed code changes that will have dramatic effects on the operation of the market without any factual analysis supporting its proposals or on the impacts in the short and long term on either participants or customers. The NEC must be changed to ensure that code change proposals are substantiated by appropriate analysis as to its impacts without creating significant value impacts on participants and increased costs for end use customers.

Origin Energy does not support the proposed NECA code changes, as we believe it does not address the concerns previously raised by NECA. We believe that the code proposals are discriminatory in nature, enhance the market power of the very participants that NECA claims it is seeking to address while placing system security at risk. The end result of the NECA proposals will be higher prices for the end use customers, a decrease in generation investment and an increased likelihood of security of supply issues.

We would recommend that NECA turn its attention to a broader market review in line with the current COAG review that does not see one aspect of the market change without due consideration of the impacts to the rest of the market.

If you wish to discuss this submission further please contact the undersigned.

Yours sincerely

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Wholesale and Trading  
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## DEPARTMENT OF TREASURY AND FINANCE

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TF01D03001

Date: 22/8/01

Mr Stephen Kelly  
Managing Director  
NECA  
Level 5  
41 Currie Street  
ADELAIDE SA 5000

Dear Mr Kelly

### **REVIEW OF BIDDING AND REBIDDING STRATEGIES**

I refer to your report of 31 July 2001 associated with generator's bidding and rebidding strategies and their effect on prices.

The South Australian Government is extremely concerned with the operation of the National Electricity Market (NEM) and its impact on the South Australian community. The Government established the National Electricity Market Task Force to examine the rules and design of the market and to recommend what action needs to be taken to improve the operations of the market in South Australia. In addition, the Government had the issue of the operation of the NEM discussed at the Council of Australian Governments and the NEM Ministers Forum, which resulted in the request for NECA to review rebidding and VoLL.

The Government is keen to ensure that inappropriate rebidding activity in the NEM is minimised to the maximum extent possible, whilst recognising that the ability for generators to rebid in certain circumstances is essential for the efficient and effective operation of the market.

Accordingly, it is important that any proposed changes to rebidding, such as the 3 hour prohibition on rebidding, are carefully considered so that they provide an overall improvement by minimising inappropriate behaviour while ensuring that the benefits associated with rebidding are not lost.

Treasury and Finance notes that a number of participants at NECA's forum on its report expressed concerns with the 3 hour rule and its potential impact on prices and market efficiency, such as limiting potential supply side responses by fast start plant and

ensure that the overall objective of ensuring that inappropriate rebidding is minimised is maintained.

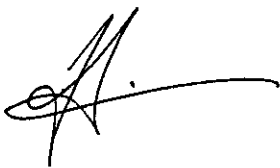
Treasury and Finance considers that NECA should actively monitor the impact of any changes on the outcomes in the market. Should the proposed changes be ineffectual, Treasury and Finance considers that NECA should reconsider other options to address inappropriate rebidding. This could include options such as the speed limiter proposal presented by NECA to the NEM Ministers Forum or giving NECA and the National Electricity Tribunal, under its Code enforcement role, the power to fine participants for inappropriate rebidding behaviour as an alternative to prosecution under the Trade Practices Act, as suggested by the NEM Task Force.

Treasury and Finance considers that the Task Force approach is consistent with the ACCC's condition of authorisation for the VoLL determination that requires that NECA review the adequacy of the current market monitoring provisions, which is to include an analysis of market behaviour rules and options for sanctions under the rules.

Treasury and Finance considered that there was support at the NECA forum, at least at an in-principle level, for the proposals aimed at addressing the technical issues associated with dispatch in the NEM, such as the operation of the interconnector and the treatment of constraints.

It is worth noting that the Government has provided in-principle support to the NEM Task Force report's recommendations associated with improving the efficiency of the dispatch process, and maximising the availability of the interconnector and providing firmer inter-regional hedging contracts. The Government looks forward to working with NECA and NEMMCO on finding an appropriate solution to these issues.

Yours sincerely

A handwritten signature in black ink, appearing to be 'JR', with a long horizontal flourish extending to the right.

John Robinson  
General Manager  
Microeconomic Reform and Infrastructure

**Comments to  
Code Change Panel  
Consultation Paper:**

**Generators' bidding and  
rebidding strategies and their  
effect on prices**

27<sup>th</sup> August 2001

**SNOWY HYDRO**  
TRADING PTY LIMITED

**Introduction**

Snowy Hydro Trading Pty Limited (SHTPL) appreciates the opportunity to respond to the Code Change Panel's draft code changes to generators bidding and rebidding strategies and their effect on prices.

Firstly, SHTPL recognise that this is a very complex issue with a great number of stakeholders. Based on other Participants' comments it is clear that some sectors of the market want change within the existing energy only market concept.

We believe that NECA is trying to find a satisfactory solution to suit a variety of stakeholders. NECA has addressed a lot of problems to date and we recognise and applaud NECA for what they have achieved. SHTPL recognise that it is difficult to find pragmatic solutions and hence it is our intention to help NECA facilitate further changes that are market efficiency enhancing.

It is our view that any imposed regulatory intervention would need to carefully balance the interaction of short and long term pricing signals and their effects on an efficient electricity market. It is our belief that it may be better to reconsider fundamentally changing the current market design, rather than regulating specific aspects of the current market. The risk with regulating certain aspects of the market is that it would result in market inefficiency. Additionally, every regulatory "band-aid" introduced will result in further regulatory intervention creating additional sovereign risk to current market Participants and at the same time deterring new entrants.

However, if the Code Change Panel still considers that it is necessary to impose the draft code changes to rebidding then we believe that our following suggestions to the Code changes will limit potential wholesale damage to the market and provide for a more pragmatic implementation of the proposed changes.

**Water Management**

Effective water management is off core importance to energy constrained hydro generators such as Snowy Hydro. For both internal operational and external factors outside our control we require the ability to rebid within the 3-hour window for effective water management reasons.

The current market structure does not optimise energy-constrained plant centrally and this function needs to be managed by the Participant. For example, we have a small storage at Geehi which if not appropriately managed through the ability to rebid may lead to a significant spot price rise for the over utilisation of that storage earlier in the day. The ability to rebid within the 3-hour window limits this potential outcome.

Internal operational factors such as small dam storages relative to potential large inflows at dams such as Guthega and Geehi require the ability to rebid within the 3-hour window if the initial factors that went into setting up the storage are

erroneous.

Additionally, our ability to manage downstream release constraints is critical in certain circumstances. The inability to manage within the 3-hour window could result in breaching our water licence and hence threaten our commercial viability.

External factors outside our control relate primarily to the uncertainty of inflows which are exasperated by reasons such as:

- (a) Pre-dispatch forecast inaccuracy
- (b) Inflow forecasting inaccuracy such as unexpected rain hitting a snow pack and causing more inflows than expected.

Our environmental obligations as part of our water license may also require the ability to rebid within the 3-hour window for environmental purposes.

It is our understanding that the intent of Clause 3.8.22 (b1) (2) allows for rebidding our water management related issues as part of "a reduction in, or change in, the nature of, fuel supply to the generating unit"<sup>1</sup>. We note that reference to "fuel" in the previous sentence should be "energy" to achieve a technology neutral definition. It is our view that the intent of this clause should be explicitly documented in the proposed code changes to include water management (both upstream & downstream) as a legitimate exemption on rebidding within the 3-hour window.

Any other interpretation of the relevant clause which would adversely affect our ability to manage water, will result in an inefficient use of water, may lead to environmental and water licence release breaches, and will result in a significant reduction in SHTPL's operational flexibility. The end effect would be unacceptable to SHTPL, will lead to market inefficiencies, and a decrease in flexible risk management products offered to the market.

In summary, any interpretation of 3.8.22 (b1) (2) which would not allow effective water management will lead to perverse market outcomes which we are adamant is an undesired outcome of the proposed code changes.

***Financial contracts including contracts with optionality and trigger points***

There are significant commercial implications associated with the ability to be able to hedge financial contracts including those with optionality and trigger points. All financial contracts require the ability to rebid within the 3-hour window based on changing externalities.

The majority of the contracts in the current market structure are

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<sup>1</sup> NECA, Proposed Rebidding Code Changes

written as financial contracts without any obligation for physical delivery. However, physical assets (such as market responsive plant) are used to underwrite and hedge these financial contracts. Hence it is imperative that all financial contracts require the ability to rebid within the 3-hour window based on changing externalities.

It is our understanding that the intent of Clause 3.8.22 (b1) (3) was to allow for this process. However, it is our view that the clause may need to be reworded to clarify that:

- (a) The option or trigger contracts can act bi-directionally. That is, the amount of contracts to be physically hedged could change either up or down within the 3-hour window.
- (b) "Binding agreements" include all financial contracts that are entered with another counter-party prior to actual dispatch.
- (c) Based on the Participant's risk management policy, the Participant has discretionary control to rebid the full or partial financially contracted quantity.

### ***Transmission Constraints***

With the current Review into the Energy Market and Network Services (RIEMNS) it is a probable outcome that with an increasing number of regions more Participants will be forced to contract interregionally (outside their regional reference code). This is necessary so as to secure enough financial contracts to underwrite cash flow requirements

This position means that more and more Participants will be continually exposed to interregional basis risk. A major determinant in the basis risk is the ability to manage transmission constraint risk and resulting price separation between the regions.

For instance, without the ability to rebid and unconstrain a constrained link such as the Snowy – New South Wales interconnector, the price divergence between the two regional reference nodes may result in a loss of tens of millions of dollars in a very short period of time. This loss would be borne by the Participant that had written the financial contract referenced to the importing regions' pricing node.

This situation exists currently under the existing market arrangements with SHTPL the only generator in the National Electricity Market with no native load and hence it is forced to write financial contracts that are outside its' regional reference node.

It is our view that another exemption category explicitly allows for the ability of a scheduled generator, scheduled network service, or scheduled load to rebid within the 3-hour window to unconstrain an interregional interconnector.

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Indicatively the code change inclusion could be in the form as follows:

- (a) The rebid is required as a result of an unexpected or reasonably anticipated interregional transmission constraint that becomes evident within the 3-hour window. The intention of the rebid must only be to unconstrain a constrained interregional interconnector or reduce the risk of constraining the interregional interconnector in order to defend a contract position in the importing region.

***Ancillary Services co-optimisation***

The Ancillary Services market currently only constitutes approximately 5% of the electricity market costs. It is our view that Ancillary Services must be sourced efficiently. More importantly, Ancillary Services costs should do not distort energy prices, which constitute the majority of the electricity costs.

Additionally, Ancillary Service providers will not receive compensation for energy constrained on/off situations. These instances will need to be managed by the active rebid of Participants if the constraints lead to material changes in the energy utilisation of energy constrained plant. Hence to manage this potential risk requires the ability to dynamically rebid.

We suggest that another exemption is included to allow Ancillary Service providers to rebid within the 3-hour window to manage co-optimised dispatch constraints.

***Other issues***

Other issues that SHTPL would like to note are:

- One of the major reasons in the past for price spikes has been the inaccuracy of NEMMCO's forecasting. With the inability of market Participants to rebid within the 3-hour window to adjust for this inaccuracy this may lead to more frequent price spikes.
- We note that the draft rebidding changes actually limit (rather than enhance) competition within the 3-hour segment before dispatch to certain market participants, namely the demand side and non-scheduled generators.
- We would like NECA to explain and justify why there isn't a complimentary obligation on the demand side for adequate disclosure and complimentary 'rebidding' restrictions. For market transparency reasons there needs to be similar obligations on the demand side.

## **Conclusion**

SHTPL recognises that this is a very complex issue involving many stakeholders. We believe that NECA is trying to find a satisfactory solution to suit all these stakeholders. NECA has addressed a lot of problems to date and we recognise and applaud NECA for what they have achieved. SHTPL recognise that it is difficult to find pragmatic solutions and it is our intent to help NECA facilitate changes that are market efficiency enhancing.

We reiterate our belief that it may be better to reconsider fundamentally changing the current market design, rather than regulating specific aspects of the current market. Regulating specific aspects of the market would result in market inefficiency, further regulatory intervention, and ultimately result in increased risks to current and intending market Participants.

Snowy Hydro Trading remains philosophically opposed to the draft code changes. Neither the less, if the Code Change Panel insists that it is necessary to impose the proposed changes then Snowy Hydro has specified our interpretation of the draft code changes in this submission. Our interpretation of the draft code changes based on discussions which NECA are:

1. Clause 3.8.22 (b1) (2) allows for rebidding within the 3-hour window for water management (upstream & downstream) related issues.
2. Clause 3.8.22 (b1) (3) will allow rebidding within the 3-hour window for financial contract commitments and contracts with optionality and trigger points which are binding prior to dispatch.

Snowy Hydro Trading recommends that the wording of these two clauses in the draft code changes need to be modified to expressly recognise these interpretations.

It is our view that a number of additional exemptions must be included to limit potential wholesale damage to the market and to provide for a more pragmatic implementation of the proposed code changes. These additions include:

3. A rebid is required as a result of an unexpected or reasonably anticipated interregional transmission constraint that becomes evident within the 3 hour window.
4. Ancillary Services Providers to be able to rebid within the 3-hour window to manage ancillary service co-optimised dispatch constraints.



If you have any inquiries on this submission then please contact Mr Kevin Ly, Manager Strategy & Market Development on (02) 9244 3862.



## Southern Hydro

28 August 2001

Mr Greg Thorpe  
NECA  
Level 5 41 Currie Street  
Adelaide SA 5000

Dear Greg,

### **Rebidding**

Thank you for the opportunity to comment on the draft Code Changes on Rebidding.

