



EnergyAustralia

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Dear Dr Roberts

Submission on the Draft Determination for Regulated Retail Electricity Prices 2013-14

EnergyAustralia welcomes the opportunity to make a submission to the Queensland Competition Authority (the Authority) on the draft determination for regulated retail electricity prices 2013-14 (Draft Determination).

EnergyAustralia is one of Australia's largest energy companies, providing gas and electricity to over 2.7 million residential and business customers. EnergyAustralia owns and operates a multi-billion dollar portfolio of energy generation and storage facilities across Australia including coal, gas and wind assets with control of over 5,600 MW of generation in the National Electricity Market.

We have been retailing in South East Queensland since the beginning of full retail contestability and have a long-term interest in the level of the regulated retail prices and the state of competition in this market. Rather than a continuation of regulatory involvement, we believe this market would benefit from pricing deregulation to help bring about cost reflectivity in retail tariffs and improvements in the level of competition.

While price regulation remains, we will continue to participate in reviews conducted by the Authority and suggest where changes could be made to bring about improvements for customers, retailers and the overall competitiveness of the market.

In this submission, we focus on:

- The estimation of the wholesale energy cost allowance in the regulated tariff – particularly on the load and spot forecasting approaches which show unusual trends and do not appear acceptable for use in modelling the market-based purchase cost of electricity.
- The need to calculate a Queensland specific retail cost and margin using a more detailed approach.
- The level of competition in South East Queensland, which we believe has declined.

- Suggested amendments to the design of the new cost pass-through mechanism.

If you would like more information on this submission, please contact me on (03) 8628 1242.

Yours sincerely

Melinda Green
Regulatory Manager - Pricing

**EnergyAustralia submission to
Queensland Competition Authority
on the
Draft Determination for
Regulated Retail Electricity Prices
2013-14**

March 2013

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1. Executive summary

The common themes amongst the key points we've raised in our submission are that the Authority should ensure a rigorous and accurate approach is used to determine the regulated retail prices for Queensland. This will help to ensure that prices reflect the level and nature of costs faced by retailers and will encourage competition.

Our major comments on each section of the Draft Determination are summarised below.

Energy costs

While we haven't altered our position on the need to include long-term generation and contracts costs in estimating the energy cost allowance, we have concentrated on reviewing elements of the market-based approach developed by ACIL Tasman.

In our view, the load forecasting methodology does not properly represent the load shape that would be expected for Queensland in 2013/14 and we go into the reasons why this may be occurring and how it could be improved. We also demonstrate that on several measures, the spot price forecasts are quite inconsistent with expected trends and are therefore not suitable for use in developing the energy cost allowance without further work and justification.

Retail costs and margin

The Authority relies heavily on retail cost and margin values published by other state retailers. We discuss where we see flaws in this approach and suggest how these could be overcome by a more detailed, bottom up, benchmarking approach.

Competition and other issues

The assessment of competition carried out by the Authority for the Draft Determination has not made the best use of available data in our opinion. We are also concerned that the Authority has found competition to be stable if not improving, when we believe that it has declined over the past year.

The inclusion of a cost pass through mechanism over the upcoming delegation period is a welcome addition. The design of the mechanism appears to be generally suitable, however we request that the Authority provides extra clarity on the eligibility criteria and does not include any materiality criteria. Our analysis of the mechanism suggests that there is no clear benefit from including a materiality clause for Queensland regulated retail prices.

Network costs

Another new residential time of use network tariff (peak smart) has been proposed by Energex. Although this tariff is unlikely to attract many customers in 2013/14, it will still require the introduction of a new regulated retail tariff. We ask if there are any steps that Energex or the Authority can take to address the inefficiencies created in this situation.

2. Energy costs

2.1. Introduction

In response to both the first and third consultation papers, we argued strongly for the inclusion of the long run marginal cost of generation (LRMC) in the calculation of the energy costs and were disappointed to see that the Authority has again rejected the use of LRMC in any form in determining Queensland regulated retail tariffs. There is an internal inconsistency in using current bidding arrangements without factoring in long term contracts in any form. Current hedge levels would not occur at the modelled hedge prices. Arguments have already been put forward on this point, which ACIL Tasman has dismissed out of hand.¹ ACIL Tasman's view of the market appears to be that credit, liquidity and supply issues are negligible and things are so well balanced that quite dramatic shifts in hedging behaviour will have no material impact on wholesale prices.

We disagree strongly with ACIL Tasman on all these points, but do not see that there is any point to again argue these theoretical points at this stage of the review. The rest of this section focuses on an assessment of the calculation approaches that ACIL Tasman has taken in coming up with the energy cost allowance for 2013/14.

Since the Draft Determination was published, we note that the Queensland Government have announced the closed of the Queensland Gas Scheme and the Clean Energy Regulator has released update STP values for 2013 and 2014. We understand that ACIL Tasman will be updating each component accordingly.

2.2. Load forecasts

2.2.1. Selection of load data

Whilst temperature data is available since 1970, only three years of data (09/10 to 11/12) are being used by ACIL Tasman in developing the load profiles. This is a concern as there were very few representative high temperature days over the three sample years. Table 1 below shows the number of working days with a max temperature 35°C or higher. The load in the post-Christmas period (1 Jan – 14 Jan) is typically lower for commercial and industrial customers than the rest of Q1, so the temperature data is outlined separately. We strongly recommend that the matching of the historic days to forecast days take into account the lower industrial and commercial loads typically found during the Christmas and early January period.

Table 1 - Brisbane daily maximum Q1 temperatures (2010-2012)

Daily maximum (°C)	1 Jan – 14 Jan	14 Jan - 31 Mar	Total Q1 2010-2012
≥38	0	0	0
37	1	0	1
36	0	0	0
35	0	1	1

This shows that every high temperature day within one of the 39 simulated years would be represented under ACIL Tasman's proposed methodology by one of only two historic days. Thus, these two days will be used repeatedly within the 39 years. This is particularly a concern as one of the two days is in the first two weeks of Jan, when load is typically lower than the rest of Q1.

