



19 October 2018

Dr Kerry Schott AO
Energy Security Board
By email: info@esb.org.au

Dear Dr Schott

OTC Transparency in the NEM Consultation Paper

The Australian Financial Markets Association (AFMA) welcomes the opportunity to provide comment to the Energy Security Board (ESB) on the OTC Transparency in the NEM Consultation Paper (“consultation paper”).

AFMA is the leading industry association promoting efficiency, integrity and professionalism in Australia's financial markets. AFMA represents the common interests of its members in dealing with issues relevant to the good reputation and efficiency and competitiveness of wholesale banking and financial markets in Australia. AFMA has more than 120 members reflecting the broad range of participants in financial markets, including Australian and international banks, leading brokers, securities companies, fund managers, energy companies and industry service providers.

As the national association for participants in the wholesale financial markets, AFMA has established trading protocols and developed standard contract documentation, as well as providing market information, dealer accreditation, training and other services to facilitate the efficient operation and development of the electricity financial markets.

In particular, and as noted in the consultation paper, AFMA has supported transparency in the OTC markets by publishing turnover data in both exchange traded and over-the-counter (OTC) electricity derivative markets for several years, with data compiled from a survey of the principal participants in the OTC electricity derivatives market and ASX Limited. This data is publically available on our website and is current up until the 2016-2017 financial year. We are currently undertaking a project to update this information for 2017-2018.

Whilst acknowledging the overall objectives of the consultation paper, AFMA's focus is on the efficiency and competitiveness of electricity financial markets. Accordingly, our comments are limited to those areas that relate to this focus. As we represent a broad range of participants in the financial markets, we also limit our comments to those in

which we believe we express a commonly held viewpoint amongst our member base. We expect that many of our members will provide you with submissions of their own on specific issues.

We note also the very short turnaround time (3 weeks) in which this consultation is taking place, which limits our ability to collect member feedback and fully ascertain and represent our members' collective viewpoints.

We also note the similarity of this consultation paper and elements of the reliability requirement contained in the ESB National Energy Guarantee – Draft Detailed Design Consultation Paper (the “NEG consultation paper”) to which we made a submission in July 2018. Consequently, we re-iterate some of the views that were in our NEG consultation paper submission.

Establishing a Trade Repository

The ACCC recommended an industry-specific trade repository as its preferred model to meet its priority objective; enhancing transparency of electricity OTC market activity and price trends.

We note that in the Final Detailed Design of the National Energy Guarantee, the ESB did not consider that the costs of establishing a trade repository were warranted to satisfy the objectives of the National Energy Guarantee (with a Market Liquidity Obligation in place).

In order for a trade repository solution to be a preferred solution, a case must be made to prove that the benefits of a trade repository outweigh the significant cost outlay and administrative burden. A number of our members believe that this case has not been made and would argue that a trade repository solution is not required.

As we noted in our submission to the NEG consultation paper, if a trade repository approach is required, a light-touch trade repository solution would be preferred by our members. Issues raised by our members in discussions around the NEG consultation paper and are still relevant to this consultation include:

- If a Market Liquidity Obligation or a similar liquidity provision arrangement is in place, then it is arguable as to whether a trade repository is necessary. This is the same conclusion as per the Final Detailed Design of the NEG.
- If a trade repository is considered necessary, then it would be important to ensure that the form and content of a trade repository is fit for the compliance purpose, and not be overly burdensome and costly to industry.
- Alternatives to trade repositories could be established to provide the requisite transparency without undue burden on industry such as a market survey mechanism.
- There are concerns about the benefits of utilising a trade repository to enhance transparency, whilst revealing commercially sensitive information about energy participants.
- It should not be automatically assumed that transparency is necessarily a positive for the development of nascent markets which are illiquid or transact periodically in large single transactions amongst a small number of participants. The academic analysis

supports the value of transparency in markets that have achieved significant transactional scale and have many participants.

In addition to the above, it should be noted that information on OTC prices and volumes are currently produced by brokers within the over-the-counter derivatives market. A price data solution involving these market participants could be explored as a trade reporting alternative.

Role of the AER

AFMA is not in a position to comment on our members' preferences for an administering body, however we suspect that a number of our members would be comfortable with the AER, although one member has nominated a preference for ASIC.

Accessibility of underlying contract information

As noted above, our members have concerns about the benefits of utilising a trade repository to enhance transparency, whilst revealing commercially sensitive information about energy participants. This comment is also relevant in the context of providing access to parties such as the AEMC and AEMO for other purposes.

Reporting

AFMA agrees with the consultation paper's statement that reporting requirements would need to be carefully designed and consulted on to ensure they're useful, not misleading, and do not distort competitive behaviour.

The consultation paper contemplates two options; individual contract trade reporting and aggregated standardised trade reporting such as AFMA's survey-based report. As confidentiality is a key concern amongst our member firms, on balance aggregated reporting is likely to be preferable to members. Individual contract trades on an anonymised basis may not be sufficient to conceal confidential information. In addition, inclusion of specific bespoke transactions could have the potential to distort the data, and not provide any useful information value to market participants, or indeed mislead.

Obligation

AFMA is not in a position to comment on how recommendation 6 should be implemented. We suspect that member views would be mixed, with some likely preferring changes to the NEL, whilst one member has suggested the Corporations Act.

Yours sincerely



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