Queensland Competition Authority

Interim Consultation Paper

Regulated Retail Electricity Prices for 2015-16

September 2014

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SUBMISSIONS

Closing date for submissions: 28 October 2014

Public involvement is an important element of the decision-making processes of the Queensland Competition Authority (QCA). Therefore submissions are invited from interested parties concerning its assessment of 2015-16 regulated retail electricity prices. The QCA will take account of all submissions received.

Submissions, comments or inquiries regarding this paper should be directed to:

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Confidentiality

In the interests of transparency and to promote informed discussion, the QCA would prefer submissions to be made publicly available wherever this is reasonable. However, if a person making a submission does not want that submission to be public, that person should claim confidentiality in respect of the document (or any part of the document). Claims for confidentiality should be clearly noted on the front page of the submission and the relevant sections of the submission should be marked as confidential, so that the remainder of the document can be made publicly available. It would also be appreciated if two copies of each version of these submissions (i.e. the complete version and another excising confidential information) could be provided. Where it is unclear why a submission has been marked 'confidential', the status of the submission will be discussed with the person making the submission.

While the QCA will endeavour to identify and protect material claimed as confidential as well as exempt information and information disclosure of which would be contrary to the public interest (within the meaning of the *Right to Information Act 2009* (RTI)), it cannot guarantee that submissions will not be made publicly available.

Public access to submissions

Subject to any confidentiality constraints, submissions will be available for public inspection at the Brisbane office, or on the website at www.qca.org.au. If you experience any difficulty gaining access to documents please contact us on (07) 3222 0555.

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THE ROLE OF THE QCA – TASK, TIMING AND CONTACTS

The Queensland Competition Authority (QCA) is an independent statutory authority that aims to promote competition as the basis for enhancing efficiency and growth in the Queensland economy.

The QCA's primary role is to ensure that monopoly businesses operating in Queensland, particularly in the provision of key infrastructure, do not abuse their market power through unfair pricing or restrictive access arrangements.

In 2012, that role was expanded to allow the QCA to be directed to: investigate, and report on, any matter relating to competition, industry, productivity or best practice regulation; and review and report on existing legislation.

Key dates

2015-16 review of regulated retail electricity prices: indicative timetable

Release of interim consultation paper	30 September 2014
Submissions on interim consultation paper due	28 October 2014
Release of public consultation timetable	11 November 2014
Release of draft determination	12 December 2014
Workshops on draft determination	early February 2015
Submissions on draft determination due	27 February 2015
Release of final determination	29 May 2015

Registration of interest

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Contacts

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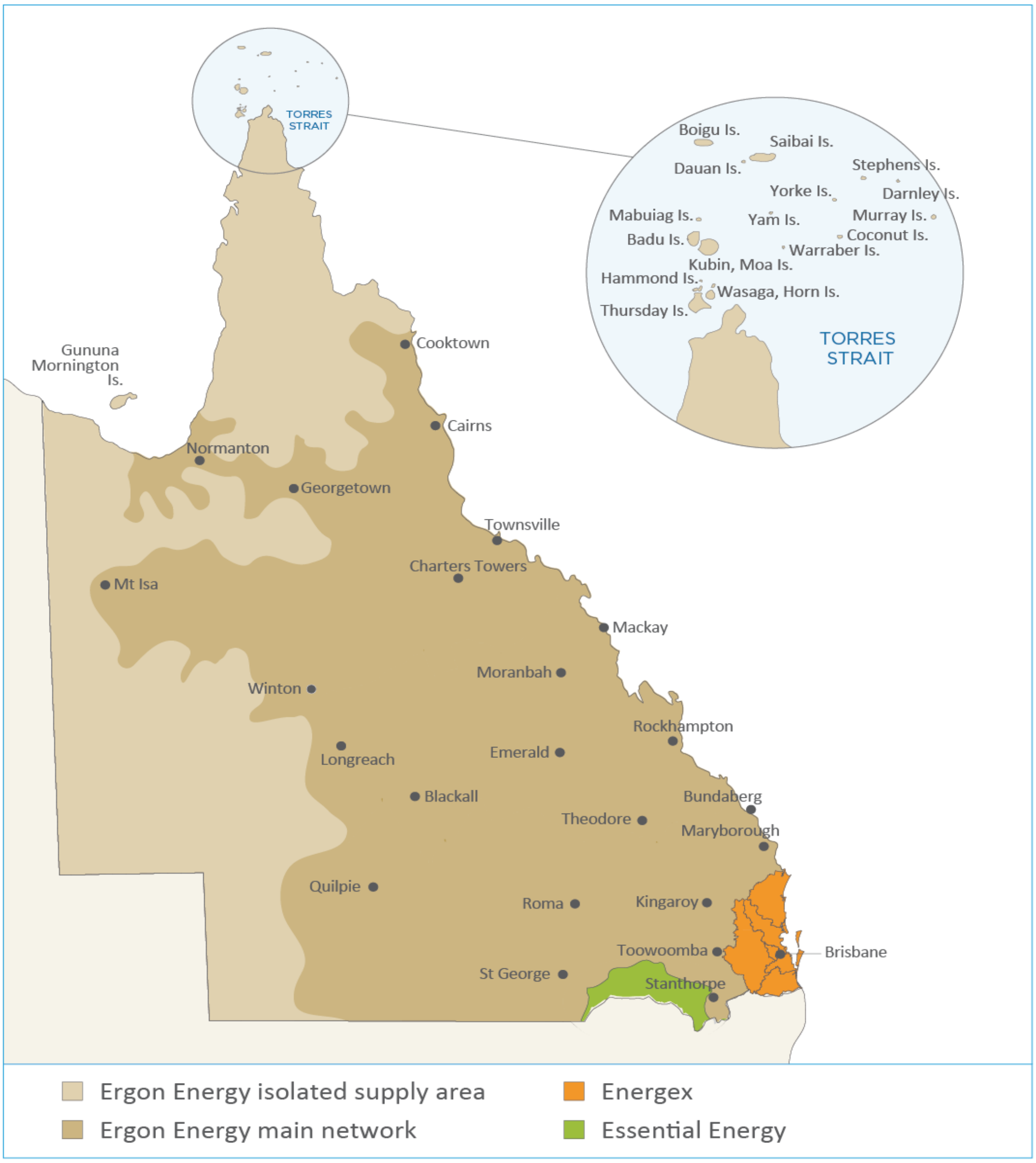
1 INTRODUCTION

The Queensland Competition Authority (QCA) has received a delegation from the Minister for Energy and Water Supply (the Minister) to determine regulated retail electricity prices (notified prices) to apply to non-market customers from 1 July 2015 to 30 June 2016 (see Appendix A).

The determination will only apply in the Ergon Energy distribution area, which covers regional and rural areas of Queensland (see map below). The Queensland Government (the Government) has legislated to remove retail price regulation in the Energex distribution area (covering south east Queensland) from 1 July 2015, which means that customers in south east Queensland will no longer have access to notified prices.

We have prepared this interim consultation paper to commence our review.

