



Regulation of Hydro Tasmania's wholesale  
electricity contract pricing activities in  
Tasmania

FRAMEWORK INFORMATION PAPER

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# TABLE OF CONTENTS

<b>1</b>	<b>PURPOSE OF THE INFORMATION PAPER .....</b>	<b>1</b>
<b>2</b>	<b>INTRODUCTION .....</b>	<b>2</b>
<b>3</b>	<b>LEGISLATIVE FRAMEWORK AND RELATED DOCUMENTS .....</b>	<b>4</b>
<b>4</b>	<b>THE WHOLESALE CONTRACT REGULATORY INSTRUMENT.....</b>	<b>6</b>
4.1	Types of financial contracts .....	6
4.2	Standard form of contracts.....	7
4.3	Contract pricing methodology .....	7
4.3.1	Baseload Cap Contract Prices .....	9
4.3.2	Peak and Baseload Swap Contract Prices .....	11
4.3.3	Load Following Swap Contract Prices .....	14
4.4	Total period for contracts .....	16
4.5	Minimum quantity offered for contracts.....	17
<b>5</b>	<b>THE WEEKLY OFFER PROCESS.....</b>	<b>18</b>
5.1	Supplementary Weekly Offer .....	18
5.2	Traffic Light Indicator .....	19
5.3	“Catch-Up” .....	20
<b>6</b>	<b>USE OF THE LOAD FOLLOWING SWAP CONTRACT PRICE OUTSIDE OF THE WHOLESALE FRAMEWORK .....</b>	<b>21</b>

# 1 PURPOSE OF THE INFORMATION PAPER

This Information Paper provides:

1. high-level background on the history of wholesale contract regulation in Tasmania;
2. an overview of the key features of the framework applied in regulating the pricing of some of Hydro Tasmania's wholesale electricity contracts;
3. a general understanding of the framework;
4. explains how and why regulated wholesale contracts are offered in Tasmania; and
5. describes the use of regulated wholesale contract pricing in determining standing offer electricity prices<sup>1</sup> since 1 July 2014.

This Information Paper is based on legislation and Government policies current as at 29 May 2023.

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<sup>1</sup> Standing offer prices are paid by small customers on standard retail contracts. Small customers are residential customers as well as small business customers on mainland Tasmania (including Bruny Island) consuming less than 150 megawatts of electricity in a year.

## 2 INTRODUCTION

Historically, residential and small business customers in Tasmania could only purchase their electricity from one electricity retailer. This changed in 2013, when the Tasmanian Government amended the *Electricity Supply Industry Act 1995* to facilitate the introduction of retail competition in Tasmania. These amendments included:

- opening the electricity retail market to competition for residential and small business customers;
- enhancing customer protection safeguards, including retaining retail price regulation and a right of reversion to a regulated contract for residential and small business customers;
- establishing the regulation of Hydro Tasmania's wholesale contract market activities;
- incorporating the existing electricity concessions framework into legislation and ensuring that it will continue in a competitive private sector retail market;
- ensuring the Regulator's functions and objectives struck the right balance for the new market structure;
- amending the non-price regulatory framework of the National Energy Customer Framework to reflect the intended divestment of Aurora Energy<sup>2</sup>; and
- providing for sensible transition arrangements to a fully competitive market.<sup>3</sup>

The regulation of Hydro Tasmania's wholesale contract activities was considered necessary to create a competitive environment for any new private sector retailers wanting to enter the Tasmania residential and small business customer market, as the aim of the regulation was to mitigate the potential retailers' concern that their retail margins could be materially reduced by the actions of a dominant generator ie. Hydro Tasmania.

Despite several new generators commencing operations in Tasmania since 2013, Hydro Tasmania remains the dominant generator.

Hydro Tasmania also owns the gas-fired Aurora Energy Tamar Valley (AETV) power station and has a 25 per cent share in Woolnorth Wind Holding Pty Ltd (Woolnorth), which operates the Musselroe, Studland Bay and Bluff Point wind farms in Tasmania. The regulation of Hydro Tasmania's wholesale contract activities does not apply to either AETV or wind farms operated by Woolnorth.

The framework for regulating Hydro Tasmania's wholesale contract activities was developed in accordance with the following design principles:

- retailers should have confidence that they can manage their wholesale risks appropriately in Tasmania;

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<sup>2</sup> The intended divestment of Aurora Energy did not occur due to a lack of interest from other parties.

<sup>3</sup> The summary of amendments is taken from the Second Reading Speech for the *Electricity Reform Implementation Bill 2013*.

- the risks of operating in the Tasmanian market should be no greater than those in other jurisdictions in the National Electricity Market (NEM);
- retailers should have the flexibility to manage wholesale market risk using similar business models to those used in other NEM jurisdictions; and
- recognise the interaction between spot and financial risk contract markets without creating unintended incentives or consequences.

The framework came into effect through approvals made by the then Minister for Finance on 30 July 2013 as set out in a Wholesale Contract Regulatory Instrument (the Instrument). Since then, the framework has been administered by the Tasmanian Economic Regulator who has made approvals and released instruments setting out those approvals.

The Regulator is also responsible for conducting investigations to determine whether amendments to the Instrument are necessary.

This Information Paper is structured as follows:

- Chapter 3 - the legislative framework governing the wholesale framework.
- Chapter 4 - how the framework is set out in the Instrument;
- Chapter 5 - Hydro Tasmania's weekly offer process; and
- Chapter 6 - how the Instrument is used in determining the wholesale electricity prices.

### 3 LEGISLATIVE FRAMEWORK AND RELATED DOCUMENTS

The framework regulating Hydro Tasmania's wholesale contract market activities is governed by the *Electricity Supply Industry Act 1995* (ESI Act) and the *Electricity Supply Industry (Pricing and Related Matters) Regulations 2023* (ESI Pricing Regulations).

Section 43G(1) of the ESI Act prescribes that the Regulator must approve:

- the financial risk contract types that Hydro Tasmania must make available to retailers associated with the purchase of electricity supplied;
- the standard form of the approved contract types;
- the methodology for calculating the prices for the approved contract types;
- the total period that a retailer may have the contract apply to prices for electricity; and
- the methodology for determining the minimum total quantity of electricity for an approved contract type.

Under section 43G(3) of the ESI Act, the Regulator must also declare a load following swap contract to be one of the approved contract types.

