

# **Changes in regulated retail gas prices from 1 July 2014**

**Gas — Final Report**  
June 2014



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# 1 Executive summary

The Independent Pricing and Regulatory Tribunal (IPART) is responsible for regulating retail gas prices for around one quarter of residential and small business customers<sup>1</sup> in NSW. These prices are those the Standard Retailers in this state – AGL, ActewAGL and Origin Energy – charge customers who have not signed a market contract with them or another retailer.<sup>2</sup>

We have now completed our 2014 price review, and made our final decisions on regulated prices for 2014/15 and 2015/16. In reaching these decisions we carefully considered the Standard Retailers' pricing proposals<sup>3</sup> and other stakeholders' submissions<sup>4</sup> – including the 140 submissions we received in response to the draft decisions we released in April this year. Many of these stakeholders argued that the proposed price increases were too high. However, we have reaffirmed our draft decisions, as the proposed increases reflect the efficient costs a new entrant retailer would incur in supplying gas to customers – including the wholesale price of gas, which is forecast to increase sharply. This reflects our view that a well-functioning competitive market is the most effective way to protect customers from retail prices that are higher than efficient levels.

This final report sets out our final decisions on the allowed price increases and explains the analysis that underpins them. The sections below provide an overview of the decisions and our reasons for these decisions, including our response to stakeholder submissions.

## 1.1 Final decisions on regulated retail gas price increases

Our final decisions are that average regulated retail gas prices can increase by up to 17.7% across NSW over the next 2 years – that is, between 14.6% and 18.1% in the Standard Retailers' individual supply areas. In reaching these decisions, we

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<sup>1</sup> All customers that consume less than 1 terajoule (TJ) per year are eligible for supply under a standard form customer supply contract.

<sup>2</sup> We set regulated retail prices paid by customers who have not signed a contract with an energy retailer or who have chosen to return to the regulated price.

<sup>3</sup> The Standard Retailers made revisions to their initial proposals, and resubmitted them. Throughout this report, references to the retailers' proposals mean the revised versions of these proposals (which are available on our [website](#)).

<sup>4</sup> Submissions to this price review are available on our website at [www.ipart.nsw.gov.au](http://www.ipart.nsw.gov.au).

also took account of updated information on network prices<sup>5</sup> and inflation<sup>6</sup> for 2014/15 and expected network prices and inflation for 2015/16.

We found that the proposals are consistent with a reasonable estimate of the change in efficient costs, and therefore made final decisions to agree to the Standard Retailers' proposed increases in average regulated prices for the 2 years to 30 June 2016. These increases are:

- ▼ **18.0% for AGL**, which supplies gas to over 80% of small regulated retail customers in NSW, covering Sydney, Wollongong, Newcastle, Dubbo, Orange, Parkes, and parts of the Riverina region. This is slightly higher than the draft decision and represents an increase of 17.3% in 2014/15 and 0.7% in 2015/16. The 2014/15 increase adds an extra \$155 to an average residential customer's annual bill and \$725 on average for small business customers.
- ▼ **17.8% for ActewAGL**, which supplies the regions around the NSW/ACT border (including Young, Goulburn, and Yass) and South East NSW (including Shoalhaven). This is slightly higher than the draft decision and represents an increase of 17.2% in 2014/15 and 0.4% in 2015/16. The 2014/15 increase adds an extra \$223 to an average residential customer's annual bill and \$861 on average for small business customers.
- ▼ **14.6% for Origin Energy (Albury/Murray Valley)**, which supplies customers on the NSW - Victorian border, including the Albury and the Murray Valley towns. This is slightly higher than the draft decision and represents an increase of 18.7% in 2014/15 and a decrease of 3.4% in 2015/16. The 2014/15 increase adds an extra \$174 to an average residential customer's annual bill and \$616 on average for small business customers.
- ▼ **18.1% for Origin Energy (Wagga Wagga)**, which supplies the South Western regions of NSW including Wagga Wagga and Gundagai and inland cities such as Tamworth. This is lower than the draft decision and represents an increase of 20.5% in 2014/15 and a decrease of 2% in 2015/16. The 2014/15 increase adds an extra \$210 to an average residential customer's annual bill and \$718 on average for small business customers.

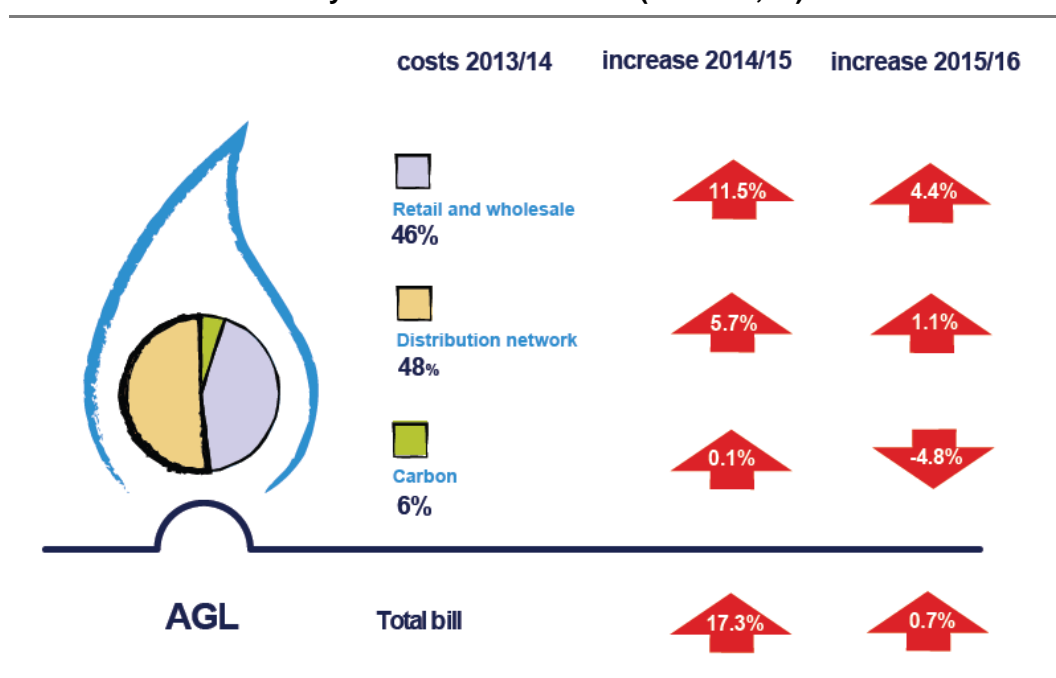
<sup>5</sup> Network costs reflect the charges that retailers must pay to deliver gas through the low pressure distribution network to homes and businesses. These charges are regulated by the Australian Energy Regulator (AER) through Access Arrangements and we take these regulated costs and include them in the retail prices. Network prices for 2015/16 have not yet been determined by the AER and we have assumed they will increase in line with inflation. If actual network prices are different to this assumption, then regulated retail prices will be different. We note that ActewAGL has a small distribution network in the Shoalhaven. These network prices are not regulated.

<sup>6</sup> Inflation for 2014/15 (2.93%) is based on IPART's standard approach, which is the March quarter-on-quarter All Capital Consumer Price Index published by the Australian Bureau of Statistics. The inflation forecast for 2015/16 (2.5%) is based on the mid-point of the Reserve Bank of Australia's target range.



Note that the regulated prices for 2014/15 include a forecast cost of carbon for this year, while those for 2015/16 include a zero cost of carbon (reflecting the market's expectation that the carbon pricing mechanism will be repealed). The removal of carbon costs in 2015/16 offsets the forecast increase in wholesale gas costs that year, resulting in small increases or decreases in average regulated retail prices (eg, see Figure 1.1 below for AGL).

**Figure 1.1 Drivers of increases in AGL's average regulated retail gas prices from 1 July 2014 to 30 June 2016 (nominal, %)**



**Note:** Totals may not add due to rounding.

If no carbon component is applied from the start of 2014/15, then the nominal increase in AGL's regulated retail prices over the next 2 years would be 11.7% in 2014/15 and 5.8% in 2015/16. The pricing agreements include provisions for adjusting regulated retail prices if the carbon price is repealed before 1 July 2015. In this event, IPART will request proposals from the retailers for removing carbon costs from prices. If repeal of the carbon price does not take effect by 1 July 2015, the carbon price for 2015/16 is unknown. In this case, we will agree with the Standard Retailers an approach to estimating the appropriate carbon component of regulated retail prices for 2015/16.

Also note that there are some small differences in the total average increases allowed under our draft and final decisions. These are due to slight differences between the updated network price and inflation forecasts we used for our final decisions and those we used for our draft decisions.

## 1.2 Why we made these final decisions

In regulating retail gas prices, we are required to consider the objects of the *Gas Supply Act 1996* (the Act).<sup>7</sup> In our view, this means our final decisions need to ensure that regulated prices reflect the efficient costs a new entrant retailer would incur in supplying gas for the next 2 years, and facilitate the continued development of competition. A competitive market drives efficiency, innovation and protects customers from unreasonable price increases.

We assessed the Standard Retailers' proposals against our own estimate of the change in the efficient costs of supplying gas over the 2-year period. For the wholesale gas cost component, we commissioned expert advice on the efficient costs that a new entrant retailer would incur in purchasing gas commodity in this period. New entrants would need to secure wholesale gas contracts at current market prices, and these prices are likely to increase in the next 2 years. For the other major cost components, we estimated the efficient costs that a new entrant retailer would incur (retail operating costs and retail margin), or used the actual costs the Standard Retailers are expected to incur (network costs).

In our view, this approach ensures that regulated prices encourage the continued development of competition over the next 2 years. In particular, including a new entrant's efficient costs ensures that regulated prices are high enough for new retailers to enter the market and recover their efficient costs.

In general, stakeholders who responded to our draft decisions did not support this approach, suggesting that we should, for example, set regulated prices based on Standard Retailers' efficient actual costs only, to reduce the impact on consumers and improve the affordability of gas over the next 2 years.

We understand stakeholders concerns about the affordability of gas prices. We also recognise that the increases in the regulated prices are relatively high compared to previous years, and may have a significant impact on some customers. However, we do not consider it would be in customers' best interests, especially in the longer term, to address these concerns by setting regulated prices below the level required to encourage further competition.

As we have previously stated, a well-functioning competitive market (which includes the threat of increased competition from new entrants) is the most effective way to protect customers from higher than efficient retail prices. Competition also drives innovation and efficiency improvements, which benefit customers. We note that over 75% of customers in NSW have already moved off regulated gas prices onto market prices.<sup>8</sup> In other states, formal regulation of retail gas prices has been removed altogether.

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<sup>7</sup> *Gas Supply Act 1996*, section 3.

<sup>8</sup> Based on information provided by the Standard Retailers and gas reticulation authorisation holders.

Formal price regulation cannot protect customers from price increases due to market factors, such as the forecast increases in wholesale gas costs. Nor can it protect customers from price increases driven by other regulatory and policy factors or general financial stress. However, to address concerns about the affordability of gas we are recommending that a review of existing concessions is undertaken to ensure current government expenditures target the most vulnerable customers (see section 1.5).

Some stakeholders also argued that the regulated price increases should be phased in over time to reduce their impact on consumers. In fact, both AGL and ActewAGL have proposed to transition their regulated prices to the level required to recover increased wholesale gas cost over the 2 years.<sup>9</sup> This is not immediately obvious because the proposed increases phased in 2015/16 are offset by the removal of the carbon cost component in this year. Origin Energy has proposed to recover no customer acquisition and retention costs, and has been transitioning its regulated prices to the level required to recover its efficient costs over a number of years. We note that this transitioning of price increases benefits consumers, and imposes a cost to the retailer in terms of revenue forgone.

### 1.3 Why gas prices are increasing

In each of the past 2 years, regulated retail gas prices<sup>10</sup> (and market prices) have increased. The main reason for these increases was sustained rises in gas network costs.<sup>11</sup> However, in the coming 2 years, gas prices will increase for different reasons.

The main reason is that the ability to export Liquid Natural Gas (LNG) is driving a fundamental change in eastern Australia's wholesale gas market. Gas reserves that previously would have supplied NSW are being directed to Gladstone (in Queensland) for export. Eastern Australia is becoming part of a single global market for commodity gas, and wholesale gas prices are being influenced by international prices. In the future, it is likely that NSW gas retailers will have to compete with offshore demand and pay export prices for wholesale gas.

<sup>9</sup> The small increase in 2015/16 reflects a zero carbon component.

<sup>10</sup> Average retail gas prices increased by 8.5% across NSW on 1 July 2013, or by between 5.2% and 9.2% in the Standard Retailers' individual supply areas. Average retail gas prices increased by 14.2% across NSW on 1 July 2012, or by between 9.3% and 14.9% in the Standard Retailers' individual supply areas.

<sup>11</sup> Recent network cost increases have primarily been the result of Jemena's successful appeal to the Australian Competition Tribunal (ACT) of the AER's final decision on the maximum prices and charges they can levy on retailers for use of the distribution network. Information on the Jemena Access Arrangement can be found [here](#). We note that the network cost component of AGL's regulated prices is continuing to increase in 2014/15.

We note that there is still uncertainty about how fast or how far wholesale gas costs will rise. In view of this uncertainty, some stakeholders argued that the price increases should be reconsidered in 2015 if wholesale gas costs do not rise as forecast. But if this were to be the case, competition would ensure that retailers' market prices reflect their lower wholesale gas costs. Customers on regulated prices could move on to a market contract to access these lower prices.<sup>12</sup> That is, if wholesale gas costs are ultimately less than forecast, we would expect increased discounts to be available on market contracts linked to the regulated price.

Some stakeholders argued that domestic gas should be retained for domestic use, and that the wholesale cost should reflect the cost of production. However, domestic gas reservations policy is a matter for government, not IPART. We note that to date, most Australian governments have been reluctant to intervene in gas markets by imposing domestic reservation policies.<sup>13</sup> We also note that such policies impose a cost on society in the form of foregone export income.

