

28 August 2009

Queensland Competition Authority  
GPO Box 2257  
Brisbane QLD 4001

[electricity@qca.org.au](mailto:electricity@qca.org.au)

Dear Sir/Madam,

**Re: Draft Report - Review of Electricity Pricing and Tariff Structures Stage 1**

The Energy Retailers Association of Australia (ERAA) welcomes the opportunity to comment on the Queensland Competition Authority's (QCA) draft report on the current review of the electricity pricing and tariff structures.

**Introduction**

The ERAA is an independent association representing retailers of electricity and gas across Australia. This includes both incumbent retailers and a number of second-tier providers. The vast majority of these retailers have significant experience in competitive energy markets across the NEM and are very familiar with the issues faced by regulators in determining appropriate pricing mechanisms within a dynamic environment.

The ERAA supports the QCA's conclusions that the Benchmark Retail Cost Index (BRCI) is flawed since it does not provide sufficient signals to customers regarding the costs of their electricity use, and it prevents the existing tariffs and prices from becoming cost reflective. The ERAA believes that the drop-off in retailer activity in the Queensland market since July 2008, and the subsequent decline in competition was due directly to the inability of the BRCI methodology to achieve cost-reflectivity.<sup>1</sup>

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<sup>1</sup> See Attached Chart on Queensland Small Monthly Transfer July 07 - June 09

The ERAA believes that the review of the BRCI represents a significant opportunity to revive competition in the Queensland market and ensure there is adequate flexibility for retailers to respond to the uncertainties which are likely to exist in the early years of the Carbon Pollution Reduction Scheme.

In reviewing this paper the ERAA has been very concerned by the particularly truncated time frame which stakeholders have been given to respond to such a comprehensive consultation. We recognise that this is not the QCA's making but nevertheless are unsure whether responses prepared in such a short time frame will adequately articulate all stakeholders' issues with the current methodology.

### **Retail Pricing Framework**

The ERAA has long held the view that price regulation is inefficient, stifles price and service competition and suppresses product innovation and in short, prevents the full benefits of competition from being realised. The ERAA however recognises this is not part of this review.

The Association strongly believes that competition represents the best form of consumer protection and thus sees the purpose of the pricing framework as being to encourage the entry or threat of entry of new firms into the Queensland market. The ERAA therefore advocates a competition orientated regulatory approach to setting regulated prices be adopted. While price regulation remains in the energy market, tariffs should be set at cost-reflective levels to promote competition by encouraging customers to transfer to market contracts, thus allowing for the phasing-out of price regulation at the end of the transition period.

The ERAA therefore considers that the way in which electricity prices are currently regulated act as the single biggest barrier in preventing an effective level of competition developing in the Queensland retail energy market. As can be seen in Queensland with the decline in retailer marketing activity since July 2008, the setting of regulated tariffs below cost has stifled competition and discouraged the entry retailers. The ERAA is also concerned that the current pricing framework is not providing the necessary signals for new investment in other parts of the electricity supply chain.

The ERAA therefore views the current BRCI as an ineffective regime and would encourage the QCA to establish a methodology whereby it sets the price to beat in the market, or a 'safety net'. Adopting such approach would provide retailers with a clear incentive to enter the Queensland market and make market offers which undercut the safety net, resulting in increased competition and better outcomes for consumers.

## **Carbon Pollution Reduction Scheme**

The CPRS, through the impact it will have on generator merit order, generator fuel costs and the likelihood of generator failure will create a market environment for retailers characterised by volatility and uncertainty. Moreover, the advent of an immature carbon market subject to volatility, which in turn increases wholesale market volatility, will significantly complicate the task of regulators in setting retail price caps. If the retail sector is to remain financially viable and competitive during this transitional period it will be of utmost importance that regulated price mechanisms are sufficiently flexible to enable retail prices to be adjusted quickly in line with costs incurred by retailers. The most appropriate response for Governments faced with such a situation would be to move to a framework whereby prices are not subject to regulation; the ERAA however recognises that this approach is again beyond the scope of this review.

As a result of the substantial volatility which is likely to exist in the early years of the CPRS, the ERAA believes that it will be critical for regulators to adopt a more flexible approach to price setting where price regulation continues. In order to provide retailers with the necessary flexibility it will be important that price determinations will be able to be 'reopened' to ensure retailers are able to cover their costs.

