

28 February 2022

Ms Emily Baker
Investigative Reporter
ABC Hobart
1-7 Liverpool Street
Hobart TAS 7000

By Email: Baker.Emily@abc.net.au

Dear Ms Baker,

Right to Information Request – 27 January 2022

I refer to your request pursuant to the *Right to Information Act 2009* (“RTI Act”) made on 27 January 2022.

I am authorised to make decisions on behalf of Hydro Tasmania in respect of applications for information under the RTI Act.

1. Your Request

Your request sought the following information:

1. *Reports and briefing related to the Energy Trading Strategy Incident of July 2020;*
2. *A copy of the Energy Trading Incident investigation;*
3. *KPMG external audit of August 2020.*

It will be collectively referred to in the body of this letter as ‘the Request’.

You indicated in the Request that you did not require the inclusion of the names of non-executive level employees.

2. Determination and Reasons for Determination of Request

- 2.1. I have determined that Item 2 of the Request is refused due to exemption under section 35(1)(a) and (b) of the RTI Act. The investigation report consists of opinions and recommendations prepared by an officer of Hydro Tasmania and records of consultations between officers of Hydro Tasmania in connection with Hydro Tasmania’s official business in the course of a compliance incident investigation. Section 35 is subject to the public interest test and in reaching this decision I have had regard to the matters specified in Schedule 1, particularly (n) and (o).

- 2.2. A document responsive to Item 1 of the Request has been refused for the same reasons covered in paragraph 2.1.
- 2.3. I have determined that Item 3 of the Request is refused due to exemption under sections 38(a)(ii) and 39(1)(b) of the RTI Act. The report details aspects of Hydro Tasmania’s business operations which could expose Hydro Tasmania to competitive disadvantage and increased risk of fraudulent activity if disclosed. Furthermore, the report was provided to Hydro Tasmania by KPMG on behalf of the Auditor-General. The ability of the Auditor-General to provide impartial and independent scrutiny of State entities relies on frank and open communication between those entities and the Auditor-General and is a process undertaken in strict confidence. Sections 38 and 39 are both subject to the public interest test and in reaching this decision I have had regard to the matters specified in Schedule 1, particularly (n), (o) and (s).
- 2.4. In relation to the balance of the Request, I have undertaken a search of the information held by Hydro Tasmania and its subsidiaries to locate any records that may be relevant to the Request and have determined that the information which can be released to you is as follows:

Document	Section of the Request	Released
Trading Position Forecast Outcomes – 19 May 2020	1	Substantially in full, minor redactions by agreement
Board Paper – 20 May 2020	1	Substantially in full, minor redactions by agreement
Board Paper – 9 June 2020	1	Substantially in full, minor redactions by agreement
Board Paper – 24 June 2020	1	In full

3. Review of Rights

You are entitled under section 43 of the RTI Act to apply for a review of the decision made under Part 2.

Any request for such a review should be made in writing within twenty (20) working days of receiving this letter and addressed to:

Mr Ian Brooksbank
Acting Chief Executive Officer
Hydro Tasmania
4 Elizabeth Street
Hobart TAS 7000

Should you have any further questions on the information provided please contact the undersigned.

This request is now considered closed.

Yours sincerely,

Laura Harle
Legal Counsel
t 6240 2813
e laura.harle@hydro.com.au

Annexure 1

Right to Information Act 2009 (Tas) – ss 35, 38 and 39

35. Internal deliberative information

- (1) Information is exempt information if it consists of –
 - (a) an opinion, advice or recommendation prepared by an officer of a public authority; or
 - (b) a record of consultations or deliberations between officers of public authorities; or
 - (c) a record of consultations or deliberations between officers of public authorities and Ministers –
- (2) in the course of, or for the purpose of, the deliberative processes related to the official business of a public authority, of a Minister or of the Government.
- (3) Subsection (1) does not include purely factual information.
- (4) Subsection (1) does not include –
 - (a) a final decision, order or ruling given in the exercise of an adjudicative function; or
 - (b) a reason which explains such a decision, order or ruling.
- (5) Subsection (1) ceases to apply after 10 years from the date of the creation of the information referred to in that subsection.

