INDEPENDENT PRICING AND REGULATORY TRIBUNAL

PUBLIC FORUM ON CHANGES IN REGULATED RETAIL ELECTRICITY

PRICES FROM ONE JULY 2012

TRIBUNAL MEMBERS

MR PETER BOXALL, CHAIRMAN
MR JAMES COX
MS SIBYLLE KRIEGER

Held at IPART offices, Level 8, 1 Market Street
Sydney, New South Wales
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INTRODUCTIONS

THE CHAIRMAN: Welcome everybody. I'm Peter Boxall, Chairman of IPART. On my right is Jim Cox, the Chief Executive of IPART and full-time tribunal member. On my left is Sibylle Kreiger, part-time member of the tribunal. We also have two members of the IPART Secretariat at the table: Alexus van der Weyden and Anna Brakey.

Thank you all for coming today. We're grateful for your assistance in undertaking what is a difficult and complex review.

ELECTRICITY - CONTEXT FOR 2012 ANNUAL REVIEW

For electricity, the context of the 2012 Annual Review is that IPART is responsible for legislating electricity prices for around half of the residential and small business customers in New South Wales.

These are the prices that EnergyAustralia, Integral Energy, and Country Energy - the Standard Retailers - charge customers who have not signed a voluntary market contract with either them or another retailer. The standard retailers were purchased by TRUenergy and Origin Energy last year, and we remain responsible for setting maximum regulated prices charged by these new owners.

However, the new owners are continuing to use the existing brand names, and we will continue to use these in this review.

We were requested to set regulated electricity retail tariffs and charges from 2010 until 2013. The Minister for Energy provided terms of reference for our review and determination in accordance with his powers under the Electricity Supply Act 1995.

The terms of reference specify the matters we must take into account and objectives we should aim to achieve in making the determination. They also set out some requirements related to how we should make the determination.

In March 2010, after a 9-month process that included extensive consultation and analysis, we made a determination on the amount by which each retailer could increase its average regulated price on 1 July 2010 and estimated the amount by which it could increase its price

on 1 July 2011 and 2012. The Determination stated we would conduct annual reviews in 2011 and 2012 to update the price increases for these years.

This review is updated to set the 1 July 2012 price increase using the approach set out in the 2010 Determination. We are updating the energy costs, having regard to new information on cost inputs and policy changes made by the Federal Government, particularly in relation to the introduction of a price on carbon emissions from 1 July 2012.

We issued a draft decision on 12 April, which also included analysis regarding the impact of the determination on households and small business customers, as well as recommendations on actions to mitigate future electricity price increases.

DRAFT REPORT

The draft report and determination set out significant increases in average regulated retail prices of about 16 per cent in nominal terms from 1 July 2012. These increases range from 10.3 per cent for Integral Energy customers and up to 19.2 per cent for EnergyAustralia customers.

Looking at the overall drivers of this 16 per cent price increase, the main reasons electricity prices are increasing are that forecast networks costs are increasing significantly, adding to 8 per cent to final retail prices.

In addition, the Commonwealth Government's carbon pricing mechanism contributes to the other half of the average price increase. The carbon pricing mechanism will increase wholesale electricity costs. These costs are a major component of the Standard Retailers' energy costs. Under our terms of reference, increases in network costs and the introduction of carbon price should be passed through so retailers can cover their costs.

We recognise that these price increases are significant and will place substantial financial pressures on some sections of the community, particularly those with lower income. In line with the terms of reference, we have reported to Government on the impact of the increased prices on customers and have provided advice on measures to mitigate future electricity price increases.

We note in the report that the New South Wales and Commonwealth Government have announced measures to address short-term affordability issues. For example, increases in the New South Wales Low Income Household Rebate and the Commonwealth Household's Assistance Package, respectively.

We consider it important that the factors driving electricity price increases are well understood by the community. We will continue to contribute to the policy debate to seek to ensure that the appropriate measures are put in place to improve the affordability of the electricity and maintain a viable electricity sector.

GAS - INCORPORATING THE IMPACT OF THE CARBON PRICE INTO REGULATED RETAIL GAS PRICES IN NEW SOUTH WALES FROM 1 JULY 2012

Today's forum will also discuss the retailer's proposals to increase retail gas prices to compensate for the additional cost of the carbon price.

In 2010, we agreed VTPAs with each standard gas retailer in New South Wales for the period 1 July 2010 to 30 June 2013. Standard retailers set their regulated retail gas prices in line with their VTPAs, and we monitor their compliance.

The Commonwealth Government's carbon pricing mechanism will place additional costs on standard retailers in supplying gas to retail customers from 1 July 2012. The VTPAs provide for standard retailers to increase gas prices to reflect these additional costs.

The standard retailers have proposed increases in residential retail gas prices of 6 to 9 per cent to compensate for the additional costs of the carbon price. Our role is to assess whether this increase is reasonable; and, if so, a Standard Retailer will be able to increase their retail gas prices on 1 July 2012 to recover these additional costs.

The additional costs will mean that the gas price increases from 1 July 2012 are likely to be larger than was previously indicated.

PROCEDURAL MATTERS FOR PUBLIC HEARING

Now, today's forum will cover both electricity and gas prices. It is an opportunity for stakeholders to understand this, seek clarification, and provide comment on the Draft Report and Determination for electricity, as well seek additional information from the gas Standard Retailers' on their proposals to increase retailer gas prices.

There will be a short presentation at the beginning of each session which will be made by members of the IPART Secretariat. I will then invite stakeholders at the round table to make comments. Following this, I will then invite comments from the floor. The second session on gas will commence immediately following the first session.

Today's workshop is being transcribed. Please press the talk button before you speak and state which organisations you represent and speak clearly for the benefit of the transcribers.

SESSION 1 - CHANGES TO REGULATED RETAIL ELECTRICITY PRICES FROM 1 JULY 2012

Now, let's move to Session 1 - changes to regulated retail and electricity prices from 1 July 2012. We'll now begin the session with a presentation on issues for discussion, which include the updated estimate of energy purchase cost allowances for 2012 and 13, including the impact of the carbon price, other green costs, including expanded renewable energy target, impacts on customers, and actions to improve electricity affordability.

