

20 December 2006



Chief Executive
Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001

Email: electricity@qca.org.au

Dear Sir

CAPITAL EXPENDITURE PASS-THROUGH APPLICATION FROM ENERGEX LIMITED

The Energy Users Association of Australia ("EUAA") appreciates the opportunity to provide a submission on the capital expenditure pass-through application from Energex Limited ("Energex"). The EUAA is a non-profit organisation focused entirely on energy issues on behalf of large business end users of gas and electricity. The EUAA currently has around 85 members and its position as the national association of larger energy users means that membership ranges across many sectors of the economy, including mining, manufacturing, construction, commercial, property and service sectors. Many of the EUAA members operate across States and we have a significant membership base in Queensland.

The EUAA is keen to see the development of the Queensland energy market to support the competitive supply of gas and electricity to end users and the views in this submission have been formed on the basis of what is in the best interests of energy users. We are uniquely placed to provide the Queensland Competition Authority ("QCA") with such a view, given our involvement in both national and State energy policy issues.

The EUAA welcomes the fact that the QCA is enquiring specifically about the potential impact on end users of the pass-through of the additional capital expenditure proposed by Energex. We believe that end users of electricity should not be subjected to piecemeal price increases within a regulatory period. This would be the case if Energex is successful in its application to pass through a significant DUOS price increase in the remaining 3 years of the current regulatory period. Electricity can be a significant input cost for major end users and price rises will directly affect the competitiveness of their businesses.

Whilst we understand that Energex Networks is under some cost pressures and is endeavouring to implement the recommendations of the Somerville *Electricity Distribution and Service Delivery* Report, we are concerned that the Energex electricity distribution network requires such a significant capital works program to be undertaken in order to meet the system service, safety and reliability standards expected by end users. The annual level of expenditure within the current regulatory period requires allocation and consumption of a significant quantity of resources and we are concerned as to whether these resources are delivering efficient outcomes or simply adding to costs without due regard to attaining greater efficiency. The EUAA would urge the QCA not to approve the pass through of an additional \$720 million of capital works expenditure if there is any possibility that the works program cannot be delivered within the regulatory period resulting in a windfall gain for the distributor.

We note that the consultants advising the QCA during the Electricity Distribution Review expressed a concern that Energex may not be able to spend their allocated capex during the current regulatory period and we had a similar concern.

Background to the Application

The capex program being pursued by Energex has largely been determined by the findings of the *Electricity Distribution Service Delivery (EDSD)* Review. It is our understanding that the QCA's April 2005 Final Determination indicated the QCA may consider any further application by Energex for pass-through of additional *system-related* capex. The current application for pass-through of an additional \$720 million comprises \$643 million system capex and \$77 million non-system capex. Consequently, we query why there is even a necessity to consider the non-system capex.

Energex states that it is making this application because the \$2.207 billion capital expenditure already approved by the QCA for the current regulatory period does not include capital works to meet its EDSD obligations¹. Whilst end users appreciate Energex's desire to deliver its EDSD obligations, we note that delays in capex project completion can undermine the rate of economic growth in Queensland. It is the EUAA's preference that no additional capex be approved for pass-through if Energex cannot demonstrate that it is delivering in a timely fashion the projects in its current capex program. We do not accept that end users should pay for the costs of delays or unforeseen cost increases in Energex's capex program. These risks should be borne by Energex's shareholders, just as the windfall from any reductions would accrue to them.

Demonstrated Investment need

Energex has forecast improvements to its service delivery under a number of annual capex scenarios. Unsurprisingly, the SAIDI improves with increased levels of capex². However, it is our concern that the forecast service improvement gains cannot be physically delivered if projects are not completed on time. The application focuses on commitments to increase the capex program and forecast improvements to network performance and service delivery. We believe it would be useful if Energex could provide data illustrating its service delivery performance to date as we expect that some projects in the currently approved capex program should already be contributing to improved service delivery.

Able to undertake the Investment wisely

Electricity demand growth and economic growth throughout Queensland means that Energex has been competing with the other Queensland network businesses (and other businesses more generally) to secure the necessary resources to support its capex program. The EUAA notes Energex has made business changes to improve the planning and delivery of network investments and welcomes this. In particular, the resourcing of business processes and activities supporting the development of the capex program appears to have increased and Energex has provided graphs benchmarking its network against other unnamed Australian electricity distribution businesses. While the EUAA believes that all electricity network businesses must further improve their technical and service performance, we believe the benchmarking undertaken by Energex only serves to illustrate the inadequacy of its network investment to date. Therefore, given the necessity of delivering the capex program to support economic growth, we believe that some assessment is required of the timely delivery of Energex' capex projects. The QCA needs to ensure that this is provided and published.

¹ Energex Limited, Application for Additional Capital Expenditure *Part A*, October 2006, p.7-8

² Energex Limited, Application for Additional Capital Expenditure *Part A*, October 2006, p.14

Demonstrated new capex only

The EUAA notes that Energex has put forward this application on the basis that it is in support of new capex projects only. We are disappointed that Energex has been unable to identify any opex efficiencies to offset DUOS price increases resulting from the application to pass-through additional capex. If the capex projects are not delivered on time, end users will simply be paying higher network charges without any commensurate improvement in network operation and service delivery. Although Energex claims that the DUOS price increases are comparable (in percentage terms) to those imposed on customers by other electricity distribution companies, the EUAA submits that customers should not be subjected to piecemeal increases in network charges throughout a regulatory period.

The EUAA understands that the QCA and its consultants are scrutinising Energex' application to pass-through additional capex to end users. Energex itself notes that it will not be able to fully satisfy its EDSD obligations even with the additional capex of \$720 million³. The EUAA believes Energex' application will provide additional revenue to the electricity distribution business without offering service performance certainty to end users.

The EUAA further considers that if this Determination is to be reopened, the QCA should undertake a thorough assessment of the capex undertaken to date to ascertain whether the provision of the infrastructure has occurred within the timelines first proposed; and secondly as to whether the existence of such a large capex program in a resource constrained market is simply pushing up the price of the inputs without delivering additional service or other benefits to end users..

If you require further information please contact Bob Davenport, Director – Policy and Regulation on (03) 9898 3900 or at bob.davenport@euaa.com.au.

Yours sincerely



Roman Domanski
Executive Director

³ Energex Limited, Application for Additional Capital Expenditure *Part A*, October 2006, p.42