

BETWEEN:

ECONOMIC REGULATION AUTHORITY Applicant

and

ENERGY GENERATION AND RETAIL CORPORATION Respondent

**RESPONDENT'S FURTHER AMENDED STATEMENT OF FACTS, ISSUES
AND
PRINCIPAL CONTENTIONS**

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PRELIMINARY

In this document:

- a. capitalised terms, unless otherwise indicated, have the same meanings as those terms in Chapter 11 of the Wholesale Electricity Market Rules (**Market Rules**); and
- b. the version of the Market Rules referred to is the version as at 1 July 2016.

A. **FACTS**

(1) **Parties**

1 The Respondent does not dispute the facts set out in paragraph 1 of the Applicant's Statement of Facts, Issues and Contentions (**Applicant's Statement**).

2 Save to say that the Respondent:

- (a) is registered under the Market Rules as a Market Generator and Market Customer; and
- (b) operated 18 gas-fired generators in the Balancing Portfolio during the ERA's investigation period (**Investigation Period**),

the Respondent does not dispute the facts set out paragraph 2 of the Applicant's Statement.

(2) **The Wholesale Electricity Market (WEM)**

3 In relation to paragraph 3 of the Applicant's Statement, the Respondent says:

- (a) the Wholesale Electricity Market (**WEM**) comprises a wholesale electricity trading component and a capacity component;
- (b) the WEM includes:
 - (i) the Reserve Capacity Mechanism (**RCM**) to ensure that adequate generation capacity is available to satisfy demand for electricity;
 - (ii) a Short Term Energy Market (**STEM**), which allows Market Participants to trade relative to their bilateral contract positions a day ahead of real time and ensures that the cheapest generators will operate to provide all of their electricity forecasted to be required for that day;
 - (iii) a competitive Balancing Market which ensures that any real time differences in electricity supply and demand that occur on the day are provided by the cheapest generators available;

- (iv) a settlement process undertaken by AEMO for the STEM and the Balancing Market which ensures settlement is net of any bilateral contract positions already advised to AEMO so that Market Participants are not charged or paid for energy they have already been charged or paid for through bilateral contracts;
- (v) the competitive supply of Load Following Ancillary Services; and
- (vi) a regulated contract market, with an administered pricing mechanism for the Respondent as, effectively, a supplier of last resort, for the provision of other Ancillary Services as set out in clause 3.11 of the Market Rules.

4 The Respondent does not dispute the matters set out paragraph 4 of the Applicant's Statement.

5 The Respondent does not dispute the matters set out in paragraph 5 of the Applicant's Statement.

6 In relation to paragraph 6 of the Applicant's Statement, the Respondent repeats paragraph 3 above.

7 Save to say that the RCM:

- (a) has the purpose of procuring at least the capacity required to sufficiently maintain system security and meet expected demand within the SWIS;
- (b) pays providers of capacity, primarily generators, for making capacity available even if they are not required to deliver electricity into the system;
- (c) has a detailed capacity planning system, a payment for providing capacity and a payment reduction or refund system which requires generators who have contracted to provide capacity to refund capacity payments by means of Capacity Cost Refunds in relation to periods when the capacity is not available or reduced;

- (d) does not necessarily procure an efficient quantity of generation capacity because it procures at least the capacity required to meet the Planning Criterion, being the capacity required to:
 - (i) meet the forecast capacity required to meet a one in ten year peak demand event plus a margin for other contingencies, such as Ancillary Services and to address the risk that some facilities may be physically unavailable when needed (clause 4.5.9(a)); and
 - (ii) limit expected energy shortfalls to 0.002% of annual energy consumption (clause 4.5.9(b)),

without consideration of the efficient costs of the facilities providing the capacity the RCM procures;

- (e) ensures that at least the capacity required to meet the Planning Criterion is procured and is not concerned with encouraging a particular configuration of generation types; and
- (f) derives the payments for capacity under the Market Rules by reference to the capital and fixed operating and maintenance costs of a specific, hypothetical peaking facility (since 1 July 2016, called the Benchmark Reserve Capacity Price or, before that date, the Maximum Reserve Capacity Price) and, at all times during the Investigation Period, the Benchmark Reserve Capacity Price acted as an effective cap on the price payable for capacity under the Market Rules so that the price payable for capacity under the Market Rules was always at least 15% less than the Benchmark Reserve Capacity Price (clause 4.29.1(b)),

the Respondent disputes each and every matter set out in paragraph 7 of the Applicant's Statement.

8 The Respondent does not dispute the matters set out in paragraph 8 of the Applicant's Statement but says further that:

- (a) the Balancing Market is a compulsory price-based dispatch and settlement process that provides for settlement of differences between the contracted positions of Market Participants, being

Market Generators and Market Customers, and the actual electricity generated, dispatched and consumed by each Market Participant in respect of each Trading Interval; and

- (b) the Balancing Market is a net settlement market, which means that a Market Participant only pays or receives the Balancing Price to the extent that its net real-time consumption and generation differs from the net amount of electricity the Market Participant is committed to buying or selling through mechanisms outside of the Balancing Market, such as under bilateral contracts or as a result of STEM trades.

