



Tasmania

RETAIL COMPETITION IN THE TASMANIAN ELECTRICITY SUPPLY INDUSTRY

INFORMATION PAPER

March 2004

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ISBN 0 7246 5009 1

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EXECUTIVE SUMMARY

This Information Paper provides an outline of the policy framework developed to support the introduction of retail competition in Tasmania's electricity supply industry.

Tasmania will, in conjunction with the completion of Basslink, become a participating jurisdiction in the National Electricity Market (NEM). This will introduce a contestable market in energy at the generation level, which will be progressively supported by the introduction of retail competition.

Retail competition will be progressively phased in for classes of 'contestable' customers, commencing in July 2006 for those customers using more than 20 GWh a year (typically with an electricity bill of more than \$1 million). These contestable customers will be followed a year later by businesses using more than 4GWh a year (typically with a bill of \$250 000). Businesses using more than 0.75 GWh a year will become contestable customers in July 2008, followed by those businesses using more than 0.15 GWh a year a year later. The contestability of the final class of residential and small business customers (by far the most numerous being about 250,000), will be subject to review in 2009 by the Government based on an assessment of the public benefit in light of the experience of the NEM to that time.

TASMANIAN RETAIL CONTESTABILITY TIMETABLE SUMMARY

Date	Power Consumption (GWh/yr)	Approx no of eligible installations as at 30/06/2003
1 July 2006	Above 20 GWh/yr	19
1 July 2007	Above 4 GWh/yr	41
1 July 2008	Above 0.75 GWh/yr	293
1 July 2009	Above 0.15 GWh/yr	1 233
1 July 2010	Under 0.15 GWh/yr	244 000

The 'contestable' customers provide the basis for new entry by retailers. These customers can participate in the wholesale market operated by NEMMCO. More likely, based on the experience of the market to date, they will consider the offerings of competing retailers, and either stay with the incumbent retailer (Aurora) or negotiate a retail contract with a competing (licensed) retailer. Negotiated contracts will progressively replace regulated tariffs, but 'non-contestable' customers will retain the security of regulated tariffs established by the independent Energy Regulator.

It should be noted that the network businesses (transmission and distribution) which together account for about 45 per cent of the final delivered electricity price, will continue to be regulated as 'natural monopolies'. It is also the network businesses which most directly influence the reliability of supply. The Energy Regulator will continue to establish reliability standards. It is in generation (energy) and retailing that competition will be most evident, although there are other related services which will also be contestable.

The key elements of the retail contestability framework can be summarised as follows:

TIMING

- retail contestability will be phased in over a four year period, commencing in July 2006, some six months after Basslink is commissioned and in service;
- the Government has reserved a final decision on whether contestability should be extended to the final tranche of customers (households and small businesses) until an assessment is made of the costs and benefits of extending competition to this customer class.

CUSTOMER CLASSIFICATION AND AGGREGATION

- for the purposes of retail contestability, contestable customers will be determined on the basis of annual electricity consumption in the twelve months prior to assessment or on the basis of estimates of electricity consumption where customers can establish future consumption levels in line with defined criteria;
- customers will be given the right to "appeal" their contestability status to the Tasmanian Energy Regulator, who will undertake an independent assessment and make a binding determination;
- aggregation of customer loads will be consistent with the arrangements which currently apply.

CUSTOMER SUPPLY MODEL AND CONTRACTING

- a contestable customer will have the choice of entering into a new retail contract with either Aurora or another retailer or to purchase electricity through the wholesale market;
- the customer contracting and supply model will not be mandated and it will be open for customers and retailers to agree a contract dealing with both the sale of electricity and the delivery (distribution) of that electricity to the premises, or where appropriate negotiate separate retail and distribution contracts;
- a deemed distribution contract, approved by the Energy Regulator, will apply to all contestable customers who are connected to the distribution network and who do not otherwise have appropriate distribution arrangements.

CUSTOMER PROTECTION AND TRANSITION

- as they become contestable, tariff customers may remain on their existing tariff arrangements for a maximum of 12 months;
- all retailers will be required to maintain base levels of consumer protection, prescribed by the Regulator, in their retail contracts;
- retail contracts may contain provisions to rollover the existing supply arrangements at the end of the contract if a replacement contract is not put in place;

- a Deemed Fallback Contract will apply to cover a situation where a customer is taking supply at a connection point for which a retailer is financially responsible but where there is no contract or tariff covering that supply;
- on the introduction of retail contestability, a Retailer of Last Resort (RoLR) scheme will be introduced to protect customers in the event of an unplanned exit by a retailer. Aurora Distribution will be the designated RoLR;
- distribution charges will continue to be regulated.

PROMOTING COMPETITION

- Aurora Retail will be required to advise customers of their impending contestability status.

LICENSING AND ON-SELLING

- a retail licence will be required for each retailer participating in Tasmania and such licences will include a range of conditions designed to protect customers and, to the appropriate extent, those conditions will be similar to the retail licence requirements in other NEM jurisdictions;
- following the introduction of retail contestability, the on-selling of electricity will be permitted to the extent currently provided for in the *Electricity Supply Industry Regulations 1996*.

BASS STRAIT ISLANDS

- contestability will not apply to King and Flinders Islands, with Island customers to remain on tariffs supported by the Government's Community Service Obligation arrangements.

FEEDBACK

In addition to outlining the policy framework which will support the introduction of retail competition in Tasmania, this Paper provides an opportunity for interested parties to comment on certain issues arising from the implementation of the framework, particularly in relation to:

- the Customer, Retailer and Distribution models in the Tasmanian electricity supply industry;
- whether retailers should be required to offer to enter into contracts with customers on standard terms approved by the Energy Regulator; and
- whether the deemed fallback contract should be put in place between:
 - the customer and the incumbent retailer; or
 - the customer and the last retailer to have supplied the customer at the relevant premises; and
- whether the proposed pricing structure for the Deemed Fallback Contract is appropriate.

1 INTRODUCTION

1.1 BACKGROUND

Tasmania has made a decision to join the National Electricity Market (NEM) in conjunction with the Basslink project. The Basslink project and NEM entry will bring a range of benefits to the Tasmanian economy and community. As part of its NEM entry arrangements, the Government has given a commitment to introduce competition within the Tasmanian electricity retail sector. Retail competition will give Tasmanian electricity customers the opportunity to choose the electricity supplier who offers the price and service which best suits their needs.

This is a fundamental shift from the present structure of the electricity supply industry based on the disaggregated Hydro-Electric Corporation (HEC) which was, until July 1998, a vertically integrated monopoly at all levels of the industry. While the HEC has been disaggregated with significant gains to stakeholders in terms of efficiency and accountability, the various sectors of generation, transmission, distribution and retailing have remained as effective monopolies in the absence of a market.

Retail contestability will be progressively introduced to customer classes and will commence in July 2006 approximately six months after Basslink has been commissioned and is in commercial service. This will be approximately 12 months after the State has joined the NEM. In a manner similar to that which occurred in other NEM jurisdictions, the introduction of retail competition in Tasmania will be phased in to ensure a smooth transition to a competitive retail market. Competition will initially be introduced for larger customers and phased-in for other customers over a four year period. The Government has reserved a final decision on whether contestability should be extended to the final tranche of customers (households and small businesses) until an assessment is made of the costs and benefits of extending competition to this customer class.