38. Information relating to business affairs of public authority

Information is exempt information –

- (a) if it is –
 - i. a trade secret of a public authority; or
 - ii. in the case of a public authority engaged in trade or commerce, information of a business, commercial or financial nature that would, if disclosed under this Act, be likely to expose the public authority to competitive disadvantage; or
- (b) if it consists of the result of scientific or technical research undertaken by or on behalf of a public authority, and –
 - i. the research could lead to a patentable invention; or
 - ii. (ii) the disclosure of the results in an incomplete state would be likely to expose a business, commercial or financial undertaking unreasonably to disadvantage; or
 - iii. the disclosure of the results before the completion of the research would be likely to expose the public authority or the person carrying out the research unreasonably to disadvantage; or
- (c) if it is contained in –
 - i. an examination, a submission by a student in respect of an examination, an examiner's report or any such similar record; and
 - ii. the use for which the record was prepared has not been completed.

39. Information obtained in confidence

- (1) Information is exempt information if its disclosure under this Act would divulge information communicated in confidence by or on behalf of a person or government to a public authority or Minister, and –
 - (a) the information would be exempt information if it were generated by a public authority or Minister; or

- (b) the disclosure of the information would be reasonably likely to impair the ability of a public authority or Minister to obtain similar information in the future.
- (2) Subsection (1) does not include information that –
- (a) was acquired by a public authority or a Minister from a business, commercial or financial undertaking; and
 - (b) relates to trade secrets or other matters of a business, commercial or financial nature; and
 - (c) was provided to a public authority or Minister pursuant to a requirement of any law.

Internal memo

Private and confidential

To:	Ian Brooksbank		
From:	[REDACTED]	Ext no:	0450 923 458
cc:	[REDACTED]; [REDACTED]		
Date:	19 May 2020	Pages:	2 (includes cover sheet)
Subject:	For Information		
Status:	For Noting		

Background

This year the construction of the Corporate Plan has been through a number of iterations. During one of these iterations, it was noted that a market position had moved to an out of the money position. A meeting was held to review the iteration with the Finance Teams, CFO and CEO where this position was bought to light.

Data

The net trading margin tables were provided in a CEO review meeting (24th April) of the projections update for the April Board meeting (29th April). These updates incorporated a significant drop in forward market price curves, which results in numerous changes in value.

One particular line was singled out and it was questioned why Hydro had a bought position in that period (financial year 2022), position highlighted below:

Victorian Positions (\$m)	FY 21	FY22	FY23	FY24
Swaps	(23)	(18)	(6)	-
Retail	4531	2	-	-
Retail Volatility	(7)	(6)	(4)	(4)
Cap	(1)	1	-	-
Other	(7)	(1)	-	-
Total Position (excl physical)	76	(23)	(12)	(4)

The above table does not account for Basslink flows or physical Victorian generation.

In the prior iteration of the Corporate Plan, this purchase position had been a positive \$2m forecast value. Market movements since that time had resulted a significant change in value for those bought positions, without a corresponding increase in value of a sold position to Momentum (as seen in the prior year).

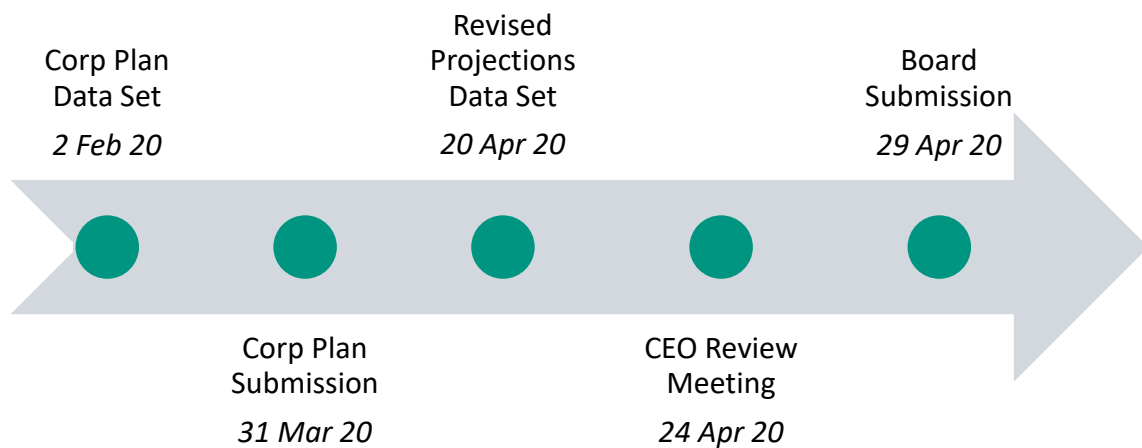
This is due to the forecast assuming that market price curves are used to determine transfer pricing on uncontracted Momentum retail loads for beyond the budget year (financial year 2020/21).

