

Ring-Fencing Compliance Report

For period 1 July 2020 to 31 December 2021

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Contents

Overview	3
1 Background	3
1.1 Purpose	3
1.2 Corporate Overview	4
2 Measures to ensure compliance	5
2.1 Obligations to establish and maintain accounts	6
2.2 Obligation not to discriminate	7
2.3 Offices, staff, branding and promotions	7
2.3.1 Physical separation/co-location	7
2.3.2 Staff sharing	7
2.3.3 Branding and cross promotion	7
2.3.4 Office and staff registers	8
2.4 Information access and disclosure obligations	8
2.5 Conduct of Service Providers	9
3 Breaches	9
3.1 Telecommunication contract novations	9
4 Other services	10
5 Transactions with affiliated entities	10
6 Waivers	11
6.1 Background	11
6.2 Temporary waivers	11
6.3 Waivers due to nature of electricity sector	11

Overview

1 Background

The National Electricity Rules (**NER**) impose specific obligations on regulated electricity network businesses to prevent regulated businesses from:

- discriminating in favour of their related parties to disadvantage competitors operating in these markets; and
- using revenue earned from regulated services to cross-subsidise contestable services.

To support these obligations, the Australian Energy Regulator (**AER**) has produced the Electricity Distribution Network Ring-Fencing Guideline (**Guideline**). The latest version of the Guideline was released on 3 November 2021.

The Guideline requires Distribution Network Service Providers (**DNSPs**) to report their compliance against the Guideline each year. One alteration in the most recent version of the Guideline was to change the reporting year from financial to calendar year. To facilitate the transition, the AER have provided for a six month delay in the provision of a compliance report for the 2020-21 regulatory year to allow for a report on compliance on the 2021 year to be included in the one report.

For the period from 1 July 2020 to 31 December 2021, Tasmanian Networks Pty Ltd (ACN 167 357 299) (**TasNetworks**) and affiliated entities, Fortytwo24 Pty Ltd (ACN 117 987 925) (**42-24**) and Marinus Link Pty Ltd (ACN 630 194 562) (**Marinus**), have undertaken a number of compliance activities, including:

- balancing separate accounts;
- separating assets using cost allocation and attribution methods;
- adherence to disclosure, protection and sharing of confidential information policies; and
- compliance training for staff and detailing exemptions, where they apply.

This Annual Ring-Fencing Compliance Report, for the 18 months ended 31 December 2021 (**Report**) is TasNetworks' submission against the reporting requirements of the Guideline.

1.1 Purpose

TasNetworks has prepared this Report and provided it to the AER in accordance with Guideline requirement 6.2 Reporting. TasNetworks does not claim confidentiality over this Report. TasNetworks confirms that the Report is compliant with the Guideline, with the exception of circumstances outlined later in this Report.

