QCOSS Energy Consumer Advocacy Project

QCOSS Submission to the QCA on Regulated Retail Electricity Prices 2013-14: Draft Determination

21 March 2013

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The Queensland Council of Social Service (QCOSS) is Queensland's peak representative body for the community services industry. QCOSS represents approximately 600 member organisations working across Queensland in a broad range of portfolios. We support organisations and work to address the causes of poverty and disadvantage. A key part of this role is our engagement with the State Government to secure the best outcomes for QCOSS members and support the needs of vulnerable Queenslanders.

QCOSS is funded by the Department of Energy and Water Supply and Department of Justice and the Attorney-General for an energy consumer advocacy project in Queensland. The purpose of this project is to advocate on behalf of Queensland consumers and particularly vulnerable and low income households in relation to energy and pricing. This work is supported by an advisory group involving other key consumer groups in Queensland.

QCOSS welcomes the opportunity to provide a submission to the Queensland Competition Authority's (QCA) Draft Determination on Regulated Retail Electricity Prices for 2013-14 and has engaged Etrog Consulting Pty Ltd to provide advice on behalf of QCOSS with a focus on the matters that impact on residential consumers in Queensland. The report from Etrog Consulting that follows was prepared in consultation with QCOSS and is submitted as the QCOSS response to the QCA Draft Determination.

This consultancy was funded by the Consumer Advocacy Panel (www.advocacypanel.com.au) as part of its grants process for consumer advocacy projects and research projects for the benefit of consumers of electricity and natural gas. The views expressed in this document do not necessarily reflect the views of the Consumer Advocacy Panel or the Australian Energy market Commission.

For further information, or to clarify any aspect of this submission, please contact Carly Allen, Team Leader Low Income Consumer Advocacy on 07 3004 6909 or email carlya@qcoss.org.au.

REPORT

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Regulated Retail Electricity Prices 2013-14: Draft Determination

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TABLE OF CONTENTS

EXECUTIVE SUMMARY 1

1. INTRODUCTION.. 4

1.1. DELEGATION FROM THE MINISTER 5

1.2. THE EFFECTS THAT CHANGES TO REGULATED RETAIL ELECTRICITY TARIFFS AND PRICES WILL HAVE ON QCOSS' CONSTITUENCY 6

1.3. STRUCTURE OF THIS REPORT 7

2. NETWORK COSTS 8

2.1. NETWORK TARIFFS FOR RESIDENTIAL CUSTOMERS 8

2.1.1. The allocation of fixed and variable charge components in network tariffs.................. 9

2.1.2. The allocation of costs between peak and off-peak components in network tariffs 9

2.2. THE AUTHORITY'S DRAFT DETERMINATION FOR NETWORK COSTS.................................. 10

2.3. ALIGNMENT OF RETAIL AND NETWORK TARIFFS.. 10

3. ENERGY COSTS.. 12

3.1. INTRODUCTION.. 12

3.2. WHOLESALE ENERGY COSTS.. 12

3.2.1. Judicial review 12

3.2.2. Potential approaches for 2013-14 to 2015-16 12

3.2.3. The market-based approach 13

3.3. OTHER ENERGY COSTS.. 16

3.3.1. Queensland Gas Scheme 16

3.3.2. Enhanced Renewable Energy Target scheme 17

3.3.3. NEM participation fees and ancillary services charges 21

3.3.4. Prudential capital.. 21

3.4. ENERGY LOSSES 23

4. RETAIL COSTS 24

4.1. RETAIL OPERATING COSTS.. 24

4.1.1. Approach to estimating retail operating costs.. 24

4.1.2. Implementing the benchmarking approach 24

4.1.3. Customer Acquisition and Retention Costs (CARC).. 25

4.1.4. Adjusting the benchmark retail operating costs allowances 28

4.2. RETAIL MARGIN 29

4.2.1. Approach to estimating the retail margin 29
4.2.2. Implementing the benchmarking approach 29

5. COMPETITION AND OTHER ISSUES 32

5.1. COMPETITION CONSIDERATIONS 32
5.1.1. The role of competitive activity to derive longer term benefits for consumers 32
5.1.2. The effects of allowing for headroom in regulated electricity prices 33
5.1.3. No explicit allowance for headroom has been included in any other jurisdiction 34
5.1.4. The role of the Authority in regard to competition in determining notified prices 35
5.1.5. Quantification of headroom allowance 38
5.2. ACCOUNTING FOR UNFORESEEN OR UNCERTAIN EVENTS 38

6. TRANSITIONAL ARRANGEMENTS 42

7. DRAFT DETERMINATION 45

FIGURES

Figure 1: Small-scale Technology Certificate (STC) prices 19

EXECUTIVE SUMMARY

This report has been prepared by Etrog Consulting Pty Ltd for Queensland Council of Social Service (QCOSS). It comments on the Draft Determination on regulated retail electricity prices to apply in Queensland from 1 July 2013 to 30 June 2014 which was published by the Queensland Competition Authority on 22 February 2013, inviting submissions from interested parties.

Our main concerns are in the following areas (section references in this report are given in brackets). On other matters, we would be concerned if the Authority were to depart in its Final Determination from its current positions in its Draft Determination.

Introduction

- The Authority must particularly take into account the impacts of price increases on struggling Queensland households and businesses when determining regulated retail electricity prices for 2013-14. (section 1.1)

- We urge the Queensland Government to ensure that its Delegations to the Authority fully reflect its instructions to the Authority, and that important matters should not be included only in the Minister's covering letters. (section 1.1)

- We urge the Authority and the Queensland Government to make available at the earliest opportunity sufficient data to enable modelling of the effects that changes to regulated retail electricity tariffs and prices will have on consumers, particularly disadvantaged and low income consumers, and also to release any modelling that they have already undertaken to support any policy decisions that have been made to date. (section 1.2)

Network costs

- The Authority should request and influence the network tariff proposals that Energex makes to the Australian Energy Regulator (AER) to provide the best outcomes for retail tariffs for small customers, to meet the objectives of stakeholders, including the Authority itself, Government, retailers, distributors and consumers. (section 2.1)

Energy costs

- The Authority should use a market-based approach rather than a cost-based approach to estimate the cost of purchasing wholesale energy. (section 3.2.2)

- The Authority should continue to base its market-based approach to estimating the cost of purchasing wholesale energy on data and information that is in the public domain, to maintain transparency in the setting of regulated retail prices. (section 3.2.3)

- We support the view that amending the Metrology Procedures is a matter for the Queensland Government to decide and initiate with the Australian Energy Market Operator (AEMO). This is something that the Government should explore further with AEMO in the coming year. The exploration should include cost-benefit analysis of various options for implementation. (section 3.2.3)

- In its Final Determination, the Authority should reduce the retail margin commensurate with its view that its revised modelling approach to wholesale energy costs takes into account the majority of risk faced by retailers. (section 3.2.3)

- The cost of the Queensland Gas Scheme should be based on 15% cover and an averaging of Gas Electricity Certificate (GEC) prices from AFMA. The length of time over which they are averaged should be the same as the length of time over which the purchasing of contracts occurs for hedging of wholesale energy costs, provided there have been a significant number of trades in that time period. (section 3.3.1)

- In estimating the cost of Small-scale Technology Certificates (STCs), the Authority should take into account the fact that an active market for STCs has developed outside the clearing house. The market price for STCs has been and continues to be well below the official $40 price. An efficient representative retailer should be expected to be taking advantage of that market and not paying $40 to purchase its STCs. (section 3.3.2)

- No explicit allowance for the costs of prudential capital should be included in the Final Determination of regulated retail prices in 2013-14. Instead this cost item should be given full consideration in the process of determining regulated retail prices for 2014-15. (section 3.3.4)

Retail costs

- New material in regard to the setting of retail operating costs from other regulators that was not available at the time of the Draft Determination should only be taken into consideration in the Final Determination of regulated retail prices in Queensland for 2013-14 if it is unambiguously applicable to the setting of retail regulated prices in Queensland. If there are any issues that arise, the material should be left for fuller consideration and consultation in the process for setting regulated retail prices for 2014-15. (section 4.1.2)

- No allowance should be made for customer acquisition and retention costs (CARC) in regulated retail electricity prices in Queensland. (section 4.1.3)

- If the Authority is to make an allowance for CARC, it should be at a much lower level than that allowed in the Final Determination for 2012-13. Any allowance should be reasonable rather than generous, and should take into account less costly channels being used to recruit new customers, as against the previous cost estimates which were based on the costs of acquiring new customers through door-knocking. (section 4.1.3)

- The gross retail margin of 5% of total costs that was allowed in the Benchmark Retail Cost Index (BRCI) calculations is realistic, and should not be any higher. Instead, it should be lower, because the retailers will be compensated based on efficient costs, rather than the BRCI mechanism that might have borne no relationship to their actual efficient costs and was not cost-reflective. Under the BRCI, retailers therefore faced higher risks than should be the case under the current framework for setting regulated retail prices. (section 4.2.2)

- In its Final Determination, the Authority should reduce the retail margin commensurate with its view that its revised modelling approach to wholesale energy costs takes into account the majority of risk faced by retailers. (section 4.2.2)

- New material in regard to the setting of retail margins from other regulators that was not available at the time of the Draft Determination should only be taken into consideration in the Final Determination of regulated retail prices in Queensland for 2013-14 if it is unambiguously applicable to the setting of retail regulated prices in Queensland. If there are any issues that arise, the material should be left for fuller consideration and consultation in the process for setting regulated retail prices for 2014-15. (section 4.2.2)

Competition and other issues

- The Authority should make no additional allowance for headroom in notified prices for 2013-14. (section 5.1.5)

- The gazetted prices should not be adjusted via a cost pass-through during the tariff year, or via a catch-up mechanism in a subsequent tariff year. One exception to the above may be if a change of Government policy requires the Authority to make changes to regulated pricing during the tariff year. In that case, we would expect the Government to provide the necessary Delegation to the Authority so that the Authority would have the capacity to implement the required changes. (section 5.2)

1. INTRODUCTION

This report has been prepared by Etrog Consulting Pty Ltd for Queensland Council of Social Service (QCOSS). It comments on the Draft Determination on regulated retail electricity prices to apply in Queensland from 1 July 2013 to 30 June 2014 which was published by the Queensland Competition Authority on 22 February 2013, inviting submissions from interested parties.

