Distribution Pricing Principles and Information Disclosure Guidelines

Prepared by the Electricity Commission

December 2009

Executive summary

1. On 5 June 2009, the Electricity Commission (**Commission**) published a consultation paper outlining a proposed model approach to an electricity distribution pricing methodology (**First Consultation Paper**). This approach used as a starting point the model pricing methodology of the Pricing Approaches Working Group (**PAWG**) (**PAWG model approach**).

2. On 30 September 2009 the Commission published a discussion paper, “Draft Distribution Principles and Methodological Requirements” (**Second Consultation Paper**), and then held a workshop for interested stakeholders on 12 October 2009 (**October workshop**), where proposed pricing principles, methodological requirements and compliance reporting were discussed.

3. Following consideration of the submissions received on the Second Consultation Paper and discussions at the October workshop, the Commission has formed the following view on a voluntary approach to a distribution pricing methodology:

    (a) a principles-based approach to a distribution pricing methodology should be adopted (**pricing principles**);

    (b) the Commission will publish guidelines to assist distributors with the preparation of the information disclosure on their distribution pricing methodology and to assist an independent expert reviewer to assess distributors’ compliance with the pricing principles (**information disclosure guidelines**); and

    (c) the Commission will initiate periodic independent expert reviews to measure distributors’ compliance with the pricing principles using the information disclosure requirements provided for in the Commerce Act 1986 (Commerce Act) initially and using the information disclosure guidelines for the following and subsequent years.

4. The Commission has noted the feedback received from submitters on the Second Consultation Paper and has adopted suggestions relating to:

    (a) clarifying and simplifying the pricing principles;

    (b) moving away from methodological requirements to guidelines on information disclosure. These information disclosures align more closely with the Commerce Commission’s preliminary view on the direction of the information disclosure requirements under the new Part 4 of the Commerce Act;

    (c) having an independent expert undertake a periodic review of distribution pricing methodologies;

(d) publishing the results of the independent expert's review (using a league-table approach for oversight); and

(e) if at any time the Commission believed that a distributor had not provided sufficient information or was materially non-compliant with the pricing principles, the Commission would seek to persuade the distributor to comply. In these circumstances, if there was no improvement, the Commission would consider direct regulation.

5. The Commission has, where appropriate, formulated the pricing principles to:

(a) reflect objectives set out in the Electricity Act 1992 (**Act**);

(b) reflect relevant objectives in:

(i) the transmission pricing methodology (**TPM**)[1]; and

(ii) the Electricity Governance (Connection of Distributed Generation) Regulations 2007 (**Distributed Generation Regulations**); and

(c) align where practicable, with the Commerce Commission's pricing principles as set out in the gas authorisation for Vector and Powerco.

6. The proposed pricing principles are as follows:

Pricing Principles		
(a)	Prices are to signal the economic costs of service provision by:	
	(i)	being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), except where subsidies arise from compliance with legislation and/or other regulations;
	(ii)	having regard, to the extent practicable, to the level of available service capacity; and
	(iii)	signalling, to the extent practicable, the impact of additional usage on future investment costs.
(b)	Where prices based on 'efficient' incremental costs would under-recover allowed revenues, the shortfall should be made up by setting prices in a manner that has regard to consumers' demand responsiveness, to the extent practicable.	
(c)	Provided that prices satisfy (a) above, prices should be responsive to the requirements and circumstances of stakeholders in order to:	
	(i)	discourage uneconomic bypass;

[1] The TPM is set out in Schedule F5 of section IV of part F of the Electricity Governance Rules 2003 (**Rules**). The Commission is currently conducting a review of the TPM, and a consultation paper was published in October 2009.

	(ii)	allow for negotiation to better reflect the economic value of services and enable stakeholders to make price/quality trade-offs or non-standard arrangements for services; and
	(iii)	where network economics warrant, encourage investment in transmission and distribution alternatives (e.g. distributed generation or demand response) and technology innovation.
(d)	Development of prices should be transparent, promote price stability and certainty for stakeholders, and changes to prices should have regard to the impact on stakeholders.	
(e)	Development of prices should have regard to the impact of transaction costs on retailers and should be economically equivalent across retailers.	

