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Australian Energy Market Commission
Level 15, 60 Castlereagh Street
Sydney NSW 2000

Submitted electronically

Inter-regional settlements residue arrangements for transmission loops
Directions paper

Snowy Hydro welcomes the opportunity to comment on the Australian Energy Market Commission (Commission) Inter-regional settlements residue arrangements for transmission loops Directions paper.

Inter-regional trade is a key feature of the NEM and has delivered significant benefits over the years. Market participants operate sophisticated multi-regional portfolios to deliver these benefits, encouraging efficient market outcomes supported by interconnectors. The introduction of Project Energy Connect will result in interregional hedging likely taking on greater importance and reinforce the ongoing need for settlement residue auctions to support interregional trade, liquidity, and the efficient functioning of the NEM.

It is for this reason, Snowy Hydro does not support the assessment undertaken by the Commission and the proposed 'netting off' approach for allocating positive and negative inter-regional settlements residue (IRSR) in transmission loops. This solution does not best promote the long term interests of consumers compared to other options. The proposed netting-off approach is inconsistent with the National Energy Objective (NEO).

We understand the concern put forward by Transmission Network Service Providers (TNSP)'s that currently the cost of negative residues is reasonably transparent and stable to large end users as a component of their Transmission Use of System (TUOS) charges. However the solution put forward by the Commission incorrectly claims that netting negative and positive residues will reduce the cost to end users. Further to this the Commission neglects to mention that this approach makes it less transparent as it would become another component of the wholesale cost of energy resulting from retailers having less efficient hedging costs.

Netting residues could increase end user costs as the impact on the value of Settlements Residue Auction (SRA) could be greater than the cost of negative residues. SRAs are not a transfer of wealth from end users to retailers, they are an instrument that allows retailers to manage their exposure to spot prices to allow them to offer competitive prices to end users.

With SRA's valued less, the overall negative impact on competition will be greater. Participants with supply side resources in one region will have less ability to manage risks in an adjacent region. This will result in less competition in adjacent regions that the Commission has not thoroughly assessed.

Alternative solution and the Consultation process

Snowy Hydro is disappointed with the way the Commission has approached this consultation with a late unexpected pivot back to an approach we understood had been discarded to solve a new problem that is not fundamentally about the SRA market. Market Participants had worked very closely with Australian Energy Market Operator (AEMO) and the Commission for over a year to form a draft determination and to assist AEMO with drafting up a rule change only for it to have been discarded with a few months' notice.

Overall we believe any netting approach put forward is problematic as potentially SRAs are valuable up to a point and then they stop being valuable. Any netting approach would likely overall reduce the amount that people would pay for SRAs, which would then make them even less valuable as it would reduce TNSPs SRA revenue, meaning you would get to the point where positive revenue was less than negative revenue in a faster time frame.

We believe greater consideration should be given to establishing an AEMO holding fund or a third party to recover negative IRSR. The main benefit of this proposal would be preserving the value of SRA's benefiting consumers and competition which is not addressed. The focus on this approach is instead only on AEMO's costs.

We do not support the alternative option of scaling the amount of SRD units sold as that would much like the "netting" approach impact the viability of SRA's.

Consumer does not benefit from the netting approach

The Commission makes the incorrect assumption in their analysis that netting the positive and negative residues will reduce the cost of negative residues to end users. That is not the case. Negative residues are an inherent part of the NEM regional structure and the cost of them ultimately has to be recovered from end users in the same way that all other market charges are. The cost of these negative residues does not disappear, now that it is not passed on through TUOS charges. In this they are no different from other AEMO charges such as the cost of ancillary services or Reliability and Emergency Reserve Trader (RERT).

End users are not directly exposed to any market payments as they typically manage their risk through entering into retail contracts which remove direct exposure to the market. There is some variability in TUOS payments but this is not the same as saying that customers have an unhedged risk.

Our main point is that the cost of negative residues can't be avoided in a regional market and that ultimately, as with all costs, consumers will pay for them. The proposed netting arrangement will not deliver any benefit for consumers and will damage the value of SRAs as a hedging instrument which will ultimately lead to less inter-regional trade and higher costs for end users. The problem is that netting of any type reduces the correlation between the value of the SRA during an interval and the price difference between regions in the pricing interval, which makes them less effective hedging instruments.

Consumers are currently benefiting from SRA units. The revenue from the SRA is only part of how consumers benefit; they also benefit from retailers' reduced hedging costs as a result of the use of SRA units to manage inter-regional price risk. The Commission should understand that SRA units could be expected to sell for less than the total value of positive IRSR.

Competition is a key benefit of the current SRA's

The Commission correctly notes that *"SRD units can support retail competition by helping retailers and gentailers manage their exposure to cost differentials across different regions. That is, SRD units can allow retailers and gentailers to provide competitive offers in regions where they do not own generation or hold swap or cap contracts, thus increasing the number of retailers active in each region. SRD units can support consumer access to cheaper electricity generated in other regions."*[1] We agree with this position and believe that low liquidity environments such as South Australia, SRA'S enable effective replication of Victorian swap positions into South Australian swaps. This helps to foster competition in regions that might otherwise suffer from a lack of market participants. The benefits of risk management practices also accrue to consumers.

