3 March 2022

Submissions
Electricity Authority
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By email: network.pricing@ea.govt.nz

Consultation rebate - congestion rebate methodology

Thank you for the opportunity to comment on the consultation paper titled *Settlement Residual Allocation Methodology: principles, options, and pass-through.*

As a guiding principle, we consider that:

- Settlement residue arising from existing losses and constraints on the grid should be assigned to those who pay transmission charges, in proportion to each customers' average injection or offtake in the regions where the losses and constraints arise.
- Settlement residue from a transmission investment should be assigned to those who pay charges in relation to that investment.

Ideally, the settlement residual allocation methodology (SRAM) should essentially mirror the transmission pricing methodology (TPM). It will be as simple or as complex as the transmission pricing methodology itself.

Given the centrality of the TPM to any discussion of settlement residual allocation methodology, we cannot discuss the latter without repeating aspects of previous submissions Contact Energy has made on the TPM. Our submission sets out in descending order of preference our position.

Contact Energy's preferred solution – SRAM aligned to an incremental improvement of existing TPM

As articulated in our cross-submission on the TPM dated 23 December 2021, we prefer incremental improvements on the status quo for the TPM. Using our guiding principle that the settlement residual allocation methodology should mirror the TPM, this would result in:

- **Settlement residue generated by each connection investment** allocated to the customer or customers who pay connection charges for that investment. These connection charges would remain broadly unchanged but:
  - include the proposal to add a funded asset component to address the free-riding problem of first movers bearing all of the capital costs of a connection asset even if other customers later connect to the asset;
  - a "pool and share" approach to anticipatory investments; and
  - the retention of the injection overhead component.

- **Settlement residue generated by each new grid investment of >$20 million** allocated to each customer who pays for this investment in proportion to the share of charges they pay for this investment. In our view, the method for calculating benefit-based charges needs to be simplified and made more transparent such that any reasonably informed electricity stakeholder can model transmission charges for themselves.

- **Settlement residue generated by investments whose cost is covered through the residual charge** allocated to customers that pay the residual charge. However, rather than allocating the settlement residue via a gross AMD allocator in the same way that the residual charge of the TPM is calculated[1], the settlement residue would be matched to simple method regions and then the applicable allocators for each region would be used to allocate the settlement residue to each customer.

Contact Energy's fall-back solution –modified Option C – full BB

Consistent with the Electricity Authority's proposals around the new TPM, we consider that a modified version of Option C would best achieve the two guiding principles outlined above. This option would see the settlement residue generated by:

- **Connection assets** allocated to the customer or customers who pay connection charges for that investment, in proportion to the share of charges they pay for this investment;

- **Schedule 1 historic benefit-based investments** allocated to the customer or customers who pay for these assets in proportion to the share of charges they pay for this investment;

- **New investments of >$20million subject to the standard method under the new TPM** allocated to the customer or customers who pay benefit-based charges for that investment, in proportion to the share of the charges they pay for this investment;

- **Low value investments of <$20 million subject to the simple method under the new TPM** allocated to the customer or customers who pay connection charges for that investment, in proportion to the share of charges they pay for this investment**.**

  As noted in our submission on the TPM dated 2 December 2021, we do not agree with the underlying assumption of the simple method that equates electricity flows to beneficiaries. The flow of electricity from a generator to a load customer does not reflect the value each party ascribes to electricity. The reality is that load customers value electricity far more than generators and this is not reflected in the current proposal of a 50:50 split between load and generation. At the very least it should be 75:25;

- **All other Transpower assets subject to the residual charge under the new TPM** allocated by matching it to simple method regions and using the applicable allocators for each region. In this instance we consider that using a non-weighted simple method approach is appropriate

[1] As noted in our 23 December 2021 cross submission on the TPM, we consider that the residual charge should be based on the existing RCPD interconnection charge but with the number of peak trading periods used as the basis to calculate the charge increased from 100 to ~500[1] (to reduce the overly strong price signals created using the existing method).

as electricity flows across different parts of the grid will correspond to existing losses and constraints.

In our TPM submission dated 2 December 2021, Contact Energy raised some specific concerns around some of the assumptions used to calculate the benefit-based charges. In addition to the point raised about the assumption underpinning the simple method, we consider:

- Benefit-based charges should not recover a portion of Transpower's overheads as these are not directly attributable to the investment. The Electricity Authority articulated this very same position on multiple occasions in consultation rounds and in correspondence to Transpower. We agree.

- Benefit-based charges should not apply to a large plant that has closed for benefit-based investments that have been commissioned within the last ten years.

We note the Electricity Authority's concerns around Option C of additional complexity and the potential for gaming. In our view, to the extent these concerns apply to settlement residue they would apply equally to the transmission pricing methodology. They are not reasons in themselves to depart from the guiding principles set out above.

If there is an obvious case of an electricity market participant gaming the system by exacerbating a constraint in a region to maximise their settlement residue, then we suggest that this settlement residue could be used to invest in alleviating the constraint rather than being assigned to the party exacerbating the constraint.

Distributors should be required to pass settlement residual rebates to customers

We agree with the Electricity Authority's proposal to require distributors pass settlement residual rebates to their customers. In our view, this is an uncontroversial proposal.

If you have any questions, please contact David.Buckrell@contactenergy.co.nz or myself.

Yours sincerely,

Chris Abbott
Chief Corporate Affairs Officer