1.2 PURPOSE OF THIS PAPER

The purpose of this Information Paper is to:

- outline the policy framework and structural arrangements which will support the introduction of retail competition in Tasmania;
- examine some of the issues underpinning the framework; and
- provide interested parties with the opportunity to comment on certain issues arising from the implementation of the framework.

The Paper is primarily targeted at those businesses affected by the first three tranches of contestability as detailed in table 3.1. Detailed information regarding the extension of contestability to the final tranche of customers (households and small businesses) and the associated cost benefit analysis will be provided closer to the anticipated roll-out of that tranche.

1.3 THE TASMANIAN GOVERNMENT'S ENERGY REFORM FRAMEWORK

The Government's energy reform framework comprises a number of interdependent elements that underpin the development of Basslink, enable the State to participate in the NEM, facilitate the introduction of natural gas to the State and allow Tasmania to develop its high quality wind energy resources.

Key elements of the reform framework include:

- the interconnection of Victoria and Tasmania via Basslink;
- the creation of additional generation competition in the Tasmanian market through the conversion of the Bell Bay Power Station to gas (from oil) and its separation from Hydro Tasmania to a new State-owned generation business as well as through the import of electricity via Basslink from interstate generators;
- encouraging the development of competing wind power projects;
- Tasmania becoming a participating jurisdiction in the NEM, the National Electricity Law and the National Electricity Code (the key instruments which govern the national electricity market) applying in Tasmania;
- retail contestability being phased-in over a period after Basslink has been commissioned;
- a vesting contract between Hydro Tasmania and Aurora Energy to underpin energy sales to non-contestable customers during the rollout of retail contestability;
- arrangements to be implemented dealing with how Basslink will be bid into the NEM and the framework under which Hydro Tasmania will make available for commercial sale inter-regional revenues arising from southward flows on Basslink;
- the ACCC having responsibility for transmission pricing, initially under Tasmanian arrangements and then under the NEC;
- the Tasmanian Energy Regulator retaining responsibility for distribution network pricing on an on-going basis and retail price regulation for non-contestable customers; and
- Tasmanian derogations (i.e. amendments) to the NEC providing for technical, procedural and administrative issues in the transition to the full electricity market arrangements.

Further details on the reform package can be found in the information paper *Meeting Tasmania's Energy Needs for the 21st Century: A Competitive Future* prepared by the Department of Treasury and Finance dated November 2000 and the Australian Competition and Consumer Commission's *Determination for Tasmanian Derogation and Vesting Contract* dated November 2001.

The Government's energy reform initiatives are on track and will deliver significant public benefits to Tasmania and the NEM more widely. These benefits include:

- a reliable and flexible additional electricity supply source to meet the State's changing electricity needs at a competitive cost;
- sustainable competition in retail supply by encouraging new market entrants in retailing and diversity of supply;
- security of supply for Tasmania in the event of drought or major energy infrastructure failure;
- a robust framework for new investment in the Tasmanian energy supply industry;
- capturing the synergies available from interconnecting the State's energy constrained hydro system with the capacity constrained, largely thermal mainland system, both in terms of improving security of supply and electricity prices;
- an additional cost-effective source of electricity to meet peak demand requirements in the Victorian region of the NEM, identified by NEMMCO as a critical need in its Statement of Opportunities and other documents;
- the development of Tasmania's wind resource and thereby assistance to Australia in meeting its international greenhouse gas commitments; and
- significant economic benefits to Tasmanian, Victorian and the national economies.

1.4 RETAIL COMPETITION OBJECTIVES

The introduction of retail contestability and consumer choice will represent a fundamental change for the industry and its customers alike. The Government has adopted a number of objectives in developing the retail contestability arrangements, including:

- providing eligible customers with the freedom to choose their preferred supplier of electricity and to promote a competitive retail market in Tasmania;
- ensuring that contestability is introduced in an orderly way and allows sufficient time for customers and Tasmania's electricity entities to adjust to the new market conditions;
- ensuring that Aurora Energy is placed on a level playing field with potential new entrants and not exposed to competitive advantages or disadvantages in a contestable retail market;
- ensuring a high level and quality of service for all customers; and
- ensuring economic protection for customers who are not able to obtain competitive supply and to protect consumers in cases where a retailer unexpectedly exits the industry.

These objectives have been used as a basis for assessing the most appropriate policy and structural framework to support the introduction of retail competition.

2 INSTITUTIONAL FRAMEWORK

2.1 OVERVIEW OF THE ELECTRICITY SUPPLY ACT 1995

The *Electricity Supply Act 1995* (ESI Act) provides the underlying regulatory arrangements for the industry in terms of customer protection, promotion of competition, technical regulation, industry performance standards and reporting, and more recently has been amended to support the policy decisions for the introduction of retail competition.¹

The basic regulatory framework remains the same as at present with an independent Energy Regulator issuing licences for regulated operations, including retailing. This licensing addresses certain requirements such as technical and financial competence and standing, and commercial integrity.

The licences also bind the entities to relevant codes and guidelines specified by the Energy Regulator.

2.2 PROVISIONS RELEVANT TO RETAIL MARKET

The amendments to the ESI Act give effect to the policy decisions underpinning the introduction of contestability in Tasmania.² The general approach has been to provide a head of power in respect of the various policy decisions which then supports the making of detailed regulations or other instruments.

In respect of retail competition, the amendments provide that Aurora Energy will have a continuing obligation as the exclusive retail franchisee holder to supply non-contestable customers at a regulated tariff.

Customer protection includes a detailed regulation making power to establish a 'retailer of last resort' (RoLR). The purpose of this is to ensure that contestable customers are protected from the effect of the unanticipated exit from the market of their contracted retailer.

The ESI Act also provides that newly contestable customers shall have a 'grace period' of 12 months where they may remain on the existing tariff supply agreement. This provides a transitional period for those customers who have not negotiated or taken up an offer to supply either from the incumbent retailer (Aurora) or some competitive retailer.

2.3 RETAIL LICENCES AND CODE

A principal regulatory mechanism is the licensing power of the Energy Regulator. There are certain minimum statutory licensing conditions, (eg financial and technical soundness as well as commercial integrity). The NEM also has ongoing prudential management for retailers through the market settlement arrangements.

The licences issued by the Energy Regulator bind the relevant entity to the *Tasmanian Electricity Code* (TEC). The TEC supplements the NEC which does not deal fully with distribution or retail performance

¹ Electricity Supply Industry Amendment Act 2003

² These amendments will be progressively proclaimed in accordance with the requirements of NEM entry and the introduction of contestability. Interested parties should go to the ESI Amendment Act 2003 rather than the ESI Act as proclaimed.

standards. The introduction of retail contestability will provide a focus on the integrity of marketing performance. Customers need to have relevant and fairly presented marketing information to ensure that any transfer to another retailer is with appropriately informed consent of the customer.

Generally it is expected that retailers will bring with them the standards and experience from the NEM. This will include business systems which reflect marketing codes in other jurisdictions. The Energy Regulator will monitor the development of the market with the assistance of the Customer Consultative Committee which has been established by the Minister for Energy. This Committee will advise the Energy Regulator on any intervention which may be needed in respect of marketing. It should be noted that the Electricity Ombudsman will continue to oversight and where necessary determine disputes between the electricity entities and customers. The Energy Regulator has a Memorandum of Understanding to exchange relevant information, including the identification of any systemic market issues. The Director of Consumer Affairs also has a role in such matters.

2.4 ROLE OF ENERGY REGULATOR

The Energy Regulator will continue as an independent authority with additional responsibilities relating to the introduction of retail contestability as well as competition in other sectors of the electricity supply industry.

