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Queensland Productivity Commission
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Electricity Pricing in Queensland: Response to Issues Paper

EnergyAustralia welcomes the opportunity to make a submission on the Queensland Productivity Commission's *Electricity Pricing in Queensland* issues paper.

EnergyAustralia is one of Australia's largest energy companies, providing gas and electricity to 2.6 million household and business accounts across the National Electricity Market (NEM) with a diverse generation portfolio of coal, gas and renewable assets. We serve approximately 100,000 retail customers in South East Queensland.

We recognise that long term policy development requires considered, objective and constructive dialogue to achieve clear economic and social outcomes. The Queensland Productivity Commission (QPC) should be congratulated on a thorough and balanced issues paper that clearly establishes and contextualises the key issues.

This inquiry will provide advice to the Government on options to improve outcomes for Queensland electricity consumers. Terms of Reference and the scope of the inquiry are very broad and as a large electricity retailer, our focus is on the end customer and this submission covers those issues that we believe are particularly important to secure the best outcomes for our customers.

EnergyAustralia believes a competitive, deregulated and nationally harmonised electricity market, where customers can choose the most suitable and lowest cost products, and where vulnerable customers are appropriately protected, delivers the best mix of outcomes for consumers.

We would welcome the opportunity to explore this proposal in greater detail with the QPC.

Yours sincerely,

Ken Macpherson
Head of Reputation

Introduction

The energy industry is going through a period of rapid transformation with new disruptive technology, embedded generation, regulatory reform and consumer trends changing each component of the traditional energy supply chain. This inquiry is timely and aligns with key priority issues in the COAG Energy Council's work plan, particularly in relation to promoting competition in retail and wholesale markets and promoting efficiencies from consistent national frameworks.

EnergyAustralia supports a competitive electricity market where the costs of electricity to customers are fair and equitable, investments are rewarded and vulnerable customers are appropriately protected. Promoting the long term interests of customers requires competition to incentivise retailers to reduce or discount prices to attract and retain customers and to encourage product innovation.

We support the harmonisation of national energy rules and regulations to create an efficiently operating energy market that minimises costs as a result of duplicated yet inconsistent regulations. Adopting the National Energy Customer Framework (NECF) in Queensland has helped to reduce the regulatory burden on retailers and ensure strong consumer protections for Queensland customers.

This submission is structured to provide comments to the inquiry following the energy supply chain, starting with our customers and the retail market, then networks and finally aspects of electricity generation and the wholesale market.

Retail

Retail electricity businesses, unlike other parts of the supply chain interfaces with mass market customers. This makes retailers most able to deliver products and services to drive further productivity and provide benefits to customers.

Commitment to Retail Price Deregulation

> EnergyAustralia supports the introduction of retail electricity price deregulation in SE Queensland on 1 July 2016.
>
> Deregulation is necessary to enable EnergyAustralia to confidently make further investments in a South East Queensland growth strategy in the near term.

Customers have been able to choose their electricity retailer in South East Queensland since 2007, however the Queensland Competition Authority (QCA) sets regulated tariffs (known as notified prices) for standard retail customers, and in the absence of full competition retailers use this as a benchmark price for market customers.

EnergyAustralia currently offers a single product called Flexi-Saver in South East Queensland which is set at the QCA regulated tariff (of 22.238cents/kWh), but currently offers a 10% pay on time discount and a $50 credit on the first bill. By comparison, AGL and Origin also offer their prices at the regulated tariff and typically offers around the same in-market discount, reflecting minimal product and price differentiation between the offers of Australia's three largest energy companies. Retail price deregulation would provide the incentive for retailers to offer different products and prices to attract new customers because retailers will have more flexibility in how they set tariff structures.

EnergyAustralia is headquartered in Victoria and has actively participated in the recent deregulation of the South Australian and New South Wales electricity markets. All of these markets have benefitted from new entrants, resulting in a greater range of products available to customers and a high level of customer engagement in the market.

The Victorian market is particularly competitive with 21 electricity retail brands and a 28% churn rate per annum, mostly away from incumbent retailers. In South Australia, there are 16 retail brands with 54 electricity products available in Adelaide alone with 81% of customers on market contracts. New South Wales has 20 retail brands, four of which entered the market following price deregulation on 1 July 2014.