I'd invite Alexus, IPART Secretariat.

MR VAN DER WEYDEN: Thanks, Chairman. I'm Alexus van der Weyden, IPART Secretariat.

OVERVIEW OF DRAFT DECISION - SIGNIFICANT PRICE INCREASES FOR 1 JULY 2012

As the Chairman highlighted earlier, regulated prices will increase by an average of 16 per cent across New South Wales from 1 July 2012. Network charges will add 8 per cent to retail prices and the introduction of the carbon price will add a further 9 per cent to retail prices.

In this session, we're going to examine these first three elements of this illustrative electricity supply chain. Namely, the cost to retailers of purchasing energy from generators; the impact of carbon on these costs; and the cost of the retailers complying with other Commonwealth and State green energy schemes.

Combined, these three components represent between 40 and 50 per cent of the final retail price and are the major costs elements that were updated as part of this annual review.

Other major components of retail prices are network prices. These are the prices that network businesses can charge retailers for transporting electricity across the poles and wires. Network prices have increased by over 70 per cent in real terms over the past 5 years and that will increase further from 1 July this year, being a major driver of final retail prices. These network prices are regulated by the Australian Energy Regulator and to ensure retailers' financial viability we will allow these network prices to be passed through into retail prices.

We have concerns that there are a number of factors that may be contributing to higher than necessary network prices. We've made a number of recommendations to mitigate further increases in network prices, and we will discuss these later on in the presentation.

UPDATING THE ENERGY COST ALLOWANCES

To supply their customers, electricity retailers must purchase energy from the National Electricity Market. They must also comply with a range of Federal and state green energy programs. These total energy costs are the largest cost component of the retail-cost base, and as I mentioned before, represent 40 to 50 per cent of final retail prices.

The terms of reference require us to set an energy cost allowance made up of the wholesale energy cost allowance; other green costs, including the large scale renewable energy scheme target; the small scale renewable energy scheme; energy losses, which occur when energy is transported over the network; and NEM fees and ancillary services.

In making the 2010 Determination, we estimated each retailer's total energy costs in each year of the determination period. We'd also indicated we would review this allowance in 2011 and 2012 to manage several uncertainties that could affect the level of these costs. This annual review updates our decisions on the key cost components, which are the first three points on the slide above.

Our determination also provides a mechanism for passing through costs associated with regulatory and taxation change events. As part of this price change from 1 July, we assessed the retailers' application for passing through additional costs associated with the change to the renewable energy target; in particular, the small scale renewable energy scheme.

DRAFT DECISION ON ENERGY COST ALLOWANCE AND COST PASS THROUGH APPLICATIONS

A draft decision on the total energy cost allowance for 2012-13 ranges from $98 to $104 / MWh. To this, we need to add a further $2 / MWh for additional costs associated with changes to retailers obligations under the RET for 2012, primarily the result of a significant over-supply of small scale renewable certificates reflecting the strong take-up of solar PV and solar hot water in 2011.

UPDATING THE ENERGY PURCHASE COST ALLOWANCE

In line with these terms of reference, we've determined an energy cost allowance for each Standard Retailer. We've asked Frontier Economics to calculate and recommend the efficient energy costs for each standard retailer using both an LRMC approach, which represents the cost of new generation required to meet retailers' loads, and a market-based approach which reflects the costs in purchasing energy from the National Energy Market.

We've used a consistent methodology to that used in our 2010 Determination; namely, we've estimated the LRMC on a stand-alone basis; meaning we built and priced a whole new theoretical generation system for each standard retailers' regulated load. We've also estimated the market costs using a point-in-time estimate of contract prices and have chosen the least risky combination of spot and contract cover.

We've also incorporated a price on carbon into generators' marginal cost, meaning we have taken a carbon-inclusive approach in determining the energy purchase cost allowance.

We've updated key input assumptions, including the cost of generation and energy demand in the NEM. We've continued to rely primarily on ACILs 2011 draft report for the QCA and indexed the key cost assumptions to 2012-13 and beyond. We've done this because we do not consider the input costs published by the Australian energy market operator to be suitable for pricing purposes. We then set each retailers' energy purchase cost allowance in line with Frontier Economics' advice, and using the higher of the LRMC and market-based costs in each year as required by the terms of reference.

In terms of updating the LRMC, our draft decision provides for an increase in the LRMC of around $13 MWh relative to 2011/12. There are two major changes which occurred since last year; a decline in the WACC primarily resulting from the historically low yield on Australian bonds leading to a drop on the annualised capital costs of generation. This is pushing the LRMC down, and in the absence of a carbon price, would have reduced the LRMC by $6 to $7 MWh.

However, a carbon price from 1 July significantly increases generators' marginal costs, and results in an increase costs of new generators' required to meet retailers' loads. The carbon price effect adds around $20 MWh or around 9 per cent to final retail prices. The net effect of these two factors is for an increase in the LRMC of around $13 MWh in 2012-13. In terms of updating the market-based cost, our draft decision provides for an increase of between $17 and $20 MWh relative to last year.

UPDATED ENERGY PURCHASE COST ALLOWANCE - MARKET-BASED ENERGY COSTS

Similar to our updated LRMC estimates, there's two factors that are pushing the market-based costs in

different ways: A decline in electricity demand in the NEM and is resulting in lower spot and contract prices. This is pushing the market-base costs down, and in the absence of carbon price, would have reduced these costs by $9 / MWh.

However, a carbon price from 1 July significantly increases generators' marginal cost and will flow through to higher spot and contract prices. The carbon price adds around $26 to $28 / MWh to the retailers' market-based purchase costs. The impact of carbon on the market-based costs is larger than on the LRMC estimates. This is because unlike the LRMC estimates which price a whole new theoretical generation system, the market based estimates reflect the actual mix of investment and dispatch in the NEM where there is a lower proportion of gas-fired generation plants, contributing to a higher average emissions intensity and, therefore, a higher carbon pass-through rate.

It is important to keep in mind that this $26 to $28 / MWh figure is not the impact of the carbon prices on wholesale prices. It's the impact on retailers' energy purchase costs, which reflects the relatively peaky nature of their load. The net effect of these two changes is for an increase in the market-based cost of $17 to $20 / MWh hour for 2012-13.

