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townsville enterprise

30 January 2015

Mr Sebastian Roberts
General Manager
Australian Energy Regulator
GPO Box 520
Melbourne Vic 3001
Email: QLDelectricity2015@aer.gov.au

Dear Mr Roberts

Submission to the QLD electricity distributors' regulatory proposals

Townsville Enterprise is the peak Regional Development Organisation and Regional Tourism Organisation for Townsville North Queensland. We represent over 350 businesses in the Townsville, Charters Towers, Hinchinbrook, Burdekin and Palm Island Shires.

The region is an economic powerhouse contributing billions to national GDP each year. However, due to a number of factors including ongoing drought in our agricultural hinterland, weak demand for resources, international, national and state conditions, and a resultant lack of business confidence, we are facing tough economic parameters and unprecedented levels of unemployment.

We write in response to the Australian Energy Regulator Issues Paper – Queensland electricity distribution regulatory proposals 2015-16 to 2019-20 released for comment in December 2014.

The high price, dramatic escalations in price in recent years and uncertainty over future price of delivered energy are one of the key constraints to economic development within our region.

The largest employers in our region are amongst those who consistently attribute energy as one of the most significant detriments to their business:

"*As a major user of energy and the largest private employer in the Townsville region, QNI is acutely aware of the need to minimise the impact of energy costs on its business. At a time of record unemployment in the region, QNI is strongly advocating the alleviation of energy pricing – to the direct benefit of not only QNI, but also its 1,000 strong workforce. QNI will continue to take its own actions to reduce its energy costs but it urges the Australian Energy Regulator to minimise any further retail energy costs, given the impact of spiralling price increases seen over the last 5 years. Moreover, the ability to generate more electricity in the North Queensland region at cheaper rates needs to be better considered. Currently, gas supply to the major regional electricity producers and industry in North Queensland is constrained by a single pipeline not connected to the national grid."* Queensland Nickel, 28 January 2015, representing it's 1,000 strong workforce.

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"…the fundamental problem is that transmission costs in North Queensland are amongst the highest in Australia, thereby stifling current and further development in the region. Currently, domestic electricity users pay similar rates across the State via a Community Service Obligation (CSO) system administrated by the Queensland Government, but no such system exists for businesses. This inequality restricts growth in regional areas and in particular North Queensland, which endures some of the highest transmission costs in Australia. For instance, Sun Metals Corporation Pty Ltd - a zinc refinery in Townsville pays $10 million per annum more in electricity transmission costs than an equivalent facility in Brisbane or Gladstone. It is recommended that the AER be the responsible body for administrating a Universal Service Obligation (USO) system, similar to the one that is currently imposed on the telecommunication industry. The telecommunication industry is obligated to ensure that standard telephone services (STS), payphones and prescribed carriage services are reasonably accessible to all people in Australia on an equitable basis, wherever they reside or carry on business. This would put two vital infrastructure industries (electricity and telecommunications) on an equal footing and help to ensure the further development of Australia." Sun Metals Corporation, 28 January 2015, impacting over 1,500 jobs in the North Queensland economy.

This extreme level of cost associated with energy has impacted the largest businesses to the smallest and - equally as important - households, particularly those impacted by the unprecedented levels of unemployment.

On behalf of businesses, communities and individuals in Townsville North Queensland we implore the AER to exercise its powers to ensure energy ceases to be the impediment to the growth, development and prosperity of this region it currently is.

Please feel free to contact me on 0401 828 024 should you wish to discuss our enclosed submission further.

Yours sincerely

Tracey Lines
General Manager Economic Development

SUBMISSION TO AUSTRALIAN ENERGY REGULATOR
QUEENSLAND ELECTRICITY DISTRIBUTION REGULATORY PROPOSALS
2015-16 TO 2019-20
ERGON ENERGY
JANUARY 2015

Townsville Enterprise is the peak Regional Development Organisation and Regional Tourism Organisation for Townsville North Queensland. We represent over 350 businesses in the Townsville, Charters Towers, Hinchinbrook, Burdekin and Palm Island Shires.

This submission is prepared in response to the Australian Energy Regulator (AER) issues paper released in December 2014. This submission is one component of a strategy aiming to remove the currently existing disadvantage imposed by high and escalating energy costs in Townsville North Queensland, and Northern Australia more broadly.

We assert that the industries and economy of Townsville North Queensland simply cannot sustain a period of electricity pricing uncertainty and increases similar to that experienced in the 2010 to 2015 period.

We believe that the National Electricity Objective is not being achieved. Electricity consumers in Townsville North Queensland are not being offered a reasonable level of service at the lowest sustainable price. The impact of prices considerably above those consumers are willing and able to pay is frustrating business and investment.

Further undermining of sector performance is certain in resources, agriculture, retail, construction and tourism without significant change in the delivered cost of energy in the region.