In the context of retail contestability, the Energy Regulator may attach conditions to any licence issued, and is responsible for maintaining the TEC to which all electricity entities are bound. Maintaining the TEC includes reviewing it to ensure it matches the requirements of customers and the market as it develops.

3 KEY ISSUES AFFECTING THE INTRODUCTION OF RETAIL COMPETITION

3.1 THE CONTESTABILITY TIMETABLE

The Government will introduce retail competition in a phased and orderly way to ensure a smooth transition to a competitive electricity market in Tasmania. The contestability timetable extends over a four-year period, as detailed in Table 3.1.

TABLE 3.1: TASMANIAN RETAIL CONTESTABILITY TIMETABLE

Date ³	Power Consumption (GWh/yr)	Approx no of eligible installations as at 30/06/2003	Annual bill likely to exceed (approx)	Indicative type of customers
1 July 2006	> 20 GWh/yr	19	\$1 000 000 +	Mineral processors/heavy manufacturing plant
1 July 2007	> 4 GWh/yr	41	\$250 000 +	Food processing plant and multi story office complexes
1 July 2008	> 0.75 GWh/yr	293	\$75 000 +	Supermarket, engineering workshop and smaller commercial complexes
1 July 2009	> 0.15 GWh/yr	1 233	\$16 000 +	Fast food restaurant, service station and large offices
1 July 2010 ⁴	Under 0.15 GWh/yr	244 000	-	Small businesses and households

The Government considers it appropriate that there be a period of market history in Tasmania prior to the commencement of the retail contestability timetable. Therefore, the retail contestability timetable will commence around 12 months after the commencement of NEM arrangements in Tasmania (May 2005) and six months after Basslink is commissioned and in service (November 2005).

3.2 CONTESTABILITY CRITERIA

Retail competition in Tasmania will be phased-in on the basis of defined contestability limits determined by energy consumption, measured in gigawatt hours per year (GWh/yr). Generally, customers will be classified according to their annual electricity consumption in the 12 months prior to the assessment. However, there will also be provisions to cover new customers and customers whose load may be growing, to enable future annual electricity consumption to be considered, where appropriate evidence can be provided.

³ Actual dates are subject to completion of Basslink. This table has been prepared on the basis that Basslink will enter commercial service in late 2005.

⁴ The State has, however, reserved a decision on whether contestability should be extended to the final tranche of customers (small commercials and households) until an assessment is made of the costs and benefits of extending competition to this customer class.

It is expected that achieving contestable status will be an important consideration for some customers. As such, a formal 'appeal' mechanism will be implemented to quickly resolve issues in relation to customers' contestability status. Customers will be able to seek a review of their contestability status from the Energy Regulator.

The experience in other jurisdictions is that in practice reviews are rare, as there is freedom to contract outside the tariff in any case, and any customer should be able to negotiate a competitive tariff.

The concept of aggregation refers to an electricity customer adding together electricity consumption at a number of sites in order to reach a particular contestability limit.

Aggregation will only be allowed in Tasmania where an entity, due to the nature of the business undertaken, requires several connection points at a "single" location. Aggregation is currently permitted in Tasmania on this basis.

For example, the University of Tasmania is able to aggregate its electricity consumption through the connection points on the Sandy Bay Campus, some of which are separated by a road. However, the University would not be able to add to this aggregation its electricity consumption at the Hobart Arts School or the Northern Campus at Launceston, as these are separate geographical locations.

3.3 OVERALL CONTRACTUAL FRAMEWORK

In developing an overall contractual framework for the introduction of retail competition, key considerations have included:

- the need to ensure that the proposed arrangements are sufficiently flexible to allow the benefits of competition to be realised;
- an appropriate level of consumer protection is maintained as contestability is progressively phased in - contestable customers in the first tranches of contestability should generally be capable of looking after their own interests;
- the importance of ensuring that there is a clear legal and contractual relationship between the customer and the retailer, and the customer and the distributor – customers may wish to change retailers while their distributor remains the same; and
- regard to the retail competition arrangements that have been introduced in other NEM jurisdictions and the desirability of uniformity in this regard.

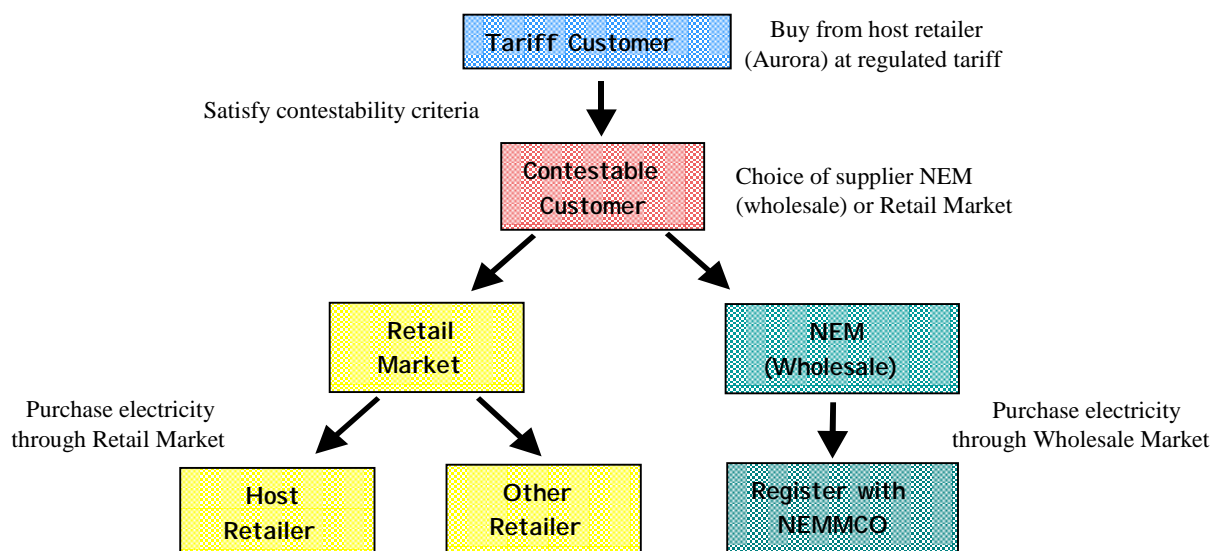
It should also be noted that these arrangements will not apply to customers connected directly to the transmission system. Such customers will have to negotiate a connection agreement directly with Transend.

3.3.1 CONTESTABLE CUSTOMER CHOICES

The NEM is about choice and flexibility. When a customer becomes a contestable customer they will be able to choose to buy the electricity supplied to the relevant premises from one of several competing retailers or directly through the wholesale market. If a customer decides to purchase directly from the wholesale market, they will need to register with NEMMCO as a Market Customer (see section 3.3.2).

Figure 3.1 depicts the options available to a tariff customer on becoming contestable. Appendix 1 outlines these options in more detail.

FIGURE 3.1: CUSTOMER CHOICES OF SUPPLIER



When a tariff customer becomes contestable they will be provided with a 12 month grace period to negotiate new supply arrangements while ensuring that supply is maintained. During this period customers will continue to be supplied by Aurora under a regulated tariff. The grace period commences on the day the customer becomes contestable and ends on the earlier of the following:

- the customer enters into a retail contract, with either Aurora or a new retailer; or
- the 12 month period expires.

