24 April 2012

Mr John Hall
Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001

Email: electricity@qca.org.au

Dear Mr Hall

Re: Draft Determination - Regulated Retail Electricity Prices 2012/13

MSF Sugar Ltd appreciates the opportunity to provide this further submission with comments on the Draft Determination Paper dated March 2012. We also support the submission from the Australian Sugar Milling Council.

Context

MSF Sugar Limited (MSF) is an integrated grower, processor, marketer and exporter of raw sugar. Now based at Gordonvale just south of Cairns in Far North Queensland, our 4 major production assets are located in this region (3 sugar mills) and at Maryborough in the Fraser Coast region (1 sugar mill). Our product is exported to Asia and must remain cost competitive.

MSF's production processes are highly dependent on having access to competitively priced electricity, which is sourced internally by producing renewable energy from bagasse (a bi-product of our sugar production), and by importing electricity from the grid. We also export significant volumes of renewable energy to the grid during the crushing season from June to November.

Overview

MSF notes that central aspects of the draft determination are materially different to (a) the Direction Notice issued by the Minister of Finance and Acting Treasurer on 11 May 2011 in accordance with the Queensland Competition Authority Act, (b) the Delegation dated 22 September 2011 to determine notified prices in accordance with the Electricity Act, and (c) various papers issued by QCA during the consultation process, including the Issues Paper and the Draft Methodology Paper.

We are particularly concerned that significant changes in the approach compared to the Draft Methodology Paper appear to be inconsistent with clear directions provided by the Minister in the Direction Notice and the Delegation referred to above.

The draft determination in its current form will result in significant cost increases for large energy users across Ergon Energy's distribution area (ie. businesses with annual usage between 100 MWh and 4 GWh). Specifically for MSF's sugar milling operations, we estimate the cost increase to be in the order of 135% or $1.35 million per annum. The cost increase for the most affected site is more than 600%.

We further note that the draft determination to apply Ergon Energy's higher network charges for large customers has been adopted by the QCA, solely on the recommendation of Ergon Energy, despite the company expressing doubts about readiness and the impact on Government policy. We note that none of the leading energy retail companies in Australia such as AGL, TRUenergy or Origin Energy raised issues with the approach outlined in the Draft Methodology Paper. We also fail to see how the recommendation and draft determination are adequately supported by sound reasoning.

Key Issues

We have chosen to limit this submission to the two key issues that combined result in a very significant cost increase and therefore competitive disadvantage for MSF. These key issues are:

1. The draft determination applies Ergon Energy's very high network charges to the regulated retail tariffs for large energy users, rather than the significantly lower Energex network charges that the QCA was directed by the Minister to apply.
2. The draft determination will no longer allow large energy users with annual consumption between 100 MWh and 4 GWh to access Tariff 22.

Electricity imports from MSF's four sugar mills are currently billed on Tariff 22, and the impact of being transferred to Tariff 54 (as advised verbally by Ergon Energy)[1] is set out in the table below:

Table 1: Summary of Annual Costs and Electricity Usage

	Mulgrave	Sth Johnstone	Tableland	Maryborough	Total
Annual Imports 2011 (MWh)	2,021	2,324	447	648	5,440
Tariff 22 for 2011/12					
Annual Cost	$372,689	$424,619	$85,516	$123,851	$1,006,675
Cost in $ / MWh	$184.44	$182.73	$191.30	$191.04	$185.06
Proposed Tariff 54 for 2012/13					
Annual Cost	$589,160	$681,802	$627,442	$462,412	$2,360,817
Cost in $ / MWh	$291.57	$182.73	$1,403.62	$713.27	$434.00
Change Compared to Current Cost	58.1%	60.6%	633.7%	273.4%	134.5%
Difference to Ministerial Direction	73.6%	76.6%	129.5%	127.1%	96.3%

[1] MSF will need further time to consider if this is an appropriate tariff, given that the National Electricity Rules state that "A Distribution Network Service Provider must not charge a Distribution Network User distribution use of system charges for the export of electricity generated by the user into the distribution network".
Given that MSF's export capacity exceeds our requirement for imports, it seems intuitively wrong to charge for demand and capacity on imports. In other words, if the network is required to establish assets to enable export of electricity from the sugar mill, it may not be appropriate to apply demand charges for the very same capacity.

Table 1 shows that the current average cost for the 4 mills is about $185 / MWh which we believe is significantly more than electricity prices paid by most Industrial & Commercial business customers in South East Queensland, NSW and Victoria.

The "Proposed Tariff 54" shows costs for each mill in accordance with tariffs in the draft determination, with an estimated increase of 135% compared to the current year. The costs at Tableland and Maryborough respectively of $1,404 / MWh and $713 / MWh illustrate how analysis based on high level assumptions of average usage and demand will not capture perverse outcomes at the granular level. In this example, the extreme increase in costs is caused by Ergon Energy's very high fixed charges and capacity charges.

We have also estimated costs for 2012/13 based on an "Intended Tariff 54" (ie. by applying Energex network charges in accordance with the Ministerial Direction) and the new Tariff 22. Both these scenarios produce outcomes that are in line with QCA's approach in the Draft Methodology Paper (refer details in Appendix A).

We estimate that the total cost under the "Proposed Tariff 54" is <u>96% higher</u> than costs under the "Intended Tariff 54" directed by the Minister.

