

30 October 2025

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Submitted electronically: via Lodge a submission | AEMC (GRC0077)

ECGS Supplier of last resort mechanism – Consultation paper

EnergyAustralia is one of Australia's largest energy companies with around 2.2 million electricity and gas accounts across eastern Australia. We also own, operate and contract a diversified energy generation portfolio across Australia, including coal, gas, battery storage, demand response, wind and solar assets, with control of over 5,000MW of generation capacity.

We appreciate the opportunity to provide feedback on the AEMC consultation paper on the Gas Supplier of Last Resort (SoLR) mechanism. As a retailer and operator of gas-powered generation, we support the objective of maintaining a secure, resilient, and flexible East Coast Gas Market (ECGS). We agree with the AEMC's assessment of the problem that there is uncertainty around how gas reliability shortfalls would be managed under existing arrangements. We therefore broadly support a well-designed, fit-for-purpose SoLR framework as it could play a valuable role in addressing this gap. However, as with all gas market reforms it is critical that changes are proportionate, preserve market-led responses, avoid unintended consequences on gas prices for consumers, and minimise regulatory burden.

Given the scale and potential market implications of the SoLR reforms, we welcome further consultation planned to ensure the final framework is workable, transparent, and consistent with the long-term interests of consumers.

Preferred Option 3B and scope of AEMO SoLR intervention

Of the options considered in the consultation paper, we broadly support Option 3b as it provides AEMO with the most levers to manage emergency gas supply risks—integrating both supply and demand response—while offering the potential for improved reliability and efficiency. In particular, option 3b would enable AEMO to procure demand response, a capability that does not exist under current arrangements.

Further clarity is needed, however, on the intended duration and scope of AEMO's SoLR powers. It is not clear to us from the consultation paper whether AEMO's SoLR

intervention powers are intended to be used only for short-term emergencies or could extend to longer-term, structural interventions such as underwriting investment or holding reserves over multiple years. It is important to call out the risk for market participants from broad or prolonged AEMO interventions could pose to both contracting practices and overall market efficiency.

While there may be a limited role for longer-term intervention, we consider that given the risks - very strong guardrails are essential. For example, AEMO should not be able to contract all available resources – such as compression, storage or pipelines - or reserve capacity – even if intended as a reliability measure. This would risk crowding out commercial contracting and undermine efficient market operation.

To preserve confidence and efficiency in the market, consideration could be given to:

- Prohibiting AEMO from contracting or reserving all available resources, ensuring sufficient capacity remains available for commercial contracting;
- Requiring AEMO to relinquish procured capacity (e.g or storage) under defined circumstances to minimise distortion and facilitate the return to normal market operation.

We support mandating ex-post transparency and reporting on any SoLR intervention - including the rationale for activation, cost recovery mechanism adopted, and costs incurred. We support periodic 6-month minimum AEMO reporting that summarises AEMO's SoLR reserve holdings, cost recoveries and any over procurement relative to the reliability standard.

We would also support the inclusion of clear, mandatory principles in the National Gas Rules (NGR) to guide AEMO's use of SoLR, including:

- **Least-distortion and proportionality**, ensuring interventions are limited in scope and duration
- **Cost-effectiveness and accountability**, with transparent reporting and post-event review.

Embedding these principles in the NGR—together with an explicit order of operations (*market response* → *AEMO directions* → *SoLR activation*)—can help provide clarity on how the SoLR mechanism should function and ensure interventions remain a genuine last-resort measure.

Cost Recovery

While Option 3B proposes a demand-based cost allocation, we are concerned this could penalise participants who have already contracted responsibly. Evidence and recent market experience highlight that demand-driven cost recovery, while transparent, can undermine incentives for prudent management, and risk socialising cost and promoting inefficient consumption.¹ A pure causer-pays approach would best align costs with those who contributed to the risk and preserve incentives for prudent contracting, but we recognise that implementing it in practice can be difficult in complex, contract-driven gas markets.

¹ See CEPA, *Recovering the costs of gas directions and the trading fund*, 20 February 2023, p 18.

