Submission to the Queensland Competition Authority

Interim Consultation Paper
Regulated Retail Electricity Prices 2015-16

October 2014

ERGON ENERGY

RETAIL

BACKGROUND

Ergon Energy Queensland Pty Ltd (Ergon Energy Retail) welcomes the opportunity to provide comment on the Queensland Competition Authority's (QCA) Interim Consultation Paper on Regulated Retail Electricity Prices for 2015-16.

Ergon Energy Retail is a proud Queensland company that provides electricity to more than 700,000 homes and businesses and helps regional Queenslanders manage their energy consumption. With our roots firmly entrenched in regional Queensland, we have a team of people servicing regional Queensland customers from our contact centres and offices located in Townsville, Rockhampton, Maryborough and Brisbane. We also firmly believe in supporting our local communities by providing regional jobs and engaging in community partnerships such as the Royal Flying Doctor Service.

The future direction of our business is aligned with the State Government's PowerQ 30-year Strategy, which aims to improve customer value, market efficiency and governance effectiveness. We do acknowledge the increasing pressure electricity prices are placing on our customers' household budgets and businesses and believe the State Government's future direction will create a cost-competitive market.

We are supportive of the State Government's move towards creating a competitive electricity market in Queensland and will eagerly observe the removal of regulated prices in the South East Queensland market from 1 July 2015 and the subsequent outcomes.

Ergon Energy Retail is supportive of the QCA in exercising its authority under delegation from the Minister for Energy and Water Supply to set electricity prices in regional Queensland based on a Network plus Retail (N+R) methodology. We believe this is a transparent methodology and is the most appropriate approach to facilitate a transition to a competitive market while the Queensland Government reviews its Uniform Tariff Policy (UTP) and Community Service Obligation (CSO) policies.

We acknowledge the challenges that exist around the UTP with the removal of regulated prices in South East Queensland in 2015-16 and the State Government's future direction for the Queensland electricity market. We believe the requirements of the Delegation assist in ensuring that we remain on the pathway to achieving a competitive electricity market in regional Queensland.

In respect of the above, we believe a consistent approach to pricing needs to be applied to ensure we continue to transition along this path. We therefore support the QCA using the same methodology for pricing for 2015-16 as used in 2014-15.

Further, Ergon Energy Retail supports tariff options that enable customers to respond to price signals, empowering them to take control of their energy costs either by load shifting or reducing total consumption. This aligns with the Queensland Government's future strategy around ensuring consumer behaviour creates a responsive electricity market.

While not specifically raised in the Consultation Paper, consideration should also be given to how to deal with the change in treatment of metering charges being classified as Alternative Control Service charges from July 2015.

In the remainder of this submission, Ergon Energy Retail has provided direct responses to each of the questions raised by the QCA in its Interim Paper. We welcome the opportunity to discuss any aspects of this submission or to provide further information directly to the QCA. Ergon Energy Retail looks forward to reviewing and providing comment on the QCA's Draft Report on Regulated Retail Electricity Prices for 2015-16.

<u>Overall Approach</u>

2.1 We seek stakeholders' views on the following:

(a) For residential and small business customers, should we:

(i) **maintain the 2014-15 approach, which is to base notified prices on South East Queensland costs? Why or why not?**

<u>Response</u>

Ergon Energy Retail supports the approach of basing notified prices on South East Queensland costs for residential and small business customers. Affordability remains a key priority for Ergon Energy Retail and its customers, who continue to expect the electricity industry to operate in a manner that provides them with access to cost efficient electricity that meets their changing needs.

(ii) **keep notified prices at South East Queensland levels, but use Ergon Distribution's tariff structures for some or all tariffs? Why or why not?**

<u>Response</u>

Ergon Energy Retail supports using South East Queensland price levels as this is consistent with the State Government's UTP commitments and the terms of the Delegation. Ultimately however Ergon Energy Retail believes retail tariffs for regional Queensland should be based on Ergon Energy Corporation Limited's (Ergon Energy Distribution) Network tariff structures. This is to ensure appropriate price signals reach Ergon Energy Retail's customers and therefore the right level of investment is undertaken on their supporting network. This is an important stepping stone in improving customer value and market efficiency, as part of the PowerQ Strategy.

