



ICRC

independent competition and regulatory commission

Final report
**Standing offer prices for the
supply of electricity to small
customers**

1 July 2014 to 30 June 2017
Report 4 of 2014, June 2014

The Independent Competition and Regulatory Commission is a Territory Authority established under the *Independent Competition and Regulatory Commission Act 1997* (the ICRC Act). The Commission is constituted under the ICRC Act by one or more standing commissioners and any associated commissioners appointed for particular purposes. Commissioners are statutory appointments and the current Commissioners are Senior Commissioner Malcolm Gray and Commissioner Mike Buckley. We, the Commissioners who constitute the Commission, take direct responsibility for delivery of the outcomes of the Commission.

We have responsibilities for a broad range of regulatory and utility administrative matters. We have responsibility under the ICRC Act for regulating and advising government about pricing and other matters for monopoly, near-monopoly and ministerially declared regulated industries, and providing advice on competitive neutrality complaints and government-regulated activities. We also have responsibility for arbitrating infrastructure access disputes under the ICRC Act. In discharging our objectives and functions, we provide independent robust analysis and advice.

Our objectives are set out in section 7 of the ICRC Act and section 3 of the *Utilities Act 2000*.

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Foreword

This report finalises the Commission's consideration of regulated retail electricity prices for 2014-17.

The principal change from the draft report is the inclusion of finalised charges for network services, as approved by the Australian Energy Regulator. Unfortunately, these have increased rather more than was expected at the time of the draft report. This has meant that the cost allowance for network charges in our cost index model has risen by 11 per cent compared to the 2.45 per cent foreshadowed in the draft report. As explained in the body of this report, this is primarily due to increases in transmission costs and the expected commissioning of the ACT's first large-scale solar generator.

On 1 July, regulated retail electricity prices will rise on average by 4.3 per cent with the cost of electricity increasing by \$1.63 per week for a typical, medium sized, residential customer. If, as has been foreshadowed by the Commonwealth government, the price on carbon is removed in the coming year, the Commission has determined that a second price change will automatically occur. This will reduce prices by 7.3 per cent on average relative to their current levels, bringing a reduction in the electricity bill of a typical, medium sized, residential customer of \$2.75 per week relative to current levels.

While we cannot be sure if and when the price on carbon will be removed, this report and its associated price direction puts in place arrangements to ensure that the benefits flow to ACT electricity customers on regulated tariffs as quickly as possible.

I commend the report to you.

Malcolm Gray
Senior Commissioner
13 June 2014

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Executive summary

Introduction

The current price direction for the supply of electricity to customers on ActewAGL Retail's regulated tariffs expires on 30 June 2014. The Independent Competition and Regulatory Commission (the Commission) was asked by the ACT Government to provide a price direction for the supply of electricity to customers on ActewAGL Retail's regulated retail tariffs for the period commencing 1 July 2014 and ending 30 June 2017.

The Commission undertook a comprehensive price investigation, including public consultation on an issues paper and a draft report. The investigation concludes with the publication of this final report and price direction.¹

Future price on carbon

The terms of reference for this price investigation require the Commission to consider the impact on electricity costs associated with the Australian Government's carbon pricing mechanism and the pass-through of those costs to regulated prices. The Australian Government has announced its intention to repeal the price on carbon with effect from 1 July 2014. At the time of publishing this report, the repeal legislation is yet to be enacted.

The Commission's current cost-index model incorporates an adjustment to the wholesale energy purchase cost to account for the price on carbon set under the Australian Government's carbon pricing legislation, the *Clean Energy Act 2011* (Clean Energy Act).

The Commission's final decision is to implement a contingent pricing mechanism. This involves the determination of two maximum average percentage price changes for 2014–15. The first includes the current legislated price on carbon. The second excludes any price on carbon from the energy purchase cost. ActewAGL Retail will implement the with-carbon-price tariffs from 1 July 2014 and the without-carbon-price tariffs subsequent to the repeal of the Clean Energy Act. In the event the repeal legislation, or the introduction of any alternative carbon reduction policy, results in some non-zero price on carbon, the Commission has included a price variation trigger.

¹ The price direction is published separately on the Commission's website at www.icrc.act.gov.au.

Form of regulation

The ACT Government has set a three-year regulatory period from 1 July 2014 to 30 June 2017 in the terms of reference provided to the Commission. The Commission proposes to maintain its current approach to the form of regulation. This includes:

- controlling prices from one year to the next using a weighted average price cap;
- using a cost-index model to set a maximum for the average price change across ActewAGL Retail's basket of regulated tariffs;
- pass-through arrangements to provide for the treatment of unexpected events that occur after the price direction has been made; and
- a number of price variation trigger mechanisms that allow the Commission to vary a price direction under particular circumstances.

Methodology for determining efficient cost – the cost-index model

The energy purchase cost model

In the draft report, the Commission thoroughly assessed its energy purchase cost model, which forms a key part of the cost-index model, paying particular attention to whether its approach to hedging costs remains appropriate. This was in response to stakeholder concerns that the model does not accurately account for the risks that electricity retailers face in the wholesale market. The Commission concluded that it is confident that its current energy purchase model accurately reflects the costs, including hedging costs that would be incurred by an efficient retailer in providing retail electricity services in the ACT.

Consistent with the conclusions in the draft report, the Commission's final decision is to adopt its current energy purchase cost model with a 23-month averaging period for the forward price and a 12-month averaging period for the carbon emissions intensity factor.

For the annual recalibrations, the Commission has assumed that there is no price on carbon and therefore the cost of carbon has been removed from the energy purchase cost equation described in the draft report.

Energy losses

The Commission has made a number of technical changes to the way it estimates the energy losses cost allowance. The effect of these changes on retail electricity prices is not material.

Retail operating costs

The Commission has reviewed its methodology for calculating retail operating costs and determined an allowance of \$13.57 per megawatt hour (MWh) in 2014–15, a 19 per cent increase over the 2013–14 cost allowance of \$11.43 per MWh.

Retail margin

The Commission has made two changes to the retail margin for 2014–15. First, the benchmark retail margin has been increased from 5.4 to 5.7 per cent drawing on research undertaken by the Independent Pricing and Regulatory Tribunal in New South Wales. Second, the Commission has changed the way it calculates the retail margin allowance to be consistent with the approach taken in New South Wales and Queensland. These changes result in a retail margin of 6.04 per cent for the next regulatory period.

Energy Efficiency Improvement Scheme

The terms of reference for this price investigation require the Commission to identify and report on the efficient costs associated with compliance with the ACT Government's Energy Efficiency Improvement Scheme (EEIS).

The Commission has applied a forward-looking assessment of the prudence and efficiency of ActewAGL Retail's forecast expenditure on the energy efficiency scheme for 2014–15 and subsequent years of the regulatory period. The Commission found ActewAGL Retail's forecast costs to be prudent and efficient and has determined an allowance of \$4.92 per MWh for 2014–15.

A competition allowance in the ACT

The Commission considers the introduction of a competition allowance in the ACT to be a high-risk strategy because there is a reasonable probability that any benefits it may produce will be long delayed, and therefore of little present value, and a distinct possibility that it will not produce benefits even in the long term.

The Commission considers that all customers in the ACT, large and small, are well served by the retail electricity market as it has developed here. The Commission therefore proposes to continue its practice of not including such an allowance in the calculation of its cost-index model for the next regulatory period.

The Commission acknowledges that the National Electricity Market (NEM) is in a continuing state of development and is of the view that monitoring of market developments should be maintained.

Retail electricity prices in 2014–15

Table ES.1 and Table ES.2 set out the Commission's final decision on the cost components used to determine the maximum allowed change in the regulated retail electricity price for 2014–15, with and without carbon costs, respectively.

The with-carbon-price maximum average percentage change in prices is 4.33 per cent in ActewAGL Retail's basket of regulated tariffs. This change will apply from 1 July 2014 until the Clean Energy Act is repealed. This nominal change is equivalent to a real (adjusted for inflation) increase in the regulated retail price of about 2 per cent.

The primary driver of the price increase is the rise in network costs. Increases in the retail operating cost allowance, costs of the EEIS and the rise in the retail margin have been largely offset by a fall in Large-scale Renewable Energy Target (LRET) and Small-scale Renewable Energy Scheme (SRES) costs and the energy losses cost component.

Table ES.1 Final decision on cost elements 2014–15 with a price on carbon

Component	2013–14 (\$/MWh)	2014–15 (\$/MWh)	% change
Energy purchase cost ^a	70.28	70.99	1.00
LRET and SRES costs	11.66	8.49	-27.16
Energy losses ^b	3.84	0.87	-77.47
Energy contracting cost	0.82	0.84	2.45
NEM fees	0.82	0.84	2.45
Total energy purchase cost	87.42	82.03	-6.17
Retail operating costs	11.43	13.57	18.76
Energy Efficiency Improvement Scheme costs	3.75	4.92	31.09
Total retail costs	15.18	18.49	21.81
Network costs	88.29	98.02	11.02
Total energy + retail + network costs	190.89	198.53	4.00
Retail margin ^c	10.90	12.00	10.13
Total costs	201.79	210.53	4.33

Notes: a The 2013–14 energy purchase cost amount has been recalculated from that contained in the 2013–14 price reset due to the adjustments to the forward price and carbon emissions intensity factor averaging periods and the Commission's desire to maintain comparability across adjacent years under the index approach.

b The 2013–14 energy losses amount has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

c The 2013–14 retail margin allowance has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

The without-carbon-price maximum average percentage change in electricity prices is minus 7.30 per cent in ActewAGL Retail's basket of regulated tariffs compared to 2013–14 prices. This change will apply in the event that the Clean Energy Act is repealed. This nominal change is equivalent to a real decrease in the regulated retail price of about 9.5 per cent.

Table ES.2 Final decision on cost elements 2014–15 without a price on carbon

Component	2013–14 (\$/MWh)	2014–15 (\$/MWh)	% change
Energy purchase cost ^a	70.28	49.00	-30.28
LRET and SRES costs	11.66	8.49	-27.16
Energy losses ^b	3.84	0.72	-81.16
Energy contracting cost	0.82	0.84	2.45
NEM fees	0.82	0.84	2.45
Total energy purchase cost	87.42	59.90	-31.49
Retail operating costs	11.43	13.57	18.76
Energy Efficiency Improvement Scheme costs	3.75	4.92	31.09
Total retail costs	15.18	18.49	21.81
Network costs	88.29	98.02	11.02
Total energy + retail + network costs	190.89	176.40	-7.59
Retail margin ^c	10.90	10.66	-2.14
Total costs	201.79	187.07	-7.30

Notes: a The 2013–14 energy purchase cost amount has been recalculated from that contained in the 2013–14 price reset due to the adjustments to the forward price and carbon emissions intensity factor averaging periods and the Commission's desire to maintain comparability across adjacent years under the index approach.

b The 2013–14 energy losses amount has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

c The 2013–14 retail margin allowance has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

Impact on customers

The Commission has estimated that the annual impact on typical bills in 2014–15 due to the with-carbon-price electricity price change of 4.33 per cent ranges from \$48 for a small residential customer to \$122 for a large residential customer. The impact on a typical bill ranges from \$127 for a small non-residential customer to \$458 for a large non-residential customer.

In the case of the without-carbon-price electricity price change of minus 7.30 per cent, typical bill impacts range from minus \$81 for small residential customers to minus \$205 for a large residential customer. The impact on a typical bill ranges from minus \$214 for a small non-residential customer to minus \$770 for a large non-residential customer.

1 Introduction

1.1 Background to the investigation

Retail competition for small electricity customers (small businesses and households) in the ACT was introduced on 1 July 2003. This followed the opening of the market in 1998 for customers consuming more than 160 megawatt hours (MWh) per year (mainly large businesses) and in 2001 for those consuming more than 100 MWh per year (mainly medium-sized businesses).

When the ACT Government decided to open the market to all customers, it also required that ActewAGL Retail offer customers consuming less than 100 MWh per year a non-negotiated standard customer contract under the *Utilities Act 2000* (the Utilities Act) incorporating a tariff approved by the Independent Competition and Regulatory Commission (the Commission). Customers on the standard contracts were subject to a suite of regulated tariffs. Standard customer contracts and the suite of tariffs were approved by the Commission on an annual basis. Alternatively, customers could choose to enter into negotiated contracts with ActewAGL Retail or other electricity retailers.

With the introduction of the National Energy Customer Framework (NECF) in the ACT from 1 July 2012, standard customer contracts under the Utilities Act have been replaced with standard retail contracts under the *National Energy Retail Law (ACT) Act 2012*. Similarly, negotiated contracts were replaced with market retail contracts. Under the NECF arrangements, the Australian Energy Regulator (AER) is responsible for the regulation of retail electricity contracts. The Commission retains responsibility for setting the regulated retail electricity price and approving ActewAGL Retail's application of price adjustments in its suite of regulated tariffs.

The current price direction for the supply of electricity to customers on the regulated tariff determined prices for the period from 1 July 2012 to 30 June 2014. The Commission's most recent decision under this price direction was to determine a real (inflation-adjusted) increase in the regulated retail price of 1.68 per cent for 2013–14. This is equivalent to a nominal increase of 3.47 per cent, which translates to annual bill increases of between \$36 and \$90 for typical residential customers and between \$98 and \$354 for non-residential customers.²

On 20 September 2013, the Treasurer signed terms of reference under the *Independent Competition and Regulatory Commission Act 1997* (the ICRC Act) for a price direction for the supply of electricity to customers on the regulated retail tariff for the period commencing 1 July 2014. This was replaced by a revised terms of reference signed by the Acting Treasurer on 2 February 2014. The revised terms of reference change

² ICRC, 2013b: 14–15.

certain terminology to ensure consistency with the NECF and prescribed a three-year period for the price direction.³

The Commission released an issues paper on 4 October 2013 and a draft report on 14 February 2014. The Commission received eight submissions on the issues paper and five submissions on the draft report, all of which are available on the Commission's website.⁴ A summary of the submissions received is provided in Appendix 2. The Commission also conducted a public hearing on the draft report, as required by the ICRC Act, on 10 April 2014 at the Commission's offices. The Commission did not receive any registrations to appear at the hearing and no members of the public attended.

The publication of this final report and price direction is the final step in the Commission's consultation process for this investigation.⁵ The Commission has considered stakeholder submissions on the draft report in this report.

1.2 Scope of the terms of reference

The Commission has been asked by the ACT Government to provide a price direction for the supply of electricity to customers on ActewAGL Retail's regulated retail tariff for the period commencing 1 July 2014 and ending 30 June 2017.

The terms of reference require the Commission to consider the following matters in its investigation:

- the impact on direct electricity costs of changes in government policies and pass-through of those costs to regulated prices including, but not restricted to:
 - the Commonwealth Government's carbon pricing mechanism;
 - Commonwealth and ACT retailer obligation energy efficiency schemes;
 - the Commonwealth Government's Large-scale Renewable Energy Target (LRET) and Small-scale Renewable Energy Scheme (SRES); and
 - any other schemes implemented to address climate change relevant to electricity pricing;

and

- the efficient and prudent cost of managing risk in purchasing electricity.

³ See Appendix 1 for a full copy of the revised terms of reference.

⁴ See www.icrc.act.gov.au.

⁵ The price direction is published separately and is available on the Commission's website.

The Commission is also required by the terms of reference to identify and report on:

- the cost allowance for the ACT feed-in tariffs (small- and large-scale) for the year(s) or period for which its determination is being made; and
- the efficient costs of complying with the *Energy Efficiency (Cost of Living) Improvement Act 2012*.

The Commission must produce its final report in sufficient time to allow ActewAGL Retail to make any necessary changes to its billing system and provide information on the new tariff to customers for implementation effective 1 July 2014.

1.3 The ICRC Act

In addition to being instructed by the terms of reference, in making a price direction the Commission is also subject to the provisions of the ICRC Act.

The Commission, in carrying out its functions under the ICRC Act, has the following objectives set out in section 7:

- to promote effective competition in the interests of consumers;
- to facilitate an appropriate balance between efficiency and environmental and social considerations;
- to ensure non-discriminatory access to monopoly and near-monopoly infrastructure.

In making a price direction, the Commission is required to have regard to the provisions set out in section 20(2):

- (a) the protection of consumers from abuses of monopoly power in terms of prices, pricing policies (including policies relating to the level or structure of prices for services) and standard of regulated services; and
- (b) standards of quality, reliability and safety of the regulated services; and
- (c) the need for greater efficiency in the provision of regulated services to reduce costs to consumers and taxpayers; and
- (d) an appropriate rate of return on any investment in the regulated industry; and
- (e) the cost of providing the regulated services; and
- (f) the principles of ecologically sustainable development mentioned in subsection (5);
- (g) the social impacts of the decision; and
- (h) considerations of demand management and least cost planning; and

- (i) the borrowing, capital and cash flow requirements of people providing regulated services and the need to renew or increase relevant assets in the regulated industry; and
- (j) the effect on general price inflation over the medium term; and
- (k) any arrangements that a person providing regulated services has entered into for the exercise of its functions by some other person.

The above requirements guide the Commission’s analysis and intermediate decisions on each element of the proposed price direction from consideration of the form of regulation through to the individual components of the price-setting methodology. Chapter 4 provides a summary of the Commission’s compliance with the terms of reference and the ICRC Act.

ActewAGL Retail became an authorised retailer under the National Energy Retail Law (NERL) on 1 July 2012, and is no longer licensed under the *Utilities Act 2000*. However, ActewAGL Retail is still subject to the price regulation provisions of the ICRC Act – as well as other relevant sections. The following is a summary of the provisions and definitions set out in the ICRC Act with respect to the application of the terms of reference and the Commission’s price direction to ActewAGL Retail.

Sections 15 and 16 of the ICRC Act provide for the referring authority to issue an industry reference in the form of terms of reference for the Commission to determine a price for regulated services. Regulated services are defined in the ICRC Act as ‘services provided in a regulated industry’. The dictionary further defines a regulated industry as ‘an industry engaged in the provision in the ACT of a utility service’. A utility service is defined as ‘the activity of selling energy to small customers within the meaning of the National Energy Retail Law (ACT)’. Furthermore, a utility is defined in the ICRC Act as a utility within the meaning of the Utilities Act or a NERL retailer.

In relation to the price direction applying specifically to ActewAGL Retail, section 15(4) of the ICRC Act states that ‘an industry reference that authorises the Commission to make a price direction about maximum prices for the sale of energy to small customers (however prescribed) may state the NERL retailer to whom the direction applies’. The Commission notes clause 3(4) of the terms of reference, where the Minister has made reference to ActewAGL Retail pursuant to section 15(4), and clauses 1 and 2, where small customer has been defined.

1.4 Structure of the final report

The remainder of the final report is structured as follows:

- Chapter 2 presents the Commission’s final decisions on the form of regulation that will apply in the next regulatory period. This includes the means of controlling prices over each year of the regulatory period, the Commission’s

cost-index model, and pass-through arrangements. Consideration is given to the issues raised in stakeholder submissions on the draft report.

- Chapter 3 provides an estimate of the efficient costs of supplying electricity to customers on the regulated tariff in 2014–15 and the Commission’s final decision on the maximum allowed change in retail electricity prices in 2014–15. It also analyses the impact of the price change on customer bills.
- Chapter 4 summarises the Commission’s compliance with the terms of reference and the ICRC Act.
- Appendix 1 reproduces the revised terms of reference.
- Appendix 2 contains a summary of submissions on the issues paper and draft report.

