Mid-term review of AGL Retail Energy's gas retail prices to 2004

INDEPENDENT PRICING AND REGULATORY TRIBUNAL
OF NEW SOUTH WALES

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1 INTRODUCTION

The Independent Pricing and Regulatory Tribunal of NSW (the Tribunal) has completed its mid term review of the prices that AGL Retail Energy (AGLRE) can charge its default tariff customers in NSW for natural gas.[1] The prices determined at this review will come into effect on 1 July 2003 and apply for twelve months.

1.1 Purpose and scope of the mid term review

When AGLRE's Voluntary Pricing Principles (VPPs) were introduced, the Tribunal stated its intention to conduct a mid term review to consider matters that were uncertain at the time of the initial review and how any such changes should be incorporated into AGLRE's prices. The review was to be conducted from 2002 at the request of either AGLRE or the Tribunal.

The scope of the mid term review was to consider material changes in AGLRE's costs of supplying gas and any relevant changes in market circumstances since the current regulatory arrangements were put in place in February 2001. The matters considered at this mid term review were:

- increases to the field price of natural gas
- additional costs incurred by AGLRE to supply the default market
- AGLRE's request to add four new miscellaneous (non-tariff) charges.

1.2 The mid term review process

On 28 March 2003, AGLRE submitted its mid term review proposal to the Tribunal (the proposal is available on the Tribunal's website www.ipart.nsw.gov.au). AGLRE developed the proposal in consultation with the AGL Customer Council and presented it to the Energy Industry Consultation Group[2] at the beginning of April. The Tribunal also held a roundtable discussion on 14 May, inviting interested parties to join members of the Tribunal and AGLRE to discuss and comment on elements of AGLRE's proposal. Written submissions were sought following the roundtable discussion.

1.3 Agreed tariff changes

The Tribunal has agreed to increases to AGLRE's default tariffs that will come into effect on 1 July 2003 and expire on 30 June 2004. The increases will result in quarterly bills for customers on these tariffs rising by approximately 8.8 percent on average.[3] This is less than the average increase of 9.6 percent requested by AGLRE.

In agreeing to the tariff changes, the Tribunal has taken into account AGLRE's costs of supplying customers on each of its default tariff plans. The Tribunal is cognisant that default

[1] Default tariffs apply to customers supplied on a standard form customer supply contract. Customers that consume more than 1 terajoule of gas per annum are not eligible for default tariffs.

[2] The Energy Industry Consultation Group is a stakeholder group consisting of representatives from electricity and gas retailers and network owners, the Energy and Water Ombudsman of NSW, the NSW Ministry of Energy and Utilities, the Public Interest Advocacy Centre, NSW Treasury and several large energy users.

[3] This is the average of four market sectors – small, medium and large residential and medium industrial. For more detailed information refer to chapter 4.

tariffs that are not cost reflective may hamper the development of competition.[4] It considers that the tariffs agreed to at this review will continue to move default tariffs towards cost-reflective levels without creating unnecessary price shocks for customers.

1.4 Structure of this report

This report is supplementary to the Tribunal's *Final Report – Review of the Delivered Price of Natural Gas to Tariff Customers Served from the AGL Gas Network in NSW* released in February 2001 and should be read in conjunction with that document.[5]

This report explains the outcome of the mid term review of AGLRE's VPPs and the rationale behind it in more detail:

- Chapter 2 provides an overview of the regulatory framework within which AGLRE's proposal was submitted, including information on the Tribunal's role
- Chapter 3 contains the Tribunal's assessment of AGLRE's proposal – including changes to AGLRE's costs and the introduction of new miscellaneous charges
- Chapter 4 sets out the outcome and price implications of the review for customers on default tariffs for different levels of gas usage.

4 Setting default tariffs artificially low may restrict competition because new retailers will find it difficult to offer a more attractive service to customers. However, tariffs set at cost reflective levels should operate in a 'neutral' manner.

5 The report is available on the Tribunal's website (www.ipart.nsw.gov.au) under Gas.

2 REGULATION IN THE NSW GAS MARKET

This chapter provides an overview of the Tribunal's regulatory role in the small retail gas market in NSW and shows how the mid term review fits into the current regulatory regime.

2.1 Overview of the Tribunal's role

The NSW Government has been progressively introducing competition into the natural gas market. Market reforms have enabled new suppliers to enter the gas retail market, and since 1 January 2002, all gas customers in NSW have been able to choose their supplier.[6] As part of the Government's framework to support full retail competition in gas, the Tribunal is responsible for:

- administering retail price regulation in the tariff market under the *Gas Supply Act 1996*
- authorising (licensing) gas retailers and network operators
- monitoring compliance with retail price regulation, authorisation conditions and customer protection regulations
- establishing 'default tariffs' during the transition to effective retail competition.