¹ ACIL Tasman , Estimated energy costs for 2013-14 retail tariffs: for use by the QCA in its Draft Determination on retail electricity tariffs, Feb 2013, pages 10-11

Noting that 70% of days over 35°C in Q1 since 1970 have occurred within the 14 Jan - 31 Mar period, this will unreasonably bias the demand forecasts to lower Queensland regional demands. Furthermore, the use of only three sample years (2009/10 to 2011/12) means that the final determination outcome will be overly dependent on a very small sample number of high demand days. This could easily bias the outcome such that a reasonable energy price was not achieved.

We believe these issues could be addressed by basing the load forecasts on a longer time period. For example, if ACIL Tasman were to use even one additional year of data in their sample (2008/09) then there would be two days after 14 Jan with temperatures over 35°C within the sample to choose from.

At the public forum held by the Authority for this review (7th March, Brisbane), ACIL Tasman stated that they didn't believe that any other years needed to be taken into account to develop an adequate load profile and that they were not trying to predict an outlying year such as 2007/08. A larger sample size is not required simply to predict an outlying year, but to increase the robustness and reliability of the methodology and hence of the pricing outcome.

ACIL Tasman's statement that additional years are not necessary also contradicts the approach that they recommended to Energex in 2012 for developing a system demand forecast for Energex's Network Management Plan 2012/13-2016/17.² This document describes a detailed approach to determining the system demand forecast for the Energex area based on an analysis of ten years of load data and 57 years of temperature data. Energex are attempting to accurately forecast peak demand, average demand and usage. This is similar to the requirements of this review. We question why ACIL Tasman would recommend that only three years of data are suitable for setting regulated retail electricity tariffs but see that a more comprehensive approach is necessary for the Energex Network Management Plan.

When creating load profiles it's important to address the effect on load when several hot days occur in a row. We found that there is a significant difference in the number of consecutive hot days in the last 5 years when comparing summer weekday temperature data with data for February in each year (figures 1 and 2). Thus, a high-level approach based on season matching may wash out the influence of relevant data. This could lead to high demand days being inaccurately modelled for this price determination. We contend that ACIL Tasman's approach has led to the production of a load forecast that doesn't reflect the peakiness of the load accurately throughout the year.

We ask that ACIL Tasman extend their analysis to include more years of load data and ensure that the profile is not compromised by a high-level approach to modelling consecutive days of high demand. If no changes are made, we ask ACIL Tasman to demonstrate that the issues outlined above are addressed appropriately by providing data to support their arguments.

² Energex, Energex Network Management Plan 2012/13 to 2016/17 (Final), Part A, Aug 2012, page 26

Figure 1 - Weekdays with maximum temperature > 32°C for three consecutive days during summer³

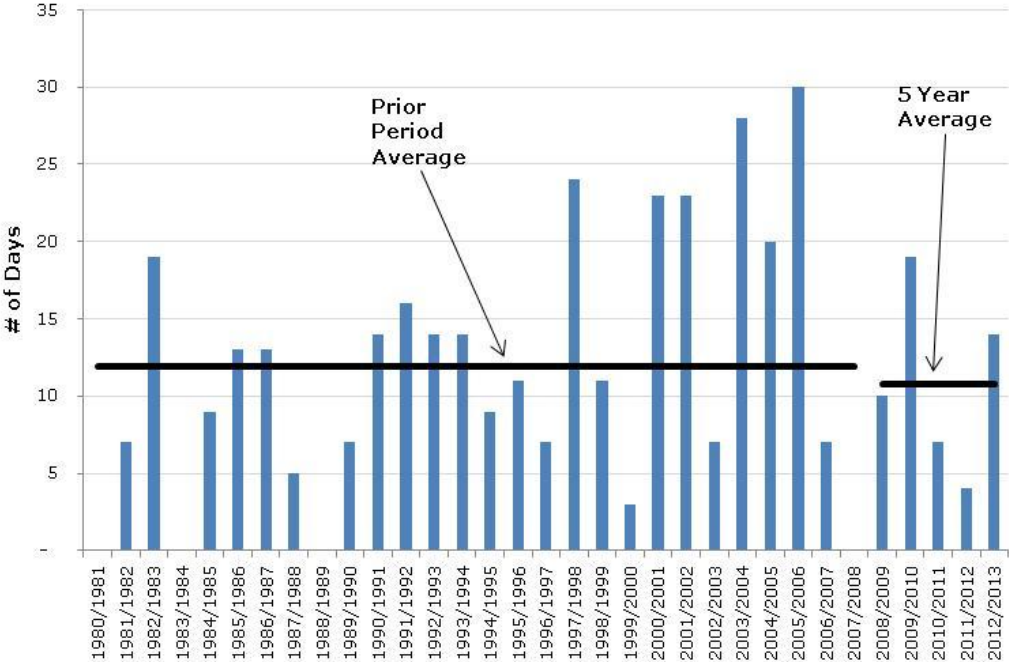
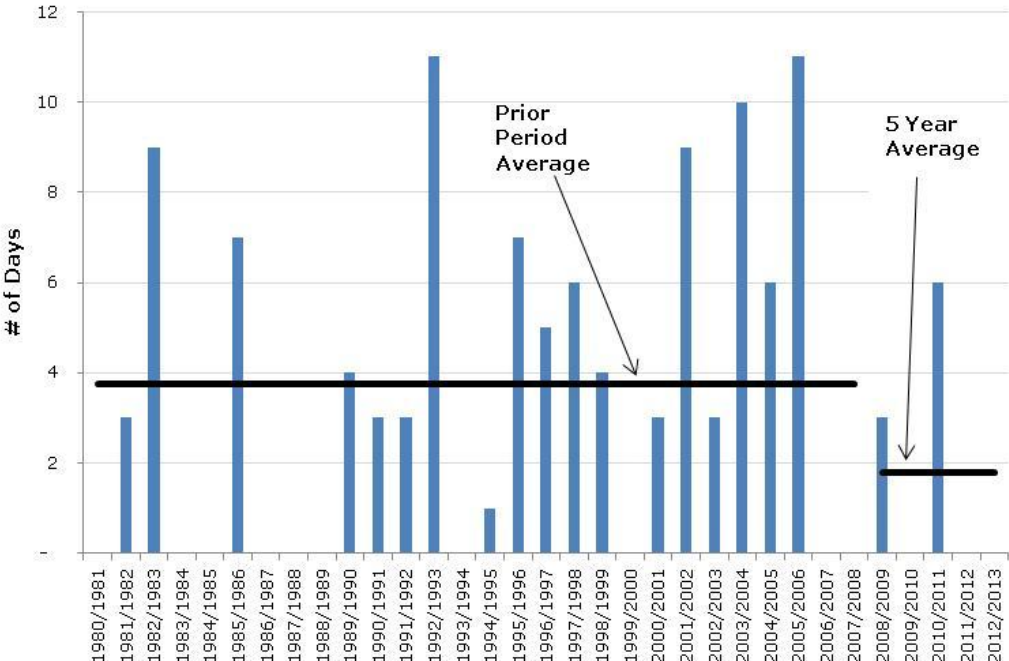


