

**Mid-term review of regulated retail prices
for electricity to 2004**

**Report and Determination
to the Minister for Energy**

June 2002



**INDEPENDENT PRICING AND REGULATORY TRIBUNAL
OF NEW SOUTH WALES**

**Mid-term review of regulated retail prices
for electricity to 2004**

**Report and Determination
to the Minister for Energy**

Determination 4, 2002

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ISBN 1 877049 27 1

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DETERMINATION 4, 2002

1 INTRODUCTION

On 1 January 2002 the NSW government opened the State's electricity retail industry to full retail competition (FRC) by allowing small retail customers¹ to opportunity to participate in the contestable market. All electricity customers in NSW are now able to choose their retail supplier.

As a consumer protection measure, regulated retail tariffs have been established for small retail customers to enable access to a basic level of service at a reasonable price.² In December 2000, the Tribunal recommended target levels for the regulated retail tariffs which reflect the cost of supplying electricity to small retail customers.³ It also developed a system for moving existing regulated tariffs towards target levels and established maximum charges for miscellaneous transactions.

The Minister for Energy adopted the Tribunal's Recommendation as a Determination for a system of regulated retail tariffs and regulated retail charges to apply for the period from 1 January 2001 to 30 June 2004.⁴ In January 2002 the Minister requested that the Tribunal conduct a mid-term review of regulated retail tariffs to review the framework in light of full retail competition. The Minister's terms of reference are set out in Attachment 1.

As a result of the review, the Tribunal has issued a new Determination under the *Electricity Supply Act, 1995* (ESA), for regulated retail tariffs from 1 August 2002 to 30 June 2004. This Determination continues the Tribunal's approach to the regulation of retail tariffs whereby targets are established for each tariff and each year the retail supplier must increase any under-recovering tariffs subject to defined price-constraints.⁵ The Minister did not request the Tribunal to review the regulated retail charges (ie miscellaneous charges), hence they are reproduced in the new Determination without change.

The Tribunal will maintain a register of regulated retail tariffs existing as at 1 July 2002. Retail suppliers may only introduce new regulated retail tariffs as the Tribunal determines.

1.1 Summary of the new Determination

This Determination:

- sets new targets for regulated retail tariffs to apply from 1 August 2002
- introduces a separate target for 'extended off-peak' tariffs
- renames the 'controlled load' tariff to 'off-peak' tariff

¹ Small retail customers are defined as customers consuming less than 160MWh per annum in the *Electricity Supply Act 1995*, section 92, and *Electricity Supply (General) Regulation 2001* section 7.

² Regulated retail tariffs apply to customers supplied under a standard form customer supply contract. Standard retail suppliers must make such a contract available to any small retail customer. Customers consuming more than 160 MWh per annum are not eligible for a regulated retail tariff.

³ The Tribunal's Recommendation is set out in *Regulated Retail Prices for Electricity to 2004 Recommendation: December 2000*, Independent Pricing & Regulatory Tribunal.

⁴ The Ministerial Determination was made under the *Electricity Supply Act 1995* (ESA) in December 2000.

⁵ Terminology in the terms of reference and the December 2000 Determination refers to 'side-constraints' which are referred to in this report as price-constraints.

- introduces a new price-constraint where regulated retail tariffs, on average, cannot increase by more than inflation⁶
- maintains that there will be no nominal price increases for those customers on tariffs that are on or above the target level
- changes the existing price-constraint for residential customers where, for those tariffs below cost reflective levels (ie below target), a maximum increase of the greater of the percentage change in CPI + 2% or \$25 is allowed
- maintains the price-constraint for business customers where, for those tariffs below cost reflective levels (ie below target), a maximum increase of the greater of the percentage change in CPI + 5% or \$50, is allowed
- makes no amendment to regulated retail charges (miscellaneous charges).

The new targets are the result of an increase in the cost components underlying the regulated retail tariffs. The long run marginal cost (LRMC) estimate of energy purchases has increased, mainly due to the cost of capital for coal fired plants and gas, and a small increase in green energy compliance costs. Retail operating costs are also forecast to rise over the next two years based on benchmarks and costs associated with full retail competition.

The introduction of a target tariff for extended off-peak will clarify the cost of supply associated with these tariffs and assists the retail suppliers in achieving cost-reflectivity of their tariffs.

The Tribunal has changed one component of the price-constraint on residential customers, (from CPI to CPI+2%) in order to move the under-recovering regulated retail tariffs closer to target levels by 2004. On average, however, prices for small retail customers will not be permitted to increase by more than inflation. The Tribunal has endeavoured to achieve cost reflectivity for the 'safety net' tariffs in a reasonable timeframe, whilst limiting large impacts on customers.

This report details the analysis that supports the Tribunal's decisions in the Determination and addresses the Minister's terms of reference:

- Chapter 2 details the changes that will affect the target levels of regulated retail tariffs
- Chapter 3 details the changes that will affect the system for moving existing regulated tariffs towards target levels and
- Chapter 4 details the other issues considered by the Tribunal.

The Tribunal took into account the views expressed in submissions to the review and at the Public Forum held on 3 May 2002.

⁶ 'Inflation' will be the percentage change in CPI-GST for each year as defined in Schedule 1 of the Determination.

2 TARGET LEVELS FOR REGULATED RETAIL TARIFFS

The Tribunal has established target levels for regulated retail tariffs according to the formula 'N+R'. In the formula, 'N' is the network component (the local distribution network service provider's (DNSP) tariff) and 'R' is the retail component (derived from the cost of supply and set by the Tribunal).

The N component is the applicable network charge for each customer and is a direct pass-through from the DNSP. It may have a fixed and variable structure. Since there are a large number of network charges in NSW, there will be many different target levels for regulated retail tariffs. This will continue to be the case even when standard retail suppliers have brought their R components into line with target levels.

The R component is made up of a fixed dollar per customer amount (fixed R), plus a variable cents per kilowatt hour (c/KWh) amount (variable R). The R component depends on which supply district the small retail customer is in, whether the small retail customer is urban or rural, and whether they have a standard or off-peak service. The Tribunal has set target values for the R components based on the cost of supply. The underlying costs are the main subject of this review.

2.1 New targets for regulated retail tariffs for 2002-2004

The Tribunal has increased both the fixed and variable components of R.

The Tribunal has determined new targets for the R components for each standard retail supplier. There are separate targets for 2002/03 and 2003/04. The N component of the target will continue to be the applicable network charge for each customer, directly added to the relevant R component. The Tribunal has introduced a separate target for extended off-peak tariffs to apply from 1 August 2002.

Table 2.1 presents the R component of the target tariffs in 2001 dollars (real terms).⁷ The 2001 values must be increased annually by inflation to arrive at the target in each year.⁸

⁷ The targets are expressed in 2001 dollars to enable comparison with the targets in the December 2000 Determination which applied previously.

⁸ Refer to the Determination for calculation of the target tariffs in nominal terms.

Table 2.1 Real R Components for basis of targets to apply in 2002/2004 (\$ 2001)

For the district supplied by the following standard retail supplier under the licence held by it immediately before 1 July 2002	Fixed R (\$)	Variable R Standard c/kwh	Variable R Off-peak ⁹ (previously 'controlled load') c/kwh	Variable R Extended Off-peak (new) c/kwh
EnergyAustralia				
Urban	\$44.25	5.51	3.57	4.44
Rural	\$44.25	5.51	3.57	4.44
Integral Energy				
Urban	\$48.75	5.78	3.65	4.29
Rural	\$48.75	5.78	3.65	4.29
Country Energy				
Urban	\$47.25	6.01	3.74	4.42
Rural ¹⁰	\$47.25	6.38	3.95	4.68
Australian Inland Energy & Water				
Urban	\$40.50	6.55	3.99	4.51
Rural	\$40.50	6.55	3.99	4.51

A comparison with the December 2000 Determination R component targets (in 2001 dollars) is provided in Appendix 2. The new targets are higher than the targets in the December 2000 Determination as a result of an increase in the underlying cost components, discussed in the following section.

2.2 Change in the cost components of the target tariffs

The Tribunal has increased the ranges for the various cost components of the target tariffs.

The Minister for Energy requested that the Tribunal consider whether there has been a material change in the cost components underlying the target tariffs in the December 2000 Determination. Overall, the Tribunal found that costs have increased since the analysis in the December 2000 Determination. Significant cost factors such as gas prices, coal plant capacity costs, retailers' costs and costs associated with the introduction of full retail competition, warrant an increase in the target tariffs.

The costs considered in this review were:

- electricity purchases (based on the long run marginal cost (LRMC) of electricity generation)
- State and Commonwealth requirements for retail suppliers to purchase 'green energy'
- energy losses that National Electricity Market Management Company Limited (NEMMCO) publishes and are approved by the Tribunal
- network charges as the Tribunal determines for distribution services and the Australian Competition and Consumer Commission (ACCC) determines for transmission services

⁹ 'Controlled Load' tariffs have been renamed 'Off-Peak' tariffs. All other aspects of the tariff remain the same. Refer to section 4.1 for clarification.

¹⁰ Rural tariffs differ from urban tariffs due to different transmission and distribution loss factors.

- fees NEMMCO imposes on retail suppliers, including charges for ancillary services
- retail operating costs and a profit margin
- costs associated with the introduction of full retail competition (contestability costs).

Table 2.2 compares the cost component values underlying the new retail targets with those used in the December 2000 Determination. Appendix 3 provides a detailed discussion of each cost component and the basis for determining the new values. A summary is provided below.

In estimating the LRMC, the Tribunal examined the impact of variations in a number of the assumptions (see Appendix 3). As a result of changes to the assumed gas price, cost of capital for coal fired plants, forecast load and compliance with the Commonwealth Mandatory Renewable Energy Targets (MRET) scheme, the Tribunal increased the range for LRMC from \$36-\$56 to \$39-\$59 /MWh (\$2001).

For retail operating costs, the Tribunal continued to use a benchmark approach. The Tribunal reviewed the available benchmarks and information on costs provided by retail suppliers. New benchmarks appear higher and retail suppliers forecast additional costs mainly in the areas of information technology and administration. The Tribunal increased the range for the benchmark operating costs to \$45-\$75 per customer to apply for 2002-2004, from \$40-\$60 (in \$2001) in the December 2000 Determination. The new range includes costs associated with contestability.

The Tribunal decided that there was no evidence to support changing the allowances for NEMMCO fees and the profit margin.

Table 2.2 Comparison of cost components in the retail target tariff

Cost component	OLD	NEW
	December 2000 Determination 2000/01 and 2001/02 (2001 dollars)	June 2002 Determination 2002/03 and 2003/04 (2001 dollars)
Energy purchases (including green energy)	<ul style="list-style-type: none"> • Range \$36 to \$56 per MWh as the weighted average for long run marginal cost (LRMC) 	<ul style="list-style-type: none"> • Range \$39 to \$59 per MWh as the weighted average for long run marginal cost (LRMC)
NEMMCO fees & ancillary services (included in Energy purchases)	<ul style="list-style-type: none"> • \$1.37 per MWh 	<ul style="list-style-type: none"> • \$1.37 per MWh
Energy losses	<ul style="list-style-type: none"> • Disaggregated loss factors published by NEMMCO specific to distribution area 	<ul style="list-style-type: none"> • Disaggregated loss factors published by NEMMCO specific to distribution area
Retail operating costs	<ul style="list-style-type: none"> • \$40-\$60 per small retail customer per year including an allowance for contestability costs. Retail operating costs were split into a fixed and a variable component 	<ul style="list-style-type: none"> • \$45-\$75 per small retail customer per year including an allowance for contestability costs. Retail operating costs are split into a fixed and a variable component
Profit margin	<ul style="list-style-type: none"> • 1.5-2.5% net profit margin 	<ul style="list-style-type: none"> • 1.5-2.5% net profit margin

2.3 Extended off-peak tariff target

The Tribunal has introduced an extended off-peak target, where the target is a weighted average of the controlled load (off-peak) and standard target

In the terms of reference the Minister for Energy requested that the Tribunal clarify off-peak versus controlled loads.

