Queensland Competition Authority

Interim consultation paper

# Regulated retail electricity prices for 2020–21

**December 2019**

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# Contents

# 1 ABOUT OUR REVIEW

## 1.1 What have we been asked to do?

We have received a delegation from the Minister for Natural Resources, Mines and Energy to set regulated retail electricity prices (notified prices) to apply in regional Queensland in 2020–21. We are delegated this task by the Minister in accordance with the *Electricity Act 1994* (Electricity Act).[1]

## 1.2 Scope of our review

Since we set prices under a delegation from the Minister, the legislation that applies to the Minister when setting notified prices also applies to us. The framework is contained in the Electricity Act and sets out factors[2] we must have regard to when making a price determination. These are:

- the actual costs of making, producing or supplying the goods or services
- the effect of the price determination on competition in the Queensland retail electricity market
- any matter we are required by delegation to consider.

We may also have regard to any other matter we consider relevant.[3]

### Matters we must consider under the delegation

The Minister's delegation includes a terms of reference, containing particular details and matters relevant to our price determination, namely:

- the period—the price determination is to apply from 1 July 2020 to 30 June 2021
- the timeframes—for publishing reports and making our draft and final price determinations (noting the final price determination must be made by no later than 26 June 2020)[4]
- particular policies or principles—we are to set notified prices having regard to, among other matters, the Queensland Government's Uniform Tariff Policy (UTP)
- pricing methodology—we are to set notified prices having regard to the Network plus Retail (N+R) cost build-up methodology
- consultation—we are required to consult at various stages before making the final price determination and consider the merits of additional consultation, including holding stakeholder workshops, on identified key issues.

A copy of the Minister's delegation, including terms of reference, is provided in Appendix A.

[1] Section 90AA of the Electricity Act.
[2] Section 90(5)(a) of the Electricity Act.
[3] Section 90(5)(b) of the Electricity Act.
[4] See s. 15 of the delegation terms of reference (Appendix A).

## 1.3 Consultation and key dates

This interim consultation paper (ICP) is the first step in our price determination process. It provides information on key issues we are considering in the context of setting notified prices for 2020–21. It provides an opportunity for stakeholders to contribute and give feedback, which we encourage via submissions.

Stakeholders are invited to provide submissions on key issues raised in the ICP, or any other matters considered relevant to our price determination. Information on making a submission is available on our website.[5]

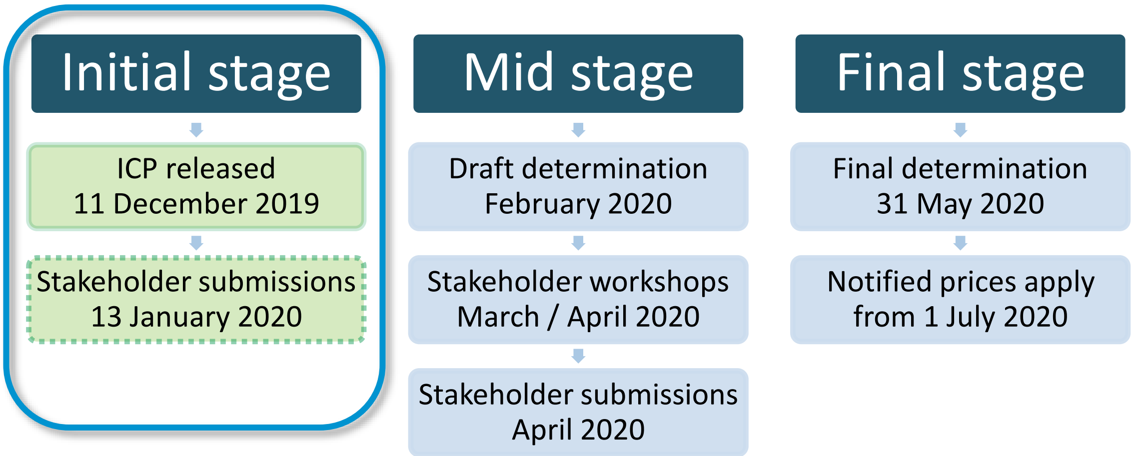
**Submissions on the ICP are due by Monday 13 January 2020.**

We will consider all stakeholder submissions, along with other relevant information, when making our draft and final determination on notified prices.

### Way forward and indicative consultation timetable

Stakeholder consultation is an integral part of our decision-making process. We invite stakeholders to participate at various stages throughout our price determination process.

The dates below give stakeholders an indication of when we will publish reports and seek further comments from stakeholders as part of our review:[6]




It is important to note these timeframes are indicative and may change. To keep up to date with the latest developments on this project, as well as other energy projects, we encourage stakeholders to subscribe to our email alerts.[7]

[5] https://www.qca.org.au/submissions/.
[6] There is flexibility in the delegation to publish the draft and final reports one month later. At this time, we have included indicative dates consistent with previous price determinations. We intend to advise stakeholders if there are any adjustments to these dates.
[7] https://www.qca.org.au/email-alerts/

## 1.4 New report format

We are aware there are a number of regulatory agencies seeking feedback on various issues in the energy sector at present. A number of stakeholders have commented that trying to participate in and provide feedback to such a large number of consultation processes, some of which are running concurrently, is proving to be a challenge.

For this reason, we prepared the ICP differently this year, with the view that stakeholders may value the ICP covering key issues, more succinctly and using simpler language.

Also, we have prepared a handbook to accompany the ICP—it provides an 'at a glance' overview of the price setting process and matters in the ICP. The handbook can help stakeholders to become quickly informed of key issues, which can make it easier to prepare submissions. It is designed to be read in conjunction with the ICP (not as a substitute).

