



# Submission to the Queensland Productivity Commission Draft Report on Electricity Pricing

*11 March 2016*

Submission on behalf of:

**QCOSS**  
Queensland Council  
of Social Service

**CCIQ** Powering  
business  
potential

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# 1 Introduction

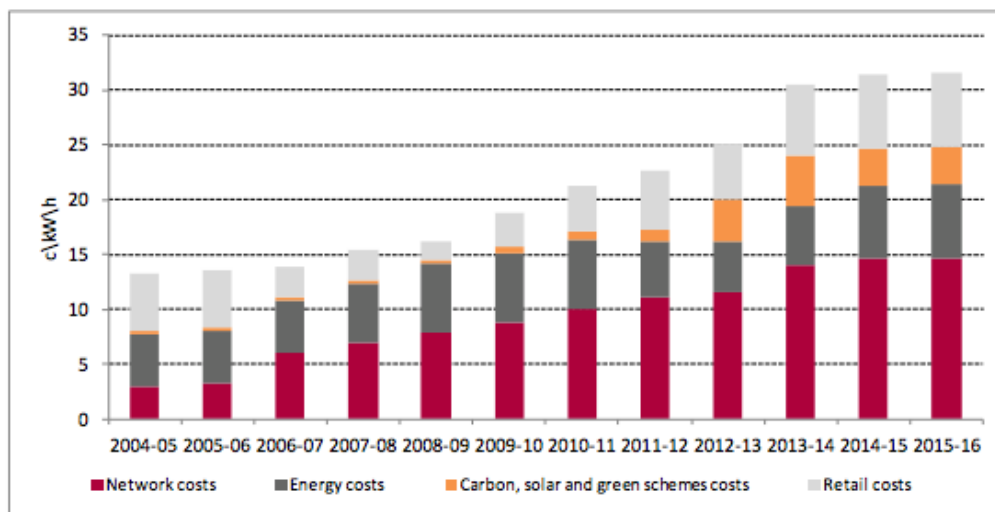
We welcome the opportunity to make this submission to the Queensland Productivity Commission (QPC) Draft Report on the Electricity Pricing Inquiry. This submission represents the diverse interests of Queensland's residential and small business energy consumers. The parties to this submission share a common focus on positive outcomes for residential and small businesses in the Queensland energy market. Below is a summary of the organisations who have contributed to this submission.

*The Queensland Council of Social Service (QCOSS) is the state-wide peak body for individuals and organisations working in the social and community service sector. For more than 50 years, QCOSS has been a leading force for social change to build social and economic wellbeing for all. Our mission is to eliminate poverty and disadvantage in Queensland.*

*The Chamber of Commerce and Industry Queensland (CCIQ) is the peak industry body in Queensland, representing 25,000 small business members. CCIQ advocates on behalf of its members to influence government policy to keep public debate focussed on business issues. Small businesses make up 97 per cent of all businesses in Queensland. There are approximately 412,000 small businesses in operation employing over 1 million Queenslanders.*

Our organisations have strong reach through our memberships and networks across the state. We view the impact of high electricity prices through the lens of residential and small business consumers across Queensland. Through this work, we are familiar with the symptoms of these high prices, including escalating financial hardship for households and limited competitiveness and growth of Queensland businesses. The flow-on impacts of this are difficult to capture and quantify, however we have previously provided information about these impacts in submissions to the QPC's Issues Paper.

For this submission, rather than focusing on the well-established impacts of these high prices on consumers, we instead focus on the causes of these high electricity prices in Queensland over recent years, the likely drivers into the future, and measures to reduce prices. We focus on the aspects of the Queensland electricity supply chain that have the most significant impacts on Queensland's electricity prices, and those that affect both small business and residential consumers alike. These drivers can be seen across the supply chain and thus we have included sections addressing the generation, network and retail sectors.



Source: Department of Energy and Water Supply

The chart above (from the QPC's Issues Paper) illustrates the trends in the breakdown of Queensland's residential electricity prices over the past 11 years. It illustrates that Queensland's electricity price rises over the past decade have been predominantly driven by increases in network charges, which account for around 95 per cent of the total electricity price increases during this period.

As a result, network charges now account for over half of Queensland's retail electricity prices. With increases in network charges being the primary driver of Queensland's price increases, this submission has a strong focus on the key drivers of the prices and productivity of Queensland's electricity networks. We believe this is an area which needs to be more strongly addressed by the QPC in the Final Report.

Generation costs account for around 20 per cent of electricity prices. While wholesale prices have remained relatively stable in the past, the QPC's projections indicate a 52 per cent increase in Queensland's wholesale prices in the next 20 years. Clearly this must also be a strong focus for the QPC in its Final Report.

Retail costs also account for around 20 per cent of Queensland's electricity prices. The retail markets of South East Queensland (SEQ) and regional Queensland are very different and the issues wide-ranging. Thus, in this submission we have focused our attention on price deregulation in SEQ as the most imminent reform in the retail market in Queensland at this time.

Given the limited resources of non-profit consumer organisations and the relatively short period for consultation, we have not explored these issues as comprehensively as might otherwise be possible. However, we trust that the QPC will undertake its own independent and thorough investigations into the issues presented in this submission, in the interests of Queensland consumers. It is important that consumers have a strong voice in this inquiry as it has the potential to shape broader social and economic outcomes for households and businesses across the state.

We thank the QPC in advance for its careful consideration of this submission.

## 2 Generation

### 2.1 Overview

This section addresses *Chapter 3: Generation* of the QPC's Draft Report (pp37-61).

The QPC's Draft Report confirms that Queensland's annual average wholesale costs for 2014-15 were the highest in the National Electricity Market (NEM).<sup>1</sup> The QPC has also forecast significant increases in wholesale prices in Queensland of 52 per cent in real terms over the next 20 years.<sup>2</sup> According to the QPC's modelling, it is clear that the wholesale market is going to be a key driver of electricity prices in Queensland in the future, and should therefore be a key area of focus for the QPC in its Final Report.

Wholesale prices in Queensland are the highest in the NEM despite the fact that the QPC has found that the Queensland wholesale market is characterised by surplus generation<sup>3</sup>, efficient generation assets and relatively low fuel costs when compared with other states. It is concerning that these benefits are not being translated into lower prices for consumers.

There are a number of issues facing the wholesale market, including falling average demand, increased volatility and falling demand in the middle of the day due to increasing penetration of rooftop solar, and rising gas prices potentially reducing the competitiveness of gas fired generation in the future.

While we note that these issues are not unique to Queensland, the structure of the generation market in Queensland does lend itself to the potential for greater detrimental effects for consumers compared to other jurisdictions in the NEM.

The Queensland wholesale market is highly concentrated and this is an issue that will persist despite the Queensland Government's decision not to merge the two government owned generators, CS Energy and Stanwell. There is evidence that volatility is increasing in the Queensland market and there has been a significant increase in the number of trading periods where these generators have had market power. Should rising gas prices result in reduced availability of gas-fired generation, the market shares of generation will change quite significantly with further increases in Stanwell and CS Energy's ability to exercise market power.

We have concerns about the risk that the Queensland generators will continue to exercise market power to the detriment of consumers, not only through rebidding practices which the QPC has acknowledged in the Draft Report, but also through other market behaviours such as the use of ramp rates, economic withholding, tacit collusion and network congestion.

The Queensland market is also showing signs of increasing volatility, due to the exercise of market power and other factors such as intermittent generation. This has the potential for flow on impacts on retail competition, which is of particular concern

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<sup>1</sup> QPC Draft Report, p37

<sup>2</sup> QPC Draft Report, p2

<sup>3</sup> QPC Draft Report, p37

given the need for a vibrant retail market when price regulation is removed in SEQ from 1 July 2016. The QPC must focus its recommendations on measures to prevent volatility where it is caused by the generators' use of market structures and flexibility within the national rules to increase prices.

As the owner of these generation assets, the Queensland Government has a responsibility to ensure they are not operating in a way that has a negative impact on wholesale prices and retail competition, regardless of whether these activities are permitted under the national rules.

We note the QPC has indicated it will investigate wholesale market issues more comprehensively in the Final Report. We believe further investigation is essential to clearly identify the specific issues that are driving high wholesale prices in Queensland and make recommendations to address these risks in the future. We believe there is scope to strengthen the QPC's recommendations relating to the wholesale market in its Final Report.

### 2.1.1 Recommendations

We generally support the QPC's recommendations in the Draft Report in relation to the wholesale market, but consider that, in a number of cases, the recommendations could be strengthened.

These areas are highlighted as follows:

**Recommendation:** That the QPC explore the possible merits of creating a new generator from Stanwell and CS Energy to provide a third Queensland government owned generator to achieve an outcome where there are three similar sized generators operating in competition.

**Recommendation:** That the QPC expand Recommendations 7 and 8 on rebidding to include the other acts of abuse of market power such as the use of tacit collusion, economic withholding, bidding low ramp rates and network congestion by the generators to increase their revenues, and that the reporting explicitly requires that the generators provide advice on the impacts of these acts on the wholesale market.

**Recommendation:** That the QPC require the investigations into renewable generation be all encompassing of all price impacts on consumers including possible risks and costs associated with:

- the potential closures of thermal generation and any impacts on reliability and wholesale competition; and
- the impact on the financial viability of the Queensland owned generators and what actions the Queensland government should take regarding any early retirement of plant.



## 2.2 Emerging risks in the generation market

Since 2008, a number of new wholesale market risks have emerged in the NEM.

Firstly, the cost of gas used for electricity generation is rising to export parity levels. The impact of this is that some gas fired generators are selling the gas directly because this is more profitable than converting it to electricity and selling it in the NEM.<sup>4</sup> Others are finding that the cost of electricity from high priced gas makes their generation non-competitive and are leaving the market, reducing the potential sources of hedges for retailers. A number of gas fired generators have already been, or will shortly be, exposed to much higher gas prices and the incentive for these generators will be to either sell their gas rights (as has Stanwell for example) or to cease or severely limit generating due to the high costs involved (as GdF Suez in South Australia has). In Queensland, this could result in up to around 3000 MW of gas fired generation leaving the Queensland market (in addition to Swanbank E owned by Stanwell which has already been closed down).

Secondly, average demand for electricity has been falling since 2010 (with the exception of a step increase in demand in Queensland in 2015 mainly due to the one-off addition of LNG market impacting demand in both peak and off-peak times). This is due to a combination of factors including impacts from the global financial crisis and reduced energy consumption in response to rising prices and various government energy efficiency measures.

Additionally, there is also falling demand in the middle of the day, as a result of an increase in solar photovoltaic (PV) roof top installation, particularly in Queensland and South Australia. This trend is expected to continue to increase significantly due to the growth in penetration of rooftop solar that is forecast in Queensland. The amount of electricity effectively displacing generation in the middle of the day is impacting on the volume of electricity that is sourced from base load generation. This reduced volume reduces the ability of base load generators to cover their fixed costs which can lead to either increased prices (to cover fixed costs) or generator closures (which reduces competition).

## 2.3 Market concentration in Queensland

The NEM is predicated on there being sufficient competition in generation such that the prices generators offer deliver the most efficient outcome for consumers. Unfortunately, due in part to the legacy of vertically integrated government-owned electricity supply arrangements, some generators are so large that competition is significantly reduced.

In 2000, the generation now under Stanwell control provided some 60 per cent of the Queensland market and CS Energy around 40 per cent. While this has reduced over time, Queensland's electricity generation sector remains the most concentrated in the NEM, with Stanwell and CS Energy controlling 64 per cent of capacity.<sup>5</sup>

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<sup>4</sup> See <http://www.afr.com/business/energy/electricity/stanwell-shutters-qld-generator-to-sell-gas-instead-20140205-ixv1f>

<sup>5</sup> QPC Draft Report, p40

The QPC acknowledges that the increase in Queensland's wholesale market prices since 2010-11 may be related to a range of reasons, including "*mothballing of capacity at Tarong Power Station in 2012*" and "*greater market concentration following the restructuring of the Queensland gencos in 2011-12*".<sup>6</sup> Tarong became a wholly owned subsidiary of Stanwell in 2011.<sup>7</sup> Since this time, Queensland's wholesale prices have risen in average annual terms relative to other jurisdictions.<sup>8</sup> The ACCC has identified that the 2011 merger was "*negative for competition*".<sup>9</sup>

The QPC has noted it will consider market concentration issues further prior to the Final Report.<sup>10</sup>

While we support the QPC's recommendation not to merge CS Energy and Stanwell, we consider this does not go far enough to address the problems resulting from the high level of market concentration in Queensland. We consider that maintaining the current separation of Stanwell and CS Energy is not sufficient, particularly given growing demand and the risk that rising gas prices may reduce competition even further in the future.

We understand that the Queensland Government initially established three government owned generators (Stanwell, CS Energy and Tarong Energy) in order to provide competition in Queensland and thereby minimise the ability of any one of the three generators to have market power. We consider that the original three generator concept may have merit. To achieve this, Tarong would not necessarily have to be reconstituted as a separate generator – rather, a third government owned generator could be created from the current two, to form three similar-sized generators. Any additional operational costs would likely be outweighed by the benefits of increased competition in the wholesale market.

We therefore recommend that the QPC explore options for a new generation entity to be created from Stanwell and CS Energy to provide a third Queensland Government owned generator in the region and that the three generators be similar sized with a similar mix of generation types and be required to compete with each other.

## 2.4 The exercise of market power in Queensland

It is clear that Stanwell is the dominant generator in Queensland and it has the installed capacity to provide nearly 4000 MW of generation<sup>11</sup>. The combined capacities of all other generators in Queensland is just over 8000 MW.