The ERAA also believes that the re-opening of a price determination due to a review of CPRS or other environment obligations should be driven by market events rather than some periodic review. While it is assumed that large retailers may be able to bear the increase costs associated with extreme price volatility and price increases in a post-carbon market, it is likely that smaller second tier retailers (and possibly some large retailers as well) may not be able to sustain such cost pressures. In order to ensure the viability of all retailers such reviews should be conducted where a retailer can proficiently demonstrate that such a review of the retail price determination is required.

## **Customers entitled to regulated tariffs**

The ERAA does not support the retention of regulated tariffs for any business customers, and in particular large customers consuming over 100 MW p.a. The regulated tariff was retained in Queensland as a transitional measure to protect customers while competition developed. Given that there has been a high degree of competition in the commercial and industrial part of the market for a number of years, the regulation of such tariffs is no longer required. The fact that there are so many large customers on regulated tariffs demonstrates that the regulated retail tariffs are lower than market based prices and must be abolished for such customers. The ERAA would propose that regulated tariffs for large customers be removed on 1 July 2010, and that a 12 month phase out period be provided for smaller business customers.

## **Network Costs**

The ERAA agrees with the QCA that use of the average increase in network costs for both the Energex and Ergon network in the BRCI is flawed. The ERAA supports the QCA's view that the objective of achieving cost reflectivity in South East Queensland is more critical to the development of competitive energy market than the distribution pricing signals that may be provided to customers on Ergon Energy's network. In order to encourage competition in the Queensland electricity market, the regulated tariff must be based on the supply of electricity to a customer in Energex network area. The Queensland uniform tariff policy should be based on the price of supplying electricity to a customer in South East Queensland and then adding on the Queensland Government's community service obligation for customers in the Ergon network area.

The ERAA also believes network charges must be passed directly through to the customers. Currently, the lack of alignment between the notified prices and network charges in terms of tariff structures creates serious difficulties when implementing this change.

The ERAA remains concerned that developing retail tariffs bottom up with an N+R approach will result in significant duplication of the existing set of notified prices due to multiple network tariffs which can be matched to a particular retail tariff.

In determining retail prices it is critical that the network costs are based on the AER's final decision, rather than the draft decision. The ERAA is concerned that as there is normally some variance between the draft and final decision, the implementation of the draft decision is likely to be incorrect.

## **Disclosure of Network Cost on Customers' Bills**

The Draft Report proposes that retailers disclose the customer's network costs as a separate line item on the bill to allow customers to identify the network component of their bill and improve the price signal. The ERAA recognises the QCA's intention of improving the transparency of network costs to Queensland customers, but is concerned that such a change will result in significant costs for retailers due to the modifications which will be needed to their billing systems. As such the ERAA believes that the costs associated with changing retailer billing systems to accommodate the disclosure of network costs on the bill will be material and will take some months to complete. Moreover, if implemented, Queensland will be the only retail market in which retailers will have to highlight such costs to customers which is clearly inconsistent with the principle of national energy market reform.

## **Customer Acquisition and Retention Costs (CARC)**

Finally, the ERAA is concerned that the draft report indicated that the pricing framework would not have regard for the costs associated with acquiring and retaining of customers. The ERAA believes such costs are fundamental to the retailing of electricity in the Queensland. The ERAA views that the exclusion of