1.2 Corporate Overview

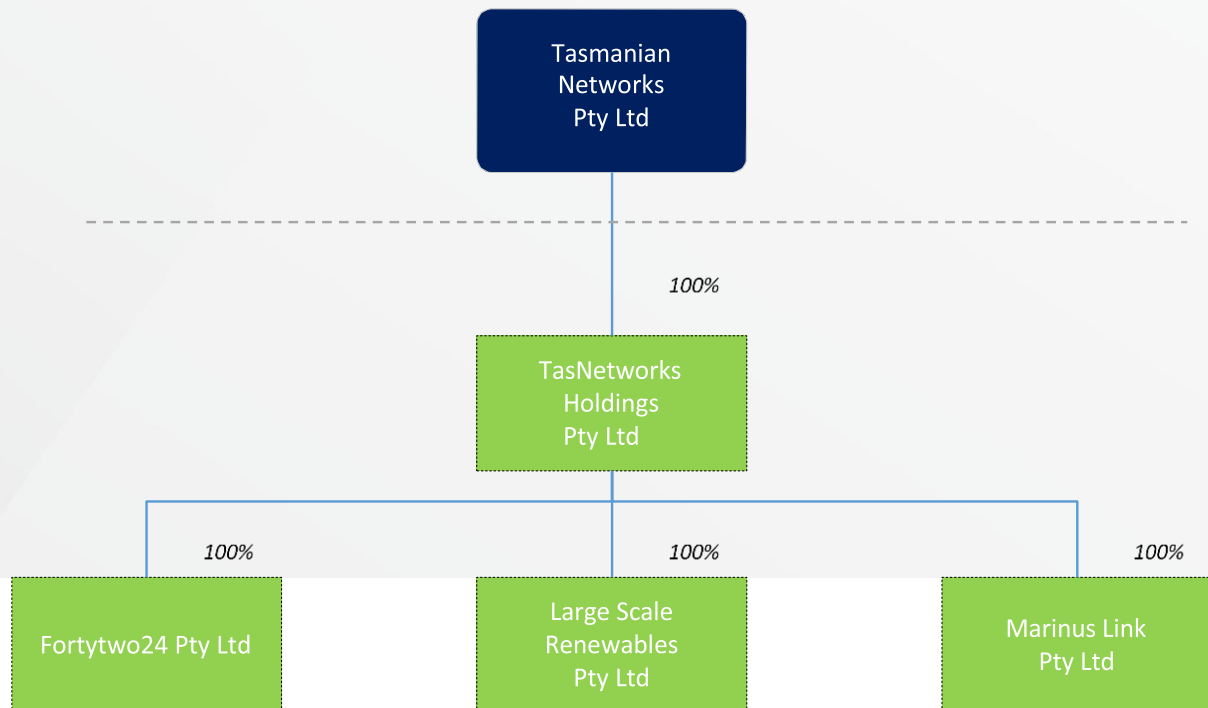
TasNetworks differs from other DNSPs, as it is an integrated transmission and distribution business. TasNetworks sought a waiver of clause 7.1(a)(ii) of the Transmission Ring-Fencing Guidelines to allow it to own and operate both the transmission business and the distribution business. TasNetworks was granted this waiver on 12 May 2014 and the AER waived TasNetworks obligation to comply with clause 7.1(a)(ii).

TasNetworks has made a key decision not to separate its transmission services from its direct control distribution services and to apply the NER definition of Transmission Services (which includes Prescribed, Negotiated and Unregulated transmission services). The provision of these services are able to continue together with regulated distribution services, with existing cost-allocation and asset sharing provisions continuing to apply. No further ring-fencing of Negotiated or Unregulated transmission services is deemed necessary.

Recognising that TasNetworks would likely provide some services that would not comply with the Guideline when first introduced, FortyTwo24 Pty Ltd (**42-24**), previously called AuroraCom Pty Ltd, became a wholly owned subsidiary of TasNetworks Holdings from 1 July 2018. Since this time, TasNetworks has created two more wholly owned subsidiaries of TasNetworks Holdings. They are:

1. Large Scale Renewables Pty Ltd; and
2. Marinus Link Pty Ltd.

Image 1 shows the relationships between the entities.



