25 January 2019

EnergyAustralia
LIGHT THE WAY

Senate Standing Committee on Economics
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Dear Sir / Madam

Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018

EnergyAustralia is one of Australia's largest energy companies with approximately 2.6 million electricity and gas accounts in New South Wales, Victoria, Queensland, South Australia, and the Australian Capital Territory. We also own and operate a multi-billion-dollar energy generation portfolio across Australia, including coal, gas, solar, wind and battery assets in the National Electricity Market (NEM).

We welcome the Committee's Inquiry into the *Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018* and the opportunity to make a submission. We encourage the Committee to closely scrutinise the Bill, informed by stakeholder submissions, as the Bill is likely to increase power prices for Australians and will lessen competition.

We hope the Committee will make the most of this opportunity to address the many problems identified by EnergyAustralia and others to date with the Bill, given their far-reaching negative consequences for Australians.

The Bill seeks to establish new electricity sector specific forms of prohibited conduct and penalties in the *Competition and Consumer Act 2010* (CCA) and, in a move that has received very little public attention since the Bill's introduction to parliament, will give the Australian Energy Regulator (AER) powers to set default retail electricity prices, overriding traditional State government responsibilities. The proposed legislation should not be taken lightly and warrants significant and in-depth public and industry consultation which has been largely absent to date.

Notably, our concern is that this Bill, if enacted, will not overcome the fundamental shortcomings of Australian energy markets created by the absence of a stable, consistent and integrated energy and climate policy. EnergyAustralia has long argued for a long-term policy to reduce carbon emissions from the sector, such as the National Energy Guarantee (NEG) to support investment in reliable and cleaner forms of energy at least cost to consumers.

The absence of a stable long-term policy only stalls necessary investment to bring prices down for customers. According to the Energy Security Board (ESB), they quantified that customers could save up to $550 a year to 2020[1] if the NEG were implemented.

[1] Energy Security Board, 'National Energy Guarantee: Final Detailed Design', 1 August 2018, p.1

What is absent and required in this Bill, are the policies that will increase investor confidence. This confidence is paramount so companies, like EnergyAustralia, can make decisions to invest in the new and replacement electricity generation that is needed to lower prices for consumers. The Australian Energy Market Operator estimates that this investment will cost between $8 billion and $27 billion over the next two decades[2]. However, adverse actions, such as the proposed *Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018* only discourage the required future investment that Australia needs.

A longer-term energy plan that enjoys broad stakeholder support such as the NEG is what is needed, not hastened distractions such as this Bill. The NEG would obligate retailers to invest in cleaner and reliable energy generation, increasing supply to put downward pressure on electricity prices.

Additionally, at the request of the Federal Government, the Australian Competition and Consumer Commission (ACCC) undertook an extensive review of the energy sector concluding in 2018 and made a range of sensible recommendations in its Final Report. The ACCC forecast that if all its recommendations were accepted customers could save up to $414 per year[3]. Yet, few of these recommendations have been implemented by governments (Federal or State) and this Bill is no substitute for well-considered actions recommended by respected experts that could deliver real savings to customers.

While we hope governments take action to deliver the above-mentioned savings to customers, EnergyAustralia has already taken significant action totalling more than $100 million to improve affordability for our customers. The majority of our actions have enduring benefit for customers and include:

- Automatically applying 15 per cent discounts on electricity and gas usage for eligible EnergyAustralia concession-card customers (such as pensioners, veterans and healthcare-card holders) on default or "standing offer" tariffs.
- Decreasing or holding electricity prices flat for EnergyAustralia customers in 2018/19 despite the costs of procuring electricity and other input costs increasing.
- Investing an additional $10 million in measures to support financially vulnerable customers, including waiving $1.8 million of energy debts for around 1,000 vulnerable customers.
- Ensuring all customers enrolled in the EnergyAustralia hardship program on a default tariff will pay a rate equivalent to the company's best generally-available post-discount price (i.e. no EnergyAustralia hardship program customer will pay standing offer tariffs for their electricity or gas).
- Introducing *Secure Saver* in 2017, a product which offers customers certainty by ensuring that their electricity and gas rates won't increase for two years.

[2] Australian Energy Market Operator, Integrated System Plan, July 2018, p.5
[3] Australian Competition and Consumer Commission, Retail Electricity Pricing Inquiry—Final Report, 11 July 2018, p.xv

Prohibited Conduct and Penalty Regime

EnergyAustralia opposes the proposed prohibited conduct and penalty regime as outlined in the Bill. The Government has offered no credible evidence that such serious interventions are necessary or that existing remedies within the national energy laws and the CCA are inadequate.

To the contrary, measures included in the Bill, such as the forced divestiture of company assets, were expressly considered and rejected by the ACCC in its 18-month review of the electricity sector as they were not considered to be in the best interest of customers. The ACCC stated on page 89 of its report that:

> *"Requiring the divestiture of privately owned assets is an extreme measure to take in any market, including the electricity market...*
>
> *"...the ACCC considers that the other recommendations made in this report will, if implemented, be a better means to restore competition to a level which serves consumers well.*
>
> *"...the ACCC does not believe it would be appropriate to intervene to unwind the way in which the market has evolved across the NEM".*[4]

Other parts of the Bill are also inconsistent with the findings and advice of the ACCC that did not identify any evidence of widespread misconduct occurring. We encourage the Committee to closely review the ACCC Final Report.

Should the ACCC identify misconduct as part of its ongoing electricity price monitoring Inquiry[5], it is our view that existing prohibitions and remedies in both the CCA and energy regulation are better equipped to respond to such behaviour.

Each of the new definitions of 'prohibited conduct' and the proposed penalties will also have a significant detrimental impact on investment in the energy sector. They have been poorly constructed and as a result will create significant uncertainty for energy companies in everyday operations. This will, in turn, add risk and cost to business and limit product innovation and retail competition. The culminating effect will be increased cost and less choice for consumers, which we understand to be opposite of the Government's intention.

EnergyAustralia also continues to have concerns about the risk that the contracting and divestiture orders. It may result in the acquisition of property on unjust terms and muddies the separation of powers doctrine by allowing the Treasurer to exercise quasi-judicial powers to punish alleged breaches of the law through contracting orders. We believe these matters may be challenged in the future, including on constitutional grounds, which will only add further uncertainty to the new penalties and enforcement regime.

Retail Pricing Powers

The retail pricing powers contained in the Bill provide the Australian Energy Regulator (AER) with powers to set default electricity prices (through a regulatory instrument that is not subject to Parliamentary scrutiny), in the form of a Default Market Offer (DMO).

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[4] https://www.accc.gov.au/system/files/Retail%20Electricity%20Pricing%20Inquiry%E2%80%94Final%20Report%20June%202018_0.pdf
[5] https://www.accc.gov.au/regulated-infrastructure/energy/electricity-market-monitoring-2018-2025

EnergyAustralia is concerned the precedent this sets in terms of the Commonwealth taking over responsibility for electricity prices from state governments through the setting of a default market offer that will see a small number of customers better off, but substantially more customers made worse off through lower discounts.