UPDATED ENERGY PURCHASE COST ALLOWANCE - LRMC REMAINS HIGHER THAN MARKET COSTS

Despite the impact on carbon being lower under the LRMC estimates, the LRMC remains higher than the market-based costs in 2012-13. For the next financial year, the LRMC will be between $13 and $14/ MWh higher than the marked-based costs.

In line with our terms of reference, we have set the EPCA as the higher of the LRMC and market-based cost. As a result, customers' bills in 2012-13 are around 5 to 7 per cent higher than they would be if they were set in line with the market-based estimate.

COST OF COMPLYING WITH OTHER GREEN ENERGY SCHEMES

In line with the terms of reference, we've included costs associated with retailers' obligations under a variety of

Federal and state green energy schemes, including: The large scale renewable energy target, which requires 41000 GWh of electricity to come from large scale renewable electricity generation by 2020; a small scale renewable energy scheme, which is an uncapped scheme and requires retailers to purchase renewable certificates created by households and small businesses that take up small-scale technologies like solar panels and solar hot water heaters; the New South Wales Energy Saving Scheme, which established legislated energy savings targets for retailers in NSW.

It is worth noting that the New South Wales Government has announced the GGAS Scheme will be discontinued following the introduction of the carbon price on 1 July. These allowances reflect our estimate of the costs an efficient Standard Retailer would incur in complying with these schemes over the Determination period. These allowances do not include the costs of any carbon price because as discussed, these are incorporated in the Energy Purchase Cost Allowance.

In making these decisions, we were guided by expert advice from Frontier Economics, and we've used the methodology consistent with our 2010 Determination and our 2011 annual review. As can be seen, there's little change in the cost of complying with these green schemes between 2011/12 and 2012/13.

THE IMPACT OF GREEN SCHEMES ON REGULATED ELECTRICITY RETAIL PRICES FROM 1 JULY 2012

However, the costs of complying with green schemes remain a major contributor to customer bills in 2012-13; adding around $315 to a typical regulated residential customer bill in NSW.

After the carbon price, which adds around $169, the next largest contributor to customer bills comes from the small scale renewable energy scheme which adds around $64 per year. This also includes a draft decision to pass through additional costs associated with the scheme.

It's important to point out this analysis is for a typical customer but for those customers who consume smaller or larger than average electricity usage, the impact of green schemes on their bills will either be smaller or larger in dollar terms.

As a result of our draft decision, a bill for a typical residential customer will increase between $182 to $381. Country Energy customers will experience the largest increases while Integral Energy customers will experience the smallest increases. These differences are primarily the result of differences in the increases in their underlying network prices and as a result of County Energy bills already being higher than their metropolitan neighbours.

We recognise that under our draft decision, the percentage price rise in average electricity bills is likely to outstrip the percentage rise in average household income and, therefore, many households will spend an increasing proportion of their income on electricity bills, particularly those in low income and high consumption households. Some households with these characteristics may spend up to 14 per cent of their disposable income on their energy bills.

While energy consumption has decreased modestly, we found that the proportion of income that households are spending on electricity has increased over the past several years and the 2012 price increases continue this trend.

RECOMMENDATIONS TO MITIGATE FUTURE INCREASES IN ELECTRICITY PRICES

While customers may be spending an increasing proportion of their income on electricity, it is important that retailers are able to pass on higher costs as a result of the continuing rise in network prices and green scheme costs if they are to remain financially viable.

IPART strongly supports measures that will help to limit electricity price increases and their underlying cost drivers while maintaining the viability of the electricity retail industry. For this reason, we've made a number of recommendations for consideration by both the New South Wales and the Federal Government, which aim to improve the effectiveness of the rules and the laws which govern the industry and to ensure reliability standards, carbon reduction schemes and green subsidies become more effective, efficient, and well targeted.

Ultimately, our recommendations are designed to ensure that electricity prices increase by no more than necessary. In particular, we consider that the National Electricity

Rules should be reviewed to remove the bias towards higher energy network prices. The National Electricity Law should be reviewed to prevent cherry-picking of network decisions through merit reviews. The Commonwealth and state green schemes should be reviewed to make sure they are efficient and cost effective and complimentary to the carbon price. The customer assistance measures, particularly the design and administration of emergency assistance funding should be reviewed to ensure it reaches customers most in need.

We recognise that some of these reviews are already taking place, and we will continue to be actively involved in them.

Thank you, Chairman.

THE CHAIRMAN: Thank you very much, Alexus. It's open to the round table for comments and questions. Who would like to go first?

MR MYATT: Just a couple questions. James Myatt from Australia Power and Gas. You prefer a question format here? When you're talking about the cost of complying with green schemes, what allowance was made, if any, for retailers' costs associated with changes to their operational systems? A lot of your discussion is based on the direct cost of complying, but what about changes to billing systems and other systems resulting from the carbon tax. What allowance has been made for that? What allowance has been made for solar and has an allowance been made for the requirement by the New South Wales Government for messages to be printed on all bills? The Federal Government wants a bill insert supplied. What cost allowance has been made for that?

We also say there's been a declining energy market. It's been acknowledged that demand has dropped. The retail cost recovery is based on an average consumption of 7 MWh. We saw in the paper yesterday that retail consumption has dropped so to make a retail cost recovery on a MWh basis is going to be less. What allowance is made to charge against a declining base? What allowance has been placed on the carbon? Obviously, our cost is going up $17 a MWh. What allowances were made for those? I guess these are some of the significant questions that I have.

MR VAN DER WEYDEN: Sure, sure.

THE CHAIRMAN: Thanks very much, James.

MS BRAKEY: The scope of this review is relatively narrow. We have a three-year Determination in place and specified parts of that Determination that would be updated, and specified that retail costs are not updated. They're not part of this annual review. This annual review is about the energy purchase cost allowances. There is also a mechanism to allow the updating of network costs. To the extent that there are incremental costs that accrue because of changes in legislation, there is a cost pass-through mechanism that is available to include costs. It has a materiality threshold, and no Standard Retailer has applied for a cost pass-through for the administrative or operational costs associated with the range of legislative changes. The retail prices include operating costs based on a build-up of costs for meeting the obligations that retailers face and to the extent that they have changed since we did that 2010 review, then those operational costs are not included.