Figure 1 Queensland distribution areas



1.1 The uniform tariff policy and regional pricing

The end of notified prices in south east Queensland from 1 July 2015 requires the QCA to reassess its approach to setting notified prices for residential and small business customers. In the absence of notified prices in south east Queensland, the QCA will need to set regional prices on a new basis, taking into account matters raised in the Ministerial delegation and the general factors identified in Queensland's *Electricity Act 1994* (the Electricity Act).

One of the matters the QCA must consider is the uniform tariff policy.

The Government's uniform tariff policy ensures that, regardless of where they live, eligible non-market customers of the same class pay the same notified prices[1]. To date, the policy has seen most notified prices based on the costs of supply for customers in south east Queensland (i.e. the Energex distribution area).

Basing notified prices on costs in south east Queensland benefits customers in regional Queensland who could otherwise face higher prices reflecting the higher costs of supplying electricity in regional areas. The cost difference between south east Queensland and regional Queensland is largely due to the higher energy and network costs of supplying electricity over long distances to a relatively sparse customer base. These additional costs are significant: the uniform tariff policy's subsidy for regional electricity customers is expected to be $655 million in 2014-15[2].

The Government has confirmed its commitment to retaining the uniform tariff policy[3]. The Minister has advised the QCA that "for the purposes of the delegation regional prices should, as much as is practicable, aim to ensure that small customers outside south east Queensland do not pay more than reasonable expectations of the prices which would be available to standing offer customers in south east Queensland" (the Minister's letter is included in Appendix B). This advice accords with paragraph 5d(i) of the delegation.

Standing offers are basic contracts with regulated terms and conditions. In markets with price regulation, standing offer prices are usually the regulated prices. In markets without price regulation, standing offer prices are set by the retailer. As pointed out by the Australian Energy Market Commission, standing offer prices are generally the benchmark prices against which retailers make discounted market offers[4].

The Government is reviewing the effectiveness and objectives of the uniform tariff policy. The QCA provided advice to the Government on the policy earlier this year.

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[1] Department of Energy and Water Supply, *Electricity On-Supply in Queensland: Discussion Paper*, 2013, p. 7; and *Ministerial Delegation to the QCA to determine regulated retail electricity prices from 1 July 2013 to 30 June 2016*, 12 February 2013, p. 1.

[2] Queensland Government, *State Budget 2014-15 - Concessions Statement*, June 2014, p. 4.

[3] See the covering letter to the delegation (Appendix A) and the letter from the Minister received on 25 September 2014 (Appendix B).

[4] Australian Energy Market Commission, *2014 Retail Competition Review, Final Report*, 22 August 2014, p. 35 & p. 182.

1.2 Review process

We will conduct a public consultation process to allow stakeholders to share their views and comment on issues of relevance to our review. An indicative timetable for the review is provided on page iii.

Submissions are invited in response to this paper and are due no later than 28 October 2014. Details on how to make a submission can be found at the front of this paper. While we have set out key issues on which we are seeking comments, stakeholders should take this opportunity to comment on any matters they consider are relevant to our review and provide detailed arguments and evidence to support their views, where possible.

We are required to publish a draft determination by 12 December 2014 and a final determination by 31 May 2015.

2 LEGISLATIVE REQUIREMENTS AND PRICING APPROACHES

When we receive a delegation to determine notified prices, we must make that determination in accordance with our obligations under the Electricity Act. In this chapter, we explain what these obligations are and the pricing approaches we could adopt given these obligations.

2.1 Legislative requirements

The Electricity Act does not specify criteria or principles that we must apply when making a price determination. Rather, we are directed to have regard to various matters. In accordance with section 90(5) of the Electricity Act, the matters we are required to have regard to in making a determination are:

(a) the actual costs of making, producing or supplying the goods or services

(b) the effect of the price determination on competition in the Queensland retail electricity market

(c) any matter required by delegation

(d) any other matter we consider relevant.

When we make a determination, we must also have regard to the objects of the Electricity Act, which are to:

(a) set a framework for all electricity industry participants that promotes efficient, economical and environmentally sound electricity supply and use

(b) regulate the electricity industry and electricity use

(c) establish a competitive electricity market in line with the national electricity industry reform process

(d) ensure that the interests of customers are protected

(e) take into account national competition policy requirements.

Key matters we are required to consider by delegation

The delegation sets out many matters we are required to consider. Consistent with the approach applied in previous price determinations, we are required to consider applying the network (N) plus retail (R) cost build-up methodology.

We are also required to consider that the Government is reviewing the effectiveness and objectives of the uniform tariff policy and options for improved regional competition.

When determining the network cost component, we must consider continuing with the same general approach we have applied in previous determinations. For residential and small business customer tariffs, this means using Energex's network charges and tariff structures for the flat rate tariffs (i.e., tariffs 11, 20, 31, 33, 41 and 91[5]). Adopting this approach would mean that network charges are below cost because they would be based on network costs in south east Queensland, not regional Queensland.

[5] Tariff 91 applies to unmetered supplies (except street lighting).

For the time-of-use tariffs (i.e. tariffs 12 and 22[6]), we must consider using Energex's network charges. However, there is a new requirement in the delegation to consider using Ergon Energy Distribution's (Ergon Distribution's) tariff structures. If this proposal is adopted, network prices would be at the same *level* as Energex's network prices, but based on the *structure* of Ergon Distribution's network tariffs. Adopting this approach would still mean that network charges are below cost, although using Ergon Distribution's tariff structures would improve price signals and encourage customers to reduce consumption during peak periods in Ergon Distribution's area, as pointed out in the delegation.

For large business customer tariffs, we must consider using Ergon Distribution's network charges. This is the approach we have adopted in previous decisions.

We are also required to consider specific issues in relation to transitional arrangements for certain tariffs, in particular:

(a) completing the rebalancing of the fixed and variable components of tariff 11 (the standard residential tariff) using the approach established in the 2013-14 determination

(b) maintaining transitional arrangements for transitional and obsolete tariffs (for example, farming and irrigation tariffs).

2.2 Possible pricing approaches

Taken together, the matters we are required to consider in the Electricity Act and objects of the Electricity Act suggest that cost-reflectivity and the promotion of retail competition are important guiding principles in making our determination. Cost-reflectivity is important for efficiency and equity reasons. Previous determinations have also been designed to support retail competition. However, as the 2015-16 determination will apply only to the Ergon distribution area, the opportunities to promote retail competition are more limited than in previous determinations.

As noted above, the QCA must also have regard to the uniform tariff policy.

Under the Electricity Act, we can also have regard to any other matter we consider relevant. We consider that the impact on customers is a very relevant factor, particularly given the significant price increases customers have faced in recent years.

Given that we are required to consider a number of potentially conflicting matters when making our price determination, we have considered a spectrum of possible pricing approaches, particularly for residential and small business customers.

Residential and small business customers

While we are not considering this approach for 2015-16, a possible approach at one end of the spectrum would be to move gradually to fully cost-reflective notified prices (i.e. reflecting the actual costs of supply to customers in each region). Cost-reflective pricing would avoid the need to subsidise electricity prices and would promote retail competition. However, it would be inconsistent with maintaining uniform tariffs (because it would result in different notified prices for customers based on their location) and would mean significant price increases, particularly for customers in western parts of the state and those supplied by isolated systems.