Figure 2 - Weekdays with maximum temperature > 32°C for three consecutive days during February³



³ Data source – Bureau of Meteorology data for Amberley, Queensland

2.2.2. Development of the 42 demand sets

Simulation of the 39 load traces

The least squares matching approach used by ACIL Tasman involves matching across all National Electricity Market (NEM) regions simultaneously based on temperature and leads to the selection of Queensland load for that day. This process is part of the day-by-day build up of the 39 annual load traces. In our interpretation, this could mean that a least squares match could result where the temperatures match most closely in the Southern states and not be a good match at all for Sydney or Brisbane. The Queensland load and prices would be expected to align with Sydney and Brisbane temperatures, but only be loosely correlated with Southern state capitals. This could result in unreasonably high or low loads (and hence prices) in the Queensland region, thus compromising the validity of the energy cost allowance.

To address this issue, we recommend that ACIL Tasman apply a weighting to the Sydney and Brisbane data in this matching process to emphasise the greater relevance of a temperature match for these cities.

Developing the 42 simulated NSLPs for Energex

ACIL Tasman outline the steps to develop the net system load profile (NSLP) traces by a process of classification, averaging and scaling.⁴ What is still not clear is if the actual Queensland load profile is properly correlated with the NSLPs developed by this method. If they are not correlated correctly then this would also throw into question the price-load correlation and any outputs produced from this data (including retail energy prices). ACIL Tasman does begin to address this point in their report by comparing annual load weighted spot price premiums for historical and forecast years,⁵ but fall short of stating what steps they have taken to ensure the correlation of the load profiles.

We request ACIL Tasman to explain their approach to retaining this correlation in their final report for the 2013/14 review.

2.3. Market-based energy costs

2.3.1. Spot price forecasts

The spot prices produced by ACIL Tasman show some trends that are strongly inconsistent with historic market outcomes. While demand has decreased in Queensland that is no reason to believe that spot prices will be considerably less volatile than they have been in other recent years. Regardless of the average demand level, generators will attempt to cover both their variable and fixed costs through their operational strategy. This means that even in years of low average demand, generators will operate to increase market volatility during opportune moments such as generator or transmission constraints and outages. We are deeply concerned that these spot price forecasts are unrepresentative of future market outcomes and do not reflect expected market volatility going forwards.

⁴ ACIL Tasman , Estimated energy costs for 12013-14 retail tariffs: for use by the QCA in its Draft Determination on retail electricity tariffs, Feb 2013, page 33

⁵ ACIL Tasman , Estimated energy costs for 2013-14 retail tariffs: for use by the QCA in its Draft Determination on retail electricity tariffs, Feb 2013, pages 18-19

A quick look at the ACIL Tasman half-hourly forecast pool prices over \$300/MWh show that there are very few high price events; only 14 half hours for the whole 2013/14 year (table 2).⁶ This data also shows that these most of these high price events are occurring relatively late on winter weeknights (around 8pm). This is inconsistent with actual demand outcomes as peak system demand, which most often drives up prices at the regional reference node, generally occurs at around 4-5pm in Queensland when commercial and industrial load is still relatively high.

Table 2 - ACIL Tasman hourly demand & Queensland pool prices for the 95th percentile simulation

