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Lyn Camilleri
General Manager, Electricity Markets Branch
Australian Competition and Consumer Commission
Level 17, Casselden Place
2 Lonsdale Street
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8 April 2020

Dear Ms Camilleri,

AGL welcomes the opportunity to provide input on the *Draft Guidelines on Part XICA – Prohibited conduct in the energy market – March 2020* (**Draft Guidelines**).

As AGL has previously stated, the ACCC's guidelines on how it will enforce Part XICA of the *Competition and Consumer Act* 2010 (CCA) when it comes into effect on 10 June 2020 will play an important role in providing AGL and other market participants with greater certainty and clarity as to how the new prohibitions are intended to operate. AGL appreciates the ACCC's detailed consideration of the issues that AGL and other market participants have highlighted in their submissions to the ACCC's initial consultation, and acknowledges that the ACCC has strived to provide as much clarity as possible in challenging circumstances and with limited time prior to the prohibitions coming into effect.

However, as is clear from the briefings and discussions with industry participants, providing clarity on how the prohibitions in the new Part XICA of the CCA are to be interpreted and applied in complex market circumstances is an extremely difficult, if not impossible, task. The Draft Guidelines issued by the ACCC provide guidance on concepts and scenarios but stops short of providing guidance on the multifaceted and nuanced situations in which market participants operate. This is not attributable to any failing on the part of the ACCC, but rather to the inherent ambiguity of the prohibitions, the complex and highly regulated nature of the energy industry, and the variability of the operations of each participant.

In the enclosed submission on the Draft Guidelines, AGL has focused on the principles to be drawn from the examples. In summary:

- AGL supports the Draft Guidelines' adoption of particular principles articulated in the Explanatory Memorandum (**EM**), including:
  - that the retail provision is concerned with sector-wide decreases in costs, rather than changes to individual retailer costs. For retailers, including vertically integrated retailers, this means that the relevant wholesale costs are the benchmark market-based costs likely to be incurred by a standalone retailer;
  - that the bidding prohibition is not intended to interfere with genuine commercial behaviour intended by the design of the spot market; and

- AGL asks that the ACCC seek to provide greater clarity in respect of some of the principles and examples outlined in the Draft Guidelines. AGL's specific concerns are detailed in the body of the submission, and include the following:
  - The retail pricing section should be amended to:
    - better reflect the fact that competition operates effectively in the market, and that the retail pricing prohibition should not operate as a de facto form of pricing regulation that requires uniformity in compliance approach;
    - review the current position in relation to frequency of changes required and fixed term contracts;
  - The contracting provision section should be amended to clearly limit its approach to the application of the prohibition to electricity financial contracts between generators and retailers; and
  - The bidding provision section should be amended to better reflect the complexity of the market circumstances and individual business operations.

AGL thanks the ACCC for its constructive engagement with market participants on the Draft Guidelines and looks forward to reviewing the final guidelines in May 2020. AGL would ask that the ACCC continue to work constructively with participants after the issue of final guidelines and the implementation date, and to consider the appropriateness of any enforcement activity in light of the lack of clarity as to what each participant's compliance obligations are under these new prohibitions.

The enclosed submission contains information that is confidential to AGL, which has been clearly marked. AGL will provide the ACCC with a public version of the submission with the confidential information redacted.

Please do not hesitate to contact me on [redacted] if you have any questions in relation to this submission.

Yours sincerely,

[redacted]

Beth Griggs
General Manager, Competition Regulation & Strategy

Consultation on ACCC draft guidelines on the Prohibiting Energy Market Misconduct Act – Submission to the ACCC

1. Executive summary

AGL thanks the ACCC for the opportunity to provide input into its *Draft Guidelines on Part XICA – Prohibited conduct in the energy market – March 2020* (**Draft Guidelines**). The Draft Guidelines contains helpful guidance on the ACCC's view of the prohibitions that will be found in the new Part XICA of the *Competition and Consumer Act* 2010 (Cth) (**CCA**) and AGL appreciates the useful examples that the ACCC has provided. It is evident from the draft that the ACCC has spent considerable time and effort to grapple with the complex issues of application raised by the *Treasury Amendment (Prohibiting Energy Market Misconduct) Act* 2020, as well as the issues raised by AGL, industry and other interested parties.

AGL appreciates the ACCC's detailed consideration of the issues that AGL and other market participants have highlighted in their submissions to the ACCC's initial consultation, and acknowledges that the ACCC have strived to provide as much clarity as possible in challenging circumstances. However, as is clear from the briefings and discussions with industry participants, providing clarity on how the prohibitions in the new Part XICA of the CCA are to be interpreted and applied in complex market circumstances is an extremely difficult, if not impossible, task. The Draft Guidelines issued by the ACCC provide guidance on concepts and scenarios but stops short of providing guidance on the multifaceted and nuanced situations in which market participants operate. This is not attributable to any failing on the part of the ACCC, but rather to the inherent ambiguity of the prohibitions, the complex and highly regulated nature of the energy industry, and the variability of the operations of each participant.