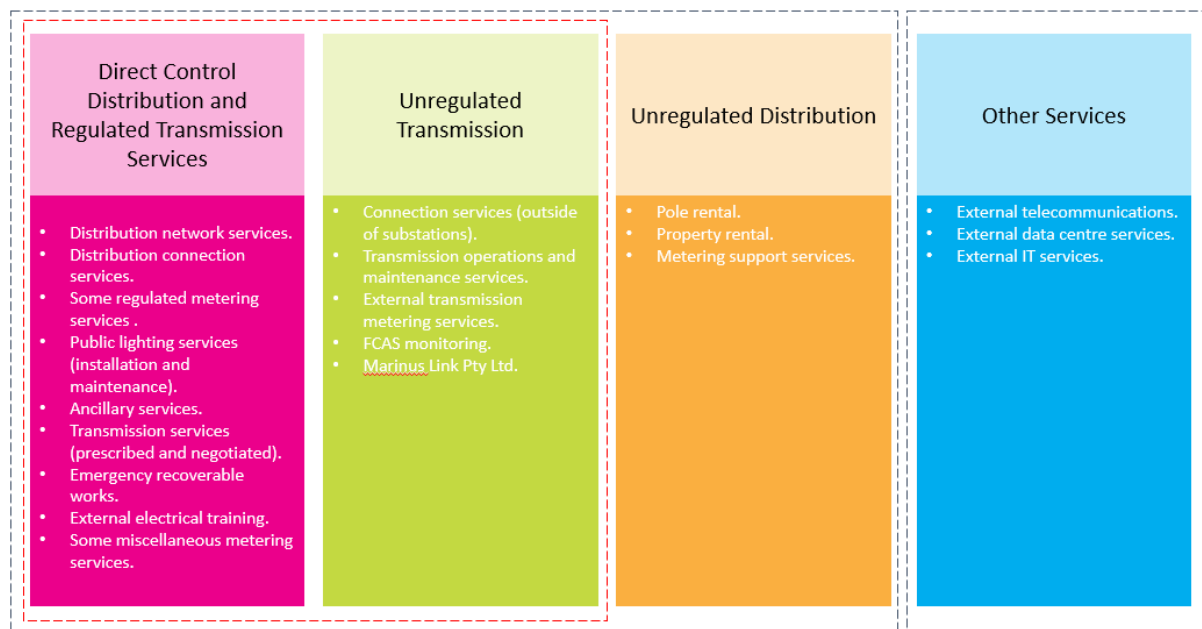
Currently, 42-24 does not undertake any contestable electricity services. It does undertake a number of 'other services' that require legal separation, including:

- Telecommunications;
- Data centre services; and
- IT Services (including Infrastructure as a Service (**IaaS**)).

Neither Large Scale Renewables Pty Ltd nor Marinus Link Pty Ltd provide distribution or other services as defined in the Guideline.

Large Scale Renewable Pty Ltd is currently non-operational. It does not own any assets, holds no data and has no staff.

Image 2 illustrates the services attributable to TasNetworks and 42-24 implemented under this Guideline



2 Measures to ensure compliance

Clause 6.2.1(b)i. of the Guideline requires that the annual compliance report must identify and describe the measures the DNSP has taken to ensure compliance with its obligations under this Guideline, for the calendar year.

A mandatory generic ring-fencing training package is available for all TasNetworks employees, including:

- an introduction to ring-fencing;
- an overview on obligations to not discriminate according to 4.1(b) and (c) of the Guideline;
- hypothetical scenarios which may be encountered by TasNetworks team members; and
- a short quiz.

Additional training was delivered in 2021, targeting employees most likely to work in both the unregulated and regulated parts of the business. This training supported the Distribution Ring-fencing Information Protocols described in section 2.4 of this report.

Measures used to ensure compliance with specific Guideline clauses are provided in the following sections.

2.1 Obligations to establish and maintain accounts

Below is an explanation of the procedures and processes used by TasNetworks to ensure that its distribution services have been classified as set out by the AER in the current Distribution Determination and do not contravene clause 3.2 of the Guideline.

Cost capture and financial management systems

TasNetworks' chart of accounts and costing systems have been established so that both operating and capital expenditure can be separately accounted for and reported in accordance with TasNetworks' AER approved Cost Allocation Method (**CAM**) and regulatory reporting requirements.

TasNetworks' principles, processes and policies all support compliance with the CAM. This includes the processes of attributing costs directly and of allocating shared costs to categories of service.

TasNetworks' cost allocation principles and policies consider the direct allocation of costs to:

- Direct Control Distribution services;
- Regulated Transmission services;
- Unregulated Transmission services;
- Unregulated Distribution services;
- Other Distribution services; and
- Negotiated Distribution services.

Costs that are not directly allocated to one particular service type (e.g. overhead costs) are subject to a shared allocation of costs between the following:

- Direct Control Distribution services;
- Regulated Transmission services;
- Unregulated Transmission services;
- Unregulated Distribution services;
- Other Distribution services; and
- Negotiated Distribution services.