This concern is shared by the Australian Energy Market Commission (AEMC) which recommended to the Council of Australian Governments (COAG) Energy Council in December 2018 that, if implemented, a DMO should be developed as a reference rate[6] only, rather than as a price cap. This is also the view of State and Territory Ministers who have agreed to work on establishing a reference rate via the National Energy Retail Law and Rules.

The AEMC found that the DMO has the following risks:

- An increase in prices for at least some customers on market offers;
- An increase in standing offer prices for those that are currently set below the cap;
- A decrease in the range of offers available in the market;
- Lower levels of innovation as 'discounts off the standing offer' become the most common offer;
- Higher barriers to entry for new retailers, as well as changes in consumer behaviour, resulting in decreased competition in the energy retail market and ultimately higher average prices for consumers[7].

EnergyAustralia endorses a reference or comparison rate and has long argued that it will reduce customer confusion and assist customers ability to compare offers on an "apples for apples" basis. Making products comparable will give customers the confidence to engage in the market and find the best deal for their circumstances.

Given there is support from COAG Energy Ministers and industry for a reference rate, and it is best implemented via the National Energy Retail Law and Rules as with other retail energy obligations, there is no discernible reason why such powers should be created in the Bill. We, therefore, suggest that the Committee recommend these provisions are removed from the Bill, if it is to proceed.

Consultation

The consultation process in developing the Bill has been far from adequate. Only three business days' consultation was provided on the draft legislation. This is despite it being a new kind of legislation in Australia, extremely complex and likely to have serious ramifications for investment in the energy sector and across the economy.

Furthermore, the Regulatory Impact Statement (RIS) prepared was only released once the legislation was tabled in Parliament. It was narrowly focussed, didn't assess all the costs and fell well short of what can be expected from the *Australian Government Guide to Regulation*[8]. The RIS also failed to quantify the likely freeze on investment this Bill (if passed into law) would create, thereby significantly understating the true cost of this legislation.

[6] A rate at which all market offers must be referenced to for advertising purposes.
[7] Australian Energy Market Commission, Advice to Standing Committee of Officials on default offer, 10 December 2018
[8] Department of Prime Minister and Cabinet, 'The Australian Government Guide to Regulation', March 2014

EnergyAustralia and other stakeholders provided extensive feedback in relation to both the initial consultation paper and draft of the Bill. Very few of our earlier comments have been adopted by the Government in the current Bill. We also note that the Government did not publish the submissions received on the initial framework and Bill, limiting public debate and discussion of the Bill.

Upon tabling the legislation in Parliament, the Government added Schedule 2 to the Bill (AER information gathering powers) which had not been consulted on prior to its introduction. These are serious and complex matters that deserve public scrutiny and proper consideration.

Based on the significant number of drafting errors and vague nature of some sections it is clear this Bill has been rushed.

The approach taken by the Government raises some serious questions about the legitimacy and integrity of the Bill.

It is imperative that the Committee thoroughly examine the details of the Bill, given the Government's process to date has not allowed this to occur. This should include hearing from experts from the ACCC and the energy market bodies[9] to test whether they think the Bill has appropriately responded to their findings and recommendations.

As the Handbook highlights, a failure to do so can lead to unintended consequences. In this case, those unintended consequences may be increased costs for electricity customers and reduced investor confidence, which have broader impacts for the Australian economy.

Conclusion

Ultimately, EnergyAustralia is concerned this counterproductive Bill will drive up power prices for consumers, inflame the energy market crisis in Australia due to the lack of policy certainty and if this Bill becomes law, will seriously detract from future product innovation, technological advancements and asset investments in the energy sector. We strongly urge the Committee to actively consult with industry and independent market bodies, and to reconsider the merits of this Bill.

On the tactic of applying "big sticks", we find it disappointing that this unmerited avenue of government intervention is being considered, let alone exercised. This Bill is no substitute for a long-term integrated energy and climate policy, such as the NEG.

The following submission outlines our numerous concerns with the Bill which we urge the Committee to consider further in making its recommendations to the Senate.

[9] Australian Energy Market Commission, Australian Energy Market Operator, Australian Energy Regulator, Energy Security Board

Should the Committee require any further information regarding this submission, please contact Lisa Gooding on [redacted]

Regards

Catherine Tanna
Managing Director

EnergyAustralia submission to Senate Economics Legislation Committee Inquiry into the Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018

25 January 2019

1. Introduction

EnergyAustralia has many concerns with the Bill. These are outlined in some detail in this submission. EnergyAustralia believes that the Committee should be made aware of the many shortcomings of the Bill, while the Committee is able to influence its contents.

Our concerns can be summarised as follows:

The Bill will further de-stabilise the Australian electricity market, that is already under the strain of years of poor government policy.

It introduces some of the most significant remedies possible under the CCA for prohibitions that are vaguely (or not at all) defined and can be recommended by the ACCC based on the low threshold of a mere "reasonable belief" of misconduct and limited rights of appeal for Treasurer ordered remedies.

This will create uncertainty and confusion. Given the significant penalties attached to the new prohibited conduct, the Government must take the time now to ensure that the Bill is clear, unambiguous and contains a brightline test (a clearly defined rule or standard composed of objective factors, which leaves little or no room for varying interpretation) so that retailers and generators are able to confidently run their business without fear of inadvertently transgressing the law.

It represents a significant incursion into the rights of private enterprises to run their businesses. The Bill allows the Treasurer, an elected official with close ties to a competing generator, to reach in and intervene in the operations, pricing and contracts of companies in a way rarely if ever seen before in Australia. What other market in Australia is subject to laws that dictate which of its upstream cost savings must be passed onto its customers and casting doubt over whether its retail costs can be taken into account or recovered? Or to allow the Treasurer to step in and perform the role of an energy trader to set the terms, volume, price and duration of energy contracts that it must offer? Or for the Treasurer to apply to a court to order that a company be split up and its assets sold off (with unknown impacts on the organisations or the market) for such misconduct. Even the most egregious breaches of misuse of market power or cartel provisions under the CCA do not carry such consequences.

The ACCC did not find widespread evidence of this prohibited conduct in the market. Nor were these changes recommended by the ACCC in this form. In fact, the ACCC expressly rejected the need for divestiture powers and labelled them "an extreme measure". Other distinguished competition experts such as Ian Harper have also argued against including sector specific competition laws in the CCA. Accordingly, there is no demonstrated need for the Bill (and almost certainly no urgency identified that would warrant or explain the hurried attempts we have seen to pass this Bill).

More importantly the Bill will not deliver the energy policy certainty or cheaper and more reliable energy that Australians are calling for.

The Government has rushed this Bill through, under shrouds of secrecy and without allowing proper scrutiny or debate by the parliament, industry, economists and competition and constitutional experts and without fully understanding the impact of the laws on the market, customers and the Australian public. It will also create significant uncertainty for both local and international investors.

2. Prohibited conduct

2.1. Retail pricing prohibition

No case for action

The Bill seeks to prohibit a corporation from failing to make reasonable adjustment to the price of electricity it offers or supplies to small customers to reflect sustained and substantial reductions in its underlying costs of procuring electricity.

This is an extraordinary and unprecedented intervention into the business decisions of a private enterprise.