MR MYATT: So retailers are expected to absorb those?

MS BRAKEY: There is a pass-through mechanism available if any additional costs are material.

MR VAN DER WEYDEN: The NSW Government has scheduled to cease GGAS and in theory that would also lower your operating costs because you don't have to comply with that scheme.

MR MYATT: I think there's also - with the wholesale cost allowance - there is a theoretical element to being able to have a viable scope of how the costs are collected. Is there any reflection at all that these are prices that are actually available to deal with? How that's managed and what's the additional risks associated with that? I mean it's a theoretical calculation on the wholesale market and the fact that a point-in-time approach has been taken when there's a three-year price cost-base so a prudent retailer would hedge it's cost well beyond the current one year frame work, which changes that cost structure one year out or your overall hedging in a very short period of time. They're important to do because you already have a cost structure that's been hedged, and I don't think - I don't know how any allowance can be made of the overall costs to retailers to buy wholesale energy.

MR VAN DER WEYDEN: Just to the first point: We do compare our modelled market results to publicly available market prices such as d-cypha data, and it's proved to be very similar each time. I don't know if Frontier wants to make further comments on that?

ANDREW HARPHAM: Thanks, Alexus. If you have a look at our report - Andrew Harpham from Frontier Economics - if you have a look at our draft report, you can see the market modelling, which can be directly compared to the transparent market results. We have in this report - and in every other of our reports to IPART - compared our estimates of spot prices or contract prices with d-Cyhpa prices and compared it also to REC prices, so we are very aware of the fact ...

MR MYATT: So you're building a retail portfolio. How much allowance have you made on contracts being made over time?

MS BRAKEY: That is an IPART decision, and we have decided to use a point-in-time estimate, so we value it …

MR MYATT: So retailers hedge an entire 100 per cent to a point-in-time.

MS BRAKEY: We're not saying you hedge all of your load at that point in time. However, we value the portfolio at a point in time. We don't value the portfolio at what you bought it at but at the current market price - similar to the way shares are valued.

MR MYATT: But you're valuing it and you say what value to cover and you're trying to cost an unrealistic economic outcome.

MS BRAKEY: But we will still value at a point-in-time, not at the purchase price. We take a point-in-time estimate of that value.

MR MYATT: Which I think is fundamentally flawed.

THE CHAIRMAN: Thanks very much, James. Other questions or comments around the table?

MS HODGE: Thank you. I'm Carolyn Hodge. I'm the senior policy officer with the Energy and Water Consumers' Advocacy Program at the Public Interest Advocacy Centre.

First of all, I'd like to thank IPART for the analysis contained in the report, especially regarding the impact of these price rises will have on residential consumers. It helps our advocacy to have some dollar figure and percentage, and I know that in country areas we've got a significant increase in percentage of people who will spend over 10 per cent of their disposable income on electricity, and that's an acceptable definition of energy poverty, so I think we really need to look at some short-term - short-term measures as to help these people cope with these increases.

The report notes the need for reform of the Energy Accounts Payment Assistance scheme in terms of design and administration. For people in the room, the EAPA scheme provides payment vouchers to help them pay their electricity bills.

Given the last two annual reviews have seen significant increases in electricity prices, does IPART consider the need to increase the funding - not to administer - but look at the way it's funded?

MR VAN DER WEYDEN: What we've said in the report is that we think there's a need for a comprehensive review of all customer assistance measures - EAPA is just one. We support a review of all assistance measures.

MS HODGE: I have to say, I don't disagree with that recommendation, but I guess what I'm looking at is that a review is more long-term - we have the review and recommendations come out of the review, and then the Government decides to accept it or not; and people will be faced with these price rises on the first of July this year.

They were also faced with similarly large price rises on the first of July last year, and that budget did not increase, and I know that's not within the recommendation of IPARTs decision-making process. So what am I interested in? Seeing perhaps a little bit more fleshing out of some short-term recommendations that could help people immediately on the first of July, and, obviously, we want to see some evidence-based policy coming through so the review is definitely needed.

And PIAC will definitely support that review, but we think that the discussion of the way the rules should change or reliability standard impacts are warranted but these are long-term measures and the flow-through to customers' bills will not result in a short period, and people who are vulnerable don't have the capacity to absorb these increases.

Thank you.

THE CHAIRMAN: Thank you very much, Carolyn. Other questions and comments?

MR PHILLIPS: Alistair Phillips from TRUenergy. I had a question in relation to AEMO input costs. I suppose the comment was AEMO costs were not suitable. Can you just expand where you don't think they are suitable?

MR VAN DER WEYDEN: I think they're suitable for AEMO's planning needs. The five scenarios that they use basically are to test the transmission network in a variety of ways; none of those scenarios reflect the most likely estimate of input costs. That's what we've said. And it's consistent with what we said in last year's annual review. We prefer to update input costs for our review in a consistent manner using costs that are considered to be a most likely estimate rather than selecting from five different 'what if' scenarios for which there is no base case.

THE CHAIRMAN: Thank you, Alistair. Anybody else? Patrick?

MR WHISH-WILSON: Thanks. Patrick Whish-Wilson from Origin Energy. Origin Energy is broadly happy with the draft report, and we appreciate IPARTs proposal, and most importantly, it allowed for the necessary pass-through of the carbon costs and the network charges and the green scheme costs.

I reiterate as IPART has identified under the draft report, the controllable costs that a retailer can actually change are actually decreasing. The increases are carbon and network driven. We have some minor issues with some of the calculations, but we'll be addressing those in our submission.

THE CHAIRMAN: Thank you very much, Patrick.

MR RUDDY: Shaun Ruddy from Alinta Energy. I thank you for the opportunity to come and have a discussion on a critical issue. From an analytical view of the retailers' price Determination - and we're not in the New South Wales market as yet - we're looking at the outcome of these determinations to buy into your decision-making in terms of when and how we enter the energy market. I would support the comments that Jim's made.

I think there is a concern that when we're looking at pricing Determination, we're only looking at certain elements in the current market, particularly not looking at a lot of the retail administration costs that go with it. Something that needs to be taken into consideration, to look at some of the relative costs, not the total relative cost, but we will put those out in a written submission.