In our experience, the metrics identifying competitive behaviour and customer engagement typically understate the level of engagement in newly deregulated jurisdictions (such as South Australia). Customer churn rates are commonly used to indicate competitive activity, however this does not capture retention behaviour by incumbents who offer large discounts to retain customers when challenged. That is, if a customer is attracted to another retailer by a strong offer, the customer's existing retailer will work to retain their existing customer by offering an even better deal. While these retained customers do not appear in the churn statistics, they have benefitted from competition.

The AEMC notes that competition is effective in the South East Queensland retail electricity market, enabling electricity customers to choose from a range of energy plans from 11 different retail brands.[1] In their 2015 review of retail competition, the AEMC considers there is sufficient competition in the South East Queensland electricity market for customers to benefit from removal of retail price regulation.

The existing South Eeast Queensland market is dominated by AGL and Origin Energy, with the two holding approximately 81% of the retail market share. EnergyAustralia is a challenger brand in this market (with a 7.5% market share in SE Queensland) but has the experience and resources to contest the incumbents on both price and product. However, making an investment to grow brand recognition and launch new products is only commercially attractive if the market conditions facilitate competition as price deregulation does.

Price deregulation of electricity in South East Queensland is important to enable EnergyAustralia to have the confidence there is a growth market in Queensland to underpin our investment in the state.

Early decision on deregulation is required to avoid service issues for customers

Timely advice on whether the Government will deregulate on 1 July 2016, or whether the QCA will be required to determine regulated tariffs, is critical to enable retailers to update billing systems and deliver timely communications to customers.

To ensure the best outcomes for consumers, retailers require adequate lead times to properly manage communications with customers and update complex billing systems. To adjust billing systems accordingly, notification of the Government's intention to implement deregulation, or otherwise, is required six months ahead of the implementation date, or by the end of January 2016 (immediately following the release of the draft Report). This is particularly relevant if the decision is to not move to deregulation and the QCA are required to determine regulated tariffs. To update billing systems, final regulated prices are required by16 May 2016, being a full six weeks ahead of the 1 July re-price.

[1] AEMC report 2015 Retail Competition Review (30 June 2015)

The late decision to postpone deregulation and the consequential delays to the QCA notified prices in early 2015 caused significant problems for retailers, including delays to billing system updates, delayed letters to customers, a significant number of bills being blocked until prices could be updated in the billing system and an inability to quote new customers before new prices were reflected in the customer care system. We would urge the Queensland Government to provide advice on its intention to deregulate in January 2016 to avoid a repeat of these issues in 2015 and ensure we can deliver the best possible service to customers.

Consumer engagement ahead of deregulation

Should the Government make an early decision to transition to deregulation, a coordinated communications plan should be established with key retailers leaving sufficient time for its implementation ahead of 1 July 2016.

Engaging and informing consumers about the benefits of a deregulated market is critical to successful market reform. Deregulation means better deals are available to customers, but it also means that customers need to be aware of the choices available and actively participating to select the best offer for each individual customer.

EnergyAustralia would point to the New South Wales Government's customer engagement and communications plan as a good example of how to communicate the benefits of deregulation to customers.

Coordinated communications from the retailers supplemented a comprehensive NSW Government strategy. A close working relationship between Government and the retailers delivered a strategy six months before of the commencement of deregulation.

As part of this strategy, customers received bill inserts prior to deregulation and a letter at the time of reprice (1 July 2014). EnergyAustralia call centres and websites had a set of FAQ's that answered a set of questions and provided further information and resources for customers. The NSW Government established a website (http://www.yourenergy.nsw.gov.au/) and ran a series of TV advertisements. The messaging to customers was simple and effective:

1. It is quick and easy to switch;
2. You can save money;
3. There is a free, independent source of information where offers can be compared; and
4. Consumer rights are protected and your energy supply will not change.

Vulnerable customers

EnergyAustralia believes the NECF consumer protections, the additional protections implemented by the Queensland Government and the market monitoring regime are adequate to protect vulnerable customers in transition to deregulation.

While deregulation drives competitive offers in the retail market, it is important to recognise that there are some customers who may be unable to participate in the market or are experiencing longer term affordability challenges. Accordingly, consumer protections and support for vulnerable customers are an important consideration in the Queensland electricity policy discussion.