[6] The delegation also requires that we consider removing tariff 13 (see chapter 5).

For instance, in 2014-15, a typical tariff 11 customer paying cost-reflective prices would pay around 140% more in western Queensland than in south east Queensland[7].

Another possibility would be to consider the approach applied for large business customers since 2012. When price regulation for large business customers in south east Queensland ended, we decided to base notified prices for large business customers outside south east Queensland on the lowest costs of supply for those customers still eligible for notified prices. This approach meant the new benchmark for pricing was Ergon Energy's east pricing zone, transmission region 1[8]. We have continued this approach for subsequent determinations. Adopting this approach for residential and small business customers would mitigate price impacts and maintain uniform tariffs compared to introducing fully cost-reflective prices. This would improve cost-reflectivity (relative to the current approach based on south east Queensland costs). It would also reduce the subsidy paid by taxpayers to subsidise electricity prices.

However, this approach would be inconsistent with the Government's interpretation of the uniform tariff policy for residential and small business customers for 2015-16 and, in some cases, price increases would be too significant to introduce in a single year. With the costs of supplying residential customers in the east pricing zone about 30% higher than in south east Queensland[9], adopting this approach would mean significant price increases.

At the other end of the spectrum, we could maintain our current approach, which would involve setting notified prices based on the costs of supply in south east Queensland, rather than regional Queensland. As raised in the delegation, this approach could also allow use of Ergon Distribution's tariff structures for some or all retail tariffs (as discussed in Chapter 3) while retaining prices at south east Queensland levels.

This approach would result in customers continuing to pay much less than the costs of supply, potentially leading to inefficient investment and decision-making and ongoing subsidisation of electricity prices by taxpayers (estimated at $655 million for 2014-15, as noted above). However, it may be considered reasonable because it would avoid the high price increases associated with the other approaches and would be consistent with the uniform tariff policy for 2015-16.

On balance, the QCA regards the current approach of basing notified prices for residential and small business customers in regional Queensland on south east Queensland costs as the most credible approach for 2015-16.

Large business customers

As noted above, we already determine notified prices for large business customers based on the lowest costs of supplying customers in regional Queensland. This approach has the benefit of being more cost-reflective and less costly to subsidise than an approach based on south east Queensland costs. It is also consistent with the requirement in the delegation to consider basing the network cost component on Ergon Distribution's network charges. While there may

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[7] Based on an estimate of a cost-reflective notified price for 2014-15 and assuming typical annual consumption of 4,243 kWh. To calculate the cost-reflective price, we applied the approach in our 2014-15 determination, but used cost-reflective energy costs, energy loss costs and network charges.

[8] Queensland Competition Authority, *Final Determination: Regulated Retail Electricity Prices 2012-13*, May 2012.

[9] This is the estimated impact in 2014-15 on a typical tariff 11 customer in the Ergon Distribution east pricing zone (transmission region one) paying cost-reflective notified prices.

be an option of moving to fully cost-reflective notified prices, we do not propose to adopt this approach because it would be inconsistent with maintaining uniform tariffs.

2.1 We seek stakeholders' views on the following:

(a) For residential and small business customers, should we:

(i) maintain the 2014-15 approach, which is to base notified prices on south east Queensland costs? Why or why not?

(ii) keep notified prices at south east Queensland levels, but use Ergon Distribution's tariff structures for some or all tariffs? Why or why not?

(b) For large business customers, should we:

(i) maintain the 2014-15 approach, which is to base notified prices on regional Queensland costs? Why or why not?

3 NETWORK COSTS

Network costs are the costs associated with transporting electricity through the transmission and distribution networks and account for around 50% of the final cost of electricity for small customers.

As regulated monopoly businesses, Powerlink, Energex and Ergon Distribution all earn regulated revenues that are determined by the Australian Energy Regulator (AER). In addition to recovering their own distribution network costs, Energex and Ergon Distribution pass Powerlink's costs on to customers in network prices that are also approved by the AER.

The delegation requires that we consider:

(a) for small customer retail tariffs (except tariffs 12 and 22), basing the network cost component on Energex network charges and tariff structures[10]

(b) for small customer tariffs 12 and 22, basing the network cost component on Energex network charges, but using the relevant Ergon Distribution tariff structures

(c) for large customer retail tariffs, basing the network cost component on Ergon Distribution network charges.

3.1 Network tariffs for small customers and unmetered supplies

For the 2014-15 determination, we used Energex's network charges and tariff structures as the basis for setting retail tariffs for residential customers, small business customers and unmetered supplies (excluding street-lighting - see section 3.2 below) because they reflected the costs of supplying customers in south east Queensland.

For our 2015-16 determination, we are only determining notified prices for regional customers. Therefore, we must decide whether to use the network charges and tariff structures of Energex or Ergon Distribution.

Level of network charges

Firstly, we must decide on the *level* of network charges. In Chapter 2, we stated our preference for basing notified prices on south east Queensland costs. This would mean setting network charges at Energex levels.

Structure of network tariffs

Secondly, we must consider whether to use the tariff *structures* of Energex or Ergon Distribution. Tariff structures can include, for example, combinations of fixed charges, demand charges and consumption charges. Consumption charges might be flat or they might vary based on the amount of electricity used or the time it is used.

In this section, we compare Energex and Ergon Distribution tariff structures and set out possible approaches for 2015-16.

[10] The delegation requires that we consider removing tariff 13 from the tariff schedule, on the basis that Ergon Distribution does not have a network tariff for this tariff and no customers in regional Queensland are accessing it (see chapter 5).

Comparison of tariff structures

Energex and Ergon Distribution tariff structures differ across residential and small business tariffs.

Table 2 compares the network tariff structures for non time-of-use tariffs. The key differences between the structures are:

(a) Energex has flat variable rates, while Ergon Distribution has three-part inclining block tariffs (IBTs).

(b) Ergon Distribution's tariffs are more heavily weighted toward the recovery of costs through fixed charges than Energex's tariffs. This would be the case even if the overall level of Ergon Distribution's tariffs was reduced to a level comparable to Energex's. This means that any tariff based on Ergon Distribution structures would result in the fixed charge forming a greater proportion of customers' bills. This would have a negative effect on customers with low consumption (i.e. it would increase their bill), but a positive effect on customers with high consumption (i.e. it would lower their bill).

(c) Energex does not have a fixed charge for its controlled load tariffs, but Ergon Distribution does.