2 Form of regulation

This chapter sets out the Commission's final decisions on the elements of the form of regulation that will control ActewAGL Retail's electricity prices for its standard retail contracts to apply over the regulatory period from 1 July 2014 to 30 June 2017. The main elements of the form of regulation comprise the cost-index model, pass-through arrangements and price direction variation triggers.

The cost-index model is used by the Commission to determine a benchmark cost of supplying electricity and the maximum allowable price change across the basket of regulated tariffs from one year to the next (a weighted average price cap). The pass-through arrangements provide for the treatment of unexpected events that occur after the price direction has been made. Price direction variation triggers are mechanisms that allow the Commission to vary a price direction under particular circumstances.

This chapter also considers relevant issues raised in the five submissions the Commission received on the draft report. Four submissions were from electricity retailers: ActewAGL Retail and the three large energy businesses. The ACT Government also made a submission. The Commission did not receive any submissions from individual customers or consumer groups.

2.1 Weighted average price cap

In the draft report, the Commission proposed to continue to use a weighted average price cap approach to control regulated prices for each year of the regulatory period, but with two adjustments to the way the weighted average price cap formula is presented. The changes were designed to improve the transparency of the formula without affecting the result of applying the formula. The first change involved focusing exclusively on the nominal percentage change. The second involved presenting the formula as the measured change in average prices that must be less than the calculated change in average costs given by the cost-index model.

The Commission received one submission on the weighted average price cap. ActewAGL Retail supported the Commission's proposed changes to the weighted average price cap formula.⁶

The Commission's final decision is to continue to use a weighted average price cap approach to control regulated prices for each year of the regulatory period commencing 1 July 2014, using the formula proposed in the draft report and set out in Box 2.1.

⁶ ActewAGL Retail, 2014: 4.

Box 2.1 Final decision on weighted average price cap formula

ActewAGL Retail must ensure that its regulated retail tariffs comply with the following formula:

$$1 + Y^t \geq \frac{\sum_{i=1}^n \sum_{j=1}^m P_{ij}^t Q_{ij}^{t-1}}{\sum_{i=1}^n \sum_{j=1}^m P_{ij}^{t-1} Q_{ij}^{t-1}}$$

where

- ActewAGL Retail has n regulated retail tariffs that each have up to m components;
- P_{ij}^t is the price that ActewAGL Retail proposes to charge for component j of regulated tariff i for year t;
- P_{ij}^{t-1} is the price that ActewAGL Retail charges for component j of regulated tariff i in the year t-1;
- Q_{ij}^{t-1} is the reference quantity for component j of the regulated tariff i defined as the actual quantity (in both customer numbers or megawatt hours) as reported by ActewAGL Retail for the 12-month period ending 31 March in year t-1;
- Y^t is the maximum average percentage change in regulated retail tariffs determined in accordance with the Commission's cost-index model.

As explained in section 2.3.2, the Commission will determine two maximum average percentage changes to apply in 2014–15.

The first set of prices will apply under the current price on carbon legislation. The maximum average percentage change for these prices is based on the 2014–15 price on carbon of \$25.40 per tonne of emitted CO₂.

The second set of prices will be implemented in the event the *Clean Energy Act 2011* (Clean Energy Act) is repealed, but will only apply if there is no price on carbon under the new arrangements. In the event of some new non-zero price on carbon, the Commission has included a price variation trigger. This is discussed in section 2.5.

2.2 Annual price recalibration process

In the draft report, the Commission maintained its view that regulated prices should be adjusted on an annual basis consistent with the Commission's current practice of annually calculating the benchmark cost of supplying electricity to customers for changes in wholesale energy, network and retail costs.

The Commission did not receive any submissions on the proposed annual weighted average price cap recalibration arrangements.

The Commission's final decision is to provide for two annual price recalibrations for the regulatory period commencing 1 July 2014. The first will determine prices for 2015–16 and the second will determine prices for 2016–17.

Essentially, the annual recalibration involves updating the parameters of the retail electricity cost-index model. This process draws on, for example, more recent forward price and load data, updated network costs and new estimates of green costs. A number of model components, such as retail operating costs, are adjusted by the change in the consumer price index. The recalibration process can also incorporate additional costs from a pass-through event.

The following process will apply for each annual recalibration:

- ActewAGL Retail will submit to the Commission on or before 10 May prior to the regulatory year in question the following information:
 - calculation of costs associated with achieving environmental objectives for the year in question, including calculation of the LRET, SRES and ACT energy efficiency scheme costs, and any proposed adjustments; and
 - full accounting of all proposed pass-through costs.
- ActewAGL Retail will submit to the Commission for verification the updated network cost allowance for the regulated customer load as soon as ActewAGL Distribution's network charges are approved by the Australian Energy Regulator (AER).
- The Commission will determine the energy purchase cost component based on data available to 31 May prior to the regulatory year in question and energy losses based on Australian Energy Market Operator (AEMO) data.

Based on this information, the Commission will determine the maximum allowed percentage by which the weighted average price cap may be adjusted. The Commission will provide its direction to ActewAGL Retail by 7 June prior to the regulatory year in question. This date assumes approved network charges are available from the AER. In the event that this is not the case, this date will be extended until approved network charges are available. ActewAGL Retail will provide the Commission with its proposed schedule of regulated retail prices, including the associated weighted average price cap calculations. The Commission will then, subject to an assessment that the proposals are consistent with the price direction, approve the proposed prices within two working days of receipt of the proposed schedule.

The Commission has also included a provision to maintain current prices into the new regulatory year in the event the AER does not approve network costs in time to allow the Commission to determine the maximum average percentage change in prices for the new prices to apply on 1 July.

Table 2.1 shows the approach to calculating the individual cost components for the price recalibrations for each year that will determine the maximum average allowed percentage change. Approved pass-through amounts measured in dollars per MWh will be included as an additional component in the cost-index model as required.

The Commission will inflate the dollar value of the pass-through amount into current prices at the time of the recalibration using the following consumer price index adjustment formula, populated with the Australian Bureau of Statistics all groups index for the weighted average of eight capital cities.

$$\Delta CPI_t = \frac{CPI_{Mar(t-2)} + CPI_{Jun(t-2)} + CPI_{Sep(t-1)} + CPI_{Dec(t-1)}}{CPI_{Mar(t-3)} + CPI_{Jun(t-3)} + CPI_{Sep(t-2)} + CPI_{Dec(t-2)}} - 1$$

Table 2.1 Final decision on annual recalibration of cost components

Component (\$/MWh)	Method
Energy purchase cost	As determined by the Commission at the time of the recalibration using the energy purchase cost model
LRET and SRES costs	Estimates from ActewAGL Retail for the 2015–16 and 2016–17 years respectively, which are verified and applied using the Commission's methodology
Energy Efficiency Improvement Scheme costs	Estimates from ActewAGL Retail for the 2015–16 and 2016–17 years as required, subject to a prudence and efficiency assessment, with costs determined using the Commission's methodology
Energy losses	Calculated using the formula in Box 2.2 using AEMO's marginal loss factor and distribution loss factor estimates for 2015–16 and 2016–17 as appropriate
Energy contracting costs	Previous year's value adjusted by the change in CPI
NEM fees	Previous year's value adjusted by the change in CPI
Retail operating costs	Previous year's per customer value adjusted by the change in CPI
Network costs	As determined and approved by the AER and applied by ActewAGL Retail to the standard retail contract customer load, and subsequently verified by the Commission
Cost pass-through	Cost pass-through verified by the Commission in current dollars as adjusted by the change in CPI
Retail margin	Use a formula for the retail margin expressed in ex post terms, equivalent to a margin of 6.04 per cent measured ex ante

2.3 Cost-index model

In Chapter 3 of the draft report, the Commission assessed the cost-index model it currently uses to determine the extent to which ActewAGL Retail can change its regulated retail tariffs over those in the previous year using the weighted average price cap formula. In the draft report, the Commission proposed the following changes to its current cost-index model:

- a return to averaging the forward price and carbon emissions intensity factor over 23 and 12 months, respectively;
- an adjustment to the energy losses formula;
- a step-up in the retail operating cost allowance; and
- an increase in the retail margin to 5.7 per cent.

2.3.1 Energy purchase cost

In the draft report the Commission re-examined the cost-index model it has been applying since 2003. In its assessment of the energy purchase cost model, which forms a key part of the cost-index model, the Commission paid particular attention to whether its approach to hedging costs remains appropriate. This was in response to stakeholder concerns that the model does not accurately account for the risks that electricity retailers face in the wholesale market.

The Commission reviewed whether the long-run marginal cost of generating electricity should factor into the energy purchase cost allowance. The Commission received submissions from energy retailers supporting the use of long-run marginal cost as a floor. In the 2010 review, the Commission considered and rejected long-run marginal cost as a floor and the draft report reaffirmed this position.

ActewAGL Retail also recommended that the Commission increase the forward price margin, a key component of the hedging cost calculation. The Commission reviewed this issue and came to the conclusion that the 5 per cent margin remains reasonable. The Commission was confident that its current energy purchase model accurately reflects the changes in costs, including hedging costs, which would be incurred by an efficient retailer in providing retail electricity services in the ACT.

The final issue considered is the averaging period for the forward price and the carbon emissions intensity factor.

Submissions on the draft report

The primary issue raised in the submissions on the energy purchase cost model was the lack of a long-run marginal cost floor in the Commission's model. ActewAGL Retail expressed a preference for, and EnergyAustralia advocated, adopting long-run marginal cost as a floor when determining energy purchase costs. Neither provided substantive discussion or evidence on this issue in their submissions, although EnergyAustralia did refer the Commission to its submission to the Australian Energy Market Commission (AEMC) review of best practice retail market regulation.⁷

⁷ See www.aemc.gov.au/Markets-Reviews-Advice/Advice-on-Best-Practice-Retail-Price-Regulation-Me for more information.

Origin addressed the Commission's reasons for not taking account of long-run marginal cost. The Commission first raised concerns about long-run marginal cost in its 2010 final technical report on the energy purchase cost methodology. In the draft report, the Commission discussed three concerns, which are:

- In competitive markets, equilibrium prices are based on short-run cost considerations.
- There is no settled methodology for calculating long-run marginal cost.
- Retail prices have no impact on generation investment incentives.⁸

Origin questioned the Commission's view that, in a competitive market, short-run marginal cost drives prices, stating:

We find it likely that even retailers that do not own generation assets rely on a mixture of shorter and longer term arrangements when procuring energy for retail customers, rather than relying solely on derivative instruments linked to changes in the spot price.⁹

On the concern about an appropriate methodology for estimating long-run marginal cost, Origin stated:

Origin contends that approaches to estimating LRMC exist upon which the ICRC could reasonably rely.¹⁰

Origin, however, accepted that the Commission is not able to address a market failure in the market for generation investment. Nonetheless, it stated that the regulator should consider market dynamics and, by implication, employ long-run marginal cost when setting prices.

The other issue that was raised in the submissions was a concern that the Commission's energy purchase cost model did not place enough weight on the load ratio portion of the uplift factor. AGL Energy and ActewAGL Retail commented on this issue.¹¹ ActewAGL Retail noted that recent trends in wholesale prices and loads have resulted in the uplift factor falling even though its load is becoming more peaky. ActewAGL Retail suggested that the forward price margin be raised to better reflect the increased hedging costs electricity retailers face at this time.

Additionally, ActewAGL Retail supported the continued use of the ICAP over-the-counter contract prices to estimate the forward price, and using a 12-month averaging period for estimating the emissions intensity factor in the calculation of the cost of carbon.

⁸ ICRC, 2014a: 32.

⁹ Origin, 2014: 2.

¹⁰ Origin, 2014: 2.

¹¹ ActewAGL Retail, 2014: 7; AGL Energy, 2014: 1.

Commission’s consideration

Long-run marginal cost

The Commission’s approach is to set a market-based energy purchase cost allowance. As described above, the Commission has never accepted consideration of long-run marginal cost as an acceptable method for determining the energy purchase cost component in the cost-index model. The Commission fully considered this issue when the current model was developed in 2010 and rejected the use of long-run marginal cost at that time. Subsequently, the Commission has reaffirmed this decision. Since 2010, the Queensland Competition Authority (QCA) has also considered this matter and in 2013 it stated:

The Authority is not convinced that the inclusion of LRMC in any form in the estimation of energy costs is warranted or necessary and maintains its view that a market-based approach should provide the best estimate of the costs that retailers will incur in the year ahead.¹²

The Independent Pricing and Regulatory Tribunal (IPART) has been required by its terms of reference to have regard to long-run marginal cost in its three previous reviews of regulated retail electricity prices in New South Wales. In its treatment of customer acquisition and retention costs, IPART focuses on the short-term cost of supply.¹³

In its review of best practice retail electricity regulation, the AEMC recommended that, should futures prices be considered unreliable due to insufficient liquidity in the futures market, a long-run marginal cost approach using the perturbation method should be used to estimate the energy purchase cost.¹⁴

The conclusion that can be drawn from the jurisdictional regulators and the AEMC is that there is little support for long-run marginal cost as a floor for the energy purchase cost component.

The Commission notes that prudent competitive businesses, when faced with price volatility in key inputs in the production process, will hedge their exposure to risk in the input market. If they hedge by purchasing in advance most of their expected demand in competitive forward markets from suppliers, they are still purchasing at prices determined by current market forces and not on the basis of long-run marginal cost considerations.

Origin argues that long-run marginal cost should be a floor below which the energy purchase allowance should not fall. That is, the market-based estimate of the energy purchase cost should only be applied where it is higher than the long-run marginal cost.

¹² QCA, 2013: 25.

¹³ IPART, 2013: 109.

¹⁴ AEMC, 2013a: 25.

This is equivalent to adopting the maximum of the market-based cost and the long-run marginal cost.

Origin argues that the long-run marginal cost floor is necessary to ensure efficient investment in generation capacity. The Commission has repeatedly stated that there is no link between retail electricity prices and incentives for investment in generation capacity. In 2010, the Commission noted:

If a regulator, in determining the cost build-up of a regulated retail electricity supplier, increases the cost of any input this flows through to the final price that the regulated business can charge. It does not flow backwards to higher input prices unless the retailer is altruistically supporting its suppliers.¹⁵

The economics are simple and clear. If a regulator grants higher purchase costs for electricity to a retailer, the gains accrue to the retailer and there are no increased incentives for investment in generation capacity. In the ACT case, ActewAGL Retail would unnecessarily benefit at the expense of small ACT electricity customers without any impact on generation investment incentives.

The Commission's hedging strategy

The Commission's energy purchase cost model estimates a market-based forward price of electricity and then applies an uplift factor to account for the cost of a conservative hedging strategy. The uplift factor consists of the load shape, the load ratio and the forward price margin. These are described in detail in Chapter 3 of the draft report.

ActewAGL Retail expressed concern that its actual hedging costs are increasing due to increased peakiness in the ACT load profile. This is in contrast to the observed reduction in the Commission's uplift factor, which implies a reduction in hedging costs. AGL Energy has expressed a similar view in its submission. To address this, ActewAGL Retail has repeated its claim made in its submission to the issues paper that the forward price margin should be raised. This would increase the uplift factor in the Commission's energy purchase cost model.

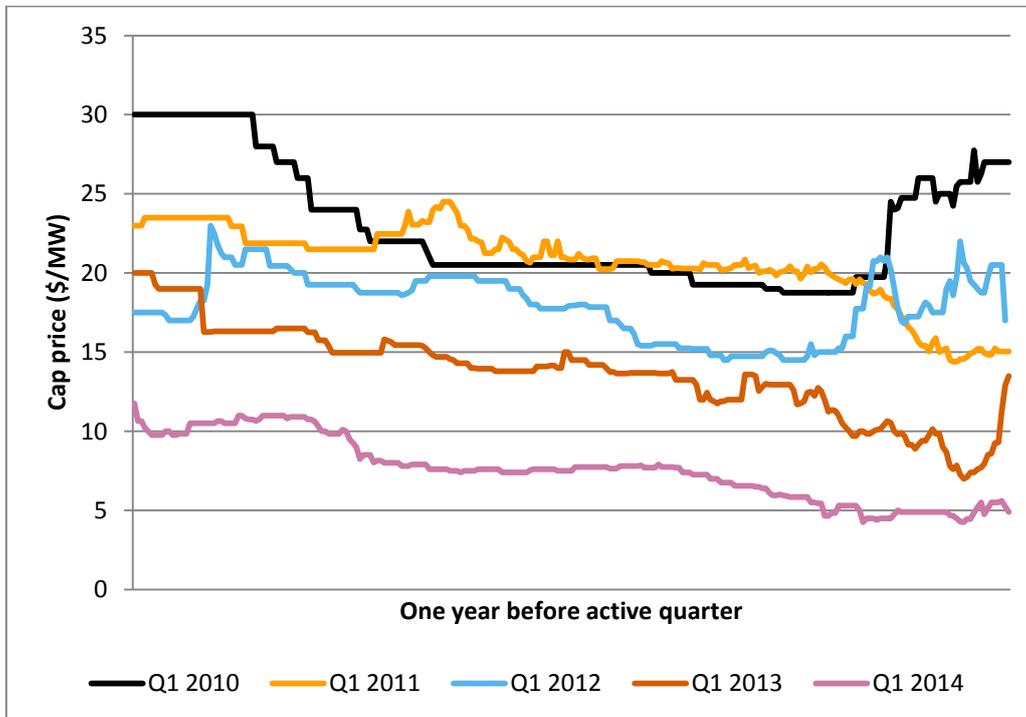
The Commission's view is that the energy purchase cost model is doing exactly what it was designed to do. As ActewAGL Retail points out, the uplift factor has been trending down over the past few years, despite the load ratio rising due to the increased peakiness of the ACT load profile. At the same time, the New South Wales spot market price for electricity has become much less volatile. Thus, the load shape has fallen over this period. The uplift factor has trended down as the impact of the reduction in the load shape has outweighed the increase in the load ratio.

To test ActewAGL Retail's claim that its actual hedging costs have been increasing, the Commission examined the market for Quarter Base \$300 Cap Products (caps) in New South Wales, which are a market-based indicator of hedging costs. Caps are a

¹⁵ ICRC, 2010: 16.

hedging instrument which insure against price spikes.¹⁶ Figure 2.1 shows the price for first-quarter caps as traded for the previous 12 months as reported by ASX Energy. As can be seen, the price of caps has fallen over the past five years.

Figure 2.1 Electricity cap prices New South Wales first quarter 2010–2014



Source: <https://asxenergy.com.au/>

If ActewAGL Retail is purchasing caps to hedge its risk exposure in the wholesale market for electricity, then its hedging costs would have fallen over the past few years.¹⁷ The Commission's model is designed to be precautionary and the available evidence shows that it is. If the Commission's model incorporated the use of caps in the hedging strategy then the uplift factor would have decreased by a more substantial amount than the recent decline.

In conclusion, the Commission's view is that the energy purchase cost model is performing as designed and is providing a conservative energy purchase cost for ActewAGL Retail. It is also worth noting that the Commission's model generates higher market-based energy purchase cost allowances than those granted by IPART in its 2013 review.¹⁸

¹⁶ See https://asxenergy.com.au/products/electricity_futures for more information.

