



Secondary Trading Of Settlement Residue Distribution Units

Stakeholder submissions invited on draft rule

The Australian Energy Market Commission (AEMC) has made a draft rule that enables auction based secondary trading of settlements residue distribution units. Submissions are due by 29 August 2017.

Enabling the Australian Energy Market Operator (AEMO) to provide a platform for secondary trading of settlements residue distribution units (units) improves liquidity in the market for units. This improved liquidity is likely to increase interstate trade of electricity, improve risk management and increase competition.

The draft rule allows for, but does not mandate the introduction of secondary trading of units via the same auction process already facilitated by AEMO. The draft rule also protects consumers from bearing any additional risk arising from secondary trading.

Settlements residue auctions and secondary trading

Regions of the national electricity market (NEM) have different levels of demand, differently priced generation and often very different wholesale prices resulting from the use of regional reference prices. Price separation of regional reference prices often occurs when interconnector capacity is not sufficient to equalise the spot price flowing from a lower to a higher priced region.

The difference between the price paid in the importing region and the price received in the exporting region, multiplied by the amount of flow for each interconnector for a trading interval, results in surplus inter-regional settlements residue.

Since August 1999, AEMO and its predecessor, the National Electricity Market Management Company (NEMMCO) have been holding auctions where units, representing a right to a certain portion of that money could be purchased by auction participants.

While the settlements residue is distributed among successful auction participants proportionally to the number of units they have purchased, AEMO forwards the auction proceeds to the TNSPs located in the importing regions. As TNSPs regulated revenue is set, all else being equal, the auction proceeds result in decreased transmission use of system charges for the TNSP's customers.

Currently, units purchased at AEMO auctions may be traded bilaterally among auction participants, but secondary trading is not permitted through the auction process. This is because the National Electricity Rules (NER) only allow AEMO to pay auction proceeds to the TNSPs and not to auction participants.

The draft rule

The draft rule, which is a more preferable rule, addresses the same issues as Westpac's proposed rule, but takes a different approach with regards to consequences of any additional risks that may arise in relation to secondary trading.

The draft rule:

- enables auction participants to offer their previously purchased units for sale at subsequent auctions facilitated by AEMO
- requires AEMO to distribute auction proceeds to either the relevant TNSP or auction participant, as the case may be
- requires AEMO to pay the relevant auction proceeds associated with the primary auction to the TNSP prior to paying out any auction proceeds to any secondary seller
- prohibits the auction rules from placing additional risks related to secondary trading on AEMO and TNSPs.

The draft rule enables AEMO to provide a platform for secondary trading of settlements residue distribution units.

The rule change request

Westpac proposed to amend the NER to allow AEMO to distribute the relevant portion of the auction proceeds to the sellers of units.

This included amending the NER to allow:

- auction participants to offer units for sale at AEMO auctions
- AEMO to pay for those units, cancel them and offer them for sale again
- AEMO to distribute part of the auction proceeds to the sellers of units
- AEMO to recover money from TNSPs, if payments fall short because of an auction participant default.

Westpac considered that these changes will provide a number of benefits, including:

- anonymous trading
- increased liquidity
- simplified execution of trades
- reduced default, credit and settlement risk for auction participants
- increased ability to optimise risks created by a changing portfolio.

Submissions

The draft determination and the draft rule are both available on the AEMC website. Stakeholders are invited to make written submissions in by **29 August 2017**.

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