The change in forward prices also resulted in substantial changes for the cost of imports, the value received on exports and the value of uncontracted Tasmanian customers. There were also impacts to non-Victorian states, especially where market transfer prices are assumed on new retail load.

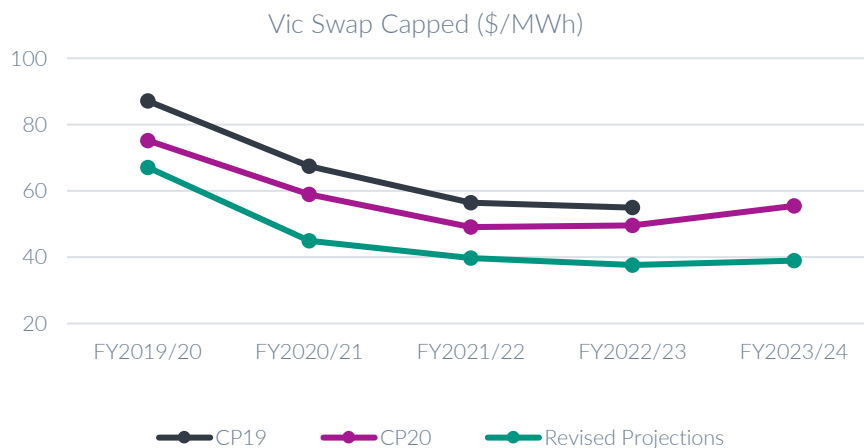
Preparation of Data

The forecast model utilises Allegro and Datamart systems to undertake MTM calculations. The calculated monthly CFD’s utilised the market price curve as prepared by Hydro’s Front Office. For the calculation of the FYE2022 forward curve, a manual adjustment of an additional \$5/MWh was added to the flat swap prices, as a managerial decision to reflect a moderate correction of market sentiment.

Corporate Plan Timeline and Major Review History



Forward Curves as at Data Set:



Hydro-Electric Corporation Board paper

Special Board Meeting date: Wednesday, 20 May 2020

STRICTLY CONFIDENTIAL

Agenda item: 1

Subject:	ENERGY TRADING INCIDENT
Sponsor:	Stephen Davy, Chief Executive Officer
Category:	For noting
Draft resolution:	The Board notes the status of the investigation into a recently understood energy trading incident.

EXECUTIVE SUMMARY

This paper has been prepared to inform the Board of an incident identified in relation to our FY2021/22 contract position. Trading activity undertaken mostly throughout CY2019 has resulted in a negative mark-to-market position and hence negative financial impacts in FY2021/22 and potentially a much smaller negative impact in FY2022/23 as a result of the significant drop in forward market prices. Preliminary analysis indicates a negative impact of \$15m to \$20m in FY2021/22, depending on assumptions made of when the C&I load sold for that year should have been bought back from the market.

An investigation utilising external expertise coordinated through Internal Audit has been initiated to identify the factors that contributed to the incident, as well as corrective and preventative actions. Initial observations from that investigation should be available at the 27 May 2020 Board meeting.

BACKGROUND

Hydro Tasmania's Energy Trading Policy requires the Risk Management Committee (RMC) and the Board to endorse the Trading Strategy on an annual basis. The obligation derives from the Treasurer's Instruction on Energy Trading Risk Management.

The Trading Strategy outlines how we intend to utilise our generation assets, wholesale contracting, gas portfolio and LGC portfolio to support our strategy to grow retail sales, support Battery of the Nation and lead Australia's energy transition, while delivering optimal returns to our shareholders. The Trading Strategy is focussed on delivering to budget and corporate plan targets in Horizon 1 (ie a 1-3 year trading plan) but also looks

ahead to ensure we are positioned to support the longer term strategic objectives of the Hydro Group.

Specifically, the Strategy states that a progressive hedging strategy will be in place for the initial 3 year horizon to ensure that a large market shift (up/down) will be mitigated by averaging out the impact over time for both our retail and physical exposures.

Throughout CY2019 it appears that we purchased mainland energy hedges to back retail sales at higher volumes than required to hedge the price risk arising from committed retail sales, and out of sync with the setting of prices for our contracted customer load.

ANALYSIS

During Corporate Plan reforecasting in late April a significant mark-to-market loss was identified in the FY2021/22 VIC contract position as a result of a trading strategy undertaken during CY2019. Following a meeting of the FMC on 12 May 2020 a compliance incident was logged and Internal Audit were requested to undertake an investigation into the incident.

