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Dear Ms Jolly

Ergon Energy's application for a waiver of obligations under the Australian Energy Regulator's Ring-fencing Guideline – Mareeba and Charters Towers depots as regional offices

Under the *National Electricity Rules*, Ergon Energy Corporation Limited (Ergon Energy) must comply with the Australian Energy Regulator's (AER) Electricity Distribution Ring-fencing Guideline (the Guideline).¹ The Guideline permits Ergon Energy to apply for a waiver of the legal and functional separation obligations. Ergon Energy is seeking to renew an existing waiver expiring on 30 June 2025, so its depots at Mareeba and Charters Towers continue to be classified as regional offices for the purposes of ring-fencing out to 30 June 2035.

Under the Guideline, the AER may in its absolute discretion grant an interim waiver.² Ergon Energy would appreciate the AER exercising this option, if it is not in a position to complete its assessment of this application prior to the current waiver expiring on 30 June 2025.

¹ Clause 6.17.2.

² Clause 5.3.3.

Ergon Energy looks forward to providing continued assistance to the AER in considering our enclosed application. Should you require additional information or wish to discuss any aspect of this application, please do not hesitate to contact myself, or [REDACTED], Policy and Regulatory Reform Specialist, on [REDACTED].

Yours sincerely

[REDACTED]

Trudy Fraser

A/Executive General Manager Regulation

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Encl: Ergon Energy's ring-fencing waiver application



Ergon Energy Ring Fencing Waiver Application

**Classification of Mareeba and Charters
Towers depots as regional offices**

3 December 2024



Part of Energy Queensland

CONTENTS

1.	Introduction	1
2.	DESCRIPTION OF WAIVER BEING SOUGHT	2
	The obligations for which the DNSP is applying for a waiver	2
	The reasons why the DNSP is applying for the waiver	2
	Details of services	3
	Proposed waiver commencement and expiry dates	6
	Potential costs if the waiver application is not granted	6
	Reasons why the waiver should be granted	6
3.	Conclusion	8

Ergon Energy's Ring-fencing waiver application

1. INTRODUCTION

Ergon Energy Corporation Limited (Ergon Energy) is a subsidiary of Energy Queensland and is a Queensland Government Owned Corporation. Ergon Energy builds, owns, operates and maintains an electricity distribution network and supplies electricity to more than 750,000 customers over a vast operating area covering one million square kilometres – around 97 per cent of the state of Queensland. Ergon Energy's supply area covers the expanding coastal and rural population centres to the remote communities of outback Queensland and the Torres Strait. There are over 150,000 kilometres of power lines and approximately one million power poles in the Ergon Energy distribution network, along with associated infrastructure such as major substations and power transformers. Ergon Energy also owns and operates 33 isolated power stations that support 39 communities across far western Queensland, through the cape and across 16 islands of the Torres Strait.

Ergon Energy's distribution area is divided into depot areas that vary both in size and number of connection points. The depot boundaries reflect population locations, geographical considerations and impacts of meteorological events (such as cyclones and associated flooding). With the exception of emergency situations, the connection points within each depot boundary are serviced by staff located at an office (depot) within the depot boundary. The boundaries of depot areas compared to the depot locations range from less than, to significantly more than, 100 kilometres (kms) in radius.

The National Electricity Rules (NER) require Ergon Energy to comply with the Australian Energy Regulator's (AER) Ring-fencing Guideline - Electricity Distribution (the Guideline). Ergon Energy supports the granting of ring-fencing waivers by the AER where appropriate. This is especially so if the harms that ring-fencing is designed to prevent can be avoided or adequately managed, and therefore certain restrictions imposed by the Guideline can be relaxed.

Clause 1.4 of the Guideline defines a regional office as having fewer than 25,000 connection points within a 100 kilometres (km) radius of that office. Classification as a regional office provides exemptions from the functional obligations under the Guideline related to physical separation, staff separation and branding separation.

On 18 December 2017, the AER granted a waiver of Ergon Energy's functional separation obligations under clauses 4.2.1 (a), 4.2.2(a) and 4.2.3(a)i. until 30 June 2025 to allow its depots at Mareeba and Charters Towers to be classified as regional offices for the purposes of the Guideline. The waiver was approved on the condition that only two types of contestable services could be provided from these depots. With the end of the current waiver period approaching, Ergon Energy is seeking a new waiver to allow the Mareeba and Charters Towers depots to continue being classified as regional offices with no conditions attached.