Section 43H of the ESI Act requires the Regulator to take the following principles into account in making an approval under Section 43G(1):

- the authorised retailers should have a choice of different contract types to enter into with Hydro Tasmania;
- an approved contract type should be commonly used in the NEM;
- an approved standard form for any contract type should be similar to the ones used in the NEM;
- the total period referred to in the approved contract types should be a duration similar to the total period generally used in the NEM;
- an approved pricing methodology for any approved contract type should be based on the price of financial risk contracts in the Victorian futures market and adjusted to accommodate any estimation of the effect of the difference between the Victorian and the Tasmanian markets; and
- an approved pricing methodology for any contract type should reflect the risk to an authorised retailer.

Section 43I of the ESI Act requires that Hydro Tasmania must offer an authorised retailer each type of approved contract and at the request of an authorised retailer, enter into an approved contract with the retailer.

Section 43M of the ESI Act prescribes that in the event that there has been a significant, deliberate or repeated failure by Hydro Tasmania to apply the approved pricing methodology to its regulated

contracts, the Regulator is to step in and approve regulated contract prices. The Regulator may also suspend the regulatory framework under certain extraordinary circumstances.

Section 43N of the ESI Act provides the Regulator with the power to fix the prices of the approve contract types under Section 43M.

Regulations 17 to 21 of the ESI Pricing Regulations set out how the Regulator must conduct an investigation to make or revoke an approval made under Section 43G of the ESI Act.

In addition to the legislative framework, the Regulator has also prepared and released the following documents to support the operation of Instrument:

- *Electricity Wholesale Contract Guideline*. This sets out the weekly regulated contract offer process and Hydro Tasmania's responsibilities in relation to contracting in the regulated wholesale electricity market.
- *Statement of Regulatory Intent Wholesale Contract Regulation*. This sets out, amongst other things, the conditions under which, and the process whereby, the Regulator may step in and fix regulated wholesale contract prices.
- *Approach to updating the inputs in Schedule 1 of the Wholesale Contract Regulatory Instrument*. This outlines the approach to update the inputs in Schedule 1 of the Instrument.
- Updated Schedule 1 Values. This contains the Schedule 1 values updated according to the approach guideline and released on the Regulator's website every 12 months.



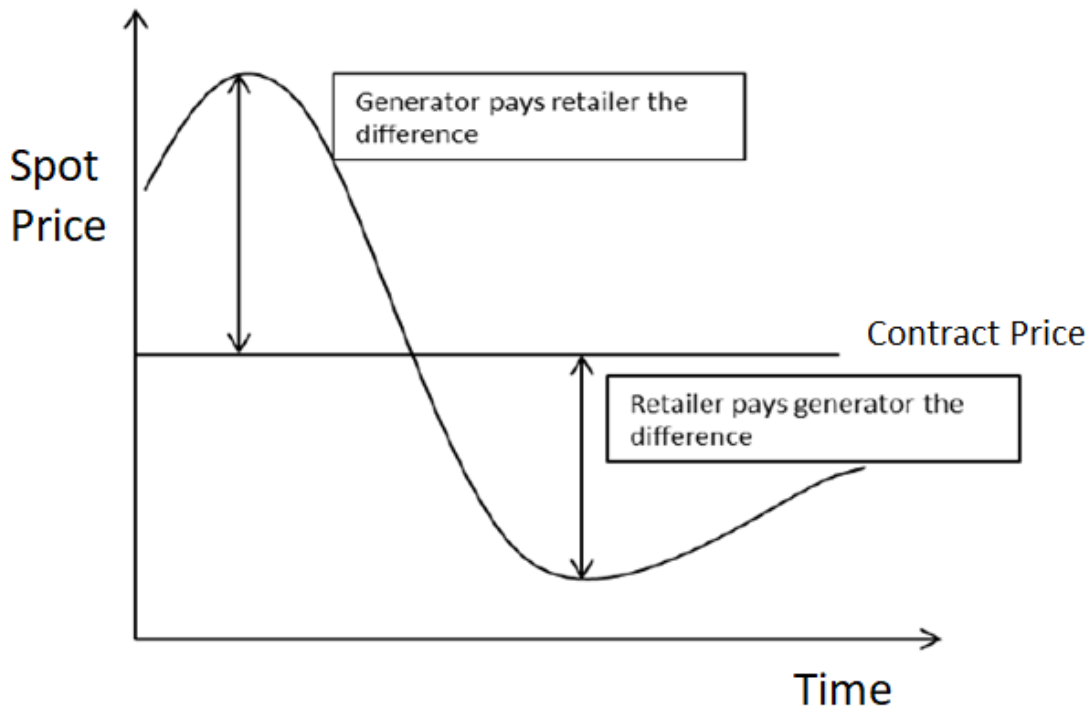
## 4 THE WHOLESALE CONTRACT REGULATORY INSTRUMENT

### 4.1 Types of financial risk contracts

Clause 3 of the Instrument sets out the financial risk contract types that are approved by the Regulator in accordance with Section 43G of the ESI Act.

In the NEM, generators and retailers can mitigate the risk associated with fluctuations in spot prices by entering into financial risk contracts with a set of agreed contract prices. That is, if the spot price is higher than the agreed contract price, the generator will pay the retailer the difference between the agreed contract price and the spot price; and if the spot price is lower than the agreed contract price, the retailer will pay the generator the difference.

Figure 1: a basic hedging contract<sup>4</sup>



Through the approvals set out in the Instrument, the Regulator approves four types of financial risk contracts. Each week Hydro Tasmania is required to offer these contracts to authorised retailers at prices calculated using a Wholesale Pricing Model that applies the formulae and principles set out in the Instrument. The four contract types are as follows:

- a baseload cap, which is a contract for a fixed amount of electricity, where the purchaser pays a premium for the right to pay a maximum of \$300 per MWh at all times during a quarter. This means that when the spot price in the market is below \$300 per MWh, the purchaser of the

<sup>4</sup> Figure 1 is based on the graph in the Productivity Commission's *Electricity Network Regulation Inquiry Report Appendix C - Hedging in the electricity market*, page 834.

contract will pay the spot price plus the premium, but when the spot price is above \$300 per MWh, the purchaser of the contract pays \$300 per MWh plus the premium;

- a baseload swap, which is a contract to trade a fixed amount of electricity for a contract price at all times during a quarter;
- a peak swap, which is a contract to trade a fixed amount of electricity for a certain price only during the peak time periods of a quarter; and
- a load following swap, which is a contract associated with the purchase of a specified quantity of electricity over the duration of the contract, where that quantity is allocated to trading intervals, in proportion to the Tasmanian net system load profile.<sup>5</sup>

An authorised retailer may seek to manage the risk associated with their customer load by using one or more of the regulated financial risk contracts or negotiating other forms of financial risk contracts (eg unregulated contracts) with Hydro Tasmania.