██████████, Head of Group Compliance has been nominated as the Investigation Lead with ██████████, Head of Internal Audit actively managing the investigation. Kate McKenzie, Chief Governance Officer, is providing oversight. PwC has been engaged to lead core investigation activities co-ordinated by Iain Semple, Partner.

No decision will be made regarding whether an investigation into the conduct of any one or more employees is warranted until the incident investigation is complete and facts are clear.

The scope of the current investigation includes:

- Trading activities undertaken within Wholesale Energy Services / Commercial during the relevant period;
- Position and risk monitoring by Middle Office / Commercial Risk; and
- Performance reporting by Finance.

The core questions that the investigation seeks to answer include:

- Was the Energy Trading Policy and Trading Strategy at that time appropriately understood by front office and middle office personnel?
- What was the rationale for the executed trades?
- Were all trading activities conducted within trading policy limits and delegations?
- What measures were in place at the time to review trading activity?
- Were the risk monitoring measures undertaken during the trading period?
- What performance reporting was undertaken over the trading activity?

The proposed deliverable is a report of factual findings that identify the factors that contributed to the incident as well as preventative actions.

Preliminary analysis suggests that this trading incident is likely to impact earnings forecasts by approximately \$15m to \$20m in FY2021/22, depending on assumptions made of when the C&I load sold for that year should have been bought back from the market.

At this point the investigation has not been tasked with providing advice on how to manage or remediate the trading position or to undertake a detailed assessment of trading performance or current risk monitoring tools and processes.

A further update on the status of the investigation will be provided to the Board at the Corporation Board meeting on Wednesday 27 May 2020. The investigation is scheduled to produce a draft investigation report by 26 May 2020.

The Chief Commercial Officer has imposed a moratorium on all electricity contract trading outside our obligations to offer Tasmanian contracts and fulfil C&I customer requests. Any trading activity required to remain in limits or address known exposures will require approval by the Chief Commercial Officer prior to execution while the investigation is on foot and until satisfactory preventative measures have been implemented.

RECOMMENDATION

It is recommended the Board notes the trading incident and the status of the investigation.

Management responsibility

Stephen Davy, Chief Executive Officer

Hydro-Electric Corporation Board paper

HEC Board Briefing Paper: Tuesday, 9 June 2020

STRICTLY CONFIDENTIAL

Item: 1

Subject:	UPDATE ON ACTIONS IN RESPONSE TO THE ENERGY TRADING INCIDENT
Sponsor:	Ian Brooksbank, Chief Financial Officer Caroline Wykamp, Chief Commercial Officer
Category:	For noting
Draft resolution:	The Board <u>notes</u> the progress made.

EXECUTIVE SUMMARY

This paper provides the Board with a progress update on immediate actions taken and planned following on from the FY2021/22 Energy Trading Incident. In summary the Front Office has:

- Commenced extending SMILES to cover the period to FY2023/24,
- Improved load forecasting processes,
- Implemented written trading plans, and
- Progressed risk appetite work.

The Back and Middle offices have put in place interim reporting measures focused on the trading position and on the Mark to Market value of the position.

Organisational structure and resourcing is being developed taking into account the reviews being conducted by PwC triggered by the FY2022 wholesale position, the recently completed PwC Internal Audit of “Wholesale Credit Management” and a “Hydro Tasmania Middle Office Review” conducted by PwC published in December 2018.

These initial actions are in addition to any actions that are recommended following completion of PwC’s investigation.

BACKGROUND

At the May 2020 Hydro Corporation Board Meeting the FY2021/22 hedge position was discussed highlighting that the Corporation has entered into a bought position in excess of the contracted retail sales position and that the forward price curve had dropped resulting in a Mark to Market loss. Preliminary analysis suggests that this trading incident is likely to impact earnings forecasts by approximately \$15m to \$20m across the four year planning period with the bulk of the negative impact occurring in FY2021/22, depending on assumptions made of when retail load sold for that year and the years either side should have been bought back from the market.

The Board is actively monitoring the investigation by Internal Audit and PwC, and requested that Management take some immediate actions to the next Board meeting.

ACTIONS TAKEN

Back and Middle Office

In parallel with the investigation by PwC, Management has developed a plan that outlines the changes that will be implemented prior to the next Board meeting. In particular,

1. changes to reporting, and
2. changes in Back and Middle Office processes

What changes to reporting are proposed?

