

Oceania

Competition-Regulatory Hybrid: The Australian Approach to Combating Wholesale Electricity Market Misconduct

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Introduction

The relationship between competition law and economic regulation has evolved from a state of conflict to one of mutual recognition. Competition law is aimed at preventing anti-competitive behaviors and strengthening market mechanisms, while economic regulation imposes constraints on business conduct to address market failures.¹ The Organization for Economic Co-operation and Development (“OECD”) has identified four institutional models used around the world for governing the interaction between competition and regulation. Among them, Australia is notable for its “super-regulator,” the Australian Competition and Consumer Commission (“ACCC”), which enforces both competition law and economic regulation. This incorporated method of enforcement, which emphasizes the use of both competition and regulatory mechanisms, is referred to here as *competition-regulatory hybrid*.

The Australian electricity sector has undergone numerous reforms due to public concerns about high electricity prices, unstable climate change policies, and emerging technologies. As a result, a new form of anti-competitive behavior, called energy market misconduct, was introduced in 2019 by inserting Part XICA into the *Competition and Consumer Act 2010* (Cth) (“CCA”). The prohibited misconduct was formally defined in the *Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Act 2019* (Cth) after a few minor amendments from the *Treasury Laws Amendment (Prohibiting Energy Market*

Misconduct) Bill 2018.² This article highlights how Australian competition law has adopted a competition-regulatory hybrid to address wholesale electricity market misconduct. This hybrid approach involves a deeper integration of anti-competitive elements and regulatory conduct rules.

I. Australian National Competition Policy Review

Section 2 of the CCA outlines the goals of the Act as enhancing the welfare of Australians by promoting competition, fair trading, and consumer protection.³ The Australian High Court established in *Qld Wire* that competition is not an end in itself but a means to protect consumer interests.⁴ The *Hilmer Report* further emphasized that competition policy aims to facilitate effective competition to promote efficiency and economic growth.⁵ The competitive conduct rules are primarily determined by the effective functioning of the competitive process, which promotes economic efficiency and community welfare.⁶ Thus, Australian National Competition Policy (NCP) prioritizes effective competition in promoting these objectives.⁷

Subsequently, another fundamental and far-reaching competition policy review, known as the *Harper Report*, further recommended that the guiding principles for competition law and policy should include promoting both users’ choice and increasing the diversity of providers. The recommendation is grounded in the central idea of promoting the long-term interests of

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¹ STEPHEN BREYER, REGULATION AND ITS REFORM 157-158 (1984).

² Revised Explanatory Memorandum, Treasury Laws Amendment (Prohibiting Energy Market Misconduct) Bill 2019 (Cth) 5-7.

³ *Competition and Consumer Act 2010* (Cth) s 2.

⁴ *Queensland Wire Industries Pty Ltd v Broken Hill Proprietary Co Ltd* (1989) 167 CLR 177, 191.

⁵ AUSTRALIAN GOVERNMENT, NATIONAL COMPETITION POLICY REVIEW 26 (1993).

⁶ *Id.*

⁷ JOHN KAIN, INDRA KURUPPUL AND ROWENA BILLING, AUSTRALIA’S NATIONAL COMPETITION POLICY: ITS EVOLUTION AND OPERATION (2003), <http://ncp.ncc.gov.au/docs/Australia%27s%20NCP%20Its%20Evolution%20and%20Operation%2C%20E-Brief%20online%2C%20June%202001%2C%20Updated%20June%202003.pdf>.

consumers through well-functioning markets.⁸ To achieve this goal, competition laws ensure that markets adapt to changing conditions arising from technological developments and sector-specific features.⁹

The Australian approach recognizes that appropriate levels of regulation can coexist with competitive sectors such as telecommunications, energy, transportation and water to effectively manage market conditions. Australian competition policy seeks to reform regulations to prevent unjustified restrictions on competition, while also recognizing the need for continuing regulation to address market failures.¹⁰ Reform of sector-specific regulations to foster well-functioning markets is a cornerstone of the Australian institutional framework, which lays the foundation for the competition-regulatory hybrid.