AGL would ask that the ACCC continue to work constructively with participants after the issue of Final Guidelines and the implementation date, and to consider the appropriateness of any enforcement activity in light of the lack of clarity as to what each participant's compliance obligations are under these new provisions.

AGL's specific comments on the Draft Guidelines are set out in detail below, but in summary our comments are as follows:

Retail pricing prohibition

AGL agrees with many of the concepts articulated by the ACCC in its Draft Guidelines, which AGL has interpreted to include the following:

- That the relevant test for considering whether there has been a sustained and substantial reduction is one that is assessed against industry based 'benchmark costs'. A retailer who manages to operate efficiently and effectively, and out-performs the market on that basis, will not be assumed to have contravened this provision if it does not pass through company specific cost savings in the short to medium term;
- That a retailer does not need to pass through cost reductions in a uniform way across its customer base, and that the application of the provision should not inhibit competitive or efficient conduct by retailers.

AGL does believe that the Draft Guidelines need to be amended to more clearly reflect the fact that the existing market design allows competition to operates effectively in the market, and that the retail pricing prohibition should not operate as a de facto form of pricing regulation that requires uniformity in compliance approach. If the retail pricing prohibition were imposed in a way that effectively requires uniformity of approach amongst retailers, it would dampen price competition that currently exists. Retailers have different

cost positions and will analyse those costs differently having regard to their competitive position. Also, in assessing what cost reductions to pass through, retailers will have regard to the need to remain competitive and to differentiate their energy plans and pricing from other retailers – all while operating in a highly regulated retail environment where there is both federal and state-based regulation in relation to how electricity plans are marketed to customers (eg reference price advertising under the *Electricity Industry Code*).

With that principle, as well as current standard industry practices, in mind, AGL suggests that the ACCC guidelines could introduce greater clarity regarding the following matters.

- ***Wholesale cost reductions:*** retailers will incur costs differently, and will assess their wholesale costs on different bases. AGL suggests that the Guidelines should have specific regard to the fact that competition in the market means that retailers offering lower priced new products throughout the year (usually in the form of increased discounts) is effectively a real time pass through of changing wholesale costs. This should be specifically taken into account when considering both the quantum of any necessary adjustment, and whether the manner in which a retailer passes such adjustment through to its customer base in reasonable.
- ***Frequency of price reductions:*** As noted above, competition in the market is the most effective means of retailers passing through reductions in cost outside of price cycles. There are a number of practical issues associated with seeking to apply this provision in a manner that would require more than annual price changes to existing products:
    - it may not be practicable to achieve this given price changes are not necessarily quick to implement, particularly if retailers are expected to pass through cost reductions across their entire book and comply with a range of advertising requirements under the *Electricity Industry Code* and Victorian regulation;
    - retailers may not be able to identify a reduction in wholesale cost as being 'sustained' rather than temporary until the passage of at least 6 months (see below);and
    - it would risk introducing 'price volatility' into customer contracts – if retailers are required to pass through changes observed over a period of months, they would likely pass through increases in the same timeframes;
- ***fixed rate contracts longer than 12 months*** – retailers should not be required to pass through a cost reduction to a customer who is on a fixed rate for a contract or benefit period of longer than 12 months. Fixed rate contracts offer benefits to consumers, including price certainty for the term of the contract and a hedge against future price increases. Some fixed rate contracts may also offer credits and other value-added benefits. Under these contracts, it is the retailer that holds the price volatility risk as it is obliged to supply electricity at that fixed rate for the term of the contract, even if the costs of supplying those contracts increases. The ACCC's expectation that retailers change a fixed rate within the contract term does not recognise these price-risk considerations;
- ***allocating adjustments between different customer groups and different tariff types*** – to ensure competition and differentiation, retailers should be able to determine how to allocate costs reductions. Provided the overall quantum of the reduction is passed through in a reasonable manner (discussed further below), each retailer should have the flexibility to make its own decisions on how to allocate those reductions, particularly given that retailers generally price having regard to their competitive position in each market and segment. This flexibility should not be removed by the operation of section 153E.

Contracting prohibition

AGL considers the guidelines could be amended to reduce the regulatory burden on generators without detracting from the effectiveness of the provision by:

- clearly limiting the definition of 'electricity financial contracts' to apply to derivatives, futures, floors, caps and collars with retailer counterparties. Generators consider many contractual arrangements each year that are not the focus of the prohibition (eg contracts with large customers). Under the current guidelines, the generators would still need to include these contracts in a participant's internal compliance processes, notwithstanding that they are not properly the focus on the provision. In specifically limiting its approach to the application of the provision, the ACCC would not reduce the effectiveness of the provision but would reduce the internal regulatory compliance burden on every generator; and
- clarifying the approach to inferring anti-competitive purpose. Conduct and decisions of generators will occur before their effect can be assessed, and against a background where any decision regarding a contract can have implications for the ability of retailers to compete. The guidelines could assist by confirming that an anti-competitive purpose would not be inferred solely from the fact that a potential consequence of a generator's contracting conduct would be to hinder or prevent another retailer from obtaining its desired hedging position or a particular electricity financial contract.