#### 1.4 How annual bills for households and small businesses are likely to change

To illustrate the impact of the increases in regulated prices on customers' annual gas bills, we have calculated an indicative annual gas bill for residential and business customers with average usage in each gas supply area (Table 1.1 and 1.2).<sup>14</sup> Customers will see significant bill increases in 2014/15. These will be followed by very modest increases in 2015/16 or, for Origin Energy customers, small decreases.<sup>15</sup>

<sup>12</sup> We note that discounts of up to 8% off the variable charge included in the regulated price are currently being offered. See <http://www.energymadeeasy.gov.au/> accessed 28 May 2014 for gas offers in the Sydney metropolitan area.

<sup>13</sup> Currently, only Western Australia has an active reservation policy. Queensland has the power to require that gas produced in the state be supplied only to the Australian market. However, it has not exercised this power as yet. See <http://www.parliament.nsw.gov.au/prod/parlament/publications.nsf/key/Gas:resources,industrystructureanddomesticreservationpolicies> (accessed 3 June 2014).

<sup>14</sup> We cannot calculate how our final decisions will affect individual customers' annual gas bills. This impact will depend on how much gas they use, which of their Standard Retailer's regulated prices they are on, and how the Standard Retailer changes these individual prices.

<sup>15</sup> As noted in section 1.1, these small increases and decreases are explained by the removal of carbon costs in 2015.

**Table 1.1 Indicative annual bill for typical residential customers (nominal \$, inc GST)**

Standard Retailer	Current bill (2013/14)	Estimated bill (2014/15)	Estimated bill (2015/16)	\$ increase over 2 years
AGL	901	1,056	1,063	162
ActewAGL	1,292	1,515	1,522	230
Origin Energy (Albury/Murray Valley)	933	1,107	1,069	136
Origin Energy (Wagga Wagga)	1,027	1,237	1,212	186

**Note:** This assumes a typical customer uses 23GJ, 45GJ, 45GJ, and 37GJ of gas per annum in the AGL, ActewAGL, Origin Energy (Albury/Murray Valley) and Origin Energy (Wagga Wagga) areas. Impact on bills includes GST.

**Table 1.2 Indicative annual bill for typical business customers (nominal \$, excl GST)**

Standard Retailer	Current bill (2013/14)	Estimated bill (2014/15)	Estimated bill (2015/16)	\$ increase over 2 years
AGL	4,201	4,926	4,959	757
ActewAGL	4,997	5,858	5,885	888
Origin Energy (Albury/Murray Valley)	3,295	3,911	3,776	481
Origin Energy (Wagga Wagga)	3,503	4,221	4,136	633

**Note:** This assumes a typical customer uses 184GJ, 246GJ, 209GJ and 231GJ of gas per annum in the AGL, ActewAGL, Origin Energy (Albury/Murray Valley) and Origin Energy (Wagga Wagga) areas. Impact on bills excludes GST.

## 1.5 What customers can do to manage their gas bills

The impact of the increases in regulated retail prices for individual customers will vary – depending on factors such as their gas usage and Standard Retailer, the regulated price they are on, and how they respond to the price increases (eg, whether they can reduce their usage to manage their bills). However, we recognise that these price increases are relatively high and are likely to be significant for some customers.

We note that these price increases only affect customers on regulated prices – the large proportion of customers on market contracts are likely to pay lower prices, but may also face price increases. Therefore, the first step for customers concerned about the affordability of their gas (and electricity) prices should be to shop around for a better deal. The free comparison service **energymadeeasy.gov.au** is a good place to start. At present, discounts of up to 8% off the variable charge included in the regulated price are being offered. In addition, other products (eg, rate fixing or freezing) and innovations (eg, no early termination fees on market contracts) are available.<sup>16</sup>

<sup>16</sup> See <http://www.energymadeeasy.gov.au/> accessed 28 May 2014 for gas offers in the Sydney metropolitan area.

In addition, customers experiencing difficulty paying gas (or electricity) bills should speak to their retailer. All energy retailers are required by law to have a published hardship charter and to operate an approved customer assistance program. While retailers may have (slightly) different criteria for eligibility to their hardship programs, the common element is that customers on an assistance program are protected from disconnection due to late bill payment, and have a tailored payment arrangement to help them manage their bills.

Some stakeholders argued that retailers should defer price increases until after winter. We note that energy retailers generally offer options for bill smoothing, where the estimated total cost of a customer's energy bills for the next year are spread across equal monthly, fortnightly or weekly instalments. This helps customers manage their budget and cash flow, and reduces the impact of changes in bills due to seasonal energy use.

Other stakeholders indicated that they had been encouraged to switch to gas from electricity because they thought gas was the cheaper fuel. We recognise that it can be difficult for customers to estimate the best fuel and price options for their circumstances. We consider there is scope for further action to address this issue and improve customers' awareness of and engagement in the competitive market. In particular, customers should have access to a resource that assists them in making decisions about whether their household should have a single or multiple sources of fuel, to estimate their likely household energy bills under different combinations of fuel type, appliances and energy price. This will assist them to manage their bills and become more energy efficient and encourage competition and product differentiation in energy retailing.<sup>17</sup> The Australian Energy Regulator's Energy Made Easy website should be expanded to include resources that assist customers to make decisions on fuel type (including information on upfront costs and on-going costs of converting fuel sources) and to estimate energy bills under different fuel type, appliance and energy price scenarios.

We also note that the NSW Government already provides a number of rebates to help vulnerable customers pay their energy bills (although these are paid on electricity bills only). These include the:

- ▼ Low Income Household Rebate – for customers who hold eligible concession cards issued by the Federal Department of Human Services or the Department of Veterans Affairs
- ▼ Family Energy Rebate – available to customers who have received the Family Tax Benefit
- ▼ Life Support Rebate – for households where residents use certain medical equipment necessary to sustain life, and

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<sup>17</sup> We consider that this is particularly important in light of full electricity deregulation from 1 July 2014.

- ▼ Medical Energy Rebate – for eligible customers who have a medically diagnosed inability to self-regulate body temperature when exposed to extremes of environmental temperatures.

We consider that these rebates should be reviewed, to ensure the public funding currently made available for customer assistance measures is used in a way that targets the most vulnerable customers.

#### Recommendations

- 1 IPART recommends that assistance is provided to households to raise awareness and understanding of, and engagement in, competitive energy markets. In particular, the Australian Energy Regulator's Energy Made Easy website should be expanded to include resources that assist customers to make decisions on fuel type and to estimate energy bills under different fuel type, appliance and energy price scenarios.
- 2 IPART recommends that the NSW Government review customer assistance measures to ensure that they are appropriately targeted at the most vulnerable customers.

We also note that the Australian Energy Market Commission (AEMC) found that retail gas customers in ActewAGL's Shoalhaven region are not currently part of the competitive market and cannot choose to switch to an alternative retailer. We recommend that the NSW Government direct the Australian Energy Market Operator (AEMO) to ensure that the Shoalhaven area is covered by the AEMO's Retail Gas Market Procedures. This will ensure that the same national regulatory framework that enables competitive supply in other gas networks in NSW applies in the Shoalhaven. We consider that it is the threat of competition that is important for driving retailer behaviour.

#### Recommendation

- 3 IPART recommends that the NSW Government direct the Australian Energy Market Operator (AEMO) to ensure that the Shoalhaven gas network area is covered by AEMO's Retail Gas Market procedures. This will ensure that the same regulatory framework that enables competitive supply in other gas networks in NSW applies in the Shoalhaven area.

## 1.6 What does the rest of this report cover?

The rest of this paper is structured as follows:

- ▼ Chapter 2 outlines the context for this review and the approach we used to make our final decisions
- ▼ Chapter 3 sets out our final decisions and discusses our assessment of the Standard Retailers' proposed changes to regulated retail prices for 2014/15 and 2015/16
- ▼ Chapter 4 explains our final decisions on the carbon component for 2014/15
- ▼ Chapter 5 analyses the impacts of the final decisions on small customers, sets out steps customers can take to reduce or manage bills and makes recommendations to the NSW Government on how to assist the most vulnerable customers
- ▼ Appendices A to C provide additional information, including why we have not used any additional customer acquisition and retention cost allowance (or competition allowance) to ensure regulated retail gas prices include sufficient incentive for competition (as we did for regulated retail electricity prices in 2013/14).



## 2 Context and approach for the review

When we reached our pricing agreements with the Standard Retailers in 2013, we specified the amount by which each Standard Retailer could increase its average regulated retail gas price in 2013/14.<sup>18</sup> Due to the high level of uncertainty in the wholesale gas market, we agreed to conduct a review in 2014 to determine the change in average regulated prices over 2014/15 and 2015/16.

We have now conducted the 2014 review during which we had regard to terms of reference provided by the NSW Government for the 2013 review, and took account of key developments in the gas sector since we concluded the 2013 review. We used the analytical approach we set out in our June 2013 final report on the pricing agreements.

The sections below discuss the terms of reference, key developments and analytical approach. Box 2.1 outlines our review process.

### 2.1 Terms of reference

The terms of reference (provided in Appendix A) require us to regulate tariffs for small retail gas customers in accordance with section 27 of the *Gas Supply Act 1996* (the Act).<sup>19</sup> It also requires us to ensure we take the objects under section 3 of the Act into account. These are:

1. to encourage the development of a competitive market in gas, so as to promote the thermally efficient use of gas and to deliver a safe and reliable supply of gas in compliance with the principles of ecologically sustainable development
2. to regulate gas reticulation and gas supply, so as to protect the interests of customers and to promote customer choice in relation to gas supply
3. to facilitate the continuity of supply of natural gas to customers, and
4. to promote the safe use of gas.

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<sup>18</sup> The Standard Retailers then set their own regulated prices to comply with the agreements, and we monitored compliance.

<sup>19</sup> Under the Act, regulated prices are available to customers consuming less than 1 terajoule (TJ) per year. We note that we received a submission on the Standard Retailers' pricing proposals from Maitland City Bowls Sports and Recreation Club. As a consumer of between 5 to 6 TJs of gas per year, Maitland City Bowls Sports and Recreation Club would not be eligible for a regulated price and would negotiate a competitive market price.

We need to balance these objectives, particularly as customers have both short and longer term interests in relation to price, quality and security of supply. In our view, this provides us with some discretion to set regulated prices based on the efficient costs a new entrant retailer would face to support competition and ultimately deliver benefits to customers in the long term.

## 2.2 Developments in energy sector since our 2013 review

Since we reached our pricing agreements with the Standard Retailers in 2013, the Australian energy sector has continued to evolve. The most significant developments in the past 12 months include:

- ▼ improvements in competition in the NSW retail market, and the Australian Energy Market Commission (AEMC) finding that this competition is effective<sup>20</sup>
- ▼ the increased internationalisation of domestic gas commodity prices
- ▼ possible changes associated with the proposed emissions reduction fund, the possible repeal of the carbon pricing mechanism and the review of renewable energy target, and
- ▼ changes to gas distribution prices.

### 2.2.1 Improving competition in the retail market

We consider that a competitive market drives efficiency, innovation and protects customers from unreasonable price increases. Since our 2013 review, the competitiveness of the retail gas market in NSW has continued to increase:

- ▼ Small retail customers have continued to move from regulated prices to market-based prices. Currently less than 25% remain on regulated prices in NSW, compared to around 31% in 2011/12.<sup>21</sup>
- ▼ Most customers who participate in the competitive market are experiencing positive outcomes.<sup>22</sup>

<sup>20</sup> AEMC, *Review of Competition in the Retail Electricity and Natural Gas markets in New South Wales, Final Report*, October 2013, p i.

<sup>21</sup> Based on information provided by the Standard Retailers and gas reticulation authorisation holders.

<sup>22</sup> AEMC, *Review of Competition in the Retail Electricity and Natural Gas markets in New South Wales, Final Report*, October 2013, p vi.

However, in submissions to the draft report some stakeholders argued that there is no real competition in the retail gas market and that prices will increase without regulation.<sup>23</sup> Our analysis suggests that the gas market is already transitioning towards a largely deregulated market (ie one where few customers remain on regulated prices). In addition, we note that AGL's share of the small customer market has decreased to around 60% (from nearly 100% at the outset of retail competition).<sup>24</sup>

Effective competition mitigates unnecessary price increases. We also note that there are asymmetric risks in setting regulated prices in a competitive market. If prices are too high customers can always look for a better deal and switch suppliers; however if prices are too low retailers may leave the market and competition would diminish, leaving customers worse off.

In our view, competition in the retail gas market in NSW now protects customers against market power by offering more choices and better price and service outcomes. On this basis, we consider that gas retail price regulation is no longer necessary in NSW<sup>25</sup> and that the removal of retail price regulation is likely to:

- ▼ Improve customer engagement in the market by removing the confusion in relation to the difference between regulated and market prices.<sup>26</sup>
- ▼ Remove the risk that price regulation distorts the competitive market, particularly given the dynamic nature of energy markets. This will encourage more retailers to enter the market, which should deliver better customer outcomes in the long term, including providing a better 'value for money' service through reduced costs and/or innovation.

We note that the Australian Energy Market Commission (AEMC) released its final report on the competitiveness of the NSW energy market in October 2013. It found that competition is delivering discounts and other benefits to small consumers in the NSW retail electricity and natural gas markets. It also found removing retail price regulation for all consumers will likely lead to more innovation, increased product choice, and competitive pricing.<sup>27</sup> Whether or not to remove retail price regulation is a matter for the NSW Government to decide.

<sup>23</sup> See eg, J Cozzi submission to Draft Report, April 2014, p 1 and P Dorrian submission to Draft Report, May 2014, p 1.

