

A NEW MANAGEMENT MECHANISM FOR POWER INDUSTRY

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1. General problem with management of the power industry

Management of the power industry means the control over production, transmission and distribution of power. Each government has a different approach to the control over the power industry but its choice falls into one of the three following management mechanisms:

a. The industry is under total control of the government that is responsible for all profits and losses. All power companies are owned by the state. This mechanism is common among countries where the economy is underdeveloped and non-state sectors are too small to engage in production and distribution of power.

b. The government has control over the power industry and allows state-owned power companies to have some autonomy in their business at two levels:

- Power companies undertake certain subcontract works (designing and building the distribution network for example) while the state controls the production, transmission and distribution of power.

- The state controls the production of power while power companies undertake the transmission and distribution of power.

This mechanism is usually found in countries where the market econ-

omy is developing, power companies have capacities to manage their business and take responsibility for losses and non-state sectors start to invest in this industry.

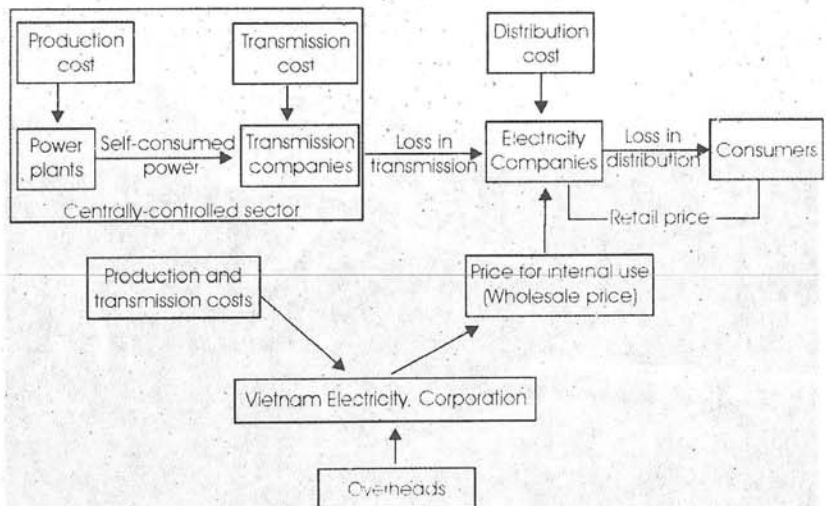
c. All sectors engage in the production, transmission and distribution of power and an organization is formed to ensure fair competition between power companies and interests of consumers.

An appropriate management mechanism can create favorable con-

ditions for the development of the power industry and force power companies to become more efficient and competitive with a view to ensuring better services and goods for consumers. That is why the mechanism for the power industry is periodically reviewed in order to introduce innovations.

2. The existing management mechanism for Vietnam's power industry

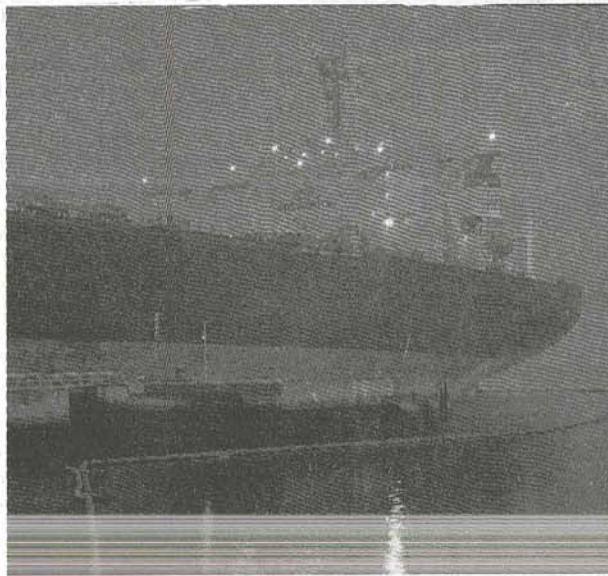
This mechanism could be presented in the following figure:



The figure shows that the centrally controlled sector includes the production and transmission stages. Costs generated in those two stages are included in the wholesale price offered by the Vietnam Electricity Corporation (VEC) to electricity companies that sell power directly to end users. There are some shortcomings of this mechanism:

- The production and transmission of power incur great expenses. If they are controlled by the VEC that is allowed to transfer these expenses to its buyers (electricity companies), the VEC has no incentive to reduce unit cost.