7. The proposed information disclosure guidelines are as follows:

Information Disclosure Guidelines		
(a)	Prices should be based on a well-defined, clearly explained and published methodology, with any revisions notified and clearly marked.	
(b)	The pricing methodology disclosed should include sufficient information on the following for an independent expert to assess compliance with the pricing principles, including:	
	(i)	how the methodology links to the pricing principles and any non-compliance;
	(ii)	the rationale for consumer groupings and the method for determining the allocation of consumers to the consumer groupings;
	(iii)	quantification of key components of costs and revenues;
	(iv)	an explanation of the cost allocation methodology and the rationale for the allocation to each consumer grouping; and
	(v)	pricing arrangements that will be used to share the value of any deferral of investment in transmission and distribution assets with the investors in alternatives such as distributed generation or load management, where this is practicable.
(c)	The pricing methodology should:	
	(i)	employ industry standard tariff formats and nomenclature, where possible; and
	(ii)	where a change to the existing pricing methodology is proposed, describe the details of the impact on consumer classes and the transition arrangements proposed to mitigate the effect of redistribution of costs and “rate shock”.

8. The Commission will work with the Commerce Commission to ensure consistency between the information disclosure requirements of the two entities in respect of distribution pricing. The Commission notes that this is likely to be an iterative process and that over time there may be further refinements to the proposed information disclosure guidelines set out in this consultation paper.

9. The Commission proposes that distributors first use the information disclosure guidelines to report against the pricing principles in March 2011 (for the 1 April 2011 – 31 March 2012 financial year). Provided that the information sought by the Commission is the same as the information submitted by distributors to the Commerce Commission, with respect to the information disclosure on pricing methodologies, , the Commission would source the information from the distributor's website. If further information is required the Commission would seek the information directly from distributors. The Commission's process seeks to avoid duplication.

10. For the 1 April 2010 - 31 March 2011 financial year, the Commission proposes that distributors report against the pricing principles prior to 1 April 2010, using the information disclosure requirements published pursuant to the Commerce Act 1986.

11. By 31 July 2010, each distributor will receive an independent expert's draft report on the compliance of the distributor's distribution pricing methodology against the pricing principles, and should respond to the Commission on the findings of this report by 31 August 2010. The Commission will publish a summary of the independent reviews by 30 September 2010, with a score for compliance with the pricing principles.

12. The Commission proposes to repeat this process (including the independent review) in the 1 April 2011- 31 March 2012 financial year, but with distributors reporting against the pricing principles using the information disclosure guidelines.

13. Subsequent reviews by an independent expert of a distributor's reporting against the pricing principles will occur only when a distributor amends its pricing methodology or has not amended a materially non-compliant pricing methodology.

14. The timetable for completing the Commission's approach to a distribution pricing methodology is set out in the following table.

Table 1 Process to complete the distribution pricing methodology approach

Date	**Event**
December 2009	Industry working group reports back on administrative issues that can be bilaterally addressed by retailers and distributors
1 December 2009	Final consultation paper published on pricing principles and information disclosure guidelines (Third Consultation Paper)
22 December 2009	Submissions due on Third Consultation Paper

Date	Event
February 2010	Publication of final pricing principles and information disclosure guidelines

15. Submitters have raised matters not directly related to developing a model approach to distribution pricing but which they suggested should be addressed as part of the distribution pricing project. The material provided for the distribution pricing project will be made available to other relevant Commission workstreams. The matters include:

    (a) the lack of a dispute resolution process;

    (b) coverage to extend to embedded networks;

    (c) Low fixed charge regulations;

    (d) rural/urban line charge relativity;

    (e) the large number of distribution businesses;

    (f) Model Use of System Agreement (MUoSA).

16. Three of the above issues are matters of government policy (low fixed charge regulations, suggestions that the distributors should be amalgamated and rural/urban line charge relativity.

17. The Commission has also facilitated an industry working group on administrative issues related to distribution pricing. At the first workshop on distribution pricing in June 2009, industry participants suggested to the Commission that there were administrative issues that could be agreed bilaterally between participants without the need for Commission guidelines or intervention. The implication was that there were relationship issues that could be addressed via Commission-facilitated focussed discussions that would reduce costs for both retailers and distributors. At the October workshop, a consensus emerged as to what administrative issues the working group could address. These were:

    (a) wash-ups;

    (b) unnecessary complexity of tariffs;

    (c) unaccounted-for electricity; and

    (d) common terminology.

18. At the subsequent meetings these issues were further refined. It is expected that the group's conclusions will be published in late December 2009.