Ergon Energy's Ring-fencing waiver application

2. DESCRIPTION OF WAIVER BEING SOUGHT

The obligations for which the DNSP is applying for a waiver

Ergon Energy is applying to the AER for the Mareeba and Charters Towers depots to be classified as regional offices such that these depots are exempted from the office sharing, staff sharing and branding obligations of the Guideline.

The reasons why the DNSP is applying for the waiver

The area served by the Mareeba depot covers a significant geographic area of 63,000 square kms with only 10,500 connection points in total, equating to less than one connection point per six square kms. Due to the proximity of the Mareeba depot to Cairns, the more populated regional centre located around 60kms to the east, there are an estimated 127,700 connection points within 100km radius of the Mareeba depot. However, of the total connections within 100km radius of the depot, only 10,300 connections (roughly eight per cent) are serviced by the Mareeba depot, with the remaining 117,400 connections serviced by other depots. As illustrated in Figure below, the Mareeba depot's proximity to Cairns results in the Mareeba depot not meeting the Guideline's definition of a regional office.

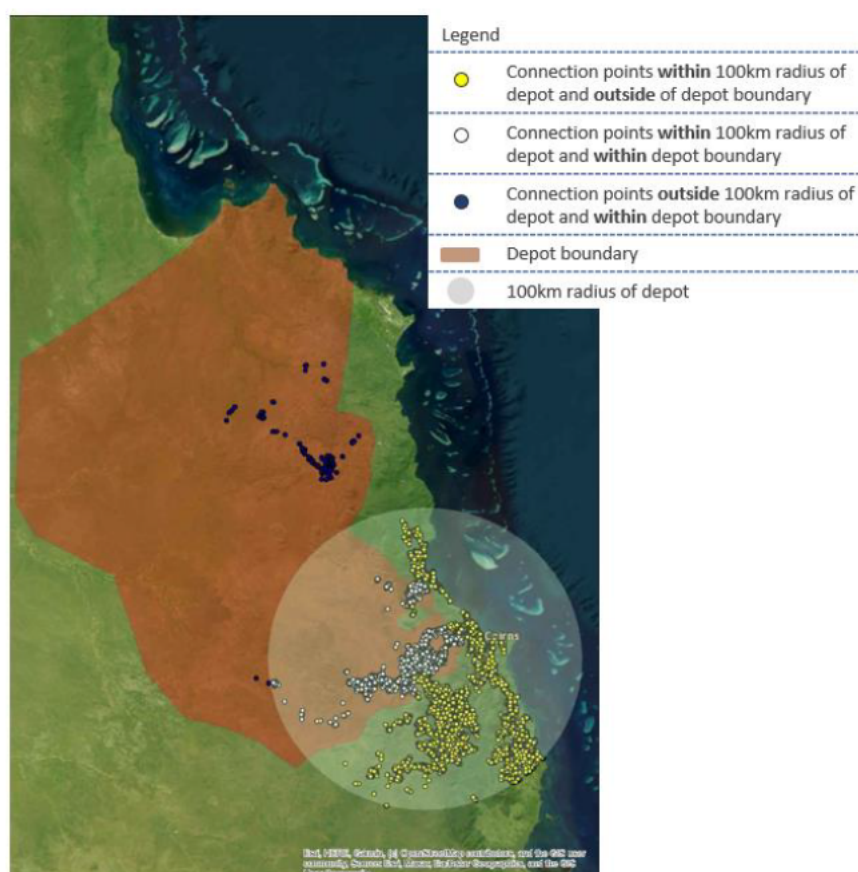


Figure 1: Mareeba depot boundary and connection points

Ergon Energy's Ring-fencing waiver application

In addition, the Charters Towers depot covers a geographic area of 55,000 square kms and serves only 6,200 connection points in total, equating to far less than one connection point per square km. Due to the proximity of the Charters Towers depot to Townsville, the more populated regional centre located roughly 100kms east of Charters Towers, there are an estimated 42,000 connection points within 100km radius of the Charters Towers depot. However, of the total connection points within 100km radius, only 5,700 connections (roughly 14 per cent) are serviced by the Charters Towers depot, with the remaining 36,000 connections serviced by other depots. As illustrated in Figure below, the proximity of the Charters Towers depot to Townsville results in the Charters Towers depot not meeting the Guideline's definition of a regional office.