Currently the December 2000 Determination establishes a standard and a controlled load target tariff for rural and urban areas. The controlled load tariff was intended to reflect the lower energy costs during off-peak periods. However, retail suppliers also offer tariffs that span off-peak and shoulder periods, known as extended off-peak (eg tariffs known as OP2, OP3 or OP4). The Tribunal has introduced a target for these extended off-peak tariffs, effective from 1 August 2002. In doing this, the Tribunal is determining a new target only, not a new regulated retail tariff.

Submissions by retail suppliers raised the issue that since extended off-peak tariffs are offered for periods which straddle both off-peak and shoulder periods, a higher energy purchase cost is incurred than for true off-peak tariffs (controlled load), however, they do incur a lower cost than the standard target. The current arrangements mean that the extended off-peak tariffs are typically classified as substantially over-recovering (because a lower energy cost is applied), when in fact they may be under-recovering, or over-recovering to a much less degree, if they were compared with the actual energy purchase costs. Being classified as an over-recovering tariff means that retail suppliers are unable to raise these tariffs when in reality the actual costs of supply might suggest it is appropriate to do so.

Retail suppliers generally support the introduction of a specific extended peak target tariff that better reflects the cost of supply. The Tribunal has introduced such a target. It is believed that the introduction of an extended off-peak target is more advantageous to retail suppliers than introducing a shoulder tariff, discussed in Section 2.4.

2.3.1 Impact of introducing an extended off-peak target tariff on over/under recovering tariffs

Table 2.3 illustrates the relationship between the extended off-peak tariff and the cost of supply for the old and new targets, that is, the extent of over-recovery. With the higher targets, the over-recovery is reduced. In some cases retail suppliers will be able to increase tariffs as the target tariffs increase with inflation.

Table 2.3 Revenue over-recovery in 2001/02 with extended off-peak tariff target based on targets in December 2000 Determination

Retail supplier	Old R component equal to existing 'controlled load' target	New R component equal to new extended off-peak target
EnergyAustralia ¹¹	\$6.1m	\$2.0m
Integral Energy	\$6.9m	\$4.2m
Country Energy ¹²	\$3.7m	\$1.8m
AIEW ¹³	\$0.07m	\$0.04m

2.4 Consideration of a shoulder target tariff

The Tribunal has not introduced a shoulder target tariff.

The terms of reference required that the Tribunal consider the merits of introducing a 'shoulder' target retail tariff. A shoulder target would apply in the period between peak and off-peak, and would apply to Time of Use (TOU) tariffs. There is no real incentive to introduce such a tariff as it does not match current purchase arrangements.

As discussed above, the Tribunal has introduced a new 'R' to account for extended off-peak tariffs.

¹¹ Addition of domestic and general supply off-peak 2 tariffs.

¹² Addition of major extended off-peak tariffs for NorthPower 1 and Advance Energy 2 only.

¹³ Addition of extended off-peak tariffs, domestic only.

3 TRANSITION TO TARGET TARIFFS

There are currently more than 500 regulated retail tariffs in NSW. Some of these are significantly higher than the applicable target level, while others are close to or lower than the applicable target level. The Tribunal maintains its view that it is not appropriate to move regulated retail tariffs to target levels immediately as it may result in significant price increases for some small retail customers. A process has been set in place to move regulated retail tariffs towards the target in each year, without having customers incur unreasonable increases.

3.1 Process for transition and timing of price changes

3.1.1 Retail tariff changes for 2002/03 will occur on 1 August 2002

Price changes for regulated retail tariffs usually occur on 1 July of each year. To accommodate this Determination, however, price changes for 2002/03 will occur on 1 August 2002, effective for 11 months until 30 June 2003. Price changes for 2003/04 will occur on 1 July 2003.

These are the only opportunities standard retail suppliers will have to change their regulated retail tariffs. As stated in the December 2000 Determination, standard retail suppliers cannot change their regulated retail tariffs more than once in a financial year.

3.1.2 Implementation of Price Changes for 2002/03 and 2003/04

The objective of price changes is to transition tariffs towards target levels in each year. Retail suppliers must determine each year whether a tariff is under-recovering, recovering, or over-recovering in relation to the target tariff applicable at that price change date. To determine whether a tariff is under-recovering or over-recovering, the retail supplier compares the total revenue from all small retail customers on that tariff during the previous 12 months, with the estimated target revenue which would have been received had the tariff been at the target applicable to that price change date (using the same number of customers and pattern and volume of electricity consumption for the previous 12 months).

The price change will be determined by¹⁴:

1. Under-recovering tariffs: Total revenue is less than the estimated target revenue and the tariff is considered to be below the target level. The tariff must increase towards or equal to the target (but not above). The increase will be limited by the constraints in section 3.2.
2. Over-recovering and recovering tariffs: Total revenue is above, or equal to the estimated target revenue. The tariff is not allowed to increase, resulting in no increase in price in nominal terms.

The Tribunal has established this process to facilitate a smooth transition to the target levels. As there are only two years remaining in the regulatory period to achieve the targets, it is important that retail suppliers use pricing strategies to achieve balanced outcomes across these two years. Retail suppliers must demonstrate to the Tribunal that they have moved the tariffs in accordance with the process.

¹⁴ Refer to the Determination for further clarification.

3.2 Constraints on price increases (price-constraints)

The Tribunal has reviewed the constraints on price increases and has determined that for each year, for the same pattern and volume of consumption:

- (i) Average prices across all small retail customers must not increase by more than the percentage change in CPI ^{GST} 15***
- (ii) Over-recovering and recovering tariffs must not increase in nominal terms***
- (iii) The annual bill for any residential customer must not increase by more than the greater of \$25 or the percentage change in CPI ^{-GST} + 2%***
- (iv) the annual bill for any business customer must not increase by more than the greater of \$50 or the percentage change in CPI ^{-GST} + 5%***

Price-constraints are rules governing the rate at which standard retail suppliers can increase the regulated retail tariff towards its target level. Note that only under-recovering tariffs can increase (section 3.1.2). The Tribunal has set these rules to achieve a reasonable balance between the impact on standard retail suppliers and the impact on small retail customers.

The Minister for Energy asked the Tribunal to consider the effect of price-constraints on the transition to the target retail tariffs by 30 June 2004. The presence of under-recovering tariffs may undermine the proper functioning of the competitive retail market, with customers being charged less than it costs to supply them.

With an increase in the cost of supply and hence the targets, the Tribunal has had to consider a change in the price-constraints to ensure that tariffs were moving towards cost-reflective levels at an appropriate rate. This Determination will allow a residential customer's bill to increase by the greater of the percentage change in CPI ^{-GST} + 2% or \$25 per annum, instead of what was previously the greater of the percentage change in CPI ^{-GST} or \$25 per annum, in the December 2000 Determination.

The Tribunal has also introduced a new price-constraint on the average price. The Tribunal believes that taken together, the new constraints balance the interests of retail suppliers and their customers.

The price-constraints are explained below and are applicable to retail price changes in the years 2002/03 and 2003/04. They apply to each price change based on the same pattern and volume of consumption as the previous year.

In each year, for tariffs that are allowed to increase under the process in section 3.1.2, the increase must be in a manner that does not result in:

- An increase in the annual bill for a small retail customer on a residential (urban and rural) regulated retail tariff of more than the percentage change in CPI ^{-GST} + 2%, or \$25, whichever is greater
- An increase in the annual bill for a small retail customer on a business (urban and rural) regulated retail tariff of more than the percentage change in CPI ^{-GST} plus 5%, or \$50, whichever is greater (this remains unchanged from the December 2000 Determination).

¹⁵ Definition of CPI is found in Schedule 1 of the attached Determination.

Additionally, across all regulated retail tariffs (residential and business),

- Average prices must not increase by more than the percentage change in CPI^{GST}.

The Tribunal will assess compliance with these constraints as part of its consideration of pricing proposals each year. Retail suppliers must demonstrate that they comply in accordance with the Minister's directions. The Tribunal's approach to checking compliance is to look at the proposed tariffs before they are introduced to see if they would breach the price constraints.

Comparison with network price-constraints

The price-constraints on network charges are summarised¹⁶ as follows:

- average prices across the network must not increase by more than the percentage change in CPI¹⁷
- for residential customers, the bill must not increase by more than the greater of the percentage change in CPI + 2%, or \$30.

The new price-constraints for retail tariffs more closely align with network price-constraints. The Tribunal recognises that the remaining difference must be accommodated via an under-recovery in retail prices.

3.2.1 Impact of price changes

Impact on customers

With the new constraint on average prices, the average bill across residential and business small retail customers will not increase by more than inflation (based on the same pattern and volume of electricity consumption).

For customers on tariffs that are under-recovering, there will be varying degrees of increases. However, the maximum increase is limited to the price-constraints in section 3.2. The Tribunal has modelled the expected impact on a bill for a typical residential customer who is on an under-recovering tariff in Table 3.1. The impact differs across supply districts and depends on whether they are a small, medium or relatively large user of electricity. On average the increases translate to less than \$1.00 per week.

Across all residential retail tariffs the net effect on residential customers will be considerably less than that demonstrated in Table 3.1 as there are a significant number of tariffs which are above target levels and customers will see a decrease in real terms. There will be a similar effect on small business customers.

¹⁶ For more detail, refer to the *Regulation of NSW Electricity Distribution Networks, Determination and Rules under the National Electricity Code*, December 1999.

¹⁷ CPI as defined in the *Regulation of NSW Electricity Distribution Networks, Determination and Rules under the National Electricity Code*, December 1999.

Table 3.1 Impact of increases in under-recovering tariffs on residential customers per annum, DCPI¹⁸ vs DCPI+2%¹⁹ increase (2000/01 to 2001/02)

Standard domestic + off-peak 1 for each district ²⁰ :	'small' residential ~ 3,000 kWh pa		'medium' residential ~ 8000 kWh pa		'large' residential ~ 18,000 kWh pa	
	DCPI	DCPI+2%	DCPI	DCPI+2%	DCPI	DCPI+2%
EnergyAustralia	\$8	\$14	\$19	\$31	\$39	\$66
Integral Energy	\$9	\$15	\$20	\$34	\$43	\$73
Country Energy ²¹	\$10	\$17	\$21	\$35	\$42	\$71
AIEW ²²	\$6	\$10	\$10	\$18	\$20	\$34

Low income households

The Household Expenditure Survey from the Australian Bureau of Statistics suggests that large electricity users are not necessarily high income households. The Tribunal is aware that the new targets and price-constraints will have an impact on some low income users. The Government does provide assistance to people who have trouble paying their bill via the Energy Accounts Payment Assistance (EAPA) scheme. The scheme is currently under review by PricewaterhouseCoopers and in a submission to the review, the Energy & Water Ombudsman (EWON) expressed concern about EAPA's effectiveness. EWON is concerned that the EAPA scheme does not meet the demand in the community and there seems to be frequent shortages of vouchers even though the scheme has been underspent in previous years.²³ The Tribunal concurs with EWON's comments and believes that there needs to be a review of the level of assistance that should be provided to each customer. An effective payments assistance scheme will provide additional protection to low income users.