Table 2 Comparison of Energex and Ergon Distribution non time-of-use tariffs

Type	*Distributor*	*Fixed*	*Variable*		
Residential (tariff 11)	Energex	c/day	Flat rate c/kWh		
	Ergon Distribution	c/day	c/kWh 1st 1,000 kWh/year	c/kWh next 5,000 kWh/year	c/kWh >6,000 kWh/year
Small business (tariff 20)	Energex	c/day	Flat rate c/kWh		
	Ergon Distribution	c/day	c/kWh 1st 1,000 kWh/year	c/kWh next 19,000 kWh/year	c/kWh >20,000 kWh/year
Small business demand (tariff 41)	Energex	c/day	Flat rate c/kWh	$/kW/month	
	Ergon Distribution	No network tariff			
Night controlled load (tariff 31)	Energex	n/a	Flat rate c/kWh		
	Ergon Distribution	c/day	Flat rate c/kWh		
Controlled load (tariff 33)	Energex	n/a	Flat rate c/kWh		
	Ergon Distribution	c/day	Flat rate c/kWh		
Unmetered (tariff 91)	Energex	n/a	Flat rate c/kWh		
	Ergon Distribution	c/day	Flat rate c/kWh		

Table 3 compares the structures for time-of-use tariffs. Ergon Distribution's residential time-of-use tariff structures are the same as Energex's (i.e. a fixed charge and variable peak, shoulder and off-peak charges), but different time periods apply to each variable charge. The main difference is that the Ergon Distribution peak and shoulder periods are limited to the summer months, which means the off-peak period accounts for a much greater proportion of time.

Unlike the residential time-of-use tariff, there is a mismatch between the structure of the Energex and Ergon Distribution small business time-of-use tariffs. Energex has peak and off-peak variable charges, while Ergon Distribution has peak, shoulder and off-peak variable charges. Like the residential tariff, the peak and shoulder periods are limited to the summer months.

Furthermore, as noted above, Ergon Distribution's tariffs are more heavily weighted toward the recovery of costs through fixed charges than Energex's tariffs. Therefore, using Ergon Distribution's tariffs would have a negative effect on customers with low consumption, but a positive effect on customers with high consumption.

Table 3 Comparison of Energex and Ergon Distribution time-of-use tariffs

Type	*Distributor*	*Peak*	*Shoulder*	*Off-peak*
Residential (tariff 12)	Energex[1]	4pm-8pm Mon-Fri 1,040 hours per year	7am-4pm, 8pm-10pm Mon-Fri 7am-10pm Weekends 4,420 hours per year	10pm-7am Every day 3,276 hours per year
	Ergon Distribution	4:30pm-9pm Mon-Fri Summer only 292.5 hours per year	3pm-4:30pm Mon-Fri 9pm-9:30pm Mon Fri 3pm-9:30pm weekends Summer only 299 hours per year	All other times 8,144.5 hours per year
Small business (tariff 22)	Energex	7:00am to 9:00pm, weekdays 3,640 hours per year	n/a	All other times 5,096 hours per year
	Ergon Distribution	11:30am to 5:30pm on summer weekdays 390 hours per year	10:00am to 11:30am and 5:30pm to 8:00pm on summer weekdays 260 hours per year	All other times 8,086 hours per year

1. Tariff 13 has the same structure as tariff 12. Ergon Distribution does not have a network tariff for tariff 13.

Possible approaches for 2015-16

We consider that there are three possible approaches we could adopt for 2015-16:

(a) continuing to use Energex's tariff structures as the basis for all retail tariffs

(b) using a mix of Energex and Ergon Distribution tariff structures (consistent with the proposal in the delegation)

(c) using Ergon Distribution's tariff structures as the basis for all retail tariffs.

Energex structures for all retail tariffs

Continuing to use Energex structures as the basis for all small retail tariffs would be consistent with our previous decisions and ensure that customers would not experience a significant change in the size of their bills as a result of a change in tariff structure.

However, this approach would continue to result in customers facing price signals that do not reflect the impact of their consumption on Ergon Distribution's network and would continue to encourage inefficient consumption and investment decisions to be made.

Mix of Energex and Ergon Distribution structures

Under this approach, Energex's structures would be used for some tariffs and Ergon Distributions' structures would be used for others. One example would be to use the approach proposed in the delegation, which is to use Energex structures for the flat and controlled load tariffs and Ergon Distribution structures for the time-of-use tariffs. The time-of-use tariffs are tariff 12 (for residential customers) and tariff 22 (for small business customers).

Using Ergon Distribution structures for time-of-use tariffs would improve cost-reflectivity and encourage customers to reduce consumption during peak periods on Ergon Distribution's network, as pointed out in the delegation. However, changing the tariff structure may result in negative impacts for some customers, although it would only affect the relatively small proportion of customers that are on time-of-use tariffs. Ergon Retail supplies about 7,500 customers (7% of its small business customers) on tariff 22[11] and fewer than 100 residential customers on tariff 12[12].

We would also need to consider the incentives for customers to move between flat rate and time-of-use tariffs, if Energex tariffs are used as the basis for the former and Ergon Distribution tariffs are used as the basis for the latter.

Ergon Distribution structures for all retail tariffs

The third approach is to base all small tariffs on Ergon Distribution structures. This would be a further step towards improving cost-reflectivity. Under this approach, all customers would be affected by the change in tariff structure. We would need to consider these impacts, noting that some customers would be better off and some customers worse off.

3.2 Network tariffs for large business customers and street lighting

For the 2014-15 determination, we based retail tariffs for large business customers and street lighting customers on the network charges of Ergon Energy's east pricing zone, transmission region one.

We understand that Ergon Distribution is planning to introduce seasonal time-of-use demand tariffs (in addition to the demand tariffs that form the basis of tariffs 44 to 46) in 2015-16[13]. If Ergon Distribution does introduce new network tariffs and we continue to set notified prices for large business customers based on Ergon Distribution's network tariffs and charges, we propose to build new retail tariffs on these using the same methodology used for existing large customer tariffs.

3.3 Obsolete and transitional retail tariffs

The delegation requires that we consider maintaining transitional arrangements for retail tariffs classed as transitional or obsolete. There is no need to determine network charges for these tariffs as they are not based on an N+R approach. Obsolete and transitional tariffs are discussed further in Chapter 5.

3.4 Approval of distributors' network tariffs for 2015-16

A new five year regulatory period for the distribution businesses will begin on 1 July 2015. Ergon Distribution and Energex are required to submit a draft revenue proposal, including network charges, to the AER by 31 October 2014. These network charges will be used in our draft determination.

The AER will publish its preliminary revenue determination on 30 April 2015. Based on the preliminary determination, the distribution businesses are then required to submit 2015-16 network charges to the AER by 21 May 2015. The AER is unlikely to approve the network charges before we must publish our final determination, which means that we may need to set notified prices based on the submitted network charges.

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[11] Based on 2012-13 data.
[12] As at 1 July 2014.
[13] Ergon Energy*, Understanding Network Tariff Reform - A guide for large commercial, industrial and rural industry customers who use more than 100MWh of electricity a year*, April 2014, p. 4.

While the AER is required to make a final determination by 31 October 2015[14], which will apply from the date it is published, any revenue differences between the preliminary and final determination will be accounted for in the remaining years of the regulatory period. Therefore, it is our understanding that the final determination will not affect 2015-16 network charges[15].

In our 2013-14 determination, we implemented a cost pass-through mechanism to account for any material differences between the network charges used in our final determination and those charged to retailers. In Chapter 5 we discuss whether we should include a pass-through mechanism in our 2015-16 determination.

