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Australian Energy Market Commission

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Inter-regional settlements residue arrangements for transmission loops

AGL Energy (AGL) welcomes the opportunity to respond to the Australian Energy Market Commission (AEMC) Inter-regional settlements residue arrangements for transmission loops draft rule determination

About AGL

At AGL, we believe energy makes life better and are passionate about powering the way Australians live, move, and work. Proudly Australian for more than 185 years, AGL supplies around 4.5 million energy, telecommunications, and Netflix customer services. AGL is committed to providing our customers simple, fair, and accessible essential services as they decarbonise and electrify the way they live, work, and move.

AGL operates Australia's largest private electricity generation portfolio within the National Electricity Market, comprising coal and gas-fired generation, renewable energy sources such as wind, hydro and solar, batteries and other firming technology, and storage assets. We are building on our history as one of Australia's leading private investors in renewable energy to now lead the business of transition to a lower emissions, affordable and smart energy future in line with the goals of our Climate Transition Action Plan. We'll continue to innovate in energy and other essential services to enhance the way Australians live, and to help preserve the world around us for future generations.

Draft determination

We broadly support the AEMC's draft rule which proposes to allocate:

- all negative inter-regional settlement residue (IRSR) by 'regional demand' - i.e. by the share of electrical energy used in each region over the prior year.
- all positive IRSR as per current arrangements - positive IRSR allocated to settlements residue distribution (SRD) unit holders, but the proceeds of settlement residue auctions (SRAs) go to the transmission network service provider (TNSP) of the importing region.

We agree the draft rule will help maximise benefits for Project Energy Connect (PEC) and the transition to net zero by enabling future renewable projects to connect to the grid and supply energy to multiple regions while delivering consumer benefits including increased inter-regional trade, reduced emissions, increased competition, and improved pricing outcomes.

We also consider the decision to not impose additional negative residue management requirements for AEMO will ultimately minimise instances of clamping when net IRSR is positive within a loop, thereby maximising benefits for consumers of transmission infrastructure.

We acknowledge the draft rule would theoretically manage the consumer risks of unpredictable extreme negative IRSR by allocating it broadly amongst all looped regions, in proportion to regional demand. However, we note the socialisation of negative IRSR in this manner may discriminate in favour of consumers in South Australia through cross-subsidisation of negative residues by consumers in New South Wales given the distribution in demand across the loop. Although we do not object to this allocation method, we believe it is likely the original rule change request was more cost and benefit reflective of where benefits accrue in the loop than the regional demand allocation method.

Proposed review of SRA arrangements in 2025-26

We do not support the proposed review of the SRA arrangements in 2025-26. We consider such a review would be premature given the uncertainty in market outcomes once PEC commences operation. We note

PEC is scheduled to commence operating at partial capacity in Q4 2026 and ramp up to full capacity by late 2027. We recommend that the AEMC only consider a review of SRA arrangements after PEC has been operation at full capacity for at least 24 months i.e. 2029-2030. This will allow adequate time to evaluate whether the regulatory settings are operating as intended and a suitable period of empirical data to analyse.

We also note there are the significant number of regulatory reviews and processes currently underway which will affect the wholesale energy market; we consider a review of SRA arrangements should be undertaken at a later stage once fundamental regulatory processes such as the independent National Electricity Market wholesale market settings review have been completed.

SRAs as a risk adjusted hedging instrument

SRAs are a key instrument in managing inter-regional price risk. Managing inter-regional risk boosts liquidity in the electricity financial market and provides retailers with more tools to manage spot price risk. Consumers are not exposed to spot prices. Retailers are responsible for purchasing electricity from the wholesale market and managing risk in various ways (financial instruments, participating in generation) and then on-selling to consumers through retail contracts. SRAs enable retailers to manage risk in their portfolios and offer competitive retail contracts to consumers.

We note the AEMC is concerned that SRA unit holders have received an apparent surplus of $1.1 billion, in nominal terms, in the period from Q2 2004 to Q1 2024 while consumers have received $0.72 for every $1 of IRSR sold in this period.

We note the AEMC has identified specific quarters with substantial SRA payoffs. It is important to consider the contextual factors around high-SRA payoff periods e.g. these could have coincided with a transmission line failure or maintenance works. The impacts on five-minute settlement to SRA payouts is also a consideration in looking over this period.

The AEMC's analysis is also based on data presented in aggregate for all interconnectors. We consider the AEMC's analysis should instead focus on outcomes across individual interconnectors and time periods. We note that even in the past 3 years net proceeds on some interconnectors have fluctuated by in excess of $100 million. The firmness of SRA's as hedging tool can change substantially – a key consideration is how useful an SRA unit is in hedging a load in an importing region. This can also significantly fluctuate year to year. Both of these are key considerations in valuation of SRA units for auction bidding.

We consider consumer interests may be better served by more closely examining the regulatory settings around transmission investment rather than SRAs. This is particularly relevant for interconnector projects; given the substantial PEC cost overruns which is likely to completely erode the expected system efficiency savings by an order of magnitude and result in material impacts to consumer bills.

If you have queries about this submission, please contact Alifur Rahman at ARahman3@agl.com.au.

Yours sincerely,

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