Bidding prohibition

AGL agrees with many of the concepts articulated in the Draft Guidelines, but believes the guidelines could introduce greater clarity regarding:

- the 'test' that should be applied in determining what constitutes 'manipulation or distortion'. The guidelines acknowledge the statement in the Explanatory Memorandum (**EM**) that the bidding prohibition is not intended to interfere with genuine commercial behaviour intended by the design of the spot market. It would be helpful if the guidelines confirmed that the ACCC also takes this view, and as such it could be formulated into a 'test' against which generators might assess their bidding conduct;
- The application of the principles in the guidelines to a generator, or gentailer, with a portfolio of generation assets. A number of examples in the guidelines refer to a generator operating a single generating system. The guidelines could assist by confirming that the principles arising from those examples also apply to a generator, or gentailer, with a portfolio of generation assets; and
- The purpose of distorting or manipulating prices. The issue is complex but it would be helpful if the guidelines included guidance as to practical principles that generators may follow to ensure they are complying with the law, including confirming that the bidding prohibition does not prevent genuine commercial behaviour intended by the design of the spot market.

Processes and remedies

AGL considers the Draft Guidelines could be amended to provide greater clarity on:

- ***when enforcement action will be taken against individuals***; and
- ***the ACCC's views on the interaction between the prohibited conduct notice and prohibited conduct recommendation*** – as AGL has previously submitted, in order to afford corporations greater procedural fairness, the ACCC should consider providing the relevant corporation with a copy of the prohibited conduct recommendation that has been provided to the Treasurer recommending a contracting or divestiture order.

2. Retail pricing prohibition

Section 153E provides that a corporation engages in prohibited conduct if it:

- offers to supply, or actually supplies, electricity to small customers (residential or small business consumers); and
- fails to make reasonable adjustments to the price of those offers or supplies to reflect reductions in its underlying cost of procuring that electricity,

(the **retail pricing prohibition**).

Based on the EM and Draft Guidelines, AGL understands that there are two steps for assessing compliance with the prohibition:

1) Has there been a reduction in the underlying cost of procuring electricity that is sustained and substantial? This is to be assessed by a retailer with reference to the two-step process that has been articulated in the EM, in AGL's previous submission, and referenced in paragraph 2.16 namely:
    a. First, consider whether there has been an industry wide cost reduction. In respect of wholesale costs this should be assessed with reference to a benchmark, market-based cost referrable to a prudent stand alone retailer; and
    b. Then, consider whether there is any individual circumstances particular to the retailer that it can properly take into account in determining its cost reduction is less than that determined by the first step.
2) If the answer to (1) is 'yes', has the retailer made adjustments to the price of its retail offers within an appropriate timeframe that are reasonable in all the relevant circumstances?

In the context of that two-step analysis, AGL considers it is important for the ACCC to reflect the fact that competition operates effectively in the market and ensure that the retail pricing prohibition does not become a de facto form of pricing regulation that requires uniformity in compliance approach across retailers, and thereby likely dampens the price competition that would otherwise exist.

This applies equally to both the question of assessing whether there has been a reduction in the underlying cost of procuring electricity and the question of whether there was a reasonable adjustment made. Retailers, depending on the nature and scope of their operations, will make different choices in relation their wholesale cost position, including how to hedge price volatility risks and how to analyse their costs, having regard to the competitive market and their competitive position. This is particularly true of vertically integrated retailers, where the mechanism of pricing from wholesale to retail will be subject to different mechanisms and will be priced according to different methodologies and assumptions. Further, in deciding how and when any reductions are passed through, retailers will have regard to the need to remain competitive and to differentiate their energy plans and pricing from other retailers.

AGL acknowledges that aspects of the Draft Guidelines recognise the above principle to some extent – for example, in the approach to individual cost reductions (example 4) and retail cost savings (example 5), and appreciate that, as per paragraph 2.29, that the ACCC does not intend for section 153E to inhibit competitive or efficient conduct. However, this aspect could be bolstered further and AGL has set out some examples below where the ACCC may wish to consider expanding this principle into the discussion of wholesale cost reductions and the timing of price adjustments, as set out below.

AGL's other specific comments regarding particular concepts and examples in the Draft Guidelines are also set out below.

