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Professor Roy Green
Chairman
Queensland Competition Authority
Level 27, 145 Ann Street
Brisbane, QLD, 4000

*By email:* electricity@qca.org.au

Dear Professor Green,

## CANEGROWERS submission to QCA Regulated Retail Price Determination 2017-18

Thank you for the opportunity to make a submission to QCA's regulated retail electricity price determination review for 2017-18.

CANEGROWERS has worked closely with QCA, AER, DEWS, Ergon and has engaged expert advice to understand the regulatory pricing framework and the factors driving electricity prices unsustainably higher across Queensland, particularly in Ergon's distribution network. Our objective is to ensure electricity prices are set in a way that provides performance incentives for all in the electricity supply chain to efficiently and effectively deliver electricity to all customers.

### Delegation

CANEGROWERS is aware of the constraints imposed on the QCA price determination process by the government delegation. Under the network (N) plus retail (R) cost build-up methodology when determining notified prices for 2017-18, QCA treats the N costs as a pass-through. The R costs (energy and retail costs) are determined by QCA.

The delegation also requires QCA to take account of the Queensland Government's Uniform Tariff Policy (UTP) so that, wherever possible, small standard retail contract customers and large non-market customers of the same class should pay no more for their electricity, regardless of their geographic location.

The delegation does not mean that Ergon's customers should pay more than the most competitive market prices available to consumers using the Energex network in south-east Queensland.

### Energex prices

The Queensland Government's decision to deregulate electricity prices in south-east Queensland is aimed at stimulating competition among retailers with respect to prices, products and services.

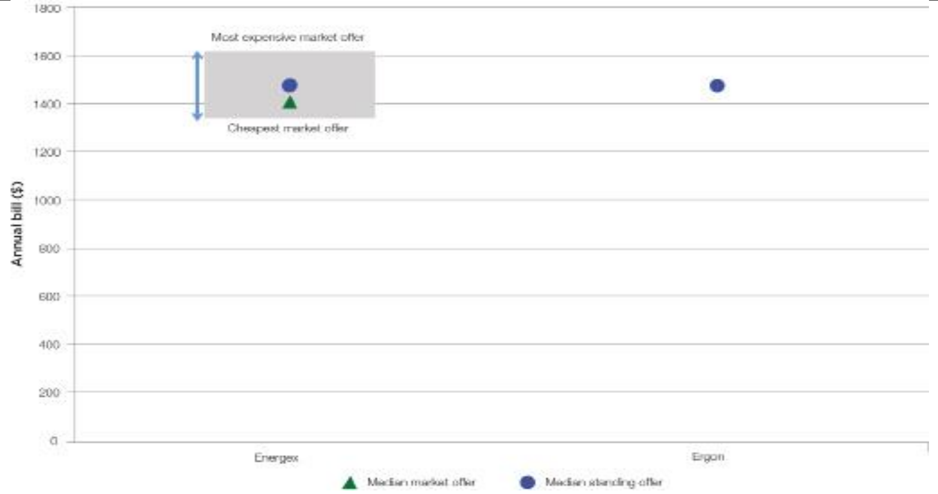
While the price effects of this competition are not yet fully apparent, in its latest (2015-16) annual report on the performance of the retail energy market the AER[1] notes there is already a range of prices on offer from 15 electricity retailers in south-east Queensland. AER reports the annual electricity bills for these offers ranged from $1340 to $1615, showing a potential

[1] AER (2016), Annual Report on the Performance of the Retail Energy Market, 2015–16,

savings to customers who shop around. The annual electricity bill for the median market offer was $1401, which was $69 less than the median standing offer (figure 1).

At the lower standing offer prices, the most competitive retailers are covering their costs of providing electricity to consumers. This suggests other retailers, charging higher prices including those with median standing offerings, are either high cost operators or are enjoying super normal profits.

**1. Range of generally available electricity offers by Queensland distribution zone (4100 kWh) – June 2016**




*Source:* AER (2016), figure 3.3

A price competitive market is characterised by price convergence over time. This is not the case in Australia's retail electricity market. There is already a range of retail prices available to consumers in south-east Queensland. The range is wider in other states which have deregulated retail electricity prices and widest in Victoria state where the electricity market has been deregulated for some time (AER 2016). The evidence is clear. The retail electricity market in Australia is not a price competitive market.

Because the median price in south-east Queensland is higher than the most competitive market price, if QCA sets prices for Ergon's customers at the median price available to customers in the Energex network, Ergon's customers will be paying higher prices for electricity than would be available in a competitive market.

The QCA process of estimating prices in regional Queensland on a cost-plus basis (including an allowance for head room on retail margins) without sufficient consideration of the efficiency dividend demanded in competitive markets on costs and margins results in a price outcome that clearly protects the interests of the monopoly retailer in regional Queensland at the expense of regional consumers.

The Finkel[2] report identifies the benefit of a transparent price setting environment:

- "Transparency is important for the efficient operation of all markets"
- This will support the security and reliability of electricity supply and minimise the impact on electricity prices.