Protections for vulnerable consumers have already been improved to facilitate the move to deregulation. The harmonised National Energy Customer Framework

(NECF) came into effect in Queensland on 1 July 2015. The NECF is overseen by the Australian Energy Regulator (AER) ensures consumers have a comprehensive array of protections such as energy hardship plans and access to a nationwide energy comparator service to help households understand and compare energy use and offers. Additional to the NECF provisions, the Queensland Government has added further protections to support their customers experiencing financial difficulty due to hardship. These additional protections include providing information about flexible payment options, requiring retailers to provide at least one market contract without exit fees, capping other exit fees at $20 and providing stipulated advance notice of price increases and the expiry of any other benefits (such as discounts).

EnergyAustralia believes the consumer protections under NECF, the additional protections implemented by the Queensland Government and the market monitoring regime are adequate to protect vulnerable customers as it moves to deregulation.

Concession Programs

EnergyAustralia supports a thorough review of the concessions framework in Queensland to determine the policy intent and develop an operationally effective program. We strongly support a move to nationally harmonised concession programs to minimise the unnecessary and additional costs of duplicated and inconsistent concessions between state jurisdictions.

Concessions are government funded payments to specific groups of consumers to assist with the cost of energy and are intended to improve outcomes for vulnerable customers. Retailers manage the payment of concessions to the customer on behalf of the jurisdictional government. Notwithstanding our desire to assist the most vulnerable customers, administering concessions are a particularly difficult issue for retailers across the NEM.

The structure and operation of concession programs are inconsistent between each State and currently EnergyAustralia is providing 19 different concessions. They are expensive to administer and any administration fee provided by the Government does not reflect the true cost of providing these services.

Concession programs require significant billing system resources and any changes to these programs (which occur frequently) require expensive system updates. In addition to bearing the real cost of the programs, the retailer also carries the risk of overpayment should any part of the concession process, including verification and other components out of our control, break down. In these scenarios, it is not appropriate for retailers to recover over-payments from vulnerable customers. Ultimately, the cost of providing these concession programs is borne by the entire customer base.

Given the complexity of jurisdictional concession schemes outlined in Appendix C of the issues paper, we strongly support a move to nationally harmonised concession programs to minimise the unnecessary and additional costs of duplicated and inconsistent concessions between state jurisdictions. Nationally harmonised concessions would also remove significant confusion between customers in different states, for example the structure and quantum of NSW and Queensland concessions are markedly different on either side of the Tweed.

The true cost of providing concessions, including system changes, commercial risk exposures and administrative support by retailers should be incorporated into the overall cost of providing the concession program by the Government.

EnergyAustralia supports a thorough review of the concessions framework in Queensland to determine the policy intent and develop operationally effective programs that consider the real costs and risks of all participants.

Regional Queensland

> The 'non-reversion policy' whereby small customers who take up an offer from another retailer may not return to Ergon Energy Retail has no benefit, is not cost effective and is a further impediment to competition in regional Queensland.
>
> Many options exist for altering the UTP and CSO and the commercial impacts should be considered before a decision is made.

EnergyAustralia only markets to large customers in regional Queensland as the combination of the Uniform Tariff Policy (UTP) and the Community Service Obligation (CSO) means that the costs of supplying small customers exceeds the returns even in the lower cost areas of the Ergon network. We acknowledge there are higher costs in supplying electricity to regional customers in a geographically large state. The changes previously proposed to the UTP and CSO by the QCA would help in part to overcome these barriers to competition.

However, regardless of the decisions around the future of the UTP and CSO, the 'non-reversion policy' should be removed immediately. This policy, set up by the Queensland Government, requires that a small customer who has transferred away from Ergon Energy Retail cannot return. The intent of the policy appears to have been to encourage competition to evolve organically, but in a one-way direction. In effect, it has given customers only one choice of retailer and creates a lot of additional costs for other retailers to acquire small customers in regional Queensland. Retailers other than Ergon Energy Retail would make substantial losses in trying to serve customers by not receiving the CSO and by incurring costs to set up compliant billing for any customers who are acquired.

This is more than a theoretical problem as large customers in regional Queensland can become small customers[2] when they reduce their usage, or when the site is taken over by a new customer with low usage. In these cases, the retailer may still not return these customers to Ergon Energy Retail. This issue acts to discourage other retailers from winning the large customers in regional Queensland as well as the small customers. While there will be some savings to the Queensland Government through very slightly lower CSO payments, these savings will be outweighed by costs borne by other retailers and ultimately consumers.