¹⁷ ActewAGL Retail claimed in its submissions to the review of the energy purchase model, which the Commission undertook from late 2009 through March 2012, that caps were part of a prudent hedging strategy. See ActewAGL Retail, 2009: 8–9.

¹⁸ IPART, 2013: 73.

Averaging period

In the draft report, the Commission proposed a return to averaging the forward price over 23 months. The Commission received no submissions on the revised forward price averaging period. In the draft report, the Commission also proposed a return to averaging the carbon emissions intensity factor over 12 months. ActewAGL Retail supported this proposal.¹⁹ The Commission will therefore adopt these changes in its final decision.

Final decision

Consistent with the conclusions in the draft report, the Commission will adopt its current energy purchase cost model with a 23-month averaging period for the forward price and a 12-month averaging period for the carbon emissions intensity factor. The proposed removal of a price on carbon will have implications for the operation of the energy purchase cost model for 2015–16 and 2016–17. This is discussed in the next section.

2.3.2 Future price on carbon arrangements

In the draft report, the Commission addressed the uncertainty over the repeal of the Clean Energy Act and associated price on carbon. The Commission proposed a flexible set of arrangements to deal with the uncertainty associated with the repeal of the Clean Energy Act. First, a pass-through arrangement, and second, a price direction variation trigger (discussed in sections 2.4 and 2.5, respectively).

The proposed carbon pass-through arrangement involves the Commission, subsequent to the repeal of the Clean Energy Act, adjusting all components of ActewAGL Retail's regulated tariffs proportionately by the change due to the removal of the price on carbon.

Submissions on the draft report

ActewAGL Retail did not support the Commission's proposal to adjust all components of ActewAGL Retail's standing offer prices proportionately to remove the price-on-carbon component, stating:

The Commission's proposal assumes that the carbon price is applied evenly on a proportional basis on all tariffs. However, that is not the case.²⁰

ActewAGL Retail advised that:

- the price on carbon is only applied to the energy (consumption) charge and not to the supply charge; and

¹⁹ ActewAGL Retail, 2014: 7.

²⁰ ActewAGL Retail, 2014: 16.

- maximum demand and capacity tariffs are passed through as network charges and do not contain a carbon price component.

ActewAGL Retail suggested that the Commission consider a contingent pricing mechanism as an alternative. This would involve the Commission determining two maximum average percentage changes, with and without a price on carbon, in the price direction.²¹

The ACT Government stated that its primary concern is to ensure that electricity businesses are not able to make windfall profits at the expense of ACT customers from the repeal of the price on carbon. The ACT Government suggested that the Commission consider a pass-through arrangement that allows the recovery of any potential windfall gains when setting electricity prices from 1 July 2015.²²

Commission’s consideration

There are two matters for the Commission to consider in responding to submissions. The first is the price adjustment mechanism following the repeal of the carbon price. The second is whether to recoup any windfall gains due to a retrospective repeal of the carbon price to 1 July 2014. The Commission also needs to clarify the effect the removal of a price on carbon will have on the operation of the energy purchase cost model for the two annual price recalibration exercises.

Price adjustment mechanisms

In light of the information provided by ActewAGL Retail in its submission, the Commission agrees that a proportionate change in all tariff components to remove the price-on-carbon component is undesirable. This is especially the case if such a change, as in the case of maximum demand and capacity tariffs, resulted in tariffs that are not cost-reflective. The Commission does not propose, therefore, to adopt this pass-through arrangement proposal in its final decision.

The Commission considers that there is merit in ActewAGL Retail’s contingent pricing proposal. Determining a with- and without-carbon-price maximum average percentage change would allow ActewAGL Retail to decide on and seek Commission approval for two sets of prices before 1 July 2014. The first set of prices would apply while the price on carbon remained in place and the second set would be implemented in the event that the Clean Energy Act is repealed. It is important to note that the without-carbon-price maximum average percentage change will only apply if there is no price on carbon under the new arrangements.

A contingent pricing mechanism removes the need for a pass-through arrangement as both sets of prices would be approved by the Commission prior to the 2014–15 regulatory year. This arrangement has the benefit of providing certainty and

²¹ ActewAGL Retail, 2014: 17.

²² ACT Government, 2014: 2.

transparency for electricity customers about the treatment of the price-on-carbon removal in electricity prices in advance of the prices taking effect.

The Commission notes that the QCA, in its draft determination for 2014–15 retail electricity prices in Queensland, has proposed a contingent pricing mechanism, albeit one that relies on Queensland Government intervention to enable a mid-year price adjustment.²³

A matter related to the practical application of a contingent pricing mechanism is the price variation requirements under the NERL. Section 23 of the schedule to the *National Energy Retail Law (South Australia) Act 2011* limits the variation of standing offer prices by retailers to only once every six months. The Commission noted in the draft report that this could result in a delay in implementing any price change following the repeal of the Clean Energy Act. The Commission also indicated its intention to ensure that any price-on-carbon arrangement does not result in the price direction conflicting with the NERL timing requirements.

Subsequent to the release of the draft report, the AER, which has responsibility for enforcing the NERL, published a compliance statement indicating that it:

will not take action against a retailer for possible breaches of certain provisions of the National Energy Retail Law in circumstances where retailers are introducing lower prices to reflect savings from the repeal of the carbon tax.²⁴

The effect of this is that the AER expects retailers to publish amended standing offer electricity prices immediately upon repeal of the carbon pricing legislation. The AER also states that it appears that carbon-price-contingent tariffs would not be constrained by the NERL variation requirements, but, to the extent of any risk that tariffs were so constrained, the AER would not pursue noncompliance in these circumstances.

The risk in relation to compliance with NERL requirements falls on ActewAGL Retail. ActewAGL Retail advised the Commission that if a contingent price schedule was established, it would rely on the AER's compliance statement if that meant that it needed to adjust its standing offer prices within six months of 1 July 2014.

The removal of the NERL timing hurdle should address the ACT Government's concerns about the potential for windfall gains for ActewAGL Retail arising from any delay in the application of without-carbon prices following the repeal of the Clean Energy Act.

In the draft report, the Commission proposed that, should the maximum average price change in the Commission's final decision be close to zero, it would give further

²³ QCA, 2013: 23.

²⁴ AER, 2014: 1.

consideration to determining no price change on 1 July 2014, followed by a price adjustment as soon as the repeal legislation was passed.

This alternative to a contingent pricing mechanism was developed as a means to remove any NECF price variation compliance risk as long as the repeal took place within six months of 1 July 2014. In view of the AER compliance statement and ActewAGL Retail's intention to rely on the compliance statement, this option is no longer necessary.

Retrospective repeal implications

The ACT Government expressed concern about windfall gains that could accrue under a retrospective repeal. In the draft report, the Commission indicated that it has no basis to assess the impact of a retrospective change in the price on carbon on ActewAGL Retail's contractual electricity purchase arrangements. Accordingly, the Commission did not propose to incorporate any pass-through amount related to potential refunding of carbon costs under a retrospective repeal scenario. Similarly, the Commission did not propose to consider any pass-through amount related to carbon-inclusive transactions that apply beyond the date that the regulated retail prices in the ACT change consequent on the repeal of the Clean Energy Act.

The QCA commented on this matter, stating that:

A further complication is that the carbon tax might be 'repealed' from 1 July 2014, even if parliament has not passed the repeal bills. If this eventuates, generators might be required to pay back carbon costs to retailers retrospectively, who could then be expected to pay these costs back to customers. It is unclear how such a process would be implemented.²⁵

The QCA did not propose to make any adjustment to prices to reimburse customers should this situation eventuate.

The Commission's view remains that it has no basis to assess the impact of a retrospective change in the price on carbon on ActewAGL Retail's contractual electricity purchase arrangements. The Commission's final decision is to not incorporate any pricing mechanism to deal with any potential customer reimbursement of carbon costs accrued between 1 July 2014 and the legislation repeal date.

Energy purchase cost model annual recalibration implications

The cost of carbon enters into the energy purchase cost model in two ways for the annual recalibrations. First, the cost of carbon is added to the carbon-exclusive energy purchase cost. Second, the load shape is adjusted for the cost of carbon to ensure comparability with historical load shapes.

²⁵ QCA, 2013: 23.

The Commission’s contingent pricing mechanism for 2014–15 properly accounts for the removal of a price on carbon as of the day that the retail electricity tariffs are adjusted. For the annual recalibrations, the Commission has assumed that there is no price on carbon and, for this reason, the cost of carbon has been removed from the energy purchase cost equation described in Chapter 3 of the draft report.

The situation is less clear cut for the load shape calculation. In the event that the price on carbon is removed after 1 July 2014, the load shape for the period of time from then until it is removed will need to be adjusted for the cost of carbon. The current energy purchase cost model provides for this possibility.

Final decision

The Commission’s final decision is to include a contingent pricing mechanism in the price direction, which requires:

- the Commission to determine two maximum average percentage changes for 2014–15. The first includes the current legislated price on carbon. The second excludes any price on carbon from the energy purchase cost;
- ActewAGL Retail to apply the with- and without-carbon-price maximum average percentage changes and provide the Commission with two sets of maximum regulated electricity prices for approval; and
- ActewAGL Retail to implement the approved with-carbon-price schedule of tariffs from 1 July 2014 and the approved without-carbon-price schedule of tariffs subsequent to the repeal of the Clean Energy Act.

In the event that the repeal legislation, or the introduction of any alternative carbon reduction policy, results in some new non-zero price on carbon, the Commission has included a price variation trigger. This is discussed in section 2.5.

The Commission has adjusted the energy purchase cost model for the annual recalibrations so that it no longer adds the cost of carbon to the carbon-exclusive energy purchase cost.

2.3.3 Large-scale Renewable Energy Target and Small-scale Renewable Energy Scheme costs

In the draft report, the Commission reviewed its current methodology for estimating the cost of meeting the national Large-scale Renewable Energy Target (LRET) and Small-scale Renewable Energy Scheme (SRES) obligations. The Commission concluded that it would maintain the current market-based approach to determining these costs.

Submissions on the draft report

ActewAGL Retail maintained the view it put forward in its issues paper submission that, should the Commission continue to use a market-based approach to estimate LRET costs, it should provide an additional allowance for volume risk, liquidity risk,

delivery risk and regulatory risk.²⁶ ActewAGL Retail also maintained its view that the current market-based approach to calculating SRES costs does not fully address the risks in the small-scale technology certificate (STC) market.

ActewAGL Retail noted that the Clean Energy Regulator is no longer updating non-binding renewable power percentage estimates and suggested that the Commission use the current non-binding estimate of 10.52 per cent for 2015 for the renewable power percentage.

EnergyAustralia maintained the preference it put forward in its issues paper submission for using long-run marginal cost rather than a market-based approach to estimate LRET costs and for SRES costs to be estimated at the \$40 clearing house price.²⁷ Origin maintained the preference it put forward in its issues paper submission for using long-run marginal cost rather than a market-based approach to estimate LRET costs.²⁸

Commission’s consideration

The Commission addressed its current approach to estimating LRET and SRES costs in Chapter 3 of the draft report, including considering submissions on the issues paper. The Commission’s draft decision to continue using its current approach rather than adopt a long-run marginal cost method was informed by the Commission’s view that there is sufficient liquidity in the large-scale generation certificate (LGC) and STC spot markets to meet ActewAGL Retail’s LRET and SRES requirements. The Commission also rejected ActewAGL Retail’s claim for an additional allowance for volume risk, liquidity risk, delivery risk and regulatory risk when estimating LRET costs. This was on the basis that there is much less volatility in the LGC market when compared to the wholesale electricity market and therefore little call for hedging. The Commission also noted that it separately provides an additional 10 per cent holding cost and a retail margin that together should cover any risk in this regard.

The Commission did not receive any substantive new arguments in submissions on the draft report that persuade it to change its draft position.

Final decision

The Commission’s final decision is to continue estimating LRET and SRES costs using its market-based approach as described in section 3.5 of the draft report.

The Commission agrees with ActewAGL Retail’s proposal to use the current non-binding estimate of 10.52 per cent for 2015 in the absence of any updated information from the Clean Energy Regulator.

²⁶ ActewAGL Retail, 2014: 7.

²⁷ EnergyAustralia, 2014: 7.

²⁸ Origin, 2014: 3.

2.3.4 Energy losses

In the draft report, the Commission proposed a number of technical changes to the way it estimates the costs of energy losses. Specifically, the Commission included NEM fees in the energy loss equation and proposed to apply the distribution loss factor only to the LRET and SRES costs and NEM fees, as set out in Box 2.2.

Box 2.2 Proposed energy loss equation in the draft report

The proposed energy loss component of the wholesale energy cost category of the electricity cost-index model will be calculated as follows in dollars per MWh:

$$\begin{aligned} \text{Energy loss} &= \text{EPC}^t \times (\text{MLF}^t \times \text{DLF}^t - 1) \\ &+ (\text{LRET and SRES}^t + \text{NEM fees}^t) \times (\text{DLF}^t - 1) \end{aligned}$$

where the following are defined for each year t :

- EPC denotes the energy purchase cost (dollars per MWh);
- LRET and SRES costs denote the total calculated costs to meet LRET and SRES requirements (dollars per MWh);
- NEM fees denote the National Electricity Market fees (dollars per MWh);
- DLF denotes the distribution loss factor applicable to the ACT;
- MLF denotes the marginal loss factor applicable to the ACT.

Source: ICRC (2014a): 67.

Submissions on the draft report

ActewAGL Retail supported the Commission's proposed changes to the energy losses equation, but expressed a preference for using the weighted marginal loss factor for both Canberra and Fyshwick connection points (the node between the regional transmission network and the ACT distribution network), and not only the Canberra connection point as is used in the draft report.²⁹ ActewAGL Retail also proposed that the Williamsdale connection point should be considered should a separate loss factor become available.

Commission's consideration

The Commission sources the marginal and distribution loss factors from AEMO. AEMO released its report on marginal loss factors for the 2014–15 financial year on 1 April 2014.³⁰ This report lists three transmission nodes for the ACT region.³¹ The

²⁹ ActewAGL Retail, 2014: 8.

³⁰ AEMO, 2014b: 32.

³¹ One of the transmission nodes in the region is for Essential Energy, the distribution service provider in New South Wales.

Commission has for all previous retail electricity reviews used the marginal loss factor assigned to the Canberra transmission node for determining the energy losses component of the cost build-up.

The cost allowance for energy losses should accurately reflect the costs that ActewAGL Retail incurs as a result of losses in the network. The allowance should also be transparent. As ActewAGL Retail advised, electricity is supplied to the Territory at two transmission nodes, with a third node at Williamsdale soon to be operational. The two active nodes are the Canberra node and the Queanbeyan (ACTEW) node. The marginal loss factor is reported for both of these nodes by AEMO.³² The marginal loss factors for these two nodes are different. The 2014–15 marginal loss factor for the Canberra transmission node is 0.9642 and is 0.9752 for the Queanbeyan (ACTEW) transmission node.

Given that there are currently two and soon potentially three transmission nodes, it seems reasonable that the marginal loss factor should be based on a weighted average where the weights are based on the relative amounts of electricity delivered. The Commission understands that the bulk of electricity supplied to the ACT is delivered through the Canberra node and that there is no publicly available information on electricity loads for each of the nodes. Given this, the Commission will continue to use the marginal loss factor at the Canberra transmission node in its calculation of the cost allowance for energy losses.

The Commission’s final decision, therefore, is to calculate the cost allowance for energy losses using the formula in Box 2.2.

2.3.5 Energy Efficiency Improvement Scheme

The terms of reference for this price investigation require the Commission to identify and report on the efficient costs associated with compliance with the ACT Government’s Energy Efficiency Improvement Scheme (EEIS).

In the draft report, the Commission proposed to continue applying its current approach to estimating EEIS compliance costs for the next regulatory period, with the addition of a forward-looking assessment of the prudence and efficiency of ActewAGL Retail’s forecast abatement costs. The Commission found ActewAGL Retail’s forecast costs for 2014–15 of about \$41 per tonne of carbon dioxide equivalent gas emitted per megawatt hour (t CO₂-e per MWh), which translates to an allowance of \$4.92 per MWh for the EEIS, to be prudent and efficient.

Submissions on the draft report

The ACT Government stated that ActewAGL Retail’s forecast abatement costs of about \$41 t CO₂-e per MWh are higher than expected when compared with costs

³² AEMO, 2014b: 32.

incurred by retailers in comparable jurisdictional schemes. The ACT Government stated that:

From this perspective, it is not clear that this would reflect an ‘efficient cost’ in the context of a final determination by the Commission.³³

The ACT Government also indicated that it believes there are opportunities for ActewAGL Retail to purchase abatement from third-party providers in a more open-market setting that could deliver costs of abatement comparable to certificate-based schemes in Victoria and New South Wales.

The ACT Government disagreed with the Commission’s proposal to apply an ex ante prudence and efficiency assessment, stating that:

I continue to believe that a retrospective assessment and adjustment is desirable and consistent with the interest of ACT electricity customers.³⁴

ActewAGL Retail supported the Commission’s proposed ex ante approach to prudence and efficiency and draft conclusion that forecast expenditure on the scheme is prudent and efficient.³⁵ ActewAGL Retail also noted the uncertainty about the future cost of the scheme due to changes in abatement factors.

EnergyAustralia maintained the view it put forward in its issues paper submission that EEIS costs should be based on tier 1 retailers (ActewAGL Retail) except when the price paid by tier 2 retailers is higher. EnergyAustralia stated that:

It would be detrimental to competition if the EnergyAustralia scheme design and the price regulation approach were to prevent tier 2 retailers from recovering their full (efficient) costs under this scheme.³⁶

Commission’s consideration

Efficient costs

The ACT Government, in its submission, questioned the draft decision on the basis that ActewAGL Retail’s forecast abatement costs are higher than those costs incurred by retailers in comparable jurisdictional schemes. The submission did not provide any information to support this claim, but offered the support of the Environment and Sustainable Development Directorate (ESDD) to provide additional information.

In reviewing the prudence and efficiency of ActewAGL Retail’s forecast costs, the Commission examined ActewAGL Retail’s procurement process to choose a contractor to undertake field activities for the program. The Commission found that

³³ ACT Government, 2014: 2.

³⁴ ACT Government, 2014: 2.

³⁵ ActewAGL Retail, 2014: 12.

³⁶ EnergyAustralia, 2014: 7–8.

ActewAGL Retail undertook an open-market and competitive tender process to select the contractor to meet its EEIS compliance requirements. ActewAGL Retail received 17 tender submissions and selected the winning contractor as providing the best value for money. In addition, the Commission found that the proposed costs are well below the penalty rate cost ceiling of about \$7.06 per MWh. On this basis, the Commission concluded that the costs are efficient.

In coming to this conclusion, the Commission also benchmarked a number of similar jurisdictional schemes. The Commission found the benchmarking exercise of limited use for two reasons. First, there was limited information publicly available on the actual cost of the various schemes. Second, and perhaps more importantly, the schemes were not directly comparable with the ACT scheme either because they were based on trading certificates and/or were subject to different energy saving targets. The ACT Government foreshadowed this issue in its submission on the issues paper:

However, I do acknowledge that jurisdictional differences in schemes combined with other regulatory and market differences mean that these costs may not be directly comparable.³⁷

The Commission requested ESDD to provide any relevant cost information to support the ACT Government's position that that ActewAGL Retail's forecast abatement costs are not efficient. ESDD provided links to a number of reports and websites related to jurisdictional energy efficiency schemes. The Commission reviewed this information and, for two reasons, found no substantive basis to change the Commission's view on the benchmarking exercise undertaken for the draft report.