At the same time, the Authority also released a report written by ACIL Tasman on estimated wholesale energy costs for use by the Authority in setting regulated electricity retail prices for 2013-14, with supporting data from ACIL Tasman, and three customer factsheets.[1]

The Authority held Post-Draft Determination Workshops for stakeholders in various locations. We were pleased to attend the workshop held in Brisbane on Thursday 7 March 2013. We would like to thank the Authority for holding the workshop, which we found very informative and useful.[2]

The Authority has requested that submissions to the Draft Determination should be received by 22 March 2013. This report has been developed in consultation with QCOSS with the understanding that QCOSS is intending to submit this report to the Authority as its response to the Draft Determination.

We have developed this report taking into account all the materials referenced above, as well as discussion at the workshop that was held on 7 March 2013.

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1 The Authority's Draft Determination and the ACIL Tasman paper and other materials have been published on the Authority's website at www.qca.org.au/electricity-retail/NEP/DraftDetermination.php.

2 The slides from presentations made by the Authority and ACIL Tasman at the workshop that was held on 7 March 2013 have been published on the Authority's website www.qca.org.au/electricity-retail/NEP/PostDraftDeterminationWorkshops.php.

1.1. Delegation from the Minister

As stated in Chapter 1 of the Authority's Draft Determination, on 5 September 2012, the Minister for Energy and Water Supply (the Minister) provided the Authority with a Delegation under section 90AA(1) of the *Electricity Act 1994* requiring it to determine notified electricity prices[3] for a three-year period from 1 July 2013 to 30 June 2016. However, while the Delegation is for a three-year period, the Authority is still required to set notified prices on an annual basis, with the first determination to apply from 1 July 2013 to 30 June 2014 (the 2013-14 Determination). On 12 February 2013, the Authority received a revised Delegation which changed the date for release of its Draft Determination from 15 February 2013 to 22 February 2013, while all other content remained the same as the 5 September 2012 Delegation. The Minister's covering letters and Delegations were provided in Appendix A to the Draft Determination.

Section 1.1 of the Draft Determination outlines various relevant requirements that the *Electricity Act 1994* and the Delegation place on the Authority. However, it does not include the following relevant comment in the Minister's covering letter of 5 September 2012:

> *it is important that the QCA take into account the impacts of price increases on struggling Queensland households and businesses.*

The Authority must particularly take into account the impacts of price increases on struggling Queensland households and businesses when determining regulated retail electricity prices for 2013-14.

We discuss these impacts further in section 6 of this report in relation to transition arrangements involving re-balancing the fixed and variable charges in Tariff 11. Our comments there include the following:

- We support the implementation of transitional arrangements for any changes to tariff structures that will have a significant impact on some consumers' costs.
- The proposal to rebalance the fixed and variable components of Tariff 11 to cost-reflective pricing will have an adverse impact on the lowest consuming households. Many low-consuming households are vulnerable consumers who are least likely to be able to adapt to significant price increases. We support a staged approach to minimise the immediate bill shock for consumers.

3 Notified electricity prices are the regulated retail electricity prices that a retailer may charge its non-market customers, as defined under section 90 of the *Electricity Act 1994*

- A transition period is essential in order to assess the impact of the changes on different customer groups and for this information to influence improvements to government policy. In particular, the shift to greater cost reflectively will necessitate changes to government concessions to ensure they are adequate and well-targeted alongside the new tariff structure. Further, the transitional timeframe provides an opportunity for consumer education to be rolled out over time to assist consumers understand and adjust to the new pricing structures.
- We prefer a smooth transition to cost reflective pricing in order to minimise bill shock for consumers who may be adversely affected. The effect on consumers should be a key consideration when determining the form of transitioning.
- The Authority should undertake substantial analysis to provide an assessment to identify the expected impacts of tariff arrangements on a range of consumer groups with varying consumption patterns, including pensioners, large working families, low-income tenants and other vulnerable households. This analysis should take into the account the existing electricity concessions available in Queensland.
- Significant changes to tariff arrangements will necessitate changes to the existing energy concessions and support arrangements, to ensure they are well-targeted and equitable for Queensland consumers.

The Authority has accepted previously that it is reasonable for submissions such as this to include comments to the Queensland Government on matters that may be outside the Authority's scope. On that basis, we note that the Authority consistently appears to place weight on the Delegations that it receives from the Minister that it does not also apply to the Minister's covering letters. We understand that this has some basis in the fact that the legislation refers specifically to the Delegation rather than to its covering letter. We believe this is somewhat anomalous, and that important matters in the covering letter should be given weight by the Authority.

> We urge the Queensland Government to ensure that its Delegations to the Authority fully reflect its instructions to the Authority, and that important matters should not be included only in the Minister's covering letters.

1.2. THE EFFECTS THAT CHANGES TO REGULATED RETAIL ELECTRICITY TARIFFS AND PRICES WILL HAVE ON QCOSS' CONSTITUENCY

QCOSS represents the interests of residential consumers, with a particular focus on low income and other vulnerable consumers.

Some low income customers are supported by a range of concessions and other measures in line with the Queensland Government's social policy objectives. In the process of tariff reform, the existing measures may be adequate or may prove highly inadequate to be effective at assisting low income consumers in future. Major restructuring of the concessions framework may be required, and it is better that this is known sooner rather than later, so that appropriate changes can be made to the concessions framework before new regulated tariffs and prices are implemented. Financial counsellors and others who advise these consumers also need prior information on how any new tariffs will affect their clients, so that they can give them appropriate advice on their use of electricity, their budgeting, and any assistance that may be available to them.

We urge the Authority and the Queensland Government to make available at the earliest opportunity sufficient data to enable modelling of the effects that changes to regulated retail electricity tariffs and prices will have on consumers, particularly disadvantaged and low income consumers, and also to release any modelling that they have already undertaken to support any policy decisions that have been made to date.

1.3. STRUCTURE OF THIS REPORT

The remainder of this report comments on various matters in the Authority's Draft Determination, and largely follows the same structure as the Draft Determination.

- Section 2 covers network costs.
- Section 3 covers energy costs.
- Section 4 covers retail costs.
- Section 5 covers competition and other issues.
- Section 6 covers transitional arrangements.
- Section 7 covers the overall draft determination.

2. NETWORK COSTS

Chapter 2 of the Draft Determination sets out the Authority's proposal on how to incorporate network costs in regulated retail electricity prices for 2013-14 in Queensland. It is divided into the following sections:

- Section 2.1 covers network tariffs for residential customers;
- Section 2.2 covers network tariffs for small business and unmetered supplies;
- Section 2.3 covers network tariffs for large customers and street lighting;
- Section 2.4 sets out the Authority's draft determination for network costs; and
- Section 2.5 covers alignment of retail and network tariffs.

Our comments here cover only network tariffs for small customers, the Authority's draft determination for network costs, and alignment of retail and network tariffs.

2.1. NETWORK TARIFFS FOR RESIDENTIAL CUSTOMERS

The Authority has noted: "Typically, network costs account for around 50% of the final cost of electricity for small customers."[4]

The Delegation sets out: "QCA must use the Network (N) plus Retail (R) cost build-up methodology when working out the notified prices and making the price determination, where N (network cost) is treated as a pass-through and R (energy and retail cost) is determined by QCA."

We recognise that the setting of network tariffs is a matter for the Australian Energy Regulator (AER), and not for the Authority. Nonetheless, as shown above, the network tariff component is a significant part of the retail tariffs, and network costs are passed through directly into regulated retail tariffs.

> The Authority should request and influence the network tariff proposals that Energex makes to the Australian Energy Regulator (AER) to provide the best outcomes for retail tariffs for small customers, to meet the objectives of stakeholders, including the Authority itself, Government, retailers, distributors and consumers.

Two areas that may be of particular concern in network tariffs are as follows:

- The allocation of fixed and variable charge components in network tariffs; and

4 Draft Decision, page 6

- The allocation of costs between peak and off-peak components in network tariffs.

2.1.1. The allocation of fixed and variable charge components in network tariffs

As mentioned in section 1.2 above, QCOSS represents the interests of residential consumers, with a particular focus on low income and other vulnerable consumers. Many low income and vulnerable consumers are relatively small users of electricity, because they do not have the high-usage electrical equipment that more affluent households may have, such as swimming pool pumps and large air conditioning systems.

That is not to say that all low income households are low users of electricity. Indeed there are also low income householders who support large families, and there are those who are high users of electricity because of medical requirements or poor quality housing and inefficient appliances. People who are home during the day may also be using more electricity because they require cooling throughout the day, while others may be able to switch off cooling when they are out during the day and rely instead on the cooling systems provided by others, such as their employers. Customers with low income who have high consumption of electricity for reasons outside their control may be particularly in need of concessions in the form of a package of support outside any tariff mechanism.

Given different tariffs that in total are revenue neutral, i.e. they bring in the same revenue when applied across the customer base, tariffs which have higher fixed charges and lower variable charges have an adverse impact on lower usage consumers as compared with tariffs which have lower fixed charges and higher variable charges. Conversely, higher usage customers would benefit from tariffs with lower variable charges and higher fixed charges.

Higher fixed charges and lower variable charges also do not provide as much of a price signal to customers to avoid inefficient usage of electricity as compared to lower fixed charges and higher variable charges. In the latter case, the higher variable charges provide more incentives to reduce unnecessary usage of electricity and to use electricity more efficiently. This is unlike the first case where the higher fixed charges are not reduced no matter how efficiently the consumer uses their electricity.

2.1.2. The allocation of costs between peak and off-peak components in network tariffs

The differential between peak and off-peak needs to be significant if it is to give customers incentives to use electricity at off-peak times rather than at peak times, and thereby contribute to more efficient use of the electricity network and generation capacity and infrastructure. In particular, the Delegation states that “QCA must consider whether its approach to calculating time-of-use tariffs can strengthen or enhance the underlying network price signals and encourage customers to switch to time-of-use tariffs and reduce their energy consumption during peak times”.

We therefore support the statement that “the Authority encouraged Energex to review its network tariffs to ensure they are sending appropriate pricing signals to customers regarding the differential network costs associated with their time of use and are providing appropriate demand management signals to customers”.[5] We note that the Authority made this comment specifically in relation to small business tariffs. We believe that this comment should also apply to residential tariffs.