9 In relation to paragraph 9, the Respondent says:

- (a) during the Investigation Period, the Respondent was only able to make Balancing Submissions for Trading Intervals in the Balancing Horizon at the times listed in the first column of the table **below** for Trading Intervals in the periods listed in the second column. The Respondent could not change the Balancing Submissions made at the time specified in the first column for Trading Intervals falling in the period listed in the third column:

Respondent's Submission / Re-submission Time	For Trading Intervals in the Balancing Horizon	Trading Intervals in respect of which the Respondent cannot re-bid after the time in First Column
Before 6:00PM	2:00AM+ (i.e. from 2:00AM on the current Trading Day until the end of the next Trading Day at 8:00AM. This equates to a 30 hour period)	Nil because in practice superseded by 10:00pm submission / resubmission
10:00PM	2:00AM+ (i.e. for a 30 hour period)	2:00AM to 7:59AM (i.e. for a 6 hour period)

Respondent's Submission / Re-submission Time	For Trading Intervals in the Balancing Horizon	Trading Intervals in respect of which the Respondent cannot re-bid after the time in First Column
4:00AM	8:00AM+ (i.e. for a 24 hour period)	8:00AM to 1:59PM (i.e. for a 6 hour period)
10:00AM	2:00PM+ (i.e. for an 18 hour period)	2:00PM to 7:59PM (i.e. for a 6 hour period)
4:00PM	8:00PM+ (i.e. for a 12 hour period)	8:00PM to 1:59AM (i.e. for a 6 hour period)

- (b) by reason of the limitations set out in subparagraph (a) above, during the Investigation Period, the Respondent's Balancing Submissions for the Balancing Portfolio could only be made between 4 and 9.5 hours before real-time; and
- (c) Balancing Submissions for any other Balancing Facility owned by a competitor of the Respondent could be resubmitted at any time for any Trading Interval that was at least 2 hours ahead: that is, other Balancing Facilities could always resubmit Balancing Submissions for a Trading Interval at least 2 hours after the Respondent was prevented from resubmitting for that Trading Interval and the Respondent could not respond competitively to those re-submissions.

- 10 The Respondent does not dispute the matters set out in paragraph 10 of the Applicant's Statement.
- 11 The Respondent does not dispute the matters set out in paragraph 11 of the Applicant's Statement.

12 Save to say that:

- (a) the Respondent was obliged under the Market Rules to operate its Balancing Portfolio as a single Balancing Facility in the Balancing Market unless System Management / the Australian Energy Market Operator has approved removal of facilities on a 'Stand Alone Facility' basis under clause 7A.4 of the Market Rules; and
- (b) the Respondent was subject to the limitations on submitting and resubmitting set out in paragraph 9 above, as well as other requirements not applicable to other Market Participants (such as the requirement to provide LFAS and other Ancillary Services and the fact that System Management dispatches the Respondent's Facilities in real-time),

the Respondent does not dispute paragraph 12 of the Applicant's Statement.

13 The Respondent denies paragraph 13 and says that the Respondent set the Balancing Price-Quantity Pairs for the Balancing Portfolio for each Trading Interval in the Investigation Period by creating a monotonically increasing price curve, which was based on the average operating cost of the marginal facility each half hour for a forecasted demand.

14 The Respondent does not dispute the matters set out in paragraph 14 of the Applicant's Statement but says that monotonically increasing prices are required for Balancing Submissions by reason of the design of the WEM.

15 Save to say that:

- (a) when scheduling and issuing Dispatch Instructions or Dispatch Orders, System Management must seek to meet the criteria stipulated by clause 7.6.1 and comply with clauses 7.6.1A to 7.6.2A of the Market Rules;
- (b) subject to System Management's obligations under clause 7.6 of the Market Rules, clause 7.6A of the Market Rules governs the relationship between System Management and the Respondent for the purpose of scheduling and dispatching the Stand Alone

Facilities for Ancillary Services and for scheduling and dispatching Facilities in the Balancing Portfolio generally (clause 7.6A.1);

- (c) a Market Participant to which a Dispatch Instruction or Operating Instruction is issued by System Management may advise System Management that it cannot comply or cannot fully comply, in which case System Management may issue a new instruction (clauses 7.7.6 to 7.7.7A of the Market Rules);
- (d) a Market Participant is not required to comply with a Dispatch Instruction, Operating Instruction or Dispatch Order in the circumstances stipulated in clause 7.10.2 of the Market Rules;
- (e) the Balancing Price is the price at which actual demand plus 1MW meets actual supply;
- (f) the Balancing Price is paid for any deviations between a Market Participant's net actual generation and actual demand and the Market Participant's Net Contract Position, as determined by AEMO pursuant to clause 6.9.13 of the Market Rules; and
- (g) the Balancing Price is the same for each Market Participant in a particular Trading Interval regardless of the price offered by each Market Generator in its Balancing Submissions,

the Respondent does not dispute paragraph 15 of the Applicant's Statement.