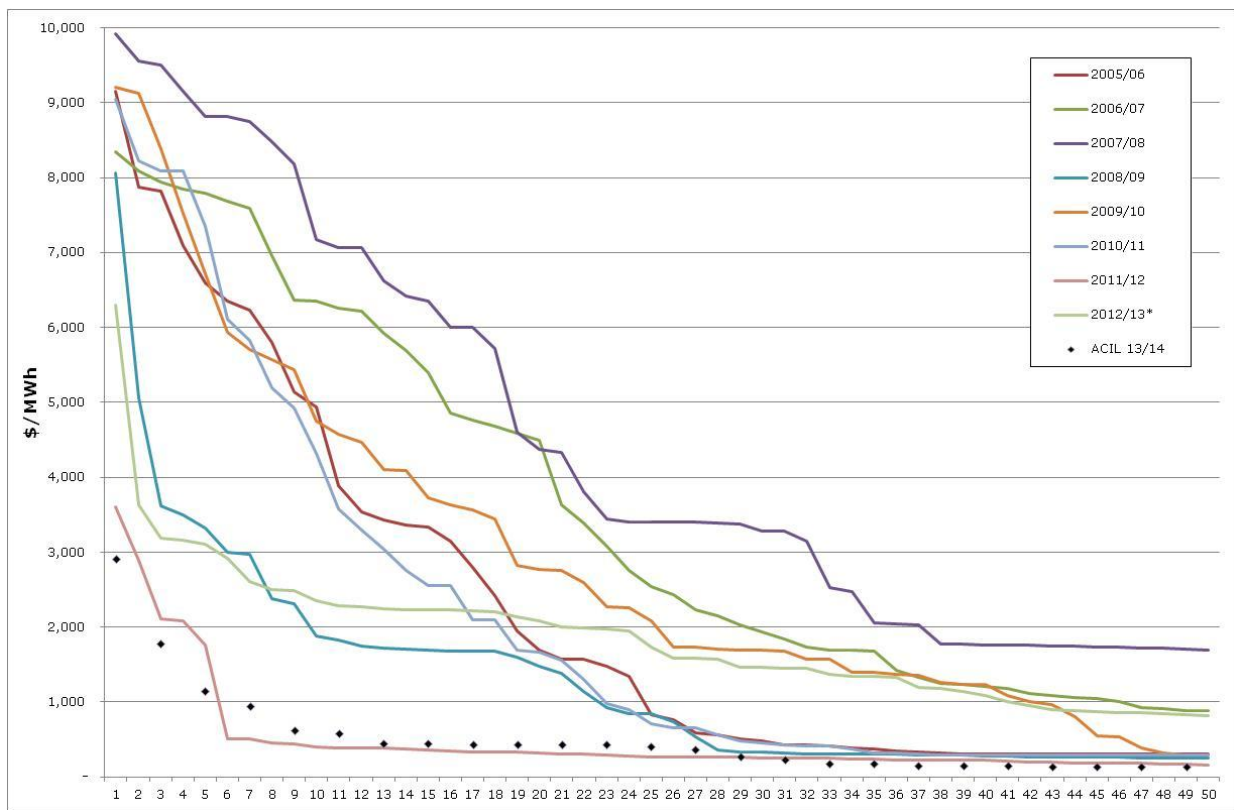
Date	Period	PowerMark Day type	Period type	Description	Energex NSLP hourly demand (MW)	Qld NEM pool price (\$/MWh, nominal at RRN)
16/07/2013	19	Working day	Peak		2,668	\$943.49
16/07/2013	20	Working day	Peak	7-9pm winter night	2,664	\$577.62
16/07/2013	21	Working day	Peak		2,480	\$2,912.05
20/07/2013	19	Working day	Peak	7pm winter night	2,104	\$436.12
22/07/2013	19	Working day	Peak	7-8pm winter night	2,414	\$440.76
22/07/2013	20	Working day	Peak		2,454	\$1,778.96
12/08/2013	20	Working day	Peak	8pm winter night	2,135	\$428.95
17/08/2013	20	Working day	Peak	8pm winter night	2,169	\$1,146.73
19/10/2013	16	Working day	Peak		1,537	\$436.17
19/10/2013	17	Working day	Peak	4-5pm spring afternoon	1,600	\$436.12
21/01/2014	18	Working day	Peak	6pm summer afternoon	1,853	\$364.27
26/06/2014	20	Working day	Peak		2,324	\$446.51
26/06/2014	21	Working day	Peak	8-9pm winter night	2,234	\$616.06
27/06/2014	9	Working day	Peak	9am winter morning	1,932	\$399.25

Another way of assessing spot prices is to use a price duration curve. We plotted Queensland spot prices from 2005/06 to the current financial year and overlaid the data produced by ACIL Tasman for the 2013/14 year (figure 3). The curve for the 2013/14 spot price forecasts is substantially lower than all but one of the previous eight years, and could arguably be described as having a probability of exceedence (POE) of 90%.

Contrary to this, we argue that this price determination should be based on a median (50% POE) year. A 50% POE forecast should in general sit around the middle of the historic outcomes shown below – this would be similar to the demands in the 2005/06 or 2010/11 years. From figure 3 below, it can be seen that this is clearly not the case with the present forecast. We would also expect to see over time, that curves in later years in figure 3 will show a general upward trend at the top end by virtue of the increasing market price cap, which will move to \$13,100/MWh in 2013/14.

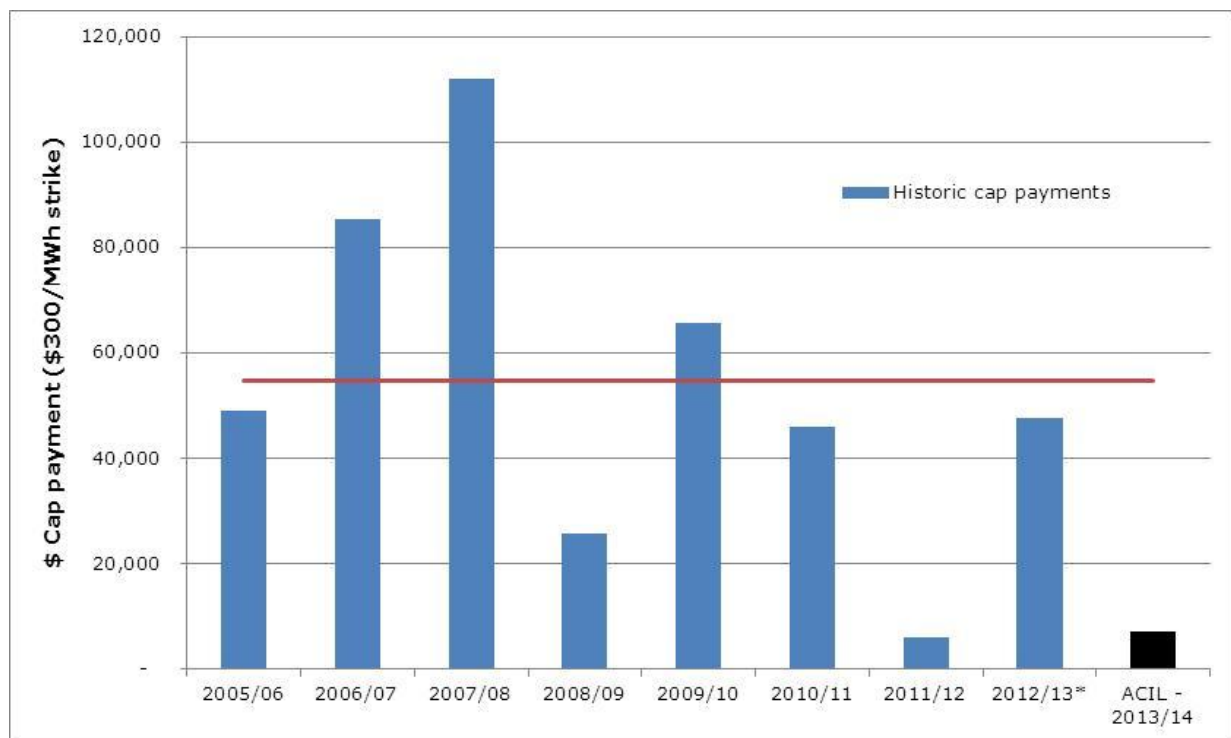
⁶ Data source: ACIL Tasman – 462 pricing scenarios and hourly settlement data: Energex NSLP

