



7 April 2004

Industry Levy
C/- MCE Market Reform
Department of Industry, Tourism and Resources
GPO Box 9839
CANBERRA ACT 2601

Dear Sir or Madam,

COMMENTS UPON MCE DISCUSSION PAPER "APPLICATION OF THE INDUSTRY LEVY TO FUND THE AER AND AEMC"

The Energy Retailers' Association of Australia ("ERAA") welcomes the opportunity to comment upon the "Application of the Industry Levy to Fund the AER and AEMC" discussion paper recently released by the Ministerial Council on Energy's Standing Committee of Officials ("SCO"). This submission provides the ERAA's views upon the consultation process itself, the positions put forward in the discussion paper and also comments upon some key issues not covered in the discussion paper which we believe need to be considered in conjunction with the allocation of an industry levy.

1. Summary of the ERAA Position

The Australian Energy Regulator ("AER") and the Australian Energy Markets Commission ("AEMC") are to be established by 1 July 2004 and, over a minimum period of 2 years, the roles of these two bodies will expand as they acquire greater responsibilities from the Australian Competition and Consumer Commission ("ACCC") and jurisdictional regulators. Until such time as the AER and AEMC are both fully established and have taken over responsibility for the regulation or market development/code management roles relating to the transmission, distribution and retail sectors (with the exception of retail pricing), for both electricity and gas, then a true understanding of the resource requirements and associated budgets cannot be delivered.

On this basis, the ERAA proposes that no additional levy (above that which industry is currently paying to fund the National Electricity Code Administrator) is to be paid by market participants for the period until the AER and AEMC roles are fully established. The jurisdictions should fund these bodies for additional costs in the intervening period as an incentive to ensure those bodies minimise their cost imposts and operate efficiently.

At the point where all costs are fully known, as are the operating structures of the AER and AEMC, industry would commence its funding, subject to 2 matters:

- demonstration that net regulatory costs are lower than those associated with the current decentralised regulatory model; and

- application of a CPI-X regime to reflect the need for efficiency and the shift to lighter handed regulation.

2. Discussion

2.1 Consultation Timeframes

The ERAA has substantial concerns over the brevity of the consultation period allocated for gathering comments from interested parties upon the application of an industry levy to fund the AER and AEMC. These natural justice concerns are heightened by a number of key issues:

- The discussion paper fails to discuss how the budgets for the AER and the AEMC will be set. Failing to consult on this important aspect has reduced the ERAA's confidence that the levy will reflect efficient costs of regulation and market development/code management.
- The costs imposed upon the industry appear to be increasing, not remaining static or decreasing.
- It is unclear whether industry concerns expressed over the industry levy will be incorporated into the relevant legislative framework due to SCO perceived timeframe pressures.
- Retailers and Generators have recently spent considerable monies fighting a dispute over market participant fees.

These issues are discussed in more detail in later sections, but in summary the ERAA is highly sensitive to the fact that this consultation process is both extremely short and incomplete in scope and hence there is a strong likelihood of delivering a high cost levy which is unjustified, inefficient and open to dispute.

2.2 Scope and Efficiency of costs

The Discussion Paper fails to address the important issue of what costs the AER and AEMC are allowed to recover from industry. Whilst the December 2003 announcement by the MCE indicated that the 2 statutory authorities would be funded through an industry levy, it was anticipated that the follow-up consultation paper would include a structured description of how budgets would be set, say through an SCI and industry consultation process, providing transparency and oversight of budget setting, including appropriate benchmarking. In this way industry would gain confidence that it was paying for efficient regulatory and market development costs, rather than 'signing a blank cheque' as is currently the case. Silence on the issue leads the ERAA to conclude that a public budget setting process is not envisaged and hence the statutory authorities will be able set their own budgets unchallenged.