(3) The ERA's investigation

16 The Respondent does not dispute paragraph 16 of the Applicant's Statement.

17 The Respondent does not dispute paragraph 17 of the Applicant's Statement.

18 The Respondent does not dispute paragraph 18 of the Applicant's Statement.

19 The Respondent does not dispute paragraph 19 of the Applicant's Statement.

20 The Respondent does not dispute paragraph 20 of the Applicant's Statement.

21 The Respondent does not dispute paragraph 21 of the Applicant's Statement.

22 The Respondent does not know, and therefore cannot admit, the matters alleged in paragraph 22 of the Applicant's Statement.

23 The Respondent does not dispute paragraph 23 of the Applicant's Statement.

24 The Respondent does not dispute paragraph 24 of the Applicant's Statement.

25 In relation to paragraph 25 of the Applicant's Statement:

(a) the Respondent admits that clause 7A.2.17 of the Market Rules is a Category C Market Rule;

(b) the Respondent does not know and cannot admit what the Applicant believes;

(c) the Respondent denies that the prices it offered in its Balancing Submissions for 12,908 of the 14,812 Trading Intervals investigated by the Applicant exceeded the Respondent's reasonable expectation of the SRMC of generating the relevant electricity and that that behaviour related to market power; and

(d) the Respondent denies that it breached clause 7A.2.17 of the Market Rules.

26 The Respondent does not dispute paragraph 26 of the Applicant's Statement.

27 The Respondent does not dispute paragraph 27 of the Applicant's Statement.

(4) Market circumstances relevant to the investigation and proceedings

28 The Respondent does not dispute paragraph 28 of the Applicant's Statement.

- 29 The Respondent does not dispute paragraph 29 of the Applicant's Statement.
- 30 In relation to paragraph 30:
- (a) the Respondent does not source gas to cover storage;
 - (b) the Respondent uses the Mondarra storage facility to manage fluctuations in supply and demand affecting its overall daily gas quantity requirements; and
 - (c) the Respondent otherwise does not dispute the matters set out in paragraph 30 of the Applicant's Statement.
- 31 The Respondent does not admit the matters in paragraph 31 of the Applicant's Statement.
- 32 The Respondent does not dispute paragraph 32 of the Applicant's Statement.
- 33 The Respondent does not dispute paragraph 33 of the Applicant's Statement.
- 34 The Respondent disputes paragraph 34 of the Applicant's Statement and says that the DMIRS data indicates that average gas prices continued to trend upwards from 2016 to 2017.
- 35 The Respondent does not dispute paragraph 35 of the Applicant's Statement.
- 36 The Respondent does not dispute paragraph 36 of the Applicant's Statement.
- 37 The Respondent does not dispute paragraph 37 of the Applicant's Statement.
- 38 The Respondent does not dispute paragraph 38 of the Applicant's Statement.
- 39 The Respondent does not admit paragraph 39 of the Applicant's Statement and says:

- (a) prices received by the Respondent for periods outside of the Investigation Period are not relevant to this case; and
- (b) the gas prices received by the Respondent under industrial gas sale agreements during the Investigation Period are not relevant to the Respondent's reasonable expectation of its SRMC.

40 Save to say that:

- (a) the North West Shelf Gas Contract (**NWS Contract**) ended on 29 November 2016; and
- (b) during the Investigation Period, the Respondent was a party to 2 contracts for the supply of gas from the Gorgon Gas Project (**Gorgon Contracts**),

the Respondent does not dispute paragraph 40 of the Applicant's Statement.

41 The Respondent does not dispute paragraph 41 of the Applicant's Statement.

42 The Respondent says that successive notices were issued on the first shown dates below which changed the Start Date for deliveries of gas from the Gorgon project to the second shown dates below:

- (a) 14 October 2015 – Revised Start Date - 1 April 2016;
- (b) 14 April 2016 – Revised Start Date – 14 May 2016;
- (c) 17 June 2016 – Revised Start Date – 1 July 2016;
- (d) 29 July 2016 – Revised Start Date – 11 August 2016;
- (e) 31 August 2016 – Revised Start Date – 15 September 2016;
- (f) 28 October 2016 – Revised Start Date – 25 November 2016;
- (g) 21 November 2016 – Revised Start Date – 28 November 2016; and
- (h) 25 November 2016 – Revised Start Date – 6 December 2016,

but otherwise does not dispute paragraph 42 of the Applicant's Statement.

43 The Respondent disputes paragraph 43 of the Applicant's Statement and says that:

- (a) the take or pay proportion of its Gorgon Contracts was [REDACTED] of the ex-Verve contract for [REDACTED] and [REDACTED] of the ex-Synergy contract for [REDACTED];
- (b) the variable quantities under the Gorgon Contracts were discretionary and the price was [REDACTED] the take or pay portion; and
- (c) the volume weighted average gas price under the Gorgon Contracts during the Investigation Period was [REDACTED].