Figure 3 - Queensland price duration curves 05/06 to 13/14 forecast - top 50 half hours



Notes: data source – QLD regional reference prices, * not complete year, ACIL data shows top 25 hourly prices

We also looked at the total cap payment over a year, that is, the payments that would be made on a cap contract with a strike price of \$300/MWh. As can be seen from figure 4, ACIL Tasman are forecasting an annual cap payment, which is only 13% of the historic average level seen since 2005/06. Based on the analysis shown below, we argue that a true 50% POE price outcome would have a cap payment of at least \$45,000-\$50,000 per year. In contrast, ACIL Tasman’s forecast implies a cap payment of only around \$7,000, or around 15% of what might be expected.

Figure 4 - Annual cap payoffs by financial year compared to the historic average

Notes: data source – QLD regional reference prices, * not complete year

2.3.2. Modelling assumptions and outputs

In the limited time available, we have not carried out any comprehensive analysis of why spot prices are not producing the expected trends. However, we suggest that ACIL Tasman should consider the following assumptions in modelling spot prices for Queensland in 2013/14 if they haven't already done so:

- Ongoing disruptions at the Callide mine which supplies the Callide B & C generators and has been impacting their dispatch.
- The shutdown of two Tarong units until the end of 2014.
- Observed recent reduction in generation from Swanbank E and Darling Downs power stations and whether this is connected to higher than expected gas prices.
- AEMO's MT PASA⁷ for Qld is currently showing a large amount of plant unavailable during Q3 2013, which may lead to higher spot prices over that timeframe.

In using market price inputs, we observe that the forward curve will change as generator units are taken offline – this has the effect of increasing hedging costs. We'd like to see some analysis of, or adjustment for, these effects as a number of units have been shut down in Queensland and other states in the last year.

In addition, to be more satisfied with the ACIL Tasman's approach to estimating the energy prices we'd like ACIL Tasman to publish:

- the assumed contract levels for the CS Energy and Stanwell portfolios;

⁷ AEMO MT PASA –Australian Energy Market Operator, Medium Term Projected Assessment of System Adequacy

- assumptions around capacity factors for each plant type (as raised at the Brisbane public forum for this review (7th March));
- details of the modelled QNI energy flows and the amount of energy being exported out of Queensland for the last 6 months; and
- monthly Queensland average peak and off peak spot prices (for prices less than and more than \$300/MWh) forecasted using *PowerMark* compared to actual spot prices (to demonstrate that *PowerMark* produces reasonable *forecast* spot prices).

2.4. Enhancing time of use signals

The Authority has investigated the possibilities for enhancing the time of use signals in the retail component of the regulated time of use tariffs as required by the terms of reference.

Although we agree that amending the AEMO Metrology Procedures (to enable customers currently in the NSLP to be settled against their own load profile) is a matter for the Queensland Government to decide, we would like to see the Authority make a formal recommendation to the Government on this matter. Not only would a move to type 5 metering for small customers assist with better price signals to customers it could also benefit competition by allowing retailers to engage with customers on energy efficiency and cost saving initiatives.

3. Retail costs and margin

3.1. Retail operating costs (ROC) & customer acquisition and retention costs (CARC)

3.1.1. Estimation of the ROC and CARC

It is disappointing that the Authority is seeking to use the past ROC and CARC values used in 2012/13 (except for regulatory fees) and intends to scale them up by the consumer price index (CPI). This approach has less chance of resulting in an appropriate level for these allowances in the regulated tariff than would a more detailed bottom up approach to assessing and benchmarking these costs.

We would be prepared to contribute confidential data to the Authority if they wished to carry out this analysis; something that we suggest should be done at least every three years or so.

Interestingly, the Authority says that they don't want to rely on retailers confidential submissions as:

*'The process of obtaining information could be data intensive and data may be may be classified differently between retailers, making comparisons difficult. While the Authority could assess cost estimates using a high level benchmarking analysis, a potential problem would arise if there was a large discrepancy between the results of the benchmarking analysis and retailers' proposed costs or even between retailers themselves. This would likely require the Authority to choose one approach (or cost estimate) over the others and there may be little basis for doing so.'*⁸

However, the Authority appears happy to rely on this same type of analysis that other regulators (IPART in particular) have undertaken for a completely different jurisdiction (sometimes for a different time period).

Later in the section, the Authority states that we and AGL did not account for the differences in costs between jurisdictions to substantiate our arguments for a higher ROC allowance.⁹ From our point of view, we see no point in providing this data where:

- the Authority has taken a position against using confidential data which may differ between retailers (as discussed above); and
- it is difficult to see how isolated cost estimates for jurisdiction-specific costs for Queensland could be sensibly applied to a ROC value determined via a high level benchmarking approach of ROC values estimated by other state regulators.

