



11 October 2010

Mr Gary Henry
Queensland Competition Authority
GPO Box 2257
Brisbane Qld 4001

by email: electricity@qca.org.au

Dear Gary

INTERIM CONSULTATION NOTICE: BENCHMARK RETAIL COST INDEX 2011-12

Origin Energy (Origin) believes that decision by the Minister for Natural Resources, Mines and Energy to initiate a benchmark retail cost index (BRCI) process for 2011-12 is prudent given the time restrictions on publishing retail electricity prices by 31 May 2011.

The time allowed for the Queensland Competition Authority (QCA) to conduct a BRCI process is itself shorter than in previous years. However, Origin takes comfort that the QCA has clearly stated in its *Interim Consultation Notice: Benchmark Retail Cost Index for Electricity 2011-12* (Interim Notice) that it intends to adopt the same methodology as used for the BRCI in 2010-11. This should ensure that the BRCI can be completed effectively for 2011-12 as almost all calculations have been consulted upon previously and the methods finalised.

Origin notes that a change in pricing methodology accompanied by retail tariff restructuring has been earmarked by the Queensland Government and Origin remains hopeful that this full review can be commenced during 2011 to ensure a fully consulted, comprehensive analysis of retail tariffs and any new methodology can be completed in time for 2012-13.

Given this impending review, it continues to be important that the BRCI process effectively adjust retail electricity tariffs to mirror the change in the cost of supplying electricity to Queensland customers so that any subsequent methodological change is not compromised before it begins.

This short submission addresses the specific questions raised by the QCA in its Interim Notice and reaffirms that the BRCI process should follow the same process that was carried out in 2010-11.

As highlighted by the QCA, the only readily identifiable change for 2011-12 will be the required estimation of the small-scale renewable energy scheme (SRES) that commences in 2011.

Cost of Energy:

The Authority seeks comments from stakeholders on any aspects of the approach to estimating the cost of energy component for the 2011-12 BRCI that they believe need to change from that followed previously.

In particular, the Authority seeks stakeholders' views on how the cost of complying with the new enhanced RET scheme should be estimated.

Origin is pleased to see that the QCA has engaged ACIL Tasman (ACIL) to provide expert advice and estimates of the cost of energy component for the 2011-12 BRCI.

This should ensure that the modelling of energy costs between 2010-11 and 2011-12 for both the long run marginal cost (LRMC) and energy purchase cost estimates is consistent with and readily comparable to the 2010-11 calculation.

It is Origin's hope that using ACIL will also ensure that the most up-to-date capital and fuel costs for generation will be able to be utilised in the LRMC modelling.

Origin further agrees with the QCA that the other energy costs components such as the Queensland Gas Scheme, Australian Energy Market Operator (AEMO) market fees and ancillary charges should be calculated applying the same methodology as used in 2010-11.

However, the significant changes made by the Commonwealth Government to the mandatory Renewable Energy Target (RET) Scheme will require both:

- an adjustment to the methodology for estimating the costs of the Large-scale Renewable Energy Target (LRET) scheme as targets and ratios previously used for RET will be impacted; and
- the introduction of a new cost component for 2011 to cover the Small-scale Renewable Energy Scheme (SRES).

Apart from the fixed price of \$40 per certificate, many of the details of the SRES operation are unknown at this stage so the QCA will initially be required to use estimates and assumptions in calculating the SRES cost for its Draft Decision. However, total SRES liability including the Small Technology Percentage (STP) based on expected small-scale RECs creation will be published by March 2011 and this will enable the QCA to effectively calculate the unit cost for the scheme for 2011.

Further assumptions will need to be made for 2012.

Origin would highlight that although the new enhanced RET schemes will become operational from 1 January 2011, the current retail tariffs in 2010-11 have not been adjusted for this added cost, despite it applying for 6 months of this financial year.

However the nature of the BRCI, being an index, will ensure that the 2011-12 retail tariffs are adjusted accordingly for the future impact of the scheme. This is because the 2011-12 BRCI, containing an allowance for SRES, will be compared to the 2010-11 BRCI, which had no such cost included.

Network Cost:

The Authority seeks comments from stakeholders on any aspects of the approach to estimating network costs for the 2011-12 BRCI that they believe need to be changed from that followed previously.

Origin supports the QCA using the same approach to determine network costs as it followed in the 2010-11 BRCI in that:

- transmission use of system (TUOS) charges are estimated based on the proportion of Powerlink's maximum allowable revenue (MAR) attributable to distribution in the previous year;
- distribution network costs for Energex and Ergon Energy are estimated based on the AER's approved annual revenue requirement; and
- no adjustments will be made for any previous annual under or over-recovery of TUOS charges or distribution revenue by Energex and Ergon Energy.

Origin would note that for 2011-12 and subsequent years, it appears as though the Energex network costs will be increasing at a greater rate than that allowed for Ergon under the AER's final decision.

As discussed in previous BRCI consultations, the BRCI uses a total network cost which averages these different rates of changes. Consequently, from 2011-12 onwards, there will be a deterioration in the cost reflectivity of retail tariffs in south-East Queensland because the BRCI allowance for network charges will always be below the network charges actually applied by Energex.

Origin understands that the QCA is constrained from acting on this issue by legislation and also notes that the average network calculation had an inverse impact in 2010-11 so this is not a significant problem for 2011-12.

However, Origin would not like to see this deterioration continue after 2011-12 and make tariff reform more difficult than need be.

Retail Cost and Margin:

The Authority seeks comments from stakeholders on any aspects of the approach to estimating retail costs for the 2011-12 BRCI that they believe need to change from that followed previously.

The QCA has continued to estimate the change in retail operating cost by escalating a benchmarked retail operating cost to account for inflation over the period.

Origin has and continues to support this method as it avoids the need for forensic cost analysis and the QCA accounts for both the impact of wages growth and price inflation on retail operating cost through the use of the Wage Price Index and Consumer Price Index.

Origin similarly supports the simple escalation of the customer acquisition and retention unit costs.

However, the other element of the customer acquisition costs is the forecast of the number of customers switching and transferring in the market. The QCA relied upon AEMO data as well as its own collected data reported by retailers to forecast the number

of customers switching retailer and transferring to market contracts within the same retailer. Origin has little transparency on these estimates and cannot readily confirm them but raises no objection with the proposed methodology.

Origin does not support the current 5 per cent allowance for retail margin and believes that this benchmark is not in line with the findings of other jurisdictions and any market data. However, Origin recognises that the BRCI is an index and any change to the retail margin for 2011-12 would need to be justified by an observable change in this cost component. Origin is not making such a claim but instead is suggesting that the figure used for retail margin in the BRCI is not an appropriate benchmark.

NEM Load:

The Authority seeks comments from stakeholders on any aspects of the approach to estimating the NEM load for the 2011-12 BRCI that they believe need to change from that followed previously.

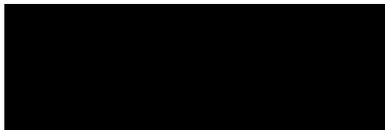
Origin supports the QCA's proposed approach for determining NEM load in the 2011-12 BRCI as that adopted in the 2010-11 BRCI.

Origin would also support the QCA continuing to provide the load data, including the initial estimates, at each stage in the BRCI process.

In summary, Origin is comfortable with the QCA's proposed approach for the 2011-12 BRCI and although the Draft Decision is not expected to be released until December 2010, would be happy to discuss any specific issues, including valuation of the SRES, prior to this time.

Please call me on (07) 3867 0620 if you have any queries regarding this.

Yours sincerely



Patrick Whish-Wilson
Regulatory Pricing Manager