The purpose of setting default tariffs is to protect customers who:

- are already connected to gas and need assurance that they will not be stranded with gas appliances but no gas retailer
- do not have a choice of retailer or who do not consciously exercise a choice of retailer
- otherwise may not benefit from a competitive market.

2.2 Current form of regulation

The default tariff regime regulated by the Tribunal applies only to residential and business customers consuming less than 1 terajoule of gas per annum (this equates to a bill of up to approximately $12,500 a year). The regime covers the majority of tariff market customers (generally households and small businesses) in NSW and all of these customers have the option of remaining on, or returning to, default tariffs.

For customers supplied by AGLRE, the current default tariff regime was put in place in February 2001. It sets a path for default tariffs through a set of Voluntary Pricing Principles (VPPs) agreed between the Tribunal and AGLRE and will remain in force until 30 June 2004.[7]

A copy of the VPPs, agreed between the Tribunal and AGLRE, is provided in Appendix 1 of this report.

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6 Although small customers are able to choose their supplier, there is currently a limited choice of gas retailers in most areas of NSW.

7 More detail on the current regime and its implementation is available in the Tribunal's publication, *Final Report - Review of the Delivered Price of Natural Gas to Tariff Customers Serviced from the AGL Gas Network in NSW,* February 2001.

3 TRIBUNAL'S ASSESSMENT OF AGLRE'S PROPOSAL

One of the primary objectives of default tariffs is that they reflect the cost of supplying gas to customers. As part of the mid term review, AGLRE informed the Tribunal that some of the costs it incurs in delivering gas to customers have risen since the introduction of the VPPs and as a result has requested an increase in tariffs for default customers. AGLRE also requested that the Tribunal agree to the introduction of a number of new miscellaneous (non tariff) charges.

This chapter outlines the Tribunal's analysis of the appropriate level of costs to incorporate into default tariffs. The Tribunal has considered the following cost increases submitted by AGLRE in providing a retail gas service:

- the field price of gas under new supply contracts entered into by AGLRE
- authorisation fees and external gas market costs
- operating costs.

3.1 Increase in the field price of gas

In December 2002, AGL Wholesale Gas Limited[8] concluded its negotiation of new gas supply contracts with gas producers on behalf AGL retail suppliers, including AGLRE. AGLRE submits that these new contracts have resulted in significant increases in the cost of gas that it will incur to supply its customers. AGLRE considers that the new arrangements have become necessary due to declining reserves in the Cooper Basin and has argued that despite the cost increases, the negotiation process has secured gas from a number of sources resulting in long-term, flexible supplies at competitive prices.

AGLRE also advised the Tribunal that it had to procure additional gas at a cost that was higher than anticipated in the VPPs over the 2002/03 year (AGLRE submitted that the shortfall amounted to $0.13 per gigajoule).

In addition, AGLRE requested the Tribunal's agreement to passing through $0.006 per gigajoule into default tariffs for estimated gas balancing costs to be incurred as a result of AGLRE's daily nominations differing from actual consumption by more than a threshold amount set by the Gas Market Company.

3.1.1 Verification of AGLRE's cost of gas

Due to confidentiality clauses in the gas supply contracts, AGLRE did not provide the Tribunal with copies of the contracts to allow direct verification of the proposed gas costs. However, at the Tribunal's request, AGLRE provided (on a confidential basis) an audit report from its external auditors, Deloitte Touche Tohmatsu, to verify that the gas costs proposed by AGLRE were consistent with the new supply contracts.

8 AGL Wholesale Gas and AGLRE are both wholly owned by the Australian Gas Light Company.

The 'agreed upon procedures' audit (under Australian Auditing Standard AUS 904) provided factual answers to questions directed at:

- reconciling the gas costs submitted by AGLRE to the supply contracts
- calculating the gas cost that would result from allocating the cheapest gas available to AGLRE to customers on default tariffs.

The audit report confirmed the costs submitted by AGLRE. A letter from Deloitte Touche Tohmatsu describing the audit process is available from the gas section of the Tribunal's website (www.ipart.nsw.gov.au).

3.1.2 Analysis of AGLRE's cost of gas

As the new supply contracts comprise a capacity charge in addition to charges for the amount of gas actually supplied, AGLRE advised that the per unit gas cost will be higher in a cold winter than in a mild winter and provided the Tribunal with a range, rather than a single gas cost, to reflect this. AGLRE proposed basing tariffs on a cost at the higher end of the range to reflect the risk of incurring the higher cost of gas in a cold winter. [9]

The Tribunal also obtained expert advice from an independent consultant (Project Consultancy Services) to inform its analysis of AGLRE's gas costs, which was provided on a confidential basis. In assessing the proposed gas cost for default tariffs the Tribunal also had regard to information provided by AGLRE, the audit report provided by Deloitte Touche Tohmatsu and other information including seasonal forecasts issued by the Bureau of Meteorology. Appendix 2 contains further information regarding the factors the Tribunal considered in assessing AGLRE's field cost of gas.

