10 May 2024

Mr Joe Dimasi
Tasmanian Economic Regulator
GPO Box 770
HOBART TAS 7001

By email: office@economicregulator.tas.gov.au

Dear Mr Dimasi,

Wholesale Contract Regulatory Instrument Pricing Investigation

Aurora Energy welcomes the opportunity to provide input to the Tasmanian Economic Regulator's Wholesale Contract Regulatory Instrument (the Instrument) pricing investigation (Investigation).

Aurora Energy supports all the Regulator's decisions in the Draft Report relating to the Instrument, the Wholesale Contract Guideline and the Statement of Regulatory Intent with the exception of those that relate to the following issues:

- Peak Swap Liquidity;
- Open Interest on Replacement Peak Futures Contract; and
- Calculation of Maximum Baseload $300 Cap Contract Price.

Attachment 1 to this letter outlines Aurora Energy response to these issues.

If you have any questions regarding this submission, please contact Giles Whitehouse, Corporate Affairs Manager, via email: giles.whitehouse@auroraenergy.com.au

Yours sincerely

Oliver Cousland
Company Secretary/General Counsel

Attachment 1 – Detailed Feedback on WCRI Investigation

Wholesale Contract Regulatory Instrument

Peak Swap Liquidity

Report reference	Regulator's proposed decisions
4.2.1	During the period when there is no listed peak futures contract and in the period until there is 100 MW in open interest in the replacement product, the Regulator proposes calculating the Victorian peak swap by applying a quarterly multiplier to the weekly Victorian baseload price.

Aurora Energy agrees with the Regulator's Draft Report that the reduction in peak swap liquidity and imminent delisting of the peak futures contract by the Australian Securities Exchange (ASX) presents a significant risk to the proper market-based functioning of the Instrument.

Aurora Energy agrees with the Regulator's assessment of options that peak swap price based on past prices, whether contract or spot, is not preferable as past prices are unlikely to reflect contemporary market conditions, even if the prices were from the corresponding quarters in previous years.

Aurora Energy is supportive of the Regulator's proposed option to determine peak prices by applying a multiplier to contemporary baseload prices. However, Aurora Energy does not support the following aspects of the proposed option:

1. the methodology that effectively averages the past four years peak to determine the baseload multipliers; or
2. or the multipliers proposed for each calendar quarter.

The Regulator's proposed multipliers based on the four-year averages place weighting to the 2021 and 2022 periods where multipliers were significantly lower then than the more contemporary periods of 2023 and 2024. Consequently, Aurora Energy contends that the multipliers proposed are not weighted sufficiently to near term/contemporary market outcomes. In determining this position, Aurora Energy observes the following:

- The Regulator notes in section 4.2.1 of the Draft Report that the wholesale electricity market is changing rapidly.
- The choice of using average outcome for respective quarters over four years fails to sufficiently recognise near-term contemporary market outcomes that observe higher peak ratios, particularly in Q2 and Q3 periods, that have increased 16 per cent and 10 per cent respectively since 2021.
- By using the four-year average since 2021, the Regulator's ratios present a discount to current peak ratios evident in the market (illustrated in Table 1 below).
    - This will have the effect of distorting the value energy in Vic peak contracts that flows through to the Instrument and create a disconnect between basis spot risk and hedging contract costs.

In determining the multipliers to apply to implement the Regulator's proposed option, Aurora Energy proposes adopting the recent two-year average peak to flat baseload multipliers from 2023 and 2024 periods to ensure the multiplier reflect contemporary outcomes. Table 1 below sets out a comparison of the prevailing forward contract market multipliers for 2024 compared to the Regulators four-year average and Aurora Energy's more contemporary two-year average.

Table 1: 2024 Peak Multipliers vs Regulator and Aurora Proposal

	Current 2024 Ratio	Regulator Proposed (4 Year Ave)	Regulator Variance to 2024 ratios	Aurora Proposed (2 Year Ave)	Aurora Variance to 2024 ratios
Q1	1.63	**1.60**	-1.8%	**1.60**	-1.8%
Q2	1.45	**1.30**	-10.3%	**1.40**	-3.6%
Q3	1.40	**1.30**	-7.1%	**1.36**	-3.3%
Q4	1.44	**1.40**	-2.8%	**1.40**	-2.8%

Aurora Energy believes implementing the multiplier option utilising the most recent two-year average will be the least distortionary and reduce potential disconnect between basis spot risk and hedging contract costs.

Open Interest on Replacement Peak Futures Contract

Report reference	Regulator's proposed decisions
4.2.1	Once the open interest in peak futures has reached 100 MW the Instrument will revert to using the ASX Energy peak futures value.

