Draft Distribution Pricing Principles and Methodological Requirements

From

Contact Energy Limited

30 October 2009

Introduction

Contact Energy welcomes the opportunity to respond to the Electricity Commission's consultation paper. Contact's response follows over the page.

For any questions related to this submission, please contact:

Peter MacIntyre
Regulatory Affairs Manager
Contact Energy Limited
L 1 Harbour City Tower
29 Brandon Street
PO Box 10742
Wellington

Email: **peter.macintyre@contactenergy.co.nz**
Phone: (04) 462 1399
Fax: (04) 499 4003

Submission

Contact's overall approach to the proposed pricing principles is to find the appropriate balance between the desire for purity in distribution pricing structure which can result in unnecessary complexity, and a pricing structure that gives certainty to retailers to pass through distribution costs without revenue risk from network charges while providing meaningful and understandable price signals to customers that incentivise an appropriate demand response. From this perspective Contact offers the following suggestions for the draft distribution pricing principles and methodological requirements.

PROPOSED PRICING PRINCIPLES

Principle (a)(i) –

- Use of the words "*subsidy free*" suggests purity in pricing that incentivises complexity. For example, some distributors will use this principle to justify summer/winter pricing, different pricing by balancing area within the same network region, urban/rural pricing, when a more pragmatic approach accepting a level of cross subsidy will still provide appropriate network investment signals that consumers will respond to without unnecessary complexity. The same argument can also be used to justify unnecessary complexity in loss factors. It is noted that network pricing signals are generally passed through by retailers unless the pricing structure is unnecessarily complex or unbillable given widely deployed metering, in which case the retailer ends up repackaging (cross subsidising) to ensure appropriate retail pricing for the various consumer categories and ability of consumers to shift load to lower cost periods. Contact would prefer to see the principle amended to
    - "*Minimise cross subsidies between customer categories, except where subsidies arise from legislation or are appropriate taking into account likely consumer behaviour and the trade-off between complexity and materiality of differences in network costs.*"

Principle (d) –

- This principle is intended to address consumer interests, but it fails to also take into account retailer interests to the extent retailers are interposed between the distributor and consumers. In this context it is not clear what "*development of prices should be transparent, promote price stability and certainty for consumers*" is trying to achieve. Contact has pointed out on several occasions that the key requirements are price <u>structure</u> stability and certainty for <u>retailers</u>, and not passing on unrecoverable network costs to retailers. Examples of concerns in this area are:

- Annually reset prices (or prices structured as annual charges) where the distributor expects to recover 100% of the annual fixed line charges off the retailer even where the retailer no longer has a contract with the consumer following the consumer relocating or closing down its business, or a new consumer moves to the site with a different profile and capacity requirement.
- The method of applying the prices results in unrecoverable costs on the retailer, examples being:
  - Variable line charges subject to loss adjustment or UFE scaling of metered consumption;
  - Charges include elements outside standard fixed/variable prices such as transmission administration charges recovered as a lump sum allocated to retailers based on monthly reconciled quantities.
- A more appropriate principle would be:
  - "*Development of prices should promote price structure stability and certainty of cost by ICP for retailers, be able to be passed through transparently given typical billing systems and widely deployed metering in the network area, and be able to be easily understood by consumers*."

Additional principle 1

- Contact would like to see a principle added to deal with annual line charges, along the following lines:
  - "*Except where a network investment agreement is signed by affected parties, prices should be structured to avoid pass through of unrecoverable charges to retailers that would arise if a consumer shifted location or ceased taking electricity at a site.*"

Additional principle 2

- Contact would also like to see a principle added to deal with pricing schedule completeness, along the following lines:
  - "*Pricing schedules should be complete and contain a unique pricing code for each fixed and variable price, and all relevant notes and*

definitions necessary for retailers to process the pricing without having to refer elsewhere."

PROPOSED METHODOLOGICAL REQUIREMENTS

Requirement (b)(v) –

- It is not clear why "*preserving the transmission pricing signal*" is relevant to methodological requirements. It would seem that more appropriate words would be "*taking into account the transmission pricing methodology and signal to the extent practicable*".

Requirement (b)(viii) –

- Given Contact's comments above re "*subsidy free*" it would seem more appropriate for the methodology to quantify the level of cross subsidies in prices for each service class, and the extent to which the cross subsidy is due to legislation. Accordingly Contact recommends that the requirement be amended to "*quantification of the average level of cross subsidy built into prices for each service class, and the extent to which the cross subsidy is caused by legislation*."