Thank you.

THE CHAIRMAN: Thank you very much. Andrew Dudgeon?

MR DUDGEON: Andrew Dudgeon from AGL. As a second tier retailer offering market contracts at a discount to the regulated price, we're extremely interested in making sure that the way IPART is setting the regulated price provides a consistent basis for long-term sustainable retail competition in the market.

I think what Patrick touched on, I suppose, is a new concern in terms of components of energy purchase costs. Specifically the WACC in terms of generation has reduced from7.8 to 6.5 per cent. We can see that IPART has updated the risk free rate and debt margin, but in terms of what that implies through the average cost of capital, there's an implied drop in the market return to the cost of equity, and we haven't seen any evidence of that in the report and probably nothing more broadly that they can point to.

I think, secondly, in terms of the short-run marginal cost of new entrant coal generation in the modelling, this is lower than the existing short run marginal cost of generation. We'd say this is slightly below what we'd see as a reasonable mark, and we highlight that to IPART.

THE CHAIRMAN: Thank you very much, Andrew. Just to make a point to reiterate what Anna said with respect to points raised by James and also, essentially, seconded by Shaun, those sorts of retail costs were taken into account in the three-year review in 2010. This is the third year of the three-year review, so as Anna pointed out, we don't have an opportunity to review these retail costs again, but they were taken into account in 2010.

Andrew Lewis from the department of--

MR LEWIS: Department of Resources and Energy. No questions.

THE CHAIRMAN: Thank you. Any final comments before I turn it over to the floor? Carolyn?

MS HODGE: Thank you. I'd just like to ask a question on whether IPART has received an updated term of reference from the Government to undertake a review following this period?

THE CHAIRMAN: No. Okay. Thank you very much. Questions from the floor. Please identify yourself, name and organisation which you represent. We have any questions or comments? No, we don't. We need to maybe have people come up to the table here. I'm having a little bit of trouble seeing. That's okay. Anybody have any questions from the floor? Comments? No? Well, thank you very much - yes, we do. Thank you.

JOHN SKINNER: My name is John Skinner from the Energy Regulator. It's more of an advertisement than a comment. We're shortly commencing a process of setting network tariffs from 2014. There's a public forum in two-and-a-half weeks to commence that process which starts very soon, in June, actually; so if you'd like a form with some information, come see me after the presentation today.

THE CHAIRMAN: Thank you very much, John. Well, in that case - sorry, one more.

RUTH ROBINSON: Hi, Ruth Robinson, the executive officer of the Physical Disability Council of New South Wales. Thank you for the opportunity of being here today. I was very, very interested in some of the recommendations that related to the design and administration for emergency assistance

funding. I think that's a really cool initiative.

However, I'd like to actually support the comments by the representative who's sitting on the other side of the room there about the need to actually look at a very speedy initiative to provide people with an opportunity to address the difficulties that they have been experiencing in the case of the people that we represent around the state for at least 12 to 18 months, that I know of, where lots of people are unable to pay their electricity bills at all who are doing amazing things to be able to scrape the money to do it, so I think looking at some funding or rebates that are speedy that provide opportunities to people in the short-term to address their needs will be really helpful.

Thank you.

THE CHAIRMAN: Thank you very much, Ruth. Any more questions from the floor? No? Thank you very much for all your questions and comments.

SESSION 2 - INCORPORATING THE IMPACT OF THE CARBON PRICE INTO REGULATED RETAIL GAS PRICES IN NEW SOUTH WALES FROM 1 JULY 2012

We can now move into Session 2, which is incorporating the impact of the carbon price of regular active retail gas prices in New South Wales from 1 July 2012.

The Standard Retailers have proposed increases in the residential retail gas prices of 6 to 9 per cent to compensate for the additional costs of the carbon price. Our role is to access whether this increase is reasonable, and, if so, Standard Retailers will be able to increase the retail gas prices on 1 July 2012 to recover these additional costs.

We will begin with an introduction from the IPART Secretariat and will then invite AGL, Origin Energy, and ActewAGL to each present their proposed increases in regulated gas prices from 1 July. And afterward, we'll have some questions from the round table and the floor. Thank you very much.

MR VAN DER WEYDEN: The carbon price will place additional costs on standard retailers in supplying gas to retail customers from 1 July this year. The VTPAs that we have for each of the Standard Retailers in New South Wales provides for retailers to increase retail gas prices to reflect the additional costs that are incurred under the carbon price.

The Standard Retailers proposed increases in residential retail gas prices of 6 to 9 per cent in gas prices, and our role is to assess whether this increase is reasonable. These additional costs will mean that the gas price increases are likely to be larger than was previously indicated on 1 July this year.

IMPACT OF CARBON ON RETAIL GAS PRICES - RETAILERS'PROPOSALS

In this session, AGL and Origin Energy will be outlining their proposals, including a carbon price on the cost of supplying gas to customers and what the impact of these proposals on customers will be. Before we do that, it's worth mentioning that the proposed price increases discussed today do not include the impact of changes in gas network prices.

Under the VTPAs changes in network gas prices are passed through into retail prices. Our understanding is that there are likely to be significant increases in network prices in the Jemena network supply area. Meaning AGL customers are likely to experience additional prices from 1 July this year. So, Chairman, if I may, I might hand it over to AGL for their presentation.

THE CHAIRMAN: Thank you, Alexus. We have Mr Dudgeon.

MR DUDGEON: Thanks, Alexus. My name is Andrew Dudgeon and I'm with AGL.

I'd like to thank IPART for the opportunity to present today. The presentation will run through the AGL application for a change in the 2012-13 New South Wales default gas prices to reflect the impact of the carbon price from 1 July 2012.

AGL PROPOSED CARBON COMPONENT - OVERVIEW

As IPART described in their opening remarks, in 2010, AGL as a Standard Retailer entered in a Voluntary Transitional Price Arrangement or VTPA with IPART. The VTPA sets out the process for determining default gas prices from 2010 to 2013.

Under the VTPA, default prices are based on an allowance for a retail component and a network component. The retail component includes wholesale gas costs, retail operating costs, and a margin allowance. The network component is simply a pass-through of the network charges incurred by AGL.

