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S09/724

Dr Michael Keating  
Chairman  
Independent Pricing and Regulatory Tribunal  
PO Box Q290  
QVB POST OFFICE NSW 1230

Dear Dr Keating

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 retail tariffs and charges in New South Wales for the period from 1 July 2010 to 30 June 2013. Please find further details in the attached Terms of Reference to the Tribunal.

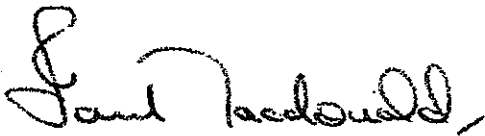
I confirm that an amendment regulation will be made shortly to extend the operation of Part 4, Division 5 of the Act to 30 June 2013, under which the Tribunal's determination may be made.

I look forward to the Tribunal's draft report and determination of regulated retail tariffs and charges in New South Wales for the period from 1 July 2010 to 30 June 2013 within six months of the Tribunal receiving the attached Terms of Reference, followed by the final report and determination within three months of releasing the draft report and determination.

As you would be aware, the Government is currently undertaking important reforms to the NSW energy industry. In order to provide potential bidders with sufficient information to effectively participate in this reform process, the Government would appreciate the Tribunal's resolution of the 2010-2013 determination as quickly as possible, whilst ensuring that stakeholder consultation processes remain intact. I understand the significant volume of work involved in producing a determination of this nature, and greatly appreciate your assistance in this matter.

If you require further information on this matter, please contact Damian Jeffree, Energy Advisor, in my office on (02) 9228 3344.

Yours sincerely



IAN MACDONALD MLC  
MINISTER FOR ENERGY

Encl

## **TERMS OF REFERENCE**

**Terms of Reference for an investigation and report by the Independent Pricing and Regulatory Tribunal on regulated retail tariffs and regulated retail charges to apply between 1 July 2010 and 30 June 2013 under Division 5 of Part 4 of the *Electricity Supply Act 1995*.**

### **1 Reference to IPART under section 43EA**

The Minister refers to IPART for investigation and report under section 43EB of the Act:

The determination of regulated retail tariffs and regulated retail charges to apply to small retail customers in each standard retail supplier's supply district in New South Wales for the period from 1 July 2010 to 30 June 2013.

#### **1.1 Background**

In accordance with its commitment to retain the offer of regulated retail tariffs at least until 2013, the Government has extended the current scheme for regulated retail tariffs and charges to apply to small retail customers supplied under a standard form contract. A regulatory amendment will be made for these purposes under section 43EJ of the *Electricity Supply Act 1995* to allow IPART to make a further determination of regulated retail tariffs and charges that will apply from 1 July 2010 to 30 June 2013.

Since January 2002, every electricity customer in NSW has had the option to negotiate a retail supply contract with any licensed retailer. Small retail customers who do not seek supply from the competitive market are deemed to receive electricity under a 'standard form' customer supply contract from their 'standard retail supplier'. Customers can also switch backwards and forwards between these alternatives. These arrangements were designed to encourage customers to test the market by providing an assurance that they can return to regulated retail tariffs. Approximately nine hundred thousand NSW customers have now moved on to negotiated tariffs.

While retail competition has delivered benefits for those participating in the market, the majority of residential and some small business customers have chosen to remain on standard form customer supply contracts which impose regulated retail tariffs and charges determined by IPART.

The NSW Government considers the reliable provision of electricity to be an essential service. It is therefore important that the financial viability of Standard Retail Suppliers is preserved, in order to ensure that they are able to continue to provide electricity to NSW customers. Network charges and energy purchase costs represent a significant proportion of the costs faced by retailers in the provision of electricity.

To promote retail competition and investment, regulated retail tariffs have been progressively moved toward fully cost-reflective levels over the course of the last three retail tariff Determinations by IPART. The 2007 Determination aimed to achieve regulated retail tariffs by 30 June 2010 that fully reflect the market-based costs of meeting each Standard Retail Supplier's obligations to their regulated customers.

This review should ensure the aims and approach of the 2007 Determination are preserved. IPART's approach should result in prices that are based on the efficient cost of supplying small retail customers, including customers who revert from negotiated tariffs.

In carrying out the review, IPART should provide advice to the Government regarding the impact of the Determination on small consumers.

## **1.2 Matters that must be taken into account**

For the purposes of section 43EB(2) of the *Electricity Supply Act 1995*, in undertaking the review from 1 July 2010 to 30 June 2013, IPART should ensure its Determination is consistent with the Government's policy aim of reducing customers' reliance on regulated prices. Regulated tariffs should reflect the efficient costs faced by a Standard Retailer Supplier meeting the forecast demand of the regulated customers they are obliged to serve.

IPART's Determination for the period from 1 July 2010 to 30 June 2013 should:

- result in prices that recover the efficient costs of supplying small retail customers; and
- apply any change to regulated tariffs on 1 July 2010 and annually thereafter on 1 July or on a date determined by IPART.

These Terms of Reference refer to three distinct cost components for Standard Retail Suppliers:

- Energy Costs;
- Retail Costs; and
- Retail Margin.

### Energy Costs

Energy costs include energy purchases from the National Electricity Market (NEM), greenhouse and renewable energy costs, NEM fees and energy losses.

For energy purchases, IPART should determine a target Energy Purchase Cost Allowance for 30 June 2013 and an Energy Purchase Cost Allowance for each year of the Determination. The Energy Purchase Cost Allowance should be set, using transparent and predictable methodology, at a level that would allow a Standard Retail Supplier to recover the efficient costs of managing the risks associated with purchasing electricity from the NEM (including the Carbon Pollution Reduction Scheme). Additionally, IPART should have regard to the efficient costs of meeting any obligations that Standard Retail Suppliers must comply with, including the costs of complying with greenhouse and energy efficiency schemes (including present and future State and Commonwealth schemes).

The Energy Purchase Cost Allowance for each year must not be lower than the least cost mix of generating plant (based on those plants earning an economic return on

their market value), including any plant that would be required to meet any regulatory obligation, (using generation technology that is available in the NEM for the relevant year/period), to efficiently meet each Standard Retail Supplier's forecast regulated load.

IPART should allow for a periodic review of the Energy Purchase Cost Allowance, including the costs of complying with greenhouse and energy efficiency schemes.

IPART should allow for energy losses as published by the Australian Energy Market Operator (AEMO).

IPART should allow for market fees and ancillary fees as imposed by AEMO under the National Electricity Rules.

### Retail Costs

Standard Retailers incur retail operating costs in supplying electricity customers, which include the costs associated with customer service (eg, operating call centres, billing and collecting revenue), finance, IT systems, and regulation (eg, licence fees).

IPART will determine an allowance for retail operating costs based on efficient costs. IPART will take into account NSW Standard Retailers' efficient costs and other available information on efficient operating costs for retailers.

IPART should also ensure regulated retail tariffs are set at a level which encourages competition in the retail electricity market by including customer acquisition costs in the retail cost allowance.

### Retail Margin

IPART will determine an appropriate retail margin giving consideration to any risks not compensated elsewhere arising from supplying regulated customers.

## **1.3 Consultation**

IPART should consult with stakeholders, conduct public hearings or workshops and consider submissions, within the timetable for the investigation and report. IPART must make its report available to the public.

## **1.4 Timing**

IPART is to investigate and provide a report of its Draft Report and Draft Determination of regulated retail tariffs and charges within six months of receiving the terms of reference and a Final Report and Determination within three months of releasing the Draft Determination. IPART is also to publish an Issues Paper and methodology paper within two months of receiving the terms of reference.

## 1.5 Definitions

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

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

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

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