In the Draft Report, The Regulator has proposed *"…that the proxy Victorian peak futures price would be calculated (and used in the weekly wholesale price calculations) from the time the current peak futures contact is delisted until such time as the new peak contract reaches open interest of 100MW. At this point the market determined peak futures price will once again be included in the regulated wholesale price calculation."*.

In proposing its position in the Report, the Regulator suggests the replacement peak futures contract will have fewer peak hours which, by itself, would reduce regulated prices whilst also noting that any reduction in price could be offset if prices are relatively higher for the replacement contract. Aurora Energy does not support the automatic inclusion of the ASX's replacement peak futures contract to once again be included into the Instrument as proposed based on the following significant issues:

1. the definition of a peak contract is the Instrument is defined as 7am to 10pm working weekdays; and
2. the Instruments Net System Load Profile (NSLP) swap price book build will need to reviewed depending on the final structure of the replacement ASX peak product.

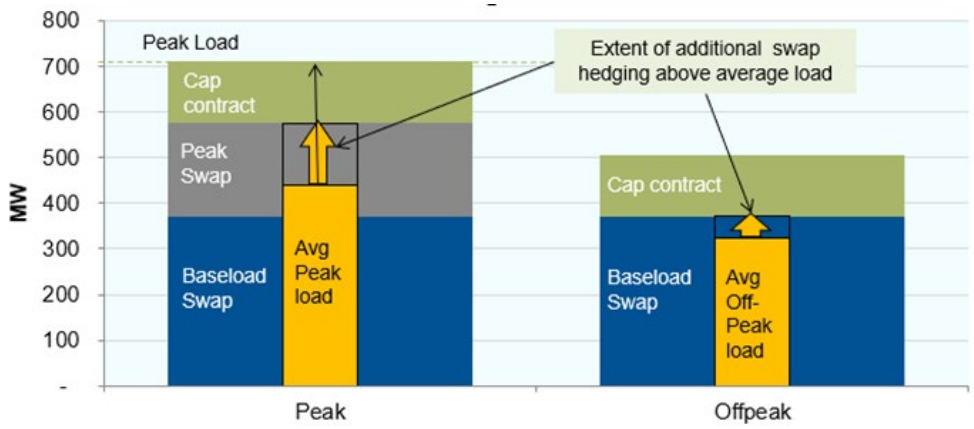
Given the Instrument defines the time period for peak swaps, the suggestion by the Regulator that the replacement peak products higher price will be offset by this mechanism covering fewer hours is not accurate. As proposed, the higher price will flow through but it will not apply for fewer hours as suggested in the Report given the peak swap hours are defined in the Instrument. This issue may be able to be overcome by changing the Instrument reference to the peak product to the ASX definition. However, this would be contingent on the replacement ASX Energy product being finalised and would also imply that ASX will introduce only one replacement product. In this context, Aurora understands that consideration is being given to multiple peak products in the ASX futures market (i.e. two separate morning and afternoon peak products). Given that ASX Energy has yet to finalise the replacement product design, it would present a significant risk to align the Instrument to a future unknown product.

Beyond the Instrument's definition of peak swap periods, Aurora Energy believes the Regulator's proposed inclusion of the replacement ASX product fails to consider the impact on the NSLP contract

book build. Aurora Energy considers this a major issue given the NSLP product is the primary input into the Wholesale Energy Price (WEP) for small customers in the Standing Offer Retail Price Determination.

In the Instrument, the NSLP contract is calculated by assessing the costs to a retailer serving the Tasmanian Net System Load of adopting an assessed prudent hedge profile to account for load fluctuations. In effect, it is a book build of the Instrument flat, peak and cap contracts to hedge the usage profile for mass market/NSLP customers as illustrated in Figure 1 below.

Figure 1: Instrument NSLP Book Build



Whilst Aurora considers that the replacement ASX peak product will be good for retailers as a stand-alone replacement product for the current peak product, the Regulator has not considered the impact and complexities that the replacement ASX peak product will have to the NSLP contract within the Instrument.

Aurora Energy contends that any change to coverage periods of peak periods will require a review of the NSLP book build to ensure that it reflects the cost to retailers to hedge the mass market/NSLP load shape. For example, should the ASX Energy peak product only cover evening periods, the NSLP book build structure would need to consider what changes are required to account for the fact that the Tasmanian NSLP/mass market demand has morning peak demand periods. In this scenario, the NSLP book build would require additional cap volumes being included given the ASX Energy product would be ineffective in hedging this period.

