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Australian Energy Regulator



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## Wholesale Market Monitoring Guidelines

The Australian Financial Markets Association (AFMA) is responding to the Australian Energy Regulator's (AER) Wholesale Market Monitoring and Reporting Guideline issues paper.

AFMA is the leading financial markets industry association promoting efficiency, integrity and professionalism in Australia's financial markets, including the capital, credit, derivatives, foreign exchange, energy, carbon, and other specialist markets. Our membership base is comprised of over 130 of Australia's leading financial market participants, including many energy firms who are key participants in the east coast gas and electricity markets.

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### Key Points

The guidelines should provide clarity about:

- a) the intended scope of the AER's information collection; and
- b) how the functions will be coordinated with the ACCC's ongoing pricing inquiries.

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### 1. Role of the guidelines

AFMA considers the guidelines are an excellent opportunity for the AER to provide the market with clarity about how the AER intends to exercise its new powers. We consider that the guidelines should provide context about what the AER hopes to achieve with its new wholesale market monitoring function, clarify how the overlap with the ACCC's pricing inquiries and other domestic and international reporting obligations will be managed and allow market participants to accurately predict the costs of complying with the new reporting obligations to allow them to budget to assign appropriate human resource to support reporting and to make any requirements system enhancements.

The issues paper indicates that the AER expects the market monitoring function to evolve as their expertise develops. While we appreciate that the AER needs to develop its understanding of these functions, AFMA considers that it is important for the AER to settle on how it intends to exercise them quite early. Our experience is that the greatest costs to participants in data reporting schemes occurs when reporting obligations change and where the objectives of data collection are not clear. Given government and the AER's laudable desire to minimise compliance costs we caution that to avoid unnecessary costs to the industry the AER needs to quickly settle on a set of enduring data reporting obligations that will not change without significant notice and consultation with market participants. We discuss how this could be done further in section 3.

#### AFMA Recommendations

- i. The guidelines should:
  - a) Set out the AER's objectives for the market monitoring function;
  - b) Provide clarity about how the reporting function will operate.

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## 2. Coordination with ACCC functions

AFMA's members' top concern regarding the AER's market monitoring functions is how the overlap with the ACCC's ongoing gas and electricity inquiries will be managed. They consider that developing effective arrangements for sharing data between the AER and ACCC is essential to avoid expensive duplication of reporting obligations. AFMA considers that the guidelines are the appropriate place to set out how the AER and ACCC expect to manage this overlap.

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### Key Points

- **The guidelines should set out how the AER's functions will be coordinated with the ACCC's ongoing pricing inquiries.**
- **Developing effective arrangements for sharing data between the AER and ACCC is essential.**

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The ACCC's gas and electricity inquiries differ in scope and duration and therefore the extent of their overlap with the AER's function varies. The electricity inquiry has not focused on the contract market only looking at it twice in November 2022 and December 2023, AFMA understands that the ACCC does not intend to do further work on the electricity contract market. It would therefore be useful if the guidelines could provide clarity that the ACCC is not expected to do further work on the contract market before its inquiry concludes in 2025.

The overlap between the ACCC's gas inquiry and the AER's functions is more concerning. The contract market is the principal focus of the gas inquiry and is expected to remain so until it concludes in 2030. AFMA's members are not at all clear how the AER's gas market monitoring function will differ from the ACCC's gas inquiry and are concerned at the potential for duplication between the two regulators and additional costs for reporting entities if they are required to report similar data to both. We consider that the guidelines should set out clearly how the two functions differ and how participants reporting obligations will be minimised.

### AFMA Recommendations

- ii. The guidelines should set out how:
  - a. the overlap between the AER and ACCC's functions will be managed;
  - b. the regulators intend to avoid duplicative and inconsistent reporting obligations.

