

21 December 2018

Dr Kerry Schott AO
Energy Security Board
By email: info@esb.org.au

Dear ESB,

Consultation on Retailer Reliability Obligation Detailed Design Issues

Thank you for the opportunity to comment on the consultation papers released on 5 December. Hydro Tasmania has specific responses to the three papers (Material Reliability Gap Definition, Firmness Principles and Response to Compliance) as provided in Attachment A.

Please contact Colin Wain (03 8612 6443, colin.wain@hydro.com.au) to discuss any aspects of this submission.

Yours sincerely



Colin Wain
Policy Development Manager

Attachment A – Hydro Tasmania Responses to Consultation Papers

Paper 1 - Material Reliability Gap Definition and Communication

- **We agree that the basis of the materiality test at T-3 and T-1 should be the same.** This is consistent with a binary approach - either there is expected to be a reliability issue or there is not.
 - To underpin this, it is **critical that the forecasting used for the T-3 determination examines a full range of scenarios including sensitivities around plant exit, demand and supply changes.** This is needed to ensure that the metric used to assess T-3 is robust to changes in supply/demand conditions and adequately informs market participants as to the risks of reliability issues.

- Hydro Tasmania believes that **Metric A (Annual regional expected USE exceeds the reliability standard) is the most appropriate test at this time.**
 - As the paper states, the expected USE methodology *“is well understood by industry, [and] such an approach should provide a relatively predictable basis for materiality assessments”*.
 - Metric B may be attractive to some industry participants as it provides a buffer against the RRO being triggered. However, Hydro Tasmania’s expectation is that if the forecast USE is above the reliability standard but by less than this ‘buffer’, then AEMO would likely move to procure resources through the RERT to address this. On this basis, retailers (and subsequently energy users) would still face additional costs.
 - Metrics A & B must be considered alongside AER’s discretion to not trigger the RRO in certain circumstances. By assessing potential RRO costs against expected RERT costs, the AER should have the information needed to balance costs and act in the interests of consumers (consistent with the NEO).
 - Alternative approaches such as C and D may reflect public understanding of reliability issues but they do not have a strong economic rationale or clear market benefits – which should be the basis for regulatory interventions.

- **The AER should have discretion in deciding whether to issue a reliability instrument.**
 - **We support the publishing of guidelines around this AER discretion.**
 - AER’s decision must balance costs against longer-term goals. While single year intervention via RERT may be least-cost in the short term, it will not be of benefit if it obscures investment signals for flexible, reliable energy resources.

Paper 2 - Firmness Principles for Qualifying Contracts

- Hydro Tasmania supports the context and discussion provided in the paper. **The four high-level principles for firmness adjustment are appropriate:**
 1. The strike price of the contract;
 2. The variability and profile of the volume settled under the contract;
 3. The likelihood of the contract providing cover to the buyer during the reliability gap; and
 4. Any other contractual terms which limit the coverage or otherwise reduce the incentive for a seller to “defend” the position.

- We agree that **additional material will need to be developed by the AER to provide further guidance on how these principles will apply**. Hydro Tasmania would welcome the opportunity for further consultation on this issue.

- Of key importance will be **the treatment of short-duration energy resources and the firmness attributed to these arrangements**. This may include for example, demand response and shallow energy storage which may be able to contribute an hour or two of response but would not be firm beyond this point. As Hydro Tasmania stated in our March submission on the NEG Design paper, for *“the Guarantee to provide an efficient transition to a portfolio of future energy resources, it must recognise and take into account the characteristics of energy technologies”*. We understand that this would be captured by principle 3 (above).

Paper 3 - Compliance / Procurer of Last Resort Cost Recovery

- It is **essential that liable entities understand their potential exposure to compliance penalties ahead of time** and can undertake risk assessment and planning. This has the greatest chance of encouraging compliance.
- Charges for non-compliance will be **most appropriate if they provide a clear incentive for future compliance and the longer-term aims of the RRO**, which is to ensure and encourage sufficient dispatchable energy resources to meet reliability standards.
- Of the options put forward to calculate the compliance shortfall, there appears to be merit in Option 2. *“Average Shortfall across the gap”*.
 - o Given the highly technical nature of this paper and the compliance payment options, we believe there would be benefit from further consultation with industry stakeholders in early 2019.