The process for the year-on-year change in these components is set out in the VTPA. Also mentioned by IPART the VTPA anticipated that during the price path, a carbon price or similar government policy might be introduced. Under clause 4.10 of the VTPA, it sets out the conditions for the inclusion of a carbon component related to the introduction of a carbon price or other greenhouse gas reduction schemes.

AGL has provided IPART with an application to apply a carbon component from 1 July 2012. AGL has calculated the carbon component by considering four separate elements.

Firstly, upstream emissions. This represents the cost impact of the carbon price on wholesale gas production and transmission, excluding any impact on distribution charges.

Secondly, downstream emissions. This reflects the carbon permit liability that retailers will be required to surrender on behalf of customers for the emissions resulting from the combustion of the natural gas.

Thirdly, the introduction of the carbon price will result in increased operating costs for AGL. AGL has estimated these costs for default gas customers and proposed an allowance in the carbon component.

Finally, the current allowance for the retail margin in the default gas price is based on a percentage range applied to retailers' revenue. To reflect the increase in wholesale gas and operating costs, AGL has included a retail margin adjustment to maintain the overall percentage margin within the current range.

AGL notes that the application being presented today does not include any changes to the other components of the default price. Any changes in these components for 2012 and 2013 will be dealt with separately under the VTPA.

GAS SUPPLY CHAIN - CARBON EMISSION SOURCES

In order to better understand the elements of the proposed carbon component, it is worthwhile considering the nature of the carbon emissions along the gas supply chain and how they are estimated for an end user.

Broadly, carbon emissions for an end user of natural gas are split into two categories: Scope 1 or downstream emissions, which result from the combustion of natural gas; and scope 3, or upstream emissions, which include all other relevant emissions that occur prior to the end user.

The main sources of scope 3 emissions are the combustion of gas and any leakage of gas that occurs during the production stage. Emissions also occur during the transmission and distribution stages; again, due to combustion and any leakage of gas that occurs.

Under the Clean Energy Act, if the facilities in these upstream stages meet a specified threshold, they will be liable for these emissions and, therefore, they will incur a cost associated with acquiring and surrendering the equivalent amount of permits.

The final stage of the supply chain is the end user themselves. Under the Clean Energy Act, the retailer is liable for these emission for small users. End users can calculate the emissions associated with their gas use. The Commonwealth Department of Climate Change and Energy Efficiency undertakes detailed modelling to calculate the amount of emissions generated per unit of gas consumed for each state of Australia. This is known as the emissions factor; and for gas, factors are published separately for upstream and downstream emissions on a tonne of carbon dioxide per GJ of gas basis.

The upstream factors are published annually for each state in a document called the National Greenhouse Accounts Factors or NGA factors. AGL notes that the NGA scope 3 emission exclude any emissions from distribution networks. This is done on the basis that if emissions from operating a distribution network do not vary significantly based on gas, then when comparing the relative greenhouse impact of using one fuel instead of another, these emissions should

be excluded.

The Department of Climate Change and Energy Efficiency also published a downstream emission factor for the combustion of natural gas. The emissions associated with the combustion represent approximately 80 per cent of emissions that occur through the supply chain.

Thank you.

EASTERN AUSTRALIAN GAS MARKET AND 2010-13 VTPA

In order to understand the impact of the carbon price through the supply chain, it is necessary to combine an understanding of carbon emissions from the previous slide, with the physical New South Wales gas supply chain and the nature of the relationship between suppliers, pipeline operators, and retailers.

A retailer such as AGL will see to manage its supply risk by acquiring gas from a number of sources. Historically, the mechanism for sourcing gas has been through long-term agreements which have been used to underwrite investment infrastructure along the supply chain. The main source of natural gas for New South Wales and hence for AGL are: The Cooper Basin, which provides a number of gas fields owned by Cooper Basin Joint Venture and are operated by Santos; the Gippsland Basin which is owned by a joint venture between ESSO Australia and BHP.

The gas from these suppliers is delivered along two main pipelines shown on the map: Moomba to Sydney pipeline and Eastern gas pipeline. As the main incumbent, AGL entered into long-dated agreements for the supply and transmission of gas to our customers in New South Wales with some agreements lasting between 15 and 20 years.

In reviewing these agreements in light of the introduction of a carbon price, AGL has confirmed that these circumstances, the notification of a price change event and its impact on prices should be provided by the supplier. To date, AGL has not received a notification of the price increase associated with our key supply agreements. However, AGL anticipates that notification will be provided by our suppliers prior to 1 July.

In the absence of formal notifications, AGLs requirement to advise IPART of the calculation of the carbon component by the First of May 2012, AGL has developed a methodology for estimating the impact of the carbon price on the wholesale cost of natural gas.

UPSTREAM CARBON EMISSIONS

So without facility-level emissions data, AGL has reviewed what data is available on the emissions intensity of the gas supply chain. In short, there is no recognised publicly available source of facility level-emissions data that AGL could use to estimate the emissions intensity of individual suppliers.

While the National Greenhouse and Energy Reporting Act places reporting requirements on these facilities, the data reported to the Department of Climate Change and Energy Efficiency is not published at a facility level, only a corporate level. On this basis, AGL have proposed using the upstream emission factor for New South Wales from the most recent publication of the NGA factors because this provides the most transparent basis for estimating the uplift due to the carbon price.

AGL notes that there is a precedent for using the NGA factors to estimate the uplift in wholesale gas costs. These emission factors are used by the Commonwealth Government to estimate the uplift in wholesale gas costs for companies applying for assistance under the jobs and competitiveness program previously known as the Emissions Intensive Trade Exposed Assistance Program.

In the NGA factors from July 2001 the scope 3 emission factors for New South Wales are published on a metro and non-metro basis. Because the gas price is applied on a state-wide basis, AGL has proposed that a single emission factor be used for our customers in New South Wales, based on a weighted average of the metro and non-metro factors. The weighted average is calculated using a forecast of the split between the coastal and non-coastal regions of the distribution network load.

This results in a load weighted average NGA factor of 14.6 kg of CO2 per GJ based on a $23 carbon price in 2012-13. This equates to a cost of 34 cents per GJ.