The Authority further stated in regard to a small business tariff: “A key concern expressed in submissions regarding this issue was the shrinking differential between peak and off-peak rates in Tariff 22 in 2012-13 or, more particularly, the increase in the available off-peak rate. However, even if it were inclined to do so, the Authority notes that differentials seen in Tariff 22 in 2011-12 (and prior years) could not be re-captured solely through time-of-use signals incorporated in the energy costs because they do not make up a large-enough component of the (total) tariff, as outlined in Table 3.1. For this reason, the bulk of any time-of-use signals in retail tariffs must come through the underlying network tariffs as they make up, by far, the largest component of the tariffs.”[6]

Though these comments were also made specifically in relation to small business tariffs, the importance of appropriate time-of-use signals coming through the underlying network tariffs applies to residential tariffs as well.

It is generally understood that peak usage is a significant cost driver for the electricity supply industry as a whole, as peak usage has to be met through investment in generation and network capacity. Less peaky load shapes are less costly to serve, and make more efficient use of the generation and network infrastructure. We are therefore concerned that when the allocation of costs between peak and off-peak components in network tariffs are passed through in retail tariffs, they should continue to provide appropriate incentives to customers to use electricity at off-peak times rather than at peak times. For residential customers, our concern relates to Tariffs 12 (time of use), 13 (PeakSmart), 31 (super economy controlled load) and 33 (economy controlled load).

2.2. The Authority’s draft determination for network costs

We support the Authority’s draft determination to base regulated retail tariffs for residential customers across Queensland in 2013-14 on Energex network tariffs and charges for residential customers.

2.3. Alignment of retail and network tariffs

Once Energex and Ergon Energy have proposed network tariffs to the AER, after they have taken into account stakeholder views, the approval of the tariffs is then a matter between the AER and the distributors.

5 Draft Determination, page 9

6 Draft Determination, page 26

The best option would be for the notified prices to reflect the actual network tariffs and prices after they have been approved by the AER. However, we understand that there is a timing issue whereby the AER may not have finalised its decision on tariff approval by the time the Authority needs to publish its Final Determination. If that is the case, then we concur with the view of the Authority that “the best option for setting 2013-14 prices would be to proceed as for last year and request Energex and Ergon Energy to supply the Authority with proposed network tariffs and prices when they are submitted to the AER in April and using these as the basis for notified prices to apply from 1 July”.[7]

7 Draft Determination, page 17

3. ENERGY COSTS

3.1. INTRODUCTION

Under the Delegation, the R component of each retail tariff is to include appropriate allowances for energy and retail costs.

3.2. WHOLESALE ENERGY COSTS

Wholesale energy costs relate to the costs incurred by a retailer in supplying electricity to cover the load of its customers. While this electricity is purchased from the National Electricity Market (NEM) (the spot market), there are a range of measures that a retailer can take in order to reduce its exposure to volatile prices in the spot market, including purchasing financial derivatives (futures, swaps, options etc.), entering longer-term power purchase agreements (PPAs) with generators, or investing in generation assets.[8]

3.2.1. Judicial review

Following release of the Authority's 2012-13 Final Pricing Determination, Origin Energy made an application for Judicial Review of aspects of the Authority's approach to estimating energy costs in that decision. On 19 December 2012, the Supreme Court dismissed Origin Energy's application.[9]

The reasons for the judgment have been published.[10] Our reading is that the judgment does not require changes to be made to the approach to be used in 2013-14.

3.2.2. Potential approaches for 2013-14 to 2015-16

We concur with the view of the Authority that it is more appropriate to use a market-based approach rather than to use a Long Run Marginal Cost (LRMC) based approach. This view is based on the reasons given by the Authority in its Draft Determination and in its previous papers and determinations on the subject. On that basis, we have chosen not to repeat the many arguments we have previously given in support of this view. Should the Authority consider a change to that view in its Final Determination, it should refer to our previous submissions on the subject, and to the Authority's own publications for reasons as to why its view should not be changed in this respect.

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8 Based on Draft Determination, page 19

9 Draft Determination, page 20

10 *Origin Energy Electricity Ltd & Anor v Queensland Competition Authority & Anor* [2012] QSC 414 (12/5527) Brisb Jackson J 19/12/2012, available at www.sclqld.org.au/qjudgment/2012/QSC/414

Our reading of the recent judgment to which we refer in section 3.2.1 above also supports the use of a market-based approach rather than to use a LRMC based approach.

The Authority should use a market-based approach rather than a cost-based approach to estimate the cost of purchasing wholesale energy.

3.2.3. The market-based approach

Including PPAs in the market-based approach

The Authority has stated: “An important attraction of the market-based approach the Authority has applied to date is the availability of necessary information in the public domain. This at least provides a reasonable degree of transparency … over the inputs to what is, of necessity, a complex and less transparent modelling process. Interweaving into that process, confidential information on PPAs or the costs of generation (not that the Authority could require generators (as opposed to retailers) to provide information) would only reduce the ability of all stakeholders to assess, understand and accept the modelling outcome.”[11]

The Authority should continue to base its market-based approach to estimating the cost of purchasing wholesale energy on data and information that is in the public domain, to maintain transparency in the setting of regulated retail prices.

Liquidity in the futures market

We welcome the view of the Authority and its consultant that the volume of futures trading is sufficient to provide robust and accurate forecasts for 2013-14.

Enhancing time of use signals

The Delegation states that “QCA must consider whether its approach to calculating time-of-use tariffs can strengthen or enhance the underlying network price signals and encourage customers to switch to time-of-use tariffs and reduce their energy consumption during peak times”. We have already discussed this in section 2.1.2 in regard to the allocation of costs between peak and off-peak components in network tariffs. Here we discuss the potential allocation of costs between peak and off-peak components in the energy cost component of retail tariffs.

11 Draft Determination, pages 23-24

The Draft Determination states: “At the outset of the 2012-13 Review, the Authority considered developing energy cost estimates that would include time-of-use signals to consumers. However, retailers pointed out that this did not reflect the way in which they are charged for electricity by AEMO, which is based on the relevant distributor’s NSLP.”[12]

In our response to the previous Consultation Paper on cost components and other issues, we supported the view that the correct way to model energy costs in the determination of regulated retail electricity prices is to match the way in which the electricity retailer settles for that energy. The Authority had suggested that allowing for time of use signals in wholesale energy costs requires smart meters.[13] We stated that we agreed that smart meters would allow for those signals. However, as an alternative to smart metering we proposed that the Authority should investigate what changes to the Metrology Procedure would be required to allow for time of use periods to be accounted for separately in wholesale settlement, and hence for differentiated wholesale energy costs in the determination of regulated retail electricity prices.

The Authority noted our proposal in its Draft Determination, stating: “In its submission, QCOSS suggested that an amendment to AEMO’s Metrology Procedures could allow customers who already have electronic meters (not accumulation meters) to be settled against their individual consumption and hence priced according to their time of use. QCOSS suggested that this change could be implemented ahead of any blanket roll-out of smart meters.”[14]

The Authority further stated: “Amending the Metrology Procedures is a matter for the Queensland Government to decide and initiate with AEMO, not something over which the Authority has any control. This may be something the Government could explore further with AEMO in the coming year. Regardless, any changes along these lines would take time and would not be possible to implement for inclusion in wholesale energy costs for 2013-14.”[15]

> We support the view that amending the Metrology Procedures is a matter for the Queensland Government to decide and initiate with the Australian Energy Market Operator (AEMO). This is something that the Government should explore further with AEMO in the coming year. The exploration should include cost-benefit analysis of various options for implementation.

[12] Draft Determination, page 26

[13] Consultation Paper, Table 3.1, page 15

[14] Draft Determination, page 26

[15] Draft Determination, page 26

We are pleased to see that the Authority is now acknowledging that allowing for time of use signals in wholesale energy costs does not necessarily require smart meters, and could be achieved through amendment of the Metrology Procedures.[16]

Using the 95th Percentile of Hedged Outcomes

The Authority stated in its previous Consultation Paper that ACIL Tasman was considering whether it should use the median of its 462 cost estimates (as it used for 2012-13), or whether a higher percentile might better reflect the volume risk faced by retailers in this period of high volume uncertainty.[17] ACIL Tasman also stated that the 95th percentile is suggested "in recognition that there are other uncertainties not specifically accounted for in the process and to minimise any residual market volume or price risk".[18]

In our response to that Consultation Paper, we stated that any change in the methodology would need to be explained and justified fully. We welcomed consideration of such a change if it would mean that the minimisation of risk in the portfolio would allow for reductions elsewhere, such as in the margin, where the return expected should now be lower because of the minimised risk.

The Authority acknowledged our input, and stated: "QCOSS suggested that ACIL should further justify this decision and that any reduction in risk due to using the 95th percentile should be accompanied by a corresponding reduction in the retail margin."[19]

The Authority has now reported that "ACIL has reaffirmed its view that using the 95th percentile of hedged outcomes is most appropriate for 2013-14 on the basis that it takes into account the majority of risk faced by retailers."[20]

We welcome this further reaffirmation by ACIL Tasman, but we are concerned that in its Draft Determination the Authority has not reflected elsewhere its view that its revised modelling approach using the 95th percentile of hedged outcomes takes into account the majority of risk faced by retailers. We propose that the Final Determination should take this into account in the retail margin, where the return expected should now be lower because of the minimised risk.

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16 Draft Determination, Table 3.1, page 27

17 Consultation Paper, page 14

18 ACIL Tasman preliminary report, page 16

19 Draft Determination, page 27

20 Draft Determination, page 27

> In its Final Determination, the Authority should reduce the retail margin commensurate with its view that its revised modelling approach to wholesale energy costs takes into account the majority of risk faced by retailers.

3.3. Other energy costs

In addition to wholesale energy costs, the Delegation requires that the Authority also consider other costs that a retailer might incur, including fees and charges imposed by AEMO, the efficient costs of meeting any obligations under environmental and energy efficiency schemes (including future State and Commonwealth schemes) and a mechanism to address any new compulsory scheme that imposes material costs on retailers.