As stated in previous submissions on this topic, Southern Hydro believes that rebidding is a competitive and dynamic process that, overall, leads to more efficient market outcomes and lower pool prices and is essential for the efficient and effective operation of the market. The NEM is a real time market and as such relies on real time responses to the price signals seen in the Spot Price. The market was designed with a dispatch algorithm that required participants to manage such issues as plant commitment, the optimisation of energy constrained resources, and the management of plant capacity changes. Fundamental to this was the availability of re-bidding within the market design.

Southern Hydro fully supports the NGF submission and believes that such devices as limiting re-bidding are likely to have unintended outcomes.

However if the Code Change Panel is to recommend implementing such changes to the Code, Southern Hydro believes there are a number of changes that must be made to the proposal to enable energy constrained plant such as ours to operate in an optimum manner and deliver all its potential benefits to the market. Rebidding is an essential tool in enabling energy constrained plant to maximise the value of our limited natural resource, and provide the maximum benefit to consumers.

Traditionally the central controllers of a vertically integrated utility optimised the use of energy constrained plant to maximise its value and maintain system security. They endeavoured to dispatch such plant at times of maximum system load or at times of minimum system reserve. The controllers knew that hydro plant has a requirement to run for a certain period on most days, but can not run continuously. The water was run at times when it was of most value to the market, reducing or eliminating the need to run expensive open cycle gas turbines.

This task of managing the limited energy supplies for hydro (and other energy constrained plant) has now been devolved to the plant owner and the only tool available to optimise this usage is through bidding and rebidding. Any Code change that limits a participant's ability

to manage its limited resources is going to lead to sub-optimal use of this energy and will not maximise its value to consumers.

### **Technical / Fuel issues**

Optimisation of energy constrained plant relates to both physical/technical optimisation and to financial optimisation.

Most of the technical issues that constrain hydro generators relate to the level of flow in the river. We are restricted in both the amount that is allowed to be discharged into the river at any time (both minimum and maximum releases) and the rate at which we can change the flow in the river. These constraints on our operation are placed on Southern Hydro by outside agencies such as the water authorities (Murray Goulbourn Water and the Murray Darling Basin Commission) who control the rivers and by the Environmental Protection Authority. Southern Hydro is required to assist in the management of river health both at times of riparian flow and during irrigation releases. For most of our schemes a regulation pond controls the final release into the river allowing some flexibility in our operation, but the small finite size of a regulation pond is itself a constraint.

Southern Hydro endeavours at all times to ensure that releases from our dams are through our power stations. This ensures that maximum value is extracted from all water released. Southern Hydro is very conscious of the impacts of greenhouse gases on the world environment and through careful use of our water attempts to lower the use of fossil fuel fired generators.

Uncontrolled releases through spillways and relief valves are also likely to be damaging to the river environment causing erosion and damage to bridges and other structures close to the river.

Southern Hydro always attempts to manage the flows in our rivers while giving the market timely information about our intentions. However it is not uncommon for us to have a requirement to re-bid our generation with very short notice to ensure that the water is used in a controlled manner that optimises both its value and its impact on the environment:

#### **Storms (or the threat of Storms)**

A storm in the catchment area, or even the reasonable expectation of a storm arriving within the next few hours can require immediate action from our operators to manage river flows and dam levels.

Depending on the initial situation we may be required to increase running from some power stations to avoid spilling the dam, or alternately we may be required to reduce running from a power station in order to leave space in a downstream dam for the water from the storm.

#### **Plant Failure**

The failure of a generator in one of our power stations may at times require changes not only to the output of that unit, but also to other units at the same station or even to generation units at other stations within the same scheme.

We have a requirement to maintain irrigation and/or riparian flows and so, unless the valuable natural resource is going to be wasted by spilling dams, we need the ability to divert generation from one unit to another at times of failure.

### **Requests from outside Regulators**

At times Southern Hydro receives requests from outside agencies to quickly change the flow in a river. One example of this would be a request from the Police or the SES to reduce flow to enable search and rescue personnel to safely perform their difficult tasks. Southern Hydro must be permitted to rebid to obey such requests.

### **Contingency Ancillary Services Calls**

Should a system event occur that causes a sudden drop in system frequency, any plant enabled for a contingency raise ancillary service will be required to generate regardless of the regional reference price. Following such an event, energy constrained plant would need to have the ability to re-bid its remaining energy so as to manage its water resources and dam and river levels. This re-bid may be needed in a very short time frame.

### **Maintenance**

Much of Southern Hydro's plant has a very low capacity factor, meaning that it only runs for a small number of hours in a year. However, as we endeavour to run it at times when it is of maximum benefit to the market, it is never certain when this will be. To ensure that the plant is available when needed we have negotiated maintenance arrangements such that, wherever possible, plant that is out of service on short term maintenance is able to be recalled with short recall times, usually one or two hours.

Should the rebidding rules be changed as proposed, we would not be able to rebid such plant as available for a period of three hours. Our flexible maintenance procedures would be lost to the market, and consumers would suffer from higher costs and reduced system security.

### **Forecasting / Pricing Issues**

Despite NEMMCO's best efforts the forecast price for a region can change significantly with the three hour limit imposed by these proposed Code changes.

### **Demand Driven**

The demand for electricity in Australia is strongly driven by the prevailing weather. The ability for the Bureau of Meteorology to forecast the exact timing of changes to the weather in South East Australia is limited. Unfortunately this combines to make the task of predicting system demand difficult.

As an example, the exact timing of the arrival at a capital city of a cool change can have enormous impacts on system demand and hence on pricing. It is not uncommon for such a change to be predicted to coincide with say the evening demand peak. Should the change be delayed by an hour or so the evening peak could be much larger than expected and last for a lot longer. In the period leading up to the peak NEMMCO will regularly update its forecasts, but if plant is banned from re-bidding within three hours of dispatch, energy constrained, peaking plant that would normally respond to these changes will not be able to respond.

## **Supply Driven**

Much of the short term price variation seen in the market is driven by changes to the performance of other plant on the system:

- Failure of generation plant;
- Return to service of generation plant;
- Network outages or restrictions; or
- Network elements returning to full service.

Such events are unpredictable and occur with very short notice. Plant such as Southern Hydro's have traditionally responded to manage the system and maintain system security. Restrictions on the ability of flexible plant to re-bid will reduce our ability to optimally use our limited resources to maximise the value of spot market trading.

## **Contractual**

Southern Hydro provides a number of valuable contract types to the market to enable participants to manage their exposure to the spot market. Fundamental to our ability to offer these products at the best price for the market is our ability to respond to market signals and generate at times of highest price.

While the current proposals allow for re-bidding for dispatch pursuant to binding contracts not otherwise able to be previously specified in a dispatch bid, there are also financial contracts that must be managed, some of which are not known until close to the event.

If these cannot be actively managed by rebidding in response to market changes which may occur close to dispatch, a significantly increased risk premium must be added to the product.

## ***Possible Consequences of a Limit on Rebidding***

As discussed above re-bidding is essential for the optimal management of energy constrained plant in the energy only NEM electricity market. An artificial limit on the timing of re-bidding will lead to:

- Waste of natural resources, as more is likely to be spilt from hydro power stations
- Increased greenhouse gas emissions due to the energy wasted in water spills and the increased need to use old and inefficient thermal plant at times of energy shortage
- Higher average energy prices as energy constrained plant can no longer optimise its output to ensure that it comes on to cap spot prices
- Increased ancillary services costs as more FCAS is needed to manage the system at times when plant can not respond to the market signals
- System security reduced as energy constrained plant runs out of energy prior to the critical time and other plant is unable to re-bid to make itself available
- Increased reliance on System Security Directions needed by NEMMCO to manage plant that is unable to respond to signals

- Higher contract prices as generators add an additional risk premium to account for their inability to re-bid to be dispatched when required
- Reduction in quantity of hedges offered as generators take a lower risk profile to account for their inability to re-bid to be dispatched when required
- Reduced incentive on DSM to participate in market as the three hour limit would impact on demand side bids in the market, while demand side response outside the market would not face the same restriction.

### **Summary**

The proposal to place a three hour limit on re-bidding except for certain limited physical/technical issues seriously impacts on the ability of energy constrained plant such as Southern Hydros' to optimise its production for the benefit of all stakeholders.

This optimisation relates to both physical/technical and financial optimisation of the output of our plant.

Any limits on the ability of energy constrained plant to optimise its output will lead to higher prices, reduced system security and limitations on the availability of derivatives contracts.

Should the Code change Panel firmly believe that something must be done and so endorse the need for Code Changes put to them by NECA, a number of amendments are needed to the draft Code Changes to minimise their impact on our ability to run our plant at the times when it is most needed. The proposed changes are marked up on the attachment to this letter.

If you have any further questions on the issues raised here please contact Mr Rob Jackson, Manager Market Development and Regulation; phone (03) 9616 1011; fax (03) 9616 1029.

Simon Maher  
CEO Southern Hydro

ATTACHMENT

**PROPOSED REBIDDING CODE CHANGES - AMENDED**

The following is Clause 3.8.22(b1) as proposed by NECA, marked up in red to show the amendments that Southern Hydro believes are required should the Code Change Panel decide that such a clause is appropriate.

- (b1) A Market Participant may not vary its available capacity previously submitted to NEMMCO in a dispatch bid, network dispatch offer, dispatch offer, or rebid in relation to a trading interval at any time after the sixth trading interval prior to that trading interval unless:
- (1) the *rebid* is required as a direct result of a mechanical breakdown, electrical breakdown or failure of equipment or the return from service following a maintenance outage, mechanical breakdown, electrical breakdown or failure of equipment that occurs after the sixth *trading interval* prior to *dispatch* and which consequently changes the capacity of:
    - (i) the *generating unit* to generate or *supply* a quantity of *energy* previously specified in a *dispatch offer* or *rebid*;
    - (ii) the *scheduled network service* to transfer a quantity of *energy* previously specified in a *network dispatch offer* or *rebid*; or
    - (iii) the *scheduled load* to consume a quantity of *energy* previously specified in a *dispatch bid* or *rebid*.
  - (2) the *rebid* is required as a direct result of a reduction in, increase in or change in the nature of, ~~fuel~~ primary energy supply to the *generating unit* or a expectation of a future reduction in, increase in, or change in the nature of, primary energy supply to the generating unit, that occurs after the sixth *trading interval* prior to *dispatch*;
  - (3) the *rebid* is of any part of capacity of a *scheduled unit*, *scheduled network service*, or *scheduled load* not *scheduled* for *dispatch* which is required to be *dispatched* pursuant to the terms of binding agreements not otherwise able to be previously specified in a *dispatch bid*, *network dispatch offer*, *dispatch offer*, or *rebid*;
  - (4) the *rebid* is required to ensure the *scheduled unit*, *scheduled network service*, or *scheduled load* is operated in accordance with *good electricity industry practice* at the time of the *rebid* that otherwise would not occur if the *scheduled unit*, *scheduled network service*, or *scheduled load* was operated in accordance with the current *pre-dispatch schedule* and other *market* information, not otherwise able to be previously specified in a *dispatch bid*, *network dispatch offer*, *dispatch offer*, or *rebid*;
  - (5) the *Market Participant*:

- (i) is operating its *scheduled generating unit* outside its *enablement limits*; and
- (ii) has received a notice from *NEMMCO* in accordance with clause 3.8.20(k) or clause 3.8.21(m), and the *rebid*:
- (iii) is made by the *Market Participant* as soon as reasonably after receiving the notice from *NEMMCO* under clause 3.8.20(k) or clause 3.8.21(m); and
- (iv) is for the minimum volume necessary to bring the *Market Participant's scheduled generating unit* within the *enablement limits*; or
- (6) the *rebid* is required in order to comply with a *direction* from *NEMMCO* and is submitted as soon as reasonably practicable following the direction from *NEMMCO*;
- (7) the *rebid* is required by an *energy constrained scheduled generating unit* or an *energy constrained scheduled load* to optimize the use of this energy in such a manner as to, based on an assessment of all the information available to the *participant* at the time, better maximise the value of *spot market* trading both within the day and across days;
- (8) the *rebid* is required to ensure the participant can manage contract positions exposed by five minute dispatch, thirty minute settlement anomaly;
- (9) the *rebid* is required in order to comply with instruction or requests from another regulating authority and is submitted as soon as reasonably practicable following the direction from that regulating authority;
- (10) the *rebid* is required on a *scheduled unit, scheduled network service, or scheduled load* as a direct result of the impact of any of the items listed in this clause 3.8.22(b1) impacting on any other another *scheduled unit, scheduled network service, or scheduled load* owned or operated by the *Participant*..



**Greg Thorpe**

**From:** BLEDSOE Erin [EBLEDSOE@stanwell.com]  
**Sent:** Tuesday, 28 August 2001 3:02 PM  
**To:** gthorpe@neca.com.au  
**Cc:** electricity.group@acc.gov.au  
**Subject:** Stanwell's response to NECA's proposed rebidding Code changes  
Trading Division

28 August 2001

Mr Stephen Kelly

National Electricity Code Administrator (NECA)

Level 5

41 Currie Street

ADELAIDE SA 5000

Email [gthorpe@neca.com.au](mailto:gthorpe@neca.com.au) <<mailto:gthorpe@neca.com.au>>

Attention: Mr Greg Thorpe

Dear Mr Kelly

**Comments on the Proposed Changes to Rebidding**

Stanwell Corporation Limited (SCL) welcomes this opportunity to provide comments on the proposed draft National Electricity Code (the Code) changes that relate to rebidding. On 13 March, SCL submitted a response to NECA on its draft report entitled 'Bidding and Rebidding Strategies and their Effect on Prices'. SCL's response stated that the five proposals presented were unacceptable from a whole of market perspective. Following the release of NECA's final report and the subsequent draft Code amendments, SCL supports the changes that improve the surveillance, monitoring and enforcement provisions in the Code. However, we have not revised our position in relation to rebidding.