## 3. Data

The types of data the AER collects and the mechanisms they use to collect them will be key to both the effectiveness of the function and the cost to participants. Our view is that the AER should only collect data from market participants where there is a clear reason for the collection and where similar data is not available from another source. We consider that there would be significant value for both the AER and participants in starting detailed work on the data requirements as soon as possible. To facilitate this AFMA encourages the AER to publish information about the actual data it is considering collecting as well as an explanation about what it anticipates using the data for to allow the industry to provide concrete feedback on how practical it will be to provide the data and if it will answer the AER's questions as well as allowing participants to determine what system enhancements are required and the timeframes these are likely to require.

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### Key Points

- **The AER should only collect data from market participants where there is a clear reason for the collection and similar data is not available from another source.**
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- **The AER should start consulting on the detailed reporting requirements as soon as possible.**
  - **The guidelines should set out how the AER intends to transition to an enduring reporting framework.**
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AFMA provides the following feedback on the information the AER may require and how it should be collected.

### **3.1. Enduring data collection model**

AFMA's members consider that it is critical for the AER to develop an enduring approach to data collection that is sustainable for both participants and the AER. In our view the two options that can meet the AER's requirements at reasonable costs to participants are:

1. Infrequent ad-hoc manual reporting; or
2. Regular standardised reporting

The first option gives the AER more flexibility but becomes increasingly onerous for participants as the volume and frequency of reporting increases. The second option is less flexible but will allow the AER to build up a higher quality, more granular data set without imposing unreasonable costs on participants. As discussed further below in section 3.3, the AER might like to consider adopting an ad-hoc approach initially and transitioning to a more standardised approach.

The difference between the two approaches can be seen in the contrast between ASIC's OTC derivative transaction reporting framework and the ACCC's pricing inquiries. On its face, ASIC's reporting framework is more onerous than the ACCC's pricing inquiries as it requires near real time reporting of all OTC derivatives. ASIC's reporting framework required reporting entities to make significant investments in automated systems to allow them to meet their obligations. While the implementation costs of complying with ASIC's rules were considerable, once built, high quality automated systems allow operations staff within reporting entities to meet their reporting obligations at relatively low ongoing cost without having to rely on input from legal and commercial staff which minimises disruption to the business. This efficiency is possible because ASIC committed to leaving the reporting obligations unchanged from year to year.

This contrasts with the approach the ACCC has adopted for its gas and electricity inquiries which relies on frequent manual reporting processes that change regularly. This approach may be appropriate for a one off information requests but it has proved extremely costly and disruptive to energy businesses when used for a long term inquiry as the changing nature of the reporting obligations prevents participants from investing in systems that would allow them to report more efficiently and requires regular involvement of legal and commercial staff to interpret requests and provide data which is costly and disruptive to their businesses.

AFMA therefore would like the guidelines to provide clarity about how the AER anticipates moving towards an enduring reporting framework.

### **3.2. Who has to provide data?**

The reach of the AER's information gathering powers is framed broadly allowing the AER to serve information instruments on "any person." As there are a range of participants in the market, with varying quantities of information relevant to the AER, AFMA would appreciate if the guidelines could provide guidance about who the AER intends to request information from.

Particularly we would like the AER to clarify if it intends to only collect information from physical market participants or if it also intends to collect information from firms that only participate in the financial market. We anticipate that extending information collection to financial market participants will increase the complexity of the AER's collection task without significantly enhancing

the quality of the information received. We suspect many financial firms will be unaware of the AER's new powers and that firms based overseas are probably unlikely to respond to information requests. We consider that this additional cost and effort will deliver limited benefit as the majority of the financial firms' contracts are likely to be with physical market participants who will have already reported the information.

### **3.3. Using existing data**

AFMA's members are very keen to avoid having to provide similar data to multiple regulators, we therefore encourage the AER to look to rely on information provided to other regulators and market bodies to the maximum extent possible and consider that it is essential that the AER and ACCC develop effective arrangements for sharing data.

The issues paper indicates that the AER proposes to use a "backwards design process" to determine information requirements based on the questions the AER is trying to answer. In principle, AFMA supports this approach but, considering the large amount of relevant data that is currently held by a number of regulators and other bodies, we encourage the AER to consider, at least initially, basing its analysis on the information that is already available to it from other sources. We consider this approach will minimise the risk that market participants will be required to provide data when similar data is available from another source or where the data is ultimately not of assistance to the AER.