Relevant additional energy costs are considered below, including:

- the Queensland Gas Scheme;
- the Small-scale Renewable Energy Scheme (SRES);
- the Large-scale Renewable Energy Target (LRET) Scheme; and
- NEM participation fees and ancillary services charges.[21]

3.3.1. Queensland Gas Scheme

ACIL Tasman previously stated: "The cost of the Queensland Gas Scheme will be based on 15% cover and an average of the Gas Electricity Certificate (GEC) prices over the past four years from AFMA."[22]

In our response to the previous Consultation Paper, we stated that we concurred that the cost of the Queensland Gas Scheme should be based on 15% cover and an averaging of Gas Electricity Certificate (GEC) prices from AFMA. We proposed that the length of time over which they are averaged should be the same as the length of time over which the purchasing of contracts occurs for hedging of wholesale energy costs. We saw no basis for an extended period for contracting for GECs as against wholesale energy.

We also stated that should the Authority consider a change in its Draft Determination to move away from using market prices to estimate the cost of GECs, it should refer to our previous submissions on the subject, and to the Authority's own publications for reasons as to why its view should not be changed in this respect.

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21 Draft Determination, pages 28-29

22 ACIL Tasman provisional report, page 16

The Authority has reported our comment and that of Stanwell, as follows:

"QCOSS supported estimating GEC costs using AFMA market data, arguing that this best reflected the actual costs faced by retailers. QCOSS also suggested that a shorter data series to be used, to coincide with the wholesale energy cost hedging period. Stanwell preferred the use of a shorter data series, suggesting a two-year data series be used. This was on the basis that:

- the GEC Scheme is under review, so participants are not entering into long term contracts;
- the GEC price has fallen dramatically in recent years; and
- new entrant retailers had purchased sufficient certificates from the market."[23]

ACIL Tasman has responded to our comments by stating: "ACIL Tasman continues to use a period of four years because there is no volume data available for GEC trades. ACIL Tasman understands from anecdotal evidence that trade volumes for GECs have fallen significantly in the past two years or so and therefore extending the period of time to estimate the costs of GECs is in our view appropriate."[24]

It appears that the Authority has accepted ACIL Tasman's position without further comment. We suggest that the Authority or its consultant should investigate volume data available for GEC trades. If there have been a significant number of trades in the past two years, then that time period of two years should be used as the time period over which GEC prices from AFMA are averaged.

The cost of the Queensland Gas Scheme should be based on 15% cover and an averaging of Gas Electricity Certificate (GEC) prices from AFMA. The length of time over which they are averaged should be the same as the length of time over which the purchasing of contracts occurs for hedging of wholesale energy costs, provided there have been a significant number of trades in that time period.

3.3.2. Enhanced Renewable Energy Target scheme

On 1 January 2011, the Renewable Energy Target scheme was split into two separate schemes – the Small-scale Renewable Energy Scheme (SRES) and the Large-scale Renewable Energy Target (LRET), collectively known as the Enhanced Renewable Energy Target.

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23 Draft Determination, pages 29-30

24 ACIL Tasman report, page 27

The Large-scale Renewable Energy Target (LRET)

The LRET sets annual targets for the amount of electricity that must be generated by large-scale renewable energy projects like wind farms. Retailers must purchase a set number of Large-scale Generation Certificates (LGCs), which is determined on the basis of achieving the annual target. The number of LGCs required to be surrendered by retailers to discharge their liability each year is determined by ORER's Renewable Power Percentage (RPP). Retailers are required to surrender STCs and LGCs to fulfil their ERET obligations. If a retailer fails to meet its obligations, it will incur a penalty.

We support the use of market-based data to estimate the costs of Large-scale Generation Certificates (LGCs). We agree with the Authority that a market-based approach is more likely to reflect the costs to retailers of complying with various environmental schemes and that it is superior to a Long Run Marginal Cost (LRMC) based approach for a range of reasons.

The Small-scale Renewable Energy Scheme (SRES)

The SRES covers small-scale technologies such as solar panels and solar hot water systems installed by households and small businesses. Retailers have an obligation to purchase Small-scale Technology Certificates (STCs) based on the expected rate of STC creation, which is determined by the Office of Renewable Energy Regulator's (ORER) Small-scale Technology Percentage (STP).

We concur with estimating SRES compliance requirements using the binding 2013 STP target for the first half of the pricing period and the non-binding 2014 target for the second half of the pricing period. This is consistent with how compliance costs were estimated for 2012-13.

Should the Authority consider a change in its Final Determination to move away from using the binding 2013 STP target for the first half of the pricing period and the non-binding 2014 target for the second half of the pricing period, it should refer to our previous submissions on the subject, and to the Authority's own publications for reasons as to why its view should not be changed in this respect.

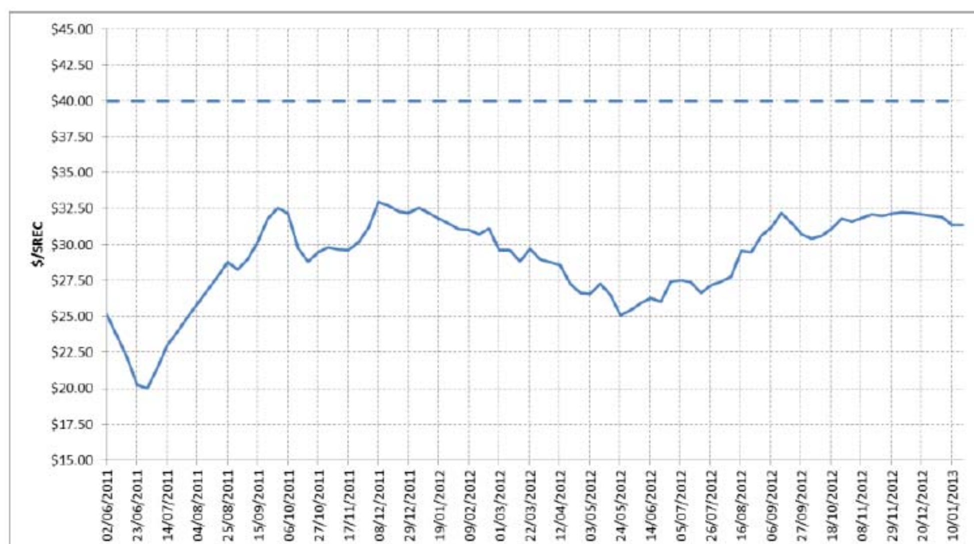
As previously, we remain concerned that in its Draft Determination the Authority continues to rely on the ORER's Clearing House price of $40 to estimate the costs to an efficient representative retailer of purchasing its STCs for 2013-14. This is notwithstanding the facts that:

- The Authority and ACIL Tasman have previously both acknowledged that STCs are being purchased based on market prices that are readily available, and continue to acknowledge that there is an active market for STCs outside the Clearing House.

- ACIL Tasman has stated that the secondary market STC price has been between $25 and $33 over the last two months.[25]

- STC prices are illustrated in Figure 1 below which we ACIL Tasman sourced from AFMA and which we have copied from the ACIL Tasman report.[26]

Figure 1: Small-scale Technology Certificate (STC) prices



Data source: AFMA

- We acknowledge that future market prices may not be the same as historic prices. As ACIL Tasman suggests, prices could be $40 in future. Equally they might continue to be a lot lower. We see no reason why the Clearing House price should be the best indicator of future market prices, and we commend market prices as the best indicator, as for other commodities which are market traded.

- The Independent Competition and Regulatory Commission (ICRC) of the ACT has used market prices for STCs in its Final Determination of regulated retail prices for 2012-14.[27]

25 ACIL Tasman report, page 47

26 ACIL Tasman report, page 48

27 *Retail prices for franchise electricity customers 2012-14*, Final report, Report 4 of 2012, June 2012, ICRC, pages 13-15, available at www.icrc.act.gov.au/energy/electricity. We note particularly that ICRC's Final Determination took this view, and not just the ICRC' Draft Report to which the Authority refers in its Draft Determination, page 32.

- The Climate Change Authority has stated that: “To provide clarity to scheme participants, the Authority recommends that the clearing house be amended to a ‘deficit sales facility’, whereby certificates are only allowed to be entered in the clearing house when the clearing house is in deficit (that is, only when regulator-created certificates have been issued to liable entities). This would allow the continued operation of the clearing house as a price cap, while making it clear that it is unable to guarantee a set price of $40 per certificate in a timely fashion. Such a change would also allow the clearing house price to be more easily amended as there would be no need for transitional arrangements for certificates on the transfer list.”[28]

- That same report from the Climate Change Authority also reveals that: “While the clearing house has provided an effective price cap, it has failed to deliver a set subsidy of $40 per STC to owners of small-scale systems (or their agents). The clearing house is a voluntary mechanism and liable entities have chosen to acquire certificates outside the clearing house where STC spot prices are around $25 to $32. This has meant the clearing house transfer list has not cleared for 18 months (the last sale was on 25 February 2011).”

- The Climate Change Authority report refers to the fact that “the existence of the clearing house has created an expectation among some non-expert participants that a $40 set price per STC is obtainable”. It is clear from this that only “non-expert participants” expect STCs to trade at $40; the Authority and its consultant should not be in this category.

- This all further undermines the relevance of $40 as the price at which STCs trade.

In this submission, and in our previous submission on the Consultation Paper, we have responded to all of the concerns raised by the Authority and ACIL Tasman in regard to using market prices for STCs. We have shown that there is a liquid market, and that prices are readily available. We propose that market prices are the best indicator of prices, as for other commodities which are market traded, rather than the clearing house, where it has been reported by the Climate Change Authority that the last sale was on 25 February 2011. As stated by ICRC: “there is a robust case for the use of market data to estimate the costs of STCs”. We commend this approach to the Authority.

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28 See *Renewable Energy Target Review*, Climate Change Authority, Final Report, December 2012, available at www.climatechangeauthority.gov.au/ret. We note particularly that this was the Climate Change Authority’s final recommendation, and not just its draft recommendation as reported by the Authority in its Draft Determination, page 32.

In estimating the cost of Small-scale Technology Certificates (STCs), the Authority should take into account the fact that an active market for STCs has developed outside the clearing house. The market price for STCs has been and continues to be well below the official $40 price. An efficient representative retailer should be expected to be taking advantage of that market and not paying $40 to purchase its STCs.

