

Funding End-User Advocacy

**SUPPLEMENTARY SUBMISSION
TO THE PRODUCTIVITY COMMISSION'S INQUIRY INTO
CLAUSE 6 OF THE
COMPETITION PRINCIPLES AGREEMENT
AND
PART IIIA OF THE TRADE PRACTICES ACT 1974**

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FUNDING END-USER ADVOCACY

1 *Summary*

The Commission sought views on ways to facilitate the participation of consumer interests in Part IIIA (and other access) decision making.

There are proposals to ensure greater consultation in the electricity and gas industries with bodies claiming to represent end-users. Such proposals are usually accompanied by calls for levying suppliers to fund bodies claiming to represent consumers.

There is presently considerable opportunity for almost any organisation or individual to comment on regulators' proposals regarding electricity and gas. Accordingly, IPA sees no reason to support the proposal that the bodies claiming to represent consumers be afforded rights, in excess of those they already have, to be involved in the decision making process.

The proposals amount to a tax on market participants (in the final analysis, the consumers) with the sums raised to be allocated to groups that claim to represent consumers. IPA considers that:

- A consumer representative role can have merit only where provision of the good or service is through a natural monopoly. The responsibilities for verifying that such markets meet consumer needs fall to agencies of government like departments of consumer affairs, the ACCC, state regulatory bodies and Ombudsmen¹. Within the limits of their budgets and legislative and ministerial guidelines, such agencies may seek advice from any bodies they consider to be useful. Unless accompanied by a reduction in funding to existing regulatory agencies, the proposal to fund outside bodies would, de facto, increase the funding for these purposes.
- There will be many bodies claiming to represent consumers, most of which represent only their sponsors and seek to obtain revenue through compulsion rather than by demonstrating their ability to provide value. Associations claiming to represent consumer interests rarely have the appropriate accountability or governance structure and are often dominated by and express the views of a small clique. If those groups are given preferred access, this could actually undermine consumer interests.
- It will be difficult to control the cost, and the coalition of interests necessary to agree a budget is likely to ensure a progressive increase year by year.
- In well-functioning markets, like the emerging gas and electricity markets, it is retailers that represent the interests of consumers; they do so not out of benevolence but out of necessity, since the retailer failing to supply goods and services that meet consumers' needs will lose market share and eventually be forced out of business.

¹ And in Victoria, it is proposed to add a further tier, the Essential Utility Services Consumer Advocacy Centre (EUSCAC).

2 Consideration of the Funding Issues

2.1 Taxation to Fund Advocacy Groups

2.1.1 Rational for Funding

It has been said that levies to fund consumer representation are common. However, such arrangements in gas and electricity pre-date the existence of markets. Where monopolies are in place, it is not unreasonable that the monopolist funds some voice from the users (though this would not obviate the normal problems of capture either by radical consumerists or by sectional user groups). We are now in the process of shifting to a full market where all customers are contestable and where retailers will be anxious to win sales by acting in the customers' interests.

2.1.2 Who Pays

Some suggest that a levy will be derived from suppliers' profits. This is not possible. If it were to occur resources would leave the industry to seek out better avenues for income. This would frustrate the development of the efficiency these industries are capable of achieving. Hence, a levy is quite clearly a tax on the retailers, the impact of which must be passed back onto the customer.

Current funding of regulatory agencies is determined by Parliaments. These provisions can be modified in the light of changing circumstances. However, an end-user advocacy function, in effect, introduces a major new body. Its funding through an impost on suppliers (and hence consumers) is the equivalent of governments hypothecating a tax to it.

2.1.3 Current Telecommunications Arrangements

One Australian industry which is in an analogous situation is telecommunications. Under the previous monopoly Telecom used to fund independent representation and research. Parliament agreed to section 593(1) of the Telecommunications Act (1997). This makes provision for Parliament to appropriate, and the Minister to disburse, funds for consumer representation and research. The funds are recouped from carrier licence fees.

