Submission to the Queensland Competition Authority on the Draft Methodology Paper: Regulated Retail Electricity Prices 2012-13

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Contents

Executive Summary

Origin Energy (Origin) appreciates the opportunity to respond to the recent Draft Electricity Methodology Paper issued by the Queensland Competition Authority (QCA) and the accompanying expert report by ACIL Tasman (ACIL).

The Draft Methodology Paper is the second paper released by the QCA as part of its determination of regulated retail electricity tariffs for 2012-13. Origin's submission to this Draft Methodology Paper should be read in the context of our response to the previous Issues Paper, which covered discussions on broader framework issues around the calculation of energy purchase and retail costs as well as the pass through of network costs.

The complexity of the task facing the QCA and its consultants cannot be underestimated. The Ministers Terms of Reference (ToR) requires the QCA to determine energy purchase costs, retail operating costs and a retail margin for 2012-13 that will include significant changes in the national and Queensland electricity market. Most important being the level of uncertainty around energy cost and the carbon tax which increases risks combined with the lack of a cost-pass through provision to mitigate such risks.

Origin believes that in order for the QCA to successfully satisfy the ToR, they must observe some fundamental principles:

- the regulated retail tariffs should be cost reflective and based on the actual costs of supply. This includes a suitable mechanism to allow for the recovery of costs that are incurred during a pricing year as a result of a new regulatory obligations or a change in market conditions;
- the methodology should encourage competition and be consistent with the Queensland Governments policy objective that consumers, where possible, have the opportunity to benefit from competition;
- the cost of energy component should seek to maintain price stability and ensure customers are not subjected to unnecessary price volatility from year to year;
- that all policy uncertainties and market risks must be fully recognised in the retail cost and retail margin allowances;
- individual tariffs should be assessed to determine their appropriateness which includes ensuring an alignment of network and retail tariff components for customers in South East Queensland; and
- the methodology needs to be transparent and repeatable from year to year to give some certainty on the process that will be undertaken and how regulated retail prices are determined. Origin recognises that given the current market circumstances, it may not be possible to use a methodology for estimating energy cost that is repeated next year but in that case, the QCA should utilise a recognised and transparent method that estimates the costs of a retailer.

These principles need to be adhered to if the QCA is to maintain an appropriate level of competition in Queensland. The greatest risk to the long-term interests of Queensland electricity consumers, retail competition and all Queensland retailers is that the energy purchase costs are under-estimated.

The absence of reliable market data, due to uncertainties around carbon, creates difficulties for the QCA as it has stated its preference for a market based methodology over the use of a long-run marginal cost (LRMC). However, a solution for this short term problem is required.

Origin proposes that in the absence of any market traded data, LRMC is the best proxy for a retailer's contracting cost. LRMC is most appropriate given the carbon uncertainty and premium factored into any market prices over this period either directly or passed through in carbon clauses that have yet to be absorbed.

Origin notes that with the finalisation of carbon policy, the contract market for 2012-13 has commenced trading with volumes and prices becoming more readily available. This does provide the QCA the opportunity to use this evolving data for the next six month period (November to April) in its market based approach. However, it would still require the use of LRMC to estimate contracted prices for the remaining period but together, such a method would provide an appropriate, defendable benchmark for a retailer's energy purchase costs for 2012-13.

As such, Origin submits that:

- given the increasing availability of contract market data, Origin believes that QCA's market approach can be partially applied but it would require the use of LRMC to reflect the energy purchase cost for those periods that no contract data exists. The long run marginal cost calculation does not include the uncertainties and risks surrounding other methods;
- the energy costs must take account of the full price of carbon; and
- the under-recovery for the 2012 SRES costs and future SRES liabilities are best addressed by basing the SRES cost input for the tariff year upon the published binding estimate for the most recent calendar year. For example, the QCA would use the binding STP estimate for 2012 for the 2012-13 tariff year.

Origin would also highlight that although the QCA has attempted to meet the majority of the key principles of the review, little consideration was given to the principles of competition or ensuring price stability for consumers of electricity in Queensland. If this was given weight then the QCA needs to consider that:

- given the absence of any specific allowance in other cost elements, such as retail margin, competition will essentially be driven by the level of the energy cost allowance. If the proposed energy allowance is insufficient or increases risks then this will lead to little or no competition in the Queensland electricity market; and
- the risk of price instability is high under a pure market based approach. A market based approach may limit the 2012-13 regulated retail tariffs but will cause large price volatility from year to year as market prices vary. Including LRMC in the calculation of energy costs will moderate the fluctuations in energy prices.

In making the 2012-13 retail pricing determination, the QCA will be faced with many policy and operational uncertainties and will need to adopt a flexible and transparent approach. By adopting the principles described above, the QCA is more likely to achieve the Minister's objectives of cost reflective regulated retail tariffs while maintaining a competitive retail energy market in Queensland and protecting the long term interests of customers.

1. Background

On the 26 June 2009, the Queensland Premier and Treasurer directed the Queensland Competition Authority (QCA) to review electricity pricing in Queensland. Origin participated in that review and was generally in agreement with the QCA's findings that:

- the benchmark retail cost index (BRCI) methodology had a number of flaws;
- the current retail electricity tariffs were unlikely to reflect the costs of supply;
- an alternative network (N) + retail (R) pricing approach would offer significant improvements to cost reflectivity compared to the existing BRCI methodology; and
- network and retail electricity tariffs should be aligned.

On 11 May 2011, the Minister for Finance and the Arts and Acting Treasurer and Minister for State Development and Trade made a Ministerial Direction requiring the QCA to investigate and report on:

- an alternative retail electricity pricing methodology for the determination of the cost components under an N + R approach; and
- an alternate set of retail electricity tariffs, based on an N+R approach, which could be applied from 1 July 2012.

On 22 September 2011, the QCA received a Delegation from the Minister for Energy and Water Utilities (the Minister) further setting out the principles for determining regulated electricity prices to apply from 1 July 2012. The Delegation included a Terms of Reference (ToR) for the price determination.

The ToR specifically states that the QCA should ensure its price determination has regard to:

- the actual costs of supplying electricity;
- the effect on competition in the Queensland retail electricity market; and,
- the Queensland Government's Uniform Tariff Policy ensuring customers of the same class pay the same tariff for their electricity supply, regardless of geographic location.

The ToR further sets out that the in the QCA's pricing determination, N (network costs) should be treated as a pass-through and R (energy and retail cost) should be determined by the QCA. Energy cost component of each regulated retail tariff should include the cost of purchasing energy, environmental and renewable energy costs, energy losses and any market fees. In terms of retail costs, the QCA must consider the retail costs that would reasonably be incurred by an efficient, representative retailer and include an appropriate retail margin giving consideration to any risks not compensated for elsewhere.

It is noted that the Government highlights that the QCA must consider the impact of price changes on consumers when determining regulated prices. Although there are likely to be customer impacts within this tariff reform process which may require some transition, Origin would encourage the minimal use of such arrangements if this large and complex process is to be completed effectively.

1.1 Retail Competition in Queensland

In making a pricing determination, Origin understands that the QCA must consider s90(5) *Electricity Act 1994* which requires the QCA to have regard to *"the effect of the price determination on competition in the Queensland retail electricity market"*. Origin believes

that this is a critical aspect that needs to be considered as part of the 2012-13 pricing determination. The issue facing the QCA is that this is an unprecedented change to regulated retail tariffs and there is little historical data on certain elements of the decision to guide the QCA.