II. Regulatory Conduct Rules in the Wholesale Electricity Market

The regulatory conduct rules in the energy market had previously focused on prohibiting market manipulation in financial transactions. The High Court held that s 1041A of the *Corporations Act 2001* (Cth) prohibited behaviors that create an “artificial price” which is contrary to “genuine supply and demand.”¹¹ In gas supply hubs, the *National Gas Rules* (Version 62) prohibited gas trading exchange members from acting fraudulently, dishonestly, or in bad faith with the intent of distorting or manipulating prices.¹² However, the electricity sector lacked specific provisions, and the only behavioral rule was the prohibition on making false or misleading offers, bids, or rebids in the

spot market under the *National Electricity Rules* (Version 186).¹³

Consumers in electricity markets typically do not have access to real-time electricity prices for their purchase decisions; consumers have no chance to hold their purchase like other industries until the electricity price is cheaper.¹⁴ By contrast, transactions among generators, generator-and-retailers (gentailers), and retailers in the wholesale market substantially determine the real-time price in the wholesale spot market and the manageable price in the derivative financial contract market.¹⁵ These interactions among wholesale market participants serve as the central stones of the ripple effects on the fluctuations of electricity prices to end-users. Any illegal behaviors or unlawful contracts in such a rippling process can exacerbate the harm to consumers’ welfare.

To protect consumers from suffering harm in this rippling process, the ACCC has monitored participants’ behaviors across the Australian National Electricity Market (“NEM”). Through this monitoring, the ACCC has identified several failures that it deemed “unacceptable and unsustainable,” including a lack of competition in the wholesale market and insufficient liquidity in the derivative financial contract market.¹⁶ Problematic behaviors that cause those failures are defined as *electricity market misconduct* in Part XICA of the CCA.¹⁷

III. Competition-Regulatory Hybrid in Part XICA of the CCA

The hybridization of competition and regulation is not a new concept, and it has led to concerns about the potential politicization and

⁸ IAN HARPER ET AL, COMPETITION POLICY REVIEW, FINAL REPORT 96, 99 (2015).

⁹ *Id.* at 20.

¹⁰ NATIONAL COMPETITION COUNCIL, ASSESSMENT OF GOVERNMENTS’ PROGRESS IN IMPLEMENTING THE NATIONAL COMPETITION POLICY AND RELATED REFORMS x (2005).

¹¹ *Director of Public Prosecutions (Cth) v JM* (2013) 250 CLR 135, [70]-[72].

¹² *National Gas Rules* (Version 62) pt 22 div 5.

¹³ *National Electricity Rules* (Version 186) cl 3.8.22A.

¹⁴ GOVERNMENT OF WESTERN AUSTRALIA, DEPARTMENT OF FINANCE AND PUBLIC UTILITIES OFFICE, MARKET POWER MITIGATION MECHANISMS FOR THE WHOLESALE ELECTRICITY MARKET ii-v (2016).

¹⁵ *Id.*

¹⁶ Commonwealth, *Parliamentary Debates*, Houses of Representatives, Sept. 18, 2019, 3353 (Josh Frydenberg, The Treasurer).

¹⁷ *Id.* at 3354.

instrumentalization of competition law.¹⁸ However, as Sioshansi has stated, the term “deregulation” in sector-specific regulations is a misnomer, as even well-functioning competitive markets require some level of regulation.¹⁹ In this regard, sector regulation requires both sophisticated regulatory rules and a commitment to promoting competition in markets.

For this reason, the Australian state provides solutions to secure the electric energy market through *market adjustments*, which are “deliberate federal government interventions across the entire electricity supply chain.”²⁰ In the electricity sector, the ACCC collaborates with other federal agencies, including the Australian Energy Market Commission (AEMC) functioning as the economic rule-maker, the Australian Energy Regulator (AER) working as an independent regulator, and the Australian Energy Market Operator (AEMO) for daily management in practice. In particular, the ACCC and the AER closely work together in pursuing common objectives to protect, strengthen and supplement competitive market processes in electricity markets.

