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Attn: Gary Henry

Dear Authority,

EUAA Submission – Efficiency Carryover Mechanism Issues Paper

The Energy Users Association of Australia (EUAA) would like to thank the Queensland Competition Authority (QCA) for the opportunity to comment on its September 2004 Issues Paper on the Efficiency Carryover Mechanism (ECM).

As you may be aware, the EUAA is a non-profit organisation focused entirely on energy issues. Members determine EUAA policy and direction. The EUAA represents a wide spectrum of end users in all Australian states and territories, including Queensland. It currently has around 75 members, predominantly business users with activities across all states and many sectors of the economy. EUAA activities cover both national and sub-national issues. Note that a significant proportion of EUAA Members have operations in Queensland and the EUAA also has a growing membership base there. (See <http://www.euaa.com.au/> for more information on the EUAA.)

Our comments below on the QCA's proposed ECM relate solely to electricity and gas.

In general, the EUAA supports the establishment of an ECM in electricity and gas. However, such an ECM should have the following characteristics:

- most of the efficiency gains should be passed on to end users – possibly something in the order of 75% for end users and 25% for the regulated business – given the importance of economic regulation translating into benefits to end users;
- the efficiency gains passed on to end users should be in the form of lower prices for all end users, but mainly for 'unprotected' ones – as 'protected' end users, such as households with air conditioning, have been, and will continue to be, sheltered from sufficiently cost-reflective prices, whereas 'unprotected' ones are subject to more cost reflective charges and often operate in trade exposed sectors;
- regulated businesses should not be allowed to unduly gain from the time value of money at the expense of end users;
- the distinction between efficiency gains and other gains should be clearly defined by the QCA and independently audited annually as part of current regulatory accounting and monitoring, without being overly onerous on regulated businesses – noting that:
 - what are gains due to efficiency is very difficult to identify in practice – recognising that it is always a matter of degree how much control a

- business has over its own processes, customers, suppliers, etc and therefore any gains;
- windfall gains due to industry-wide or economy-wide factors should not, as a matter of course, be exempted – such gains being passed on to end users is a feature of competitive markets;
 - gains due to unduly reducing service quality, avoiding investment or maintenance, should not be considered as an efficiency gain;
- symmetry should only go so far as punishing regulated businesses for not achieving its efficiency factors, not their customers – as this is what happens in competitive markets;
 - both capital expenditure savings, as well as operating expenditure ones (as clearly defined by the QCA), should be considered as part of an ECM – as such savings can legitimately be made through more innovative approaches to efficiency such as demand management;
 - in the case of electricity, the ECM should apply to both the 4 year regulatory period ending in June 2005 and the next 5 year period starting in July 2005.

In addition to the comments above, the EUAA would like to make the following points regarding the Issues Paper:

- the process going forward is not clear – the EUAA believes it should include a draft and final position/decision paper of some description;
- it is unclear what the QCA's current approach is vis-à-vis efficiency gains and how this currently effects end users and regulated businesses;
- it is unclear to what extent regulated businesses in Queensland and elsewhere have made efficiency gains in practice and, if so, how much;
- more research appears to be needed on what is done across all regulated industries (eg telecommunications) and overseas (eg NZ, UK, USA and Canada) as well as what leading experts (academic economists and otherwise) are suggesting;
- the attempt at using simple and practical examples (in Tables 1, 3 and 4) is very welcome, however, except for Table 1, the associated explanations could be clearer;
- a more explicit assessment of the pro's and con's of the various approaches to ECMs would be welcome, preferably using benefit-cost analysis (BCA).

If the QCA has any questions or comments regarding this submission, or any other related matter, then please contact Mr Darren Nelson – Manager, Policy and Regulation – on darren.nelson@euaa.com.au and/or 03 9898 3900.

Regards,

Mr Roman Domanski
Executive Director