3.1 We seek stakeholders' views on the following:

- **(a) Should we continue to use Energex's tariff structures as the basis for retail tariffs for residential and small business customers?**
- **(b) Alternatively, should we use Ergon Distribution's tariff structures for some or all retail tariffs for residential and small business customers?**
- **(c) Are there any other issues we should consider?**

[14] National Electricity Rules, clause 11.60.4(c).
[15] AEMC, *Rule Determination: National Electricity Amendment (Economic Regulation of Network Service Providers) Rule 2012*, 29 November 2012, pp. 260-261.

4 ENERGY AND RETAIL COSTS

In setting the R component of notified prices, we include allowances for energy costs and retail costs. The delegation does not set out any specific matters we are required to consider in relation to setting the R component.

4.1 Energy costs

Energy costs are those a retailer incurs, either directly or indirectly, in purchasing electricity to meet the demand of its customers. In our 2014-15 determination, we estimated energy costs on the basis of advice from our consultant, ACIL Allen.

We have again engaged ACIL Allen to provide advice for our 2015-16 determination in accordance with the terms of reference (ToR) for its engagement (available on our website). We consider that engaging the same consultant for this review will provide continuity and certainty to stakeholders.

We have instructed ACIL Allen to provide cost estimates for both south east Queensland and regional Queensland. In previous decisions, we have used the south east Queensland estimates to set notified prices for residential and small business customers and the regional Queensland estimates to set notified prices for large business customers.

Energy cost components

In previous decisions, we have included allowances for a range of energy costs, which can be broken into five general categories:

(a) wholesale energy costs

(b) Renewable Energy Target (RET) costs

(c) National Electricity Market (NEM) participation fees and ancillary services charges

(d) prudential capital costs

(e) energy losses.

A brief explanation of each of these components is provided below. A detailed explanation of how each cost component was estimated for 2014-15 is provided in our 2014-15 determination and ACIL Allen's reports, which are available on our website.

Wholesale Energy Costs

Wholesale energy costs relate to the costs incurred by a retailer in purchasing electricity to meet the demand of its customers. This electricity is purchased from the NEM, also known as the 'spot market'.

The spot market is a particularly volatile market where half-hourly settlement prices can range from -$1000 per MWh to $13,500 per MWh. There are a range of measures that a retailer can take in order to reduce its exposure to volatile prices, including purchasing financial derivatives (for example, swaps, caps and options), entering long-term power purchase agreements (PPAs) with generators or investing in generation assets as a natural hedge.

In the past, we have generally considered two alternative approaches for determining wholesale energy costs — a hedging-based approach and a long-run marginal cost (LRMC) approach[16]. However, we have made clear our preference for using a hedging-based approach, in particular because it is transparent and best reflects the actual costs that retailers incur when purchasing electricity from the NEM in a given year, taking into account their hedging activity in the derivatives market. Hedging-based approaches are also widely preferred by other Australian regulators and have been endorsed by the Australian Energy Market Commission (AEMC) in its final report on best practice retail price regulation, produced for the Standing Council on Energy and Resources (SCER)[17].

Renewable Energy Target costs

The RET scheme, comprised of the Large-scale Renewable Energy Target (LRET) and Small-scale Renewable Energy Scheme (SRES), is aimed at increasing renewable energy generation and reducing greenhouse gas emissions from the electricity sector. The intent of the RET is to provide incentives for the electricity sector to deliver the equivalent of 20 per cent of Australia's electricity from renewable sources by 2020.

In February 2014, the federal government announced a review of the RET scheme by an expert panel, which finalised its report in August 2014. The review panel made several recommendations which, if adopted, could affect retailers' costs in 2015–16. We intend to determine RET costs in our draft and final determinations based on the legislated RET policy in place at the time of each decision.

NEM participation fees and ancillary services charges

Retailers are required to pay NEM participation fees and ancillary services charges to the Australian Energy Market Operator (AEMO). NEM participation fees cover the costs of operating the electricity market. Ancillary services charges cover the costs of the services used by AEMO to manage power system safety, security and reliability.

Prudential capital costs

Prudential capital costs are incurred by retailers when providing financial guarantees to AEMO and hedging providers.

Energy Losses

When electricity is transported from generators to final customers, some losses occur across the transmission and distribution networks. To ensure that retailers supply enough electricity to meet demand, they must purchase sufficient electricity to allow for those losses.

[16] In previous reviews, we also considered a statistical model that estimated the price a retailer might be willing to pay to enter hedging contracts (the price distribution approach).

[17] AEMC, *Final Report, Advice on best practice retail price methodology*, 27 September 2013.

> **4.1 We seek stakeholders' views on the following:**
>
> **(a) Is there any new information available to suggest alternative approaches to those used in the 2014-15 determination might be more appropriate?**
>
> **(b) What improvements could be made to the current approaches?**
>
> **(c) Any there any other issues we should consider when estimating energy costs?**

4.2 Retail costs

The second element of the R component is retail costs, which include retail operating costs (ROC) and a retail margin. In 2014-15, these elements comprised approximately $183 (12%) and $81 (5%) respectively, of the bill of a typical residential customer on tariff 11[18]. In previous decisions, we have estimated retail costs using a benchmarking approach.

ROC

ROC are the costs associated with services provided by a retailer to its customers and typically include the costs associated with customer administration, call centres, corporate overheads, billing and revenue collection, IT systems, and regulatory compliance. In past decisions, we have also included an allowance to reflect the costs that retailers incur in a competitive market to attract new customers and retain existing customers. These are known as customer acquisition and retention costs (CARC).

In previous determinations, we have set three different ROC allowances to reflect the costs of supplying small, large and very large customers. We propose to continue to set different allowances for 2015-16, because we consider that the costs of supplying large customers are likely to be higher than the costs of supplying small customers.

We recognise that competition is extremely limited in regional areas, particularly for residential and small business customers. We will consider whether it is appropriate to continue to include an allowance for CARC in notified prices for small customers.

If we use the same approach to setting notified prices for large business customers as previous decisions (see Chapter 2), we consider that an allowance for CARC should continue to be included because there is some competition in the large customer market (see Chapter 5).

Retail margin

The retail margin represents the reward to investors for retailers' exposure to systematic risks associated with providing customer retail services. For our 2014-15 determination, we applied a retail margin of 5.7% of total costs for all cost-reflective tariffs. This was consistent with the retail margin adopted by IPART in its 2013 decision on regulated retail electricity prices in NSW[19].

Proposed approach for 2015-16

In our 2014-15 determination, we indicated that we would reconsider using a benchmarking approach in future determinations depending on the regulatory framework established to set notified prices in regional Queensland. Given the uncertainty about the regulatory framework

[18] GST inclusive.

[19] IPART, *Review of regulated retail prices and charges for electricity from 1 July 2013 to 30 June 2016*, June 2013, chapter 7.

that will apply beyond 2015-16, we propose to continue to use a benchmarking approach to estimate retail costs for 2015-16, rather than a potentially data-intensive and costly bottom-up approach.

We expect that our 2014-15 retail cost estimates will provide a good starting point for our analysis.