The Tribunal agreed to a gas cost for 2003/04 in the middle of the range proposed by AGLRE in recognition that there is some weather related risk involved in supplying gas to the default market in NSW. The Tribunal considers that this provides a reasonable estimate of the costs that AGLRE would incur in an average winter although it has also considered factors specific to the period in question.

In relation to AGLRE's under recovered gas costs for 2002/03, the Tribunal has decided to agree to the pass through of an additional $0.13 per gigajoule until the expiry of the current VPPs on 30 June 2004. The Tribunal is concerned that this amount should not be locked into tariffs going forward and has agreed with AGLRE that recovery of this amount will not continue into the next regulatory period.

In relation to AGLRE's request to incorporate gas balancing costs into default tariffs, the Tribunal concluded that as the proposed gas balancing charge was not a cost but an incentive for retailers to stay in balance the amount should not be passed through to customers on default tariffs. This decision was supported by the Public Interest Advisory Centre (PIAC). The Tribunal also noted the submission from the Ministry of Energy and Utilities (MEU) that the incentive mechanism is currently under review by the Gas Market Company and therefore, may not be an issue in future regulatory reviews. EnergyAustralia (EA) noted that additional operating costs would be incurred to reduce the gas balancing charge.

[9] AGLRE's calculations are based on a cold winter occurring in one year out of every ten.

3.2 Non-gas cost increases

3.2.1 Authorisation fees and market costs

AGLRE proposed passing through to default tariffs the external costs it incurs as a supplier in the retail market. These costs are authorisation fees, calculated and levied by the Tribunal in its energy licensing role, and Gas Market Company (GMC) charges.[10]

PIAC supported the pass through of authorisation and GMC costs once they are known with certainty and provided that only the amounts applicable to AGLRE's default tariff customers are passed through in default tariffs.

Both authorisation and GMC costs have been verified by the Tribunal as costs that AGLRE has incurred in supplying gas and the Tribunal and AGLRE have agreed that AGLRE's full costs should reflect the proportion of customers supplied by AGLRE that are on default tariffs.

3.2.2 Other operating costs

The Tribunal also assessed AGLRE's request to pass through some other items of operating expenditure incurred since February 2001. AGLRE submitted that much of this expenditure relates to the introduction of full retail contestability (FRC) in the gas market.

PIAC considered that operating costs should be assessed for pass through on an individual basis. However, the Australian Consumers' Association (ACA) expressed dissatisfaction with price increases based on the implementation of FRC as it did not consider that prices should rise due to competition reforms. The ACA was also unsympathetic to mid term revisions of specific operating costs designed to correct the original arithmetic of AGLRE.

In relation to AGLRE's proposed pass through of costs associated with the industry standardisation of business to business transactions, the MEU recognised that there will be benefits flowing from standardisation. However, the MEU noted that as the governance arrangements are currently under development the consideration of costs associated with the project should be deferred until the relevant costs can be clearly identified. PIAC also supported this view.

When the VPPs were put in place in February 2001, the Tribunal and AGLRE agreed to the pass through of 'prudent' costs associated with the implementation of FRC outside the side constraints imposed by clause 3 of the VPPs. This was considered appropriate due the uncertainty in the level of costs that would be incurred.

In late 2001 and early 2002 the Tribunal undertook a review of the business-specific costs of implementing FRC for all regulated energy businesses in NSW. At the time of this review the Tribunal advised AGLRE that it considered some of the costs to be reasonable costs incurred to supply customers on default tariffs but not costs associated with the introduction of FRC. The Tribunal did not agree to pass through of these costs at that time but advised AGLRE that it would decide at the mid term review of VPPs whether to agree to the

10 The Gas Market Company was set up to develop and operate retail market arrangements relating to full retail contestability and to facilitate competition in the gas retail market.

recovery of these operating costs. In its mid term review proposal, AGLRE submitted several of these items for the Tribunal's re-consideration.

The Tribunal has assessed the additional costs submitted by AGLRE and has agreed to recovery of approximately 70 per cent of the costs submitted on the basis that they were reasonable costs incurred by AGLRE in supplying natural gas to customers on default tariffs.

3.3 Miscellaneous charges

The VPPs require AGLRE to obtain the Tribunal's approval to vary its miscellaneous charges. At the mid term review, AGLRE sought to impose four additional miscellaneous charges, three of which are external charges levied by AGL Gas Networks Limited (AGLGN).

The Tribunal assessed whether the following new charges should be introduced:

- after hours reconnection fee
- meter testing charges
- special meter read and network disconnection charges.

The Tribunal also assessed AGLRE's proposal to charge customers an administration fee to the meter testing, network disconnection and special meter read charges in addition to passing through the amount billed to AGLRE by the network operator.

PIAC's submission commented on AGLRE's miscellaneous charges on a general level stating that there should be some standardisation between electricity and gas charges. However, it noted that as there will be reviews of both electricity and gas retail charges over the next twelve months this issue may be better dealt with at this time.