However, it is unclear on what basis the Government has formed a view that this is a problem that warrants the prohibition proposed in the Bill. The ACCC did not identify a failure by retailers to pass on reductions in the costs of procuring electricity to consumers as an issue in its review of electricity markets. We are not aware of any other regulator or expert calling for such an intervention into retail pricing.

The ACCC identified the major causes of price increases over the last decade to be increases in network costs (in part driven by excessive reliability standards set by state governments), increases in government green schemes costs and the abrupt exit of large fossil fuel generators as the result of a changing generation mix in the NEM[10]. The ACCC made 56 recommendations to address the issues it found and a prohibition of the type proposed in the Bill was not one of them.

In summary, the retail pricing prohibition is seeking to solve a problem that does not exist and will likely increase costs for customers and reduce retail competition and innovation (discussed further below).

Further, EnergyAustralia has several specific concerns with the retail pricing prohibition as currently proposed:

1. It is vague and uncertain which will add to the costs of compliance for retailers

2. It fails to reflect how electricity retailers *actually* set their retail prices. (notwithstanding the Explanatory Memorandum's effort to say otherwise).

3. It will have unintended consequences for energy consumers (for example, reduced competition and innovation).

4. The interaction with a default market offer and other state regulation is unclear.

Each concern is further discussed below.

The Bill is drafted in vague and uncertain terms

A breach of this prohibition carries the same pecuniary penalties as would apply to other breaches of Part IV of the CCA. These are some of the largest penalties available under Australian law.

However, as drafted, it is extremely difficult to determine whether or not retail pricing conduct would be prohibited.

[10] Australian Competition and Consumer Commission, Retail Electricity Pricing Inquiry—Final Report, 11 July 2018, pp.i-xxv

The Bill does not define:

- What is "a reasonable adjustment"?
- What is the relevant "price" of the electricity offers?
- What are "sustained and substantial" reductions?
- What is the "underlying cost of procuring electricity"?
- How soon do the price reductions need to be made?

This creates the untenable situation where a corporation, operating in a highly competitive and dynamic retail environment, is exposed to serious financial penalties for breaching a standard of conduct that is ill-defined. This means that the responsibility for interpreting the laws will fall to the Courts, which can take years and in the meantime stifle competition and innovation.

While the Explanatory Memorandum goes to some lengths to attempt to define what is intended by this prohibition (again, confirming the vague and uncertain drafting adopted by Treasury), this is of little comfort to energy retailers, given that those guiding principles do not appear in the Bill and therefore are not required to be taken into account by the regulator, the Treasurer or the courts in enforcing these provisions.

Specifically, EnergyAustralia is concerned that the Bill would require retailers to reduce their retail electricity prices even in circumstances where the overall costs of supplying electricity to consumers have increased (for example due to an increase in retail or other costs that offset the reduction in wholesale costs). The Bill should be amended so that regard must be had to any increase in the overall costs of *supplying* electricity to customers.

The Bill also does not reflect the complexity of setting prices based on forecast demand and costs.

The Explanatory Memorandum also suggests that the application of the law (for example, what would be considered a "reasonable adjustment") will differ depending on the retailer's circumstances. EnergyAustralia sets retail prices based on wholesale market prices and is indifferent to our ownership structure. The ACCC acknowledged this in its discussion of 'transfer pricing' (the price a generator sells electricity to its retail arm at)[11]. It is unacceptable that a law that has such significant consequences will be applied inconsistently across retailers, thereby creating an uneven playing field and distorting competition.

To work, the law must be capable of being clearly applied to any given conduct or express defences that can be relied upon by all retailers, especially where there are serious punitive consequences if the law is breached.

The Bill should also make clear, on its terms, that retailers are not required to pass through savings that would undermine a retailer's viability or risk management strategies. The Bill does not define what "price" must be reduced to reflect reductions in underlying costs. Discounting is very common feature of electricity retail market. Retailers often adjust the discounts or offers promoted each quarter, based on their retail strategy and business performance.

[11] Ibid. p.125

It is not clear from the current drafting of the Bill if the retail "price" that must be adjusted is the price before or after any discounts are applied – and how more novel pricing options offered by some retailers, such as fixed rate plans, prepaid plans, "low rate" plans where the discount is built into the base rates or customised pricing plans based on customers' expected usage should be treated. If a retailer increases their advertised discounts for a quarter to win customers, and wholesale energy costs decrease at the same time it could lead to an unsatisfactory result where the retailer is required to further reduce an already heavily discounted price and where the current price becomes the new baseline price to measure future price reductions against.

Any ambiguity in the drafting or application of the prohibition could discourage discounting or the size of discounts retailers are willing to offer.

Retailers are also increasingly offering new and innovative plans, such as fixed rate plans, pre-paid plans, "smoothed" plans where customers pay a set amount per month based on their forecast usage etc. These plans are carefully developed based on pricing assumptions over the term of the plan. The onerous obligations introduced by the retail pricing prohibition and uncertainty in relation to which prices are impacted by the laws could result in retailers withdrawing more creative pricing options from the market.

There is no guidance in the Bill as to what "reasonable adjustments" might be made, nor any guidance in the Bill as to how a corporation's "underlying cost of procurement" is to be calculated. In addition, there is no guidance on how quickly or how often the "reasonable adjustment" must be made, nor whether a corporation is later able to increase prices when costs increase.

EnergyAustralia is particularly concerned that its cost of generation might be misapplied as an "underlying cost of procurement" even though that is not the same as the marginal price in electricity spot markets. It is also not the same as the cost of electricity financial contracts that hedge volume and price risks. Any calculation based on a generator's production costs is not appropriate as it may not account for the very significant capital costs associated with generation plant. The Committee should recommend that further analysis be done to confirm that "the underlying costs of procuring electricity" is the correct reference point for the prohibited conduct and, if so, that further clarification be added to the Bill to define what is intended to be captured by the phrase.

As currently drafted, all of these matters would need to be litigated in order to be resolved. To compound the risks for retailers, the ACCC's ability to bypass the court system and make recommendations directly to the Treasurer mean that it will be placed in a unique position where it will effectively be able to determine how to interpret ambiguous laws, and enforce them without recourse to an independent umpire. We submit that all of the critical elements of the prohibition should be clearly and objectively defined in the Bill itself.

Finally, the definition of "residential customer" in the Bill is in slightly different terms to the definition used throughout the National Energy Retail Law (NERL) and Victorian Energy Retail Code (ERC), and the definition of "small business customer" imposes a new threshold as illustrated in the below table. This inconsistency creates uncertainty and risks for corporations in complying with multiple regulatory obligations, which increases costs for customers.