The 'non-reversion policy' is therefore inefficient, a hindrance to competition, is not leading to positive outcomes for customers or retailers and should be removed.

We don't offer any particular recommendations regarding the optimal way to amend the UTP and CSO as it would require a more detailed analysis of the options. A fuller analysis of the unsubsidised costs of supplying customers in regional Queensland would be useful, especially to identify where some towns may be served more cost effectively in future by a local rather than state-wide solution.

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[2] A small electricity customer uses less than 100MWh per annum

Transmission and distribution

> EnergyAustralia supports initiatives to alleviate pressure on our customers and in this context we support the AER's scrutiny of network revenue proposals and applaud the Queensland Government's decision not to appeal the AER final determinations.
>
> As the energy industry transforms, the role of network businesses should not, without appropriate consideration and ring-fencing protections, extend into provision of contestable services.

Network costs have risen dramatically across the NEM over the past decade and have driven large increases in retail electricity costs to households and businesses. In Queensland, which has a large and diverse transmission and distribution system, network costs have escalated by 243% in real terms in the past decade and account for approximately 45% of a typical residential bill. Network driven price increases have contributed to increased cases of hardship amongst households.

EnergyAustralia supports the approach of the AER to benchmark distribution network revenue determinations and ensure their allowable revenue reflects the recovery of efficient costs while ensuring reliability can be maintained. This will ease pressure on our customers and we commend the Queensland Government's decision to respect the AER's final determinations.

EnergyAustralia supports the principle of network tariff reform which seeks to ensure tariffs reflect the efficient cost of providing electricity to consumers. This will encourage more efficient use of network infrastructure and minimise costs over the longer term.

Tariff reform should be mandatory for networks if it proceeds and retailers will then be able to incorporate those tariffs into retail service offerings that reflect customers' preferences and needs. Distributors, retailers and government each have a role to promote awareness of the rationale for network tariff reform and the opportunities it affords to customers. "Opt–in" or opt-out" arrangements are problematic, both for consumers but also for retailers who will incur significant costs to develop systems that can accommodate all available tariffs; the extent of take-up under either approach cannot be predicted with any certainty. Furthermore, such arrangements maintain cross subsidies inherent in current tariff structures and undermine the benefits of reform.

We await the Queensland networks' Tariff Structure Statements and welcome the opportunity to contribute to the AER's consultation process. From the perspective of the retailer, and recognising that the retailer is the interface with the customer, we recommend a consistency of approach to tariff reform across networks as far as possible. This will enable them to be incorporated into customer care and billing systems and to be communicated to customers. We note that the Victorian distribution networks have proposed to introduce monthly demand charges and expect the Queensland networks may adopt a similar approach, particularly if their tariff structure for larger customers provides some indication.

Finally, the future for distribution networks is changing with the widespread deployment of distributed energy and the potential of storage technology. The current distribution regulatory framework is based around long term monopoly owned assets with a regulated rate of return, however around Australia we have already started to see some distribution businesses seeking to include batteries in their regulated asset base as part of proposed network augmentation and otherwise move into contestable non-network activities.

Distribution businesses are not well placed to capture the full value of battery technology and other contestable services to consumers and across the supply chain. These non-network services would be more efficiently delivered to consumers if subject to competitive market forces. To enable this, as a minimum monopoly network services need to be carefully defined and differentiated from contestable services and network revenue determinations should avoid any bias in favour of network solutions

Network businesses should also be subject to appropriate ring-fencing requirements (which are adequately monitored and enforced) in order to ensure competitive neutrality is maintained. It is important, from the customer's perspective, that network costs reflect the efficient costs of providing the service and a single clear channel of communication exists between the retailer and the customer. As such, EnergyAustralia looks forward to the AER's new guideline for ring-fencing, which we understand will be in place towards the end of 2016.

Generation

Generator consolidation

To ensure improved outcomes for consumers, we support healthy competition in the wholesale market and a deep and liquid contract market into the future.

Unlike other NEM states, EnergyAustralia does not own or operate generation in Queensland, but rather contracts wholesale supply to meet our mass market loads, which are currently relatively small. With liquidity in the Queensland contract market, we currently have ongoing access to contracts to meet our needs.

