Country Energy's submission to the Independent Pricing and Regulatory Tribunal

Justification Statement

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Regulated Retail Gas Price Proposal

1 January 2005

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1 Overview

Country Energy proposes to increase retail gas tariffs from 1 May 2005. The increase is proposed under the Voluntary Transitional Pricing Arrangement (VTPA) agreed between Country Energy and IPART.

The VTPA states that-
"
- *should CE consider it necessary as a result of special circumstances (including the ability to reflect changes in network prices) to vary average default prices outside of the limits in (i) and (ii) above then the Tribunal's agreement is required:*
    - *CE must advise the Tribunal no later than 4 months before the date of effect of the increase (eg by 1 March for 1 July increase).*
    - *CE must provide a justification statement to the Tribunal specifying the basis of the increase and providing relevant information supporting the increase. "*

This justification statement sets out the proposed increases, and the reasons for the increase including supporting relevant information. Overall, the total increase in annual retail revenue is proposed to be $576,328, or 4.18% as shown in *the attachments to this statement*. This increase is necessary to ensure that over time:

- Network charges and wholesale purchase costs increases are fully recovered, and
- Regulated retail gas tariffs achieve cost reflectivity

Areas highlighted in this statement include:

- Our proposed increases, including reasons and supporting information,
- The current position of Country Energy's regulated retail gas business,
- An analysis of the base retail costs, including network prices, commodity and transportation charges, FRC costs, operating costs and net margin.
- A summary of the impact on customers in relation to the price proposal

Country Energy would welcome the opportunity to meet with the Tribunal to discuss this submission in further detail, particularly the scenario modelling over the next regulatory period.

2 Country Energy's proposal

This submission is a proposal to increase regulated retail gas prices from 1 May 2005. The increase will apply to low usage customers using < 1 TJ in Tumut, Gundagai, Cooma, Bombala, Wagga Wagga, Uranquinty, Culcairn, Holbrook, Henty and Temora.

As outlined in the VTPA, increases greater than CPI must be submitted to the Tribunal for approval four months before the date of the increase. Country Energy is proposing an increase of greater than CPI and the reasons for this are as follows:

- Country Energy gas networks have increased network prices for all customers, excluding Wagga Wagga and Uranquinty customers, by an average of 9.8% from November 2004.

- Network prices for Wagga Wagga and Uranquinty, are increasing on 1 January 2005 by CPI.

- Wholesale purchase cost will increase by an average of 4% from 1 January 2005.

The proposed regulated retail increase is important to ensure cost reflectivity of Country Energy's regulated retail tariffs is, at a minimum, maintained at current levels to allow Country Energy to recover an appropriate net margin.

In addition, Country Energy requests that consideration be given to passing through increases resulting from the revision of the Access Arrangement for the Wagga Wagga and Uranquinty networks. The increases allowed in these areas are unknown at the present time and as such specific details have not been provided.

Country Energy gas networks have asked for significant increases within the Access Arrangement, and we are requesting the ability to pass through these increases to the regulated retail tariffs when they occur.

3 Current Position

Country Energy offers regulated gas retail tariffs to approximately 20,000 small retail customers. Gas is supplied to a number of areas within our electricity supply area, being Wagga Wagga, Uranquinty, Henty, Walla Walla, Temora, Holbrook, Culcairn, Cooma, Bombala, Adelong, Gundagai and Tumut. Country Energy's gas customers are predominantly located in the Wagga Wagga area.

Figure 1 Snapshot of regulated gas customers

Premises	Minimum Charge Revenue	Fixed Charge Revenue	Variable Charge Revenue	Total Revenue	Annual MJ
21,891	$ 5,995	$ 3,444,936	$ 10,324,544	$ 13,775,475	984,809,801

During the period of the previous Voluntary Pricing Principle in place between Country Energy and the Tribunal significant improvement was seen in the cost reflectivity of gas prices for customers supplied under a standard form contract. However, costs have increased and are further forecast to increase on average at a rate of greater than CPI.

Below is a comparison between base retail costs for 2004 versus 2004 annual revenue. As shown the shortfall is approximately 1% for the year, however it is worth noting that this analysis does not factor in the recent network prices changes in November.

