



4 March 2016

Mr Kim Wood
Principal Commissioner
Queensland Productivity Commission
PO Box 12112
George St QLD 4003

Dear Mr Wood

RE: ELECTRICITY PRICING INQUIRY – DRAFT REPORT

ERM Power Limited (ERM Power) welcomes the opportunity to respond to the Queensland Productivity Commission's (QPC) Draft Report for its Electricity Pricing Inquiry.

About ERM Power Limited

ERM Power is an Australian energy company that operates electricity generation and electricity sales businesses. Trading as ERM Business Energy and founded in 1980, we have grown to become the fourth largest electricity retailer in Australia, with operations in every state and the Australian Capital Territory. We are also licensed to sell electricity in several markets in the United States. We have equity interests in 497 megawatts of low emission, gas-fired peaking power stations in Western Australia and Queensland, both of which we operate.

General comments

ERM Power welcomes QPC's Draft Report, which recommends a number of significant reforms to the Queensland (QLD) electricity market that will encourage the development of a competitive retail market, and ultimately benefit QLD electricity consumers. In particular, we strongly support the following draft recommendations:

- that the QLD Government should not merge CS Energy and Stanwell;
- that deregulation of South East QLD (SEQ) electricity prices should commence as planned on 1 July 2016; and
- that the QLD Government should reform its Uniform Tariff Policy by implementing a network Community Service Obligation (CSO).

Full implementation of these draft recommendations by the QLD Government is expected to support ERM Power's active participation in the small electricity consumer market in SEQ, and entry into regional QLD. QLD businesses stand to benefit from the availability of ERM Power's market-leading customer service and innovative product offerings when considering their electricity product options.

The attached submission responds only to those draft recommendations where ERM Power has particular views.



If you would like to discuss this submission further, please contact Jenna Polson on 03 9214 9347, or jpolson@ermpower.com.au.

Yours sincerely,

[signed]

Jon Stretch
Managing Director & CEO

RESPONSE TO DRAFT RECOMMENDATIONS

Draft recommendation 4

The Queensland Government should not merge CS Energy and Stanwell, given the likely reduction in competition in Queensland's already concentrated wholesale electricity market and the likely consequence of higher wholesale electricity prices.

ERM Power strongly supports this recommendation. Given the combined market share of these government-owned generator-retailers, a merger would increase their wholesale price-setting power and reduce retailers' hedging options to the extent that already-stagnant retail competition would deteriorate further. This would ultimately lead to increased retail electricity prices, materially outweighing any economic efficiency benefits that Government may have realised.

Draft recommendation 7

The Queensland Government should require CS Energy and Stanwell to develop and adhere to a common voluntary Code of Conduct (the Code) in respect of their rebidding behaviour. The Code should be developed as part of a public consultation process.

We welcome recognition of the QLD Government's role in ensuring its generation assets comply with both the "letter and spirit" of the National Electricity Rules' good faith rebidding provisions. We support the concept of a Code of Conduct, outlining the basis for rebidding behaviour by CS Energy and Stanwell. We agree that making such a Code publically available would support market confidence in the generators' behaviours. However, it is unclear whether this can be achieved through a voluntary Code. ERM Power believes that a mandatory Code of Conduct for CS Energy and Stanwell is a more appropriate response to ensure the intent of this draft recommendation is delivered.

Draft recommendation 8

The Queensland Government should require CS Energy and Stanwell to report to the Government, on an annual basis, all late rebids submitted to the Australian Energy Market Operator. This report should be audited by an independent body, and the findings of the audit made available to the public.

ERM Power supports the intent of the draft recommendation to require CS Energy and Stanwell to undertake annual reporting on all late rebids performed, to increase transparency and accountability for rebidding behaviour. Having said that, it is unclear the extent to which additional reporting obligations may alter the QLD generators' behaviours beyond what would have otherwise occurred.

Additional scrutiny of the implications of CS Energy and Stanwell's behaviours for the retail market is more likely to be of value. Not only do these generators represent the majority sources of trading instruments for retail businesses, but they also operate their own retail businesses. It is important that a retailer's affiliation with CS Energy or Stanwell does not provide a competitive advantage through access to contract terms or information that may not be accessible to other retailers. ERM Power recommends a monitoring and auditing regime to ensure the behaviour of CS Energy and Stanwell does not have adverse implications for the retail market.

Draft recommendation 9

The Queensland Government's Renewable Energy Taskforce should consider:

- the cost and price impacts of a Queensland target;
- the merits of including small scale solar in a renewable energy target; and
- the benefits of an inter-jurisdictional approach to emissions reduction policy.

The QLD Government has appointed a Renewable Energy Expert Panel which will lead a public inquiry into establishing a 50 per cent renewable energy target by 2030.

