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Mr Charles Millsteed
Chief Executive Officer
Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001

Dear Mr Millsteed

Ergon Energy Retail submission to the Regulated Retail Electricity Prices for 2022-23 Draft Determination

Ergon Energy Queensland Pty Ltd (Ergon Energy Retail) welcomes the opportunity to provide comment to the Queensland Competition Authority (QCA) on its Regulated Retail Electricity Prices for 2022-23 Draft Determination (Draft Determination).

Wholesale Energy Costs (WEC)

Ergon Energy Retail acknowledges the methodology used by the QCA to estimate WEC is consistent with prior years and supports in principle the key steps taken to estimate the WEC for a given load and year. However, Ergon Energy Retail notes that ACIL Allen's (ACIL) hedge modelling is heavily weighted towards caps (over 50%) and remains of the view that such a heavy weighting is extremely difficult to achieve in practice. There are many market participants seeking to employ a similar strategy to ACIL's modelled hedge strategy and caps are highly sought after.[1] Figure 4.11 suggests that ACIL's modelled hedge position assumes more than 1000 MW of caps for Q4 and Q1[2]. Ergon Energy Retail looked at ASX data on 31 March 2022. The current open interest for Q122 caps is 876 MW and for Q123 it is 577 MW. The open interest position is indicative of the caps held by electricity retailers for hedging purposes. While it can be expected that Q123 open interest position will increase, it is highly unlikely that one retailer would be able to purchase over 1000 MW of ASX cap contracts for the period (as all market participants must compete for this product). Ergon Energy Retail therefore requests that ACIL reconsider its weighting of cap products in its hedging strategy taking into account the current liquidity of cap products.

Ergon Energy Retail also recommends publication of ACIL's energy modelling data spreadsheet to help improve assessment and understanding of ACIL's analysis surrounding estimation of the WEC. The QCA published this data up until 2020-21 before ceasing its publication from 2021-22. This spreadsheet was very useful for transparency and ease of interpreting the ACIL cost of energy report, noting the graphs in the report are often small and difficult to assess.

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[1] ACIL Allen, *Estimated energy costs for 2022-23 retail electricity tariffs: Draft Determination, February 2022*, p. 25
[2] Ibid., p. 42

Reliability and Emergency Reserve Trader scheme

Compensation of the Australian Energy Market Operator (AEMO) fees relating to the Reliability and Emergency Reserve Trader (RERT) scheme must be included in notified prices as these fees are levied by AEMO on retailers to maintain power system reliability. As at end March 2022, Ergon Energy Retail have incurred costs for two RERT events which need to be incorporated into the 2022-23 notified prices:

- 25 May 2021 (as captured in the Draft Determination 2022-23), and
- 1 February 2022 (post the Draft Determination).

Ergon Energy Retail has paid invoices to AEMO representing its share of both events, further noting that RERT costs are beyond the control of a retailer. We note that the final costs for the 25 May 2021 RERT event were published in AEMO's RERT Quarterly Report Q2 2021 (published August 2021). Further, we acknowledge that AEMO has indicated the final costs associated with the 1 February 2022 RERT event will be published in the quarterly RERT report due in May 2022. Should the final RERT costs be unavailable in time for the QCA Final Determination, Ergon Energy Retail remains firmly of the view that the AEMO draft estimate of RERT costs should be used for the 2022-23 prices, with the cost pass-through mechanism correcting any over or under recovery of RERT costs in the 2023-24 notified prices. Our confidential invoice and Settlement Report from AEMO is attached as evidence of the materiality of this cost. Our request for confidentiality of these documents is also attached.

NEM Management Fees

Ergon Energy Retail notes ACIL's advice[3] related to the change in calculation methodology for National Electricity Market (NEM) Management Fees, from using the AEMO's forward estimate of upcoming NEM fees (that corresponded to the year of the determination) to applying NEM fees from the latest available AEMO document which results in a 12-month lag in fee recovery

Ergon Energy Retail appreciates the clarification from ACIL that it has changed its methodology, and requests that future changes in methodology for determining energy costs be more clearly articulated in ACIL (and QCA) reports at the time of the methodology change. In our view the QCA should have consulted on this change in methodology as it is creating recovery shortfalls for retailers.

Ergon Energy Retail acknowledges the change in approach to determining NEM Fees is because AEMO no longer publishes NEM fee forecasts. However, this means that as new fees are introduced (as occurred in 2021-22) the cost of these fees must be absorbed by retailers until the following year when the notified prices allow for the recovery of these new fees (in arrears).

We are also aware of an upcoming step change in AEMO fees for 2022-23. AEMO is currently consulting on options to recover its sizeable deficit (forecast to be $106 million in 2021-22) and future escalating costs from industry (beginning in 2022-23)[4]. Using the new ACIL methodology whereby retailers will recover AEMO fees in arrears, retailers must

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[3] Ibid., pp. 26-27

[4] AEMO, *Presentation to Finance Consultation Committee Draft FY23 Budget & Fees*, 4 March 2022, Available at: https://aemo.com.au/-/media/files/stakeholder_consultation/working_groups/other_meetings/financial-consultation/2021-22/fcc-meeting-3-presentation.pdf?la=en

absorb a material increase in fees for 12 months. Given the pressure on retail costs driven by the reduction in the retail allowance and escalating regulatory costs, this will be difficult to absorb.

We also expect the impact to retailers of this lag will be further compounded by the change in fee recovery structure for Market Customers commencing 1 July 2023.

Our preference is that the QCA provide a short-term allowance for the recovery of the AEMO deficit. Consequently, we request that QCA consult with AEMO regarding the quantum of this debt recovery and how AEMO intend to recover this deficit from market customers to inform the short-term allowance.