Origin notes the QCA's commentary in the Draft Methodology Report with regards to the level of competition in South East Queensland and the number of retailers that are participating in both the small and large customer segment[1]. This analysis by the QCA suggests that retail competition in Queensland is effective and prices should be deregulated in the near future. However Origin understands that this issue will not be considered until the Australian Energy Market Commission (AEMC) conducts its review of competition in Queensland in 2013. Until this time, Origin urges the QCA to ensure the methodology framework is:

- transparent around the modelling approach and quantifying all the relevant risks;
- flexible and provide opportunities for pass through of direct and indirect costs; and
- focussed on the end goal of competitive markets and price deregulation as agreed by the Minister under the AEMA principles.

The market will only remain competitive as long as regulated retail prices reflect the actual costs and risks of operating in the market.

[1] QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p12.

2. Representative Retailer

Origin notes the QCA considers that an appropriate definition of a representative retailer is one that:

- is an incumbent retailer of sufficient size to have achieved economies of scale;
- serves small and large retail customers in South East Queensland and other jurisdictions across the NEM;
- retails electricity on a standalone basis; and
- is not vertically integrated with an electricity generator[2].

Origin supports the approach of providing clarity around the fundamental construct of how a representative retailer should be defined. While Origin supports the majority of the assumptions the QCA has made about a representative retailer, comments on each of the elements are discussed below:

- *an incumbent retailer of sufficient size to have achieved economies of scale:* There are two issues with this approach. Firstly, the use of the incumbent retailer ignores the higher cost base of a new entrant retailer and second, in is uncertain how the QCA will define the impact of economies of scale? The retail cost allowance must be sufficient to maintain competition in line with the ToR;
- *serves small and large retail customers in South East Queensland and other jurisdictions across the NEM:* Origin accepts that the majority of retailers operate across jurisdictional borders and supply an array of customers. However, it is not clear how this assumption is built into the other elements of the pricing framework as the risks of market customers and, in particular, interstate competitive operations are different and may vary by jurisdiction;
- *retails electricity on a standalone basis*: This reflects the state of competition in the Queensland energy market and appears reasonable; and
- *is not vertically integrated with an electricity generator*: Origin agrees with this assumption in terms of the principle of "competitive neutrality". However, it should be recognised power purchase agreements are integral to the energy portfolio of both integrated and stand alone retailers.

In further defining the characteristics of a representative retailer, there are important changes that are occurring in the energy market which Origin believes the QCA should consider carefully when determining a representative retailer's costs. These include:

- the changes to tariff structures, removal of tariffs and new tariff arrangements from 1 July 2012 will be a significant expense item from a capital and ongoing cost point of view. Billing systems need to be re-designed, effective communication provided to customers and customers will need to be moved from obsolete tariffs to more appropriate tariffs. Origin also expects a substantial increase in calls to our service centre as customers query inclining tariff block structures, the new voluntary time of use tariff and why they have been forced onto new tariff arrangements. This will specifically impact on the operating costs for retailers operating in the Queensland electricity market in 2012-13;
- the costs of administration and reporting obligations under the carbon tax from 2012;
- the implementation of the National Energy Consumer Framework (NECF) from July 2012. The NECF will create a national framework for the regulation of the sale and

[2] QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p13-14.

supply of energy, including billing, marketing and customer/retailer relationship. A significant amount of work is already being undertaken to prepare for these regulatory changes; and

- other changes in the regulatory environment which may impact on a retailer's costs. For instance, the Government has been considering the implementation of green energy initiatives including emission graphs on bills, mandatory green energy offers as well as discussions around enhancing hardship policies. Any required changes to systems and processes to accommodate these measures are likely to be costly. There should be opportunities for reasonable recovery of those costs in the regulatory pricing framework.

Origin considers that the QCA should explicitly identify and consider the impact of future regulatory and market developments and make appropriate allowance in the retail operating costs for changes retailers have to make in systems and processes as a result and ongoing management and reporting of the various arrangements. This is particularly important given the QCA's proposed definition of retail margin does not allow for regulatory change risk.

Moreover, the various industry changes listed above have, in turn, implications for the benchmarking approach. It is most unlikely that these future retail operating costs are adequately reflected in the previous benchmarking decisions whether in Australia or overseas.

3. Treatment of Network Costs

It is essential that the N+R pricing framework explicitly allows for the full cost pass through of network tariffs to consumers in regulated retail prices. Furthermore, in Queensland, Origin supports the QCA's views that the N component of each tariff should be equal to the approved Energex network price.

Origin's specific comments in response to the network issues raised in the Draft Methodology Paper are set out below.

Table 3.1 Origin's Response to network issues

Issue	QCA Proposal	Origin Response
Domestic Inclining block and time of use tariffs	Energex's network tariffs should be the basis for determining the retail tariffs	Agreed
Tariffs for farmers, irrigators and customers supplied under the Rural Subsidy Scheme	T66 aligns with NT8300 T67,68 align with NT8500/8600 T62, 65 align with NT8700/8800	Agreed
Tariff for Ergon Energy's large customers greater than 4GWh	QCA could require Energex to calculate one or two network tariffs that reflect the average to its cost reflective network tariffs for all of its very large customers.	Matter for Ergon Energy.
Streetlighting asset charge for Ergon Energy	No asset charge will be included in the streetlighting network tariff.	Matter for Ergon Energy.
Obsolete and declining block retail tariffs	Removal of obsolete tariffs from 1 July 2012. T21 customers moved to network tariffs 8500/8600. T37,62,63,64 customers moved to network tariffs 8700/8800	Origin agrees with the proposed network tariff assignment except for T37. Origin and Energex have agreed that T37 customers will move to network tariff 8500/8600 as a default.
Other tariffs (prepaid) card meters	Create a regulated retail tariff available only to small customers on card operated meters based on one, of the charges in Energex's small customer inclining block tariff.	Matter for Ergon Energy.
Watchman lights/traffic signals	Align retail tariffs 81 (traffic signals) and 91 (watchman service lighting) with network tariff 9600.	Agreed.
Maintaining alignment of retail and network tariffs	Request Energex to supply the QCA with its proposed network prices when submitted to the AER and use these as the basis for notified prices to apply from 1 July. Should there be any change to these proposed tariffs, regulated retail prices could be adjusted after 1 July to this.	Agreed.

4. Energy Cost Component

4.1 Estimating Wholesale Energy Cost

Carbon pricing has introduced significant uncertainty into the electricity market for 2012-13. Establishing a new tariff structure based on a cost build up approach from the 2012-13 year is problematic as uniquely it coincides with the introduction of carbon pricing in Australia. Both ACIL and the QCA appear to have accepted, based on carbon uncertainties, there is an absence of sufficient trading data in forward electricity contracts that will preclude the implementation of a reliable market based methodology[3] for the entire year.

The market conditions have created difficulties for the QCA as it advocates a market based methodology best reflects the actual costs of a retailer's wholesale energy purchase costs. However, the absence of reliable market data makes this challenging for the 2012-13 contract year.

Origin takes the view that the approach selected for 2012-13 must take account of the current situation and the calculation of the energy cost component must rely on an alternative method, even if only for one year.