Glossary of abbreviations and terms

Act	means the Electricity Act 1992
Commerce Act	means the Commerce Act 1986
Commission	means the Electricity Commission
Consumer	means any person who is supplied electricity for consumption and includes a distributor, retailer or generator where the distributor, retailer or generator is supplied with electricity for its own consumption
Distributed Generation Regulations	means the Electricity Governance (Connection of Distributed Generation) Regulations 2007
Distributor or Electricity Distribution Business (EDB)	means any electricity industry participant who owns or operates a network (that is not an embedded network) other than Transpower
First Consultation Paper	means the consultation paper, *Distribution Pricing Methodology – consultation paper on a model approach*, published by the Commission on 5 June 2009
ICP	means a point of connection on a local network or embedded network, having the attributes set out in rule 1 of schedule E1 of the Electricity Governance Rules 2003
GPS	means the Government Policy Statement on Electricity Governance published in May 2009
Load Group	means a category of consumers from which load-dependent costs (i.e. costs incurred by a distributor to provide network capacity to supply the load on its network) will be recovered
MUoSA	Model Use of System Agreement
Network	means the lines, and associated equipment, owned or operated by a distributor in a contiguous geographic area or areas;
PAWG	means the Pricing Approaches Working Group, which was a consultative group formed by the Electricity Networks Association for the purpose of developing voluntary model approaches to distribution pricing in New Zealand
PAWG model approach	means the recommended model approach for distribution pricing set out in the PAWG report

PAWG report	means the PAWG report, *Model Approaches to Distribution Pricing* dated February 2005
Retailer	has the meaning set out in part A of the Rules
Rules	means the Electricity Governance Rules 2003
Second Consultation Paper	means the paper, *Discussion Paper – Draft Distribution Pricing Principles and Methodological Requirements*, published by the Commission on 30 September 2009
TPM	means the Transmission Pricing Methodology set out in Schedule F5 of Section IV of part F of the Rules

Contents

1. Introduction

1.1 Consultation undertaken on a model approach

1.1.1 On 5 June 2009, the Electricity Commission (**Commission**) published a consultation paper entitled "Distribution Pricing Methodology, Consultation paper on a model approach" (**First Consultation Paper)**[2] outlining a proposed model approach to an electricity distribution pricing methodology and asking interested stakeholders to comment. This approach used as a starting point the model pricing methodology of the Pricing Approaches Working Group (**PAWG**) (**PAWG model approach**).

1.1.2 The Commission held a workshop on 17 June 2009 for interested stakeholders to discuss the content of the First Consultation Paper and to facilitate the preparation of submissions. Submissions on the First Consultation Paper closed on 10 July 2009. The Commission received 27 submissions[3].

1.1.3 Based on the submissions received, the Commission reviewed the initial proposed approach and developed a revised approach. On 30 September 2009 the Commission published, for consultation, a discussion paper entitled "Draft Distribution Pricing Principles and Methodological Requirements" (**Second Consultation Paper**)[4] outlining the following preliminary view on a model approach to a distribution pricing methodology:

(a) a principles-based approach to a distribution pricing methodology should be adopted; and

(b) guidelines (methodological requirements) should be provided to assist stakeholders with interpreting and implementing the proposed pricing principles.

1.1.4 On 12 October 2009 the Commission held a workshop for interested stakeholders to facilitate the preparation of submissions. Submissions on the

[2] The First Consultation Paper can be viewed at http://www.electricitycommission.govt.nz/pdfs/opdev/transmis/pdfsconsultation/distribution-pricing-methodology.pdf.

[3] The submissions received can be viewed on the Commission's website at http://www.electricitycommission.govt.nz/submissions/substransmission/distrib-pricing.

[4] The Second Consultation Paper can be viewed on the Commission's website at http://www.electricitycommission.govt.nz/pdfs/opdev/transmis/distrib-pricing/discussionpaper-Sep09.pdf

Second Consultation Paper closed on 30 October 2009. The Commission received 18 submissions[5].

1.1.5 The Commission notes that some of the issues raised at the workshops and through submissions are contractual issues that might be resolved once Model Use of System Agreements (**MUoSA**) are in place. There is a clear distinction between the distribution pricing and the MUoSA[6] workstream as the focus of the development of a model approach to distribution pricing is to assist distributors in structuring their distribution prices so as to deliver the most economically efficient outcome while the MUoSA on the other hand will set out model distribution arrangements between retailers and distributors.

1.2 Principles-based model approach

1.2.1 The Commission has now completed an assessment of the submissions and has formed the following view on a model approach to a distribution pricing methodology:

(a) a principles-based approach to a distribution pricing methodology should be adopted (**pricing principles**);

(b) the Commission will publish guidelines to assist distributors with the preparation of the information disclosure on their distribution pricing methodology and to assist an independent expert reviewer to assess distributors' compliance with the pricing principles (**information disclosure guidelines**); and

(c) the Commission will initiate periodic independent expert reviews to measure distributors' compliance with the pricing principles, using the information disclosure requirements provided for in the Commerce Act initially and using the information disclosure guidelines for the following and subsequent years.

1.3 How to provide feedback

1.3.1 The Commission is seeking stakeholders' feedback, through written submissions, on the pricing principles and the proposed process for distributors to report against the pricing principles, along with feedback on the information disclosure guidelines. In respect of the pricing principles and the information disclosure guidelines, the Commission has taken into account the substantive matters

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5 The submissions received can be viewed on the Commission's website at http://www.electricitycommission.govt.nz/submissions/substransmission/draft-pricing-principles.