With an actual recorded peak demand of 9097 MW recorded on 1 February 2016, it is clear that with some 8000 MW of regional generation (excluding Stanwell's notional generation capacity) coupled to an import limit of about 600 MW,<sup>12</sup> Stanwell

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<sup>6</sup> QPC Draft Report, p42

<sup>7</sup> QPC Draft Report, p41

<sup>8</sup> QPC Draft Report, p41

<sup>9</sup> QPC Draft Report, p43

<sup>10</sup> QPC Draft Report, p43

<sup>11</sup> This would include returning Tarong unit #2 into service. After closure of two units in 2012, one unit was reintroduced the following year and the second unit was forecast to return to service in 2015 although it has not yet to provided power into the grid

<sup>12</sup> Due to congestion in the NSW and Powerlink networks this import limit is frequently much lower than 600 MW



is in the position of having, at times, market power to set spot prices in Queensland because it must be dispatched in order to meet Queensland demand.

While in theory, the calculations might indicate that Stanwell has market power when the regional demand exceeds about 8600 MW, in practice, the trigger point for being able to exercise market power is significantly lower than this, because:

- Not all generation will be available at all times;
- Not all generators will be able to be dispatched to their maximum capacity; and
- The maximum capacity of the interconnectors might not be available for flows into Queensland.

However, even if we assume a trigger point of 8600 MW, we can see that, based on Queensland demand and the Queensland generation available excluding Stanwell, Stanwell would have had a number of periods when it had market power<sup>13</sup> in the past 10 years (in 2009, 2010, 2011, 2012 and 2015), but that these periods of having market power only occurred infrequently and usually for only around six or seven trading periods in the year.<sup>14</sup>

However in the first two months of 2016, Stanwell has already had clear market power for a total of 43 trading periods where the peak demand exceeded the 8600 MW trigger point. The clear conclusion is that even with the actual demand recorded in 2015-16 being lower than what was forecast, there has still been a massive increase in the number of trading periods when Stanwell had market power.

There is also an expectation that Stanwell will have market power more frequently in future years as AEMO is forecasting that peak demand in Queensland will rise significantly in future years (see below table).

**Table 1 Queensland summer 10% POE for operational maximum demand**

	2015 NEFR (MW)	2015 NEFR update (MW)
2014- 15	9,465	9,216
2015- 16	9,691	9,263
2016- 17	10,130	9,832
2017- 18	10,282	10,015
2018- 19	10,366	10,103
2019- 20	10,493	10,230
2020- 21	10,630	10,366
2021- 22	10,610	10,347
2022- 23	10,767	10,505
2023- 24	10,832	10,570

Source: AEMO NEFR 2015 update

Of further concern is that the above analysis is based on the assumption that all gas fired generation will be available for dispatch. Should rising gas prices result in

<sup>13</sup> It is noted that having market power is different to exercising that market power

<sup>14</sup> With the exception of 2009 and 2010 when there were 19 and 27 trading periods respectively when demand exceeded this trigger point

reduced availability of gas generation, the market shares of generation will change significantly with Stanwell further increasing its ability to exercise market power.

The new rules implemented by AEMC are untested.<sup>15</sup> However, under the rules, when there is the exercise of market power, the AER can only monitor its use and the market impacts. There is no ability for the AER to provide redress for consumers or to prevent it being repeated. We therefore agree with the QPC that intervention by the Queensland Government is warranted, above and beyond what is required under the National Rules.<sup>16</sup>

We support the QPC's Recommendation 7 to require the government owned generators develop a public Code of Conduct that acts to support consumer interests. We also support Recommendation 8 to impose a process of self-reporting to the shareholder on actions that the generators have taken related to the exercise of market power. We consider that both of these recommendations should not only highlight the activity related to rebidding, but should include any actions where the use of market power is abused. This should be reported on in detail to the shareholder, including an assessment of the impacts these acts have on the wholesale market.

Market power can be exercised in a number of ways to the detriment of consumers. While the QPC has focused its analysis and recommendations specifically on rebidding, we consider there is a strong need for the QPC to widen the scope of its investigation and recommendations to also consider the impact of:

- Volatility
- Economic withholding of capacity
- Tacit collusion
- Bidding of low ramp rates and
- Use of network congestion

We discuss each of these aspects further in this section.

### **2.4.1 Volatility**

Volatility risk is an important consideration for both retailers and generators in the wholesale market. Retailers face volume risk where their book build (what they sell to their customers) does not match the volumes they have contracted with generators. Generators face risk where they are not able to deliver to the hedges they have with retailers, or when the transmission system does not allow the generator to deliver its output. In these instances, the generator still has to notionally source the electricity from the market and will incur the cost of the market price at the time.<sup>17</sup>

These risks are priced into the cost of electricity by both generators and retailers so limiting volatility in the market reduces the risks (and hence costs) faced by retailers and generators.

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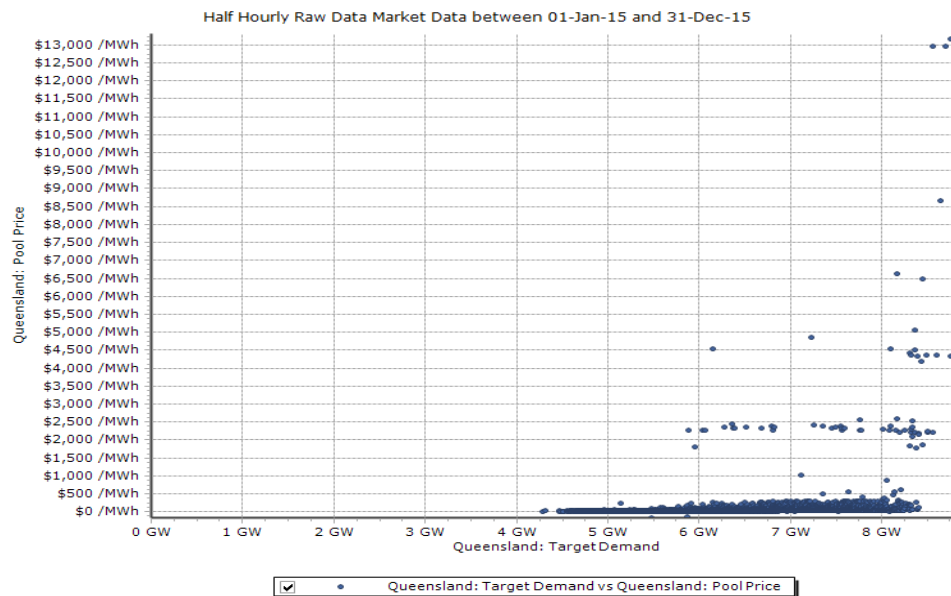
<sup>15</sup> The new provisions will take effect from 1 July 2016.

<sup>16</sup>QPC Draft Report, p50

<sup>17</sup> While the generator would make some savings through avoiding its short run costs, it has to effectively incur the cost of the difference between the strike price and the market price.

If wholesale market pricing is stable, the risks faced by retailers and generators are low. However this risk increases markedly as the volatility of the market increases. The greater the risk to retailers and the greater the risk premium retailers add to their prices to accommodate the increased risk.

The Queensland regional market is quite volatile and so the risks for a retailer (and generator) in this market are very high. The following chart shows the variation of price relative to demand in the Queensland region for 2015.



Source: NEM data via NEM-Review

Periods where prices are greater than \$500/MWh have an inordinate impact on the average cost of electricity. For example, the impact of the prices above \$500/MWh in the Queensland market for 2015 increased the annual average price by 33 per cent. Further, although there is an expectation that prices increase with increasing demand, it is clear that many of the high price events are not related to high demand drivers. This lack of correlation adds an extra layer of risk to both generators and retailers.

Calendar year	Average spot price \$/MWh	# price excursions above \$300/MWh	Severity of excursions % increase of average annual price caused by the price excursions
2010	\$26	23	17%
2011	\$35	38	21%
2012	\$43	37	3%
2013	\$68	172	16%
2014	\$51	78	29%
2015	\$52	81	36%
2016 to end February	\$83	52	60%

Source: NEM data via NEM-Review

The data above shows that, in combination of the various measures, the overall Queensland market is exhibiting increasing volatility. It is clear that the increasing volatility in the Queensland market needs to be reduced to ensure retail competition remains effective.

The causes of increasing volatility are many and include:

- The exercise of market power;
- Use of rebidding to prevent actions from other parties to effect change;<sup>18</sup>
- Increasing congestion in the network preventing a lower priced generator being dispatched and a higher priced generator being called to meet regional demand;
- Generators offering lower ramp rates than they are capable of, requiring higher priced generators being dispatched when there is increasing demand or preventing lower priced generation being dispatched when demand is falling;<sup>19</sup> and
- The need for short term high priced generation to be dispatched to address changes in the market that cannot be accommodated by base load generation.

Overall, it is considered that volatility will increase in the market from a number of different causes. While we recognise that some causes cannot be readily addressed, they should be clearly identified. Further, those that arise from the exercise of market power should be addressed in the recommendations made in the QPC's Final Report.

#### 2.4.2 Rebidding

It is accepted that rebidding can be a process which provides a benefit to consumers as it has been previously estimated that perhaps more than 90 per cent of rebids are to reduce the costs of electricity.<sup>20</sup> Unfortunately for consumers, it is the impacts of rebids to higher prices that create the major problem due to the excessive levels that rebid prices can go to. A few rebids at the market price cap swamp the value of a larger number of rebids for small reductions. Rebidding late in a trading period also acts to prevent competition.

There is little doubt that rebidding should be maintained, but the concern is where rebidding (especially when a generator has market power) causes considerable harm to consumers.

The QPC acknowledges that the increase in Queensland's wholesale market prices since 2010-11 may be related to a range of reasons, including "*an increase in the instances of late rebidding by generators*".<sup>21</sup> The AER also noted the incidence of "*opportunistic generator rebidding behavior*" in Queensland.<sup>22</sup>

The QPC appropriately highlights that there is no evidence that generators in Queensland (including Stanwell and CS Energy) have operated outside the rules.

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<sup>18</sup> This was the focus of a recent rule SA government rule change proposal.

<sup>19</sup> This was the focus of a recent AER rule change proposal.

<sup>20</sup> The National Electricity Code Administrator (NECA), the forerunner of AEMC, on its report on rebidding in 2001

<sup>21</sup> QPC Draft Report, p42

<sup>22</sup> QPC Draft Report, p49

However, this merely points out that the rules are not sufficient to prevent actions by generators to garner revenues above what is efficient and would occur in an effective competitive environment.

We therefore agree with the QPC's Recommendations 7 and 8 for specific actions to monitor the actions of Stanwell and CS Energy in relation to rebidding. We consider that the recommendations should not only highlight and report on the rebids that have been made, but should also include an assessment of the impacts on the wholesale market that the rebids caused.

We also support the QPC's recommendation that the owner of Stanwell and CS Energy (the Queensland government) should have the ability to address actions by its generators that might lead to a less acceptable outcome for consumers than is achieved under the rules.

### **2.4.3 Economic withholding**

Generator market power has been exemplified in a number of states but most notably in South Australia (SA) during 2008-2010. In that exercise of market power, the generator performed what is called "economic withholding of capacity". Economic withholding is where a base load generator, knowing that it must be dispatched regardless of the price it offers, either in its initial bid or through rebidding, offers its capacity at a price just below those prices offered by generators that are occasionally dispatched<sup>23</sup>.

This practice is very effective and reflects that the wholesale market price cap is set at a value that is effectively 250-300 times the actual cost of production. Such a multiple allows the generator to only be dispatched for a small fraction of what it might be capable of providing and yet still achieve the same revenue.

This practice is prevented in many overseas markets but is permitted in the NEM. In the absence of national rules to protect consumers from this activity, we consider there is opportunity for the QPC to mitigate the risk of this occurring in the Queensland wholesale market by incorporating economic withholding of capacity as an abuse of market to be covered by the Code of Conduct and reporting requirements alongside rebidding under Recommendations 7 and 8.

### **2.4.4 Tacit collusion**

The NEM is an extremely open and transparent market so each generator has ready access to information on other generators, how they bid, their price points and even their costs of production.

Further, thermal generation is usually classified into three main elements - base load, intermediate and peaking. While the overall number of generators might be high, the competition between the three elements is generally much less strong. Low competition in each element, combined with an open and transparent market, allows generators to learn how other generators will act under a set of circumstances and therefore notionally collude in a legal way. This is referred to as "tacit collusion".

The import of tacit collusion allows generators to refine their bidding strategies to maximise their revenue without overtly colluding. It also allows those generators

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<sup>23</sup> Usually these generators (eg peaking plants) offer prices that are close to the market price cap

which are price-takers to know that if they bid their product at the minimum price allowed in the market, they are likely to receive prices that will still allow them to readily cover their costs.

For example, wind farms have a very low operating cost and so bid their capacity into the market at the minimum market price, knowing that most of the time, a thermal generator will be bidding into the market at a higher price because it needs to cover its short run marginal costs. Wind farms know that by combining the marginal cost from a thermal generator and the revenue from renewable certificates, its long run costs will be covered. Thermal generators use tacit collusion to ensure that, for most of the time, they will recover at least their short run marginal costs, and over the longer term, their long run costs.

It is important to recognise that tacit collusion does occur when assessing the relative competition that generators face. We again consider that options to mitigate this risk in the Queensland market should be incorporated into the QPC's recommendations in the Final Report. We consider there is opportunity for the QPC to incorporate tacit collusion as an abuse of market to be covered by the Code of Conduct and reporting requirements alongside rebidding under Recommendations 7 and 8.

#### **2.4.5 Network congestion**

Network congestion occurs when there is no ability for the element of the network to increase its capacity to transfer more power even though the market would be best served if a greater flow was possible. Networks are incentivised to minimise the impacts of congestion through operating practices and minor projects to achieve greater carrying capacity and these incentives delivered some benefits.