ERM Power shares stakeholder concerns that disparate jurisdictional policies increase regulatory uncertainty, which can undermine efficient market operations and investment decisions. The history of both federal and jurisdictional renewable and energy efficiency subsidy schemes introduced in Australia in the past decade clearly demonstrates the unintended market distortions and costs that can be created by unstable policy.

Any jurisdictional or inter-jurisdictional renewable energy or emissions reduction scheme must be well-designed, developed in close consultation with industry, and must have bipartisan, long term objectives.

Draft recommendation 10

In order to achieve least-cost carbon abatement, the Queensland Government should work with the COAG Energy Council to find opportunities for collaboration on carbon policy, as an alternative to pursuing independent action.

ERM Power supports collaboration with other jurisdictions to develop a consistent policy approach to carbon reduction.

Draft recommendation 11

The Queensland Government should not intervene in the solar PV market to achieve a 3000 MW capacity target for solar PV uptake in Queensland by 2020.

Modelling undertaken by ACIL Allen for the Draft Report clearly demonstrates the disproportionate costs required to achieve the election commitment to install one million rooftop solar PV systems (or 3,000 MW capacity) by 2020. Given modelling shows that the absence of intervention would only delay target achievement by two years, we agree that these costs are not justified. ERM Power therefore supports this draft recommendation for the QLD Government to abstain from interventions in the solar market to achieve targets by 2020.

Draft recommendation 14

Where network businesses are engaged in potentially competitive functions, the holding company should:

- ensure priority is given to the core activities of the businesses being the provision of electricity network services;
- ensure there is robust ring-fencing between the competitive and monopoly functions;
- undertake market testing of any commercial interactions between the functions; and
- consider a longer-term strategy of full structural separation of the energy services business and the natural monopoly distribution businesses.

ERM Power is anxious that competitive neutrality is maintained by ensuring that regulated network businesses cannot compete with contestable parties for competitive services. Where this is allowed, contestable providers are likely to find themselves at a disadvantage, and the price and service quality

benefits of competition are likely to be compromised. This is particularly important as the market transitions from one focussed on energy supply to one that's focussed on meeting a broader range of customers' energy management needs through distributed generation, storage and other demand-side solutions.

ERM Power supports the draft recommendation to ensure robust ring-fencing exists between monopoly and contestable functions of network businesses. However, we note that the effectiveness of this policy will depend on the precise definition of these functions and allowable interactions between them. For example, it is important that customer data collected for network purposes and network intellectual property is not transferred to contestable entities.

We acknowledge that in an environment where solutions are quickly evolving, and can deliver a range of valuable customer, network, and market benefits, ruling an unambiguous approach to ring-fencing may appear daunting. Nonetheless, it is a critical issue for the development of the customer solutions market.

The Australian Energy Regulator will soon be consulting on a review of its Electricity Ring-fencing Guideline. We are hopeful that this process will result in a robust and nationally-consistent approach to network ring-fencing, and recommend the QLD Government engage closely with this process.

Draft recommendation 19

The Queensland Government should prepare for its review of the effectiveness of the National Energy Retail Law (NERL) in Queensland by determining:

- whether the information retailers are required to publish in the market is sufficient to encourage effective consumer choice;
- whether the arrangements are sufficiently flexible to apply to new products and services, and do not unnecessarily stifle innovation or limit competition;
- whether the current retail market framework is applicable to new or alternative service providers and provides a level playing field for all participants while ensuring adequate consumer protections are retained; and
- options to improve the competitiveness of standing offers, including requiring retailers to publish their standing offer prices on the same day which is likely to have consumer benefits.

The QLD Government has successfully implemented the National Energy Retail Law (NERL) to ensure a comprehensive level of customer protections for small customers, and we fully expect a review to confirm the adequacy of this reform.

Information provision

ERM Power supports increased transparency for customers, and therefore welcomes the draft recommendation for the NERL review to consider the sufficiency of information provided to customers to enable retail choice. To use a specific example, our experience shows that many customers are confused by the common retailer practise of referring to offers as a percentage discount, without clear publication or explanation of the actual rates to be charged. This practise was referenced by QPC in its Draft Report. This ambiguity can mislead customers and result in choices contrary to customers' interests. This could be addressed through changes to the information provision requirements placed on retailers and we encourage a review into this issue and potential solutions.

Competitiveness of standing offers

We do not believe the competitiveness of standing offers is an appropriate measure of the effectiveness of the NERL in protecting customers and supporting retail competition, and therefore oppose the draft

recommendation for this to be a specific consideration under the NERL review. The primary objective of a standing offer is to provide default contractual protections for both customers and retailers that are transparent and fair. The primary objective of a standing offer is not to provide highly competitive prices; that need is met by market offers.

