# Response to Queensland Productivity Commission

## Draft Report: Electricity Pricing in Queensland

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## Summary

While the terms of reference for the review see the Queensland Productivity Commission (QPC) making recommendations to the Queensland Government, Stanwell appreciates the opportunity to respond to QPC's draft report into electricity pricing in Queensland.

Stanwell welcomes the QPC's recommendations to minimise government intervention and improve structure and reporting relationships with energy GOCs as key initiatives which could reduce market distortions and improve GOC operating efficiencies.

Stanwell also is strongly of the view that the introduction of a code of conduct between GOCs to monitor re-bidding practices could have an adverse impact on competition and add complexity to electricity rules which are already monitored and enforced by a variety of regulators.

## Government Interventions (Recommendations 1, 2, 10, 15)

1 *To ensure the development of an efficient electricity market, the Queensland Government should not favour any technology over another, and allow the market to evolve to meet consumer demand.*

2 *To ensure the development of an efficient electricity market, government intervention should be limited to circumstances of clear market failure, and all government intervention should only occur after there is a clear demonstration that the benefits outweigh the costs.*

10 *In order to achieve least-cost carbon abatement, the Queensland Government should work with the COAG Energy Council to find opportunities for collaboration on carbon policy, as an alternative to pursuing independent action.*

15 *To ensure that national regulatory frameworks effectively respond to the development of new technologies and business models, the Queensland Government should work proactively with the COAG Energy Council on reform in this area.*

**Stanwell response**

Stanwell considers that each of these recommendations encourages good regulatory practice from governments of all levels. Stanwell supports efforts to enhance market design through national harmonisation and cooperation as well as the minimisation of unnecessary government intervention.

## Government Interventions (Recommendations 23, 24, 50)

23 *If the Queensland Government accepts draft recommendation 22, market participants should be advised of the timing of deregulation as soon as possible.*

24 *To support the move to price deregulation and promote greater customer participation in the SEQ retail electricity market, the currently planned customer engagement campaign should:*

- *Provide sufficient advice and information to consumers to assist with comparing offers, and be tailored to address the needs of vulnerable customer groups; and*
- *Provide assistance to non-government group organisations (NGOs) to assist vulnerable and disadvantaged consumers to fully participate in the market.*

50 *The Queensland Government should seek COAG agreement for the administration of energy concessions to be part of the broader Australian Government social security system, to improve efficiency and equity.*

**Stanwell response**

Stanwell considers that each of these recommendations encourages good regulatory practice. Stanwell also appreciates the announcement of impending regulatory changes with a maximum reasonable forewarning in order to allow market participants to incorporate the changes at lowest cost.

## Government Owned Corporation structure (Recommendations 4-6,)

4 *The Queensland Government should not merge CS Energy and Stanwell, given the likely reduction in competition in Queensland's already concentrated wholesale electricity market and the likely consequence of higher wholesale electricity prices.*

5 *The Queensland Government requirement for CS Energy and Stanwell to achieve operating efficiencies should be complemented by a strengthening of the shareholder oversight role to ensure clear targets for improving performance are set and achieved.*

6 *To reduce the combined market concentration of CS Energy and Stanwell, the Queensland Government should confirm that it does not intend to increase the size of the existing Government owned corporation generation capacity.*

**Stanwell response**

Stanwell supports the QPC's recommendation and the State Government's decision not to merge the two state-owned generators.

Stanwell supports the QPC's recommendation for the strengthening of shareholder oversight of the business through the setting of clear financial performance targets which will ultimately deliver improved operating efficiencies. In this regard, Stanwell notes that the Queensland Government is in the process of preparing a shareholder mandate (as per the State Government's Mid-Year Review announcement in December 2015), expected by the end of April 2016, which is intended to provide clear targets for financial performance and efficiency improvement.

The Queensland electricity market is oversupplied until at least 2020/21 and no new generation build is required prior to that date. The Queensland Government should investigate allowing its generators to renew or transition their portfolios to be in line with the market-led transition to a renewable energy led market. Stanwell also anticipates that this will be clarified through its shareholder mandate.

## Large scale Generation (Recommendations 7, 8)

7 *The Queensland Government should require CS Energy and Stanwell to develop and adhere to a common voluntary Code of Conduct (the Code) in respect of their rebidding behaviour. The Code should be developed as part of a public consultation process.*

**Stanwell response**

Stanwell does not consider that the QPC has accurately characterised market design and existing processes in relation to rebidding, and does not support the recommendation. We consider that the Code of Conduct envisaged in the recommendation is likely to be:

- anti-competitive;
- redundant;
- distortionary;
- expensive; and
- inconsistent.

Currently the rules require that generator bids be made with a genuine intent to honour them, and allow for bids to be updated as new information becomes available. In December 2015, AEMC published a final determination on a rule change which replaces these "good faith" provisions with an obligation "not to mislead" through action or omission. These new rules are due to come into effect on 1 July 2016. Throughout AEMC's rule change process, Stanwell consistently supported the principle of clarifying that rebids must be made as soon as reasonably practicable[1].