In actual fact, SCL wishes to express deep regret and reservation in relation to the proposed three-hour prohibition on rebidding. In particular we believe that the proposal has the potential to:

- raise the average spot price in the National Electricity Market (NEM);
- result in increased and unnecessary load-shedding; and
- distort new investment signals for peaking plant.

In addition, SCL's earlier response recognised that customers in some jurisdictions, namely South Australia (SA), are currently subject to higher electricity prices relative to customers in other NEM jurisdictions. However, we consider that such prices provide *transparent* signals necessary to promote efficient generation investment and any intervention or restriction will only distort this process. As a result, we were particularly, disappointed to learn of the Media Release issued by the SA Treasurer on 6 August entitled 'Olsen Success in Electricity Market Rule Changes'. This release indicates that that the Code change process might be subject to political influence.

Following from this SCL believes that it is essential for the effective operation of the NEM for NECA to be considered an independent body promoting changes which will result in NEM-wide benefits.

Turning to the issue at hand, we understand that NECA has notified the Australian Competition and Consumer Commission (the Commission) of its intention to seek authorisation for the rebidding Code changes. We believe this indicates that NECA is now unwilling to reconsider other options. Given this situation, SCL urges NECA to limit any proposed change to SA and introduce a sunset clause. We do not believe the current SA demand/supply imbalance provides sufficient reason to put at risk the benefits the NEM delivers to its customers.

Further to these comments, SCL wishes to indicate support for the position being presented by the National Generators Forum (NGF) in its submission on this issue.

SCL welcomes the work of NECA in developing an efficient market for electricity.

However, we cannot support changes that only provide short-run benefits in one jurisdiction and net negative outcomes for the NEM as a whole. As a result, we look forward to learning of the Commission's response on this issue.

Yours faithfully

Tony Stone

Spot Market Manager

Enquiries: Erin Bledsoe

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header.htm



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28 August 2001

Greg Thorpe  
NECA  
Level 5, 41 Currie Street  
Adelaide  
SA 5000

Dear Mr Thorpe

Please find enclosed Synergen Power Pty Ltd's submission to NECA, regarding the proposed Code changes to bidding and rebidding. (You should already have received a copy of this document via e-mail.)

If you require any clarification to the points raised in this paper, please feel free to contact Mike Downey (on 03 9617 8406) or myself (on 03 9617 8485).

Yours sincerely

**Chris Smyth**  
Market Operations Trader  
ANP Trader



**Australian National Power**

**Synergen Power Pty Ltd**

**Submission To Proposed Code Changes Regarding Generator Bidding  
And Rebidding In The National Electricity Market**

28 August 2001

Synergen welcomes the opportunity to comment on the National Electricity Market (NEM) code changes proposed by NECA, concerning bidding and rebidding. Although we understand the sentiment behind the proposals, in our view the proposals violate the key market principle of non-discrimination by having a disproportionately adverse effect on a peaking generator such as Synergen. It is our contention that the proposals will damage the efficiency of the NEM, deter new investment and ultimately reduce reliability of electricity supply.

**Background**

Synergen Power Pty Ltd ("Synergen") owns and operates four peaking power stations, comprising nine generating units, in the South Australian region.

<b>Station</b>	<b>Number of units</b>	<b>Fuel source</b>	<b>Synchronisation time (minutes)</b>	<b>Winter capacity*</b>
Dry Creek	3	Gas	~5	152 MW
Mintaro	1	Gas	~20	90 MW
Snuggery	3	Distillate	~1 (from synchronous compensation)	63 MW
Port Lincoln	2	Distillate	~11	50 MW
<b>TOTAL</b>	<b>9</b>			<b>355 MW</b>

\*Capacity is inversely related to ambient temperature; hence Synergen's capacity is lower in summer

In the absence of hydro generation in South Australia, Snuggery and Dry Creek in particular represent the fastest-response generators in the region. Overall, Synergen is the "generator of last resort" in South Australia.

These units all have very high running costs, which means Synergen is reluctant to commit them to market unless:

- (a) We are confident we are experiencing *extremely* high pool prices for a short period of time (i.e. many thousands of dollars);

or,

- (b) If prices are high, but not in excess of "many hundreds" we are confident that the period of high pool prices will last for more than one or two trading intervals.

Because these conditions arise rarely, Synergen units are idle for approximately 90 per cent of the time. When our units are committed to market, they generally have the effect of suppressing prices, often diminishing the very circumstances that led to

their commitment in the first place. Hence, run times tend to be short, meaning we only have limited time to recover our generation costs from pool revenue.

Synergen's key revenue earning capacity comes from its ability to sell insurance products in the contract market. Counterparties (retailers in particular) value Synergen's ability to respond rapidly to market events – and its ability in many cases to cap high pool prices. Accordingly, counterparties are prepared to pay Synergen option fees for cap products that assume a portion of their market risk. If the effect of NECA's proposed rebid changes is to impair our ability to manage that risk, it is likely to lead to increases pool prices and/or a reduction the quality of the risk management products we are able to make available to retailers and other counterparties.

Because the NEM is an energy-only market (i.e. generators are not paid for capacity, as in other energy markets), the only means of earning revenue open to Synergen are via the pool and contract markets. These are interdependent: if Synergen cannot function effectively in the spot market, its effectiveness in the contract market is also diminished.

### **Why rebidding is important to Synergen**

As indicated above, peaking generators such as Synergen rely on the ability to respond rapidly to unfolding and frequently unpredictable market events. The ability to rebid is important for maintaining our business's viability.

Synergen's units are characteristic of the high-cost peaking plant tranche. For this type of plant, start-up costs are typically much greater than their (high) steady-state running costs, due to the cost of fuel and the severe life usage cost of starts. This means that the genuine "marginal cost" is variable, depending on the commitment cycle.

In other words, because the "marginal cost" per megawatt-hour generated for a thirty-minute run (e.g. in response to a ten-minute price spike to VoLL) is much greater than the marginal cost of a run of several hours (e.g. to respond to pool prices of several hundred dollars resulting from a plant failure in the region), we cannot sensibly determine a "running cost" to offer the units at.

Synergen, as fast-start plant, is dispatched to the NEM via the "Fast Start Inflexible Profile", which issues a commitment signal whenever the price reaches the price we are bid at, regardless of whether the projected run is economic. We currently manage this by rebidding: by "stopping the commitment cycle" if the start would be uneconomic.

#### **Rebidding capacity to lower-priced bands:**

This is an essential capability for a peaking unit. Synergen's general bidding pattern is to both cover our contract position and to offer uncontracted capacity at a price that will contribute to the unit's running costs. As circumstances unfold, volume is then rebid to ensure dispatch so we can ensure we are generating to cover our contract position. Without this capability, there is a real likelihood that a peaking unit will be unable to ensure its dispatch when spot prices sit at intermediate levels where dispatch would be uncertain.

#### **Rebidding capacity to higher-priced bands:**

The ability to rebid capacity to higher-priced bands is important to prevent Synergen from over-reacting to small-scale events. For example, a unit with

capacity offered at \$180/MWh to cover a contract position will be dispatched if there is a short-duration small-scale price “spike” of, say, only \$200/MWh.

Very short-term price spikes, even small ones, are the market mechanism for signaling an energy shortage, and it is a peaking generator’s role to respond to these signals. If, however, such a generator simply cannot respond in time to resolve a *momentary* energy shortage there is no physical reason why it needs to be started. Therefore, the appropriate course of action is to rebid the unit to prevent the start.

If the market indications are that a small-scale price “spike” is likely to last for only five or ten minutes, then the unit needs to be immediately decommitted by bidding the unit unavailable at short notice. If we do not do this, the unit will undergo a start-up sequence and begin generating at a market price well below the cost of committing the unit – and below the contract price as well. Repeated actions of this nature will erode the financial viability of a peaking unit, and create a significant barrier to future investment in peaking generation.

From the point of view of system security, we should note that some Synergen gas turbines are only capable of sustaining a limited number of starts per day. For Synergen to maintain its position as the generator of last resort, we must avoid unnecessary start-ups.

#### **Response to NECA’s proposed code changes**

Synergen realises there is public concern, especially in South Australia, at developments in the NEM, but we also urge caution in introducing code changes without fully understanding their effects. If changes are introduced without a full analysis of their likely effect, it is likely they will have unintended and adverse consequences – and may end up exacerbating the “problem” they are intended to solve.

Addressing each of the proposed code changes in turn:

#### **A requirement for generators’ initial offers and rebids to represent their genuine intentions at the time they are made**

Synergen concurs with the intent of this provision. However, we believe this proposed change, as it has been expressed to date, is too simplistic.

Synergen, as a peaking generator, expresses its “genuine intentions” at the time of submitting NEM bids or rebids. However, it is very important for us to be able to reassess the situation when the SPD software initiates a commit signal, to ensure the commitment of our units will be economically viable. As described previously, our decision to generate at a particular price depends on our judgement of how long that price is likely to last.

So, for example, even if we have submitted a bid to generate at \$180/MWh it cannot be inferred that we “genuinely intend” to start that unit every time the price reaches that level and we receive a commitment signal. The “intention” is valid for sustained operation, but cannot be inferred for short commitment cycles. Continuing this example, if the price “spikes” to \$200 for only ten minutes our prudent course of action would be to rebid the unit as unavailable. Assessing the likely duration of high-price events frequently requires rapid analysis and judgement on the part of our traders.



We strongly disagree with the provisions of NECA's proposed new code clause 3.8.22(A), which places the onus of proof onto generators to show that all bids and rebids represent their genuine intention at the time the offer was made. On extreme days, when the presence of a peaking generating unit is most crucial for maintaining system security, such a generator is likely to make literally dozens of rebids as the situation unfolds. Particularly in South Australia, rebids are made through discussion and rapid analysis. It would be very onerous to require us to have to revisit all such rebids long after the event, and the added time required to manage the quality assurance process necessary to support the reverse onus of proof may well compromise South Australian system security.

**Further strengthening information disclosure obligations surrounding rebidding to ensure the reasons for rebids are authorised at an appropriately senior level**

Synergen takes its trading function very seriously. For our own internal risk management, we have carefully documented policies and procedures in place to ensure that only suitably authorised personnel are in a position to lodge offers and rebids. We do not regard NECA or the Code as having a role in determination of generators' risk policies.

**Increasing flexibility in the treatment of short-term loading constraints consistent with maintaining system security, and allowing NEMMCO to contract for a wider range of network ancillary services, in order to remove short-term price spikes**

Synergen would welcome efforts to eliminate any price spikes that have no real basis in maintaining system security. However, we are concerned at any suggestion that NEMMCO have undue discretion in implementing short-term loading constraints; this would introduce an unacceptable level of subjectivity in management of system security – and ultimately price determination.

Furthermore, by creating incentives for generators to shift energy to the Ancillary Services market, NECA's proposals are potentially distorting both the energy and Ancillary Services markets.

**Prohibiting rebidding, except for essential physical reasons connected with the operation of the plant, within three hours of dispatch**

Synergen is strongly opposed to this provision. As explained above, the ability to rapidly rebid plant is crucial to the operation of peaking generators. Hence, we believe the implementation of this change will compromise the viability of peakers, which in turn will reduce incentives for future investment in such plant. In the long run, this will raise the cost or limit the availability of risk-management products for other participants – which will have a detrimental effect on overall system reliability and risk mitigation.

Furthermore, because the proposed code changes are specifically targeted at generators' very short-term interaction with the market, they will affect the viability of those generators who rely on short-term interaction the greatest. That is: peakers. Consequently, the proposed changes violate the key market principle of non-discrimination on the grounds of technology.

In our view:

- The onus of proof is on NECA to demonstrate the need for such a drastic change to the market rules;
- NECA has not adequately demonstrated that there is a market flaw or a "problem" that needs to be solved;
- No detailed analysis of the effect of the code changes has been published which will justify the changes.

If indeed, there was a "problem" attributable to the current rebidding rules, the approach NECA has taken ("Ban all rebids, with some exceptions") is inappropriate and unwieldy, especially in the light of NECA's own admission that the vast majority of generator rebids are legitimate. By declining to state exactly what rebids it regards as unacceptable – and then proposing a specific ban on those – NECA is tacitly admitting the weakness of its own assertion of there being a "problem".

We are sceptical of NECA's assertion that a list can be devised in advance that will exhaustively cover all circumstances where a rebid might (in NECA's words) "legitimately" be submitted. Given the dynamic and complex nature of the National Electricity Market, we believe there will always be circumstances where a "legitimate" rebid should be made that the Code has not anticipated. Consequently, the list of exemptions will grow ever longer and will need to be continually revised as new circumstances arise.

We concur with the National Generators' Forum introductory response to this proposal (presented at the NECA forum to discuss this code change on August 14).

Although NECA has proposed a prohibition on short-term rebidding, we note that there is no corresponding proposal to curtail short-term demand-side management. We regard this as unfair. Participants who can rapidly shed load can essentially compete with us, and it is discriminatory to limit our flexibility without imposing similar constraints on them.