## 1.5 Structure of this paper

We have structured the ICP in two parts:

- Overarching framework—which covers the key issues forming part of the broad policy and pricing considerations that affect how we set notified prices. Often these are matters in the delegation we need to consider (chapter 2)
- Cost build-up components—which covers how the policy and pricing considerations are applied and key issues to consider when calculating notified prices, including the cost elements that form part of the overall notified prices and other costs (or issues) relevant to setting notified prices (chapter 3).

# 2 OVERARCHING FRAMEWORK

This chapter provides our views on key issues to consider in this year's price determination, including overarching framework matters that impact how we set notified prices.

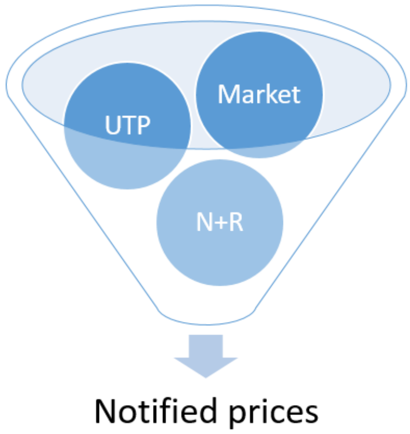
The key issues we have identified largely consist of matters included in the Minister's delegation (and terms of reference) that we must consider when setting notified prices. For instance, the Minister has refined how the UTP should apply, and has provided additional considerations impacting the underlying network tariffs used as the basis for determining notified prices.

Beyond this, there are other matters that are relevant in setting notified prices. For instance, we have provided information on how particular policies may be considered and applied.

We need to have regard to the following key issues when making our price determination this year:

- the Queensland Government's UTP
- the methodology for calculating notified prices
- new pricing matters, including default tariffs and large customer tariffs.

We will consider stakeholder views on these matters and other matters that stakeholders identify as relevant to our review.




## 2.1 Context and market environment

The electricity sector is undergoing major structural reforms. These are expected to have considerable impacts on the electricity market environment, including how market participants operate and manage risks.

The Australian Energy Regulator (AER) is current undertaking two reviews that will have a direct impact on the electricity market environment in Queensland, namely:

- default market offer (DMO) for south east Queensland (SEQ)—the AER sets a DMO that limits the prices charged to residential and small business customers on a standard retail contract. The DMO was first introduced in 2019–20. The AER has indicated it will issue a final determination on the 2020–21 DMO by April 2020
- 2020–25 regulatory determination process for Energex and Ergon Distribution (distributors)[8]—the AER sets network revenues and tariffs for distributors in Queensland. As part of this process, Energy Queensland (the parent company of Energex and Ergon Distribution) submitted its Tariff Structure Statement (TSS), which proposes new network tariffs with increasingly complex structures to facilitate a move towards greater cost reflectivity (see Box 1 for more detail on the network tariff reforms and timing).

[8] For more information on these reviews, go to the AER's website at: for Ergon—https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/ergon-energy-determination-2020-25 and for Energex—https://www.aer.gov.au/networks-pipelines/determinations-access-arrangements/energex-determination-2020-25.

The Minister's cover letter indicates these are important considerations for setting notified prices this year. Additional considerations are included in the delegation to reflect this.[9]

### Box 1—Network tariff reforms

Energy Queensland is proposing to replace the flat-rate network tariff for small customers in SEQ with more complex network tariffs (as default tariffs) from 2020–21 onwards. The AER is considering these as part of the 2020-25 regulatory determination process.

The network tariffs (proposed under the TSS) continue to evolve. Since its first submission in January 2019, Energy Queensland has amended its TSS submissions three times. Due to the complexity of this process, the AER delayed its draft decision from September to October 2019.

In its draft decision, the AER indicated that substantial changes to the TSS will be required for Energy Queensland to comply with the National Electricity Rules. At this stage, Energy Queensland is expected to submit another revised proposal in December 2019—with the AER's final decision due by 30 April 2020.

The complex and rapidly evolving nature of the 2020–25 TSS means it is unlikely there will be much certainty on the network tariff structures and pricing prior to the TSS's finalisation in April 2020.

## 2.2 The Uniform Tariff Policy (UTP)

The terms of the delegation require us to consider the Government's UTP—which provides that **wherever possible, customers of the same class should pay no more for their electricity, and should pay for their electricity via similar price structures, regardless of their geographic location**.

Some additional considerations in the delegation are that 'regional customers continue to access price structures that are similar to those accessed by the majority of similar South East Queensland customers'. Further, that regional customers are also 'provided new and additional choice of retail tariffs resulting from the national network tariff reform agenda'.

While the UTP is broadly consistent with previous years in terms of cost considerations, the price structure aspect is a new matter to this review.

On that basis, we are considering approaches that take into account both costs and tariff structures as part of this price determination. Given this, we will consider setting notified prices having regard to:

- cost considerations—noting we have previously set notified prices:
  - for small customers—based on the costs of supply in SEQ
  - for large business customers—based on the costs of supply in the Ergon Distribution pricing region with the lowest cost of supply—that is, east zone, transmission region one
- tariff structure considerations—where the delegation directs us to consider:

[9] See the Minister's cover letter (Appendix A).

- maintaining existing retail tariffs and structures
- options for introducing new retail tariffs (based on the AER's approved new network tariff structures)
- options for potentially aligning the existing retail tariffs with new network tariffs (based on the AER's approved new network tariffs with similar structures).

In previous determinations, having regard to the UTP has benefitted most customers in regional Queensland. This is because it reduces the cost most customers pay by setting notified prices at a level much lower than the actual cost of supply. The cost difference is met by the Queensland Government through the payment of a community service obligation subsidy to Ergon Energy Queensland (expected to be $498 million in 2019–20).[10]

Given the timing of our review, and the uncertainties associated with the network tariff reforms, we are not able to provide an indication to stakeholders on:

- the new retail tariffs based on the new network tariff structures
- the potential to align existing retail tariffs with new network tariffs with similar structures.