The reporting changes proposed (in the timeframe available) will be spreadsheet based with a view to operationalising in the medium term. The changes are on two fronts, firstly Position Reporting by State and year and secondly, mark to market valuation of the wholesale and retail books by state and by year. It should be noted that the spreadsheet report is an interim solution in the interests of time. Once developed the reporting will be migrated to a non-spreadsheet production environment.

These new reports will be provided to the Board at the June 24th, 2020 meeting via the Financial Management Committee.

What changes [are] being made in Back and Middle Office processes?

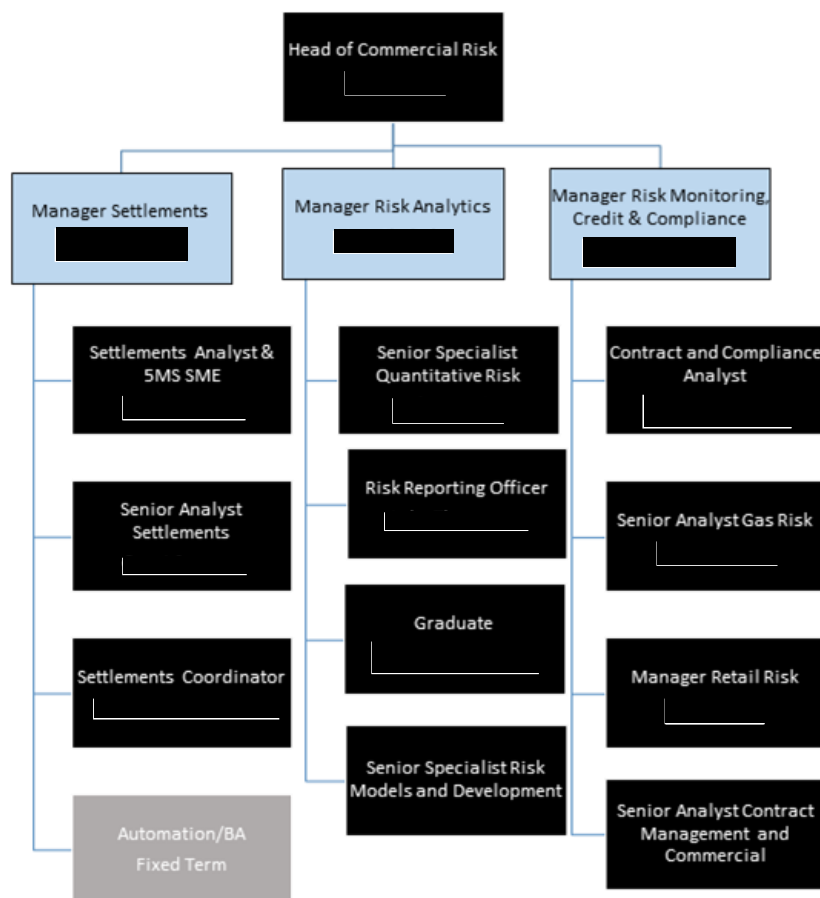
There is currently a review of the Back and Middle offices being conducted by PwC triggered by the FY2021/22 wholesale position. This review will inform the changes necessary to improve processes, reporting and oversight. Further, there is also a recently completed PwC Internal Audit of “Wholesale Credit Management” and a “Hydro Tasmania Middle Office Review” conducted by PwC published in December 2018.

Management proposes to use the content of the three reports/reviews mentioned above to shape the changes to the Back and Middle office processes. It is envisaged that these changes will clarify at a very minimum:

- What accountabilities sit within the two offices,
- Segregation of duties both within the two offices and with the Front Office,
- What is the optimal structure and people capability needed to meet the accountabilities identified,
- What systems and processes are needed to deliver the accountabilities,
- What reporting is appropriate?

In the immediate term, the Middle office is developing a spreadsheet based reporting tool to deliver improved/additional reporting. Management envisages putting structure and process recommendations to the September RMC and Board for endorsement.