#### **Proposed exemptions to the rebid prohibition**

NECA are proposing to allow exemptions to the rebid prohibition in the following circumstances:

- (1) *"(If) the rebid is required as a direct result of a mechanical breakdown, electrical breakdown or failure of equipment that occurs after the sixth trading interval prior to dispatch and which consequently changes the capacity of:*
- (i) the generating unit to generate or supply a quantity of energy previously specified in a dispatch offer or rebid;*
  - (ii) the scheduled network service to transfer a quantity of energy previously specified in a network dispatch offer or rebid, or;*
  - (iii) the scheduled load to consume a quantity of energy previously specified in a dispatch bid or rebid."*

#### Comment

This provision does not mention the rebidding of plant back in once repairs have been completed. An unintended consequence of this omission could be the degradation of short-term PASA data. The duration and extent of short-term unplanned outages are generally not

known until the outage is finished. To avoid an unnecessary three-hour wait, generators will then be required to rebid the failed plant's quantity out of the market in accordance with this provision every thirty minutes.

Nor does this provision allow for portfolio management of an outage. For example, we have three units at Dry Creek. If, while generating with two of the units, we suffer an unplanned outage on one of them one obvious course of action would be for us to start the third Dry Creek unit, or a unit at one of our other stations. However, as this proposal currently stands, we would be prevented from doing this.

We note with concern that if this scenario occurred at a time of high prices, this proposed code change will give a generator an incentive to non-conform, by simply generating anyway – thus receiving the pool price. Obviously, behaviour like this would have extremely serious implications for system stability.

- (2) *"(If) the rebid is required as a direct result of a reduction in, or change in the nature of, fuel supply to the generating unit that occurs after the sixth trading interval prior to dispatch;"*

Comment

Clearly this provision is applicable to Synergen's gas-fired units. We are frequently energy constrained, particularly in summer when gas availability is reduced. Typically, such curtailments occur simultaneously with peak electricity demand. Rebidding is crucial to enable us to manage fuel constraints.

However, this proposal does not recognise the key role played by portfolio management in situations of energy limitation, or even potential energy limitation.

- (3) *"(If) the rebid is the part of capacity of a scheduled unit, scheduled network service, or scheduled load not scheduled for dispatch which is required to be dispatched pursuant to the terms of binding agreements not otherwise able to be previously specified in a dispatch bid, network dispatch offer, dispatch offer, or rebid;"*

Comment

Synergen views this provision with deep concern. By virtue of our nature as a peaking generator, it is common in times of a tight supply-demand balance for other market participants to want to contract with us on a short-term basis with little notice.

These are typically financial contracts. Hence we are not contractually obliged to generate against them – merely to provide the financial cover to our counterparties. However, unless we can generate, there is no point in us contracting, thus cutting off a key revenue source for us and eliminating a source of risk management for our counterparties.

Furthermore, we regard these contracts as being commercial-in-confidence and are reluctant to divulge their provisions to a third party such as NECA. Such disclosure would be required under NECA's

proposal to regard all rebids as not being based upon reasonable grounds unless evidence is supplied to the contrary.

Short-term contracting like this is an important part of Synergen's operations; more so, we suspect, than to other generators, such as base-loaders. We see this proposed provision as having a disproportionate effect on Synergen relative to other generators and hence we believe it is in violation of the fundamental market principle of technology non-discrimination.

Furthermore, this is likely to be detrimental from the point of view of other market participants. If confidentiality cannot be assured, we may be disinclined to enter into short-term contracts on the same terms as have existed previously.

- (4) *"(If) the rebid is required to ensure the scheduled unit, scheduled network service, or scheduled load is operated in accordance with good electricity industry practice at the time of the rebid that otherwise would not occur if the scheduled unit, scheduled network service, or scheduled load was operated in accordance with the current pre-dispatch schedule and other market information, not otherwise able to be previously specified in a dispatch bid, network dispatch offer, dispatch offer, or rebid;"*
- (5) *"(If) the Market Participant*
- (i) is operating its scheduled generating unit outside its enablement limits; and*
  - (ii) has received a notice from NEMMCO in accordance with clause 3.8.20(k) or clause 3.8.21(m),*  
*and the rebid:*
  - (iii) is made by the Market Participant as soon as reasonably after receiving the notice from NEMMCO under clause 3.8.20(k) or clause 3.8.21(m); and*
  - (iv) is for the minimum volume necessary to bring the Market Participant's scheduling unit within the enablement limits."*
- (6) *"(If) the rebid is required in order to comply with a direction from NEMMCO and is submitted as soon as reasonably practicable following the direction from NEMMCO."*

Comment

These three provisions are all, on the face of it, prudent and sensible reasons for permitting a rebid.

### **Summary**

Rebidding is an essential part of Australia's chosen energy-only wholesale market model, where market efficiency demands real-time response to changes in the physical market. In particular, rebidding is of great importance to peaking generators such as Synergen. Curtailing the ability of peakers to respond to rapidly changing market conditions will inevitably diminish the value of such generators and the effectiveness of the NEM. This reduces incentives for future investment and hence will compromise the longer-term security and reliability of electricity supply.

Even a limited rebid prohibition (say, for three hours prior to dispatch time) would severely restrict peakers' ability to respond to price spikes. Preventing peakers from bidding volume down may prolong and exacerbate price spikes when they occur - thus having the opposite effect to that intended by the framers of the proposed Code changes.

We have given a number of examples of rebids that we regard as wholly legitimate for sensible operation of peaking and energy-limited plant in the NEM. According to the letter of NECA's proposed code changes, these rebids would be prohibited or - at the very least - would be the subject of contention and review.

Synergen's view is that NECA's proposed system of "all rebids prohibited but with specified exemptions" will lead to constant review and revision as new circumstances where rebids are "legitimate" come to light. We believe that generators and the regulator will find themselves in frequent value-subtracting and inefficient dispute as additions, alterations and changes are made to an increasingly cumbersome regulatory framework.

For this reason, we reiterate our view that if NECA has indeed identified a problem with the current code regarding bids and rebids, it would be far more intellectually rigorous to specify the problem, and then identify and prohibit the generator behaviour it is attempting to curtail.

Synergen extends an offer to work with NECA and other market participants to develop changes that can alleviate potential threats to the integrity of the market, but which do not have the detrimental effects of the proposed rebid prohibitions.

**Dan Foster**  
Energy Trading Manager  
ANP Energy



Ref:

28/08/2001

Mr Greg Thorpe  
NECA Ltd  
Level 5  
41 Currie St  
Adelaide SA 5000

Dear Greg

**PROPOSED REBIDDING CODE CHANGES**

Please find attached the Tarong Energy submission to the Code Change Panel in respect of the above proposed Code changes.

Yours sincerely

Greg Hesse  
MANAGER MARKET OPERATIONS AND REGULATION

Encl

Enquiries:

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## 1. Executive Summary

Tarong Energy Corporation (TEC) is pleased to make the following submission to the Code Change Panel (CCP) in respect of the Proposed Rebidding Code Changes.

In summary

- TEC queries whether the protected provisions of the Code regarding a price competitive spot market for electricity prevent the proposed Code changes proceeding without the unanimous approval of the Ministers of all participating Jurisdictions.
- TEC believes the proposed changes will affect radical changes to fundamental market design principles and that changes to such fundamentals
  - Will induce considerable market uncertainty and sovereign / regulatory risk into the market; and
  - Such changes should not be considered without the input of all participating jurisdictions regardless of whether NECA has the power to implement these changes.
- The NECA Issues Paper clearly endorses the considerable and positive outcomes which the current market arrangements, including rebidding, have delivered to customers (including lower prices).
- TEC submits that NECA has not evidenced any detriment flowing from the conduct complained of in the NECA Issues Paper to warrant the proposed changes.
- TEC contends that the proposed changes do not, on balance, operate to improve the efficiency of the market and that the anti-competitive detriment of those changes outweighs any public benefit that is sought to be achieved.
- Moreover TEC fears that the proposed changes will have a number of unintended negative consequences, not the least of which are
  - The inclusion of an inflexible bidding risk premium into both contract market and spot market prices.
  - The removal or dampening of pure market signals to existing and future participants.
  - The suppression of innovation in the contract market.
  - The further removal of incentives for the development of transparent demand side responses.
  - Discrimination between baseload and fast start / energy limited plant.
  - Discrimination between scheduled and non-scheduled generators and loads.

## 2. Market Design Fundamentals

### 2.1. A Unique Market Dynamic

The fact that electricity cannot be stored in significant amounts makes the National Electricity Market (NEM) unique. The proper functioning of the NEM requires an instantaneous balancing of supply and demand that no other market shares. Real-time management of the supply side is essential as the demand side has less capacity to be managed. Instantaneous pricing, or as near to as possible, provides the signals required to balance the physical market as required and because of this the ability of all participants to respond in real-time is essential.

### 2.2. Protected Provisions

The Code provides that:

Under the provisions of the National Electricity Law, a provision of the Code which is classified as a protected provision may not be amended except with the unanimous approval of the Ministers of all participating jurisdictions (*NEC 1.1.3*).

### 2.3. Market Objectives, Code Objectives, NECA and NEMMCO

Clauses 1.3, 1.4, 1.5 and 1.6 of the *NEC* are protected provisions.

Relevantly, market design fundamentals which are contained in protected provisions include:

- the Market Objectives that:
  - the electricity market be competitive (*NEC 1.3(b)(1)*);
  - that new entrants should not be treated more or less favourably than existing participants (*NEC 1.3(b)(4)*); and
  - particular energy sources or technology should not be treated more or less favourably than others (*NEC 1.3(b)(5)*);
- The Code Objectives that:
  - the Code be a light-handed regulation of the market to achieve the Market Objectives (*NEC 1.4(b)(1)*); and
  - “in particular” that the Code provides for “detailed market rules including ... **spot price determination** ...” (*NEC 1.4(b)(6)(ii)*);
- NECA’s objective is to “**administer** the ongoing development of, and changes to, the Code” but this objective is tightly constrained by the fact that NECA’s warrant to develop the Code is limited to “the [achievement] of the market objectives” (*NEC 1.5.2(d)*) viz a competitive, level-playing-field, spot price market for the real-time demand, pricing and dispatch of evanescent electricity.
- NECA’s function is only to “manage changes to the Code” (*NEC 1.5.3(d)*), no more, no less.

The proposed changes to the rebidding rules corrupt the immediacy of the market and the relationship intended to exist between the evanescent commodity in question (unstorable electricity), real-time demand and the correlative real-time pricing implicit in the concept of a spot price.



The legislatures' intention regarding this is clear. If the legislatures' intention was otherwise than the concept of real-time pricing the term "spot price" would never have been employed. Real-time spot pricing cannot occur unless market participants are free to rebid in real-time in response to the real-time exigencies of supply and demand and commercial competitiveness.

As a protected provision any change to this market axiom (*NEC 1.4(b)(6)(ii)*) requires the unanimous approval of the Ministers of all participating jurisdictions.

The proposed changes to rebidding would allow certain market participants to rebid in accordance with the proposed exceptions to the three hour rule but the rest of the market would be prevented from competitively pricing against that rebid.

This would lead to the anomalous result that a generator who suffers a physical breakdown could, with the remainder of their portfolio, profit from the resulting supply shortage, but competitors to that generator who had not suffered a contemporaneous breakdown would be unable to respond for three hours, potentially the whole period of under-supply. Reliable generation should be applauded and encouraged not disadvantaged. Any such result is antithetical to the competitive market axiom (*NEC 1.3(b)(1)*) and as a protected provision would require the unanimous approval of the Ministers of all participating jurisdictions.

NECA is not, and should not be, a policy making organ. It has no such mandate. It certainly has no mandate for adventurism in the exercise of its powers regarding the "administration" and "management" of changes to the code. At best it has a surveillance and reporting function. That it has no such mandate is clearly recognised by NECA's *Statement of Corporate Intent for 2001/2002* in which NECA acknowledges that:

NECA can only fulfil [its] mission within the broader public policy framework which is properly the responsibility of our Member Governments and the Commonwealth to lay down ... We look forward to the focus the [Ministerial Council on Energy] and the [Energy and NEM Policy Forum] will provide for governments to play a fuller and more active role in shaping the objectives and future development of the market. We also look forward to taking an appropriate part in COAG's independent review of energy market directions. (*SCI p2*)

## **2.4. A Spot Market**

The Spot Market as it currently operates, facilitates real time decision making by participants to allow management of hedge contract positions against generation or retail positions.

The level of volatility in the spot market is a reflection of not only the natural supply and demand variables but also of the levels of hedge contracting as participants trade the uncontracted portion of their portfolio's on the spot market. Higher levels of contracting contribute to lower levels of volatility in the spot market as participants ensure their hedge positions are covered and thus have less desire for either lower prices or higher prices.

Price itself in the spot market is more a function of the supply/demand balance. Attempts to artificially 'fix' any perceived price and or volatility 'problems' in the spot market, in an arbitrary manner, will do nothing to change an inherent supply/demand characteristic at a given moment in time. Neither will it encourage greater levels of contracting by introducing increased levels of regulatory risk.

The policy boundaries established in the Code clearly identify what the upper and lower limits of spot price should be. Further they also provide for clearly defined cumulative limits beyond which price capping will be affected. Where price capping is introduced the policy requires that suppliers be compensated for lost market opportunities. The Code also clearly expects that where intervention is required at times of supply scarcity, such intervention can be priced at VoLL. Any constraints introduced that artificially limit price movements within these policy bounds would materially impact on the fundamental market design.