We intend to update stakeholders on this as part of our draft determination, noting stakeholders will have an opportunity to provide further comments as part of this review.

**Consultation question 1**

Stakeholders are invited to comment on the considerations affecting how we have regard to the UTP when setting notified prices, in light of the network tariff reforms underway.

## 2.3 The N+R methodology

The terms of the delegation require us to consider:

- using the N+R cost build-up methodology when setting notified prices[11]
- applying this approach flexibly in order to allow for uncertainty associated with the network tariff reforms.

While the delegation is broadly consistent with previous years—and how we have applied the N+R methodology in previous price determinations, the delegation allows for more flexibility in applying this methodology which is a new matter for this price determination.

We are considering approaches that take into account the N+R methodology, as well as the circumstances in which we may need have regard to the additional flexibility afforded.

Given this, we will consider applying the N+R methodology having regard to:

- the standard approach—building up notified prices using the new network tariffs as the basis for determining the structure of retail tariffs (i.e. passing through the N component) and adding the R component (i.e. energy and retail costs) determined by us

[10] Queensland Government, *Budget Strategy and Outlook 2019–20*, Budget Paper 2, p. 20.
[11] number 5(d) of the terms of reference.

- the more flexible approach—maintaining the existing suite of retail tariffs (i.e. adjusting the N component with a suitable index) and adding the R component (i.e. energy and retail costs) determined by us.

These considerations, coupled with the timing of our review and the uncertainties associated with the network tariff reforms, impact how the N+R approach may be applied this year—more specifically, how the N component for notified prices is determined under the N+R methodology. This is discussed in detail under 'network costs' in section 3.1.

### Consultation question 2

Stakeholders are invited to comment on the approaches to applying the N+R methodology for this price determination, in light of the network tariff reforms underway.

## 2.4 New pricing issues

### 2.4.1 Nominating default tariffs

The terms of the delegation require us to consider the '**nomination of a primary tariff for each class of small customer to apply to a customer's electricity account in the event the customer does not nominate a primary tariff when opening an electricity account**'.

Additionally, the Minister's cover letter said we should consider 'nominating Tariff 11 to be a default residential tariff and Tariff 20 a default small business tariff, to apply when a customer does not nominate a tariff when they seek to establish an electricity account'. Further, that 'this default designation should not limit customers from selecting alternative tariffs they are eligible for if they choose to do so'.

This matter has not formed part of previous delegations and is a new matter to consider for this price determination.

A default retail tariff may provide small regional customers with additional certainty, considering the network tariff reforms. We consider certainty is likely to be a relevant factor for stakeholders under these circumstances.

Implementing default retail tariffs, in line with the Minister's proposal, would result in:

- the default primary tariff being equivalent to the existing flat-rate retail tariffs currently accessed by small regional customers (i.e. tariff 11 and tariff 20)
- regulated retailers being compelled to offer the default retail tariffs if a customer does not nominate a primary tariff when setting up an electricity account.

### Consultation question 3

Stakeholders are invited to comment on the new matter of introducing primary default tariffs that would apply if a customer does not nominate a primary tariff when setting up an electricity account.

### 2.4.2 Individually Calculated Customers (ICC) tariffs

Individually Calculated Customers (ICC) are very large business customers generally consuming over 40 GWh each year. Generally, these are large industrial users such as smelters and other heavy industry.

The terms of the delegation require us to consider, for ICC tariffs, allowing for an option of passing through the customer’s individual network tariffs, while stating the methodology to apply for the R component.

This matter has not formed part of previous delegations and is a new matter to consider for this price determination.

The Minister has described the policy intent as follows:

> Ergon distribution has also proposed to the AER to reassign some Connection Asset Customers (CAC) to Individually Connected Customers (ICC) in 2020-21 when they have been identified as an outlier to their costs to serve. This has the potential to significantly lower the network charges for some of these customers. The Government considers it important that any potential reduction in network charges be passed through to customers via notified prices. However, to ensure existing ICC customers are no worse off, the QCA should also maintain Tariff 53.[12]

We consider optionality is likely to be a relevant factor and is in the interests of stakeholders, particularly those who would be otherwise worse off (in the circumstances the Minister suggests).

Stakeholders, when considering this matter, should note that such an approach would result in:

- Tariff 53 being maintained and
- customers on ICC tariffs having the option of accessing a notified price based on the site-specific network charges (determined by the AER) and the R component (energy and retail costs) determined by us.

**Consultation question 4**

We seek stakeholder comments on the new methodology for determining ICC tariffs, including any other issues we should consider in assessing these.

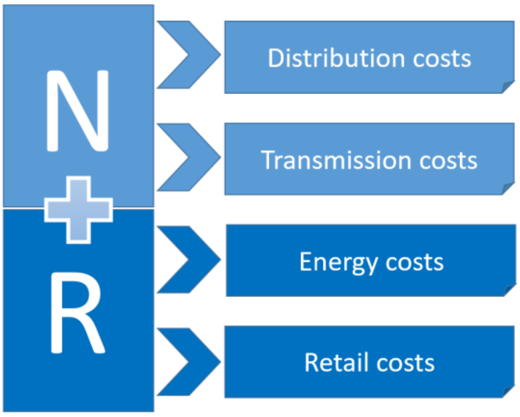
[12] See Minister's cover letter, p. 3 (Attachment A).

# 3 COST BUILD-UP COMPONENTS

This chapter provides our views on key issues to consider in this year's price determination, including on the individual cost build-up components we use to set notified prices.

Many of these key issues are identified in the delegation (and terms of reference) which we must consider when setting notified prices. For instance, the Minister has provided additional matters for us to consider in determining the network component to reflect the network tariff reforms currently underway.

Beyond this, there are other matters that are relevant in setting notified prices. For instance, we have provided information on the energy and retail cost build-up components, including approaches to setting these cost elements and other factors which may be relevant to consider. We have also discussed other costs and matters relevant to setting notified prices, including adjustments we need to consider when setting notified prices.