By providing an instrument to manage inter-regional price risks, hedging encourages agreements to supply consumers from areas where costs are lower. SRD units encourage efficient investment in generation, storage and large loads. By providing a tool to manage the

[1] AEMC, Inter-regional settlements residue arrangements for transmission loops, Directions paper, 19 June 2025

differences in wholesale prices across regions, SRD units work together with wholesale and contract markets to provide clear incentives for generators, storage and large loads to locate in appropriate places, without being biased towards a particular region because they cannot manage inter-regional price risk.

Under the netting-off proposal, generators will face significantly greater basis risk when seeking to offer interregional hedges. The only way for generators to manage this risk will be to reduce the volume of offered contracts outside their home regions, undermining the NEM as a national market. Smaller generators, particularly new entrants without access to their own sources of generation as a self-hedge, will be damaged most by this change. Consumers will ultimately be worse off as incumbent retailers face less competition.

In short, devaluing SRA's as a hedging tool will mean that these instruments are relied on less, reducing competition, with predictable consequences for consumers. This has not been adequately addressed by the Commission.

Negative Residue concerns are valid

Snowy Hydro is sympathetic to the TNSPs concerns about the cost to them of managing negative residues. We understand that allocating this cost to TNSPs is a legacy of how the NEM was set up and that there are probably better ways to do it.

The real problem identified is the way costs are currently allocated to TNSPs. A range of options for addressing this were identified to the Commission but instead of appropriately considering other approaches to cost allocation they were dismissed in favour of netting. The Commission prematurely dismissed these options without seeking stakeholder input as it seems there is a fairly strong view in changing the cost allocation arrangements in preference to netting.

TNSPs are concerned in bearing the financing costs associated with negative residues. They have proposed netting as a partial solution that might keep their costs similar at current levels. As the competitive part of the market has been saying throughout this process, damaging the value of SRAs as a hedging instrument will instead lead to higher wholesale market costs – resulting in higher costs for end users. The Commission should not seek to alleviate a cashflow issue for networks by reducing competition for consumers. Yet, that is the effect of the netting-off proposal.

SRA's must consider post 2030 Market Design

The Commission has highlighted that they *"remain concerned that the SRA framework is not working as effectively as it could in the long-term interests of consumers, and consider that a future review could review this framework across both radial interconnectors and transmission loops."*[2] Snowy Hydro believes that the Commission should not pre-empt this discussion with their position regarding netting in the PEC SRA proposed solution. SRA's should be considered within the context of the broader financial contract market due to their role in enhancing liquidity and firming trade across regions.

The financial contract market has formed a key part of the Energy Panel's Post 2030 Market Design Review and the Commission could put a significant dent in the progress undertaken in this forum by devaluing the use of SRAs.

As noted in our previous submission to the review, consumers are not directly exposed to spot prices. Retail customers typically buy electricity from energy retailers at contract prices rather than being exposed to regional spot prices. Instead the wholesale component of retail prices is determined using a risk-adjusted hedged book which is usually over several years in order to

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[2] AEMC, Inter-regional settlements residue arrangements for transmission loops, Directions paper, 19 June 2025

minimise exposure to high spot prices. This means pricing impacts on end consumers are not easily observed through pool prices only.

Hedging risks through SRD units, market participants can significantly reduce their own and in turn customers' exposure to high price events. By firming future wholesale revenue and costs through such risk management strategies, risk premiums within consumer profiles and contracts are lowered.

Future Review

If the Commission is to continue with the netting approach, this should remain only for PEC. The issues addressed in this paper are primarily an issue on the transmission loop where unclamped negative residues will be part of normal market operation and can accrue quickly to very large values. We think the status quo is manageable for the rest of the NEM.

Overall Snowy Hydro believes the value of any review will be limited unless time has been allowed to assess current changes and their impacts. It will be important to gather evidence regarding the impact of all of these to inform any further review and reform. Our preference is to not undertake the review until a later period.

About Snowy Hydro

Snowy Hydro Limited is a producer, supplier, trader and retailer of energy in the National Electricity Market ('NEM') and a leading provider of risk management financial hedge contracts. We are an integrated energy company with more than 5,500 megawatts (MW) of generating capacity. We are one of Australia's largest renewable generators, the third largest generator by capacity and the fourth largest retailer in the NEM through our award-winning retail energy companies - Red Energy and Lumo Energy.

Snowy Hydro appreciates the opportunity to respond to the Commission's Inter-regional settlements residue arrangements for transmission loops Directions paper. Any questions about this submission should be addressed to panos.priftakis@snowyhydro.com.au.

Yours sincerely,

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