4.2 QCA Proposal

The Draft Methodology Paper sets out the QCA's preference to pursue a market-based approach over a LRMC proposal as it takes the view that LRMC:

- is an estimate of generation costs as opposed to purchasing costs of a retailer;
- ignores the prevailing market conditions which may have an influence on the purchasing cost of some retailers; and
- is not a product of the operation of the spot price in the NEM.

Origin maintains that the LRMC is a key element for pricing the energy products of its retail business. Origin is a large retailer operating within all NEM jurisdictions with the risk policy of a prudent retailer. As such, the prevailing market conditions will only be one factor impacting on the wholesale energy cost structure built into Origin's retail pricing position.

A prudent retailer must purchase adequate cover to insure against high market prices whether they occur or not. Origin takes the view a representative retailer's energy purchase cost structure will never track with the NEM spot price at a singular point in time and therefore believes the statement:

> *"The Authority also continues to question why this security [LRMC] would be needed with regulated prices but not if the market was entirely deregulated, in which case only market costs would be available"*[4]

is based on an erroneous assumption that the energy pricing policy of a prudent retailer is inextricably linked to the NEM spot price.

Compared to a simulated modelling approach, a robust forward looking market based methodology utilising an appropriate hedging and risk strategy may, as a proxy method, replicate the energy costs of a representative retailer.

[3] refers to the energy purchase cost methodology used in previous BRCI modelling
[4] QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p23

Based on insufficient trading data being available to use a "real data" market based methodology, the QCA has proposed an approach recommended by ACIL to establish energy purchase costs that is new and untested. Origin views this approach as fundamentally flawed as it is solely a black box model that takes no account of the risk premium paid by a prudent retailer. As such, Origin strongly believes the methodology proposed as Approach 3 fails to both observe the requirements of the TOR and the objectives for constructing a new tariff structure to emulate actual costs.

In its draft methodology for estimating energy purchase costs report (Report), ACIL considered four methods for establishing wholesale energy purchase costs:

1. Long Run Marginal Cost;
2. Market Based Approach;
3. Annual Price Distribution; or
4. Combination of LRMC and Market Based Approaches.

The separate methods are considered in detail below.

4.2.1 Long Run Marginal Cost (Approach 1)

Origin does not agree ACIL's arguments rejecting the use of LRMC as these points equally apply to Approach 3, which in turn, is recommended by ACIL.

Origin believes that LRMC provides several advantages including:

- It is a forward looking approach that better approximates the actual costs of retailers' purchases through power purchase agreements;
- it is linked to the NEM as generation investment influences the prices in the spot and contract market, along with other factors, but it is not wholly dependent on market conditions at a singular point in time; and
- it is an estimate for average energy purchase cost that has theoretical merit as well as being readily modelled and identifiable. Contracting to mitigate future market risks increases a retailer's average purchasing costs. Attempting to ascertain the necessary risk premium to be added onto a distribution of simulated average spot price costs (Approach 3) increases the risk that this value will be understated.

Most importantly, using LRMC will provide stability over time. Market conditions impact wholesale prices and varying price signals will result in significant price shocks both up and down.

The LRMC is not affected by the volatility of wholesale energy markets and acts to smooth the energy cost allowance over time. Therefore, LRMC holds an advantage over a market based method as it will have a stabilising effect on tariffs from one year to the next, rather than exposing consumers to significant variations in market prices each year.

In contrast, a market methodology will not maintain price stability. The LRMC calculation will also counterbalance the absence of reliable market data and is the best option of the approaches canvassed by ACIL. The difficulties associated with establishing an appropriate simulated market price model (Approach 3), the multitude of assumptions and the absence of an appropriate risk premium negates the validity of it as a market methodology and therefore it is inferior to a LRMC method.

In Origin's view, this supports using LRMC either in itself or within the Market Based approach described in the following section.

4.2.2 Market Based Approach (Approach 2)

A number of issues were raised regarding the application of retailer contracting methodologies in relation to Approach 2:

- *"It is also difficult to determine a contracting strategy that is representative of a prudent retailer …Arriving at a hedging strategy which represents an appropriate approach in the current circumstances presents significant difficulties."*[5]
- *"A further weakness of this approach is the need to determine an appropriate retailer hedging strategy and providing estimates of forward contract prices. While some contracts are bought in over the counter trades at transparent market prices a high proportion of retailer hedges are bought through bilateral negotiations with generators. In these cases the prices and other terms are not known."*[6]
- *"...does not take into account bilateral contracts for difference (CFDs) between generators and retailers. These contracts can form a high proportion of the retailers' contracts and may contain quite different price, volume and term conditions to the over the counter contracts presented in public sources."*[7]

Origin would note that these points were not a concern in previous tariff reviews conducted by ACIL using the same methodology.

The difficulty obtaining contract prices for the 2012-13 period is cited by the QCA as the main reason for not using its preferred Market Based approach this year. Origin agrees that this is a severe limitation to using this method in isolation.

Origin agrees with ACIL's recommendation that there is insufficient liquidity in the contract market prices for 2012-13 to support a market based approach. Over the past two years there has been minimal trading in the 2012-13 contract market due to the uncertainty of the Federal Government carbon pricing scheme.

This has improved in recent weeks since the scheme has been legislated. However, even if liquidity improves by early 2012 it is doubtful the average contract prices for 2012-13 will provide a singular, reliable guide due to the limited 6 month trading timeframe. This is the predicament for a market based method without reliance on an alternative method.

The previous application of the market based method was based on a two year hedging horizon. Origin proposes that the latter six months of that period will be able to be sourced as previously (eg. d-cypha) while the preceding 18 months will need to be constructed from a different source, namely LRMC based information. For example the cost of $300/MWh caps for the hedge portfolio would be based on the LRMC of an open cycle gas turbine (OCGT). With this adjustment, the Market Based approach could be used.

4.2.3 Annual Price Distribution (Approach 3)

Origin is strongly opposed to the recommendation by ACIL that its Annual Price Distribution (Approach 3) is the most reasonable and robust approach to estimate energy cost available today. Origin does not credit this method as practical, robust or sustainable.

As recognised by ACIL, this approach has little transparency to allow verification of the input and the model calculations. The risks associated with this approach far exceeds the margin allowed for in this tariff review and is far greater than the risks associated with utilising the LRMC or in a more liquid market, the Market-Based approach (Approach 2).

[5] ACIL Tasman, *Draft methodology for estimating energy purchase costs*, November 2011, p13.
[6] Ibid, p13.
[7] Ibid, p12.

The mean outcome of the proposed model does not resemble an approach of a prudent retailer nor does it bear any resemblance to the actual cost of supplying energy in Queensland[8]. Notwithstanding the effort involved in the model to produce 820 data years of half hourly prices involving variations in weather driven demand and plant outage outcomes, an obvious flaw in the approach is its failure to account for actual cost.

Origin questions the likely outcome for retailers if there is an extreme weather year or unpredictable generator pressures in a given year. Such an outcome will see retailers exposed to high market prices and any retailer without adequate hedge cover will falter, resulting in market failure and serious impacts upon competition. An acceptable approach must preserve the current competitive pressures in Queensland by establishing an adequate energy purchase cost; Approach 3 does not achieve this.

