7 January 2013

Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001

Via email: electricity@qca.org.au

Dear Sir / Madam,

Re: Regulated Retail Electricity Prices 2013/14

Thank you for the opportunity to comment on Regulated Electricity Prices 2013-14 in relation to Transitional Issues (issued October 2012) and Cost Components & Other Issues (December 2012) . MSF Sugar Limited (MSF) also supports submissions from the Australian Sugar Milling Council and Canegrowers that will no doubt emphasise that this is an important matter for the entire sugar industry in Queensland.

MSF Sugar Limited (MSF) is an integrated grower, processor, marketer and exporter of raw sugar. Our production processes are highly dependent on having access to competitively priced electricity, which is sourced internally by producing renewable energy from bagasse (a bi-product of our sugar production), and by importing a small amount of electricity from the grid when our production plants are not operating.

Our suppliers are sugar cane farmers in Far North Queensland and Maryborough. At the present time farmers are negatively impacted by the strong Australian dollar as well as higher costs on insurance, fertilizer, contract labour and fuel. Farmers that irrigate the crop are particularly exposed to changes in regulated electricity tariffs.

Summary of the Key Issues

MSF have a number of concerns with the proposed approach to determine regulated electricity prices because it appears likely that all business customers outside South East Queensland (SEQ) will soon be paying the highest electricity prices in the country.

This unfavourable outcome for Industrial & Commercial (I&C) customers and farmers in regional Queensland reflects:

1. A departure from the long standing and generally accepted Uniform Tariff Policy for electricity in Queensland
2. That Ergon Energy's network tariffs are very high compared to Energex and similar regional networks in NSW and Victoria

3. The wholesale energy and retail cost components of the regulated electricity tariffs include inflated costs and margins, and even customers that do not have a choice to move away from regulated pricing have to pay an additional 5% headroom component to the large energy retail companies.

Further details of these issues are provided below.

Discussion of Issue No 1 – Departure from the Uniform Tariff Policy

It has been long standing policy in Queensland that electricity customers have access to the same tariffs as other customers in the same Class, regardless of where they are located within the state.

Having attended the QCA's information session in Cairns in November 2012 we understand that the Authority has been asked to determine tariffs for business customers outside SEQ based on Ergon Energy's network tariffs (which are significantly higher than Energex's charges). This is consistent with QCA's position in April 2012 when the Authority failed to follow directions from the previous Minister to apply Energex's network tariffs due to a "technical" interpretation of how to determine regulated prices.

We understand that the "technical" argument was not documented but that the logic went something like this:

- I&C customers in South East Queensland have full access to the contestable electricity market
- Contestable electricity prices in SEQ are based on Energex's network tariffs, so contestable electricity prices in SEQ will always be lower than or equal to regulated prices (i.e. I&C customers in SEQ do not need access to regulated electricity prices)
- The Minister has determined that I&C customers in SEQ will no longer have access to regulated electricity prices. Consequently, it can be argued that these customers are no longer relevant when determining regulated prices
- In other words, by taking away something that SEQ customers did not need in the first place, it is now possible apply Ergon Energy's higher network prices for business customers outside SEQ.

In reality, this represents a departure from the Uniform Tariff Policy because the customer's cost of electricity will now be determined by Class and location. In order to correct this anomaly, we encourage the QCA to look for alternative and broader solutions that can achieve cost reflectivity whilst maintaining the Uniform Tariff Policy, even if these solutions may take longer to implement.

Discussion of Issue No 2 – Ergon Energy's Network Tariffs

The QCA has asked for views on the suitability of Ergon Energy's network tariffs for large customers. We note that these tariffs have never really been commercially tested because the majority of customers have only ever been exposed to regulated retail tariffs. By reading the Authority's Consultation Paper we understand and agree that there are serious doubts in relation to:

- The departure from uniform prices between SEQ and regional Queensland
- The lack of appropriate time-of-use signals in Ergon Energy's tariffs

- The fact that Ergon Energy have introduced site-specific network tariffs for customers within the same Class. Unless there is also a common tariff that is accessible to all customers within a Class, this would clearly represent a further departure from the Uniform Tariff Policy
- The fact that many large customers will experience significant price increases.

