



**Statement of Regulatory Intent - Wholesale Contract
Regulation**

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Office of the Tasmanian Economic Regulator

Level 5, 111 Macquarie Street, Hobart TAS 7000

GPO Box 770, Hobart TAS 7001

Phone: (03) 6166 4422 Fax (03) 6233 5666

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GLOSSARY

“**Act**” means the *Electricity Supply Industry Act 1995*.

“**Authorised Retailer**” has the same meaning as in the **Wholesale Contract Regulatory Instrument**.

“**audited wholesale pricing model**” means the model used to calculate wholesale contract prices that **Hydro Tasmania** provided to the Regulator on 20 December 2013 and as revised from time to time.

“**Compliance Enforcement Policy**” means the *Compliance Enforcement Policy, Version 1, November 2010* issued by the **Economic Regulator** and as revised from time to time.

“**Economic Regulator**” means the Tasmanian Economic Regulator established under the *Economic Regulator Act 2009*.

“**Guideline**” means the *Electricity Wholesale Contract Guideline*.

“**Hydro Tasmania**” means the Hydro-Electric Corporation (ARBN 072 377 158).

“**Regulations**” means the *Electricity Supply Industry (Pricing and Related Matters) Regulations 2013*.

“**Statement**” means this Statement of Regulatory Intent.

“**Wholesale Contract Regulatory Instrument**” means the instrument that specifies the regulated contracts **Hydro Tasmania** must offer to **Authorised Retailers**. The instrument is:

- (i) the approval made by the Minister for Finance on 29 July 2013 (as amended from time to time), in accordance with sections 43G and 43O of the *Electricity Supply Industry Act 1995* and Regulation 20 of the *Electricity Supply Industry (Pricing and Related Matters) Regulations 2013*, having taken into account the principles set out in section 43H of the *Electricity Supply Industry Act 1995*; or
- (ii) the approval made by the Regulator (as amended from time to time), in accordance with section 43G of the *Electricity Supply Industry Act 1995*, having taken into account the principles set out in section 43H of the *Electricity Supply Industry Act 1995*.

1 INTRODUCTION

1.1 Purpose

The purpose of this **Statement** is to provide clarity to stakeholders on key processes the **Economic Regulator** may undertake with respect to its administration of the electricity wholesale regulatory framework. The framework obligates **Hydro Tasmania** to calculate prices for specified financial contract products and to make weekly offers in respect of those contracts to **authorised retailers** operating in Tasmania.

This document should be read in conjunction with the *Statement of Reasons on the Statement of Regulatory Intent, Economic Regulator's Guideline*, the *Statement of Reasons on the Electricity Wholesale Contract Guideline* and the *Consultation Paper on the draft Electricity Wholesale Contract Guideline* (December 2013).

1.2 Structure

This **Statement** is structured as follows:

- Chapter 2 sets out the **Economic Regulator's** proposed criteria for deciding that **Hydro Tasmania** has failed to comply with its legislative obligations with respect to the calculation of wholesale contract prices. The Chapter also details the **Economic Regulator's** proposed process for fixing prices in these circumstances;
- Chapter 3 sets out the **Economic Regulator's** proposed criteria for deciding that a supply disruption event has occurred. The Chapter also outlines the **Economic Regulator's** proposed process for fixing prices if such an event occurs; and
- Chapter 4 discusses the proposed process for updating the inputs set out in Schedule 1 of the **Wholesale Contract Regulatory Instrument**.

2 FAILURE TO CORRECTLY APPLY APPROVED METHODOLOGY

This Chapter discusses the conditions under which the **Economic Regulator** may fix regulated wholesale contract prices if the **Economic Regulator** is satisfied that **Hydro Tasmania** has failed to correctly apply the approved methodology in calculating wholesale contract prices and one of the criteria in section 43M(1) of the **Act** has been met.

2.1 Legislative obligations and basis for stepping in

Section 43M(1) of the **Act** provides for the **Economic Regulator** to decide to approve the fixing of prices for regulated products if satisfied that there has been a significant, deliberate or repeated failure by **Hydro Tasmania** to correctly apply the approved pricing methodology.

Section 43M(1) also requires the **Economic Regulator** to advise **Hydro Tasmania** and each **authorised retailer** that retails electricity in Tasmania, when the **Economic Regulator** will approve the fixing of prices in the contracts **Hydro Tasmania** is required to offer to retailers.

Where an approval to fix prices is made under section 43M(1), section 43N(1) provides the **Economic Regulator** with the power to fix prices. In accordance with section 43N(2), the **Economic Regulator** is required to fix prices using the approved pricing methodology for those contracts.