44 The Respondent disputes paragraph 44 of the Applicant's Statement.

45 Save to say that:

- (a) the commencement of the substitution period in the [REDACTED] Gas Swap Arrangement was deferred to 14 November 2016;
- (b) during the substitution period, the maximum volume the Respondent was entitled to deliver to [REDACTED] was [REDACTED];
- (c) at the Respondent's request, the commencement of the supply period for the return of gas was deferred until 28 April 2018; and
- (d) the Respondent was entitled to nominate a maximum of [REDACTED] to be supplied by [REDACTED],

the Respondent does not dispute paragraph 45 of the Applicant's Statement.

46 The Respondent does not dispute paragraph 46 of the Applicant's Statement.

47 Save to say that:

- (a) the Respondent entered into a gas contract with [REDACTED] for the period from 21 July 2016 to 31 October 2016;

(b) the initial supply period was for an [REDACTED] contract quantity of [REDACTED]; and

(c) the contract was not relevant to the Respondent's reasonable estimate of its SRMC of gas during the Investigation Period,

the Respondent does not admit paragraph 47 of the Applicant's Statement.

48 In relation to paragraph 48 of the Applicant's Statement, the Respondent says that:

(a) [Blank]

(b) the contract was not relevant to the Respondent's reasonable estimate of its SRMC of gas during the Investigation Period; and

(c) otherwise does not admit the allegations in the paragraph.

(5) The Respondent's change to input costs

49 The Respondent does not dispute paragraph 49 of the Applicant's Statement.

50 The Respondent does not dispute paragraph 50 of the Applicant's Statement.

50A The Respondent admits paragraph 50A of the Applicant's Statement.

51 Save to say that:

(a) estimated start-up costs and estimated gas fuel costs are two significant input costs used to determine the Respondent's SRMC for the Balancing Portfolio during the relevant Trading Intervals; and

(b) the determination of the Respondent's reasonable expectation of its short run marginal cost in a Trading Interval would vary depending upon:

(i) the estimate of input costs and start-up costs used in that Trading Interval; and

(ii) the estimate of input costs, start-up costs and associated plant run times in subsequent Trading Intervals; and

- (iii) the modelling assumptions made in determining the estimated SRMC,

the Respondent disputes paragraph 51 of the Applicant's Statement.

52 As to paragraph 52 of the Applicant's Statement, the Respondent:

- (a) admits that there is a relationship between the estimated input costs used to calculate its SRMC and the prices in a Balancing Submission;
- (b) says that relationship is complex and that there is an interrelationship between estimated inputs and assumptions made across Trading Intervals which can affect prices in a Balancing Submission: for example in some cases increasing inputs such as gas or start-up costs can increase the prices in some Balancing Submissions and decrease the prices in other submissions; and
- (c) otherwise does not admit the allegations in the paragraph.

52A The Respondent disputes paragraphs 52A and 52B and says:

- (a) the relationship between the estimated input costs used to calculate its SRMC and the prices in a Balancing Submission is complex;
- (b) there is an interrelationship between estimated inputs and assumptions made across Trading Intervals which can affect prices in a Balancing Submission;
- (c) if Synergy were to increase its gas and/or start-up costs, this would change the assumptions its uses to prepare its Balancing Submissions for generators in the Balancing Portfolio. In some cases, increasing inputs such as gas or start-up costs can increase the prices in some Balancing Submissions and decrease the prices in other Balancing Submissions.

53 As to paragraph 53 of the Applicant's Statement, the Respondent:

- (a) does not dispute paragraph 53(a) of the Applicant's Statement;

(b) says the Respondent's revised estimated start-up costs, were, in total higher than its estimated total start-up costs using its previous method of calculation; and

(c) otherwise disputes the allegations in the paragraph.

(a) Change in calculation of gas input price

54 The Respondent repeats paragraph 51 but otherwise does not dispute paragraph 54 of the Applicant's Statement.

55 The Respondent does not dispute paragraph 55 of the Applicant's Statement.

56 As to paragraph 56 of the Applicant's Statement, the Respondent:

(a) calculated estimated gas input prices on an opportunity cost basis in Periods 2 and 3;

(b) advised the ERA of this change in approach on 8 August 2016; and

(c) otherwise does not admit paragraph 56 of the Applicant's Statement.

Period 1

57 Save to admit that the Respondent applied an estimated gas input price of [REDACTED] (undelivered) to calculate its SRMC during Period 1, the Respondent does not admit paragraph 57 of the Applicant's Statement.

58 [Blank].

Period 2

59 The Respondent does not dispute paragraph 59 of the Applicant's Statement.

60 Save to say that in Period 2 the Respondent:

(a) changed the way it estimated its gas input cost relative to how it estimated that value in Period 1 to reflect the future value of gas; and

(b) subsequently refined its estimate of the future value of gas by reference to an opportunity cost model,

the Respondent otherwise disputes paragraph 60 of the Applicant's Statement.