Not considering the impact on the NSLP product presents a significant risk that the NSLP product will be distorted from market outcomes, by way of the NSLP contract no longer reflecting a prudent book build of contracts to hedge the mass market/NSLP demand profile. In addition, Aurora Energy also expects that the price of the NSLP contract under the Instrument will likely increase as the expected higher price of the replacement ASX Energy peak product flows through to the NSLP contract. As Aurora Energy has already noted, this higher price won't be offset by a reduction in the hours it applies for and this higher NSLP contract price that would flow through to mass market customer prices through the WEP methodology in the Standing Offer Determination.

Based on the issues noted above, being the unknown periods that ASX Energy's replacement peak futures contract will cover, as well as the impact on the NSLP book build approach, Aurora Energy does not support the Regulator's proposal that once the open interest in peak futures has reached 100 MW that the Instrument would revert to using the ASX Energy peak futures value.

Aurora Energy recommends that the peak multipliers proposed by the Regulator remain in effect for the full period of the Determination. In addition, to ensure that the Instrument continues to make available contracts consistent with that available in other jurisdictions, Aurora Energy also proposes

that once the ASX Energy replacement peak product/s is finalised and sufficient open interest is evident, the Regulator shoulder re-open the Price Investigation to incorporate this into the instrument. This would include necessary adjustments to the NSLP book build methodology to ensure that it is an accurate reflection of the retail costs to hedge the mass market/NSLP profile.

Calculation of Maximum Baseload $300 Cap Contract Price

Report reference	Regulator's proposed decisions
4.2.4	The Regulator proposes that the Tasmanian baseload cap price equals the lesser of the Victorian baseload cap price and the price calculated using the current baseload cap price formula in clause 11.1 of the Instrument

As the Regulator has noted in the Draft Report, in its direct consultation as part of the Price Investigation, Aurora Energy suggested that the Victorian cap price can be used for the Tasmanian cap price due to a greater alignment between Victorian and Tasmanian prices. The Regulator has in part adopted this approach in its draft decision to adopt the lesser of the Victorian baseload cap price and the price calculated using the current baseload cap price formula in clause 11.1 of the Instrument.

Based on the proposed amendments to clause 11.1 in the Draft Report, in implementing this draft decision the Regulator has chosen to take the lesser of the two prices by choosing the lowest price by quarter. Aurora Energy supports choosing the lesser of the Victorian baseload cap price and the price calculated using the current baseload cap price formula in clause 11.1 but not in the quarterly manner proposed by the Regulator. Aurora Energy believes the proposed approach that chooses the lowest quarterly contract does not recognise the costs of peaking capacity is recovered over a full year nature that capacity costs are recovered and if implemented as proposed will result in distortionary market outcomes.

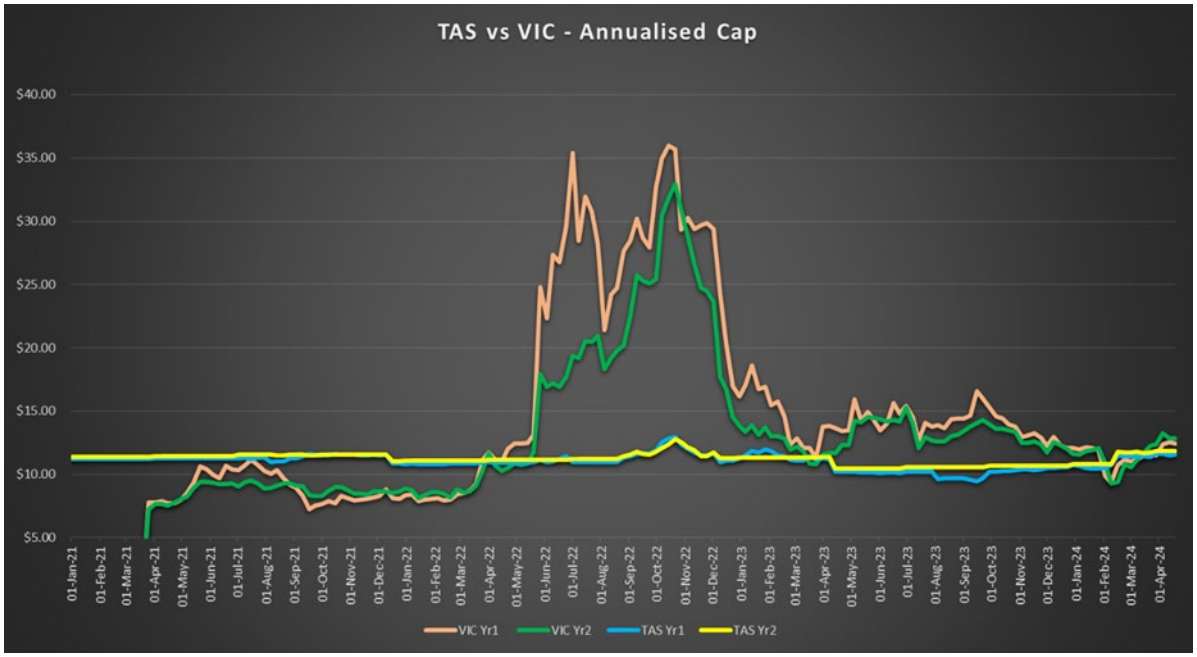
Currently in the Instrument, the Tasmanian Cap price reflects the cost of a gas fired peaking generator being built in the future with the costs of this generation discounted back to the current year. This annualised cost is then apportioned across quarters to determine the individual quarterly cap prices. This apportioning is primarily based on demand across the quarters that is invariably higher in winter quarters rather than summer given Tasmania's peak demand and, therefore, capacity risk is driven by heating demand. This results in an annualised cap costs of circa $11/MWh being recovered across each quarter's contracts at different price levels, as illustrated in Figure 4 of the Draft Report. Similarly, in Victoria, given capacity risk is primarily associated with cooling demand in summer, the annual cost of peaking capacity is recovered primarily through Quarter 1. By choosing the lowest contract between Victoria and Tasmania by quarter the differences between annual recovery of peaking costs are not recognised. This suggests that Tasmanian and Victorian contacts can be used interchangeably which is not the case given limited interconnection and variation in demand from an intraday perspective.