3.3.3. NEM participation fees and ancillary services charges

Given that changes in NEM participation fees and ancillary services charges are relatively stable from year to year, we agree with the Authority that it is reasonable to use historical data in forecasting these costs.[29]

3.3.4. Prudential capital

The Authority has included an explicit allowance for prudential capital for the first time.[30] Its proposal seems to lack some detail and rigour, as follows:

- The Authority states that "following further consideration of the issue raised in submissions this year, the Authority is now of the view that these costs may not be included in the benchmarked retail operating costs and that it might be appropriate to account for these prudential costs in the context of estimating the cost of energy". We agree there may be a case for separate itemisation of costs of prudential capital in setting regulated retail prices, but the case is far from proven by the Authority. We believe that before these costs are separately itemised, there should be stronger case that that they "*may* not be included" already and that "it *might* be appropriate to account for these prudential costs" separately.

- There is no reported analysis of how other regulators treat such costs.

- ACIL Tasman's calculations for AEMO prudentials seem very rough. While there may be justifications for these costs, the case is not made, and the following would seem to require at least explanation if not revision:[31]

    - ACIL Tasman seems to use a 95th percentile future pool price estimate for "average future price". This does not seem right.

    - ACIL Tasman takes a volatility factor of 1.5 and a bank charge of 2.5% as proposed by QEnergy without any apparent validation.

29 Draft Determination, page 33

30 Draft Determination, page 34

31 ACIL Tasman report, pages 50-51

- It is unclear what the “Loss factor of 1.5” represents. Multiplication by a factor of 1.5 seems to indicate losses of 50%, but that is not clear.

- The multiplication, division and multiplication of 42 is unclear.

- There appears to be a mistake in ACIL Tasman’s formula of 2.5%/(42/365) which we think is intended to read 2.5%*(42/365).

- QEnergy’s submission to the Consultation Paper stated: “For most retailers, accessing bank guarantees to cover their entire load with AEMO … is both prohibitively expensive and prohibitively leveraging.”[32] If that is the case (and ACIL Tasman does not appear to address fully whether it is or not), it is unclear why ACIL Tasman appears to be modelling that scenario.

- QEnergy stated further: “For a non-vertically integrated incumbent retailer of the type identified as the model retailer within the Authority’s 2012-13 Determination, most of the prudential capital required by AEMO is managed through the acquisition of either reallocation hedges, or straight hedges with separately purchased reallocation credits available through a traded market. Under a reallocation hedge – or through a reallocation certificate – the guarantee requirement is passed to another party, say a generator.” QEnergy added that “most retailers either hedge their full load using straight hedge cover with reallocation credits purchased against all of it, or use reallocation hedges of the type dismissed by ACIL”. While we are not advocating accepting everything QEnergy says without evaluation of its merit, we believe some further attention should be paid to these arguments by the Authority in devising appropriate modelling of prudential costs.

• In ACIL Tasman’s calculations for hedge prudentials, there are various unsourced assumptions, including the price scanning range (PSR), the intra commodity spread charge, and the spot isolation rate, the return on cash lodged with the clearing house, and rounding of $9500 to $10,000 “in order to allow for some ongoing future uncertainty”. None of this fits with the transparency that was discussed and lauded in section 3.2.3 of the Authority’s Draft Determination, and which we commended in our section 3.2.3 above.

32 QEnergy submission, pages 5-6

In summary, we believe that there is more justification required at minimum, and potentially correction of arithmetic errors and assumptions. At this late stage, it seems that the Authority will not have an opportunity to provide a robust set of justifications and calculations before the Final Determination is published. That will not meet the Authority's requirement under the Minister's covering letter to the September Delegation "to undertake a rigorous consultation process with all relevant parties" and to undertake "a strong consultation process" on this key issue. Given this, we propose that further consideration of the inclusion of an explicit allowance for prudential capital in regulated retail prices should be left till 2014-15. In the process of setting regulated retail prices for 2014-15, the inclusion of an explicit allowance for prudential capital should be considered, focusing on whether these costs are already included in benchmarked retail costs, the views of other regulators, robust and justified assumptions, and accurate calculations and formulae.

No explicit allowance for the costs of prudential capital should be included in the Final Determination of regulated retail prices in 2013-14. Instead this cost item should be given full consideration in the process of determining regulated retail prices for 2014-15.

3.4. ENERGY LOSSES

A retailer must purchase sufficient energy to supply its customers and allow for the distribution losses that will be incurred, and the transmission losses from the reference node.

We agree that the Authority should apply transmission and distribution losses published by AEMO to all energy cost components. We note that all loss factors will be updated for the Final Determination using the latest available information, which will include the 2013-14 loss factors, which are to be published by 1 April 2013.[33]

33 Draft Determination, page 35

4. RETAIL COSTS

The Delegation requires that the Authority must use the Network (N) + Retail (R) cost build-up methodology when working out notified prices. Chapter 4 of the Draft Determination discusses retail costs and sets out the Draft Determination on an appropriate allowance for retail operating costs and an appropriate retail margin.

4.1. RETAIL OPERATING COSTS

Retail operating costs relate to the costs of the services provided by an electricity retailer to its customers and typically include customer administration (including call centres), corporate overheads, billing and revenue collection, IT systems, and regulatory compliance.

In the past, the Authority has also considered retail operating costs to include customer acquisition and retention costs (CARC), which include costs associated with marketing, advertising and sales overheads.

4.1.1. Approach to estimating retail operating costs

There are two generally accepted approaches to estimating retail operating costs:

- A bottom-up approach, which requires detailed information on each cost component; and
- A benchmarking approach, which relies on publicly available information and is therefore less data intensive.

The two approaches can also be used together, with benchmarking used to assess the reasonableness of costs estimated under a bottom-up approach. Regulators in other jurisdictions tend to use a combination of a bottom-up analysis and benchmarking.[34]

We support the use of benchmarking to determining the retail operating cost allowances, subject to the following issues. Besides the arguments set out in the Draft Determination,[35] there is now not sufficient time available for the Authority to consult on a bottom-up approach for the estimation of retail operating costs for 2013-14.

4.1.2. Implementing the benchmarking approach

We support the Authority's Draft Determination that the estimation of retail operating costs should be based on the costs of large retailers that are likely to have achieved economies of scale, consistent with the Authority's representative retailer definition.

34 Draft Determination, page 37

35 Draft Determination, pages 37-38

The Authority is intending to take any new material presented by IPART in regard to retail operating costs into consideration in making its Final Determination.[36] We are concerned that new material in regard to the setting of retail operating costs from other regulators that was not available at the time of the Draft Determination should only be taken into consideration in the Final Determination of regulated retail prices in Queensland for 2013-14 if it is unambiguously applicable to the setting of retail regulated prices in Queensland. If there are any issues that arise, the material should be left for fuller consideration and consultation in the process for setting regulated retail prices for 2014-15.

New material in regard to the setting of retail operating costs from other regulators that was not available at the time of the Draft Determination should only be taken into consideration in the Final Determination of regulated retail prices in Queensland for 2013-14 if it is unambiguously applicable to the setting of retail regulated prices in Queensland. If there are any issues that arise, the material should be left for fuller consideration and consultation in the process for setting regulated retail prices for 2014-15.

4.1.3. Customer Acquisition and Retention Costs (CARC)

We continue to believe that there is no justification for including an allowance for CARC in retail operating costs.

Treatment of CARC in other Australian jurisdictions

Customer acquisition costs and retention costs were originally included in retail price determinations in NSW in 2007 when IPART was required to consider a mass market new entrant, and this approach was then copied in other Australian jurisdictions.

Not all jurisdictions accepted this approach.

Victoria

There was never any allowance for customer acquisition costs or retention costs in any of the regulated retail tariffs that were set in Victoria, and competition still thrived. Victoria was still then considered to be the most competitive electricity market with the highest rates of customer churn and transfer anywhere in the world. This shows that an allowance for customer acquisition costs or retention costs is not required in order for competition to develop and thrive.

36 Draft Determination, page 39

ACT

In the ACT, ICRC has consistently refused to include an allowance for CARC in its regulated retail prices, and has only allowed instead for “sales and marketing, being primarily the costs of communicating the TFT [Transitional Franchise Tariff] arrangements” as efficient costs.[37]

For example, in a previous determination, ICRC countered arguments that an allowance for CARC needed to be included in regulated tariffs to encourage competitive behaviour, by stating the following:[38]

> *… the Commission considers that a ‘regulated’ franchise tariff, where franchise customers are able to benefit from ActewAGL Retail’s economies of scale and where customer acquisition costs are not included in the franchise tariff, is likely to provide greater benefits to customers than a notional ‘competitive’ tariff that is determined by the Commission.*

We concur with this view of ICRC. CARC has no place in regulatory tariff determinations that have appropriate terms of reference.

Proposed treatment of CARC in Queensland

The regulated retail electricity tariffs apply to customers that have not chosen a competitive market offer, and to customers that specifically request to be put on a regulated tariff. There are no customer acquisition costs or retention costs involved in offering regulated retail electricity tariffs, and no allowance should be made for such costs in the regulated tariffs. While some jurisdictions have included these costs in their calculations on setting regulated retail tariffs, this was because their Terms of Reference required them to do so.

No allowance should be made for customer acquisition and retention costs (CARC) in regulated retail electricity prices in Queensland.

37 *Final determination: Investigation into retail prices for non-contestable electricity customers in the ACT*, ICRC, May 2003, section 4.7, available at http://www.icrc.act.gov.au/__data/assets/pdf_file/0009/16677/finaldeterminationretailpricesmay2003cw.pdf – and quoted in later ICRC determinations ever since

38 *Final Decision: Retail prices for non-contestable electricity customers 2010–12*, Report 7 of 2010, ICRC, June 2010, page 54, available at http://www.icrc.act.gov.au/__data/assets/pdf_file/0018/194310/Report_7_of_2010_11_June_2010.pdf

We note that the previous inclusion of CARC by the Authority in Queensland explicitly allows for marketing to support a competitive market. It implicitly recognises that there is effective competition in the electricity market in the Energex area, because an efficient representative retailer would only be expending any funds on customer acquisition and retention if that was the case. Because of the Queensland Government's Uniform Tariff Policy, it also has the side effect that Ergon Energy customers are paying for the costs of customer acquisition and retention, even where there is no effective competition, and therefore no funds are being expended on those activities.