The chart of accounts structure enables costs to be attributed directly to the categories of services provided by TasNetworks or 42-24, or automatically allocates costs between them.

Incurred costs are allocated to the following chart of account dimensions in the financial systems:

- responsibility centre/department/cost centre - defined as the area in the business that is responsible for the work performed;
- functional area - defined as the nature of the work being performed and is also used to identify between capital and operating expenditure as well as the type of work and associated service classification (work category); and
- cost element/General Ledger code - defined as the nature of the costs incurred such as labour or contracted services.

The above dimensions form the basis of the cost hierarchy. Each dimension is assigned to a service classification. By establishing a clear relationship between dimensions and the categories of services, the financial systems ensure that costs are correctly attributed to the relevant service.

TasNetworks has three main types of costs:

- directly allocated or attributable costs (such as timesheet labour, materials, fleet, invoices for contracted services or via journal such as licences fees, etc.);
- on costs for labour, materials and fleet; and
- shared costs (allocated on the basis of causal cost allocators).

2.2 Obligation not to discriminate

Clause 4.1 of the Guideline places the obligation on the DNSP to not discriminate (either directly or indirectly) between a related electricity service provider and a competitor (or potential competitor) of a related electricity service provider (**RESP**) in connection with the provision of:

- i. direct control services by the DNSP (whether to itself or to any other legal entity); and/or
- ii. contestable electricity services by any other legal entity.

This obligation does not apply to TasNetworks, as the subsidiaries are not engaged in the provision of contestable electricity services.

2.3 Offices, staff, branding and promotions

2.3.1 Physical separation/co-location

Clause 4.2.1(a) of the Guideline obligates the DNSP to use offices that are separate from any offices from which a RESP provides contestable electricity services.

This clause does not apply to TasNetworks, as the subsidiaries are not engaged in the provision of contestable electricity services. Despite this 42/24 has moved to offices that are physically separated from the rest of TasNetworks.

2.3.2 Staff sharing

Clause 4.2.2(a) of the Guideline obligates the DNSP to ensure that its staff involved in the provision or marketing of direct control services are not also involved in the provision or marketing of contestable electricity services by a RESP.

This clause does not apply to TasNetworks, as the subsidiaries do not provide contestable electrical services.

2.3.3 Branding and cross promotion

Clause 4.2.3(a) of the Guideline obligates the DNSP to use branding for its direct control services that is independent and separate from the branding used by a RESP for contestable electricity services, such that a reasonable person would not infer from the respective branding that the DNSP and the RESP are related.

The DNSP must not advertise or promote its direct control services and its contestable electricity services that are not direct control services together (including by way of cross-advertisement or cross-promotion).

The DNSP must not advertise or promote contestable electricity services provided by a related electricity service provider other than the DNSP itself.

While this clause does not apply to TasNetworks, as the subsidiaries do not provide contestable electrical services, TasNetworks has enacted controls to ensure content on its website does not breach clause 4.2.3(a).

2.3.4 Office and staff registers

Clause 4.2.4 (a) of the Guideline obligates the DNSP to establish, maintain and keep a register that identifies:

- i. the offices to which it has not applied clause 4.2.1(a) by reason of clauses 4.2.1(b)i. or 4.2.1(b)iii.; and
- ii. the staff positions (including a description of the roles, functions and duties) of those of staff positions to which it has not applied clause 4.2.2(a) by reason of clauses 4.2.2(b)i.a., 4.2.2(b)i.b., 4.2.2(b)iii. or 4.2.2(d);
- iii. the staff positions referred to in clause 4.2.4(a)ii. which are held, or have been held within the previous three months, by a member of staff whose access to electricity information ceased upon, or in the 12 months prior to, commencing in that position, and the dates on which that member of staff commenced to hold and (if applicable) ceased to hold that position.

Clause 4.2.4 (b) states that ‘no later than 15 January, 15 April, 15 July and 15 October each year, a DNSP must publish, on its website, an updated version of each of the registers referred to in clause 4.2.4(a). The DNSP must ensure that the information published in each updated version is current to the end of the calendar month that is immediately prior to the required publication date for that updated version under this clause 4.2.4(b)’.

