

10 August 2017

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

Dear Mr Dimasi

Updating the Schedule 1 inputs – Consultation Paper

Thank you for the opportunity to comment on the Consultation Paper in relation to the proposed approach to updating the Schedule 1 inputs of the Wholesale Contract Regulatory Instrument.

Hydro Tasmania supports the proposed approach outlined in the Consultation Paper for updating all of the Schedule 1 inputs except for the proposed method for calculating the Off-Peak Cap Values.

The Consultation Paper proposes to continue to use the same method to calculate the “Off-Peak Reference Cap Value” and the “Off-Peak Cap Value”, which is based on historical off-peak spot prices. Hydro Tasmania believes that the value of the off-peak caps, as determined by the current methodology, do not reflect the value that market participants are prepared to pay for hedging the associated power supply risk in off-peak periods.

As outlined in the Consultation Paper, the value of the Victorian “Off-Peak Reference Cap Value” under this methodology would be \$0.002 / MWh. This valuation implies that off-peak caps are effectively “free” or that the market believes that there is no risk of price in Victoria exceeding \$300 in the off-peak periods. Hydro Tasmania believes that this valuation is inconsistent with market outcomes and does not take into account risks perceived by market participants.

As an alternative approach, Hydro Tasmania suggests that an independent broker’s market curve is used to determine off-peak values. Under this method, the off-peak cap value would match the market’s expectation of future value and reflect market participants’ willingness to pay for cap products. In implementing this approach, the following steps are proposed:

- The off-peak price should be determined as a minimum of all quarterly off-peak caps prices from the future 3year periods. This would cover all calculation periods (2 years) and the Instrument’s Schedule 1 values refreshment (1 year).
- Prior to Schedule 1 values being updated, it is proposed to use 2 weeks of data for the forward curves to determine the Victorian Off-Peak Cap price. This would enable the price of the forward curves to be averaged across a 2 week period to enable the final value to be reflective of the market over a longer period rather than reflective of a price on a particular day.
- Tasmanian Off-Peak Caps would be determined as a product between the Victorian Off-Peak Cap value (determined earlier) and the ratio between Tasmanian Flat Caps and Victorian Flat Caps time weighted values over 2 years (restricted by the Instrument’s calculation horizon).

Hydro Tasmania appreciates the consultative approach OTTER has adopted in reviewing and updating the inputs and we are happy to discuss the issues outlined in this submission further with you. Please contact John Cooper (john.cooper@hydro.com.au or (03) 6230 5313) if you have any questions or need additional information.

Yours sincerely

A handwritten signature in blue ink that reads "John Cooper". The signature is written in a cursive style with a large initial 'J' and 'C'.

John Cooper
Policy and Regulatory Analyst