First, while additional data was provided on jurisdictional scheme costs, it has little comparative value as the methods used to estimate costs are not done on a like-for-like basis. One of the reports provided was the AEMC's 2013 report on electricity price trends. This presents a cost comparison for the energy efficiency schemes in New South Wales, Queensland, Victoria, South Australia and the ACT.³⁸ The ACT costs in this comparison are based on actual retailer costs, the New South Wales and Victorian costs are based on scheme penalty rates, and the Queensland costs are estimated using long-run marginal cost methods. The Commission has been unable to find any useful like-for-like comparison of jurisdictional scheme costs.

Second, even if a like-for-like cost comparison was available, there is still a fundamental issue of comparing the costs of jurisdictional schemes that are different in structure. For example, the New South Wales scheme is certificate based, which creates market incentives for organisations other than retailers to undertake abatement, which generates certificates. These certificates are then available for purchase by retailers to meet their energy efficiency obligations. In contrast, the ACT scheme is not

³⁷ ACT Government, 2013: 2.

³⁸ AEMC, 2013b.

certificate based, and essentially requires retailers to generate abatement activities themselves.

To conclude, ActewAGL Retail has provided the Commission with a firm basis for assessing efficient costs in the form of a competitive tender that resulted in a market-based cost for providing energy efficiency abatement services in the ACT. The additional benchmark information sourced from ESDD does not provide a corresponding basis for assessing efficient costs. The Commission's view remains that the forecast abatement costs submitted by ActewAGL Retail are efficient.

Ex ante versus ex post

The Commission has applied an ex ante rather than an ex post approach to assessing prudence and efficiency of the EEIS for two reasons. First, the Commission is setting a forward-looking EEIS allowance. This is consistent with the AEMC's advice on best practice retail price regulation, which recommends using forward-looking estimates of cost-index model parameters where available. Second, ActewAGL Retail has a contract for the provision of abatement activity services that locks in the costs per activity undertaken by the contractor. Given these contractual arrangements, an ex post assessment would arrive at the same result as an ex ante process.

The Commission has not been provided with any further argument sufficient to persuade it to change this conclusion.

Open-market opportunities

The Commission understands that section 14 of the *Energy Efficiency (Cost of Living) Improvement Act 2012* provides for liable retailers to meet their energy savings obligations by acquiring approved abatement factors as an alternative to the retailer directly undertaking the activities. The acquired abatement must relate to an eligible activity in the ACT.

The Commission has not been able to identify any eligible open-market opportunities for acquiring abatement from third-party providers in the ACT. Under the legislation, activities undertaken in other states do not qualify. What is clear, as the Commission concluded in the draft report, is that ActewAGL Retail undertook a rigorous and open-market tender process to select a contractor to directly implement the required EEIS activities.

Tier 1 and tier 2 costs

EnergyAustralia requested that the Commission set a floor for the EEIS cost allowance to reflect the higher of a tier 1 retailer's costs or the tier 2 retailer's costs. The Commission considered and rejected this request in the draft report. EnergyAustralia has not provided any further substantive argument to persuade the Commission to alter its draft decision.

Future abatement factors

In the draft report, the Commission noted the uncertainty in relation to the future costs of the scheme due to potential changes to the EEIS abatement factors:

The Commission understands that the scheme administrator is contemplating changes to the abatement factors to match changes being undertaken in the Victorian scheme on which the ACT scheme is based. The Commission will consider any new information on this matter that arises after the draft report is released and make necessary adjustments in the final decision.³⁹

On 22 April 2014, ESDD provided the Commission with the Scheme Administrator's decision on the revised abatement factors for stand-by power controllers that will apply in 2015. ActewAGL Retail advised the Commission that there is not sufficient time before the final price determination to revise its current EEIS compliance plan, and seek ACT Government approval of the plan, to take account of the revised factors. The Commission will therefore use ActewAGL Retail's current forecast costs and make any necessary cost adjustment at the 2014–15 price recalibration.

Final decision

The Commission's final decision is to:

- continue applying its current approach to estimating EEIS compliance costs for the next regulatory period, including a forward-looking assessment of the prudence and efficiency of ActewAGL Retail's forecast abatement costs, as described in Chapter 3 of the draft report;
- determine a prudent and efficient allowance of \$4.92 per MWh for 2014–15; and
- deal with cost uncertainty in relation to the abatement factors in the 2015–16 price reset as a cost adjustment following the Commission's usual practice.

2.3.6 Feed-in-tariff scheme

The terms of reference for this price investigation require the Commission to identify and report on the cost allowance of the ACT feed-in-tariff arrangements for the years or period for which the price determination is made.

In the draft report, the Commission noted that as ActewAGL Distribution's Transitional Regulatory Proposal for 2014–15 contained no information on jurisdictional scheme costs, including feed-in-tariff costs, the Commission was not in a position to report on these costs. The Commission indicated that it would report on feed-in-tariff costs in the final report.

³⁹ ICRC, 2014a: 154.

Submissions on the draft report

The submission from the ACT Government is the only submission that addressed the issue of the feed-in tariff. The ACT Government requested that period-specific information on the costs of the feed-in-tariff schemes be included in the final report on a per MWh basis and requested household impacts.

Commission's consideration

The terms of reference state:

The Commission must identify and report on the cost allowance of the ACT Feed-in Tariffs (small and large scale) for the year(s) or period for which its determination is being made.

In the draft report, the Commission stated that it could not at that point in time report on the cost allowance for the feed-in-tariff scheme as the information was unavailable. This is supported by the following quote from ActewAGL Distribution's transitional regulatory proposal to the AER:

ActewAGL Distribution wrote to the AER on 6 January 2014 requesting the AER to determine that the Energy Industry Levy, the Utilities Network Facilities Tax and the Feed-in Tariff (Large Scale) are jurisdictional schemes. On 29 January 2014, the AER published its determination that each of these schemes is a jurisdictional scheme. As a result, forecast amounts for the proposed jurisdictional schemes are not included in the indicative opex estimates for 2014–19.

Under the transitional provisions in clause 11.35.2(a) ActewAGL Distribution must comply with the jurisdictional scheme pricing proposal requirements from the date it is “required to submit a pricing proposal for the first regulatory period of the next regulatory control period.” ActewAGL Distribution will submit its proposal for recovery of jurisdictional scheme amounts as part of the 2014/15 Network Pricing Proposal.⁴⁰

The Commission will comply with the terms of reference and report the cost allowance for the feed-in-tariff scheme. The Commission is only able to report on the jurisdictional scheme costs for the 2014–15 regulatory year as this is the only year for which ActewAGL Distribution is required to report. The Commission cannot yet provide information on cost allowances for the feed-in-tariff scheme costs for 2015–16 and 2016–17. These costs will be identified and reported on as part of the annual recalibrations.

ActewAGL Distribution provided its 2014–15 network pricing proposal to the AER on 21 May 2014 and revised the proposal on 5 June 2014. The AER subsequently approved the revised proposal. The Commission used the approved proposal to identify the implied cost allowance for the feed-in-tariff scheme. This is reported in Chapter 3.

⁴⁰ ActewAGL Distribution, 2014b: 40.

2.3.7 Retail operating costs

In the draft report, the Commission reviewed its methodology for calculating retail operating costs. The Commission noted that it was not convinced of the need to adjust the retail operating cost allowance to reflect any potential cost disadvantage associated with economies of scale. However, the Commission found that, due to its decision to set the allowance on a per MWh basis rather than per customer basis from 2007–08, the ACT retail operating cost allowance of approximately \$107 per customer in 2013–14 is significantly below the allowances provided in Queensland, New South Wales and Tasmania when considered on a per customer basis.

In order to realign the ACT allowance with those of other jurisdictions that assess retail operating costs on a per customer basis, the Commission proposed a step-up in the per MWh allowance that would have applied in 2014–15 to match the allowance had the Commission continued assessing this cost on a per customer basis since 2007–08. This proposal resulted in an allowance of \$12.26 per MWh in 2014–15, a 7 per cent increase over the 2013–14 cost allowance of \$11.43 per MWh.

Submissions on the draft report

AGL Energy's submission on the draft report addressed the issues of the level of the retail operating costs and the existence and magnitude of economies of scale. AGL Energy noted that the Commission's step-up in the retail operating cost allowance still left the allowance below the retail operating cost allowances in New South Wales and Queensland.

On the issue of economies of scale, AGL Energy provided information on Australian Power and Gas (APG), which AGL Energy acquired in October 2013. AGL Energy noted that APG's operating costs per customer as of 30 June 2013 were \$252 per customer. AGL Energy claims that this figure is about \$130 per customer higher than AGL Energy's cost per customer. Overall, AGL Energy strongly disagrees with the Commission's assessment on the economies of scale issue.

In its submission, ActewAGL Retail made similar claims to those made by AGL Energy. ActewAGL Retail also noted that the Commission's step-up still resulted in a retail operating cost allowance below those in other jurisdictions. ActewAGL Retail was also concerned that there is no allowance for economies of scale. Finally, ActewAGL Retail noted that by not including any allowance for retaining customers, it is not recovering legitimate and appropriate costs of providing retail services in a competitive market.

Commission's consideration

The submissions identified three issues for consideration regarding the retail operating cost allowance. These issues are the relative level of the Commission's retail operating cost allowance compared to other jurisdictions, whether an adjustment for economies of scale should be included, and the merits of an allowance for customer acquisition and retention costs. These issues will be treated in turn.

Level of retail operating costs

Table 2.2 shows the comparative retail operating cost allowances across jurisdictions in 2014–15 as calculated by the Commission. The values for the ACT and New South Wales are equal to the 2013–14 cost allowances indexed by the current change in the consumer price index, which is 2.45 per cent.⁴¹ The cost allowance for Queensland is taken from the QCA’s December 2013 draft determination on regulated retail electricity prices for 2014–15.⁴² The retail operating cost allowance for New South Wales is estimated as the New South Wales Government announced on 7 April 2014 that retail electricity price regulation will be phased out over the next two years.⁴³ Hence, IPART will not be reporting a retail cost allowance for 2014–15.

Table 2.2 Retail operating cost allowance across jurisdictions 2014–15 (2014–15 prices)

\$ per customer per year	ACT	New South Wales	Queensland
Retail operating cost	114.40	114.68	119.56

Sources: ICRC (2014a); IPART (2013); QCA (2013).

As can be seen in Table 2.2, the Commission’s cost allowance is \$0.28 less than the estimated allowance IPART would have granted in New South Wales. The Commission’s allowance is \$5.16 less than the QCA’s allowance.

The difference between the Commission’s retail operating cost allowance and the New South Wales value is small. There is a significant difference between how the two cost allowances were determined. The Commission’s draft decision on the retail operating cost is equal to the 2007–08 retail operating cost allowance indexed to 2013–14. This resulted in the allowance of \$111.66 per customer in 2013–14 prices reported in the draft report. IPART, on the other hand, undertook a comprehensive review of retail operating costs in its 2013 investigation, which reported a retail operating cost allowance of \$110 per customer in 2012–13 prices.⁴⁴ IPART intended to index this figure for the expected three years of its price determination. The figures for the ACT and New South Wales shown in Table 2.2 are indexed values to 2014–15 prices of the Commission’s and IPART’s values.

The difference between the IPART and QCA retail operating cost allowances is attributable to treatment of late payment fees in the two jurisdictions. In 2013, IPART adopted \$110 per customer (2012–13 prices) for its retail operating cost allowance, which excluded an allowance of \$3.80 for late payment fees. The QCA benchmarked

⁴¹ The 2013–14 value for New South Wales (\$111.94 per customer) can be found in Table 3.5 of the Commission’s draft report. The value for the ACT (\$111.66 per customer) can be found in Table 3.6 of the draft report. Tasmania has adopted IPART’s determination for the retail operating cost allowance.

⁴² QCA, 2013: 33.

⁴³ O’Farrell, 2014: 1.

⁴⁴ IPART’s 2013 retail operating cost exercise did increase the cost allowance by 33 per cent from the amount granted in the previous price determination.

the IPART figure but included the \$3.80 as Queensland does not have an explicit late payment fee.

ActewAGL Retail does not collect late payment fees *per se* but does charge a disconnection notification fee to customers who have reached the end of the grace period for paying their electricity bills.⁴⁵ This grace period includes the time period from the original bill plus the time given on a bill reminder. This latter period is stated in the standard customer contract as not less than six business days.⁴⁶ Hence, the Commission's view is that ActewAGL Retail collects the equivalent of late payment fees as is done in New South Wales. The Commission will therefore use IPART's benchmark of \$110 per customer in 2012–13 prices.

Economies of scale

The Commission did not include an allowance for economies of scale in the draft report or in previous reviews. Economies of scale are defined as the reduction in average costs as output increases. If there are significant economies of scale in retail electricity, then businesses with a large number of customers will have lower per customer costs than businesses with a small number of customers. ActewAGL Retail and AGL Energy have claimed that ActewAGL Retail is too small to take advantage of economies of scale inherent in the provision of retail electricity services.

ActewAGL Retail's argument for the inclusion of an extra allowance for economies of scale rests on the claim that it is a small retailer relative to other retail electricity suppliers. ActewAGL Retail is much smaller than the three largest retail electricity suppliers, AGL Energy, Origin Energy, and EnergyAustralia. On the other hand, there are numerous small to medium-sized retail electricity providers competing for customers in the NEM as shown in Table 3.4 in the draft report. Many of these businesses are not much different than ActewAGL Retail in terms of number of customers and many of these businesses operate in most states in the NEM. If there were significant economies of scale, these businesses would be unable to compete with their larger rivals.

AGL Energy's evidence for the existence of economies of scale relies on the retail operating cost per customer of APG. AGL Energy cited APG's operating costs per customer as \$252 as of 30 June 2013, more than twice the Commission's proposed allowance in the draft report. APG is not an appropriate benchmark as it was running at a loss at that time.⁴⁷ From 30 June 2011 to 30 June 2013, APG's operational expenses, which were provided on an outsource arrangement, doubled, and its bad debt expense more than quadrupled, while its customer base only grew by 75 per cent.

⁴⁵ ActewAGL Retail, 2013a: 6.

⁴⁶ ActewAGL Retail, 2013b: 6.

⁴⁷ APG, 2013: 1.

The Commission remains unconvinced that there is a need for the inclusion of an extra allowance for economies of scale.

Customer acquisition and retention costs

While the Commission included a small element of retail competition-related costs in its 2003 cost benchmarking assessment, the Commission has never granted a separate allowance for customer acquisition and retention costs.

In the draft report, the Commission followed the view expressed by the AEMC in its review of best practice retail electricity price regulation:

The advice of the AEMC is that the competition allowance should encompass all the elements that may previously have been included to facilitate competition, such as customer acquisition and retention costs, adjustment of the retail margin or the calculation of cost estimates based on a hypothetical new entrant.⁴⁸

Given the Commission's decision not to include a competition allowance in the ACT, it follows that the Commission will not include any additional customer acquisition and retention costs.

Annual recalibration

In the draft decision, the Commission proposed adjusting the revised per MWh allowance by the change in the consumer price index at each annual price recalibration exercise. The Commission recognises that doing so could result in the per MWh allowance once again diverging from the benchmark per customer allowance. A better approach would be to adjust the per customer allowance by the change in the consumer price index and then convert this to a per MWh allowance at each annual price recalibration exercise.

Final decision

The Commission will adopt IPART's retail operating cost allowance of \$110 per customer in 2012–13 prices indexed to 2014–15. This cost allowance is converted into dollars per MWh in Chapter 3. The Commission's objective is to provide ActewAGL Retail with a retail operating cost allowance that is not below the standard industry benchmark. The Commission will not include an allowance for late payment fees – as QCA has done – as there is evidence that ActewAGL Retail is collecting a similar fee from tardy customers. The Commission has also not included an allowance for economies of scale. The Commission will adjust the per customer allowance by the change in the consumer price index and then convert this to a per MWh allowance at each annual price recalibration exercise.

⁴⁸ ICRC, 2014a: 7.

2.3.8 Retail margin

In the draft report, drawing on research undertaken for IPART by SFG Consulting, the Commission proposed a retail margin of 5.7 per cent for the next regulatory period. This results in an increase from the current retail margin of 5.4 per cent adopted in 2010.

The Commission uses an ex ante approach to calculating the retail margin cost allowance. It does this by multiplying the retail margin by total costs exclusive of any retail margin allowance. The Commission has calculated the retail margin allowance in this fashion since 2007. The Commission has also benchmarked the retail margin to that adopted by IPART over this time period.

Submissions on the draft report

In its submission, AGL Energy stated:

A significantly higher retail margin allowance should be considered for the ACT market given the lack of margin for error in its benchmarks for retail costs.⁴⁹

AGL Energy considers that the Commission's refusal to grant a competition allowance – unlike IPART or QCA – implies that the Commission should raise the retail margin above those granted in other jurisdictions.

ActewAGL Retail stated in its submission on the draft report that ActewAGL Retail faces similar systematic risks as regulated retail electricity businesses in other jurisdictions and should be granted a comparable retail margin. It pointed out that the Commission's approach is not consistent with the approach adopted in New South Wales and Queensland. In those jurisdictions, the retail margin cost allowance is calculated on an ex post basis. This ensures that the retail margin allowance as a percentage of total costs inclusive of the retail margin allowance is equal to the retail margin.

ActewAGL Retail demonstrated the difference between the ex ante and ex post approaches. Its calculations showed that the Commission's ex ante retail margin allowance of \$10.98 per MWh in the draft report would have been \$11.64 per MWh if the ex post approach was used.

Commission's consideration

The retail margin can be expressed in ex ante or ex post form as follows.

$$(1) \quad r_a = \frac{RMA}{CB}$$

$$(2) \quad r_p = \frac{RMA}{CB + RMA}$$

⁴⁹ AGL Energy, 2014: 3.

where:

r_a is the ex ante retail margin;

r_p is the ex post retail margin;

CB is the retailer's total cost build-up excluding the retail margin; and

RMA is the retailer's retail margin allowance.

To calculate the retail margin allowance for a given retail margin, these equations must be rearranged to express the retail margin allowance in terms of the retail margin and the cost build-up as follows:

$$(1a) \quad RMA = r_a \times CB$$

$$(2a) \quad RMA = \frac{r_p}{1 - r_p} \times CB$$

If the given retail margin is expressed in the ex ante form, the first equation is used. If the retail margin is expressed in the ex post form, the second is used.

In past determinations and the draft report, the Commission has used equation (1a), substituting the IPART benchmark retail margin for r_a . Since the IPART benchmark retail margin is expressed in the ex post form, this is incorrect and equation (2a) should have been used. For a given IPART benchmark retail margin, the effect was to provide a lower retail margin allowance.⁵⁰

The Commission agrees with ActewAGL Retail's submission that equation (2a) should be used to calculate the retail margin allowance in the final report.⁵¹ In order to ensure like-with-like comparisons are made in the proportionate change in the cost index, the Commission has also recalculated the retail margin allowance for 2013–14 using equation (2a).⁵²

The Commission's final decision is to apply a retail margin of 6.04 per cent in ex ante terms.⁵³ This is equivalent to a retail margin of 5.7 per cent applied ex post.