[1] submissions available at http://www.aemc.gov.au/Rule-Changes/Bidding-in-Good-Faith

**The recommendation is likely to be anti-competitive**

*"The Code would set out, in general terms, the basis upon which each business will decide to submit a rebid to AEMO, pursuant to the NER."*[2]

Stanwell considers that a proposal to have ***any*** two generators reach an understanding, even in general terms, relating to the basis upon which they will submit price and volume offers to the market is inappropriate and is likely to be viewed by the ACCC as anti-competitive.

Stanwell and CS Energy are competitors under the Competition and Consumer Act. This Act prohibits any understanding between the two generators relating to their bidding behaviour.

**The recommendation is redundant**

All generators in the National Electricity Market (NEM) are required to comply with the National Electricity Rules. Large scheduled generators, such as Stanwell, are subject to explicit requirements in relation to the generation offers they present to the market, which are both more onerous than those placed on some of their competitors[3] and carry significant financial and reputational penalty in the event of contravention.

As noted in the QPC draft report, rebidding is (primarily) regulated through the monitoring and enforcement of clauses 3.8.22 and 3.8.22A by the Australian Energy Regulator (AER). Clause 3.8.22A is the only NER clause designated as a *rebidding civil penalty* with an attendant fine of up to $1 million for both corporations and individuals in the event of contravention. No other NER clause attracts a potential fine that exceeds $100,000.

Clause 3.8.22A contains a mandatory behavioural statement of conduct. The proposal to develop a voluntary code of conduct in an environment where a comprehensive mandatory code exists is extremely unlikely to alter behaviour or increase market confidence.

**The recommendation is likely to be distortionary**

The proposal to develop a guide to rebidding conduct and publish it on Stanwell and CS Energy's websites in order to increase market confidence implies that other parties (including competing generators) would be able to rely on that guide in evaluating their individual strategies. The ACCC has previously expressed concerns about such 'signalling' behaviour, and its potential to damage competition. The Final Report of the recently competed *Competition Policy Review* (the Harper Review) stated, at page 368:

> *'Price signalling has the potential to harm the competitive process. Competitors may be able to use the disclosure of price information as a means of co-ordinating their pricing decisions. Depending on the form of price signalling and the market circumstances, price signalling may reduce the commercial risks for competing firms to engage in co-ordinated behaviour and thereby increase the likelihood of anti-competitive pricing outcomes.'*

Assuming that such a document could be legally and practically developed, making such a representation would risk distorting market expectations, particularly where two or more generators were to make such representations.

Strategy documents or behavioural indicators which are formed at a high level also provide significant scope for subjective interpretation, especially in relation to a market as complex as the NEM. Because of this subjectivity, either rebidding action or inaction by the code signatories could be interpreted by other parties as not being aligned with the code, perversely decreasing rather than increasing market confidence.

**The recommendation will be expensive**

The proposal to have representatives of each company - as well as interested parties and regulators – publicly consult is likely to be expensive and time consuming. Representatives are likely to be relatively high-level employees covering a range of areas from market expertise,

[2] *Electricity Pricing Inquiry draft report*, QPC, page 50

[3] Non-scheduled generators and loads are not required to submit offers to the market operator.

physical plant knowledge, stakeholder relations and legal. Given the likely lack of benefit and the questionable legality of such a process, Stanwell does not consider such expense efficient.

**The recommendation is inconsistent**

As a Government Owned Corporation, Stanwell's activities are overseen by a Board of Directors that is appointed by its two shareholding Ministers; the Queensland Treasurer and the Queensland Minister for Energy and Water Supply.

Stanwell's independent Board oversees the operations of Stanwell so that it is compliant with the Government Owned Corporations Act 1993 (Qld), the Corporations Act and the relevant laws associated with operating within the NEM.

The key principles of corporatisation for the government owned generators mandate that they must set clear performance targets, operate commercially (and on equal terms with private sector operators) to achieve those targets and that they must be enabled to operate autonomously from shareholders under the guidance of their independent Boards.

The QPC recommendation is inconsistent with these principles of corporatisation.

The recommendation is also inconsistent with the QPC's own work which recommends:

*To ensure the development of an efficient electricity market, government intervention should be limited to circumstances of clear market failure, and all government intervention should only occur after there is a clear demonstration that the benefits outweigh the costs.*

There is no evidence of clear market failure. Indeed there is significant evidence that the market is working as intended. Further, the benefits of the proposed intervention clearly do not outweigh the costs, as addressed in response to recommendation 8 below.

*8 The Queensland Government should require CS Energy and Stanwell to report to the Government, on an annual basis, all late rebids submitted to the Australian Energy Market Operator. This report should be audited by an independent body, and the findings of the audit made available to the public.*

**Stanwell response**

Stanwell opposes this recommendation as it:

- represents poor regulatory practice;
- is redundant; and
- is discriminatory.

"Late rebids" is a concept which has arisen only recently – during AEMC's consultation on the good faith rebidding rule change proposal. Stanwell has repeatedly expressed concern that the term 'late rebids' risks misrepresentation, and believes that this recommendation confirms our concern.