PIAC identified the administration fees proposed by AGLRE as a major issue of concern. It does not consider that AGLRE has provided adequate justification for the imposition of these fees and notes that agreeing to them would 'set a very dangerous precedent' across energy and water sectors. The MEU suggested that AGLRE should provide the basis for the administration charge to the Tribunal (including its cost allocation methodology) for assessment.

The Tribunal has agreed to the introduction of the four new charges. However, the Tribunal did not agree to the inclusion of an administration fee for network charges. The Tribunal has resolved to undertake a more detailed investigation in relation to the issue as part of the next regulatory review. This will assist in promoting consistency across gas retailers and between the electricity and gas retail sectors where appropriate and will allow the Tribunal to better assess the cost reflectivity of the proposed charges.

A list of AGLRE's miscellaneous charges that will apply from 1 July 2003 is contained in Appendix 3.

3.3.1 After hours reconnection fee

AGLRE advised that the after hours reconnection fee would not replace the existing reconnection charge but would be imposed when a customer asks to be reconnected outside business hours. AGLRE advised that its reason for seeking introduction of this fee was to meet its obligations under the *Gas Supply (Natural Gas Retail Competition) Regulation 2001*.[11] This legislation requires that the supplier use its best endeavours to recommence supply on the day of a customer's request, if the request is made after 3pm on a business day and the customer pays an after hours reconnection charge to the supplier.

The Tribunal's primary concern was that customers should be made aware that they are able to be reconnected for the lesser fee of $77 if they wait until the following business day.

AGLRE and the Tribunal have agreed that information regarding both charges will be provided to customers seeking reconnection by the following means:

- the options for reconnection will be clearly outlined on a card left by AGLRE at the time of disconnection providing information to customers on how to obtain reconnection
- call centre staff will explain both options when a customer contacts AGLRE to request reconnection of supply.

3.3.2 Meter testing charges

The meter testing fee is imposed if a customer has requested a meter test and the meter is found to be accurate. In the event that the meter is found to be inaccurate the network operator, in this case AGLGN (another company wholly owned by the Australian Gas Light Company), and the retailer bear the costs. Meter testing charges were not previously reflected in the VPPs but were collected by AGLRE on behalf of the Department of Fair Trading. The service is now provided by AGLGN and retailers are to be charged.

The Tribunal considers it appropriate for AGLRE to pass through network charges on a user pays basis to regulated customers as proposed.

However, as noted above, the Tribunal has not agreed to include an administration fee in the final charge billed to customers. The Tribunal will review this issue prior to the start of the next regulatory period.

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11 Reg. 18(2)(c).

3.3.3 Special meter read and network disconnection charges

The Tribunal considers it appropriate for AGLRE to pass through network charges on a user pays basis to default customers as proposed. These charges are external to AGLRE and are regulated by the Tribunal in its role as access regulator for AGLGN's gas network.

The Tribunal has not agreed to include an administration fee in the final charge billed to customers but will review this issue prior to the start of the next regulatory period.

4 OUTCOMES AND PRICE IMPLICATIONS

The tariffs resulting from the mid term review will come into effect on 1 July 2003. The impact of the changes on customers for different levels of gas usage is discussed below. Also discussed in this chapter is information provided by AGLRE on the customer assistance plan it has developed to assist customers who are having difficulty paying their gas bills (referred to as the 'Staying Connected' policy).

4.1 Price outcomes

The majority of the cost increase will be passed through in usage charges rather than in the quarterly supply fee. However, the Tribunal has agreed to a small increase in the fixed supply fee for customers on the residential economy rate (Everytime Plus plan).

Table 4.1 Agreed tariffs for default customers using less than 1 TJ (1)
1 July 2003 – 30 June 2004

Tariff plan	Charge (2)
Everytime Easy	
Supply fee ($ per quarter)	39.91
Energy rate – all (cents per MJ)	1.488
Everytime Plus	
Supply fee ($ per quarter)	40.92
Energy rate – first 5,500 MJ per quarter (cents per MJ)	1.460
Energy rate – remainder (cents per MJ)	1.420
Everytime Value	
Supply fee ($ per quarter)	51.47
Energy rate – first 4,500 MJ per quarter (cents per MJ)	1.187
Energy rate – remainder (cents per MJ)	1.340
Industrial & Commercial (standard)	
Supply fee ($ per quarter)	52.01
Energy rate – first 150,000 MJ per quarter (cents per MJ)	1.433
Energy rate – remainder (cents per MJ)	1.168
Industrial & Commercial (Newcastle and Lower Hunter)	
Supply fee ($ per quarter)	52.01
Energy rate – first 150,000 MJ per quarter (cents per MJ)	1.433
Energy rate – remainder (cents per MJ)	1.168
Riverina Fruit and Seed Drying	
Energy rate (cents per MJ)	1.140

Notes:
(1) These tariffs apply to customers in NSW where AGLRE is the endorsed standard supplier.
(2) The charges in this table include GST.