AFMA considers that when the AER begins performing these functions the most practical and lowest cost way for it to develop its analytical capability and increase its understanding of the market will be to identify and use the information that is currently available to it, either publicly or from other sources, and see to what extent it can be used to answer the AER's questions. We consider that this approach will allow the AER to develop its analytical capacity and market understanding at minimal cost to the market and that this will then put the AER in a better position to identify any additional data requirements based on the results of this work.

Existing data sources that AFMA considers the AER should utilise include:

1. Data held by the ACCC as part of its gas and electricity inquiries
2. ASIC's OTC derivative reporting data
3. Futures market data held by ASIC
4. Data held by AEMO, particularly:
  - Data it holds to facilitate its planning functions
  - Trade data captured on the Gas Bulletin Board
  - Gas Supply Hub trade data

### **3.4. What do you need to collect?**

The issues paper identifies the following four areas of particular interest for the AER's market monitoring function; liquidity, access to markets and barriers to entry and participation, participant's risk positions and incentives for offer behaviour. AFMA provides the following input on what data may give the AER insights in these areas and where we think data collection is unlikely to offer much assistance.

#### **A. Liquidity**

AFMA considers that liquidity is one of the key criteria that the AER should look at to assess the functioning of Australian energy markets and we note the AER's current reporting already looks at market liquidity using ASIC and AEMO data. Liquidity has several meanings but in the context of the AER's market monitoring powers we think the key concept is market liquidity:

*the ability of investors to trade assets in the market (for example, an asset is liquid if it can be easily sold in large amounts with only small changes in its price).<sup>1</sup>*

Market liquidity is generally measured by looking at the spread between bids and offers on a market and the volume of the product that is traded.

Broadly, market liquidity is a concept that is relevant to fungible traded products. In AFMA's view it is an appropriate measure for standardised derivatives and standardised physical gas and pipeline capacity products traded on the Gas Supply Hub (GSH). But we think it is an inappropriate measure for less fungible products such as bilateral gas transport and supply contracts, and non-standard derivative contracts.

The ASX and ASIC hold the data the AER would need to understand liquidity in futures markets and AEMO holds the information necessary to understand liquidity in the GSH. ASIC also holds data on OTC gas and environmental product transactions but not on OTC electricity derivatives. AFMA's understanding is that futures market liquidity is a good indicator of overall liquidity in the electricity market as the majority of trading occurs on exchange. We therefore encourage the AER to perform its initial market liquidity analysis based on the information available from ASIC, ASX and AEMO and determine the extent to which OTC derivative data would assist based on this initial analysis.

OTC electricity derivative transactions are not directly comparable to futures transactions as they are traded less frequently, are typically larger and are transacted on different credit terms. We therefore suggest that it is probably inappropriate to attempt to use the same analytical tools to look at OTC transactions as are used for futures markets. AFMA's suggestion is it might be most helpful for the AER to initially collect data regarding the number of OTC trades and volume of energy they represent, possibly in a similar way to the former AFMA Electricity Derivatives Turnover Report. We think this would allow the AER to understand the scale of the OTC market relative to the listed market and would allow you to assess the value of requiring additional information about OTC transaction.

## **B. Access to markets**

Access to futures markets is essential for participants in the electricity market and is increasingly important for gas market participants. Bell Potter's decision to withdraw from clearing ASX energy futures in 2022 highlighted the importance of the futures markets as many small retailers and financial market participants found themselves suddenly unable to access the ASX. AFMA therefore understands the AER's desire to investigate factors that may inhibit access to futures markets, but we consider this type of investigation is more suitable for a one-off thematic review rather than ongoing monitoring and that ASIC or the Commonwealth treasury would be better placed to do this work than the AER.