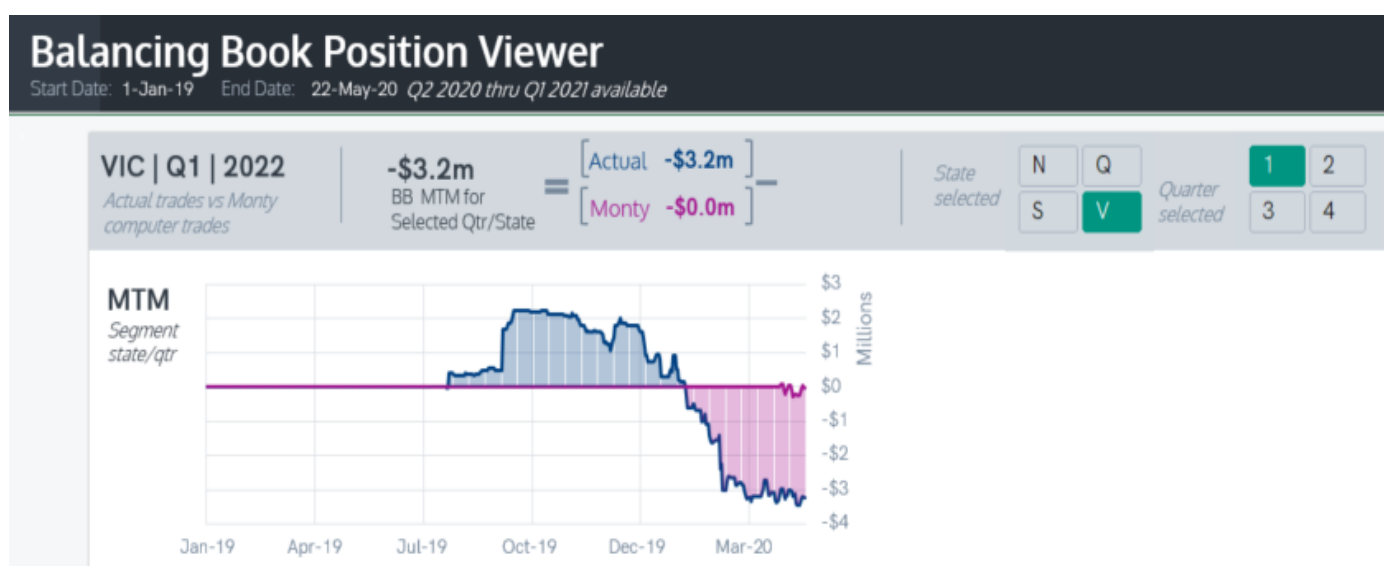
It should also be noted that in late April 2020, after a review by the Commercial Risk manager, the Commercial Risk team was restructured, see below. This restructure allows for closer management of the three core functions of Commercial Risk as the previous structure had all members reporting to a single Manager.



Front Office

As previously advised, all discretionary trading has been suspended as an interim measure, with all trades being approved by the Chief Commercial Officer. Front Office have also been progressing the smiles and performance reporting as part of the recommendations from the PwC Middle Office review Dec 2018. We are working on extending the smiles framework and balancing book reports out to FY2023/24. We are also progressing with moving reporting from excel to an enterprise application with the support of IS&S. The original plan was to move from the position and performance excel prototypes to enterprise application once satisfied with the prototypes and we are in line with our original plan.

1.3 Example of Balancing Book view of mark-to-market position for Q1 Vic 2022



Other Front Office activities

The wholesale portfolio team are continuing on:

- improving the load forecast for mass-market load in position report highlighting the price exposed load out for the trading term
- refreshing the electricity hedging strategy, with endorsement from the FMC ensuring the trading team are aligned with the strategy
- establishing monthly written trading plans with documented lookback on performance
- obtaining approval for any trading activity by the Chief Commercial Officer as per the monthly trading plan until the Chief Commercial Officer is satisfied to hand over to the Head of Wholesale Portfolio
- progressing the commercial financial risk appetite framework which underpins the limits and approaches to short and long term hedging strategies

RESTRICTED DOCUMENT

- In line with the risk appetite, establish our long-term Tasmanian generation position hedging strategy and include in our trading books and smiles framework

RECOMMENDATION

The Board notes the progress made on actions taken to understand and manage the FY2021/22 Trading incident and on the actions taken to improve process.

Submitted by: Caroline Wykamp – Chief Commercial Officer
Ian Brooksbank – Chief Financial Officer

Prepared by: Caroline Wykamp – Chief Commercial Officer
Ian Brooksbank – Chief Financial Officer

Hydro-Electric Corporation Board paper

HEC Board Briefing Paper: Wednesday, 24 June 2020

STRICTLY CONFIDENTIAL

Item: 6.6

Subject:	UPDATE ON ACTIONS IN RESPONSE TO THE ENERGY TRADING INCIDENT
Sponsor:	Ian Brooksbank, Chief Financial Officer Caroline Wykamp, Chief Commercial Officer
Category:	For noting
Draft resolution:	The Board <u>notes</u> the progress made.