## 4.2 Standard form of contracts

Clause 4.1 of the Instrument sets out a standard form contract for each regulated financial risk contract.

The standard form contract is in place to ensure that all authorised retailers have access to regulated financial risk contracts on the same terms and conditions.

The approved standard form for each regulated financial risk contract comprises:

- the ISDA 2002 Master Agreement;
- the Hydro Tasmania Schedule for the Authorised Retailer (included in Schedule 2 of the Instrument); and
- the confirmation for that regulated financial risk contract (included in Schedules 3 to 6 of the Instrument).

The standard form in the Instrument provides for a number of permitted and required alterations to be made to the standard form (eg for volume and price).

If retailers do not wish to use the standard form contracts, they can negotiate an alternative standard form contract with Hydro Tasmania to apply to regulated contracts. The alternative standard form contract must be approved by the Regulator.

## 4.3 Contract pricing methodology

Clauses 6 to 16 of the Instrument prescribe the methodology for calculating the maximum prices for the four types of approved financial risk contract that Hydro Tasmania must offer.

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<sup>5</sup> The Tasmanian net system load profile is determined by the Australian Energy Market Operator (AEMO).

The Instrument defines peak and off-peak hours in accordance with the ASX's definition. Under this definition, peak hours are 7:00 am to 10:00 pm in any business day on Eastern Standard Time and the remaining hours are off-peak hours.<sup>6</sup>

The Instrument applies an Open Interest Liquidity test to the Victorian futures contract prices. Open Interest in the ASX Energy Market is the total number of contracts that are not closed or delivered at the close of business on the previous day. The Open Interest is the level of liquidity trading in the Victorian energy futures market. A low level of Open Interest is an indication that either no trading is occurring, or trading is occurring outside of the open market, therefore the Victorian futures contract prices in the market may not adequately reflect the market prices.

The methodology described in the Instrument only uses the actual Victorian peak swap and / or baseload cap contract prices for any forward quarters where the Victorian Open Interest for peak swap and / or baseload cap exceeds 100 MW or the forward quarter is less than four quarters from the current quarter.

For quarters where the Open Interest for the Victorian baseload cap contract is below 100 MW and / or is more than four quarters from the current quarter, the Victorian baseload cap contract price from the same quarter last year will be used. In contrast, for quarters where the Open Interest for the Victorian peak swap contract is below 100 MW and / or is more than four quarters from the current quarter, the Victorian peak swap contract price is calculated from past Victorian baseload swap, baseload cap and peak swap contract prices.

The methodology in the Instrument is underpinned by two key relationships between swap contract prices:

- a)  $\text{Swap} = \text{Capped Swap} + \text{Cap}$
- b)  $\text{Baseload} = \text{Sum of the time weighted ratio of Peak and Off-Peak}$

Under the Instrument, the Victorian cap contract prices are first removed from the Victorian swap contract prices to derive the Victorian capped swap prices for peak, off-peak and baseload contracts. The relationships between the Victorian contracts are shown in Table 1, where the contracts in bold are inputs not determined by the methodology.

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<sup>6</sup> This differs from how distributors and retailers define peak and off-peak hours across distribution areas in Victoria and Tasmania.

**Table 1: Relationship between the different Victorian contract types**

Contract type	Swap	Capped Swap	Cap
Baseload	<b>Baseload swap contract price</b>	Baseload capped swap price = baseload swap contract price - baseload cap contract price	<b>Baseload cap contract price</b>
Off-Peak	Off-Peak swap contract price = time weighted difference between the baseload swap contract price and the peak swap contract price	Off-peak capped swap price = off-peak swap contract price - off-peak cap contract price	<b>Off-peak cap contract price</b>
Peak	<b>Peak swap contract price</b>	Peak capped swap price = time weighted difference between the baseload capped swap price and the off-peak capped swap price	Peak cap contract price = time weighted difference between the baseload cap contract price and the off-peak cap contract price

The Victorian capped swap prices are then used to calculate the Tasmanian capped swap prices. The Tasmanian swap contract prices are the sum of the Tasmanian capped swap prices and the Tasmanian cap contract prices.

The capped swaps are not market contracts, they are creations under the Instrument, which are intended to represent the price of swaps without the risk of high prices. This is because high prices in the Victorian and Tasmanian spot market occur at different times in a year, and this is factored into the methodology through the capped swaps. For the Victorian spot market, high prices tend to occur in the summer months, while for the Tasmanian spot market, high prices tend to occur in the winter months ie when load is at its highest in each jurisdiction.

### 4.3.1 Baseload Cap Contract Prices

The Tasmanian baseload cap contract price is a major component in the calculation of Tasmanian baseload and peak swap contract prices. It is designed so that if the price in the spot market exceeds \$300 per MWh, the generator is required to pay the retailer the difference between the spot price and \$300 per MWh during a specific contract period. Therefore, a retailer would only purchase this contract from Hydro Tasmania if a retailer thinks the risk of a price over \$300 per MWh is high and the cost it will incur from the price being above \$300 per MW is greater than the cost of purchasing the baseload cap contract.

The methodology uses the Victorian baseload cap contract price as the market-based benchmark and weights it by the estimated risk that the maximum load will exceed the non-major storage capacity in Tasmania. This is then adjusted by the weighted real cost of building a generic gas-fired open cycle peaking generator. To prevent the calculated Tasmanian baseload cap price from being negative, the methodology uses an estimated Tasmanian off-peak cap contract price as the Tasmanian baseload cap contract price when the calculated baseload cap price is negative.