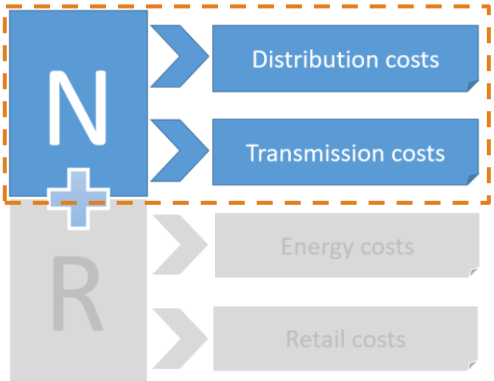

This chapter discusses costs under:

- the N component—distribution and transmission costs associated with transporting electricity to customers
- the R component—the costs of buying and selling electricity to customers
- other costs and price matters.

We will consider stakeholder views on these matters, and any other matters stakeholders identify as relevant to our review.

## 3.1 Network component (N)

The costs of transporting electricity through transmission and distribution networks are regulated by the AER. In addition to recovering their own distribution network costs, distributors also pass Powerlink's transmission network costs (also approved by AER) through to customers as part of the network prices.




The terms of the delegation require us to consider determining the N component in a manner that reflects overarching framework matters—that is, the UTP and N+R methodology previously discussed (see Chapter 2), namely:

- the standard N+R approach to pass through the N component:
  - using the AER's approved new network tariff structures to introduce new retail tariffs
  - using the AER's approved new network tariffs to potentially align existing retail tariffs with new network tariffs with similar structures
- the flexible N+R approach—to maintain the existing suite of retail tariffs, we would adjust the existing N component with a suitable index.

While the standard approach to determining N is broadly consistent with the approach we have applied in previous price determinations, the delegation allows for flexibility in determining the N component—under the flexible N+R approach, which is a new matter to this review.

On that basis, we are considering the usual and flexible N+R approach to determining the N component as well as the circumstances in which we may need to apply the more flexible option provided in the delegation.

### N component under the standard N+R approach

As discussed previously, the standard N+R approach involves passing through the N component. This approach results in retail tariff structures that reflect the underlying network tariff structures approved by the AER.

We note the usual approach, which would involve setting prices based on the new network tariffs (yet to be approved by the AER), would likely provide stakeholders with additional optionality, beyond the suite of existing retail tariff structures currently available. The Minister has identified this as a benefit, among others, likely to result from the network tariff reforms.

However, under this approach, we could not provide the same level of certainty to stakeholders on notified prices that may apply, or indicate how much consultation time would be available in light of the timing of network tariff reforms.

### N component under the flexible N+R approach

Given the timing of our review, and the uncertainties associated with the network tariffs reforms, applying the flexible N+R approach allows us to:

- maintain the existing suite of retail tariffs by setting the N component using the price indexation approach (i.e. adjusting existing network costs with a suitable index)
- provide stakeholders with certainty on how notified prices would be set, including sufficient opportunity to consult on the proposed retail tariffs, prior to our final price determination.

We note that using the flexible approach would allow us to set notified prices consistent with the previous review timeframes. Also, the adjustment to network costs (under the price indexation approach) would ensure the expected network cost reductions for 2020–21 are passed through to customers on notified prices.

In terms of adjusting the network costs with a suitable index, we are considering whether an X-factor approach, similar to that being considered by the AER, is appropriate. The X-factor approach is essentially an index-based approach that allows the pass through of network revenue changes.[13] Under this approach, we could employ the AER's X-factors to escalate/de-escalate the network charges of individual tariff components using the 2019–20 network tariffs as a starting point.

[13] As part of the revenue determination process, the AER produces five X-factors for the purposes of revenue smoothing (the X-factor for the first year is also known as $P_0$). Mathematically, X-factors are weights that are applied to allowable revenue for one year to calculate the allowable revenue for the next year using a price formula of the form—(CPI-X). See footnote 8 above for a link to AER’s review.

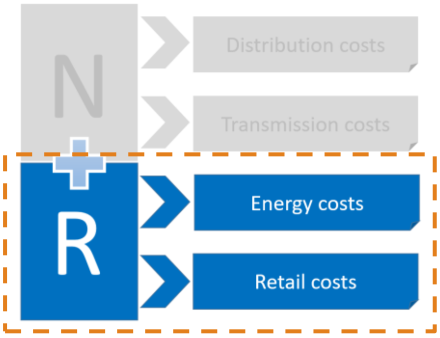
We note that, as part of the DMO process (discussed in section 2.1), the AER has proposed to use an 'X-factor' indexation method to adjust network costs.[14] This approach would ensure that the network cost reduction for 2020–21 is passed through to customers on notified prices.

### Consultation question 5

We invite stakeholder comments on these matters, particularly on any appropriate network price indexation methodologies we should consider applying, if it becomes necessary. Are there any other matters we should consider?

## 3.2 Retail component (R)

The R component consists of energy and retail costs. These include the costs of retailers purchasing electricity to supply to their customers, the costs of running their general operations, and a return for the risk they face by operating in the market.




### 3.2.1 Energy costs

Energy costs relate to the costs retailers incur when purchasing electricity to meet the demands of customers. These costs include wholesale energy costs, other energy costs (including the Renewable Energy Target) and energy losses.

#### Wholesale energy costs

Retailers incur wholesale energy costs when purchasing electricity from the National Electricity Market (NEM) to meet the electricity demand of their customers. Retailers typically adopt a range of strategies to reduce their exposure to rapidly changing wholesale electricity prices when purchasing from the NEM, including:

- pursuing a 'hedging strategy' by purchasing financial derivatives, such as ASX futures
- entering long-term power purchase agreements with generators
- investing in their own electricity generation.