⁵⁰ This is because for $0 < r < 1$, $r/(1-r) > r$.

⁵¹ Comparing (1a) and (2a), it can be seen that treating the 5.7 per cent benchmark retail margin as expressed in ex post terms is equivalent to adopting an ex ante retail margin of 6.04 per cent, as noted in ActewAGL Retail's submission.

⁵² To see why this is necessary, consider the possibility that the retail margin has always been expressed in the ex post form, but has never changed. In this case, recognising that the retail margin is expressed in the ex post form and switching from (1a) to (2a) should have no effect on the proportionate change in the cost index at the time of the change because there has been no change in costs arising from a change in the retail margin consistently expressed.

⁵³ The Commission will apply an unrounded value in its calculation of the allowance. The 6.04 per cent rounded value is provided for presentational purposes.

2.3.9 Competition allowance

In the draft report, the Commission considered the case for the introduction of a competition allowance in the ACT. The Commission concluded that including a competition allowance at this time is not in the best interests of ACT electricity customers. The Commission noted that it is probable that any benefits it may produce will be long delayed and of little present value, and there is a distinct possibility that it will not produce benefits even in the long term.

The Commission considered that all customers in the ACT, large and small, are well served by the retail electricity market as it has developed here. The Commission proposed to continue its practice of not including such an allowance in the calculation of its cost-index model for the next regulatory period. The Commission acknowledged that the National Electricity Market (NEM) is in a continuing state of development and was of the view that monitoring of market developments should be maintained. Thus, the Commission came to the conclusion that, should market developments change markedly, further consideration of introducing a competition allowance may be warranted.

In examining the competition allowance issue, the Commission had regard to the AEMC's recent advice on best practice retail electricity price regulation. One of the key recommendations made by the AEMC is that, should a jurisdiction decide to promote competition, a separate and transparent competition allowance should be included on top of the efficient cost of supplying retail electricity services. The Commission, therefore, addressed the very specific question of whether to introduce a competition allowance in the ACT in the draft report.

Submissions on the draft report

All five submissions on the draft report commented on the issue of the inclusion of a competition allowance. Each of the electricity retailers was critical of the Commission's draft decision on this issue, whereas the ACT Government supported the draft report position of not granting a competition allowance.

The ACT Government noted that the Commission agreed with the ACT Government's view put forward in its submission on the issues paper. In that earlier submission, the ACT Government's argument for no competition allowance was:

Previous investigations, including those undertaken by ICRC and AEMC, indicate that the regulated price is not a critical impediment to the development of competition in the ACT. Instead they note the size of the market, high levels of consumer satisfaction with existing services and a well known local brand as impediments. An allowance for competition will not address these issues. The failure of significant competition to develop in the gas retail market, where prices are not regulated, is noteworthy in this regard.⁵⁴

⁵⁴ ACT Government, 2014: 2.

The submissions by the electricity retailers all maintained that some form of support for competition was needed in the ACT in order for competition to blossom in the Territory.

ActewAGL Retail reiterated its position that it has incurred, and will continue to incur, customer acquisition and retention costs as it faces potential competition. ActewAGL Retail stated:

Under the Commission’s proposed price direction, ActewAGL Retail is not recovering legitimate and appropriate commercial costs of providing retail services in a competitive market.⁵⁵

Thus, ActewAGL Retail believe that by not granting customer acquisition and retention costs, the Commission is not allowing it to recover its efficient costs of providing retail electricity services in the ACT.

Most of the electricity retailers’ submissions claimed that a competition allowance was necessary for competition to become effective in the ACT and that the ACT Government was not acting in accordance with agreements made within the remit of the Council of Australian Governments (COAG) energy reform process.

As an example, EnergyAustralia stated in its conclusion on this issue:

In addition, it is hard to understand why the ACT Government is going against the commitment made by all states at COAG/SCER around moving towards price deregulation in retail energy markets.⁵⁶

On this issue, Origin stated:

We are concerned that the ICRC may have departed from its legislated role to promote effective competition, undertaking a theoretical analysis of whether greater retail competition is *prima facie* desirable and using this as a basis for rejecting a customer acquisition allowance.⁵⁷

Origin was critical of the Commission’s theoretical analysis of the retail electricity market and the Commission’s evidence that retail electricity prices are lower in the ACT than in New South Wales and Victoria.

However, we would highlight that by re-opening debates about the benefits of competition in retail electricity markets and by positing a special status for retail electricity markets with respect to the benefits of competition in markets generally, the ICRC runs counter to over a decade of concerted reform in the energy sector,

⁵⁵ ActewAGL Retail, 2014: 10.

⁵⁶ EnergyAustralia, 2014: 11.

⁵⁷ Origin, 2014: 1.

championed by successive Federal and state governments across Australia and agreed by the Council of Australia Governments in the Australia Energy Market Agreement.⁵⁸

and

We reject the notion put forward in the ICRC's analysis that the electricity market has special characteristics whereby prices set by regulators will be more efficient than prices set under effective competition. We acknowledge that no approach to price discovery is perfect, but maintain that regulated pricing in an environment of negligible competition is a model replete with cost and risk. We also reject the notion that because prices are lower in the ACT than some prices in deregulated jurisdictions that ACT residents are benefiting from an efficient price or that the current pricing model is sustainable over the medium term.⁵⁹

Commission's consideration

In the draft report, the Commission assessed whether a competition allowance in the ACT should be included in the regulated retail tariff. In doing so, it followed the approach outlined by the AEMC to assess an allowance in addition to the efficient costs of the incumbent retailer. The Commission did not address the broader issue of whether there should be competition in the retail electricity market.

The Commission examined the retail electricity market and found that there are aspects of the market that, when applied to current ACT circumstances, raise doubts about the likelihood that a competition allowance would provide benefits to ACT consumers at this time. These doubts include the effect of increased customer switching on a retailer's hedging costs, the imperfections in observed consumer behaviour driven by search costs or brand loyalty, and the effect that vertical integration will have on market outcomes. After considering all of the evidence, the Commission came to the view that a competition allowance may not improve consumers' welfare. As the Commission stated in its draft report:

If prices do initially rise by the full amount of the competition allowance, it is not clear if there is enough scope within the cost structure of a typical retailer to effect economies sufficient to offset the effects of the higher costs of sustaining competition. If there are, it seems very likely that it will be some considerable time before they materialise.⁶⁰

The Commission examined the process by which competition improves the welfare of consumers as well as the conditions required to improve consumers' welfare. The Commission does not reject the notion that competition may provide significant net benefits in the future. However, the Commission is not satisfied that the inclusion of a competition allowance in the cost benchmark, which would have the effect of

⁵⁸ Origin, 2014: 3.

⁵⁹ Origin, 2014: 4.

⁶⁰ ICRC, 2014a: 136.

immediately increasing the regulated retail price above its assessed efficient level, is likely to improve the welfare of ACT consumers.

The Commission also notes Origin's concern that the Commission is not following the objectives of the ICRC Act in relation to promoting competition. The first objective in section 7 of the ICRC Act requires the Commission to promote competition only when it is in the best interests of consumers to do so. The Commission has determined that introducing a competition allowance at this time is not in the best interests of ACT consumers.

Final decision

The Commission's final decision is to not include an allowance for competition on top of its build-up of efficient costs for the upcoming regulatory period.

2.3.10 Cost-index model summary

Table 2.3 provides a summary of the Commission's final decisions on the components of the electricity cost-index model to be applied for the regulatory period commencing 1 July 2014.

Table 2.3 Final decisions on the retail electricity cost-index model

Component	Method
Wholesale energy costs	
Energy purchase cost	Use the energy purchase cost model set out in Appendix 3 of the draft report, averaging the forward price and carbon emissions intensity factor over 23 and 12 months, respectively For the annual recalibrations, the cost of carbon is not added to the carbon-exclusive energy purchase cost
LRET and SRES costs	Base the price of LGCs and STCs on publicly available spot price data averaged over an 11-month period and include an allowance for funding costs as set out in section 3.5 of the draft report
Energy losses cost	Use the formula set out in section 2.3.4
Energy contracting costs	Adjust the energy contracting costs by the annual change in the CPI
NEM fees	Adjust NEM fees by the annual change in the CPI
Retail costs	
Retail operating costs	Provide for step-up for 2014–15 to match the IPART benchmark and then adjust the per customer retail operating cost allowance by the annual change in the CPI
Energy Efficiency Improvement Scheme costs	Subject costs to prudence and efficiency assessment and then apply the formula set out in section 3.10 of the draft report
Network costs	
Retail margin	Use a formula for the retail margin expressed in ex post terms, equivalent to a margin of 6.04 per cent measured ex ante
Competition allowance	n.a.

2.4 Pass-through arrangements

The current price direction that ends on 30 June 2014 provides for:

- pass-through reviews for regulatory and tax change events within-year as well as during the annual price reset process;
- the ability for both the Commission and ActewAGL Retail to initiate a pass-through review; and
- an aggregate materiality threshold of 0.25 per cent of annual regulated revenue.

In the draft report, the Commission proposed restricting regulatory and tax change pass-through reviews to the annual recalibration process. The Commission also proposed making the symmetric provision for the both the Commission and ActewAGL Retail to initiate a pass-through review more transparent. The Commission did not contemplate any change to the materiality provision.

2.4.1 Submissions on the draft report

ActewAGL Retail did not support the Commission's proposal to only allow regulatory and tax change pass-throughs as part of the annual recalibration process, stating:

Requiring all pass through events be lodged as part of the annual reset process removes a potential mechanism to ensure prices reflect the costs of unforeseen events that are beyond ActewAGL Retail’s control as soon as possible.⁶¹

ActewAGL Retail also raised two concerns in relation to the Commission’s symmetric pass-through initiation mechanism. The first concern was the lack of any explicit requirement for the Commission to give notice to ActewAGL Retail that it is considering a pass-through review. The second concern was the lack of any means for ActewAGL Retail to respond to a potential review. ActewAGL Retail recommended that the Commission consider including a mechanism that:

- provides ActewAGL Retail with sufficient notice that the Commission has initiated a pass-through event;
- discloses to ActewAGL Retail material that is relevant or to be relied on in the Commission’s decision; and
- gives ActewAGL Retail an opportunity to provide a submission responding to the material before the Commission.⁶²

ActewAGL Retail also maintained its long-held view that a materiality threshold for pass-through events is not warranted on the basis that such events are outside of ActewAGL Retail’s control, and stated:

Accordingly, it would be unreasonable for a specific threshold to apply as prices cannot adjust to reflect changes in cost occurring in an open market environment.⁶³

2.4.2 Commission’s consideration

Timing of pass-through events

In the draft report, the Commission stated that restricting pass-through events to the annual price reset process will reduce the administrative burden associated with the additional effort required for within-year reviews.

In response to ActewAGL Retail’s concerns about the potential to delay price adjustments necessary to reflect cost changes beyond its control, the Commission will take into account the full costs or benefits from the date of the pass-through event when calculating the pass-through allowance. This is detailed in section 2.4.3.

In addition, should ActewAGL Retail face any external event beyond its control with material cost implications, section 24E of the ICRC Act provides ActewAGL Retail with the ability to trigger a reference for a variation of the price direction. This effectively provides a fallback position should ActewAGL Retail find itself in a

⁶¹ ActewAGL Retail, 2014: 15.

⁶² ActewAGL Retail, 2014: 15–16.

⁶³ ActewAGL Retail, 2014: 16.

position that threatens its financial viability due to a within-year regulatory or tax change event that cannot be processed until the next annual price reset.

On balance, the Commission's final decision is to maintain its draft position and restrict regulatory and tax change pass-through reviews to the annual recalibration process.

Commission-initiated pass-through review process

Clause 8.1.4 of the proposed price direction provides for the Commission to initiate a regulatory or tax change pass-through event in the absence of an application from ActewAGL Retail.⁶⁴ The Commission agrees that the mechanism permitting the Commission to initiate and determine a pass-through event should clearly provide for participation by ActewAGL Retail. The Commission will amend the arrangements to require the Commission to:

- advise ActewAGL Retail that it is intending to initiate a pass-through review as part of an annual recalibration process;
- provide ActewAGL Retail with a document outlining the Commission's proposed review decision, including relevant material on which the decision is based; and
- provide ActewAGL Retail with the opportunity to respond to the Commission's proposed decision.

Materiality threshold

As the annual recalibration of the cost-index model parameters does not have a materiality consideration, it is not appropriate for consistency reasons to apply it to possible pass-throughs that can now only occur as part of an annual reset process. The Commission's final decision is to remove the pass-through materiality threshold.

2.4.3 Pass-through arrangements summary

Event description

A regulatory change event is a decision made on or after 31 May 2014 and before 30 June 2017 by any 'authority' (any government or any minister, agency or directorate, instrumentality or other authority of government and the Commission, the AEMC, the AER or AEMO) that has the extent of materially varying the nature, scope, standard or risk of providing services to regulated retail tariff customers, or the manner in which those services are provided. A regulatory change event includes obligations in respect of:

- any customer hardship program;
- retailer of last resort events;

⁶⁴ ICRC, 2014b: 9.

- environmental schemes, including the LRET and SRES and the Energy Efficiency Improvement Scheme; and
- changes in distribution or transmission charges.

A regulatory change event does not include obligations in respect of:

- any decision, determination or ruling in relation to energy loss factors; and
- smart-metering trials.

A tax change event means the imposition of a relevant tax, the removal of a relevant tax, or a change in the way a relevant tax is interpreted or calculated. A relevant tax is any tax, levy, impost, deduction, charge, rate, duty or withholding tax that is levied on ActewAGL Retail by any authority (as defined above) and is payable by ActewAGL Retail, other than:

- income tax and capital gains tax;
- stamp duty;
- AEMO fees;
- fees payable by ActewAGL Retail in respect of its retail licence;
- penalties, charges, fees and interest on late payments, or deficiencies in payments, relating to any tax; and
- any tax that replaces or is equivalent or similar to any of the taxes referred to above (including any state-equivalent tax).

Initiation and timing of review and price adjustment

ActewAGL Retail and the Commission may initiate a regulatory change or tax change pass-through event review. ActewAGL Retail may make an application to the Commission and the Commission may initiate a pass-through review for a regulatory change or tax change event when the Commission is undertaking the annual price recalibration process for 2015–16 and 2016–17.

The Commission will notify ActewAGL Retail in advance of initiating a review and provide ActewAGL Retail with an opportunity to respond to the Commission’s review findings before making a final decision on the pass-through event.

Calculating the pass-through amount

The Commission will calculate the pass-through amount when considering a pass-through event as part of an annual recalibration process, having regard to the following matters:

- the implications for the efficient costs of ActewAGL Retail’s actions, including whether ActewAGL Retail has taken or omitted to take any action where such action or omission has increased the magnitude of the costs incurred;

- the need to ensure that ActewAGL Retail does not recover costs to the extent that provisions have already been made or otherwise taken into account;
- the need to ensure that ActewAGL Retail recovers only any actual or likely increment in efficient costs to the extent that such an increment is solely a consequence of a pass-through event from the date the event occurred;
- in the case of a regulatory change event, any costs that ActewAGL Retail has incurred prior to, but in preparation for, the occurrence of that regulatory change event; and
- in the case of a tax change event, any change in the way another tax is calculated, or the removal or imposition of another tax which in the Commission’s opinion is complementary to the tax change event concerned.

In addition, in considering any pass-through event, the Commission may consult with affected stakeholders to the extent the Commission considers appropriate.

For a regulatory change or tax change pass-through event that occurs during 2014–15 or 2015–16, the Commission will include the value of the pass-through event, which can be either negative or positive when determining the maximum average price change, in the cost-index model.

2.5 Price variation triggers

In section 9 of the proposed price direction, the Commission proposed five price direction variation trigger events that are not present in the current price direction. The proposed events were:

- (a) an act of terrorism;
- (b) a major natural disaster;
- (c) a significant change to ActewAGL Retail’s financial or corporate structure;
- (d) an unforeseen or force majeure event that severely restricts ActewAGL Retail’s ability to provide services; or
- (e) a change, or changes, made on or after 31 May 2014 and before 30 June 2017 to the price-on-carbon arrangements set out in the Clean Energy Act where the change(s) cannot be passed through under Part B and its subclauses.

2.5.1 Submissions on the draft report

ActewAGL Retail requested an explanation for the inclusion of the additional price variation triggers in the proposed price direction. ActewAGL Retail also stated:

If the Commission prefers a price variation trigger for changes to carbon arrangements, ActewAGL Retail considers that further detail on what is intended should be provided.⁶⁵

2.5.2 Commission's consideration

First four triggers

The ICRC Act provides ActewAGL Retail with the ability to trigger a variation of the price direction. Section 24C of the ICRC Act allows for variations, which require the consent of the Commission. As noted in section 2.4.2 of this report, section 24E of the ICRC Act provides for a nonconsent variation should ActewAGL Retail face any external event beyond its control with material cost implications.

Section 24F of the ICRC Act allows the Commission to initiate, at its own discretion, a reference for a variation of the price direction. However, clause 2 of section 24F limits the Commission to initiating a variation when a price variation trigger that is listed in the price direction has occurred. Therefore, to provide the Commission with a symmetric ability to trigger price direction variations, trigger mechanisms in the price direction are required. It is for this reason that the Commission included the first four of the five proposed triggers. The Commission also notes that these triggers are consistent with those included in clause 11 of the current Regulated Water and Sewerage Services Price Direction.⁶⁶

Price-on-carbon trigger

As discussed in section 2.1, the contingent pricing mechanism relies on there being no price on carbon following the repeal of the Clean Energy Act. Should the foreshadowed repeal legislation, or any replacement carbon reduction policy, result in some non-zero price on carbon, the price-on-carbon trigger will permit the Commission to vary the price direction to ensure that the price on carbon is properly accounted for in the retail electricity price. This trigger allows the price direction to be varied where the contingent pricing mechanism is not applicable.

If this particular trigger occurs, the Commission will initiate a reference for a price variation. The reference will be limited to determining how the new price-on-carbon arrangements can be best incorporated into the Commission's cost-index model to ensure that regulated prices accurately reflect the new arrangements.

The Commission has adjusted the wording of the trigger in the price direction to reflect the Commission's decision, discussed in section 2.3.2, to provide for a contingent pricing mechanism rather than the pass-through arrangements proposed in the draft report.

⁶⁵ ActewAGL Retail, 2014: 4.

⁶⁶ ICRC, 2013a: 13.

Cost-index model trigger

The Commission has included another broader trigger event that relates to the effect of any legislative provision or government policy that causes any component of the Commission's cost-index model to become unworkable. For example, should the Clean Energy Act remain in force in its current form in 2015–16, the price on carbon will be set through an emissions trading scheme which would render the current energy purchase cost component of the cost-index model unworkable. This trigger mechanism would permit the Commission to vary the price direction to ensure that the price on carbon under an emissions trading scheme is properly accounted for in the retail electricity price.