Underlying cost of procuring electricity

- *Wholesale cost reductions*:
  - AGL agrees with the concept outlined in example 4 of the Draft Guidelines that the relevant cost is the industry-wide, market based wholesale costs incurred by a prudent retailer, and that a retailer who manages to procure a lower cost than this 'benchmark' (eg via a single particularly low-cost hedging contract) will not, of itself, result in the corporation having achieved a sustained and substantial reduction in its underlying cost of procuring electricity.
  - The ACCC does need to consider that a retailer may have a different view on, and methodology for, analysing its cost position. The ACCC should include a further example that elaborates on these principles further, particularly in relation to wholesale costs. For example:
    - while the AER may issue a determination in relation to the DMO reducing costs by a specified proportion, a particular retailer may take a genuinely different view of reductions in its market-based costs and thus reduce prices by a different amount;
    - if there is an increase in costs in a region in one year followed by a decrease the following year, a retailer that decided to absorb a significant proportion of increased costs in the first year should not have to reduce its costs in the second year by the same amount as a retailer that did not absorb any of the initial increase.
    - If a retailer's customers have moved through the year from one product to a lower priced product, that reduction can be factored into the retailer's quantification of its savings resulting from cost reductions.
  - paragraph 2.16 in the Draft Guidelines acknowledges the relevance of the individual circumstances of a particular retailer. It would be helpful if the guidelines could provide further guidance with an example of circumstances which result in many retailers in the industry experiencing a sustained and substantial cost reduction but, for one particular retailer, does not result in a cost reduction. This may arise, for example, because of long term hedging arrangements entered into by that particular retailer or the price for large scale generation certificates acquired by the particular retailer a long term under power purchasing agreements.
- *Sustained and substantial reductions:* paragraph 2.19 notes that the longer a reduction is lasting and expected to last, the more reason there is for a retailer to be considering price changes. It also suggests that the ACCC will recognise that seasonal fluctuations in wholesale electricity costs are not representative of a longer-term trend. AGL notes that there are many factors in addition to seasonality that impact forward prices (and spot prices) and it is often extremely difficult to assess whether these impacts are temporary or likely to have a longer term impact on contract prices. AGL would ask that the ACCC clarify its position in respect the meaning of 'sustained', and its view on more frequent price changes (as set out below) in light of this complexity.

Reasonable adjustment

- *frequency of price adjustments*: paragraph 2.25 and example 9 suggests that the ACCC expects retailers to make price changes outside of its usual price setting schedule if there were cost reductions that were continuing, large and unexpected, and the retailer's next price reset process was not commencing soon. AGL considers out of price cycle changes should be the exception rather than the norm for the following reasons:
  - Firstly, it is important to note that there is ongoing discounting activity in the retail electricity market and the scale of this discounting is a relevant circumstance that should be taken into

account when a retailer is deciding when and how much of a cost reduction it needs to pass through at any point in time to comply with section 153E. In essence, increasing discounts on new offers (ie lowering the effective rate a customer pays on new products) to meet competition is a 'real time' pass through of cost savings. Consumers are free to shop around in between annual price changes to access lower rates, and any industry wide reduction in costs will lead to increasing levels of discounts as competitors use these reductions to improve their offers and attract customers. These real-time pass throughs of reduced costs need to be accounted for when considering both the quantum of the 'saving' to the retailer, and whether a retailer has made reasonable adjustments;

- Second, given fluctuations in wholesale costs, it is likely that a sustained and substantial reduction, or a longer-term downward trend, could only be identified after a period of 6 months (or more) has passed. Example 9 uses the example of an environmental cost but the more complex example relates to a wholesale cost reduction. It would assist to have an example where a retailer identified a downward trend after 6 months but then, just as the retailer commences analysing how to adjust its prices outside of its annual price setting process, wholesale costs start increasing again, with forecasts unclear on whether that trend is set to continue. In AGL's view, it would be reasonable in that situation for the retailer to hold off on making any adjustments and to consider making adjustments only once it reached its annual price setting process;
- Third, price changes require planning, customer communications and system changes. For example, [redacted]. The Draft Guidelines do not provide clarity on what the ACCC considers is a reasonable period of time for a price change after a reduction is established. Example 9 simply states "shortly" but internal analysis and decision-making processes, the need to prepare and issue customer communications, and system changes are difficult to do quickly. The process of giving effect to price changes has become more complicated (and thus time-consuming) with different pricing regulation frameworks in Victoria versus the other NECF states, and the rules around reference pricing and best offer advertising which are designed to ensure greater transparency in electricity pricing and allow consumers to compare plans;
- Fourth, if retailers were to change prices more frequently than once a year, it would likely drive price volatility for consumers – if retailers are obligated to pass through price decreases within 3 months (for example), they will then need to increase prices to reflect any upward movements over a similar time frame. This would seem to be inconsistent with the regulatory framework in the electricity sector that seeks to limit volatility of costs and therefore prices, and price stability has also been a principle of more recent regulatory reforms including the introduction of the Default Market Offer and the Victoria Default Offer, both of which are set annually.

- *Fixed rate contracts*: example 10 in the Draft Guidelines suggest that it would be unreasonable for a retailer to not adjust prices within the term of a fixed rate contract that is longer than 12 months if there is a relevant cost reduction. AGL would strongly encourage the ACCC to reconsider its position on this. The application of the provision in this manner misunderstands the nature of fixed rate contracts in the electricity sector. In particular, AGL notes that:
  - under fixed rate contracts, price volatility risk, including the risk of higher prices, is shifted to from the customer to the retailer. That is, the retailer is contractually obliged to provide electricity at those prices for the term of the contract, irrespective of its underlying cost of procuring electricity, including network costs, and other costs;
  - the retail pricing prohibition does not address increases in supply chain costs. The ACCC's view that retailers should break a fixed rate contract that is longer than 12 months to pass

through cost reductions would introduce a one-way ratchet mechanism that may dissuade retailers from offering such contracts or potentially increase the fixed rate at which they offer the contract to account for the risk of having to pass through a cost reduction alongside the inability to pass on a cost increase;