In previous determinations, we used estimates of wholesale energy costs based on a market hedging approach, which takes into account retailers' hedging strategies. This approach is transparent and we consider it best reflects the actual costs retailers incur when purchasing electricity from the NEM in a given year. This approach is also adopted by other regulators and endorsed by the Australian Energy Market Commission (AEMC).[15]

In previous determinations, we used market data up until January for the draft determination. This has allowed us to account for the most current information (including any developments that

[14] The AER noted that in the absence of the relevant approved network tariffs, it would use the X-factors in its network revenue determinations to forecast how network costs will change.
[15] AEMC (September 2013), *Advice on best practice retail price methodology*, final report.

occur over the potentially volatile summer period), while still meeting our draft determination deadline.

Subject to stakeholder views, we are minded to adopt a similar approach for 2020–21.

## Other energy costs and losses

Retailers incur other energy costs when purchasing electricity from the NEM, namely:

- Renewable Energy Target (RET) costs—associated with the purchase of certificates to meet the targets mandated under the RET[16]
- NEM management fees and ancillary services charges—the costs levied by Australian Energy Market Operator (AEMO) to cover the cost of operating the NEM and services used to manage power system safety, security and reliability
- prudential capital costs—the costs a retailer incurs to provide financial guarantees to AEMO and to lodge initial margins with the ASX for futures contracts

Also, retailers incur costs associated with energy losses. This is because retailers need to purchase more electricity than is demanded by customers to allow for losses that occur when electricity is transported (via transmission and distribution networks).

In previous determinations, we used estimates of other costs and losses based on reliable sources of information and applying judgment to ensure these costs appropriately reflect those likely to be incurred by retailers[17]:

| | |
|---|---|
| RET costs | •Large-scale Renewable Energy Target (LRET) costs—estimated using a market-based approach, where Large-scale Generation Certificate (LGC) prices were based on forward prices for certificates in the market<br>•Small-scale Renewable Energy Scheme (SRES) costs—estimated using data and targets from the Clean Energy Regulator |
| NEM fees and ancillary charges | •NEM management fees—estimated using AEMO's budget and fee projections<br>•Ancillary services charges—estimated using the average historical costs observed over the preceding 52 weeks |
| Prudential costs | •Prudential costs—estimated using AEMO's prudential requirements and margin requirements for trading in the ASX futures market |
| Energy losses | •Energy losses—estimated by applying transmission and distribution loss factors published by AEMO, in a manner that aligned with AEMO's settlement process |

[16] The RET, comprised of the Large-scale Renewable Energy Target (LRET) and Small-scale Renewable Energy Scheme (SRES), provides incentives for the electricity sector to increase generation from renewable sources and reduce greenhouse gas emissions.

[17] For further information on how these costs are estimated, see ACIL Allen's reports for the 2018–19 and 2019–20 price determinations available on our website, www.qca.org.au

### Consultation question 6

Do stakeholders consider any changes should be made to our approach for estimating energy costs, or particular categories of energy costs?

Are there any other issues we should consider when estimating energy costs?

### 3.2.2 Retail costs

Retail costs are the costs of running a retail business. They include costs such as administration, operating call centres, operating billing systems and revenue collection. They also include a return to investors for retailers' exposure to systematic risks associated with providing retail electricity services.

The delegation does not specify a particular approach or methodology to apply for setting the retail cost allowance, with one exception—consistent with previous determinations, we exclude residential and small business customer metering costs from notified prices.

In previous price determinations, we have set the allowance for retail operating costs using an established benchmark (set as part of the 2016–17 price determination process), adjusted for inflation.

This year, we are considering whether:

- to establish new retail cost allowances, based on more recent market data, noting market changes (such as the AER's DMO and the network tariff reforms) may impact retailer pricing strategies and costs observed in the market; or
- maintain our approach and apply the established benchmark, adjusted for inflation, noting this would provide stakeholders with increased certainty over the level of costs to expect.

We are open to stakeholder submissions on which approach is more appropriate at this time.

### Consultation question 7

We seek stakeholder comments on approaches to setting the retail cost allowance (including those set out above). Are there any other matters we should consider when estimating retail costs?

## 3.3 Other matters

### 3.3.1 Standing offer adjustment

For this determination, the delegation requires us to consider incorporating a 'standing offer adjustment' amount into notified prices for residential and small business customers. This is intended to ensure notified prices reflect:

- the price a regulated retailer would charge 'standard contract customers' (a requirement under the Electricity Act)
- the cost a small customer would pay in SEQ on a standard contract (having regard to the Government's UTP).

In addition, the Minister considers an adjustment of similar magnitude to last year (e.g. five per cent) is appropriate and reflects the more favourable terms and conditions in standard contracts.

However, when considering the magnitude, the delegation states:

> …. should the application of this value result in a bill that exceeds the equivalent Default Market Offer as set by the Australian Energy Regulator for southeast Queensland, that value should be discounted so that the resulting bill does not exceed the equivalent Default Market Offer.

While the approach to incorporating a standing offer adjustment is broadly consistent with last year—and the approach we have applied in previous determinations, the delegation provides a constraint on the level of adjustment (equivalent to the DMO set by the AER for SEQ) and for us to discount the standing offer adjustment in certain circumstances—i.e. where notified prices we calculate are higher than the DMO set by the AER.

Given the timing of our review, and the timing of the AER's DMO process, we are considering having regard to:

- our previous approach—of including a standing offer adjustment and setting the level of this adjustment at five per cent, subject to further information being available on the DMO for southeast Queensland to assess whether the value should be reduced.

Consistent with our consultation timetable, we expect to release a draft price determination by the end of February 2020—we are hopeful by this time, and with the benefit of the AER's draft DMO price being released, it will be evident whether we need to consider adjusting the value of the standing offer adjustment incorporated into notified prices this year.

