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Regulated Retail Electricity Prices (2015-16) – Interim Consultation Paper

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Queensland Competition Authority's (the Authority) Regulated Retail Electricity Prices (2015-16) Interim Consultation Paper.

The esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of 34 electricity and downstream natural gas businesses. These businesses own and operate some $120 billion in assets, employ more than 51,000 people and contribute $16.5 billion directly to the nation's Gross Domestic Product.

A key objective of retail price regulation should be to facilitate the development of competition and provide a transition to price deregulation. There is a range of challenges associated with achieving this in regional Queensland. Application of the state's Uniform Tariff Policy (UTP) directly impedes retail competition and limits the Authority's ability to set prices that are cost-reflective. But the 2015-16 pricing determination still provides an important opportunity to lay groundwork for a competitive retail market in regional Queensland. This can be achieved by transitioning regulated prices to more cost-reflective levels and improving price signals for regional Queensland consumers.

Transitioning electricity tariffs to cost-reflective levels (ideally through market deregulation), and implementing targeted assistance measures funded on budget, remains the most efficient means of delivering sustainable and competitive electricity supply in regional Queensland. Such an approach would ensure social welfare outcomes are met (i.e. those customers most in need of support receive it) and the inefficiencies associated with non-cost-reflective pricing are avoided.[1]

Where prices continue to be regulated, the Association believes the N (network) + R (retail) methodology remains appropriate for determining retail prices in regional Queensland. But as noted by the Authority, the removal of retail price controls in south east Queensland (SEQ) creates additional issues that must be considered, including: the basis/structure of network tariffs; rebalancing the main residential tariff

[1] For more detailed comments in relation to the UTP and associated community service obligation (CSO) payments, please see the Association's response to the Authority's *Retail Electricity Price Regulation in Regional Queensland Issues Paper* and *Industry Assistance in Queensland Issues Paper*.

(Tariff 11); and the appropriateness of headroom allowance. The esaa has provided comment on these key issues below.

Retail tariffs should be based on Ergon Energy's network costs and tariff structures

The UTP has delivered notified prices that are lower than the costs of supply for most regional customers. As a result, price signals are impeded and the ability of consumers to make rational decisions relating to energy consumption is diminished. Coupled with tariff structures that have historically been heavily biased toward high variable charges, this has implications for system utilisation and efficient investment in electricity supply infrastructure.

To address this issue, the Association considers the approach to price setting should be based on the costs of supplying electricity to regional Queensland rather than SEQ. This would involve setting retail tariffs in line with the lower of Ergon Energy's cost-reflective network charges initially and progressively transitioning all customers to fully cost-reflective levels over time. The key benefits to this approach are more efficient pricing outcomes and a sustained reduction in the Queensland Government's exposure to high and variable subsidy costs.

To the extent this approach cannot be achieved for residential and small business customer tariffs under the Ministerial Delegation, at a minimum, all tariff structures should be based on those in the Ergon Energy distribution area. The proposal to base the time-of-use tariffs (Tariff 12 and Tariff 22) on Ergon Energy's pricing structure is a positive step in this regard. But the limited uptake of time-of-use tariffs to date may mean this is not a meaningful change. This will be particularly evident if the change further exacerbates any apparent pricing disparity relative to Tariff 11.

Given retail prices will no longer be regulated in SEQ from 1 July 2015, incorporating Ergon Energy's network tariff structures would also help mitigate any customer concern around potential pricing disparities between the two markets. For example, the regulated price in regional Queensland could potentially be set at a lower rate than the standing offer in SEQ from 1 July 2015. This could adversely affect consumer perceptions of retail price deregulation in SEQ, despite the availability of discounted market offers.

Imbalances in the fixed/variable components of current tariff structures should continue to be addressed and Tariff 11 transitioned to cost-reflective levels

Where prices continue to be based on SEQ costs, it is essential to complete the rebalancing of the fixed and variable components of Tariff 11 to make it cost-reflective by 1 July 2015. While regulated prices in regional Queensland should ultimately be based on Ergon Energy's costs and tariff structures, this rebalancing will help address the inequity of current tariff structures. It will also provide consumers with more incentive to consider switching to a cost-reflective time-of-use tariff, which is a more efficient tariff for shaping energy consumption patterns.

Headroom allowance should be retained

Recognising the fact that retail competition in regional Queensland is currently limited, the esaa is not supportive of removing the headroom allowance for notified prices. The UTP subsidy has blown out significantly in recent years, with the cost estimated at $655 million for 2014-15 and further increases anticipated. Given prices are held so far below cost in regional Queensland, removing the headroom allowance and further adding to the subsidy would not be appropriate.

Removal of the headroom allowance also has the potential to artificially accentuate future price increases where prices are regulated. The Queensland Government is currently considering options to apply the state's UTP in a way that enables competition to flourish. If this occurs and retail prices continue to be regulated in regional Queensland, the headroom allowance would once again be highly applicable. But reintroducing the five per cent allowance on top of any other cost increases for a given period would unnecessarily exacerbate the extent of any overall price increase. This is despite the commensurate benefits stemming from more retail competition (e.g. discounted market offers).

Any questions about our submission should be addressed to Shaun Cole, by email to shaun.cole@esaa.com.au or by telephone on (03) 9205 3106.

Yours sincerely

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