<sup>24</sup> See IPART, *Customer service performance of gas retail suppliers – Information Paper*, December 2013, p 19.

<sup>25</sup> Some stakeholders also support full retail prices deregulation. See, eg, AGL submission to Draft Report, May 2014, p 1; EnergyAustralia submission to Draft Report, May 2014, p 2; Energy Retailers Association of Australia submission to Draft Report, May 2014, p 1 and Energy Supply Association of Australia submission to Draft Report, May 2014, p 2.

<sup>26</sup> The AEMC's survey found that few participants knew if they were on a regulated or market price, suggesting there is a lack of understanding about the difference between regulated and market prices, which potentially influences effective customer engagement in the market. Roy Morgan Research, *Survey of Residential Customers of Electricity and Gas in NSW: Effectiveness of Retail Competition*, February 2013, p 53.

<sup>27</sup> AEMC, *Review of Competition in the Retail Electricity and Natural Gas markets in New South Wales, Final Report*, October 2013, p i.

In April this year the NSW Government announced that retail electricity prices will be fully deregulated from 1 July 2014.<sup>28</sup>

We also note that the Australian Energy Market Commission (AEMC) found that retail gas customers in ActewAGL's Shoalhaven region<sup>29</sup> are not currently part of the competitive market and cannot choose to switch to an alternative retailer.<sup>30</sup> We recommend that the NSW Government direct the Australian Energy Market Operator (AEMO) to ensure that the Shoalhaven area is covered by the AEMO's Retail Gas Market Procedures. This will ensure that the same national regulatory framework that enables competitive supply in other gas networks in NSW applies in the Shoalhaven. We consider that it is the threat of competition that is important for driving retailer behaviour.

#### Recommendation

- 1 IPART recommends that the NSW Government direct the Australian Energy Market Operator (AEMO) to ensure that the Shoalhaven gas network area is covered by AEMO's Retail Gas Market procedures. This will ensure that the same regulatory framework that enables competitive supply in other gas networks in NSW applies in the Shoalhaven area.

### 2.2.2 Increasing internationalisation of gas markets

Gas retailers purchase wholesale gas for their customers' use and need to be able to recover these efficient costs. Increasingly, Australian domestic gas markets will be influenced by the international market. This market – particularly the international demand for gas – is changing the incentives faced by domestic producers and consumers of fossil fuels (including natural gas).

It is clear that the domestic price of wholesale gas is moving towards the international market price. In the medium term, the supply and demand dynamics in the eastern Australian gas markets are uncertain. For example, higher international prices for gas have altered the expectations of some gas producers, which in turn have provided incentives for further development of gas supplies. However, limited LNG export capacity in the medium term may mean that there is limited scope for some producers to access these international prices.

In the longer term, we expect domestic gas prices to move towards international levels. With export capability there will be a single market for gas and export exposure will link the domestic gas commodity price to the international price. These changes are currently driving increases in wholesale gas prices. But again,

<sup>28</sup> <http://www.resourcesandenergy.nsw.gov.au/energy-consumers/energy-sources/electricity/removal-of-electricity-price-regulation>

<sup>29</sup> There are less than 3,000 small gas customers in the Shoalhaven region.

<sup>30</sup> AEMC, *Review of Competition in the Retail Electricity and Natural Gas markets in New South Wales*, Final Report, October 2013, p 51.

there is considerable uncertainty about how fast and how far prices will rise. One contributing factor is a lack of clarity about additional LNG projects in Australia, which means the timing and extent of longer term increases in LNG export capacity is not known.

In addition, the international market is continually changing, eg a recent gas supply agreement signed between Russia and China at around 30% below current world prices,<sup>31</sup> which could impact whether or not additional LNG projects in eastern Australia are developed and influence both future domestic prices and quantities. While the domestic gas price will be linked to the international price in the future, movements in these prices are symmetric. That is, if the Russia-China agreement were to move international prices down, we would expect downwards pressure on domestic prices.

In submissions to the draft report stakeholders raised a number of issues around the wholesale gas market in eastern Australia, including:

- ▼ reserving gas for domestic use, and
- ▼ the adequacy of gas supplies, and in particular the development of Coal Seam Gas (CSG) and associated health and environmental issues.

### Domestic gas reservations

The position that domestic gas should be retained for domestic use, and at a price that reflects the cost of production, was taken by a number of stakeholders.<sup>32</sup> We note that domestic gas reservations policy is a matter for government, but that it is a policy that imposes a cost on society.

To date, most Australian governments have been reluctant to intervene in gas markets by imposing domestic reservation policies. Currently, only Western Australia has an active reservation policy. Queensland has the power to require that gas produced in the state be supplied only to the Australian market. However, it has not exercised this power as yet.<sup>33</sup> Given there will be a single, international market for gas, a domestic reservations policy would impose a cost on society in the form of foregone export income.

<sup>31</sup> See Jacobs SKM, *New Contract Gas Price Projections*, Report, May 2014, p 31. Available on the IPART website ([www.ipart.nsw.gov.au](http://www.ipart.nsw.gov.au)).

<sup>32</sup> See, eg, Jeremy Buckingham MLC submission to Draft Report, May 2014, p 1; J Bock submission to Draft Report, May 2014, p 1; M Bou submission to Draft Report, May 2014, p 1; R Harrop submission to Draft Report, May 2014, p 1 and S Wright submission to Draft Report, May 2014, p 1.

<sup>33</sup> See <http://www.parliament.nsw.gov.au/prod/parliament/publications.nsf/key/Gas:resources,industrystructureanddomesticreservationpolicies> for discussion of domestic reservation policies in Australia (accessed 3 June 2014).

## Domestic gas supply

Several stakeholders argued that a shortage of supply is no reason to increase prices or allow Coal Seam Gas (CSG) development. These stakeholders generally have concerns around the safety of CSG and consider that IPART is not meeting the requirements of the Act (in terms of promoting the safe use of gas) by allowing a price increase that facilitates CSG development.<sup>34</sup>

The objectives of the Act apply to us in the context of setting regulated retail prices for natural gas. The safe development of CSG resources is ensured by safety, environmental and planning regulation, not price regulation.

The driver of the price increases under our draft decisions is a structural change emerging in the wholesale gas market. Gas reserves previously contracted to NSW are being directed to Gladstone (in Queensland) for export. With the development of export capability there will be a single market for gas and export exposure will link the domestic gas commodity price to the international price. Going forward, NSW is likely to have to compete with offshore demand and pay export prices, leading to a rise in the cost of gas. These changes are currently driving increases in wholesale gas prices.<sup>35</sup>

We acknowledge that another factor that could affect wholesale gas prices is the impact of competing sources of gas supply such as CSG. There is currently considerable development in the CSG industry in Australia. However, the impact of additional CSG supply on domestic gas prices is uncertain. Many other factors – eg, domestic and international gas demand and the availability of LNG export capacity – may influence the price of gas in NSW. As previously mentioned, the international market is not static, with changes in the supply and demand for gas having an impact on both the price and quantity of domestic wholesale gas.

Overall, we expect the process of transitioning to international gas price levels is unlikely to be smooth. The changing market dynamics have the potential to lead to increasing levels of price uncertainty in the gas market for some time.

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<sup>34</sup> See, eg, K Taylor submission to Draft Report, May 2014, p 1.

<sup>35</sup> See, eg, Jacobs SKM, *New Contract Gas Price Projections*, Final Report, 28 May 2014, pp i-iii. Available on the IPART website ([www.ipart.nsw.gov.au](http://www.ipart.nsw.gov.au)).

### 2.2.3 Changes to green schemes

Since we made our pricing agreements with the Standard Retailers in 2013, the Commonwealth Government has:

- ▼ introduced into federal parliament a package of bills to repeal the carbon pricing mechanism<sup>36</sup>
- ▼ released its emissions reduction fund (ERF) Green Paper, and
- ▼ commenced a review of the renewable energy target (RET) to make sure it is working efficiently and effectively, which is to be completed by mid-June 2014.

Our regulatory framework allows for the carbon price to be removed from regulated prices should the mechanism be repealed.

### 2.2.4 Changes to gas distribution network prices

Gas distribution network costs (which account for around half of a typical customer bill) are currently passed through to small retail customers in their gas bills. The Standard Retailers have no control over these costs, as they typically depend on the network prices set out in the gas distribution access arrangements determined by Australian Energy Regulator (AER).

For the past 3 years (2011/12 through 2013/14), the average network costs passed through most gas customers in NSW (those connected to the Jemena distribution network) increased materially. As Table 2.1 shows, these customers face further material increases in average network costs in 2014/15.

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<sup>36</sup> We note that Senate voted down this legislation on 20 March 2014.



**Table 2.1 Regulated gas distribution access arrangements**

Gas retail supplier	Gas distribution network supplier	Period of access arrangement	Allowed real price changes in remaining years <sup>a</sup>
AGL	Jemena	1 July 2010 – 30 June 2015	8.39% in 2014/15
ActewAGL <sup>b</sup>	ActewAGL (Australian Capital Territory)	1 July 2010 – 30 June 2015	0% in 2014/15
	Jemena (Capital region)	1 July 2010 – 30 June 2015	8.39% in 2014/15
Origin Energy	Envestra (Wagga Wagga)	1 July 2010 – 30 June 2015	2.5% in 2014/15
	Central Ranges Pipeline (Tamworth)	1 July 2004 – 1 July 2019	0% pa until 2018/19
	Envestra (Albury)	1 January 2013 – 31 December 2017	0% pa until end 2017

<sup>a</sup> Price increases exclude inflation.

<sup>b</sup> The Shoalhaven natural gas network which ActewAGL uses to supply its Shoalhaven customers is not regulated. However, ActewAGL's pricing proposal includes no real network price increases for the Shoalhaven network in 2014/15 and 2015/16.

**Note:** Average price increases will depend on a number of external factors including pass through amounts for unaccounted gas and carbon costs.

**Source:** AER, *Access Arrangement information for the access arrangement JGN's NSW gas distribution networks 1 July 2010 – 30 June 2015, Amended by order of the Australian Competition Tribunal, 30 June 2011, Further amended with regard to mine subsidence expenditure, 26 September 2011, June 2010, p 32.* AER, *Access Arrangement Information for the ACT, Queanbeyan and Palerang gas distribution network 1 July 2010-30 June 2015, Amended by order of the Australian Competition Tribunal, 23 September 2010, April 2010, pp 66 & 85.* AER, *Access arrangement variation for the Wagga Wagga gas distribution network 1 July 2010-30 June 2015, September 2010, p 5.* IPART, *Access Arrangement for the Central Ranges Pipeline Gas Network, November 2005, p 15.* AER, *Access Arrangement Final Decision Envestra Ltd Albury & Victoria Gas Distribution System 2013 – 2017, Part 1, March 2013, p 14.*

In the final year of the current regulatory period (2015/16), the change in network costs is uncertain for most customers, as the access arrangements for the Jemena, ActewAGL and Envestra (Wagga Wagga) networks are due to expire on 30 June 2015. Several policy and regulatory developments may influence network tariffs included in the renewed access arrangements, including the AER's new determinations which will apply under amended National Gas Rules (NGR)<sup>37</sup> and changes to the Limited Merits Review Regime for gas businesses.<sup>38</sup>

<sup>37</sup> In November 2012, the Australian Energy Market Commission (AEMC) released a final determination and amendments to the economic regulation provisions in the NGR. See <http://www.aemc.gov.au/news/announcements/final-determination-made-on-network-regulation-rule-changes.html>

<sup>38</sup> The National Gas Law (NGL) includes a limited merits review regime to provide parties affected by the AER's decisions with recourse to a review mechanism. In December 2013, a number of significant changes to the regime, including a strengthened materiality threshold, increased user and consumer consultation, removed the risk of prohibitively high costs being awarded against users and consumers in a review. See <https://scer.govspace.gov.au/files/2011/12/EMRWG-Bulletin-21-Proclamation-of-LMR-Amendments1.pdf>



Until details on the renewed access arrangements are available, we have assumed no real increases in network charges in 2015/16.

### **2.3 Our analytical approach for agreeing average price increases from 1 July 2014**

To assess the Standard Retailers' pricing proposals for 2014/15 to 2015/16 we did not reconsider key features of the 2013 agreements, such as the form of regulation. Rather, our approach included:

1. Assessing each retailer's proposed increase in average regulated prices, and forming a view on whether the resulting prices are reasonable and balance the objects in the Act.
2. Based on this assessment, making final decisions on whether to agree to each retailer's proposal.
3. Analysing the impact of the price changes on customers.

As noted in section 2.1 above, in assessing whether the proposed price increases meet the objects of the Act we considered whether they ensure that regulated prices reflect the efficient costs a new entrant retailer would incur in supplying gas for the next 2 years and facilitate the continued development of competition.

As in past reviews, we have formed our own view on the reasonable range for the forecast efficient costs of supply by analysing the forecast retail costs of supply, and including network and carbon costs. The approach we used is similar to the one we used for the 2013 review.

In response to our draft report, a number of stakeholders commented on our analytical approach to this price review. Some stakeholders broadly agree with our approach (in the absence of full retail price deregulation).<sup>39</sup> Other stakeholders did not support our approach. For example, the Public Interest Advocacy Centre (PIAC) argued that we should set prices at a level that reflects efficient costs of supply rather than costs that would be faced by a new entrant supplier.<sup>40</sup> In our view reflecting the actual efficient costs of incumbent retailers' is not in customers' long term interests. We consider that it is in customers' best interests that prices are set at efficient, cost reflective levels to allow entry into the market by new retailers and drive competition. Competition is the best protection for customers and our final decisions should facilitate competition.

<sup>39</sup> See, eg, AGL submission to Draft Report, May 2014, p 1 and EnergyAustralia submission to Draft Report, May 2014, p 1.