We intend to update stakeholders as part of our draft determination—noting stakeholders will have an opportunity to comment on this (and other matters in the draft determination), and we will consider any comments provided, as part of developing our final determination.

We are open to alternative approaches and we invite stakeholder submissions on this matter, including on whether our proposed approach is not appropriate and any alternative approaches stakeholders suggest.

**Consultation question 8**

We invite stakeholder submissions on the standing offer adjustment, including on the appropriateness of our proposed approach and alternatives stakeholders suggest.

### 3.3.2 Competition and headroom–large business customers

In making a price determination, we are required to have regard to, among other things, the effect of the price determination on competition in the Queensland retail electricity market.[18]

For determining the notified prices for large and very large business customers, we consider it relevant to examine whether incorporating a headroom adjustment is appropriate. This is because such an adjustment is intended to facilitate and encourage competition in the large customer market segment in regional Queensland and encourage customers to seek more attractive market offers.

In previous determinations, we have incorporated a headroom adjustment of five per cent into notified prices for large business customers.

[18] Section 90(5)(a)(ii) of the Electricity Act.

Subject to stakeholder comments, we are considering an allowance for headroom of five per cent for notified prices in 2020–21. This would be consistent with the approach applied in previous determinations (i.e. a five per cent headroom has been applied since 2012–13) and also will continue to ensure notified prices may continue to encourage the development of competition in this market.

#### Consultation question 9

We invite stakeholder submissions on the headroom adjustment, including on the appropriateness of our proposed approach and alternatives stakeholders suggest.

### 3.3.3 Obsolete tariffs

Under the Minister's delegation, we set notified prices for standard tariffs using an N+R approach. The introduction of this methodology, and reform to large customer network tariffs, meant that a number of retail tariffs no longer reflected the structure, and/or price level, of the network tariffs paid by retailers. Some customers would face substantial bill impacts if they had to move to standard business tariffs which other regional businesses pay. For that reason, we decided most of these tariffs should continue to be available for a period of time to allow businesses time to adjust their business operations to the new retail tariffs.

In previous determinations we decided that obsolete tariffs 47 and 48 should remain available until they expire 30 June 2022, and all other obsolete tariffs[19] would expire on 30 June 2020.

Since the release of our final determination of 2019–20 notified prices, the Queensland Government made a policy decision to extend the availability of tariffs 20 (large), 21, 22 (small and large), 37, 62, 65, and 66 by one year.

The Minister's delegation asks us to consider maintaining these revised expiry dates for obsolete tariffs.

#### Consultation question 10

We invite stakeholder submissions on obsolete tariff expiry dates, including views on the revised dates set by the Minister (detailed above).

[19] Tariffs 20 (large), 21, 22 (small and large), 37, 62, 65, and 66.

# APPENDIX A: DELEGATION

Queensland Government

The Hon Dr Anthony Lynham MP
Minister for Natural Resources, Mines and Energy

Ref CTS 23694/19

10 DEC 2019

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BRISBANE QLD 4000

Dear Professor Menezes

Pursuant to section 90AA of the Electricity Act 1994 (the Act), I have delegated to the Queensland Competition Authority (QCA) my functions under section 90(1) of the Act for the determination of regulated retail electricity prices in regional Queensland for 2020–21. I enclose a copy of the delegation, which includes the terms of reference of the price determination.

The government's uniform tariff policy (UTP) and costs to consumers are important considerations when setting regulated retail electricity prices in regional Queensland. The attached delegation and terms of reference for 2020–21 are generally consistent with the approaches in my delegation and terms of reference for 2019–20, however, there are some important additional considerations. Many of these are associated with managing potential adverse impacts on retail customers of the anticipated changes to network tariffs, including continued advancement of network tariff reform by Queensland's electricity distributors and the Australian Energy Regulator (AER) as well as the commencement of the new 2020-25 distribution regulatory control period.

Network tariff reform is critical to sending the right pricing signals to electricity retailers so that electricity networks are utilised more efficiently, generating savings that flow through to customers in the form of reduced network charges. However, in general, network tariff reform should not create perceptions of differential treatment amongst a class of retail customers based on their geographical location or the type of meter they have. It is important regional customers continue to access price structures that are similar to those accessed by the majority of similar South East Queensland customers, unless they specifically choose an alternate tariff. I am also seeking to ensure all current standard retail tariffs (standard tariffs) are retained in their current form, and where practicable, customers are provided new and additional choice of retail tariffs resulting from the national network tariff reform agenda.

In 2019, the AER set Default Market Offers (DMO) as maximum bill amounts at certain consumption levels in applicable distribution areas in the national electricity market. Under the UTP, the South East Queensland DMO represents the ceiling that should be set for an equivalent notified price. Further, the government notes that standard contracts provide additional value to customers compared to market contracts, for example, through additional protections contained in the terms and conditions of standard contracts.

In order to reflect the intent of the UTP when network tariffs are undergoing significant reform and to maintain existing standard tariff arrangements, I have provided clarity about the scope and application of the UTP. The QCA should also give consideration to including an adjustment in notified prices that appropriately reflects the additional value of the terms and conditions of standard retail contracts. In addition, I consider the standing offer adjustment made by the QCA in previous determinations appropriately reflects this additional value and as such, the QCA should consider including an adjustment of a similar magnitude in notified prices for 2020–21 while ensuring that notified prices do not exceed the equivalent South East Queensland DMO where set.

Under national Power of Choice reforms, all new and replacement meters must be advanced digital meters. Due to my concerns about the cost impact on small customers and the limited realisation of benefits being delivered to customers, on 5 April 2019, I asked the QCA for advice on the benefits of the digital meter roll out in Queensland. As the government remains concerned about the cost of digital meters for small customers and the slow progress toward benefit realisation by the electricity supply industry as identified by the QCA, this delegation again excludes the determination of notified prices for retail metering services for residential and small business customers. I intend to set these charges separately based on the responding advice the QCA provided to me on 13 September 2019.