By choosing an approach that selectively chooses the lesser of the Tasmanian or Victorian contracts by quarter, the Regulator's draft decision reflects neither a market-based approach or a methodology based on economic principles set in the Instruments current methodology. Whilst this will produce the lowest cap contract price in Tasmania, in not fully accounting for the annualised cost recovery through contract markets of peaking generation that should occur under a market-based approach, Aurora Energy contends that resulting unintended consequences and market distortions may present a risk to retailers in managing wholesale risk effectively in Tasmania. By way of example, market participants who can access these contracts may acquire higher levels of cap contracts than they otherwise, effectively taking optimistic positions. This could also include participants buying Tasmanian contracts

under the Instrument to manage wholesale risk in other jurisdictions, should it be easier to access contract volume under the Instrument rather than through futures markets in Victoria. In turn, with the Instrument having limits on volumes of caps that must be sold by Hydro Tasmania, this may limit the volume of cap contracts available under the Instrument for retailers that genuinely need to access sufficient volume for them to manage wholesale exposure for Tasmanian customer load.

Whilst Aurora Energy does not support the draft decision on regulated cap contracts as proposed by the Regulator in its current form, Aurora Energy would be supportive of a variation to the proposed decision. Specifically, Aurora Energy proposes choosing the lesser of the Victorian baseload cap price and the price calculated using the current baseload cap price formula in clause 11.1 but do so by comparing the annualised cap price, rather than the quarterly price, and then applying the quarterly recovery profile of Tasmanian demand (as currently apples in the Instrument).

As Graph 1 below illustrates, based on analysis of annualised (Yr1: 1-4 quarters ahead, and Yr2: 5 to 8 quarters ahead) Victorian forward cap prices vs that calculated in the Instrument, Victorian cap prices have regularly been lower than the annualised value calculated in the Instrument.



Under Aurora Energy's proposed approach, when the Victorian cap contract at an annualised level is lower than the annual cap cost under the current methodology in the Instrument, the Victorian price will apply and then be profiled to Tasmanian demand across the quarters.

This outcome will:

- allow for the Tasmanian cap price to be lower than that currently calculated in the Instrument when the annualised Victorian contract cap contract falls below the derived methodology in the instrument.
- Protecting Tasmanian customers should the Victorian cap contract increase.
- Reduce unintended consequences and market distortions that exist in the Regulators current proposed decision.

This outcome would be achieved by way of the following changes to clause 11.1 of the Instrument.

$$BCV=MAX(FSF\times ABRCVFLEX+MIN(PCV,BRCVA)-ABRCVFLEX,OCV)$$

BRCVA = Weighted average Annualised Vic Cap (BRCV)

- weighted by days.
- Separate price will be calculated for each of the 2 years ahead (quarters 1 to 4 and 4 to 8)