Generators can use congestion in the network to exercise market power to raise prices. Generators like Stanwell and CS Energy have a fleet of generators which can be used in ways that, in the event of congestion, can bid their outputs in ways that increase their opportunity to exercise market power. Alternatively, generators with just one power station do not have the capabilities to bid their generators to maximise the opportunity to benefit from network congestion.

It is accepted that the costs for augmenting the transmission network preclude achieving a "congestion free" network as this would not be efficient. Equally, maximising the use of network congestion to enhance revenues above the efficient level is not in the interests of consumers. We consider the QPC should investigate the extent to which the Queensland generators' use of network congestion constitutes abuse of market power and consider how this can be mitigated through the QPC's Recommendations 7 and 8.



### 2.4.6 Ramp rates

Generators offer two basic services - energy into the market and the ability to increase/decrease the rate of change in the amount of output that it provides - this is usually referred to as the generator's "ramp rate". The AER recognised that generators can maximise their revenues by bidding in ramp rates well below the capabilities of most generation plant<sup>24</sup> and as a result proposed a rule change to limit the ability of generators to use ramp rates as a tool to prevent competition for a period of time.

The reason for the proposal from the AER was to ensure that generators provided ramp rates which reflected the abilities of the generators in a way that would be used if the generators were subject to central dispatch as applied before deregulation of the electricity supply chain. Under the historic approach, a generator would be ramped up or down to maximise the benefit to consumers. Now, ramping up and down reflects the preparedness of generators to match the needs of the market and therefore they can bid in (and rebid) very low ramp rates so as to maximise their revenue stream.

In its proposed rule change<sup>25</sup>, the AER used as examples of the practice of using ramp rates to maximise revenues and to cause inefficient outcomes, such as counter price electricity flows. These examples were those used in Queensland and which had caused considerable price volatility and resulted in inefficient outcomes.

Given the AER has already identified that the Queensland government-owned generators<sup>26</sup> have used ramp rates to drive wholesale market prices higher, which is of concern to consumers, regardless of whether this exercise of market power was permitted within the rules. We therefore consider this should be explicitly addressed in the QPC's analysis and under Recommendations 7 and 8.

## 2.5 Renewable generation

While renewable generation is fundamental to reducing carbon emissions, incorporating renewables into the wholesale market is not a costless exercise and imposes costs on consumers above and beyond the headline costs for the renewable energy certificates.<sup>27</sup>

As highlighted in the chart below (which plots the mean demand for the last six calendar years on a time of day basis), there is falling demand in Queensland in the middle of the day, as a result of an increase in solar photovoltaic (PV) roof top installation. This trend is expected to continue to increase significantly due to the growth in penetration of rooftop solar that is forecast.

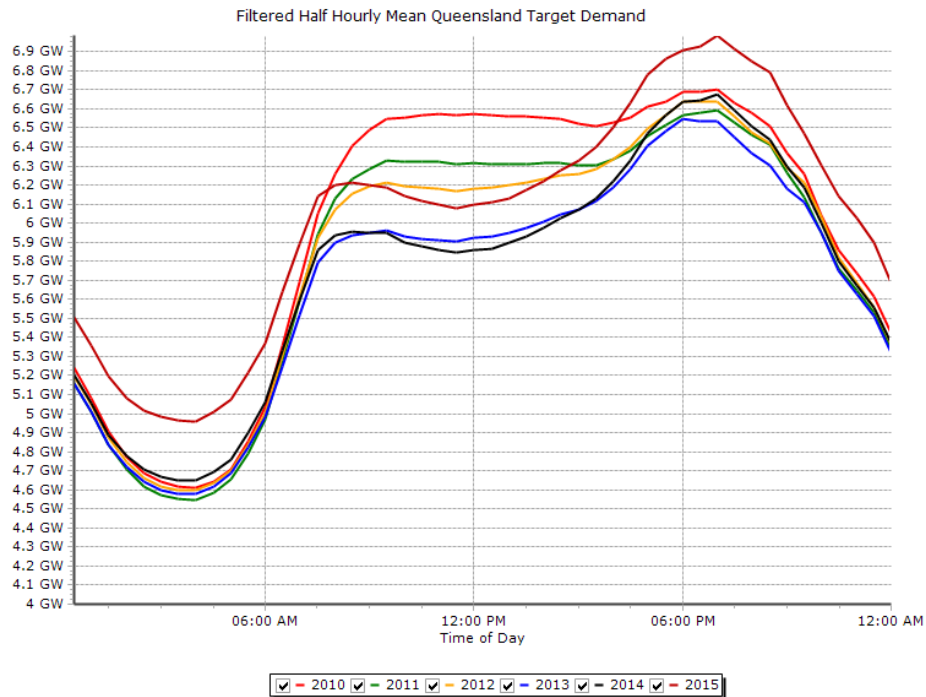
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<sup>24</sup> For example, a hydro generator has a ramp rate measured in many 10's of MW per minute and is therefore very able to very quickly respond to changes in demand. The rules allow such a generator to offer a ramp rate as low as 3 MW per minute. So CS Energy with its Wivenhoe hydro generator could offer only 3 MW/minute ramp rate and so use this market power to game the market

<sup>25</sup> <http://www.aemc.gov.au/getattachment/af45d045-07c8-474e-958f-5b7a0a6dd997/Rule-change-request.aspx> submitted 21 August 2013

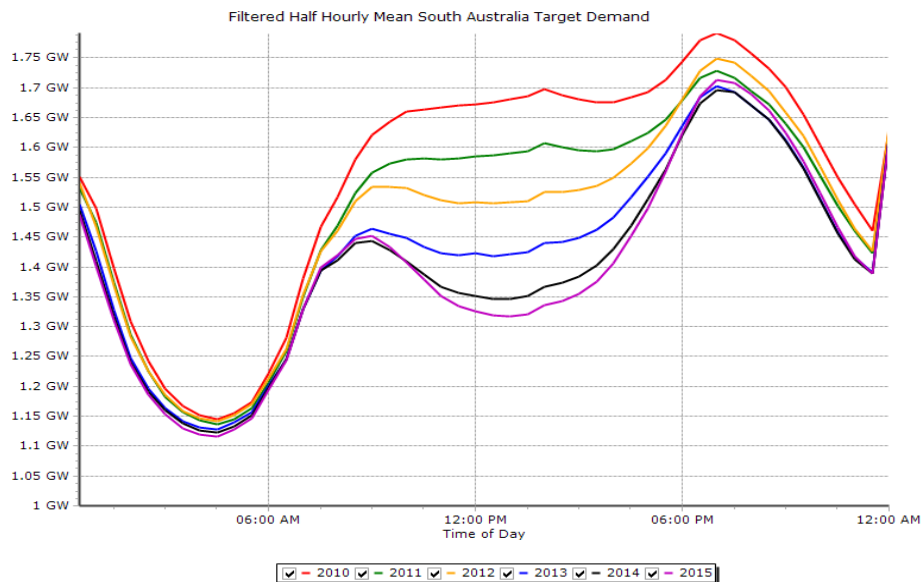
<sup>26</sup> Ibid. for example page 15

<sup>27</sup> These are the certificates for large renewables under the LRET and small renewables under the SRES.



Source: NEM data via NEM-Review

To demonstrate the longer term effects of this, the following chart shows the impact of rooftop solar PV in SA where penetration (in relative terms) is much higher than in Queensland. This chart shows that as solar penetration increases, the midday "sag" in demand increases markedly. This is what is likely to be seen more clearly in Queensland as solar penetration increases as the QPC has forecast.



Source: NEM data via NEM-Review

What is important to note is that the amount of electricity effectively displacing generation in the middle of the day is impacting on the volume of electricity that is sourced from base load generation. The impact on generators of this reduced volume

is an issue that cannot be overlooked as it reduces the ability of generators to cover their fixed costs. The outturn of loss of volume either results in increased prices to cover the fixed costs, or by generator closures which results in less competition. Neither of these outcomes is good for consumers.

For example, in South Australia, in 2014 there were four base load generators serving a base load about a quarter of that of Queensland and generator hedges offered to retailers were reflective of this competition. In 2016, effectively there will be just two base load generators and retail hedge prices have doubled and secondary market liquidity has to all intents disappeared. A further complication is that both of the remaining base load generators are owned by the two dominant retailers in SA leading to a loss of retail competition as those retailers without generation have to source hedges from their competitors.

The increasing amount of intermittent generation (such as solar PV and wind farms) creates the need for more fast start generation (which is also more expensive in \$/MWh terms) to meet the short term fast starts needed to manage the loss of one source of supply (for example rooftop solar when clouds collect or from wind farms when the wind drops) and the dispatch of lower cost base load generation which due to slower ramp times needs more time to match the change in the demand.

Intermittent generation also imposes requirements for fast start generation to be dispatched for relatively short periods of time because base load generation is not able to respond quickly enough to maintain security of supply. To maintain supply, thermal generators are dispatched to make up the short fall. If ramp rates on base load generators cannot match the rate of reduction in wind farm output, fast start generators (such as open cycle gas turbines) are dispatched until the base load generator can "catch up" with the shortfall in generation and allow the fast start generator to offload.

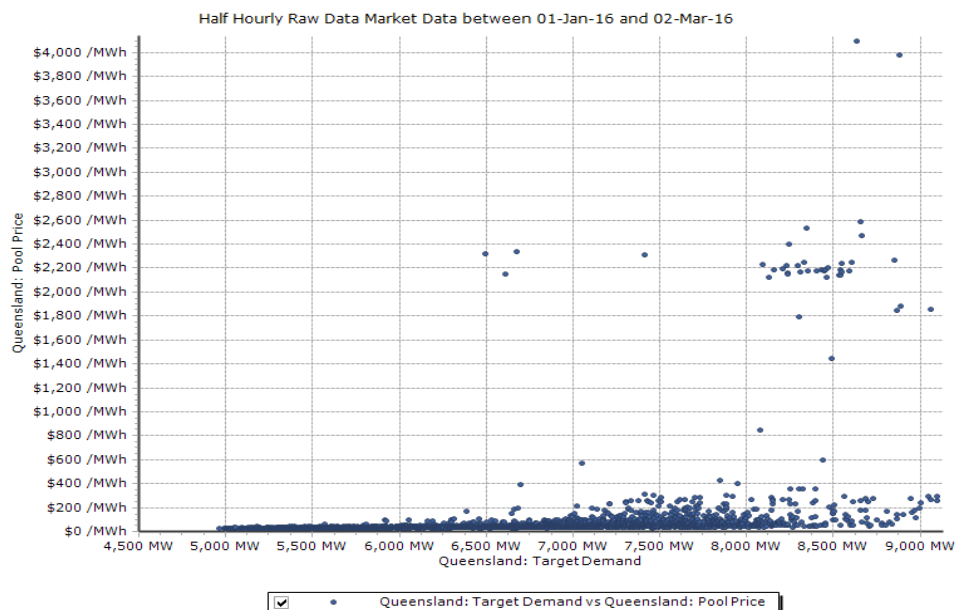
Fast start generators operate for short periods of time and therefore have to price their output at high prices in order to recover their fixed costs.<sup>28</sup> Typically, a fast start generator might only operate for one or two dispatch periods (i.e. 5 - 10 minutes) until the base load generator has time to pick up the demand and they tend to price their output at close to the market price cap. This volatility is revealed by the number of trading periods with prices at \$2000 and \$4000.<sup>29</sup>

The following chart highlights this:

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<sup>28</sup> The market price cap is based on the price an open cycle gas turbine needs for its output if it is only dispatched for a few hours each year

<sup>29</sup> \$2000 /MWh reflects one dispatch period at market price cap and \$4000 two dispatch periods at MPC



Source: NEM data via NEM-Review

A significant increase in penetration of roof top solar PV is forecast (perhaps to a level of 3000MW). This will significantly impact the volatility of the market and the frequency and extent of dispatch of high priced generators for relatively short periods of time. This increases volatility and therefore the risk premium that retailers have to accommodate in their risk premiums.

Much of the renewable generation introduced into the generation mix in the NEM is intermittent in nature and its supply into the market is somewhat unpredictable. Rooftop solar PV is impacted by the time of day and the weather (particularly cloud cover) can have a significant impact both intraday, between days and between seasons. Wind generation is impacted by the weather, timing, seasons and wind speeds.

This intermittency has a significant impact on a number of elements in the wholesale market but also in the provision of networks. To accommodate the impacts of this variability, costs are incurred in the networks and in the wholesale market.

Networks have to be sized to carry the large amounts of energy generated from wind farms but the utilisation of the networks is, over the long term, very low as wind generation has a capacity factor of between 25 per cent and 35 per cent. This implies that networks serving wind farms are utilised<sup>30</sup> for about a third of the time. For comparison, Millmerran Power Station operates consistently with a capacity factor of about 90 per cent utilisation.

As networks are sized for the maximum output, consumers are paying for significant unused spare capacity for networks supplied from renewable generation, whereas the networks serving a thermal base load power station are consistently loaded to near their maximum capacity.

<sup>30</sup> This is the ratio between actual output and theoretical maximum output

Thus, intermittency in generation imposes less efficient investment in networks. The impact on network costs must be considered when seeking to implement increasing amounts of renewable generation.

It is important to note that, as renewable generation displaces thermal generation, the cost impacts on thermal generation are significant due to the need to recover large fixed costs over a declining volume. This naturally increases the prices needed to be offered to recover the fixed costs. Yet due to the intermittency of supply from renewable generators, to maintain security of supply, there must be thermal generators standing by and available for the periods when the sun is not shining and/or the wind not blowing. As thermal generators are capital intensive, having these plants idle adds considerably to the overall cost of generation which must be recovered from consumers.