Figure 2 2004 Base Retail costs versus 2004 Revenue

Total Revenue Requirement	Current 2004 Revenue	Revenue Shortfall	% Shortfall
$ 13,922,159	$ 13,775,475	$ 146,684	1.06%

In addition to recent network price changes, wholesale gas purchase costs will increase from 1 January 2005 for all areas. The analysis below compares known 2005 base retail costs to current 2004 annual revenue. This analysis does not include any assumption of increases under the new Wagga Wagga Access arrangement. At a minimum the shortfall for 2005 will be 4.19%, if no price changes occur within the year.

Figure 3 Known 2005 Base Retail costs versus 2004 Revenue

Total Revenue Requirement	Current 2004 Revenue	Revenue Shortfall	% Shortfall
$ 14,352,421	$ 13,775,475	$ 576,946	4.19%

As shown in Figure 4, current annual revenue will not recover the full costs of supply when compared to 2005 base retail costs. The situation improves as shown below in Figure 5 when compared to the proposed revenue for 2005. However depending on the level of future network use of system increases, the situation may potentially worsen.

Figure 4 2005 Base retail costs versus 2004 retail revenue

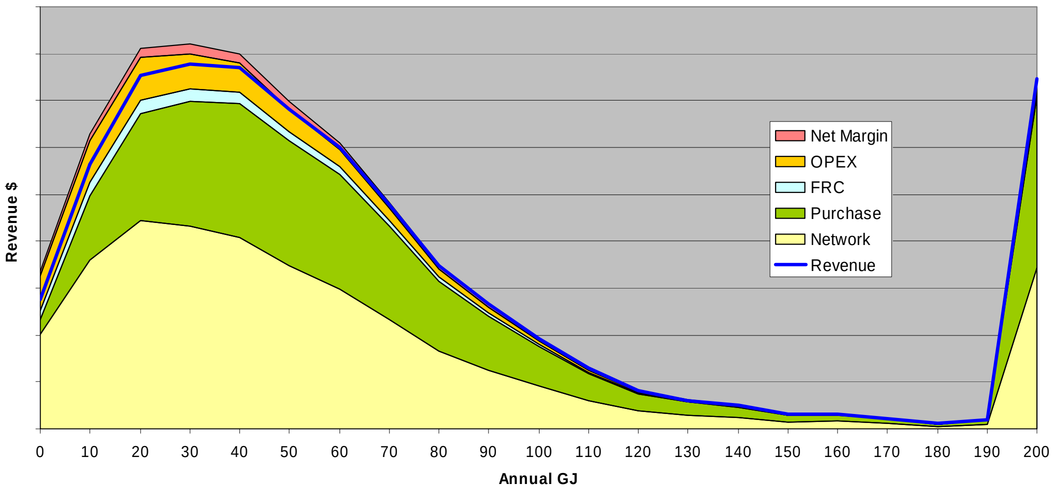
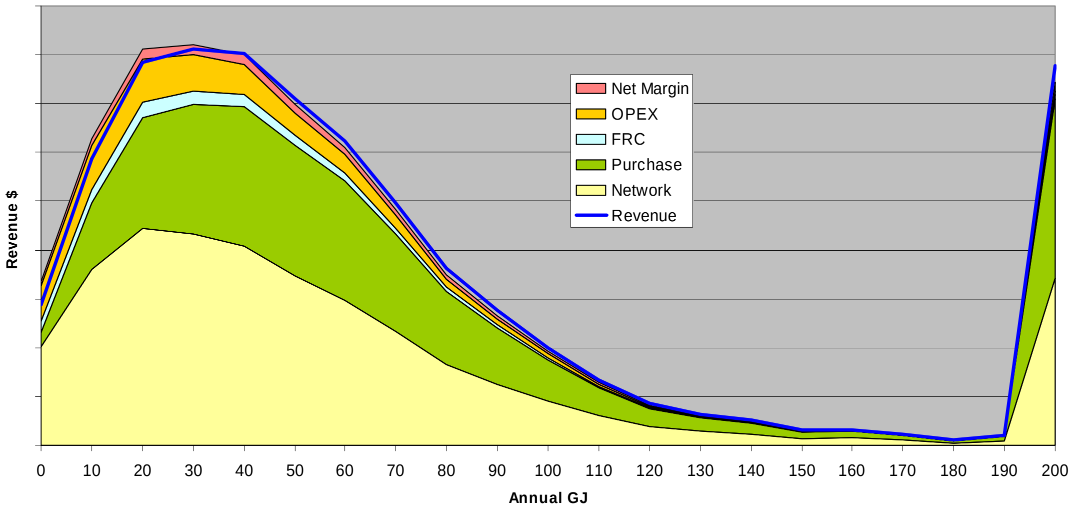


Figure 5 2005 Base retail costs versus 2005 retail revenue



4 Cost Information

Country Energy offers regulated tariffs for gas supply to approximately 20,000 customers. Gas is supplied to a number of pockets within Country Energy's electricity supply area, being Wagga Wagga, South West Slopes, Cooma, Bombala, Adelong, Gundagai and Tumut.