61 The Respondent disputes paragraph 61 of the Applicant's Statement.

62 As to paragraph 62 of the Applicant's Statement, the Respondent:

(a) assumed it had opportunities to inject stored gas of [REDACTED] and extract up to [REDACTED] at the Mondarra storage facility;

(b) otherwise disputes the allegations in the paragraph.

Period 3

63 The Respondent does not dispute paragraph 63 of the Applicant's Statement.

64 The Respondent repeats paragraph 62 and otherwise denies paragraph 64 of the Applicant's Statement.

65 The Respondent repeats paragraph 62 and otherwise disputes paragraph 65 of the Applicant's Statement.

(b) Updated Generator Start-up Costs

66 The Respondent does not dispute paragraph 66 of the Applicant's Statement.

67 Save that the update to the Respondent's start-up costs resulted from a reduction in the operating time of the Respondent's gas plant, the Respondent does not dispute paragraph 67.

68 The Respondent disputes paragraph 68 of the Applicant's Statement and says:

(a) nominal forecasts prepared by the Respondent with respect to predicted starts over the short term were undertaken for the purpose of scheduling maintenance and did not represent the Respondent's latest expectation of the total number of lifetime starts applicable to its facilities;

- (b) decisions related to the retirement date of the Respondent's facilities were not based solely on notional lifetimes and/or operational goals but were made in response to, among other things, market conditions and other factors outside the Respondent's control;
- (c) because the retirement dates for facilities such as generation plant are uncertain, until a final decision is made to retire a facility on a date certain, it was not possible to accurately predict a definitive number of lifetime starts applicable to a facility;
- (d) the Respondent assumed that [REDACTED]
[REDACTED]
[REDACTED]; and
- (e) the Respondent's approach to start-up costs was consistent with common industry practice amongst facility operators and was reasonable.

69 The Respondent does not admit paragraph 69 of the Applicant's Statement.

(6) Costs included in the Respondent's start-up costs

70 The Respondent disputes paragraph 70 of the Applicant's Statement.

71 The Respondent repeats paragraph 68 above and otherwise disputes paragraph 71 of the Applicant's Statement.

72 The Respondent disputes paragraph 72 of the Applicant's Statement and says that, by reason of the design of the RCM, some recovery of initial capital costs must occur in the other markets, including the Balancing Market. That is:

- (a) when the RCM has no spare capacity, it only provides for, at most, the recovery of capital costs for the hypothetical 160MW liquid-fuelled OCGT (see paragraph 7(f)), being the lowest cost facility to build to provide capacity and only when the RCM price results from an auction, an event which has never happened in the WEM;

- (b) any other type of facility in any other circumstance must recover its fixed costs and its operating costs through a combination of revenues from the RCM and the Balancing Market and any other sources available to it;
- (c) the RCM price adjusts downwards when there is excess capacity and as there has always been excess capacity in the WEM and no auction, even the hypothetical 160MW OCGT could not recover the costs of its initial built capital without also receiving revenue from other markets;
- (d) other than in the circumstances described in (a), the RCM price is not designed for cost recovery; rather it is a price that provides a signal that:
 - (i) new capacity is needed when there is no excess capacity (because the RCM price approaches the price that would enable the hypothetical 160MW OCGT to be built and recover its costs); or
 - (ii) no new capacity is needed when there is excess capacity (because the RCM price is insufficient to enable the hypothetical 160MW OCGT to be built); or
 - (iii) capacity needs to be removed from the market when there is too much excess capacity (because the RCM price is so low that the currently built facilities are unable to remain viable with a combination of RCM, STEM, Balancing, Bilateral and Ancillary Services revenue).

73 In relation to paragraph 73 of the Applicant's Statement:

- (a) the Respondent repeats paragraph 68 above;
- (b) it was reasonable to expect that the actual cost for any capital part or any particular variable maintenance costs would be higher than the Respondent's estimate due, for example, to facilities' actual lifetimes differing from expectations and the unexpected failures of parts before the end of the parts' expected lifetimes; and

(c) the Respondent otherwise disputes the allegations in the paragraph.

74 The Respondent repeats paragraphs 68 and 73 above and otherwise disputes paragraph 74 of the Applicant's Statement.

75 The Respondent repeats paragraphs 68 and 73 above and otherwise disputes paragraph 75 of the Applicant's Statement.

76 The Respondent repeats paragraphs 68 and 73 above and otherwise disputes paragraph 76 of the Applicant's Statement.

77 The Respondent admits paragraph 77 of the Applicant's Statement.

(7) Fixed operating and maintenance costs

78 In relation to paragraph 78 of the Applicant's Statement:

(a) a portion of the Respondent's costs incurred under the heading "routine maintenance" would not be incurred but for the operation of its facilities, and are therefore variable in nature;

(b) the Respondent's allocation of maintenance costs reflected the Respondent's reasonable expectation that a portion of its maintenance costs are incurred as a result of corrective rather than preventative maintenance; and

(c) the Respondent disputes the allegations in the paragraph.