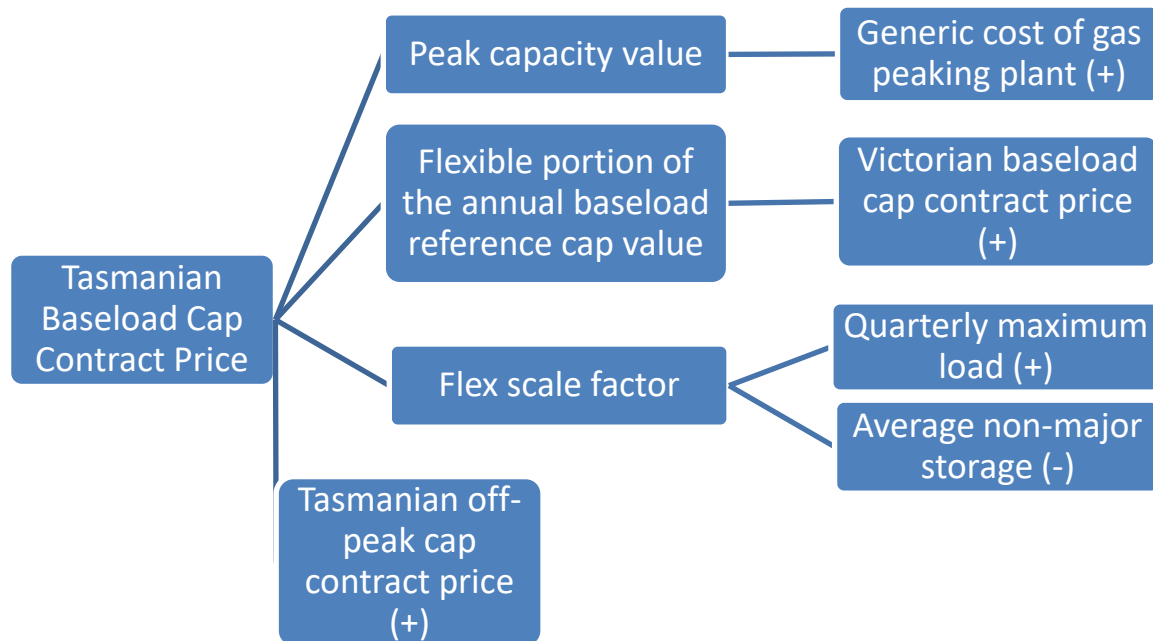
### ***Methodology***

Under the Instrument, the Tasmanian baseload cap contract is the higher of two values, the Tasmanian off-peak cap contract price as set by the Regulator annually, or the sum of the **peak capacity value** and the **flexible portion of the annual baseload reference cap value** weighted by the **flex scale factor**:

- the **flex scale factor** is the weighted difference between the largest annual maximum load in the last three years and Hydro Tasmania's average non-major storage level over 12 years;
- the **flexible portion of the annual baseload reference cap value** is the weighted difference between the current Victorian baseload cap contract price and the lowest Victorian baseload cap contract price in the current and next three quarters;
- the **peak capacity value** is the weighted real cost for building a generic gas fire open cycle peaking generator as estimated by the Regulator annually and set out in Schedule 1 of the Instrument; and
- the Tasmanian off-peak cap contract price (**off-peak cap value**) is calculated by the Regulator annually from the average Tasmanian off-peak spot prices in the last ten years and set out in Schedule 1 of the Instrument.

Figure 2 below breaks down the Tasmanian baseload cap contract price into basic inputs, which are determined outside of the methodology. The signs in the brackets behind every basic input indicate the relationship between the input and the Tasmanian baseload cap contract price, i.e., when the value of the input increases for a particular quarter, the Tasmanian baseload cap contract price will increase (+) or decrease (-) respectively for that quarter.

Figure 2: Breakdown of the Tasmanian baseload cap contract price by input



### 4.3.2 Peak and Baseload Swap Contract Prices

The methodology uses the Victorian peak and baseload swap contract prices as the market-based benchmark, then removes the calculated Victorian peak and baseload cap contract price and adjusts them by import and export conditions over Basslink, electricity generation and customer load in Tasmania, and the Tasmanian baseload cap contract price to calculate the peak and baseload swap contract prices in Tasmania.

#### *Methodology*

The Tasmanian peak swap contract price is the sum of two components:

- the **peak capped swap value**, which is the energy component of the swap and is calculated from the sum of the Victorian peak swap contract prices and time weighted by the difference between the Victorian off-peak cap contract price and the Victorian baseload cap contract price, multiplied by the **average peak marginal loss factor** and adjusted by the **peak import price premium**; and
- the **peak cap value**, the capacity component of the swap, is calculated from the time-weighted difference between the Tasmanian baseload cap contract price and the Tasmanian off-peak cap contract price.

The Tasmanian baseload swap contract price is the sum of two components:

- the **baseload capped swap value**, which is the energy component of the swap and is the weighted **peak capped swap value** and **off-peak capped swap value**; and
- the **baseload cap value**, which is the capacity component of the swap and is the Tasmanian baseload cap contract price.

The Victorian off-peak cap contract price (**off-peak reference cap value**) is calculated by the Regulator annually from the average Victorian off-peak spot prices in the last ten years with the result set out in Schedule 1 of the Instrument.

The **off-peak capped swap value** is calculated by subtracting the **off-peak cap contract price** from the weighted difference between the Victorian baseload swap contract price and the Victorian peak swap contract price, multiplied by the **average off-peak marginal loss factor** and adjusted by the **off-peak import price premium**.

The **average peak and off-peak marginal loss factors** are calculated from the **energy surplus**, the **maximum export marginal loss factor** and the **maximum import marginal loss factor**, which represent the average expected price difference between Tasmania and Victoria during peak hours and are the result of transmission losses and / or constraints over the Basslink interconnector. The **maximum export marginal loss factor** and the **maximum import marginal loss factor** are set by the Regulator in Schedule 1 of the Instrument and updated annually.

The **peak** and **off-peak import price premiums** are calculated using a quadratic function of the percentage of time importing and are proportional to the difference between the Victoria peak swap contract price and the Victorian off-peak cap contract price.

The **energy surplus** is the difference between the sum of **forecast hydro generation** and **wind generation** and the **forecast energy demand**. The **forecast hydro generation** is calculated from Hydro Tasmania's actual quarterly hydro yield, while the **forecast wind generation** and the **forecast energy demand** are, respectively, AEMO's latest generation and demand forecasts.