Included within this section is a current snapshot of Country Energy's regulated retail gas customer base, and an analysis of the base retail costs for these customers.

4.1 Network Prices

Country Energy gas networks have recently implemented a network price change for the following areas:

- Tumut, Gundagai and Adelong
- Henty, Holbrook, Culcairn and Temora
- Cooma and Bombala

The price change effective from 1 November 2004 involved restructuring of existing tariffs into fixed and single variable components. The average network price change for all areas is 9.8%, with the average for the regulated retail customers being approximately 6.1%. The price changes have greatly assisted in simplifying the existing network tariff structures, and will increase the ability for existing tariffs to achieve cost reflectivity with a fixed and variable structure.

This retail price proposal assumes an effective date of 1 May 2005. Based on this implementation date, the network increase in these areas will effectively be under recovered for 6 months.

Network prices are increasing on 1 January 2005 by CPI (2.29%) for the following areas:

- Wagga Wagga, and
- Uranquinty

The two Network prices changes as described above will increase average network costs by approximately 3.10%.

The increase effective 1 November 2004 for areas outside Wagga Wagga has been assumed for a full year in 2005, and no impact in 2004 to demonstrate the effect of the change.

Increases resulting from the revision of the Access Arrangement for the Wagga Wagga and Uranquinty networks are not yet know. Country Energy gas networks have asked for significant increases within the Access Arrangement, and Country Energy is requesting the ability to pass through these increases to the regulated retail tariff when known.

4.2 Wholesale Gas Costs Forecast

Wholesale gas costs are increasing for all areas from 1 January 2005 by an average of 4%.

4.3 FRC Costs

Country Energy has partially recovered FRC costs allowed within the regulated retail gas tariffs. The Voluntary Pricing Principle allowed for recovery of FRC costs. The Tribunal has allowed Country Energy, to recover all of these costs as reasonable costs associated with the introduction of contestability, through its default gas tariffs.

The recovery period expires on 30 June 2005 which effectively results in a reduction of the base retail costs, however this reduction is countered by forecast increases in network charges. Therefore Country Energy believes the FRC costs component should remain as part of the regulated retail tariff to assist in recovering past network increases and also future unknown network increase.

4.4 Operating costs

Annual operating costs of $50.71 have been assumed for regulated retail gas customers for the 2004/05 financial year. This amount was determined during IPART's recent review of regulated retail tariffs by Country Energy. This amount is in line with the Voluntary Pricing Principles previously in place between IPART and Country Energy.

4.5 Net Margin

A net margin of 2.5% has been assumed and is based on the allowed net margin documented within the Voluntary Pricing Principles previously in place between IPART and Country Energy.

5 Customer Impacts

All increases proposed for regulated retail gas customers are within CPI + 5%. The table below provides a summary of the average increases proposed by customer class. As shown, customers in Cooma and Bombala and business customers in Tumut, Gundagai, Temora and Culcairn will see no change at all.

Figure 6 Average increase proposed by customer class

Customer Group	Increase	Average Annual Increase per customer	Average quarterly increase
Wagga Wagga Residential	4.50%	$ 26.73	$ 6.68
Wagga Wagga Comercial/Industrial	6.45%	$ 138.38	$ 34.60
Temora/Culcairn Residential	7.35%	$ 29.08	$ 7.27
Temora/Culcairn Business	0.00%	$ -	$ -
Cooma/Bombala Residential	0.00%	$ -	$ -
Cooma/Bombala Business	0.00%	$ -	$ -
Tumut/Gundagai Residential	0.98%	$ 5.07	$ 1.27
Tumut/Gundagai Business	0.00%	$ -	$ -

The maximum increase seen by any consumer will not exceed CPI + 5%. Country Energy has extensively modelled the increase to determine the maximum increases.