4.2 We seek stakeholders' views on the following:

(a) Are there are any compelling reasons why the benchmarking approach should not be used to estimate retail costs in 2015-16?

(b) What matters should we consider when deciding whether to include an allowance for CARC?

(c) Are there any other issues we should consider when estimating retail costs?

5 OTHER ISSUES

This chapter discusses other issues relevant to our review, including:

(a) competition and headroom

(b) whether we should include a cost pass-through mechanism

(c) the possible removal of tariffs 13 and 41 from the tariff schedule

(d) transitional arrangements for tariff 11 and tariffs classed as transitional or obsolete.

5.1 Competition and headroom

Under section 90(5)(a) of the Electricity Act, we are required to have regard to the effect of our price determination on competition in the Queensland retail electricity market. We must also have regard to the objects of the Electricity Act[20], which include:

(a) establishing a competitive electricity market in line with the national electricity industry reform process

(b) taking into account national competition policy requirements.

Where it is effective, we consider that competition provides the best means of delivering the goods and services that customers demand at prices that reflect efficient costs. In previous decisions, we have included an allowance for excess profit or 'headroom' to facilitate the development of retail competition in south east Queensland for residential and small business customers and in regional Queensland for large business customers. Since the 2012-13 determination, we have set this allowance at 5% of cost-reflective prices.

However, we recognise that retail competition is extremely limited in regional Queensland as a result of the subsidy arrangements underpinning the uniform tariff policy. This is particularly the case for residential and small business customers, where more than 99% are supplied on a standard contract and pay notified prices, compared to around 30% in the competitive south east Queensland market.

The Queensland Government is considering options to improve competition in regional areas, including changing the way that subsidies are paid[21]. One option under consideration is to provide subsidies to Ergon Energy's distribution business, rather than its retail business. This would remove the key barrier to competition and allow retailers to compete on a more even playing field. The timeframe for these reforms is unclear.

The notified prices we determine for residential and small business customers will be well below the costs of supply in 2015-16. This would mean that the inclusion of any reasonable level of headroom would not be sufficient to promote retail competition. We will consider whether headroom should continue to be included in notified prices for small customers.

On the one hand, it may be argued that headroom should be retained because removing it would move customers further away from cost and increase the subsidy paid by taxpayers. On

[20] *Electricity Act 1994*, s. 3.

[21] Department of Energy and Water Supply, *PowerQ: a 30-year strategy for Queensland's electricity sector*, June 2014, pp. 32-33.

the other hand, it may be argued that headroom should not be included, because it will not promote retail competition in regional Queensland.

As outlined in Chapter 2, in previous decisions we have determined notified prices for large business customers based on the lowest costs of supply in regional Queensland. While we have previously acknowledged that there are still some impediments to competition in this market, retail tariffs for large customers (excluding transitional tariffs) are now cost-reflective for many regional customers. Around 27% of large regional customers have moved to a market contract with a retailer other than Ergon Retail, compared to fewer than 1% of small customers[22]. Where notified prices are set on a cost-reflective basis, we consider that the inclusion of headroom is appropriate to facilitate competition and encourage retailers to compete for customers.

5.1 We seek stakeholders' views on the following:

(a) Should headroom continue to be included in notified prices for residential and small business customers? Why or why not?

(b) Should headroom continue to be included in notified prices for large business customers? If so, at what level? If not, why not?

(c) What other issues should we consider in relation to competition and headroom?

5.2 Cost pass-through mechanism

Cost pass-through mechanisms are used by regulators to account for the risk that the costs allowed for in regulated prices are higher or lower than actual costs. Cost pass-through mechanisms are usually included in multi-year price determinations and restricted to events that are outside the control of the regulated entity.

We applied a cost pass-through mechanism for the first time in our 2014–15 determination to pass-through an under-recovery of costs in 2013–14 associated with the SRES. We also decided that the mechanism could be used to account for material differences in network charges, in the event that the charges billed to retailers (usually the AER-approved charges) differed from those used to set notified prices. However, there was no difference in 2013-14.

Circumstances have now changed. Firstly, the new delegation requires that we determine notified prices for one year, replacing the previous three-year delegation. This means that we would not be able to guarantee the pass-through of any under or over-recovery of costs in 2015-16, because we do not have a delegation to determine notified prices beyond 2015-16. Secondly, the notified prices we determine for 2015–16 will not be cost-reflective for residential and small business regional customers. It is questionable whether a pass-through mechanism is necessary if actual costs are not reflected in notified prices.

[22] Calculated using information provided by Ergon Retail.

5.2	**We seek stakeholders' views on whether a cost pass-through mechanism should be included when setting notified prices for 2015–16.**

5.3 Possible removal of tariffs 13 and 41

The delegation requires that we consider removing tariff 13 from the tariff schedule, on the basis that Ergon Distribution does not have a network tariff for this tariff and no customers in regional Queensland are accessing it.

If Ergon Distribution tariff structures are used for the time-of-use tariffs, the reasons given in the delegation may provide a valid basis to remove tariff 13. However, if we decide to continue to use Energex tariff structures, we will need to consider whether it should be retained or removed.

There may also be valid reasons to remove tariff 41. Tariff 41 is a low voltage demand tariff that is available to small business customers and has fixed, variable and demand charges. Ergon Distribution does not have an equivalent network tariff with this structure and Ergon Retail advised that it supplies fewer than 300 customers on tariff 41. If tariff 41 is removed, customers would be moved to one of the other small business tariffs, either tariff 20 or 22.

We encourage customers and retailers to comment on the potential removal of tariffs 13 and 41.

5.3	**We seek stakeholders' views on whether tariffs 13 and 41 should be removed from the tariff schedule.**

5.4 Transitional arrangements

Under the delegation, we are required to consider:

(a) completing the re-balancing of the fixed and variable components of tariff 11 using the approach established in the 2013-14 determination

(b) maintaining transitional arrangements for tariffs classed as transitional or obsolete, which includes farming and irrigation tariffs.

Re-balancing the fixed and variable components of tariff 11

In our 2013-14 determination, we implemented a three-year transitional arrangement to re-balance the fixed and variable components of tariff 11 so that it would be cost-reflective for south east Queensland customers by 1 July 2015. This approach involved gradually increasing the fixed charge, while making off-setting reductions to the variable charge. We considered that tariff 11 should be transitioned, rather than directly moved, to cost-reflectivity, to strike an appropriate balance between:

(a) limiting increases in the fixed charge, to ease the financial pressure on customers with low levels of consumption

(b) moving the variable charge closer to cost, to reduce the cross-subsidy paid by customers with high levels of consumption.

The delegation requires that we consider completing the rebalancing using the approach established in the 2013-14 determination. We consider that this approach would be appropriate if we were continuing to set notified prices for south east Queensland customers, because it would complete the transition to cost-reflectivity. It is also likely to be appropriate if we maintain this approach for regional Queensland, because it would complete the transition to a notified price that reflects the costs of supply in south east Queensland.

We will consider these issues as part of our review.