The Commission's final decision is to include the five price direction variation trigger events proposed in the draft report and the additional cost-index model trigger event discussed above, as set out below:

- (a) an act of terrorism;
- (b) a major natural disaster;
- (c) a significant change to ActewAGL Retail's financial or corporate structure;
- (d) an unforeseen or force majeure event that severely restricts ActewAGL Retail's ability to provide services;
- (e) a change, or changes, made on or after 31 May 2014 and before 30 June 2017 to the price-on-carbon arrangements set out in the Clean Energy Act or the introduction of any new Australian Government carbon reduction legislation or policy that results in a non-zero price on carbon; and
- (f) the cost-index model, its components or the determination of Y^t under clause 8 becoming unworkable due to a legislative provision, government policy or other cause (or any number or combination of the aforementioned).

2.6 Form of regulation summary

The Commission's final decisions on the form of regulation for the next regulatory period are summarised in Table 2.4.

Table 2.4 Commission's final decisions on the form of regulation

Component	Draft decision
Length of regulatory period	Three years (specified in the terms of reference)
Form of price control	Weighted average price cap where the allowed change in the average price is constrained by the change in the Commission's cost-index model
Timing of price control	Annual recalibration of the parameters of the retail electricity cost-index model to determine regulated retail prices for 2015–16 and 2016–17
Cost pass-through arrangements	Regulatory and tax change pass-through events reviewed as part of the annual recalibration process
Trigger events	<p>The following trigger events are included:</p> <ul style="list-style-type: none"> • act of terrorism; • major natural disaster; • significant change to ActewAGL Retail's financial or corporate structure; • unforeseen or force majeure event that severely restricts ActewAGL Retail's ability to provide services; • changes to the price-on-carbon arrangements under the Clean Energy Act or the introduction of any new Australian Government carbon reduction legislation or policy that result in a non-zero price on carbon; and • the cost-index model becoming unworkable due to a legislative provision, government policy or other cause.

3 Setting the regulated electricity price for 2014–15

3.1 Introduction

This chapter sets out the efficient costs of supplying electricity to customers on standard retail contracts in 2014–15, the first year of the next regulatory period. The chapter concludes with the Commission’s final decision on the efficient costs and their constituent components and the allowed percentage change that will apply in the weighted average price cap for 2014–15.

3.2 Energy purchase cost

3.2.1 Forward price

The forward price is calculated using carbon-exclusive contracting data provided by ICAP. The forward price for 2014–15 has been calculated over a 23-month averaging period from 1 July 2012 to 31 May 2014. ICAP provides annual financial year contract data, while the Commission’s energy purchase cost model is constructed on a quarterly timeframe. Because of this difference, the Commission has adopted a single annual forward price for the relevant financial year rather than individual quarterly prices.

Table 3.1 shows the forward prices for each calendar year quarter for the 2013–14 and 2014–15 financial years, as calculated by the Commission.

Table 3.1 Quarterly forward prices 2013–14 and 2014–15 (dollars per MWh)

Year	Q3	Q4	Q1	Q2
2013–14	39.77	39.77	39.77	39.77
2014–15	41.03	41.03	41.03	41.03

Source: Commission’s calculations based on ICAP data.

3.2.2 Uplift factor

Load shape

The load shape captures the relationship between the spot price and electricity load. The load shape is calculated using New South Wales spot prices and the net system load profile for ActewAGL Distribution, both reported by AEMO.

The quarterly average load shape for 2013–14 and 2014–15 is shown in Table 3.2, and the underlying quarterly load shape data from 2003–04 through 2013–14 is presented in Table 3.3.

Table 3.2 Quarterly average load shape 2013–14 and 2014–15

Year	Q3	Q4	Q1	Q2
2013–14 (average 2003–04 through 2012–13)	1.120	1.096	1.246	1.125
2014–15 (average 2003–04 through 2013–14)	1.113	1.093	1.225	1.117

Source: Commission's calculations using data from AEMO load profiles and AEMO aggregated price and demand data files.

Table 3.3 Quarterly load shape 2003–04 through 2013–14

Year	Q3	Q4	Q1	Q2
2003–04	1.251	1.043	1.192	1.104
2004–05	1.148	1.164	1.207	1.082
2005–06	1.114	1.149	1.360	1.145
2006–07	1.161	1.080	1.207	1.387
2007–08	1.134	1.075	1.105	1.100
2008–09	1.123	1.096	1.294	1.119
2009–10	1.086	1.254	1.254	1.109
2010–11	1.067	1.024	1.561	1.036
2011–12	1.047	1.032	1.035	1.043
2012–13	1.065	1.040	1.032	1.048
2013–14	1.044	1.070		

Source: Commission's calculations using data from AEMO load profiles and AEMO aggregated price and demand data files.

An implication of using carbon-exclusive, over-the-counter contract prices is the need to base all load shape calculations after 1 July 2012 on the carbon-exclusive contract price. This ensures consistency within the assumptions underlying the energy purchase cost model. Hence, the cost of carbon has been subtracted from all half-hour spot prices before calculating the load shape for 2013–14 and 2014–15.

Load ratio

The load ratio for each quarter is calculated as the maximum of the observed ratio of the quarterly maximum load to the quarterly average load using AEMO data. To complete the calculation of the load ratio, the Commission adds 0.1 to the observed maximum to allow for the possibility of a higher peak. The load ratio for 2013–14 and 2014–15 and the underlying load data are shown in Table 3.4.

Table 3.4 Quarterly load ratio 2013–14 and 2014–15

Year	Q3	Q4	Q1	Q2
2003–04	1.786	2.156	1.702	2.013
2004–05	1.828	1.905	1.724	2.108
2005–06	1.808	1.960	1.888	2.063
2006–07	1.768	1.801	1.885	2.148
2007–08	1.927	1.708	1.891	1.863
2008–09	1.746	1.821	2.250	2.061
2009–10	1.764	2.172	2.236	2.196
2010–11	1.754	1.975	2.440	2.115
2011–12	1.868	2.137	2.039	2.001
2012–13	1.815	2.489	2.469	2.261
2013–14	2.030	2.193		
Maximum through Q4 2012–13	1.927	2.489	2.440	2.196
Maximum through Q4 2013–14	2.030	2.489	2.469	2.261
Load ratio 2013–14	2.027	2.589	2.540	2.296
Load ratio 2014–15	2.130	2.589	2.569	2.361

Source: Commission's calculations using data from AEMO load profiles.

Load weights

Quarterly load weights are required to calculate the annual average energy purchase cost. The load weight for each quarter is equal to the historical average load in that quarter divided by the sum of the historical average load for all four quarters. The historical average load for a quarter is the simple average of the loads for that quarter for the period 2003–04 through 2013–14. The load used is the net system load profile for ActewAGL Distribution as reported by AEMO. The quarterly load weights for 2013–14 and 2014–15 are shown in Table 3.5.

Table 3.5 Quarterly load weights 2003–04 through 2013–14

Year	Q3	Q4	Q1	Q2
2003–04	109.621	71.384	64.911	93.947
2004–05	108.849	68.535	65.910	90.063
2005–06	110.759	70.952	70.791	104.097
2006–07	109.656	70.494	70.773	95.027
2007–08	110.995	68.837	68.338	94.735
2008–09	114.401	67.694	70.945	96.657
2009–10	109.033	73.936	68.545	94.249
2010–11	111.748	66.593	63.059	94.546
2011–12	102.113	62.356	59.446	94.205
2012–13	101.811	59.272	58.250	85.369
2013–14	95.348	59.536		
Average through Q4 2012–13	108.899	68.005	66.969	95.281
Average through Q4 2013–14	107.667	67.235	66.097	94.327
Load weights 2013–14	0.321	0.201	0.197	0.281
Load weights 2014–15	0.321	0.201	0.197	0.281

Source: Commission's calculations using data from AEMO load profiles.

3.2.3 Cost of carbon

The cost of carbon is equal to the price on carbon multiplied by the emissions intensity factor. AEMO calculates and reports the daily emissions intensity as the carbon-dioxide-equivalent intensity index measured in t CO₂-e per MWh. The Commission has applied a 12-month averaging period ending as near as possible to 31 May 2014 for determining the final emissions intensity factor. The emissions intensity factor is the average of the daily emissions intensity as reported by AEMO. The NEM daily emissions intensity index has been used.

The price on carbon under the Clean Energy Act for 2014–15 is \$25.40. Table 3.6 presents the cost of carbon calculations for 2013–14 and 2014–15.

Table 3.6 Cost of carbon 2013–14 and 2014–15

Year	Price on carbon (\$/t CO ₂ -e)	NEM emissions intensity factor (t CO ₂ -e/MWh) ^a	Cost of carbon (\$/MWh)
2013–14	24.15	0.875	21.13
2014–15	25.40	0.866	21.99

Sources: *Clean Energy Act 2011*; AEMO data.

Note: ^a The 2013–14 emissions intensity factor has been recalculated from that contained in the 2013–14 price reset using a 12- rather than 14-month averaging period.

3.2.4 Energy purchase cost for 2013–14 and 2014–15

Table 3.7 shows the energy purchase cost calculated for 2013–14 in the Commission’s previous determination.

Table 3.7 Energy purchase cost 2013–14

Component	Q3	Q4	Q1	Q2
Forward price (\$/MWh) (A) ^a	40.95	40.95	40.95	40.95
Load shape (B)	1.12	1.10	1.25	1.13
Load ratio (C)	2.03	2.59	2.54	2.30
Forward price margin (D)	0.05	0.05	0.05	0.05
Uplift factor (E = (1 – D) × B + D × C)	1.16	1.17	1.31	1.18
Energy purchase cost (\$/MWh) (A × E)	47.71	47.94	53.69	48.48
Annualised load-weighted energy purchase cost				
				Carbon-exclusive
				49.15
				Carbon-inclusive
				70.28

Source: ICRC (2013b): 9.

Note: a The 2013–14 energy purchase cost amount has been recalculated from that contained in the 2013–14 price reset due to the adjustments to the forward price and carbon emissions intensity factor averaging periods and the Commission’s desire to maintain comparability across adjacent years under the index approach.

Table 3.8 shows the calculated draft energy purchase costs for 2014–15. The quarterly load weights from Table 3.5 are multiplied by the quarterly energy purchase cost in Table 3.8 and summed to give the 2014–15 annual carbon-exclusive energy purchase cost of \$49.00 per MWh. The cost of carbon of \$21.99 per MWh was added to the carbon-exclusive amount to provide the 2014–15 carbon-inclusive energy purchase cost of \$70.99 per MWh. This is \$0.71 per MWh more than in 2013–14.

Table 3.8 Energy purchase cost 2014–15

Component	Q3	Q4	Q1	Q2
Forward price (\$/MWh) (A)	41.03	41.03	41.03	41.03
Load shape (B)	1.11	1.09	1.22	1.12
Load ratio (C)	2.13	2.59	2.57	2.36
Forward price margin (D)	0.05	0.05	0.05	0.05
Uplift factor (E = (1 – D) × B + D × C)	1.16	1.17	1.29	1.18
Energy purchase cost (\$/MWh) (A × E)	47.74	47.93	53.01	48.39
Annualised load-weighted energy purchase cost				
				Carbon-exclusive
				49.00
				Carbon-inclusive
				70.99

Source: Commission’s calculations.

3.3 Large-scale Renewable Energy Target and Small-scale Renewable Energy Scheme costs

The costs of complying with the national LRET and SRES requirements are calculated in this section using the market approach set out in Chapter 3 of the draft report. Key data inputs into the cost calculations are provided in Table 3.9.

Table 3.9 Large-scale Renewable Energy Target and Small-scale Renewable Energy Scheme data 2014 and 2015

	2014	2015
Renewable power percentage	9.87%	10.52%
Average LGC spot price (\$/certificate)	36.14	31.15
Small-scale technology percentage	10.48%	10.10%
Average STC spot price (\$/certificate)	32.22	38.60
Half-yearly load weights	0.528	0.472

Sources: Clean Energy Regulator; ICAP data; ActewAGL Retail half-yearly load weight data.

The draft LRET and SRES costs for 2013–14 and 2014–15 are summarised in Table 3.10.

Table 3.10 Large-scale Renewable Energy Target and Small-scale Renewable Energy Scheme costs 2013–14 and 2014–15 (dollars per MWh)

	2013–14	2014–15
LRET	4.44	3.96
SRES	5.10	4.18
Cost adjustment from previous year	2.12	0.34
Total cost	11.66	8.49

Source: Commission's calculations.

The average price of LGCs for calendar year 2014 is \$36.14. The price of LGCs for calendar year 2015, averaged over the 11-month period from 1 July 2013 to 31 May 2014, is \$31.15. This increases to \$34.26 when adjusted by 10 per cent for the opportunity cost of holding certificates over a 12-month period. The renewable power percentage for 2014 is 9.87 per cent and estimated at 10.52 for 2015.⁶⁷ This generates a draft LRET allowance for 2014–15 of \$3.96 per MWh.

For the SRES, the average price of STCs for calendar year 2014 is \$32.22. The price of STCs for calendar year 2015, averaged over the 11-month period from 1 July 2013 to 31 May 2014, is \$38.60. This becomes \$42.46 when adjusted for the holding cost. The

⁶⁷ See <http://ret.cleanenergyregulator.gov.au/About-the-Schemes/About-the-renewable-power-percentage/About-the-renewable-power-percentage>. As the Clean Energy Regulator has not published a binding estimate for 2015, the current non-binding estimate of 10.52 per cent for 2015 has been used.

small-scale technology percentage for 2014 is 10.48 per cent and is estimated at 10.10 per cent for 2015.⁶⁸ This generates a draft SRES allowance for 2014–15 of \$4.18 per MWh.

The Commission's approach allows for a cost adjustment resulting from any difference between the actual 2014 small-scale technology percentage and renewable power percentage and the forecast numbers used in the 2013–14 decision. ActewAGL Retail submitted an adjustment factor of \$0.34 per MWh for LRET and SRES costs for 2013–14 to be included in 2014–15 costs.⁶⁹ The Commission agrees with ActewAGL Retail's estimate, and has included this amount in the LRET and SRES cost allowance for 2014–15 costs.

The total LRET and SRES cost allowance for 2014–15 is \$8.49 per MWh. This is \$3.17 per MWh less than the allowance for the previous year.

3.4 Energy losses

The distribution loss factor as reported by AEMO for 2014–15 is 1.0438.⁷⁰ The marginal loss factor as reported by AEMO for the Canberra connection point in 2014–15 is 0.9642.⁷¹ Using the formula in Box 2.2 generates an energy loss allowance of \$0.87 per MWh for 2014–15. This is about 77 per cent less than the energy losses component granted in 2013–14. The main reason for this is the reduction in the marginal loss factor over this period.

3.5 Energy contracting costs

The energy contracting cost allowance is adjusted by the annual change in the consumer price index. The Commission has calculated an allowance of \$0.84 per MWh for energy trading and management costs for 2014–15. This is based on an adjustment of the 2013–14 cost allowance of \$0.82 per MWh for a change of 2.45 per cent in the consumer price index.

3.6 National Electricity Market fees

The cost allowance for NEM fees is adjusted by the annual change in the consumer price index. The Commission has calculated an allowance of \$0.84 per MWh for NEM fees for 2014–15. This is based on an adjustment of the 2013–14 cost allowance of \$0.82 per MWh for a change of 2.45 per cent in the consumer price index.

⁶⁸ See <http://ret.cleanenergyregulator.gov.au/For-Industry/Liable-Entities/stp>.

⁶⁹ ActewAGL Retail, 2014: 8.

⁷⁰ AEMO, 2014a: 16.

⁷¹ AEMO, 2014b: 32.

3.7 Retail operating costs

As discussed in section 2.3.7, the Commission has decided to increase the retail operating cost allowance per customer to match the IPART benchmark of \$110 per customer in 2012–13 prices. This is \$114.68 in 2014–15 prices. This value is converted into an allowance of \$13.57 per MWh for retail operating costs for 2014–15 using customer numbers and energy usage for the year to 31 March 2014 provided by ActewAGL Retail. This represents a 19 per cent increase over the 2013–14 cost allowance of \$11.43 per MWh.

The allowance of \$12.26 per MWh proposed in the draft report was calculated using customer number and energy usage data to 31 March 2013. The final allowance of \$13.57 per MWh has been calculated using updated information. The new data shows a significant decrease in the average per customer energy usage. This has resulted in a higher per MWh allowance than proposed in the draft report.

3.8 Energy efficiency scheme costs

As discussed in section 2.3.5, having reviewed ActewAGL Retail's proposed expenditure, activities and expenditure processes, the Commission is satisfied that ActewAGL Retail's forecast expenditure on the EEIS is prudent and efficient. The Commission has therefore granted an EEIS cost allowance of \$4.92 per MWh for 2014–15. This is 31 per cent more than the allowance of \$3.75 per MWh granted for 2013–14.

3.9 Network cost allowance

Consistent with the draft decision, as network costs are unavoidable for all retail businesses, the Commission has in its final decision passed through the network costs determined by the AER. In the draft report, having no reliable information at the time, the Commission proposed adjusting the network cost allowance for 2014–15 by the change in the consumer price index. This proposal increased the 2013–14 network cost allowance of \$88.29 per MWh to \$90.45 per MWh.

The AER published ActewAGL Distribution's revised network pricing proposal for 2014–15 for all ACT customers on 5 June 2014. This proposal, which was subsequently approved by the AER, indicates that total network revenue has increased by about 9 per cent from 2013–14, as shown in Table 3.11.

Table 3.11 ActewAGL Distribution network revenue components 2013–14 and 2014–15

Components	2013–14 (\$)	2014–15 (\$)	% change
Distribution use of system	166,327,003	155,007,678	-6.8
Transmission use of system	39,460,285	64,356,444	63.1
Jurisdictional schemes	20,959,000	28,682,570	36.9
Total	226,746,288	248,046,692	9.4

Sources: ActewAGL Distribution (2014a); ActewAGL Distribution (2013).

The main drivers for this rise in network revenues are increases in transmission and jurisdictional scheme costs.⁷²

ActewAGL Distribution reported two reasons for the higher transmission costs. First is the reallocation of costs associated with ActewAGL Distribution's assets that support TransGrid's transmission service to Cooma to transmission rather than distribution charges. The second reason is a return to normal charges after the refund of the over-recovery of transmission costs in earlier years.

ActewAGL Distribution stated that the higher jurisdictional scheme costs in 2014–15 are:

largely due to the commencement of the large scale feed-in tariff scheme and offset by the refund of feed-in tariff revenue estimated to be over-collected in 2013/14.⁷³

Based on ActewAGL Distribution's approved network charges, ActewAGL Retail proposed a network cost allowance of \$98.02 per MWh to apply to regulated retail tariffs. The Commission examined this proposal and determined an allowance of \$98.02 per MWh as the network cost allowance for 2014–15.

The 2014–15 allowance is about 11 per cent higher than the 2013–14 allowance of \$88.29 per MWh. This increase is higher than the percentage increase in total network revenue due to the increase in customers on the regulated retail tariff in 2014–15 without a corresponding increase in energy consumed, compared to the previous year.

Identifying feed-in tariff compliance costs

The Commission reviewed ActewAGL Distribution's revised 2014–15 network pricing proposal to the AER to identify and report on the feed-in-tariff cost allowance as required by the terms of reference. Feed-in-tariff costs are not directly incurred by ActewAGL Retail but are passed on to its ACT customers through the network cost allowance.

⁷² See ActewAGL Distribution (2014a) for more detail of how the network revenues are calculated.