In the event that a contestable customer enters a retail contract and that contract ends prior to the expiry of the grace period, the customer is not entitled to move back on to the regulated tariff. In addition, it is important to note that the grace period provisions only apply to a customer being supplied on the basis of a tariff at the time they become contestable.

Where a customer was being supplied by Aurora under a negotiated contract and that contract expires or is terminated before that customer meets the contestability criteria, that customer may again be supplied under a tariff.

It is envisaged that almost all contestable customers will be supplied with electricity under a retail contract which they enter into with a retailer. There will be two types of retail contract available to a contestable customer, a *Standard Customer Retail Contract* and a *Negotiated Contract*.

The *Standard Customer Retail Contract* is intended to be the base level contract for retail competition. Any retailer may publish and offer to enter into a standard contract with contestable customers. If a contestable customer is satisfied with the terms of the *Standard Customer Retail Contract* offered by a

retailer and the price offered, they will enter into a contract with the retailer on those terms and at that price.

Negotiated Contracts, on the other hand, allow retailers and contestable customers to negotiate not only the price, but also the other terms of the contract under which the customer is supplied. Retailers are not obliged to offer to enter into Negotiated Contracts.

The TEC will require retailers, in their retail contracts, to comply with certain measures designed to protect consumers. These measures will apply to *Standard Customer Retail Contracts* and *Negotiated Contracts*. The consumer protection measures outlined in the TEC will be reviewed again prior to the introduction of full retail contestability and may be more stringent for smaller customers than for larger customers.

It is envisaged that both the *Standard Customer Sale Contract* and the *Negotiated Contract* will contain provisions to rollover the existing supply arrangements at the end of the contract if a replacement contract is not put in place. This will maintain continuity of supply for the customer and ensure that a contractual relationship continues to exist between the retailer and the customer.

A number of industrial customers have existing contractual arrangements. These contracts will not be affected by the roll-out of retail contestability. If at the end of an existing contract, the customer meets the contestability criteria, it will face the choices outlined above.

Comments are sought on whether retailers should be **required** to offer to enter into contracts with customers on standard terms approved by the Energy Regulator. If so, should this obligation apply in the case of all contestable customers, or only those customers who become contestable in a particular tranche of the contestability timetable (eg, those falling into the last tranche or last two tranches?)

3.3.2 FALLBACK ARRANGEMENTS

There will be fallback arrangements to cover a situation where a customer is taking supply at a connection point for which a retailer is financially responsible but there is no retail contract or tariff covering that supply. A *Deemed Fallback Contract* will apply in this situation and will provide the retailer and distributor with an alternative to disconnection while enabling the costs associated with supplying electricity to be recouped.

A *Deemed Fallback Contract* may arise in the following example situations:

- a tariff customer becomes contestable, and the 12 month grace period expires without the customer entering into a retail contract with a retailer;
- a contract customer's retail contract comes to an end, the contract does not contain a rollover provision, the customer fails to enter into a retail contract with a retailer and the contestable customer is not disconnected under the terms of the original retail contract;
- a new contestable customer takes over premises from another party and fails to enter into a retail contract with a retailer. This could be because of oversight (eg, the other party fails to notify its retailer) or because the customer is not able to negotiate terms it considers appropriate; and

- a retailer terminates a retail contract with a contestable customer in accordance with its terms (for example, because the customer fails to pay), but for some reason the customer's premises are not disconnected.

The contractual relationship between the customer and the retailer which supplied the customer immediately before the incident which resulted in the customer not otherwise having a contract will be created, or deemed, by regulations made under the ESI Act.

The *Deemed Fallback Contract* will be a standard set of terms and conditions to be proposed by the retailer and approved by the Energy Regulator. The price charged by a retailer under a *Deemed Fallback Contract* will also be regulated. For a large customer, the price will be the regulated network price plus the spot price plus a retail margin proposed by the retailer and approved by the Energy Regulator. For a small customer, the price will be determined by reference to a schedule proposed by the retailer and approved by the Energy Regulator.

The retailer will have an obligation to advise contestable customers that a *Deemed Fallback Contract* is in place and of other contract options, including entering into a *Standard Customer Retail Contract* or a *Negotiated Retail Contract*.

It should be noted that a *Deemed Fallback Contract* will not apply to a customer who takes supply directly from the transmission network.

Comments are sought on whether:

- the deemed fallback contract should be put in place between:
 - the customer and the incumbent retailer; or
 - the customer and the last retailer to have supplied the customer at the relevant premises; and
- the proposed pricing structure of the deemed fallback contract is appropriate.

3.3.3 RELATIONSHIP BETWEEN CUSTOMERS, RETAILERS AND THE DISTRIBUTOR

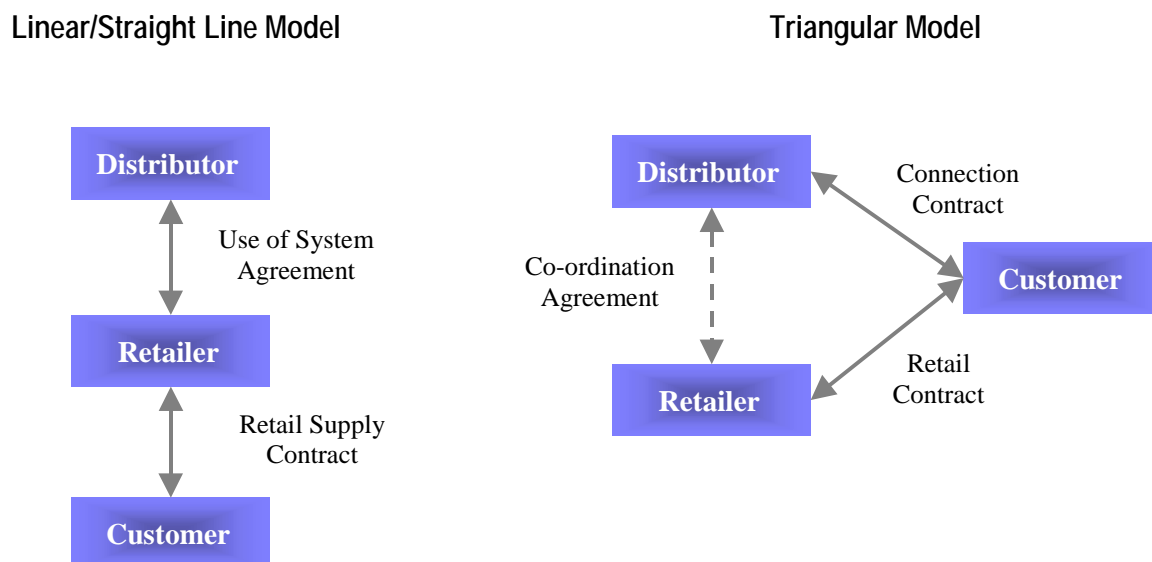
Under the new arrangements:

- the customer's retailer is responsible for selling the electricity consumed at the customer's premises;
- the customer's distributor is responsible for delivering that electricity to the customer's premises.

There are effectively two models to define the relationships between customers, retailers and the distributor.

The first is the linear or straight line model, where the customer has a contractual relationship with the retailer only. The second is the triangular model, which involves the customer having a direct contractual relationship with both the retailer and distributor. The models are shown diagrammatically in figure 3.2.

FIGURE 3.2: CUSTOMER/DISTRIBUTOR/RETAILER MODELS



The linear model has generally been utilised in a retail franchise environment where there is only one retailer and has historically been the option adopted in Tasmania to define relationships between customers, retailers and the distributor.