With respect to the last two bullet points above, we believe it would be highly inappropriate to force these customers to seek contestable contracts because (a) this course of action is not even considering the interest of customers, and (b) it will look like another “technical” manoeuvre to remove customer access to regulated prices in order to profess that the Uniform Tariff Policy is still alive. As an alternative and more appropriate course of action we understand and agree that tariff EDHT1 may be a viable alternative for High Voltage customers.

For the avoidance of doubt, when the underlying cost issue relates to network charges, then there is nothing a large energy user can achieve through negotiations with a retail company (refer Section 3.2 of QCA’s advice to the Minister for Energy & Water Supply dated November 2012 which seems to suggest otherwise).

Finally, MSF would like to make two further points in relation to Ergon Energy’s network tariffs:

- MSF are currently facing the prospect of having to pay very high fixed charges and demand charges relative to our annual import of electricity. Consequently, we would welcome a method of determining fixed charges and demand charges that better recognises (a) that sugar mills are predominantly suppliers of electricity to the grid, and (b) the fact that the mills’ maximum import demand will not occur during the Summer period when the network may be constrained. (This reduces the impact that our imports may have on the network’s infrastructure requirements).
- We note that the QCA may introduce unintended problems by having a different approach to calculating network costs for residential and business customers. Specifically, Ergon Energy will now have a strong incentive to further increase network tariffs for business customers relative to residential customers in order to minimise the Government’s Community Service Obligations. This is similar to the situation in Victoria before the introduction of Full Retail Contestability, which at the time was fully exploited by the Victorian distribution companies in their quest to maximise revenue.

Discussion of Issue No 3 – Energy Costs, Retail Costs and Margins

We are of the view that the QCA may hinder rather than promote competition if it continues to accommodate retailers’ perennial demands to increase cost elements and margins in the regulated electricity tariffs. This concern is particularly relevant in the residential market where the true measure of success is whether customers receive competitive prices and service (i.e. customer switching rates is not a good indicator of effective competition). We have noted that due to the established practice of only offering about 10% discount to “bundled” prices published by incumbent retailers, even when actual margins are as high as 30-40%, incumbent retailers in Victoria have been allowed to extract extremely high profit margins over the last 5 years.

We are pleased to note that the QCA will apply market prices rather than Long Run Marginal Cost to determine wholesale electricity prices. Furthermore, we agree with previous submissions that the respective cost elements for residential and business customer tariffs are too generous in the following areas:

- The actual market price of Small-scale Technology Certificates is well below $40
- Acquisition and retention costs are not real costs for the majority of customers in Ergon Energy's distribution area
- With respect to retail margins, evidence from the contestable market suggests that:
    - The percentage margin should be significantly reduced for large I&C customers (i.e. the QCA may apply a sliding scale from say 2.0 - 5.4 %)
    - Operating costs are included in the retail margin for large I&C customers (i.e. not regarded as a separate cost component)
- It is not appropriate to make allowance for headroom when the majority of customers have no real choice but to remain on the regulated tariff. This item alone will be worth millions of dollars in extra revenue for the retail company Ergon Energy Queensland (EEQ).
- A cost pass through mechanism for once-off costs should not be considered unless it clearly sets out how these costs are to be offset against earnings from headroom and excessive margins.

In summary, if there is to be a transfer of money from electricity users to electricity retail companies over and above actual costs, we believe the QCA must demonstrate ex ante how it expects this to benefit energy users in the long run. In order to firmly establish accountability for determination of regulated electricity prices it is also sensible to undertake post implementation reviews to confirm that that the expected benefits have actually been achieved.

<u>Concluding Remarks</u>

The current price determination process is important to all electricity customers outside SEQ as it will determine the price path for many years to come. The hope is that the price path for regional Queensland will follow that of SEQ.

We wish to stress that revenues earned by sugar cane growers and millers are largely determined in the export markets for raw sugar, and that it is essential for the industry to remain cost competitive. Therefore, the entire industry needs access to competitively priced electricity.

Should you wish to discuss any details of this submission please call myself on (07) 4043 3324 or email gunnarandresen@msfsugar.com.au.

Our CEO Mike Barry is also more than happy to be contacted direct on 0401 896 999.

Yours sincerely,

[redacted]

Gunnar Andresen
Commercial Manager