Origin's concerns with Approach 3 include:

- there is no material justification for basing the resultant energy purchase cost on the mean outcome of the simulations; It does not recognise the required risk margin (balance sheet capacity) required to withstand the volatility implied in ACIL's methodology;
- ACIL's recommendations to adopt the Annual Price Distribution approach are inconsistent with its criticism of the black box nature of the Market Based approach; and
- it is based on historic pool price modelling projected forward with no mechanism for future market costs to be incorporated such as changes in market bidding dynamics due to carbon or industry restructure.

These issues are described in more detail below.

Mean Price of Simulations and Risk Margin

ACIL has claimed that:

> *"The approach recognises that it is appropriate for a prudent retailer to hedge risks through energy purchase contracts which will attract a premium over the expected spot market price under "normalised" weather, outage and other conditions. Under the approach it is contended that the retailer will be prepared to pay price of electricity which is represented by the mean of possible prices outcomes…."*[9]

The volatility of pool cost outcomes from ACIL's proposed Annual Price Distribution approach imply a significant level of risk margin required to withstand the year on year variation in cash flows. Using the last 10 years of pool price outcomes this theoretical model would have estimated the mean cost of energy purchases at $43/MWh. However, over this period the cost has ranged from as high as $62/MWh in 2007 down to $32/MWh in 2005. Due to a prudent hedging strategy actual energy costs have exhibited much less volatility but have however reflected a significant premium above the mean of $43/MWh.

A prudent retailer must possess sufficient balance sheet capacity and liquidity to withstand these extreme events or limit their impact through hedging. Hedging profiles are typically designed to cover a 1 in 20 year extreme event. Consequently Origin believe the contract premium evident both historically and in the forward markets reflects the asymmetrical impact of these extreme events and their potentially disastrous impact on a retail business. Origin feels that ACIL's proposed methodology fails to capture these risks in the following areas:

[8] ACIL Tasman, *Calculation of energy costs for the 2011-12 BRCI Final Decision*, 30 May 2011, p10.
[9] ACIL Tasman, *Draft methodology for estimating energy purchase costs*, November 2011, p20.

- the use of one historical demand year pattern to imply consumer behaviour over a number of weather scenarios. The use of this one particular year will significantly understate load volatility and for this reason is not a prudent approach; and
- the risk premium inherent in the contract prices would be materially larger than the difference between the median and the mean of the price distributions implied in ACIL's proposed methodology.

In summary Origin consider the risk premium inherent in contracts prices and hedge portfolios to be appropriate and materially larger than difference between the median and the mean of the price distributions implied in ACIL's proposed methodology.

Although ACIL's method considers other costs and risks of a retailer that may warrant a further premium to the mean outcome, it concludes that these are unnecessary. ACIL has presented[10] factors that are likely to influence energy purchase costs and remarkably ACIL has assumed these factors are accounted for by using the mean except for the time value of money in forward contracting. It is imprudent that ACIL would assume that a representative retailer would not be prepared to pay more than the mean of the price distribution.

Origin argues there is no theoretical basis for taking the mean, as a retailer will hedge load at the best available market prices and through various instruments according to its own risk policies to ensure the viability of the business.

Reliance on Black Box

To cite weaknesses with Approach 3 it is appropriate to use ACIL's report:

> *"It relies on a proprietary market simulation model, a "black box", into which assumptions concerning generation capacity, load growth, outages and generator bidding behaviour are brought together using a replica of the AEMO market settlement algorithm to produce half-hourly regional reference prices (RRPs)."*[11]

> *"…. the "black box" nature of such models ….. contain many implicit assumptions about the way the market operates … These model features have usually been developed over time on the basis of the modellers' research and experience and they are not easy for an outsider to verify."*[12]

These arguments are presented as weaknesses of the Market Based Approach (Approach 2) however they are more relevant criticisms of Approach 3.

Approach 3 makes no attempt to limit the resulting volatility of the pool price distributions via hedging, unlike the Market Based approach. The Market Based approach, while also dependant on the black box outputs for its spot price modelling is counterbalanced with the application of a hedge portfolio to stabilise the cost of the energy purchases. The nature and purpose of hedging is to reduce the dependence of a retailer on the spot market. This is born out in the results of the Market Based approach where the hedged cost is far less volatile, albeit more expensive (the risk premium) on average than the unhedged pool costs.

Approach 3 is solely dependent on the outputs of the black box model (*PowerMark*) therefore any criticisms of a black box methodology are far more applicable to it than to any of the alternative approaches.

[10] ACIL Tasman, *Draft methodology for estimating energy purchase costs*, November 2011, p19.

[11] ACIL Tasman, *Draft methodology for estimating energy purchase costs*, November 2011, p12.
[12] lbid, p12.

Changes to market bidding behaviour

ACIL also concluded regulatory proposals or changes will not impact 2012 prices but Origin believes the impact of the carbon pricing is a regulatory change and is a valid and eminent risk. Although the market is aware carbon will be introduced, it still poses a risk to retailers in the tariff year as the $23 per tonne carbon price will result in an unknown impact upon the NEM prices at this stage which modelling can only partly resolve.

In addition, the rationalisation of the Queensland Government owned generators into two companies will lead to market concentration that will deliver more co-ordinated bidding strategies than previously and has already had a marked effect on pool prices. This may yield higher pool prices for 2012-13 once the carbon tax commences.

The application of the NEM bidding strategies as described by ACIL in the black box modelling appear to reflect (recent) history and therefore to do not readily accommodate these structural market changes where history does not exist.

4.3 Origin's Preferred Approach

Origin proposes that the QCA's preferred Market Based Approach can be accommodated within the constraints of the 2012-13 circumstances. In short, this method, as used previously within the BRCI framework, could be supplemented where contract prices are not available with an LRMC cost base for the hedge contract prices.

Origin considers this view has merit as the current trading activity for forward contracts in 2012-13 has improved in December with more certainty emerging around carbon pricing. However, the available market data will span at most a six month trading period (i.e. November-April) and requires blending with LRMC to accommodate the shortened availability of market data balancing the LRMC method with prevailing market conditions.

While conditions exist that curtail energy market trading, retailers are forced to resort to other methods of hedging protection, the LRMC is a reasonable proxy for the value of energy purchase costs in times of market uncertainty. In Origin's view, the QCA should accept the LRMC is also an appropriate marker of the energy purchase cost for a prudent retailer in a competitive market.

Origin submits this method will construct an appropriate benchmark for a representative retailer's energy purchase cost for 2012-13.

4.4 Customer Load Forecasts

The QCA believes estimating energy costs by tariff class will better approximate the proportion of a retailer's total energy costs incurred rather than allocating total energy costs uniformly across all tariff classes. Based on this, the QCA proposes to rely on load forecasts for individual tariffs provided by Energex for 2012-13 year and on the forecasts in AEMO's Electricity Statement of Opportunities (ESOO) for demand and consumption forecasts in each NEM region. This cannot be achieved with the limited customer profiling in Queensland.

For energy purchase costs, for all tariff classes, to be cost reflective the load profile must be based on the current Queensland NSLP minus non-residential customers consuming greater than 100MWh per annum. This is the profile for which each retailer settles the load of tariff customers in the Queensland market except for controlled load tariff 31 and 33 which should be treated separately.