The telecommunications model has a number of differences from a proposal sent to the ACCC by NECA². These include provision for:

- an annual appropriation made by the Parliament with the Minister (not as in the proposal, an appointee) determining how much of this shall be actually spent;
- a strict requirement for any consumer funded representation to demonstrate its consumer ties (and for this reason the Communications Law Centre is not significantly funded).

Most funding, around \$800,000 last year, actually went to three organisations: the Consumers' Telecommunications Network, the Small Enterprise Telecommunications Centre and the National Federation of the Blind Citizens of Australia.

² NECA, *End-user advocacy in the national electricity market*, November 2000.

2.2 Government Agencies as Consumers' Representatives

It is our view that a formally constituted and funded consumer advocacy body would assume functions which are already being undertaken.

Bodies charged with ensuring efficient outcomes and taking into consideration all interests include NECA, the ACCC, and the Office of the Regulator-General and the Ombudsman in Victoria (with other jurisdictions having comparable agencies). As previously mentioned, the Victorian Government is even suggesting a further agency, the Essential Utility Services Consumer Advocacy Centre (EUSCAC), as an additional tier. The body the proposal would create is at best a waste of money and at worst could lead to inefficiencies. The proposal is akin to that about which the Commission has sought advice.

The regulatory bodies act as honest brokers between different interests to take decisions on price and service in monopoly areas. They must necessarily provide their own input where they consider a party is insufficiently represented.

It is the deemed existence of monopoly elements in the electricity and gas supply industries (the wires and pipes) that gives rise to the need for regulatory oversight and regulatory bodies at the state and national levels. The price and service controls that the regulatory bodies possess are designed precisely to prevent monopoly elements exploiting their positions in the marketplace. To the degree these bodies with the designated responsibilities consider they need to solicit additional views that canvas a consumer perspective, they are funded to do so. In fact several agencies already provide some such funding to ensure they are fully apprised of views that take this perspective.

However, determining the prices and/or revenues for these natural monopoly facets of supply is a matter of estimating costs of supply and putting in place appropriate incentives to ensure efficiency. It is not obvious that consumer representatives have expertise in these matters.

2.3 Controlling the Costs and Determining Who Should be Funded

The only rationale for any funding or regulatory control is the existence of natural monopoly. Already we are seeing entrepreneurial interconnects undermining monopoly in electricity transmission and developments like Powercor's Docklands grid impacting on the monopoly of local distribution. Distributed energy in the form of co-generation will further diminish the need for regulation.

In the case of gas, the Australian Competition Tribunal has recognised the superiority of commercial rivalry over regulation in overturning the NCC's decision to regulate the Duke Energy pipeline into Sydney.

In these circumstances, even if there were a justification to do so, it is not advisable to introduce yet another rate-payer funded body into the energy supply industry.

In addition, deciding the aggregate level of funding for the group will be difficult. In the case of the national electricity market, the starting bid for those seeking funding was \$2.7 million per annum, most of which was to be spent on their own remuneration and travel.

The Energy Users Group, in its Submission to NECA on this matter, said *“Determining funding priorities is a matter best left to end-users themselves through the National End-User Council, which end users have already moved to establish”*. In this regard, the Public Interest Advocacy Centre (PIAC) has drawn attention to the likelihood of a coalition of advocates carving up the cake between themselves (and presumably leaving too little for PIAC). PIAC argues that there is nothing to be gained from research financed by a levy that simply benefits business and other large users who should be capable of funding their own research.

We see merit in the arguments PIAC raises. We also maintain that if an organisation is to have claims on public funding it should demonstrate it is truly representative. We know of no organisation that purports to represent consumers that has a mass support base of consumers. The most widely known organisation is the Australian Consumers Association (ACA). This has just 650 members. ACA claims it does not accept money from governments at least on an “on-going” basis.