<sup>40</sup> See, Public Interest Advocacy Centre (PIAC) submission to Draft Report, May 2014, p 4. In PIAC's view "it is extremely unlikely that new retailers will seek to enter the small retail gas market over the remainder of the period of the current VPA".

Lock the Gate Alliance asserted that, by allowing gas retailers to pass on world parity prices, IPART is failing to protect consumer interests as required under the Act.<sup>41</sup> We consider that our final decisions protect customers' interests by ensuring that gas producers are indifferent between supplying domestic and international markets and also by facilitating competition in the retail gas market. We also note that, as set out in section 2.2.2, to the extent that export opportunities are foregone then that represents foregone income to Australia.

Some stakeholders argued that IPART had effectively 'rubber stamped' the retailers' proposals and that these price increases lead to increased retailer profits.<sup>42</sup> We do not agree with this. We have independently assessed the efficient costs faced by a retailer entering the market. We engaged expert advice and undertook our own analysis.

We note that we did not accept all of the retailers' initial pricing proposals. Originally AGL and ActewAGL proposed an additional competition allowance in regulated prices.<sup>43</sup> Having reviewed the proposals we concluded that there is already sufficient competition in the retail gas market and that there is no clear need for an additional incentive in regulated prices to move customers on to market contracts more quickly.<sup>44</sup> AGL and ActewAGL subsequently submitted revised pricing proposals with no additional competition allowance.<sup>45,46</sup>

We also note that EnergyAustralia considers that regulated retail prices may not reflect the wholesale and operating costs of potential new entrants, but that this could be offset by the inclusion of a competition allowance or higher retail margin.<sup>47</sup>

<sup>41</sup> See Lock the Gate Alliance submission to Draft Report, May 2014, p 2.

<sup>42</sup> See, eg, S Romeo submission to Draft Report, May 2014, p 1 and Anonymous submission.

<sup>43</sup> See AGL Proposal, 11 February 2014, pp 21-22 and ActewAGL Proposal, 11 February 2014, p 6.

<sup>44</sup> See Appendix B.

<sup>45</sup> See AGL Addendum to proposal, 21 March 2014 pp 1-2 and ActewAGL Addendum to proposal, 25 March 2014, p 1.

<sup>46</sup> Origin did not include an additional competition allowance and Origin's proposal was accepted as submitted.

<sup>47</sup> EnergyAustralia submission to Draft Report, May 2014, p 2.

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**Box 2.1      Process for this review**

The process we followed in conducting this review included public consultation and detailed analysis. As part of this process, we:

- ▼ Received pricing proposals from the Standard Retailers for 2014/15 and 2015/16 (ie, the remainder of the regulatory period).
  - ▼ Released a Fact Sheet in February 2014. This paper outlined our proposed approach for assessing the Standard Retailers' pricing proposals and invited all interested parties to make a submission in response to the Standard Retailers' pricing proposals.
  - ▼ Sought information from the Standard Retailers and other sources in relation to the forecast cost of supplying gas over the period.
  - ▼ Engaged consultants, Jacobs SKM, to provide expert advice on wholesale gas costs.
  - ▼ Conducted our own analysis in line with the approach outlined in section 2.1, and considered stakeholder submissions and comments.
  - ▼ Received revised pricing proposals from the Standard Retailers in March 2014.
  - ▼ Made draft decisions, considering all relevant material above.
  - ▼ Held a public forum on the draft report to provide stakeholders with the opportunity to comment on our draft decisions.
  - ▼ Considered all submissions and stakeholder comments in making our final decisions.
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### 3 Assessing the proposed increases in total prices

We assessed each Standard Retailer's pricing proposal for 2014/15 and 2015/16 (the remainder of the 2013 regulatory period) in line with the approach set out in Chapter 2. In particular, we considered each retailer's proposed increase in average regulated prices, and formed a view on whether the resulting prices are reasonable and balance the longer and shorter term objectives for this review.

To help us form our view, we analysed the forecast efficient retail costs that a retailer is likely to incur in supplying gas to customers over the 2-year period. However, in contrast to the approach we previously used for reviewing regulated electricity prices we did not assess and make decisions on each individual forecast cost component in the retailers' proposals. Instead, we used a more holistic approach that involved:

- ▼ analysing each of the retail costs of supply and considering stakeholder comments to form a view of the reasonable range for each of these efficient costs over the remainder of the regulatory period
- ▼ using the above ranges, and the expected network and carbon costs,<sup>48</sup> to inform our view of the reasonable change in regulated retail prices over this period, and
- ▼ deciding whether to agree to the retailer's proposed price changes, based on whether or not they are consistent with this reasonable change.

The sections below provide an overview of our final decisions and then discuss the analysis which helped us make these decisions.

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<sup>48</sup> We note that the Standard Retailers' pricing proposals did not include a carbon component for 2015/16. The regulatory framework allows the retailers to propose a carbon component for 2015/16 in February 2015, should a carbon price continue to apply.

### 3.1 Overview of final decisions on proposed increases in regulated retail gas prices

- 1 IPART's final decisions on the proposed increases in the regulated gas prices are to:
  - Agree to AGL's proposal to: increase the retail component by CPI+21.0% in 2014/15 and CPI+6.4% in 2015/16, pass-through actual distribution network charges in both years, and include a carbon component of \$1.76/GJ in 2014/15.
  - Agree to ActewAGL's proposal to: increase the retail component by CPI+24.7% in 2014/15 and CPI+7.2% in 2015/16, pass-through actual distribution network charges in both years, and include a carbon component of \$1.75/GJ in 2014/15.
  - Agree to Origin Energy's (Albury/Murray Valley) proposal to: increase the retail component by CPI+26.2% in 2014/15 and CPI+3.2% in 2015/16, pass-through actual distribution network charges in both years, and include a carbon component of \$1.78/GJ in 2014/15.
  - Agree to Origin Energy's (Wagga Wagga) proposal to: increase the retail component by CPI+36.3% in 2014/15 and CPI+2.9% in 2015/16, pass-through actual distribution network charges in both years, and include a carbon component of \$1.78/GJ in 2014/15.

These final decisions reaffirm our draft decisions and reflect our assessment that the Standard Retailers' proposed average regulated price changes are reasonable. In our view, the proposed changes will result in prices that provide sufficient protection to the minority of small retail customers who remain on regulated prices, and also include sufficient incentive for retailers to compete in the competitive market and consumers to enter this market.

The Council of Social Service of NSW (NCOSS) and PIAC recommend that price increases should be further transitioned or smoothed over the remaining 2 years of the Voluntary Pricing Agreements (VPAs).<sup>49</sup> Having had regard to the impacts of price increases on customers, both AGL and ActewAGL propose to transition wholesale gas cost increases over 2 years.<sup>50</sup> Origin Energy is recovering no customer acquisition and retention costs and has been transitioning regulated retail prices to efficient levels over a number of years.<sup>51</sup> We note that this may result in regulated retail prices that do not reflect the full efficient costs faced by a new entrant retailer (or other incumbent retailers, as highlighted by EnergyAustralia (see section 2.3).

<sup>49</sup> See Council of Social Service of NSW (NCOSS) submission to Draft Report, May 2014, p 2 and PIAC, p 6.

<sup>50</sup> See, eg, AGL Proposal, 11 February 2014, p 6.

<sup>51</sup> See Origin Energy Proposal, 11 February 2014, p 9.

We also note that the reasonable range for the forecast efficient retail cost components over the regulatory period is large. This reflects the high degree of uncertainty about the extent of expected increases in wholesale gas costs. In reaching our view on the reasonable range for these costs we considered expert advice and stakeholder comments.

## 3.2 Analysing the retail costs of gas supply

The retail costs of gas supply<sup>52</sup> reflect the controllable costs retailers incur in supplying gas to customers. These include wholesale gas costs, retail operating costs and a retail margin. To analyse these costs, we commissioned expert advice on the potential range for wholesale gas costs, and considered the analysis undertaken for the 2013 price review.

### 3.2.1 Wholesale gas costs

Wholesale gas costs include gas commodity and transmission costs, the costs associated with being able to serve peak demand, and market-related costs. All 3 Standard Retailers have proposed significant increases in gas commodity costs over the remainder of the regulatory period and this cost increase is the main driver of the increase in regulated retail gas prices.<sup>53</sup>

As Chapter 2 discussed, the domestic price of gas commodity is moving towards the international market price, increasing the costs of supplying gas to retail customers. However, the process of transitioning to international price levels is unlikely to be smooth, with changing market dynamics having the potential to lead to increasing levels of price uncertainty in the medium term. As a result of this uncertainty there are a range of views about current and future gas prices in NSW, and a corresponding range of views about the costs of supplying gas to retail customers.

For this review, we asked Jacobs SKM to provide advice on the potential range for the wholesale gas costs an efficient new entrant gas retailer serving the small customer market in NSW is likely to face over remainder of the regulatory period. Jacobs SKM based its advice on new gas contract prices in NSW. In particular, it considered:

- ▼ new contract gas price projections, estimated using MMAGas (Jacobs SKM's proprietary modelling tool), and
- ▼ publicly available reports of recent domestic and export contract prices.

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<sup>52</sup> The retail costs of gas supply are referred to as the 'R component'. Regulated prices are the sum of the R component and network and carbon costs.

<sup>53</sup> Proposed costs for additional deliverability, transmission and market costs are broadly in line with our estimates of efficient costs for the 2013 price review.

Jacobs SKM's final report is available on our website.<sup>54</sup>

We also considered the benchmark wholesale gas costs that were established as part of our 2013 gas price review. In work commissioned for that review, ACIL Tasman (ACIL) modelled projected gas prices at Moomba and Longford under a number of scenarios. This resulted in projected price ranges from \$6.46 to \$8.31/GJ in 2014/15 and \$6.40 to \$8.28/GJ in 2015/16.<sup>55</sup> (ACIL's report from the 2013 review is available on our website.<sup>56</sup>)

In our view, Jacobs SKM's advice and ACIL's previous advice establish a reasonable range for forecast efficient costs over the remainder of the regulatory period. We consider this range (shown in Table 3.1) captures the uncertainty in relation to estimates of gas commodity costs over this period. For 2014/15 and 2015/16, all 3 Standard Retailers have proposed gas commodity costs that are within this range.

**Table 3.1 Reasonable range for wholesale gas costs over remainder of regulatory period (\$2013/14/GJ)**

	2014/15	2015/16
Jacobs SKM 2014		
<i>Final advice</i>	\$6.25 - \$9.00/GJ	\$6.75 - \$9.00/GJ
<i>Modelled prices:</i>		
- Long run LNG netback	\$6.52 - \$9.38/GJ	\$7.09 - \$8.60/GJ
- Short run LNG netback	\$6.04 - \$8.39/GJ	\$6.72 - \$9.74/GJ
ACIL 2013	\$6.46 - \$8.31/GJ	\$6.40 - \$8.28/GJ

**Notes:** ACIL figures were inflated from \$2013 using inflation of 1.4%.

**Sources:** Jacobs SKM, *New Contract Gas Price Projections*, Report, May 2014, p 33 and 36. Available on the IPART website ([www.ipart.nsw.gov.au](http://www.ipart.nsw.gov.au)). ACIL Tasman, *Costs of gas for the 2013 to 2016 regulatory period*, Final Report, Public Version, June 2013, p 25.

Both NCOSS and PIAC argued that we should adopt a more conservative approach to wholesale gas costs. In particular, PIAC recommended that we should use a gas commodity cost of \$7/GJ for 2014/15.<sup>57</sup> In addition, NCOSS and PIAC argued that Origin's Albury/Murray Valley customers should pay a price that reflects Victorian wholesale gas prices, as this is where their gas comes

<sup>54</sup> Jacobs SKM, *New Contract Gas Price Projections*, Final Report, 28 May 2014. Available on the IPART website ([www.ipart.nsw.gov.au](http://www.ipart.nsw.gov.au)).

<sup>55</sup> These ranges reflect the midpoint of ACIL's projected prices under its low and medium scenarios for each source of gas supply. The low price scenario reflects production costs, while the medium price scenario reflects estimates of the liquefied natural gas (LNG) netback price. That is, the price at which an exporter would be indifferent between re-selling gas in the domestic market or exporting it as LNG. In broad terms, the LNG netback price is calculated as the (market) LNG price less liquefaction and pipeline transportation costs. ACIL figures were inflated from \$2013 to \$2013/14 using inflation of 1.4%.

<sup>56</sup> ACIL Tasman, *Costs of gas for the 2013 to 2016 regulatory period*, Final Report, Public Version, June 2013.

<sup>57</sup> See NCOSS, p 2 and PIAC, p 5.

from.<sup>58</sup> PIAC recommended that gas commodity costs of \$5.59/GJ and \$6.50/GJ should be used over the next 2 years for regulated retail prices in this region.<sup>59</sup>

Jacobs SKM forecast a price at Gippsland (Victoria) of \$6.00 to \$7.00 over the remainder of the regulatory period; the price at Moomba is forecast to be \$8.00 to \$10.00.<sup>60</sup> The retailers' pricing proposals are consistent with this, and are based on a portfolio approach to procuring gas supply.

It is prudent and efficient for a retailer to have a portfolio of gas supply. AGL and Origin source gas from both Moomba and Longford to serve the eastern Australian market. Historically, gas has entered NSW almost equally from these 2 sources. Therefore we considered it appropriate to estimate the price to the small customer market in NSW as the average of the costs of supply across the portfolio as a whole (see our 2010 review).<sup>61</sup> The (lower) price at Longford compared to Moomba is reflected in all 3 retailers' proposed wholesale gas costs.

We further note that:

- ▼ Capacity constraints at Longford are temporary – Origin is one of 3 shippers/retailers who have agreed to pay for expanding the Vic-NSW interconnector.<sup>62</sup>
- ▼ Prices in Origin's Albury/Murray Valley area have historically not recovered efficient costs.<sup>63</sup>
- ▼ Origin's pricing proposal is towards the lower end of the reasonable range (see section 3.3).