Figure 3 below breaks down the Tasmanian baseload swap contract price into basic inputs, which are determined outside of the methodology. The sign in the brackets for each basic input indicates the relationship between the input and the Tasmanian baseload swap contract price, i.e., when the value of the input increases for a particular quarter, the Tasmanian baseload swap contract price will increase (+) or decrease (-), respectively, for that quarter.

Figure 3: Breakdown of baseload swap contract prices by input

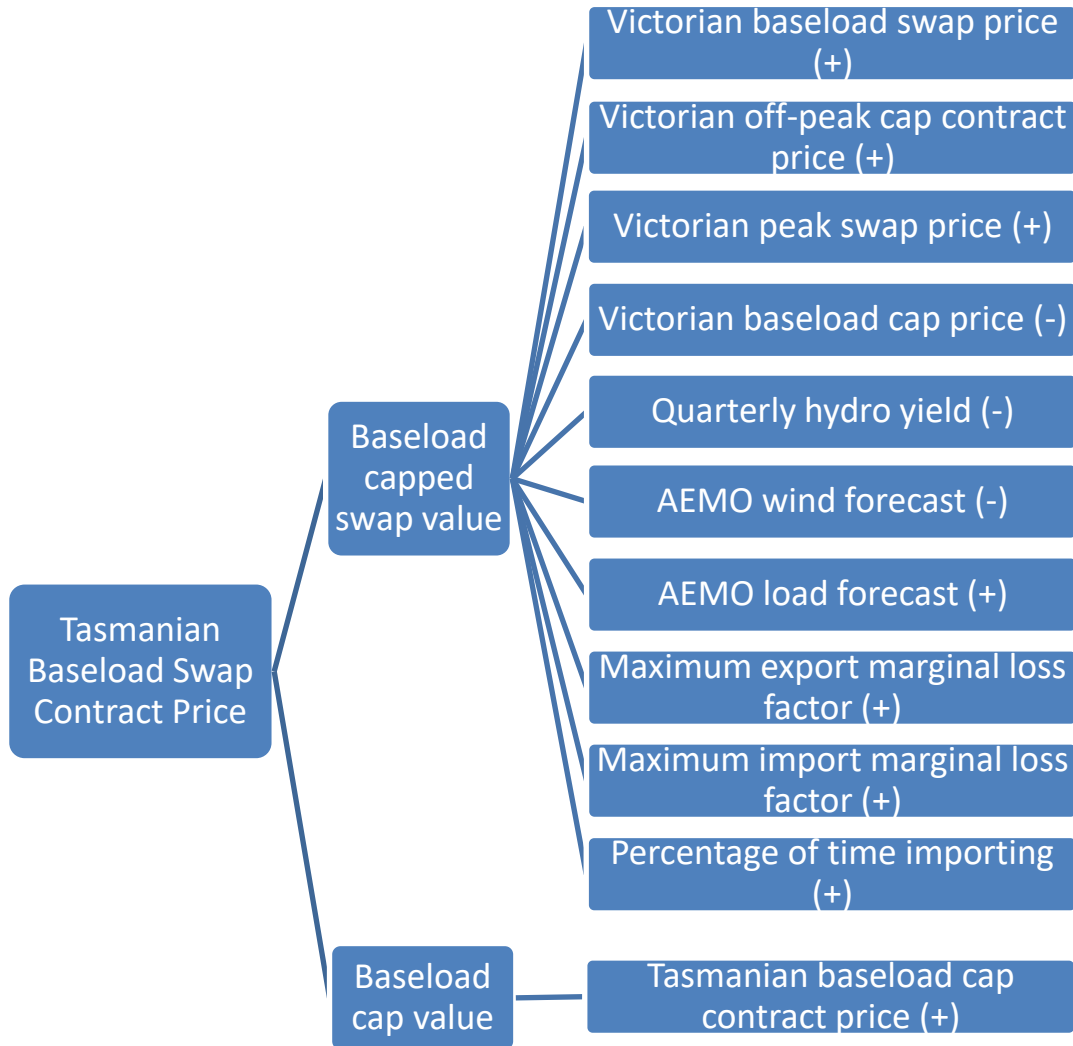
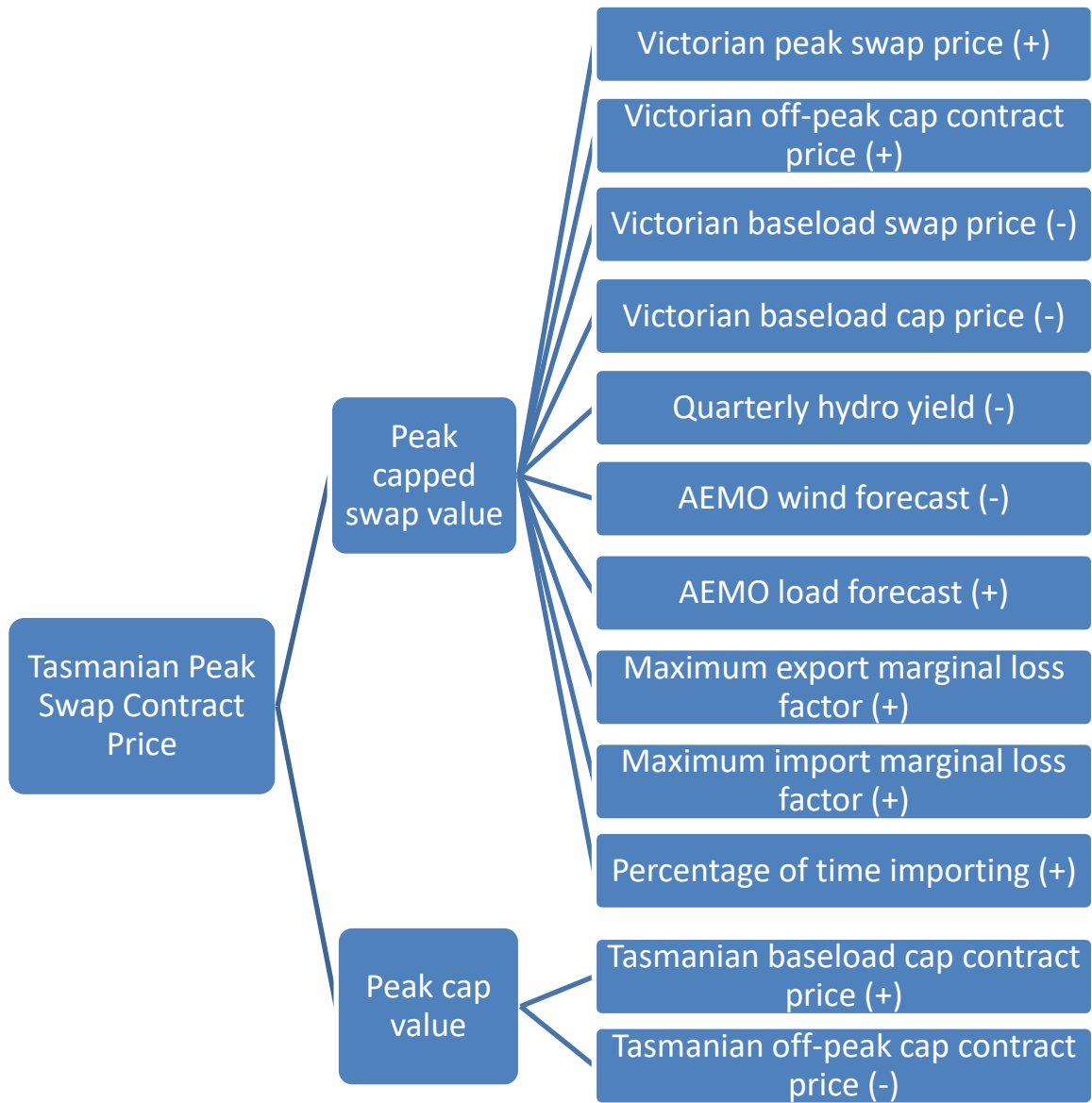