With no specific and detailed analysis of Queensland ROC and CARC having been done for years, there is no certainty that the ROC and CARC allowances are close to the right values, nor that that they were set correctly in the first place. How is it possible that the Authority has taken the view that the CARC allowance is 'on the generous side'?¹⁰ What point of reference is there for Queensland ROC and CARC?

When a regulator goes about setting a regulated price in a high level manner without regard to the particular characteristics of the market, it signals to retailers that there is additional regulatory risk in the regulated price than there would be otherwise. Even if the regulator determines the right cost in one year, there is little confidence that this cost will continue to be correct. In all, the Authority's approach suggests to us that a quick and predictable outcome is more desirable than accuracy in setting a cost reflective regulated tariff.

⁸ QCA, Draft Determination, pages 37-38

⁹ QCA, Draft Determination, page 39

¹⁰ QCA, Draft Determination, page 40

3.1.2. The representative retailer for the purposes of calculating ROC

The Authority also disagreed with the proposals we and AGL put forward suggesting that ROC should be estimated on the basis of a smaller or new entrant retailer on the basis that this wouldn't be an efficient cost, and as they already allow for 'headroom' to sustain an appropriate level of competition.¹¹ The terms of reference, however, require the Authority to:

- have regard for the actual costs of making, producing or supplying the goods and services to customers – we suggest that the actual costs of smaller retailers are relevant to this as they make up part of the market too; and
- the effect of competition in the Queensland retail electricity market.

If the Authority takes this approach to all aspects of the regulated tariff then there will be little ability for smaller and newer retailers to compete. We believe we are already seeing this occurring (see discussion in section 4.1.1).

3.1.3. Inclusion of ROC for solar customers

We have reviewed the *Queensland Competition Authority Act (1997)* and the *Queensland Electricity Act 1994* and do not believe that the Authority are restricted in including the retail costs associated with servicing customers with solar panels installed at their premises.¹² As we've outlined in our last submission to this review, these costs have escalated alongside the number of customers who have taken up solar panels in the last few years.¹³

There are several reasons why we think it appropriate that the Authority should allow include solar customer service costs in the ROC allowance:

- The activities involved in servicing customers who sell their generation as opposed to receiving electricity supply are intimately linked with the activities related to supplying customers with electricity. For example, solar customer on feed-in tariffs cannot be on a feed-in tariff alone, they also must take supply of electricity. In addition, a customer with solar panels typically has only one meter and one retailer receives all data from that meter whether it is generation or usage data.
- Retail contract type has no bearing on the ability for customers to install solar panels and access a feed-in-tariff in Queensland. Regulated tariff customers are able to access solar feed-in tariffs, and so solar costs do not just arise from customers on market contracts.
- The solar-related services that retailers provide to customers do not relate only to the 'sale of electricity'. Solar panels also enable the customer to use the electricity they generate and contribute to sustainable energy generation.

Therefore, we ask the Authority to review their approach and include an amount in the ROC allowance to account for costs retailers incur in servicing solar customers.

¹¹ QCA, Draft Determination, page 38

¹² QCA, Draft Determination, page 41

¹³ EA, Response to Consultation paper on QCA Regulated Retail Tariff Review 2013-14: Cost Components and other issues, Jan 2013, page 19

3.1.4. Application of ROC to tariffs

We support the continued application of ROC to the fixed component of retail tariffs and provided our reasons for this in our last submission.¹⁴

3.2. Retail margin

As for the approach to the retail operating costs, we are also mystified as to why the Authority would dismiss the need to carry out a detailed analysis to determine an appropriate retail margin for Queensland regulated tariffs as being:

*'a highly subjective process to (a) comprehensively establish what [the] differences are [between jurisdictions]; and (b) quantify the impact of those differences on the retail margin.'*¹⁵

The Authority intend to base the Queensland retail margin in whole, or in part, on the retail margin that IPART have determined (or will determine) using the same method, but for NSW. To us, this appears to be more highly subjective than undertaking, in Queensland, a similar process to that used in NSW by IPART. To carry this out once every few years in Queensland should not be particularly onerous and would help to ensure that the regulated tariff is set at an appropriate level.

Although we disagree with the method used to set the margin, we do agree that the margin should be applied on an equal percentage basis to each component of the regulated tariffs. Our views on this were outlined earlier.¹⁶

¹⁴ EA, Response to Consultation paper on QCA Regulated Retail Tariff Review 2013-14:Cost Components and other issues, Jan 2013, page 20

¹⁵ QCA, Draft Determination , page 45

¹⁶ EA, Response to Consultation paper on QCA Regulated Retail Tariff Review 2013-14:Cost Components and other issues, Jan 2013, page 21

4. Competition and other issues

4.1. Competition

4.1.1. The state of competition in Queensland

On the measure of market switching, competition has certainly declined in the retail electricity market in Queensland over the past year (see the dashed trend line for the last 12 months in figure 5 below). Transitioning regulated tariff customers to cost reflective pricing will help to improve competition however, we acknowledge the challenge faced. Although the Authority takes some steps towards this aim in the Draft Determination, we don't believe that the transition approach alone will necessarily achieve a sustainable and healthy level of competition.

There is also strong evidence contained in Sapere report of retailer interviews for the Australian Energy Markets Commission review of competition for NSW that smaller retailers are withdrawing from the NSW retail energy market on the basis that the regulated tariff is set too low.¹⁷ Although this report focuses on NSW, comments collected also suggest that there is nervousness about competition and regulatory risk in Queensland as well.

In our view, the reason for the decline in competition over the last 12 months is that the tariffs continue not to be cost reflective and were set at too low a level for 2012/13. The Draft Determination does take some small positive steps towards improving cost reflectivity, but has also taken a backward step in allowing customers to access to transitional tariffs that were previously obsolete. We believe it would be possible to deregulate Queensland pricing soon for small customers and this would further optimise prices to a more efficient level than they are currently.