In regard to changes to the residential tariff 11:

- If the inclining block tariff impacts the load profile of residential customers, this is unlikely to have a major impact upon the NSLP. However, if there is an impact this will not be apparent until the tariff is implemented and will be taken into account in the NSLP for 2013-14; and
- there should not be a separate load profile established for residential customers on voluntary time of use tariff nor should the load of these customers be removed from the NSLP. The time of use tariff is voluntary and customers may move between inclining block tariff and time of use with no penalty once every year. While the tariff remains voluntary it must continue to be settled based on the NSLP.

The final modelling challenge relates to the selection of only one year of load history to base the model on. There are many features of customer load that are always at risk of occurring, but may or may not actually occur in any given year. The purpose of hedging for a retailer is not to predict the individual outcomes of any one year, but to insure against a wide variety of likelihoods. An excellent example of this is demonstrated in the Final Decision for the 2011-12 BRCI.

ACIL highlight:

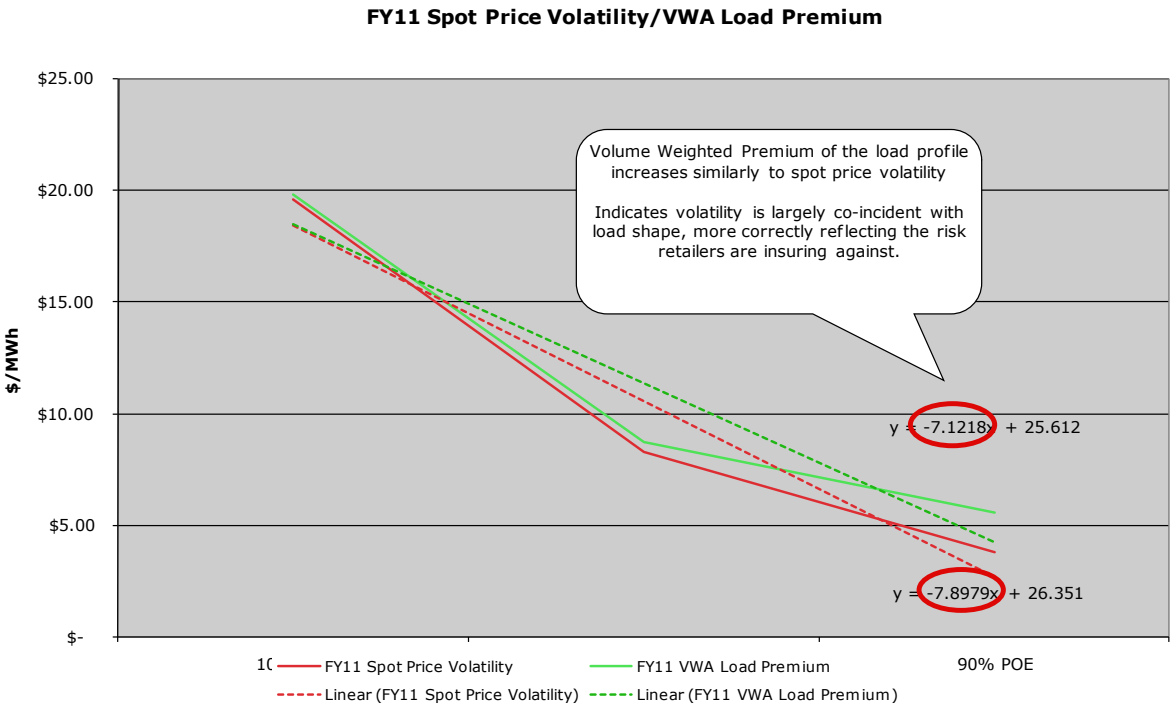
> *"The quarterly RRP changes between the Final Decision for the 2010-11 BRCI and the Final Decision for the 2011-12 BRCI…the most significant change occurs in the December quarter in 2011, where prices are lower by around $46/MWh in the 10%POE, $21/MWh in the 50%POE, and $10/MWh in the 90%POE. This is due to a lower and less peaky load trace in the December quarter 2010, reflecting the mild wet conditions in this quarter compared to the December quarter 2009."*[13]

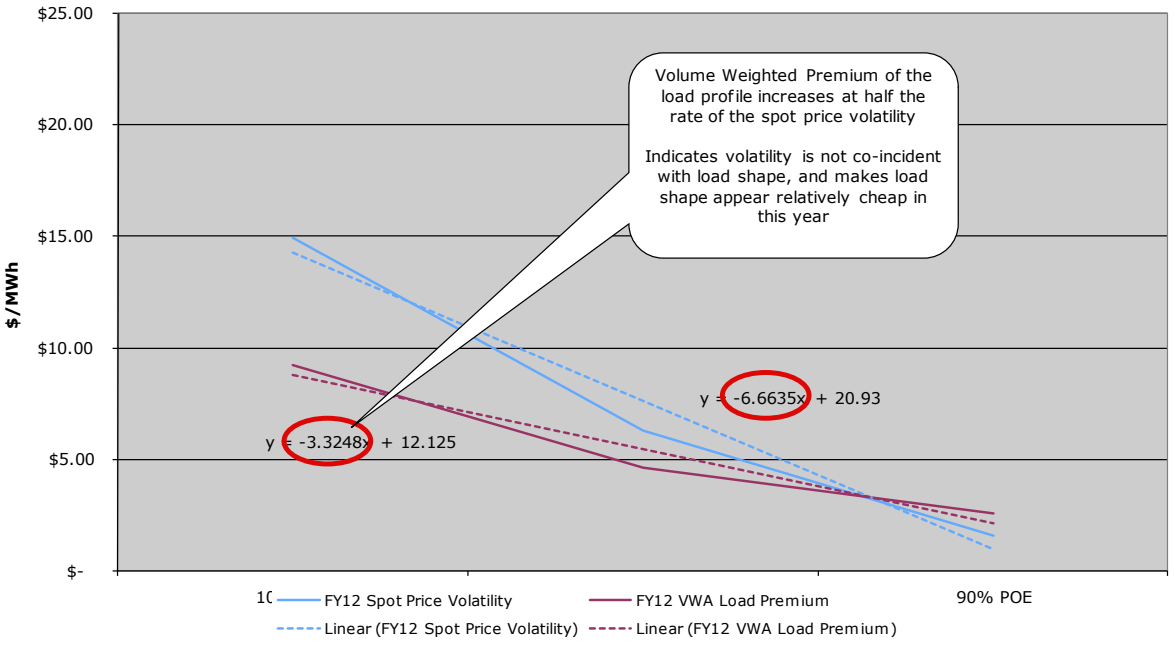
It is important to reflect the full range of possible load (weather) outcomes as this is what the retailer must insure against. One does not know at the time of hedging (1-3 years in advance) if the weather conditions will be extreme or mild for example on any given day, week or month. So the retailer's hedge portfolio must accommodate the envelope of plausible outcomes, not just the behaviour (in hindsight) of a particular year in history. In the 2011-12 Final Decision this is worth circa $4/MWh for the 50%POE load forecast.

Further, the relationship between price volatility and load forecast is also critical. The relationship between spot price volatility and Volume Weighted Premium is highlighted in the charts below where the 2010-11 load data was highly co-incident with spot price volatility, while the 2011-12 load profile reflected a 50% co-incidence. In this example the 10% POE load cost differs by more than $10/MWh due to this attribute.

Finally, the relationship between load and weather is often non-linear at the extremes. Therefore mapping a year of mild load outcomes to 40 years of weather history will almost certainly understate the volatility in load that occurs with some of the weather conditions of the past 40 years. It is essential that the load/weather relationship is based on more than one year of load data.

