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QCA Draft Report - Benchmark Retail Cost Index 2009/10

Thank you for the opportunity to comment upon the Authority's draft report for the *Benchmark Retail Cost Index 2009/10*.

CPRS

The 50% weighting of LRMC in the wholesale cost estimate will unacceptably delay the ability of retailers to pass through the full costs of an emissions trading scheme. This is confirmed by the Commonwealth Treasury's modeling on the impact of a CPRS which identified increases in electricity prices of 17-24 per cent directly related to the scheme, well above the 4-8 per cent increase identified in the CRA analysis. Full pass-through of emissions pricing is consistent with the policy intent of both the Federal Government's CPRS, and the Queensland Government's BRCI.

In the short to medium term, LRMC calculations will underestimate the impact of emissions pricing as it does not account for the rent captured by the marginal generator, which is capable of pricing based on the average carbon intensity of the market, higher than its own plant's intensity level. Whilst LRMC will converge over-time with wholesale contract prices (which will capture the additional costs of a CPRS) the delay in reaching that equilibrium will significantly impact the profitability of retailers, their market entry strategies, and the overall competitiveness of the market.

TRUenergy recommends that the marginal cost calculated in accordance with the current LRMC method is adjusted to reflect the forecast carbon intensity of the NEM for the regulatory period. Overtime, these intensity levels will converge, whereby eventually no correction will be necessary. In the meantime however, such an approach maintains the integrity of the Authority's current approach to estimating wholesale costs, whilst recognising the structural impact of emissions pricing, and the inability of the LRMC approach using technology specific carbon intensities to allow retailers to pass through the full cost of the scheme. It provides a transparent correction factor, the impact of which will diminish over-time, until it is no longer required.

Customer Acquisition Costs

TRUenergy has raised on a number of occasions that CRA's estimate of "*transfers to a market contract with the same retailer*" only measures internal transfers from a standard contract to a market contract, and not transfers from one market contract to

another market contract. CRA confirmed at the workshop that our understanding is correct.

The current calculation has a negative impact on the BRCI, as the number of internal standard-market transfers will decline over time, whilst the number of internal market-market transfers will increase over time. However, the Authority has not addressed this issue in the draft decision. As no jurisdiction collects data on the number of internal market-market transfers, we recommend that the measure is dropped from the calculation.

In addition, we have been concerned in the past with CRA's predictions of customer transfers for the forthcoming year, and the subsequent correction of that estimate in the base calculation for the following year. To avoid the need for any predictions and corrections, we recommend that the BRCI calculation uses the customer transfer rate for the preceding 12 month period as at the data cut-off date, with no subsequent corrections for the actual transfer rate. Although the resulting input will be a statistical lag, such an approach removes the need for any predictions, and avoids the impact of subsequent data corrections.

Regression vs step-change

TRUenergy does not support the Authority's draft decision to adopt the regression approach. As detailed in our previous submission, the 2009/10 estimated capital costs for all plant types were outside the 90% confidence limit of the regression analysis, with three of the four well outside the 95% confidence level.

If the Authority insists on the regression approach, TRUenergy recommends the time series is reduced from 15 years to 10 years as suggested in the report. This would at least go some way to mitigating the variation between the 2009/10 estimate and the regression estimate.

Headroom

The Authority claims that *"it has no objective or quantitative evidence that the level of headroom has been eroded."* That is incorrect. In their second draft report, in direct response to concerns that headroom had been eroded, CRA found that *"the decision to recalculate (costs from a previous year) decreased the theoretical retailer's headroom by around 2.4%."* The 2009/10 should be increased to account for this impact.

Please contact me on (03) 8628 1122 if you require additional information.

Yours sincerely,

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