2.2 Proposed interpretation of key terms

None of the terms significant, deliberate or repeated are defined in the **Act** or in the **Regulations** and, for the purposes of the **Statement**, the **Economic Regulator** proposes interpreting each of these terms as follows.

- (1) Significant - the prices calculated by **Hydro Tasmania** for regulated contracts differ by five per cent or more from the prices calculated by the **Economic Regulator** using the **audited wholesale pricing model**.
- (2) Deliberate - a circumstance in which the **Economic Regulator** considers, based on information it has obtained, that **Hydro Tasmania** has intentionally used a methodology to calculate prices that is inconsistent with the **Wholesale Contract Regulatory Instrument**.
- (3) Repeated - the prices calculated by **Hydro Tasmania** for regulated contracts differ by any amount from the prices calculated by the **Economic Regulator** using the **audited wholesale pricing model**:
 - on two or more occasions during any 30 day period on a rolling basis; or

- on more than six occasions during any 365 day period on a rolling basis.

Should any of these situations arise, the **Economic Regulator** would consider stepping in to fix prices and, subsequently, undertaking a compliance investigation.

2.3 Proposed process

The **Economic Regulator** intends adopting the following process in forming a view on whether there has been a significant, deliberate or repeated failure by Hydro Tasmania to correctly apply an approved methodology in the calculation of prices.

- The **Economic Regulator** would initially seek an explanation from **Hydro Tasmania** staff as to the reason for the variation. If the reason for the variation is adequately explained and justified and the problem quickly rectified, no further action would be necessary.
- If the issue is not resolved to the satisfaction of the **Economic Regulator**, the **Economic Regulator** would approve the stepping in and fixing of prices.
- The **Economic Regulator** would then notify both **Hydro Tasmania** and each **authorised retailer** that retails electricity in Tasmania of its approval to fix prices.
- The **Economic Regulator** would then calculate the prices and Hydro Tasmania would be required to sell regulated contracts in line with these prices.
- **Hydro Tasmania** would be required to post the prices determined by the **Economic Regulator** on its website.
- The **Economic Regulator** would then undertake a compliance investigation in line with its **Compliance Enforcement Policy**.
- The **Economic Regulator** would then notify **Hydro Tasmania** and each **authorised retailer** that retails electricity in Tasmania of the outcomes of its compliance investigation and direct **Hydro Tasmania** to implement the results arising from the compliance investigation.
- Once the **Economic Regulator** is satisfied that Hydro Tasmania has implemented the outcomes of the compliance investigation and is compliant with the **Wholesale Contract Regulatory Instrument**, the **Economic Regulator** would direct **Hydro Tasmania** to resume responsibility for calculating prices and would inform each **authorised retailer** that retails electricity in Tasmania of when this would occur.

Regulation 26 of the **Regulations** also allows an **authorised retailer** to apply to the **Economic Regulator** to make an approval to fix prices. If the **Economic Regulator** receives such an application, the **Economic Regulator** is required to conduct a compliance investigation before considering whether to make an approval under section 43M(1) of the **Act** to fix prices. Upon receipt of such an application, the

Economic Regulator is also required to follow the investigation, notification and reporting requirements set out in Regulations 26, 27, 28 and 29.

2.4 How will prices be set if Hydro Tasmania fails to correctly apply the approved methodology?

As noted in section 2.1, if the **Economic Regulator** declares that there has been a significant, deliberate or repeated failure by **Hydro Tasmania** to correctly apply the approved pricing methodology and the **Economic Regulator** chooses to fix prices in respect of regulated contracts, the calculation of these prices must be in accordance with the approved pricing methodology. The approved methodology is outlined in the **Wholesale Contract Regulatory Instrument**. As such, the **Economic Regulator** would fix prices by carrying out the relevant calculations using the copy of the **audited wholesale pricing model Hydro Tasmania** has provided to the **Economic Regulator**. **Hydro Tasmania** will need to provide any data which it creates as input to the model to the **Economic Regulator**.

3 SUPPLY DISRUPTION EVENT

This Chapter discusses the proposed process under which the **Economic Regulator** may fix regulated wholesale contract prices when, in the **Economic Regulator's** opinion, a supply disruption event has occurred.

3.1 Legislative obligations and basis for stepping in

Sections 43M(2) of the **Act** provides for the **Economic Regulator** to step in and fix prices where there has been a 'supply disruption event'. The **Economic Regulator** must consult with the Treasurer before invoking this clause.

Section 43M(3) of the Act defines a supply disruption event as:

“...an event (other than a drought) that, in the opinion of the Regulator, is likely to cause a prolonged interruption to a substantial quantity of the electricity that would otherwise be supplied under normal circumstances by Hydro”.