EXECUTIVE SUMMARY

This paper provides the Board with a progress update on further actions taken and planned following on from the FY2021/22 Energy Trading Incident.

The Back and Middle offices have put in place interim reporting measures focused on the trading position and on the Mark to Market value of the position.

Organisational structure and resourcing assessment is ongoing and will take into account the reviews being conducted by PwC triggered by the FY2021/22 wholesale position, the recently completed PwC Internal Audit of “Wholesale Credit Management” and a “Hydro Tasmania Middle Office Review” conducted by PwC published in December 2018.

These actions are in addition to any actions that are recommended following completion of PwC’s investigation.

BACKGROUND

At the May 2020 Hydro Corporation Board Meeting the FY2021/22 hedge position was discussed, highlighting that the Corporation has entered into a bought position in excess of the contracted retail sales position and that the forward price curve had dropped resulting in a Mark to Market [**MtM**] loss. Preliminary analysis suggests that this trading incident is likely to impact earnings forecasts by approximately \$15m to \$20m across the four year planning period with the bulk of the negative impact occurring in FY2021/22, depending on

assumptions made of when retail load sold for that year and the years either side should have been bought back from the market.

The Board is actively monitoring the investigation by Internal Audit and PwC, and requested that Management take some immediate actions to the next Board meeting. These immediate actions were reported to the Board in a paper dated 9 June 2020. This paper outlines progress made on interim Mark to Market and Position Reporting completed since that update.

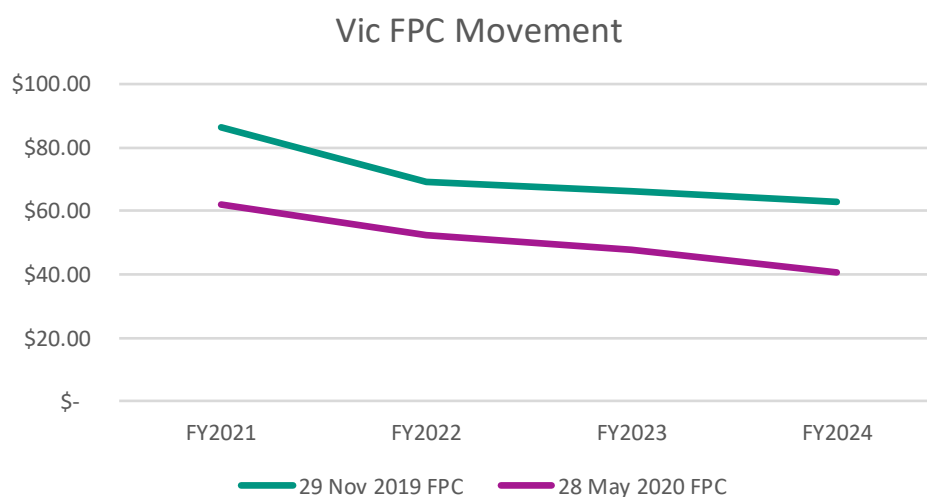
The Middle Office has developed an interim, excel based model for Mark to Market and Position Reporting and the output from this model is discussed below. It is management's intention to migrate the analysis and reporting to an enterprise solution which will include SMILES, Monty and the Balancing Book (MtM, Position) once the logic and structure of the reporting is agreed.

MARK TO MARKET REPORTING

Mark to Market is calculated for Victoria by financial year capturing the MtM value of both the wholesale and retail positions is presented in the table below. Due to the progressive hedging approach that was undertaken prior to the Victorian Default Offer being in place, hedges for FY2021 were purchased earlier, when the market was lower resulting in a positive \$22.5m MTM in November 2019. As retail sales grew in early 2020, this length reduced. These sales were made at slightly higher levels than the purchased price, resulting in a positive \$5.1m MTM at the end of May 2020.