NECA has no Prices Surveillance Function except Reportage of Market Events. The Code provides that:

The ACCC will scrutinise market conduct by Code Participants through the provisions of the Trade Practices Act and will monitor prices, where necessary, through the Prices Surveillance Act 1983 (*NEC 1.2.1(c)*).

Though the price at a given time may reflect a short term imbalance in supply and demand, which in itself provides a signal for a particular market requirement, the average price across a period of time will more truly reflect the underlying supply/demand balance of the market in question. As such, appropriate market signals are supplied to existing and potential entrants on both the supply and demand side. It is essential to any open market attempting to deliver economic benefit, that these signals remain as undistorted as possible to allow both timely, adequate and appropriate investments to be made.

The concept of a spot price itself, in terms of this market, becomes an oxymoron if the proposed changes proceed in current form. To quote *The Language of Money* by Edna Carew, spot is "a financial term meaning 'now' or 'immediate'." In terms of the effect that a 3 hour restriction on rebidding implies to price, will the spot price really be a true spot price any more? What will happen is that unscheduled participants (principally loads) will continue to vary their position between the 3-hour cutoff and spot time. However, scheduled participants (principally generators) will be unable to respond to most changes after the 3-hour cutoff. Moreover, those participants who develop physical problems that require rebidding escape the 3-hour cutoff so that there is a persistent time mismatch between various parts of the market that doesn't occur at present. Arguably the resulting price will no longer be a true spot price as required by the Market Design Principles in clauses 3.1.4, 3.2.2 and 3.4 and especially the immediacy of time requirement in clause 3.9.1(a)(7).

## **2.5. An Energy Only Market Price**

The NEM is designed as an energy-only market where the energy price encapsulates a range of factors, both internal and external that impact on participants. These factors include, but are not limited to:

- Demand forecast errors, irrespective of cause
- Network constraints
- Price forecast errors
- Competitive conditions
- Sales position, (i.e. a significant number of retailers use generation plant as cost optimisation)
- Plant input cost variation (i.e. variations in cost and availability of gas, oil, coal and water))
- Inter-relationships with other markets (ancillary services, MNSP position, regions)
- Internal financial position, and
- Plant condition (Gross capability (major failures), intermediate estimates of capability ie. reducing loading on suspect plant like mills to reduce the short term prospect of failure and short term decisions by operators and engineers on issues like cycling)

To manage the impact of these many factors and to maximise allocative efficiency, participants use the rebidding provisions of the Code. If rebidding was to be restricted for any or all of these reasons the efficiency of the market would be damaged. Specific examples of how TEC manages these impacts through rebidding are included in Section 6 of this submission.

In particular, TEC draws the Panels' attention to clause 3.1.4 of the Code, which sets out the principles that underlie the market rules (ie Chapter 3 of the Code). TEC submits that the proposed changes offend a number of these principles, namely:

- It will require greater NEMMCO intervention and decision-making in the operation of the market
- It will reduce transparency and market efficiency
- It will introduce a special treatment of scheduled participants when compared to the existing position where the rebidding provisions allow scheduled participants (supply and demand) the same flexibility as non-scheduled participants (supply and demand).

In addition, clause 3.1.4(b) explicitly states a market design principle that the market rules are not intended to regulate anti-competitive behaviour.

TEC asks that the Panel address the question of how the proposed changes can avoid offending these market design principles.

### **3. Statutory Framework of the NEM, the NEL, the NEC and NECA**

The National Electricity Market (*NEM*) is created by complimentary state legislation including the *Electricity – National Scheme (Qld) Act 1997 (E-NS(Q)A)* a schedule to which is the *National Electricity Law (NEL)*.

The *National Electricity Code (NEC)* is a code of conduct approved initially by the Ministers of participating jurisdictions under s6(1) of the *NEL* and thereafter amended in accordance with the code change provisions of the *NEC* and the *NEL* (s3 *NEL*, "Code"). Amendments to the *NEC* need to be certified with a certificate to which the seal of NECA has been duly affixed (s6(4) *NEL*).

The *NEM* has mandatory and exclusive legal effect as, under fear of severe penalty, no person may engage in electricity generation, transmission, distribution or conveyance to customers (either wholesale or retail) unless they are registered as a Code Participant under the *NEC* and no person save for NECA and NEMMCO may administer or operate a competing market for the dispatch of electricity generating units or loads unless authorised to do so by the *NEC* (s9 *NEL*).

Being an instrument ("any document") made under, inter alia, the *E-NS(Q)A*, the *NEC* and any amendments to the *NEC* certified by the affixation of NECA's seal are both Statutory Instruments for the purposes of s7 of the *Statutory Instruments Act 1992 (Qld) (SIA)* (See also clauses 22 and 42 of the Schedule 1 to the *NEL*).

A Statutory Instrument such as the *NEC*, or a NECA-certified amendment to it, may not exceed the power conferred by the authorising law, in this case the *E-NS(Q)A* and the *NEL* (s 21 *SIA*). The *NEL* authorises NECA to certify amendments to the *NEC* but the statutory instruments by which NECA does this must be "required or permitted" by the authorising law or "necessary or convenient" to be prescribed for "carrying out or giving effect to the authorising law or other law" (s22 *SIA*).

Before exercising its power to promulgate amendments to a statutory instrument like the NEC, NECA should detail :

- how the authorising law requires or permits the proposed change, and
- why it is necessary or convenient to be changed to carry out or give effect to the authorising law or some, and if so which, other law;

and should clearly and precisely formulate the equivalent of a regulatory impact statement consistent with the best-practice guidelines appearing in s44 of the SIA including:

- the policy objectives of the proposed change and the reasons for them,
- the way the policy objectives will be achieved by the proposed change and why this way of achieving them is reasonable and appropriate,
- an explanation of how the proposed change is consistent with the policy objectives of the authorising law,
- if the change is inconsistent with the policy objectives of other legislation (eg the *National Competition Law*, the *Trade Practices Act*, the *Legislative Standards Act*, the *Judicial Review Act*), an explanation of the relationship with that legislation and the reasons for the inconsistency'
- identify any reasonable alternative way(s) of achieving the policy objectives (including the option of not making any change) and why such alternatives have been rejected;
- an assessment and quantification of the impacts, benefits and costs of implementing the proposed change and a comparison of the impacts, benefits and costs of all reasonable alternatives; and
- an assessment of the consistency of the proposed change with "fundamental legislative principles" and, if inconsistent with "fundamental legislative principles", the reasons for the inconsistency.

Although these guidelines are not strictly binding on NECA, they provide a persuasive analogue for the task being undertaken by NECA and should not be ignored by NECA.

"Fundamental legislative principles" are those principles referred to in s4 of the *Legislative Standards Act 1992 (Qld)* (LSA) and encapsulate the principles relating to the proper promulgation of rules having mandatory legal effect on the citizenry under threat of State-sanctioned criminal or civil penalty and these principles, in the words of the section, "underlie a parliamentary democracy based on the rule of law". Section 4(2) LSA provides that those principles include requiring mandatory legal rules to have "sufficient regard to the rights and liberties of individuals and the institution of Parliament".

Whether a mandatory legal rule has sufficient regards to the rights and liberties of individuals depends on whether the rule:

- makes rights and liberties or obligations dependant on administrative power only if the power is sufficiently defined and subject to appropriate review;
- is consistent with the rules of natural justice;
- allows the delegation of administrative power only in appropriate cases and to appropriate persons;
- does not reverse the onus of proof without adequate justification;
- provides appropriate protection against self-incrimination
- does not adversely affect rights and liberties or impose obligations retrospectively;
- provides for the compulsory acquisition of property only with fair compensation; and
- is unambiguously drafted in a sufficiently clear and precise way. (Refer s4(4) LSA)

Whether subordinate legislation has sufficient regard to the institution of Parliament depends on whether it:

- is within the power given by the authorising law which allows the subordinate legislation to be made,
- is consistent with the policy objectives of the authorising law,
- contains only matter appropriate to subordinate legislation, and
- amends statutory instruments only. (Refer s4(5) LSA)

When exercising its powers and discretions under the *NEL* and the *NEC*, *NECA* and the Code Change Panel (CCP) are subject to the *Judicial Review Act 1991 (Qld) (JRA)*. The exercise of *NECA*'s powers and discretions under a statutory instrument such as the *NEC* involves the making of decisions of an administrative kind under an "enactment" (which includes a statutory instrument such as the *NEC* according to s3 *JRA*) and these are reviewable decisions in accordance with s4 of the *JRA*.

The making of reports and recommendations prior to the making of decisions under the *NEL* or the *NEC* by *NECA* or the CCP are deemed by s 6 of the *JRA* to also be reviewable decisions for the purposes of the *JRA*.

Section 20 of the *JRA* gives an aggrieved person the right to apply to a court for a review of a decision and s21 gives a similar right of review in relation to conduct or proposed conduct engaged in for the purpose of making a decision and, pursuant to s8 of the Act, this includes the doing of anything preparatory to the making of a decision especially the taking of evidence and the holding of any inquiry or investigation.

The grounds for reviewing decisions or acts preparatory to the making of decisions under ss20 and 21 of the *JRA* are, *inter alia*, that:

- the decision-maker lacks jurisdiction;
- the decision is not authorised by the enactment under which it purports to be made;
- the making of the decision is an improper exercise of the power conferred by the enactment [s20(2)(e) and 21(2)(e)]; or
- there is no evidence or other material to justify the decision [s20(2)(h) and 21(2)(h)];

For the purposes of s20(2)(e) and 21(2)(e) an improper exercise of power includes, *inter alia*,

- exercising a discretionary power in accordance with a rule or policy without regard to the merits of a particular case;
- an exercise of a power that is so unreasonable that no reasonable person could so exercise the power; and
- an exercise of power in such a way that the result of the exercise of power is uncertain.

For the purposes of s20(2)(h) and 21(2)(h) a decision without justification will arise when there is no evidence or material from which the decision-maker could reasonably be satisfied that a required matter was established or the decision-maker bases their decision on a fact which does not exist (s24 *JRA*).

A decision-maker to whom the *JRA* applies must give written reasons for their decision upon request (s32 *JRA*).

In light of TEC's view that the proposed changes affect radical changes to fundamental market design principles including matters touching on the protected provisions of the Code, TEC submits that in terms of the *JRA NECA*

- lacks appropriate jurisdiction;
- is not authorised to make the changes;
- has not provided adequate evidence to justify the changes;
- is seeking to apply a rule or policy regardless of merits of the matter;
- could not reasonably recommend the proposed changes;
- has proposed changes that are sufficiently uncertain in their operation as to be an improper exercise of power; and
- has based the recommended changes upon the existence of facts which either do not exist or have not been shown cogently to exist.

#### **4. Proposed "Solutions" to the "Rebidding Problem"**

##### **4.1. Application of the TPA – s45, 46 & 47**

TEC disagrees with the conclusion reached in the Code Change Panel's July 2001 Report (at page 7) that bidding and rebidding conduct is:

"likely to be immune from action under section 46 as a result of the operation of section 46(6)"

TEC submits that there are two reasons why section 46 of the Trade Practices Act does apply to bidding and rebidding conduct by generators.

Firstly, section 46(6) of the Trade Practices Act removes the application of section 46 of the Act from conduct which would constitute a contravention of sections 45, 47 or 50 of the Act *but for* the operation of an authorisation which renders that conduct lawful for the purposes of the Trade Practices Act. To come within section 46(6) the conduct must contravene those sections of the Act. In other words, it must constitute:

- a general anti-competitive contract, arrangement or understanding;
- an exclusionary contract, arrangement or understanding;
- a price fixing contract, arrangement or understanding;
- exclusive dealing; or
- an anti-competitive acquisition of shares or assets.

The purpose of section 46(6) is to protect the operation of an authorisation of conduct of that type where that conduct *also* amounts a misuse of market power contrary to section 46. It does not legitimise conduct which is contrary to section 46 and which is not also in breach of one or more of sections 45, 47 and 50 of the Act. The bidding and rebidding conduct with which NECA is concerned is unilateral conduct. It does not involve any contracts, arrangements or understandings, exclusive dealing or acquisition of shares or assets. Consequently, section 46 of the Trade Practices Act is clearly applicable to that conduct in the appropriate circumstances.

The second reason that section 46(6) does not remove the application of section 46 of the Trade Practices Act from bidding and rebidding conduct is that an authorisation under the Trade Practices Act only authorises that conduct which the authorisation specifically permits. In the case of the authorisation granted by the ACCC in respect of the Code, the immunity only extends to the Code and conduct in accordance with the express terms of the Code.

In the context of the bidding and rebidding provisions of the Code, the authorisation has the effect that the act of bidding and rebidding in accordance with the Code is all that is authorised. If, in the course of bidding and rebidding, a generator engages in conduct which is not expressly and specifically required or permitted by the Code and which contravenes a provision of the Trade Practices Act, such as sections 45, 46, 47, 48 or 50, then the authorisation will not protect that conduct. If this were not the case, then the authorisation would permit a generator to enter into a price fixing arrangement with another generator in connection with bidding and rebidding. The reason that the authorisation does not protect this conduct is that it does *not* cover everything that is done in connection with action taken in accordance with the Code.

Consequently, section 46 of the Trade Practices Act does apply to bidding and rebidding conduct by generators and this method of regulation of this type of market conduct is open to enforcement by the ACCC.