¹⁸ Δ CPI = 2.9%, side-constraint on increases in under-recovering tariffs in the December 2000 Determination.

¹⁹ Δ CPI+2% = 4.9%, side-constraint on increases in under-recovering tariffs in new Determination.

²⁰ Assumes customer purchases 60 per cent of electricity at standard and 40 per cent off-peak and that the existing fixed price and variable price both increase by the side-constraint percentage.

²¹ Figures for area of Dubbo.

²² Shows a rural tariff in Broken Hill as the urban tariffs are close to the target, requiring an increase smaller than Δ CPI+2%.

²³ EWON submission, April 2002 to *PricewaterhouseCoopers Energy Accounts Payment Assistance Scheme (EAPA) Issues Paper*, www.ewon.com.au.

4 OTHER ISSUES CONSIDERED BY THE TRIBUNAL

4.1 New regulated retail tariffs

The Tribunal has not introduced any new regulated retail tariffs for 2002/03.

The terms of reference for the review required the Tribunal to consider “*the circumstances in which standard retail suppliers may introduce regulated retail tariffs in addition to the transitional and target retail tariffs*”.

The Tribunal continues to believe that a regulated retail tariff should be a basic option without special features. This implies keeping the number of regulated retail tariffs available to a minimum, and offering choice in services under negotiated contracts in the contestable market.

Standard retail suppliers have indicated that they do not want to introduce any new regulated retail tariffs in 2002/03. However, they do want the flexibility of doing so in the future as there could be specific circumstances where new regulated retail tariffs could be warranted prior to the regulatory period finishing in 2004.

To accommodate such circumstances, the Tribunal recommends that the Minister refer any proposals for new regulated retail tariffs to the Tribunal for consideration in accordance with Section 43EA of the *Electricity Supply Act, 1995* (ESA). In this way, new regulated retail tariffs will be considered on a case-by-case basis.

The standard retail supplier would need to place a request with the Minister in time for the Tribunal to undertake public consultation prior to the new tariffs taking effect from the next price change date. The Tribunal believes that this mechanism will be appropriate for the remaining two years of this regulatory period.

The Tribunal’s decision not to introduce any new regulated tariffs was also considered in light of existing and future levels of competition (section 4.2) and extended off-peak tariffs (section 2.3).

4.1.1 Consideration of ‘green tariffs’

The terms of reference requested the Tribunal to consider arrangements for introducing ‘green tariffs’. Currently retail suppliers can have green tariffs comprising of a regulated retail tariff and a green premium. These green tariffs are generally based on a ‘green power’ purchase arrangement. Customers elect to be on these tariffs voluntarily. While the base tariff is regulated, the premium is not. The Tribunal believes that the current arrangements provide standard retail suppliers with the flexibility to introduce appropriate green tariffs and hence there is no need to have green tariffs regulated as separate retail tariffs.

4.2 Promotion of competition

The Electricity Supply Act states that the Tribunal must have regard to “*the effect of the Determination on competition in the retail electricity market*”.²⁴ Additionally, the terms of reference for this review refer to the effect on competition of (under-recovering) tariffs set by the Tribunal.

The Tribunal has set the target level of the regulated retail tariff to be cost reflective. One of the intentions of setting target tariffs at the efficient level is to achieve consumer protection without stifling competition. Economically efficient retail suppliers should be able to compete using other tariffs – either by providing a value-added service to the customer at an appropriate price, or by offering more attractive contracts than the standard retail supplier. Competition should occur of its own accord in an efficient market and the regulated retail tariffs should remain as the ‘default’ or safety net.

Many submissions to the review insisted that an additional margin within the regulated retail tariff is required to encourage competition. These views are discussed further in Appendix 3 in relation to profit margins. The Tribunal strongly believes that this is not desirable from an economic efficiency perspective and maintains that the regulated retail tariffs should be neutral with respect to competition.

In terms of the effect on competition of new regulated retail tariffs, new regulated retail tariffs may hinder the development of the contestable market. If more choice of regulated tariffs is offered, consumers will not be inclined to consider negotiated contracts. This is particularly relevant given that the NSW market has only recently been opened to full retail contestability (FRC). There has been little time for competitive retail suppliers to differentiate themselves or establish competitive tariffs with value-added services.

4.2.1 Impact of under-recovering tariffs on competition

If a tariff is under-recovering, it implies that it is not recovering the cost of providing the service. If the regulated tariff is below cost, competition may not occur as it is difficult for a competitive retail supplier to offer more attractive services.

Under the December 2000 Determination, the Tribunal recognised that not all tariffs would be at their target level by 2004. This was due to some tariffs starting significantly below the target level in 2000. The Tribunal balanced the need for cost reflectivity against imposing price shocks on customers and determined a path for moving these under-recovery tariffs towards cost-reflective levels.

In this Determination, the forecast level of under-recovery is not significantly different from the level in the December 2000 Determination, given the increase in targets and changes in the price-constraints. Table 4.1 shows the predicted level of under-recovery in revenue under this Determination compared to what would have occurred if the December 2000 Determination targets and price-constraints were maintained.

²⁴ *Electricity Supply Act 1995*, section 43EB(2)(b).

**Table 4.1 Under-recovering revenue forecast at 2004
June 2002 Determination compared to December 2000 Determination**

Retail supplier	Revenue (\$2001) under old "R" and price-constraints	Revenue (\$2001) under new "R" and new price-constraints
EnergyAustralia	\$7.4m	\$5.7m
Integral Energy	\$5.0m	\$8.1m
Country Energy ²⁵	\$12.5m	\$9.9m
AIEW	\$0.5m	\$0.7m

4.3 Renaming the 'controlled load' tariff to 'off-peak' tariff

In the December 2000 Determination, the Tribunal set a 'controlled load' variable R component as part of the target tariffs. The intent was to reflect the lower energy costs of off-peak consumption.

Consistent with the introduction of a variable R 'extended off-peak' component, the Tribunal has decided to use the term 'off-peak' instead of 'controlled load'. This should remove any confusion. The 'off-peak' component of the target tariffs applies to consumption on separate off-peak tariffs and the off-peak component of time-of-use (TOU) tariffs where consumption occurs in a defined off-peak period only.

4.4 Regulated retail charges (miscellaneous charges) for small retail customers

The Tribunal has not amended the regulated retail charges.

The Tribunal set maximum allowable charges for the list of regulated retail charges in the *Electricity Supply Amendment Act, 2000* (Amending Act), as part of the December 2000 Determination. Regulated retail charges are:

- Fees for dishonoured bank cheques.
- Late payment fees.
- Security deposits.

The terms of reference for this review did not ask the Tribunal to consider or review the charges set in December 2000. As a result, the charges set in the December 2000 Determination remain valid and form part of the new Determination without change. Table 4.2 lists the maximum value of regulated retail charges which are to apply. Standard retail suppliers may choose not to charge regulated retail charges, or to charge below the maximum.

²⁵ Addition of NorthPower and Advance Energy only, Great Southern Energy (GSE) results not available.

Table 4.2 Regulated retail charges

Charge for miscellaneous service	Maximum allowable charge
Fee for dishonoured bank cheque	Twice bank fee
Late payment fee	\$5.00
Security deposit	1.5 times the average quarterly account or 1.75 times the average 2-monthly account, or 2.5 times the average monthly account

The December 2000 Report, Appendix 4, provides the rationale behind these charges.

APPENDIX 1 TERMS OF REFERENCE

Terms of reference for an investigation and report by the Independent Pricing and Regulatory Tribunal on regulated retail tariffs to apply between 1 July 2002 and 30 June 2004 under Division 5 of Part 4 of the *Electricity Supply Act 1995*.

Background

The *Electricity Supply Act 1995* sets out arrangements for determining regulated retail tariffs for small retail customers (less than 160 MWh per annum). The Tribunal's report of December 2000, *Regulated Retail Prices for Electricity to 2004*, was taken to be a determination²⁶ under Section 43EB of the *Supply Act 1995* for the period 1 January 2001 to 30 June 2004.

Small retail customers in NSW can seek supply from the competitive market or they can remain with their standard retail supplier on a regulated 'safety net' tariff. Customers can also switch backwards and forwards between these alternatives. These arrangements are designed to encourage customers to test the market by providing a safety net if a customer's market experience is unsatisfactory. Customers will seek competitive retail supply if the market price is less than the regulated safety net tariff and/or if competitive retail suppliers offer superior service to the standard form contract associated with the regulated safety net arrangements.

The Tribunal's current determination of regulated retail tariffs aimed, in part, to rationalise the number of tariffs through time through the setting of a 'target' level for each regulated retail tariff and a transitional process for moving regulated retail tariffs towards that level over time.

Standard retail suppliers are able to increase regulated retail tariffs that are currently below their target level in line with IPART determined price constraints.

Target levels are 'end-points' for existing regulated retail tariffs. The duration of the transition to the target tariff for an individual customer will depend on how cost reflective the small retail customer's regulated retail tariffs was when the transition commenced. Standard retail suppliers are not able to increase regulated retail tariffs that are currently above the relevant target level, so that these tariffs will decrease in real terms. However, it seems likely that a number of customer tariffs will remain below the target level for some time and this indicates that customers are being charged less than it costs to supply them. The presence of these under-recovering tariffs may undermine the proper functioning of the competitive retail market.

²⁶ See clause 37, Schedule 6, *Electricity Supply Act 1995*.

Matters for consideration

For the purpose of section 43EB (2)(a) of the *Electricity Supply Act 1995*, the Tribunal is to consider whether there are any factors that would lead the Tribunal to form the view that there has been a material change in the following cost components in the setting of cost-reflective 'target' tariffs since the determination was issued and if so whether this justifies a change in the level of the target tariffs to apply from 1 July 2002 to 30 June 2004:

- an allowance for electricity purchase costs based on an assessment of the long-run marginal cost of electricity generation
- an allowance for purchases of 'green energy' consistent with retail supplier licence obligations
- energy losses as published by NEMMCO
- network charges as determined by the Independent Pricing and Regulatory Tribunal and the Australian Competition and Consumer Commission
- fees (including charges for ancillary services) as imposed by NEMMCO under the National Electricity Code
- an appropriate Retail Gross Margin
- the allowance for annual indexation based on the Consumer Price Index and expected movements in regulated components and NEMMCO fees.

Consistent with the requirement of section 43EB (2)(b) of the Supply Act, the Tribunal should review the system of tariffs to determine whether the tariffs that are currently below the relevant target level are likely to materially undermine the effective operation of the competitive electricity retail market. If the market is adversely affected by these below target tariffs the Tribunal should determine the changes necessary to the system of regulated retail tariffs to ensure the market operates effectively.

More specifically, the Tribunal is to take account of the following matters in undertaking its mid term review:

- the effect of price constraints in facilitating the rationalisation of existing regulated tariffs and the transition to the target retail tariffs by 30 June 2004
- clarification of the circumstances in which standard retail suppliers may introduce regulated retail tariffs in addition to the transitional and target retail tariffs, in particular arrangements for introducing 'green tariffs'
- clarification of off-peak versus controlled loads including the merits of introducing a 'shoulder' target retail tariff and
- arrangements for the recovery of all reasonable full retail competition costs.

The Tribunal may consult with stakeholders as appropriate, within the timetable for the investigation and report. The Tribunal's report is to be made publicly available.