B. ISSUES

79 The Respondent says that the issues that arise in the Application are:

(a) Issue 1: Did the Respondent offer prices in its Balancing Submissions during the relevant Trading Intervals the subject of the application in excess of its reasonable expectation of the SRMC of generating the relevant electricity?;

(b) Issue 2: Did the Respondent have market power in the Balancing Market during the relevant Trading Intervals the subject of the application?; and

- (c) Issue 3: Was the Respondent's pricing behaviour related to market power in the Balancing Market?

C. CONTENTIONS

ISSUE 1: WHETHER THE RESPONDENT OFFERED PRICES IN ITS BALANCING SUBMISSIONS IN EXCESS OF ITS REASONABLE EXPECTATION OF THE SRMC OF GENERATING THE RELEVANT ELECTRICITY?

80 The Respondent does not dispute paragraph 80 of the Applicant's Statement.

81 The Respondent says that, by reason of the matters set out in paragraph 100 below, for the purpose of Clause 7A.2.17 the Respondent's estimated SRMC includes its estimated start-up costs and estimated gas costs, and otherwise disputes paragraph 81 of the Applicant's Statement.

82 In relation to paragraph 82 of the Applicant's Statement:

- (a) Estimated fuel costs and estimated start-up costs are two input cost components of the Respondent's reasonable expectation of SRMC; and
- (b) the Respondent otherwise admits the paragraph.

83 The Respondent repeats the matters set out in paragraph 81 above and says that:

- (a) the matters in paragraph 83 of the Applicant's Statement are inconsistent with the matters in paragraph 81 of the Applicant's Statement; and
- (b) otherwise admits the matters set out in paragraph 83 of the Applicant's Statement.

(1) The Respondent offered prices in its Balancing Submissions during Period 1 consistent with its reasonable expectation of its SRMC

84 The Respondent disputes the matters set out in paragraph 84 of the Applicant's Statement.

85 The Respondent disputes the matters set out in paragraph 85 of the Applicant's Statement.

86 In relation to paragraph 86 of the Applicant's Statement, the Respondent:

- (a) repeats paragraphs 68, 73, 77 and 78 above; and
- (b) otherwise disputes the allegations in the paragraph.

(2) The Respondent offered prices in its Balancing Submissions during Period 2 consistent with its reasonable expectation of the SRMC

87 The Respondent disputes the matters set out in paragraph 87 of the Applicant's Statement.

88 The Respondent disputes the matters set out in paragraph 88 of the Applicant's Statement.

89 Save to:

- (a) admit that the Respondent adopted the same approach to estimating its start-up costs in Period 1 and Period 2; and
- (b) repeat the matters set out in paragraphs 68, 73, 77 and 78 above, the Respondent disputes paragraph 89 of the Applicant's Statement.

90 In respect of paragraph 90 of the Applicant's Statement:

- (a) in forming a reasonable estimate of SRMC, Market Participants were not required to have perfect foresight;
- (b) [Blank]
- (c) it was reasonable for the Respondent to base its estimate of the market price of gas on [REDACTED]
[REDACTED]
[REDACTED];
- (d) [Blank]
- (e) in respect of paragraph 90(e) of the Applicant's Statement:
 - (i) the spot and short term markets for the supply of gas were relatively illiquid;

- (ii) it was reasonable for the Respondent to assume that the purchase of substantial volumes of firm gas for its generation requirements would have significantly increased prices in the spot and/or short term markets for the supply of gas; and
- (iii) by reason of the above, it was not unreasonable for the Respondent to estimate that the price at which the Respondent could purchase firm gas in the volumes it required for generation would be significantly higher than the price of gas in the spot market or short term market without those purchases,

(f) the Respondent otherwise disputes the matters set out the paragraph 90.

91 The Respondent repeats the matters set out in paragraph 90 above and otherwise disputes the matters set out in paragraph 91 of the Applicant's Statement.

92 The Respondent repeats the matters set out in paragraph 90 above and the matters set out in paragraphs 81, 83 and 100 below and otherwise disputes paragraph 92 of the Applicant's Statement.

(3) The Respondent offered prices in its Balancing Submissions during Period 3 consistent with its reasonable expectation of SRMC

93 The Respondent disputes paragraph 93 of the Applicant's Statement.

94 The Respondent disputes the matters set out in paragraph 94 of the Applicant's Statement.

95 Save to:

- (a) admit that the Respondent adopted the same approach to estimating its start-up costs in Period 3 as it used in Period 1 and Period 2;
- (b) repeat the matters set out in paragraphs 68, 73, 77 and 78 above;
- (c) repeat the matters set out in paragraphs 89 and 91 above,

the Respondent disputes the matters set out in paragraph 95 of the Applicant's Statement.