- most small customers that enter into fixed price contracts for terms beyond 12 months are relatively sophisticated buyers of electricity and have made a decision to lock in a rate for a particular time period to hedge the risk against future price increases, have budgeting certainty and obtain credits and other value-added benefits that can often apply. This length of time is not unusual for consumer contracts in other industries – for example, in telecommunications, where the 24-month term is a standard contract for both mobile and fixed services. Also, home loans are offered with both a fixed and variable rate, with fixed rate home loans having more competitive rates;
- some customers, including some that operate small businesses, value the certainty associated with contracts that fix the price for more than 12 months, as it assists with budgeting. For example, many leases run for a term well beyond 12 months;
- to the extent the ACCC is concerned that consumers will be locked into a fixed rate for a longer than 12-month period when there are cheaper market offers, AGL notes that fixed rate contracts do not always lock the customer into the retailer. For example, AGL's last offered 24-month contract (Essentials Plus) potentially allowed customers to change their plan at any time or leave AGL without an exit fee. Thus customers on a fixed price contract remained free to shop around for a better deal at any point in time.

AGL further notes that from 1 July, retailers in Victoria are required to offer any ongoing financial benefits for the duration of a contract and are prohibited from making any price increases prior to the end of the contract term. These changes were introduced to ensure price certainty and clearer contracting practices[1] – the ACCC's draft approach of requiring a retailer to amend a fixed rate within a contract term appear to run counter to this. It could potentially lead retailers to cease offering longer than 12-month contracts with a fixed rate. AGL therefore requests that the ACCC review its position on fixed rate contracts. **At the very least, the potential impact to retailers is such that the ACCC should only adopt this position in respect of fixed rate contracts entered into post-10 June 2020.**

- *Allocating adjustments between different customer groups and different tariff types*:
  - Paragraph 2.26 in the Draft Guidelines recognises that retailers may pass on cost reductions to different tariff types in different amounts. It would be helpful if paragraph 2.26 could be expanded to identify some of the other characteristics which may be relevant to a retailer's determination of how to allocate cost reductions such that the ACCC will consider them to be reasonable adjustments. For example, it may be that a retailer wishes to:

[1] Essential Service Commission (Victoria), *Ensuring energy contracts are clear and fair – final decision*, 28 February 2020.

- Allocate cost reductions associated with a particular region predominantly or wholly to customers in that region;
- Allocate cost reductions that became apparent to the retailer at a particular point in time to customers on plans entered into prior to that time;
- Allocate cost reductions associated with use of electricity at a particular time of day to customers that on tariffs that have prices specifically applicable to that particular time of day;
- Offset cost reductions against cost increases that are associated with particular tariffs; and/or
- Weight the adjustments toward customers on higher effective tariffs, and not pass through any reduction to customers on the lowest tariffs. Again, as noted above, these customers who are on the lowest tariffs may already be benefitting from higher discounting that a retailer may have been able to make available due to individual cost reductions arising out of efficiency gains or potentially even reductions in the underlying cost of procuring electricity (or both).

In AGL's view, provided the overall quantum of the reduction is passed through in a reasonable manner, a retailer should retain the flexibility to determine how to allocate those cost reductions. This will ensure that retailers are able to still compete on price and differentiate their plans from those offered by other retailers.

– Further, example 12 in the Draft Guidelines reaches the conclusion that a retailer would need to pass through a cost reduction to customers on higher priced offers as well as customers on the more aggressively priced offer. AGL would ask that the guidelines consider the inverse, whether or not it would be reasonable for a retailer to only pass through a cost reduction to the customers on a higher priced offer.

3. Prohibition on failure to offer electricity financial contracts

Section 153F provides that a corporation engages in prohibited conduct if it:

- fails to offer electricity financial contracts;
- limits or restricts its offers to enter into electricity financial contracts; or
- offers to enter into electricity financial contracts in a way that has, or on terms that have, the effect or likely effect of preventing, limiting or restricting acceptance of those offers; and

the corporation does so for the purpose of substantially lessening competition in any electricity market (the **contracting prohibition**).

AGL's submissions regarding this aspect of the Draft Guidelines are set out below.

Lack of liquidity

Paragraphs 3.18 and 3.20 of the Draft Guidelines recognise that a corporation will not engage in prohibited contracting behaviour unless the purpose is to substantially lessen competition, and that purpose is distinct from effect. As a practical matter, liquidity in electricity financial contracts will fluctuate across time, and the

increasing penetration of generation that does not offer financial contracts (such as intermittent renewable generation) is a significant driver of liquidity reduction. It would be helpful if the guidelines made clear that a lack of liquidity in financial contract markets is not of itself sufficient to constitute a contravention of the contracting prohibition by any one or more generators.

Electricity financial contracts

In a practical sense, generators will derive significant benefits from being able to clearly identify which contracts, or potential contracts, are subject to the contracting prohibition. While AGL understands the ACCC's general approach will be to focus on actual, or potential, electricity financial contracts with counterparties who are participants in the electricity industry[2], the Draft Guidelines do not currently provide as much certainty as AGL considers should be possible. Specifically, paragraph 3.7 of the Draft Guidelines does not exclude any counterparties and paragraph 3.5 provides very little practical limitation as to the types of contracts that are covered.