"Late rebids" will be defined in the National Electricity Rules (NER) from July 2016 relating solely to the time at which the rebid is entered in market systems relative to the first dispatch interval to which changes are made. The AEMC review highlighted that it was not whether a rebid occurred close to dispatch or not which was of concern, but a delay between the formation of the intent to rebid and the actual submission of the rebid[4]. Accordingly AEMC's Final Determination places a new obligation on generators to enter rebids as soon as practicable after they become aware of a change in circumstances, in addition to the existing requirement to have the capability and genuine intention to honour the bid. It is this new obligation which is intended to increase confidence in the market. AEMC has also recommended enhanced record keeping requirements for "late rebids" which is intended to aid the regulator in its analysis and enforcement. As noted in

[4] AEMC 2015, *Bidding in Good Faith, Final Rule Determination*, 10 December 2015, Sydney
"*The existing good faith provisions do not prohibit a generator submitting an offer, in the knowledge that it may be honoured, but then subsequently changing its intentions for dispatch without reflecting those intentions in a rebid as soon as practicable.*"

the QPC draft report, these arrangements have not yet formally come into effect and Stanwell is currently in the process of upgrading systems to ensure compliance with these requirements

**The recommendation represents poor regulatory practice**

AEMC investigated the possibility of mandatory reporting in relation to "late rebids", however, chose not to implement this as such reporting would have a significant cost which outweighs any potential benefit. The QPC is now proposing to require specific participants to incur this inefficient cost with no identified additional benefit. Stanwell considers this to be poor regulatory practice.

**The recommendation is redundant**

In 2004, Queensland joined with other jurisdictions to establish the AEMC and AER to assume responsibility for the regulation of the NEM at a national level. It appears that the QPC is now proposing to re-insert the State of Queensland into the regulation of the national market through additional measures relating to re-bidding in the Queensland region of the NEM.

Under the NER, the AER has the right to require the furnishing of information relating to rebidding. In addition, the rule changes due to commence in July 2016 require participants to retain additional information in relation to rebidding which must be available to the regulator, if requested. The ability for the AER to investigate any rebidding of interest provides sufficient market oversight. This comprehensive coverage by the AER will not be enhanced by the QPC's recommendation of infrequent third party analysis of an arbitrary subset of this information.

Stanwell also considers that the proposal to have the independent auditor publish a report is redundant when considered in light of the regulators' existing reporting and ability to directly undertake enforcement action. Rebid reasons are currently available the day after they occur[5] with both AEMO and AER producing event reports in relation to extreme prices in addition to AER quarterly compliance reports and additional commentary. AER also works directly with market participants to support ongoing compliance and/or initiate enforcement action as necessary. It is unclear what value an auditor could add to these arrangements.

**The recommendation is discriminatory**

The proposal to place additional, costly regulatory burdens on Stanwell and CS Energy is discriminatory and places these generators at a commercial disadvantage compared to competitors. The proposal is justified in the draft report as being related to common ownership and market share.

The notional link between market share and the need for additional requirements is weak. As presented in the draft report, the combined market share of Stanwell and CS Energy in Queensland is only marginally higher than that of AGL and Origin Energy in NSW (63 per cent vs 56 per cent) and the combined market share of the largest three generators in each state is all but identical (Qld 74 per cent vs NSW 75 per cent).

As noted in response to recommendation 7, Stanwell and CS Energy are separately corporatised and managed companies. They are treated as competitors under the Competition and Consumer Act and regard themselves as such. They should not be considered as a combined entity any more than two privately owned or listed companies would be as this is against the spirit of corporatisation.

It is also notable that the recommendation does not apply to the Government Owned Corporations Ergon and Energex which own or control generation and load curtailment, much of which is not subject to NER rebidding rules and as such is less transparent than the activities of scheduled generators.

The proposal to single out Queensland's government owned generators for these additional regulations is contrary to the principle of competitive neutrality. While these principles are usually concerned with eliminating advantages enjoyed as a result of public ownership, the 1994 Competition Principles Agreement, to which Queensland is a party, states:

[5] AEMO publishes all rebids in the infoserver database at the end of each trading day (4am).

*"The objective of competitive neutrality policy is the elimination of resource allocation distortions arising out of the public ownership of entities engaged in significant business activities.'*

The proposals flagged by the QPC seem to introduce the very distortions that the competitive neutrality principles are designed to eliminate.

## Shareholder interests (Recommendation 20)

*20 The Queensland Government should consider a simplification of reporting relationships with the GOCs and adopt an active best practice approach as the Government shareholder.*

**Stanwell response**

Stanwell believes its reporting requirements should be more closely aligned to a company with ASX reporting obligations i.e. updating shareholders through appropriate market channels every six months. This relieves Stanwell from monthly and quarterly reporting requirements and improves the overall efficiency of the business. Capital expenditure items such as statutory overhauls could be approved by shareholders through the endorsement of a GOC's annual Statement of Corporate Intent.