One of the key weaknesses of this model is that the contractual obligations it applies do not match the actual relationships between customers and market participants. As such, the distributor has little ability to manage its risk. In addition, the linear model is more difficult to manage within a contestable environment where there may be a number of retailers, with customers switching between retail companies.

The triangular model is likely to develop as the arrangement preferred by market participants and customers for customer, retailer, distributor relationships in the Tasmanian electricity supply industry, although it will not be mandated. The triangular model has been adopted in most other jurisdictions in relation to both electricity and gas and is being adopted in the Tasmanian natural gas regulatory framework.

The triangular model provides a better allocation of risk and more accurately reflects the actual relationships between customers and market participants. As the customer will have a contractual relationship with both the distributor and retailer, it will be necessary to require the distributor and retailer to enter into arrangements for the retailer to act as an agent for the distributor in relation to some functions. This is referred to as the Coordination Agreement in the diagram above. The Coordination Agreement ensures that, unless the customer elects to deal with the distributor directly (as may be the case for some larger customers), customers will only deal with one party, the retailer. This approach ensures a simple and efficient customer interaction regime and avoids outcomes such as separate contractual negotiations and billing, unless the customer actively elects to negotiate directly with the distributor.

In addition, the distributor will be required to prepare a standard connection (or distribution) agreement to be made available to all customers. The terms and conditions of this standard connection agreement would apply to all customers unless different distribution arrangements are specifically negotiated. Where there is no negotiated distribution contract, a contractual relationship on the terms of the standard agreement will be deemed to exist by legislation.

Comments are sought on customer, retailer and distributor models in the Tasmanian electricity supply industry.

3.3.4 PARTICIPATION IN THE WHOLESALE MARKET

A contestable customer may participate directly as a wholesale customer in the NEM. Customers wishing to pursue this option must register with NEMMCO as a market customer and purchase electricity through the wholesale market. Market customers are required to meet NEMMCO's prudential and metering requirements. In addition, market customers must establish settlement systems that link into NEMMCO's systems and settle with NEMMCO on a weekly basis.

Because of the volatility of the pool price, market customers will generally enter into hedging contracts with other market participants and purchase other risk management products.

3.4 RETAIL ELECTRICITY PRICES

The price which Tasmanians pay for electricity is made up of a number of cost components, including: transport charges for use of the transmission and distribution networks, the costs of purchasing energy and ancillary services from generators and charges to cover the retailer's overheads, including a small profit margin.

Currently, all components of retail electricity prices are regulated, although with the forthcoming transition towards the State's participation in the NEM and the roll-out of retail contestability, this will begin to change. These changes are shown in the following table.

FIGURE 3.3 – COMPONENTS OF RETAIL ELECTRICITY PRICES

Currently (Tariff Customers)		Following Retail Competition (Contestable Customers)
Gross retail margin for tariff customers set by Energy Regulator, with tariff charges subject to side constraints set by Energy Regulator.	Retail Prices	Delivered prices are negotiable between customers and retailers.
Wholesale energy price for tariff customers reflects a physical vesting contract between Hydro Tasmania and Aurora approved by the ACCC.	Energy and Purchase Costs	Wholesale energy prices will be set by the competitive market reflecting the net impact of spot market purchases and hedging contracts.
System controller and ancillary service costs overseen by Energy Regulator.	Transmission Costs	Other charges such as NEMMCO fees and ancillary service costs apply.
Revenue cap set by the ACCC covering all customers. Charges determined by Transend in accordance with the TEC.	Distribution Costs	Revenue cap set by the ACCC covering all customers. Charges determined by Transend in accordance with the NEC.
Maximum allowable revenue cap set by Energy Regulator. Charges determined by Aurora in accordance with the TEC and subject to oversight by Energy Regulator.		Maximum allowable revenue cap set by Energy Regulator. Charges determined by Aurora in accordance with the NEC and subject to oversight by Energy Regulator.

3.5 INFORMATION DISCLOSURE

Aurora Energy will be required to advise customers of their impending contestability status. The Energy Regulator will issue a written direction outlining the information which Aurora must provide, together with the timeframes and manner for providing the notification. The Energy Regulator will publish and regularly update a list of the retailers licensed to operate in the Tasmanian electricity supply industry.

3.6 RETAILER OF LAST RESORT

Under NEM arrangements, when a retailer fails to pay for electricity it purchases through the wholesale market (amongst other things), the retailer may be suspended by NEMMCO. The practical effect of this may be that it is unable to fulfil its retail contract obligations to customers with supply being terminated through no fault of the customer.

The ESI Act has been amended to provide for the establishment of a RoLR scheme. The detailed supporting arrangements relating to the RoLR scheme will be prescribed by regulations.

Under the RoLR scheme, contestable customers of a suspended retailer will be automatically transferred to the designated RoLR. The RoLR will supply electricity on the basis of a deemed contract, approved by the Energy Regulator, for a maximum period of three months. The RoLR will be required to notify customers of their transfer under the RoLR scheme.

The price charged by the RoLR will be the wholesale pool price and other costs plus a retail margin approved by the Energy Regulator.

Consistent with the position adopted in most other NEM jurisdictions, the RoLR function will be undertaken by Aurora Energy as the distributor during the phasing in of contestability.

Aurora will not be exposed to a net financial or competitive advantage or disadvantage through undertaking the role of the RoLR. Ongoing fixed costs associated with the provision of the RoLR scheme, prior to the scheme being invoked, will be spread across all customers through distribution charges.

3.7 METERING AND RETAILING

Metering is a critical element in the implementation of a market for electricity. This operates at both an inter-entity (wholesale) and customer level. At an inter-entity level, the Energy Regulator has made certain TEC provisions which will support the installation of NEM compliant metering in a cost effective manner for NEM entry.

The initial tranches of contestable customers already have NEM compliant metering in place. This reflects the value in the energy transaction and the customer interest in managing the energy supply contract. As the market develops and the contestability tranches embrace customers with lower consumption levels, there is an obligation on the Energy Regulator in his capacity as 'metrology coordinator' to ensure that appropriate metrology procedures are in place to support the market. The arrangements in the NEM are currently under review and the Energy Regulator is participating in this review, including consultation with interested parties.

The TEC has a detailed Retailing code as Chapter 9. This includes the standards and rules for retail metering, data collection and access. These provisions are already in place and ensure appropriate access to, and integrity of data in a non-contestable retailing environment. These provisions have been satisfactory to date, but it is appropriate to review them and ensure they are consistent with 'best practice' based on the Tasmanian experience to date as well as looking forward to the NEM.

The TEC provides for a customer charter by the franchised retailer. This should continue and, subject to consultation, may be extended to the distributor. There are also provisions in respect of connection, payment options and other retailing and distribution activities which will be reviewed.

3.8 RING FENCING

In Tasmania, Aurora Energy undertakes the dual roles of electricity distribution and retailing. Following the introduction of the contestable market, Aurora Retail should not gain any competitive advantage from the fact that Aurora Energy also undertakes the role of distributor, eg through preferential dealings

or the provision of competitive information from Aurora Distribution to Aurora Retail. There is a degree of ring-fencing already in place within Aurora to separate its two roles for accounting and regulatory purposes.

New entrant retailers will be required to deal with Aurora Distribution in relation to the distribution arrangements for contestable customers.