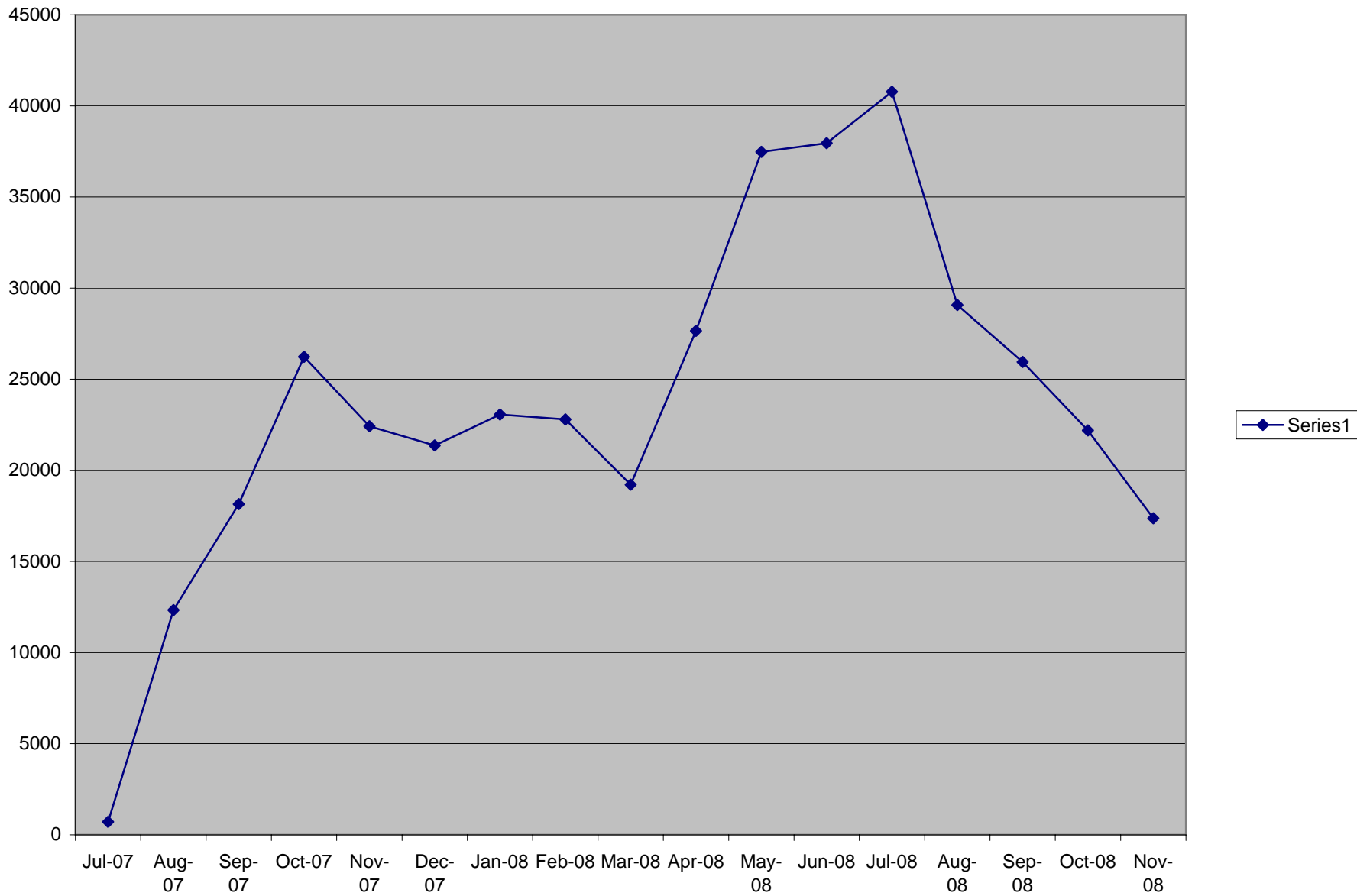
costs from the framework would act as a barrier to entry of retailers, thereby impeding the growth of competition in the market.

Should you have any questions in relation to this submission please feel free to contact me on (02) 9437-6180 to facilitate such discussions.