ERM Power's standing offer is intended to be only applied to ensure reasonable worst case cost recovery for usage by customers who have temporarily been assigned the tariff. Our intent is to transition customers to a market offer as soon as is possible. We have no intent for the standing offer to be market competitive.

QPC specifically raises the potential regulatory requirement for all retailers to publish standing offers on the same day. We note this requirement was recently introduced in Victoria. We understand the intent of this policy is to improve the competitiveness of standing offers which, as we describe above, we believe is a misplaced objective. Further, we believe the result of this obligation actually results in the opposite effect. By reducing the times at which a retailer can update its standing offer prices, a retailer's ability to respond efficiently to market conditions is also reduced. The result is likely to be application of a risk premium to protect the retailer against future changes, with the customer paying higher rates than where prices had been calculated based on actual costs. ERM Power does not believe this is an appropriate consideration under the NERL review.

Draft recommendation 22

Deregulation of the SEQ retail electricity market should commence as planned on 1 July 2016.

ERM Power strongly supports this draft recommendation, noting the Minister's recent commitment for full implementation on 1 July 2016.

Draft recommendation 26

Monitoring the efficiency and effectiveness of standing offers should form part of the Queensland Government's market monitoring arrangements for SEQ.

It is unclear on what basis QPC recommends the efficiency and effectiveness of standing offers should be assessed, under the QLD Government's market monitoring arrangements for SEQ.

Given our views on the competitiveness of standing offers discussed above, we believe market monitoring of standing offers should be limited to assessing the proportion of customers that are supplied under standing offer contracts compared to market offer contracts.

Draft recommendation 30

To facilitate retail competition in regional Queensland, the Queensland Government should implement a network CSO, although changes to the UTP arrangements should be considered to offset some of the additional costs to the State Budget.

ERM Power strongly supports this draft recommendation. We believe the implementation of a network CSO in regional QLD will facilitate the development of a competitive retail market, increasing consumer choice of electricity products and services. ERM Power looks forward to bringing its own retail offerings to this region following the full implementation of this draft recommendation.

Draft recommendation 32

A date of no later than 1 July 2019 should be considered for the implementation of a network CSO and retail competition for regional Queensland.

ERM Power encourages the implementation of a network CSO at the earliest opportunity. Delaying this reform only prolongs the consumer benefits of retail competition, and risks increased implementation costs. It is unclear why 1 July 2019 would reflect the earliest opportunity, and we encourage QPC to consider a more rapid transition.

Draft recommendation 35

The 'non-reversion' policy should be removed from the Electricity Act 1994 and the restriction on Ergon Energy (Retail) competing to retain existing customers should be removed.

We oppose the draft recommendation to remove the non-reversion policy and restriction on Ergon Energy (Retail) competing to retain existing customers. ERM Power believes the most effective approach to supporting a smooth and timely transition to retail competition in regional QLD is for Ergon Energy (Retail) to be acquired by a private entity. Maintaining the restriction on Ergon Energy (Retail) competing to retain existing customers would facilitate the QLD Government's exit from the electricity retail market.

Public ownership of Ergon Energy (Retail) represents a significant political risk to the QLD Government. Retaining control of this entity ensures the continued public association of the Government with electricity prices, including the negative sentiment that often follows. Privatisation (together with the implementation of a network CSO) represents an opportunity for the Government to distance itself from this issue.

Further, privatisation hastens the transition of existing Ergon Energy (Retail) customers to more competitive offers, and exposure to retail choice. The transition would provide an opportunity for these customers to become educated about retail choice and the range of offers that may be available to them.

ERM Power urges QPC to reconsider its draft recommendation.

Draft recommendation 37

The Queensland Government should ensure meters capable of measuring charges for the relevant tariff options are in place for customers on transitional and obsolete tariffs.

ERM Power supports the contestable provision of advanced metering to small customers. Advanced metering empowers customers to make informed choices about their electricity products and services by providing data that illustrates how usage fluctuates during the day. This is important when considering a transition to more cost-reflective tariff structures, and the suitability of energy management solutions such as generation, storage, and other demand-side measures. In regional QLD, there is the particular issue of transitional and obsolete tariffs, which further justifies the case for advanced metering to those premises.

The Australian Energy Market Commission made its final decision on the *Competition in metering and related services* rule change in 2016, establishing a national regulatory framework to support contestable metering provision to small customers from 1 December 2017. This is a significant and well-considered reform that should be implemented in full in all jurisdictions to support efficient development of this new market. We understand that the QLD Government is considering introducing measures to encourage the installation of advanced metering prior to the implementation of the national framework. ERM Power

considers it very important that any such measures are considered in close consultation with stakeholders to ensure that they facilitate and not hinder the transition to the national framework in 2017.