AFMA's understanding is that the two main factors that inhibit access to energy futures markets are the availability of clearers and the cost of margining. The high volatility and relatively small scale of the Australian energy futures market are the main factors limiting the number of clearers interested in clearing energy products and contribute to the relatively high margin requirements for energy products. Clearers find it commercially challenging to clear energy products as the market is more volatile than other markets they operate in, and they need to commit resources to developing expertise in the underlying products to ensure they can appropriately manage these risks. Justifying these costs can be difficult as the small scale of the market means that they are only likely to earn limited revenue from energy products, this has led to a limited number of clearers clearing ASX energy products and has complicated access to alternative markets such as FEX Global. Similarly, the high level of volatility in the energy market has led to margin costs being higher than for other listed products as the clearing house needs higher margins to manage its potential exposure to a default.

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<sup>1</sup> <https://www.apra.gov.au/apra-explains-liquidity-banking>

AFMA thinks there is potential for government policy to help address some of these issues and to increase market access and is happy to contribute to the discussion, but we do not think that additional data collection will provide much illumination. We suggest that the challenges of access to energy futures markets would be more appropriately explored as a separate policy initiative by the Department of Climate Change, Energy, the Environment and Water (DCCEEW) and Treasury, rather than as part of the AER's wholesale market monitoring function.

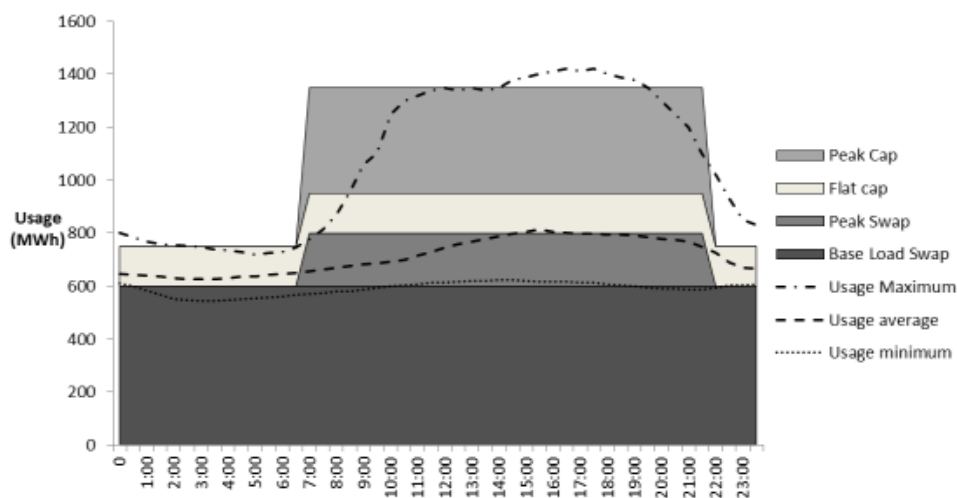
### C. Risk positions

In previous submissions AFMA has noted that the AER does not have any powers regarding financial markets and that it only has very limited powers regarding participants risk management arrangements.<sup>2</sup> We have therefore questioned the value of the AER collecting data related to risk management when it will be unlikely that it will be able to take any action as a result of its observations and where the commercial sensitivity of the data means that it is unlikely that the AER will be able to publish any analysis that will be of much value to either policy makers or the market.

Despite our reservations about the value of the AER collecting this data, we think the most practical way for the AER to understand risk within energy firms would be to collect aggregate data showing how firms manage their exposure to their customers forecast demand.

While slightly dated the below diagram from the Productivity Commissions 2013 Electricity Network Regulatory Frameworks Inquiry is helpful in understanding how energy firms typically consider market risk.<sup>3</sup>

**Figure C.2 Illustrative risk management approach**



Underlying data are hypothetical and are for illustrative purposes only.

Energy firms will typically forecast their customers expected minimum, average and maximum demand and will then use a combination of physical assets (generation or physical gas supply) and financial contracts to manage this risk. We suggest that the most useful information for the AER would be:

- a) Firms expected demand – either from retail load for retailers or from sold contract positions for generators
- b) A high-level breakdown of the physical assets and financial instruments that they use to manage this risk, similar to the hypothetical approach in the diagram above.