We recognise however the complexity of this approach and the evolution currently underway with respect to network tariff structures in both network businesses, which will require a process of transition from using Energex network tariff structures to using Ergon Energy Distribution network tariff structures.

As a first stage, as raised in the Delegation, this transition involves switching customers to Tariff 12 and Tariff 22 based on Ergon Energy Distribution's network tariff structures. While Ergon Energy Retail supports this approach from 2015-16, we note that it would require either a reprogramming of meters or complete replacement in order to reflect the seasonal time of use pricing.

Taking into consideration the number of customers on Tariff 22, it may be appropriate for the QCA to consider making Tariff 22 a short-term transitional tariff (e.g. for one-year) to ensure a smooth and orderly transition for customers. For example, customers could transition to the new Tariff 12 and Tariff 22 upon replacement of their electricity meter in accordance with Ergon Energy Distribution's replacement schedules.

(b) For large business customers, should we:

(i) **maintain the 2014-15 approach, which is to base notified prices on regional Queensland costs? Why or why not?**

<u>Response</u>

Ergon Energy Retail supports maintaining the 2014-15 approach in line with the Queensland Government's UTP of using East Transmission Zone 1 Network costs for large business customers. This is reflective of the overall move towards creating an efficient market, while providing an appropriate transition to more cost reflective tariffs.

Importantly, this approach remains appropriate while the Queensland Government remains committed to the UTP in its current form. We acknowledge the impacts this has on industry groups, such as agriculture, and we are working with them to help them manage their energy consumption and look for efficiencies in their farming practices.

<u>Network Costs and Structures</u>

3.1 We seek stakeholders' views on the following:

(a) Should we continue to use Energex's tariff structures as the basis for retail tariffs for residential and small business customers?

(b) Alternatively, should we use Ergon Distribution's tariff structures for some or all retail tariffs for residential and small business customers?

(c) Are there any other issues we should consider?

<u>Response</u>

Please see above comments outlined in 2.1.

Energy Costs

4.1 We seek stakeholders' views on the following: **(a) Is there any new information available to suggest alternative approaches to those used in the 2014-15 determination that might be more appropriate?**

Response

Ergon Energy Retail supports the approach used in the 2014-15 determination for wholesale energy costs to provide for investment certainty. We agree that Renewable Energy Target (RET) costs should be based on the legislated policy in place at the time of setting 2015-16 retail prices.

(b) What improvements could be made to the current approaches?

Response

We have noticed that the recent RET review and speculation on the future of the RET scheme has reduced liquidity in the Large-scale Generation Certificate (LGC) market. It has had a noticeable impact on prices for LGCs and therefore we caution that this may distort the output of modelling undertaken by QCA's consultants and impact the 2015-16 LRET allowance.

If the future of the RET schemes becomes clearer, particularly if a bipartisan position on the scheme emerges, there could be a step-change in the price of certificates. The price for an electricity retailer to acquire certificates to meet 2016 and 2017 surrender requirements could be very different to the previous two year's historical prices.

As a general comment, we would encourage the QCA to source the most up-to-date publicly available data to support any decisions in this area, and caution against using historical prices as a predictor of the compliance cost to retailers for the 2016 and 2017 surrender requirements. Due to the risk of the RET scheme being abolished, many retailers would have delayed purchasing LGCs beyond the February 2015 surrender requirements. Actual market prices, after the changes to the RET schemes are known, would be a much better indicator of actual compliance costs.

(c) Any there any other issues we should consider when estimating energy costs?

Response

We have no further comments at this point of time.

Retail Costs (ROC and CARC)

4.2 We seek stakeholders' views on the following: **(a) Are there are any compelling reasons why the benchmarking approach should not be used to estimate retail costs in 2015-16?**

Response

Ergon Energy Retail supports the QCA's proposal to continue with the benchmarking approach.

(b) What matters should we consider when deciding whether to include an allowance for CARC?

Response

Ergon Energy Retail believes that it is important to continue to provide the CARC allowance to avoid "price shock" when the price is deregulated (in alignment with current State Government policy direction and the PowerQ Strategy), or a network CSO is considered (as alluded to in the Strongest & Smartest Choice Plan). Its removal would distort the market and would make it more difficult to transition to an effective competitive market in regional Queensland. Removing an allowance for CARC would also result in regional Queensland being out of alignment with South East Queensland where the CARC is accounted for in prices, thereby also deviating from the intent of the UTP.