The definition of a supply disruption event excludes a drought in Tasmania as this is considered to be a normal commercial risk for **Hydro Tasmania** that will be reflected in the methodology for pricing the approved contracts.

Sections 43N(3) and (4) provides that, where the **Economic Regulator** is to fix prices in response to a supply disruption event, the **Economic Regulator** does not have to use the approved pricing methodology in calculating prices for the affected contracts. This is because a supply disruption event is likely to render the approved pricing methodology invalid.

3.2 Forming a view on the impact of a supply disruption event

Whilst a supply disruption event is defined in section 43M(3) of the **Act**, the **Economic Regulator** is required to form a view on whether the event has caused a *prolonged interruption to a substantial quantity* of the electricity normally supplied by **Hydro Tasmania**.

In forming this view, the **Economic Regulator** proposes that it will consider:

- estimates of the impact on generation capacity relative to the total generation capacity at the time of the disruption (including seasonality impacts) and likely demand;
- the likely duration of the disruption; and
- any other matters that the **Economic Regulator** deems relevant.

3.3 Proposed process

The **Economic Regulator** intends adopting the following process if the **Economic Regulator** considers that a supply disruption event has occurred.

- The **Economic Regulator** would **review information provided by Hydro Tasmania**, authorised retailers and other market participants.
- The **Economic Regulator** would initially review the circumstances to consider whether the event met the Regulator's criteria for a supply disruption event as soon as reasonable practicable.
- If the **Economic Regulator** considered the event was a supply disruption event the **Economic Regulator** would consult with the Treasurer on the nature of the event and the proposed actions to be taken.
- Following consultation with the Treasurer, the **Economic Regulator** would notify **Hydro Tasmania** and all **authorised retailers** operating in Tasmania that the Regulator had declared the event to be a supply disruption event and the **Economic Regulator** intends fixing prices.
- The **Economic Regulator** would instruct Hydro Tasmania to set all regulated contracts prices at \$300.
- **Hydro Tasmania** would be expected to continue to offer contract volumes consistent with the **Wholesale Contract Regulatory Instrument**
- The **Economic Regulator** would then conduct an investigation to consider:
 - the nature of the event and its impact on the market;
 - the likely timeframe for the impact of the event to remain;
 - whether a different pricing methodology is more appropriate than the resumption of the original methodology from the audited pricing model; and
 - if a different methodology is required, develop and implement that methodology as soon as is reasonably practicable.
- If the **Economic Regulator** determined that a different methodology was more appropriate it would advise **Hydro Tasmania** that it is required to adopt that methodology going forward.
- **Hydro Tasmania** would be expected to provide catch up volumes consistent with the principles outlines in clause 26 of the **Wholesale Contract Regulatory Instrument** and for all volumes not sold when the price was set at \$300.

Depending on the nature of the cause of the disruption event, the **Economic Regulator** may suggest that the Government consider introducing new legislative or regulatory requirements to put the **Economic Regulator's** methodology into law or to implement a new methodology as it saw fit.

4 PROCESS FOR UPDATING INPUTS

This Chapter discusses the proposed process under which the **Economic Regulator** may update the inputs contained in Schedule 1 of the **Wholesale Contract Regulatory Instrument**.

4.1 Background

The **Economic Regulator** is responsible for the inputs in Schedule 1 of the **Wholesale Contract Regulatory Instrument** which are key inputs into the regulated wholesale pricing framework. The following section outlines the considerations and process the **Economic Regulator** intends following in updating those inputs.

4.2 Basis for updating the values

The **Economic Regulator** may consider updating the inputs in Schedule 1 of the **Wholesale Contract Regulatory Instrument** as a result of one or more of the following actions:

- the **Economic Regulator** itself may initiate a review of the inputs;
- **Hydro Tasmania** may approach the **Economic Regulator** to initiate a review; or
- **authorised retailers** or other stakeholders may approach the **Economic Regulator** to initiate a review.

4.3 Proposed process

In updating the inputs, the **Economic Regulator** intends adopting the following process:

- assess the proposal for the update and decide whether or not an update is appropriate;
- publicly consult on the nature of any changes on the **Economic Regulator's** proposed changes; and
- if the **Economic Regulator** decides to update the inputs it will notify both **Hydro Tasmania** and **authorised retailers** operating in Tasmania of the nature and timing of the update.

The **Economic Regulator** would, whenever practicable, undertake consultation with **Hydro Tasmania** and **authorised retailers** in relation to any proposal to update values under the **Wholesale Contract Regulatory Instrument** prior to doing so. However, there may be situations where there is a requirement to rectify an issue

with the values in a more timely manner such that the opportunity to consult with stakeholders may be limited. However, in these limited instances, stakeholders could request a further review of the inputs after the values have been updated.