The government is committed to customers in regional Queensland having more choice in electricity tariffs while maintaining the UTP. With this in mind, the government supports efforts by Ergon retail to develop new tariff structures in regional Queensland. In setting prices for 2020–21, I encourage the QCA to consult closely with retailers operating in regional Queensland, in particular regarding the continuation of existing standard tariffs. These consultations will also be key in the establishment of any new standard tariffs reflecting new network tariffs approved by the AER for the 2020–25 period.

You will note that the government has refined the definition of the UTP to clarify that it applies to the structure of retail tariffs, as well as the price level. This ensures customers are not treated differently because of where they live in Queensland.

Customers often do not nominate a tariff when they seek to establish an electricity account. To expedite account establishment in the interest of customers, Ergon retail generally assigns Tariff 11 for residential and Tariff 20 for small business customers as default tariffs when this occurs, reflecting current underlying network tariff assignment. However, it is likely that default network tariff assignment practices will change from 1 July 2020. Further clarification is provided to assist the QCA in its application of the UTP and maintain existing retail tariff assignment practices to avoid potential risks of adverse and unintended outcomes for customers in the first year of new network tariffs. The QCA should consider nominating Tariff 11 to be a default residential tariff and Tariff 20 a default small business tariff, to apply when a customer does not nominate a tariff when they seek to establish an electricity account. This default designation should not limit customers from selecting alternative tariffs they are eligible for if they choose to do so.

I note that timing of decisions made by the AER as part of its Queensland distribution determinations for the 2020–25 regulatory control period may present challenges to the QCA's usual regulated retail price determination timeframe. Some flexibility is provided in this delegation in terms of both timing and price setting methodology to manage this risk.

Recognising that some customers accessing obsolete legacy tariffs would face challenges adjusting to standard business tariffs, I extended the phase-out dates by one year to 1 July 2021. As these obsolete tariffs are not based on the actual costs of supplying electricity, the expiry date should be maintained and all customers on these tariffs will need to switch to a standard business tariff before 1 July 2021. I understand Ergon distribution is proposing to the AER new tariffs more suited to the needs of these customers, who will continue to be supported through the UTP.

Ergon distribution has also proposed to the AER to reassign some Connection Asset Customers (CAC) to Individually Calculated Customers (ICC) in 2020-21 when they have been identified as an outlier to their costs to serve. This has the potential to significantly lower the network charges for some of these customers. The government considers it important that any potential reduction in network charges be passed through to customers via notified prices. However, to ensure existing ICC customers are no worse off, the QCA should also maintain Tariff 53.

Public consultation is a vital part of the QCA's process for determining retail electricity prices. In this regard, the terms of reference requires that the draft determination should be issued in February 2020, but not later than the end of March 2020, with public consultation to follow, and a final determination should be delivered by 31 May 2020, but not later than 26 June 2020.

The government is committed to delivering lower electricity bills. My department will consult with the QCA on specific wording for the 2020–21 gazette, ensuring regional customers continue to benefit from the electricity cost protection provided by the UTP.

If you have any questions, [redacted] Executive Director, Consumer Strategy and Innovation, Department of Natural Resources, Mines and Energy will be pleased to assist you and can be contacted on telephone [redacted]

Yours sincerely

**Dr Anthony Lynham MP**
Minister for Natural Resources, Mines and Energy

Att

[redacted] DELEGATION TO QCA

DEPARTMENT OF NATURAL RESOURCES, MINES AND ENERGY

*Electricity Act 1994*

ELECTRICITY (MINISTERIAL – QCA) DELEGATION (NO. 1) 2019

**Power to delegate**

1. Under section 90AA(1) of the *Electricity Act 1994* (the Act), the Minister may delegate to the Queensland Competition Authority (QCA) all or any of the Minister's functions under section 90(1) of the Act.

**Powers delegated**

2. Subject to the limitations and requirements listed in paragraphs 3 and 4, I delegate the functions of the Minister under section 90(1) of the Act to the QCA.

3. The functions of the Minister specified in paragraph 2 above must only be exercised for the purpose of deciding the prices, or the methodology for fixing the prices, for the tariff year 1 July 2020 to 30 June 2021 that a retail entity may charge its Standard Contract Customers in Queensland, other than:
   (a) Standard Contract Customers in the Energex distribution area; and
   (b) notified prices for retail metering services for residential and small business customers.

4. Pursuant to section 90(5)(a)(iii) of the Act, in exercising the functions specified in paragraphs 2 and 3 above, the QCA must have regard to the terms of reference in the schedule.

**Revocation**

5. All earlier delegations of the Minister's powers under section 90(1) of the Act are revoked.

6. Unless earlier revoked in writing, this delegation ceases upon gazettal by the QCA of its final price determination on regulated retail electricity tariffs for the 2020–21 tariff year under section 90AB of the Act.

This delegation is made by **The Honourable Anthony Lynham MP**, Minister for Natural Resources, Mines and Energy:

**Signed:**

**The Honourable Anthony Lynham MP**
**Minister for Natural Resources, Mines and Energy**

**Dated:** 9/12/19

[redacted] **DELEGATION TO QCA**

**SCHEDULE**
**Terms of Reference**
**Section 90(5)(a)(iii) and 90AA of the Act**

***Period for which the price determinations will apply (section 90AA(3)(a) of the Act)***

1. These Terms of Reference apply for the tariff year 1 July 2020 to 30 June 2021.

***Policies, principles and other matters the QCA must consider when working out the notified prices and making the price determinations (sections 90(5)(a)(iii), 90AA(3)(c) and 90AA(3)(d) of the Act)***

2. The policies, principles and other matters that the QCA is required by this delegation to consider are:

   (a) On 1 July 2016, price regulation in the Energex distribution area was removed for small customers. This means that notified prices do not apply to customers in the Energex distribution area;