DOWNSTREAM COMBUSTION CARBON EMISSIONS

The second part of the carbon component represents the cost of the emissions associated with the combustion of natural gas by the end user. Under the Clean Energy Act, a retailer of natural gas is liable for the potential greenhouse gas emissions embodied in the natural gas for supply to small users.

The amount of greenhouse gas emissions that result from the combustion of natural gas is defined under the National Greenhouse and Energy Reporting Measurement Determination. Taking into consideration the emission of carbon dioxide, methane and nitrous oxide from the gas combustion, the emission factor is 51.33 kg of CO2 per GJ; multiplying this emission factor by a $23 carbon price in 2012 results in a cost of $1.18 per GJ.

Thirdly, AGL has included an allowance in the carbon component to reflect the increase in operating costs associated with the introduction of a carbon price.

RETAIL COST ALLOWANCE ADJUSTMENT

As part of our 2012-13 budgeting processes, AGL has developed forecasts of the operational cost of complying with the legislation for our gas customers, and on this basis, AGL has proposed to IPART that an additional 13 cents per GJ be included to allow for costs such as IT system changes specifically related to carbon.

Additionally, staff is required to manage the permit liability and other compliance elements of the scheme; and for 2012-13, AGL has reviewed the impact of the introduction of a carbon price on current bad and doubtful debt levels. As a result, AGL has forecast an increase in our debt provisions and additional credit management and collection activities.

To come up with the proposed cost allowance, AGL has taken these carbon-related costs and apportioned the relevant cost to our customer segments. AGL anticipate that further details of the carbon-related operating costs will be provided to IPART as part of the review process.

The final element of the carbon component is an adjustment to maintain the current level of retail margin in the default price. The uplift in retailers costs due to carbon price means that unless a specific allowance is made to adjust the retail margin, then the percentage margin would reduce as a total of AGLs revenue.

AGL has proposed an amount of 13 cents per GJ in order to maintain the current margin within the recommended reasonable range of 7.3 per cent to 8.3 per cent that was used in IPARTs final report for regulated gas prices in June 2010.

In summary, AGL has proposed a carbon component under the VTPA of $1.78 per GJ to apply to default prices from 1 July 2012. AGL notes that this carbon component excludes any change to the retail or network components of the VTPA as mentioned previously.

CARBON COMPONENT - ANNUAL BILL IMPACT

Finally, as part of our application, AGL has summarised the likely impact on customers’ bills from the introduction of the proposed carbon component. If the proposed carbon component is approved by IPART, it will be included in the usage charge for customers.

No amendment is proposed to the fixed supply charge part of the bill. Factoring in this increase in the usage rate for a typical household customer that uses 23 GJ per year of gas, the proposed amount would result in an increase of 6.3 per cent in their overall gas bill or around $45 per year, including GST.

The increase as a percentage of customers' bills changes depending on the customers' level of usage. This is because the proposed flat increase in the usage rate would be applied to tariffs that have a declining block structure.

Thank you for your time this morning.

THE CHAIRMAN: Thank you very much, Andrew. Next, we have Patrick from Origin.

MR WHISH-WILSON: Patrick Whish-Wilson from Origin. I'm a regulatory pricing manager for Origin. This will be very quick because I think we've covered most of the components that was passed through. As you know, the carbon scheme

starts from 1 July, and Origin's a Standard Retailer - has been a Standard Retailer for Murray Valley and Albury. We also act as country Energy in Wagga Wagga and Gundagai as well, so we made application for the carbon components.

As Andrew specified, there's four major areas with carbon that will have an impact. One is related to the customer consumption. The second one is third party gas suppliers and getting the physical gas to the customer; and the thirdly, the additional costs of actually administering the scheme because it's quite complex; and fourth is the network costs that we are averaging from the distribution network that we haven't seen as yet.

Please note that for Origin's application, we didn't include distribution costs. We also don't include number 3 costs associated with the retail cost of administering the scheme. We agree with AGL that there are costs for the scheme and are significant; but at this point in time, we are not in a position to rigorously provide them to IPART, so we have not included them.

So if we go to the first two elements of the cost. The first one is direct emissions which is the factor that Andrew went into detail on, so I'm not going to talk in detail about that. Of course, it is a direct emission of cost.

The second is indirect emission. This is where we differ from AGL. This refers to the costs - the emission costs from the gas suppliers and the transition pipeline. Origin was in a position to have many of the gas fields that we utilised and we've done this throughout our whole part - across Australia, so we will vary in that regard.

And the final figure at the bottom as with AGL will be uplifted by retail margins to ensure that it applies as to the previous VTPA. Here's a summary of our costs: The direct cost using the NGA factor is $1.18. It is the indirect costs of scope 3 areas, that will vary. See, we've got it split it up between wellhead and transmission costs. We actually work through the wellhead cost, which is basically the emission intensity for each gas field used to supply Wagga Wagga, and then use the actual length of the transmission pipelines used to transport it to them. At the end of the day, they're small costs, but that's why the costs are so specific and you get a variation from Wagga Wagga and Albury/the Murray Valley.

So here is the customer impact on the major two regions: There's been other regions in the country that are small, but they vary depending on customers using up to $1.55. For Murray Valley customers, it's a $75 dollar cost. Wagga Wagga, which you can check the percentage, as you see, are also significant, 7.1 per cent. The costs are higher because at Albury cost rises were much lower than in New South Wales. We haven't included impacts on business components which is dependent on the use of the customer. We're talking 7 to 9 per cent, depending on the usage or their actual position, but I haven't got any more detail. Our application is with IPART, if you wish to look at it. I thought that would be enough today.

THE CHAIRMAN: Thank you very much, Patrick. I'm advised that ActewAGL couldn't be here. We got a rather short notice on that. What I'd like to do now is throw it up to questions. Firstly, the round table? Any questions or comments and then to the floor. Questions? Comments around the table ? Jim?

MR COX: Just ask this for my own benefit. It seems to me that the dollar impacts are higher for Origin than AGL. I'd like to understand the impact relating to that?

MR WHISH-WILSON: Sorry, the actual dollar is lower. It's a total impact mainly based on consumption, so our Origin customers use 14 GJ compared to--

MR COX: I think you showed us where it says the increase is 9 per cent. There's a lower figure for AGL, 6 or something. I'm trying to understand what's behind the increase, different methodology or circumstance?

