stanwell

22 March 2013

Dr Malcolm Roberts
Chairperson
GPO Box 2257
Brisbane QLD 4001
Email: electricity@qca.org.au

Dear Dr Roberts,

Regulated Retail Electricity Prices 2013-14 – Draft Determination

Stanwell Corporation Limited (Stanwell) welcomes the opportunity to provide comments on the 2013-14 Regulated Retail Electricity Prices Draft Determination (the Draft Determination). Stanwell has been actively involved in the consultation process and as outlined in early submissions our key interest relates to the development of the energy costs components. We are largely supportive of the Queensland Competition Authority's (the Authority) proposal to use a market-based approach in the calculation of energy costs. We, however, have a number of specific concerns regarding its application in certain areas. Each of our specific issues is outlined below.

Inclusion of prudential costs

With respect to prudential costs, according to the Draft Determination, the Authority considered this issue in its 2012-13 Review in the context of retail operating costs and at that time considered that these were likely already accounted for in the operating cost estimate. However, following further consideration of the issue raised in submissions this year, the Authority is now of the view that these costs may not be included in the benchmarked retail operating costs and that it might be appropriate to account for these prudential costs in the context of estimating the cost of energy. Further, ACIL is of the view that retailers that hedge through futures will face higher prudential capital requirements than retailers that enter into Power Purchase Agreements (PPAs) or invest in generation. On this basis, ACIL has proposed to include an additional allowance of $0.631/MWh for prudential capital.

Stanwell acknowledges the points raised by stakeholders and the issues facing small and new entrant retailers, as these businesses are likely to have a higher proportion of market risk underpinned by financial derivatives. In practice, however, the additional allowance is applied across all retailers including the two large incumbents who do not necessarily face the same level of prudential costs due to their use of PPAs and or individual investments in generation. Given the high market share of the two incumbent retailers, this will largely result in a wealth transfer from customers to these businesses. We suggest the Authority reconsider its position on including an allowance for prudential costs or propose alterative options for addressing this issue.

Further, Stanwell is very supportive of the Authority's proposal not to increase the headroom and retailer operating cost components. We are concerned, however, that the inclusion of prudential costs could be viewed as an indirect increase in the headroom. In our earlier submission, we raised serious concerns that the level of competition, expected to be driven by setting the headroom at or above five percent, has not materialised. We consider any increase in the headroom, direct or indirect, is not in the long-term interests of electricity consumers.

Access to modelling results

In our first round submission, Stanwell raised the issue of ensuring that the modelling reflected actual market behaviour, which may not align with short-run marginal fuel cost (SRMC) bidding assumptions. This is particularly relevant in the case of gas-fired plant operated by vertically integrated retailers (which typically operate at below SRMC). While ACIL has outlined in its Draft Report, that its models are used extensively to generate results for a range of clients it is still important for stakeholders to verify these outcomes. This not only applies in the context of the current draft determination, but provides stakeholders with the confidence that the modelling approach produces reasonable outcomes if it is going to be used in subsequent pricing determinations.

We appreciate the Authority's efforts in raising our concerns with ACIL and that some modelling data has been made available. We are still concerned without access to a broader set of data, stakeholders are unable to undertake a full assessment of the results. Stanwell has requested high level modelling results (e.g. capacity factors, emissions intensity and interconnector flows) be released publically. We request that at a minimum the Authority reviews the data and advises stakeholders of its appropriateness. Greater transparency improves the overall integrity of the process. As outlined below, the information already provided has assisted in understanding the underlying distribution of price outcomes.

Use of 95th percentile for determining hedged prices

We note ACIL on request, has provided spot and hedge price results and based on our initial analysis the difference between the median and 95th percentile is relatively small. Based on the information supplied, the use of the 95th percentile is unlikely to have a material impact on overall energy costs inputs. This is not surprising given the relatively tight distribution of expected prices. It is, however, concerning that ACIL have not outlined a strong case for departing from the medium forecast. The only reasoning provided is that it is to account for the higher load risk in 2013-14 than in previous years. Why this period provides greater risk than previous (or future periods) is unclear. It is also important to recognise that in January, Powerlink provided a revised demand forecast which includes a lower energy and peak demand forecast for 2013-14 suggesting that the use of the 95th percentile to account for higher load risk is unwarranted.

While this difference may not be material in this instance, it could become relevant (if continued to be applied) if there is a greater spread of outcomes in the future. Further, without access to more detailed results on the operation of generation plant (i.e. bidding behaviour, capacity factors etc) it is difficult to make a full assessment of whether the difference is significant (e.g. different bidding behaviour may result in a similar median price but an increased level of volatility and a greater spread of outcomes.)

Treatment of Gas Electricity Certificates

On 8 March 2013, the Queensland Government announced that the Queensland Gas Scheme (the Scheme) will close on 31 December 2013. In terms of the impacts for this pricing determination, we note that total costs will fall as the 2014 targets no longer apply. It is, however, equally important that any market response (i.e. price change) following the announcement is also considered. Prior to the release of the Final Determination, Stanwell would appreciate the Authority outlining how it intends to address this issue.

We would welcome the opportunity to discuss a number of specific issues with you directly. Our contact on this specific matter is Ms Erin Bledsoe and she can be contacted on 07 3228 4529 or be e-mail at erin.bledsoe@stanwell.com.

[redacted]

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