

TasNetworks

Ring-Fencing Waiver Applications

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July 2017



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1. Introduction

This document comprises TasNetworks' applications for waivers from aspects of the Australian Energy Regulator's (AER) distribution ring-fencing guideline (**the guideline**). We also have enclosed a request for a no action letter regarding some aspects of the information access and disclosure provisions related to our new affiliated entity.

Below is a summary of TasNetworks' waiver applications. These waiver applications form a key component of our overall compliance plan and approach which has also been submitted to the AER.

Temporary waivers

The Australian Energy Regulator has indicated that it is likely that a number of services will be reclassified as part of the upcoming framework and approach consultation processes. We are seeking a temporary waiver for these services to avoid unintended impacts and costs of separation, prior to them being reclassified as direct control services for the 2019-24 regulatory control period.

Legal separation implementation

A six month delay allows a considered transition to a new operating model and legal structure. It allows all necessary structural, contractual and operational changes to be efficiently put in place and resourced efficiently and appropriately in light of considered advice, including legal and tax advice, and requires shareholder approval prior to its establishment.

Type 1-4 metering services

We are seeking a temporary waiver to allow TasNetworks staff and contractors to provide this service, and to work from co-located sites with the regulated distribution business, including the continued use of the TasNetworks brand to allow the use of TasNetworks branded offices, website, trucks, uniforms and other equipment. This will allow additional time for TasNetworks, in conjunction with Aurora Energy, to transition these meters over to a new metering provider under the upcoming Power of Choice Reforms.

2. Waiver Applications

2.1. Introduction

The electricity market in Tasmania is unique and there are differences in the role that TasNetworks plays in this market compared to the role of other Distribution Network Service Providers (**DNSPs**). Tasmania is a small market with a limited number of players. As a result of the guideline, TasNetworks will restructure aspects of its business to ensure compliance with the guideline. In addition, TasNetworks is seeking a number of waivers for some specific services that are currently provided.

The following waivers can be grouped into two areas:

- 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
- Waivers that reflect the nature of the electricity sector in Tasmania in that there are no viable alternative providers of the service.

TasNetworks has provided the following waiver applications based upon the requirements and criteria within the current guideline. Below we have outlined the key considerations as required by the guideline for each.

2.2. Temporary Waivers for negotiated and unclassified services

In July 2017, the AER finalised the Framework and Approach for TasNetworks for the upcoming 2019-24 regulatory period. This initial step in the regulatory process has resulted in a significant update of the service classifications that will apply to TasNetworks from 1 July 2019. The current service classification for our 2017-19 regulatory period will apply until the updated service classification comes into effect on 1 July 2019.

Whilst the guideline is closely linked to the service classification process within the Framework and Approach, the National Electricity Rules, as they currently apply, do not allow for updates to service classification within a regulatory period.

Part of the compliance strategy for TasNetworks is to transition a number of currently negotiated, unregulated or unclassified services to alternative control services (as recognised in the updated Framework and Approach) at the beginning of the next regulatory period. In the period between the commencement of the guideline and the beginning of the next regulatory period (1 July 2017) TasNetworks is seeking waivers for the services outlined in Table 2.1. These waivers are purely of a temporary nature and from 1 July 2019 TasNetworks will be in full compliance with the guideline in respect to the services shown in Table 2.1.

Table 2.1 Current negotiated, unregulated or unclassified services

Service	Description	Current classification (July 17 – June 19)	Future Classification (July 19 – June 24)
Network safety services	Examples include: <ul style="list-style-type: none"> • Provision of traffic control services by the distributor where required • Fitting of tiger tails, high load escort, night watch (private security and flood lighting services). • De-energising wires for safe approach (e.g. for tree pruning) 	Not classified	Alternative Control Service
Planned Interruption – Customer Requested	Where the customer requests TasNetworks to move a planned interruption and agrees to fund the additional cost of performing this distribution service outside of normal business hours	Not classified	Alternative Control Service
Inspection services - private electrical installation	Inspection of and reinspection by a distributor of: <ul style="list-style-type: none"> • private electrical wiring work undertaken by an electrical contractor • private inspection of privately owned LV and HV network infrastructure 	Not classified	Alternative Control Service
Inspection of private assets under Tasmanian Government direction	Private pole inspections (Tasmanian Government stipulates as common distribution service)	Unclassified	Standard Control