We were particularly concerned regarding the statement of the Authority in its Final Determination for 2012-13 that it would "maintain the current, perhaps generous, CARC component going forward".[39] This was presented without any further analysis.

Any allowance for CARC should be reasonable, not generous. Analysis of Table 4.3 on page 58 of the Final Determination for 2012-13 showed clearly that the Queensland allowance for CARC was above that allowed in NSW and South Australia, and in other jurisdictions no allowance for CARC was given. If there has to be an allowance for CARC in Queensland, it should instead be much lower, given that only a proportion of customers in Queensland are reasonably open to contestability, as against all customers in those other two states. We propose that if there is to be an allowance for CARC in Queensland, it should be set at a rate benchmarked against the previous allowances in NSW and South Australia, with an adjustment for the proportion of customers in those areas of Queensland where there is effective competition.

The Draft Determination states: "The Authority is also of the view that, if anything, the allowance it has made in the past is on the generous side. However, for this Draft Determination, the Authority will base its allowance for CARC on that provided for 2012-13, suitably escalated to reflect inflation between years."[40] We do not understand this view. If the allowance has been in the past that is generous, that should be corrected now to an allowance for 2013-14 that is reasonable rather than generous.

We also note that the CARC allowance was set based on an assumption that customers would be gained primarily through door-knocking.

- EnergyAustralia announced in February 2013 that it would no longer use door-to-door sales to sign up potential customers by the end of March, and called on other energy retailers to follow EnergyAustralia's lead and discontinue unannounced doorknocking.[41]

39 Final Determination 2012-13, page 58

40 Draft Determination, page 40

41 *Knock Knock...Who's there? Not EnergyAustralia*, EnergyAustralia, 25 February 2013, available at www.energyaustralia.com.au/about-us/media-centre/current-news/knock-knock

- AGL withdrew from door-knocking in Queensland and South Australia in October 2012, and announced in February 2013 that it would now also cease unsolicited door-to-door sales activity to residential customers across New South Wales and Victoria.[42]
- Origin Energy has also been reported to have distributed more than three million "Do Not Knock" stickers so customers would not be disturbed.[43]

Given these initiatives, it would be prudent that any CARC allowance would be lowered to account for less costly channels being used to recruit new customers from now on.

> If the Authority is to make an allowance for CARC, it should be at a much lower level than that allowed in the Final Determination for 2012-13. Any allowance should be reasonable rather than generous, and should take into account less costly channels being used to recruit new customers, as against the previous cost estimates which were based on the costs of acquiring new customers through door-knocking.

4.1.4. Adjusting the benchmark retail operating costs allowances

We agree that it is appropriate to make some adjustments to account for jurisdictional differences where reliable information on the individual cost components exists, but we continue to caution that with substantial adjustment up or down, the benchmark approach will lose its validity, as it will morph into an actual costs approach that is not properly thought through. We do not believe that an additional explicit allowance should be made to cover regulatory fees, unless it is shown that regulatory fees are materially different in Queensland as against in other jurisdictions. If they are materially different, then it is the difference and not the full amount that should be added to or subtracted from the retail operating costs allowance.

We agree with the Authority's Draft Determination that it is not appropriate to increase the allowance based on retailers' claims of increases in selected existing costs or to account for new costs in the absence of evidence about movements in all other cost elements.[44]

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42 AGL withdraws from unsolicited door-to-door sales, AGL, 26 February 2013, available at www.agl.com.au/about/ASXandMedia/Pages/AGLwithdrawsfromunsoliciteddoor-to-doorsales.aspx

43 See for example www.abc.net.au/pm/content/2013/s3699798.htm and www.heraldsun.com.au/news/victoria/electicity-and-gas-supplier-energyaustralia-axes-intrusive-door-knockers-after-customer-complaints/story-e6frf7kx-1226584788982. The stickers are available from https://www.originenergy.com.au/sticker.

44 Draft Determination, pages 40-41

4.2. RETAIL MARGIN

The retail margin represents the reward to investors for committing capital to a business and for accepting risks associated with providing retail electricity services.[45]

4.2.1. Approach to estimating the retail margin

In previous BRCI decisions and the 2012-13 Determination, the Authority set the retail margin on an earnings-before-interest, tax, depreciation and amortisation (EBITDA) basis which meant that an allowance for depreciation and amortisation was implicitly included and the retail margin was calculated as a percentage of total costs.

There are generally two alternative approaches to estimating the retail margin:

- Undertaking an extensive and detailed financial analysis of the appropriate retail margin, such as a bottom-up and/or expected returns approach; or
- Assessing the appropriateness of the current retail margin by benchmarking it against margins adopted in other jurisdictions.[46]

We support the Authority's benchmarking approach. Besides the arguments set out in the Draft Determination,[47] there is now not sufficient time available for the Authority to consult on a bottom-up approach for the estimation of retail operating costs for 2013-14.

4.2.2. Implementing the benchmarking approach

We do not believe that it was appropriate to increase the margin from 5% to 5.4% in 2012-13. The justification for the increase seemed to be that 5.4% is the mid-point of the reasonable range of 4.8% to 6% found by consultants in NSW.[48] The justification was made notwithstanding that the current retail margin of 5% also falls within the reasonable range. The Authority itself said that "the current 5% margin in Queensland is not unreasonable" and "the new pricing approach being established in this determination should reduce the risks faced by retailers in Queensland relative to the previous BRCI approach, including better alignment of the cost structure and price structure and the pass through of network costs".[49]

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45 Draft Determination, page 44

46 Draft Determination, page 44

47 Draft Determination, pages 44-45

48 Final Determination for 2012-13, pages 74-75

49 Final Determination for 2012-13, pages 74-75

This being the case, the allowed margin in 2012-13 should have been lower, and certainly not higher, than the previous 5% level under the BRCI.

The arguments on page 75 of the Final Determination for 2012-13 regarding an LRMC floor are also not relevant to the retail margin since those are not systematic risks. If a LRMC floor were appropriate, it would have been incorporated in the energy costs. The Authority rightly did not include LRMC in energy costs, and the retail margin is not the place to add something extra to offset a good decision elsewhere in a pricing determination.

The Authority also stated: "The Authority also notes that, unlike IPART, it has included a specific allowance for head room of 5% which, in combination with the margin, means that the potential gap over total allowed costs available to retailers is close to 11% in total."[50] This is far in excess of any such allowance in other Australian jurisdictions.

> The gross retail margin of 5% of total costs that was allowed in the Benchmark Retail Cost Index (BRCI) calculations is realistic, and should not be any higher. Instead, it should be lower, because the retailers will be compensated based on efficient costs, rather than the BRCI mechanism that might have borne no relationship to their actual efficient costs and was not cost-reflective. Under the BRCI, retailers therefore faced higher risks than should be the case under the current framework for setting regulated retail prices.

We have also noted in section 3.2.3 above that we are concerned that in its Draft Determination the Authority has not reflected elsewhere its view that its revised modelling approach using the 95th percentile of hedged outcomes takes into account the majority of risk faced by retailers. We repeat here the proposal we made there, which is that the Final Determination should take this into account in the retail margin, where the return expected should now be lower because of the minimised risk.

> In its Final Determination, the Authority should reduce the retail margin commensurate with its view that its revised modelling approach to wholesale energy costs takes into account the majority of risk faced by retailers.

50 Final Determination for 2012-13, page 75

As with the retail operating costs that were discussed in section 4.1.2 above, the Authority is intending to take into account in preparing its Final Determination, any new evidence regarding the appropriate level of margin that might become available once IPART's current analysis of retail margins is released.[51] As with retail operating costs, we are concerned that new material in regard to the setting of retail margins from other regulators that was not available at the time of the Draft Determination should only be taken into consideration in the Final Determination of regulated retail prices in Queensland for 2013-14 if it is unambiguously applicable to the setting of retail regulated prices in Queensland. If there are any issues that arise, the material should be left for fuller consideration and consultation in the process for setting regulated retail prices for 2014-15.

New material in regard to the setting of retail margins from other regulators that was not available at the time of the Draft Determination should only be taken into consideration in the Final Determination of regulated retail prices in Queensland for 2013-14 if it is unambiguously applicable to the setting of retail regulated prices in Queensland. If there are any issues that arise, the material should be left for fuller consideration and consultation in the process for setting regulated retail prices for 2014-15.

51 Draft Determination, page 46

5. COMPETITION AND OTHER ISSUES

5.1. COMPETITION CONSIDERATIONS

In its Final Determination for 2012-13, the Authority decided to include an additional allowance for headroom of 5% of cost-reflective prices for all tariffs.

We have many concerns regarding this decision, which we discuss in this section of our report.

5.1.1. The role of competitive activity to derive longer term benefits for consumers

We understand that the Delegation requires that, in making a price determination for each tariff year, the Authority must have regard to the effect of the price determination on competition in the Queensland retail electricity market.

We also accept that there is some longer term benefit to be derived by maintaining an actively competitive market rather than pursuing a short term minimum price approach which may stifle or eliminate competition from the market.

However, we have some concerns with the following paragraph in the Final Determination for 2012-13:[52]

> The longer term benefit derives from the downward pressure on prices that competition naturally brings to the market. By setting regulated prices somewhat higher than full cost, retailers will be attracted to enter the market and, as they compete for market share, non-regulated prices will be driven down. The more active the competition, the closer retailers will reduce prices to their individual, efficient costs of supply. While regulated prices will be unaffected, customers should be able to access lower priced market offers from competing retailers. Consumers should also benefit from improved service quality and choice.

It may be true that "by setting regulated prices somewhat higher than full cost, retailers will be attracted to enter the market and, as they compete for market share, non-regulated prices will be driven down" in the shorter term. But the best way to achieve longer term benefits for consumers is not to attract retailers because there is an artificial extra margin in the supply chain for them to exploit. Rather, retailers should be attracted to a market because they can operate more efficiently and innovatively, and provide better customer service than the incumbents. That is the way to achieve sustainable entry to give longer term benefits.