⁷³ ActewAGL Distribution, 2014a: v.

The network pricing proposal separately identifies jurisdictional scheme costs from distribution and transmission costs. ACT jurisdictional schemes comprise the small-scale feed-in tariff, the large-scale feed-in tariff, the utilities network facilities tax and the energy industry levy. As shown in Table 3.11, ActewAGL Distribution has estimated jurisdictional scheme costs of \$28.68 million for 2014–15, accounting for about 11.6 per cent of total network revenue.

As shown in Table 3.12, ActewAGL Distribution has estimated feed-in-tariff costs of \$21.83 million for 2014–15, \$13.96 million for the small-scale scheme and \$7.87 million for the large-scale scheme. The total feed-in-tariff costs represent 8.80 per cent of total network revenue.

Table 3.12 ActewAGL Distribution feed-in-tariff costs 2014–15

Fit costs	2014–15 costs (\$)	% of total network revenue	\$/MWh
Feed-in tariff, small-scale	13,961,000	5.63	5.52
Feed-in tariff, large-scale	7,866,000	3.17	3.11
Total	21,827,000	8.80	8.63

Sources: ActewAGL Distribution (2014a) and the Commission's calculations.

In its submission to the draft report, the ACT Government asked the Commission to present the feed-in-tariff costs on a per MWh basis for ease of comparison with other components of the cost-index model.⁷⁴ This calculation requires multiplying the network cost allowance by the proportion of total network costs that can be attributed to feed-in-tariff costs.

On this basis, using the final network cost allowance of \$98.02 per MWh, the Commission has calculated an implied feed-in-tariff cost allowance of \$8.63 per MWh for 2014–15. On average for ACT customers, this translates to \$69 per year. The Commission's estimate of annual feed-in-tariff costs for 2009–2014 was about \$27 per customer.⁷⁵

As discussed in section 2.3.6, the Commission is only able to report at this time on the feed-in-tariff cost allowance for 2014–15. The Commission will identify and report on costs for 2015–16 and 2016–17 in the annual recalibration exercises.

⁷⁴ ACT Government, 2014: 1.

⁷⁵ The Commission's estimate was based on spreading costs evenly over the five-year ActewAGL Distribution determination period and was for the small-scale scheme only. The number of small-scale scheme installations was steadily growing over this period, so that the costs in the last year of the period would be significantly above the average.

3.10 Retail margin

The retail margin to be applied in 2014–15 was discussed in detail in section 2.3.8. The Commission’s final decision is to increase the retail margin from 5.4 per cent in 2013–14 to 6.04 per cent applied to all cost components excluding the retail margin allowance. This generates an allowance of \$12.00 per MWh for 2014–15.

3.11 Final decision on cost elements

Table 3.13 and Table 3.14 set out the Commission’s final decision on the cost components used to determine the maximum change in the regulated retail electricity price for 2014–15, with and without carbon costs, respectively.

The with-carbon-price maximum average percentage change in prices is 4.33 per cent in ActewAGL Retail’s basket of regulated tariffs. This change will apply from 1 July 2014 until the Clean Energy Act is repealed. This change is equivalent to a real (adjusted for inflation) increase in the regulated retail price of about 2 per cent.

The primary driver of the price increase is the rise in network costs. Increases in the retail operating cost allowance, costs of the EEIS and the rise in the retail margin have been largely offset by a fall in LRET and SRES costs and the energy losses cost component.

Table 3.13 Final decision on cost elements 2014–15 with a price on carbon

	2013–14 (\$/MWh)	2014–15 (\$/MWh)	% change
Energy purchase cost ^a	70.28	70.99	1.00
LRET and SRES costs	11.66	8.49	-27.16
Energy losses ^b	3.84	0.87	-77.47
Energy contracting cost	0.82	0.84	2.45
NEM fees	0.82	0.84	2.45
Total energy purchase cost	87.42	82.03	-6.17
Retail operating costs	11.43	13.57	18.76
Energy Efficiency Improvement Scheme costs	3.75	4.92	31.09
Total retail costs	15.18	18.49	21.81
Network costs	88.29	98.02	11.02
Total energy + retail + network costs	190.89	198.53	4.00
Retail margin ^c	10.90	12.00	10.13
Total costs	201.79	210.53	4.33

Notes: a The 2013–14 energy purchase cost amount has been recalculated from that contained in the 2013–14 price reset due to the adjustments to the forward price and carbon emissions intensity factor averaging periods and the Commission's desire to maintain comparability across adjacent years under the index approach.

b The 2013–14 energy losses amount has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

c The 2013–14 retail margin allowance has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

The without-carbon-price maximum average percentage change in prices is minus 7.30 per cent in ActewAGL Retail's basket of regulated tariffs relative to the 2013–14 tariffs. This change will apply in the event that the Clean Energy Act is repealed. This change is equivalent to a real decrease in the regulated retail price of about 9.5 per cent.

Table 3.14 Final decision on cost elements 2014–15 without a price on carbon

	2013–14 (\$/MWh)	2014–15 (\$/MWh)	% change
Energy purchase cost ^a	70.28	49.00	-30.28
LRET and SRES costs	11.66	8.49	-27.16
Energy losses ^b	3.84	0.72	-81.16
Energy contracting cost	0.82	0.84	2.45
NEM fees	0.82	0.84	2.45
Total energy purchase cost	87.42	59.90	-31.49
Retail operating costs	11.43	13.57	18.76
Energy Efficiency Improvement Scheme costs	3.75	4.92	31.09
Total retail costs	15.18	18.49	21.81
Network costs	88.29	98.02	11.02
Total energy + retail + network costs	190.89	176.40	-7.59
Retail margin ^c	10.90	10.66	-2.14
Total costs	201.79	187.07	-7.30

Notes: a The 2013–14 energy purchase cost amount has been recalculated from that contained in the 2013–14 price reset due to the adjustments to the forward price and carbon emissions intensity factor averaging periods and the Commission's desire to maintain comparability across adjacent years under the index approach.

b The 2013–14 energy losses amount has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

c The 2013–14 retail margin allowance has been recalculated from that contained in the 2013–14 price reset to maintain comparability across adjacent years under the index approach.

3.12 Impact of the final decision on customers

3.12.1 The with-carbon-price case

Table 3.15 presents estimated increases in the 2014–15 electricity bills for a range of typical residential customers resulting from the with-carbon-price electricity price increase of 4.33 per cent.⁷⁶ A small customer may be representative of a single person living in an apartment, an average customer of a small family in a townhouse, and a large customer of a large family in a detached house. The annual impact on these typical bills due to the price increase ranges from \$48 for a small customer to \$122 for a large customer.

⁷⁶ The Commission has no information on the reduction in electricity consumption that the Energy Efficiency Improvement Scheme has brought about and therefore cannot estimate the impact of the scheme on the bills of customers in 2014–15 who will benefit from this scheme.

Table 3.15 Estimated annual bill changes for residential customers 2014–15 with a price on carbon

Customer consumption type	Annual usage (kWh)	Estimated annual bill 2013–14 (\$)	Estimated annual bill 2014–15 (\$)	Change (\$)
Large	12,000	2,804	2,926	122
Average	8,000	1,959	2,044	85
Small	4,000	1,114	1,162	48

Source: Commission's calculations.

Table 3.16 presents estimates of annual bill increases for a range of typical non-residential customers resulting from the with-carbon-price electricity price increase of 4.33 per cent. The impact on a typical bill ranges from \$127 for a small non-residential customer to \$458 for a large non-residential customer.

Table 3.16 Estimated annual bill changes for non-residential customers 2014–15 with a price on carbon

Customer consumption type	Annual usage (kWh)	Estimated annual bill 2013–14 (\$)	Estimated annual bill 2014–15 (\$)	Change (\$)
Large	40,000	10,562	11,020	458
Average	25,000	6,750	7,043	293
Small	10,000	2,939	3,066	127

Source: Commission's calculations.

3.12.2 The without-carbon-price case

Table 3.17 presents changes in the 2014–15 electricity bills for residential customers under without-carbon-price electricity prices. The annual impact on these typical bills due to the minus 7.30 per cent price change ranges from minus \$81 for a small residential customer to minus \$205 for a large residential customer.

Table 3.17 Estimated annual bill changes for residential customers 2014–15 without a price on carbon

Customer consumption type	Annual usage (kWh)	Estimated annual bill 2013–14 (\$)	Estimated annual bill 2014–15 (\$)	Change (\$)
Large	12,000	2,804	2,599	-205
Average	8,000	1,959	1,816	-143
Small	4,000	1,114	1,032	-81

Source: Commission's calculations.

Table 3.18 presents estimates of annual bill changes for non-residential customers. The impact on a typical bill ranges from minus \$214 for a small non-residential customer to minus \$770 for a large non-residential customer.

Table 3.18 Estimated annual bill changes for non-residential customers 2014–15 without a price on carbon

Customer consumption type	Annual usage (kWh)	Estimated annual bill 2013–14 (\$)	Estimated annual bill 2014–15 (\$)	Change (\$)
Large	40,000	10,562	9,791	-770
Average	25,000	6,750	6,258	-492
Small	10,000	2,939	2,724	-214

Source: Commission's calculations.

4 Compliance with the terms of reference and the ICRC Act

This chapter first sets out how the Commission’s investigation complies with the terms of reference. Second, it considers how the price direction complies with the provisions of the ICRC Act, and particularly the requirements of section 20(2).

4.1 Compliance with the terms of reference

Table 4.1 Compliance with the terms of reference

Clause	Requirement	Draft report chapter	Final report chapter	Comments
2	The price direction will be for the period of 1 July 2014 to 30 June 2017 with provision for annual reviews by 30 June 2015 and 30 June 2016.	2, 6	2	The price direction applies for a three-year period and provides for annual price recalibrations.
3.1a	The Commission must consider the impact on direct electricity costs of changes in government policies and pass-through of those costs to regulated prices including, but not restricted to:			
i	the Commonwealth Government’s carbon pricing mechanism	2, 3, 5, 6	2, 3	The energy purchase cost model incorporates the cost of carbon. A contingent pricing mechanism and price variation triggers have been included in the price direction.
ii	Commonwealth and ACT retailer obligation energy efficiency schemes	3, 5	2, 3	The prudent and efficient costs of the ACT Government’s EEIS are included in the cost build-up.
iii	the Commonwealth Government’s Large-scale Renewable Energy Target and Small-scale Renewable Energy Scheme	3, 5	2, 3	LRET and SRES costs are included in the cost build-up.
iv	any other schemes implemented to address climate change relevant to electricity pricing.	n.a.	n.a.	
3.1b	The Commission must consider the efficient and prudent cost of managing risk in the cost of purchasing electricity.	3, 5	2, 3	The energy purchase cost model incorporates a hedging strategy.
3.2	The Commission must identify and report on the cost allowance of the ACT feed-in tariffs (small- and large-scale) for the year(s) or period for which its determination is being made.	3, 5	2, 3	The costs of the ACT feed-in tariffs for 2014–15 are identified and reported in section 3.9 of the final report. The Commission cannot yet provide information on

Clause	Requirement	Draft report chapter	Final report chapter	Comments
				cost allowances for 2015–16 and 2016–17 as this information is not available. These costs will be identified and reported on as part of the annual recalibrations.
3.3	The Commission must identify and report on the efficient costs of complying with the <i>Energy Efficiency (Cost of Living) Improvement Act 2012</i> .	3, 5	2, 3	The costs of the ACT Government's EEIS are identified, assessed for prudence and efficiency, and reported.
3.4	The Commission must produce its final report in time sufficient to allow ActewAGL Retail to make any necessary changes to its billing system and to provide information on the new tariff to customers for implementation effective 1 July 2014.	n.a.	2, 3	Final report released on 13 June 2014.

4.2 Compliance with the ICRC Act

4.2.1 Objectives

Table 4.2 Compliance with section 7 of the ICRC Act

Section 7	Requirement	Draft report chapter	Final report chapter	Comments
(a)	To promote effective competition in the interests of consumers	4	2	The Commission considered whether a competition allowance should be included in the regulated retail electricity price in the ACT in order to promote competition. The Commission concluded that the introduction of a competition allowance in the ACT to be a high-risk strategy because there is a strong possibility that any benefits it may produce will be long delayed, and therefore of little present value, and a distinct possibility that it will not produce benefits even in the long term.
(b)	To facilitate an appropriate balance between efficiency and environmental and social considerations	2, 3, 4, 5, 6	2, 3	The Commission's retail electricity cost-index model is designed to recover the efficient costs of providing retail electricity services in the ACT. This includes the efficient costs of various environmental measures such as the price on carbon, the national LRET and SRES, and the ACT energy efficiency schemes. Social considerations are taken into account first by ensuring that the regulated price is based on efficient costs. The Commission also

Section 7	Requirement	Draft report chapter	Final report chapter	Comments
				considers submissions from consumer rights organisations, and the ACT community considers the impacts of proposed price changes on customer electricity bills.
(c)	To ensure non-discriminatory access to monopoly and near-monopoly infrastructure	n.a.	n.a.	

4.2.2 Section 20(2)

Table 4.3 Compliance with section 20(2) of the ICRC Act

Section 20(2)	Requirement	Draft report chapter	Final report chapter	Comments
(a)	The protection of consumers from abuses of monopoly power in terms of prices, pricing policies (including policies relating to the level or structure of prices for services) and standard of regulated services	2, 3, 5	2, 3	The Commission applies a weighted average price cap form of control to ActewAGL Retail's suite of regulated retail electricity tariffs. The price cap is based on the recovery of efficient costs. Together these actions protect consumers from the abuses of monopoly power in terms of prices.
(b)	Standards of quality, reliability and safety of the regulated services	3, 5	2, 3	The Commission's retail electricity cost-index model, and in particular the retail operating cost component, is designed to cover the efficient costs of providing retail electricity services. This includes the costs of meeting quality, reliability and safety standards. As a specific example, the payment of ancillary services fees, which is captured in the cost-index model, assists AEMO in providing for safe and reliable delivery of electricity to all consumers.
(c)	The need for greater efficiency in the provision of regulated services to reduce costs to consumers and taxpayers	3, 5	2, 3	The Commission's retail electricity cost-index model is based on the efficient costs of providing retail electricity services in the ACT. As an example, to determine the energy purchase cost allowance, the Commission has adopted an approach based on independent and verifiable market data and a range of assumptions based on industry standards to provide a reasonable estimate of the cost of purchasing wholesale energy from a competitive market pool.
(d)	An appropriate rate of return on any investment	2, 3, 5	2, 3	The Commission is proposing a retail margin of 6.04 per cent of the

Section 20(2)	Requirement	Draft report chapter	Final report chapter	Comments
	in the regulated industry			total efficient cost of providing retail electricity services. The Commission is confident that this provides an appropriate rate of return on investment in the retail electricity industry.
(e)	The cost of providing the regulated services	3, 4, 5	2, 3	<p>The Commission's retail electricity cost-index model is designed to recover the efficient costs of providing retail electricity services in the ACT.</p> <p>The Commission considers that the allowance granted for retail operating costs is a reasonable balance between the need to allow cost recovery and the need to require the incumbent to operate efficiently.</p>
(f)	The principles of ecologically sustainable development	3, 5	2, 3	<p>The Commission's retail electricity cost-index model includes the efficient costs of various environmental measures such as the price on carbon, the national LRET and SRES, and the ACT energy efficiency schemes. These costs reflect to some extent the environmental costs incurred in the consumption of electricity that the Australian Government and ACT Government consider should be passed through to consumers.</p>
(g)	The social impacts of the decision	3, 4, 5	2, 3	<p>Social considerations are taken into account first by ensuring that the regulated price is based on efficient costs. The Commission also considers submissions from consumer rights organisations and the ACT community and considers the impacts of proposed price changes on customer electricity bills.</p> <p>In addition, the Commission has had regard to the social impacts of its decisions by not including a competition allowance. This was on the basis that the Commission considers the introduction of a competition allowance in the ACT to be a high-risk strategy because there is a strong possibility that any benefits it may produce will be long delayed, and therefore of little present value, and a distinct possibility that it will not produce benefits even in the long term.</p>
(h)	Considerations of demand management	3, 5	2, 3	<p>The ACT Government's energy efficiency scheme has a demand-</p>

Section 20(2)	Requirement	Draft report chapter	Final report chapter	Comments
	and least-cost planning			management element. The costs of this scheme are accounted for in the cost-index model.
(i)	The borrowing, capital and cash flow requirements of people providing regulated services and the need to renew or increase relevant assets in the regulated industry	3, 5	2, 3	The Commission's retail electricity pricing provides for the efficient costs of providing retail electricity services in the ACT. This includes a retail margin of 6.04 per cent of the total efficient cost. The Commission is confident that this provides sufficient room to meet the borrowing, capital and cash flow requirements and meet the retail industry investment requirements.
(j)	The effect on general price inflation over the medium term	3, 5, 6	2, 3	The Commission ensures that only efficient costs are applied in the cost-index model. A number of components of the model are adjusted each year by the change in the consumer price index.
(k)	Any arrangements that a person providing regulated services has entered into for the exercise of its functions by some other person	3, 5	3	The recovery of energy losses in the cost-index model is mandated in the NEM framework and therefore meets the section 20(2)(k) requirement.

Appendix 1 Terms of reference

Australian Capital Territory

Independent Competition and Regulatory Commission (Price Direction for the Supply of Electricity to Certain Small Customers) Terms of Reference Determination 2014

Disallowable instrument DI2014–10

made under the

Independent Competition and Regulatory Commission Act 1997 ('the Act'), Section 15 (Nature of industry references) and Section 16 (Terms of industry references).

1. Interpretation

In this instrument:

"*National Energy Retail Law (ACT)*" has the same meaning as in the *National Energy Retail Law (ACT) Act 2012*.

"*small customer*" has the same meaning as in the *National Energy Retail Law (ACT)*.

"*standing offer prices*" has the same meaning as in the *National Energy Retail Law (ACT)*.

"*ActewAGL Retail*" means the partnership of ACTEW Retail Ltd (ACN 074 371 20) and AGL ACT Retail Investments Pty Ltd (ACN 093 631 586).

2. Reference for investigation under Section 15

Pursuant to section 15(1) of the Act, I refer to the Independent Competition and Regulatory Commission (the 'Commission') the provision of a price direction for the standing offer prices for the supply of electricity to those persons who are a *small customer*, and who consume less than 100MWh of electricity over any consumption period of 12 consecutive months.

The price direction will be for the period of 1 July 2014 to 30 June 2017 with provision for annual reviews by 30 June 2015 and 30 June 2016. Pursuant to section 15(4) of the

Act, the price direction determined by the Commission under these terms of reference is to apply only to the authorised electricity retailer **ActewAGL Retail**.