5.4 We seek stakeholders' views on the following:

(a) What issues should we take into account when deciding whether to complete the rebalancing of tariff 11 using the approach established in the 2013-14 determination?

Transitional and obsolete tariffs

Some business customers are supplied under transitional or obsolete tariffs. These include farming and irrigation tariffs. Customers on these tariffs are often paying below the cost of supplying customers in the lowest cost area of the state (i.e. south east Queensland).

In previous determinations, we decided that most of these tariffs should continue to be available for several years because many customers would face significant financial impacts if they were moved to an alternative tariff.

As proposed in the delegation, we propose to maintain the transitional arrangements for these tariffs.

Escalating transitional and obsolete tariffs

We propose to continue to escalate transitional and obsolete tariffs in accordance with the methodology established in the 2013-14 determination and continued in the 2014-15 determination. This involves escalating the charges in each tariff based on the percentage increase in the charges in the alternative tariff that customers would otherwise pay, plus an additional escalation to ensure that charges under the transitional and obsolete tariffs do not fall further below cost in dollar terms.

Consistent with previous decisions, if the underlying cost increase is low, we will consider whether higher escalation factors are needed to prevent these tariffs falling further below cost. This is the approach we adopted to set carbon-exclusive notified prices in our 2014-15 determination, where we applied an increase of 10% to all transitional and obsolete tariffs.

Transition period

We established transitional time periods in our 2013-14 determination and decided to maintain these periods in our 2014-15 determination. Tariffs 21, 37, 62, 65, 66, 20 (large) and 22 (small and large) were made available until 2020 and tariffs 41 (large) and 43 (large) were made available until 30 June 2015.

We consider that maintaining these time periods will provide certainty to customers. Therefore, consistent with our approach in the 2014-15 determination, we do not propose to make any changes, unless an analysis of customer impacts indicates that a tariff could be removed earlier without causing significant customer detriment.

Access to transitional tariffs

In our 2013-14 determination, we decided that all non-market customers should have access to transitional tariffs, subject to individual tariff terms and conditions[23]. We made this decision to ensure equitable access for all businesses. The delegation requires that we consider continuing to allow access for all regional customers.

In the 2014-15 determination, we noted that we would consider closing access to transitional tariffs to new customers if there was a significant increase in the number of customers accessing transitional tariffs, and thereby an increase in the subsidy paid by taxpayers. However, we did not find that there had been a significant increase and decided to continue to allow open access. We propose to undertake a similar assessment as part of this price review.

5.5 We seek stakeholders' views on the following:

(a) Is there any new information that suggests the overall approach we propose to take for transitional and obsolete tariffs is no longer appropriate?

(b) What other issues should we should consider (please provide supporting evidence where possible)?

[23] New customers cannot access tariffs classified as obsolete. We made this decision on the basis that they had been obsolete for some time (tariff 37) or because they would be removed in a shorter timeframe (tariffs 41 (large) and 43 (large)).

GLOSSARY

A	
AEMC	Australian Energy Market Commission
AEMO	Australian Energy Market Operator
AER	Australian Energy Regulator
C	
CAC	Connection asset customer
CARC	Customer acquisition and retention costs
CSO	Community service obligation
c/day	cents per day
E	
EECL	Ergon Energy Corporation Limited (electricity distribution arm)
EEQ	Ergon Energy Queensland (electricity retail arm)
Electricity Act	*Electricity Act 1994* (Qld)
G	
GWh	Gigawatt hour
Government	Queensland Government
I	
IBT	Inclining block tariff
K	
kWh	kilowatt hour
L	
LRET	Large-scale Renewable Energy Target
LRMC	Long-run marginal cost
N	
NEM	National Electricity Market
Notified prices	regulated retail electricity prices
P	
PPA	Power purchase agreement
Q	
QCA	Queensland Competition Authority
R	
RET	Renewable Energy Target
ROC	Retail operating costs

S	
SCER	Standing Committee on Energy and Resources
SRES	Small-scale Renewable Energy Scheme
T	
ToR	Terms of Reference

APPENDIX A: MINISTERIAL DELEGATION AND COVERING LETTER

Queensland Government

Office of the
Minister for Energy and Water Supply

QLD COMPETITION AUTHORITY
0 1 SEP 2014
DATE RECEIVED

CLLO CIC-14109

Level 13 Mineral House
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29 August 2014

Dr Malcolm Roberts
Chairman
Queensland Competition Authority
GPO BOX 2257
BRISBANE QLD 4001

Dear Dr Roberts

I refer to the current Delegation and Terms of Reference (ToR), issued to the Queensland Competition Authority (QCA) on 12 February 2013, for determining regulated retail electricity (notified) prices for the three-year delegation period 2013-14 to 2015-16, as authorised under section 90AA(1) of the *Electricity Act 1994*.

As you would be aware, the Queensland Government is undertaking wide-ranging reform of the electricity sector. These reforms, announced in June 2013, have been established with the objectives of ensuring:

1. electricity in Queensland is delivered in a cost-effective manner for customers;
2. Queensland has a viable, sustainable and competitive electricity industry; and
3. electricity is delivered in a financially sustainable manner from the government's perspective.

The introduction of market monitoring in South East Queensland (SEQ) by 1 July 2015, subject to a number of pre-conditions being met, is a key reform to the electricity sector designed to improve competition and reduce pressure on prices. To facilitate this, on 20 May 2014, the *National Energy Retail Law (Queensland) Bill 2014* and the *Electricity Competition and Protection Legislation Amendment Bill 2014* were introduced into the Legislative Assembly.

However, this Government remains committed to the Uniform Tariff Policy (UTP) and the QCA will continue to set notified prices for the Ergon Energy Corporation Limited distribution region, while Government finalises a strategy for introducing competition into regional Queensland in the future.

Page 1 of 2

In this context, I thank the QCA for the advice provided in April 2014, on matters relating to the UTP and options for retail price regulation in regional Queensland. Government has considered the QCA's advice and I have attached a new Delegation and ToR on the matters the QCA is required to consider in its regional price determination process for 2015-16. Following Government consideration, this report can now be publically released and there may be benefit in releasing it concurrently with the QCA's Interim Consultation Paper on 2015-16 regulated regional prices.

The new Delegation and ToR will assist in building on the measures already undertaken to deliver on Government's longer term reform objectives. The ToR will provide a platform for improved competition in regional Queensland and in the longer term, consumer benefits that will flow from this.

I would like to take this opportunity to thank the QCA for its ongoing work on regulated retail electricity prices.

Should you require anything further, please contact Mr Benn Barr, General Manager- Energy Pricing, Consumer and Retail, on (07) 3199 4901, or email benn.barr@dews.qld.gov.au.

Yours sincerely

Mark McArdle
Minister for Energy and Water Supply

Att: Delegation and Terms of Reference

Page 2 of 2

ELECTRICITY ACT 1994
Section 90AA(1)

DELEGATION

I, Mark McArdle, the Minister for Energy and Water Supply, in accordance with the power of delegation in section 90AA(1) of the *Electricity Act 1994* (the Act), delegate to the Queensland Competition Authority (QCA) the function under section 90(1) of the Act of deciding the prices that a retail entity may charge its non-market customers for customer retail services in the Ergon Energy Corporation Limited (EECL) distribution area for the tariff year 1 July 2015 to 30 June 2016.

