

SUBMISSION TO THE QUEENSLAND COMPETITION AUTHORITY DRAFT DETERMINATION 2016-17

CHAMBER OF COMMERCE AND INDUSTRY QUEENSLAND SUBMISSION

20 April 2016

1.0 About the Submission

The Chamber of Commerce and Industry Queensland (CCIQ) makes this submission in response to the Queensland Competition Authorities (QCA) Draft Determination for 2016-17 regulated retail electricity prices for regional Queensland. The intent of this submission is to highlight the impact of pricing determinations on the competitiveness and profitability of Queensland businesses.

CCIQ would like to acknowledge the QCA for their efforts in previous years to keep price increases for small businesses on tariffs 20 and 22 to a minimum. As such, it comes as a shock to small businesses in regional Queensland that the QCA draft determination seeks to increase retail prices for small businesses by a staggering 9.3 per cent for tariff 20.

CCIQ is extremely disappointed by the draft determination and believes the price increase will cripple small business customers, particularly after almost a decade of exorbitant electricity costs.

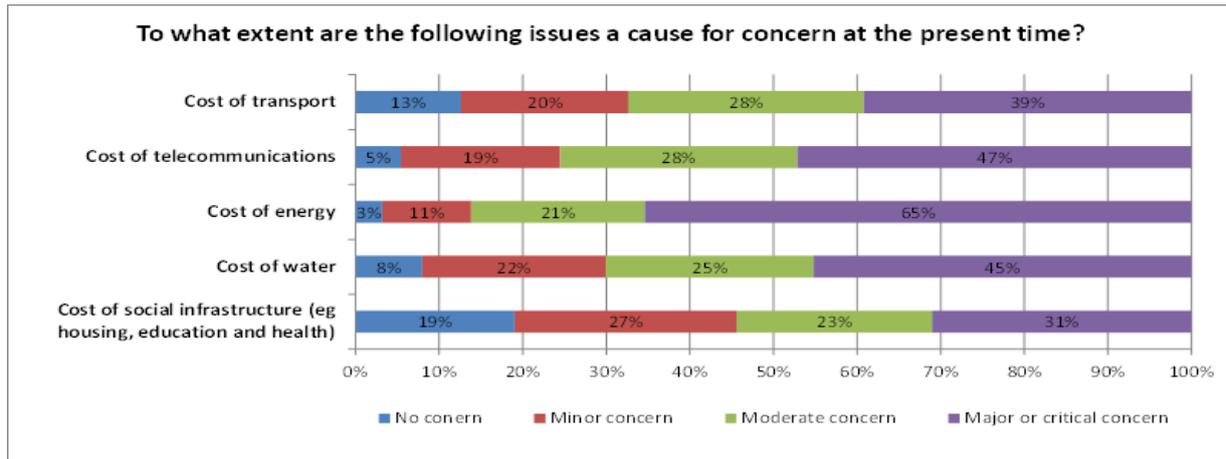
The Queensland Government has legislated to remove retail price regulation in the Energex distribution area (South East Queensland) from 1 July 2016. The delegation provided to the QCA notes that, without further legislative change, notified prices will only apply to customers in Ergon Energy's distribution area (regional Queensland).

CCIQ has strongly advocated for fundamental reforms across the entire energy sector in Queensland to relieve small businesses of the rising cost of electricity that has occurred over the past 8 years.

It comes as little consolation that the increase is a result of a change in methodology calculations. CCIQ purport that methodologies that result in such high increases for small businesses are unsustainable and counterproductive to the future of the electricity industry.

2.0 Pricing Impacts on Small and Medium Businesses

Queensland small businesses have seen unsustainable increases in electricity prices in recent years. Electricity prices have, on average, doubled for business over the past seven years, which has created an enormous hurdle for businesses trying to remain competitive. CCIQ recently surveyed more than 1100 small businesses across the state ahead of the Queensland state election in 2015 to determine key issues. Of those businesses surveyed it was identified that increasing electricity prices is currently the most significant business issue with 65% of Queensland businesses surveyed indicating a major or critical concern with the cost of energy.



