

21 December 2007

Essential Services Commission of South Australia  
Level 8, 50 Pirie Street  
Adelaide SA 5000

### **Review of Gas Standing Contract Prices 2008/09 – 2010/11 Issues Paper**

Simply Energy welcomes the opportunity to comment on the Essential Services Commission of South Australia's Review of Gas Standing Contract Prices 2008/09-2010/11 Issues Paper.

#### **Retail margin for second-tier retailers**

Gas standing contract prices act as a strong signal for gas market contract prices. In order to be competitive, retailers have typically set market contract prices at a discount to the standing contract prices. This means that, in order to maintain an effective competitive market in the gas retail sector, standing contract prices must be set at a level that allows second-tier retailers to discount the standing contract prices by a competitive amount, and still make a reasonable return on investment.

Assuming no adverse movements in the costs of supplying gas during the price path period, including that hedge prices for gas remain within current forecasts, Simply Energy considers that the prices proposed by Origin, and set out in the Issues Paper, are at a level that will allow second-tier retailers to make an adequate return for investing in the gas retail market.

#### **Additional costs of second-tier retailers to be taken into account**

In order to promote a competitive gas retail market, the determination of gas standing contract prices should take into account costs necessarily incurred by second-tier retailers in respect of their gas market contracts that are over and above those costs incurred by the incumbent retailer. Neither the 'prudent' retailer methodology nor an investigation into the actual costs incurred by the incumbent retailer appears to take account of these additional costs.

A number of factors increase the costs and risks for second-tier retailers participating in the South Australian gas retail market, and therefore limit the competitiveness of second-tier retailers as compared with the incumbent:

- The first is lack of access to network capacity. Historically, Origin has contracted full capacity to the Adelaide city gates. The extent of Origin's continued control over the city gas remains of concern. Any second-tier retailer seeking access must contract with Origin for allocation of spare capacity.
- Origin remains the main user of MAPS. Most gas supplied by second-tier retailers is sourced through SEA Gas at a less competitive rate. Sourcing gas through MAPS is more competitive because the gas supply costs and the network tariffs are less.
- The gas wholesale market in South Australia is very illiquid. It is difficult for second-tier retailers to access gas at competitive prices and terms. Further, swing gas is provided exclusively by Origin. This has the effect of increasing wholesale gas prices for second-tier retailers as compared to Origin.

An assessment of the costs that make up the standing contract prices must include these additional costs incurred by second-tier retailers, so as to enable second-tier retailers to remain competitive and so maintain an incentive for second-tier retailers to stay in the market.

In addition, the determination of gas standing contract prices must also take into account the costs incurred in respect of acquiring market contract customers (such as sales and marketing costs) and the costs of managing and seeking to reduce customer churn.

Simply Energy would be happy to provide to the Commission, on a confidential basis, further information about the additional costs incurred by it as described above.

If you would like to discuss any of these comments in further detail, please contact Nick Koutroumanis, Assistant Commercial Manager, on (03) 8807 1135.

Yours sincerely

Nick Koutroumanis  
**Commercial Manager**