AGL considers that, for the purposes of this prohibition:

- the potential counterparties to an electricity financial contract should be limited to parties who are retailers in the electricity industry and should exclude other parties such as governments and commercial or industrial clients; and
- the types of contracts covered should be limited to those commonly referred to as electricity financial contracts, being derivatives, including futures, floors, caps and collars.

AGL observes that:

- generators consider many potential contracts each year that are not the focus of the contracting prohibition but may nevertheless contain rights that may be derived from or relate to the price of electricity on a spot market. For example, contracts with commercial or industrial customers and contracts associated with government grants and funding for generation projects often contain rights that at least potentially relate to the price of electricity. Such contracts should not be considered 'electricity financial contracts' for the purpose of this prohibition;
- although 'purpose' is also an element of the contracting prohibition, it should not be necessary for a generator to be required to assess this element for every potential contract it considers under which there are rights that may be derived from or relate to the price of electricity on a spot market. As is noted in the Draft Guidelines, there is often considerable complexity associated with assessments of purpose under the Act;[3]
- the rationale for an approach in the guidelines that leaves the interpretation of electricity financial contracts so open is not clear. The EM clearly suggests that the focus of this provision is to address any inability of retailers (as opposed to other parties) to obtain appropriate hedging contracts, with the underlying concern that if retailers cannot access hedging products there is a risk that this will result in a lessening of competition in an electricity market;

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[2] Such approach accords with the Revised Explanatory Memorandum, *Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2019* (**Revised Explanatory Memorandum**), which states, at paragraph 2.61: "This definition is intended to cover the range of derivative contracts that are used by participants in the electricity industry to wholly or partially manage their exposure to spot market prices".
[33] Draft Guidelines, paragraph 3.21, refers to purpose potentially being inferred from conduct of a corporation, its officers or other relevant circumstances.

- for the reasons outlined above, there would be significant practical benefits for generators if the guidelines provided greater certainty and removed any potential application beyond financial contracts as defined between generators and retailers.

Interaction between spot market and contracts

Example 17 in the Draft Guidelines acknowledges that a generator is entitled to engage in conduct for commercial gain by looking across its portfolio, and decide not to sell contracts at the prevailing price if it believes that the present market price does not properly reflect value (provided that it does not have the purpose of substantially lessening competition). AGL considers it would be helpful for the guidelines to confirm that:

- a generator simply seeking to maximise profits in this way is not in and of itself considered to have an anti-competitive purpose; and
- the ACCC would not generally seek to infer an anti-competitive purpose from the circumstances set out in example 17.

It would also be helpful if Example 17 could be amended to clarify that the same principle applies:

- where a corporation ceases to offer contracts that cover a period longer than one-month;
- where Generator A is also a retailer; and
- where Generator A has a portfolio of generation assets,

(again assuming there is no anti-competitive purpose to foreclose competition in the relevant retail market).

Anti-competitive purpose

Paragraph 3.20 clarifies that section 153F is concerned with purpose, rather than effect. Of course, the conduct and decisions of generators will occur before their effect can be assessed. As such, it would be helpful if paragraph 3.20 could confirm that an anti-competitive purpose would not be inferred solely from the fact that a potential consequence of a vertically integrated generator's contracting would be to hinder or prevent another retailer from obtaining its desired hedging position or a particular electricity financial contract.

It would also assist market participants if the ACCC could explain the circumstances in which it would infer an anti-competitive purpose from the conduct of the corporation or from other relevant circumstances, as permitted by section 153J. For instance, in example 21, it would be helpful if the guidelines could confirm that the principle would remain unchanged in circumstances where Retailer B asserts to Generator A that it would not be fully hedged for Quarter 6 without the contract it had sought and Generator A believes this assertion to be accurate.

Counter party concentration

Paragraph 3.33 recognises that the contracting prohibition should not force generators to enter into contracts they otherwise would not have due to legitimate counterparty risk. It would be helpful if this paragraph could also confirm that counterparty risk may arise due to excess concentration of contracts with a particular counterparty.

4. Spot market bidding prohibition

Sections 153G and 153H provide that a corporation engages in prohibited conduct if:

- the corporation:
    - bids or offers to supply electricity in relation to an electricity spot market; or

  - fails to bid or offer to supply electricity in relation to such a market; and
- with respect to:
  - the basic case, the corporation does so:
    - fraudulently, dishonestly or in bad faith; or
    - for the purpose of distorting or manipulating prices in that market; or
  - the aggravated case, the corporation does so:
    - fraudulently, dishonestly or in bad faith; ***and***
    - for the purpose of distorting or manipulating prices in that market (emphasis added) (together, the **bidding prohibition**).

AGL's submissions regarding this aspect of the Draft Guidelines are set out below.