While we do not consider that Queensland is in the same position as South Australia with regard to renewables penetration at this time, it does point out that this issue will have increasing importance in Queensland as penetration of renewable generation increases.

This submission does not seek to address the merits and demerits of renewable generation, but simply highlights that increased renewable generation does introduce costs and benefits into the wholesale market in a number of ways. These costs can lead to higher prices, greater volatility and reduced retail competition. These aspects must be recognised in order to ensure appropriate actions to mitigate any detrimental effects on consumers and thereby maximise the benefits of renewable generation.

## 3 Networks

### 3.1 Overview

This chapter addresses *Chapter 4: Networks* of the QPC's Draft Report (pp62-83).

The QPC's Draft Report rightly points out that *"increasing network costs have been the primary contributor to electricity price increases in Queensland over the last decade"*.<sup>31</sup> In fact, the QPC notes that the network component of retail prices has grown by 257 per cent in real terms since 2004-05, and these increases have been the main factor behind the 87 per cent increase in retail prices over the same period.<sup>32</sup>

We cannot emphasise enough that these price increases are presenting significant hardship for residential consumers and major competitiveness challenges for Australian businesses. This is impacting on the ability of these businesses to sustain their businesses and crucially jobs including in regional areas. The price modelling in the QPC's draft report is projecting retail price stabilization for residential and commercial customers after the next regulatory period out to 2035. Overall retail prices are forecast to decrease by 13 per cent for residential customers and 8.7 per cent for commercial customers. This is over a 20 year period and is not significant price relief.

Despite extensive evidence of the contribution of network price rises to the retail prices and the evidence put forward in submissions<sup>33</sup> to the QPC's Issues Paper on the impact of these high prices on households and businesses, the QPC has restricted its recommendations relating to the Queensland network sector to five recommendations, all of which essentially reflect "business as usual". We do not consider that these recommendations address the fundamental cause of the problems leading to high and unsustainable electricity prices that, as the draft report predicts, Queensland households and businesses are locked into for the foreseeable future.

The QPC's Draft Report finds that the networks' component of prices will decrease by 40 per cent by 2021 and then stabilise for the remaining projected period to 2035. Forecasting is always a difficult task; however given the QPC's wholesale prices are forecast to increase by 52 per cent, the retail price projections appear to strongly rely on the accuracy of the network price projections to deliver projected price stabilisation. In our view, this is a risk and as such there is no room for complacency in this regard. The QPC in its Final Report must make every effort to explore all avenues to identify ways to place downward pressure on prices.

We further contend that the very large increase in prices over the last ten years have resulted in very high profit outcomes for the three Queensland network businesses. Our view is that profits are reflective of inefficient prices (monopoly prices).

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<sup>31</sup> QPC (2016), Draft Report Electricity Pricing Inquiry, P63

<sup>32</sup> Ibid

<sup>33</sup> QCOSS and CCIQ submissions to the QPC Issues Paper and can be found on the following by clicking [here](#).



The QPC has not sufficiently assessed the reasons for the Queensland networks' price increases over the last ten years and in particular has not looked at the growth in the networks' regulatory asset bases (RABs) despite acknowledging on p82 that both distributors RABs increased by 168 per cent over the ten year period to 2014-15. The QPC does acknowledge that the poor productivity in the industry has been largely attributable to capital investment decisions<sup>34</sup>, however there are no recommendations identified to address the cost implications of these decisions and in particular the build-up of very large RABs as a result. Only by investigating the efficiency of these past investment decisions will it be possible to find sustainable and justifiable solutions which can lead over time to fair returns on the assets and efficient prices.

Despite recent rule changes, the national regulatory framework is currently unable to address the build-up of the RABs. We therefore recommend the Queensland Government pursue opportunities for NEM reform to address this as part of their role on the COAG Energy Council.

This however is not sufficient as the COAG processes are not timely and so we also recommend that the QPC investigate the asset values to see if they are appropriate and efficient, and recommend to the Queensland Government what scope there is to reduce the valuation of the RABs.

We acknowledge that there may be a conflict for the Queensland Government between its policy and shareholding roles with such a recommendation. The QPC Electricity Pricing Inquiry provides an opportunity to have an honest and transparent discussion with the Queensland community regarding the decisions that are required to address Queensland's excessive electricity prices. The governance and oversight arrangements need to be such that they provide confidence to the community that consumers are only paying for costs that are appropriate and efficient.

### 3.1.1 Recommendations

We make the following recommendations to the QPC for consideration for its Final Report.

**Recommendation:** That the QPC investigate the appropriateness of the Queensland network businesses' returns by comparing them to the returns being achieved by the networks in the other jurisdictions in Australia, and the returns of blue-chip ASX50 companies in all other sectors of the Australian economy.

**Recommendation:** That the QPC provide more transparency about the assumptions underpinning its price projections especially its forecasts in relation to network prices.

**Recommendation:** That the QPC's Draft Recommendation 12 is strengthened to include improved scrutiny and transparency of the performance reporting of the Queensland networks and that consumers and other key stakeholders have a formal role in the oversight of the Queensland networks' performance monitoring.

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<sup>34</sup> Draft Report Electricity Pricing Inquiry, P9

**Recommendation:** The QPC draft recommendation 15 be expanded and strengthened so that Queensland Government, in its responsibility for energy policy, proactively progresses NEM reform to address the excessive RABs.

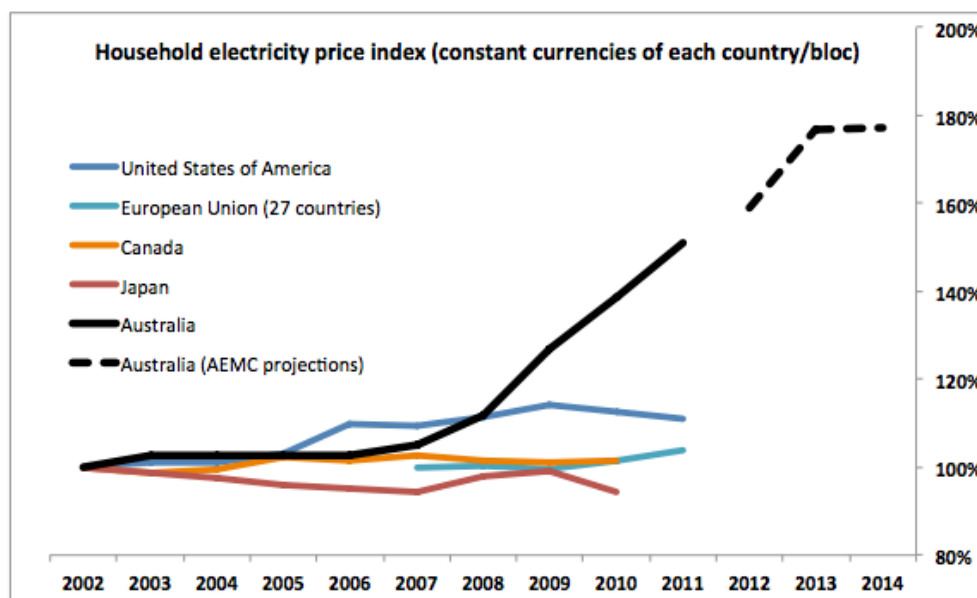
**Recommendation:** That the QPC thoroughly investigate a range of possible options to reduce the excessive RABs and ensure that the revenues reflect fair returns on the Queensland Government's investment in the networks.

**Recommendation:** That the QPC revise its draft recommendations 20 and 21 to:

- Better reflect the commentary in the draft report that outlines the specific improvements required to the governance arrangements; and
- Clarify that the intended outcome is to bring balance to the conflicting roles and competing interests between energy policy (in the long term interests of consumers) and shareholders' interests.

### 3.2 Inefficient network prices

Prior to 2006, Australia's electricity prices were reasonably stable with annual price increases closely tracking CPI. However, as illustrated in the chart below<sup>35</sup>, since 2007 Australia's electricity prices have increased sharply, whereas the prices in other countries have remained relatively stable. As a result, Australia's electricity prices are now amongst the highest in the world.



On average, Australian electricity prices doubled from 2007 to 2012, although the increases varied by jurisdiction.<sup>36</sup> It is now well understood that Australia's electricity

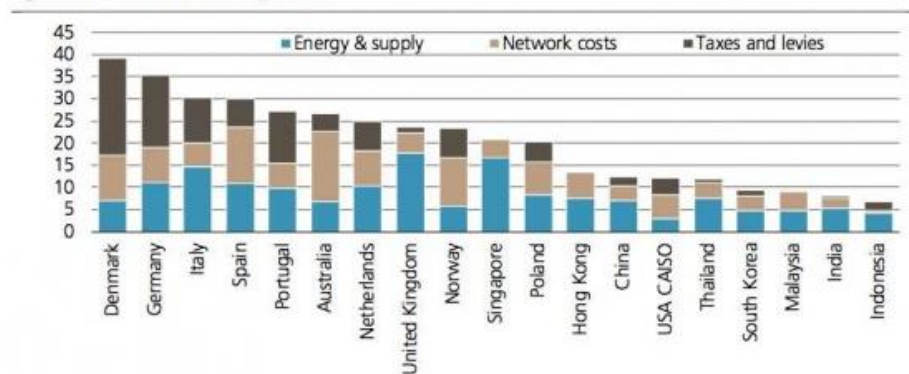
<sup>35</sup> Electricity Prices in Australia: An International Comparison, EUAA, March 2012

<sup>36</sup> Productivity Commission: Electricity Network Regulatory Frameworks - Inquiry Report , 26 June 2013

price increases have been driven by dramatic increases in network prices (the charges from the monopoly transmission and distribution networks).

As the chart below illustrates, network prices account for a much larger share of Australia's electricity prices than other countries. It illustrates that in 2013 Australia's average network charges accounted for around 60 per cent of the total electricity price, whereas in other countries network charges accounted for between 20-25 per cent of electricity prices.

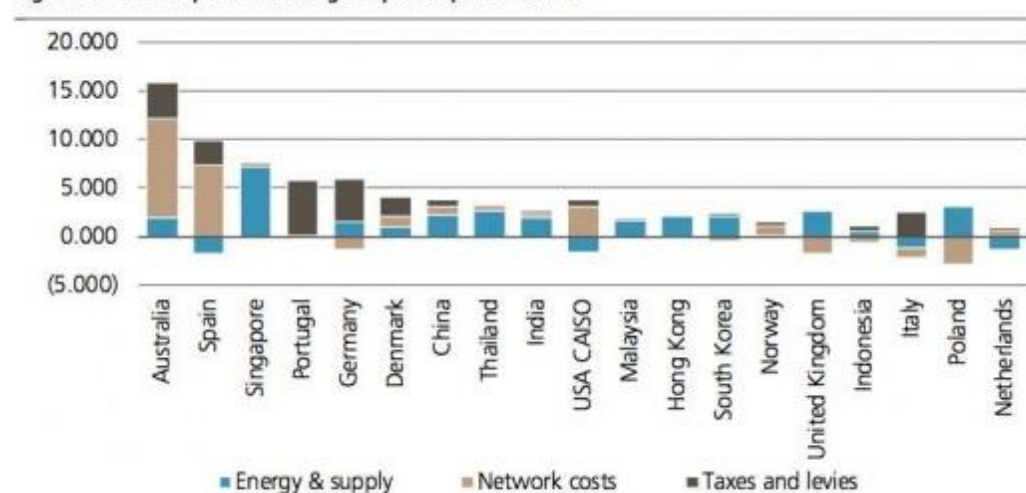
Figure 1: 2013 tariffs (US cents per kWh)



Note: Residential tariffs for Australia, Europe and the US; national average for Asian markets.  
Source: Power utility companies, government databases, UBS estimates

This has not always been the case. The chart below illustrates the change in the key components of each country's electricity prices from 2007-13. It illustrates that the vast majority of the growth in Australia's electricity prices was due to growth in network charges, which significantly outstripped the impact of changes in the other components. By contrast, network charges have had a much smaller impact on the changes of electricity prices in other countries.