96 Save to say that the matters set out in paragraphs 89 and 91 above apply equally to Period 3, the Respondent disputes the matters set out in paragraph 96 of the Applicant's Statement.

97 Save to repeat the matters set out in paragraph 91 above, the Respondent disputes the matters set out in paragraph 97 of the Applicant's Statement.

98 Save to repeat the matters set out in paragraph 91 above, the Respondent disputes the matters set out in paragraph 98 of the Applicant's Statement.

99 As to paragraph 99 of the Applicant's Statement:

(a) during Period 3 the Respondent assumed that it could store ██████████ in December 2016 by injection at the Mondarra storage facility;

(b) at the start of Period 3 (1 December 2016) the Respondent's working gas balance was ██████████, leaving ██████████ available for injection at the Mondarra storage facility;

(c) by the end of December 2016 if the Respondent chose to exercise its opportunity to inject the full amount of gas it was physically able to inject each day, the Respondent had the opportunity to inject up to ██████████ into the Mondarra storage facility; and

(d) the Respondent otherwise disputes the allegations in the paragraph.

100 Further, and in the alternative to paragraphs 89 – 92 and paragraphs 95 – 99 above, the Respondent says that:

(a) at the time that it was forming its reasonable expectation of SRMC in Period 2 and Period 3, firm fuel supply of sufficient volume to meet the Respondent's generation capacity was required by the Market Rules in order for the Respondent to qualify for Capacity Credits (clause 4.11.1);

(b) by reason of (a) above, it was reasonable and necessary for the Respondent to enter into firm, long term gas contracts of sufficient

volumes to meet the Respondent's generation capacity, such as the Gorgon Contracts;

- (c) the Respondent is required to bid all of the capacity of its generation units into the Balancing Market;
- (d) it is therefore reasonable for the Respondent to recover the actual cost of the gas it has contracted to buy to operate rather than to operate at a loss, which would be contrary to the Market Objectives in the Market Rules;
- (e) if the Respondent were required to set its Balancing Submission prices by reference to the spot or short term price of gas:
 - (i) the Respondent would have a strong incentive to inefficiently minimise its use of long-term gas supply agreements and rely on spot-sourced gas; and
 - (ii) the volumes of gas required by the Respondent would have exceeded the volumes available under the Gorgon Contract and in the spot market or, even if available, would have resulted in inefficient spot prices exceeding estimated gas input prices used by the Respondent;
- (f) a construction of clause 7A.2.17 of the Market Rules that required the outcome pleaded in the preceding subparagraph would be inconsistent with the wholesale market objective of promoting economically efficient, safe and reliable supply of electricity; and
- (g) the proper construction of clause 7A.2.17 of the Market Rules is that:
 - (i) in forming its reasonable expectation of the cost of the gas which it requires to produce its next incremental unit of production in its gas-fired units for the purpose of its Balancing Submission, the Respondent may have regard to the actual cost of the gas which it has

contracted to buy for the purpose of producing the relevant electricity; and

- (ii) in forming its reasonable expectation of the inputs (including plant run time and fuel costs) which it requires to produce its next incremental unit of production in one Trading Interval, the Respondent must take into account reasonable expectations of the inputs (including plant run time and fuel costs) which it requires to produce its next incremental unit of production in one or more subsequent Trading Interval.

101 Further and in the alternative to paragraphs 89 – 92, paragraphs 95 – 99 and paragraph 100 above, the use of the Respondent's estimate of gas input prices and start-up costs in the Respondent's offers in the relevant Trading Intervals the subject of this Application did not result in the Respondent offering prices in its Balancing Submissions in excess of its reasonable expectation of the SRMC of generating the relevant electricity.

ISSUE 2: WHETHER THE RESPONDENT HAD MARKET POWER DURING THE INVESTIGATION PERIOD?

102 The Respondent does not dispute the matters set out in paragraph 100 of the Applicant's Statement.

103 The Respondent:

- (a) -disputes the matters set out in paragraph 101(a) – (h) of the Applicant's Statement;
- (b) repeats the matters pleaded at paragraph 50A;
- (c) says that on its proper construction, market power in clause 7A.2.17 is the ability to raise prices above competitive levels profitably and there is no evidence that, in the relevant Trading

Intervals during the Investigation Period, the Respondent was able to raise prices above competitive levels profitably.

(1) The Respondent's ability to set the Balancing Price or materially influence the Balancing Price in the Balancing Market

103 The Respondent disputes the matters set out in paragraph 102 of the Applicant's Statement.

104 In relation to paragraph 103 of the Applicant's Statement:

- (a) by reason of the Respondent's position as both a Market Customer and a Market Generator, it is not always in the Respondent's interest for the Balancing Price to be high;
- (b) the Respondent did not and could not know if it would be exposed to the Balancing Market as a net buyer or a net seller in any particular Trading Interval and therefore did not and could not know whether it would be commercially advantageous for there to be a high Balancing Price or a low Balancing Price at the time of making its Balancing Submissions;
- (c) [Blank]
- (d) the Respondent had a large number of customer loads assigned to it, which are heavily temperature-dependant, which means that those loads may have consumed, in real time, more or less than expected at the time the Respondent made its Balancing Submissions;
- (e) the Respondent had a large number of generation facilities and the dispatch of those facilities was determined by System Management, based primarily on comparison of the Respondent's Balancing Submissions and all other Market Generators' Balancing Submissions, subject to the matters set out in paragraphs 15(a) to 15(d) above;
- (f) the Respondent otherwise disputes the allegations in the paragraph.

