

Essential Services Commission Act 2002

NOTICE OF REFERENCE UNDER PART 7

Standing Contract Prices of AGL from 2005

1. BACKGROUND

- 1.1 Pursuant to Part 7 of the *Essential Services Commission Act 2002* ("**the Act**") an industry Minister may, by written notice, refer any matter relating to a regulated industry to the Essential Services Commission ("**the Commission**") for the Commission to conduct an inquiry into that matter.
- 1.2 By virtue of section 14D of the *Electricity Act 1996*, the electricity industry is a regulated industry for the purposes of Part 7 of the Act.
- 1.3 The Hon Patrick Conlon, Minister for Energy ("**the Minister**") is the Minister administering the *Electricity Act 1996*.
- 1.4 Pursuant to section 36AA of the *Electricity Act 1996* the Governor may declare an electricity entity to be subject to section 36AA of the *Electricity Act 1996*.
- 1.5 By proclamation in the Gazette, edition of 12 September 2002 (p.3384), AGL South Australia Pty Ltd ACN 091 105 092 ("**the electricity entity**") is a declared electricity entity pursuant to section 36AA of the *Electricity Act 1996*.
- 1.6 The Government has announced a legislative amendment process in response to the recommendations of the Report by the Independent Pricing and Regulatory Tribunal (IPART) of March 2004. These changes will be pursued whilst the price inquiry to which these terms of reference apply is in progress.
- 1.7 It is anticipated that the Commission's final report and determination (should the Commission consider it appropriate) will be issued pursuant to the new legislative regime.

2. REFERENCE

I PATRICK CONLON, Minister for Energy, hereby refer to the Commission the matter described in paragraph 3.1 of the Terms of Reference for the Commission to investigate pursuant to Part 7 of the Act, in accordance with the Terms of Reference specified below.

3. TERMS OF REFERENCE

The following are the Terms of Reference for the inquiry specified pursuant to section 35 of the Act:

- 3.1 The Commission is to investigate the standing contract price proposal (“the Proposal”) that will apply to small customers from 1 July 2005 for a period of no less than three years.
- 3.2 In assessing the proposal, the Commission’s evaluation will be limited to reviewing the electricity entity’s prudent controllable costs which, together with the relevant network tariffs, comprise the final standing contract prices charged to small customers. There should be no provision for specific headroom allowed in the prudent controllable costs determined by the Commission.
- 3.3 On completion of the inquiry, the Commission may issue a determination under Part 3 of the Act in conjunction with the making of its final report on the inquiry.
- 3.4 In determining whether the electricity entity’s controllable costs are justified as the prudent costs incurred in supplying small customers, in addition to the requirements of Parts 2 and 3 of the Act, the Commission is to have regard to:
 - 3.4.1 the electricity entity’s justification for its proposed charges, presented as part of the proposal;
 - 3.4.2 the wholesale electricity contracts and hedging strategies that would be utilised by a prudent electricity entity in providing the standing contracts to each of the residential and business customer classes in South Australia;
 - 3.4.3 the electricity entity’s actual underlying wholesale electricity contracts, hedging strategies and other arrangements for securing electricity for supply in South Australia, as well as the method for allocating these costs between large and small customers and within the small customer class;
 - 3.4.4 the retail operating costs that would be incurred by a prudent electricity entity in delivering the range and standard of services that are required of the electricity entity in providing standing contract services to South Australian small customers;
 - 3.4.5 the electricity entity’s actual operating costs in providing standing contract services to South Australian small customers, and the method of allocating its costs between the different customer classes;
 - 3.4.6 the electricity entity’s proposed margin on standing contract sales, and its actual margin achieved in recent years, and whether these

are reasonable having regard to the entity's investment in the business, the risks of standing contract retailing in South Australia, and the equivalence with standing contract retailer margins interstate without Government risk management schemes;

- 3.4.7 any cross-subsidies between, and within, business and residential small customer classes, and whether these cross-subsidies are justified to prevent a disproportionate price impact on any small customer group;
- 3.4.8 the prices charged and costs incurred in providing comparable services in other States and Territories of Australia, and whether the reasons for any differences can be justified; and
- 3.4.9 any other factors the Commission considers relevant.

4. CONDUCT OF INQUIRY

- 4.1. Following the receipt of these terms of reference, the Commission's inquiry process shall consist of at least the following:
 - 4.1.1 The publication of a notice of inquiry, as required pursuant to section 36 of the Act, no later than 7 days following receipt of these terms of reference;
 - 4.1.2 The release of an issues paper within 1 month of receipt of these terms of reference, in whatever form the Commission considers appropriate, setting out the information it requires the electricity entity to provide by a date specified in the Paper, and seeking comment on the key issues it should address in its investigations;
 - 4.1.3 The release of a Discussion Paper following the release of the electricity entity's proposal, as the basis of a consultation process on the proposal and on other information available to the Commission on components of the electricity entity's controllable costs;
 - 4.1.4 The release of a draft decision and determination (if applicable) to the Minister and electricity entity for comment no later than one week prior to the public release of a draft decision and determination;
 - 4.1.5 The release of a draft decision and determination (if applicable) no later than 30 November 2004, including provision for a bridging price for the period to 30 June 2005; and
 - 4.1.6 The submission of a final report and price determination (if applicable) to the Minister and electricity entity no later than 31 March 2005, and to the public no later than 7 days thereafter.

- 4.2 The final price determination (if considered appropriate) should allow for an adjustment within the period for which the determination applies based on such factors and as frequently as considered appropriate by the Commission.
- 4.3 The consultation process may consist of a public hearing, public seminar or workshop but the Commission may receive and consider any written submissions as it thinks appropriate.

5. DEFINITIONS

In this notice:

- 5.1 “business customer class” means those small customers not included in the residential customer class and excluding unmetered supplies;
- 5.2 “controllable costs” refer to those costs of the electricity entity which comprise the wholesale cost of electricity, retail operating costs, retail profit margin and any other cost (other than network charges) incurred by the electricity entity in carrying out its obligations under relevant legislation;
- 5.3 “proposal” refers to the document or documents provided by the electricity entity to the Commission in response to its initial information request as set out in the Issues Paper. The documents may include confidential components which the Commission must not publicly release and must treat in accordance with section 30 of the Act;
- 5.4 “residential customer class” means the group of small customers consuming electricity in premises wholly or principally as private residence; “small customer” has the meaning given to it in the *Electricity Act 1996*; and
- 5.5 “standing contract price” has the meaning given to it by section 36AA(6)(b) of the *Electricity Act 1996*

Dated May 2004

HON PATRICK CONLON MP
Minister for Infrastructure
Minister for Energy
Minister for Emergency Services