52 Final Determination for 2012-13, page 82

We are concerned that creating artificial headroom to attract retailers will not encourage efficiency or lower pricing. Rather, there is significant danger that it will attract retailers offering no better service. We do not believe that this contradicts the Authority's comment that regulation is an imperfect substitute for competition.[53] There may be benefit in attracting retailers per se, but it should not require an explicit allowance for headroom to achieve that in an efficient manner.

Following the logic of the Authority, without headroom, competition will be stifled. This means that the Authority thinks that retailers will not compete when regulated prices are set at what the Authority considers to be cost-reflective prices with a reasonable margin. We disagree with that assertion, on the basis that we believe retailers can compete in that scenario, through a combination of offering superior customer service, innovative product development, more efficient and economic purchasing and operations, and perhaps accepting lower margins.

But if the Authority's logic is accepted, then the implication is that headroom will drive down prices no further than the level at which they would have been had no headroom been allowed – because that is the level at which the Authority believes competition is stifled.

5.1.2. The effects of allowing for headroom in regulated electricity prices

The overall effects of adding headroom could thus include:

- No additional longer term benefits in improving customer service or lower prices than would have been achieved without headroom.
- Short term additional costs incurred by all consumers until competition drives prices down to the levels at which they would have been without explicit allowance for headroom.
- Longer term ongoing additional costs for headroom for those customers who through inertia, lack of access to clear comparative information, or other reasons, remain on price-regulated tariffs even though more competitive offers might be available to them.

53 Final Determination for 2012-13, page 83 – based on analysis by the Australian Energy Market Commission

- Ongoing longer term additional costs for customers in the Ergon Energy area that do not have access to competitive offers. As noted by the Authority, the disparity between the lower market prices available to the majority of customers in SEQ and the higher notified prices customers elsewhere must pay may be inconsistent with and undermining the intent of the Uniform Tariff Policy. The application of the Uniform Tariff Policy may need to be reviewed as progress is made towards deregulation in SEQ.[54] The application of headroom by the Authority further serves to undermine the intent of the Uniform Tariff Policy.

One of the cornerstones of the retention of retail price regulation even after retail competition is introduced is to provide a safety net for those customers who have not yet embraced competition, or are unable or unwilling to do so. Customers who remain on regulated tariffs even after competition is introduced should be assured by the role of the Authority that they are paying a reasonable price based on cost-reflective prices and a reasonable margin. Instead, by advocating for "headroom" of an additional 5% the Authority is essentially proposing to regulate that customers who remain on regulated tariffs pay 5% more than they should be paying.

A further point regarding the regulated tariffs is that the terms and conditions of supply are also set out in regulation, whereas the market offers available to customers may vary those. It may not be possible for customers to obtain competitive offers that have terms and conditions that replicate the standard terms and conditions. Adding headroom will therefore mean that customers who desire to benefit from the standard terms and conditions may only be able to do so at a premium to efficient supply costs, on an ongoing basis. Allowing retailers to charge a premium for standard supply is not justifiable.

5.1.3. No explicit allowance for headroom has been included in any other jurisdiction

As noted by the Authority, "an explicit allowance for headroom has not been included by regulators in setting regulated retail electricity prices in any other jurisdiction to date".[55] For example, IPART has stated in the past:[56]

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54 Drat Determination, pages 3 and 51.

55 Draft Determination, page 49

56 *NSW Electricity Regulated Retail Tariffs 2004/05 to 2006/07*, Final Report and Determination, IPART Determination No 1, 2004, June 2004, page 8, available at www.ipart.nsw.gov.au/files/d8cd67c3-b819-4497-b5d0-9f4f010fafd8/Det04-1.pdf.

> A number of stakeholders suggested that the Tribunal should set target tariffs *above* cost-reflective levels for standard retailers, to provide greater encouragement for competitive entry. The Tribunal does not consider this to be appropriate. It considers that charges to customers should be based on the costs of supply *and no more*. It strongly believes that including an allowance in target tariffs for costs that are not incurred by standard retailers is not desirable from an economic efficiency perspective.

5.1.4. The role of the Authority in regard to competition in determining notified prices

The Delegation requires the Authority to base its determination on an N + R cost build-up methodology, where:

- The N (network) cost component is treated as a pass through; and
- The R (energy and retail) cost component is determined by the Authority.

If the Authority makes an additional allowance for headroom, it will have gone outside of the remit of the Delegation by instead basing its determination on an N + R + headroom methodology, where:

- The N (network) cost component is treated as a pass through;
- The R (energy and retail) cost component is determined by the Authority; and
- An additional allowance is determined by the Authority for headroom – which is not a component that is specified in the Delegation.

In its Final Determination for 2012-13, the Authority countered this argument as follows:[57]

> QCOSS suggested that the Authority was going beyond its Delegation because head room was not explicitly mentioned in the Delegation. However, as noted above, the Authority is required by the Delegation (and the Electricity Act) to have regard to the effect of its determination on competition in the Queensland retail electricity market. Under the Electricity Act, the Authority may also have regard to any other matter it considers relevant.

The equivalent wording in the current Delegation is that the Authority must have regard to the effect of the price determination on competition in the Queensland retail electricity market. We do not dispute that there are several matters to which the Authority may or must have regard. But that does not change the fact that the paragraph 5(c) of the Delegation sets out that the Authority must base its determination on an N + R cost build-up methodology, and not an N + R cost build-up + headroom methodology

57 Final Determination for 2012-13, page 83

In its Draft Determination, The Authority countered this argument as follows:[58]

> QCOSS and Queensland Consumers Association also argued that the Authority has gone outside the remit of the Delegation by including headroom because this means that it has not based its determination on an N+R methodology. However, the Authority considers that the N+R framework is intact, but in setting the R component it is not precluded from including headroom to satisfy the requirements of the Electricity Act and Delegation that it must consider the effect of its determination on competition in the Queensland retail electricity market.

Our response to that is that the Delegation sets out that the R component comprises “energy and retail **cost**”. Headroom is not a cost. The Final Determination for 2012-13 was very clear: cost-reflective tariffs and prices were shown in Chapter 5. The final determined tariffs and prices in Chapter 7 of the Final Determination for 2012-13 were not the same as the cost-reflective tariffs and prices in Chapter 5, because the determined tariffs and prices included headroom. The determined tariffs and prices were thus clearly shown not to be cost-reflective.

In the Draft Determination for 2013-14, the Authority presents its draft determined tariffs and prices without the same clarity. Chapter 7 of the Draft Determination for 2013-14 does not separately set out cost-reflective vs. draft determined prices. Appendix D is headed “Cost reflective retail tariffs and prices”, but the tariffs shown in Appendix D are not cost-reflective, because they include headroom on top of assessed costs.

In the Authority’s own words:

- Headroom represents “excess profit” in prices.[59]
- “The Authority considers that setting notified prices somewhat higher than the Authority’s estimate of the efficient cost of supply will attract retailers …”[60]
- “The Authority has decided to again include an allowance for headroom, above its estimate of the efficient costs of supply”[61]

Tariffs that include “excess profits” for retailers and tariffs which are set “somewhat higher than the Authority’s estimate of the efficient cost of supply” are <u>not</u> cost reflective tariffs. They are tariffs set at levels above the levels at which cost reflectivity would be exhibited.

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58 Draft Determination, pages 50-51

59 Draft Determination, page 48

60 Draft Determination, page 50

61 Draft Determination, page 51

The Draft Determination states that “the Authority considers that part of its role in setting notified prices is to provide a transition to effective competition and eventual price deregulation, particularly in SEQ”.[62]

The Draft Determination further states: “Notified prices should also encourage customers to exercise market choice and seek out the best deal in the competitive market.”[63]

We have read carefully the Delegations, the covering letters to the Delegations, and the Government’s submission to the Interim Methodology Paper, and we do not see anywhere that notified prices should be set at a level that encourages customers to seek out other better deals. Nor do we see it stated that a key objective is to transition to price deregulation. This is notwithstanding “the Government's policy objective that consumers, wherever possible, have the opportunity to benefit from competition and efficiency in the market place”.[64]

The Authority points out that under the Australian Energy Market Agreement, the various jurisdictions have agreed to phase out retail price regulation if effective competition can be demonstrated.[65] But that does not imply that the Minister’s current Delegation to the Authority to set regulated retail prices has the objective of achieving that demonstration.

Rather, we read the reason why the Authority is still regulating prices as being that “the Government is not convinced that residential and small business customers are adequately protected from the effects of a move to a fully deregulated market in order for price regulation for this customer segment to be removed at this time.”[66]

We continue to sense some tension between the Government on the one hand seeing regulated retail prices as a means to protect customers from the effects of a move to a fully price-deregulated market, while the Authority sees regulated retail prices as a means of transition to price deregulation.

We note the final report published by the Independent Competition and Regulatory Commission (ICRC) of the ACT on 8 June 2012, which stated:[67]

62 Draft Determination, page 2 and page 48

63 Draft Determination, page 48

64 Government Submission to the Interim Consultation Paper, page 16, available at www.qca.org.au/files/ER-QLDGov-Submission-InterimConsultationPaper-1112.pdf

65 Draft Determination, page 2 and page 48

66 Government Submission to the Interim Consultation Paper, page 7

67 *Retail prices for franchise electricity customers 2012-14*, Final report, Report 4 of 2012, June 2012, ICRC, page 6, available at www.icrc.act.gov.au/energy/electricity

> It is also important to note that the Commission's remit is the preparation of a price direction for the next two years and that this is a fundamentally different task to the establishment of a competitive market. The decision to remove the regulated tariff is a decision that rests with the ACT Government. The Commission considers it appropriate under the current legislative framework to continue to base the efficient costs on those that would be incurred by an incumbent retailer receiving a reasonable retail margin.

The Authority should be similarly clear regarding its remit.

5.1.5. Quantification of headroom allowance

As stated above, the Final Determination for 2012-13 included an additional allowance for headroom of 5% of cost-reflective prices for all tariffs.

The allowance was made without any quantification of the benefits (if any) that customers might see, set against the additional costs that customers might incur from this additional allowance.

The inclusion of an explicit allowance for headroom should at least be accompanied by regulatory cost-benefit and other regulatory impact analysis. A range of figures should be presented in such analysis, and the most appropriate one chosen, based on the analysis.

This is all notwithstanding our view that there should be no such additional headroom allowance in the tariffs.