Timing

The Tribunal is to investigate and provide a report of its determination of regulated retail tariffs by 1 June 2002.²⁷

Definitions

‘Regulated retail tariff’ means a tariff for or in relation to the supply of electricity required to be charged to a small retail customer under a standard form customer supply contract, being a tariff specified in a determination in force under Division 5 of Part 4 of the *Electricity Supply Act 1995*.

‘Small retail customer’ means a customer that consumes electricity at less than 160MWh per year as prescribed in clause 7 of the *Electricity Supply (General) Regulation 2001*. A small retail customer is eligible for supply under a standard form customer supply contract.

‘Standard retail supplier’ means a retail supplier to whose retail supplier’s licence is attached a standard retail supplier’s endorsement. A standard retail supplier must impose tariffs and charges for or in relation to supplying electricity under a standard form customer supply contract in accordance with any relevant determination of the Tribunal under Division 5 of the *Electricity Supply Act 1995*.²⁸

‘Standard form customer supply contract’ means a contract entered into under Division 3 of Part 4 of the *Electricity Supply Act 1995*.

²⁷ The Tribunal was granted an extension to the review to enable the final results of the contestability study to be included.

²⁸ The standard retail supplier for each supply district is the existing local retail supplier for that district, based on the existing local network supply areas – Australian Inland Energy and Water, Country Energy, EnergyAustralia and Integral Energy.

APPENDIX 2 COMPARISON OF REGULATED RETAIL TARIFF R COMPONENTS IN REAL TERMS²⁹

Table A2.1 R Component (\$2001) June 2002 Determination (new) compared to December 2000 Determination (\$2001) (old)

	Fixed R (\$) new	Fixed R (\$) old	Variable R Standard c/kwh new	Variable R Standard c/kwh old	Variable R Off-peak c/kwh new	Variable R Off-peak ³⁰ c/kwh old	Variable R extended Off-peak c/kwh (new)
Energy Australia							
Urban	\$44.25	\$37.50	5.51	5.16	3.57	3.55	4.44
Rural	\$44.25	\$37.50	5.51	5.16	3.57	3.55	4.44
Integral Energy							
Urban	\$48.75	\$37.50	5.78	5.41	3.65	3.61	4.29
Rural	\$48.75	\$37.50	5.78	5.42	3.65	3.70	4.29
Country Energy³¹							
Urban	\$47.25	\$37.50	6.01	N/A	3.74	N/A	4.42
Rural	\$47.25	\$37.50	6.38	N/A	3.95	N/A	4.68
Australian Inland Energy & Water							
Urban	\$40.50	\$37.50	6.55	5.87	3.99	3.96	4.51
Rural	\$40.50	\$37.50	6.55	5.86	3.99	3.95	4.51

²⁹ The table is expressed in real terms (2001 dollars) to enable comparison with the previous targets which were published in the December 2000 Determination.

³⁰ 'Controlled Load' tariffs have been renamed 'Off-Peak' tariffs. All other aspects of the tariff remain the same. Refer to section 4.1 for clarification.

³¹ Country Energy previously existed as NorthPower, Advance Energy and Great Southern Energy, which had different variable rates per retailer.

APPENDIX 3 ANALYSIS OF COST COMPONENTS IN THE RETAIL TARGETS

Cost of purchasing electricity: Long Run Marginal Cost (LRMC)

The Tribunal has shifted the range for LRMC to between \$39 and \$59/MWh (\$2001), which includes green energy costs and National Electricity Market Management Company Ltd (NEMMCO) fees

Under its terms of reference for setting regulated retail tariffs, the Tribunal is required to base its allowance for the cost of purchasing electricity on an assessment of the long-run marginal cost (LRMC) of electricity generation. In the December 2000 Determination, the Tribunal set its target tariffs based upon an estimate of LRMC of electricity generation in the range of \$36 to \$56 per MWh (in 2001 dollars). This included an allowance for compliance with the NSW state green energy scheme.

The Tribunal took a number of factors into consideration in deciding on the range for the LRMC of electricity generation during the 2000 Determination, including:

- the government's proposed electricity tariff equalisation fund (ETEF)
- the Cap Gemini Ernst and Young (CGEY) study that the Tribunal commissioned
- other studies of LRMC of electricity generation
- existing licence requirements for greenhouse energy purchases.

The estimate of LRMC

A number of submissions to the review have suggested that the Tribunal's allowance for energy purchase costs is too low. In particular, some submissions questioned whether some of the assumptions underlying the original LRMC remained valid. Specific concerns raised in submissions to the review were:

- the proportion of energy supplied in the peak may be under-estimated
- the price of gas (as a fuel for Combined Cycle Gas Turbines (CCGT)) may be too low
- the capital cost of coal fired plant may be too low — the originally modelling applied a capital cost of \$950/kW³² of capacity whereas NEMMCO has used a value of \$1200/kW.³³

The Tribunal also considered the impact of NEMMCO's revised load forecasts.³⁴

The Tribunal examined the impact of these variations in assumptions on the estimate of LRMC generated by the CGEY model. The definition of the peak had little effect on the model results as the key driver is the proportion of energy supplied by different plant types rather than the definition of peak period itself. It is likely that the CGEY modelling understated the LRMC for EnergyAustralia because of the use of bulk supply rather than franchise load data. However, the Tribunal has adopted an average NSW-wide estimate of LRMC for all retail suppliers rather than retail supplier-specific estimates so this downward bias should not be reflected in EnergyAustralia's target tariffs.

³² *Inter-regional Planning Committee (2001), IRPC Stage 1 Report.*

³³ NEMMCO, *Proposed SNI Interconnector, Report No. V014*, 26 October 2001.

³⁴ NEMMCO, *Statement of Opportunities* contained in ESAA (2001), Electricity Australia 2001.

The combined effect of changes to the assumed gas price, cost of capital for coal fired plants and forecast load lead to the Tribunal to shift the range for LRMC upward. The most important factor was the assumed coal plant capital cost — not surprising given that the majority of electricity supplied in New South Wales is supplied by coal-fired generation plant.

Green energy compliance costs

Green energy purchase costs form part of the LRMC of energy purchases, however, since the Determination in December 2000, there have been significant changes in the obligations on retail suppliers with respect to reducing greenhouse gases and utilising renewable electricity generation. These changes are:

- the proposed extension and tightening of the New South Wales state benchmark licence requirements and
- the introduction of the Commonwealth's Mandatory Renewable Energy Target (MRET) scheme.

An outline of these changes is included in Appendix 4.

At the time of the December 2000 Determination, retail suppliers faced only the provisions of the *Electricity Supply Act 1995* that required electricity retail suppliers to develop greenhouse gas reduction strategies as part of their licence conditions. These obligations were included in the LRMC estimate at the time. The key feature of the changes to be implemented from January 2003, is that the benchmark targets become binding. Retail suppliers failing to meet their targets would be subject to a \$15/tonne penalty for every tonne of CO₂-equivalent they fall short, however the Government is also introducing a range of changes intended to mitigate the cost of compliance.

The Government has modelled the expected cost of compliance of both the State and Commonwealth schemes.³⁵ This modelling shows that compliance costs will rise over the next ten years as interim targets become more demanding and lower cost abatement opportunities are exploited. Over the next ten years, the Government modelling suggests that the combined State and Commonwealth requirements will generate average compliance costs of around \$2.20/MWh.

The Tribunal's original estimate of LRMC was based upon modelling that assumed the benchmark licence requirements were binding and that there would be sufficient gas co-generation to satisfy the required benchmarks. The LRMC estimate did not however include any allowance for compliance with the Commonwealth MRET scheme which was not finalised at the time. Government modelling suggests that over the remaining life of the regulatory period, MRET scheme compliance costs will average around \$0.25 cents/MWh. EnergyAustralia and Integral Energy have suggested their compliance costs to 2004 would be around this \$0.25/MWh while Country Energy have submitted an average of around \$0.37/MWh. The Tribunal has decided to include an allowance in the range of \$0.25–\$0.37/MWh to cover MRET compliance costs.

³⁵ The Government *Position Paper on greenhouse-related licence conditions for electricity retail suppliers (December 2001)* details the modelling framework and preliminary results. These results have subsequently been revised following public consultation.

Net impact on the electricity purchase cost allowance

The Tribunal has adopted the government modelling as the basis for the green energy costs to include in the LRMC. The allowance in the LRMC is in the range of \$0.50 to \$2.20/MWh.

The Tribunal's changes to estimated LRMC and green energy compliance costs increase the allowance for electricity purchase costs to \$39 –\$59/MWh (real 2001 dollars).

National electricity market (NEM) fees

The allowance in the LRMC for NEM fees for 2003 and 2004 will be \$1.37/MWh

The allowance for NEM fees and ancillary charges was set in the December 2000 Determination at \$1.37/MWh for 2001 and \$1.30/MWh for 2002 and 2003. This was based on the expectation that NEM fees would fall and ancillary charges would remain unchanged in real terms.

In line with the expectation, NEM fees have fallen by around 9 cents/MWh since 1999/00, however in contrast, ancillary charges have increased by 9 cents/MWh. These changes have offsetting impacts on total NEM fees.

In light of the analysis and NEMMCOs forecasts, the Tribunal believes it is appropriate to keep the allowance for NEM fees for 2002 and 2003 at the 2001 level, \$1.37/MWh, rather than the forecast of \$1.30/MWh provided for in the December 2000 Determination.

Table A3.1 Estimate of total NEM fees and charges

(\$/MWh)	2001 (actual)	2002 (2001 dollars)
NEM Fees	\$0.39	\$0.30
Ancillary Charges	\$0.98	\$1.07
Total Retail supplier Fees and Charges	\$1.37	\$1.37

Retail operating costs including contestability costs

The Tribunal has increased the range for retail operating costs to \$45-\$75 (\$2001), which includes contestability costs

In the December 2000 Determination, the Tribunal adopted a benchmark range for retail operating costs of between \$40 to \$60 per customer per annum (in \$2001) which included a preliminary \$5 allowance for contestability costs. The range was based on cost benchmarks from other jurisdictions, having reviewed NSW retail suppliers' costs. This approach has been maintained for this review, with contestability costs individually assessed.

Data submitted to this review indicates that retail suppliers have incurred total operating, maintenance and depreciation costs in the range \$41 to \$62 per customer in 2001.³⁶ This is close to the allocated range, however, retail suppliers' projections indicate that operating costs will increase substantially above this between 2002 and 2004. Retail suppliers argued that the current \$40 - \$60 operating cost allowance is inadequate.

³⁶ With the exception of AIEW whose costs are over \$85 per customer. The analysis excludes all advertising, marketing, promotion and FRC related costs.

The Tribunal conducted discussions with the retail suppliers to identify the key factors driving the upward trend. It is recognised that the majority of the increase in costs is attributable to computer processing, billing and revenue collection. These costs are in addition to contestability costs which have been claimed separately.

The Tribunal obtained updated information on benchmark costs available for other jurisdictions. The benchmarks are presented in Table A3.2. Since the December 2000 Determination, OFGEM (UK) have revised their initial proposals and the Essential Services Commission of Victoria (ESC) have conducted a review of retail electricity tariffs (December 2001). The Tribunal recognises that in comparison to the more recent benchmarks from electricity jurisdictions, the Tribunal's allowance in the December 2000 Determination is at the lower end of the range.