Figure 4 below breaks down the Tasmanian peak swap contract price into basic inputs, which are determined outside of the methodology. The signs in the brackets for each basic input indicates the relationship between the input and the Tasmanian peak swap contract price, i.e., when the value of the input increases for a particular quarter, the Tasmanian peak swap contract price will increase (+) or decrease (-), respectively, for that quarter.



Figure 4: Breakdown of the peak swap contract prices by input



### 4.3.3 Load Following Swap Contract Prices

The load following swap contract is designed to provide retailers with flexibility in hedging customer load where the hedging profile must account for load fluctuations. Most of the load following swap price is based on the time-weighted sum of the Tasmanian peak and off-peak swap contract price, which represent the cost of baseload electricity consumption. The load weighted Victorian contract premium and the load weighted Tasmanian baseload cap price are added to represent the cost of additional hedges during peak time and the cost of high prices in Tasmania respectively.

## Methodology

The load following swap contract price is the sum of three components:

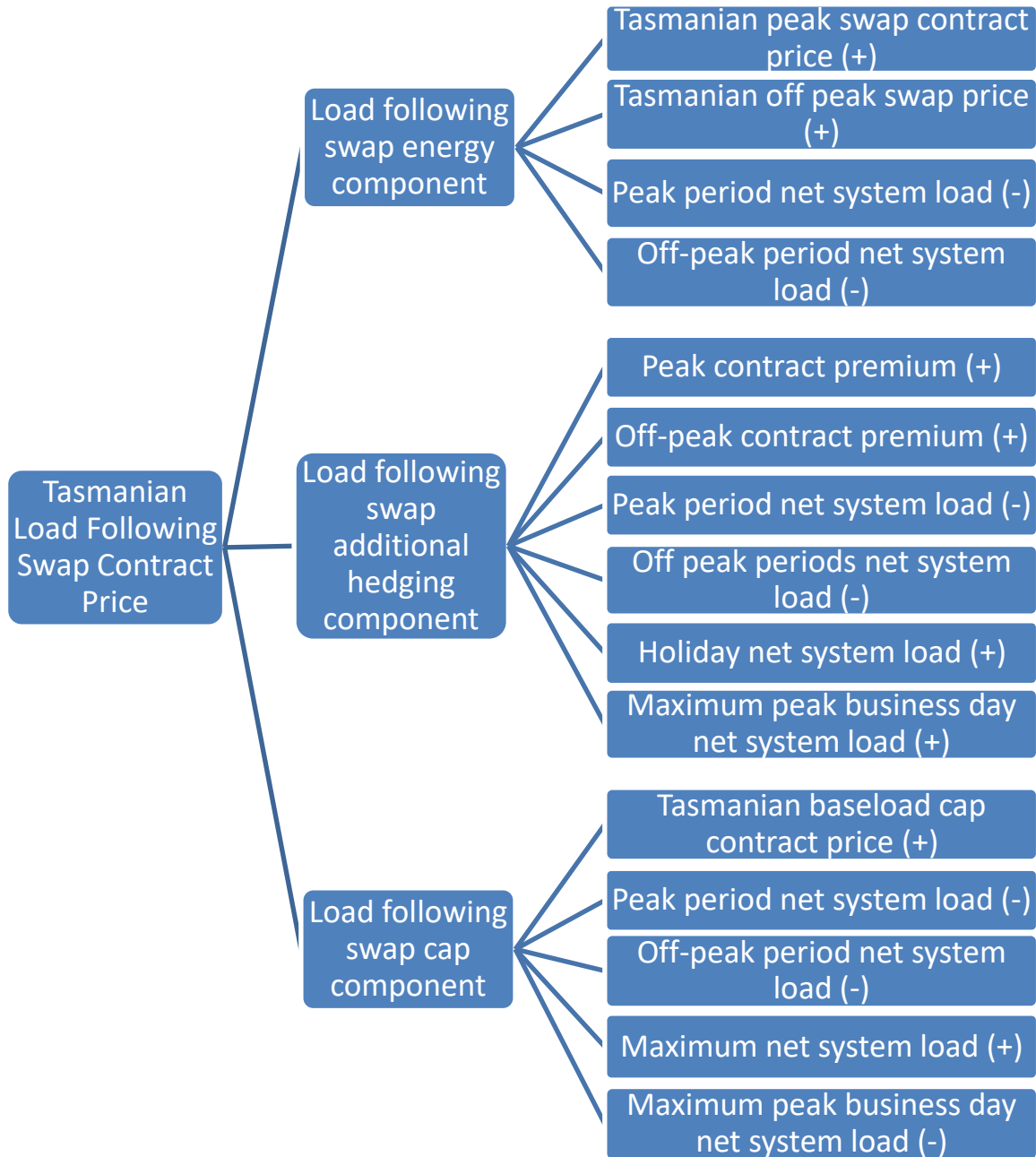
- the **load following swap energy component**, which accounts for the majority of the price in most quarters, and is the sum of the Tasmanian peak swap contract price and the Tasmanian off-peak swap contract price, weighted by the **average load on the distribution system during peak and off-peak periods** in a quarter;
- the **load following swap additional hedging component**, which is the **peak and off-peak contract premiums** weighted by the difference between the **average load on the distribution system during non-business periods and off-peak periods**, and the difference between the **average maximum load on the distribution system during business day peak periods and average load during peak periods** in a quarter; and
- the **load following swap cap component**, which is the baseload cap contract price multiplied by the difference between the **average maximum load on the distribution system during a quarter and during peak time periods** of that quarter.