The Energy Regulator is developing ring fencing guidelines to address the issue of Aurora being both a retailer and distributor in a contestable environment and will undertake an assessment of the underlying issues and consult on the content and nature of such guidelines. These guidelines will be consistent with the relevant provisions of the NEC to ensure that the Tasmanian electricity industry complies with the national market framework..

3.9 ON-SELLING AND RESUPPLY OF ELECTRICITY TO EMBEDDED NETWORK CUSTOMERS

Within the wider distribution network there are smaller 'embedded' distribution networks, eg caravan parks, large commercial sites such as shopping centres or commercial buildings, ports. As the term reflects, on-selling of electricity occurs when a customer purchases electricity from a retailer and then on-sells it to other customers. This on-selling is not considered to be retailing for the purposes of the ESI Act.

This is the arrangement currently provided for by the *Electricity Supply Industry Regulations 1996* and will continue in the NEM.

3.10 TREATMENT OF THE BASS STRAIT ISLANDS

Hydro Tasmania currently owns the generation and network infrastructure on the Bass Strait Islands (King and Flinders Islands) as well as being responsible for retail supply.

The Bass Strait Islands are not part of the interconnected Tasmanian power system and will not be part of the national market when Tasmania is interconnected by Basslink. Hydro Tasmania will have continuing responsibility for supply of electricity on the Bass Strait Islands, including to the extent appropriate, supply supported by the Government through a Community Service Obligation (CSO) arrangement. The majority of customers on the Islands are low consumption customers and fall within the lowest contestability tranche (10 customers out of a total of around 1500 customers are above the 150 MWh limit).

Bass Strait Island customers will have the continuing benefit of a franchised supply and the Energy Regulator is supporting this through the development of a TEC chapter specific to the circumstances of the power systems on the Islands. This code has already been consulted upon and will include performance standards and appropriate reporting requirements, supported by a licence issued by the Energy Regulator.

Thus, electricity customers on the BSI will continue to have the benefit of the ESI Act and regulatory arrangements including the CSO which supports the obligation to supply imposed on Hydro Tasmania through its charter.

4 NEXT STEPS

The transition to a competitive market will involve a number of implementation issues including those that:

- relate to the practical and technical side of implementation (i.e. metering, data collection and settlement);
- are more legislative/regulatory in nature (i.e. contractual relationships and fallback arrangements); and
- relate to the need for a wider range of customer, business and industry involvement in the implementation process.

It is important that customers and industry are aware of the overall timetable for transitioning to a competitive market, well in advance, and have the capacity to provide input to the implementation process and related issues.

This Information Paper provides an opportunity for industry, special interest groups, retailers and customers to provide input into issues arising from the implementation of the framework supporting the introduction of retail competition.

Written comments should be submitted by 31 May 2004 to:

The Secretary
Department of Treasury and Finance
GPO Box 147
HOBART TAS 7000.

Further information in relation to the Information Paper can be obtained by contacting the Energy Market Branch, Department of Treasury and Finance, on (03) 6233 6554.

5 GLOSSARY OF TERMS

5.1 ACRONYMS EXPLAINED

ACCC	Australian Competition and Consumer Commission
BSI	Bass Strait Islands
CSO	Community Service Obligation
ESI Act	Electricity Supply Industry Act 1995
FRC	Full retail competition
GWh	Gigawatt hours
MWh	Megawatt hours
NCC	National Competition Council
NEC	National Electricity Code
NEM	National Electricity Market
NEMMCO	National Electricity Market Management Company Limited
RoLR	Retailer of Last Resort
TEC	Tasmanian Electricity Code
UoSA	Use of System Agreement

5.2 AN EXPLANATION OF TERMS

Aggregation	Electricity customer pooling consumption at a number of metering points in order to meet the contestability criteria.
Contestable customer	Is a customer who is eligible to buy electricity from its host retailer, another retailer or through the wholesale market.
Deemed Fallback Contract	The <i>Deemed Fallback Contract</i> comes into effect when there are no other contractual arrangements in place between a retailer and contestable customer.

ESI Act	The ESI Act provides the underlying regulatory arrangements for the industry in terms of customer protection, promotion of competition, technical regulation, industry performance standards and reporting, and more recently has been amended to support the policy decisions for the introduction of retail competition.
Host Retailer	The Host Retailer is Aurora.
Negotiated Contract	The <i>Negotiated Contract</i> is intended to allow retailers and contestable customers to negotiate not only the price, but also the other terms of the contract under which the customer is supplied with electricity.
Non-contestable customer	Is a customer who may only buy electricity from its host retailer.
Standard Customer Retail Contract	The <i>Standard Customer Retail Contract</i> is intended to be the base level contract for retail competition

6 LIST OF KEY PUBLICATIONS

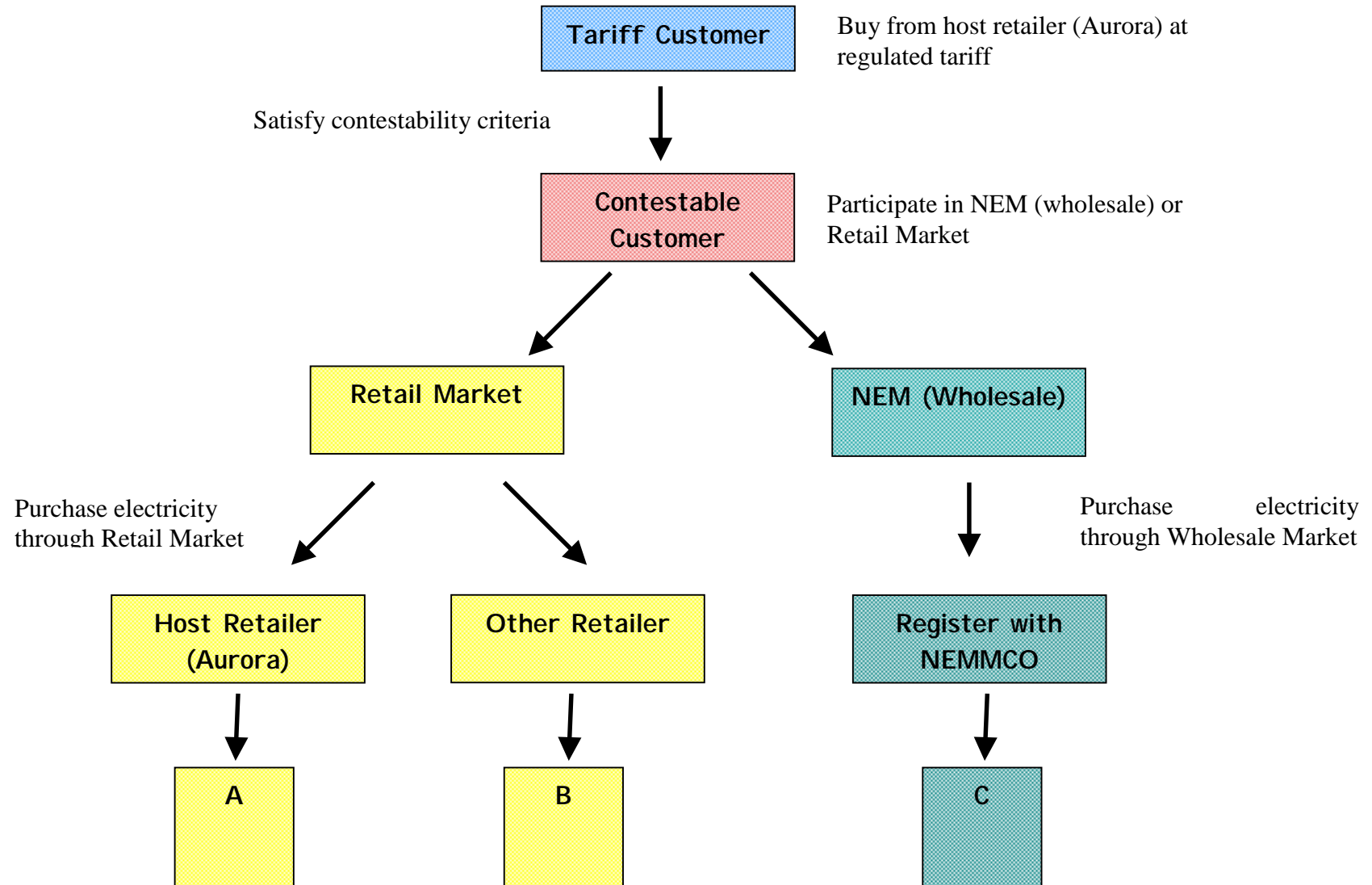
Treasury has published a number of papers dealing with Tasmania's Energy Reform Framework, of which entry to the National Electricity Market and the introduction of retail contestability are key components. These publications, which are listed below, can be found on the Energy Markets page of Treasury's website at www.treasury.tas.gov.au.