The Energy and Water Ombudsman NSW (EWON) requested that IPART consider including a reopening clause in the pricing agreements to allow the price rise to be reconsidered in 2015 if the wholesale price of gas does not rise as forecast.<sup>64</sup> We consider that if wholesale gas costs increase by less than forecast then the competitive markets should remove any inefficiencies in the regulated price. The minority of customers still on regulated prices can always move to a market contract.<sup>65</sup> If wholesale gas costs are ultimately less than forecast, we expect the discounts available on market contracts to increase.

<sup>58</sup> See NCOSS, p 2 and PIAC, pp 7-8.

<sup>59</sup> See PIAC, Ibid.

<sup>60</sup> See Jacobs SKM, p 36.

<sup>61</sup> See <http://www.aer.gov.au/node/11715>. In 2008/09 and 2009/10 pipeline flows into the NSW and the ACT were almost equally split between the Eastern Gas Pipeline/NSW-Victoria Interconnect and the Moomba to Sydney pipeline. IPART calculations.

<sup>62</sup> See <http://www.apa.com.au/investor-centre/news/asxmedia-releases/2013/apa-to-further-expand-vic-nsw-interconnect.aspx>

<sup>63</sup> See Origin Energy Proposal, 11 February 2014, p 8.

<sup>64</sup> See Energy and Water Ombudsman NSW (EWON) submission to Draft Report, May 2014, p 2.

<sup>65</sup> We note that discounts of up to 8% off the variable charge included in the regulated price are currently being offered. See <http://www.energymadeeasy.gov.au/> accessed 28 May 2014 for gas offers in the Sydney metropolitan area.



### 3.2.2 Retail operating costs

Retail operating costs are the costs a retailer incurs in performing the functions required to serve its customer base. This includes the costs of billing and revenue collection, call centres, marketing, and an appropriate allocation of corporate overheads. Retail costs could also include the costs associated with customer acquisition and retention.

In our 2013 price review, we found the reasonable range for efficient retail operating costs (ROC) **excluding** customer acquisition and retention costs<sup>66</sup> (CARC) to be \$94 to \$113 per customer (\$2013/14). We considered that this range would remain appropriate for the duration of the regulatory period. (Our analysis of retail operating costs for the 2013 price review can be found in our June 2013 [final report](#).) For 2014/15 and 2015/16, all 3 Standard Retailers have proposed retail operating costs excluding customer acquisition and retention costs that fall within our reasonable range.

We note that AGL's and ActewAGL's agreed regulated prices for 2013/14 recover some customer acquisition and retention costs. As set out in section 2.3, we considered whether it would be appropriate to recover **additional** customer acquisition and retention costs (or a 'competition allowance') through regulated retail gas prices in 2014/15 and 2015/16. In general, we concluded there is no clear need for an additional incentive or competition allowance in regulated retail prices in NSW. However, we acknowledge that the position may be different in some of the small(er) standard supply areas. (Appendix B provides further information on our analysis of the need for an additional competition allowance in regulated retail gas prices.)

### 3.2.3 Retail margin

For our 2013 price review, we engaged Strategic Finance Group (SFG) to assist us in estimating a reasonable range for the retail margin of gas retail suppliers. SFG's final advice was that this range is 6.3% to 7.3% of earnings before interest, tax, depreciation and amortisation (EBITDA).<sup>67</sup> We have received no new evidence during this annual review to suggest that a change to this reasonable range would be appropriate. For 2014/15 and 2015/16, all 3 Standard Retailers have proposed a retail margin that falls within our reasonable range.

<sup>66</sup> Customer acquisition and retention costs (CARC) include marketing campaigns, discounts and other incentives for customers to switch retailers or market offers. In our 2013 electricity price review, we set a distinct allowance for CARC, in addition to the allowance for retail operating costs (ROC), which covered customer service (eg, operating call centres, billing and collecting revenue), finance, IT systems and regulation (eg, paying licence fees).

<sup>67</sup> This range reflects the results of all 3 of the approaches it used, and places equal weight on each result. See SFG, *Estimation of the regulated profit margin for gas retailers in New South Wales*, Final Report, June 2013, p 7.

### 3.3 Assessing Standard Retailers' pricing proposals for 2014/15 and 2015/16

Based on the analysis discussed above, we have formed a view on the reasonable change in regulated retail prices for each Standard Retailer. As in past reviews, we formed this view by establishing a reasonable range for the forecast efficient retail costs of supply (the R component) and adding actual network and carbon costs (the N and C components).

Then we compared this range to each retailer's pricing proposal, to decide whether the pricing proposal is reasonable and balances the longer and shorter term objectives for this price review. We did not assess and make a decision on the individual cost components underlying the retailers' proposals.

#### 3.3.1 Establishing the reasonable range for the R component

To establish the reasonable range for the R component, we used the analysis discussed in section 3.2 above and the following scenarios:

- ▼ **A low price scenario.** This scenario reflects the lower end of our reasonable ranges of efficient gas commodity costs and retail margin, the midpoint of our reasonable range for retail operating costs and the recovery of some customer acquisition and retention costs.
- ▼ **A high price scenario.** This scenario reflects the upper end of our reasonable ranges of efficient gas commodity costs and retail margin, the midpoint of our reasonable range for retail operating costs and the recovery of some customer acquisition and retention costs.

Table 3.2 shows the assumptions underlying our 2 scenarios.

**Table 3.2 Assumptions used in pricing scenarios for 2014/15 and 2015/16 (\$2013/14)**

	Assumption	Comments
<b>Low case scenario</b>		
Gas commodity costs	6.52/GJ in 2014/15 and 7.09/GJ in 2015/16	Consistent with Jacobs SKM and ACIL advice
Retail costs	\$115/customer	Midpoint of ROC range and recovery of some CARC
Retail margin	6.3%	Bottom of benchmark range
<b>High case scenario</b>		
Gas commodity costs	\$8.39/GJ in 2014/15 and \$8.60/GJ in 2015/16	Consistent with Jacobs SKM and ACIL advice
ROC and CARC	\$115/customer	Midpoint of ROC range and recovery of some CARC
Retail margin	7.3%	Top of benchmark range

Table 3.3 shows the price increases associated with our 2 scenarios, and sets out the implied price increase for 2014/15 as well as the cumulative increase after both 2014/15 and 2015/16 (ie, over the remainder of the regulatory period).

**Table 3.3 Increases in the regulated retail prices (R+C+N) for 2014/15 and cumulative (2014/15 to 2015/16) under the scenarios (\$2013/14)**

	Low case scenario		High case scenario	
	2014/15	Cumulative	2014/15	Cumulative
<b>Modelled increase</b>				
AGL	CPI+11.2%	CPI+7.7%	CPI+18.8%	CPI+14.1%
ActewAGL	CPI+8.0%	CPI+4.0%	CPI+16.9%	CPI+11.4%
Origin (Albury/Murray Valley)	CPI+14.3%	CPI+7.7%	CPI+26.1%	CPI+17.3%
Origin (Wagga Wagga)	CPI+16.3%	CPI+11.4%	CPI+25.8%	CPI+19.3%

**Source:** IPART modelling. We have used actual network price increases. Carbon costs are included in the price change for 2014/15 only.

### 3.3.2 Comparing each retailer's pricing proposal to the reasonable range for the total cost of supply (R+N+C components)

The Standard Retailers' pricing proposals for 2014/15 and 2015/16 are set out in Table 3.4, as well as the cumulative increase over both years. Both AGL's and Origin Energy's pricing proposals fall within the range established by the scenarios set out above. We have made final decisions to agree to AGL's and Origin Energy's pricing proposals.

ActewAGL's pricing proposal is slightly higher than the increase implied by the top end of the reasonable range for all 3 underlying retail cost components. We acknowledge that using the top end of the range is likely to lead to an upward bias in regulated retail prices, and favour the longer term objectives for this price review over the shorter term objectives.<sup>68</sup> However, we consider that this is appropriate for ActewAGL's regulated prices, as ActewAGL has a much larger proportion of customers on regulated retail prices than the average across NSW. In our view, ActewAGL's pricing proposal will encourage retailers to enter the market and customers to participate in it, consistent with the long term objectives for this review. Accordingly, we have made a final decision to agree to ActewAGL's pricing proposal.<sup>69</sup>

<sup>68</sup> Conversely, using the bottom end of the reasonable range for all 3 underlying cost components is likely to lead to a downward bias on regulated retail prices, and favour the shorter term objectives for this price review over the longer term objectives.

<sup>69</sup> We note that we agree an *average* change in regulated retail prices. Standard Retailers with more than one supply area can apply different price increases across different areas, as long as they comply with the *average* increase.

**Table 3.4 Standard Retailers' pricing proposals for 2014/15 and 2015/16 (\$2013/14)**

Proposals	2014/15	2015/16	Cumulative
AGL	CPI+13.9%	CPI-1.8%	CPI+11.9%
ActewAGL	CPI+13.9%	CPI-2.0%	CPI+11.6%
Origin (Albury/Murray Valley)	CPI+15.3%	CPI-5.8%	CPI+8.6%
Origin (Wagga Wagga)	CPI+17.1%	CPI-4.4%	CPI+11.9%

**Source:** Standard Retailers' proposals.

## 4 Assessing the proposed increase in the carbon component

In supplying their customers, Standard Retailer's incur costs in complying with the Federal Government's Carbon Pricing Mechanism (CPM). This mechanism, which commenced on 1 July 2012, places direct costs on around 350 entities<sup>70</sup> by requiring them to pay for their carbon emissions. Many of these liable entities will be part of the gas supply chain that delivers gas to households and businesses in NSW.

The Standard Retailers have estimated the carbon costs they will incur in 2014/15 and propose to pass these through in regulated gas prices. As Chapter 3 discussed, our final decision is to agree to the Standard Retailers' pricing proposals, including the amount of carbon costs to be passed through in regulated gas prices in 2014/15. Our regulatory framework allows for the carbon price to be removed from regulated prices should the mechanism be repealed.

The sections below present our final findings on the retailers' proposed carbon cost components, and outline our approach to assessing the reasonableness of their proposals.

### 4.1 Overview of final finding on proposed carbon cost components

- 1 IPART's final findings on the proposed carbon cost components of regulated retail gas prices in 2014/15 are that:
  - AGL's proposal of \$1.76/GJ is reasonable.
  - ActewAGL's proposal of \$1.75/GJ is reasonable.
  - Origin Energy's (Albury/Murray Valley) proposal of \$1.78/GJ is reasonable.
  - Origin Energy's (Wagga Wagga) proposal of \$1.78/GJ is reasonable.

Each Standard Retailer's proposed carbon cost component reflects the legislated increase in the carbon price in 2014/15. Note that the findings above are expressed in nominal amounts.

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<sup>70</sup> <http://www.cleanenergyregulator.gov.au/Carbon-Pricing-Mechanism/Liable-Entities-Public-Information-Database/LEPID-for-2012-13-Financial-year/Pages/default.aspx> as at 21 March 2014.

## 4.2 Our assessment of the retailer's proposed carbon cost components

Under the *Clean Energy Act 2011* (Cth) gas producers and network operators are liable for the emissions associated with their facilities (ie, extracting and transporting gas), and natural gas retailers are liable for the emissions associated with their customers' usage of gas.

The carbon cost component of regulated gas prices needs to reflect an estimate of the costs that are directly payable by the entities along the supply chain. These costs are estimated as a function of the price of carbon emissions and the amount of emissions from the supply chain. From 1 July 2014, the price of carbon emissions is legislated at \$25.40 per tonne CO<sub>2</sub>-e<sup>71,72</sup>, up 5.2% from the current carbon price of \$24.15. Table 4.1 summarises the retailers' proposed changes in their carbon cost components for 2014/15.

**Table 4.1 Standard Retailers' proposed carbon cost components for 2014/15 (\$nominal, per GJ)**

Standard Retailer	Current	2014/15	
	\$/GJ	\$/GJ <sup>a</sup>	% change
AGL	\$1.72	\$1.76 <sup>b</sup>	+2.1%
ActewAGL	\$1.72	\$1.75 <sup>b</sup>	+1.7%
Origin – Albury/Murray Valley	\$1.56	\$1.78	+13.9%
Origin – Wagga Wagga	\$1.63	\$1.78	+9.0%

<sup>a</sup> The carbon costs presented in this table differs slightly from those in the retailers' written proposals, as we have applied our own forecast of inflation.

<sup>b</sup> The difference between AGL's and ActewAGL's proposed carbon costs is due to rounding.

**Source:** IPART, *Review of regulated retail prices and charges for gas – From 1 July 2013 to 30 June 2016 – Final Report*, June 2013, p 43; Standard Retailers' proposals to IPART, February 2014; and IPART calculations.

In assessing each Standard Retailer's proposed carbon cost component for 2014/15, we compared the proposals with our estimates of reasonable carbon costs, which were based on:

1. the legislated carbon price of \$25.40 per tonne CO<sub>2</sub>-e in 2014/15
2. the most recently published National Greenhouse Account (NGA) emissions factors<sup>73</sup>
3. the retailers' proposed retail margins.

<sup>71</sup> <http://www.cleanenergyregulator.gov.au/Carbon-Pricing-Mechanism/About-the-Mechanism/Fixed-Price-2012-15/Pages/default.aspx> accessed 24 March 2014.

<sup>72</sup> CO<sub>2</sub>-e means CO<sub>2</sub> equivalence, ie, the amount of CO<sub>2</sub> emissions that would have the same amount of global warming impact as the greenhouse gas being considered. See <http://ecometrica.com/white-papers/greenhouse-gases-co2-co2e-and-carbon-what-do-all-these-terms-mean/>

<sup>73</sup> The NGA emissions factors include estimates of the typical CO<sub>2</sub>-e emissions intensity of a gas supply chain (ie, production and transportation of gas) as well as the emissions intensity of gas consumption (ie, the burning of gas). Source: Australian Government – Department of Industry, Innovation, Climate Change, Science, Research and Tertiary Education, *Australian National Greenhouse Accounts – National Greenhouse Accounts Factors*, July 2013, pp 14, 71.