[13] ACIL Tasman, *Calculation of energy costs for the 2011-12 BRCI Final Decision*, 30 May 2011, p37.





4.5 Accounting for Energy Losses

Origin accepts the proposed approach by the QCA to adopt the most recent transmission and distribution loss factors relevant to the Energex area published by AEMO available at the time of finalising the price determination. The wholesale energy cost will need to be escalated by these losses.

4.6 Carbon Pricing

The QCA propose to have ACIL run two pricing scenarios through its spot price model *Powermark*; one that is carbon-inclusive and one carbon-exclusive. These two pricing scenarios are based on the uncertainty surrounding the carbon price.

Origin believes that, given the high level of uncertainty regarding the impact of a price on carbon, exacerbated by a lack of liquidity, the introduction of a carbon price should be treated by the QCA as a separate and fully accounted for cost pass-through. As such, Origin does not support an allowance for carbon pricing in its pool price model as recommended by ACIL. The legislated carbon price is an input cost from July 2012 for electricity generation, and as such should be treated as a cost pass-through.

Origin's concerns with the ACIL calculation is the carbon tax impact has been modelled through its *Powermark* model rather than used as a pass through cost. The result of using the *Powermark* model is uncertain but Origin believes there is a genuine risk the costs will be underestimated. For example, ACIL used its *Powermark* model in a recent study of Solar Feed-in tariffs for South Australia. The model estimated the impact of carbon tax at $11 per MWh which is significantly less than the cost at the National or South Australian level of carbon intensity.

The introduction of the Carbon Tax also still has many regulatory features yet to be defined and understood. There is a broad expectation in the market that the $23/t CO_2-e tax will be passed through the energy price at the market carbon intensity (circa 0.9 tCO_2-e = $21/MWh). A 20 per cent error in this estimate is worth ±$4.15 per MWh, again a material risk to the retailer that cannot be hedged.

4.7 Queensland Gas Scheme

As many established retailers cover their long term liability for GECs, the need to trade regularly is removed. Retailers take up long term purchase agreements for GECs that provide for a fixed cost thereby avoiding short term price fluctuations. Origin has previously submitted that the LRMC more closely resembles the price paid by integrated retailers for GECs. In general, Origin supports a method to estimate the costs of GECs by using the long run marginal cost of gas-fired generation plant mix. While the QCA has decided to base GEC pricing on market data available from AFMA, Origin supports the proposal to use a longer time series of data to estimate GEC costs for 2012-13.

Market expectations are that the scheme will cease after commencement of carbon pricing but the scheme is based on the calendar year so it is likely to continue throughout 2012 as a minimum. However Origin believes it is sensible to calculate GEC costs for both 2012 and 2013 as actual costs until the Queensland Government announces otherwise.

4.8 Renewable Energy Target Scheme

To fulfil their RET obligations, retailers are obliged to surrender certificates for both markets. The impact of these schemes is material and if not properly quantified will encroach upon a retailer's margin. A retailer has no means of managing this risk and is reliant on regulated prices to allow for full and correct recovery of these schemes.

4.8.1 LRET

The QCA proposal is to calculate the LRET in the same manner as for the BRCI 2011-12. Origin has some concerns with an LRET estimate based on weekly market prices for Large-scale generation certificates (LGC) as published by AFMA. The estimated cost of LRET is based on market prices for LGC which includes the period of depressed REC prices.

As previously submitted, Origin believes using the data from a period of uncertainty when the REC market was depressed will under-estimate the actual costs to retailers. Origin does not consider the method proposed by ACIL to calculate a market price for LGCs will meet the requirements of a retailer's LRET liability for 2012-13. It is acknowledged the QCA is not privy to the price paid for LGCs in long term contracts but disputes the market price of LGCs is a better indication of the LGC price. Origin seeks adequate consideration of its retail liability.

ACIL has indicated the market prices have reacted over time according to the prevailing market conditions, for example, they fell when there was an oversupply and have recovered somewhat since the split of the LRET and SRES schemes. Origin believes this is hardly surprising the market price would react according to prevailing market conditions however this does not resolve the concern that, as previously submitted, the AFMA market data it is not the actual price paid by retailers.

Origin supports a calculation for the price of LGCs based on the LRMC of wind generation for two reasons:

- the two year historical market prices for LGCs is distorted; and
- the more recent market prices will not take account of the impact of carbon.

The LRET forward contracts market has been illiquid in the lead up to the legislated carbon position and will not resemblance the price paid by retailers in 2012 and 2013 for LGCs. Basing the market price on distorted historical data won't meet the actual obligations of a retailer to meet LRET.

As such, if the QCA is to continue with its market calculation for LRET then the price should be based on 18 months of previous data recorded by AFMA. This would take into account market prices from 1 January 2011 when the Expanded Renewable Energy Scheme commenced.

Origin believes this is the more robust approach than using two years of previous data as it will not include six months of distorted low REC prices. The average pricing suggested by ACIL is not a true indication of price as small or large trades at low or high prices will distort the average.

4.8.2 SRES

Origin agrees with the formula for calculating the SRES cost allowance outlined by ACIL including the $40 clearing house price. However, while the SRES costs are based on the non-binding estimate or an alternative forecast there will be general concern relating to the resolution of any differences between the final estimate and any estimate used in the final tariff calculation.

Origin's concerns stems from the QCA's decision to not allow any transitional recovery to account for the substantial forecast error triggered by the advice of ACIL in calculating the 2011 STP for the 2011-12 tariffs. ACIL predicted the take up of solar would significantly reduce the published non-binding estimate of 16 per cent in March 2011. ACIL's failed to recognise the significant overflow of certificates from 2010 would increase the March (2011) STP estimate, not diminish it, significantly impacting a retailer's margin. It appears that the losses to retailers will be in the order of $5.60 per MWh for the first six months of 2012. Such a risk is unsustainable and unreasonable.

The Ministerial Direction is explicit in its requirements for a retailer to supply customers based on actual costs of supply and the:

- failure of the draft methodology to provide for future accountability of errors and omissions in forecast; and
- deficiencies in the proposed cost pass through mechanism to include anticipated and unanticipated cost variations;

is a major concern for Origin.

Failure to take account of the significant shortfall in 2012 SRES costs will undermine the objectives of tariff review and ignore the underlying costs of supply. Origin considers that assuming the non-binding estimate for 2013 STP will suffice[14] (as indicated by ACIL Tasman) is inadequate unless there is certainty around a mechanism to adjust future tariffs for discrepancies. In this context and in the absence of an adequate pass through mechanism, an approach using actual costs of a retailer on a calendar year basis (compared with the 2012-13 financial year) as the underlying SRES cost component will mitigate these risks.

Therefore Origin, consistent with our submissions during the 2011-12 BRCI consultation[15], proposes that the QCA should apply the actual costs for 2012 SRES liability as the 2012-13 SRES costs. This would resolve the forecast error risk inherent in basing the SRES costs on the tariff year (as was done in the BRCI process). This approach relies on the actual cost of supply and introduces a six month timing lag between the time the costs are incurred and the recovery of those costs through prices yet has the advantages of:

- being reliable as it replicates the retailer SRES liability without the need for forecasting;
- is consistent with the terms of reference as it is derived from the actual cost of supply for SRES liability. The terms of reference do not confine the actual cost of supply to the tariff year in the same manner as the BRCI methodology and therefore the basis of denying the proposal in 2011-12 is no longer valid;
- removes the uncertainty of forecasting as ORER publish an annual STP for each compliance year going forward which will provide an exact measure of the liability. The binding STP for 2012 will be published prior to the release of the QCA's final pricing determination;
- enables retailer's to recoup the appropriate 2012 STP for a 12 month period and justifies the QCA's comments in the 2011-12 Final Decision[16]; and
- removes the requirement to include a cost pass through mechanism to wash up the actual SRES differences.