Table A3.2 Benchmark comparisons from other jurisdictions (\$2001)

Jurisdiction	Range (\$/customer)	Context
Victoria (Essential Services Commission)	\$50-80	<i>Office of Regulator General's decision including FRC, Dec 2001</i>
UK Public Electricity Suppliers (PESs)	\$68-\$84 ³⁷	Regulator's final proposals for 2001 (98/99 prices), Dec 1999, includes metering costs
Pan European Countries (Data Monitor)	\$46-\$98 ³⁸	<i>Utilities Market Report by Data Monitor, Sept 2001</i>
Tasmanian Electricity	\$81	<i>OTTER decision, 1999, includes metering costs</i>
UK Public Electricity Suppliers (PESs)	\$34-67 ³⁹	Regulators' proposals, Oct 1999 includes metering costs
US Electricity industry ⁴⁰		- Telecommunications Industry benchmark
• Flaim (2000)	\$34	- Electricity industry benchmark includes metering costs and customer acquisition costs
• Joskow (2000)	\$131-\$186	
• Jacobs (1999)	\$264	- Electricity Industry benchmark, includes metering costs and customer acquisition costs

In submissions to this review, there is comment that a common benchmark ignores the variability of customer size and type between retail suppliers. However, the Tribunal maintains the view expressed in the December 2000 Determination, that default service costs should reflect an industry standard. It is evident from the data submitted, that while a number of retail activities exhibit economies of scale, retail suppliers' costs are similar on a per customer basis, which suggests that a range for operating costs is appropriate.

As a result of its analysis, the Tribunal believes that an increase in the operating cost range is appropriate, and has set the range for 2002-2004 at \$45-\$75 per customer which includes a provision for contestability costs.

³⁷ OFGEM, December 1999, *Reviews of Public Electricity Suppliers 1998 to 2000 Supply Price Control Review, Final Proposals*. Supply business costs (retail operating costs) are reported to be in the range £34-£42 (1998/99 prices). Estimates provided above are conservative given current exchange rates are £0.36/ AS, however for this calculation, we have assumed exchange rates for 1999 as being closer to £0.50/ AS.

³⁸ Pan European countries are France, Italy and Spain. The report indicates European electricity retail suppliers' are averaging costs in the range US\$25-50. We have assumed US\$0.54/ AS.

³⁹ IPART, *Regulated Retail Prices for Electricity to 2004*, Determination, December 2000.

⁴⁰ IPART, *Regulated Retail Prices for Electricity to 2004*, Determination, December 2000.

Contestability costs

The initial retail operating cost range included an allowance of \$5 for contestability costs, as at that stage the amount of costs likely to be incurred was not known with any certainty. At the time, the Tribunal indicated that the allowance would be updated once further analysis was undertaken during the mid-term review.

The Tribunal engaged a consultant who provided an initial report on each retail supplier and a supplementary report. In addition, the retailers were provided with the opportunity to discuss their claim and the consultant's recommendation with the Tribunal. The Tribunal has now concluded its review of contestability costs incurred, and likely to be incurred, by the respective retail suppliers and has incorporated these costs in the retail operating cost range.

Profit Margin

Tribunal has maintained the retail profit margin at 1.5-2.5 per cent

The net profit margin represents the reward to investors for committing capital to a business. The level of profit margin is influenced by the level of risk associated with energy purchasing costs, customer default and bad debt, and competition from electricity substitutes. In its December 2000 Determination, the Tribunal allowed a net profit margin in the range of 1.5 to 2.5 per cent of sales turnover. The basis for this decision was:

- energy purchasing risks have been eliminated by proposed Electricity Tariff Equalisation Fund (ETEF) arrangements and so a premium for this risk is not required
- the regulated customer base is likely to evolve to a 'riskier' profile as the competitive retail market matures
- the risk differential between small retail customer groups is likely to be very small and does not warrant differential margins in regulated retail tariffs and
- it is not desirable from an economic efficiency or equity perspective to build an additional margin into the net profit margin that promotes customer switching.

During the mid-term review, the Tribunal re-examined these factors and concluded that the assessment of the profit margin in the December 2000 Determination remains appropriate for the remaining term of the regulatory period. The reasons supporting the Tribunal's decision are set out below.

Energy purchase risk eliminated

The New South Wales Government established the ETEF at the start of 2001. At the time of the original Determination these arrangements were still being finalised. The ETEF effectively allows retail suppliers to purchase electricity to supply regulated customers at a fixed price determined by the ETEF administrators.⁴¹ This arrangement should eliminate all energy purchase price risk for retail suppliers supplying customers who remain on the regulated tariff.

The Tribunal's original decision not to allow a margin for energy purchase price risk remains appropriate.

⁴¹ There are two prices — a peak and an off-peak price which vary across retail suppliers.

Benchmarks

For the December 2000 Determination, the Tribunal examined benchmarks for the net profit margin established in the previous Determination and also the experience in the United Kingdom. Since then, the ESC in Victoria conducted a review of regulated retail prices in its jurisdiction and specifically identified benchmarks for net profit margins based on similar sources as the Tribunal's December 2000 Determination.

The consultants that undertook the benchmark review for ESC recommended a range of 2.5 per cent to 5 per cent for the net profit margin in Victoria. In its submission, EnergyAustralia argued that this finding supported its call for an increased profit margin in New South Wales regulated retail tariffs.

The Tribunal believes that this is not an appropriate range for New South Wales. The primary reason is that retail suppliers in Victoria do not have access to a scheme similar to ETEF that eliminates energy purchase price risk. The consultants took explicit account of energy purchase price risk in recommending a higher range for Victoria than is in place in New South Wales.

Riskiness in customer base

As full retail competition (FRC) progresses, it seems reasonable to expect that the regulated customer base would become more 'risky'. More profitable customers are attracted into the contestable market, leaving a smaller regulated customer base comprising of less profitable customers.

With retail competition only just being extended to small retail customers, the Tribunal believes it is too early to judge the impact of FRC on business risk. One possible measure of future impact is the extent to which the regulated customer base is expected to alter. The Ministry of Energy and Utilities (MEU) publishes monthly data on customers who have chosen new service offerings⁴² ie switched to a new retail supplier or to a negotiated contract. As at 29 May 2002, approximately 95,000 customers had moved.⁴³ In volume terms, the effect on regulated sales might be higher if higher value (volume) customers are the first to be attracted away.

In setting an allowance for the net profit margin between 1.5 and 2.5 per cent in its December 2000 Determination, the Tribunal recognised that standard retail suppliers should receive a higher margin for serving small retail customers in the context of a contestable market. To the extent that increase customer churn rates are correlated with an increase in the riskiness of a retail supplier's customer base, then retail suppliers should receive a higher net profit margin to compensate for this risk. However, in the Tribunal's opinion, this is a question of what value *within* the current range should be applied rather than whether the range should be increased.

The Tribunal believes that the current range provide sufficient compensation to retail suppliers for the increased risk they are likely to face as FRC impacts on their customer base.

⁴² Aggregate number of electricity and gas customers.

⁴³ Ministry of Energy & Utilities, *Number of Customers Exercising Choice May 2002*, www.doe.nsw.gov.au.

Allowance to promote competition

As discussed in section 4.3 of the Report, some submissions to the mid-term review have argued for the inclusion of an additional allowance to promote competition. AGL's submission⁴⁴ argues that regulated prices do not provide sufficient scope for second tier retail suppliers to effectively compete in all segments of the New South Wales electricity market. In regard to the net profit margin, they challenge the Tribunal's decision to exclude an additional margin to encourage competition. They point out that:

- second tier retail suppliers do not have access to the ETEF so require a higher margin for risk, reducing their ability to compete for regulated customers
- value added services incur additional costs which are paid for out of the premium customers might be prepared to pay — value adding does not address the problem of competing against low regulated margins
- the level of 1.5 to 2.5 per cent does not adequately cover the risk of bad debt.

AGL notes that the margin ought to take into account 'the level of risk for energy purchases'.

Pulse Energy also submitted that the Tribunal should allow 'headroom' in its tariffs to encourage competition.⁴⁵ They suggest that a business facing wholesale energy price risk would require a return of between 8 to 10 per cent on revenues to adequately compensate its investors.

The Tribunal believes that its arguments against setting artificially high tariffs to promote competition remain valid. In principle, if the Tribunal has established benchmarks that reflect the efficient costs, then there is not a case for including a margin to promote competition.

Nevertheless, it should be noted that the energy cost component of the retail margin has been set on the basis of the LRMC rather than the average market price. To the extent that the market price is below the estimated LRMC, costing energy on this basis is likely to offer retail suppliers the opportunity to undercut the regulated retail tariff.

Loss factors

The Tribunal has updated the loss factors to represent the sales estimates provided by retail suppliers

The target levels of regulated retail tariffs include a retail supplier-specific, separate dollar per MWh component for small retail customers (urban and rural) to account for energy losses.

The Tribunal based its cost estimates in the December 2000 Determination on the disaggregated loss factors applicable in 2001, as published by NEMMCO. These were broadly consistent with the aggregate cost projections of the standard retail suppliers.

⁴⁴ AGL submission, 25 March 2002 to *Mid-Term Review of Regulated Retail Prices to 2004*, www.ipart.nsw.gov.au.

⁴⁵ Pulse Energy submission, 19 March 2002 to *Mid-Term Review of Regulated Retail Prices to 2004*, www.ipart.nsw.gov.au.

The Tribunal has obtained more recent information from the retail suppliers to enable it to review the original values and have included the estimates in Table A3.3 in the target value.

Table A3.3 Tribunal's Loss Factor Assumptions for 2002-2004

Loss Factors (transmission loss factors plus distribution loss factors)	Urban %	Rural %
EnergyAustralia	5.4	5.4
Integral Energy	8.3	8.3
Country Energy ⁴⁶	10.8	17.7
Australian Inland Energy & Water	20.0	20.0

Source: calculated on loss factors published by NEMMCO.

Network Component 'N'

Network charges remain as a pass-through item in the final charge

Network charges have been included in the regulated retail tariff as a pass-through item, whereby the actual network charge (N) incurred is added to the retail component (R) to arrive at the target tariff. The Tribunal remains of the view that this is the most appropriate way to apply network charges within the current tariff structure. The reasons for this decision under the December 2000 Determination remain valid and are outlined in the December 2000 Report.

A related topic which was raised at the Public Forum was the inconsistency of network price-constraints with retail price-constraints. This is addressed in this report *Chapter 3 – Transition to Target Tariffs*.

⁴⁶ The loss factors for Country Energy have changed as a result of the amalgamation of the former areas and the averaging of the transmission and distribution loss factors.

APPENDIX 4 GREEN ENERGY OBLIGATIONS

New South Wales benchmark licence obligations

At the time of the December 2000 Determination, retail suppliers were required as part of their licence conditions to develop greenhouse gas reduction strategies. In particular, these strategies were to outline the steps required for the retail supplier to meet its *emissions* benchmark requirement. The emissions benchmark was based upon the overall benchmark objective of reducing emissions from electricity supplied to NSW customers to 5 per cent below the 1989/99 per capita levels by 2000-01 (calculated as 7.27 tonnes CO₂ equivalent (CO₂-e)).

A key element of the original framework is that there were no immediate penalties for failing to meet the emission benchmarks.

A review of the operation of the benchmark scheme found that it failed to meet its objectives of reducing emissions to the benchmark level. Actual emissions were 8.42 tonnes per capita compared to the target level of 7.27 tonnes. This failure of the scheme has prompted the Government to revise key elements of the scheme and extend its operation. From 1 July 2002, electricity retail suppliers will be required to gradually reduce their emissions (from current levels) to achieve the benchmark of 7.27 tonnes per capita.

The Government is amending the design of the benchmark scheme to improve incentives for compliance. Key changes are listed below.

