

11 MAY 2012

DATE RECEIVED



Wednesday, 9 May 2012

Mr Brian Parmenter
 Chairman
 Queensland Competition Authority (QCA)
 Level 19
 12 Creek Street
 Brisbane QLD 4000

Dear Mr Parmenter,

Re: Queensland Competition Authority (QCA) review of regulated electricity prices 2012-13

I am writing to you as Chairman of the QCA to draw attention to some significant industry concerns that arise from the recent draft decision on regulated electricity prices in Queensland.

We are aware that the new Government led by Campbell Newman has decided to freeze the main domestic tariff, tariff 11, aside from passing on carbon costs and accept this outcome cannot be changed. Our comments relate to other regulated tariffs and the methodology adopted by the QCA generally.

As a matter of principle it is the view of the Energy Retailers Association of Australia (ERA) that electricity and gas prices must always reflect the costs face by retailers, which as you are aware, are overwhelmingly wholesale electricity costs and network charges. In the medium term we will be advocating that a regime of price monitoring and retail competition is the best way to set prices and provide consumers with protection and choice.

While acknowledging the reality of a freeze for tariff 11 in 2012-13, we remain very concerned about the QCA's draft determination released on 30 March, 2012 as it relates to all regulated tariffs in Queensland. In particular we believe the methodology used to set the wholesale electricity component of these tariffs, dramatically underestimates the costs retailers actually face, and therefore will squeeze out all "headroom" and effectively end competition in Queensland. It is a methodology modelled on the price setting process for the Australian Capital Territory (ACT) where competition has ceased to exist due to a lack of retail head room.

The draft decision pays no regard to the long term power purchase agreements that underpin the development of generation in Queensland, and which set the costs that retailers have to pay to hedge the Queensland mass market load, regardless of short-term movements in the market price.

In recommending this outcome we believe the QCA has failed to have due regard to its requirement under Section 90 (5) (a)(ii) of the Electricity Act to have regard to the impact of its determinations on competition in the retail electricity market.

We do recognise the QCA process and the terms of reference for its review were set by the previous Government and was something over which you could not have any control. That said, we now urge you to consult with the Government and give due consideration to the implications of the QCA draft



determination on competition in Queensland. This will impact the ability of consumers to access cheaper pricing as there will be no incentive for retailers to offer market contracts in Queensland. Customers will also be exposed to large price swings in the future, even as soon as next year.

Further, as would be aware, there will be a \$150 million plus budgetary impact of the determination on the Community Service Obligation (CSO) payments the Government must make to Ergon Energy. This arises from the increasing gap between the recommended QCA tariffs and the actual costs to supply Ergon customers.

ERAA fundamentally supports the use of LRMC as a floor in setting the wholesale energy cost allowance over the sole reliance on the QCA's Market Based approach. However to the extent the QCA/ACIL's Market Based approach is to be relied upon it contains a key deficiency regarding its approach to carbon costs. Fundamentally, the assessment of the market based cost of carbon is materially understated, reflecting a market intensity of 0.87 tCO2-e/MWh (at the QLD Regional Reference Node). As a matter of principle, retailers will be largely hedged (as per ACIL modelling), either with AFMA based pass-through products or physical generation assets - both of which are exposed to the actual cost of the Clean Energy legislation. The AFMA pass through clause in futures contracts allows for the cost of the contract to be uplifted by average intensity of the NEM, which in turn reflects the total permits/tax surrendered under the Clean Energy legislation; similarly a cost pass through from a generator will also reflect direct costs arising under the Clean Energy legislation. Generally, only a small portion of most retailers' exposure would remain to pool and therefore 0.87 is unlikely to reflect most retailers' costs.

I believe a number of my members have made representations to the Government and the QCA on these issues but I wanted you to understand these are matters of broad industry concern. I would be happy to facilitate discussions between the Government and a range of ERAA members active in Queensland to discuss how industry concerns may be addressed.

Retailers and the ERAA have made submissions to the QCA on its draft decision but we believe the outcomes of that draft decision go beyond just pricing outcomes and extend into the Government's policy of encouraging retail competition in Queensland and investment in new generation facilities in Queensland, threatening long term security of supply. That is why I am writing to yourself, the Minister for Energy and Water Supply and the Treasurer about this important matter. I urge you and the QCA to give the points I have made due consideration.

Yours faithfully,

Cameron O'Reilly
Chief Executive Officer