- *Meeting Tasmania's Energy Needs for the 21st Century: – A Competitive Future, Information Paper, November 2000.*
- *Authorisation of Tasmania's NEM Entry Arrangements – Enhancements to Tasmania's Energy Reform Framework, June 2001.*
- *Entry to the National Electricity Market – Information Paper, April 2003.*

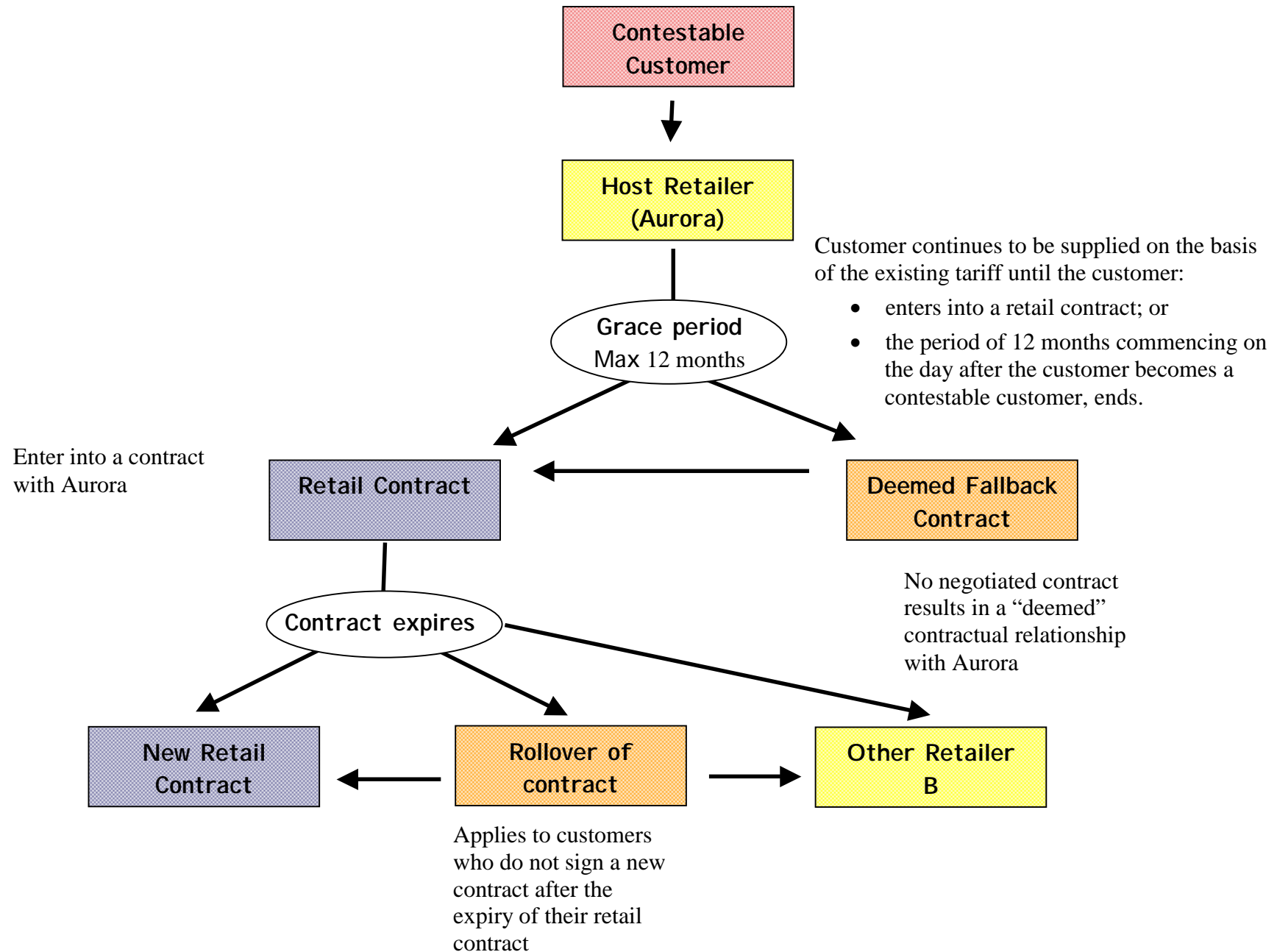
In addition, reference can also be made to the following publication by the Australian Competition and Consumer Commission in relation to Tasmania's entry to the NEM:

- *Determination – Application for Authorisation – Tasmanian Derogations and Vesting Contract, November 2001.*