As a measure of last resort, the prohibitions under Part XICA of the CCA combine regulatory conduct rules with competition law elements to combat electricity market misconduct. The approach taken in Part XICA of the CCA is therefore consistent with the hybridized institutional context found in Australia, which is crucial in regulating the wholesale electricity market. The competition-regulatory hybrid in Part XICA of the CCA, contributing to the broader regulation framework, aims to balance freedom of competition and sector-specific interventions or regulations. The two prohibitions under Part XICA are addressed in detail below.

A. Prohibited Conduct in the Spot Market

Part XICA of the CCA contains two misconduct prohibitions aimed at the electricity wholesale market. The first prohibition, set out in ss 153G and 153H, relates to *prohibited conduct in the spot market*, and is designed to prevent generators from engaging in activities to manipulate the physical spot market of the NEM.²¹ Such activities include discretionary maintenance to create price spikes, and low-balling bids followed by a last-minute increase in price.²² Two elements must be established to prove a prohibited conduct has occurred: (a) bidding, rebidding, or failing to bid in the spot market, and (b) a two-limb test to determine whether the behavior is fraudulent, dishonest, or in bad faith, and whether it was carried out with the purpose of manipulating or distorting prices.²³

Compared to the pre-existing regulations established for each energy sector, ss 153G and 153H display a combination of anti-competitive elements and regulatory tools to promote competition in markets. In ss 153G and 153H, misconduct is prohibited *per se*, that is, regardless of whether the conduct has the purpose, effect, or likely effect of substantially lessening competition (the “SLC test”). Behaviors such as bidding, rebidding or failing to bid in the spot market are considered anti-competitive if either limb of the test under ss 153G(b) and 153H(b) is confirmed.

The first limb seeks to determine whether the conduct is fraudulent, dishonest or in bad faith. The fraudulent nature of the behavior is subject to a regulatory focus, which is similar to that addressed in previous regulations for gas supply hubs. These standards aim to ensure participants compete using fair and lawful means; maximizing profits and results can only be achieved without any unfair harm to competition. The wrongful nature of behaviors

¹⁸ A. Douglas Melamed, *Antitrust: The New Regulation*, 10(1) ANTITRUST 13 (1995); Spencer Weber Waller, *Prosecution by Regulation: The Changing Nature of Antitrust Enforcement*, 77(4) OREGON LAW REVIEW 1383 (1998).

¹⁹ Fereidoon P. Sioshansi, *Introduction: Electricity Market Reform – Progress and Remaining Challenges*, in COMPETITIVE ELECTRICITY MARKETS: DESIGN, IMPLEMENTATION, PERFORMANCE 2 (Fereidoon P. Sioshansi ed., 2008).

²⁰ ACCC, RESTORING ELECTRICITY AFFORDABILITY AND AUSTRALIA’S COMPETITIVE ADVANTAGE: RETAIL ELECTRICITY PRICING INQUIRY FINAL REPORT (2018) iv.

²¹ ACCC, GUIDELINES ON PART XICA: PROHIBITED CONDUCT IN THE ENERGY MARKET 3-4, 24-33 (2020).

²² *Id.* at 24-25. Section 153G applies to the basic case, while s 153H relates to the aggravated case.

²³ *Id.* at 26-27.

“in bad faith” is determined by considering the context of a particular bidding process. The concern of bad faith behaviors arises from the possibility of market failure where participants make seemingly rational decisions to maximize their own profits, but those decisions prove harmful to the community. These behaviors are seen as breaching communal standards and industrial rules, requiring a regulatory focus on fraud-based norms to capture them appropriately.

The second limb of ss 153G(b) and 153H(b) prohibits behaviors that manipulate or distort prices in the bidding process. These behaviors seek to create an “artificial price” through unfair and unacceptable means in the spot market. Such fraudulent conduct damages market competition by artificially deforming the price signal between genuine supply and demand, leading to further distortion of the competitive process. The focus on wrongful purpose in ss 153G(b) and 153H(b) aims to distinguish behaviors relating to artificial prices with a fraud-based intent from permissible behaviors leading to the same effect but having a genuine commercial purpose. The ACCC employs a case-by-case analysis using circumstantial evidence to ascertain the behaviors’ purpose.²⁴