Cost effective energy supply and future pricing certainty are essential components of the region's growth and development. As asserted in the Federal Government's Energy Green Paper released in September 2014: "*Reliable and affordable energy, used productively, supports business competitiveness, lowers the cost of living, and grows export income.*" Broader State and Federal Government agendas of developing Northern Australia and decentralising Queensland cannot occur without an electricity supply that is secure, cost effective and importantly, gives a degree of certainty over future pricing.

We commend the Australian Energy Regulator in its intent for an informed and transparent consultative process. We also commend the clear and concise manner of delivering the messages. Given distribution comprises approximately 40% of total delivered energy cost, the importance of the revenue determination currently underway cannot be overstated.

We commend the reiteration that the National Electricity Law and National Electricity Rules focus squarely on outcomes for electricity consumers. Townsville Enterprise considers appropriate energy supply and pricing as a fundamental component for successful businesses within the region and economic performance of the region as a whole.

We believe the changed circumstances the market faces since the last determination period must be reflected, namely:

- Substantially lower cost of infrastructure financing;
- Less onerous network security and reliability standards;
- Reforms driven by the Queensland Government aimed at improving network efficiency; and
- Most significantly, flat or declining demand for electricity.

We propose that in all revenue discussion and figures, the Solar Feed-in-Tariff (FIT) is reported and illustrated as a separate stream to general revenue.

In response to specific questions raised by the AER:

Q1. Do you think that the distributor's capital expenditure proposals are adequately justified?

The Regulatory Asset Base (RAB) is already significant and is forecast to grow by another 28% over the next five years, primarily due to the proposed capital expenditure (CAPEX). The level of CAPEX must not be permitted to be higher than the rate of depreciation given the significant over investment in the previous period and weak demand projections.

Further justification is required based on:

- The inability of depreciation to offset inflation, which inherently increases the RAB regardless of any new CAPEX;
- Falling load factors;
- Relaxation in reliability and security standards; and
- Reduced level of demand to account for potential developments in technology in a rapidly evolving market for which no allowance has been made.

Additionally, electricity peak demand and consumption projections require scrutiny (ref Figure 8[i]) as Ergon's past projections have been found to be optimistic. Informed local expectations are for flat or declining consumption over the projection period. Forecast RAB in the previous determination period far exceeded actual RAB. Businesses in the region cannot afford for this error to be repeated.

Asset age is not the only determining factor when replacing assets. The duty cycle and condition also needs to be considered. Any asset replacement expenditure program should be supported by a quality maintenance system incorporating risk management and condition monitoring programs.

The lower input costs of commodities such as copper should show a significant reduction in purchase costs such as transformers, electrical cables etc.

We commend the close examination of Ergon's proposed increase in connections expenditure in 2014/15 which remains at that level for the duration of the regulatory control period in contrast to a modest increase in demand and consumption for the same period.

Q2. Are the distributor's operating expenditure proposals justified?

Operating expenditure (OPEX) is also a substantial driver in determining the average rate of return. Ergon is proposing a 2.6% reduction but comparing the current period against the proposed period on a like for like basis (removing meter reading and customer services) actually shows an increasing trend, so further justification is required.

- The proposal for an efficiency benefit sharing scheme payment of $146.1 million is not supported given:
    - The excessive escalation of real prices in the determination period;
    - The OPEX efficiency benchmarking by the AER has Ergon in the bottom quartile for both measurements, which predicates that their base OPEX is materially inefficient; and
    - Relaxation in reliability and security standards.

Q3. Do you consider that any departures from the Rate of Return Guidelines are justified?

In our opinion the current rate of return is significant for a monopoly entity with a guaranteed revenue stream that operates in a low risk business environment. Any departure to the Rate of Return Guidelines would only be considered if it is of benefit to the consumer.

The rate of return achieved must not be permitted to be higher than that based on a nationally consistent benchmark to ensure the most efficient financing.

Ergon carries no risk on consumption and is now proposing to pass through costs associated with high risk events. Ergon enjoyed a high weighted average cost of capital (WACC) under the current regulatory period as a result of the global financial crisis.

Q4. Do you consider the distributor has adopted practices set out in the Consumer Engagement Guideline to build genuine consumer engagement across all business activities? Do you consider the proposals reflect the engagement they had with you and issues you raised?

- We commend Ergon's thorough engagement program and the correct assertion that consumers seek relief from rising prices.

Other Issues

Metering:

- Any approach needs to incentivise both the distributor and consumer.

Cost Pass Through:

- If distributors are permitted to apply during a regulatory period for prices to be adjusted (upwards) due to an unexpected and material cost different to allowances, consumers must be protected in the same manner if conditions demand a downwards adjustment.
- If the Pass Through is accepted, then assurance needs to be given that the base apex is restated with any historical costs relating to the accepted events are removed.
- Accepting the Pass Through also de-risks the distributor's business and should also be reflected in the WACC.

We commend Ergon's resistance to previous reliability standards which would have resulted in even higher prices for consumers had they been implemented.

We commend the Queensland Government's adjustment of previous reliability standard settings. These adjustments must be reflected in pricing policy for consumers.

i AER, Issues Paper, December 2014