<sup>2</sup> [AFMA submission to DCCEEW consultation on Wholesale Market Monitoring and Reporting Reforms](#)

<sup>3</sup> [Appendix C to Productivity Commissions 2013 Electricity Network Regulatory Frameworks Inquiry](#)

AFMA considers that aggregated data is likely to be the best way for the AER to understand risk management within energy firms both as this is how the firms themselves think about risk and as it will avoid the AER needing to expend resources attempting to piece together contract by contract data and information about physical assets to ultimately produce a very similar result.

#### **D. Offer decisions**

Generators decisions about how to offer their capacity to the market are complex involving a combination of the firms' overall risk management strategy and short-term physical market factors such as constraints, outages and NEM price spikes. The AER currently expends significant resources analysing generating behaviour based on their observation of the extensive publicly available data on the physical market and AFMA does not think that participants hold any additional data that would assist the AER to understand the physical market drivers of participant behaviour.

An understanding of generators risk management approach could assist the AER to understand their decisions to offer generation to the NEM. We suggest that the generators high level risk positions (as discussed above in section C) will probably be the most useful information to assist the AER understand generator behaviour. But we caution that the generators risk positions are only one factor in their decisions to offer capacity that is probably more likely to help the AER understand long term trends in offering behaviour rather than short term behaviour, which is often influenced by physical market issues.

#### **3.5. What don't you need to collect?**

As stated in our earlier submissions AFMA considers that the AER should only collect data that will assist them to perform their market monitoring function.<sup>4</sup> We note that the Bill's provisions about the scope of the information the AER may collect are slightly more limited than initially proposed but we continue to think that the following types of information are unlikely to assist the AER to perform its functions and suggest the guidelines should clarify that they will not collect this information:

1. **Contracts for the transmission or distribution of electricity** – in the current regulated open access framework it is unclear what value these contracts would have for the AER.
2. **Contracts relating to fuel and other inputs used in the generation of electricity** – the information in these will primarily relate to the cost of coal, gas and liquid fuels. These are all tradable commodities with easily observable prices. We do not think individual firms supply contracts would provide enough value to warrant collection of the data.

Additionally, our members think the guidelines should place the following restrictions on the collection of gas contract information:

1. Impose a de-minimis threshold for collecting gas contract information to reduce the cost of compliance by avoiding having to report data about large numbers of small contracts. We suggest that this could be set at contracts with a term of less than 3 months or a total contract quantity below 500TJ.
2. Not require the provision of correspondence regarding the process of entering into gas contracts. Members experience from the ACCC's gas inquiry is that providing this information is extremely time consuming and we do not consider that it is necessary for the AER's market monitoring.

#### **3.6. The collection process**

As discussed above the AER's approach to data collection will be the main influence on the cost of the market monitoring function for market participants. While AFMA considers that the critical

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<sup>4</sup> [AFMA submission to DCC/EEW consultation on Wholesale Market Monitoring and Reporting Reforms](#)

factor is for the AER to settle on an approach to data collection and limit changes to it we also have the following comments on how the collection process should be designed.

#### **A. Frequency**

The frequency of data collection will clearly have a significant impact on the cost of complying with the reporting obligations. AFMA's observation is that in both the gas and electricity markets participants' contracting behaviour is generally driven by managing peak summer and winter demand, with the shoulder seasons generally being relatively quiet periods, and that most contracting is done 12-24 months in advance. We therefore suggest that there will be limited benefit in very frequent data collection as participants will typically build up their position between 24 and 12 months before the relevant peak period and then will make only limited changes in the 12 months before the relevant peak period.

As a result, AFMA's view is that 6 monthly data collection is likely to be adequate for AER's purposes as it will be sufficiently granular to allow the AER to observe how participants manage their exposures to seasonal peaks.

#### **B. Notices, orders and general information powers**

The AER will have three mechanisms to collect information; its general information gathering powers, Market Monitoring Information Orders and Market Monitoring Information Notices. The general information powers are fairly broadly framed but only allow the collection of information that already exists. Orders and notices can require participants to collect data in a particular form with orders applying to a class of people and notices applying to a single person.