Source: Refer to <https://www.cciq.com.au/assets/2015-State-Election/2015-State-election-Super-7-Foldout.pdf>

The QCA provides that in 2016-17, typical customers on the main small business tariff (tariff 20) can expect an increase of \$197 or 9.3 per cent in their annual bill. Typical small business customers on the seasonal time-of-use tariff (tariff 22A) can expect an increase of \$569 or 13.6 per cent. These increases have been driven primarily by higher energy costs and retail costs. Bill impacts will vary depending on each individual customer’s level and pattern of consumption.

CCIQ understands the QCA had limited time to prepare the draft determination, however it was disappointing to see the report omitted the usual level of detail provided on the impacts for small business customers.

3.0 QCA Methodology

Consistent with the approach from previous determinations, the QCA is required to consider applying the network (N) plus retail (R) cost build-up methodology and the Queensland Government’s uniform tariff policy (UTP).

The network cost component is determined on the basis of using Energex’s network charges and tariff structures for non-time-of-use tariffs. This means the uniform tariff policy has resulted in network charges being below cost because they are based on network costs in south east Queensland, rather than regional Queensland. The QCA have noted that the current arrangements do not allow for cost reflectivity and results in customers continuing to pay much less than the cost of supply, potentially leading to inefficient investment and decision-making, as well as ongoing costs to taxpayers.

The QCA provide that setting cost-reflective notified prices (i.e. reflecting the actual costs of supply to customers in each region) 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. It would also mean significant price increases, particularly for customers in western parts of the state, and those supplied by isolated systems. For instance, a typical tariff 11 customer paying cost-reflective prices in 2014–15 would pay around 140% more in western Queensland than in south east Queensland.

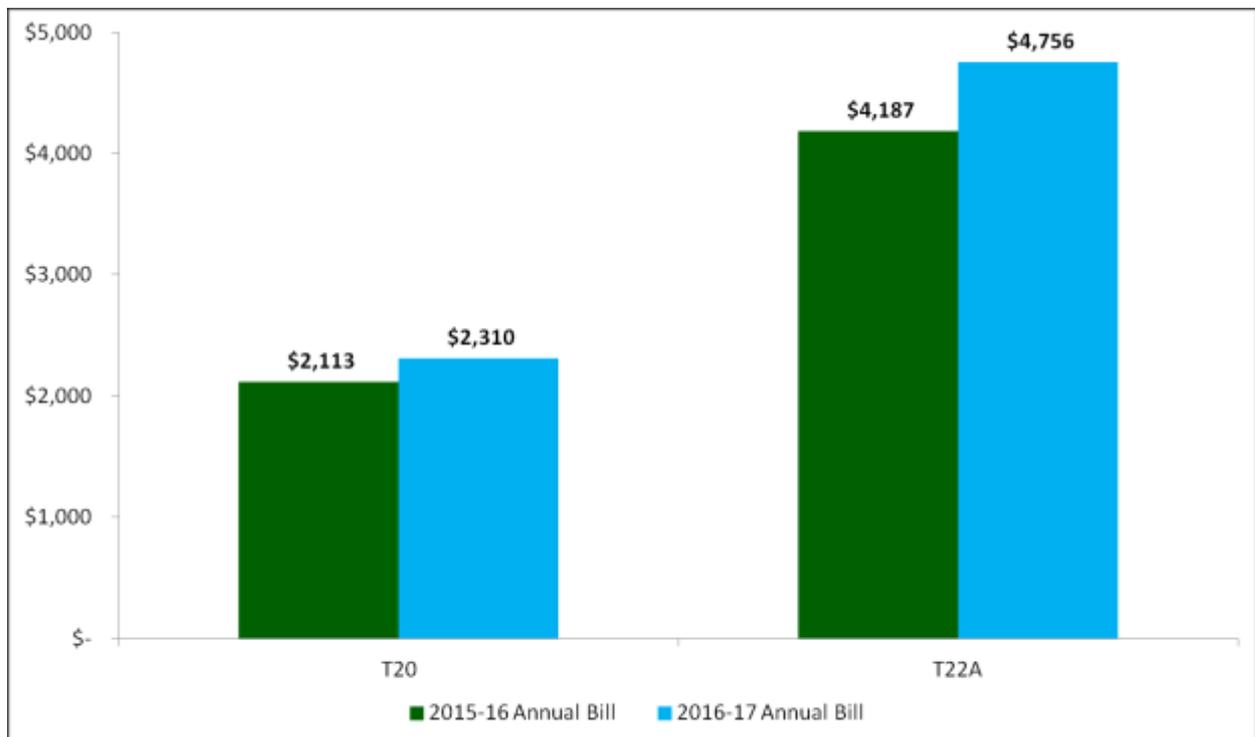
CCIQ note that notified prices based on the cost of supply in regional Queensland would be prohibitively expensive for small business customers. This measure would prove more costly

