



'APPLICATION of the INDUSTRY LEVY to FUND the AER & AEMC'

The following comments by Eraring Energy relate to the MCE Discussion Paper 'Application of the Industry Levy to fund the AER and AEMC' dated March 2004.

1. Units of Power & Energy

The discussion paper is less than rigorous when describing the units of 'power' and units of 'energy' that may form the basis of allocation of the industry levy.

The technical units for energy are any of GWh, MWh or kWh for electricity and any of GJ, MJ or kJ for gas.

The technical units for power (or capacity) are any of MW or kW for electricity and any of GJ/day, MJ/day and MJ/hour for gas.

Thus section 3.4.1 should read:

- Energy throughput ...eg MWh or MJ
- Transmission capacity... eg MW or MJ/hour
- Peak load ... eg MW or MJ/hour

Sections 3.5.1 and 3.5.2 should read kWh (not kW)

2. Objectives

The objectives mentioned in Section 2 refer to providing an *'incentive for the AEMC and AER to be financially responsible'*. Whilst this is a very important aim to have these bodies accountable it is difficult to see how an industry levy would achieve this.

3. Economic & Financial Principles for Funding

Section 3.1 describes the primary cost pools for the AEMC and AER being 'common costs' (eg general administrative functions that underpin all sectors) and the 4 activity costs relating to markets and transmission in each of the electricity and gas sectors.

Issues of fairness and equity need to be addressed:

- Allocation of the common costs between these 4 activities.

–Whilst the common costs could be split between electricity and gas based on delivered energy such arrangement may have no relationship to the extent of work required of AEMC/AER in regard to these sectors. We would support an allocative method that initially apportions common costs based on expected workload for the first year and then adjusts the proportions each year thereafter as experience is gained in the extent of the workload.

- Ensuring that costs relating to a given activity are correctly allocated to that activity.

–Given the advanced nature of the electricity market and the developing nature of the



gas market, it could be argued that there will be an equal workload on AEMC/AER for these activities. Again, we would support an allocative method that initially estimates activity costs based on expected workload for the first year and then adjusts the activity costs for the next year to capture (budget – actual) activity costs for the past year and forecast activity costs for the next year. This way each activity ultimately bears the costs of AEMC/AER work solely for their activity area.

- Ensuring that the 'extraordinary costs' (especially establishment costs) are fairly allocated across the 4 activities

–It is expected that there will be some capital costs as well as some once-off administrative costs involved in setting up the AEMC/AER. It would be unfair to recover all of this expenditure in the first year of operation since this would cause a spike in levies that would be unpalatable to consumers. It is suggested that the 'extraordinary costs' be recovered over a 5 year period not unlike the arrangement used by NEMMCO when it was first established. The allocation between activities should ultimately recover the share of these costs based on the proportion of workload of the AEMC/AER over the 5 year period.

- Incorporation of Incremental Revenues

–Incremental revenues from publications and conferences will most probably be only a small fraction of the total AEMC/AER costs. Accordingly a simple approach is recommended such as reducing the 'common costs' by any revenues before allocation to activities as detailed earlier.

- Degree of Capture and Transparency

–The paper raises the possibility of regional offices and consequently the possibility of allocating these costs to the activity within that region. It also requests feedback on the degree of detail and transparency. Our view is that as far as reasonably possible, costs relating to a specific activity are ultimately charged to that activity via the levy. This would ensure fairness between the activities and avoid cross activity argument.

However in regard to the levy to be applied to a given activity, our view is that there should be a common national levy across all regions for that activity. This view is premised on the assumption that the levy in a given activity would be spread over and energy base rather than over a capacity or peak demand approach. (see latter comment). Thus for example if there were extra offices required in one region due to the workload there would also most likely be a higher energy base in that region and overall a fair allocation would result.

Of course in regard to the AEMC/AER being financially responsible it would be hoped that the need or otherwise for regional offices would be minimised.



4. Cost Recovery from Participants

Eraring Energy supports the 'user-pay' principle particularly the end-user as the most appropriate to bear the industry levy for AEMC/AER activities.

Eraring Energy recommends that the industry levy be based on an energy approach -- that is the cost be spread on a kWh consumption basis for electricity activities and on a MJ consumption basis for gas activities.

In the case of electricity market activities and electricity transmission activities, a combined levy should be applied to wholesale purchases from NEMMCO as the simplest most direct way and would match the current process whereby NEMMCO recovers its own costs through fees and recovers monies to cover NECA costs. Retailers would in turn allocate the cost to ultimate consumers after allowing for energy losses in distribution networks. Large consumers who purchase directly from NEMMCO would cover their own internal energy losses.

In the case of gas market activities and gas transmission activities, a combined levy should be applied to wholesale purchases from the gas market operator as the simplest most direct way. Retailers would in turn allocate the cost to ultimate consumers. In the interim period before the commencement of the full gas market, the combined levy would be charged directly to gas retailers and large gas consumers.

Alternative methods of allocating the levy based on the number of end users, transmission capacity, peak load, voltage or pressure, net revenue etc are totally inappropriate. Similarly spreading the levy across the spectrum of generators (or gas producers), transmission systems, distribution systems and end-users is unnecessary and would increase costs due to the extra complexity.