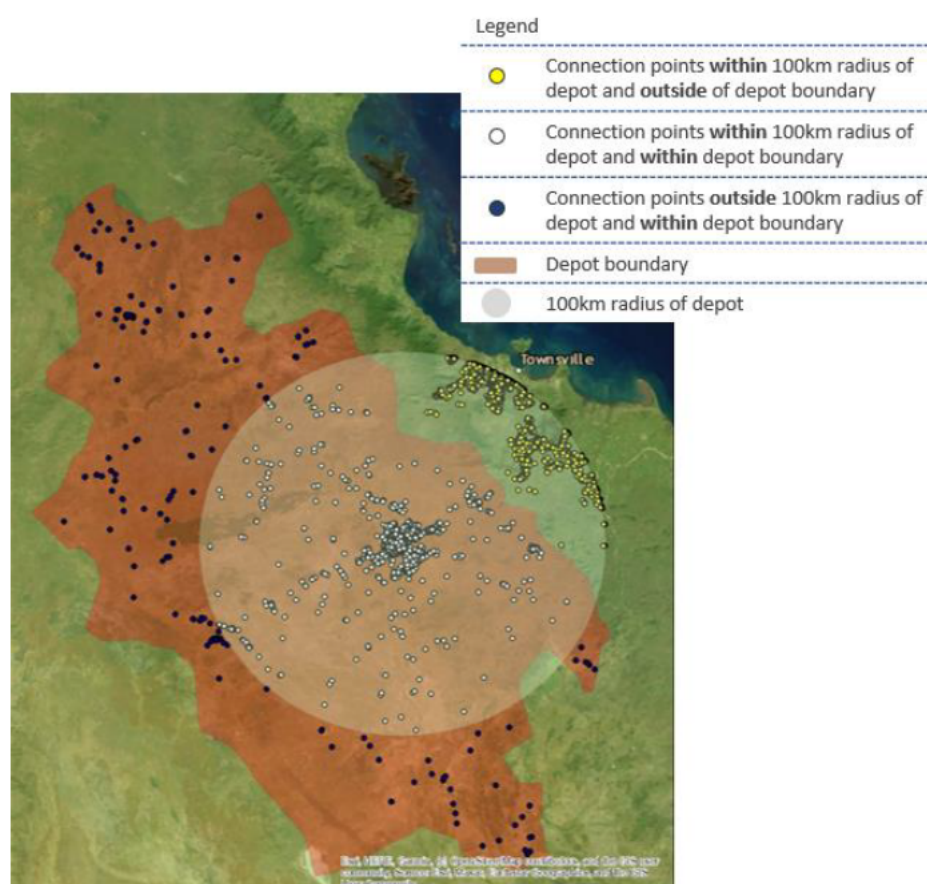


Figure 2: Charters Towers depot boundary and connection points

Details of services

In the AER's 2017 decision, the AER granted the waiver on the condition that it only applies to the provision of the following services:

- contestable metering services, including installation, testing, faults and repairs; and
- pole installation, replacement and repairs on customer property.

Ergon Energy's Ring-fencing waiver application

Despite acknowledging that Ergon Energy offers services in regional areas where competition may be limited or non-existent, we understand it is important that the AER test for the existence of competition to avoid granting a waiver that could harm the potential development of competitive markets.

Applying a waiver with conditions related to services

While Ergon Energy agrees it is possible for some service providers based in Cairns and Townsville to provide contestable services within the boundaries of the Mareeba and Charters Towers depot areas, this would most likely only occur in the locations close to those major population centres.