4.2 Impact on customers

The impact of the price changes on the quarterly bills of customers are shown in the table below.

Table 4.2 Impact of the tariff changes on quarterly bills

	Current bill ($)	New bill ($)	Change ($)	Change (%)
Small residential customer (using 5 GJ per annum)	53.47	58.51	5.05	9.44
Medium residential customer (using 23 GJ per annum)	111.23	121.63	10.40	9.35
Large residential customer (using 45 GJ per annum)	179.41	195.32	15.90	8.86
Medium industrial customer (using 200 GJ per annum)	715.06	768.66	53.60	7.50

This table assumes that residential customers are on the tariff plan that results in the cheapest quarterly bill.[12] Customers can contact AGL directly (enquiries: 131 245) to find out which plan best suits their level and pattern of consumption.

4.3 Customer assistance plans

AGLRE advised the Tribunal that it has implemented a new national hardship policy developed in consultation with the AGL Customer Council called 'Staying Connected'. It is available to assist customers that are unable to pay their account either due to ongoing hardship or temporary difficulties.

The policy aims to provide support to customers by tailoring a solution to their specific needs by implementing one or more of the following alternatives:

- assisting the customer in minimising energy consumption
- negotiating an individual payment plan to reduce outstanding debt
- reviewing any extra fees or charges due
- suspending an outstanding debt for a particular period of time
- providing referral to other citizen's advice programs where appropriate.

Customers may access the hardship policy by approaching AGLRE personally or through referral by a financial counsellor.

12 That is, the Everytime Easy plan for the small residential customer and the Everytime Value plan for the medium and large customers in the table.

APPENDIX 1 VOLUNTARY PRICING PRINCIPLES

AGL Retail Energy Ltd (AGLRE) voluntarily agrees to the following pricing principles:

1. Default tariffs will be available to all tariff customers whose consumption is below 1 TJ a year until 30 June 2004.

2. A review of the VPPs arrangement will be conducted from 2002 or under special circumstances, either at the request of AGLRE or the discretion of the Tribunal, to consider matters such as:

   - additional costs as a result of any difference between the CPI exclusive of GST and the actual escalation of AGLRE's costs
   - changes in AGLRE's cost components such as the field price of natural gas or impacts of regulatory decisions on haulage rates
   - any decision on consumption profiling that deems a profile other than the market profile that has been used for cost allocation
   - changes in market circumstances that in the Tribunal's opinion warrant a review of VPPs.

3. Default tariffs should be broadly cost reflective. A transition period is required to achieve cost reflectivity during which customers should not be exposed to undesirable price shocks. AGLRE will implement tariff changes over the period 2000/01 to 2003/04 subject to the following price constraints:

   Residential tariffs
   The bill of an individual residential customer in a financial year is not to exceed the bill for the corresponding period of the preceding financial year (for the same pattern and volume of gas consumption) by more than $15 (in nominal terms) or 3 per cent in real terms, whichever is the greater.

4. AGLRE's current tariff plan over the period 2000/01 and 2003/04 is shown in Table 1. Default tariffs are set out for the first two years (ie 2000/01 and 2001/02). Price movements beyond 2001/02 are to be regarded as indicative only subject to the mid term review. CPI index for adjusting prices is defined in paragraph 11.

Table A1.1 Agreed tariff plan for tariff customers using <1 TJ (1) (excluding pass through of full retail contestability costs) (2)

Tariff	2000/01(3) *(March 2001)*	2001/02	2002/03 (Indicative only)	2003/04 (indicative only)
Residential general:				
Supply charge	\$2.50/qtr	-	\$3.75/qtr	\$3.75/qtr
Energy rate	-	CPI_1^{-GST}	-	-
Residential economy:				
Supply fee	\$2.50/qtr	-	\$2.50/qtr	CPI_3^{-GST} + 3%
Energy rate	-	CPI_1^{-GST}	CPI_2^{-GST}	1st block:CPI_3^{-GST} + 3% 2nd block:CPI_3^{-GST} – X% (4)
Residential economy plus:				
Supply fee	3%	CPI_1^{-GST}	CPI_2^{-GST} + 3%	CPI_3^{-GST} + 3%
Energy rate				
1st block	3%	CPI_1^{-GST}	CPI_2^{-GST} + 3%	CPI_3^{-GST} + 3%
2nd block	-	CPI_1^{-GST}	CPI_2^{-GST} – 1%	CPI_3^{-GST} – 1%
Business 0-1TJ:				
Supply fee	-	CPI_1^{-GST} + 3%	CPI_2^{-GST} + 3%	CPI_3^{-GST} + 3%
Energy rate	-	CPI_1^{-GST}	CPI_2^{-GST} – 1%	CPI_3^{-GST} – 1%

Note:
1. This tariff plan applies to tariffs in NSW excluding Yass. Price changes in Yass will be subject to the price constraints in paragraph (3).
2. The CPI index for adjusting prices is CPI exclusive of GST.
3. This will be in addition to the increase of 1.9 per cent on 1 July 2000.
4. The value of "X" will be determined at a mid term review.