Where it is possible to objectively and transparently identify the parties whose actions or inaction necessitated AEMO's intervention, we recommend that a causer-pays approach should, in principle, be the default starting point. For example, if a participant failed to secure sufficient gas or pipeline capacity ahead of time, and this shortfall directly contributed to a reliability risk requiring AEMO intervention, it would be reasonable for that participant to bear a proportionately higher share of the costs. This approach does not penalise prudent contracting and holds those who contributed to the need for intervention accountable, consistent with economic efficiency and fairness principles.

The cost recovery mechanism could also vary depending on the type of intervention or event. Demand-based allocation might be appropriate for short-term balancing actions, whereas causer-pays or hybrid recovery may be better suited to predictable or preventable events where causation can be reasonably established.

Where it is not practicable to identify causers, a demand-based recovery is preferable to a flat or equal-share approach. It aims to link costs to entities' demand during a shortfall and provides some incentive to contract prudently. However, it also socialises costs across all participants in the affected location and period, including those that managed their exposure responsibly. Costs are allocated based on consumption, not contractual position, which weakens fairness and incentives for effective risk management.

We do not support flat or equal-share recovery, as these methods fail to meet efficiency and fairness objectives and further erode incentives for prudent contracting.

To improve equity, a hybrid approach could be explored. For example, a portion of costs could first be allocated to identifiable causers (e.g. uncontracted or under-nominated shippers), with the remainder recovered on a demand basis. Participants who can demonstrate firm supply arrangements or compliance with scheduling obligations could receive partial exemption or discounting.

Irrespective of the approach adopted, transparency and governance are critical. As discussed, AEMO should publish post-event reports outlining the drivers of interventions, how costs were attributed, and any refinements to the methodology.

Ultimately, the preferred approach should balance equity, and administrative simplicity. Where causation can be reasonably established, a causer-pays model should apply; otherwise, a proportionate, transparent, and contract-sensitive demand-based recovery may be appropriate.

We would also support a commitment to post-implementation review to test whether the adopted cost mechanism remains proportionate and effective over time.

Triggers and transparency

We agree with the assessment that there is a lack of transparency and predictability in the current preconditions and triggers for gas intervention. As outlined in our reliability standard submission, we support a tiered risk/threat signalling framework to provide clear, predictable triggers for SoLR activation.

The probabilistic metric should be transparent, with confidence intervals and scenario assumptions published. The process for market notices, reserve establishment, and intervention should be clear and timely, giving the market a real opportunity to respond before AEMO acts. Enhanced transparency and reporting, including timely market notices and post-intervention reports, are essential for market confidence.

On the duration of AEMO intervention, we would support alignment between the time horizons considered in the reliability standard and those underpinning the SoLR framework. This will help promote consistency in how reliability risks are assessed and how AEMO's powers are applied.

Lastly, as mentioned above, we would support a clear hierarchy of market operations. The SoLR framework should codify in the NGR an explicit order of operations: market response → AEMO directions → SoLR activation. This hierarchy should be underpinned by transparent criteria, signalling thresholds and the reliability standard, and governance processes that maintain confidence in both the proportionality and sequencing of AEMO's actions.

VGCR and reliability Standard

The consultation paper proposes using the Value of Gas Customer Reliability (VGCR) as a cap on SoLR costs but notes challenges in its application and the need for strong, transparent governance.

As outlined in our reliability standard submission, we agree that the VGCR must be robust, transparent, and independently reviewed by a body such as the AER. The VGCR should reflect the true value of reliability across all customer classes, including those unable to reasonably load shed, and be linked to intervention triggers and price settings to ensure consistency between reliability assessment and cost recovery.

Overall, a well-calibrated and regularly reviewed VGCR will be critical to maintaining market confidence, guiding efficient investment and contracting decisions, and ensuring SoLR costs remain proportionate to customers' value of reliability.

If you would like to discuss this submission, please contact me on 03 9060 0934 or via email at maria.ducusin@energyaustralia.com.au.

Regards

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