(c) Are there any other issues we should consider when estimating retail costs?

Response

Affordability remains a key priority for Ergon Energy Retail and its customers and therefore we urge the QCA to continue to consider regional Queensland customers in the same light as their South East Queensland counterparts. We believe the QCA should retain the current methodology for estimating retail costs for 2015-16.

Competition and Headroom

5.1 We seek stakeholders' views on the following: **(a) Should headroom continue to be included in notified prices for residential and small business customers? Why or why not?** **(b) Should headroom continue to be included in notified prices for large business customers? If so, at what level? If not, why not?**

Response

Ergon Energy Retail acknowledges that in making its determination, the QCA is required under the *Queensland Electricity Act 1994* to consider competition and National Competition Policy requirements when making determinations.

We support the retention of the headroom allowance as it remains a key component of retail tariff pricing and allows a competitive market in Queensland to develop (as per the PowerQ Strategy).

Further, it is important to continue to provide the headroom allowance to avoid "price shock" when the price is deregulated (in alignment with current State Government policy direction and the PowerQ Strategy), or a network CSO is considered (as alluded to in the Strongest & Smartest Choice Plan). Its removal would distort the market and make it more difficult to transition to an effective competitive market in regional Queensland.

(c) What other issues should we consider in relation to competition and headroom?

Response

As noted above, Ergon Energy Retail supports the ongoing CSO reform process, which will remove a key blockage to introducing effective competition in regional Queensland. Effective competition will provide customers with a cost-competitive electricity market in Queensland and provide for improved market efficiency. However, the complexity of the issues which must be addressed to give effect to the CSO and competition reform mean that an appropriate transition timeframe is required to ensure that industry and customer impacts are managed.

Cost Pass Through Mechanism

5.2 We seek stakeholders' views on whether a cost pass-through mechanism should be included when setting notified prices for 2015–16.

Response

Ergon Energy Retail acknowledges that a one-year derogation provides limitations on QCA's ability to provide meaningful pass-through mechanisms. We believe the issue that will be most affected by this is the setting of the RET costs. As previously noted, we believe the QCA is best placed to follow policy decisions at the time of decision, while taking into consideration publicly available data. In the absence of the ability to apply a pass-through mechanism, we believe an appropriate risk allowance should be maintained to allow for risk events.

Removal of Tariff 13 and 41

5.3 We seek stakeholders' views on whether tariffs 13 and 41 should be removed from the tariff schedule.

Response

Ergon Energy Retail has one customer on Tariff 13 and does not envisage that the removal of this tariff would significantly impact that customer. We will support the QCA's final decision and will support the customer in selecting and moving to an appropriate tariff alternative.

We do however have a number of customers on Tariff 41. Our initial analysis on current tariffs and structures indicates that moving these customers to an optimised alternate tariff, being Tariff 22 in most cases, would leave half of them materially worse-off. As Tariff 22 is also currently subject to review, it may be prudent to maintain Tariff 41 until customers have greater clarity after the pricing and structure of Tariff 22 is finalised.

We urge the QCA to consider this in their deliberations. If a decision is made to remove the tariff, we will work directly with impacted customers to transition them to an appropriate tariff and help those negatively impacted to look at options for efficiencies in their energy consumption.

Fixed and Variable Charges for Tariff 11

5.4 We seek stakeholders' views on the following:

(a) What issues should we take into account when deciding whether to complete the rebalancing of Tariff 11 using the approach established in the 2013-14 determination?

Response

In order for customers to make informed choices, Ergon Energy Retail believes it is appropriate for the QCA to complete the three-year transition process that it has undertaken to rebalance the fixed and variable changes for Tariff 11. This is consistent with the UTP and the Delegation.

Transitional and Obsolete Tariffs

5.5 We seek stakeholders' views on the following:

(a) Is there any new information that suggests the overall approach we propose to take for transitional and obsolete tariffs is no longer appropriate?

(b) What other issues should we should consider (please provide supporting evidence where possible)?

Response

Ergon Energy Retail supports the continuation of the current approach taken by QCA on the basis that the current transitional price path provides certainty for customers, retailers and the network in making long-term decisions in regards to investment, tariff development and optimisation of energy consumption. It also provides consistency with respect to the fact that the QCA has a one-year delegation.