Service	Description	Current classification (July 17 – June 19)	Future Classification (July 19 – June 24)
Miscellaneous metering services	Various new metering services as a result of the power of choice reforms which include: <ul style="list-style-type: none"> • Meter recovery and disposal – type 5 and 6 current transformer metering • Distributor arranged outage for the purpose of replacing metering • Correction of metering and market billing data • Meter disposal 	Not classified	Alternative Control Service
Legacy pre-payment Meters	The operation and maintenance of legacy pre-payment meters, and associated services as a specific service for retailers.	Not classified	Alternative Control Service
Registered participant support services	Services and information provided by the distributor and proposed market participant associated with connection arrangements and agreements made under Chapter 5 of the NER	Not classified	Alternative Control Service
Site inspection	Site inspection services in order to determine the nature of the connections service sought by the connection applicant	Not classified	Alternative Control Service
Public lighting	Provision, construction and maintenance of public lighting and emerging public lighting technology	Alternative control/negotiated	Alternative Control Service
Provision of electrical training to third parties	The provision of distribution network related training services to third parties	Not classified	Alternative Control Service

a) The obligation in respect of which the DNSP is applying for a waiver

TasNetworks is seeking a waiver in respect to the obligations under the functional separation provisions for the list of currently unregulated services in Table 2.1. Specifically, TasNetworks is seeking a waiver for the following provisions.

Chapter 4 – Functional Separation

Under clause 4.2.5 of the guideline, TasNetworks is applying for a waiver of all obligations under - 4.2 including:

4.2.1 Physical separation/co-location

4.2.2 Staff sharing

4.2.3 Branding and cross-promotion

4.2.4 Office and staff registers

Additionally, under clause 4.4.2 of the guideline we are seeking a waiver from the following obligation:

4.4.1(a) Conduct of Service Providers

b) The reasons why the DNSP is applying for the waiver

The waiver is a temporary waiver to ensure compliance from the inception of the guideline. The waiver recognises that TasNetworks has made appropriate steps to offer previously unclassified services as direct control services. However given that service classification cannot change during a regulatory control period, the waiver avoids a technical non-compliance with the guideline.

c) Details of the service, or services, in relation to which the DNSP is applying for the waiver

- Network safety services
- Planned Interruption – Customer requested
- Inspection services – Private electrical installation
- Inspection of private assets under Tasmanian Government direction
- Miscellaneous metering services
- Legacy pre-payment meters
- Registered participant support services
- Site inspections
- Public lighting
- Provision of electrical training to third parties

d) The proposed commencement date and expiry date (if any) of the waiver and the reason for those dates.

It is proposed that the waiver for these services will commence on 1 January 2018 until the end of the next regulatory control period on 30 June 2019.

e) Details of the costs associated with the DNSP complying with the obligation if the waiver of the obligation was refused

TasNetworks estimates that most of the additional costs of complying with the guideline for these services would be as a result of temporarily changing business processes and creating staff duplication. It is likely that these costs would be large given the variety of services that are currently unclassified.

In addition, we would also need to establish a new brand, branding material, website and relocate to new premises.

Given the temporary nature of the waiver request and the period of non-compliance it would be an inefficient and costly process to make these changes, and then reverse them in a year and a half as the new service classification comes into effect.

f) The regulatory control periods(s) to which the waiver would apply.

2017-19 (1 January 2018 – 30 June 2019)

g) Any additional measures the DNSP proposes to undertake if the waiver were granted

Through the regulatory process, for these services, TasNetworks will ensure that prices and service descriptions are developed to be aligned with future alternative control prices and service descriptions. The intention of TasNetworks is that customers continue to have access to these services until their classification is changed at the beginning of the next regulatory period.

We will also continue to apply our Cost Allocation Methodology (**CAM**) to these services to ensure no cross-subsidisation exists.

h) The reasons why the DNSP considers the waiver should be granted with reference to the matters specified in clause 5.3.2 (a) including the benefits, or likely benefits, of the grant of the waiver to electricity consumers.

Given that none of the above services are considered competitive (including by the AER in the R19 service classification), and that each of the services will become direct control services from 1 July 2019, there will be no benefits of increased competition for customers to offset the higher costs of implementing functional separation for the short period until 1 July 2019 and then dismantling this separation after 1 July 2019.

