origin

11 March 2016

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

Lodged online

Dear Mr Wood

**Electricity Pricing in Queensland – Draft Report**

Origin Energy (Origin) welcomes the opportunity to provide a response to the Queensland Productivity Commission's Electricity Pricing in Queensland Draft Report.

Origin recognises the challenge for the Queensland Government to maintain productivity in the supply chain while at the same time encouraging innovation. The Queensland Productivity Commission (QPC) has examined a complex span of issues in a short period. We commend the work undertaken by the QPC and believe it has delivered a balanced and constructive set of recommendations. Notably, the introduction of retail electricity price deregulation will act as the catalyst for the delivery of more efficient prices, greater product offerings and a robust customer protection framework.

We also believe that with the right framework customers in regional Queensland can also access the benefits of a more competitive electricity market.

Origin's responses to specific issues identified in the draft report are set out below.

*Supply Chain Productivity*

The QPC correctly identifies that the emergence of smart technology has the potential to provide significant economic benefits that extend across the entire supply chain. The QPC also notes that the emergence of new business models will create potential risks and challenges including negative impacts on the profitability and investment incentives of traditional electricity service providers.

Irrespective, Origin strongly supports the principle that the market must apply a technology neutral approach to delivering customers' energy needs as this underpins the efficient economic delivery of services. This is best achieved through a consistently applied set of regulatory rules that provide certainty and impartiality. We believe that a common driver of market failure and the loss of economic benefits is a breakdown of the price signal.

To avoid a breakdown of the price signal requires a sufficiently competitive market where the rules allow for easy entry and exit and the absence of price distortions. For these reasons, we would be concerned if the Government saw its role to intervene in the Queensland market to engineer certain outcomes. The impact of the solar bonus scheme on network prices should serve as an example of how selective intervention can distort incentives and result in adverse outcomes for consumers.



Origin Energy Limited ABN 30 000 051 696 • Level 45, Australia Square, 264-278 George Street Sydney NSW 2000
GPO Box 5376, Sydney NSW 2001 • Telephone (02) 8345 5000 • Facsimile (02) 9252 9244 • www.originenergy.com.au

To the extent intervention is required to facilitate a competitive market, we support the position that intervention is best addressed through the national energy framework including the COAG Energy Council and where necessary changes to the National Electricity Rules.

*Generation*

Origin supports the QPC's recommendation and the Government's subsequent announcement not to merge CS Energy and Stanwell. As we have stated in our previous submission, a merger could materially lessen competition in the wholesale supply of electricity and the level of liquidity in the wholesale contract market resulting in potentially higher wholesale pool and contract prices to the detriment of Queensland consumers.

We also support the recommendation for CS Energy and Stanwell to develop and adhere to a common voluntary Code of Conduct in respect of their rebidding behaviour. We also support an annual assessment of compliance with the Code.

*Networks*

As the QPC points out, there are a number of inter-related factors that influence the level of network prices including: 1) the structure and cost reflectivity of network tariffs; 2) the impact of emerging storage technologies; and 3) the current revenue cap form of regulation.

How these factors interact is often complex and subject to an evolving policy landscape. As the QPC has pointed out, reforms have either commenced, or are about to, on a number of current and emerging issues through national policy agencies.

We are strongly of the view that in an evolving market environment that the role of the network businesses must be clearly defined. In this regard, the Australian Energy Regulator's review of national ring-fencing is a critical piece of work to ensure the necessary governance structures are in place to promote competition in storage technologies. A successful ring-fencing framework will promote choice and innovation which will complement other key reforms such as competition in metering and network tariffs.

For these reasons, we agree with the QPC that the Queensland Government should work proactively with the COAG Energy Council on reforms in these areas to ensure consistency in the development of market of rules.

*Solar Bonus Scheme*

Origin supports the progressive decarbonisation of the electricity sector in Australia and views the increased deployment of solar technologies as a key part of this transition.