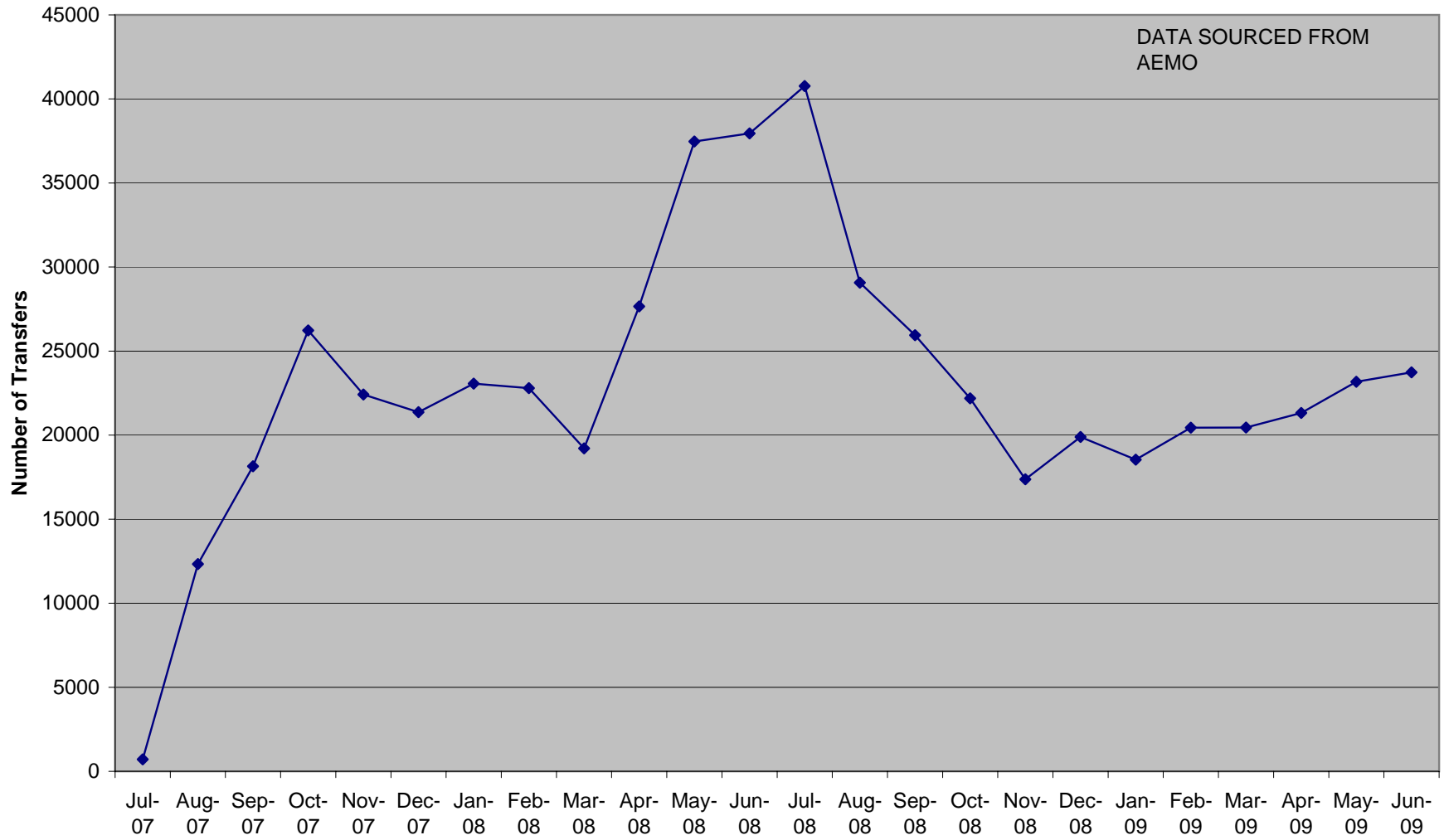
Yours sincerely



Cameron O'Reilly  
Executive Director  
**Energy Retailers Association of Australia**



Queensland Small Monthly Transfer July 07 - June 09



**Small Monthly Transfer Total**

	Aug-07	Sep-07	Oct-07	Nov-07	Dec-07	Jan-08	Feb-08	Mar-08
NSW								
VIC								
QLD								

44536  
32586  
29095  
24871  
19537  
22099

Apr-08	May-08	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08
				33624	29772	29601	24242	27313
				51484	50083	55230	48341	53514
				29096	25946	22192	17370	19891

Jul-07	711
Aug-07	12,330
Sep-07	18,148
Oct-07	26,230
Nov-07	22,421
Dec-07	21,368
Jan-08	23,064
Feb-08	22,796
Mar-08	19,214
Apr-08	27,660
May-08	37,473
Jun-08	37,949
Jul-08	40,772
Aug-08	29,069
Sep-08	25,946
Oct-08	22,192
Nov-08	17,370
Dec-08	19,891
Jan-09	18,543
Feb-09	20,446
Mar-09	20,453
Apr-09	21,316
May-09	23,172
Jun-09	23,737

Jan-09	Feb-09	Mar-09	Apr-09	May-09	Jun-09	Jul-09
26060	28453	31111	28925	33808	33127	36541
48858	57978	47433	57116	58001	58446	62187
18543	20446	20453	21316	23172	23737	26461