The potential for cross subsidisation and discrimination from granting this waiver is negligible as it is unlikely that another entity would look to (or would be able to) compete with TasNetworks in the provision of the services. Our CAM will continue to ensure that cross subsidies will not eventuate through the limited period that the waiver will apply.

2.3. Temporary Legal Separation Waiver

TasNetworks commenced operation in 2014 following the merger of Aurora Energy's distribution function with Transend's transmission function. This restructure ensured that the then new TasNetworks business structure was best placed to take advantage of efficiencies and synergies between the network businesses. TasNetworks has been able to significantly reduce operating costs as a result of this restructure.

The restructure of the predecessor TasNetworks business was implemented prior to the introduction of ring fencing for DNSPs. Consequently the service catalogue of TasNetworks includes a number of services that generate external non-regulated revenue. For those services that would be considered 'Other Distribution Services' under the guideline, TasNetworks is implementing a number of steps to ensure compliance with the requirements of the guideline. For those services that fall outside of our core distribution and transmission services, TasNetworks is proposing to establish a new legal entity to provide those services. This will ensure that TasNetworks is compliant with the guideline in relation to legal separation.

The new legal entity will be a commercial entity that will provide a number of services into what are contestable, or potentially contestable, markets.

TasNetworks has identified the following existing services that will be delivered from the new entity.

- External Telecommunications
- External Data Centres
- External IT Services
- Operation and maintenance support for isolated distribution networks not part of the NEM (Bass Strait Islands)

These services fall within 'Other Services' for the purpose of the guideline.

The necessary work required to establish a new business is extensive, and given a realistic timeframe in establishing this business, a temporary waiver is sought to allow for this work to be completed.

a) The obligation in respect of which the DNSP is applying for a waiver.

TasNetworks is seeking a temporary waiver for the legal separation provisions of the guideline under clause 3.1 Legal Separation. This would allow TasNetworks as a DNSP to provide Distribution and Transmission Services in conjunction with what is considered 'Other Services' under the guideline.

Specifically, under clause 3.1 (e) of the guideline, TasNetworks is seeking a waiver for:

3.1 Legal Separation

b) The reasons why the DNSP is applying for the waiver

TasNetworks is making the appropriate steps to ensure compliance with the guideline. Given TasNetworks' structure prior to the introduction of the guideline, TasNetworks is required to take a number of steps to ensure that the DNSP no longer provides what are considered to be 'Other Services' under the guideline.

The establishment of a new business carries a number of requirements, particularly as TasNetworks is a state-owned company. Our shareholder will need to be comfortable that the new business meets expectations around its role in the Tasmanian market. In addition, any new subsidiary company requires shareholder approval prior to its establishment.

Significant work is also required to establish appropriate governance arrangements, business processes and legal and taxation arrangements for a new entity.

c) Details of the service, or services, in relation to which the DNSP is applying for the waiver

- External Telecommunications
- External Data Centres
- External IT Services
- Operation and maintenance of isolated distribution networks not part of the NEM (Bass Strait Islands)

These four 'Other Services' are currently provided by TasNetworks.

d) The proposed commencement date and expiry date (if any) of the waiver and the reason for those dates.

The waiver will apply from 1 January 2018 – 30 June 2018

e) Details of the costs associated with the DNSP complying with the obligation if the waiver of the obligation was refused

TasNetworks believes that the costs would fall into three categories:

- The additional cost that would be incurred from expediting the establishment of the new business;
- The additional risks that would present themselves from not having undertaken the appropriate steps to ensure the new legal entity is established in an orderly manner (including a thorough due diligence process);
- The risk that current major business initiatives underway will need to be reassessed or re-scoped, duplicating costs; and
- Increased legal and tax expenditure due to expediting the establishment of the new business.

f) The regulatory control periods(s) to which the waiver would apply.

2017-2019 (part only)

g) Any additional measures the DNSP proposes to undertake if the waiver were granted.

We will continue to apply our CAM to these services to ensure no cross-subsidisation exists.

h) The reasons why the DNSP considers the waiver should be granted with reference to the matters specified in clause 5.3.2 (a) including the benefits, or likely benefits, of the grant of the waiver to electricity consumers.