The Authority discusses the maximum discounts available from some retailers being as high as 11% off the total bill compared to the regulated residential price. This would indicate that there is some desire for those participants currently retailing in Queensland to compete, however it may only be to retain their existing customers and not to attract new customers. It is observable that some retailers will offer larger discounts to customers when they are seeking to switch retailers. This trend was recently evidenced in NSW in the reports done by AEMC consultants, Sapere and Roy Morgan, for the NSW Review of competition.¹⁸ We believe the same situation exists in Queensland.

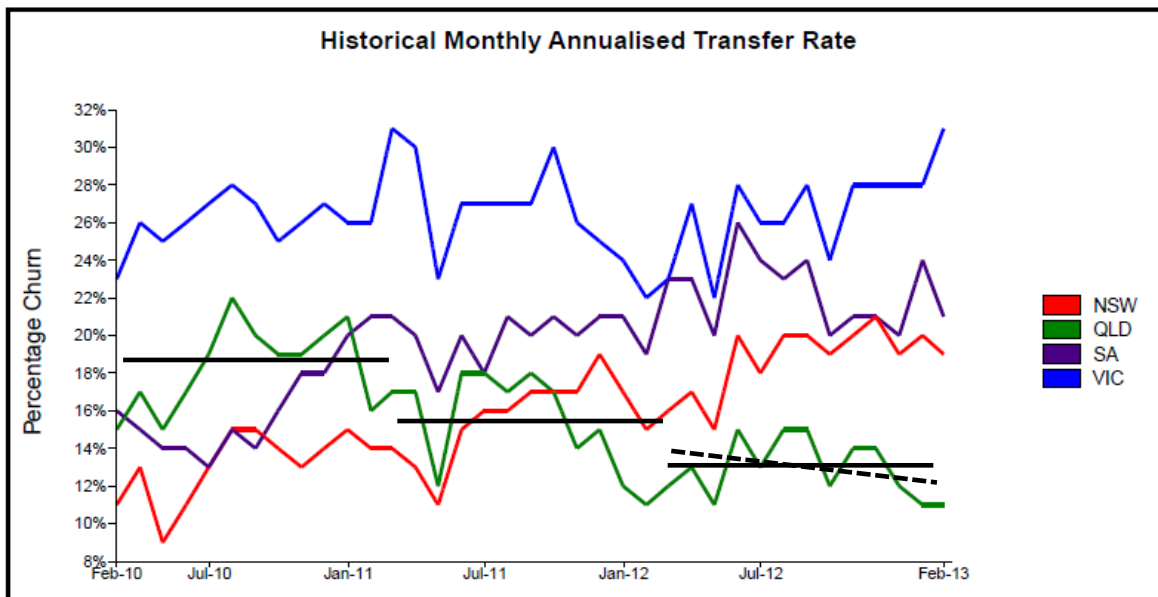
It is critical that the Authority have a strong focus on encouraging competition given the current environment. We don't believe the level of the regulated tariff in the Draft Determination for 2013/14 will do much to improve competition in Queensland. Also with high price increases for residential customers in particular, we expect that bad debt levels will continue to increase. This will also deter competition.

4.1.2. Assessment of competition levels

The Authority appears to be relying on misleading indicators when judging that competition is stable (if not improving) in Queensland. We have another month of switching data collated by AEMO (figure 5) which shows that Queensland competition has declined by an average of around 2-4% per year comparing the last three annual periods. That is, the average switching rate was 13% over the last 12 months compared to an average of 15% for Mar 11 – Feb 12 and 19% for Mar 10 – Feb 11 as shown by the solid black bars in figure 5.

¹⁷ Sapere, Review of Competition in the Retail Electricity and Natural Gas Markets in New South Wales [for AEMC]- Report of Interviews with Energy Retailers, February 2013, pages 11, 36-37

¹⁸ Sapere, as above, page 10. Roy Morgan, Retail Competition in the NSW Electricity and Natural Gas Markets: Focus Groups with Residential and Small Business Consumers, page 18

Figure 5 - Monthly annualised switching data for the NEM¹⁹

Note: The solid black lines show average transfer rate for each of the last 3 years, while the dashed line shows the linear trend line in the annualised transfer rate for the most recent 12 months.

There may be 15 retailers in Queensland as the Authority mentions, however, we question how 'active' these retailers are. In our last submission, we proposed a detailed method using AEMO data that the Authority could use to determine the level of switching activity attributable to each retailer.²⁰ Although this data is not publicly available, it does come from an independent source and the results could presumably be published at a higher level in a way that does not identify any particular retailer.

We do not understand the Authority's reluctance to rely on data that is not completely public when very good data is available from independent sources and is used by other state regulators in their pricing determinations. The fact that the data is not publicly available should not be an issue in this case. The assessment of competition does not lead directly to a numerical outcome that applies to prices and it is unlikely to be seen as controversial by stakeholders if it is clear a detailed analysis has been undertaken. We urge the Authority to take a more detailed look into the state of competition in Queensland and not to rely on high level data when better information exists.

4.2. Transitional tariffs

Whilst we would prefer that the Authority allow a one, or even two year, transition period for tariff 11, we have no issues with the transition method. It is disappointing that the tariff 11 freeze will continue to affect such a major group of customers for another two years as it has flow on impacts to other initiatives (such as the introduction of residential time of use pricing) and adversely affects competition.

Allowing access to obsolete tariffs delays the move to cost reflectivity by up to seven years. The Authority should aim to close off the transition tariffs in a shorter amount of time if possible – e.g. by taking larger transition steps in years where network tariff and other changes are small or

¹⁹ AEMO, Monthly retail transfer statistics, <http://aemo.com.au/Electricity/Data/Metering/Retail-Transfer-Statistical-Data>, February 2013

²⁰ EA, Response to Consultation paper on QCA Regulated Retail Tariff Review 2013-14: Cost Components and other issues, Jan 2013, page 22

negative. It is very unusual to make transitional tariffs open to new customers where they are based on previously obsolete tariffs.