TasNetworks’ Shared Office Register details all the shared offices where TasNetworks provides direct control services and contestable electricity services as defined by the Guideline. The [Shared Office Register](#) is available on TasNetworks’ external website, as per the Guideline requirements. From 1 July 2020 to 31 December 2021, TasNetworks had no shared offices through which contestable electricity services were provided.

TasNetworks’ [Shared Staff Register](#) details all TasNetworks shared staff providing contestable electricity services as defined by the Guideline. The **Shared Staff Register** is available on TasNetworks’ external website, as per the Guideline requirements. From 1 July 2020 to 31 December, TasNetworks had no shared staff providing contestable electricity services.

2.4 Information access and disclosure obligations

TasNetworks has developed protocols and registers to:

- prevent the disclosure of information (clause 4.3.2 of the Guideline);
- prevent the sharing of information (clause 4.3.3 of the Guideline); and
- establish an information sharing register (clause 4.3.4 of the Guideline).

TasNetworks has published its [Information Sharing Protocol](#) on its external website, as per clause 4.3.3(d) of the Guideline. This document sets out the process through which TasNetworks will share information, pursuant to clause 4.3.3 of the Guideline, and the disclosure of information, pursuant to clause 4.3.2 of the Guideline.

TasNetworks’ Information Sharing Protocol also contains a link to our information sharing register. TasNetworks’ **Information Sharing Register** details all the legal entities who have requested to be included on the information sharing register and any confidential information that they have requested as defined by the Guideline. TasNetworks released its information sharing register on its external website, as per the Guideline requirements.¹

¹ Currently there is nothing reported on the Register since TasNetworks does not have a related entity providing electricity services.

To assist staff with managing information within the TasNetworks Group (including the subsidiaries), TasNetworks has published an internal document titled Distribution Ring-fencing Information Protocol. This document addresses clauses from the Guideline associated with information access and disclosure. Additionally, a training program was developed and delivered to those teams identified as most likely to be impacted by the information sharing requirements in the Guideline.

2.5 Conduct of Service Providers

TasNetworks must ensure that any new or varied agreement between TasNetworks and a service provider includes provisions requiring the service provider to comply with clause 4.4.1(a) of the Guideline. TasNetworks must also not directly or indirectly encourage or incentivise a service provider to engage in conduct contrary to clause 4.4.1(b) of the Guideline.

To ensure compliance with these obligations under the Guideline, TasNetworks has now completed a review of our contract templates and all ring-fencing obligations are clearly defined. The existing ring-fencing clauses were not been amended as part of this review. In addition, TasNetworks has procured a software platform to manage creation of contracts. This platform enables certain commercial contract content to be changed but other content such as the ring-fencing clauses will not be able to be deleted or amended. Penetration testing is currently underway with operational roll-out planned for late March-early April 2022.

3 Breaches

As required by Guideline clause 6.2.1(b)ii, TasNetworks has identified the following breach, which has been reported to the AER as per clause 6.3.

3.1 Telecommunication contract novations

In September 2017, in preparation for the introduction of ring-fencing, TasNetworks identified 49 telecommunications contracts which would require novation from TasNetworks to 42-24. Due to complex nature of the agreements, and the time expected before novations could be completed, TasNetworks applied for and was granted a waiver to continue to provide the services until 30 June 2018.

In June 2018, TasNetworks identified the possibility that some of the more complicated novations might overrun the 30 June 2018 deadline. At waiver expiry, 13 contracts remained outstanding. However, owing to the pre-emptive measures put in place, the expectation that contracts would soon be novated and the attendant lack of implications for the provision of contestable electricity services, TasNetworks did not submit a breach report considering the ring-fencing materiality threshold for reporting was not met.

Despite TasNetworks continued efforts, over the course of 2018-19, little further progress on novating contracts was made. This was solely due to a lack of any incentive for counterparties to execute the novation documentation. Owing to the slowed progress, TasNetworks informed the AER and sought advice on what further actions could be taken.

