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Australian Energy Regulator
GPO Box 3131
Canberra ACT 2601

Electronic Submission

Enhanced Wholesale Market Monitoring and Reporting Guideline Issues Paper

Snowy Hydro welcomes the opportunity to comment on the Issues Paper for the Enhanced Wholesale Market Monitoring and Reporting Guideline (Issues Paper).

Snowy Hydro Limited is a producer, supplier, trader and retailer of energy in the National Electricity Market and a leading provider of risk management financial hedge contracts. We are an integrated energy company with more than 5,500MW of on-demand generation capacity. We are one of Australia's largest renewable generators, the third largest generator by capacity and the fourth largest retailer in the NEM through our award-winning retail energy companies - Red Energy and Lumo Energy. We are one of the NEM's largest investors in wind and solar power purchase agreements, helping to underwrite more than 2GW of new variable renewable energy capacity.

Guiding Principles

Snowy Hydro supports the AER's principles for collecting information to perform its enhanced functions: ie.

- 1. We will collect information that is reasonably required for the purpose of performing our wholesale market monitoring functions under the energy laws.*
- 2. We will maximise benefit for the market and ultimately consumers by being clear about the specific use of information we collect.*
- 3. We will seek to limit participant burden.*
- 4. We will, where reasonably practicable and appropriate to do so, rely on public information and/or information collected by other agencies (including in our public reporting).*

Snowy Hydro further supports the AER's proposal to "take a targeted incremental approach to collecting information to perform our expanded powers and we intend to prioritise collecting information that will inform key areas of focus."

The need to take a targeted, incremental approach is particularly important given the structural changes underway in energy markets, which has been accompanied by a significant increase in compulsory information reporting requirements. While Snowy Hydro supports the goal of greater transparency and openness, compulsory information

reporting and disclosure requirements create additional resourcing and compliance costs for market participants. It is important, therefore, that reporting requirements are designed so that the costs are proportionate to the benefit obtained.

In this submission Snowy Hydro comments on the collection of over-the-counter (OTC) contract information generally and the burden on market participants associated with the production of that information.

OTC Contracts

As acknowledged in the Issues Paper, contracts are a critical part of wholesale electricity and gas markets and are an important determinant of economic outcomes for market participants. Electricity and gas can be contracted via futures contracts or OTC contracts; market participants frequently use a combination of both. A key distinction between the two market structures is that futures markets are transparent. As such, reporting bodies already have access to detailed information about activities and outcomes in the futures market.

While OTC markets are not typically visible to third parties, in practice pricing outcomes for OTC contracts closely mirror those in futures markets. The reason for this is that market participants have a strong incentive to arbitrage away any differences between the two markets. Indeed some market participants, such as hedge funds and financial institutions, actively seek out such arbitrage opportunities. This means that futures contracts and OTC contracts, for a given product type, do not differ systematically in their pricing. Furthermore, electricity and gas are marginal markets. This means that the traded price will be set by the marginal supplier; the price at which participants buy and sell the commodity will reflect the cost of marginal supply. It follows, therefore, that the marginal supply is a reasonable proxy for the price at which a commodity is being traded within the market.

Snowy Hydro considers that the close pricing outcomes of futures and OTC markets should inform the AER's approach to information gathering. That is, for many, if not most, contract or security types, production of OTC data is likely to yield little meaningful information beyond that which can already be obtained from futures markets. Given the additional resourcing burden associated with the production of OTC contract data, Snowy Hydro considers that its collection should be minimised to the extent reasonably possible (see below).

Participant Burden

Snowy Hydro supports the AER's principle to limit the participant burden associated with the use of its information gathering powers. As mentioned, compulsory information disclosure requirements for market participants have increased in recent years. While it may have been possible, initially, for market participants to absorb the cost of data gathering and production within existing resourcing arrangements, the continuing increase in the reporting burden means that for many businesses this will no longer be

feasible, and that dedicated, additional resourcing is required to perform this task. Furthermore, given the time taken to collate data, reporting timelines invariably overlap with internal reporting requirements, drawing resources away from completing other tasks such as half and year end financial reports.