Ergon Energy Retail also recommends that ACIL update the wording in its final 2022 Estimated Energy Costs report given the February report refers to "projected fees"[5] which may give the impression that NEM fees are based on a forward estimate rather than the new 12 month lag methodology.

Retail Costs

The electricity market is undergoing rapid transformation as Australia moves towards a net zero emissions future. As consumers increasingly adopt distributed energy resources and demand greater protections, the regulatory and compliance framework for the electricity industry grows in complexity and breadth. With increasing change comes additional compliance costs.

Ergon Energy Retail remains concerned that the retail cost allowance does not provide for the material costs impact of regulatory reform from the last two years[6]. With significant and costly regulatory reforms (e.g. Consumer Data Rights, Energy Security Board Wholesale Market Reforms and the Better Bills Guideline) continuing to be rolled out, we request the QCA consult with a broad range of retailers to assess the financial impacts of retail compliance with these upcoming reforms, and make provision for the recovery of these costs in the notified prices.

Ergon Energy Retail recommends that the QCA determine a separate regulatory allowance which enables retailers to recover the costs of regulatory reforms incorporated in AEMO's Regulatory Implementation Roadmap, noting these reforms are focussed on initiatives with material IT system implementation impacts, and other key/strategic reforms which are driving retailer systems investment and compliance costs.

Ergon Energy Retail recommends a more frequent Retail Costs Review than it has previously employed. We again recommend that the QCA adopt a maximum of three years between reviews (i.e. a new retail cost allowance baseline to commence from 1 July 2024 at the latest) given the significant upcoming regulatory reforms and rapidly changing electricity market.

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[5] Ibid., p. 50

[6] Note the retail cost component of notified prices is based on 2020-21 market retail costs escalated by inflation each year.

New Pricing Matters

Ergon Energy Retail welcomes the QCA's draft decision to rationalise the existing retail tariffs, and agrees with the proposed removal of the residential and small business seasonal retail tariffs (tariffs 12A, 14, 22A and 24) and the small business demand tariff 41 from 30 June 2023. This transition period enables retailers to work with impacted customers over the coming twelve months to explore alternative retail tariffs which suit the customer's needs. Ergon Energy Retail also supports the expiry of small business retail tariff 20A on 1 July 2022 as no customers have adopted this tariff, and notes the QCA's guidance around the large business seasonal demand tariff 50. While we acknowledge this important first step towards rationalising the retail tariff suite, we remain committed to further rationalisation in the coming years.

Ergon Energy Retail acknowledges the research and analysis the QCA has progressed on exploring tariff structures for electric vehicles (EV). We appreciate that determining the optimal EV tariff structure is an extensive piece of work best conducted outside the annual price setting process. Ergon Energy Retail supports the Queensland Government's *Zero Emission Vehicle Strategy 2022-2032* position that customers should make informed and cost effective decisions about when and how they charge their vehicles[7]. We consider that EV tariffs should reflect actual costs of supply in the same manner as petrol and diesel prices reflect market prices and conditions. Retail tariffs for EV charging must therefore incentivise customers to charge at times of low wholesale prices and low demand on the network. However, where a customer elects to charge an EV during a peak period (that is, between 4pm and 9pm), then the customer should pay the actual wholesale and network costs aligned to this time period. Consequently, in our view, this would be best achieved through a non-flat retail tariff.

Further, Ergon Energy Retail supports the Queensland Government position that solar charging of EVs is an excellent opportunity to benefit from Queensland's solar resources while providing network and wholesale benefits, and reducing emissions[8]. Solar charging can be incentivised through a 'solar soaker' retail tariff. This is best achieved via a time-varying wholesale energy component, which would result in cheaper daytime electricity driven by surplus solar generation, delivering benefits to all consumers, especially those without the means to install solar photovoltaic systems. Ergon Energy Retail supports the QCA continuing to explore how it could determine wholesale energy costs in a more cost-reflective manner. A starting point is whether the methodology the QCA used to determine the former time-varying feed-in tariff could be applied to retail tariffs (EV and existing notified prices).

Ergon Energy Retail notes that in the longer term EV pricing will move to dynamic pricing in aggregated Virtual Power Plant (VPP) arrangements where EV owners will receive benefits for the energy storage capacity of their vehicles. These potential future arrangements will be unsuited to regulatory pricing.

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[7] Queensland Government, *Queensland's Zero Emission Vehicle strategy 2022-2032*, p. 38
[8] Ibid., p. 39

Clarifications

Inflation

To clarify the statement in Ergon Energy Retail's response to the QCA Interim Consultation Paper 2022-23, Ergon Energy Retail did not suggest a change in how the QCA determines the inflation rate for use in its determination but was simply noting the level of inflation experienced in Queensland during 2021. Ergon Energy Retail supports the escalation of the retail cost component to account for inflation.

Electric Vehicle Tariffs

In the QCA's Draft Determination 2022-23 (p.16) the QCA referenced a view stated in the *Network Electric Vehicles Tactical Plan: Summary* document published by Ergon Energy Network and Energex. However, this view was incorrectly attributed to Energy Queensland, noting that Energy Queensland did not make a stakeholder submission to the QCA's Interim Consultation Paper 2022-23.

Ergon Energy Retail would welcome the opportunity to discuss these matters further with the QCA. Should the QCA require additional information in relation to any aspect of this submission, please contact Andrea Wold, Manager Retail Policy, Compliance and Assurance on 0428 384 448.

Yours sincerely

Ayesha Razzaq
Executive General Manager Retail