After initial conversations with the AER, TasNetworks lodged a breach report in March 2019. The AER responded in April 2019 informing TasNetworks that the AER considered TasNetworks to be in breach of Clause 3.1 of the Ring-Fencing Guideline. After further discussions with the AER, it was agreed that TasNetworks would submit an initial report by 31 May 2019, and quarterly thereafter, to inform the AER on the progress being made to transfer the remaining contracts.

In June 2020, the AER instigated a meeting with TasNetworks to discuss the progress of the telecommunication novations. At this meeting, the AER agreed with TasNetworks that there was little TasNetworks or 42-24 could do to expedite the progress of the novations. As such, TasNetworks and the AER agreed to continue to report quarterly as to the progress of the contract novations. As of 31 December 2021 there currently remain 3 contracts requiring novation.

4 Other services

Clause 6.2.1(b)iii. of the Guideline requires DNSPs to report all Other services provided by the DNSP in accordance with clause 3.1 of the Guideline. TasNetworks did not provide any Other services, that being services that are not transmission or distribution services in the period of this Report.

5 Transactions with affiliated entities

TasNetworks and its affiliate, 42-24, are parties to a Master Business Services Agreement under which TasNetworks provides 42-24 with:

- corporate services (which include Board, Company Secretary and General Counsel support, commercial services, financial analysis and reporting, information management, information technology and human resources);
- access to staff to perform work on behalf of 42-24; and
- access to assets for 42-24 to fulfil relevant contract obligations.

Corporate services are charged on either a fixed charge or do and charge basis. Access to staff and assets are charged based on relevant pricing principles that recover operating expenses, overheads and asset costs.

TasNetworks and 42-24 are also parties to an intercompany loan agreement, under which 42-24 is able to borrow funds from TasNetworks. The loan agreement is currently not active.

While, TasNetworks and its affiliate Marinus Link Pty Ltd (**Marinus**) are parties to a Master Business Services Agreement under which TasNetworks provides Marinus with:

- insurance;
- external audit;
- corporate shared services (such as Board and governance and finance and administration); and
- access to staff to perform work on behalf of Marinus.

Corporate shared services are charged on an agreed annual fee utilising the cost allocation methodology. Access to staff is charged on a 'do and charge' basis.

TasNetworks and Marinus are parties to an intercompany loan agreement. Under this agreement, Marinus is able to borrow funds from TasNetworks who have borrowed them from Tasmania's central borrowing authority, Tasmanian Public Finance Corporation (**TASCORP**). There is also currently a 12 monthly rolling agreement, whereby TasNetworks generally agrees to support Marinus as a going concern. This may include not seeking repayment of any loan repayments until such time as it is able to do so. It also includes a requirement for Marinus to pay interest to TasNetworks at a rate equivalent to the cost of funds that Marinus would be able to borrow at.

6 Waivers

6.1 Background

TasNetworks has had two types of waivers, namely waivers:

- of a temporary or transitional nature, where the cost of complying immediately from the introduction of the Guideline would outweigh any benefits that would accrue in this timeframe; and
- that reflect the nature of the electricity sector in Tasmania in that there are no viable alternative providers of the service.

6.2 Temporary waivers

TasNetworks did not have any ongoing temporary waivers in place for the period 1 July 2020 to 31 December 2021.

6.3 Waivers due to nature of electricity sector

TasNetworks sought a number of temporary waivers in 2017 that primarily arose due to the timing between the commencement of the Guideline and service classification decisions and/or the ability to establish the necessary legal structures. A further waiver was sought in 2019 to assist with TasNetworks exiting from the provision of services related to the provision of Aurora Pay As You Go (APAYG) metering support services. All these waivers have now expired.

TasNetworks has had no further requirement to apply for any additional waivers and therefore has no active waivers. Copies of TasNetworks' previous waivers and the AER's decisions can be found on the [AER's website](#).

A maintained register of waivers is publically available via TasNetworks' [website](#).