AFMA's observation is that the order and notice powers are likely to be more useful for the AER than the general information powers as they allow the AER to specify how data is provided. Of the two we consider that orders are likely to be the most appropriate for the contract monitoring function as they are designed to apply to a class of people and we anticipate that, generally, the AER will wish to collect information from a class of people rather than just from an individual firm. Orders also have additional transparency benefits as they are public, and the AER must consult before publishing an order. AFMA would appreciate it if the guidelines could provide guidance about when the AER expects to use each type of information powers and in our view the guidelines should express a clear preference for using orders in most circumstances.

#### **C. Backwards looking data**

The Bill allows the AER to collect data for the period 5 years before it commences. Requiring participants to provide backward looking data is significantly more costly and administratively burdensome than current and forward-looking data as it will be less readily available, will require more interpretation and may be stored in archived or retired IT systems. AFMA therefore encourages the AER to be cautious about requesting backward looking data and to the extent that they think they need historic data we encourage them to rely on data that was previously collected by other regulators or market bodies. Specifically, we want to point out that the ACCC's Gas inquiry commenced in 2017 and their electricity inquiry commenced in 2018 so we would expect that the ACCC will have high quality data for these periods.<sup>5</sup> We therefore encourage the AER to attempt to rely on this data rather than requesting additional data from participants.

### **3.7. Confidentiality**

Given that much of the information the AER will be collecting will be confidential, we think it is appropriate that the guidelines provide clarity about how the AER will deal with confidential information. Currently the AER's handling of confidential information is governed by its 2017 Confidentiality Guidelines which are primarily directed at the handling of information provided by

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<sup>5</sup> The ACCC's electricity reports look at wholesale market contracting from January 2021.



network service providers, we consider that the AER should either review these guidelines to ensure they are suitable for the market monitoring functions or develop dedicated guidelines for the new function.

AFMA has previously raised concerns about the use of market monitoring information for the AER's compliance activities, while we appreciate that no restrictions have been placed on this we think the guidelines could clarify that these powers will not be used to collect information where the main purpose of the information collection is compliance and enforcement and should provide guidance about when information collected under these powers will be used for compliance and enforcement functions.

Publishing information about the market is a significant part of the AER's market monitoring function. While we appreciate the benefits of providing this transparency the AER will need to be careful about what information it chooses to disclose. We think it would be helpful for the guidelines to set out how it intends to disclose information. We think the guidelines should set out a strong preference for publishing de-identified aggregated data where possible. We also think the guidelines should include a process for consulting with the data provider before disclosing their confidential information to allow them to identify information that should not be published and to comment on any findings the AER is proposing to make.

#### **AFMA Recommendations**

- iii. The AER should publish detailed proposed data requirements at the earliest possible time to facilitate participants providing feedback on their proposed approach.
- iv. The guidelines should provide clarity about who the AER expects to collect information from.
- v. The AER should provide guidance about how they expect to move to a mature reporting framework.
- vi. The AER should conduct initial analysis based on information that is already held by other regulators and they should use insights gained from this work to determine any additional data requirements.
- vii. The policy challenges of futures market access should be explored by DCCEE and Treasury, rather than as part of the AER's market monitoring function.
- viii. The AER should request aggregated data to understand firms risk positions.
- ix. The guidelines should clarify that the AER will not collect information about the transmission or distribution of electricity or the cost of fuel for generators.
- x. The guidelines should impose a de-minimis threshold for collecting gas contract data and clarify that the AER will not require the provision of correspondence regarding the negotiation of gas contracts.
- xi. Data should be collected once every 6 months.
- xii. The guidelines should provide clarity about under what circumstances the AER will use its general information powers, issue notices and make orders.
- xiii. The AER should rely on the ACC's historic contract market data rather than requesting data from market participants.
- xiv. The guidelines should deal with the treatment of confidential information.
- xv. The AER's existing confidentiality guideline should also be updated.

AFMA would welcome the opportunity to discuss this submission further and would be pleased to provide further information or clarity as required. Please contact me at [lgamble@afma.com.au](mailto:lgamble@afma.com.au) or 02 9776 7994.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Lindsay Gamble', written in a cursive style.

Lindsay Gamble

**Head of Energy and Carbon**