

Dr Peter Boxall
IPART
PO Box Q290
QVB Post Office NSW 1230
SENT BY EMAIL

10 May 2012

Dear Dr Boxall,

Re: Changes in regulated electricity retail prices from 1 July 2012

Thank you for the opportunity to provide a response to IPART's 'Changes in regulated electricity retail prices from 1 July 2012 Draft Report'.

QEnergy is a Transitioning electricity retailer currently operating in Queensland and preparing to enter the NSW small customer market. We primarily offer our services to small business customers, with a strong focus on building relationships in a personalised way.

QEnergy has had particular success in offering choice to customers who have not previously had the opportunity to benefit from competition, such as in regional Queensland and the Northern Territory. Now with 8,000 customers, QEnergy looks forward over the next years to growing our customer base by offering our services to small businesses across the National Energy Market.

QEnergy would like to congratulate IPART on the research done to consider the impact of rising electricity prices on households, particularly vulnerable households, as well as its recommendations on how to mitigate these impacts through regulatory change. We largely agree with IPART's conclusions as to the important steps to take to mitigate these issues, which we see as being important for the industry as a whole to correct.

From a pricing perspective, QEnergy considers that the Draft Report largely takes a reasonable approach to recognising changes in the relevant markets since IPART's initial determination. There are however three issues on which we wish to make comment:

- IPART's price-setting mechanism and its implications for passing on carbon prices;
- the cost pass-through mechanism as it relates to SRES costs;
- the impact of increased prudential support requirements post 1 July 2012 because of the introduction of a price on carbon.

The price-setting mechanism and its implications for passing on carbon prices

Generally speaking, QEnergy supports IPART's methodology for setting standard pricing, being a Weighted Average Price Cap that allows the Standard Retailers to set individual regulated retail prices subject to this cap. This effectively indexes the current suite of Standard Retail offer prices and escalates them in line with an increase in costs of the basket of goods considered by IPART through the determination process.

We also note that whilst the energy purchase cost allowance for Long-Run Marginal Costs of generation (LRMC) is higher in the Draft Report than the allowance for market-based prices, the increase in costs over the previous year – which is what ultimately determines customer prices – is significantly lower because of the reduction in WACC used to calculate the LRMC.

Further, the use of a pool-based methodology to calculate carbon costs in our view does not actually reflect the retailer costs of hedging this scheme. This is because the federal political environment has been so uncertain – see for example the opposing positions of the two parties and the precarious nature of the current parliamentary structure – that retailers have generally chosen to purchase full pass-through contracts to hedge their load. Under these contracts, the Australian Financial Markets Association pass-through calculation is applied to underlying 'black' contract prices, being the NEM pool intensity for that period multiplied by the carbon price for that period.

Thus, whilst IPART has allowed for the pass-through of carbon using a carbon-inclusive approach to modelling the LRMC, this methodology in combination with the decrease in LRMC costs because of the fall in the WACC means that the actual increases in costs faced by a prudent retailer are not reflected in the outcome.

The cost pass-through mechanism as it relates to SRES costs

QEnergy would like to commend IPART on recognising the genuine cost imposte imposed on retailers through the poor forecasting performance of SRES liabilities for 2012, which is required to be acquitted by retailers throughout the year but has largely been unable to be collected because of timing issues in jurisdictional price-setting processes. To demonstrate the impact that this has had, QEnergy plotted announcements as to SRES percentages below which demonstrate the impact and the volatility:

Publication Date	31/03	29/07	16/12	Final
2012 SRES Percentage	16.75	20.87	23.95	23.96

QEnergy hopes that IPART will continue to understand the impact that this unforeseen cost volatility has on retailers, and continues to make recompense as has been the case in the Draft Report.

Capital requirements and return on capital

To participate in the electricity markets, retailers must provide prudential capital to the Australian Energy Markets Operator, as well as to hedge counterparties for swap hedging and to Network Service Providers for network collections.

Following the introduction of a carbon price on 1 July 2012, prudential requirements to AEMO will increase by around 20%. These costs are often overlooked by regulators, and QEnergy considers that the cost of funding this increase should be considered either as a retail cost or through an increase in the return on capital.

Thank you again for the opportunity to comment on these issues. If you have any queries or comments regarding this letter, please do not hesitate to contact Kate Farrar, Managing Director on (07) 3339 9500.

Yours sincerely



Kate Farrar
Managing Director