   (b) Uniform Tariff Policy — the Government's Uniform Tariff Policy, which provides that, wherever possible, customers of the same class should pay no more for their electricity, and should pay for their electricity via similar price structures, regardless of their geographic location. However, as residential and small business customers paying notified prices are on standard retail contracts, the Government is of the view that the QCA must consider incorporating into notified prices, an appropriate value reflecting the more favourable terms and conditions of standard retail contracts compared to market contracts. Should the application of this value result in a bill that exceeds the equivalent Default Market Offer as set by the Australian Energy Regulator for southeast Queensland, that value should be discounted so that the resulting bill does not exceed the equivalent Default Market Offer;

   (c) Default tariffs – nomination of a primary tariff for each class of small customer to apply to a customer's electricity account in the event the customer does not nominate a primary tariff when opening an electricity account;

   (d) Framework – use of the Network (N) plus Retail (R) cost build-up methodology when working out the notified prices and making the price determination, where N (network cost) is treated as a pass-through and R (energy and retail cost) is determined by the QCA;

   (e) When determining the N components for each regulated retail tariff:

      (i) For residential and small business customer Tariffs 11, 20, 31 and 33 - basing the network cost component on the relevant Energex network charges to be levied by Energex and the relevant Energex tariff structures;

(ii) For all other residential and small business customer tariffs - basing the network cost component on the price level of the relevant Energex network charges to be levied by Energex, but utilising the relevant EECL tariff structures, in order to strengthen or enhance the underlying network price signals and encourage customers to switch to time-of-use and demand tariffs and reduce their energy consumption during peak times;

(iii) For large business customers who consume 100MWh or more per annum - basing the network cost component on the relevant EECL network charges to be levied by EECL;

(iv) For Individually Calculated Customers (ICC), consider a methodology that allows for the pass through of the customers' individual network charges;

(v) For all existing Standard tariffs as set out in Part 2 of the current Tariff Schedule – maintaining these tariffs including price structures and access criteria unless otherwise set out in this delegation, and for those that do not have a network tariff of similar price structure and access requirements in the tariff year, or existing applicable network tariff structures are altered or extinguished - basing the network cost component on the most suitable network tariff consistent with e(i), (ii) and (iii) above;

(vi) In the event of significant uncertainty of both the prices and price structures of network tariffs to apply during the tariff year, and the QCA determines that there is insufficient time for the determination of the N component as set out in (e)(i), (ii) and (iii) above, use of a price indexation methodology to determine the N component for all existing Standard tariffs as set out in Part 2 of the current Tariff Schedule;

(f) Transitional Arrangements – maintaining the current phase-out dates of obsolete tariffs (i.e. Tariffs 20 (large), 21, 22 (small and large), 37, 47, 48, 62, 65, and 66);

(g) Continue enabling retailers to also charge Standard Contract Customers for the following customer retail services that are not included in regulated retail tariffs:

(i) Amounts in accordance with a program or scheme for the purchase of electricity from renewable or environmentally-friendly sources (whether or not those additional amounts are calculated on the basis of the customer's electricity usage), but only if:

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(a) the customer voluntarily participates in such program or scheme;
(b) the additional amount is payable under the program or scheme; and
(c) the retailer gives the customer prior written notice of any change to the additional amount payable under the program or scheme;

(h) Continuing Ergon Energy Queensland Pty Ltd's EasyPay Reward scheme.

***Consultation Requirements (section 90AA(3)(e) of the Act)***

*Interim Consultation Paper*

3. The QCA must publish an interim consultation paper identifying key issues to be considered when making the price determination.

4. The QCA must publish a written notice inviting submissions about the interim consultation paper. The notice must state a period during which anyone can make written submissions to the QCA about issues relevant to the price determination.

5. The QCA must consider any submissions received within the consultation period and make them available to the public, subject to normal confidentiality considerations.

*Consultation Timetable*

6. The QCA must publish an annual consultation timetable within two weeks after submissions on the interim consultation paper are due, which can be revised at the discretion of the QCA, detailing any proposed additional public papers and workshops that the QCA considers would assist the consultation process.

*Workshops and Additional Consultation*

7. As part of the interim consultation paper and in consideration of submissions in response to the interim consultation paper, the QCA must consider the merits of additional public consultation (workshops and papers) on identified key issues.

*Draft Price Determination*

8. The QCA must investigate and publish its draft price determination on regulated retail electricity tariffs, with each tariff (except for pricing for ICC determined under 2.(e)(iv) above) to be presented as bundled prices appropriate to the retail tariff structure.

9. The QCA must publish a written notice inviting submissions about the draft price determination. The notice must state a period during which anyone can make written submissions to the QCA about issues relevant to the draft price determination.

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10. The QCA must consider any submissions received within the consultation period and make them available to the public, subject to normal confidentiality considerations.

***Final Price Determination***

11. The QCA must investigate and publish its final price determination on regulated retail electricity tariffs, with each tariff (except for pricing for ICC determined under 2.(e)(iv) above) to be presented as bundled prices appropriate to the retail tariff structure, and gazette the retail tariffs.

***Time frame for QCA to make and publish reports (section 90AA(3)(b) of the Act)***

12. The QCA must make its reports available to the public and, at a minimum, publicly release the papers and price determinations listed in paragraphs 3 to 11.

13. The QCA must publish the interim consultation paper for the 2020–21 tariff year no later than one month after the date of this Delegation.

14. The QCA must publish the draft price determination on regulated retail electricity tariffs, and this should occur in February 2020, but not later than March 2020.

15. The QCA must publish the final price determination on regulated retail electricity tariffs for the 2020–21 tariff year, and it should have the retail tariffs gazetted by 31 May 2020, but not later than 26 June 2020.

(SCHEDULE ENDS)