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8 February 2013

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Chairman
Australian Energy Market Commission
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Dear Mr Pierce,

RPR0001 Issue Paper - Review of Competition in the Retail Electricity and Natural Gas Markets in NSW

Jemena Gas Networks (NSW) Limited (JGN) welcomes this opportunity to comment on the Australian Energy Market Commission's (AEMC's) issues paper on the review of the competition in the retail electricity and natural gas markets in New South Wales (NSW) for small customers that consume less than 160MWh of electricity or 1TJ of gas each year.

JGN has actively supported the development of contestability for small customers in the NSW gas retail market since contestability was introduced in 2002. Over the period since then, JGN has noted an increase in the level of competition in the NSW gas market. There has been an increase in the number of retailers who are competing for customers¹ and a steady increase in the number of customers transferring between retailers².

JGN supports the AEMC's review into the effectiveness of competition and hopes that the feedback obtained from participants will assist the AEMC to make recommendations that improve competition, and ultimately ensures the future competitiveness of natural gas in the NSW energy market.

The following is JGN's response to the questions posed in the paper.

Barriers to Entry

The current NSW gas retail market design has provided a ready means for retailers to enter and compete in the gas retail market for small gas customers.

Unlike other jurisdictions, retailers are able to choose the level of automation they wish to invest in to operate within the market. They may commence operations in NSW with only a

¹ These trends are also apparent from information published in the Independent Pricing and Regulatory Tribunal of New South Wales, December 2012 'Information Paper - Customer service performance of gas retail suppliers - 1 July 2007 - 30 June 2012'. There are seventeen licensed retailers in the NSW market as at 30 June 2012. Eight out of the seventeen supplied gas to small gas retail customers that consumed less than 1 TJ of gas per annum in 2011/2012. JGN notes that two nationally significant retailers have entered the market in past three years.

² Please refer to the graph below, which shows the number of completed customer transfers that have been recorded on a monthly basis between 1 January 2002 and 31 December 2012 within JGN's gas network.

rudimentary market interfacing capability by utilising third party suppliers to meet market system requirements and by gaining remote, self service access to JGN's own distribution IT system for managing customer sites. Then, as the volume of transactions warrants, they may upgrade these systems to utilise interfaces with higher levels of automation.

This flexibility allows retailers to avoid the high entry cost of investing in high volume automation, yet transition to automated systems when economically efficient to do so.

Gas usage in NSW

Gas is a discretionary fuel in NSW, especially in the warmer coastal regions. While households in NSW connect to electricity as a matter of course, only 62% of NSW households have gas infrastructure available, and of those, only 70% are connected. The warmer climate in NSW presents a challenge for businesses seeking to promote the uptake of gas by small customers.

To connect to gas, a household that already has electricity connected will incur:

- the cost of connection
- the cost of gas appliances which are generally more expensive than equivalent electric appliances;
- The cost of internal plumbing to connect the appliances to the meter; and
- the cost of maintaining a second energy account including standing charges that are independent of the volume consumed

In addition, when an electrical appliance, such as a water heater fails, there is only a small window of opportunity to replace it with a gas appliance. In practice, a customer will often decide that it is more convenient to replace like with like. This is particularly the case, where the customer's premises are not already connected to gas given the time required to arrange and complete a new service connection. These factors mean that there are relatively high barriers to converting "electricity" households to gas in NSW.

JGN further observes that most gas retail activity is directed towards winning a larger share of the existing gas customer base over connecting new customers to gas. This is because transferring an existing customer between suppliers is typically less complex and expensive than persuading a customer who is already connected to electricity, to connect to gas as well.

For the reasons described above considerable marketing effort is required to grow the gas customer base in NSW, and not merely drive the exchange of consumers within the existing customer base between participants.

Marketing of Gas in NSW

JGN has an incentive to market gas to end-use customers in order to increase the utilisation of gas assets and to increase the size of the gas network. This in turn provides a more cost effective service to individual consumers by providing a larger customer base over which fixed costs may be amortised.

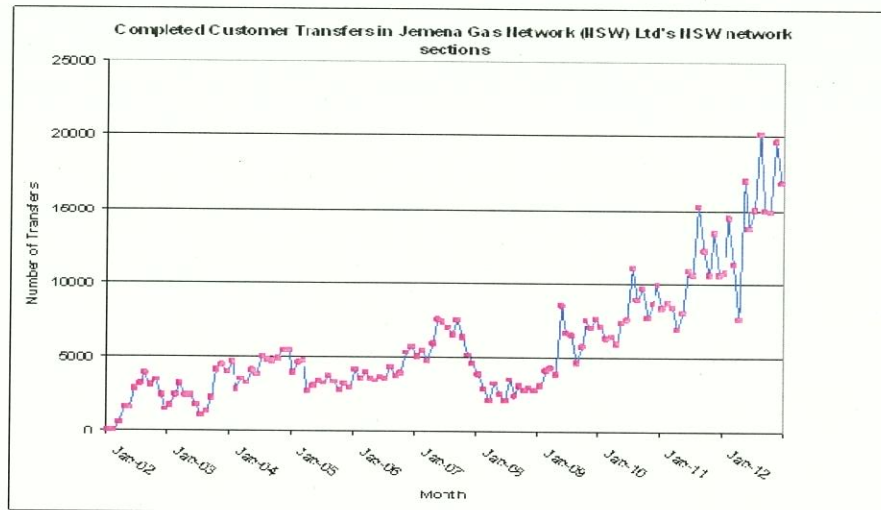
JGN has employed a number of strategies to increase its customer base and increase the penetration of gas consuming appliances such as gas water heaters and gas central heating in NSW. JGN does this by:

- Partnering with property developers to ensure that new homes are connected to gas and fitted with gas appliances at the outset, by better planning infrastructure expansion and simplifying the connection process.
- Partnering with retailers, to provide more streamlined end to end processes for connecting consumers and arranging supply.
- Partnering with appliance manufacturers and installers to assist make gas connections to existing homes simple and cost effective.
- Promoting the benefits of natural gas generically to maximise awareness.

The Australian Energy Regulator (AER) has recognised the cost of marketing activities and an allowance for marketing expenditure has been included in the costs that JGN can recover through the regulated tariffs that it charges to retailers.

Gas Retail Competition in NSW

While network growth requires specific investment, competition for existing customers is prevalent in NSW. An increasing number of customers are exercising choice by switching between retailers year to year. The graph below shows the number of completed customer transfers that JGN has recorded on a monthly basis from 1 January 2002 to 31 December 2012.



Considerations for future development of competition in NSW

An important consideration regarding the future development of the NSW gas market is the cost of gas to consumers. Higher gas costs would lead to less market growth.

The cost of compliance to market procedures is a significant component of the cost that is ultimately passed to consumers. Care should be taken when implementing market changes in NSW to ensure that there is a net benefit to the consumers who ultimately fund any change.

Recently there has been pressure, particularly from retailers and AEMO, to standardise market systems between jurisdictions. This proposed harmonisation would require significant costly changes to JGN's systems when, as we have noted above, existing systems are flexible and efficient and do not present barriers to entry. JGN is particularly concerned that the changes that would be required to achieve harmonisation will not provide a net benefit to consumers.

Should the AEMC wish to discuss any aspect of the information presented above, please contact Maheshini (Mesh) Weerackoon on (02) 9455 1531.

Yours sincerely,

Peter Harcus
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