The **peak and off-peak contract premium** are set by the Regulator in Schedule 1 of the Instrument and updated annually. The **peak and off-peak contract premiums** are the Regulator's estimate of the difference between the peak and off-peak swaps in Victoria and average spot prices in Victoria during peak and off-peak time periods.

The Tasmanian off-peak swap contract is not an approved contract type, it is created under the methodology and used to calculate the baseload and peak swap contracts price. The price of the off-peak swap contract is calculated following a similar methodology as the price of the Tasmanian peak swap contract, as shown in section 4.3.2 of this paper. The basic inputs for the Tasmanian off-peak swap contract price are the same as the basic inputs for the Tasmanian peak swap contract price, apart from addition of the Tasmanian baseload cap contract price.

Figure 5 breaks down the Tasmanian load following swap contract price into basic inputs, which are determined outside of the methodology. The sign in the brackets for each basic input indicates the relationship between the input and the Tasmanian load following swap contract price, i.e., when the value of the input increases for a particular quarter, the Tasmanian load following swap contract price will increase (+) or decrease (-), respectively, for that quarter.

Figure 5: Breakdown of the load following swap contract price into components



#### 4.4 Total period for contracts

Clause 19 of the Instrument prescribes the period that Hydro Tasmania is required to offer the financial risk contracts for.

Hydro Tasmania is required to offer the regulated financial risk contracts for the eight forward quarters, provided there is more than 100 MW of Open Interest in Victorian Baseload Swaps in that quarter. Hydro Tasmania is not required to offer financial risk contracts for the current quarter.

In each of the eight forward quarters in which the Test is met, Hydro Tasmania is required to offer the four regulated Tasmanian financial risk contracts for the relevant quarter. If the Test is not met in a particular quarter, Hydro Tasmania is not required to offer regulated financial risk contracts in that quarter until the Test is met.

As discussed earlier, the 100 MW Open Interest Liquidity Test recognises that there may be times when the published Victorian futures contract market prices used in the pricing methodology does not adequately reflect the market price in Victoria due to limited trading in that market.

## 4.5 Minimum quantity offered for contracts

Clause 23.4 of the Instrument sets out the minimum quantity (ie volume of electricity) that must be offered to retailers via the regulated contracts.

For each of the eight forward quarters in which the Open Interest Test is met, Hydro Tasmania must make available at least the Absolute Minimum Energy Offer Volume and the Absolute Minimum Capacity Volume for that quarter. The Absolute Minimum Energy Offer Volume is calculated from the Absolute Minimum Capacity Offer Volume, which is determined annually by the Regulator in Schedule 1 of the Instrument.

The Absolute Minimum Capacity Volume is the capacity volume that Hydro Tasmania offers each week for eight forward quarters where the Open Interest Liquidity test has been met. It is calculated by allocating the annual small customer<sup>7</sup> load on the distribution system into each of the four quarters in a year using a seasonal factor, then dividing the quarterly small customer load by the number of hours in that quarter and by the 104 weeks in the eight forward quarters that the volume is to be offered for purchase.

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<sup>7</sup> In Tasmania, a small customer is an electricity customer with annual consumption less than 150 MWh as defined in Regulation 4 of the *National Energy Retail Law (Tasmania) Regulations 2022*.

## 5 THE WEEKLY OFFER PROCESS

Under the Instrument, Hydro Tasmania must publish the prices and volumes of approved regulated energy and capacity contracts available to authorised retailers each week on its website.

The weekly offer process is set out in the current *Electricity - Wholesale Contract Guideline*.

The prices published by Hydro Tasmania are verified by the Regulator on Tuesday each week prior to publication at 12pm, to ensure the prices comply with the pricing methodology set out in the Instrument.

The authorised retailers must nominate the volume of energy or capacity they want to purchase from Hydro Tasmania for that week by 2pm on the same Tuesday.

After receiving the nominated volumes from authorised retailers, Hydro Tasmania checks whether the aggregate of the nominated volumes from all retailers exceeds the volume of energy and / or capacity offered in that week for the contract quarter.

If the aggregate of the nominated volumes does not exceed the volume offered, the authorised retailers receive their nominated volume.

Where the aggregate of the nominated volumes requested by authorised retailers exceeds Hydro Tasmania's weekly offer, Hydro Tasmania must apply the scaling rules to the entire nominated volume. Clause 27 of the Instrument sets out the scaling rules that are used to determine the minimum volume of each type of regulated contract that must be offered to each authorised retailer.

Under the scaling rules, priority access to 90 per cent of the Absolute Minimum Capacity Offer in any given week is given to authorised retailers serving small customers. These authorised retailers' priority access is based on their share of the Tasmania small customer market (in terms of the small customer load).

The 90 per cent reserve percentage for priority access is set by the Regulator in Schedule 1 of the Instrument and has been reviewed by the Regulator annually since 2017 to ensure that authorised retailers have a reasonable opportunity to enter the Tasmania market or expand their retail customer base in Tasmania.

Where scaling is required, Hydro Tasmania must provide the authorised retailers with confirmed volume of energy or capacity contracts by 3pm on the same Tuesday.

### 5.1 Supplementary Weekly Offer

In each of the eight forward quarters where Hydro Tasmania is required to offer regulated contracts, Hydro Tasmania will be required to make an additional Supplementary Weekly Offer, if it still has headroom after taking into account contracts already sold for that quarter and the unsold Absolute Minimum Volume (as discussed in Section 4.5 of this paper) at the time.