Our view is that no additional headroom allowance is warranted for 2013-14. It should therefore be obvious that if the Authority nonetheless includes an additional headroom allowance in its Final Determination, it should be set as low as possible, and fully justified.

The Authority should make no additional allowance for headroom in notified prices for 2013-14.

5.2. ACCOUNTING FOR UNFORESEEN OR UNCERTAIN EVENTS

In its 2012-13 Determination, the Authority considered that it would be appropriate to include some form of mechanism to account for the material impacts of unforeseen or uncertain events on retailers' costs.

However, the Authority considered that it did not have the capacity to include a within-year cost pass-through mechanism in its determination because it was only delegated the task of determining prices for one year and had no ongoing role in administering the determination. It also considered that it would not be possible for it to commit to some form of catch-up mechanism which would allow for unforeseen cost impacts from one year to be accounted for in setting prices for the following tariff year. This was because the Authority had only been delegated the function of setting notified prices for the 2012-13 tariff year, and the Minister could have decided not to delegate the function to the Authority in the following year, making any commitment potentially worthless.

The Authority has now been delegated the task of determining prices for a three-year period, but is still required to make annual price determinations. While this suggests that an intra-year cost pass-through mechanism to apply within a tariff year is still not possible (as the Authority is required to set prices annually, for the tariff year, in prospect), the Authority considers that it could now include a pass-through mechanism to allow for certain costs incurred during one tariff year to be recovered when setting prices for the following tariff year.[68]

The Authority notes that other regulators commonly include cost pass-through mechanisms in their multi-year price determinations.[69]

It is our view that it is generally not appropriate to revise tariffs based on unforeseen events. It deflects responsibility from retailers to mitigate the effects of such events, even though they are the parties that are generally best placed to do just that. It is inequitable to pass such risks onto consumers who have no means of mitigating them.

Retailers lack incentives to control costs if they can just pass through costs that they incur in a given category. For example, it has previously been suggested that unforeseen AEMO charges (such as a reserve trader or direction event) may be types of events that would be subject to cost pass-through events occurring. That type of event generally occurs because retailers have not contracted adequately for wholesale purchases, so allowing such an event to have cost pass-through is counter-productive.

A further issue is that in their previous submissions, retailers have claimed in the context of setting wholesale energy costs that if allowances are too high in any given year, the retailers will simply ‘compete away’ the extra allowance. ACIL Tasman has recognised this in its report, stating: “The concept of a make good adjustment for previous years is not appropriate in the estimate of energy costs as the estimate must be made in relation to the single year of 2013-14. A make good concept also has little merit in a market that is subject to competitive forces.”[70]

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68 Draft Determination, pages 56-57

69 Draft Determination, page 57

70 ACIL Tasman report, page 28

> The gazetted prices should not be adjusted via a cost pass-through during the tariff year, or via a catch-up mechanism in a subsequent tariff year. One exception to the above may be if a change of Government policy requires the Authority to make changes to regulated pricing during the tariff year. In that case, we would expect the Government to provide the necessary Delegation to the Authority so that the Authority would have the capacity to implement the required changes.

We also believe it is somewhat too late now to introduce a catch-up mechanism for 2013-14, as there is now no opportunity for the Authority to consult on the finer details. We suggest instead that implementation if it is to occur should be delayed to 2014-15. Besides all the issues that we have raised above, catch-up mechanisms can be complex and there are many parameters to consider. For example:

- If a catch-up mechanism determined that tariffs would otherwise have been set say 0.2c/kWh higher, is the approach simply to add 0.2c/kWh to each tariff in the following year?
- Should an adjustment be made on the basis that the total kWh expected to be supplied the following year may differ from the total supplied the previous year? Should those total kWh only include customers on notified prices, or should they also include energy consumed by customers on equivalent market prices?
- Would new customers face adjustments to their charges in the following year, even though they were not customers in the previous year from which the catch-up is being applied?
- Is it consistent with the Delegation for prices to be set that are not cost-reflective for a particular tariff year, given that they may include adjustments relevant to a previous tariff year?

If the Authority does still choose to implement a cost pass-through or catch-up mechanism, then the following parameters should apply. The application of cost pass-through or catch-up should be strictly limited to events that would be wholly outside an efficient representative retailer's control. The events that might be considered would need to be tightly defined in the Authority's determination of prices. The circumstances that might trigger a cost pass-through or catch-up mechanism should be capable of adjusting prices up or down; they should definitely not be one-way. The trigger should also not be dependent on retailer initiation, which might be actioned only if the mechanism would be likely to put prices up, and not down.

The Authority has suggested that it might allow for a catch-up mechanism to allow the pass through of SRES costs.[71] We suggest that if this is implemented it should only be on the basis of the difference between actual binding STP targets and resulting SRES liabilities, and should not take into account changes in the cost of buying each STC.

71 Draft Determination, page 72

6. TRANSITIONAL ARRANGEMENTS

We support the implementation of transitional arrangements for any changes to tariff structures that will have a significant impact on some consumers' costs. As outlined by the Authority, the proposal to rebalance the fixed and variable components of Tariff 11 to cost-reflective pricing will have an adverse impact on the lowest consuming households. Many low-consuming households are vulnerable consumers who are least likely to be able to adapt to significant price increases. We support a staged approach to minimise the immediate bill shock for consumers.

We support the Authority's interpretation of the Minister's Delegation as requiring the Authority to implement a stepped approach. We also note that the covering letter to the Delegation recommends the Authority "... fully utilise the three-year delegation period ..." and that this approach is suggested so the Authority can "... take into account the impacts of price increases on struggling Queensland households and businesses" and "ensure that Queensland households experience a smooth transition from the freeze".

A transition period is essential in order to assess the impact of the changes on different customer groups and for this information to influence improvements to government policy. In particular, the shift to greater cost reflectively will necessitate changes to government concessions to ensure they are adequate and well-targeted alongside the new tariff structure. Further, the transitional timeframe provides an opportunity for consumer education to be rolled out over time to assist consumers understand and adjust to the new pricing structures.

Consumer education will be critical in ensuring a smooth transition to new pricing arrangements over time and reducing bill shock for consumers. A sustained campaign of consumer education over time is likely to be more successful than quickly rolling out consumer education ahead of significant change prior to 1 July 2013. Consumers should be given time to adjust and understand the implications of the reforms.

We prefer a smooth transition to cost reflective pricing in order to minimise bill shock for consumers who may be adversely affected. The effect on consumers should be a key consideration when determining the form of transitioning.

We also refer to the Minister's statement that "the Government expects the Authority to ensure that Queensland households experience a smooth transition from the freeze". As we pointed out at the workshop held in Brisbane on 19 December 2012, the Authority does not control the underlying network charges that are taken as costs that are to be reflected in "cost-reflective" tariffs. Non-smooth changes in network costs outside the Authority's control could materially undermine the Authority's best efforts to put in place smooth transition of retail tariffs.

The level of the Energex fixed network charge to retailers for residential customers on Tariff 11 has a material impact on the mismatch for low usage customers between the current (frozen) charges in Tariff 11 and the cost-reflective levels. It will therefore be necessary for the Authority to have close regard to changes in the structure and level of the underlying network charges in designing the particular form of transitioning of retail tariffs that the Authority implements.

The Queensland Government's submission to the Interim Consultation Paper noted that "2015-16 (the final year of the Delegation period) represents the first year of a new network revenue determination from the Australian Energy Regulator (AER). The Government acknowledges that this will make the forecasting of the N component of retail tariffs challenging." Clearly this makes smooth transition to the 2015-16 level and structure of Tariff 11 particularly challenging.

The Minister's covering letter to the September 2012 Delegation states that "it is important that the QCA take into account the impacts of price increases on struggling Queensland households and businesses". To meet this expectation, the Authority should undertake substantial analysis to provide an assessment to identify the expected impacts of tariff arrangements on a range of consumer groups with varying consumption patterns, including pensioners, large working families, low-income tenants and other vulnerable households. This analysis should take into the account the existing electricity concessions available in Queensland.

To date, the Authority's analysis of different customer types seems to amount to typifying various consumption levels,[72] without regard to the customers' concessions entitlements. Concessions are separately listed in the Draft Determination,[73] but are not linked to bill impacts. This is no substitute for actual socio-economic, demographic (and firmographic) analysis which takes account of those customers' concessions entitlements.

For example, the Authority has typified a "frugal single elderly person" as using 2200 kWh per annum, and shows this person's bill impacts without regard to their concessions. What is required is analysis of the range of bills of single elderly persons and their distribution. This analysis also needs to take into account the impacts that concession entitlements have on the percentage changes and the actual dollar amounts by which bills will change when tariffs become more cost-reflective. This might result in findings that are quite different from the Authority's finding that a "typical increase" for such a customer based on the Draft Determination would be 26% or $171 per annum.

72 Draft Determination, Table 7.5, page 101

73 Draft Determination, Table 6.2, page 73

While we appreciate that the Authority has no jurisdiction over government policy, the Authority must consider the impact of regulated retail tariffs as a whole to undertake effective assessment of the impact of price changes on consumers. Using information from other jurisdictions to inform calculations without considering the different concession arrangements provides a skewed snapshot of what is really going on in households struggling with energy affordability in Queensland. It is our strong view that significant changes to tariff arrangements will necessitate changes to the existing energy concessions and support arrangements, to ensure they are well-targeted and equitable for Queensland consumers.

The Authority's analysis of the impact of price increases on consumers will be an important input to the Queensland Government's own policy assessment and implementation. It will provide the Queensland Government with information to enable it to model the extent to which concessions are providing adequate and equitable outcomes across customer segments, and to make appropriate adjustments to the concessions framework, alongside the changes to the tariffs that are delegated to the Authority.

7. DRAFT DETERMINATION

Chapter 7 sets out the Authority's Draft Determination of regulated retail electricity prices (notified prices) to apply from 1 July 2013 to 30 June 2014, as well as expected customer impacts.

As discussed in section 5.1 above, we do not believe that headroom should be included in cost-reflective retail tariffs and prices.[74]

We are concerned at the magnitude of the residential customer impacts set out in section 7.4 of the Draft Determination. We again draw attention to The Minister's covering letter to the September 2012 Delegation which states that "it is important that the QCA take into account the impacts of price increases on struggling Queensland households and businesses".

74 Draft Determination, page 95