As the Issues Paper notes, Queensland wholesale prices have gradually risen from $55/MWh to a forward price of $90/MWh in Q1 2016 driven by steady, increased electricity demand in Queensland primarily from LNG ramp-up. This follows a sustained period of low demand, generation over-supply and increased solar generation and reflects a wholesale market operating as it was designed.

The proposed merger of the government-owned generators (CS Energy and Stanwell) impacts 63% of Queensland's generation capacity and has the ability to diminish competition in the wholesale market. EnergyAustralia supports healthy competition in the wholesale market and a deep and liquid contract market into the future.

Renewables

Reliability and cost of energy to households and businesses are vital criteria in assessing new renewable energy policies and initiatives.

A nationally consistent approach to reduce emissions provides the most efficient and lowest cost way to achieve Australia's emissions reduction goals.

An integrated approach to energy and climate change policy nationally, and within states, is needed to overcome the barriers to consistent longer-term policies that need to work together across competing objectives.

Isolated targets to one form of technology, such as renewable energy, are unlikely to provide for the most efficient reduction of emissions. For this reason state-based renewable energy targets are not our ideal mechanism.

Instead the focus should be on providing access to small scale distributed generation or energy efficiency upgrades for those who have traditionally missed out and are arguably most in need, such as renters and social housing occupants.

The Queensland government has made substantial commitments in relation to the development of renewable energy in the state. These include a state target of 50% renewables by 2030, installation of solar on a million rooftops (approximately 3,000MW) by 2020, establishing a fair price for solar exports to the grid and trialling a 40MW renewable energy auction. Recognising that Queensland has the best solar resource in eastern Australia, we understand the desire of the Queensland Government to attract investment with greater support for renewable energy, particularly large-scale and household solar.

EnergyAustralia supports a nationally consistent approach to renewable energy policy and this provides a more efficient way of reducing emissions and deploying renewable energy to consumers. State-based renewable energy schemes that provide subsidies to certain participants do so by introducing distortions to the market that increase electricity bills.

With a focus on improved outcomes for the customer, deployment of renewable energy should be balanced with providing reliable and cost-effective supply of electricity. Wholesale market conditions and the technical capability of transmission networks may enable a modest amount of additional renewables to be added, but careful analysis of predicted outcomes of additional renewables should be undertaken prior to firm commitment being made by Government. To achieve 50% renewables by 2030 from a starting point of 5% in 2015, significant thermal baseload generation would be required to be replaced by solar. Notwithstanding the excellent solar resource in Queensland, the defined solar afternoon peak generation profile would suggest this may be difficult without storage and increased gas fired generation.

Feed-in tariffs implemented by various State/Territory governments have played a significant role in encouraging almost 1.5 million household solar PV installations across the country. However, overly generous feed-in tariffs have created a $5 billion cost subsidy from those without solar PV to those that do have solar[3]. In Queensland it is forecast the generous Solar Bonus Scheme will cost $3.4 Billion by 2028 and is adding up to $276 to each Queensland household electricity bill in 2015/16[4]. This has placed an unnecessary cost burden on non-solar consumers, particularly vulnerable consumers. We comment on this further in response to the QPC's inquiry into Solar Feed-in Pricing.

The current regulatory framework prevents the benefits of distributed generation being equally shared amongst all customer groups. We encourage the Government to consider changes to reduce the split incentive by supporting small scale customers who have historically missed out on subsidies to gain access. This includes renters, tenants of public housing, retirement villages or apartment occupants who, for various reasons, have been unable to access solar generation.

We recognise and welcome the desire of the Government to develop more renewables, particularly given the world-class renewable resources available in the state. However, national policies such as the Renewable Energy Target and funding through ARENA are expected to bring through substantial investment into the Queensland renewable market, particularly for large-scale solar. The Government needs to ensure any policy mechanisms do not overshoot what these measures will deliver and put extra costs on consumers as we have seen with the Solar Bonus Scheme.

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[3] The Grattan Institute, *Sundown, Sunrise: How Australia Can Finally Get Solar Power Right,* May 2015, p.15

[4] QCA: Estimating a fair and reasonable solar feed-in tariff for Queensland. March 2013