for business customers who are unable to shift usage outside of the peak times. Whilst this tariff would be more cost reflective and provide sharper pricing signals, it would be ineffective on a small business restricted by the times they use electricity. CCIQ are pleased to see that the QCA consider the impact on customers as a very relevant factor, particularly given the significant price increases customers have faced in recent years.

4.0 Summary of QCA Draft Determination

The review conducted by the QCA will set regulated retail electricity prices in the Ergon Energy distribution area, which covers regional and rural areas of Queensland. On current forecasts small business tariffs 20 (flat rate) and 22A (time of use) are expected to increase by \$197 (9.3) per cent and \$569 (13.6 per cent) respectively. The QCA has applied their determination on the basis of the latest forecasts for network, energy, retail and green scheme costs. The new tariff prices for the 2016-17 period recommended in the QCA draft determination are outlined in the below table.

Annual bills for typical small business customers (GST inclusive)



Source QCA Draft Determination 2016-17

5.0 Increases in electricity prices

The QCA provide that the increases in electricity prices have been primarily driven by higher energy costs and retail costs. Wholesale energy costs and the Renewable Energy Target (RET) are estimated to add 4.8 per cent to a typical bill for a small business customer on tariff 20 and increases in retail costs are estimated to add 3.8 per cent.

The increases in the small business bills are a result of the change in approach to calculating the retail operating costs (ROC) and retail margin. Previously, the QCA have benchmarked other regulatory decisions to set retail operating costs and margins. Instead the QCA have:

- adopted a separate retail cost allowance for small businesses;
- estimate total retail cost allowance for small business tariffs based on benchmarking observations, applied as fixed and variable components.

The retail costs are made up of the ROC and a retail margin. Previously the ROC was estimated using benchmarks from IPART decisions. The retail margin was based on the retail margin adopted by IPART from the 2013-16 decision on regulated retail prices in NSW.

The results of the change in market data benchmarking is that the average total retail costs are higher for small business customers than for residential customers. The market data indicates that retailers recover a greater proportion of retail costs from the variable component of small business tariffs, compared to the QCA's previous assumptions.

There are also significant differences in how retailers allocate retail costs between fixed and variable components. The data indicates that a greater proportion of retail costs are recovered through variable charges on small business tariffs than is the case for residential customer tariffs as seen in the following graph.

Figure 5 Benchmark average total retail costs by retailer - Small business customers



Note: Assumes average annual consumption of 16,370 kWh.

Source QCA draft determination 2016-17

CCIQ believes that the sample of observations might not be the best source to use to average retail costs. The analysis indicates that the retail costs of serving customers on small business tariffs are higher than residential customers due to a number of factors including:

- different customer risk profiles and potentially a greater likelihood of default for small business customers
- the need for different marketing approaches and customer acquisition and retention strategies; and
- greater use of manual process and more individual contact with small business customers compared to residential customers.