The following are the Terms of Reference of the price determination:

Terms of Reference

1. These Terms of Reference apply for the tariff year 1 July 2015 to 30 June 2016.

2. The QCA is to calculate the notified prices and publish an annual price determination, in the form of a tariff schedule, in accordance with these Terms of Reference.

3. In accordance with section 90(5)(a) of the Act, in making a price determination for each tariff year QCA must have regard to the matters set out in paragraph 5 of these Terms of Reference.

4. In accordance with section 90(5)(b) of the Act, QCA may have regard to any other matter that QCA considers relevant.

5. The matters that QCA is required by this delegation to consider are:

   (a) It is the Government's intention, that from 1 July 2015, price regulation in the Energex distribution area will be removed for small customers and replaced with a market monitoring approach. This will mean that notified prices will only apply to customers in the EECL distribution area;

   (b) Uniform Tariff Policy Review - As part of Government's longer term electricity sector reform program a review of the effectiveness and objectives of the Uniform Tariff Policy and Community Service Obligation, and options for improved regional competition is currently being undertaken;

   (c) Framework - QCA must use the Network (N) plus Retail (R) cost build-up methodology when working out the notified prices and making the price determination, where N (network cost) is treated as a pass-through and R (energy and retail cost) is determined by QCA;

(d) When determining the N components for each regulated retail tariff, QCA must consider the following:

(i) For residential and small business customer tariffs (with the exception of Tariffs 12 and 22) in the EECL distribution area - basing the network cost component on the network charges to be levied by Energex and the relevant Energex tariff structures;

(ii) For Tariff 12 residential time-of-use and Tariff 22 small business time-of-use tariffs in the EECL distribution area - basing the network cost component on the network charges to be levied by Energex, but utilising the relevant EECL tariff structures, in order to strengthen or enhance the underlying network price signals and encourage customers to switch to time-of-use tariffs and reduce their energy consumption during peak times;

(iii) For Tariff 13 residential peaksmart time-of-use, as EECL does not have a network tariff for this tariff, and no customers access the tariff, it is proposed that this tariff be removed from the tariff schedule; and

(iv) For large business customers in the EECL distribution area who consume 100MWh or more per annum - basing the network cost component on the network charges to be levied by EECL.

(e) Transitional Arrangements - QCA must consider:

(i) for the standard regulated residential tariff (Tariff 11), complete the rebalancing of the fixed and variable components of Tariff 11 using the approach established in the 2013-14 Determination;

(ii) maintaining transitional arrangements for tariffs classed as transitional or obsolete (i.e. farming, irrigation, declining block, non-domestic heating and large business customer tariffs), and

(iii) continuing to allow all EECL customers access to tariffs designated as transitional in 2013-14.

Interim Consultation Paper

6. QCA must publish an interim consultation paper identifying key issues to be considered when calculating the N and R components of each regulated retail electricity tariff and transitioning relevant retail tariffs.

7. QCA must publish a written notice inviting submissions about the interim consultation paper. The notice must state a period during which anyone can make written submissions to QCA about issues relevant to the price determination.

8. QCA must consider any submissions received within the consultation period and make them available to the public, subject to normal confidentiality considerations.

Consultation Timetable

9. QCA must publish an annual consultation timetable within two weeks after submissions on the interim consultation paper are due, which can be revised at the discretion of QCA, detailing any proposed additional public papers and workshops that QCA considers would assist the consultation process.

Workshops and additional consultation

10. As part of the interim consultation paper and in consideration of submissions in response to the interim consultation paper the QCA must consider the merits of additional public consultation (workshops and papers) on identified key issues.

Draft Price Determination

11. QCA must investigate and publish its draft price determination on regulated retail electricity tariffs, with each tariff to be presented as a bundled price.

12. QCA must publish a written notice inviting submissions about the draft price determination. The notice must state a period during which anyone can make written submissions to QCA about issues relevant to the draft price determination.

13. QCA must consider any submissions received within the consultation period and make them available to the public, subject to normal confidentiality considerations.

Final Price Determination

14. QCA must investigate and publish its final price determination on regulated retail electricity tariffs, with each tariff to be presented as a bundled price, and gazette the bundled retail tariffs.

Timing

15. QCA must make its reports available to the public and, at a minimum, publicly release the papers and price determinations listed in paragraphs 6 to 14.

16. QCA must publish the interim consultation paper for the 2015-16 tariff year no later than one month after the date of this Delegation.

DELEGATION TO QCA

17. QCA must publish the draft price determination on regulated retail electricity tariffs no later than 12 December 2014.

18. QCA must publish the final price determination on regulated retail electricity tariffs for the 2015-16 tariff year, and have the bundled retail tariffs gazetted, no later than 31 May 2015.

19. This Delegation revokes my previous Delegation issued on 12 February 2013.

DATED this 28th day of ~~XX 2014~~. August 2014

SIGNED by the Honourable)
Mark McArdle,) ....
Minister for Energy and Water Supply) *(signature)*

APPENDIX B: ADDITIONAL LETTER FROM THE MINISTER

Queensland Government

Office of the
Minister for Energy and Water Supply

Ref CTS 23690/14

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25 September 2014

Dr Malcolm Roberts
Chairman
Queensland Competition Authority
GPO BOX 2257
BRISBANE QLD 4001

Dear ~~Dr Roberts~~ Malcolm

I write with respect to paragraphs 5(b) and 5(d)(1) of the Terms of Reference in the delegation under s90AA of the *Electricity Act 1994* dated 28 August 2014.

There have been a number of recent statements questioning this Government's commitment to the Uniform Tariff Policy (UTP) and the Community Service Obligation (CSO) payment that underpins it. As identified in the delegation, the Government is reviewing the effectiveness and objectives of the UTP and CSO, and options for improved regional competition. I understand that due to this process there could be some uncertainty and therefore, I feel it is important to formally re-affirm the Government's support for the UTP and provide advice regarding the Government's interpretation of the UTP.

The Government determined before making the delegation that for the purposes of the delegation regional prices should, as much as is practicable, aim to ensure that small customers outside south east Queensland do not pay more than reasonable expectations of the prices which would be available to standing offer customers in south east Queensland.

It is clear the matters which the QCA has been asked to consider in the delegation are consistent with this approach. In particular, the specific network tariffs identified to underpin the retail tariffs for small customers demonstrate the Government's preference that the prices regional customers will pay are consistent with customers in south east Queensland. In addition, the matters set out in the delegation were developed to maintain consistency with the approach used in the previous delegation.

In noting this, I also understand the delegation sets out matters the QCA must consider and it is reasonable to expect that the QCA may consider other approaches in its consultation.

Should you require anything further, please contact Mr Benn Barr (General Manager- Energy Pricing, Consumer and Retail) on 3199 4901, or email benn.barr@dews.qld.gov.au.

Yours sincerely

Mark McArdle
Minister for Energy and Water Supply