TEC also notes that clause 3.1.4 of the Code expressly provides that:

"These market rules are not intended to regulate anti-competitive behaviour by Market Participants which, as in all other markets, is subject to the relevant provisions of the Trade Practices Act 1974 and the Competition Codes of participating jurisdictions."

#### **4.2. Incorporation of s52 and s51A of the TPA**

The proposed rebidding code changes appear to attempt to incorporate some aspects of sections 51A and 52 of the Trade Practices Act in the Code in relation to rebidding. The proposed new clause 3.8.22A provides, in effect, that a dispatch offer, bid or rebid must not be made unless the market participant has "reasonable grounds for believing" that the offer, bid or rebid "will not be varied by a subsequent rebid under clause 3.8.22".

TEC submits that this change to the Code is unnecessary and unworkable. The proposed clause 3.8.22A is unworkable because it cannot be complied with. A market participant may have reasonable grounds for believing that a bid is *not likely* to be varied by a subsequent rebid but could *not* have reasonable grounds for believing that a bid *will not* be varied as there is always a possibility that a bid will need to be varied due to an unforeseeable or unforeseen event. The proposed clause 3.8.22A would prevent a market participant from bidding unless they could predict that there would definitely not be any events which require rebidding.

This proposed change to the Code is unnecessary because sections 51A and 52 of the Trade Practices Act already apply to the conduct of market participants pursuant to the Code. TEC submits that these provisions are quite adequate in regulating the conduct in question and, in particular, have the benefit that they have been the subject of a substantial amount of judicial interpretation and application and so are less likely to give rise to confusion or ambiguity in what conduct is expected of market participants.

## **5. Flawed Economics**

### **5.1. Allocative Efficiency**

#### **5.1.1. Pumped Storage Plant**

The present provisional rebidding regime allows inter temporal optimisation of energy offers to the market.

With regards to pump storage generation plant, efficient delivery of energy to the market is contingent on maintaining the margin between revenue derived from peak generation and the cost of off peak pumping.

The price/demand forecast as signalled to participants is updated on a 30 minute cycle. Current rebidding arrangements allows participants to utilise updated information regarding off peak price/demand to optimise real time scheduling of generation. Specifically, changes to forecast price for pumping in up to 24 hours time will need to be reflected in the offer prices for generation that may be happening now.

The proposed rebidding restrictions will force generators to offer energy into the market based solely on day ahead forecasting. Whilst day ahead forecast is suitable for determining the general price/demand profile, it is sub optimal for effective pump storage plant dispatch. Market efficiency is best achieved by participants being able to manage these inter-temporal optimisations in real-time, without arbitrary time restrictions on their decision making.

Without the provision for real time optimisation the commercial risk associated with pump storage operation is increased. Clearly the level of risk, whether higher or lower, will be reflected in the level of returns required for participants to remain in the market.

#### **5.1.2. Coal Fired Plant**

Loading on a coal fired generation unit rises and falls due to market forces. Technical limitations determine that as unit loading varies it is, at times, necessary to place mills in and out of service. Commercial and unit stability considerations determine it is desirable to limit the number of mill cycles.

Utilising the 30 minute update of the price/demand forecast, participants are able to evaluate the impact of any signalled variations to forecast unit loading. Rebidding within a portfolio, on a real time basis may present to the market a similar commercial outcome whilst preventing excessive mill cycling. Without the rebidding provision, operations become more inflexible and the potentially higher operating costs resulting from potential mill cycling will need to be reflected in the primary offer.

Coal fired plant loading capacity will vary depending on ambient conditions, short term plant configuration and coal quality. The current provision for rebidding enables a generator to offer to the market short term increases in coal fired plant capacity during abnormal system conditions or as determined by improved plant conditions. In most cases this will not be possible to determine on a day ahead basis, and sometimes only in real time. The proposed code changes will severely limit the ability of all generators, peaking or base load, to provide short term capacity increases and the subsequent benefits to the market that occur.



## **5.2. Anti-competitive Effects**

### **5.2.1. Negation of Price Signals**

As noted above the principles to apply in the determination of spot market prices are set out in clause 3.9.1. In particular, clause 3.9.1(a)(7) provides that:

“Spot prices and dispatch prices provide Market Participants with signals as to the value of providing or cost of consuming electricity at a particular location at a particular time”

To be valid market signals, prices must be able to move fluidly in response to market forces and not be distorted by arbitrary regulation. There is a risk that in attempting to remove “unwarranted price spikes” the NECA proposals may remove the signals required by participants to respond to market events, and in the longer-term to delay investment decisions.

TEC submits that there is no warrant for the removal of, or damping of, existing price signals in the market which are within the policy boundaries set by the Jurisdictions.

### **5.2.2. Hurdle to Entry of new Peaking Plant**

Arguably the NECA proposals will limit the ability of participants to maintain flexible control over their plant during short-term market events. Given the peaky nature of demand in some areas of the NEM this may discourage the investment in new peaking plant required in those areas. Discouragement of new peaking plant through an attempt to limit price spikes in some way, is anti-competitive. Appropriate price signals have been given over the past year or more so as to give rise to numerous announcements of intention to install peaking plant in Victoria and South Australia. As these regions are very ‘peaky’ the existing open market has inspired the correct response to the signals given over recent volatile periods. As the market events which justify the investment in this plant are typically of short duration, proposals to remove the short-term flexibility of this plant will create a barrier to entry.

## **5.3. The Stifling of Market Innovation**

While the Code is properly limited to the operation of the physical market and does not concern itself directly with the secondary or derivative contract markets, TEC submits that any Code changes should not be such as to hinder the risk management activities of participants operating in these secondary markets. The proposed Code changes will have the effect of stifling innovation and creativity in the management of risk through the hedge contract market.

Because the proposed Code changes provide exemptions to the rebidding prohibition that are limited to physical events, they are removing the ability for participants to structure financial contracts whose volume and/or price terms may be subject to short-term variations. Generators will be unable to manage the risks that are associated with contract structures such as whole-of-meter hedges or look-back options.

Such products can add enormous value to the market and give retailers and customers the ability to more closely align their hedge position to their underlying physical demand. However, the proposed Code changes would remove the ability of generators to manage these risks on behalf of counterparties and such innovative product offerings will most likely quickly disappear.

Additionally, generators may seek to protect themselves from the consequences of reduced flexibility in managing their dispatch arrangements to suit their contract positions, by inserting new forms of Force Majeure clauses into hedge contracts. Such clauses would seek to protect generators from the risk of being unable to readjust their portfolio dispatch following a plant failure for a period of 3 hours.

TEC submits that such consequences could not support NECA's assertion that these changes are for the benefit of customers.

## **6. Specific Detriment to be Suffered by Tarong Energy**

### **6.1. Economic Operation of Energy Limited Plant**

National Electricity Code Chapter 1, Section 1.3 - Market Objectives (a protected provision), states "a particular energy source or technology should not be treated more favourably or less favourably than another energy source or technology."

The proposed code changes appear to breach this key market principle by denying participants with fast start or energy limited plant, such as Wivenhoe, the opportunity to manage their assets optimally, ie. *less favourable treatment*.

- As Wivenhoe Power Station is a pumped storage hydro type generator, the short run marginal cost of Wivenhoe generation is wholly dependant on the variable pumping price. This means that on a day to day basis the economics of Wivenhoe generation change in line with the most recent pumping cost, which in turn is derived from the pool price during pumping.

TEC currently generates with Wivenhoe when an economic margin above the short run marginal cost can be achieved for a minimum amount of time. This is managed on a real time basis by self dispatching the plant when price and demand show a more than reasonable certainty of achieving this economic margin over the minimum time required.

Restricting economic rebids and real time management of Wivenhoe's operation in this case will be unworkable and TEC will have no choice but to initially offer Wivenhoe dispatch at levels to ensure that the risk of uneconomic generation in comparison to recent pumping is sufficiently covered. In short, TEC will be forced to generate with Wivenhoe less to ensure that it remains economic when it does run.

Example. Consider the case where pumping finishes at 06:30 and Wivenhoe is required to generate at 07:30. If the pool price during pumping was much higher than forecast due to loss of generation elsewhere in the system this would impact TEC on two counts. Under the proposed new rules, not only would TEC be unable to rebid its pumping load within 3 hours of dispatch to maybe move it to a more economic time, but also would not be able to adjust its previously offered bid for Wivenhoe generation to ensure that the new short run marginal cost is reflected in its bid. Should such a reduction in flexibility be introduced, the risk created by this inflexibility will need to be priced into initial offers.

- As a pumped storage generator Wivenhoe is energy limited by the amount of water in the upper reservoir (Splityard Ck Dam), the level of which is managed through pumping from Wivenhoe dam. This energy limitation simply means that once total capacity generation is used at Wivenhoe it cannot be recovered until the market allows for enough pumping time to restore the dam levels. The new rules will limit the ability to manage the available energy on an ongoing basis throughout a given day to optimise the commercial outcomes for TEC.

If Wivenhoe energy has already been used through dispatch of a lower bid which required it to run constantly across the early part of a day, the remaining energy may not be enough to continue operation into the evening peak or to protect TEC's position in the event of a contingency. As this is an undesirable position the initial bids on Wivenhoe will need to be conservative so as to retain an energy reserve to cover contingencies that may occur elsewhere in the TEC portfolio.

The market as a whole will lose as TEC makes initial bids for Wivenhoe generation higher to avoid any situation where Wivenhoe is unavailable to cover Tarong Power Station contingencies.

## **6.2. Portfolio Rebidding Following Technical Rebid**

The 3 hour rebidding restriction and intent of initial bid proposals appear to remove the ability of a participant to rebid other units within a portfolio when a technical rebid has been required. This change will affect availability and pricing in the hedge contract market, as participants seek to protect themselves from the increased risk.

- The ability to respond to plant failures by rebidding other units within a portfolio remains essential for management of hedge contract positions. Given the loss of a Tarong unit, rebids would ordinarily be submitted for the rest of the portfolio to limit exposure to pool price. Under the proposed new rules, Wivenhoe for example would be unable to be rebid to cover loss of a Tarong unit.

The immediate effect following authorisation of the proposed rules, will be a change in the level of contracted energy TEC will be willing to offer going forward. This will be to ensure that TEC will never be left 'short' in the event of unplanned Tarong Power Station outages.

The market effect seen after implementation, will see higher pool prices as higher priced energy is dispatched to replace a failed unit instead of the replacement plant within a portfolio.

## **6.3. Operational Uncertainty**

It is unreasonable to expect that in a dynamic market consisting partially of un-scheduled load, for an unstorable commodity, with supply based on physical plant with varying levels of reliability, that bids placed a day ahead, will not require change. The proposed requirement concerning placing only those bids which to the best of the participants knowledge will not require change is an unacceptable solution, to an unstated problem. Technical limitations and unplanned events occurring within the generation/transmission and supply system changing the supply/demand balance, will leave participants with obsolete 24 hour plus old bids trying to manage a dynamic real time position.

Where does NECA see energy prices going during a major contingency involving loss of several base load generating units? Presently both the participant(s) involved and competitors will often reoffer generating plant at lower prices than initially bid during such a contingency. If not allowed to rebid in such an event, prices must rise to the level bid, which will include a higher risk premium than currently exists to compensate for the loss of flexibility.

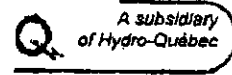
## 7. Unintended Consequences

Certain unintended consequences of the proposed changes will tend to create further uncertainty and hence risk for all participants in the National Energy Market. These appear to have been unforeseen by NECA, given that it is hard to believe that any public benefit gained would outweigh the effects of the retrograde steps proposed. Instead of creating greater transparency in the market, the inflexibility inherent in the proposed changes will encourage some participants to remove themselves from the market and join the already 'invisible' operations of existing unscheduled participants/loads.

- The few remaining scheduled loads will be encouraged to change to non-scheduled. As these are large loads this will have a major effect on the accuracy of the predispach forecasts that NECA intends participants to place faith in for their initial bids.
- Smaller capacity generation units currently operating as scheduled units will be encouraged to become unscheduled to avoid the inflexible restrictions placed on their operations. This further level of uncertainty placed on the remainder of participants will see the need for a greater risk premium placed on generation bids.
- It is not realistic to assume that NECA will be able to foresee and define all necessary exceptions and variations to the exceptions necessary to maintain an efficient market. Unfortunately, by putting in place a closed set of defined exceptions someone will eventually get caught in circumstances where exception would have been deserved and be subject to penalty. Better to let fluid market forces have effect than let artificial regulation reign.

# **TransÉnergie Australia Pty Ltd**

**ACN 084 240 602**



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27 August 2001

Mr Greg Thorpe,  
NECA,  
Level 5, 41 Currie Street,  
Adelaide, SA 5000.

Dear Mr Thorpe,

## **Re: Generators' bidding and rebidding strategies and their effect on pool prices**

NECA has recently published a report "Generators' bidding and rebidding strategies and their effect on pool prices" (the Report) that details the results of its investigation into generators' bidding and rebidding strategies and their effect on prices. An outcome of the Report is that draft National Electricity Code (the Code) changes have been submitted to NECA's Code Change Panel. This submission is in response to the NECA Code Change Panel's consultation on those draft Code changes.

TransÉnergie Australia Pty Ltd (TransÉnergie) is of the firm belief that price signals should determine the behaviour of National Electricity Market (NEM) participants. For example, prices provide crucial signals for much-needed new infrastructure investment and for demand-side responses. It therefore follows that the NEM price signals need to be efficient so that market participants respond in the 'correct' manner, and the NEM delivers the maximum level of benefits.