Headroom for supplementary offers is calculated as follows:

$$\begin{aligned} \textit{Headroom for supplementary offer} \\ &= \textit{Total Tasmanian Load} - \textit{Total contract already sold} \\ &- \textit{Unsold Absolute Minimum Volume} \end{aligned}$$

Depending on the amount of headroom available in Hydro Tasmania's contract book, there are two types of Supplementary Weekly Offers:

- a Full Supplementary Weekly Offer of 20 MW (44 GWh) per week if the amount of headroom is greater than 130 MW (200 GWh); and
- a Reduced Supplementary Weekly Offer of 10 MW (15 GWh) if the amount of head room is between 0 MW (0 GWh) and 130 MW (200 GWh).

The 130 MW capacity or 200 GWh energy (referred to as Capacity or Energy Buffers in Schedule 1 of the Instrument) used in determining whether the Full Supplementary Weekly Offer or Reduced Supplementary Weekly Offer applies, have been designed to enable a staged transition in the volume of regulated contracts that must be offered.

The values for the Supplementary Offer Capacity and Energy Volumes, Reduced Supplementary Offer Capacity and Energy Volumes, and Capacity and Energy Buffers have been reviewed and determined by the Regulator annually since 2017.

## 5.2 Traffic Light Indicator

The weekly offers published on Hydro Tasmania's website include traffic light indicators advising authorised retailers of the energy and capacity contract volumes available for each of the eight forward quarters for any given week.

The conditions for each traffic light indicator are also set out in the Instrument. Each traffic light indicator is represented by a different number in the weekly offer.

- Green light as represented by the number 3, means Hydro Tasmania's headroom is greater than the capacity buffer (130 MW) and the energy buffer (200 GWh) and Hydro Tasmania must make available the Absolute Minimum Weekly Offer and the Full Supplementary Weekly Offer;
- Amber light as represented by the number 2, means Hydro Tasmania's headroom is between zero and the capacity buffer (130 MW) and the energy buffer (200 GWh) and Hydro Tasmania must make available the Absolute Minimum Weekly Offer and the Reduced Supplementary Weekly Offer;
- Red light as represented by the number 1, means that Hydro Tasmania has no available headroom and Hydro Tasmania only needs to make available the Absolute Minimum Weekly Offer.

It is at Hydro Tasmania's discretion whether the Traffic Light Indicator is changed from green. This means that Hydro Tasmania may choose to maintain green light conditions (and the associated full

Supplementary Offer volume) even if it has less than 130MW (200GWh) of headroom in its contract book.

The Instrument states that Hydro Tasmania cannot switch immediately from green to red and must spend at least 12 weeks at amber before going to red. This will allow authorised retailers the opportunity to build a contract position using the Reduced Supplementary Offer during the amber period before the volume of contracts that are made available for a quarter is reduced to the Absolute Minimum Weekly Offer only.

### 5.3 “Catch-Up”

If contracts for a quarter are not required to be offered in any week because the open interest for the Victorian baseload swap contract for that quarter does not meet the Open Interest Liquidity Test, then a "catch-up" volume for that week, and any other weeks where the liquidity test is not met, will be made available in the future as part of the weekly volume release.

Hydro Tasmania publishes the weekly and cumulative "catch-up" volumes as part of its weekly offer.

## 6 USE OF THE LOAD FOLLOWING SWAP CONTRACT PRICE OUTSIDE OF THE WHOLESALE FRAMEWORK

The Regulator calculates Aurora Energy's annual notional maximum revenue (NMR) as a means of determining annual standing offer prices. Aurora Energy's NMR is made up of the following components:

- Wholesale energy costs;
- Metering costs;
- Network costs;
- Market participation charges levied by AEMO;
- Renewable Energy Target costs;
- Retail costs (cost to serve); and
- Retail margin.

Since the commencement of wholesale contract regulation in Tasmania on 1 July 2014, section 40AB(3) of the ESI Act has required the Regulator to use load following swap contract prices, as calculated under the Instrument in accordance with section 43G(1) of the ESI Act, in determining wholesale energy costs.

Specifically, wholesale energy costs are estimated by multiplying the wholesale electricity price (WEP) by the forecast total number of customers and by the distribution and marginal loss factors.<sup>8</sup>

The WEP used in this calculation is a weighted average price for load following swap contracts from the previous eight quarters. Clause 4.1 of the [2022 Standing Offer Price Approval Guideline](#) sets out the method the Regulator will use in calculating the WEP for each financial year covered by the 2022 Determination (ie the 2022-23, 2023-24 and 2024-25 financial years). The method is as follows:

- (a) multiply the weekly regulated load following swap (LFS) price for each respective quarter of the relevant year by the weekly Absolute Minimum Capacity Offer Volume for that quarter for eight quarters preceding the start of each quarter of the relevant year;
- (b) for those weeks where Hydro Tasmania is not required to offer regulated contracts, set the respective Absolute Minimum Capacity Offer Volumes to zero;
- (c) for all future weeks for which there is no regulated LFS price at the time that the Regulator calculates the WEP, use the respective weekly point-in-time regulated LFS price for that quarter of the relevant year in the week that the Regulator calculates the WEP; and

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<sup>8</sup> More information on wholesale energy costs and the other components of Aurora Energy's NMR can be found in the Regulator's [2022 Standing Offer Price Determination](#) and in the Regulator's [2022 Standing Offer Electricity Pricing Investigation Final Report](#).



(d) divide the sum of the values calculated in accordance with Clause 4.1(1)(a) by the sum of the weekly Absolute Minimum Capacity Offer Volumes for the eight quarters preceding the start of each quarter of the relevant year.

The Guideline also requires the Regulator to provide the calculated WEP to Aurora Energy by no later than 24 May each year for inclusion in Aurora Energy's annual pricing proposal (under the Guideline, Aurora Energy's proposal is due one week later on 31 May). Where weekly load following swap prices are not yet available, the weekly load following swap prices from the last available week in May prior to calculation are used for pricing for all future weeks. Consequently, the weekly load following swap prices from this week in May have a disproportionate effect, relative to the other load following swap prices, on the WEP for the following financial year.