Guidance on the purpose of distorting or manipulating prices

AGL appreciates the discussion in the Draft Guidelines of the various factors that may be relevant to assessing whether a generator's purpose in particular conduct was to distort or manipulate prices. AGL again acknowledges the significant effort the ACCC made in seeking to provide clarity in respect of this highly ambiguous provision. However, the issue is complex, and while the Draft Guidelines provide guidance on a number of scenarios and concepts, it is difficult to extrapolate guidance on the complex and nuanced situations in which participants operate. There is still no articulation of a 'test' that the ACCC will apply, or that a participant can apply to be assured of the ACCC accepting compliance with the provisions. Unless the circumstances mirror those outlined in a particular example, participants will still be in the position of not knowing with any certainty whether the ACCC will consider their bidding behaviour complaint with these provisions or not.

AGL would ask that the guidelines include greater guidance as to practical principles that generators may follow to ensure they are complying with the law. For example:

- Paragraph 4.26 acknowledges the statement in the EM that the bidding prohibition is not intended to interfere with genuine commercial behaviour intended by the design of the spot market. It would be helpful if the guidelines confirmed that the ACCC also takes this view, and as such, that it could be formulated into a 'test' against which generators might assess their bidding conduct;
- Paragraph 4.21 observes that courts, in other contexts, have taken a view that assessing market manipulation involves an assessment of whether conduct results in a price that does not reflect the forces of supply and demand. It would be helpful if the guidelines confirmed the ACCC's view of how this might apply to the circumstances of an energy only market, and confirm that this case law does not, in its view, diminish to any the extent the ability of generators to engage in genuine commercial behaviour intended by the design of the spot market;
- The bidding and rebidding rules in the National Electricity Law (**NEL**), Australian statutes of general applicability and case law suggest that the bidding prohibition is aimed at acts of intentional deception and/or seeking to bid in a non-genuine way to achieve perverse outcomes, with the concept of 'perverse' clearly excluding those outcomes and bidding practices that align with the design of the NEM. AGL would ask that the ACCC consider offering confirmation that its interpretation of the provision accords with this view.
- Example 28 recognises that a generator may bid capacity at levels above marginal cost where such bid may result in a spot price higher than would otherwise have been the case in circumstances where this outcome would allow the generator to recoup some of the fixed costs

associated with its generator. It would be helpful if the guidelines could confirm that a generator may adopt a like strategy in other circumstances intended by the design of the spot market, including for example to optimise its portfolio of assets in a profit maximising way reflective of its contract position;

- Example 29 acknowledges that a generator may rebid capacity into a lower price band to defend a contract position. It would be helpful if this example could also confirm that a generator is also entitled to rebid capacity into a higher price band to defend or optimise a contract position.
- Example 31 observes that a generator claiming a unit is unavailable when that is not the case for the purpose of seeking to profit from any resultant increase in the spot price would contravene the bidding prohibition. AGL accepts this characterisation of the conduct. It would be helpful if the ACCC could consider an example whereby a generator does not claim the unit is unavailable, but legitimately rebids capacity from a unit into a higher price band in the hope that this may result in a higher spot price that would help it to recoup fixed costs associated with that unit, and/or other units operated by the generator. In AGL's view, which also seems to accord with principles outlined in other examples, this conduct would not contravene the bidding prohibition.
- It would be helpful if the guidelines made clear that generators seek to make an economic return on investment over the long term, and that any assessment of generator profitability should:
    - occur over a period of time reflective of the life of the relevant generation assets; and
    - account for the lack of certainty at any point in time that a generator will have opportunity in the future to recover any further component of the fixed costs associated with those generation assets. As is recognised in paragraph 4.24 of the Draft Guidelines, the generation fleet is currently undergoing a major transformation, with a growing share of renewable generation capacity that has a very low marginal operating cost. Other technologies that provide opportunities to reduce costs, including storage, are also growing in importance.[4] This presents very specific challenges to thermal generators recovering their costs and potentially limits the opportunities for them to do so.

Portfolio of generation assets

The Draft Guidelines contain a number of examples of generators operating a single generating system.[5] Paragraph 4.28 of the Draft Guidelines acknowledges that some corporations bidding strategies are conducted at a portfolio level, but does not make clear that the same principles apply. It would be helpful if paragraph 4.28 could make clear that the principles in all of the examples in this section apply equally to a generator, or gentailer, with a portfolio of generation assets. For example:

- the situation in example 26 may result in a generator with a portfolio of assets having peaker plants being dispatched for a small number of hours on each of the three days at prices above the operating cost of those peakers in circumstances when those peakers would not otherwise have been dispatched on those days; and
- the situation in example 28 may result in the generator achieving high prices that assist it not only to recoup fixed costs associated with its base load generator, but also to recoup fixed costs associated with peakers that it operates, but which are rarely dispatched due to high operating costs.

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[4] ACCC, Restoring electricity affordability and Australia's competitive advantage, Retail Electricity Price Inquiry, Final Report, June 2018, page 47.
[5] Examples 23, 24, 26, 27, 28 and 29 in this section of the Draft Guidelines refer to a generator operating a single generating system.

Material conditions and circumstances

Paragraph 4.17 helpfully identifies, in a non-exhaustive list, examples of changes in matters that may constitute changes in material conditions and circumstances. It would be helpful if the guidelines could confirm that this list also includes changes in:

- dispatch prices;
- contract position;
- performance of generating units – eg failure to perform as expected due to extreme weather conditions;
- availability of other assets in a generator's portfolio; and
- interconnector performance.