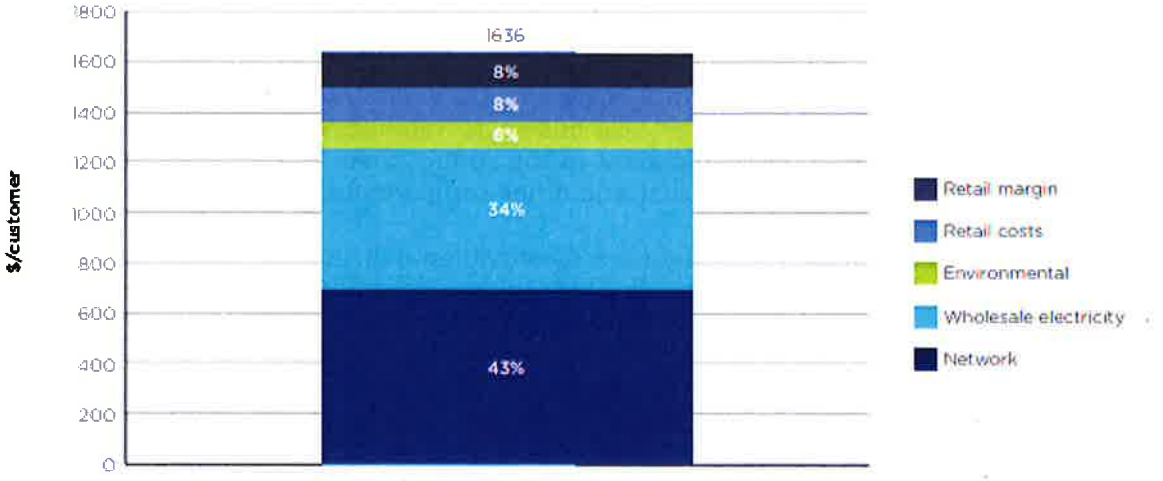
State	Small business customer threshold	Reference
Proposed Commonwealth threshold	A customer who purchases, or proposes to purchase, electricity at a rate less than 100 MWh a year and is not a residential customer in relation to that electricity.	s153B
New South Wales	A business customer who consumes below a rate of 100 MWh per year. This is on a customer, not supply point, basis.	NERL, ss 5, 6, 7 National Energy Retail Law (Adoption) Regulation 2013 (NSW), cl 4
Australian Capital Territory	A business customer consumes below 100 MWh per annum. This is on a customer, not supply point, basis.	NERL, ss 5, 6, 7 National Energy Retail Regulations, cl 8
South Australia	A business customer who consumes below 160 MWh per annum. This is on a customer, not supply point, basis.	National Energy (Retail Law) South Australia Act 2011 (SA), s 17 National Energy Retail Law (Local Provisions) Regulations 2013 (SA), cl 5(2)
Tasmania	A business customer who consumes below 0.15 GWh per year. This is on a customer, not supply point, basis.	NERL, ss 5, 6, 7 National Energy Retail Law (Tasmania) Regulations 2012, cl 7
Victoria	A "small business customer" is a person whose aggregate consumption of electricity taken from the relevant supply point has not been, or in the case of a new supply point, is not likely to be, more than 40MWh per year. This is on a supply point basis.	*Electricity Industry Act 2000* (Vic), s 3 Orders in Council and ERC
Queensland	A business customer consumes below 100 MWh per annum. This is on a customer, not supply point, basis.	NERL, ss 5, 6, 7 National Energy Retail Regulations, cl 8

Failure to reflect how electricity retailers set prices

The drafting of s153E does not reflect the way that electricity costs are factored into retail prices.

For the Committee's reference, in its most recent review of the electricity market, the ACCC provided the following breakdown of a small customer bill[12].

[12] Ibid. p.5



Retailers package these costs up to provide customers with different plan options. How each cost forms part of a retail price differs:

- **Wholesale costs:** The dynamic nature of electricity prices (which change every five minutes) means that retailers generally set prices for small customers[13] a year in advance based on forecast demand and wholesale prices. As a general practice, this involves retailers taking a gradual hedge position which takes into account total demand (how much customers use across the entire customer base) and a customer's demand profile (when customers use), and purchasing electricity contracts from a variety of sources. These costs will vary by location as each NEM region has its own regional reference price and unique conditions (e.g. weather, demand profile, interconnection)

  Different retailers will make different assessments about risk, and make different arrangements for hedging that risk, with different time periods, so costs will vary retailer-by-retailer.

- **Network costs:** Network costs are determined by AER and vary by location (up to five areas within a State) and the type of tariff a customer is assigned by the network business according to their usage and meter type. Retailers often have little time between getting final regulatory decisions on network costs and having to set retail prices so must make judgment calls on to what degree and how network costs are passed on.

- **Environmental costs:** Similarly, to wholesale costs, retailers must purchase renewable (or energy efficiency) certificates in advance and include the relevant cost based on demand and supply factors.

- **Retail costs and margin:** How retailers include retail costs and margin will vary according to individual business pricing strategies. Retail costs include sales, service and marketing costs, billing costs, credit and collection activities, and (the not insignificant) costs of complying with the complex and un-harmonised regulatory regimes. These represent legitimate and necessary aspects of the retail market and necessary to support robust competition and innovation in the market. Decreases in wholesale, network and environmental scheme costs cannot be viewed in isolation from the overall retail operating costs of the organisation.

[13] Usually taken to mean residential and small business customers

Retailers, at the end of the supply chain, need to be able to reflect changes in all cost components of a bill (including network costs and environmental costs) and achieve reasonable returns to ensure a sustainable business. Retailers should not be forced to pass through reductions in one component of the supply chain without also being able to consider the impact of increases in that and other components.

This may have an unintended consequence of providing a structural reason for retailers to immediately pass on cost increases in order to provide scope for later discounting what might otherwise be absorbed by retailers. For example, an increase in non-wholesale market costs might be offset by a reduction in wholesale market costs. Currently, retailers may allow these to offset each other. However, if any reduction in wholesale market costs must be passed on, then such offsetting will no longer be feasible. To address this risk, retailers will instead need to pass on such cost increases immediately to reduce the risk of being non-compliant with the CCA when wholesale prices fall. This appears to conflict with the Government's intention to lower prices for customers.

With the growth of solar generation in the NEM – large scale solar farms and household/business installation – when electricity is demanded from the grid is changing. There is an emerging 'hollowing out' of demand during sunny days, creating an overall 'peakier' demand profile. This, coupled with the relatively unpredictable nature of wind, means there is an increased need for flexible generators to manage this shape (e.g. batteries, fast start generators) and the importance of rebidding in the NEM to respond to these price signals (periods of higher demand and/or lower renewable generation).

As such, EnergyAustralia progressively hedges customers' load to ensure that customers are not exposed to often volatile wholesale prices. That is, while the wholesale price may decrease for a period, we still need to be able to insulate customers from the costs associated with the shape of the customer load profile. It is not clear under the proposed changes how these costs will be considered. Without hedging customers would likely face increased confusion as their electricity prices mirrored the constant fluctuations in the wholesale prices. We assume this is not the intention of the proposed change.

s153E should also factor in future price forecasts – not just look at a price reduction by reference to retail prices set up to 12 months prior to reflect how retailers price wholesale market costs.

Impacts on innovation in the retail sector

The retail electricity market is evolving, particularly with the increasing penetration of solar and battery technologies. In some states customers can access a range of products from over twenty retailers to suit their energy needs. This is a change from a decade ago when prices were regulated by State Governments and customers were given little or no choice.

For example, EnergyAustralia has at least four plans available in each NEM jurisdiction which allows customers to choose a product that suits their preferences. In addition, we offer solar and battery packages (with finance options) for those that wish to take more control of their energy. We are also undertaking a demand management trial which rewards customers for using less at times of high stress on the grid.