MR WHISH-WILSON: Circumstance. Once again, the Albury and Murray Valley will show it's 9 per cent because their dollar - their gas price is much lower than for New South Wales; so it's a bigger per cent and a lower impact.

THE CHAIRMAN: Thanks, Jim. Other comments or comments around table? Alexus?

MR VAN DER WEYDEN: Thanks. There's been a bit of discussion on network prices. Does Peter want to comment on the increases from 1 July, including what is likely to

be effected as a result of carbon on their distribution costs?

MR HARCUS: Peter - Jemena, Peter Harcus. Prices are regulated and the access arrangements were approved last year. We have submitted our prices to the AER and they are subject to approval. We're not sure of We're in the process of seeking approval and have not received any feedback yet on that.
Yes, the prices we submitted to the AER include the impact on carbon. It's cost reflective and varies very much in accordance with the NGER calculation methodology, so there's - there's a flow-through of carbon costs, and an increase to the volumetric charge.

MR VAN DER WEYDEN: Can I just ask one for you? Have you got a figure, rough figure, of the likely price increase for 1 July?

MR HARCUS: Well, it's an average figure and includes inflation. The price was set for the last three years, the first two years used the original decision. There's an x-factor that was approved for that part of 8.6 per cent so with CPI 3 per cent, so there's an average if 11.7 per cent in that pricing.

MR VAN DER WEYDEN: Plus carbon?
MR HARCUS: Yes, but its minimal.

THE CHAIRMAN: Thank you. Carolyn?

MS HODGE: Perhaps this is a question for the retailers here who are dual fuel retailers like AGL and Origin. Given that they're looking at carbon prices for the First of July for electricity and for gas, I was wondering if you could tell me - if you could foresee an increase in calls to come through as the price flows to customers' bills?

MR DUDGEON: I'd say I think our teams are adequately resourced, but what we're doing at the moment in terms of being able to brief customer service representatives, particularly customer service teams to be able to explain to people the nature of the impact related to the carbon prices and what that will do in terms of impacts on their bills and fuel prices and deal broadly in what we can do in terms of energy efficiency or, I suppose, bill payments or anything like that; what we can try and do as a result of the impact on that.

MR WHISH-WILSON: I just agree with Andrew's comments. The team of people working on this carbon implementation is enormous. It's implementing what you would call a super hybrid program that is focused 1 July.

MS HODGE: Do you feel, though, that their call centres are well equipped in instruction of additional costs? Not just about carbon, per se, but price rise flow? Regulated retail prices will reflect the mark of this as well as related retail prices. I'm guessing that people are struggling now; after 1 July will be struggling even more so in looking for help, and I just want to understand whether the call centre will be well equipped to take those calls reasonably quickly. The community organisations will be able to get through to negotiate? We have a hardship team that deals with payments and people will have access to a program to identify themselves or identified by your staff as being in a hardship?

MR PHILLIPS: We - in terms of what Patrick mentioned - in terms of the amount of resources and the teams that are looking into the noncompliance of this and that type, it's focused through our retail business; and communication and customer impact; that is something that is definitely facilitated through managers. We're also in a situation of seeing - helping our customers deal with the impacts of the carbon price, along with other things, but I suppose it's really as we said in a number of ways: It's not just at the call centres. It's also about the message of the bill which both with the New South Wales Government introduced so you'll see some customers going through to the IPART tool to get their information as well as you got the Commonwealth Government as well. They set up a call centre as well to look at - I suppose get information about the introduction of the carbon price, so I think, yes, there's been pressure on the call centres, but also things which are also being done by Government to help customers deal with the new policy.

THE CHAIRMAN: Thanks, Alistair. Any other questions around the table for the retailers, for AGL and Origin or IPART? Comments? No? Thank you very much. Questions or comments? We have one out at the back.

MALE SPEAKER: Good morning. I'm name is (indistinct) from the Carbon Management Consulting Firm. This question is addressed primarily to retailers, but, obviously, IPART

Secretariat may also answer it. I'm asking this question from the understanding that the construction of the carbon price is meant to facilitate a shift towards more renewable energy and technologies so - and I also understand from presentation by the retailers that the impact of the carbon price is meant to be passed through completely to the end users. How will it affect a customer, say, who has a 100 per cent green power, green gas contract and is currently paying a premium over the prices that have been put in the gas contract? Assuming I'm on a 100 per cent green gas contract, I'm already paying to offset carbon emission through the 100 per cent green gas contract; given that the carbon price is being passed and the green power contracts involve a premium or whether these basic would - how would it effect these groups of customers as well?

Thank you.

MR WHISH-WILSON: No, it's a good question. I know as I was talking originally in having a huge team. With people, that's one of the questions. An example you gave when you're a 100 per cent wind customer. That - I know they're looking at the idea of how do we exclude carbon customers bills because they're already paying the green. But that's one of the questions. Some customers are paying ten per cent so how do we offset that. All I can guarantee is that it's being looked at and to make sure that people aren't being doubled up for a contribution to the green.

THE CHAIRMAN: Andrew Dudgeon?

MR DUDGEON: I probably wouldn't have any more to say than what Pat's contributed. As he said, we have a lot of people working on the VTPA, but we don't have any green gas products that would otherwise be impacted by it.

THE CHAIRMAN: Thank you. Any other questions, comments from the floor? No? All right. Any final comments around the table? No? That just leaves me to wrap it up and thank you all very much around table and the floor for their contribution.

Just to remind you that submissions to the draft reports are due on the 10th of May 2012. All submissions, comments, and questions should be made directly to IPART. Anyone with questions regarding how to make a submission should contact IPART Secretariat.

The next stage of this review is the release of our Final Report and Determination in mid-June. This is necessary to ensure that new prices can come into effect by 1 July 2012. So we do ask stakeholders to ensure that your submissions are received by the due date, given you're tight timeframe for the completion of the review. Also we cannot guarantee any submissions received after May 10 will be considered.

Transcription of today's proceedings will be available on IPARTs website in a few days.

Finally, just once again, thank you very much for attending.

THE TRIBUNAL ADJOURNED ACCORDINGLY