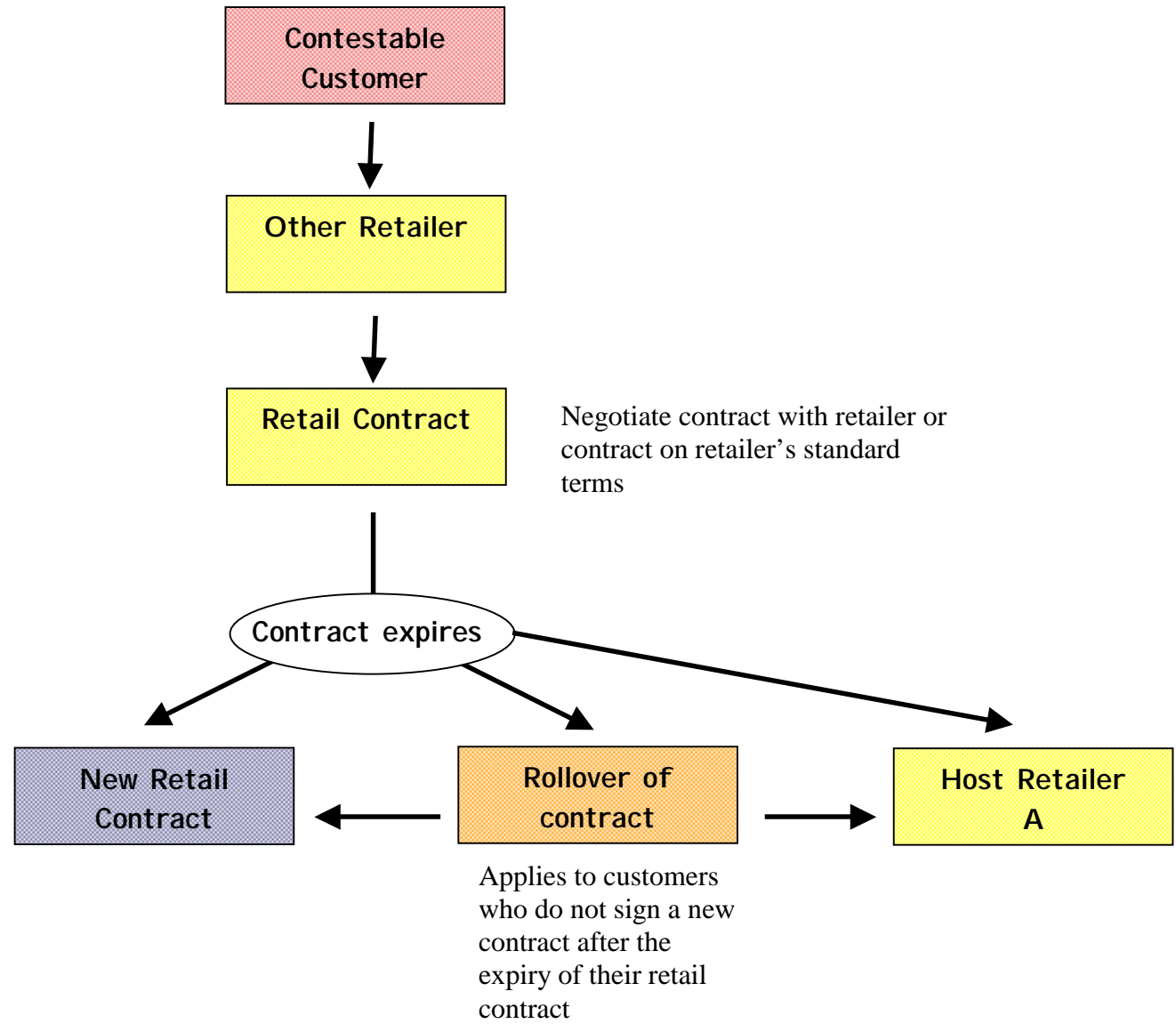
APPENDIX 1 - SUMMARY OF CONTESTABLE ELECTRICITY CUSTOMER CHOICES



A - HOST RETAILER (AURORA)



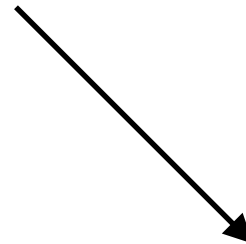
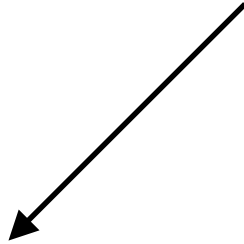
B - OTHER RETAILER



C - NEM (WHOLESALE)

Register with NEMMCO as market customer and purchase electricity through wholesale market

Market customers are required to meet NEMMCO's prudential and metering requirements. Settle electricity purchases with NEMMCO on a weekly basis



Buy from spot market

Accept responsibility to pay spot market prices to NEMMCO for electricity consumed and associated costs

Enter into contract to hedge

Manage the risk of volatile spot market prices by entering into long and short term hedge contracts that set an agreed price for electricity

Monitor market

Monitor market and review consumption requirements. Adjust hedge contract position as required

RETAIL CONTRACTUAL FRAMEWORK - SUMMARY

Almost all contestable customers will be supplied electricity under a retail contract which they enter into with a retailer (either their host retailer, Aurora, or another retailer).

The retail contract will normally be entered into following an approach by the host retailer or another retailer, but the customer may also seek offers from retailers, for example by issuing a request for tender.

The contract is likely to be at an agreed price but otherwise on the retailer's standard terms (called a standard customer retail contract).

In some cases, however, the retailer and the customer may specifically negotiate the terms of the contract (called a negotiated contract). This may be because the customer has special requirements or because the customer wants to "standardise" its electricity purchasing arrangements across more than one jurisdiction.

Standard Customer Retail Contract

The *Standard Customer Retail Contract* is intended to be the base level contract for retail competition. All retailers will be able to provide this form of contract.

If the customer is happy with the terms of the retailer's standard form contract and the price offered, they will enter into a contract with the retailer on those terms and at that price.

Any retailer may offer to enter into a standard contract with contestable customers.

Any retailer may publish a standard contract.

Negotiated Contract

The *Negotiated Contract* is intended to allow retailers and contestable customers to negotiate not only the price, but also the other terms of the contract under which the customer is supplied with electricity. Retailers will not be obliged to offer a negotiated contract.

Generally, terms and conditions may be varied.

Any retailer may offer to enter into a Negotiated Contract.

There is no obligation to publish a Negotiated Contract.

Customer protection

Base levels of consumer protection are required in *Retail Contracts*, and will be prescribed by the *Tasmanian Electricity Code*.

The *Standard Customer Retail Contract* and the *Negotiated Contract* may contain provisions to rollover the existing supply arrangements at the end of the contract term if a replacement contract is not put in place

Deemed Fallback Contract

The *Deemed Fallback Contract* comes into effect when there are no other contractual arrangements in place between a retailer and contestable customer for the sale of electricity and the customer is not participating directly in the wholesale market. Such situations include the following:

- a tariff customer becomes contestable, and the 12 month grace period expires without the customer entering into a retail contract with a retailer;
- a contract customer's negotiated contract comes to an end (either it expires or it is terminated), and the contract customer fails to enter into a retail contract with a retailer (and the contestable customer is not disconnected under the terms of the original retail contract);
- a new contestable customer takes over premises from another party and fails to enter into a retail contract with a retailer. This could be because of oversight (eg, the other party fails to notify its retailer) or because the customer is not able to negotiate terms it considers appropriate;
- a retailer terminates a retail contract with a contestable customer in accordance with its terms (for example, because the customer fails to pay), but for some reason the customer's premises are not disconnected; and
- a customer participating directly in the wholesale market is suspended or ceases to be registered as a market customer under the National Electricity Code, does not enter into a retail contract with a retailer and is not disconnected.

Under a Deemed Fallback Contract:

Terms and conditions may not vary.

The contractual relationship, which will be between the customer and the host retailer (Aurora) will be created, or deemed, by regulations made under the *Electricity Supply Industry Act 1995*. This arrangement will be reviewed as the later tranches of contestability commence.

Aurora must develop or submit for approval to the Regulator deemed fallback contract terms.

There will be an obligation to advise contestable customers that a Deemed Fallback Contract is in place and of other contract options, including a Standard Customer Retail Contract and a Negotiated Retail Contract.

The prices charged by the retailer will be regulated, with the form of regulation depending on the size of the customer, as follows:

- for a large customer, the price will be the regulated network price plus the spot price plus a retail margin proposed by the retailer and approved by the regulator; and
- for a small customer, the price will be determined by reference to a schedule proposed by the retailer and approved by the regulator.

INQUIRIES

Inquiries regarding the Information Paper on Retail Competition in the Tasmanian Electricity Industry should be directed as follows:

Energy Markets Branch
Department of Treasury and Finance
21 Murray Street
HOBART TAS 7001

Telephone: (03) 6233 6554
Facsimile: (03) 6233 5646

Further information on Tasmania's energy reform framework is available on the Internet at www.treasury.tas.gov.au.