CCIQ believes that these circumstances may not be consistent with small business usage in Queensland as it relies too heavily on outcomes observed in other jurisdictions.

While CCIQ understands that there have been calls for the QCA to undertake a more comprehensive review of the retail cost, this has resulted in detrimental impacts on pricing for small businesses. CCIQ believe that the QCA should reconsider continuing the previous approach of using the Queensland retail operating cost benchmark.

It is difficult for small businesses to accept that a change in methodology is required when it impacts negatively on their overall electricity costs.

The 2016-17 price increase is not only unsustainable, it is also inconsistent with the State Government's commitment to Queensland small businesses that electricity pricing is stabilising and coming down.

6.0 Uniform Tariff Policy

A key concern for CCIQ is the future direction of the uniform tariff policy (UTP) and regional pricing. The State Government is committed to retaining the UTP so that residential and small business customers do not pay more than the prices that would be available to standing offer customers in south east Queensland. The end of notified prices in south east Queensland from 1 July 2016 requires that the QCA reassess their approach to setting notified prices for residential and small business customers in regional Queensland. In the absence of notified prices in south east Queensland, the QCA needs to set regional prices on a new basis, according to their obligations under the *Electricity Act 1994* and taking into account matters raised in the delegation.

The QCA provide that they will continue to base notified prices for residential and small business customers on the cost of supply in south east Queensland. The QCA plan to determine notified prices based on expected standing offer prices in south east Queensland. CCIQ believe that a case could be made for the QCA to set prices somewhere between the market contract prices and standing offer prices available in south east Queensland.

CCIQ stress that until such a time that the Queensland Government decide to reform the current arrangements of the uniform tariff policy, little can be done to improve the effectiveness of its operation. Ideally, CCIQ would like to see the uniform tariff policy applied to Ergon Distribution so as to increase competition in the retail market for regional Queensland.

7.0 Solar Bonus Scheme

Significant costs have been incurred by distributors in complying with the Queensland Government's Solar Bonus Scheme (SBS). Solar feed-in tariffs under the SBS will continue to be a major cost for small business customers. The costs of the SBS have almost doubled since 2013-14.

CCIQ supports the recommendation made by the Queensland Productivity Commission (QPC) in their draft report on electricity pricing in Queensland for the Queensland Government to consider the merits of an earlier end to the SBS than the planned 2028 closure. CCIQ believe the Queensland Government should commit to removing the impost of costs associated with the SBS to relieve pressure from consumers subsidising excessive feed-in-tariff rates.

8.0 Network costs

For small business customer retail tariffs (tariff 20), the QCA have decided to base the network cost component on Energex network charges and tariff structures. For small business customer time-of-use retail tariffs (tariff 22A), the QCA will base the network cost component on Energex network charges, but use the relevant Ergon Distribution network tariff structures.

This is a similar approach to the 2015-16 determination. Basing the time-of-use tariffs on Ergon Distribution's network tariff structures allow for improved cost reflectivity. CCIQ is satisfied with this approach.

CCIQ stresses that the QCA needs to ensure that consumers are adequately educated about their options in relation to moving to time of use tariffs.

9.0 Other issues

Improving competition in regional Queensland is an important issue that needs to be considered by the Queensland Government. CCIQ supports the recommendation made by the QPC in their draft report on electricity pricing to implement a network CSO no later than 1 July 2019. CCIQ supports the QCA in its recommendation to remove key barriers to competition in the market and allow retailers to compete on a more even level playing field.

10.0 Conclusion

CCIQ appreciates that many of these issues are outside the scope of this review and the responsibilities of the QCA. However, CCIQ strongly urges the QCA and the Queensland Government to ensure that the full and compounding impact of this and previous years electricity price increases for Queensland small businesses are considered in the final determination for 2015-16 regulated tariff prices.

CCIQ believes the 2016-17 draft determination will be poorly received by the business community. Queensland small businesses are coming to the end of their tether with electricity affordability. CCIQ urge the QCA to consider the future implications for small businesses when making the final determination.