Regrettably, this method will not allow retailer's to recoup all previous under-recovery of previous SRES liabilities.

4.9 NEM participation fees and ancillary services charges

Origin supports the proposal to use an estimate for the cost of market fees and ancillary fees based on the methodology used in previous BRCI decisions.

[14] ACIL Tasman, *Calculation of energy costs for the 2011-12 BRCI Final Decision*, 30 May 2011, p22.
[15] Origin Energy, Submission to the 2011-12 BRCI Draft Decision, February 2011.
[16] *"The legislation does not allow the Authority to simply use historical values in place of forecasts (unless no better basis for the forecasts is available) or to provide a 'true-up' between actual and forecast costs in subsequent years. The BRCI is meant to be a self-correcting index and any forecast errors should be compensated for in subsequent years." QCA, 2011-12 Final BRCI Decision, p21-22.*

5. Retail Costs

The QCA proposes to consider retail costs in two separate categories[17]:

- *Retail Operating Costs (ROC)*: the operating costs that a representative retailer incurs in performing the retail functions required to serve its customer base; and
- *Customer Acquisition and Retention Costs (CARC)*: the marketing costs involved with acquiring new customers and retaining existing customers. The costs also include the costs of transferring customers.

Origin supports these two separate retail cost categories and these costs being treated on the same basis. That is, the total retail cost allowed each year includes bother CARC and ROC and they will change in the same manner. This approach appears appropriate given the way the market has matured and the manner this issue is dealt with by other Regulators.

5.1 Estimating Retail Operating Costs (ROC)

Origin notes the QCA proposes to use the current retail cost allowance as a starting point and to benchmark that allowance against those recently accepted in other jurisdictions. Origin supports this benchmarking approach as long as it is based on the current escalated Queensland retail operating cost as determined in the 2011-12 BRCI determination.

As noted in our submission to the Issues Paper, while we support a benchmarking approach, caution needs to be taken when analysing and comparing available information. This is given the different methodologies and parameters used by Regulators in approving retail costs and the ongoing market changes. This is particularly true in the retail sector where retailers operate under separate regulatory and market frameworks.

In particular, Origin has been most concerned with the data provided by the incumbent New South Wales retailers for the IPART pricing determinations and has not been able to reconcile this data with other market data and with our own experience of the costs of operating in a contestable market either as an incumbent or as a new entrant retailer. Further, historically, standard retailers in New South Wales have operated within a framework of shared systems and services. Such an assumption cannot be made to a Queensland retailer and careful analysis of benchmark data must be made to adjust for this factor.

Origin further believes that there should be distinctive cost pass through categories to take into account Queensland specific requirements. This may include items such as:

- allowance for licence fees which are significantly higher in Queensland than any of the other jurisdictions;
- the cost impact of the reform to retail tariffs in 2012-13 which will require significant system changes, customer communication and increased resourcing of service centres in response to increased customers queries;
- the cost of implementing the National Energy Consumer Framework (NECF) from July 2012 which will also require major system and process amendments; and
- any other changes in regulatory requirements that may arise in this process such as implementation of green energy initiatives including emission graphs on bills or additional Government assistance measures.

[17] QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p33-44.

Other ROC benchmarks do not take these additional costs into account. It should be noted that clause 13 of the QCA's regulatory fees framework provides a specific provision for the pass through of Queensland regulatory fees.

The QCA will have to exercise some subjective judgement on the reasonableness of the available information and forecast on what factors need to be adjusted for future developments. Origin is firmly of the view that if interstate benchmarks are to be relied upon, they need to be appropriately escalated to take into account the current dynamic market environment and the structure of the Queensland electricity market.

It is well known that if a retailer's costs are greater than an allowed benchmark, retailers will aim to drive costs down. If a retailer has actual costs below an allowed benchmark, they will drive costs down further to achieve higher returns. This drives dynamic efficiency and is in the long term interests of electricity consumers.

5.2 Customer Acquisition and Retention Costs (CARC)

Origin understands the QCA proposes:

- treating CARC in the same manner as other retail costs, as done in the 2011-12 BRCI decision; and
- including the current (suitably escalated) 2011-12 allowance in the retail cost estimate[18].

Origin supports the QCA's proposed approach. As noted by the QCA, the inclusion of CARC is necessary to ensure the competitive functioning of the Queensland electricity market. CARC is a real cost incurred by retailers participating in a competitive market from both a market and non-market perspective. In order to continue to encourage new entrant activities, CARC must cover all costs a retailer incurs in acquiring, retaining and transferring a customer.

5.3 Retail Margin

The ToR requires the QCA to set a retail margin allowance on the basis of the margin requirements for an efficient Queensland representative retailer giving consideration to any risks not compensated for elsewhere in the pricing determination. The QCA proposes to meet this criteria by establishing a retail margin that is based on the assessment of the systematic risks (economic cycle risks) facing the representative retailer. This is based on the assumption that all other risks (the non-systematic risks) are captured in other components of the regulatory package[19].

Origin questions how the QCA proposes the non-systematic risks will be covered off given the QCA has taken the view that there is no provision for a cost pass through mechanism. This is particularly important for changes to green energy schemes, carbon tax and the introduction of the NECF. If no cost pass through provision is provided for or individual elements are not appropriately adjusted, then the retail margin needs to cover off both systematic and non-systematic risks. Although this approach would differ to the other NEM jurisdictions, some State Regulators have recognised the importance of a cost through provision and thus there has been not a need to include non-systematic risks as part of the margin.

[18] QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p36-37.
[19] Ibid, p40.

An example of a non-systematic risk which retailers operating in Queensland have been required to absorb the cost of include changes to the Renewable Energy Target (RET) Scheme when it was split into two separate schemes - SRES and LRET. Two main issues arose with the introduction of the SRES scheme:

- The QCA's estimated SRES target was grossly understated for 2010-11; and
- The BRCI legislation, at the time, did not allow the QCA to incorporate SRES costs for the first six months of the SRES scheme in 2011.

These costs were significant and retailers were required to wear these costs with no mechanism or no risk allowance to mitigate them. In a national electricity market, electricity retailers will seek markets where they can find the best value and if the risks are high, the willingness to supply electricity customers in the Queensland market will decline. Retailers should not be required to carry the risks or costs associated with the introduction or change to Government regulated schemes.

In determining an appropriate retail margin, it is understood that the QCA proposes to undertake an assessment of the appropriateness of the current margin of 5 per cent in the context of margins adopted in other jurisdictions. In this assessment, the QCA will pay particular regards to the analysis underpinning the most recent IPART estimate and will consider its' applicability to a representative Queensland retailer. It is also understood that the QCA intends to draw on other publicly available information where relevant[20].

