27 February 2015

Dr Malcolm Roberts
Chairman
Queensland Competition Authority
GPO Box 2257
Brisbane 4001

Email: electricity@qca.org.au

Dear Dr Roberts

REGULATED RETAIL ELECTRICITY PRICES FOR 2015-16

Origin Energy (Origin) appreciates the opportunity to comment on the Queensland Competition Authority's (QCA) Draft Determination on Regulated Retail Electricity Prices for 2015-16.

The QCA's decision for 2015-16 will only apply in the Ergon Energy distribution network as a result of the introduction of market monitoring in south east Queensland (SEQ) from 1 July 2015. As a result, Origin considers the QCA approach for this determination is an important first step towards putting in place the necessary pricing reforms to support a transition to full retail competition in the Ergon network.

Pricing approaches

As part of its Delegation, the QCA is required to ensure that regional prices should, as much as practicable, aim to ensure that small customers outside of SEQ do not pay more than reasonable expectations of the prices that would be available to standing offer customers in SEQ.

Origin recognises that the Delegation requires the QCA to consider network charges for 2015-16 only. In making its decision, the QCA has elected to use Energex tariff structures as the basis for flat rate tariffs and Ergon Distribution tariff structures for time-of-use tariffs.

Origin encourages the QCA to place greater weighting on the implications of the recent changes to the National Electricity Rules, which requires network businesses to develop individual cost reflective tariffs. The approach the QCA adopts this year may influence the calculation of future notified prices and may give rise to transitional issues for Ergon customers due to the disconnect between the regulated retail price and Ergon's network tariffs. We would encourage the QCA to reconsider the merits of adopting Ergon tariff structures when setting the regulated retail electricity price for 2015-16

Energy costs

As part of our submission to the QCA's Discussion paper, we proposed a number of ways that the QCA could enhance its current hedging-based approach that would more accurately capture the wholesale market cost of supply. While we note the QCA has settled on its approach, we consider it prudent to summarise our concerns with the approach used in the Draft Decision.

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In our view, the QCA's hedging based method does not appropriately reflect the dynamic of the wholesale market with respect to the relationship between contract and pool prices. Under the QCA's approach, the portfolio cost is at its lowest under a scenario when pool prices are at their highest and the supply demand balance is at its tightest; conversely, portfolio costs are at their highest under a situation when pool prices and demand are at their lowest.

Our experience is that when the supply demand balance is tight, generators have more ability to price contracts at higher values to reflect the value of scarce capacity. Furthermore, we consider that historic practise demonstrates that when pool prices are high so too are contact prices.

As a result (and as detailed more fully in previous submissions), we maintain our view that it is unrealistic to assume retailers will consistently be able to profit from buying an insurance product and that the higher the pool price scenario, the lower the wholesale energy cost.

In our submission to the QCA's Discussion paper we also raised a number of concerns with the approach taken to generate load profiles. ACIL's presentation of modelled Energex demand simulations (Figure 4) shows that the current approach continues to under-represent load variability. The top 100 hourly demands in ACIL's upper and lower demand simulations sit within the boundary created by the actual demand traces for each of the last four years. We would expect that upper and lower demand simulations would sit outside recent historic demands as they are intended to represent extreme conditions. A tight range of demand distributions naturally leads to a more efficient 'model hedge position' in turn understating modelled energy costs.

Retail costs

Origin supports the QCA's decision to include an allowance of 5% for headroom on the basis that this margin is consistent with previous decisions and would:

- assist the transition towards cost reflectivity;
- be consistent with how large business customers are treated in regional Queensland; and
- lessen the subsidy paid by taxpayers.

In addition, we support the decision to maintain a mechanism to allow the pass through of differences between certain costs included in 2014–15 notified prices and actual costs. We also recognise that due to the regulatory framework, the QCA cannot commit to a pass-through mechanism beyond 2015-16

Origin supports the QCA's decision to complete the transition to a tariff 11 notified price that reflects the costs of supply in south east Queensland using the approach established in the 2013-14 determination.

However, we do not agree with the QCA's decision to continue to allow all business customers to have access to transitional tariffs. Notwithstanding that the QCA highlighted that it did not find that there had been a significant increase in customers accessing transitional tariffs, we remain of the view that, with the exception of those customers that have previously made investments in good faith, there is no justifiable reason for these tariffs to be extended to other customers who have not been exposed to the same level risk.

Closing

We understand that as with previous years the QCA will update its analysis before making a final determination and consider this an important process given the historic improvement in contract liquidity in this period and recent movements in contract market prices.

Origin would be pleased to discuss any matters raised within this response further with the QCA. Please contact Sean Greenup in the first instance on (07) 3867 0620.

Yours sincerely

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