1.1 Previous MTM		29/11/19 FPC				
Region	Instrument	FY2021	FY2022	FY2023	FY2024	Total
VIC	Swaps	\$19.1 M	-\$1.2 M	-\$2.4 M		\$15.5 M
	Other trades	\$3.9 M	\$1.1 M	\$0.0 M		\$5.0 M
	C&I contracted	-\$0.3 M	\$3.2 M	\$1.7 M	\$0.2 M	\$4.8 M
	MM fixed price	-\$0.2 M	\$1.4 M			\$1.2 M
VIC - Total		\$22.5 M	\$4.5 M	-\$0.8 M	\$0.2 M	\$26.5 M
1.2 Current MTM		28/5/20 FPC				
Region	Instrument	FY2021	FY2022	FY2023	FY2024	Total
VIC	Swaps	-\$22.5 M	-\$22.9 M	-\$9.3 M	-\$0.0 M	-\$54.8 M
	Other trades	-\$3.4 M	\$0.3 M	-\$0.3 M	-\$0.1 M	-\$3.5 M
	C&I contracted	\$13.5 M	\$10.8 M	\$6.2 M	\$2.1 M	\$32.7 M
	MM fixed price	\$17.5 M	\$1.8 M			\$19.3 M
VIC - Total		\$5.1 M	-\$10.0 M	-\$3.4 M	\$2.0 M	-\$6.4 M
	Total Change	-\$17.5 M	-\$14.5 M	-\$2.6 M	\$1.7 M	-\$32.9 M

The MtM value of the long position changed from November 2019 to May 2020 as detailed in the table above. The vast majority of the change was driven by the fall in the Forward Price Curve (FPC) which bottomed late April 2020, see graph and table below.



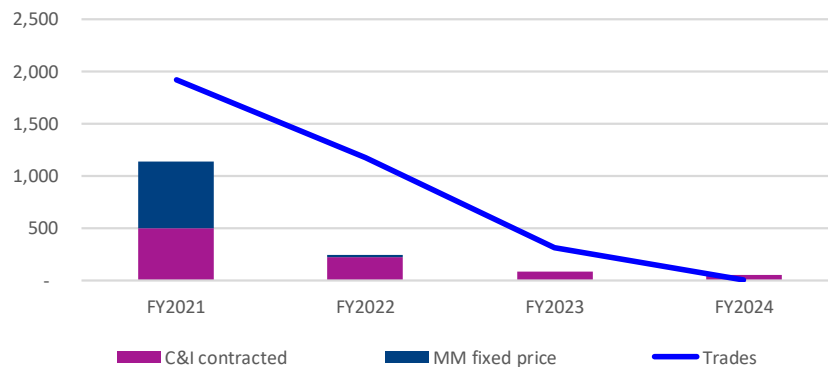
Region	\$/MWh	FY2021	FY2022	FY2023	FY2024
VIC	29 Nov 2019 FPC	\$86.23	\$69.14	\$66.31	\$63.02
	28 May 2020 FPC	\$62.06	\$52.30	\$47.99	\$40.76
	FPC Change	-\$24.17	-\$16.84	-\$18.32	-\$22.26

Note, due to the complexity of the calculation and the need for independent review, the analysis has been limited to the Victorian region recognising this region has the biggest load and MtM value. The remaining regions will be included once the Victorian model outputs are validated internally and by PwC as part of their review.

POSITION REPORTING

As previously discussed, trading in the period February 2019 to November 2019 resulted in a long mainland position which is most evident in Victoria given Momentum's load profile. The graph below depicts the Victorian position by financial year. The gap between the top of the bars and the trades blue line represents the overbought position.

Vic Position Nov 2019



FRONT OFFICE

We have draft balancing book reports out to FY2023/24. Middle office will review the balancing book mark-to-market calculations and circulate to the Board during July.

If we had the balancing book mark-to market positions available in January 2020 for FY2021/22, we would have been alerted to the long position and the mark-to-market change. The charts below show our bought contracts for Victoria CYQ1 2022. This shows the growing peak and off-peak contracts from July 2019 and our mark-to-market position moving negative from January 2020.



The wholesale portfolio team are still continuing on:

- improving the load forecast for mass-market load in position report highlighting the price exposed load out for the trading term
- refreshing the electricity hedging strategy, with endorsement from the FMC ensuring the trading team are aligned with the strategy

- establishing monthly written trading plans with documented lookback on performance
- obtaining approval for any trading activity by the Chief Commercial Officer as per the monthly trading plan until the Chief Commercial Officer is satisfied to hand over to the Head of Wholesale Portfolio
- progressing the commercial financial risk appetite framework which underpins the limits and approaches to short and long term hedging strategies
- In line with the risk appetite, establish our long-term Tasmanian generation position hedging strategy and include in our trading books and smiles framework

RECOMMENDATION

The Board notes the progress made on actions taken to understand and manage the FY2021/22 Trading incident and on the actions taken to improve process.

Submitted by: Caroline Wykamp – Chief Commercial Officer
Ian Brooksbank – Chief Financial Officer

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