3. **Terms of reference for investigation under section 16**

Pursuant to section 16(1) of the Act, I require that the Commission consider the following matters in relation to the conduct of the investigation:

1. The Commission should consider the following matters:
 - a. The impact on direct electricity costs of changes in government policies and pass through of those costs to regulated prices including, but not restricted to:
 - i. the Commonwealth Government’s carbon pricing mechanism;
 - ii. Commonwealth and ACT retailer obligation energy efficiency schemes;
 - iii. the Commonwealth Government’s Large-scale Renewable Energy Target and Small-scale Renewable Energy Scheme; and
 - iv. any other schemes implemented to address climate change relevant to electricity pricing.
 - b. The efficient and prudent cost of managing risk in the cost of purchasing electricity.
2. The Commission must identify and report on the cost allowance of the ACT Feed-in Tariffs (small and large scale) for the year(s) or period for which its determination is being made.
3. The Commission must identify and report on the efficient costs of complying with the *Energy Efficiency (Cost of Living) Improvement Act 2012*.
4. The Commission must produce its final report in time reasonably sufficient to allow **ActewAGL Retail** to make any necessary changes to its billing system and to provide information on the new tariff to customers for implementation effective 1 July 2014.

Katy Gallagher MLA

Acting Treasurer

2 February 2014

Appendix 2 Submissions

A2.1 Submissions on the issues paper

	Date received	Submitter	Key issues raised/information provided
1	8 October 2013	Mr Joe Wyder	Requested more detail on how the weighted average price cap is applied to residential tariffs.
2	15 November 2013	AGL Energy Limited	<p>Supported the weighted average price cap.</p> <p>Recommended a maximum regulatory period of three years.</p> <p>Supported pass-through arrangements but with no materiality threshold.</p> <p>Supported pass-through arrangements to deal with the price on carbon uncertainty.</p> <p>Expressed a preference for the long-run marginal cost approach to determining energy purchase costs but had no major concerns with the Commission's continued use of a market-based model.</p> <p>Noted that hedging an entire load through a single market could not be considered a conservative hedging strategy.</p> <p>Suggested that increasing peakiness in the ACT load ratio due to the growth in solar rooftop systems should be reflected in the energy purchase cost model.</p> <p>Supported continued use of forward carbon-exclusive contract prices to provide flexibility to deal with the price on carbon uncertainty.</p> <p>Suggested that the Commission use long-run marginal costs rather than a market-based approach to estimate LRET costs.</p> <p>Does not support a market-based approach to estimate SRES costs.</p> <p>Contended that it is contradictory to have a policy of full retail contestability and price regulation based on benchmark costs that preclude entry of competition in the market.</p> <p>Argued that basing retail operating costs on an incumbent retailer is not incompatible with including an allowance for customer acquisition and retention costs.</p> <p>Suggested that due to diseconomies of scale, ACT retail operating cost benchmarks should be significantly higher than those determined in New South Wales and Queensland.</p> <p>Proposed that the retail margin be increased to 5.7 per cent to maintain consistency with regulatory benchmarks in New South Wales and Queensland.</p>
3	15 November 2013	Energy Supply Association of Australia	<p>Supported retail price deregulation.</p> <p>Supported setting regulated price at a commercial level which includes customer acquisition and retention costs.</p> <p>Expressed a preference for the long-run marginal cost approach to determining energy purchase costs.</p> <p>Requested that the Commission take into account NECF standing offer price timing requirements and risks associated with retrospective repeal of the price on carbon legislation.</p>
4	15 November 2013	EnergyAustralia Pty Ltd	<p>Noted that the limited number of retailers servicing customers on the regulated tariff is potentially due to price regulation of this segment of the market.</p> <p>Cautioned against using the New South Wales load shape for</p>

Date received	Submitter	Key issues raised/information provided
		<p>calculating the ACT energy purchase cost.</p> <p>Noted that price volatility may increase due to Australian Bureau of Meteorology predictions of higher-than-average summer temperatures.</p> <p>Disagreed with AEMC’s market-based approach to determining energy purchase costs recommendation in favour of the long-run marginal cost approach.</p> <p>Disputed the findings of the Essential Services Commission’s discussion paper on Victorian retailer margins.</p> <p>Supported the weighted average price cap.</p> <p>Recommended a two- to three-year regulatory period.</p> <p>Supported pass-through arrangements with an appropriate materiality threshold.</p> <p>Expressed the following concerns with the Commission’s cost-index model:</p> <ul style="list-style-type: none"> • It is based on incumbent rather than new-entrant retailer. • The energy purchase cost should reference a long-run marginal cost floor. • It does not include any competition allowance or headroom. <p>Supported a more conservative approach to hedging through an explicit volatility allowance in the cost build-up.</p> <p>Supported continued use of forward carbon-exclusive contract prices and pass-through arrangements to provide flexibility to deal with the price on carbon uncertainty.</p> <p>Suggested that the Commission use long-run marginal cost rather than a market-based approach to estimate LRET costs.</p> <p>Recommended that SRES costs be estimated at the \$40 clearing house price.</p> <p>Raised concerns that the Commission has developed a pessimistic view of competition in the ACT.</p> <p>Stated that the retail operating cost allowance should reflect diseconomies of scale and not be benchmarked against other larger jurisdictions.</p> <p>Stated that the retail operating cost allowance should include customer acquisition and retention costs.</p> <p>Suggested that EEIS costs should be based on tier 1 retailers (ActewAGL Retail) unless the compliance costs for tier 2 retailers are higher.</p> <p>Supported full pass-through of network costs.</p> <p>Recommended a retail margin of at least 5.7 per cent.</p>
5	15 November 2013 ActewAGL Retail	<p>Recommended that the regulated retail tariff should be removed.</p> <p>Supported the AEMC recommendation that a stable and predictable regulatory framework should be applied.</p> <p>Supported the Commission’s energy purchase cost model with an increase to the forward price margin.</p> <p>Supported a higher retail cost allowance on the basis that the ACT now has the lowest allowance, even before taking into account diseconomies of scale and customer and acquisition and retention costs.</p> <p>Supported continued use of forward carbon-exclusive contract prices and pass-through arrangements to provide flexibility to deal with the price on carbon uncertainty.</p> <p>Recommended that the retail margin be increased to at least 6 per cent in line with other jurisdictions.</p> <p>Proposed a maximum two-year regulatory period subject to</p>

Date received	Submitter	Key issues raised/information provided
		<p>flexible pass-throughs and a predictable annual reset process.</p> <p>Expressed concern about the risks faced under price regulation related to the repeal of the price on carbon legislation.</p> <p>Disputed the findings of the Essential Services Commission's discussion paper on Victorian retailer margins.</p> <p>Supported the weighted average price cap.</p> <p>Supported pass-through arrangements with no materiality threshold.</p> <p>Sought assurance that the current pass-through formula can be applied in a neutral way to within-year pass-throughs.</p> <p>Recommended that the Commission include a specific carbon pricing mechanism pass-through arrangement.</p> <p>Maintained a preference for basing energy purchase costs on long-run marginal costs but recognises, in the interests of a transparent and stable regulatory framework, the Commission's previous preference to use a market-based approach.</p> <p>Raised concerns that the decrease in the calculated uplift factor from 2009–10 and the increasing difference between the forward price and the time-weighted spot price mean that the Commission's hedging approach is no longer conservative.</p> <p>Requested that the Commission reconsider its 5 per cent forward price margin assumption.</p> <p>Recommended that the Commission revert to using a 23-month averaging period for calculating the forward price and cost of carbon.</p> <p>Suggested that the Commission use long-run marginal cost rather than a market-based approach to estimate LRET costs.</p> <p>Recommended that SRES costs be estimated at the \$40 clearing house price.</p> <p>Expressed a clear preference for benchmark retail operating costs to be based on a new entrant, which should include an allowance for customer acquisition and retention costs.</p> <p>Recommended that the retail operating cost allowance should be \$114 to \$178 per customer when diseconomies of scale are taken into account.</p> <p>Raised concerns about the risks of an ex post prudence and efficiency assessment of EEIS costs.</p>
6	20 November 2013 ACT Civil and Administrative Tribunal	<p>Submitted that no allowance should be made in the energy purchase cost model simply for the possibility of an increase in price volatility in the future.</p> <p>Submitted that there has been little customer churn and insignificant costs in acquiring and retaining customers in the ACT in recent years.</p> <p>Stated that the purported benefits of competition in retail electricity markets in other jurisdictions are not well supported by actual experience.</p> <p>Submitted that decisions by other jurisdictional regulators should be treated cautiously as market conditions differ from those in the ACT.</p> <p>Rejected the inclusion of a customer acquisition and retention cost allowance.</p> <p>Submitted that there should be evidence that competition in the ACT market would lead to a long-term reduction in retail prices before a competition allowance is accepted.</p> <p>Supported the weighted average price cap approach.</p>

Date received	Submitter	Key issues raised/information provided
		<p>Recommended a two- or three-year regulatory period.</p> <p>Supported the retention of the current materiality threshold for pass-through arrangements but recommended that the current set of allowable pass-through events be reduced.</p> <p>Supported the Commission’s market-based approach to determining wholesale energy purchase costs rather than adopting a long-run marginal cost approach.</p> <p>Supported a market-based approach to determining LRET and SRES costs.</p> <p>Suggested that the Commission require the price reduction consequent on removal of the price on carbon to flow through to prices quickly.</p> <p>Submitted that the current retail margin should not be increased.</p>
7	21 November 2013 Origin Energy Limited	<p>Argued that previous ACT determinations have materially understated the cost of meeting the small customer load.</p> <p>Noted that the lower volatility in New South Wales spot prices has lowered costs for only those retailers buying energy on a short-term basis.</p> <p>Submitted that considerable uncertainty remains in the market due to the carbon pricing issue, the impact of green schemes and changes in consumption and load shape due to embedded generation.</p> <p>Rejected the findings of the Essential Services Commission report on retailer margins in Victoria.</p> <p>Supported the weighted average price cap approach.</p> <p>Recommended a two- to three-year regulatory period with annual reviews of wholesale costs.</p> <p>Supported pass-through arrangements including for the cost of carbon.</p> <p>Questioned the Commission’s approach of not including customer acquisition and retention costs for an incumbent retailer.</p> <p>Supported basing energy purchase costs with reference to long-run marginal cost.</p> <p>Recommended that the Commission adopt an allowance for the costs of prudential requirements associated with bank guarantees for futures hedges.</p> <p>Supported continued use of forward carbon-exclusive contract prices and pass-through arrangements to deal with the price on carbon uncertainty.</p> <p>Suggested that the Commission use long-run marginal cost rather than a market-based approach to estimate LRET costs as there is insufficient liquidity in the LGC market.</p> <p>Noted that the Commission’s allowance for energy contracting costs is significantly lower than that provided in New South Wales.</p> <p>Argued that standard retail operating cost allowance in the ACT is much lower than that provided in other jurisdictions.</p> <p>Urged the Commission to consider creating an allowance to encourage further development of competition in the ACT market.</p>
8	28 November 2013 ACT Government (Minister for the Environment and Sustainable Development)	<p>Stated that the ACT Government remained committed to retail price deregulation should effective competition emerge and be sustained in the ACT.</p> <p>Requested that the Commission make it clear that the Commission’s discretion to set the length of the regulatory period does not limit the ACT Government’s ability to deregulate price within the period that is determined.</p>

Date received	Submitter	Key issues raised/information provided
		<p>Did not support the inclusion of a competition allowance in regulated retail prices.</p> <p>Supported the Commission undertaking an ex post assessment of ActewAGL Retail's expenditure on the EEIS.</p> <p>Suggested that the Commission could consider and compare cost incurred by retailers administering similar schemes in other jurisdictions.</p>

A2.2 Submissions on the draft report

Date received	Submitter	Key issues raised/information provided
9 26 March 2014	ACT Government (Minister for the Environment and Sustainable Development)	<p>Supported the draft report position on not granting a competition allowance.</p> <p>Requested that period-specific information on the costs of the feed-in-tariff schemes be included in the final report on a per-megawatt-hour basis.</p> <p>Stated that ActewAGL Retail's forecast abatement costs for the EEIS are too high compared to other jurisdictions and that the Commission should apply a retrospective cost assessment and adjustment. Recommended that the Commission investigate opportunities provided under the EEIS legislation for ActewAGL Retail to pursue lower cost open-market abatement from third-party providers.</p> <p>Stated a preference for ensuring that electricity businesses are not able to make windfall profits at the expense of ACT customers from the price on carbon uncertainty. Suggested the Commission consider a pass-through arrangement to recover any potential windfalls when setting electricity prices from 1 July 2015.</p>
10 28 March 2014	AGL Energy Limited	<p>Supported the Commission's energy purchase cost model but stated that the load ratio, which measures the peakiness of the load is under-represented in the uplift factor.</p> <p>Submitted that the Commission's higher retail operating cost proposal remains below that of New South Wales and Queensland.</p> <p>Disagreed with the Commission's conclusion that the competitive performance of small Victorian utilities reflects economies of scale. Argued instead that it reflected the ability of small utilities to set prices at levels that reflect their own costs and risks in a deregulated market. Stated that evidence shows that larger retailers such as AGL Energy have significantly lower average operating costs than smaller utilities such as Australian Power and Gas.</p> <p>Did not support the Commission not making an allowance for necessary customer acquisition and retention costs.</p> <p>Submitted that the Commission's view on a competition allowance will continue to delay the development of competition in the ACT and noted that customers could avoid a competition allowance by entering into market contracts.</p> <p>Supported a higher retail margin for the ACT market given the lack of margin for error in the retail operating cost allowance.</p> <p>Submitted that the Commission has not outlined how the draft report will promote competition.</p>

	Date received	Submitter	Key issues raised/information provided
11	28 March 2014	ActewAGL Retail	<p>Supported the weighted average price cap and the Commission's two proposed adjustments to the price cap formula.</p> <p>Requested an explanation for the inclusion of the additional price variation triggers in the proposed price direction and in particular requested more detail on the Commission's proposed trigger for the price on carbon arrangements.</p> <p>Supported referencing long-run marginal cost when determining the energy purchase cost but noted the Commission's preference to maintain its market-based model.</p> <p>Argued that the Commission's hedging strategy is not conservative due to a decreasing trend in the uplift factor and an increased load ratio. Submitted that the forward price margin should be increased to at least 6.5 per cent.</p> <p>Supported continued use of ICAP over-the-counter contract forward prices and averaging the emissions intensity factor over 365 days to 31 May when calculating the cost of carbon.</p> <p>Maintained its view that the market-based approach to calculating SRES costs does not fully address the risks in the market. Submitted an adjustment factor of \$0.34/MWh for LRET and SRES costs for 2013–14 to be included in 2014–15 costs. Noted that the Clean Energy Regulator no longer publishes renewable power percentage non-binding estimates and suggested that the Commission use the current non-binding estimate of 10.52 per cent for 2015.</p> <p>Supported the Commission's proposed changes to the energy losses calculation, but expressed a preference for using the weighted transmission loss factor for Canberra and Fyshwick, and not only the Canberra connection point as implied in the draft report.</p> <p>Supported continuing to adjust energy contracting costs and NEM fees by the change in the CPI.</p> <p>Did not support the Commission's conclusions on economies of scale, arguing that Australian Power and Gas and Simply Energy serve triple the ACT customer base nationally. Argued that the Commission's proposed step-up in the retail operating cost allowance does not go far enough in comparison with other jurisdictions.</p> <p>Submitted that by not including any allowance for retaining customers, ActewAGL Retail is not recovering legitimate and appropriate costs of providing retail services in a competitive market.</p> <p>Maintained its view that retail price regulation should be removed.</p> <p>Provided a copy of ActewAGL Retail's approved 2014 Compliance Plan for the EEIS. Supported the Commission's ex ante approach to prudence and efficiency and the Commission's draft conclusion that expenditure on the scheme was prudent and efficient. Noted future uncertainty about the cost of the scheme due to changes in abatement factors.</p> <p>Supported the Commission's proposal to continue passing through network costs as determined by the AER.</p> <p>Argued that the Commission's proposed increase in the retail margin to 5.7 per cent is not consistent with the manner in which IPART and the QCA have applied their increased retail margins. Recommended that the Commission consider applying the 5.7 per cent in a consistent manner or apply a 6 per cent margin using its current method.</p> <p>Did not support the Commission's proposal to only allow</p>

Date received	Submitter	Key issues raised/information provided
		<p>regulatory and tax change pass-throughs as part of the annual reset process.</p> <p>Raised concerns that the proposal to allow the Commission to initiate pass-through events had no provisions for ActewAGL Retail to respond to any potential claim. Recommended that the Commission consider including a response mechanism.</p> <p>Maintained its view that a pass-through materiality threshold is not warranted.</p> <p>Did not support the Commission's proposal to adjust prices post 1 July 2014 proportionately to remove the price-on-carbon component. Proposed further discussion with the Commission on the carbon price event pass-through mechanism and suggested the Commission consider determining two maximum allowable percentage changes in average prices – with and without a price on carbon – as one option.</p> <p>Noted that the Commission's proposed annual price reset procedure is similar to that applied in the current price direction.</p>
12	28 March 2014 EnergyAustralia Proprietary Limited	<p>Did not support the retention of price regulation in the ACT, or the Commission's proposal to not provide a competition allowance. Argued that as a result, not only will ACT consumers not receive the benefits of full competition – examples of which were provided – but that the ACT Government and Commission's views will threaten what little competition is currently available in the ACT. Submitted that, in addition, these views will result in inconsistencies in regulatory design and administration across jurisdictions.</p> <p>Expressed concern that the ACT Government is not meeting its COAG commitment to move towards retail price deregulation.</p> <p>Recommended that the Commission set regulated prices with reference to a hypothetical efficient new-entrant retailer.</p> <p>Maintained its preference for a long-run marginal cost floor approach to calculating the energy purchase cost, consistent with other jurisdictions.</p> <p>Suggested that the Commission use long-run marginal cost rather than a market-based approach to estimate LRET costs and that SRES costs be estimated at the \$40 clearing house price.</p> <p>Maintained its view that EEIS costs should be based on tier 1 retailers (ActewAGL Retail) except when the price paid by tier 2 retailers is higher.</p>
13	28 March 2014 Origin Energy Limited	<p>Did not support the Commission's decision not to grant a competition allowance and raised a concern that the Commission has not met its legislative requirement to promote competition in the ACT. Expressed concern that the Commission's decision runs counter to decades of electricity market reform and rejected the notion that the retail electricity sector has special characteristics that mean regulated prices will be more efficient than those set under effective competition.</p> <p>Maintained its preference for determining energy purchase costs with reference to long-run marginal costs. Questioned the Commission's view that there is no settled long-run marginal cost methodology.</p> <p>Maintained its preference for using long-run marginal cost rather than a market-based approach to estimate LRET costs.</p>

Abbreviations and acronyms

AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
Clean Energy Act	<i>Clean Energy Act 2011</i> (Commonwealth)
COAG	Council of Australian Governments
Commission	Independent Competition and Regulatory Commission
CPI	consumer price index
EEIS	Energy Efficiency Improvement Scheme
ESDD	Environment and Sustainable Development Directorate (ACT)
ICRC	Independent Competition and Regulatory Commission
ICRC Act	<i>Independent Competition and Regulatory Commission Act 1997</i> (ACT)
IPART	Independent Pricing and Regulatory Tribunal (New South Wales)
kWh	kilowatt hour
LGC	large-scale generation certificate
LRET	Large-scale Renewable Energy Target
LRMC	long-run marginal cost
MWh	megawatt hour
NECF	National Energy Customer Framework
NEM	National Electricity Market
NERL	National Energy Retail Law
QCA	Queensland Competition Authority

Abbreviations and acronyms

SCER	Standing Council on Energy and Resources
SRES	Small-scale Renewable Energy Scheme
STC	small-scale technology certificate

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