Outside of such locations, there are larger geographic footprints in the two depot areas that would otherwise only be served at much higher costs and with longer wait times for customers, or go unserved, in the absence of the depots being enabled to provide various contestable services under a ring-fencing waiver. This is supported by a market scan of the communities within the areas, based on the identification of electrical licence holders by their location using the Queensland Electrical Safety Office's electrical licence register¹ and the information about the services each licence holder can provide, based on their online presence. The market scan (see the **confidential** Appendix 1) reveals a patchwork of licenced electrical contractors sparsely spread across the two depot areas.

In terms of the first conditional service—provision of contestable metering—no licenced electrical contractors in these two depot areas offers this service. As such, there is not a competitive market within which customers can choose different service providers each time a need arises, for example to conduct maintenance on or rectify a fault with a meter.

In terms of the second conditional service—provision of pole installation, replacement and repairs on customer property—the market scan suggests there is only one active electrical contractor listing the provision of power pole services in the Mareeba depot service area. However, that one electrical contractor only provides services to very limited parts of this depot's service area. There are no electrical contractors listing this particular service within the Charters Towers depot service area.

Ergon Energy also highlights the 'provider of last resort' and 'community service' aspects of the contestable electricity services that would be provided under a renewed ring-fencing waiver, particularly given the distances required to reach customers, and therefore the associated time and resources. For example, the distance between:

- Mareeba and Laura to the northern part of the Mareeba depot area is 265 kms, requiring 2 hours and 50 minutes of driving time: and
- Charters Towers and Conjuboy near the northern border of the Charters Towers depot area is 257 kms, requiring 2 hours and 40 minutes of driving time.²

¹ <https://fswgap.worksafe.qld.gov.au/elis/views/licenceTypes.xhtml>.

² <https://www.google.com.au/maps>.

Ergon Energy's Ring-fencing waiver application

These drive times do not consider challenges such as inclement weather and road works, which extend driving time and may require work crews to take alternative longer routes if they are available. They are also similar to the drive times required in other DNSP depots that are classified as regional offices under the Guideline, where the AER does not impose conditions on the types of contestable services that can be provided.

In practice, an Ergon Energy work crew may travel from the depot for at least several hours to reach a customer, only to find that it cannot solve one of the customer's problems that it identifies while on site, because the contestable electricity service that would solve that one problem is not covered by the existing waiver conditions set by the AER. In such a situation, the Ergon Energy work crew will return to their depot, while the customer must test the availability of alternative service providers who may be based even further away than the depot (i.e., in Cairns or Townsville) and will base their quote on the time and resources required to travel the longer distance. The customer may be without supply during this period. Once the contestable electricity work is completed, the Ergon Energy work crew may be required to revisit the site, particularly to re-energise if it had to de-energise the premises on its first visit.

Prospects for growth in competition

Competition will grow in areas where there is sufficient growth in demand for the relevant contestable electricity services. Growth in demand for essential services would require additional customers over time, which generally occurs where populations grow. However, while Queensland's major population centres are projected to have significant growth, populations in smaller regional communities are projected to remain at about current levels. For example, out to 2046, the population in the local government area for:

- Mareeba is projected to slightly increase by 1% or less every five years; and
- Charters Towers is projected to slightly decrease by less than 0.5% every five years.³

On that basis, it is unrealistic to expect that competition for contestable electricity services will grow in the geographic areas served by the Mareeba and Charters Towers depots. In fact, as the costs of conducting business rise, it may become more difficult for existing service providers to continue operating in regional areas.

In addition, the expertise required for contestable electricity services is of great value to key regional industries such as mines. Once these regional industries directly employ local people with this expertise, that expertise is no longer available to provide the relevant contestable electricity services to the communities in that location. The expertise is solely dedicated to meeting the extensive needs of those industrial sites.

³ <https://www.qgso.qld.gov.au/statistics/theme/population/population-projections/regions>, see Projected population, by five-year age group and sex, Queensland and regions, 2021 to 2046 (table).

Ergon Energy's Ring-fencing waiver application

As a result, Ergon Energy recommends that the AER renew the regional office status for the Mareeba and Charters Towers depots without a condition on the types of contestable electricity services, in alignment with other regional offices.

Proposed waiver commencement and expiry dates

Ergon Energy proposes that the waiver commences on 1 July 2025 (as the current waiver expires) and expires on 30 June 2035.⁴ This aligns with the Guideline's provision that the AER may grant a waiver for a term that coincides with part or all of the DNSP's current regulatory control period, next regulatory control period, or both periods.⁵ Ergon Energy recommends this maximum period allowed under the Guideline to provide certainty to the two depots and because there is no prospect for growth in competition over this timeframe.