TransÉnergie considers that rebidding represents an essential flexibility to enable generators and market network service providers to respond to changes in physical, and legitimate commercial, circumstances. It is imperative for the effective operation of the market. Artificially constraining prices that properly reflect the underlying dynamics of the market will distort those crucial signals and jeopardise the new investment already committed or planned, and future prospective investment, in the market.

The Report indicates that a large number of the very high spot prices experienced over last summer arose from extremely short-term spikes as a result of inefficiencies in the market rules or the way those rules are applied in practice. The Report further indicates that a number of the very high spot prices experienced over last summer arose as a result of

individual generators taking advantage of those inefficiencies to artificially to drive up prices.

TransEnergie supports the further development of the NEM in order to eliminate such inefficiencies and also price outcomes directly related to those inefficiencies. However, extreme care needs to be exercised to differentiate between higher spot price outcomes due to market inefficiencies, and higher spot price outcomes that are a legitimate market response. Elimination of higher spot prices that are a legitimate market response will not lead to a more efficient market; rather, it will be to the detriment of the market itself. TransEnergie is also concerned that a focus on the elimination of market inefficiencies does not inadvertently increase the likelihood of events that could potentially lead to more significant inefficiencies than presently exist. For example, the Code lays out procedures and practices that NEMMCO is required to follow in order to maintain power system security. Clause 4.2.6 (b) of the Code (General Principles for Maintaining Power System Security) outlines one such procedure viz

*'Following a credible contingency event or a significant change in power system conditions, it is possible that the power system may no longer be in a condition which could be considered secure on the occurrence of a further contingency event. Following a contingency event (whether or not a credible contingency event) or a significant change in power system conditions, NEMMCO should take all reasonable actions to adjust, wherever possible, the operating conditions with a view to returning the power system to a secure operating state as soon as practical to do so, and, in any event, within at most thirty minutes.'*

It is noted that the proposed Code changes delete the text 'as soon as practical to do so, and, in any event'. While it is agreed that this Code change could potentially eliminate higher price outcomes by permitting NEMMCO to operate the market in an insecure state for a longer period, to do so will be at the potential expense of power system security. Under the occurrence of a further contingency the price outcomes as a result of such a NEMMCO decision (to operate for a longer period in an insecure state) could well be many times worse than those occurring had NEMMCO maintained power system security as its first priority. On that basis TransEnergie does not consider that NEMMCO should be permitted to sacrifice power system security in order to achieve potentially lower price outcomes.

In conclusion, while TransEnergie supports NECA's efforts to eliminate high price outcomes arising from market inefficiencies, TransEnergie considers that changes such as those proposed for Clause 4.2.6 (b) have the real potential to lead to increased, and not reduced, market inefficiencies. Therefore TransEnergie cannot support the proposed change to Clause 4.2.6(b) of the Code.

Regards,



Dr. A. Cook  
Managing Director



28 August, 2001

Geoff Henstock

NECA

*By email:* [ghenstock@neca.com.au](mailto:ghenstock@neca.com.au)

Dear Geoff

**TXU Submission to the code change panel on rebidding code changes**

Please find attached a submission on this paper on behalf of TXU, registered in the NEM as a market customer, network service provider and generator.

For any enquires, please call me on (03) 8628 1280.

Yours truly,

Ben Skinner

Mgr Physical Markets

## Summary

- TXU supports, in general, NECA's attempts to clarify the workings of the TPA, the application of hard network constraints and the need to ensure that bids reflect genuine intentions. We do however note some difference of opinion from industry experts in these areas, and suggest that the implementation requires further refinement following consultation with those experts.
- The 3 hour rebidding restriction is an ill considered mechanism that results in outcomes almost exactly opposite to its intentions. We suspect the regulator has little understanding of the process of marginal generator dispatch in the NEM. We urge the regulator to defer this rule for consultation with industry expertise before attempting such major alterations.
- The 3 hour rebidding rule unfairly discriminates against:
  - Energy Limited Plant,
  - Slow starting marginal plant with a recall time between 30 minutes and 3 hours,
  - Scheduled generation as opposed to non-scheduled generation, and
  - Scheduled load and generation as opposed to non-scheduled load.

In each case Torrens Island is unfairly discriminated against.

- By banning the response of marginal plant such as Torrens Is, NECA has ensured a free-ride for non-marginal plant performing the sorts of behaviour that NECA wants to inhibit. This rule will actually reinforce such behaviour.
- The double negative process of "blanket ban except for..." is much less effective than an explicit ban on the actual behaviour. The 3 hour rule is inoperable until many more exceptions are added.
- The 3 hour rebidding rule is unenforceable in its current form. The necessity to respond to predispatch is a fundamental part of market design. Attempting to ban it will be recognised by NECA's monitoring and surveillance as absurd, and the rule is likely, in the long run, to be ignored by both the industry and NECA.
- If implemented in its current form, TXU will have great difficulty in using its Torrens Island capacity to underwrite its South Australian retailing activity, and may force our retreat from that market.

## Responses to initial consultation

TXU is disappointed by the apparent failure of NECA to consider the points raised in our submission. Despite being a market customer to twice the energy that we generate, our arguments appear to have been considered only within the "Individual generators commented generally supported...the NGF" sentence, which we did not. This does not provide comfort that NECA has taken sufficient time to consider the complex impacts of such a radical change to market design.

TXU Torrens Island averages 26 rebids per day (up to 130 some days) that mostly affect the next 3 hours and do not fall into the current exclusions. We believe therefore we need to be consulted before NECA recommends a rule change that over-turns our operating practices. NECA must try to understand why we have to rebid before they ban us from doing it.

The first page of that submission was dedicated to the fundamental need for rebidding flexibility of energy limited plant in response to an altering electricity market (rather than changing fuel conditions as excepted). It was also raised in hydro



submissions. This has not been mentioned in the NECA response, and there is no exception provided for that purpose.

Our 26 rebids per day are simply a design requirement for this plant type in a 5 minute gross pool. TXU is not accused by NECA of participating in the kind of behaviour it considers unconscionable, and yet we are going to be much more adversely impacted by the change than those who are. Paradoxically, our rebidding activity has been to lessen the impact of that behaviour, and some of it to protect our position following that type of behaviour in a competitor. Such self-protection will now be banned.

Many of the points below are reiterations of our earlier submission. We hope the code change panel takes the opportunity to consider them.

### **Slow Start Marginal Plant**

60% of the time the South Australian electricity price is below the cost of the standing losses of a Torrens unit. We therefore attempt to commit these marginal units only when we anticipate prices in excess of that level.

The startup time is a critical determinant of our profitability, by allowing us to reduce the standing losses through operating fewer units whilst being ready to participate quickly should prices move up. Torrens Island has created ingenious operating regimes to reduce recall times, creating much greater efficiencies through fewer standing losses: a great success of the deregulated market concept.

We typically keep several units in a warm state that permits recall in under three hours, at moderate cost to us. Should the dispatch or short term predispatch prices move up for any reason, we recall these units. Because we are registered as "slow-start" (takes over 30 minutes to start), a re-bid is required to commit the unit. The proposal provides no exception for this activity.

*Sub 3 hour recall of marginal plant is actually banned by the code change proposal! Is this NECA's intention?*

Similarly, if prices fall beneath our costs, we presently decommit units through a rebid, again for which there is no proposed exception. *Does NECA intend to force us to run below cost when prices are low?*

Please consider the following quote from the NECA monitoring and surveillance report of 22-28 July 2001.

"From early in the afternoon of 25 July, forecast prices for that evening rose significantly to around \$600/MWh in all regions... Commitment of units at Torrens Island and Newport, and further band shifting to lower prices at Eraring, close to despatch saw maximum prices at \$50/MWh".

The new rebidding rules would have barred the response seen from each of Torrens Island, Newport and Eraring. By NECA's own admission, prices would have been 12 times higher had the new rules been in place.

The NECA rules permit the commitment of registered fast-start units to an unexpected price change, but bar those who for technical reasons take a little longer. This is an unfair discrimination against our plant type, effectively downgrading our response capability to that as if we were technically very slow start, i.e. could not start or shutdown with less than 3 hours notice.

The following scenarios are quite realistic and will be reasonably common if the recommended code changes are enforced in their current form:

1. ***Interconnector de-rate***

**1000hrs:** SA prices forecast at under \$35 for rest of day. Torrens B1 and B2 200MW units committed, providing more than sufficient SA reserves. B3 & B4 units are offline but physically capable of starting in 1 to 2 hours.

**1030hrs:** Lightning de-rates interconnector by 250MW. The storm is expected to last until 1600hrs and constraint is entered by NEMMCO into predispach. The two on-line Torrens units are dispatched to maximum load, but the forecast now predicts extreme high prices, set by a competitor's initial offer, from 1130hrs lasting for the duration of the storm.

B3 & B4 are capable of starting prior to the extreme prices, but cannot due to the rebidding restriction. They are recalled and bid to synchronise in 3 hours-1330h and shutdown at the end of the storm-1600hrs.

**1130-1330hrs:** Prices set near VoLL by liquid fuel gas turbines, despite no physical reason not to run Torrens units B3 & B4. TXU loses several million dollars as a result of being exposed to sold hedges and retail equivalent to the capacity of 4 units when only 2 units were running.

**1330hrs:** B3 & B4 come on-line, the earliest permissible time under the rebidding restriction and immediately increase output.

**1330-1600hrs:** Liquid fuel gas turbines shutdown, SA price falls to low levels set by B3 & B4.

**1400hrs:** Weather forecast update indicates storm will last till 2000h. Predispach is updated showing near VoLL prices set by liquid fuel gas turbines 1600-2000hrs: the period following B3 & B4 shutdown.

TXU unable to alter shutdown plans for B3 & B4 due to 3 hour rebidding constraint. Enters rebid to restart units 3 hours from the present: 1700hrs and run until 2000hrs.

**1600hrs:** B3 & B4 forced to shutdown due to rebidding rule despite interconnector still being de-rated.

**1600-1700hrs:** Gas turbines restart and set near VoLL prices. TXU loses further several million dollars.

**1700hrs:** B3 & B4 resynchronise.

**1700-1800hrs:** Gas turbines shutdown and prices fall.

**1800hrs:** Storm clears early and interconnector rating increased to 500MW.

**1800-2000hrs:** SA prices fall to very low levels set by interstate plant, below operating costs of B3 & B4. Units forced to remain on-line by 3 hour bidding constraint.

2. ***3 hour competitor rebid***

**1000hrs:** SA prices forecast at under \$35 for rest of day. Torrens B1 and B2 200MW units committed, providing more than adequate SA reserve. B3 & B4 units are offline but capable of starting in 1 to 2 hours.

**1015hrs:** Baseload competitor raises price of large volume to near VoLL for the period 1330-1600hrs. Acceptable under 3 hour rule.

**1040hrs:** Predispach updates showing for 1330-1600hrs B1 & B2 at full load, with prices set by competitor near VoLL.

TXU recalls warm B3 & B4 units, but forced by 3 hour rule to defer synchronisation until 1400hrs and bids to shutdown at the end of the forecast high prices at 1600hrs

**1050hrs:** Baseload competitor rebids to lower price of large volume for the period 1400-1600hrs. Acceptable under 3 hour rule.

**1330-1400hrs:** Price set near VoLL. B1 & B2 only on line and at full load. TXU loses heavily, baseload competitor earns substantially.

**1400hrs:** Baseload competitor output increases as per bids sent 1050hrs simultaneously with B3 & B4 coming on-line.

**1400-1600:** B3 & B4 forced to remain on-line due to 3 hour rule despite prices being below running cost.

Note particularly the second scenario, where the rebidding restriction inhibits our response to exactly the sort of behaviour that NECA wishes to prevent. NECA is therefore providing the initiator with a mechanism unfettered by competitor response, actually encourage more instances of this behaviour.

Given the opportunity, we could provide NECA with many such examples where the new rules potentially drive perverse outcomes. Before implementing changes that may have such outcomes, NECA needs to thoroughly scenario test them using actual market trading experience. It is recognised that no NECA staff have any NEM trading experience, so TXU is willing to assist by participating in an industry working group for that purpose.

### **Energy Limited Plant & Rebidding**

The ability to operate a plant such as TXU Torrens Island in the NEM, which has finite fuel resources, is critically dependent upon the ability to alter offers at short notice. Torrens Island typically holds rights to daily gas supply of between 25 and 40% of its full load consumption. To a small extent, expensive oil can be used to supplement, however we rely mostly upon the expectation that unlimited base-load plant will supply off-peak demand, and Torrens Island will only reach high outputs for a few hours per day.

This approach is common for gas and hydro plant, and is an efficient method of allocating limited fuel supply to support a peaky electricity demand. Although it existed well before the NEM, the NEM's simple dispatch process with bidding and rebidding flexibility has allowed its continuance, with decision making and risk held by the participant.

The limited fuel is rationed by an iterative bidding and rebidding process. The initial bids of the power station are priced such that the fuel will be released to the desired daily volume. If this occurs, then it implies that the fuel will earn maximum return, by being loaded highest at times of best price. It follows also that the fuel is also being consumed at time of maximum benefit to the customer.

Should the pre-dispatch forecast indicate that the plants will consume more or less than the desired volume, then rebidding occurs to refine that rationing. Because the fuel supply is fixed, then it follows that bid prices will tend to be low when the market is weak, and bid prices will tend to be high when the market is tight.