An additional layer of mandatory reporting and data collection would also increase the risk of operating in the competitive market and hence new investors would incorporate a higher risk premium for new entrant generation plant. The regulator should properly assess any situation that would warrant collecting confidential data, understand the risks and costs associated with its collection and clearly identify the use of the data.

- **OTC Data**

Production of OTC data can be particularly resource intensive and time-consuming. The process of responding to information requests for such data is not simply a matter of identifying the relevant contract and disclosing the requested details to the reporting authority.

Take, for example, a structured OTC electricity contract. Such a contract will usually take the form of a confirmation executed under an ISDA Master Agreement. That ISDA Master Agreement may have been amended on multiple occasions, through variations and/or restatements. It may also have been novated to another party. It may be subject to a third party security arrangement, which has the practical effect of amending its contract terms. The confirmation which records the specific transaction may also have been amended on one or more occasions. In short, the terms and conditions of an apparently straightforward OTC transaction may be spread over a number of separate legally-complex contract documents, frequently totalling hundreds of pages.

- **Confidentiality Provisions**

Most OTC contracts are subject to express confidentiality provisions. Even when reporting requirements are mandatory and have the force of law (and therefore override contractual confidentiality restrictions), confidentiality provisions usually require a counterparty to be notified of the request. This imposes additional administrative requirements before the documents or information can be produced.

- **Power Purchase Agreements**

Although usually transacted under ISDA Agreements, there are some important differences between power purchase agreements (PPAs) for new wind and solar projects and standard OTC contracts. Most new wind and solar projects in the NEM are developed under project finance arrangements, through a special purchase vehicle. The PPA is the key instrument which underwrites the project. PPA contracts are, therefore, more complex because they must deal with both the project and planning risk of a new asset build (given the PPA effectively underwrites the construction of the asset, they must be struck before even a final investment decision has been made), as well as the

sale of energy and, where applicable, green products. In Snowy Hydro's experience, planning and approval uncertainty and delays means PPAs are typically amended on multiple occasions before the project is even commissioned and generating electricity. Again, this adds to the complexity of the documentation.

Responding to Information Requests

In Snowy Hydro's experience, the complexity of OTC contracting arrangements means that responding, for example, to a compulsory information request in relation to a multi-year OTC contract can require tracing through half a dozen or more contract documents. While the initial task of data gathering may be performed by a firm's trading function, the legal complexity of contract documents usually means that a review by a legally-qualified person is required before the requested information can be submitted. Smaller market participants may not have an in-house legal function and will need to engage external lawyers to assist responding to the request. Furthermore, all but the very smallest market participants will have contractual relationships with a number of counterparties, multiplying the volume of contracts responsive to compulsory information requests.

Larger participants are better able to accommodate this resourcing burden, but the task of responding to information requests adds to costs for all market participants, large and small. At a time of high energy prices, it is critical that cost imposts on market participants are minimised to the extent reasonably possible. Ultimately, an increased cost of business will put upward pressure on energy prices.

Collection Framework

With the above considerations in mind, Snowy Hydro recommends that OTC data is collected only to the extent that no comparable publicly traded market data exists, or where it does exist, it should be obtained only in order to reference/ benchmark public market data. The AER should first explore all existing sources of information before making requests from market participants. Furthermore such data should not be collected at a frequency of greater than once per year and historical data should not be sought for more than two years' prior.

The AER's market monitoring should be clearly separated from its compliance and enforcement functions. Snowy Hydro considers that current information gathering powers under the National Electricity Law and National Gas Law are adequate to support investigations of potential breaches of the law and rules, and that data should not be collected under the market monitoring function for enforcement purposes. Utilising information compulsorily gathered under the guise of market monitoring for the enforcement would undermine trust in regulators' information gathering functions.

Finally, Snowy Hydro does not support exempting smaller market participants from reporting requirements. It would be inequitable for market participants to be subject to different reporting requirements and the reporting thresholds would inevitably be

arbitrary. The solution is to avoid unnecessarily burdensome reporting requirements in the first place, allowing consistent reporting requirements for all market participants.

Snowy Hydro appreciates the opportunity to respond to the AER on this matter.