- Retail supplier obligations will relate to emissions performance against a benchmark rather than obligations to prepare a strategy, which will be removed.
- Penalties for a retail supplier not meeting its emissions benchmark will be introduced. These will be structured as a dollar amount per tonne of CO₂-e by which the retail supplier has exceeded its benchmark. The current proposal is that penalties will be administered by IPART.
- Reducing uncertainty for retail suppliers by (1) calculating their share of total allowable emissions as the ratio of their sales to the market to (the regulator's) start of year forecast of total sales for the year; and (2) applying a pool coefficient based on its value in an earlier year.
- Increasing the flexibility of the scheme to reduce the cost of compliance by:
 - allowing increases of output from existing generators beyond a baseline to be assignable, thereby encouraging greater use of relatively 'greenhouse-friendly' plant
 - allowing the trading of certificates representing tonnes of CO₂-e abated
 - introducing limited provisions to bank surplus certificates, and for a limited shortfall allowance to be carried forward to the next year without penalty.
- Removal of pro-rata rules relating to interstate generation.
- Extended liability to cover customers that purchase electricity directly from the pool.
- Treating increases in output above a baseline from existing zero-emissions generators as capable of being assigned, regardless of the cause of the increase.
- Allowing retail suppliers to retain credits for fuel substitution if the customer switches retail suppliers, and allowing these credits to be tradeable.

- Allowing Category A generation to be assignable and tradeable.

The penalty for failing to meet the benchmark targets will be linked to the cost of achieving the target. This will effectively cap the compliance cost of the benchmark requirements for retail suppliers. The Government has announced that it will set the value of the penalty at a maximum of \$15/tonne.

Commonwealth Mandatory Renewable Energy Targets (MRET)

Retail suppliers are also subject to the Commonwealth Government's Mandatory Renewable Energy Target (MRET) scheme. This scheme commenced in 2001 and requires that wholesale purchasers of electricity proportionately contribute towards the generation of 9,500GWh of renewable energy per year by 2010. The scheme has a set of enforceable interim targets, set out Table A4.1. Liable parties need to surrender renewable energy certificates to the Office of the Renewable Energy Regulator to meet their obligation under the targets. Those businesses not meeting these interim targets are liable for a penalty of \$40/MWh, redeemable if the shortfall is made up within three years.

Table A4.1 Interim targets for MRET scheme

Year	Required additional GWh
2001	300
2002	1100
2003	1800
2004	2600
2005	3400
2006	4500
2007	5600
2008	6800
2009	8100
2010-2020	9500

Source: Office of Renewable Energy Regulator.

APPENDIX 5 LIST OF SUBMISSIONS

Organisation	Name
AGL Energy Sales & Marketing	Canale, Sandy
Australian Inland Energy and Water	Ray, Adrian
Coolamon Ganmain Anglican Parish	Edyvean, Beryl
Country Energy	Murray, Craig
Country Women's Association of NSW	Brill, Jan L
Country Women's Association of NSW	Last, Pauline
Country Women's Association of NSW	Maloney, Merle
Country Women's Association of NSW	Mattingly, Joyce
Country Women's Association of NSW	Phegan, Anne. E.
Country Women's Association of NSW	Terlich, Gwen
Currawarna Rural Fire Brigade	Astridge, Nan
EnergyAustralia	Broad, Paul
EnergyAustralia	Maltabarow, George
Eraring Energy	Grove-White, Gerry
Institute of Public Affairs	Moran, Alan
Integral Energy	Powis, Richard
Macquarie Generation	Welfare, Luke
Nature Conservation Council of NSW	Ridge, Kathy
Origin Energy Retail	Hughson, Beverley
Public Interest Advocacy Centre	Benson, Trish
Public Interest Advocacy Centre	Wellsmore, Jim
Pulse Energy	Robertson, Stephen
TXU Electricity Limited	Demarte, Caryle

APPENDIX 6 GLOSSARY OF ACRONYMS

2001 dollars (\$ 2001)	Dollars expressed in 2001 dollars, ie real terms
ACCC	Australian Competition and Consumer Commission
AGL	The Australian Gas Light Company
AIEW	Australia Inland Energy & Water
Amending Act	The <i>Electricity Supply Amendment Act, 2000</i>
CGEY	Cap Gemini Ernst & Young
CO ₂ -e	CO ₂ equivalent
Code	National Electricity Code
CPI	Consumer Price Index
Determination	Refers to the Determination accompanying this report
December 2000 Report	Report accompanying the <i>Recommendation in December 2000, Regulated Retail Prices for Electricity to 2004 Final Report, December 2000</i>
EAPA	Energy Accounts Payment Assistance scheme
ESA	The <i>Electricity Supply Act, 1995</i> as amended by the Amending Act
Electricity Supply Act	The <i>Electricity Supply Act, 1995</i> as amended by the Amending Act
ETEF	Electricity tariff equalisation fund
EWON	Energy & Water Ombudsman NSW
GSE	Great Southern Energy
GST	Goods & Service Tax
GWh	Gigawatt hour (one GWh=1000 megawatt hours (MWh) or one million kilowatt hours (kWh))
IPART	The Independent Pricing and Regulatory Tribunal of NSW established under the <i>Independent Pricing and Regulatory Tribunal Act, 1992 (NSW)</i>
kWh	Kilowatt hour (the standard unit of energy which represents the consumption of electrical energy at the rate of one kilowatt over the period of one hour)
LRMC	Long Run Marginal Cost
Minister	Minister for Energy
MRET	Mandatory Renewable Energy Targets
MWh	Megawatt hour (one MWh=1000 kilowatt hours)
NEC	National Electricity Code
NEM	National electricity market

NEMMCO	National Electricity Market Management Company Limited
N component	Network component of the target for a regulated retail tariff
OP2, OP3, OP4	Names of tariffs provided by retailers which will be subject to the extended off-peak tariff
R Component	Retail component of the target for a regulated retail tariff
Recommendation	December 2000 Recommendation which was issued as a Determination under the ESA in December 2000
Tribunal	The Independent Pricing and Regulatory Tribunal of New South Wales established under the <i>Independent Pricing and Regulatory Tribunal Amending Act, 1992</i>

Determination

Determination in a report of the Tribunal to the Minister for Energy
under section 43EB of the *Electricity Supply Act 1995*



INDEPENDENT PRICING AND REGULATORY TRIBUNAL
OF NEW SOUTH WALES

1 PREAMBLE

- 1.1 The NSW government has progressively opened its electricity retail industry to competition.
- 1.2 All customers are now permitted to choose their retail supplier for electricity, including small retail customers (currently defined as those consuming less than 160MWh per year).
- 1.3 If a small retail customer does not wish to negotiate supply in the competitive market, the customer may obtain supply from its 'standard retail supplier' under a standard form customer supply contract and under a regulated tariff (section 34 of the ESA). A standard retail supplier is a retail supplier to whose licence is attached a standard retail supplier's endorsement in respect of a designated supply district (section 33A of the ESA).
- 1.4 It is a condition of a standard retail supplier's licence that tariffs and charges for the supply of electricity under a standard form customer supply contract must be in accordance with any relevant determination of the Tribunal (section 36 of the ESA). The Minister may refer to the Tribunal, for investigation and report, the determination of regulated retail tariffs or regulated retail charges, or both (section 43EA of the ESA). If such a referral is made, the Tribunal may determine these in a report to the Minister (section 43EB of the ESA).
- 1.5 In December 2000, the Tribunal published a recommendation in a report to the Minister entitled *Regulated retail prices for electricity to 2004*, made under an arrangement entered into between the Premier and the Tribunal on 14 July 2000. The recommendation was taken to be a determination under section 43EB of the ESA (clause 37 of Schedule 6 to the ESA). It applied for the period 1 January 2001 to 30 June 2004 ('December 2000 determination').
- 1.6 On 29 January 2002 the Tribunal received a referral from the Minister to undertake a mid-term review of the December 2000 determination to assess the robustness of regulated retail prices following the introduction of full retail competition. The Minister requested the Tribunal under section 43EA of the ESA to investigate and report on the determination of regulated retail tariffs for the period 1 July 2002 to 30 June 2004. This Determination is made pursuant to that referral.

2 DEFINITIONS AND INTERPRETATION

2.1 Definitions

Average Prices means average prices over all regulated retail tariffs immediately prior to the relevant Price change date, expressed in cents per kilowatt hour. Average prices are calculated by dividing the total revenue from all small retail customers on regulated retail tariffs, in the 12 months immediately prior to the Price change date (in cents), by the total consumption in that period (in kWh). The total revenue for this purpose is to be calculated as if the tariffs applying immediately prior to the Price change date applied to the entire 12 month period (whether or not this was actually the case)

business day means a day other than a Saturday, Sunday or public holiday in New South Wales

Commencement Date means the date that this Determination commences, namely 1 July 2002

CPI has the meaning set out in Schedule 1

CPI^{-GST} has the meaning set out in Schedule 1

DCPI₁^{-GST} means the change in CPI between 1999 and 2000 exclusive of the net impact of GST and is the number derived from the application of the formula described in Schedule 1

DCPI₂^{-GST} means the change in CPI between 2000 and 2001 exclusive of the net impact of GST and is the number derived from the application of the formula described in Schedule 1

DCPI₃^{-GST} means the change in CPI between 2001 and 2002 exclusive of the net impact of GST and is the number derived from the application of the formula described in Schedule 1

December 2000 determination is defined in clause 1.5

Determination means this determination

ESA means the *Electricity Supply Act 1995 (NSW)*

Estimated Average Prices means estimated average prices over all regulated retail tariffs from the relevant Price change date, expressed in cents per kilowatt hour. Estimated average prices are calculated by dividing the total revenue that would be derived from all small retail customers on regulated retail tariffs in the 12 months immediately following the Price change date (in cents) by total consumption (in kWh). The total revenue for this purpose is to be calculated:

- (a) as if the relevant tariffs would apply for the entire 12 month period commencing on the Price change date (whether or not this is actually the case); and
- (b) by applying the relevant tariffs to the pattern and volume of electricity consumption of the relevant customers for the 12 months immediately preceding the Price change date

green premiums are any amounts voluntarily payable by a customer in respect of electricity that is generated from renewable energy sources or other sources of energy that provide improved environmental outcomes

GST means the Goods and Services Tax as defined in *A New Tax System (Goods and Services Tax) Act 1999 (Cth)*

miscellaneous network charges are any charges levied by a distribution network service provider on a standard retail supplier for network services other than use of system services in relation to a relevant small retail customer

Miscellaneous transaction is a transaction listed in clause 8.4

network use of system component means the charge levied by a distribution network service provider on a standard retail supplier for use of system services provided by a network service provider in relation to a relevant small retail customer, for the year commencing on a Price change date

nominal terms means amounts expressed in dollars of the day

NMI means National Metering Identifier, and is as defined in the National Electricity Code

Price change date is defined in clause 5.1

Target level for a regulated retail tariff is the level specified in clause 5.2

Termination date means the date that this Determination ends, namely 30 June 2004 or such earlier or later date as may lawfully be provided

Total Previous Year's Bills means, in relation to a small retail customer, the total of the bills issued to that customer for the 12 months immediately preceding a Price change date. The total of the bills for this purpose is to be calculated as if the tariffs applying immediately prior to the Price change date applied to the entire 12 month period (whether or not this was actually the case)

Tribunal means the Independent Pricing and Regulatory Tribunal of New South Wales established under the *Independent Pricing and Regulatory Tribunal Act 1992 (NSW)*

use of system services is as defined in the National Electricity Code

2.2 Interpretation

- 2.2.1 Words and phrases used in this Determination that are defined in the ESA have the same meaning as in the ESA.
- 2.2.2 In the interpretation of this Determination a construction that would promote the purpose or object expressly or impliedly underlying the ESA is to be preferred to a construction that would not promote that purpose or object.
- 2.2.3 The reference to an Act, Code, legislation or law includes regulations and other instruments under it and consolidations, amendments, re-enactments or replacements of them.
- 2.2.4 A schedule means a schedule to this Determination.
- 2.2.5 Words importing the singular include the plural and vice versa. For instance, the reference to a tariff (or regulated retail tariff) includes tariffs (or regulated retail tariffs) and vice versa.
- 2.2.6 Where a word is defined in this Determination (including because of the operation of clause 2.2.1), other grammatical forms of that word have a corresponding meaning.
- 2.2.7 The explanatory notes and footnotes do not form part of this Determination, but in cases of uncertainty may be relied on for interpretation purposes.
- 2.2.8 A reference to a customer or a small retail customer, unless the context otherwise provides, is a reference to a small retail customer being supplied with electricity by its standard retail supplier, under a standard form customer supply contract.
- 2.2.9 For any purpose under this Determination that involves counting or determining the number of customers, each relevant NMI is to be regarded as one customer.