The benefit of granting the waiver will be that TasNetworks will be able to ensure that the necessary due diligence processes, legal and taxation advice and statutory requirements are in place prior to the establishment of the new entity. This considered approach mitigates potential risks, and will allow TasNetworks to ensure that the new business is established in a way that does not impose additional costs on customers due to not taking the appropriate time to ensure risks are well-managed.

For the six months that the waiver is in place, TasNetworks will continue to ensure that the CAM is adhered to and that separate accounting records are maintained (as is currently the case). This will eliminate any risk of cross-subsidisation occurring.

In addition, the services which are intended to be delivered from the new entity are not 'contestable electricity' services, thus the potential for any discrimination prohibited by the guideline in relation to the provision of these services is not present.

2.4. Type 1-4 legacy meters – Meter Provider Role Waiver

Current situation until 30 November 2017

Currently TasNetworks is the Meter Provider (**MP**) for approximately 3,000 type 1-4 meters connected to our distribution network. The Retailer for these sites is currently the responsible person for these sites. TasNetworks is the MP and currently owns the meters on these sites. For the existing type 6 meters on our network TasNetworks is currently the responsible person as well as the MP. TasNetworks, through contractual arrangements, is the responsible person for a number of type 1-4 transmission meters.

The provision of type 1-4 distribution meters is currently a contestable market. Given our ability to leverage existing systems and expertise, TasNetworks has previously been active in this space.

Situation post December 2017

TasNetworks has made the decision not to become a Metering Coordinator (**MC**) for type 1-4 meters under the Power of Choice reforms which come into effect on 1 December 2017. As required under the National Electricity Rules, TasNetworks as the DNSP will continue to be a MC (and MP/Meter Data Provider (**MDP**)) for existing type 6 meters on our network.

TasNetworks has made a commercial decision not to remain in the type 1-4 distribution meter market. It has become clear through discussions with Aurora Energy that they would like TasNetworks to remain as the MP for the existing type 1-4 meters connected to the distribution network. TasNetworks still intends to remove itself from this market however is seeking a waiver to transition out of this role over a longer period. This is purely to allow Aurora to fully implement its strategy for these meters over the next 2 years.

It is TasNetworks' intention that a number of restrictions will be contractually applied between relevant parties. This is to provide certainty to all participants that TasNetworks is only performing a temporary role for legacy meters. TasNetworks will restrict the services it provides from December 1 2017 to our type 1-4 distribution meters. For example, the following scenarios would trigger an end to TasNetworks' transitional MP role for individual sites:

- Communications fault
- Meter fault
- Retail contract ends or is renewed with customer
- Meter test required
- MC engages a different/new MDP.

TasNetworks considers that by only being the MP, and not providing the above associated services, this is likely to support better competition or innovation for metering technology in Tasmania.

a) The obligation in respect of which the DNSP is applying for a waiver

TasNetworks is seeking a waiver in respect to the obligations under the functional separation provisions for all type 1-4 distribution meters that TasNetworks is the MP for as at 1 December 2017. Specifically, TasNetworks is seeking a waiver for the following provisions:

Chapter 4 – Functional Separation

Under clause 4.2.5 of the guideline, TasNetworks is applying for a waiver of all obligations under - 4.2 including:

4.2.1 Physical separation/co-location

4.2.2 Staff sharing

4.2.3 Branding and cross-promotion

4.2.4 Office and staff registers

Additionally, under clause 4.4.2 of the guideline we are seeking a waiver from the following obligation:

4.4.1(a) Conduct of Service Providers

b) The reasons why the DNSP is applying for the waiver

TasNetworks is seeking a temporary waiver to continue to be the MP for approximately 3,000 type 1-4 legacy distribution meters. This will provide additional time for TasNetworks, in conjunction with Aurora Energy, to transition these meters over to a new MP under the Power of Choice reforms.

c) Details of the service, or services, in relation to which the DNSP is applying for the waiver

TasNetworks is seeking to continue to be the MP for the existing type 1-4 distribution meters currently provided to customers connected to the distribution network.

d) The proposed commencement date and expiry date (if any) of the waiver and the reason for those dates.

1 January 2018 – 1 July 2019

These dates will allow TasNetworks to make alternative arrangements for these existing meters without adding unnecessary pressure on Aurora Energy to replace these meters in a narrow timeframe.

e) Details of the costs associated with the DNSP complying with the obligation if the waiver of the obligation was refused.