Using this approach, we found that the retailers' proposed carbon costs are reasonable. (See Appendix C for our assessment of proposed carbon costs.)

### 4.3 Potential repeal of the Carbon Pricing Mechanism

The Voluntary Pricing Agreements include provisions for adjusting prices to reflect reductions in carbon related costs, for example if the CPM is repealed before 1 July 2015. In this event, IPART will request proposals from the retailers for removing carbon costs from prices. If the repeal of the CPM does not take effect by 1 July 2015, the carbon price for 2015/16 is unknown. In this case, we will agree with the Standard Retailers an approach to estimating the appropriate carbon price for 2015/16.

We note that if no carbon component applied from the start of 2014/15, then the nominal price increases over the next 2 years would be:

- ▼ For AGL: 11.7% in 2014/15 and 5.8% in 2015/16.
- ▼ For ActewAGL: 10.7% in 2014/15 and 6.6% in 2015/16.
- ▼ For Origin Energy (Albury/Murray Valley): 8.7% in 2014/15 and 5.5% in 2015/16.
- ▼ For Origin Energy (Wagga Wagga): 12.6% in 2014/15 and 5.0% in 2015/16.<sup>74</sup>

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<sup>74</sup> Source: IPART calculations.

## 5 Impact of price increases on customers

We received around 140 submissions on our draft decisions, with many stakeholders concerned about the impact of gas price increases on the affordability of gas for all customers. The impact of the increases in regulated gas price over the 2 years from 1 July 2014 on individual customers will vary – depending on factors such as their gas usage and Standard Retailer, the regulated price they are on, and how they respond to the price increases (eg, whether they can reduce their usage to manage their bills).

Given this, we conducted a set of analyses to explore the likely range of impacts on customers. In particular, we analysed:

- ▼ the impact of the final decisions on annual gas bills for typical residential and small business customers for each Standard Retailer
- ▼ gas and energy bills as a proportion of household disposable income, and how this varies for different households in the metropolitan NSW.

The sections below summarise our key findings, outline the measures and assistance available for customers concerned about bill increases and discuss our analysis in detail. Box 5.1 provides a brief overview of who uses gas in NSW, and what gas is used for.

### 5.1 Overview of key findings on the impact of the price increases on customers

Under our final decisions, the annual gas bills of ‘typical customers’ – those with average gas usage in metropolitan NSW and in non-metropolitan NSW – increase by:

- ▼ about \$136 to \$230 for residential customers over the 2 years to 30 June 2016 and
- ▼ about \$481 to \$888 for small business customers over the 2 years to 30 June 2016.



To consider the impact of gas price increases on household energy affordability, we looked at both gas bills and combined electricity and gas (ie, energy) bills.<sup>75</sup> A useful measure of energy affordability is the proportion of household disposable income spent on energy. Our analysis indicates that for the **majority** of households (more than 75%) that use gas, gas bills will represent less than 2% of their disposable income in 2014/15 and energy bills will represent less than 6% of their disposable income. However, some low-income households will spend more than 6% of their disposable income on energy.

We also found that household expenditure on energy bills as a proportion of disposable income will increase only marginally between 2013/14 and 2014/15. One reason for this is that electricity prices will decrease slightly in 2014/15, and this decrease will to some extent offset the increase in gas bills for dual fuel households.

## 5.2 Addressing concerns about customer impacts and affordability

Many stakeholders objected to the draft decisions and raised concerns about the affordability of the proposed price increases for customers in general,<sup>76</sup> and for low income households in particular.<sup>77</sup> Some of these stakeholders argued that gas is an essential service and should be priced so that it is affordable to everyone and/or that price increases should be kept in line with wage movement or CPI.<sup>78</sup>

<sup>75</sup> We note that on 7 April 2014 the NSW Government announced that [retail electricity prices will be fully deregulated from 1 July 2014](#). We have used the Government's transitional tariff for 2014/15, ie, a fall in residential bills of 1.5%, for the purpose of this analysis.

<sup>76</sup> See eg, N Melick submission to Draft Report, May 2014, p 1; L Wren submission to Draft Report, May 2014, p 1; K Taylor submission to Draft Report, May 2014, p 1; W Wenzel submission to Draft Report, May 2014, p 1; C Dunne submission to Draft Report, May 2014, p 1; J Tanious submission to Draft Report, May 2014, p 1; A Elliot submission to Draft Report, May 2014, p 1; K Berger submission to Draft Report, May 2014, p 1; G Manzi submission to Draft Report, May 2014, p 1; R Manzi submission to Draft Report, May 2014, p 1; N Chami submission to Draft Report, May 2014, p 1; M Chami submission to Draft Report, May 2014, p 1; B Chami submission to Draft Report, May 2014, p 1; A Rumble submission to Draft Report, May 2014, p 1; H Petterson submission to Draft Report, May 2014, p 1; M Mac submission to Draft Report, May 2014, p 1; C Upton submission to Draft Report, May 2014, p 1; D East submission to Draft Report, May 2014, p 1; G Ellison submission to Draft Report, May 2014, p 1; A Pradhan submission to Draft Report, May 2014, p 1 and J Ventoura submission to Draft Report, May 2014, p 1.

<sup>77</sup> See eg, M Bou submission to Draft Report, May 2014, p 1; D Comer submission to Draft Report, May 2014, p 1; M Ryan submission to Draft Report, May 2014, p 1; C Upton submission to Draft Report, May 2014, p 1; A Rumble submission to Draft Report, May 2014, p 1; C Shaw submission to Draft Report, May 2014, p 1; L Wren submission to Draft Report, May 2014, p 1; S Willet submission to Draft Report, May 2014, p 1; Lock the Gate submission to Draft Report, May 2014, p 3; NCOSS, p 1; PIAC, p 8 and EWON submission to Draft Report, May 2014, p 1.

<sup>78</sup> See eg, S Leveque submission to Draft Report, May 2014, p 1; A Elliot submission to Draft Report, May 2014, p 1 and G Ellison submission to Draft Report, May 2014, p 1; M Hanna submission to Draft Report, May 2014, p 1 and R Jones submission to Draft Report, May 2014, p 1.

We recognise that these increases in regulated gas prices are relatively large. They also come after a sustained period of large increases in energy (ie, gas and electricity) prices. Gas prices have increased by about 40% in real terms between 2006/07 and 2013/14, while regulated retail electricity prices increased by more than 80% over the same period. The price increases for 2014/15 are likely to be significant for some customers. Providing effective, targeted assistance to vulnerable customers is preferable to holding prices below efficient levels for all customers. We also consider that setting regulated prices at a level that reflects the efficient costs faced by a new entrant retailer facilitates competition. Competition should drive innovation and efficiency.

We note these decisions are about regulated prices - many of the prices in the market are lower. As a first step, customers concerned about gas or electricity prices should shop around for a better deal. The free comparison service available online at [energymadeeasy.gov.au](http://energymadeeasy.gov.au) is a good place to start. At present, discounts of up to 8% off the variable charge included in the regulated price are being offered. In addition, other products (eg, rate fixing or freezing) and innovations (eg, no early termination fees on market contracts) are available. We also note assistance is available from the NSW Government and energy retailers for customers experiencing hardship.

### 5.2.1 Government funded assistance

The NSW Government offers a number of rebates to help customers pay their energy bills (however, these rebates are paid on electricity bills).<sup>79</sup> These rebates include the:

- ▼ Low Income Household Rebate – for customers who hold eligible concession cards issued by the Federal Department of Human Services or the Department of Veterans Affairs
- ▼ Family Energy Rebate – available to customers who have received the Family Tax Benefit
- ▼ Life Support Rebate – for households where residents use certain medical equipment necessary to sustain life, and
- ▼ Medical Energy Rebate – for eligible customers who have a medically diagnosed inability to self-regulate body temperature when exposed to extremes of environmental temperatures.

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<sup>79</sup> See <http://www.resourcesandenergy.nsw.gov.au/energy-consumers/financial-assistance/rebates>

NCOSS and PIAC recommend that the energy rebate should be a fixed percentage of an eligible customer's actual bill, largely because lump sum rebates can provide relatively larger benefits to customers with smaller energy bills.<sup>80</sup> We note that percentage based rebates provide reduced incentive to reduce or manage consumption by responding to cost reflective price signals (and are more difficult to control from a government budgeting perspective than lump sum payments).

Work carried out by Deloitte (commissioned by the Energy Supply Association of Australia) concluded there is no one form of concession considered to be the single optimal, best practice structure; the UK typically favours lump sum rebates and percentage based concessions are more prevalent in the USA.<sup>81</sup>

Recent work carried out by National Economic Research Associates (NERA) (and Deloitte) suggests that some low income customers may be better off on capacity or critical peak tariffs and that these style of pricing can assist these customers managing their bills.<sup>82</sup> Innovative pricing structures that incentivise all customers to be more efficient in their energy use can lower bills. We encourage retailers to include different pricing structures/options in their suite of customer assistance measures.

NCOSS also recommends that energy efficiency programs should focus on low-income households and that minimum energy efficiency standards should apply for rental properties.<sup>83</sup> We note that these issues are policy matters for the NSW Government.

EWON requested that IPART make recommendations to Government to lessen the impact of the large price increase, endorsing the recommendations of the National Energy Affordability Roundtable.<sup>84</sup> We have made 2 recommendations for Government to consider on reviewing customer assistance measures and improving customers' market engagement (see section 5.2.3 below). These recommendations are consistent with some of the Roundtables' recommendations. We consider that the public funding currently made available for customer assistance measures should be directed to the areas of highest need.

## Recommendation

- 2 IPART recommends that the NSW Government review customer assistance measures to ensure that they are appropriately targeted at the most vulnerable customers.

<sup>80</sup> See NCOSS, p 3 and PIAC, pp 8-9.

<sup>81</sup> See, Deloitte, *Improving energy concessions and hardship payments policies*, February 2013, p 24.

<sup>82</sup> See <http://www.aemc.gov.au/getattachment/ae0759ea-c36c-41f8-bf34-832440d8dc24/Session-4-%E2%80%93-NERA-presentation-by-Adrian-Kemp-%E2%80%93-cas.aspx> p 26 and Deloitte Op. Cit., p 4.

<sup>83</sup> See NCOSS, pp 3-4.

<sup>84</sup> See EWON submission to Draft Report, May 2014, p 2.

### 5.2.2 Retailer provided assistance

Energy retailers are required by law to have a published hardship charter and to operate a customer assistance program (which is subject to approval by the AER).<sup>85</sup> While retailers may have (slightly) different criteria for eligibility in to their financial hardship programs, the common element is that when a customer is part of an assistance program, they are protected from disconnection and a tailored payment arrangement is developed to help them manage their account.

PIAC recommends that IPART highlights the damage of bill shock from a significant price increase in mid-winter and that retailers should defer price increases until the end of winter 2014.<sup>86</sup> We note that energy retailers also generally offer options for bill smoothing, where the estimated total cost of a customer's energy bills for the next year are spread across equal monthly, fortnightly or weekly instalments. This helps customers manage their budget and cash flow, and reduces the impact of changes in bills due to seasonal energy use.

NCOSS recommends that retailers should commit to best practice customer hardship programs.<sup>87</sup> We note that under the National Energy Consumer Framework (NECF), the retailers' customer hardship programs have to be approved by the Australian Energy Regulator.<sup>88</sup>

### 5.2.3 Improving customer engagement in the market

Some stakeholders indicated that they had been encouraged to switch to gas from electricity for environmental or energy efficiency reasons or because, at the time, gas was the cheaper fuel.<sup>89</sup> In making decisions about fuel sources and appliances, customers need access to information to make informed choices. This includes information on price levels and structures and price trends. We note that Australian Energy Market Commission (AEMC) publishes a regular report on residential energy price trends.<sup>90</sup>

<sup>85</sup> See <http://www.aer.gov.au/retail-markets>

<sup>86</sup> See PIAC, p 8.

<sup>87</sup> See NCOSS, p 4.

<sup>88</sup> See <http://www.aer.gov.au/retail-markets>

<sup>89</sup> See eg D East submission to Draft Report, May 2014, p 1; H Petterson submission to Draft Report, May 2014, p 1 and D Pearce submission to Draft Report, May 2014, p 1.

<sup>90</sup> See eg <http://www.aemc.gov.au/Markets-Reviews-Advice/Retail-Electricity-Price-Trends-2013#>

We consider there is scope for further action to improve customers' market awareness and engagement in this area. In particular, customers should have access to a resource that allows them to estimate household energy bills under different combinations of fuel type, appliance and energy price.<sup>91</sup> This will assist customers – in particular low income households – to make informed decisions, including on the most efficient fuel type, how to manage their bills and to become more energy efficient.<sup>92</sup> It should also encourage competition and product differentiation in energy retailing.

#### Recommendation

- 3 IPART recommends that assistance is provided to households to raise awareness and understanding of, and engagement in, competitive energy markets. In particular, the Australian Energy Regulator's Energy Made Easy website should be expanded to include resources that assist customers to make decisions on fuel type and to estimate energy bills under different fuel type, appliance and energy price scenarios.

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<sup>91</sup> In making decisions about fuel sources and appliances, customers need to be aware of the usage associated with different options and also the fact that a fixed charge is levied on both gas and electricity supply regardless of actual usage.

<sup>92</sup> We consider that this is particularly important in light of full electricity deregulation from 1 July 2014.