- 2.2.10 Nothing in this Determination affects the ability of a standard retail supplier to charge a small retail customer for green premiums, in addition to regulated retail tariffs, where the small retail customer so elects. A small retail customer may elect to pay green premiums without affecting that customer's status as having chosen to be supplied under a standard form customer supply contract rather than a negotiated customer supply contract.
- 2.2.11 A reference to a bill or to total revenue (other than in clause 8 or Schedules 2 or 3) means:
- (a) a bill or total revenue inclusive of the applicable amount (if any) of GST payable; and
 - (b) a bill or total revenue as if it contained no amounts other than for or derived from regulated retail tariffs and GST on them (Examples of the excluded amounts are amounts for regulated retail charges for Miscellaneous transactions, green premiums or miscellaneous network charges).
- 2.2.12 A time of use tariff, which contains more than one variable rate for consumption depending upon the time that the consumption occurs, is considered to be a single tariff. Accordingly:
- (a) the reference in clause 5.2(c) to no Fixed R being allowed for off-peak means, in respect of a time of use tariff that is relevant for peak and off-peak periods, that there is one Fixed R for that time of use tariff; and
 - (b) the references in clause 5.2(d)(i) and (ii) to 'each tariff' set out in the table for Variable R include references to each relevant rate which forms part of a time of use tariff.

3 APPLICATION OF DETERMINATION

- 3.1 This Determination is made under section 43EB of the ESA.
- 3.2 This Determination commences on the Commencement Date and ends on the Termination Date.
- 3.3 This Determination sets the regulated retail tariffs that standard retail suppliers can charge small retail customers:
- (a) whose premises are in a standard retail supplier's supply district; and
 - (b) who are supplied electricity at those premises by a standard retail supplier under a standard form customer supply contract.
- 3.4 The December 2000 determination is repealed from the Commencement Date, with the exception of clause 7 and Schedules 2 and 3 of that determination (Regulated Retail Charges) and any other provisions necessary to give effect to that clause and those Schedules. For convenience, clause 7 and Schedules 2 and 3 of that determination are reproduced as clause 8 and Schedules 2 and 3 of this Determination (with minor amendments that do not affect the substance).

4 REGULATED RETAIL TARIFFS

4.1 Retail tariffs of each of the standard retail suppliers, EnergyAustralia, Integral Energy, Country Energy and Australian Inland Energy and Water:

- (a) that were, as of 30 June 2002, applicable to that standard supplier's small retail customers under a standard form customer supply contract; and
- (b) that are on the register kept by the Tribunal for the purpose of this clause,

other than any component of those tariffs that represents a green premium, will be taken to be the regulated retail tariffs for each of them in the relevant supply district for the purpose of this Determination, from the Commencement Date.

5 TARGET LEVELS OF REGULATED RETAIL TARIFFS

5.1 Under this Determination, there is a Target level for each regulated retail tariff and for each of the periods:

- (a) 1 August 2002 to 30 June 2003; and
- (b) 1 July 2003 to 30 June 2004.

Alternatively, a retailer may elect for either or both of those periods to commence up to 14 days after 1 August 2002 and 1 July 2003 respectively. Each date on which those periods commence (that is, 1 August 2002 and 1 July 2003, or, if elected by a retailer, up to 14 days after those dates) is a 'Price change date'.

5.2 The Target level for a regulated retail tariff is:

$N + R$

Where

- (a) N is the applicable network use of system component for the small retail customer and
- (b) R is a retail component, comprising:
 - (i) a fixed charge ('**Fixed R**') expressed in dollars per customer per year; and
 - (ii) a variable charge ('**Variable R**') expressed in c/kWh (cents per kilowatt hour).
- (c) **Fixed R** at the Target level for each regulated retail tariff (with the exception of off-peak and extended off-peak, for which no Fixed R is allowed) of each standard retail supplier supplying the relevant supply district is:
 - (i) in the case of a Price change date for the 2002/03 period:
the relevant amount for each standard retail supplier set out in the following table $\times (1 + \Delta\text{CPI}_1^{-\text{GST}}) \times (1 + \Delta\text{CPI}_2^{-\text{GST}})$; and
 - (ii) in the case of a Price change date for the 2003/04 period:
the relevant amount for each standard retail supplier set out in the following table $\times (1 + \Delta\text{CPI}_1^{-\text{GST}}) \times (1 + \Delta\text{CPI}_2^{-\text{GST}}) \times (1 + \Delta\text{CPI}_3^{-\text{GST}})$

Fixed R (\$ per customer per year)

Standard retail supplier	Fixed R
For the supply district of EnergyAustralia under the licence held by it immediately before the Commencement Date.	44.25
For the supply district of Integral Energy under the licence held by it immediately before the Commencement Date.	48.75
For the supply district of Country Energy under the licence held by it immediately before the Commencement Date.	47.25
For the supply district of Australian Inland Energy and Water under the licence held by it immediately before the Commencement Date.	40.50

- (d) **Variable R** at the Target level for each regulated retail tariff of each standard retail supplier supplying the relevant supply district is:
- (i) in the case of a Price change date for the 2002/03 period:
the relevant amount for each standard retail supplier and for each tariff set out in the following table $\times (1 + \Delta\text{CPI}_1^{\text{-GST}}) \times (1 + \Delta\text{CPI}_2^{\text{-GST}})$; and
 - (ii) in the case of a Price change date for the 2003/04 period:
the relevant amount for each standard retail supplier and for each tariff set out in the following table $\times (1 + \Delta\text{CPI}_1^{\text{-GST}}) \times (1 + \Delta\text{CPI}_2^{\text{-GST}}) \times (1 + \Delta\text{CPI}_3^{\text{-GST}})$.

Variable R (c/kWh)

	Urban			Rural		
	standard	off-peak	extended off-peak	standard	off-peak	extended off-peak
For the supply district of EnergyAustralia under the licence held by it immediately before the Commencement Date.	5.51	3.57	4.44	5.51	3.57	4.44
For the supply district of Integral Energy under the licence held by it immediately before the Commencement Date.	5.78	3.65	4.29	5.78	3.65	4.29
For the supply district of Country Energy under the licence held by it immediately before the Commencement Date.	6.01	3.74	4.42	6.38	3.95	4.68
For the supply district of Australian Inland Energy and Water under the licence held by it immediately before the Commencement Date.	6.55	3.99	4.51	6.55	3.99	4.51

For the purposes of the above table and the definitions below:

controlled load means a load which is active only at certain times, where such times are determined by the network

extended off-peak rates apply in respect of all of a customer's controlled load where that load is active both during off-peak periods and at times other than off-peak periods

off-peak periods are from 10:00pm to 7:00am on business days and all times on days other than business days, unless otherwise agreed by the Tribunal with the standard retail supplier following a written request from that standard retail supplier

off-peak rates apply:

- (a) where a customer has time of use metering, to that customer's electricity consumption during off-peak periods; and/or
- (b) in respect of a customer's controlled load where that load is active only during off-peak periods

peak periods are from 7:00am to 9:00am and 5:00pm to 8:00pm on business days, unless otherwise agreed by the Tribunal with the standard retail supplier following a written request from that standard retail supplier

rural rates apply in respect of customers to whom the standard retail supplier applies rural tariffs

shoulder periods are from 9:00am to 5:00pm and 8:00pm to 10:00pm on business days, unless otherwise agreed by the Tribunal with the standard retail supplier following a written request from that standard retail supplier

standard rates apply:

- (a) where a customer has time of use metering, to that customer's electricity consumption during peak and shoulder periods; and
- (b) where a customer does not have time of use metering, to all electricity consumption of that customer other than controlled loads

urban rates apply in respect of customers to whom the standard retail supplier applies tariffs other than rural tariffs

[**Note:** The target levels set out in this clause 5.3 apply to the relevant geographical areas, or supply districts, supplied by EnergyAustralia, Integral Energy, Country Energy and Australian Inland Energy and Water as at 30 June 2002.

If the supply district of a standard retail supplier changes from that described in clause 5.3, the Tribunal intends to request that the Minister refer to it, for investigation and report, the determination of regulated retail tariffs under section 43EA of the ESA, based on the changed supply district.]

5.3 Each regulated retail tariff is considered to be at the Target level for that tariff and for that Price change date if the standard retail supplier's total estimated revenue from that tariff for the year commencing on the Price change date would equal the total estimated revenue that a tariff whose components are at the level in clause 5.2 would give for that year.

5.4 For the purposes of clause 5.3, a standard retail supplier's total estimated revenue from a tariff for a year commencing on a Price change date is to be calculated:

- (a) as if the relevant tariff would apply for the entire 12 month period commencing on the Price change date (whether or not this is actually the case); and
- (b) by applying the relevant tariff to the pattern and volume of electricity consumption of customers on that tariff for the 12 months immediately preceding the Price change date.

5.5 Although the test of whether a regulated retail tariff is at the Target level is by reference to the standard retail supplier's total revenue from that tariff (calculated in accordance with clauses 5.3 and 5.4), where practicable a standard retail supplier should ensure that regulated retail tariffs reflect the structure and levels specified in clause 5.2.

6 REGULATED RETAIL TARIFFS TO MOVE TOWARD TARGET LEVEL

6.1 A standard retail supplier may only amend a regulated retail tariff on a Price change date and in the manner specified in this Determination.

6.2 A standard retail supplier who has a regulated retail tariff that, immediately prior to a Price change date, is at or above the Target level for that tariff and for that Price change date (calculated under this Determination), must not increase that tariff in nominal terms.

- 6.3 Subject to clause 6.4, a standard retail supplier who has a regulated retail tariff that, immediately prior to a Price change date, is below the Target level for that tariff and for that Price change date (calculated under this Determination), must increase that regulated retail tariff up to, but not exceeding the Target level for that tariff and for that Price change date. The increase in the tariff is to be effective from the Price change date.
- 6.4 If a standard retail supplier is unable to increase a regulated retail tariff to the Target level without breaching one or more of the price constraints in clause 7, then the standard retail supplier must increase that regulated retail tariff to the maximum extent allowed by those constraints, without breaching any of them or exceeding the Target level.