***CANEGROWERS urges QCA to set retail prices in Ergon's regional Queensland network at levels equivalent to the most competitive retail price offerings in South-East Queensland. There is no justification for an alternative approach.***

[2] Finkel, Moses, Munro, Effeney and O'Kane (2016), Preliminary report of the independent review into the future security of the national electricity market, December.

One consequence of setting prices in regional Queensland higher than competitive market prices is that the Queensland Government's Community Service Obligation (CSO) payment to Ergon to support the UTP will be lower than otherwise would be the case. The delegation makes no reference to the QCA making a trade-off between the level of prices in regional Queensland and the size of the consequent CSO.

**Errors in Ergon's 2016 Tariff Structure Statement**

In August, the Australian Energy Regulator (AER), gave provisional approval to Ergon's Tariff Structure Statement (ETSS). CANEGROWERS is concerned that the network tariff structure proposed by Ergon is not cost reflective and is inconsistent with the National Electricity Rules (NER), as amended by the Australian Energy Market Commission in 2014.

CANEGROWERS, again engaging the electricity market expertise of SRG, has raised its concerns that many of the conclusions contained in the AER draft decision are contradicted by the publicly available evidence provided in Ergon's 2016 Distribution Annual Planning Report (DAPR). Ninety-eight per cent of Ergon's the low voltage network has enough spare capacity to meet all forecast peak demand growth for the foreseeable future. SRG demonstrates that Ergon's TSS overstates the level of congestion on its network by two orders of magnitude (a factor of approximately 375) (SRG report attached). The scale of this pricing distortion is $1.8 billion over five years.

CANEGROWERS is working with AER as it revisits its draft decision to accept Ergon's TSS.

The ETSS is not cost reflective, CANEGROWERS is concerned that using the associated tariff structures "to strengthen or enhance underlying network price signals" as required by section 5(d)(ii) of Delegation will exacerbate the pricing problems in regional Queensland.

SRG advises that the AER appears to have used approaches and methodologies similar to those it applied in reviewing the ETSS in reviewing other distributor's tariff structure statements. This also appears to be the case for the AER's draft decision on the Energex TSS. Simply put, the Energex N that QCA is required to pass through in setting Ergon's retail tariffs is too high. When combined with Ergon's proposed tariff structure customers who use most of their power over the summer period, home owners, irrigators and businesses will be penalised.

There are very significant questions over the rules and design of the National Electricity Market. Finkel notes that the existing rules and design are simply not up to the task. CANEGROWERS is concerned that the present rules are being applied in a way that protects the interests of Ergon at the expense of its regional consumers.

***CANEGROWERS concern is that the underlying cost basis generated from the flawed N+R methodology is simply too high as are the resulting prices. The theoretically calculated "cost reflective" prices are significantly higher than the "actual" cost of supplying electricity.***

**Ergon's load profile**

CANEGROWERS urges QCA to base its energy charges on Ergon's load profile rather than the Energex load profile. With a flatter load profile and fewer peaks than the Energex load profile Ergon is expected to be able to source energy at a lower cost than Energex. Consumers in regional Queensland should receive the benefit of this more attractive energy use profile.

***CANEGROWERS recommends QCA uses Ergon's load profile rather than the Energex load profile when determining the energy component of charges in the Ergon network.***

**Transitional and Obsolete tariffs**

At no time since the introduction of the N+R pricing framework has QCA provided any information on the size of the notional gap between the irrigation tariffs T62, T65 and T66 and so called cost reflective tariffs. That the historic irrigation tariffs are not based on the N+R pricing framework does not mean that the tariffs do not cover the actual costs of supplying electricity to irrigators.

With irrigation tariffs more than doubling over the eight years to 2015-16, Ergon's revenue take from these tariffs is likely to have increased sharply over the same period. This is a significant increase considering Ergon's network investment decisions over the period have been driven by its over estimates of the needs of its urban and industrial users and future consumption increases are driven by the LNG industry, not by the needs of irrigated agriculture.

***QCA has provided no valid justification for increasing irrigation tariffs at a faster rate than other electricity tariffs.***

The QCA's past pricing decisions have resulted in a significant transfer of wealth from those using transitional tariffs to Ergon.

**Conclusion**

Not taking account of customer load profiles or the impact of disruptive technologies, regulated retail electricity prices in regional Queensland are encouraging consumers to seek alternative energy sources, accelerating the onset of disruptive alternative energy technologies and discouraging regional economic activity. The distorted tariffs resulting from the QCA retail price determination process for regional Queensland are undermining public confidence in the integrity of the process.

CANEGROWERS supports cost reflective pricing. The evidence suggests, that some electricity prices in regional Queensland are higher than the actual costs of supplying electricity and are inconsistent with the Queensland Government's UTP.

CANEGROWERS calls on the QCA to respond to the points raised in this submission and ensure retail electricity prices in regional Queensland prices are set in a way that provides performance incentives for all in the electricity supply chain to efficiently and effectively deliver electricity to all customers, including irrigators.

Yours faithfully

Dan Galligan
Chief Executive Officer

**Attachments**

1. SRG report prepared for CANEGROWERS, "Errors in Australian Energy Regulator's Draft Decision on Ergon Energy's 2016 Tariff Structure Statement" (November 2016).