This type of retail innovation and any future innovation will be threatened as segmented or tailored products may be in breach of the CCA if savings are not passed in the manner

in which the bill requires. It may also impact investments in retail projects and trials, if it is unclear that costs can be recovered from customers over time. These limitations and uncertainty will only be to the detriment of customers and reduce positive experiences with the retail electricity market.

Interaction with a default market offer

The AER is currently developing a default market offer (DMO) price with a final determination scheduled to be made by 30 April 2019. The Government has been clear that it intends to use the DMO price as some form of "safety net" for electricity customers[14]. It appears the Government does not intend to give effect to a DMO in the National Energy Retail Law like the ACCC recommended, and instead intends to give effect to it through a mandatory industry code with annual price determinations in accordance with ss44AH and 51AE to be introduced by this Bill.

We note that Victoria is also considering introducing rules that prohibit a retailer from changing a customer's price at all during their 12 month benefit period. It is unclear how such a prohibition would interact with the retail price prohibition.

In any case, the interaction with DMO and retail pricing prohibition in s153E is not clear, but it appears that they would operate concurrently. Navigating duplicated and inconsistent retail pricing laws will only add to retail operating costs.

We also note that the Explanatory Memorandum has also signalled that once the AER has implemented a default market offer, it is the Government's intention to add an additional penalty to the regime to allow the Treasurer to make an order that a corporation's retail electricity offers are capped for a period at the level of the default market offer[15]. It is unclear from the Explanatory Memorandum what conduct would warrant or trigger such a penalty. However, the current Bill must be viewed in light of these future intentions of the Government.

We have made further comments on S44AH in section 4.

2.2. Prohibited conduct – electricity financial contract liquidity

No case for action

In its 18-month review of the electricity market the ACCC undertook a thorough investigation of electricity contract activity and found no evidence of businesses withholding contracts. It did, however, consider there to be a lack of transparency in contract markets and recommended further reporting to the AER[16].

The review also recommended that given the unique circumstances of the South Australian market that a market making obligation be implemented there and reviewed after two years[17].

Given that both of these recommendations are being progressed by the Energy Security Board and there are already regulatory controls and a well-established penalty regime in the CCA for corporations that manipulate markets to lessen competition, specific arrangements for the electricity sector in the CCA appear unnecessary. We therefore recommend that this form of prohibited conduct be removed so that the changes that

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[15] Page 89, Explanatory Memorandum
[16] ACCC - p.122
[17] Ibid. p. 130

are already in train can be given the opportunity to work and the impacts properly understood.

Over capture and uncertainty

EnergyAustralia is concerned with the open-ended nature of this condition which is applied at the corporate **group** level. There are many legitimate reasons why a corporation may not offer contracts. For example, corporations will have individual energy market risk policies that will govern the extent to which contracts may be sold and the extent to which capacity must be reserved to meet risk measures within the corporation's set risk appetite. Going forward, every decision would need to be assessed against these new laws.

The Bill also allows the ACCC to infer that the corporation is acting for a prohibited purpose, even if it was also acting for a legitimate purpose.

The Bill also fails to indicate the quantity of electricity financial contracts that a corporate group is expected to offer and under what circumstances. This may lead to disputes about the level of contracting an asset should be expected to make available through electricity financial contracts and in what forum (e.g. over the counter or through the futures exchange). While the Explanatory Memorandum does provide guidance on some matters, there is no binding obligation on the ACCC, Treasurer or the Courts to have regard to the Explanatory Memorandum in interpreting the Bill, nor does it adequately cover all situations.

The Bill should provide defences for completing contracts already on foot and decisions made in accordance with a corporation's risk management strategy and should allow the corporation to retain a "buffer" for unplanned maintenance and outages, so as to provide a "safe harbour" to reduce regulatory risk and compliance costs.

EnergyAustralia also has concerns about the ambiguity and inconsistency of the drafting in some parts of the Bill, notably:

- Whether a contract is on terms that have the effect or likely effect of preventing, limiting or restricting acceptance of those offers is very broad language and will capture legitimate commercial conduct. For example, there will be legitimate counterparty credit assessment reasons for including terms that could be unfairly interpreted as restricting acceptance.

- The Bill refers to substantially lessening competition in "*any electricity market*". However, the ACCC approaches market definition differently (and more narrowly) to the courts by preferring a State-based market approach, rather than a looking at the market as a national energy market. This is particularly problematic where the determination of whether conduct has occurred rests with the ACCC.

- Refusal to supply an electricity contract could be captured by misuse of market power provisions already in the CCA. While section 46 carries an additional limb that requires a court to find that the corporation has a substantial degree of market power, it is unlikely that a corporation *without* substantial market power could substantially lessen competition by withholding contracts. Indeed, the only example of a breach given in the Explanatory Memorandum[18] is an example of a misuse of market power: a vertically-integrated retailer with a dominant position

[18] Example 2.13 at [2.73].

refusing to contract with a competing retailer for the purpose of forcing the retailer from the market.

- Under the current Bill, there is no requirement to establish that the conduct had the effect of substantially lessening competition before a contracting order may be applied. This could result in the ACCC and Treasurer pursuing conduct that ultimately had no substantial impact on the market.

These deficiencies in the Bill should be amended if the Committee does not accept our recommendation above that this section is removed altogether.

2.3. Prohibited conduct – electricity spot market

No case for action

It is unclear why this prohibition is required. The ACCC in its review of the electricity market found that "clear instances of market manipulation are not a major feature of the market today[19]". The ACCC did recommend broader market manipulation rules similar to those implemented in the gas market[20], however they failed to recognise some of the fundamental differences between electricity and gas markets, including 24/7 trading at five-minute intervals and more complex contract portfolios.

In any case, the NER already contains strict requirements governing offers and bids in the wholesale market[21] which were extensively reviewed in 2014 to 2015[22].

Further, recent investigations have found no evidence of systemic abuse of market power:

- The AEMC found that the cost of price spikes, for which rebidding is the primary cause, has fallen since 2015, not increased. Where volatility has increased between 2015 and 2017 this has been driven by other factors unrelated to rebidding (i.e. demand is different to forecast, fuel costs)[23].
- The AEMC also found no case for making market design changes to the rebidding rules, that rebidding can lower wholesale prices as well as increase them, and its impact on customer bills is not material[24].
- The AER found no observable evidence of behaviour that would be traditionally associated with the exercise of market power in electricity markets, such as rebidding significant capacity at prices near the price cap close to dispatch, withholding significant capacity or shifting lower priced capacity to higher priced bands[25].
- The AER also found that withdrawal of large low-cost generators combined with increasing coal and gas costs have been the major drivers of wholesale price increases. For example, in New South Wales the AER found that since October 2016 there was a 'step change' where capacity that was offered at lower prices ($0-$50/MWh) is increasingly being offered at prices between $50-$150/MWh based on those factors[26].

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[19] Ibid. p.96
[20] Ibid
[21] For example, NER, cl 3.8.22A(1).
[22] Australian Energy Market Commission, Bidding in Good faith, 10 December 2015
[23] Australian Energy Market Commission, Gaming in Bidding Assessment (Grattan Response), 28 September 2018, p.i
[24] Ibid
[25] Ibid
[26] Australian Energy Regulator, 'AER electricity wholesale performance monitoring: NSW electricity market advice', December 2017

EnergyAustralia recommends that the Committee request the leaders of the aforementioned agencies to test the claims made by the Government that these powers are necessary to respond to market manipulation by energy companies.