7 PRICE CONSTRAINTS

- 7.1 At each Price change date, a standard retail supplier must limit price increases as follows:
- (a) in the case of a Price change date for the 2002/03 period:

$$\text{Estimated Average Prices}(2002/03) \leq \text{Average Prices}(2001/02) \times (1 + \Delta\text{CPI}_{2-\text{GST}})$$
- (b) in the case of a Price change date for the 2003/04 period:

$$\text{Estimated Average Prices}(2003/04) \leq \text{Average Prices}(2002/03) \times (1 + \Delta\text{CPI}_{3-\text{GST}}).$$
- 7.2 A standard retail supplier must ensure that the total amount of the bills that would be issued to any residential customer for the 12 months immediately following the Price change date would not exceed the greater of:
- (a) \$25 above Total Previous Year's Bills; and
- (b) the amount of:
- (i) in the case of a Price change date for the 2002/03 period:

$$\text{Total Previous Year's Bills} \times (1 + \Delta\text{CPI}_{2-\text{GST}}) \times 1.02;$$
 or
- (ii) in the case of a Price change date for the 2003/04 period:

$$\text{Total Previous Year's Bills} \times (1 + \Delta\text{CPI}_{3-\text{GST}}) \times 1.02.$$
- 7.3 A standard retail supplier must ensure that the total amount of the bills that would be issued to any business customer for the 12 months immediately following the Price change date would not exceed the greater of:
- (a) \$50 above Total Previous Year's Bills; and
- (b) the amount of:
- (i) in the case of a Price change date in 2002/03:

$$\text{Total Previous Year's Bills} \times (1 + \Delta\text{CPI}_{2-\text{GST}}) \times 1.05;$$
 or
- (ii) in the case of a Price change date in 2003/04:

$$\text{Total Previous Year's Bills} \times (1 + \Delta\text{CPI}_{3-\text{GST}}) \times 1.05.$$

- 7.4 For the purposes of clauses 7.2 and 7.3, the total amount of the bills that would be issued to a customer for the 12 months immediately following a Price change date is to be calculated:
- (a) as if the relevant tariff would apply for the entire 12 month period commencing on the Price change date (whether or not this is actually the case); and
 - (b) by applying the relevant tariff to the pattern and volume of electricity consumption of the relevant customer for the 12 months immediately preceding the Price change date.

8 REGULATED RETAIL CHARGES

- 8.1 Regulated retail charges apply to all small retail customers who elect to be supplied with electricity by a standard retail supplier under a standard form customer supply contract.
- 8.2 Regulated retail charges are charges that standard retail suppliers may charge to small retail customers supplied electricity under clause 8.1.
- 8.3 Regulated retail charges are separate from and additional to the regulated retail tariffs.
- 8.4 The maximum that a standard retail supplier may charge under a standard form customer supply contract for a Miscellaneous transaction listed below, is the maximum regulated retail charge corresponding to the Miscellaneous transaction listed.

Regulated retail charges – Maximum charge

Miscellaneous transaction	Maximum regulated retail charge
Fee for a dishonoured bank cheque	2 times the regular fee charged by the Bank to which the cheque is presented
Late payment fee	\$5.00
Security deposit	1.5 times average quarterly electricity account ¹ , or 1.75 times average 2-monthly electricity account, or 2.5 times the average monthly electricity account Interest may not be levied on a security deposit

- 8.5 A standard retail supplier may not impose a charge or fee for a Miscellaneous transaction (whether the transaction is described as a Miscellaneous transaction or otherwise) except as permitted by this clause 8 and Schedules 2 and 3.
- 8.6 A standard retail supplier may impose a regulated retail charge on a small retail customer for a dishonoured bank transaction only if the standard retail supplier actually incurs a bank fee for that dishonoured bank transaction.

¹ The amount of the average account will vary between standard retail suppliers, depending on average tariff levels and average consumption. The amount of the average retail account should be calculated as part of the tariff setting process, and the amount of the required security deposits posted on the standard retail suppliers' tariff schedules.

8.7 A standard retail supplier may only impose a regulated retail charge on a small retail customer for a late payment transaction in accordance with Schedule 2.

8.8 A standard retail supplier:

- (a) can only require a small retail customer to pay a security deposit where the requirements set out in Part A of Schedule 3 are met; and
- (b) must repay a security deposit to a small retail customer in accordance with Part B of Schedule 3 as soon as the relevant small retail customer meets the requirements in Part B of Schedule 3.

SCHEDULE 1 DEFINITION OF CPI^{GST} (CLAUSE 2)

Definition of CPI^{GST}

1.1 Interpretation

CPI means the consumer price index, All Groups index number for the weighted average of eight capital cities as published by the Australian Bureau of Statistics, or if the Australian Bureau of Statistics does not or ceases to publish the index, then CPI will mean an index determined by the Tribunal that is its best estimate of the index.

CPI^{GST} means the CPI exclusive of the net impact since 1 July 2000 of the GST and changes to any other Commonwealth, State or Territory taxes or charges, consequent upon the introduction of the GST, being either:

- (a) an index published by a person appointed by the Tribunal which is that person's best estimate of CPI^{GST}; or
- (b) an index determined by the Tribunal that is its best estimate of CPI^{GST}.

1.2 Application of the formula

DCPI₁^{-GST} means the number derived from the application of the following formula:

$$DCPI_1^{-GST} = \left(\frac{CPI_{Mar2000} + CPI_{June\ 2000} + CPI_{Sep2000}^{-GST} + CPI_{Dec2000}^{-GST}}{CPI_{Mar1999} + CPI_{Jun\ 1999} + CPI_{Sep\ 1999} + CPI_{Dec1999}} - 1 \right)$$

DCPI₂^{-GST} means the number derived from the application of the following formula:

$$DCPI_2^{-GST} = \left(\frac{CPI_{Mar2001}^{-GST} + CPI_{Jun2001}^{-GST} + CPI_{Sep2001}^{-GST} + CPI_{Dec2001}^{-GST}}{CPI_{Mar2000} + CPI_{Jun2000} + CPI_{Sep2000}^{-GST} + CPI_{Dec2000}^{-GST}} - 1 \right)$$

DCPI₃^{-GST} means the number derived from the application of the following formula:

$$DCPI_3^{-GST} = \left(\frac{CPI_{Mar2002}^{-GST} + CPI_{Jun2002}^{-GST} + CPI_{Sep2002}^{-GST} + CPI_{Dec2002}^{-GST}}{CPI_{Mar2001}^{-GST} + CPI_{Jun2001}^{-GST} + CPI_{Sep2001}^{-GST} + CPI_{Dec2001}^{-GST}} - 1 \right)$$

where:

- CPI is as defined and where the corresponding subtext (for example Jun₂₀₀₀) means the CPI for the quarter and of the year indicated (in the example, the quarter ending in June of the year 2000)
- CPI^{GST} is as defined and where the corresponding subtext (for example Jun₂₀₀₁) means the CPI for the quarter and of the year indicated (in the example, the quarter ending in June of the year 2001).

SCHEDULE 2 LATE PAYMENT FEE (CLAUSE 8)

1. Late payment fees must not be levied:
 - (a) during the period of an extension of time the small retail customer has to pay the electricity retail bill, agreed between the standard retail supplier and the small retail customer; or
 - (b) where a small retail customer has made a billing related complaint in relation to the relevant electricity retail bill to the Energy and Water Ombudsman NSW or another external dispute resolution body where that complaint is unresolved; or
 - (c) during the period of an instalment arrangement, where the small retail customer has entered into an instalment arrangement with the standard retail supplier to pay the electricity retail bill.
2. A late payment fee must be waived:
 - (a) where the small retail customer has contacted a welfare agency/support service for assistance; or
 - (b) where payment or part payment is by EAPA voucher²; or
 - (c) on a case by case basis as considered appropriate by the standard retail supplier or the electricity industry ombudsman under an approved electricity industry ombudsman scheme under the ESA.
3. A late payment fee may only be levied:
 - (a) on or after the date which is at least 5 business days after the due date shown on the electricity retail bill that is the subject of the late payment; and
 - (b) after the small retail customer has been notified in advance that the late payment fee will be charged if the account is not paid, or alternative payment arrangements entered into, within 5 business days of the due date.

² A voucher issued under the Energy Accounts Payments Assistance Scheme. This Scheme is administered by the NSW Department of Community Services.

SCHEDULE 3 SECURITY DEPOSITS (CLAUSE 8)

Part A

Residential small retail customers

A standard retail supplier may require a security deposit from a residential small retail customer prior to connection only if that small retail customer:

- (a) has left a previous supply address without settling an electricity retail bill (**debt**) owed to the standard retail supplier or any other standard retail supplier, the debt remains outstanding and the small retail customer has refused and refuses to make an arrangement to pay that debt; or
- (b) has been responsible for the illegal use of electricity within the previous two years; or
- (c) does not have a satisfactory credit history in the reasonable opinion of the standard retail supplier or cannot demonstrate satisfactory credit history with another retail supplier to the reasonable satisfaction of the small retail supplier, and the standard retail supplier has offered the small retail customer an instalment plan or other payment option (for example pay as you go by instalments, direct debit) and the small retail customer has refused, or failed to agree to the offer.

A standard retail supplier must not require a security deposit from a residential small retail customer after connection.

Business small retail customers

A standard retail supplier may require a security deposit from business small retail customers prior to connection only if the small retail customer:

- (a) does not have a satisfactory credit history in the reasonable opinion of the standard retail supplier or cannot demonstrate a satisfactory credit history with another retail supplier to the reasonable satisfaction of the small retail supplier; or
- (b) is a new business; or
- (c) has been responsible for the illegal use of electricity within the previous two years.

A standard retail supplier must not require a security deposit from a business small retail customer after connection.

Types of Security Deposit

A small retail customer must only choose from the following types of security deposits:

- (a) **cash, cheque or credit card** from residential or business small retail customers;
- (b) **annual security levy** from business small retail customers only;
- (c) **guarantees**, including **Department of Housing guarantees** from residential small retail customers, and **bankers' guarantees** from business small retail customers.

Part B

Return of security deposits paid by cash, cheque or credit card

A small retail customer who is required to pay a security deposit, and who pays in the form of cash, cheque or credit card, is eligible for that deposit to be refunded when they have completed:

- (a) for residential small retail customers - on time payment of bills for one year from the date of the first bill; or
- (b) for business small retail customer - on time payment on time of bills for two years from the date of the first bill and the maintenance of a satisfactory credit rating in the reasonable opinion of the standard retail supplier.

When this occurs, the standard retail supplier must inform the small retail customer, in writing, of the amount that is refundable, and credit that amount to the small retail customer's account within 10 business days.

Maximum duration of requirement for annual security levy or guarantee

A small retail customer who is required to pay a security deposit and does so in the form of an annual security levy or guarantee, is eligible for the levy to cease or the guarantee to be discharged when:

- (a) for residential small retail customers - on time payment of bills for one year from the date of the first bill; or
- (b) for business small retail customers - on time payment of bills for two years from the date of the first bill and the maintenance of a satisfactory credit rating in the reasonable opinion of the standard retail supplier.

A standard retail supplier must inform a small retail customer who meets the above requirements that an annual security levy or guarantee is no longer required. A small retail customer must be informed in writing, and within 10 business days, of the above requirements being met.

Cessation of supply

If a standard retail supplier requires a small retail customer to pay a security deposit, and the small retail customer requests that the standard retail supplier cease supplying electricity to the small retail customer's supply address, the standard retail supplier must:

- (a) inform the small retail customer in writing of the amount of the security deposit held; and
- (b) pay the amount either to the small retail customer or into the small retail customer's account.

This must occur within 10 business days of the small retail customer ceasing to take supply.