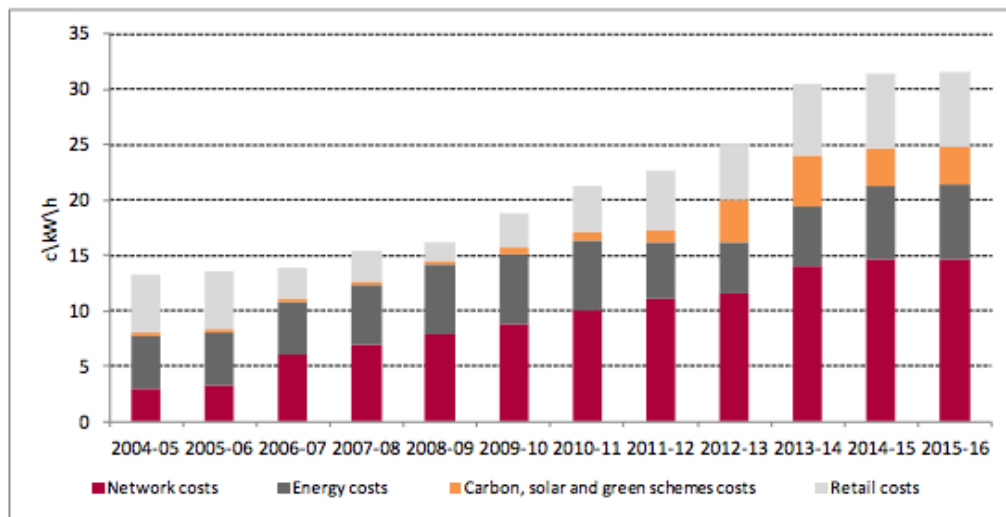
Figure 5: US cents per kWh change in power prices 2007-13



Source: Power utility companies, government databases, UBS estimates

Of particular concern is that Queensland's network price increases have been much higher than in other Australian states. The chart below illustrates the trends in Queensland's residential electricity prices (Tariff 11) over the past 11 years.<sup>37</sup>

**Figure 3 Average Queensland annual Tariff 11 cost component breakdown (c/kWh, nominal)**



Source: Department of Energy and Water Supply

This chart illustrates that:

- Queensland's residential electricity prices doubled from 2007/08 to 2013/14.
- The price rises over the past decade have been driven by increases in network charges, which increased six-fold from 2004/05 to 2014/15, accounting for around 95 per cent of the total electricity price increases during the period.
- As a result, network charges now account for around half of Queensland's retail electricity prices, whereas in 2004/05 they accounted for around 20 per cent
- By contrast, Queensland's generation and retail costs have remained relatively stable

These price increases are presenting significant hardship for residential consumers and major competitiveness challenges for Australian businesses. We refer the QPC to our earlier submissions to the QPC's Issues Paper where these impacts are documented.<sup>38</sup>

As Queensland's network prices have increased, so too have the profits of Queensland's network businesses. Over the five year period 2008-2013:<sup>39</sup>

- Powerlink Queensland's net profit after tax (NPAT) increased by 520 per cent
- Energex's net profit after tax (NPAT) increased by 256 per cent
- Ergon Energy's net profit after tax (NPAT) increased by 266 per cent

<sup>37</sup> Queensland Productivity Commission (QPC) Electricity Pricing Inquiry, Issues Paper, October 2015

<sup>38</sup> QCOS and CCIQ submissions to the QPC Issues Paper and can be found on the following by clicking [here](#).

<sup>39</sup> All NPAT figures are derived from the Queensland networks' Annual Financial Reports

Our premise is that the very high profits which the Queensland networks are making are an indication of excessive returns at the expense of Queensland energy consumers. We understand that the Australian Energy Regulator (AER) cannot address the level or growth of profits in its revenue determinations. The test is the actual returns generated by the businesses and, over time, these should be within reasonable limits of the returns generated by businesses with similar risk exposures. It is quite legitimate therefore for the QPC, in its task to investigate options to place downward pressure on electricity prices, to investigate the appropriateness of these returns by comparing them to the returns being achieved by the networks in the other jurisdictions in Australia, and the returns of blue-chip ASX50 companies in all other sectors of the Australian economy.

We consider there needs to be increased transparency around the returns that the Queensland government is realising from its electricity networks. We are concerned that these returns are being realised in the context that the Queensland electricity networks are amongst the most inefficient networks in Australia. As outlined by various studies,<sup>40</sup> the productivity and capital efficiency of Queensland's electricity networks is poor and is rapidly declining. We understand that this is in contrast to the Victorian networks which are more efficient, spending substantially less capital and operating expenditure both in absolute terms and after normalisation for changes in network outputs such as peak demand and energy delivered. The Victorian networks' efficiency has not been at the expense of safety or reliability.

**Recommendation:** That the QPC investigate the appropriateness of the Queensland network businesses' returns by comparing them to the returns being achieved by the networks in the other jurisdictions in Australia, and the returns of blue-chip ASX50 companies in all other sectors of the Australian economy.

Therefore it is of concern that the QPC's Draft Report has failed to acknowledge the unsustainability of 'business as usual'. The Queensland networks' excessive investments have resulted in a large degree of excess system capacity and significant declines in their asset utilisation levels. This has been driven in large part by consumers reducing their consumption in response to the dramatic increases in the Queensland network prices. In addition, consumers are increasingly moving to self-generation as the costs of distributed generation are becoming more attractive, thereby further reducing the energy being delivered by the Queensland networks.

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<sup>40</sup>For example:

EUAA: Australia's rising prices and declining productivity: the contribution of its electricity distributors, 2011

EUAA: A comparison of outcomes delivered by electricity transmission network service providers in the NEM, October 2012

PIAC: Privatisation and the regulatory valuation of electricity distribution network service providers in NSW: Evidence and Issues

Total Environment Centre (TEC): Write-downs to address the stranded assets of electricity networks in the National Electricity Market: evidence and argument, April 2015

Electricity Network Regulatory Frameworks: Productivity Commission Inquiry Report, 9 April 2013

Grattan Institute, *Putting the customer back in front: How to make electricity cheaper*, December 2012

Senate Select Committee on Electricity Prices: Reducing Energy Bills and Improving Efficiency

Utilities Policy: Independent Regulation of Government-Owned Monopolies: An Oxymoron?, December 2014

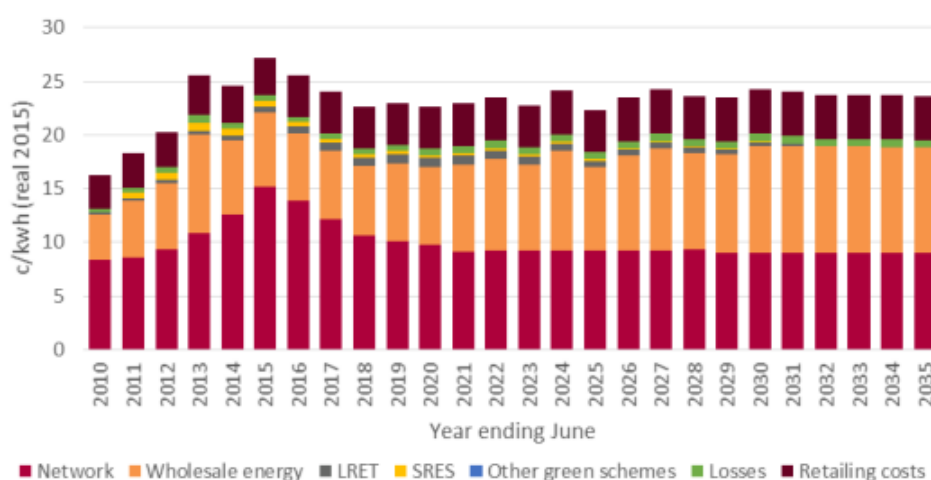
AER, 2015 Annual Benchmarking Reports, November 2015

The Garnaut Review Update Paper 8: Transforming the Electricity Sector. Garnaut R. (2011)

The natural outcome of the continuation of these trends is the well documented “death spiral” – that is, as the move towards distributed generation increases, the burden of paying for the Queensland networks’ costs will be placed on a smaller consumer base until those consumers can no longer afford to stay connected to the network. Continuation of the network death spiral will be destructive to the value of the Queensland Government’s energy network businesses.

Consequently, we would like to raise some concerns regarding the assumptions underlying the QPC’s future network price projections, as illustrated in the diagram below. The QPC has assumed that the network cost component of electricity bills will reduce by 40 per cent in real terms from 2015 to 2020 and that those price reductions will be maintained for the following 14 years.

**Figure 38 Projected real residential electricity prices—Energex**



Some industry analysts have questioned the credibility of the assumptions contained within the QPC’s Draft Report. For example, as stated by Giles Parkinson: <sup>41</sup>

*“It assumes a whole range of numbers that are questionable at best, and appears to use these to reach conclusions that favour the incumbent industry and the interests of ‘big energy’.*

*Almost every recommendation it makes targets the very technologies that it notes are challenging the status quo of the big incumbents – which in Queensland are as powerful and unassailable (and state owned) as anywhere in the country.”*

The QPC’s projections also appear to be inconsistent with those of the AER. For example, the AER’s 2015-20 revenue determination for Energex applied a maximum revenue reduction of less than 20 per cent from 2015-2020, with maximum network price reductions (based on credible load forecasts) of around 15 per cent. The QPC

<sup>41</sup> <http://reneweconomy.com.au/2016/queensland-inquirys-big-fail-on-rooftop-solar-and-battery-storage-45778>



in its draft report is projecting the contribution of networks costs to the bills to reduce by over twice that level by 2020.

We are concerned about the implications should these projections not manifest. Given the projections for wholesale prices to increase by 52 per cent, we are concerned that retail prices may continue to rise should these network price projections not manifest as the QPC has forecast.

Furthermore, the QPC's forecasts that 40 per cent reduction in the network component of bills will be maintained from 2021-2035 are difficult to comprehend, especially given the existing value of the RABs. For this to manifest, we consider there would need to be a very significant reduction in the RAB and/or the WACC, neither of which have been highlighted in the Draft Report.

Given the importance of these projections, it is concerning that the QPC has not been more transparent about the basis for their projections and the underlying assumptions. We suggest the QPC needs to be more transparent about this in its Final Report. At a minimum, we recommend that the Final Report should explain the implications of the RABs for future network prices and what assumptions have been made in relation to the RABs in the QPC's network price projections.

**Recommendation:** That the QPC provide more transparency about the assumptions underpinning its price projections especially its forecasts in relation to network prices.

### 3.3 Queensland's networks regulatory asset bases

The QPC's draft report acknowledges that industry's poor productivity performance is largely attributable to capital investment. Inefficient and excessive capital investment has led to the significant growth in the RABs. The Queensland networks' RABs have grown at the highest rates in Australia, growing by over 400 per cent over the past 15 years, during which the Victorian networks' RABs grew by less than 200 per cent. The RABs will only start to fall slowly over time, and these very large RABs mean that, going forward, households will be locked into the current very high prices for the foreseeable future.

The key driver of the high prices is the growth in the returns on what have become excessive RABs. This is well documented by a number of recent high level reports such as the Senate Inquiry<sup>42</sup> which concluded that:

*"While there are several areas of the framework that may warrant attention, the committee considers the treatment of the regulatory asset bases (the capital expenditure investments of each network business) is the fundamental cause of high network costs and will continue to be a major driver of revenue for network businesses in the future"*

We accept that electricity supply is a capital intensive industry; however the Queensland networks' returns on their RABs account for a very large proportion of their revenues, and these returns drive the majority of the Queensland networks'

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<sup>42</sup> Australian Government (2015), *Senate Inquiry into The Performance and Management of electricity Network Companies*.

prices. Over the previous regulatory period, the Queensland networks' returns on their RABs accounted for: <sup>43</sup>

- 77 per cent of Powerlink Queensland's total revenue allowances
- 75 per cent of Ergon Energy's revenue allowances
- 74 per cent of Energex's revenue allowances

Given the contribution of the returns on and of capital to the revenue allowances, they are clearly an area the QPC must investigate further and in particular the RABs. The scope for reductions in the WACC has already been well researched during the recent AER's Revenue Determinations for Energex and Ergon. Indeed much of the recent AER Final Decision which resulted in reduced revenue allowances was due to the reduced cost of debt.

The increase in the RABs has resulted in growing inefficiency and lack of productivity in the networks. QCOSS in its submission<sup>44</sup> to the AER on Ergon and Energex's regulatory proposal in January 2014 put forward substantial evidence on the increase in RABs and how this resulted in poor outcomes for consumers. We repeat some of the key evidence here for Energex, noting that this analysis could also be done for Ergon. In the below Table 3.1 for Energex, we have extracted and analysed the network in terms of the growth in assets, customer numbers, peak demand (in MVA), and the amount of energy delivered at on-peak and off-peak times. This table also illustrates key metrics such as the amount of assets used to deliver peak demand (asset/peak), the amount of assets used per customer (asset/customer), and the amount of delivered energy per asset (delivered energy/asset).

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<sup>43</sup> 'Return on capital' plus 'return of capital' (depreciation) allowances – as per the AER's revenue determinations

<sup>44</sup> QCOSS Submissions to the AER Revenue Determination 2015-2020 (Regulatory Proposal) and can be found by clicking [here](#) and the Preliminary Decision by clicking [here](#).