### Box 5.1 Who uses gas and what for?

Only some NSW households use mains gas<sup>a</sup> - about half of households in the Sydney metropolitan area<sup>b</sup> and about 40% of all NSW households.<sup>c</sup>

Gas is more commonly used by higher income households than those with lower incomes. For example, our Sydney (2010) household survey found that about 60% of high-income households use gas compared to about 40% of low-income households.<sup>d</sup>

Gas is used instead of electricity for cooking, hot water and/or space heating. Some households use gas for all 3 purposes, while others use it for only 1 or 2 purposes. In Sydney in 2010, about one third of households with gas used it for cooking and hot water and another third used it for all 3 purposes.<sup>e</sup>

How much gas a household uses depends on a number of factors, including:

- ▼ What it uses gas for. Households that use gas only for cooking use a small amount of gas, while those that use gas for 2 or 3 purposes use far more gas.
- ▼ How many people are in the household, particularly if gas is used for hot water.
- ▼ The type and size of dwelling, particularly if gas is used for heating.
- ▼ The climate zone, particularly if gas is used for heating.<sup>f</sup>

<sup>a</sup> Mains gas refers to gas supplied by gas distribution pipes connected to the dwelling.

<sup>b</sup> IPART, *Residential Energy and Water Use in Sydney, the Blue Mountains and Illawarra - Results from the 2010 household survey*, December 2010, p 75.

<sup>c</sup> Calculated from information provided by Jemena Gas Networks.

<sup>d</sup> IPART, *Residential Energy and Water Use in Sydney, the Blue Mountains and Illawarra - Results from the 2010 household survey*, Appendix E, Table 1, December 2010.

<sup>e</sup> IPART, *Residential Energy and Water Use in Sydney, the Blue Mountains and Illawarra - Results from the 2010 household survey*, December 2010, pp 82-83.

<sup>f</sup> See IPART, *Determinants of residential energy and water consumption in Sydney and surrounds. Regression analysis of the 2008 and 2010 household survey data*, December 2011, Chapter 4.

## 5.3 Impact of final decisions on typical customer bills in each supply area

To estimate the potential impact of our final decisions on customers, we have calculated an indicative annual gas bill for residential and business customers with average usage in each gas supply area (Table 5.1 and 5.2).<sup>93,94</sup>

<sup>93</sup> AGL, the Standard Retailer for the Sydney metropolitan region, has only one regulated tariff for residential customers and one for business customers. The other standard retailers have a number of different residential and business tariffs, and supply more than 1 region (with different regional network tariffs).

<sup>94</sup> We cannot calculate how our final decisions will affect individual customers' annual gas bills. This impact will depend on how much gas they use, which of their Standard Retailers' regulated prices they are on, and how the Standard Retailer changes these individual price.

This analysis indicates that in the 2-year period to 2015/16:<sup>95</sup>

- ▼ Typical residential customers will face an increase of between \$136 and \$230 in their annual gas bill.
- ▼ Typical small business customers will face increases of between \$481 and \$888 in their annual gas bill.

Almost all of the increases will occur in 2014/15, and will be followed by small increases or decreases in 2015/16 (Table 5.1 and 5.2).

**Table 5.1 Indicative annual bill for typical residential customers of each Standard Retailer (nominal \$, inc GST)**

	Current bill (2013/14)	Estimated bill (2014/15)	Estimated bill (2015/16)	\$ increase over 2 years
AGL	901	1,056	1,063	162
ActewAGL	1,292	1,515	1,522	230
Origin Energy (Albury/Murray Valley)	933	1,107	1,069	136
Origin Energy (Wagga Wagga)	1,027	1,237	1,212	186

**Note:** This assumes a typical customer uses 23GJ, 45GJ, 45GJ, and 37GJ of gas per annum in the AGL, ActewAGL, Origin Energy (Murray Valley) and Origin Energy (Wagga Wagga) areas respectively. Bills are for regulated prices and include GST.

**Source:** AGL, ActewAGL and Origin; IPART calculations.

**Table 5.2 Indicative annual bill for typical business customers of each Standard Retailer (nominal \$, excl GST)**

	Current bill (2013/14)	Estimated bill (2014/15)	Estimated bill (2015/16)	\$ increase over 2 years
AGL	4,201	4,926	4,959	757
ActewAGL	4,997	5,858	5,885	888
Origin Energy (Albury/Murray Valley)	3,295	3,911	3,776	481
Origin Energy (Wagga Wagga)	3,503	4,221	4,136	633

**Note:** This assumes a typical customer uses 184GJ, 246GJ, 209GJ and 231GJ of gas per annum in the AGL, ActewAGL, Origin Energy (Murray Valley) and Origin Energy (Wagga Wagga) areas respectively. Bills are for regulated prices and exclude GST.

**Source:** AGL, ActewAGL and Origin; IPART calculations.

<sup>95</sup> The increases in typical gas bills do not take account of any increases in energy rebates available to low and middle-income households from 1 July 2014. Energy rebates are credited to electricity bills.



## 5.4 Energy bills as a proportion of disposable income

To consider the impact of the final decisions on households we focused on household energy bills as a proportion of household disposable income, where disposable income means income after accounting for tax.<sup>96</sup> This is a useful measure, as it takes into account movements in household incomes as well as energy bills. In addition:

- ▼ We looked at combined electricity and gas (ie, energy) bills, because this provides a more complete picture of energy affordability than looking at gas bills alone.
- ▼ We focused our analysis on metropolitan NSW (Sydney, Blue Mountains, Illawarra, Hunter and Central Coast) because we have detailed information on energy usage, energy costs, and household characteristics from our Household Surveys in these areas. We included in the analysis only households that use both mains gas and electricity (ie, dual fuel households).
- ▼ We focused on impacts in 2014/15, because almost all of increase in gas prices occurs in this year.
- ▼ We took into account rebates on energy bills, but we show gas bills without energy rebates.<sup>97</sup>

The section below discusses the key findings of our analysis.

### 5.4.1 How do energy bills as a proportion of disposable income vary in metropolitan NSW?

We also looked at expenditure by dual fuel households on energy as a proportion of disposable income. Using the data on electricity and gas usage from our household surveys data, information about changes in average energy usage since our surveys,<sup>98</sup> our final decisions on regulated gas prices and the Government's announcement regarding electricity price deregulation and the price decrease of 1.5% under the transitional tariff for 2014/15, we found that more than 75% of all dual fuel households in the Sydney metropolitan area will spend less than 6% of their disposable income on energy bills in 2014/15. In addition, only 7% of households in this area are likely to spend more than 10% of their disposable income on energy.

<sup>96</sup> We also took into account the Commonwealth Government's Household Assistance Package, which was introduced in 2012 to compensate households for the introduction of the carbon. For an explanation of how we did this, and for more information about the Package, see IPART, *Changes in regulated electricity retail prices from 1 July 2012 – Final Report*, June 2012, pp 68-69 and 76-82.

<sup>97</sup> The rebates are for energy, and typically appear on a customer's electricity bill.

<sup>98</sup> Information from the NSW electricity network businesses shows that average electricity consumption per household fell by about 12% between 2009/10 and 2012/13.



As Figure 5.1 shows, median household spending on energy across all income categories will be just less than 4% of disposable income. However, looking at different income categories, median household spending on energy varies quite widely:

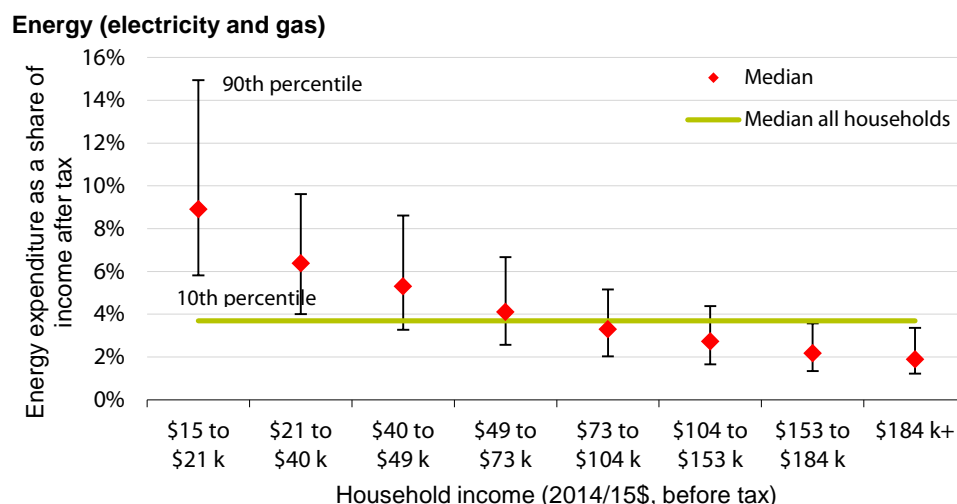
- ▼ In the middle and higher income categories (more than \$49,000 per year), median household spending on energy will range from about 2% to 4% of disposable income.
- ▼ In the 2 low-income categories (\$40,000 or less per year), median spending on energy will range from around 6% to 9% of disposable incomes.

Between households with similar disposable incomes in the lower income categories, there is substantial variation. For example, in the lowest income category, households with median energy use are likely to spend about 9% of their disposable income on energy, while those in the 10th percentile will spend about 6%, and those in the 90th percentile will spend about 15%. In the second lowest income category, median households will spend about 6% of their disposable income on energy, while those in the 90th percentile will spend almost 10% on energy.<sup>99</sup>

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<sup>99</sup> For information about why energy bills vary so much between low-income households in Sydney, see IPART, *Changes in regulated electricity retail prices from 1 July 2012 - Final Report*, June 2012, Appendix E.

**Figure 5.1 Annual spending on energy as a share of disposable household income — Sydney and surrounding regions, 2014/15**



**Note:** The income for the middle of each band is used to calculate disposable income. Disposable income as a share of household income is derived from ABS household income distribution data for 2009/10. Income for each band is inflated to 2012/13 using the change in average weekly earnings. Income forecasts for 2013/14 and 2014/15 use NSW Treasury's forecast increase in the average wage index of 2.75% and 3% respectively. Disposable income is further adjusted for the impact of the carbon compensation package. Distributions are presented without weighting survey responses.

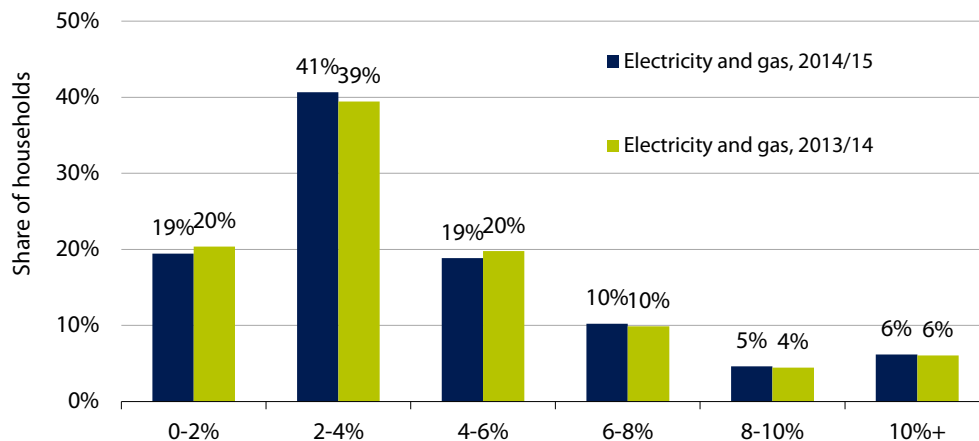
A **percentile** is the value below which a certain percentage of observations fall. For example, the 10th percentile is the value below which 10% of the observations may be found. In the above diagram, 10% of customers in each income band would fall below the bottom of the vertical line (paying less than that amount) and 10% of customers would pay more than the top of the vertical line.

**Sources:** IPART Household Surveys, 2008 and 2010; ABS, ABS, Average weekly earnings, Australia, November 2011 and November 2013, Catalogue 6302.0, Table 11A; NSW Government, 2013-14 Half-Yearly Review, 20 December 2013, p 29; IPART calculations.

Despite the increase in gas prices, household expenditure on energy bills as a proportion of disposable income will increase only marginally between 2013/14 and 2014/15 (Figure 5.2). One reason for this is that electricity prices will decrease slightly in 2014/15, and this decrease will to some extent offset the increase in gas bills for dual fuel households.<sup>100</sup>

<sup>100</sup> On 7 April 2014 the NSW Government announced that [retail electricity prices will be fully deregulated from 1 July 2014](#). We have used the Government's transitional tariff for 2014/15, ie, a fall in residential bills of 1.5%, for the purpose of this analysis.

**Figure 5.2** Distribution of annual spending on energy as a share of disposable household income — Sydney metropolitan area, 2013/14 and 2014/15



**Note:** Disposable income as a share of household income is derived from ABS household income distribution data for 2009/10. Income for each band is inflated to 2012/13 using the change in average weekly earnings. Income forecasts for 2013/14 and 2014/15 use NSW Treasury's forecast increase in the average wage index of 2.75% and 3% respectively. Disposable income is further adjusted for the impact of the carbon compensation package. Customer bills have been adjusted to reflect lower average electricity consumption per household. Customer bills are net of the Low Income Household Rebate. We have assumed that average electricity prices in the Sydney metropolitan region will decrease by 1.5% in nominal terms, in line with the Government's transitional tariff.

**Data source:** IPART Household Surveys, 2008 and 2010; ABS, ABS, Average weekly earnings, Australia, November 2011 and November 2013, Catalogue 6302.0, Table 11A; NSW Government, 2013-14 Half-Yearly Review, 20 December 2013, p 29; IPART calculations.

Our June 2013 final report from the 2013 price review provided additional analysis of the impact on residential customers of increases in energy prices since 2006/07. In broad terms, most of this analysis remains valid for the 2 years to 2015/16 and is therefore not repeated here.<sup>101</sup>

<sup>101</sup> IPART, *Review of regulated retail prices and charges for gas From 1 July 2013 to 30 June 2016 – Final Report*, June 2013, chapter 8.