Representational claims on the part of self-appointed consumer cadres are reminiscent of analogous claims of groups maintaining that they were the “vanguard of the proletariat”. People claiming to speak for consumers without having a mandate from them may no more represent their views and interests than did East European socialist parties who made a similar claim on behalf of workers.

Indeed, many “consumerist” organisations out of ignorance of the way that markets operate will act in ways that are inimical to consumer interests. Such actions may include seeking that suppliers take measures to connect remote areas at no extra cost or that they extend non-commercial payment terms to customers in arrears. Measures like this are founded on a false premise that the cost is borne by the supplier. In fact, the operations of markets and of financial systems are such that the costs are ultimately paid by other consumers, either in higher prices or in reduced levels of service.

This raises the issue of what are the true costs of regulation that requires a compulsory payment from consumers which is hypothecated to particular activities. The costs imposed by regulations or taxes are rarely confined to the immediate impact or the sums directly raised. Numerous studies have identified two other sorts of costs accompanying the direct costs. These are, first the paperburden and corresponding lobbying costs the regulated businesses are obliged (or feel obliged) to incur as a result of the regulations. Secondly, they are the market distortion costs resulting from their compliance. While we are not in a position to estimate the magnitude of these additional costs, on average the paperburden costs are twice the direct costs and the distortions caused by compliance are tenfold the direct costs.

2.4 Retailers as Consumer Representatives

The analysis used to justify the proposal for a levy to fund “representative” bodies is that consumers are diffuse, inclined to “free ride” and individually gain little to make it worthwhile for them to fund a lobby organisation. On this basis, it would be possible to argue for a levy to finance such bodies for almost every activity. After all, do not the same issues arise with motor cars and houses, to say nothing of small item and “impulse” purchases? We do not have such bodies generally because markets that comprise many buyers and many sellers ensure adequate disciplines on suppliers, who are required to give good value and respond to consumers’ needs.

The retailer becomes the customers’ agent in most markets, discovering consumer needs, matching these with the producers’ offerings and in the process bringing about revisions to these needs and offerings. Competition, and the wish of all parties to maximise their welfare, brings efficient outcomes from this interaction.

Littlechild³ identifies and describes the valuable functions that electricity retailers undertake. Once the retail function ceased to be regulated, retailers asked their customers what price system they wanted: uniform time of day, interruptible and so on. At the same time they asked generators what could be supplied and went about matching these requirements and offerings. Customers for their own part shopped around to get the best deals.

This has allowed consumers, retailers and generators to make better informed decisions about what is available, in the process raising the performance of suppliers and re-shaping the demands of users. Like gas and electricity, most lines in supermarkets have margins of only a few percentage points of the final price, yet the retailers are major interpreters of the consumer needs and hence value-drivers.

3 Concluding Comments

As far as supporting the consumer is concerned, IPA subscribes to Adam Smith’s view *“Consumption is the sole end and purpose of all production, and the interests of producers ought to be attended to, only insofar as it may be necessary for promoting that of the consumer.”*

Some of the bodies campaigning most vigorously for funding are represented by experienced people with useful analytical perspectives on the electricity industry. In spite of this, IPA questions whether any of them have any legitimate representational claims. Some may draw attention to a high readership of their literature, but on that basis the Sydney Daily Telegraph could mount much more powerful claims to be representative.

³ Stephen C Littlechild *Why we need electricity retailers: A reply to Joskow on wholesale spot price pass-through*, The Judge Institute of Management Studies, University of Cambridge, 22 August 2000

IPA has no objection to regulatory and quasi-regulatory bodies, consistent with their charters, financing the provision of advice from able people. However to introduce a new charge for this would be an unjustified impost on the consumer. And to set up a body at arms length from the accountability process is not acceptable.

IPA is conscious of the ability of taxpayer funded advocacy groups to obtain influence out of all proportion to their representation and, once established, to perpetuate themselves indefinitely. We therefore urge the Productivity Commission to reject this proposal.