5. Where customers have accepted a competitive offer under a contestable gas retail market, they will be able to revert to AGLRE's default tariffs without penalty once they have met their contractual obligations.

6. AGLRE will be able to pass through to customers costs associated with implementing full retail contestability (FRC) in addition to the price constraints specified in clause (3) and the tariff plan in clause (4). Costs associated with FRC include but are not limited to costs imposed by the Gas Retail Market Board (GRMCo), and other external agencies, increases in network charges and prudent costs incurred by AGLRE. The costs will be recovered in accordance with established cost allocation and recovery mechanisms or if there is no established mechanisms, the Tribunal will determine a mechanism to recover these costs including an assessment of such costs.

7. AGLRE will not vary miscellaneous fees and charges without prior approval of the Tribunal.

8. AGLRE must notify the Tribunal in writing at least one month prior to amending its default tariffs for residential, industrial or commercial customers. This notification must include the following:

   (a) an estimate (and associated methodology) for the expected impact on revenue of the proposed price changes. If the estimated revenue impact is positive, evidence must be supplied showing that either:

- costs have increased for supplying that particular tariff customer or class of customer, or
- existing prices did not cover costs associated with that particular tariff customer or class of customer.

Costs may include an allowance for an appropriate margin.

(b) a breakdown of the costs of supply into fixed costs per customer and costs which vary with the absolute magnitude of gas consumption per customer (in $ per GJ)

(c) a customer impact analysis detailing in tabular form:

- number of customers in particular consumption ranges
- current cost of gas per annum associated with consumption at the midpoint of the relevant range
- proposed cost per annum associated with consumption at the midpoint of the relevant range
- absolute and proportional change in the cost per annum associated with consumption at the midpoint of the relevant range.

(d) other supporting information required by the Tribunal.

9. Under this voluntary agreement the Tribunal will monitor price changes to determine whether they accord with the voluntary pricing principles set out in paragraph (1) to (8) above. Nothing in these voluntary pricing principles removes the Tribunal's ability to impose a gas pricing order pursuant to section 27 of the Gas Supply Act or indeed any other powers of the Tribunal.

10. AGLRE will provide information relating to the development of a competitive gas retail market, if requested by the Tribunal.

11. On 1 July 2001, tariffs may be adjusted as set out in Table A1.1. For the purpose of pricing adjustment, $\mathbf{CPI_1^{-GST}}$ means the number derived from the application of the following formula:

$$CPI_1^{-GST} = \left(\frac{CPI_{Jun2000} + CPI_{Sep2000}^{-GST} + CPI_{Dec2000}^{-GST} + CPI_{Mar2001}^{-GST}}{CPI_{Jun1999} + CPI_{Sep1999} + CPI_{Dec1999} + CPI_{Mar2000}} - 1 \right) \times 100\%$$

and

On 1 July 2002 and 1 July 2003, tariffs may be adjusted as set out in Table A1.1, subject to the mid term review. For this purpose, $\mathbf{CPI^{-GST}}$ means the number derived from the application of the following formula:

For the year 2002/03:

$$CPI_2^{-GST} = \left(\frac{CPI_{Jun2001}^{-GST} + CPI_{Sep2001}^{-GST} + CPI_{Dec2001}^{-GST} + CPI_{Mar2002}^{-GST}}{CPI_{Jun2000} + CPI_{Sep2000}^{-GST} + CPI_{Dec2000}^{-GST} + CPI_{Mar2001}^{-GST}} - 1 \right) \times 100\%$$

and for the year 2003/04:

$$CPI_3^{-GST} = \left(\frac{CPI_{Jun2002}^{-GST} + CPI_{Sep2002}^{-GST} + CPI_{Dec2002}^{-GST} + CPI_{Mar2003}^{-GST}}{CPI_{Jun2001}^{-GST} + CPI_{Sep2001}^{-GST} + CPI_{Dec2001}^{-GST} + CPI_{Mar2002}^{-GST}} - 1 \right) \times 100\%$$

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

CPI^{-GST} means the CPI exclusive of the net cumulative impact since 1 July 2000 of:

a) the GST; and

b) changes to any other Commonwealth, State or Territory taxes or charges, consequent upon the introduction of the GST

and is calculated as:

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

(B) an index published by the Tribunal that is its best estimate of CPI^{-GST}.