## Appendices



## A Terms of Reference



**Chris Hartcher MP**  
Minister for Resources and Energy  
Special Minister of State and  
Minister for the Central Coast

V12/4188

Dr Peter Boxall  
Chairman  
Independent Pricing and Regulatory Tribunal  
PO Box Q290  
QVB POST OFFICE NSW 1230

Dear Dr Boxall

Pursuant to section 43EA(1) of the *Electricity Supply Act 1995* (the Act), I am referring to the Tribunal for investigation and report, the determination of regulated electricity retail tariffs and charges in New South Wales for the period from 1 July 2013 to 30 June 2016. Please find further details in the attached Terms of Reference to the Tribunal.

I confirm that an amendment regulation will be made to extend the operation of Part 4, Division 5 of the Act to 30 June 2016, under which the Tribunal's determination may be made.

With regard to gas tariffs and charges, I note that the current standard tariffs for gas small retail customers, previously agreed by the Tribunal and the standard gas retailers under Voluntary Transitional Pricing Arrangements (VTPAs) are due to expire on 30 June 2013.

I further request that the Tribunal continue to regulate the standard tariffs for small retail gas customers for the period 1 July 2013 to 30 June 2016, in accordance with section 27 of the *Gas Supply Act 1996* (the Act). I request that the Tribunal ensure that either new VTPAs or gas pricing orders are in place for the period 1 July 2013 to 30 June 2016.

In regulating such prices, the Tribunal should ensure that the objects under section 3 of the Act are taken into consideration, and that stakeholders are consulted as part of the review process. In order to ensure that standard retail gas tariffs reflect the efficient costs of supplying natural gas to small retail customers, I request the Tribunal to consider whether it should undertake a review of these costs, and to undertake such a review if deemed necessary.

I look forward to the Tribunal's final report on both these matters in time for commencement on 1 July 2013.

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V12/4188

If you require further information on this matter, please contact Jessie Foran, Senior Policy Advisor for Energy, in my office on (02) 9228 5289.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Chris Hartcher'.

**Chris Hartcher MP**

Encl. 27.9.12



## B Customer acquisition and retention costs

IPART's terms of reference for the 2013 review of regulated retail gas prices indicate that we must ensure the objects under section 3 of the *Gas Supply Act 1996* are taken into account. Among other things, these objects include:

- ▼ to encourage the development of a competitive market in gas
- ▼ to regulate gas reticulation and gas supply, so as to protect the interests of customers and to promote customer choice in relation to gas supply.

In their original pricing proposals for 2014/15 and 2015/16, AGL and ActewAGL noted that we included an allowance for customer acquisition and retention costs (CARC) in setting prices in our 2013 review of regulated retail prices for electricity (and that we had used this allowance to ensure that regulated prices provided sufficient incentive to encourage competition). AGL and ActewAGL initially proposed that a consistent approach be adopted for regulated retail gas prices; however, their revised proposals do not include any additional competition allowance.<sup>102</sup>

We have not previously included a specific competition allowance in assessing the reasonable range for gas prices (although some of the Standard Retailers have included some customer acquisition costs in their proposals). We therefore considered whether a CARC or a similar competition allowance in the retail gas price is required.

### B.1 Approach to setting the incentives in regulated gas prices

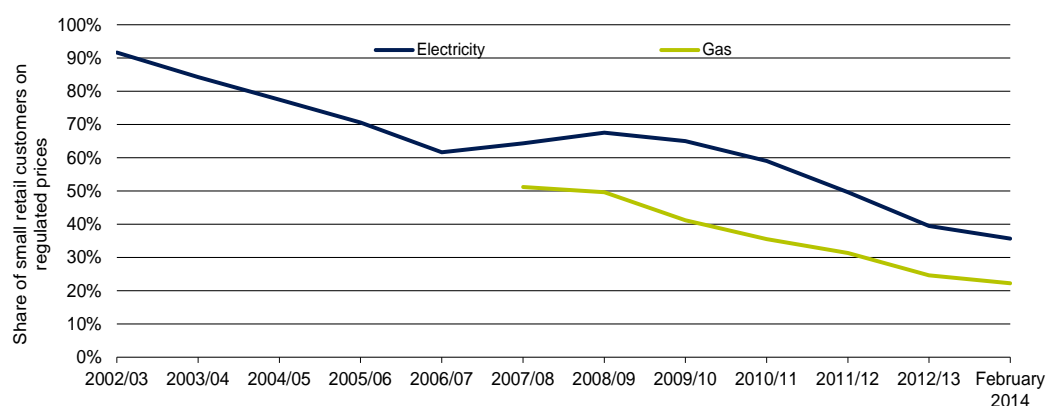
For electricity, our 2013 determination included an incentive in regulated retail prices that is consistent with a reasonable transition path to a largely deregulated market. This balanced the short term objective of setting prices that reflect efficient costs against the longer term objective of promoting competition. Our view is that, over time, a higher incentive will lead to a more rapid transition to a largely deregulated market and a lower incentive to a less rapid transition.

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<sup>102</sup> AGL submissions, 11 February 2014, pp 21-22 and 21 March 2014, pp 1-2; ActewAGL submissions, 11 February 2014, p 6 and 25 March 2014, p 1.

Across NSW and as at February 2014, the share of small customers on regulated prices in the gas market is smaller than in the electricity market (Figure B.1).<sup>103</sup> In both markets, the share of customers on regulated prices has declined over the past 4 years.

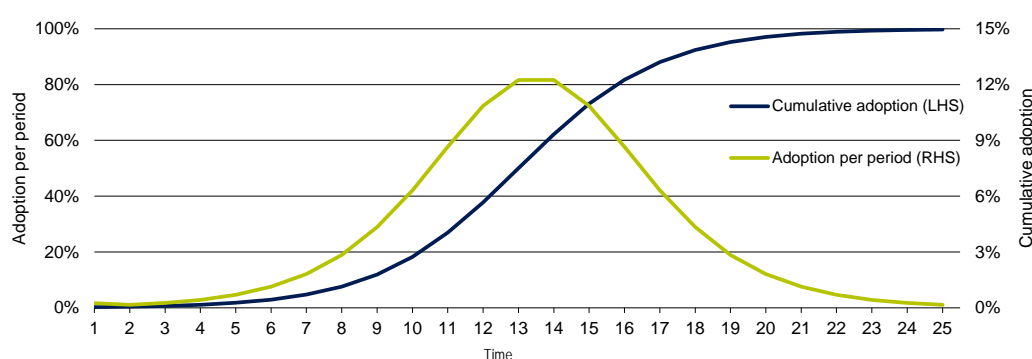
**Figure B.1 Share of small retail customers on regulated prices for electricity and gas**



**Data source:** IPART calculations based on information provided by distributors and retailers.

We consider it likely that the rate of uptake of market offers will slow, as the share of customers remaining on regulated prices is smaller. This would be consistent with the S-shaped curve of diffusion, which can be used to analyse the adoption of market offers (Figure B.2).

**Figure B.2 S-shaped adoption curves for market offers**



**Data source:** Rogers, E. M. (1962) *Diffusion of innovations*. New York: Free Press.

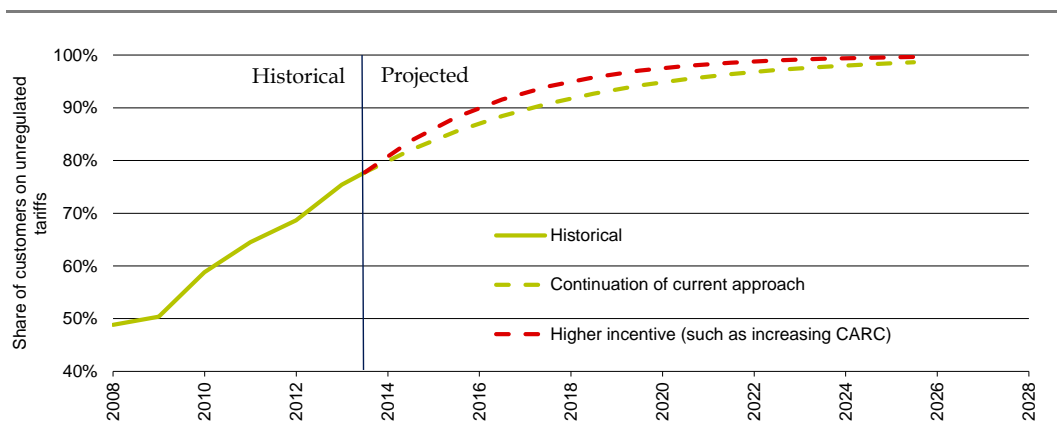
<sup>103</sup> We note that on 7 April 2014 the NSW Government announced that [retail electricity prices will be fully deregulated from 1 July 2014](#).

Our view is that a level of CARC should be allowed that will lead to a reasonable transition to a largely deregulated market for gas. We anticipate that, across NSW, the vast majority (90%) of small gas retail customers will be on market offers within 4 years, if we accept the revised pricing proposals made by the Standard Retailers (Figure B.3).

If we allowed for an additional CARC allowance, beyond that allowed in our current approach, then this would speed up the movement off regulated prices further.

The number of customers switching to market offers will of course depend on factors other than the regulated retail price. For example, the substantial increases in regulated prices proposed for some areas would likely lead to more customers looking for alternative offers.

**Figure B.3 Customers on market offers under alternative regulatory incentives**



**Note:** The standard transition model is an S-shaped function. This analysis uses a Gompertz function:  $\frac{\dot{c}}{c} = -\alpha \log\left(\frac{c}{\bar{c}}\right)$  where  $c$  is the share of adopters (in this case of an unregulated price or market offer),  $\dot{c}$  is the rate of change of adopters,  $\bar{c}$  is final adoption level (in this case 100%) and  $\alpha$  is a parameter that determines the speed of change. The speed of change under alternative incentives is mapped to historical observed changes.

**Data source:** IPART calculations.

## B.2 Reasonable transition path

The Jemena gas distribution network serves the majority of gas customers in NSW (AGL and ActewAGL are the Standard Retailers on this network). Our analysis indicates that this market has transitioned more rapidly than electricity,<sup>104</sup> with 90% of small customers likely to be on market offers within 4 years. Accordingly, we consider that there is no reason to make an adjustment to regulated retail prices to incorporate an additional CARC allowance.

For other smaller distribution areas there is potential for competition (except for the Shoalhaven area at present). For these areas, there may be scope to allow for an additional incentive in regulated retail prices to encourage retailers to enter and customers to participate in the competitive market.

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<sup>104</sup> Although we note that with the NSW Government's announcement of full retail electricity price deregulation, there will be no customers on regulated electricity prices from 1 July 2014.

## C Assessment of proposed carbon costs

This appendix sets out the input values, assumptions and calculations we have used to undertake our assessment of the Standard Retailers' proposed carbon costs.

**Table C.1 Carbon price per tonne CO<sub>2</sub>-e in 2014/15 (\$ nominal)**

\$25.40
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**Source:** <http://www.cleanenergyregulator.gov.au/Carbon-Pricing-Mechanism/About-the-Mechanism/Fixed-Price-2012-15/Pages/default.aspx>

**Table C.2 NGA emissions factors from 1 July 2013 (kg CO<sub>2</sub>-e/GJ)**

	Metro	Non-Metro
<i>Upstream</i>	12.8	13.5
<i>Consumption</i>	51.33	51.33

**Source:** Australian Government – Department of Industry, Innovation, Climate Change, Science, Research and Tertiary Education, *Australian National Greenhouse Accounts – National Greenhouse Accounts Factors*, July 2013, pp 14, 71.

**Table C.3 Retailer specific inputs**

	AGL	ActewAGL	Origin
<b>Share of gas customers in metro vs. non-metro regions<sup>a</sup></b>			
<i>Metro</i>	50%	50%	0%
<i>Non-metro</i>	50%	50%	100%
<b>Retailers' emissions factors (kg CO<sub>2</sub>-e/GJ)<sup>b</sup></b>			
<i>Upstream emissions factor</i>	13.15	13.15	13.50
<i>Consumption emissions factor</i>	51.33	51.33	51.33
<b>Proposed retail margin<sup>c</sup></b>			
	7.0%	7.3%	7.0%

<sup>a</sup> Sourced from the retailers' proposals for AGL and ActewAGL. Assumed for Origin, on the basis of the notes to Table 37 in: Australian Government – Department of Industry, Innovation, Climate Change, Science, Research and Tertiary Education, *Australian National Greenhouse Accounts – National Greenhouse Accounts Factors*, July 2013, p 71.

<sup>b</sup> Calculated as the weighted average Metro vs non-metro emissions factors as per Table C.2, using the share of customers in metro vs. non-metro regions as weights.

<sup>c</sup> Sourced from the retailers proposals.

**Table C.4 Estimated reasonable carbon costs 2014/15 (\$ nominal /GJ)**

	AGL	ActewAGL	Origin
<i>Upstream costs</i>	0.33	0.33	0.34
<i>Consumption costs</i>	1.30	1.30	1.30
<i>Margin</i>	0.11	0.12	0.12
<b>Total</b>	<b>1.75</b>	<b>1.76</b>	<b>1.76</b>

**Source:** IPART calculations on the basis of the carbon price (Table C.1) and the retailer specific inputs in Table C.3.

**Table C.5 Proposed carbon costs vs. estimated reasonable carbon costs**

	AGL	ActewAGL	Origin
<i>Proposed total carbon costs (\$2014/15)</i>	1.76	1.75	1.78
<i>Deviation from reasonable estimates</i>	+0.2%	-0.4%	+0.8%

**Note:** The proposed carbon costs in this table differ slightly from those in the retailers' proposals, as we have used our own forecast inflation numbers.

**Source:** Standard Retailers' proposals and IPART calculations.