Prohibition is inconsistent with market design

The NEM is designed to operate in such a way so that AEMO can find the lowest cost way of meeting demand, so the grid can operate securely, from all the bids it receives from all generators. In this way the marginal megawatts needed to be dispatched will set the price in any region. It can be inferred that any bid is therefore influencing price; that is the very design and purpose of the market. Therefore, it will be difficult to differentiate between conduct that simply reflects a decision to make a bid or offer on the basis of forecast supply and demand balance and conduct that distorts or manipulates prices, leading to both enforcement and compliance difficulties in the future.

The design and intent of the market should be an express factor – as the market is designed so that all bids influence price. There should be an express defence in the Bill for behaviour that is genuine commercial behaviour as intended by the design of the electricity spot market.

A prohibition which limits the ability of generators to bid during periods in a manner that seeks to recover their efficient costs over time and respond to market signals is inconsistent with the market design insofar as pricing signals being a signal for new investment. Therefore, the Bill is likely to be detrimental to the NEM investment environment and customers over the longer term. Given AEMO estimates it will cost between $8 billion and $27 billion[27] to replace retiring generation over the next two decades as the energy sector transitions to cleaner technologies, regulatory frameworks should support - not hinder - this investment. We encourage the Committee to consider the long-term investment chilling effects of the legislation more closely.

Unclear drafting

Several key terms in s153G and s153H of the Bill are not well defined or not defined at all which make interpretation and understanding the possible implication difficult. If this section is retained, we recommend that the following key terms in the Bill are defined:

- "Fraudulently, dishonestly or in bad faith".
- "Distorting or manipulating prices"

s153G outlines 'prohibited conduct – electricity spot market (basic case)' whilst s153H outlines 'prohibited conduct – electricity spot market (aggravated case)'. Combining "fraudulently, dishonestly or in bad faith" with the "purpose" requirement in the aggravated case is confusing. It is unclear to EnergyAustralia what the intent is of having both cases.

The Explanatory Memorandum to the Bill provides that "given the complexities of the market, it is not possible to exhaustively prescribe the conduct which will and will not have the purpose of distorting or manipulating prices". This clearly demonstrates how difficult it will be for energy companies to comply with the new laws.

EnergyAustralia submits that the effect of the conduct on competition should also be taken into account, to ensure that enforcement action under this provision is directed towards conduct that actually has the effect of substantially lessening competition.

[27] Australian Energy Market Operator, op.cit, p.5

2.4. Standard and onus of proof

The Bill introduces some of the most significant penalties available under the CCA. Yet there is no requirement for allegations of prohibited conduct to be tested and proven in court (with due process and rules of evidence applying) before the Treasurer can make a contracting order, or before the ACCC can issue a public warning notice or an infringement notice or recommend a divestiture order be pursued.

Instead, the Bill allows the ACCC to recommend a contracting order or divestiture order, or issue a public warning notice, based on a mere "reasonable belief" that a breach has occurred, and the Treasurer can make the order if he or she is "satisfied" that is the case.

This is a lower standard of proof than is currently required for an infringement notice under s51ACC of the CCA (which requires the ACCC to have reasonable grounds to believe that a person has contravened an infringement notice provision and carries a maximum penalty amount of $12,600 for a corporation (or $126,000 for a listed corporation).

The Bill also reverses the traditional onus of proof. If the Bill becomes law a corporation would need to convince the ACCC that there is no breach, rather than the ACCC needing to prove a contravention in court, on the balance of probabilities.

s153J(2) states that a corporation can be taken as acting for the purpose of substantially lessening competition or distorting or manipulating prices in the electricity spot market "even though, after all the evidence has been considered, the existence of that purpose is ascertainable only by inference from the conduct of the corporation or of any other person or from other relevant circumstances." EnergyAustralia considers it to be entirely inappropriate that a corporation's purpose can be inferred, and possibly penalties applied, that is potentially inconsistent with the evidence presented.

Given the gravity and first of its kind penalties associated with contraventions in the Bill EnergyAustralia considers the standards and onus of proof to be alarmingly low and recommend that the Committee seek further independent legal advice to ensure they are appropriate.

3. Penalty regime

3.1. Public warning notices

s153L gives the ACCC the power to issue public warning notices. Public warning notices have the ability to significantly prejudice the commercial activities of a corporation. Given the low standard of proof (discussed in section 2.4) the ACCC is required to meet to issue a notice EnergyAustralia is deeply concerned that a corporation could be negatively impacted by an unreasonable public warning notice. Corporations should have the right to seek an injunction against any warning notice being made public. To the contrary, we believe that such public warning notices could seriously prejudice the interests of the corporation in question, particularly in relation to current commercial negotiations.

The timeframe for a corporation to respond to a draft public warning notice is 21 days. Given the complexity of the allegations that a notice would likely contain this timeframe is unreasonably short. The Commission should also be required to take time to review and respond to the corporation's response before issuing the notice.

Corporations should also be able to seek urgent injunctive relief and/or merits review of the ACCC's determination.

As discussed in section 2.4, the threshold of "reasonably believes" is lower than the threshold for other kinds of public warning notices, which requires the objective test of "reasonable grounds" (e.g. s51ADA). This should be part of further legal review of the Bill.

3.2. Prohibited conduct notices

s153P empowers the ACCC to give a corporation a prohibited contract notice stating one or more recommendations for the kind or kinds of order the Treasurer or the Court could make under Division 5 or 6. The corporation is only allowed 45 days to respond which, given the likely complexity of the notice, is also unreasonably short.

EnergyAustralia also considers that any prohibited conduct notices should be confidential as between the parties unless otherwise agreed and that corporations should be able to apply for variation or revocation of notices.

Concerningly, the Bill does not allow for merits review of decisions made by the ACCC or the Treasurer. EnergyAustralia recommends that the Bill be revised to include an express right to full merits review before a court (e.g. Australian Competition Tribunal) for all decisions of the ACCC and/or Treasurer.

3.3. Contracting orders

Giving an elected official (i.e. Treasurer) the right to dictate the terms, prices, quantities of a contract between private companies is a serious intervention into what is a complex trading operation. Generation businesses could be forced to go short into a market and incur significant financial losses as the result of a contracting order. Publishing contracting orders may also have significant impact on the ability of the corporation to trade in the market.

A contracting order will be difficult to administer. An obligation to offer a certain amount of contracts on "commercial terms" is open to significant argument as to whether proposed terms are commercial or not. It is also worth noting that electricity contracts are financial hedging instruments and not directly linked to the delivery of electricity. This means that, if one party is forced to trade at a price that is not fair market value (as judged by market expectations of future spot prices), then the mark to market value of that contract will not be zero. This would represent nothing more than a wealth transfer between party A and party B with no direct link to customer outcomes.