However, as we have stated in our previous submission, subsidised feed-in-tariff arrangements result in a wealth transfer from those households without solar PV to those who had installed it. Requiring retailers to fund the existing but closed Solar Bonus Scheme would simply create further market distortion and result in retailers no longer offering voluntary rates as these are likely to be withdrawn to fund any co-contribution requirement.

*Retail Markets and Consumers*

Origin has previously highlighted the importance of increased consumer knowledge as part of an evolving and maturing market. In this regard, we support the need for increased customer engagement ahead of the introduction of retail price deregulation. We believe the Government's proposed Electricity Consumer Engagement Program is well placed to engage with industry and community-based organisations to provide consumers with the necessary awareness and knowledge to obtain the electricity contract that best meets their needs.

As part of the Government's review of the National Energy Retail Law (Qld), we acknowledge those areas of focus recommended by the QPC.  In developing a review framework, we consider there is a benefit from observing the outcomes of similar frameworks that are currently operational in other deregulated markets; notably Victoria. This will allow the Government to better understand which initiatives have achieved their intended outcomes and which did not and the reasons why. This will better allow the Government to make informed decisions and to establish a review framework that is relevant to observing consumer outcomes.

*Deregulation in SEQ*

Origin supports the QPC's recommendation that electricity retail price deregulation should commence on 1 July 2016.

As the QPC notes, under the Australian Energy Market Agreement (AEMA), all Australian states and territories have committed to phase out retail price regulation for electricity (and natural gas) where effective retail competition can be demonstrated. Under the AEMA, the Australian Energy Market Commission (AEMC) is responsible for assessing the state of competition in electricity and gas retail markets.

In its most recent assessment, the AEMC concluded that competition in the SEQ retail electricity market was effective. This is similar to conclusions made by the QCA that also found evidence of considerable third party retailer entry into the SEQ market which had resulted in significant numbers of markets offers and clear evidence of customer switching to obtain discounts.

We believe the introduction of retail price deregulation will further drive innovation in the provision of retail products and improvements in service and consumer experience over time.

We believe the Government's Electricity Consumer Engagement program will act as a valuable resource to educate consumers and promote understanding of the availability of key consumer tools such as the AER's Energy Made Easy to ensure they can identify and access the energy products that best meets their needs.

Based on the experience in other jurisdictions, we believe that creating greater customer awareness that customers can save by choosing the energy plan that best meets their needs is fundamental. It must also be recognised that this does not always translate into customers switching retailers or market contracts, but what is important is that customers have the confidence to make those decisions if they choose.

*Market Monitoring*

We believe the threat of the re-introduction of price controls under the Minister's reserve pricing powers provides a strong safeguard against any weakening of efficient market outcomes under a deregulated market.

In terms of monitoring market performance, we support the primary use of available market information such as existing COAG Energy Council commissioned reports and the AER retail performance reports. Where necessary this could be complemented with targeted SEQ specific data as well as secondary sources such as the Energy Ombudsman. The collection of targeted, concise and consistent data will better allow Government to draw a meaningful conclusion about the effectiveness of the SEQ retail electricity market without the need to replicate analysis already undertaken by other agencies.

*Increasing Retail Competition in Regional Queensland*

The QPC identifies that to expand competition in regional Queensland that third party retailers need to access the Uniform tariff Policy (UTP) Community Service Obligation (CSO) to allow them to compete with the incumbent Ergon Retail.

We agree with the QPC recommendation that a network CSO provides the most effective means of creating incentives for retailers to enter the market.

The QPC calculate that under this option the net impact on the State budget would be between $90M and $150M per annum. Origin understands that the upper bound value of $150M is based on the existing cost to serve differential of $127M plus a cost differential for customers with an existing market offer of $23M.

The QPC acknowledge that at least in the initial years, it is likely that the net impact on the State budget would be lower as some part of Ergon Retail's profit would continue to be returned to the State through dividends, depending on the rate at which Ergon Retail customers switch to market contracts. The QPC assume a switching rate of 30 per cent with Ergon Retail retaining a level of its existing profitable non-market customers.