5. Processes and remedies

AGL appreciates the ACCC's outline of factors that it will consider when taking enforcement actions and considers that the discussion in section 6 of the Draft Guidelines ('Enforcement and Remedies') assists in clarifying how the ACCC will deal with potential breaches of Part XICA. In particular, the availability of an administrative resolution, as for other breaches of the CCA, is helpful as there are likely to be circumstances where there are minor or technical breaches of Part XICA that do not cause any detriment.

That being said, AGL considers that the Draft Guidelines could be amended to provide greater clarity on:

- when enforcement action will be taken against individuals; and
- the ACCC's views on the interaction between the prohibited conduct notice and prohibited conduct recommendation – as AGL has previously submitted, in order to afford corporations greater procedural fairness, the ACCC should consider providing the relevant corporation with a copy of a prohibited conduct recommendation that has been provided to the Treasurer that recommending a contracting or divestiture order.

5.1. Enforcement against individuals

While the Draft Guidelines set out some factors that the ACCC will consider before taking enforcement action, it makes no specific reference to the question of individual liability. Until such time as there is settled law, enforcement action against individuals should only be taken if there is evidence of a flagrant and deliberate disregard of the law.

In respect of the retail pricing prohibition and more technical contraventions of the contracting and bidding prohibitions, the ACCC should take into account whether an individual's actions are predicated on a different and genuine view of compliance with the law and in accordance with legitimate, business-as-usual conduct that has existed in the sector prior to the Act coming into force. Further, there is a question as to the appropriateness of penalising senior individuals for breaches of the retail pricing prohibition, as there can be genuine differences in views as to whether there has been a substantial and sustained reduction in the cost of procuring electricity and the reasonableness of any consequential adjustment (or non-adjustment).

AGL understands there may be other existing ACCC policies that the ACCC could cross-refer to in its Draft Guidelines to more clearly articulate the circumstances in which will take action against individuals. Alternatively, it would assist if the ACCC could include a statement to the effect that the ACCC will be taking a measured approach to enforcement action against individuals, with only the most deliberate and egregious breaches likely to warrant individual liability.

5.2. Prohibited conduct notices and recommendations

As AGL has previously submitted, in order to afford corporations greater procedural fairness, the ACCC should consider providing a corporation the subject of a prohibited conduct recommendation that has been provided to the Treasurer that recommends a contracting or divestiture order (**Recommendation**) with a copy of that Recommendation.

AGL does not consider that the prohibited conduct notice (**Notice**) process in section 153P is sufficient to provide this procedural fairness for a number of reasons:

- First, section 153S(3) provides that Recommendation may differ from recommendations in a prohibited conduct notice.
- Second, the section 153P process simply notifies a corporation that the ACCC considers it has engaged in prohibited conduct which may lead to a contracting or divestiture order and the reasons why the ACCC believes that to be the case. There is no requirement on the ACCC to set out the specific details and evidence that has led the ACCC to this belief.
- Further, while a corporation may make representations to the ACCC following receipt of a Notice (section 153P(2)(f)), there is no obligation on the ACCC to respond to those representations in advance of giving the Treasurer a Recommendation.

The Draft Guidelines do not elaborate on the level of detail that the ACCC is likely to include in a Notice. This is to be contrasted with paragraph 6.45 of the Draft Guidelines, which states that the ACCC will provide the Treasurer with sufficient information, data and evidence to support its recommendation, as well as its views on the appropriate terms and conditions. If the ACCC considers that the Notice should reflect and mirror the contents of a Recommendation, as per AGL's discussion with the ACCC on 24 March, such that there is already procedural fairness afforded, then that interpretation of sections 153P and 153S should be reflected in the Draft Guidelines.

AGL appreciates that ACCC is obligated to give the corporation a copy of a 'no Treasurer action notice' (section 153U), so a corporation will be made aware where its representations resulted in the ACCC deciding no further enforcement action is required. Presumably, if it does not receive a 'no Treasurer action notice', a corporation could assume that the ACCC has given the Treasurer a Recommendation. However, this is a deficient process in light of the seriousness of the potential contracting order or application to the Federal Court for a divestiture order that could follow once the ACCC has given its recommendation to the Treasurer, for reasons that include:

- First, without knowing that a Recommendation has been made to the Treasurer, or its contents, a corporation cannot properly assess the decision to issue the Recommendation, the commercial impact of the potential contracting or divestiture order and its legal options in relation the Recommendation and consequential steps.
- Second, such an approach may result in the corporation being unaware of a Recommendation until up to 45 days after it had been made as a result of the time period in section 153R(1).

To ensure procedural fairness, the relevant corporation should have access to the materials that the ACCC has provided the Treasurer so it understands the case that the ACCC has put to the Treasurer and the terms of the contracting order that could be imposed or the nature of the divestiture order the Treasurer may seek from the Federal Court. At the very least, the ACCC should consider informing when a Recommendation has been given to the Treasurer and what contracting or divestiture terms have been proposed.