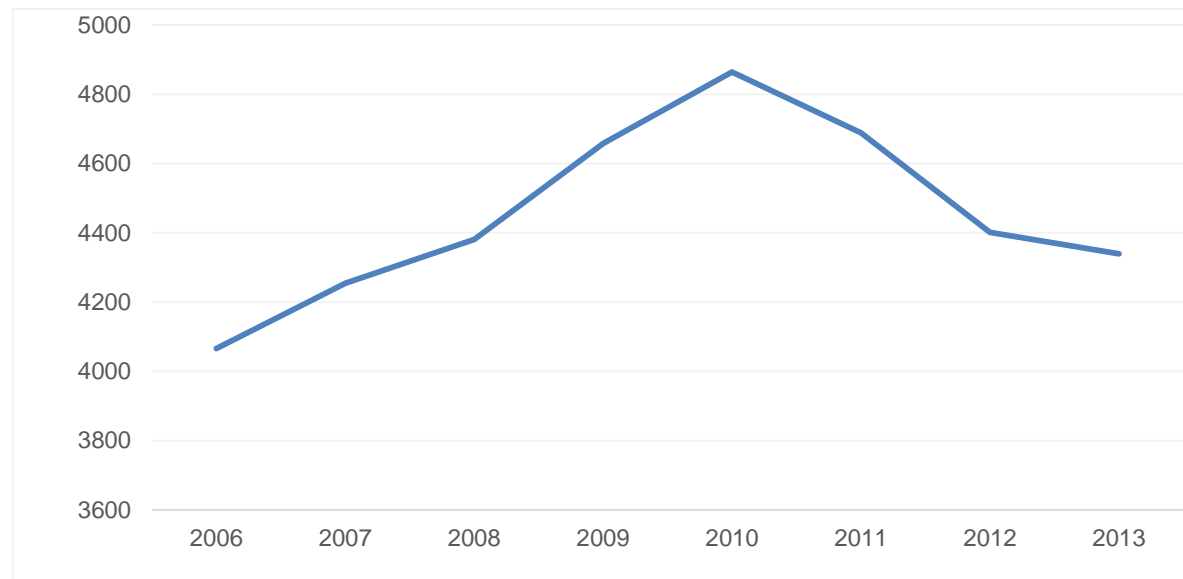
**Table 3.1 Key delivery information and metrics for Energex network 2006-2013**

	units	2006	2007	2008	2009	2010	2011	2012	2013
<b>Assets \$m</b>	\$,000	4,077	4,478	4,881	5,369	6,151	6,789	7,346	7,963
<b>Customer numbers</b>	number	1212064	1236101	1263763	1287436	1307554	1326564	1343865	1359712
<b>Energy delivered</b>	GWh	20618	20707	21155	21994	22193	21454	21210	21055
<b>Peak demand</b>	MVA	4066	4254	4381	4658	4865	4689	4401	4339
<b>On-peak deliveries</b>	GWh	10939	10899	11062	11611	11630	11192	10896	10557
<b>Off-peak deliveries</b>	GWh	10704	10796	10905	11329	11465	11105	11001	10909
<b>Asset/cust omer</b>	\$/cust	3364	3623	3863	4171	4705	5118	5467	5857
<b>Asset/peak</b>	\$m/MVA	1002959	1052826	1114181	1152633	1264646	1447947	1669245	1835317
<b>Delivered energy/asset</b>	kWh/\$	5.056	4.623	4.334	4.096	3.607	3.160	2.887	2.644

Source: Energex RIN, RAB and Operational data tabs, Table 4.1, Closing value for asset value, Table 5.1 Energy delivery, Total energy delivered, Table 5.2.1 Distribution customer numbers by customer type or class, Table 5.3.3, Coincident Raw System Annual Maximum Demand, Table 5.1.2 Energy - received from TNSP and other DNSPs by time of receipt, Energy into DNSP network at On-peak times Energy into DNSP network at Off-peak times

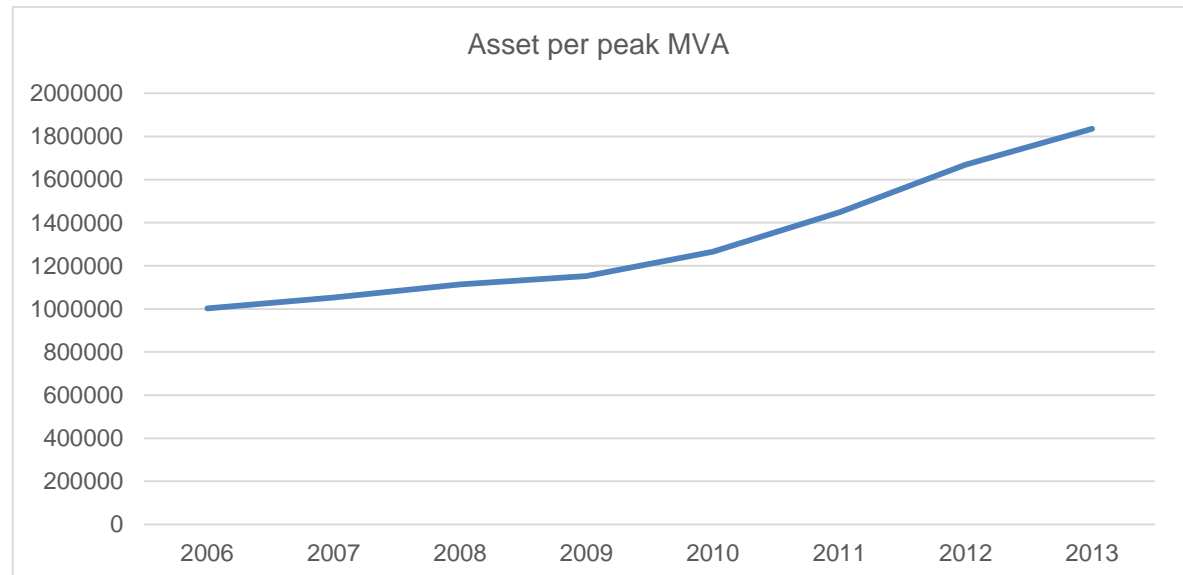
For graphical purposes we also present some of the metrics in Table 3.1 below.

**Chart 3.1 Energex peak MVA 2006-2013**



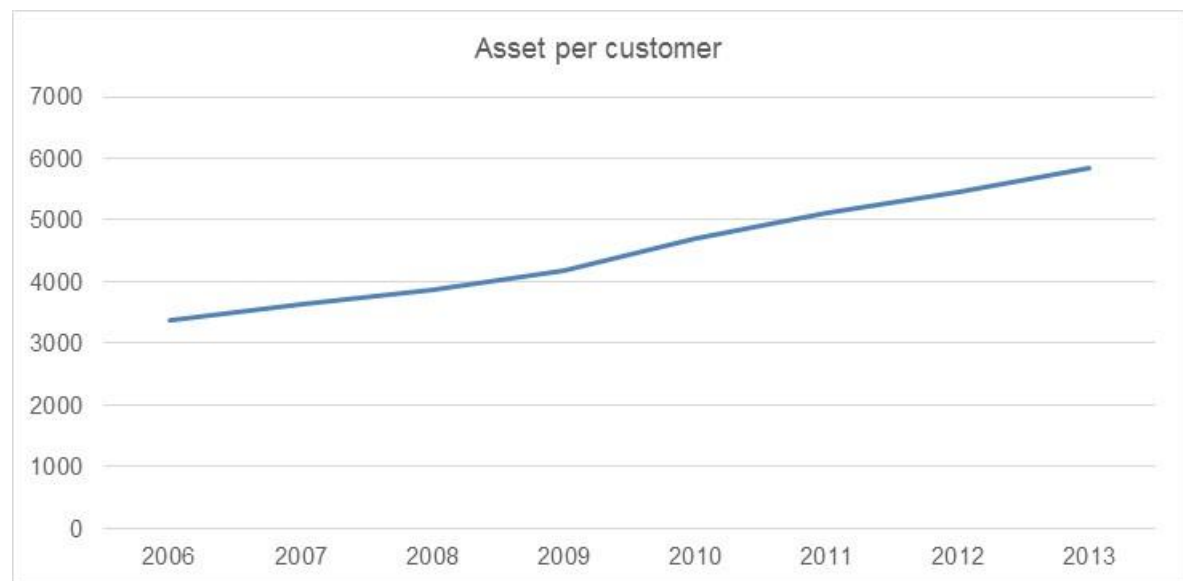
Source: Table 3.1 analysis

**Chart 3.2 Growth in assets used to deliver peak MVA – Energex network – 2006-2013**



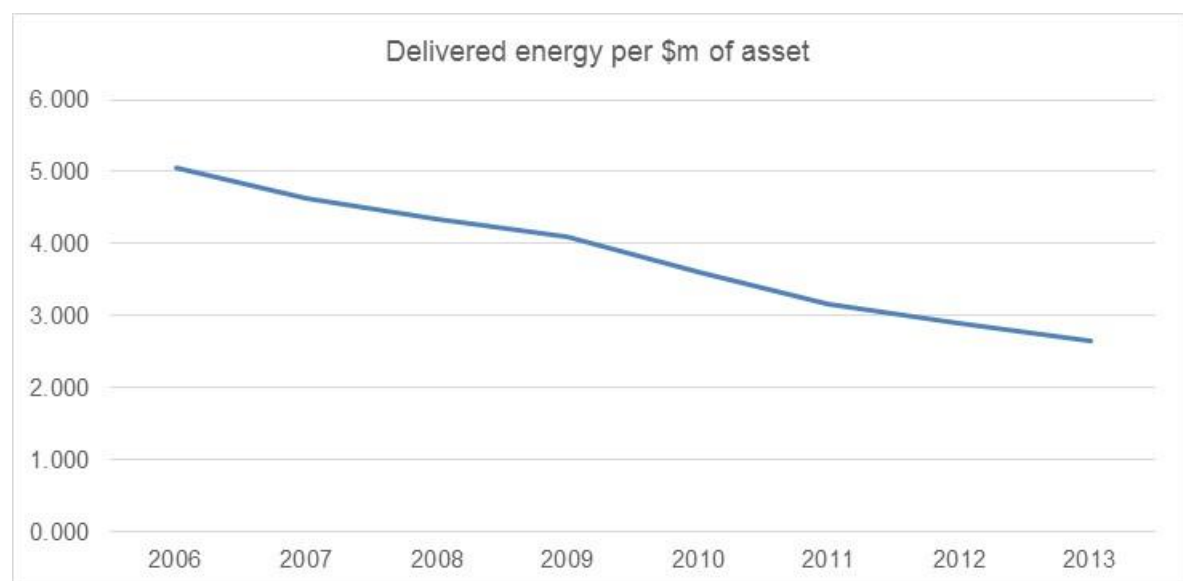
Source: Table 3.1 analysis

**Chart 3.3 Growth in assets per customer – Energex network – 2006-2013**



Source: Table analysis

**Chart 3.4 Delivered energy per \$m of assets – Energex network – 2006-2013**



Source: Table 3.1 analysis

Chart 3.1 shows that peak demand on Energex's network rose until 2010 and has declined since then. While Charts 3.2 and 3.3 show that assets used to deliver peak demand and assets per customer grew rapidly between 2006 and 2013.

Chart 3.4 shows that the delivered energy per \$million of assets declined rapidly and consistently over the period from 2006 to 2013.

We also know as previously mentioned that over the past 15 years the Queensland networks' RABs have grown at much higher rates than the networks in the other states and that the Queensland networks' levels of over-investment are the highest in

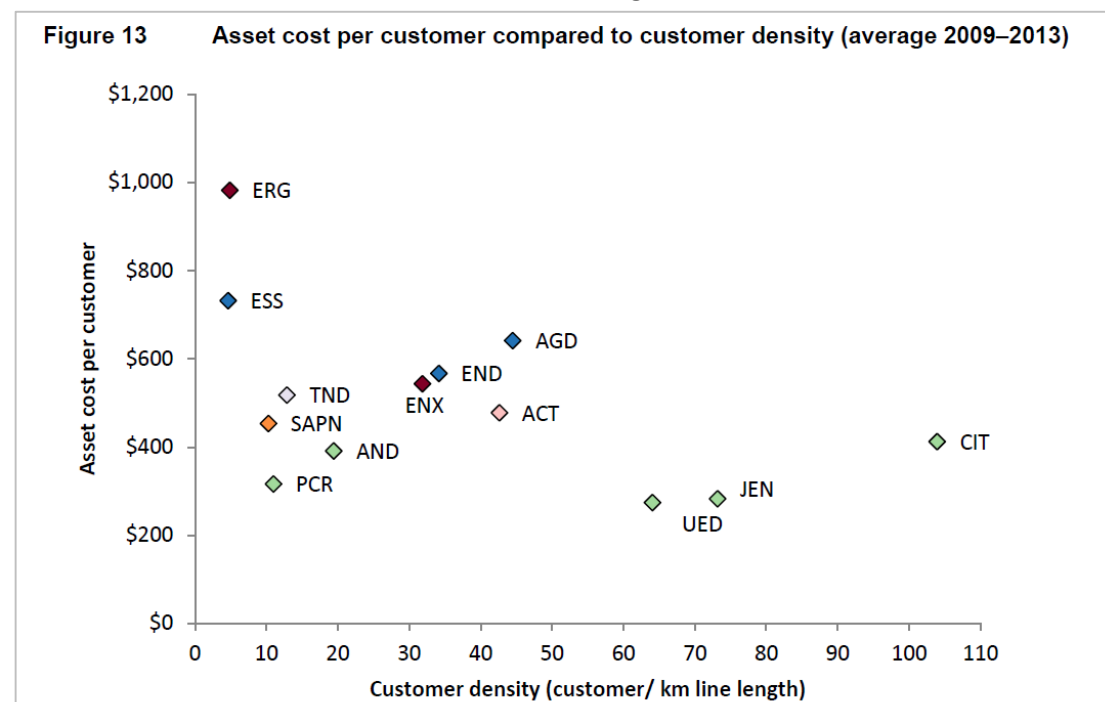
Australia. It is not surprising therefore that the Queensland networks perform poor on capital efficiency measures.

The AER published its first benchmarking report for NEM distributors - *Electricity distribution network service providers' annual benchmarking report* - in November 2014. QCOSS welcomed the release of this report and the value it offers to consumers in terms of improved transparency and information with which to assess the expenditure claims put forward by distributors.

To measure capital efficiency, the AER applied an asset cost per customer adjusted for customer density over the 2009-2013 period to assess the capital efficiency of NEM distributors.<sup>45</sup> Asset cost is defined as the sum of charges for the use of capital, namely depreciation and return on investment (rate of return or WACC) for the given period.

Chart 3.5 shows the performance of Energex and Ergon on this measure.<sup>46</sup> The results show that the Queensland and NSW distributors (marked in maroon) performed poorly compared with the Victorian and South Australian distributors, that is, they applied a high amount of assets to deliver services after allowing for the relative customer density of their two networks. This is confirmed by the measure of State-wide Multi-factor Productivity (MTFP) in the AER's benchmarking report.<sup>47</sup>

**Chart 3.5 Performance of NEM distributors against asset cost**



<sup>45</sup> AER, *Electricity distribution network service providers Annual benchmarking report*, November 2014, p25.

<sup>46</sup> AER, *Electricity distribution network service providers' Annual benchmarking report*, November 2014, p26.

<sup>47</sup> AER, *Electricity distribution network service providers' Annual benchmarking report*, November 2014, figure 17, p. 32.



