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

Thank you for the opportunity to comment upon the Authority's *Review of Electricity Pricing and Tariff Structures - Stage 1 Draft Report*.

Network charges

TRUenergy supports the recommendation for network charges to be treated as a cost pass-through for retailers. However, the proposal for network charges to be separately identified on a customer's bill would be prohibitively costly.

All jurisdictions which retain price regulation allow for the pass-through of network charges, but none of these jurisdictions require the separate identification of network charges. Contrary to the draft report, doing so would not provide any price signal to the customer, as behavior will always be in response to the total bundled price. The structure of any underlying cost component is irrelevant.

In addition, we are concerned by the comment in the executive summary that the N component would be based upon the AER's draft decision, and not the final decision. By definition, network price pass-through requires the pass-through of the final approved network prices; otherwise retailers remain exposed to network price risk. If the Authority has concerns with the timetable of incorporating final network prices into the adjusted retail prices, the release timing of retail prices should be pushed back to allow this to occur. It may require, for example, that new retail prices commence in mid July, rather than 1 July.

Customer acquisition costs

TRUenergy's main concern with the Authority's approach to setting the BRCI has been that, whenever presented with alternatives as to the level at which a cost component should be set, the option chosen has invariably been the one consistent with the lowest BRCI outcome. This approach has been a significant contributor to the decline of tariffs below cost-reflective levels, and was most evident in the 2008/09 final decision; the Authority, faced with a plausible BRCI range of 5.38% to 13.2% range, set the BRCI at 5.38%.

In this case, the Authority can choose to adopt either the views of a regulator which accepts customer acquisition costs as a legitimate cost component in setting regulated prices, i.e. IPART, or another regulator which does not, i.e. ICRC. Given the current state of the Queensland market, and the acknowledged lack of cost-reflectivity in retail prices, the Authority should be pursuing all reasonable opportunities to achieve cost reflectivity. This is not done by excluding a cost component that another regulator considers as being fair and reasonable.

In respect to the merits of the two alternatives, TRUenergy notes that the ACT retail market is the least competitive contestable jurisdiction in Australia, and that the non-inclusion of customer acquisition costs is a contributor to the lack of competitive activity. The rate at which customer acquisition costs are set, other things being equal, is self-reinforcing, whereby the lower the allowance, the fewer funds available to new entrant retailers to fund customer acquisition campaigns.

Three year price path

TRUenergy does not support setting a three year price path for the period commencing 1 July 2010. There is insufficient liquidity in the forward contract market, and too much uncertainty surrounding the design of the CPRS, to justify such an approach at this time. Given the uncertainty, there is no benefit to either retailers or consumers in doing so.

Annual review of costs

If a three year price path is adopted, it is essential that the underlying wholesale cost estimate is reviewed on a regular basis, and we support the six-monthly review proposal. However there should be sufficient flexibility in the arrangements for a review to be triggered at any time, in response to a significant market event. Such a view is also consistent with the Model 2 of the AEMC's report on the impact of climate change policy on price regulation, whereby the review of wholesale costs could be retailer-initiated.

Re-opening provisions should also reflect the asymmetrical risks of retail price regulation. If costs are overestimated, competition will ensure that any excess margins will be rapidly eroded by new entrant retailers responding to price signals in a national market. On the other hand, underestimating prices is unsustainable, potentially leading to retailer withdrawal (as has already occurred in Queensland) or failure, and the collapse of investment signals.

Furthermore, and given the current lack of cost-reflectivity in retail prices, a 10% re-opener for cost underestimates is too low. Over the course of a three year determination, two consecutive underestimates of 9.5% would not be grounds for a re-opener, but would impose a 19% revenue shortfall on retailers in the third year. Any underestimate of wholesale costs should be grounds for a re-opener.

Energy purchase cost estimate

TRUenergy supports a market-based approach to the setting of wholesale costs. However, the Authority appears to have misunderstood our recommendation that the market price allowance should not be allowed to fall below the long-run

marginal cost (LRMC). We were not suggesting, as claimed by the Authority, that "an LRMC may provide a useful indication of the floor for the derived market price."

The point is that market prices may, and periodically will, fall below LRMC levels, and that in those circumstances long-term forward contracting will diminish and generation investment decisions delayed unless the retail allowance is maintained at the LRMC level. Our recommendation for an LRMC floor in the wholesale cost allowance is consistent with the New South Wales Minister's Terms of Reference to IPART for their 2010-13 retail price review.

Business Customers

TRUenergy supports the Authority's consideration of whether business customers should have access to regulated tariffs. Electricity is an input cost, not an essential service, for business customers, and they should be required to negotiate electricity prices on the same basis as other input costs. However, the suggested three to five year time frame is excessive, and would be of little benefit other than to further delay the development of competition for that sector. A twelve month notification period, including a comprehensive education program, has proven sufficient in Victoria.

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

Yours sincerely,

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