It is also unlikely that the ACCC and the Treasurer can tailor a contracting order without a significant amount of information about the business to ensure it does not have unintended effects. It is entirely unrealistic to believe that the ACCC can make any meaningfully accurate recommendation about this within the 45-day process contemplated by s153QA, or that the Treasurer will be able to decide on the order without any further information from the ACCC. However, that appears to be what is contemplated by the Bill which provides for no information gathering or discovery process beyond the ACCC consultation process that must be completed during the 45-day period following the issue of a prohibited conduct notice.

By way of illustration, if a vertically-integrated business is required to contract more generation capacity than is appropriate under its risk policy, then the business will need to buy generation capacity from the market, reducing supply and potentially at different prices. This may have flow-on effects to retail pricing and ultimately, increase prices for

customers. However, not only would the Treasurer be able to order that vertically-integrated business to offer electricity financial contracts, it may order the quantity, period, price range and other terms for those electricity financial contracts. It also appears that the Treasurer could order the business to contract with a third party with a sub-standard credit rating, further intervening in internal financial and operational controls. In effect, the contracting order could be forcing a corporation to sell a contract that is uneconomic or beyond risk limits.

Further, the order may be in place for three years. This is a long period of time, and no justification at all has been advanced for it.

Given the possible impact and lack of rigorous process to inform a contracting order, EnergyAustralia recommends that it be removed as a possible penalty in the Bill. However, if it is retained we recommend that the Bill be revised to include an express right to full merits review before a court (e.g. Australian Competition Tribunal).

If retained, we also recommend that s153Y be amended to remove the right of the Treasurer to vary a contracting order of his/her own initiative. Given the gravity of the penalty any changes the Treasurer wishes to make should only be on the express advice of the ACCC.

There should be defences available, including if the corporation can establish before a court that the prohibited conduct did not occur.

Conflict of interest

Given the Federal Government is the sole shareholder of Snowy Hydro (and the Treasurer is the shareholding Minister) EnergyAustralia is concerned about a possible conflict of interest for the Treasurer in issuing a contracting order against a competitor of Snowy Hydro. Any contracting order may directly or indirectly benefit Snowy Hydro so it would be inappropriate for the Treasurer to have such power.

3.4. Divesture orders

No case for action

The Government has not established a market failure which requires a court, upon the recommendation of the Treasurer, to have this power, particularly as the ACCC has not sought this. In fact, in considering whether a mechanism to force divestiture is required, the ACCC concluded that it was not appropriate to intervene to unwind the way in which the market has evolved[28]. The Chair of the ACCC, Rod Sims, has previously advised the Committee that he was not consulted directly before the Government decided these powers were necessary[29].
We do not agree that a power of divestiture is a proportional or targeted remedy that will deliver lower prices for customers. Further, it is difficult to imagine the circumstances in which forcibly breaking up an energy company would be necessary to prevent the company from continuing or repeating the prohibited conduct in the future, as would be required under the "proportionality" test to be applied by the Treasurer and the Federal Court. The result will be massive interference and interruptions to the company's business, potentially impacting on a business's ability to operate as an ongoing concern – for an extremely unlikely judicial outcome.

[28] ACCC, op.cit., p.89
[29] Rod Sims comments to Senate Economics Legislation Committee, 25 October 2018.

The orders could potentially force companies to close, resulting in job losses. Such changes could also have negative flow-on effects on the electricity market and ultimately for customers. We, therefore, recommend that the Committee remove the divestiture penalty from the Bill. Further reasons are outlined below.

Achieving fair value

As the Bill is currently drafted, a divesture process would be required to be completed within 12 months. This is a short period of time to find a buyer and complete such a complex transaction.

In any case, it is highly unlikely that the forced sales process will deliver a price for the assets that reflects their true value, as the business will not be able to reject deals it regards as not commercially viable and buyers will know that. As a consequence, there is a real possibility that the business will not receive just value for the assets. The implications of this are very significant and threaten to fundamentally undermine business confidence in making investments, particularly in relation to new generation.

The broader economic impact of proposing divestiture

Forced divestiture, or the threat of, also has the potential to discourage investment more broadly across the economy. Investors looking at any part of the economy will be watching closely to see if the proposed powers are introduced because it could signal a willingness or intention to introduce them in other sectors. Concerningly, there are already some members of Parliament calling for these powers to be extended beyond the energy sector to apply to banks, supermarkets and petrol stations[30].

We recommend that the Committee seek the views of businesses in other sectors to understand the broader economic impacts of creating divestiture powers.

We also note that the Treasurer and other proponents of the Bill have cited other instances of divestiture powers overseas, including in the United States and United Kingdom. However, we believe that this is a false equivalence as none of the overseas divestiture powers are linked to sector specific laws. Rather than simply adopting positions taken in overseas laws, we should first ensure that they are suitable for Australian market conditions.

Conflict of interest

As discussed above, given the Federal Government is the sole shareholder of Snowy Hydro there is a potential conflict of interest for the Treasurer in issuing penalties under the changes proposed in the Bill. Whilst this risk is diminished somewhat by having the Federal Court as the ultimate decision maker in the case of divestment, the issue remains nonetheless as the Treasurer is required to make the recommendation to the court.

The amendments to the Bill proposed by the Member for Kennedy[31] may provide a further conflict concern if the practical effect of the amendments would mean that a government-owned asset could only be sold to another government. This could create a situation where Snowy Hydro could be the only possible buyer of an asset (or assets) being forcibly divested.

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[30] See comments in Kelly, J. 'Liberals in a bind over call to expand 'big stick' break-up powers', *The Australian,* 22 November 2018

[31] Amendments to Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2018 proposed by B. Katter MP, 6 December 2018

4. AER information gathering powers

4.1. Retail pricing regulation powers

Negative impacts of a default market offer

s44AH of the Bill facilitates the conferral of functions related to the regulation of retail electricity prices on the AER[32]. This could take the form a mandatory industry code which would, amongst other things, provide that a retailer's standing offer prices cannot exceed the amount determined by the AER. Regulations made for in s44AH(b) of the CCA would confer on the AER the function of determining these amounts. This could take the form of the DMO.

The Explanatory Memorandum to the Bill indicates that if this approach is taken the necessary regulations would be made before April 2019, and commence on 1 July 2019[33].

Regulating retail electricity prices is an extreme and complex matter. In recent advice to the Council of Australian Governments (COAG) Energy Council the Australian Energy Market Commission (AEMC) recommended that a DMO should be developed as a reference rate[34] only, rather than as a price cap[35].

The AEMC found that the retail market is workably competitive, with no evidence of excessive retailer margins and that the DMO has the following risks:

- An increase in prices for at least some customers on market offers;
- An increase in standing offer prices for those that are currently set below the cap;
- A decrease in the range of offers available in the market;
- Lower levels of innovation as 'discounts off the standing offer' become the most common offer;
- Higher barriers to entry for new retailers, as well as changes in consumer behaviour, resulting in decreased competition in the energy retail market and ultimately higher average prices for consumers[36].