<u>Discussion of Issue 1 – Network Tariffs</u>

This draft determination could make large energy users in Queensland question the regulatory process, especially since the above mentioned Direction Notice and Delegation could not be any clearer:

> *Direction Notice - 1.1 The N component*
> *Network costs should be treated as a pass through to customers. The N cost component of each tariff should be equal to the approved ENERGEX network price for the relevant tariff year.*
>
> *Delegation – Network Costs*
> *In determining the network cost component of each regulated retail tariff, the Authority must consider the network charges to be levied by ENERGEX for each tariff for the relevant tariff year.*

We note that QCA has adopted this recommended approach for residential and small customers, but not for large energy users. This is a glaring inconsistency which, if implemented, will cause significant pain for farmers and food processing companies in Central and North Queensland at a time when many of these businesses are still trying to recover from weather related events in the previous 2 years.

QCA has noted the inconsistency in its discussion in paragraph 1 on page 12 of the Draft Determination Paper. QCA then states:

> *However, the Government's decision to not allow large customers in the Energex network area to access notified prices <u>does give cause for thought</u> on whether, while ever this policy stance is maintained, it would be more appropriate to set large customer tariffs (for the State) based on Ergon Energy's network charges.*

> *In these circumstances, <u>there are arguments</u> to support basing regulated retail tariffs for large customers on either the Energex or Ergon Energy network tariffs and charges.* [2]

QCA provides no further reasons to substantiate why it is fair and reasonable to go against the Direction Notice and Delegation. MSF is of the firm view that this vaguely worded paragraph does not provide a valid reason to award significant price increases to large energy users. The difference in network charges alone is more than <u>$1.1 million per annum</u> for MSF.

Furthermore, we believe that there are obvious reasons why large customers in the Energex network area will not (and should not) have access to notified prices, because these customers are similar to Industrial & Commercial customers in NSW and Victoria that no longer have access to regulated retail prices. The simple explanation is that all regulated tariffs are intended to be phased out over time when there is sufficient competition in the market. This is the sign of the successful implementation of a competitive retail market and there is no longer a need to provide a safety net for customers.

The situation in Ergon's network area is obviously very different because there is no competition and Ergon Energy is effectively a monopoly supplier. Notified prices are required to ensure a safety net for all customers (ie. residential and business), consistent with the prevailing Community Service Obligations in Queensland. The Delegation from the Minister of Finance and Acting Treasurer sets out the method for determining these prices.

<u>Discussion of Issue 2 – Access to Tariff 22</u>

Although the concept of a dedicated set of tariffs for large customers was only introduced late in the process, the Draft Determination Paper does not discuss why MSF and other sugar milling companies can no longer access Tariff 22 or a similar tariff, and/or explain why this change will take place with immediate effect.

We have, however, observed submissions by energy users, such as the submission from Canegrowers dated 9 December 2011, which urges the QCA to consider an approach that allows customers to adjust to a new regime over a period of time. MSF agrees with this sentiment and we suggest that a transition period is relevant for all customers that are negatively impacted by the removal of tariffs and/or non-eligibility to existing tariffs.

However, as illustrated by the potential cost increase for the Tableland Mill, even the most generous transition period may not be enough to correct the underlying problem related to the proposed network charges.

<u>Concluding Remarks</u>

MSF notes that the short response time of only 2 weeks for the Draft Determination Paper has made it difficult to examine the full impact of changes from the Draft Methodology. For example, further investigation may find that Tariff 54 is not appropriate for sugar mills.

We acknowledge that pricing issues in the Queensland electricity market are complex and that significant obstacles must be overcome in order to create an efficient market. We concur that the guidance provided by the Minister is an important step in the right direction for

[2] MSF has underlined the key arguments provided by QCA

Queensland, provided that it is implemented in a consistent form for all customer segments and in accordance with its stated intentions.

I would welcome the opportunity to discuss further any of the issues raised in this submission and stress the importance of these policy decisions on our business. My contact number is 0401 896 999.

Yours sincerely,

[redacted]

Mike Barry
Chief Executive Officer

APPENDIX A

Table 2: Details of Annual Costs and Electricity Usage

Summary of Cost and Usage	Mulgrave	Sth Johnstone	Tableland	Maryborough	Total
Annual Imports 2011 (MWh)	2,021	2,324	447	648	5,440
<u>Tariff 22 for 2011/12</u>					
Annual Cost	$372,689	$424,619	$85,516	$123,851	$1,006,675
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Difference to Ministerial Direction	73.6%	76.6%	129.5%	127.1%	96.3%
<u>Intended Tariff 54 for 2012/13</u>					
Annual Cost	$339,449	$386,034	$273,377	$203,639	$1,202,499
Cost in $ / MWh	$167.99	$166.13	$611.56	$314.11	$221.06
Change Compared to Current Cost	-8.9%	-9.1%	219.7%	64.4%	19.5%
<u>New Tariff 22 for 2012/13</u>					
Annual Cost	$384,731	$442,380	$85,832	$124,299	$1,037,242
Cost in $ / MWh	$190.40	$190.37	$192.01	$191.73	$190.68
Change Compared to Current Cost	3.2%	4.2%	0.4%	0.4%	3.0%

Note:
Annual costs are based on the assumption that Tariff 54 will charge for the required demand and capacity for imports, rather than the available capacity for exports. However, there may be an argument to suggest that both demand and capacity should be set to zero when exports of electricity exceed imports (as is the case for all sugar mills) in Australia. This is a particular issue that needs further investigation.