Potential costs if the waiver application is not granted

In the absence of a waiver, the costs for Ergon Energy associated with complying with the ring-fencing requirements would include:

- The costs of duplicating certain staff positions to separate the provision of direct control services from contestable electricity services in compliance with staff separation obligations.
- The costs of sending separate direct control service and contestable electricity service crews to a customer's premises over in some cases very long distances to comply with staff separation obligations.
- The costs of setting up secure access sections in the Mareeba and Charters Towers offices to physically separate staff providing direct control services from staff providing contestable electricity services, to comply with the physical separation /co-location obligations.

Reasons why the waiver should be granted

Clause 5.3.2(a) of the Guideline provides that the AER, in assessing a waiver application and deciding whether to grant a waiver or refuse to grant a waiver, must have regard to:

- the National Electricity Objective (NEO);
- the potential for cross-subsidisation and discrimination if the waiver is granted or refused; and

⁴ Covering the 2025-30 and 2030-35 regulatory control periods.

⁵ As per clause 5.3.4(b), noting that Ergon Energy considers the current regulatory period as the 2025-30 period, given that the existing waiver for the isolated systems ends on 30 June 2025.

Ergon Energy's Ring-fencing waiver application

- whether the benefit, or likely benefit, to electricity consumers of the DNSP complying with the obligation (including any benefit, or likely benefit, from increased competition) would be outweighed by the cost to the DNSP of complying with that obligation.

National Electricity Objective

Granting this waiver is consistent with the NEO because it will promote efficient investment in, and efficient operation and use of, electricity services for the long-term interests of customers, with a particular focus on price, quality, safety, reliability and security of supply for customers that require the contestable electricity services in these regional areas. This is because, without the waiver, customers would be likely to face higher wait times for services if separate crews need to be dispatched and, also, Ergon Energy would incur higher costs, which would likely be passed onto customers.

Cross subsidisation

To avoid cross subsidisation, Ergon Energy will continue to apply its AER-approved Cost Allocation Method (CAM) in relation to the provision of any contestable electricity services. The CAM sets out how Ergon Energy allocates costs towards the provision of services. Separate accounts are also being maintained to demonstrate this clearly and transparently. This should address concerns about the potential for cross subsidisation of contestable services by customers connected to Ergon Energy's regulated distribution network.

Discrimination

In terms of non-discrimination, Ergon Energy will continue to comply with its non-discrimination obligations under the Guideline for all services. It is important to note that customers requiring the contestable services proposed under this waiver application still have the option of attempting to access the services of competitive providers. However, in practice, competitive providers are:

- not available in these locations;
- only available when the work required is above a certain threshold of dollar value, to make the service provision economic for the competitive provider (i.e. potentially only where a minimum number of customers are requesting the work at the same time);
- available but at a considerable premium on the price, to recover the costs associated with travelling outside their usual areas of operation; and/or
- available but not within a timeframe that meets the customers' requirements.

Ergon Energy's Ring-fencing waiver application

Benefits to customers versus costs to Ergon Energy

Without the waiver, customers who require the contestable electricity services face significant impacts, including higher wait times and costs, and there will be no benefits due to there being little to no competition for the provision of these services. In addition, continuing to provide a waiver would not have any impacts on customers of regulated distribution services, nor result in additional compliance costs for Ergon Energy.

3. CONCLUSION

The proposed continuation of the current classification of the Mareeba and Charters Towers depots as regional offices is necessary, because the underlying statistics for connection points in effect remains the same as in 2017. Risks of cross subsidisation will be managed by Ergon Energy continuing to use its CAM to ensure regulated operating and capital expenditures are not being used to provide unregulated services within the geographic areas served by these two depots. There is also effectively no real competition across the large areas served by these depots for the contestable services the depots can provide and therefore no opportunity for Ergon Energy to discriminate. Ergon Energy also considers there will be no harm to customers, rather, a waiver will promote the achievement of the NEO for customers who are otherwise disadvantaged due to their regional locations.