When a market disturbance occurs, such as the loss of a base-load generator or a reduction in the capacity of an importing interconnector, then the dispatched volume of a marginal energy limited plant will naturally increase. If bid prices are unchanged this will cause premature exhaustion of the energy supply, resulting in possibly load-shedding or at least a dramatic rise in price. The rebidding function, which allows the generator to more carefully ration his energy, clearly results in a more secure supply

and lower average price. Such behaviour is often misinterpreted as a participant taking advantage of an unexpected failure in a competitor to exercise unreasonable market power.

It is important to understand that this process also allows us to provide contract and retail liquidity of a notional volume much greater than we physically generate. Torrens Island typically generates about one-fifth of the contractual and retail energy exposure that it is used to protect.

It is important to understand that:

- The need to perform iterative rebidding is not caused by changes in the nature of fuel supply, it is caused by shifts in the electricity market. Therefore it is not one of the present exceptions.
- This rebidding is not evil. It is simply a mechanism of achieving inter-temporal energy optimisation that is critical for any power system.

### **Contract/Retail liquidity and bidding/rebidding flexibility**

When offering firm contracts to retailers or physically to customers, a generator needs confidence that it is capable of operating to its desired volume at a given price. This means that should prices rise, it can commit a standby unit quickly, or if prices are forecast to be higher later, that it can reallocate its limited fuel to the optimal time.

It is on the public record that Optima Energy was vested with nearly double the maximum daily contract notional energy volume than it had daily gas allocation. This position is quite acceptable thanks to the ability to ration fuel through re-bidding, and to increase its bids when forced to operate on liquid fuel. It would be impossible to take on such a position without that flexibility as the generator could not guarantee that it would be able to conserve the fuel to protect its contracts for the very high priced periods. Thus rebidding supports contracting and retailing liquidity and allows for more firm contracts in the wholesale market.

Since the start of calendar year 2001, TXU's sent out generation energy has been only 44% of the total notional volume of its SA retail load and contracts written against the SA pool price.

Thanks to the current rebidding flexibility, Torrens Island was able to support the successful entry of TXU and other non-host retailers into the SA retail market. If the proposed rules were implemented, TXU would have no choice but to retreat from that activity. It is notable that rebidding flexibility has been opposed by parties who would gain from that scenario.

### **Equity with demand and unscheduled generation**

The question can be asked, in a free market, why should a supplier have to rebid at all? Why not just independently vary output? Because a degree of predictability is required for any power system to function, the process of rebidding is a necessity, and large generators have participated in providing rebids that are helpful to the market as a whole, system security, and are released to public scrutiny.

However this does not apply to small generator units (<30MW) or the demand-side. Indeed there is already a very large amount of controllable demand-side not subject to the bidding obligations placed on generation. The interruption (or non-interruption) of this demand is effectively identical to a generator's last-minute rebid, but as there is no public record, it is impossible to audit for anti-competitive or misleading behaviour. For example, it is conceivable that a participant could utilise interruptible demand to game ramping effects or the 5 minute/30 minute anomaly. This would be unprovable with the present double standard regarding provision of information by the demand side.

In most states, the flexibility and volume of interruptible load aggregators actually gives them considerable market power which in some states is arguably greater than the largest generator portfolio. In fact, there are suspicions that this was exercised on 3 May 2001 in a manner that exploited the 5/30 minute anomaly. Due to the nature of its hidden operation, we have no way of confirming that suspicion.

The proposed code change does not inhibit this type of behaviour and actually exaggerates the current market power advantages of load aggregators.

### **Double Negative**

The present rule is couched in the framework "Sub-3 hour rebidding is banned except for....". This has forced NECA to already form a large list of exclusions, and if NECA wants to avoid the perverse outcomes listed above, it will need to add many more.

NECA needs to ask itself, what percentage of rebids sub 3 hour does it consider manifestly harmful? We suspect NECA would estimate this as less than 1%.

It appears sub-optimal to inhibit 1% by banning 100% except 99%.

As stated in our earlier submission, NECA needs to clearly identify unacceptable market behaviour and explicitly combat that. We fully support attempts by NECA to improve their own resources and access to powerful enforcement regimes.

Having done this, they should not need to impact the free and efficient operation of the market through rebidding flexibility.

### **Enforcement of 3 hour rule**

If the proposed rule change, with its prohibition of the optimisation of energy allocation and sub 3 hour self-commitment will create such operational difficulties that we doubt that a pragmatic NECA surveillance and monitoring group would actually enforce them. It would be unfortunate if our business and the policeman had to routinely ignore breaches of the code to get sensible outcomes.

There will remain a great number of sub 3 hour rebids (e.g. our 24 per day average) and attempting to analyse each one against the complex exclusion list would swamp any resources that NECA could utilise. These resources are better dedicated the way they are now, identifying and focussing upon instances of actual offensive behaviour, rather than judging innumerable rebids against complex exclusions.

### **Other Issues**

Outside of the 3 hour rebidding restriction, TXU is generally supportive of NECA's intent in these code changes. We do however note two areas where industry experts have conflicting technical views to NECA:

- There is considerable legal opinion obtained by participants that conflicts with NECA's legal opinion about the extent to which rebidding is already subject to the TPA.
- NEMMCO is reluctant to respond to the code changes regarding transmission constraints without direct support and instruction from the reliability panel.

TXU is unqualified to comment upon these issues, but notes that those who are qualified do have concerns. Given our view that NECA needs to take on more industry experience regarding the rebidding limit, then we also have some sympathy to the conflicting views above.

TXU supports the moves by NECA to ensure that bidding reflects participants' genuine intentions at the time. We look forward to the same moves regarding unscheduled generation and demand side participation.



Yallourn Energy - Second Submission to NECA on Rebidding Ver 2.2  
27- Aug – 2001



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Mr Geoff Hanstock  
NECA, Level 5 41 Currie St  
Adelaide SA 5000  
Fax 8213 6300  
Email ghenstock@neca.com.au

CC:  
Mr: Sanjay Khushalani, Manager Market Operations  
Mr. M. Smith, CEO Yallourn Energy  
Mr. A. Bonwick, Director Marketing, Yallourn Energy

Dear Geoff,

We welcome an opportunity to contribute and influence the review process on re-bidding and the proposed code changes.

We are very concerned that the consultation process appears flawed; the majority of key and fundamental issues raised in the first round of submissions have not been addressed. We seek a formal response on the specific issues raised in our submission.

To increase the effectiveness of this review, we seek this response well ahead of the deliberation of the NECA Code Change Panel.

Yallourn Energy fully supports the NGF submission. The attached submission amplifies some of the key points addressed by NGF, and raises a number of supplementary issues.

Yallourn Energy - Second Submission to NECA on Rebidding Ver 2.2  
27- Aug - 2001

Thank You

Yours Sincerely

David Hoch  
Strategist  
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## **Yallourn Energy submission to NECA regarding the proposed code changes on rebidding**

Yallourn Energy fully supports the NGF submission and takes this opportunity to provide an individual submission to amplify some of the key elements and to provide additional arguments for the way forward.

### **1 Re-bidding is effective and essential**

The case for rebidding/reoffering has been clearly established during the code authorization and numerous subsequent reviews, spanning a period of several years. More recently NECA's own report shows that there is an overall reduction of prices as a result of rebidding/reoffering. The key overriding principle is that the market should be economically efficient.

Some of the principal features and elements necessary for delivering efficiency in the current market are as follows:

- Energy only market
  - Simplicity
  - Transparency
  - Efficient behaviours based on real time market signals and responses
  
- Management of risk in the spot market
- Inter-temporal elements and risks are managed entirely by the participants (dispatch, energy constraints, cycling on plant etc)

- The plant, transmission system and load conditions change rapidly, and often without prior warning.
- The energy only market design dictates that capacity needs to be paid for through the energy market. This necessitates high prices for limited durations which also implies price volatility.
- Ability to manage risks by responding to changed market and physical conditions by bidding/rebidding and offering/reoffering.

The current market design is based on a clearing engine without inter-temporal optimisation. Unlike some of NEMs' earlier precursors, participants need to manage commitment and decommitment (min on time, min off time, startup cost). Given the importance of market signals and the role of rebidding/reoffering in leading to efficient outcomes, any significant change to rebidding/reoffering must be made in the context of the overall market design. Otherwise, there is a high risk of market failure as a direct result of tinkering with the market rules.

Current documents from NECA do not define any specific problems, but propose a number of perceived solutions.

However well meaning, regulatory intervention in the market can result in unexpected behaviours and outcomes, as recent events in California clearly demonstrate. When contemplating changes, the process needs to be holistic and transparent, with clear problem definition in place.

**Outcome sought:**

(i) In summary, fully optimized real time rebidding/reoffering is an integral and essential feature of the energy only market and must not be altered unless as part of a review of the overall market trading arrangements.

**2 The case for “bidding”**

In the current NEM market, there is an almost complete absence of bids by customers/loads when compared to the supply side offers. This leads to an essentially one sided market, with prices set by generator offers. Large loads vary their consumption

without disclosing their intentions to the market. There is a need for response symmetry in the market, where loads explicitly disclose their intentions via bids. This would lead to more transparent forecasting by NEMMCO, and loads would be subjected to the same bidding requirements as supply participants.

For any switchable load the current rules would apply exactly, whilst other loads could be treated as an aggregate volume which bid at Voll. There needs to be an obligation on loads to at least disclose their volumes, even if the load may not be switchable and eligible as a dispatchable load. Appropriate rule changes need to be instigated by NECA to foster market efficiency, particularly with respect to current “non-market loads”.

**Outcome sought:**

- (i) Implement the HPS proposed code change to include demand side participation.
- (ii) Review the existing code for demand side to foster disclosure and market based response.

**3 Physical delivery and market signals**

The curfew on rebidding violates economic efficiency principles by delaying and blunting the spot price signals to participants. In fact, it would provide misleading information to the market and distort physical market outcomes. For example, the clearing of physical faults in the market would not be impacted by the ramp rate implementation, but responses by participants would be affected. Delayed responses by supply and demand would magnify the underlying physical problems. Under such a regime, participants would be exposed to various levels of unmanageable risk due to inconsistent dispatch and pricing.

Given the concerns regarding the supply/demand balance in Vic and SA regions, it is imperative that effective pricing signals (both magnitude and timeliness) be consistently provided under the existing energy only market arrangements. This is the most appropriate way to attract peaking plant investment and demand side response.

Energy market signals must be consistent with the system reliability criteria. Specifically, the value of Voll must be appropriate to the EENS (expected energy not served) criteria. Otherwise, inappropriate level of Voll, and/or blunting its application by ramp rates, will result in on-going intervention by the reserve trader (essentially market failure).

The proposed code changes are likely to lead to market failures as follows:

- Spot Market
  - Medium term - not delivering the necessary capacity and/or efficiency (resulting in ongoing intervention)
  - Short term – short term response blocked leading to inefficient outcomes, frequent and ongoing reliance on NEMMCO directions to resolve short term system security issues.
- Contract market
  - Due to the increased level of risk to generators resulting from the 3hr rebidding, it is **highly likely that the liquidity of the contract market will be reduced, and prices increased.**

**Outcome sought:**

(i) Clearly demonstrate to market participants that NECA is committed to market based mechanisms and the need to allow the market to work effectively by withdrawing the current proposed code changes.

(ii) Issue a clear regulatory statement, which demonstrated that NECA is focussed on market efficiency and performance, and is not driven by “popular politics”.

**4 Market information – current and additional**

Yallourn fully supports NECA's role in market surveillance, monitoring and reporting. By making information freely available, transparency of outcomes is fostered. NECA has already demonstrated that this approach has led to improved behaviours and increased efficiencies in the market.

An additional transparency could be achieved by making the bid/offer stack available to the market in real time. This would assist participants in more effectively managing their risks. Precedents for such a scheme are well established in other markets, such as the stock exchange.

**Outcome sought:**

- (i) NECA needs to clearly identify specific behaviours leading to perceived market inefficiencies.
- (ii) The impacts of the behaviours must be well analysed and substantiated by NECA.

## **5 SOE**

Yallourn supports the development and implementation of an effective code of ethics to foster market integrity and confidence. NECA commenced a process of developing the SOE some time ago, however it was never finalised or implemented.

SOE would effectively cover specific market behaviours which were deemed to be detrimental to market efficiency and/or integrity. It has been acknowledged that the market is perceived to be working well with some exceptions. The SOE would specifically deal with such exceptions, without the need to rely on the code.

Some examples of behaviours that may be covered are as follows:

- Misleading the market
- Gaming 5/30 minute prices
- Exploiting ramp rate limitations

**Outcome sought:**

- (i) NECA should implement an effective SOE instead of seeking code changes.

## **6 Efficient and practical solutions**

The proposed code changes will not deal with the perceived problems, such as the price spiking from overconstrained dispatch. There are effective forums dealing with the 5/30 minute pricing anomaly and the formulation of network constraints. These groups are the effective and appropriate forums for addressing these issues.

**Outcome sought:**

- (i) NECA should encourage the existing NEMMCO forums, and where appropriate, increase the sense of urgency in resolving the above mentioned problems.
- (i) The code changes are ineffective and inappropriate in dealing with these problems and must be withdrawn

**7 Process to increase efficiency**

There is a need for an effective and formal process to be established to progressively increase the efficiency of the electricity market. Such a process would need to be holistic, with a good balance between short and longer term tradeoffs.

**Outcome sought:**

- (i) The process should be facilitated by NECA as part of its regulatory role under existing code provisions.