Customers can be subjected to major swing changes in retail tariffs by virtue of tariff rebalancing by network companies trying to maximise their revenue. Trying to protect customers from these swings, whether they are a long term legacy issue or an ad hoc occurrence, is difficult for a regulator or a retailer to manage. These are separate issues that are best dealt with through approaches to distributors or the Australian Energy Regulator. To treat this transition issue in a detailed and long-term manner way when setting retail tariffs places undue costs and risk on retailers; we have no direct control over these matters.

4.3. The cost pass through mechanism

We are pleased that the Authority believes it could establish a cost pass through mechanism to allow the recovery of costs for prior years when setting tariffs for the next tariff year. Ideally, we would like to see this mechanism extend to the first and final years of the regulatory period as well. If this is not possible, we still contend that it an adjustment should be made to the retail margin to recognise the risk that retailers face in being unable to pass costs these on in tariffs.

4.3.1. The design of a cost pass through mechanism

There are some elements of the mechanism proposed by the Authority that we feel could be improved. In particular, we suggest modifying the clause that specifies what costs are eligible for pass through and removing the materiality clause:

Eligibility

The term 'unforeseen'²¹ could potentially be problematic in assessing eligibility. Many potential cost pass through events will not be completely unforeseen. For example, it's hardly a surprise that SRES costs are often significantly different in the latter half of the tariff year. Perhaps the wording around 'unforeseen' events should be replaced with a reference to 'uncontrollable' events. Often the issue is that the timing and magnitude of the change is uncertain or unknown, but the event itself can easily be unforeseen. This should not affect the eligibility for a cost pass through event.

Materiality

In terms of the materiality clauses specified by the Authority, we believe the primary issue is the commercial impact to retailers. When it comes to considering the impact to customers of a cost pass through amount, the assessment should be limited to how the costs are best applied to tariffs. That is, should the costs be applied as a fixed or variable amount, and should they apply to all tariffs or just a few.

However, the Authority outlines that one criterion they may apply to cost pass through reviews is:

*'(b) the impact of the cost pass-through amount (positive or negative) on regulated tariff retail electricity prices and average customer bills.'*²²

²¹ QCA, Draft Determination, page 62, point (a)

²² QCA, Draft Determination, page 64

This clause appears to imply that a cost pass through may not be allowed based on the **level** of price impact on customers. We suggest that it is not in fact necessary to consider the cost level impact on customers.

The reason is that the intention is to include the cost pass through amount in the tariffs for the next tariff year – that is, from the following July. If the cost pass through amount is small, then there should be no problems with allowing the pass through as there will be no additional costs incurred by retailers for implementing tariff changes as tariffs will be changing regardless. On the other hand, if the cost pass through amount is large, then there is a greater necessity for retailers to pass this through to customers to ensure that they are not financially penalised for events outside of their control. If retailers are penalised in this way then it will have a negative impact on competition.

Therefore, we believe that where the mechanism only allows a cost pass through amount to be included in tariffs at the time of an annual price change, no materiality clause is required. Although it may sound counterintuitive to not consider price level impacts to customers, we believe that the mechanism already takes account of these issues and that the materiality assessment should be removed entirely.

5. Network costs

5.1. The introduction of tariff 13

Energex's proposed new time of use 'peak smart' network tariff (7600) for residential customers will be available to customers who have a 'demand response ready' air conditioner installed. These air conditioners are remotely controllable by Energex to allow them to reduce individual customers' demand at time when the system demand is peaking. The new 7600 network tariff is aligned in structure and price to the existing 8900 network tariff, which is associated with regulated tariff 12 that was introduced last year. The only proposed difference between network tariffs 7600 and 8900 is that the off peak network prices is 2c/kWh lower in the off peak period (10pm to 7am every day) for the new 7600 'peak smart' network tariff.

While we understand the need for Energex to invest in demand reduction initiatives, we are concerned that every new niche tariff that Energex creates produces a new regulated retail tariff. The regulations in Queensland necessitate all retailers being able bill customers on regulated prices in particular circumstances. Therefore, for every new, small customer network tariff that Energex establishes there is a significant amount of downstream work created. This adds costs and adds to the hindrances to competition that already exist in Queensland (i.e. transitional tariffs, tariff 11 not being cost reflective, may soon be the only state that hasn't taken up the National Energy Customer Framework, etc.).

We think it unlikely that many customers will take up tariff 13 as:

- It won't be attractive compared to tariff 11 in 2013/14 - based on the proposed prices published in the Draft Determination.
- Very, very few customers have taken up tariff 12 (we heard at the public forum held by the Authority that the number of customers may now be in the double digits).
- Tariff 13 is barely more attractive than tariff 12 with the off peak rate being 2c/kWh cheaper. Customers do get an upfront flat incentive payment to install a 'demand response ready' air conditioner, but apart from this would probably not find additional benefit from moving onto tariff 13 compared to other available tariffs.

For 2013/14, we would like to see Energex leave network tariff 7600 closed to customers so that retailers are not in the position of having to deal with another new regulated tariff without seeing if tariff 12 will eventually become somewhat more popular.

We also don't see how it is in the interests of customers or retailers to create new regulated tariffs for each new network tariff put out by Energex. Is there any possibility for the Authority to review the need to create new regulated tariffs in these situations? From a practical level, tariff 12 would be an obvious fall back tariff if a retailer needed to make a regulated tariff available to one of these peak smart customers.

Although we acknowledge the need to address network constraints as is the objective of the 7600 network tariff, we believe that taking the steps outlined in this submission will stimulate competition and increase the likelihood of market based solutions being introduced to address network demand issues. A competitive approach will foster rather than inhibit retailer innovation.