105 In relation to paragraph 104 of the Applicant's Statement:

- (a) the Respondent repeats the matters set out in paragraph 105;
- (b) [Blank]
- (c) by reason of clauses 7A.2.1(b) and 7A.2.9(d) of the Market Rules, the Respondent does not know at the time it makes its Balancing Submissions what prices and quantities its competitors will include in their Balancing Submissions for the same Trading Interval, and so it does not know the amount of electricity it will be required to produce in a Trading Interval;
- (d) Balancing Submissions for any other Balancing Facility owned by the Respondent's competitors can be resubmitted at any time for any Trading Interval that is at least 2 hours in the future (i.e. can be submitted 2 hours before real-time) (see clause 7A.2.2(b));
- (e) as a result of the matters in (c) and (d), any market power that the Respondent would otherwise have (which is denied) is materially diminished or mitigated because it is unable to affect the final Balancing Price in the way that other Market Participants are permitted to do;
- (f) [Blank]
- (g) as a result of the matters in (c), (d) and (e), and each of them, the Respondent did not have market power in the Balancing Market as it was not able to profitably alter Balancing Prices from competitive levels for the relevant Trading Intervals by reason of using its gas price input and gas plant start-up methodologies; and
- (h) the Respondent disputes the allegations in the paragraph.

(2) The Balancing Market

106 As to paragraph 105 of the Applicant's Statement, the Respondent :

- (a) repeats paragraph 8 above; and
- (b) otherwise does not admit the allegations in the paragraph.

107 As to paragraph 106 of the Applicant's Statement:

- (a) the Respondent repeats paragraph 8 above;

- (b) says that the Respondent's proportion of total accredited generation capacity and total dispatched energy in the WEM:
 - (i) includes capacity and energy the Respondent is required by the Market Rules to make available for ancillary services, which are excluded from the Balancing Market; and
 - (ii) in any event is not relevant to market power in the Balancing Market as described in paragraph 8 above;
- (c) the total accredited generation capacity and total dispatched energy in the WEM is not relevant to a consideration of the pricing behaviour of the Respondent in relation to the Trading Intervals the subject of the Applicant's investigation set out in paragraph 22;
- (d) in any event, the Respondent's pricing conduct did not result in an increase to its proportion of total accredited generation during the Investigation Period as compared to its proportion prior to the Investigation Period either:
 - (i) generally; or
 - (ii) for Trading Intervals where the Respondent's gas plant was the marginal plant which set the Balancing Price, using its gas price input and gas plant start-up methodologies.
- (e) the Respondent repeats the matters set out in paragraphs 105, 106 and 107 above; and
- (f) the Respondent disputes the allegations in the paragraph.

(3) Alleged price discrimination during Period 2 and Period 3

108 The Respondent does not admit paragraph 107 of the Applicant's Statement.

109 As to paragraph 108 of the Applicant's Statement:

- (a) the Respondent admits that, in Period 2 and Period 3, it applied a gas input price in its estimate of the prices it offered in Balancing

Submissions which was above the price at which it sold gas in the industrial gas market;

- (b) says the price of gas in the industrial gas market is not relevant to the Respondent's estimate of its SRMC; and
- (c) the Respondent otherwise disputes the allegations in the paragraph.

110 As to paragraph 109 of the Applicant's Statement:

- (a) for the reasons set out in paragraphs 105, 106 and 107 above, the Respondent disputes that it has market power in the Balancing Market at the relevant times;
- (b) if the prices of the Respondent's gas input costs in its Balancing Submissions had been equivalent to the prices at which it was selling gas in the industrial gas market this would have been more likely to result in a substantial lessening of competition in the Balancing Market in breach of the *Competition and Consumer Act 2010* (Cth); and
- (c) the Respondent disputes the allegations in the paragraph.

ISSUE 3: WHETHER THE RESPONDENT'S PRICING BEHAVIOUR DURING THE INVESTIGATION PERIOD RELATED TO ITS MARKET POWER

111 The Respondent disputes paragraph 110 and 110A of the Applicant's Statement and says that, even if it had market power (which is denied), having regard to the matters set out in paragraphs 106 and 108 above and each of them, the Respondent's pricing behaviour during the Investigation Period was not related to market power.

The Respondent contravened clause 7A.2.17 of the Market Rules

112 The Respondent disputes paragraph 111 of the Applicant's Statement.

DATED: 9 May 2021

Squire Patton Boggs (AU)