Based on the QPC's analysis, we understand that the upper bound cost estimate of $150M is predicated on a loss of Ergon Retail's entire market share. Applying the QPC's assumption of a switching rate of 30 per cent, a full loss in the first year seems implausible. We would expect that adopting a switching rate in year one would deliver a cost to serve differential significantly less than $150M, and that the cost would be significantly less for an extended period.

Furthermore, as the QPC acknowledge Ergon Retail is likely to retain its existing profitable non-market customers. We also expect that it would retain a core number of non-market customers despite the switching rate assumption. As a result, it is not clear how the QPC has factored these into its calculation of costs to the State budget.

While we recognise the work the QPC has undertaken in estimating costs on the State budget we consider that the calculations require further explanation and transparency with respect to: 1) Ergon Retail annual retained customer levels; 2) treatment of profit retention; 3) inclusion of any financial benefits of expanded competition; and 4) a clearly defined annual transition path from the costs in year one to the full upper bound costs.

In terms of transitioning to competition, the QPC has recommended that should the Queensland Government decide to move to a network CSO, it should set a target date for full implementation of no later than 2019 in order to provide time to prepare Ergon Retail for regional competition.

Origin recognises that significant structural separation of the network and retail elements of Ergon's business is necessary to support an expansion in retail competition. However, preparedness for competition is not new and that the system requirements for certain functions (i.e. NMI information) under retail competition are already known with little or no change to these requirements over recent time. For example, we note that the QCA has issued a notice to Ergon Networks under the Electricity Industry Code advising Ergon that it will no longer be permitted to operate under the minimalist transitioning arrangement from 30 July 2016. We would expect that in light of the QCA's decision that Ergon has already made progress to automate systems.

To allow customers in regional Queensland to access the benefits of a more competitive electricity market, we believe greater consideration is needed to bring forward the implementation date.

*Role of Local Service Providers*

Origin supports the QPC's recommendation for the Queensland Government to wait upon the outcome of the AEMC's local generation network credit determination prior to considering a Queensland-specific approach. We agree that as a general principle, unilateral action by a state government would be an inefficient option to resolve impediments in the harmonised national frameworks approach to network pricing.

*Electricity Concessions Framework*

Origin considers that the objective of any concessions framework should be to target those most in need. To the extent that the existing scheme does not achieve that objective then consideration needs to be given how to re-distribute the existing available funds rather than extend the existing rebate and concession allowances. In this regard, we support the QPC's recommendation that the Queensland Government should determine clear policy intent for its concessions framework. In terms of the design of such a framework, we maintain our support for the QCOSS design principles.

We also support the recommendation for the Queensland Government to seek COAG agreement for the administration of energy concessions to be part of the broader Australian Government social security system, to improve efficiency and equity

*Network Tariffs and Impediments to Demand-Side Participation*

The QPC noted that while a transition to mandatory demand charging is not imminent or even a certainty, the Queensland Government should use this period to prepare for the potential transition, in particular by identifying customers vulnerable to impacts of tariff reform and designing programs to mitigate impacts.

We agree that decisions taken in the transitionary period will largely shape the success of the reform process. One aspect we strongly believe must be taken is ensuring tariff reform is underpinned by sufficient relevant customer interval billing data to not only allow networks to develop the most effective tariffs but to also ensure customers have the best opportunity of understanding and being able to respond to price signals. This will enable a richer understanding of the impact of different tariff structures and parameter values on different customer cohorts, notably vulnerable and low income households. This in turn will facilitate more targeted customer engagement and facilitate more refined network and retail product offerings.

For these reason we support both the recommendation for the Government to improve customer usage data set as well as establishing a working group to develop tools to help customers understand tariff reform and to identify the impacts on different cohorts.

*Further Information*

If you have any questions regarding this submission please contact Sean Greenup in the first instance on (07) 3867 0620.

Yours sincerely

Keith Robertson
Manager, Wholesale and Retail Regulatory Policy
(02) 9503 5674 Keith.Robertson@Originenergy.com.au