This view is shared by the NSW Independent Pricing and Regulatory Tribunal (IPART) which found that:

> "Re-introducing price regulation or a 'default tariff' is likely to lead to lower levels of competition and higher prices.
>
> In the short term a default tariff could help disengaged customers from paying excessive prices. However, over time it is likely to result in less customers actively shopping around in the market as the benefits from switching fall. In turn, this smaller market for 'active' customers would lead to less vigorous competition and innovation, with fewer retailers competing in this market.[37]"

[32] Explanatory Memorandum, S7.1
[33] Ibid. S7.6
[34] A rate at which all market offers must be referenced to for advertising purposes.
[35] Australian Energy Market Commission., Advice to Standing Committee of Officials on default offer, 10 December 2018
[36] Ibid.
[37] NSW Independent Pricing and Regulatory Tribunal, Review of the performance and competitiveness of the retail energy market in NSW, From July 1 2017 to 30 June 2018 (Draft), p.9

EnergyAustralia agrees with the AEMC and IPART that a DMO is a bad outcome for customers.

We also consider that there is a significant risk wholesale market risk associated with a DMO. There is a risk DMO will effectively set wholesale prices in a region, which, if wrong and prices are held artificially low, it will constrain generation maintenance, potentially affecting reliability and investability in the wholesale market.

It is our view that a reference price should be implemented to enable customers to easily compare offers and find the best deal for them. EnergyAustralia has long argued that a reference rate should be implemented as a useful tool to help customers better understand and engage in the retail market[38].

Intrusion on States' rights

The proposal to enable the AER to establish price controls via a compulsory industry code enabled by this Bill is a gross misuse of Federal powers and an intrusion on States' rights. It would be in direct conflict with the Australian Energy Market Agreement (AEMA) - an agreement between NEM jurisdictional governments on energy matters – which affirms that State or Territory Governments retain responsibility for the right to apply retail price regulation where competition is not yet effective for a market, group of users or a region[39].

State and Territory Governments recently reaffirmed their rights under the AEMA during the COAG Energy Council meeting on 19 December where "Ministers noted the States' and Territories' position that Commonwealth legislation should not be used to set reference prices or otherwise regulate electricity pricing without the agreement of the relevant jurisdiction"[40].

It also highlights the difficulties retailers face in dealing with multiple, and at times conflicting, regulatory regimes. Understanding and meeting different regimes limits innovation in retail markets and increases the costs of doing business – both of which are to the detriment of customers. As stated above, EnergyAustralia supports establishing a reference price to enable easy comparison of retail offers. This should be done through a cooperative process facilitating by the COAG Energy Council to ensure it is implemented in a consistent and sensible manner.

4.2. Regulatory scrutiny of industry code

Changes proposed in the Bill clarify that regulations made for s44AH(b) of the CCA may confer power on the AER to make disallowable or non-disallowable legislative instruments. The regulation prescribing the industry code as a mandatory code is a disallowable instrument. However, the proposed regulation-making power expressly allows the regulation to provide that subsequent changes to the industry code are automatically incorporated in the mandatory code. This is not the case for other mandatory codes under the CCA.

This means that subsequent changes would not be disallowable, so any process for consultation or review of the changes are not catered for in the Bill. This could give the

[38] For example, EnergyAustralia submission to Future Security of the National Electricity Market, Preliminary Report, EnergyAustralia submission to Review of Electricity and Gas Markets in Victoria, EnergyAustralia submission to ACCC Electricity supply & prices inquiry.
[39] Australian Energy Market Agreement, S14.15, December 2013
[40] COAG Energy Council, Meeting 21 Communique, December 2018

AER unfettered power over energy retailers without the appropriate scrutiny of Parliament.

Further, these powers were not part of the consultation paper nor the draft legislation that was circulated for limited consultation. Therefore, the new AER powers have not been properly analysed or tested properly with stakeholders, including consumer representatives.

In summary, the proposal to given the AER unchecked powers of retail price regulation in the CCA is a far reaching intervention which breaks with COAG agreements, has not been adequately examined via a robust consultation process and, most importantly, is likely to increase prices for customers. Given this, we recommend that s44AH be removed from the Bill and that the Federal Government continue to work with industry and the COAG Energy Council to implement a reference rate as soon as practicable.

3. Constitutional validity

EnergyAustralia submits that the contracting order and divestiture regimes under the Bill raises serious issues and could potentially be challenged on Constitutional grounds despite the changes made following the first exposure draft. These issues could result in any contracting or divestiture orders made being immediately challenged in the High Court, adding additional (and not insignificant) costs, time and uncertainty to the enforcement regime.

3.1. Acquiring property other than on just terms

The Bill (and Explanatory Memorandum) openly acknowledge that the Bill potentially results in an acquisition of property from a person other than on just terms, in contravention of section 51(xxxi) of the Constitution.

Section 153ZC of the Bill purports to address this potential breach of the Constitution by asserting that, in effect, none of the proposed provisions have effect to the extent that their operation would result in the acquisition of property otherwise than on just terms within the meaning of the Constitution.

EnergyAustralia submits that this does not answer the Constitutional problem as a matter of principle and is unlikely to answer it as a matter of law: the legislation either complies with the Constitution or does not. In a practical sense, this band-aid attempt to address the constitutional defects of the legislation may only delay the inevitable Constitutional challenge to a later time when the Treasurer seeks to make the contracting orders under the CCA or when the court makes a divestiture order.

There is also a very significant risk that a forced divestment process will result in an acquisition by a third party that is not on just terms. The Bill does not provide any defence or right to revoke or vary an order on the basis that the corporation is unable to dispose of the asset on just terms because, for example, there are few bidders and those bidders offer very low prices because they know the generator must sell. This was included in an earlier confidential consultation draft of the Bill but was apparently removed from the version of the Bill introduced to Parliament (with no explanation as to why in the Explanatory Memorandum). It also does not address the fundamental question of whether the acquisition is on just terms.

Market value, as assessed at a point in time and by reference to what a purchaser is prepared to pay for an asset, will not take into account the same factors that would

otherwise be required to arrive at a price on "just terms". A forced sale would not consider broader matters of fairness and the subjective value of the integrated asset to the corporation.

Contracting orders may also result in an acquisition of property other than on just terms, as they would require the corporation to offer, and enable third parties to acquire, property (in the form of intangible financial rights derived from electricity) from the corporation on terms, including price, specified by the Treasurer. There is a real risk that those terms may not be just terms, particularly if the Treasurer elects to use this power to reduce wholesale or retail electricity prices and justifies that as being proportionate to the (alleged) misconduct, in circumstances where there is very limited information available to the Treasurer about wholesale energy pricing in the market generally.

3.2. Breach of the separation of powers doctrine

The Bill also gives the Treasurer the power to address an alleged breach of the law through a contracting order, without the need for a court to independently determine that a breach has occurred and that such an order is appropriate and proportionate. Instead, the Treasurer makes his or her own determination based on a recommendation from the ACCC, based on the low standard of reasonable belief for the ACCC, and satisfaction for the Treasurer that a breach of legislation has occurred, and that a proportionate means for preventing future breaches is either contracting orders or divestment.

In our view this is an extraordinary approach. The circumvention of the courts, in favour of executive orders, to remedy alleged but unproven breaches of the law, in legislation that has clearly been rushed and failed the Government's own Guide to Regulation 41 is unprecedented, manifestly unfair and extremely damaging to business and investor confidence. Section 2.4 provides further details on our concerns about the standard of proof that must be satisfied for the ACCC to seek a remedy.

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[41] Department of Prime Minister and Cabinet, 'The Australian Government Guide to Regulation', March 2014