The costs of complying with the guideline in respect of providing type 1-4 distribution meters would essentially fall onto Retailers and their customers. Should the Retailer or customer go to market for replacement of these meters before 1 January 2018, the ability to source a deal on favourable terms would diminish.

f) The regulatory control periods(s) to which the waiver would apply.

2017-2019 (part thereof)

g) Any additional measures the DNSP proposes to undertake if the waiver were granted.

- TasNetworks will cooperate with Aurora Energy to exit the type 1-4 meter space prior to the end of the waiver period. TasNetworks will also commit to not being the MP for any new Type 1-4 distribution meters from 1 December 2017.
- TasNetworks will seek to provide training to all staff (set out further below) that would be providing these services, prior to the implementation of the guideline.

h) The reasons why the DNSP considers the waiver should be granted with reference to the matters specified in clause 5.3.2 (a) including the benefits, or likely benefits, of the grant of the waiver to electricity consumers.

Should TasNetworks have to comply with the ring fencing guideline and functionally separate existing type 1-4 meters, it is likely that we would choose to exit the market as of December 2017. TasNetworks has done a considerable amount of work around the costs and benefits of our future role in the metering market. Based on this work, TasNetworks will not actively pursue opportunities (either as a DNSP or through an affiliated entity) in the type 1-4 meter space, and we intend to transition out of the type 1-4 meters.

As TasNetworks transitions out, for those customers who have a type 1-4 meter provided by TasNetworks, it is likely they would need to find an alternative MP. Given time constraints and the focus of the major retailer in Tasmania, if TasNetworks exited the market as of December 2017 this is likely to cause significant inconvenience and an increase in costs for customers who use the 3000 type 1-4 distribution meters. These customers would benefit from a gradual transition over to a new MC by July 2019.

TasNetworks will use internal training to ensure that those staff members who work across regulated and unregulated metering do not engage in behaviour that may be discriminatory. We will use the CAM to ensure that cross subsidisation does not occur. This concern is also mitigated by our commitment to not become the MP for any new Type 1-4 distribution meters from 1 December 2017.

3. No Action Letter

3.1. No Action Letter

The final component of TasNetworks' compliance strategy is to seek a no action letter in relation to the provisions of 4.3.2 and 4.3.3 of the guideline.

These clauses require TasNetworks to:

- Keep confidential information confidential;
- Only use the confidential information for the purpose for which it was acquired; and
- Not disclose confidential information to anyone, subject to the requirements of the section.

TasNetworks' reading of these clauses is that this requires information to also be kept confidential from a related entity not providing 'Contestable Electricity Services'.

TasNetworks is committed to complying with the intention of these provisions. TasNetworks believes there is a risk of a technical breach of these clauses due to the utilisation of shared IT systems between TasNetworks and its new legal entity (being established to comply with the guideline).

The no action letter is sought on the basis of the potential breach being technical in nature and of minimal consequence given the nature of the services conducted by the new legal entity.

As previously indicated in this plan, the new legal entity will not contain Contestable Electricity Services. Rather, the entity will be focused on TasNetworks' External Telecommunications, Data Centre, IT services and Bass Strait Islands O&M support currently undertaken within the DNSP. TasNetworks accepts that should the new legal entity begin to provide Contestable Electricity Services then the no action letter would cease to apply and the business would need to take the appropriate steps to ensure that confidential information is retained purely within the DNSP.

3.2. Background to request

Following the merger of Aurora Energy and Transend, TasNetworks has invested significant funds to roll out SAP across the current business to create a single way of working for the business. TasNetworks also utilises a shared internal intranet across all functions. Given recent expenditure to establish these systems, TasNetworks does not believe duplicating aspects of this expenditure to avoid this technical guideline breach is prudent. This is particularly so given the consequence (in relation to the harms the guideline is trying to address) of information being shared across the two entities is low.

TasNetworks is committed to having in place the appropriate controls to ensure that confidential information is handled in a correct manner when dealing with external parties (as is currently the case). The no action letter will only be applicable for information flows between the DNSP and the newly established entity (an entity not providing Contestable Electricity Services).

3.3. Content of the no action letter

TasNetworks would appreciate the opportunity to discuss with the AER the specifics of the requested no action letter, including reviewing a draft of the letter prior to its finalisation to ensure the wording reflects the nature of the request.