- At present, the VEC can't work out exact distribution costs suffered by different electricity companies in different provinces or zones, so it tends to set limits on these costs and adjusts these limits every year to real



costs incurred. This practice fails to encourage electricity companies to reduce losses of power in distribution and charge customers exact prices according to purposes of their use of power because the better they do their tasks the lower the limit set by the VEC.

- The salary scale set by the VEC is too egalitarian and fails to encourage local electricity companies because it isn't based on their business performance.

In short, shortcomings of the existing management mechanism applied to the power industry come from a basic cause: the accounts of all costs incurred in production and transmission stages are kept by the VEC while local electricity companies keep accounts of distribution costs. These shortcomings should be dealt with by adjusting the existing management mechanism.

3. A new management mechanism

First of all, we should accept that the new mechanism will be applied in a newly developed market economy in Vietnam where the competition isn't quite fair, so it can't be a perfect one and it only aims at improving the business performance of both VEC and local electricity companies. The basic solution is to keep separate accounts of production, transmission and distribution costs. Steps to take are as follows:

a. Allowing power plants to keep independent accounts:

- Determining costs and sales of each power plant: At this first stage, the power plant is required to keep an account of all costs with a view to finding ways to reduce them.

- Helping power plants improve its performance: The VEC assigns certain works to power plants so they can increase their sales and make some profits.

- Allowing independent accounts and equitization of some power plants: At this stage, power plants that complete the two previous stages successfully are allowed to become affiliates of the VEC. The VEC concentrates resources in successful power plants and it could equitize small ones because this equitization won't cause harm to its leading role in the industry.

b. Allowing transmission companies to keep independent accounts:

This step aims at separating transmission companies and developing them into affiliates of the VEC. It in-

cludes: (1) working out average costs of transmission and using them as target limits set for transmission companies, (2) allowing transmission companies to keep accounts of their own business, and (3) turning them into affiliates of the VEC and equitizing some of them.

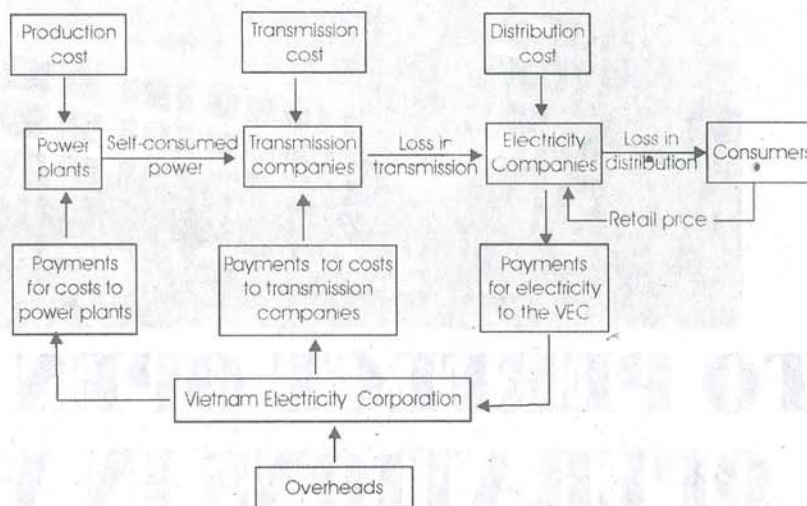
c. Giving more autonomy to local

ization for example).

- Commercializing goods and services of electricity companies.

The new management mechanism could be presented in the following figure:

In this new mechanism, the VEC still has control over the production and sale of electricity but it has



electricity companies:

- Emphasizing financial relation, instead of administrative one, between the VEC and electricity companies.

- Encouraging better business performance of electricity companies by adopting a new salary scale and system of targets assigned annually to these companies.

- Diversifying ownership of certain electricity companies (by privati-

accounts of production, transmission and distribution kept separately. The VEC sums up overheads, costs and sales; and works out profits and losses of subsidiaries. Affiliates that are allowed to keep independent accounts take full responsibility for their business performance. Net profit of the VEC is used for covering overheads and giving subsidies to independent affiliates in forms of expenses on maintenance of capacity and reasonable wholesale price. These subsidies are based on plans for annual expenditures approved beforehand by the VEC.

This mechanism can help (1) tapping resources of affiliates, (2) encouraging competition between electricity companies, (3) encouraging improvement in labor productivity and reduction in costs, (4) creating equal and cooperative relations between affiliates, and (5) creating preconditions for fair competition in the power industry in the future.

Changing the management mechanism is no easy task. It requires a scientific and overall scheme to phase it in. The power industry had better work out this project and submit to the Government as soon as possible ■