Origin agrees with this approach but strongly advocates that the market differences in determining the retail margin in Queensland and New South Wales need to be considered. The NSW margin was part of a regulatory framework where the energy cost allowance was based on an LRMC floor approach which provided certainty and mitigated retailer risks. The use of a market based approach, as proposed in Queensland, adds further uncertainty.

If the QCA does not take into account LRMC in the Queensland energy cost allowance or provide a cost-pass through mechanism as specifically provided for in other jurisdictions, the margin rate will have to be appropriately escalated to take into account these framework differences.

[20] QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p40.

6. Setting the R component of Retail Tariffs

It is understood that the QCA proposes to allocate elements of the R component on the following basis:

- *Energy Costs:* allocate energy costs on a fully variable basis;
- *Retail Operating Costs:* allocate 75 percent of retail costs (including CARC) on a fixed basis and the remainder 25 percent on a variable basis; and
- *Retail Margin:* apply the retail margin equally (on a percentage basis) to each component (fixed and variable) of retail tariffs[21].

In general, Origin agrees that the above approach appears reasonable. However, it should be noted that there is a large fixed cost component to the selling and supplying of electricity in Queensland in both the transmission and distribution network charges as well as retail operating costs. In the retail market for electricity, there are additional fixed costs that arise due to the contracting nature of obtaining adequate wholesale hedges.

Given these elements, Origin believes that a minimum of 75 per cent of retail costs should be fixed.

Origin is firmly of the opinion that its regulated electricity tariffs should reflect the underlying costs of supplying electricity to its customers. This means a tariff structure which has a fixed component and variable stepped components that as closely as possible mirrors the actual costs incurred by a retailer.

[21]QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p41-43.

7. Accounting for Unforeseen Events

It appears the QCA has taken the view that they may not be able to include a cost pass through mechanism in the pricing framework as the Ministers Delegation only requires the QCA to determine prices from 1 July 2012 to 30 June 2013. Origin is concerned with this view, particularly if there is no mechanism to allow cost recovery for past events in future determinations or for the QCA to include estimated costs within an upcoming determination.

As noted, the risks most relevant to a cost pass through provision are the non-systematic risks that can arise due to uncertainties around the introduction of unforeseen market events or policy developments such as a carbon tax, implementation of national energy consumer framework or Queensland specific green initiatives (ie. mandatory offering of a green product and greenhouse benchmarks on bills). Retailers incur real costs at the time the scheme or new regulatory requirement is introduced. This was evident in 2010-11 when substantial changes were made to the RET scheme during the year. There was a requirement for retailers to absorb these higher costs for a period of time which had the potential to significantly impact on a retailer's ability to financially survive in the electricity market.

Origin submits that if the pricing methodology framework does not allow for a specific cost pass through provision, one of the following approaches needs to be adopted for the incorporation of costs:

- the determination includes an allowance in retail and/or energy costs to account for future events or changes that are expected during the pricing determination period. That is, if there is a likelihood that a future event will occur, then forecast costs based on available data or benchmarks should be included within the next determination. If the costs allowed are found to be too high or low, then an appropriate adjustment can be made in the following year;
- subsequent determinations allow for costs to be adjusted appropriately to account for events that have occurred within the past 12 months. For example, if there has been an introduction of a new regulatory requirement, the costs should be included and adjusted upwards to take account of this event; or
- non-systematic risks need to be covered off in the calculation of the retail margin.

Retailers face inherent risks with regulated tariffs being set for a fixed period of time as the regulatory framework requires assumptions to be made regarding future energy costs, changes to retail costs and appropriate returns. These risks are the greatest for retailers supplying small standard customers on a regulated tariff as revenue is constrained by the level of the tariff. There needs to be cost recovery to account for these events.

8. Other Issues

8.1 Transitional Arrangements

Origin agrees with the QCA that social welfare concerns regarding the changes in tariffs should be dealt with by the Government through financial assistance rather than through distorting electricity prices. It is Origin's belief that customers need to see the full, cost reflective charge for their electricity consumption and this is even more important with the introduction of the carbon tax. If such a scheme is to have the desired impact on customer behaviour, actual prices need to be transparent.

Origin further agrees with the QCA that they should consider tariff impacts in the draft determination and specify whether any transitional arrangements are warranted. It is difficult at this time to forecast these impacts and which customer groups will see a change in their average annual bill.

8.2 Tariff Gazette Issues

Origin notes that Draft Methodology Paper states that the Queensland Government will be responsible for determining the associated eligibility criteria and other terms and conditions for tariffs[22] while the QCA will only be responsible for determining retail tariffs and prices. While Origin understands that this may be the case, Origin would urge the QCA and the Government to work closely together to develop a Gazettal that reflects all the concerns and issues raised by relevant parties. Some key issues that Origin believes needs to be addressed as part of a review of the Gazette are set out below.

8.2.1 Expression of Tariff Rates and Blocks in the Gazette

Service fees and fixed charges in the Queensland Government Gazette are currently expressed based on a monthly rate. There has been much debate in the market about the basis for pro-rating the monthly rate or minimum payment into a daily rate for instances whereby a customer has only consumed energy at a premises for part of a month (i.e. 15 days). To ensure all customers are being charged on the same basis, the monthly rates should be converted to a daily rate and expressed in the gazette on this basis. Daily rates would also align with the manner in which all retailer systems (to Origin's knowledge) are designed to bill.

In addition to this, it will be important that the steps for the inclining block steps are expressed on a daily rate. To alleviate debate and ensure that customers are being charged the same, regardless of retailer, appropriate tariff rates and block steps should be displayed on a daily basis in the Queensland Government Gazette.

8.2.2 Application of Tariffs

Origin requests that the QCA and Government review the conditions that apply to the various retail tariffs. In particular, the tariff combinations that should be allowed and whether there should be restrictions on certain combinations of tariffs. For example, there are residential customers with a single domestic NMI, but they have multiple meters. Origin does not believe that it is in the spirit of the tariff reform for customers to be able to have the combination of a TOU tariff and an IBT tariff on separate meters, but on the one NMI.

[22] QCA, *Regulated Retail Electricity Prices 2012-13 - Draft Methodology Paper*, November 2011, p47.

8.2.3 Fees and Charges

A noted in the Draft Methodology Paper, the Gazette currently only allows for the charging of two regulated fees to regulated customers[23]. These fees relate to the request for historical billing data and for payments that are dishonoured. Origin requests that the Queensland Government consider expanding on the fees and charges which a retailer can charge customers.

Of particular expense to retailers are the costs associated with late payments and credit card fees. Retailers incur significant administrative costs when customers do not pay their bill by the due date and incur third party fees for customers paying by credit card. Origin believes that retailers should be able to recover the costs it incurs in these instances.

It should be noted that many States now allow for the charging of these fees to regulated customers and an amount is deducted from the retail costs allowance to account for the collection of such fees and charges. If the Queensland Government is not amenable to the inclusion of additional fees and charges for regulated customers, the retail cost allowance should be escalated upwards to account for these differences.

Origin proposes that any fees and charges would be established on a cost reflective basis and applied on a fair and reasonable basis.

8.2.4 High Voltage Discount in Gazette

Origin believes that the voltage discounts provided with the high voltage tariffs should be removed. It is no longer relevant to the market environment and almost all customers will be considered Large and have no access to notified prices. If it is still relevant to Large tariff customers in the Ergon area then the discount should be limited to those customers in the Ergon region.

[23] Ibid, p47.