

Mr Paul Baxter
Senior Commissioner
The Independent Competition and Regulatory Commission
GPO Box 296
CANBERRA ACT 2601

12 May 2009

via email: icrc@act.gov.au

Dear Mr Baxter,

Draft Decision Retail Prices for Non-contestable Electricity Customers, April 2009

AGL Energy Limited (**AGL**) welcomes the opportunity to provide comments on the 'Draft Decision Retail Prices for Non-contestable Electricity Customers, 2009-2010' (**Draft decision**) by the Independent Competition and Regulatory Commission (**the Commission**).

Summary

In its submission in response to the Issues paper¹ AGL expressed general support for the approach proposed by the Commission. AGL notes that the Commission has not proceeded on the basis suggested in the Issues Paper. Rather, the Commission has adopted a significantly different methodology in determine the draft regulated energy purchase cost. AGL has some concerns with the methodology now being suggested by the Commission, which are detailed further below.

AGL further notes that the Draft Decision does not account for the costs incurred by retailers in acquiring and retaining customers. As has been consistently noted by AGL in previous review processes, in failing to recognise this cost, which is incurred by all efficient retailers operating in the market, the Commission risks understating retail operating costs.

AGL is concerned that both of these issues have the potential to lead to an underestimate of the costs incurred by a new entrant retailer operating in the ACT. As the Commission is aware, understating the regulated costs can lead to diminished levels of competition.

Energy Purchase Costs

AGL is surprised to note that the Commission has significantly changed its approach to the determination of the regulated Wholesale Electricity Cost (**WEC**).

The Commission indicated in its Issues Paper that it would assess the WEC with reference to an assumption that a prudent retailer would layer in its hedging requirements over a 24 month period. Such an approach has precedent, and AGL is largely supportive of such an

¹ *Issues paper on Retail Prices for Non-contestable Electricity Customers 2009-2010*, February 2009

- > Being selected as a member of the Dow Jones Sustainability Index 2006/07
- > Gaining accreditation under the National GreenPower Accreditation Program for AGL Green Energy®, AGL Green Living® and AGL Green Spirit
- > Being selected as a constituent of the FTSE4Good Index Series



approach. The Commission now appears to be suggesting that the following hedging strategy can be assumed in determining a regulated WEC:

- Flat swaps purchased in even increments over a 24 month period;
- Peak swaps and cap contracts purchased in uneven increments over a 12 month period, with approximately 80% of the hedging requirements acquired in the month of June 2008

AGL has significant concerns with such an approach, as it does not appear to have any correlation with methodologies adopted in other jurisdictions, nor does it conform with AGL's expectations as to a 'prudent retailer' hedging strategy. AGL would welcome an opportunity to discuss this with the Commission further, both to seek a greater understanding of the rationale underpinning this proposed approach, and to suggest ways in which the approach suggested in the Issues Paper could be applied.

Allowance for Efficient Retail Cost

AGL maintains its view that an allowance for operating costs should be set at a level that includes all costs in attaining, retaining and servicing customers. Most importantly, they should be set in such a manner so as to allow and encourage a greater number of retailers to compete in the ACT market. It is common practice for new entrant retailers to use the regulated tariff by way of a benchmark tariff and apply a discount against this benchmark when competing for customers.

The Commission itself has identified that it plays a crucial role in setting the price for both negotiated and non-negotiated contracts². By excluding acquisition costs from the total Transitional Franchise Tariff (**TFT**), the Commission is in effect setting a TFT that risks discouraging new entrant retailers entering the ACT market.

AGL also notes that it is also important to ensure cost parity with other jurisdictions for similar services/products where applicable.

Pass through mechanism

AGL advocates the inclusion of a general pass through provision to allow the recovery of efficient and prudent costs where there is a material change in the cost base of a retailer in comparison to that allowed by the Commission when the price path, being the TFT in this instance, is determined.

AGL looks forward to contributing further to the Commission's review. For any enquires in relation to this submission please contact Carol Lydford, Manager Regulatory Pricing Strategy on (02) 9921 2511 or email carol.lydford@agl.com.au

Yours sincerely,

Beth Griggs
Head of Price Regulation

² Issues Paper Retail Prices for Non-contestable Electricity Customers 2009-2010

- > Being selected as a member of the Dow Jones Sustainability Index 2006/07
- > Gaining accreditation under the National GreenPower Accreditation Program for AGL Green Energy®, AGL Green Living® and AGL Green Spirit
- > Being selected as a constituent of the FTSE4Good Index Series