B. Prohibited Conduct to Financial Contract Liquidity

Section 153F of the CCA outlines the second prohibition of the *prohibited conduct to financial contract liquidity*. It aims to stop participants from unreasonably withholding financial contracts for the purpose of substantially lessening competition.²⁵ To establish a violation of this prohibition, three key elements must be established: (a) parties who are relevant to the financial contract, (b) the party’s behavior must fall into one of three categories: failing to offer the contract while the party is able to offer, limiting or restricting an offer while the party is

able to offer, or making offers that limit or restrict acceptance and (c) the behavior must have the purpose of substantially lessening competition.²⁶

All participants aim to reduce their exposure to uncertain price volatility in the spot market; it is therefore challenging to define an acceptable level of risk management strategies. As such, s 153F(b) emphasizes the nature of offers in electricity financial contracts to ensure equitable and sufficient availability, particularly for those at a disadvantage.²⁷ On the one hand, s 153F(b) lists behaviors that can exploit the structural and positional disparities among participants to create advantageous positions over other competitors for self-benefit. On the other hand, these behaviors are subject to exemptions for the sake of effective competition to genuinely manage participants’ financial risks.²⁸

Section 153F(b) therefore prohibits such behaviors only if they serve an anti-competitive purpose of substantially lessening competition under s 153F(c) (the previously mentioned “SLC test”).²⁹ This provision is crucial to ensuring that disadvantaged participants have reasonable and adequate access to financial contracts allowing them to manage their risks against price fluctuations in the spot market, as market liquidity creates competitive pressure and enables fairer competition, particularly for the non-vertically integrated firms and new entrants with structural disadvantages.

The application of the SLC test under s 153F(c) is consistent with other parts of the CCA; however, s 153F(c) targets conduct with the *purpose* of SLC, rather than the effect.³⁰ The ACCC clarifies that the effect of SLC is not directly determinative of the purpose of SLC for listed behaviors in s 153F(c), although that impact may help prove the purpose of SLC.³¹ The SLC need only be a substantial purpose rather than a sole purpose, requiring an

²⁴ *Competition and Consumer Act 2010* (Cth) s 153 J.

²⁵ ACCC, *supra* note 21, at 16.

²⁶ *Id.* at 16-20.

²⁷ *Id.* at 21, 23.

²⁸ *Id.* at 21, 24.

²⁹ Revised Explanatory Memorandum, *supra* note 2, at 29.

³⁰ *Id.* at 26.

³¹ ACCC, *supra* note 21, at 20.

objective assessment of all relevant circumstantial evidence.³² Although this subjective assessment may be difficult to prove in practice, the adoption of the wrongful purpose element in s 153F(c) recognizes an independent fraud-based ground of liability rather than focusing on proving anti-competitive outcomes. It therefore reflects a regulatory focus aimed at combating specific problems in the wholesale electricity market.

Conclusion

The Australian National Competition Policy aims to promote economic efficiency and consumer welfare by fostering effective competition, particularly through reform of sector-specific regulations. This approach is based on a competition-regulatory hybrid model that combines elements of competition law and sector regulation. In the electricity sector, protecting consumer interests in the long term necessitates both sophisticated regulatory rules and a commitment to promoting competition in markets.

Part XICA of the CCA addresses two types of prohibited conduct in the wholesale electricity market within this hybrid institutional context. Sections 153G and 153H prohibit manipulation and distortion in the spot market, using a two-limb test that considers both regulatory norms and anti-competitive evidence. The first limb focuses on communal standards and fraud-based norms, while the second limb ascertains the purpose of the conduct on a case-by-case basis. Section 153F prohibits conduct that affects the liquidity of financial contracts in the electricity market, with a particular emphasis on ensuring equitable and sufficient availability for disadvantaged parties. This prohibition is subject to the SLC test, which assesses all relevant circumstantial evidence to determine whether the conduct has an anti-competitive purpose.

Overall, Part XICA of the CCA integrates both anti-competitive elements and regulatory conduct rules to capture misconduct in the wholesale electricity market. This reflects the hybridized approach in Australia to the interaction between competition law and sector regulation.

³² *Competition and Consumer Act 2010* (Cth) ss 4F(1)(b), 153J.