



Stanwell Corporation Limited Submission

Queensland Competition Authority Draft Determination

Regulated Retail Electricity Prices 2012-13

April 2012

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About Stanwell Corporation

Stanwell Corporation Limited (Stanwell) is a diversified energy company and Queensland's largest power generator with a capacity to supply more than 45% of the state's power needs. A State Government-owned corporation employing almost 1000 people and with a \$1 billion turnover, Stanwell provides safe and reliable electricity for sale through the National Electricity Market (NEM).

On 1 July 2011, Queensland's government owned generators of Tarong Energy, Stanwell and CS Energy merged into two entities. Stanwell's portfolio was strengthened with the addition of Tarong, Tarong North, Mica Creek and Swanbank B and E power stations.

Stanwell now has a generation capacity of 4,526 megawatts, and generation assets valued at more than \$4.3 billion, with diversified gas, hydro and coal-fired plants operating from 11 geographically dispersed sites.

Key Issues with Respect to the Estimated Energy Purchase Costs for 2012/13 Retail Tariffs

Stanwell recognises the importance of ensuring cost-reflective retail tariffs to Queensland electricity retail customers. The Queensland Competition Authority's (QCA) revised regulated retail electricity prices methodology will have a significant impact on market outcomes, as it sets out how much retailers can afford to pay for energy. It is important that the methodology does not distort the market, but instead relies on the development of a competitive market (both wholesale and retail electricity markets) to ensure efficient price signals, which in turn are passed through to customers as efficient retail prices.

In the main the methodology proposed by the QCA in the Draft Determination will provide for a cost-reflective, unbiased estimate of energy purchase costs. Stanwell's comments on the Draft Determination focus on areas where it believes the proposed methodology is not appropriately cost reflective including:

- the proposed Gas Electricity Certificate (GEC) pass through;
- Small scale Technology Certificate (STC) prices; and
- The calculation of the NEM intensity utilised in the carbon pass through calculation.

GEC Pass through

For the 2011/12 BRCI the cost of compliance with the Queensland GEC scheme was based on a two-year average of the AFMA prices for GECs. ACIL Tasman notes that where a market price for inputs to the calculation of retailers' EPC can be sourced reliably and consistently it should provide the best guide to the cost of the compliance with the scheme.

However ACIL Tasman also goes on to note because GECs have been acquired by various means and the GEC market is now oversupplied the AFMA GEC prices have been averaged over an extended 4 year period.

Stanwell believes that the two year average should be maintained and that by using the 4 year average it is likely that Queensland consumers will not be paying competitive prices for GECs. In particular GEC pricing for the Regulated Retail Electricity Prices determination for 2012/13 should be estimated on an average of the last 2 years of spot prices for the following reasons:

- New entrant retailers in Queensland have been successful in sourcing GECs efficiently from the market rather than from long term GEC contracts;
- General consensus that state-based initiatives like NSW GGAS and Queensland GEC schemes will be dismantled with the introduction of carbon pricing, meaning the willingness of retailers to enter into long-term contracts has diminished. Any forward contracts written are also likely to be priced on a cost of carry basis from the current spot price. The QCA should err on the side of the customer in this case given the likelihood of the schemes complete removal in the short term, and;
- Both of the largest integrated and incumbent retailers (Origin and AGL) also have the capability to create substantial GECs from Queensland gas-fired generation (Darling Downs Power Station and Townsville Power Station respectively). Both retailers would have little or no requirement to enter into additional GEC contracts of any nature other than perhaps to reduce their inventory.

STC Costs

Stanwell believes that it is inconsistent with the Government's stated aim of cost-reflective retail tariffs to impose pass through costs of \$40 per certificate to customers when average costs for the last 12 months to retailers were <\$30 per certificate and expectations are of continued oversupply in the market. Incentives must be maintained for retailers to minimise costs to end use customers. Simply pricing the pass through at the penalty regardless of what costs retailers face in meeting their obligations will provide windfall gains to retailers, increasing costs to the customer and distorting wholesale and retail markets.

ACIL Tasman notes that the current clearing house price for STCs is \$40/STC, whereas the market price is around \$31/STC. However they go on to state that to use the market price would pose a difficulty because of the need to forecast the proportion of STC likely to be traded in the tariff year. Furthermore, while AFMA quotes a market price for STCs the volume traded at this price is unknown. ACIL advised the Authority that there were difficulties with using market data because it would require forecasts of the proportion of STCs likely to be traded in 2012/13. Given that the STC market is for spot sales and information on the volume of STCs traded in the open market is not publicly available, ACIL recommended the Authority continue to use the Clearing House price.

ACIL is correct in stating that most STC trading occurs in the spot market. As the most actively-traded of Australian environmental markets, data is readily available from market participants, and all spot transactions are recorded in the registry transfer details. Like GECs, it can be assumed that most STC transfers are driven by spot trades. It should also be noted that energy related brokers such as ICAP now produce a daily settle price for STCs (and LGCs).

There appears to be enough market data available to estimate the market cost of meeting Small-scale Renewable Energy Scheme obligations. Accordingly, it is important that the methodology does not incorporate inefficiencies with respect to the scheme design (i.e. incorporating the clearing price in estimating compliance costs).

Carbon pass through

ACIL Tasman has used its proprietary, "black-box" PowerMark model to estimate average NEM carbon intensity of 0.8696 in Calendar Year 2013. This is a significant decrease from an average NEM carbon intensity of 0.9223 in Financial Year 2011/12 (to 24 March 2012). Stanwell modelling indicates a \$23/tonne carbon price in 2012/13 will not markedly change the merit order.

ACIL Tasman has noted elsewhere the uncertainty of gas availability for gas-fired generation given increasing demand from the LNG industry (Coal Seam Gas in NSW: Implications for Energy Security and Economic Sustainability, 19 March 2012), specifically:

"Over the past five years there have been at least eight proposals for liquefied natural gas (LNG) plants based on CSG feed from the Bowen and Surat Basins.... If all of the proposed projects were to be developed to the ultimate capacities announced by their respective proponents, the total installed liquefaction capacity would be well in excess of 60 million tonnes of LNG per year... 60 million tonnes of LNG is equivalent to about 3,300 PJ of gas. Allowing for additional gas used in production, transportation and processing, gross CSG production required to support this level of LNG development would be around 3,800 PJ/a. The entire Eastern Australian domestic gas market currently consumes around 750 PJ/a (p9-10)."

While the industry will not be at full capacity in 2012/13, with recent announcements that some projects have less proven gas than anticipated (for example, Santos' announced in February 2012 that its current 2P reserves were not sufficient to support the entire development), it is expected that the major players will be retaining as much gas as possible to feed their projects.

Coupled with forecast gas price increases as demand from the LNG industry increases, the average NEM carbon intensity may not decrease to the level used in the draft determination in 2012/13.

Stanwell recommends that the QCA adopt the more likely NEM Intensity of 0.92 in line with current actual outcomes.

Conclusion

Stanwell appreciates the importance of ensuring cost-reflective retail tariffs to Queensland electricity retail customers. Stanwell believes that in the main the QCAs proposed methodology will provide a cost-reflective, unbiased estimate of energy purchase costs however there is an ability to more appropriately incorporate current market prices particularly with respect to GEC and STC costs.