The above analysis demonstrates that the Queensland networks are relatively inefficient on a number of capital metrics which suggests that the RABs are grossly inflated due to unnecessary and inefficient investments. The QPC in its draft report states (P82) that *“Energex and Ergon Energy’s RAB grew 168 per cent cumulatively from 2004–05 to 2014–15. At the same time, however, distribution network utilisation has fallen from an average of around 38 per cent in 2006 to 33 per cent in 2015”*. It then states that *“As discussed earlier, much of the growth in the RAB was attributable to meeting reliability standards, and being able to provide electricity at peak periods”*.

We find it disappointing that the QPC, by default, did not investigate further this falling utilisation in the networks in its draft report, and seems to accept that the price rises have been predominantly driven by exogenous factors and that there is limited scope to prosecute lower prices in the networks area.

Numerous studies over recent years ascertain the reasons for the networks’ different investment rates.<sup>48</sup> All of those studies have concluded that exogenous factors (such as differences in customer density, demand growth, reliability standards or ageing assets/historic under-investment), do not explain the dramatic differences in the networks’ investment levels. In essence, the studies have demonstrated that these factors do not explain the excessive investment rates of the Queensland networks.

Furthermore, we are especially concerned that the QPC has claimed that the networks’ “efficiency programs in recent years have been successful”<sup>49</sup> when there is

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<sup>48</sup> For example:

EUAA: Australia’s rising prices and declining productivity: the contribution of its electricity distributors, 2011

EUAA: A comparison of outcomes delivered by electricity transmission network service providers in the

NEM, October 2012

PIAC: Privatisation and the regulatory valuation of electricity distribution network service providers in New

South Wales: Evidence and Issues

Write-downs to address the stranded assets of electricity networks in the National Electricity Market: evidence

and argument. Report commissioned by the Total Environment Centre (TEC), April 2015

AER 2015 Annual Benchmarking Reports, November 2015

Electricity Network Regulatory Frameworks: Productivity Commission Inquiry Report, 9 April 2013

The Garnaut Review Update Paper 8: Transforming the Electricity Sector. Garnaut R. (2011)

Putting the customer back in front: How to make electricity cheaper. Grattan Institute, December 2012

Senate Select Committee on Electricity Prices: Reducing Energy Bills and Improving Efficiency

Independent Review Panel, Electricity Network Costs, Final Report

PIAC: Privatisation and the regulatory valuation of electricity distribution network service providers in New

South Wales: Evidence and Issues

AER 2015 Annual Benchmarking Reports, November 2015

Replacement Cost Asset Valuation and Regulation of Energy Infrastructure Tariffs, David Johnstone, University of

Sydney, 2003

<sup>49</sup> QPC (2016), *Inquiry into Electricity Prices*, Draft Report, P62

independent evidence that the networks have not implemented some of the recommendations of the Queensland Government Independent Review Panel (IRP) on Network costs<sup>50</sup>. For example, the recent review by Deloitte Access Economics<sup>51</sup> identified that the Queensland distributors have not implemented the IRP's recommendation that they market test the ICT services provided by SPARQ (a joint venture owned by Energex and Ergon Energy). Those ICT costs account for over a third of the Queensland distributors' capitalised overheads and have been identified as being 61-65 per cent higher than efficient levels. There are a number of other examples of efficiencies not delivered that have been provided in the Deloitte review.

The QPC should be putting in place mechanisms to seek out further efficiencies and not just from the merger between the distributors. Therefore the QPC must ensure that any "savings" from the networks efficiency programs are made at least transparent and ideally should be passed on to Queensland consumers. In particular we recommend that there is a strengthening of Draft Recommendation 12 which deals with the strengthening of the shareholders' oversight function following the merger of the distribution companies to also include:

**Recommendation:** That the QPC's Draft Recommendation 12 is strengthened to include improved scrutiny and transparency of the performance reporting of the Queensland networks and that consumers and other key stakeholders have a formal role in the oversight of the Queensland networks' performance monitoring.

### 3.4 Limitations of the national regulatory framework

Under the current regulatory rules, the AER has no power to address the Queensland networks' excessive RABs. Rather, the rules require the AER to provide the networks with guaranteed returns on their RABs. This was one of the conclusions of the Senate Inquiry which stated:

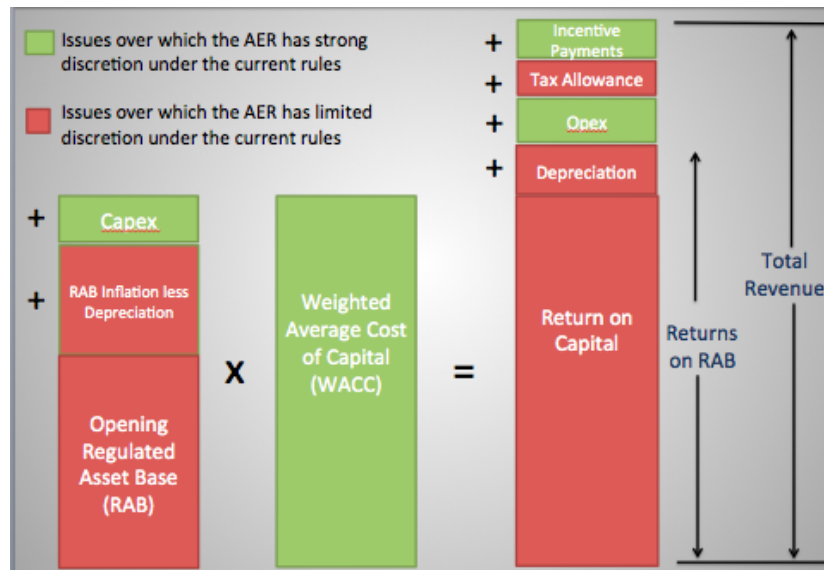
*"Despite numerous reviews, recent rule changes and positive signs from the AER as a result of its recent draft determinations, the committee considers that fundamental problems with the regulatory framework for electricity network businesses remain"*

The following diagram illustrates how returns on the networks' RABs dominate their revenue allowances and limit the ability of the AER to determine efficient revenues. Those limitations have been demonstrated by the outcomes of the AER's recent revenue decisions which have resulted in the Queensland electricity networks' prices being retained at excessive levels, with ongoing price increases over the next five years.

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<sup>50</sup> Queensland Government Independent Review Panel (IRP) on Network Costs, Final Report

<sup>51</sup> Deloitte Review of the Queensland Distributors' Labour and Workforce Practices



Importantly, the Queensland networks' excessive prices are being retained despite the major fall in interest rates compared to the previous regulatory period – the 'risk free rate' has fallen by around 3.5 per cent compared to the rate that prevailed during the previous regulatory period. If the risk free rate had remained at a similar level to the previous regulatory period, then the Queensland networks' prices would be significantly higher than the AER's recent determinations.

Returns on excessive RABs are key drivers of the networks' revenues and will continue to drive prices and profits as the networks' RABs continue to grow over the next regulatory period. As stated by previous AER Board Member, Ed Willett, when commenting on the outcomes of the AER's latest revenue determinations: *"Network prices remain too high."*<sup>52</sup>

We also point to the inadequacy of the recently introduced ex-post review provisions where, in response to widespread concerns regarding over-investment and gold plating by the networks, the AEMC's 2012 rule changes included some new rules that theoretically provide the AER with the potential to perform 'ex-post' reviews of the efficiency of capex incurred by the networks after 2014.

However, the AER's powers to perform those reviews are subject to numerous caveats and constraints that are likely to render them ineffective. For example:

- Despite the AEMC's acknowledgement that the AER's capex allowances are not necessarily efficient, the capex efficiency review is restricted to the networks' incremental spend above the AER's total capex allowance. As a result, the networks are guaranteed to recover their total capex allowances – irrespective of whether the allowances are efficient.
- It is clear from the AEMC's 2012 rule change determination and from the AER's guideline for implementing the rule changes that the AEMC and the AER expect that any capex reductions arising from the capex overspend review are likely to be extremely rare.

52 Australian Energy Regulator Annual Report 2014–15

- The AER has introduced a number of further hurdles to performing the ex-post review that will mean that it is unlikely to identify anything other than the most blatant inefficient capex overspend.

The lack of effective optimisation and ex-post capex review provisions for the NEM networks contrasts sharply with the provisions contained within other jurisdictions in Australia and overseas. For example, the Western Australian Electricity Networks Access Code and the Australian National Gas Rules require the regulator to apply a range of optimisation and 'ex-post' review tests. In a recent determination, the WA regulator (the ERA) excluded over \$200 million of capital expenditure already incurred by Western Power from its RAB, as the ERA determined that the investments did not meet the efficiency requirements of the Code. The WA regulator was highly critical of the lack of optimisation and ex-post review powers in the National Electricity Rules (NER), and considers that the powers contained within the WA Access Code are essential for ensuring the efficiency of the capital base. The WA regulator is also highly critical of the deficiencies in the National Electricity Rules (NER) that provide strong incentives for networks to "game" the regulator by over-forecasting their requirements.

Critically, our view is that deficiencies in the National Electricity Rules (NER) result in the Queensland networks being rewarded with windfall profits for their "over-forecasting errors", thereby receiving 'return on capital' allowances for capital investments that they do not incur. The Queensland networks have consistently received major windfall profits from over-forecasting demand over previous regulatory periods.

There are clear deficiencies in the national rules under which the government-owned network operate relating to the RABs, which are having significant negative impacts on the electricity prices paid by Queensland consumers. We understand that the Queensland Government works within and in conjunction with the COAG processes to achieve NEM reforms. We would however be expecting that the QPC Final Report address the excessive RABs.

Going forward, we would be looking to the QPC to recommend what proactive steps the Queensland government can take in addressing the size of the RABs in their investigation and recommendation for the Final Report. As already identified above there is limited scope for the national regulator to address these inefficient and inappropriate RABs under the current arrangements. Consequently, reform to the NEM's regulatory framework on the issue of excessive RABs is required and the Queensland government needs to work proactively with the COAG Energy Council on these urgent NEM reform challenges to the economic regulatory framework.

The QPC's Draft Recommendation 15, as currently worded, states that the Queensland Government should work proactively with the COAG Energy Council on national regulatory framework developments relating to "new technologies and business models". We recommend:

**Recommendation:** The QPC draft recommendation 15 be expanded and strengthened so that Queensland Government, in its responsibility for energy policy, proactively progresses NEM reform to address the excessive RABs.

### 3.5 Options for the Queensland Government

While we consider there should be NEM reform relating to the excessive RABs, we note that COAG processes are deliberative and consultative processes amongst many jurisdictions and often take many months if not years to arrive at agreed solutions. Therefore, the QPC should consider the impact of these excessive RABs and set out options to address their excessive valuations. As the owners of the assets, the Queensland Government has the powers to direct the networks to undertake certain activities. Therefore we recommend:

**Recommendation:** that the QPC thoroughly investigate a range of possible options to reduce the excessive RABs and ensure that revenues reflect fair returns on the Queensland Government's investment in the networks.

We note that Chapter 7 of the QPC Draft Report acknowledges the difficulty that the Queensland government has in managing its conflicting roles as energy policy setter and its role as an owner (and financier) of electricity companies. We recognise that implementing this recommendation would create necessary tension between these different roles. However, we do not agree with the QPC when discussing the challenges of the Queensland government's conflicting roles, where it asserts that the main outcome of the conflict is reduced profitability of the GOCs. As stated by the QPC:<sup>53</sup>

*"Non commercial obligations, which are generally not required of private sector counterparts, place constraints on the revenue-earning potential of GOCs and commensurately **lower returns to the shareholder**"*

Clearly the QPC's perceived outcome (lower Government Owned Corporation profits) is not supported by the returns outlined above and conclusions of various studies referenced within this submission.

The QPC Electricity Pricing Inquiry provides an opportunity to have an honest and transparent discussion with the Queensland community regarding the decisions that are required to address Queensland's high electricity prices. Our view is that the QPC Inquiry must ensure that the governance and oversight arrangements need to be such that they provide confidence to the community that a balanced outcome results between shareholder and electricity consumers' interests.

This issue was highlighted by the Grattan Institute in 2012, which recommended that:<sup>54</sup>

*"Effective 'Chinese walls' between the energy and treasury and finance functions of government may be needed in order to effectively separate governments' roles as both shareholder and financier of distributors. This is likely to reduce some incentives for governments to unduly increase investment in these companies. However, it may not completely eliminate the conflicting government objectives imposed on companies, nor the potential for political interference."*

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<sup>53</sup> Queensland Productivity Commission, Electricity Pricing Inquiry, Draft Report, 3 February 2016

<sup>54</sup> Putting the customer back in front: How to make electricity cheaper, Grattan Institute, December 2012

There is clearly a need for improved governance arrangements to enable the Queensland government to better manage its conflicting roles with respect to electricity prices. The QPC in its draft recommendations 20 and 21 does not adequately address the major improvements required to the governance arrangements to enable the Queensland Government to more effectively manage its conflicting roles. We recommend:

**Recommendation:** that the QPC revise its draft recommendations 20 and 21 to:

- Better reflect the commentary in the draft report that outlines the specific improvements required to the governance arrangements; and
- Clarify that the intended outcome is to bring balance to the conflicting roles and competing interests between energy policy (in the long term interests of consumers) and shareholders' interests.

## 4 Deregulation in South East Queensland

### 4.1 Overview

This section addresses *Chapter 8: Deregulation in SEQ* (pp115-146) and parts of *Chapter 6: Retail markets and consumers* (pp94-104) of the QPC's Draft Report.

We acknowledge that the QPC's recommendation to deregulate electricity prices in SEQ has been accepted by the Queensland Government and will be implemented from 1 July 2016. We agree with the QPC's finding in *Recommendation 18* that deregulation represents a point of significant change for consumers in the market and therefore should be accompanied by government involvement to foster trust and credibility in the reform.