CPI is as defined and where the corresponding subtext (for example $_{\text{Jun2000}}$) means the CPI for the quarter end of the year indicated (in the example the June quarter for the year 2000);

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

APPENDIX 2 COST OF GAS ANALYSIS

The Tribunal considered a number of issues in coming to its conclusion regarding the appropriate field cost of gas that should be passed through in default tariffs. As noted previously, AGLRE submitted a range to the Tribunal due to the structure of its new gas supply contracts. At the lowest end of the range was the cost that AGLRE would incur in a mild winter and at the high end of the range was the cost it would incur in a cold winter.

In general, submissions took the view that the gas cost selected should not be based on the cold winter scenario but should reflect the cost of gas in an 'average' winter. EnergyAustralia (EA) considered that agreeing to a pass through of AGLRE's mild winter gas cost only would lead to significant under recovery, which could create a barrier to competition by holding tariffs below the cost of supply. EA's view was that AGLRE's cold winter gas cost would be appropriate but at the very least the Tribunal should give consideration to gas costs that would be incurred under an average winter scenario.

In order to determine an appropriate point in the range, the Tribunal:

- assessed the weather risk faced by AGLRE by estimating the likelihood that the cold winter gas cost would be incurred by AGLRE
- employed a consultant to independently estimate AGLRE's 2002/03 and 2003/04 gas costs from available industry information
- considered the relevance of Victorian spot market prices to NSW contract prices.

This appendix outlines the main points considered by the Tribunal.

Assessment of the weather risk faced by AGLRE

The Tribunal looked at the likelihood that AGLRE would incur the cold winter gas cost over the next twelve month period. It analysed information provided by AGLRE as well as seasonal forecasts from the Bureau of Meteorology (BOM).

AGLRE advised that the mild winter gas cost is based on the gas cost it would incur if demand was at 2002 levels. AGLRE provided information showing that 2002 was one of the warmest winters in the past 50 years (measured by historical annual heating degree days).[13] However, the historical information also shows an overall trend towards warmer winters.

The Tribunal noted the BOM's seasonal outlook (issued on 15 May 2003) which forecast a milder than average winter this year. The Tribunal considered this provided some direction as to where in AGLRE's gas cost range would reflect the appropriate level of weather risk. However, the Tribunal was aware that the gas cost agreed at this mid term review would be in place for part of the 2004 winter and the BOM outlooks for that far in advance are less reliable.

AGLRE felt that a second reason the mild winter gas cost was inappropriate was that the coldest day in 2002 was also comparatively warm. The information provided by AGLRE showed that in general the coldest day of the year is not well correlated with the coldness of the winter overall (in other words, a relatively warm winter can still have a few very cold

[13] Heating degree days is an industry standard based on the deviation of the day's average from 18 degrees.

days). However, AGLRE also noted that peak demand does not necessarily occur on the coldest day of the year because demand on any given day is driven by a combination of three factors:

- season (day of the year)
- day of the week
- temperature on the day (measured by heating degree days).[14]

Industry information

The Tribunal contracted Project Consultancy Services (PCS) to provide an independent and confidential estimate of the gas cost that would be incurred by AGLRE over the twelve month period from 1 July 2003. PCS calculated a gas cost based on industry information taking into account contract structure, alternative sources of gas, weather sensitivity and hedging costs, and provided a confidential report to the Tribunal.

The PCS report focused on current industry and market issues. PCS also met with AGLRE to discuss some of the commercial issues involved in contracting for secure gas supply for customers on default tariffs in NSW. The report addressed most of the issues raised in EA's submission.[15]

The independent estimate of gas costs provided by PCS confirmed that setting a gas cost in the range proposed by AGLRE would be appropriate and that for the year 2003/04, a cost in the middle of the range proposed by AGLRE would provide a reasonable estimate of the cost likely to be incurred by AGLRE over the period.

Victorian spot market prices

In December 2002, the Victorian Essential Services Commission (ESC) calculated an estimate of the cost of gas in Victoria based on prices in the Victorian wholesale spot market.[16] The ESC considered that spot market prices provide a reasonable estimate of the actual cost of gas for Victorian retailers. In its report the ESC stated that:

> The Commission remains of the view that in the absence of any alternative, it provides the most reasonable basis for deriving a benchmark of the total costs associated with gas purchasing. … the Commission considers that the wholesale spot price is likely to provide a good proxy for the cost of purchasing gas for its entire load (including the additional costs associated with extra capacity in those periods).

However, Victorian regulated companies argued that spot market prices were not a good estimate of their actual gas prices because:

- only around 8 per cent of Victorian gas is traded on the spot market
- suppliers entering into longer term contracts require a premium over the spot market price

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14 Temperature is thought to affect demand only when the day's average is less than 18 degrees.

15 EA's submission is available on the Tribunal's website (www.ipart.nsw.gov.au).

16 Essential Services Commission 'Special Investigation: TXU's proposed gas retail tariff amendments' Final Report December 2002, pp 15-20.

- there are a number of costs that are not taken into account, such as those associated with additional peak supply contracts
- spot market prices are retrospective
- recent years have been particularly warm whereas actual retailer costs must include an allowance for capacity required for extreme winters irrespective of whether they eventuate.