Whilst the MCE's primary objective in establishing the AER and AEMC may not be to minimise the cost of regulation and market development, it is certainly a matter of keen interest amongst ERAA members. The rationalisation of regulatory bodies over time is expected to reduce the costs imposed on the industry (and ultimately passed through to consumers) and this aim should be borne in mind when developing the scope of the 2 bodies, their budgeting approval processes and the levy structure.

The aggregation of regulatory responsibilities into fewer agencies will generate both economies of scale and scope. Furthermore, as the shift to lighter handed regulation continues, the cost of regulation should decline over time (see the Productivity Commission recommendations for monitoring of networks). To help induce the realisation of these efficiencies, a CPI-X regime should apply to regulatory costs.

The ERAA has concerns that unless the MCE has reason to tightly control the costs of the AER and AEMC, costs will in fact escalate beyond current levels despite rationalisation. The ERAA are also concerned that without industry scrutiny of the costs incurred by the AER and AEMC, then the fee structure can become prone to dispute.

In response to these issues, the ERAA makes 2 proposals:

- a) the MCE be responsible for the costs of the AER and AEMC (over and above existing NECA costs) during the establishment and initial operating phase until such time as efficient costs structures and cost reporting mechanisms are in place (a 2 year period is suggested); and
- b) a 1 month consultation period with industry over budgeted costs and cost allocation should be required in order to allow comment upon costs incurred by the 2 bodies prior to their approval by the MCE.

It is the ERAA's view that these 2 steps are vital if the industry is to gain confidence that costs will be appropriately controlled, through MCE oversight and secondly that industry will have opportunity to review and comment upon budgets.

2.3 Transfer of Costs from ACCC to AER

The ERAA notes that AER staff are to be seconded from the ACC into the AER. According to the Memorandum of Understanding and the Code change Process documentation (recently released by SCO for comment also), these same staff will, at times, undertake work on behalf of the ACCC when authorisation matters arise from Code change processes. It is not discussed within the MOU documentation whether the ACCC will (rightly) pay for those staff during times of secondment back to the ACCC. The ACCC has always been funded through general revenues, rather than industry levies. The ERAA sees no reason when the ACCC is undertaking its functions as a competition regulator, regardless of whether it is using AER staff, why it would charge those costs to the energy industry. On this basis, the ERAA suggests that appropriate resource management systems will be required to monitor the time (and hence proportion of costs) AER staff spend undertaking ACCC work. In this way, costs can be appropriately allocated.

2.4 Establishment cost allocation between gas and electricity

The ERAA supports the allocation of costs between gas and electricity sectors based upon the respective costs incurred by the bodies when undertaking regulation or market development for the separate sectors. On this basis we query the relevance of the concept of ensuring that the levy does not impact the competitive neutrality of the two sectors.

2.5 Allocation of Costs to Regulated Sectors

The ERAA supports the comments in the discussion paper which favour allocating costs to the regulated segments of the electricity and gas sectors. We agree that allocating costs to the regulated segment has least impact upon the competitive market environment and would also simplify the transition process, whereby retailers may not be able to pass through levy costs from day 1, due to long-term contractual arrangements with customers, or a lack of levy allowance in regulated tariff rates. We believe however that regulated businesses would be able to recover the full costs, even if this is at a point in the future. However, the ERAA considers that isolation of costs to regulated sectors is most relevant should the quantum of the levy be relatively low, purely for the purposes of lowering the associated administrative cost. In the case where costs of the AER and AEMC become more significant, cost reflective allocation amongst industry sectors becomes more appropriate.

2.6 Transition Arrangements

The ERAA is keen to ensure that the levy arrangements are fully understood as soon as possible in order that any changes to customer pass-through arrangements can be made where required. In this regard, we expect that the AER and AEMC costs cannot be levied upon the industry until such time as they are performing their full complement of roles and as a result have a complete picture of their cost structures and associated recovery arrangements.

We would be pleased to discuss the comments contained in this submission if required. In this regard, please do not hesitate to contact me on 0419 444112.

Yours sincerely

Deane Russell
Executive Director