We note that deregulation is commencing during a period of significant change in the electricity market, including growth in uptake of solar and changing tariff structures enabled by advanced meters. We also agree with the QPC's finding that there is a low level of consumer trust in the energy market at this time, and that this may present an underlying barrier to effective consumer participation in the market in SEQ.<sup>55</sup> It is therefore necessary to ensure deregulation is implemented alongside strong consumer safeguards, robust market monitoring arrangements and effective consumer engagement strategies to ensure the benefits of deregulation are able to be realised by residential and small business consumers.

#### 4.1.1 Recommendations

We have identified a number of areas where we believe the QPC's recommendations relating to deregulation in SEQ could be strengthened.

**Recommendation:** That the QPC investigate the merits of different approaches in order to make a recommendation that ensures the efficiency of the standing offer prices offered by retailers in SEQ from 1 July 2016. We suggest the QPC could consider a range of approaches in forming its recommendation, including:

- Adopting 'transitional' mechanisms, such as those implemented when prices were deregulated in SA and NSW, to limit increases in standing offer prices in the early stages of reform.
- Requiring retailers to publish their standing offer prices on the same day alongside a statement justifying why their standing offer prices are more, the same or less than previously.

**Recommendation:** That the QPC's Recommendations 25 and 26 more explicitly outline the package of specific indicators the QCA will report on, as outlined in the QPC's Draft Report, including those that have been recommended to the AEMC and a wide range of non-price indicators, as proposed in this submission.

**Recommendation:** That the QCA be given appropriate information gathering powers to obtain the necessary information from retailers; to undertake the proposed market

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<sup>55</sup> QPC Draft Report, p99



monitoring, and that clear compliance processes be introduced to ensure accurate, consistent and timely reporting of information across all retailers.

**Recommendation:** That the QCA be given the flexibility to identify and propose investigations into emerging energy market issues that may sit outside their specific reporting requirements.

**Recommendation:** That the Queensland Government's Customer Education Campaign commence prior to the introduction of deregulation on 1 July 2016 and include a focus on sustainable behaviour change to ensure consumers benefit from deregulation in the long term.

**Recommendation:** That Recommendation 24 be expanded to reflect the role of NGOs in assisting a wider range of residential and business consumers to engage and participate in the market.

**Recommendation:** That the QPC consider inter-jurisdictional experiences by exploring the arrangements for consumer advocacy in other states where prices have been deregulated to ensure consumer participation at a broader systemic policy level.

## 4.2 Efficiency of standing offers

We support the transitional arrangements<sup>56</sup> adopted by the Queensland Government under the NERLQ Bill 2014 to only permit retailers to increase their standing offer prices once in the first year of deregulation (rather than six monthly) and that no new fees be permitted for standing offer contracts for the first two years. In light of evidence emerging from other states where prices have been deregulated, we believe there may also be opportunity to investigate a number of additional transitional arrangements to provide further certainty and protection for consumers.

The QPC's Draft Report refers to several separate analyses – by the Australian Energy Market Commission (AEMC), Essential Services Commission (ESC) Victoria, St Vincent de Paul Society and CME – which suggest that the standing offer prices in Victoria are above industry average total costs.<sup>57</sup> The Draft Report also cites evidence of growing price dispersion in the Victorian market, with retailers offering market contracts priced at the marginal cost of supply, often with conditional pay-on-time discounts. It is understood that “*rising competitive intensity produces a higher dispersion of prices*”.<sup>58</sup> There is a suggestion that there is a cross subsidy across electricity consumers in this environment – with those on standing offers subsidising the discounts of market contract customers.

We agree with the QPC that “*well-structured standing offer arrangements play an important role and can discipline the market and increase transparency*”.<sup>59</sup> We also agree with the QPC that concerns about the effectiveness of current standing offer

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<sup>56</sup> QPC Draft Report, p143

<sup>57</sup> QPC Draft Report, p125

<sup>58</sup> Simshauser, & Whish Wilson – Reforming Reform: Differential Pricing and Price Dispersion in Retail Electricity Markets June 2015

<sup>59</sup> QPC Draft Report, p104

arrangements in the NEM “warrants further consideration by the Government”.<sup>60</sup> From our perspective, it is important to ensure standing offer prices are efficient and transparent for a number of reasons:

- There is a reasonably high proportion of customers in SEQ on standing offers (around 30 per cent of the residential market).
- There are likely to be many more customers<sup>61</sup> not captured in standing offer customer numbers who are on a market contract but are disengaged and paying standing offer prices or prices close to them.
- The QPC found that “most retailers generally advertise their market price as a percentage discount off a reference rate (standing offer price)”.<sup>62</sup> As such, customers are likely to continue to look for discounts when choosing offers in the market. Improved transparency about the base from which those discounts are made would reduce complexity and risk for consumers when shopping around.

We note the QPC has agreed with some stakeholders that “*requiring all retailers to publish their standing offers on the same day would make it easier for customers to compare and understand different electricity offers, which would help to promote greater competition in the standing offer market*”.<sup>63</sup> We consider this to be a good approach, as it not only encourages retailers to price their standing offers more competitively, but it also levels the playing field by ensuring the standing offer prices are set on the same day which provides more transparent and consistent “benchmarks” for customers who at any given time may be comparing discounted offers across different retailers. However, the QPC has only recommended this be investigated in 2018 as part of the review of the NERL which creates a risk in relation to standing offer prices in the meantime.

We note other jurisdictions have introduced transitional measures specifically targeted at improving the efficiency of standing offer prices upon the introduction of price deregulation. For example, when the South Australian Government introduced price deregulation in 2013, they negotiated a two year price freeze with the largest electricity provider AGL. Notably, price dispersions in South Australia have not increased to the levels experienced in Victoria.

In NSW, the government implemented a “transitional tariff” in 2014 when deregulation was introduced. All residential and small business consumers who had not switched to a market contract prior to deregulation, were switched over to a “transitional tariff” which was capped to rise no higher than CPI. Since that time, close to 40 per cent of NSW electricity consumers who were on the “transitional tariff” have moved onto a market contract, with 20 per cent of consumers remaining on the “transitional tariff”.<sup>64</sup> The “transitional tariff” arrangement expires in July 2016.

We present these options for the QPC’s consideration. We recommend the QPC investigate the merits of these and other approaches to protect consumers from increases in standing offer prices beyond efficient levels with the introduction of retail

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<sup>60</sup> QPC Draft Report, p141

<sup>61</sup> Exact figures are unknown as this information is not currently reported on.

<sup>62</sup> QPC Draft Report, p129

<sup>63</sup> QPC Draft Report, p104

<sup>64</sup> IPART – Removal of electricity price regulation. <http://www.resourcesandenergy.nsw.gov.au/energy-consumers/energy-sources/electricity/removal-of-electricity-price-regulation>

price deregulation from 1 July 2016. While we generally support the recommendation that standing offer prices be published on the same date be introduced from 1 July 2016, we consider it may also be beneficial for the QPC to compare and contrast a range of possible approaches to achieving this outcome.

Overall, we consider a mechanism should be introduced from 1 July 2016 to ensure standing offer prices are efficient. We believe this is necessary to strengthen consumer confidence and ensure positive outcomes for consumers in the early stages of price deregulation.

### 4.3 Market monitoring arrangements

The Queensland Government has an important role to help promote effective competition in the retail market and ensure that emerging issues are quickly identified and addressed. Robust market monitoring is critical to ensuring there is accurate and transparent information about the outcomes for consumers in the deregulated environment. We agree with the areas identified by the QPC as being important to be included in the QCA's market comparison report. These include:

- "A comparison of standing and market offer prices for the more commonly used offers and tariff structures"
- "Standing offer prices"
- "Most common market offer prices by number of customers"
- "Lowest generally available market offers"
- "A comparison of the types of discounts available for each relevant tariff type"
- "Commentary on the extent to which not meeting conditional discounts affect what customers pay"
- "A comparison of bills for customers on standing offers and market offers, with and without conditional discounts"
- "An historical analysis of standing and market offer pricing trends for specific tariffs and general commentary on the emergence of new types of tariff structures or offers"
- "An analysis of changes in the underlying electricity supply costs"
- "An indication of overall trends in the cost of supplying electricity in SEQ and whether price changes in the market are broadly consistent with changes in underlying costs".<sup>65</sup>

We believe these measures should be stated more explicitly in Recommendations 25 and 26. The current recommendations do not sufficiently ensure that these indicators will be part of the market monitoring arrangements.

We particularly emphasise the need for market monitoring to provide information about what consumers are actually doing in the market and the outcomes they are achieving, rather than just collecting information about what is available in the market and estimates of what bills might be or consumers might save on various available contracts. Without information about what consumers are actually doing, it is impossible to assess how well the market is working for the benefit of consumers.

We note the QPC has also discussed the need for the market monitoring framework to draw on EWOQ complaint data and identify the bill impacts for customers. We

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<sup>65</sup> QPC Draft Report, p140-141

suggest the assessment of bill impacts be included in the QCA's annual report and that it include a range of example customer types including those with solar PV and controlled load tariffs to provide a holistic assessment of the range of consumer outcomes in the market.

We also note the QPC has agreed with several suggestions by stakeholders that the AEMC should monitor:

- “Non-price competition, including developments in customer service that are designed to improve the customer's experience. This would further highlight the benefits of rivalry and competitive tension between retailers”.
- “A broader definition of the product market (i.e. electricity and gas) is appropriate to take into account functional and temporal aspects of the increased penetration of rooftop solar PV on retail electricity markets”.
- “Retention behaviour by incumbents who offer large discounts to retain existing customers who may be attracted to another retailer's offer. These customers do not appear in the churn statistics, but arguably they have benefited from competition”.
- “A more detailed examination of retail margins, the subsidisation of market contract customers by standing offer customers, and the overall cost of electricity for consumers in SEQ”.<sup>66</sup>

With regard to the benefits of non-price competition described above, we believe service quality associated with hardship programs that support residents and businesses with financial difficulties is important, as there is limited public and transparent information about this in the market. Similarly, the QCA's monitoring should also report on quantity and scope of other non-price benefits being delivered by retailers; such as energy efficiency audits and other services to reduce energy costs, as these can add significant value for customers.

We recommend the QPC direct the QCA to monitor each of the above aspects in the Queensland market should the AEMC not incorporate these indicators into their review processes.

Critically, to be able to do undertake its role effectively, the QCA must be provided with all necessary authority to be able to gather the appropriate information and data on consumer involvement with the market, including the contracts consumers are currently utilising and information about those consumers who are not engaging with the market. We note this is an existing limitation for the AEMC in their review of the effectiveness of competition across the NEM.

We note the QPC has suggested “*the QCA could effectively monitor price changes in SEQ by requesting relevant information from retailers (or potentially through an arrangement with the AER)*”.<sup>67</sup> We recommend a robust procedure must be in place to ensure the information can be gathered and publicly reported as part of the market monitoring approach. This may require legislative change where the QCA does not have the necessary authority. It will be important that there are clear compliance processes for reporting to ensure the information provided is accurate, timely and consistent, and thus readily comparable across all retailers.

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<sup>66</sup> QPC Draft Report, p137

<sup>67</sup> QPC Draft Report, p140

While we agree it is preferable that the QCA does not duplicate existing reports, we consider it necessary for the QCA to undertake some activities that may be being undertaken under other reporting frameworks if those agencies are not able to respond to the specific needs of the Queensland market. For example, we acknowledge that the AEMC is limited in its ability to add or amend its questions in its consumer surveys in order to ensure consistency and comparison of data with previous years and across jurisdictions. The QCA should be given the flexibility to capture emerging issues in its reporting if the AEMC is unable to do so.

Finally, we note the Energy Minister will retain the ability to request the QCA to undertake a more comprehensive independent investigation into the state of competition in the SEQ market at any time. Given the status of the energy market and emerging technologies and business models, we suggest the QCA also be given flexibility to identify and propose investigations into energy market issues that may emerge in Queensland and may sit outside its specific reporting requirements. This flexibility is essential to ensure the issues are able to be identified as they emerge and are not unnecessarily stalled by procedural delays. The market monitoring framework must be versatile enough to meet emerging market conditions, and any subsequent issues that arise from deregulation.

## **4.4 Consumer engagement and participation**

We understand the Queensland Government is developing a Customer Education Campaign to engage and inform residential and small business consumers in SEQ ahead of deregulation. We support this approach as a necessary component to ensuring the success of the reform.

We emphasise that the focus of the campaign is ultimately behaviour change and thus must go beyond simple advertising messages and information provision. We also emphasise the need for consumers to not only shop around in response to the immediate campaign, but also continuously and regularly participate in the market to ensure the competitive market continues to deliver positive outcomes for consumers. The focus of this campaign must therefore be on achieving long term behaviour change.

The campaign must also capture a range of consumers and address their specific needs, including vulnerable consumers, residential and small business customers. We refer to the QPC's Recommendation 24 which identifies the need to provide assistance to vulnerable consumers through NGOs. We consider that NGOs have a vitally important role and should be engaged to reach a broader range of consumers including non-profits, small businesses and special interest groups. We suggest Recommendation 24 be expended to reflect the role of NGOs in assisting a wide range of consumers to fully participate in the market.

Finally, given the importance of consumer participation during this period of significant change in the SEQ electricity market, it is essential that there are mechanisms to ensure not only effective consumer participation in the market at an individual level, but also at a broader systemic policy level. We consider there is opportunity for the QPC to consider inter-jurisdictional experiences by exploring the arrangements for consumer advocacy in other states where prices have been deregulated.