The Tribunal considered that there were a number of difficulties with using spot market prices in Victoria to estimate the underlying contract price of gas for a retailer in NSW and therefore did not use this information as the basis of its decision. However, the Tribunal considered that Victorian spot market prices were a relevant consideration as the market is an alternative source of gas and therefore likely to impact on the hedging costs of retailers in NSW.

APPENDIX 3 SCHEDULE OF MISCELLANEOUS CHARGES

AGLRE's current retail miscellaneous charges that will apply from 1 July 2003, including those determined at this mid term review, are set out below.

Description of fee	Fee excl. GST	Fee incl. GST
Account establishment fee	$20.00	$22.00
Account establishment fee (pensioner)	$10.00	$11.00
Collector call	$30.00	$33.00
Disconnection/reconnection	$70.00	$77.00
After hours reconnection	$100.00	$110.00
High bill field visit	$49.00	$53.90
Late payment fee	$10.00	$11.00
Dishonoured payment	$21.00	$23.10
Special meter read	$36.36	$40.00
Network disconnection fee	$90.91	$100.00
Meter testing charges:		
- 12 cubic metres	$42.00	$46.20
- 33 cubic metres	$60.00	$66.00
- 85 cubic metres	$80.00	$88.00
- 300 cubic metres	$300.00	$330.00
- 880 cubic metres	$800.00	$880.00
Security deposit	Residential - $100	Residential - $100
	Business – 2.5 times the average monthly account.	Business – 2.5 times the average monthly account.
	Refund after bills paid on time for 2 years.	Refund after bills paid on time for 2 year.

Account establishment fee: applies to 'new' customers being established onto the system for the first time.[17]

Collector call fee: applies when a contractor goes to a premise to disconnect supply but the customer decides to enter into an agreement which may include making a payment to the contractor. The contractor deposits all funds into an AGLRE account.

Disconnection/reconnection fee: applies on reconnection when a customer has been previously disconnected for debt or has asked for a seasonal disconnection & reconnection. Note that a comparison to electricity is not appropriate as a gas reconnection requires on site pressure tests and relights (as opposed to removing/replacing a fuse). A fee of $55 (inclusive of GST) applies for a disconnection only, a fee of $22 (inclusive of GST) for reconnections only, total fee of $77.

17 Note that if a customer moves to another premises that is also on gas, the fee is waived at the new residence.

After hours reconnection fee: applies on reconnection when a customer makes a request for reconnection after 3pm on a business day and requests that reconnection be carried out the same day.

High bill field visit/investigation fee: is payable when a field officer is called out to the customer's premises following a high bill enquiry. The enquiry involves at least two clerical checks, at no charge, before a field officer is sent. The officer can spend up to two hours on site examining the installation. If no fault is found on AGLRE's side of the meter there is a charge; if a fault is discovered at AGLRE's installation there is no charge.

Late payment fee: is payable when a lettergram (disconnection notice) is sent. This happens when a customer fails to contact AGLRE for a payment arrangement, and after the bill and reminder notices are sent and not paid. The fee is waived if the customer seeks assistance with financial counsellors in line with AGLRE's agreement with the AGL Customer Council.

Dishonour fee: is charged if cheque and/or card payments fail.

Special meter read fee: applies when a customer requests a meter read outside of the normal meter reading cycle. A customer might request a special meter read if the meter is inaccessible at the time of the scheduled meter read, or in order to change his/her retailer or switch to a negotiated customer supply contract (or back to default tariffs).

Network disconnection fee: is applied when the network operator is required to disconnect and/or remove a meter.

Meter testing charges: are applied when a customer requests a meter test and the meter is found to be accurate.

Security deposit / refundable advance: is paid by a tenant or business customer who has not been responsible for a supply address before, or a domestic or business customer who does not have a satisfactory credit history.[18] Advances are refunded if customers pay their account on time for 2 years.

18 Note that no GST is added to refundable advances.

APPENDIX 4 LIST OF PARTIES INVOLVED IN CONSULTATION

List of submissions received:

Organisation	Name
Australian Consumers' Association	Charles Britton
EnergyAustralia	Nick Saphin
NSW Ministry of Energy and Utilities	Brian Steffen
Public Interest Advocacy Centre	Trish Benson

List of attendees at the roundtable discussion held by the Tribunal on 14 May 2003:

Organisation	Name
AGL Retail Energy	Sean Kelly
AGL Retail Energy	Kamlesh Khelawan
AGL Retail Energy	Frier Bentley
Australian Consumers' Association	Charles Britton
EnergyAustralia	Mark Flynn
NSW Ministry of Energy and Utilities	Elsie Choy
NSW Ministry of Energy and Utilities	Anthony Poon
Origin Energy	Blair Friedrich
Public Interest Advocacy Centre	Jim Wellsmore
Public Interest Advocacy Centre	Trish Benson