6 http://www.electricitycommission.govt.nz/opdev/retail/model

contained in the submissions received to date. The Commission would appreciate comments on issues such as drafting and any new substantive issues submitters consider are raised in this Consultation Paper, rather than reiteration of points made in previous submissions.

1.3.2 The Commission's preference is to receive written submissions in electronic format (Microsoft Word). It is not necessary to send hard copies of submissions to the Commission, unless it is not possible to do so electronically. Submissions in electronic form should be emailed to submissions@electricitycommission.govt.nz with "Distribution Pricing Principles and Information Disclosure Guidelines" in the subject line. The Commission will acknowledge receipt of all submissions electronically. Please contact Kate Hudson if you do not receive electronic acknowledgement of your submission within two business days.

1.3.3 Your submission is likely to be made available to the general public on the Commission's website. Submitters should indicate any documents attached, in support of the submission, in a covering letter and clearly indicate any information that is provided to the Commission on a confidential basis. However, all information provided to the Commission is subject to the Official Information Act 1982.

1.3.4 If submitters do not wish to send their submission electronically, they should post one hard copy of their submission to the address below.

Kate Hudson
Electricity Commission
Level 7, ASB Bank Tower
2 Hunter Street
Wellington

Tel: 0-4-460 8860

1.3.5 Submissions should be received by **5pm** on **Tuesday 22 December 2009**. Please note that late submissions are unlikely to be considered.

2. Background

2.1 Key reasons for a model approach

2.1.1 The overarching reason for the development of a model approach to a distribution pricing methodology is to assist distributors in structuring their distribution prices to deliver the economically efficient outcomes[7].

2.1.2 The Commission expects that the benefits of such an approach will lead to:

(a) distributors charging for distribution services in a way that:

(i) encourages the efficient use of electricity by end users;

(ii) encourages efficient investment in distribution, transmission, distributed generation (including renewable generation), and technology innovation;

(iii) maintains or enhances investment in energy efficiency and demand-side management;

(iv) signals the full costs of transporting each additional unit of electricity to users; and

(b) facilitating retail competition by reducing the transaction costs faced by retailers competing for electricity consumers across multiple distribution networks. In particular, a model approach to a distribution pricing methodology should benefit consumers on smaller distribution networks where retailers do not have the same economies of scale in systems and processes to accommodate varying approaches to distribution pricing[8].

2.2 The Commission's initial view on a model approach

2.2.1 The First Consultation Paper set out a voluntary model approach to a distribution pricing methodology, which in the Commission's view furthered the Commission's principal objectives under the Electricity Act 1992 (**Act**) and gave effect to the objective in paragraph 100 of the 2009 Government Policy Statement on Electricity Governance (**GPS**), which states that "*the Commission should develop, in consultation with interested parties, principles or model approaches to distribution pricing and monitor their uptake*".

2.2.2 Consistent with the outcome of the distribution pricing process facilitated by the Electricity Networks Association in 2004 - 2005, which culminated in the early

[7] See the First Consultation Paper [page 11].

[8] Ibid at paragraph 2.5.2.

2005 report setting out the PAWG model approach (the **PAWG report**), the Commission noted in the First Consultation Paper its view that a single model for distribution pricing, with flexibility in its implementation, would be the most efficient means of furthering the objectives described above.

2.2.3 The proposed model approach set out in the First Consultation Paper was based on the PAWG model approach, which the Commission understood received widespread acceptance from distributors and retailers at the time of its development and publication.

2.3 PAWG model approach

2.3.1 In the Commission's view, adopting the PAWG model approach would be consistent with seeking to further the retail competition objective described above. By seeking to ensure that distributors' pricing methodologies are developed in largely the same manner, the PAWG model approach could lower the transaction costs faced by retailers competing across multiple networks.

2.3.2 However, there are potential problems with the PAWG model approach as its prescriptive nature raises issues around intervention in the context of price setting under Part 4 of the Commerce Act. The Commerce Commission has noted concerns over pricing methodologies that are set in an overly prescriptive manner [9] including:

(a) the information asymmetry between distributors and the regulator in determining the level of prescription (or the possibility that neither party has access to relevant information)[10];

(b) the lack of flexibility on the part of distributors to respond to changes in market conditions and consumers' demand[11]; and

(c) the compliance costs associated with greater prescription[12].

2.3.3 These problems mean that adopting a model approach based on the PAWG model approach could have lower economic efficiency benefits over time than

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9 See the Commerce Commission's *Input Methodologies Discussion Paper*, 19 June 2009 at paragraph 9.52 [The Commerce Commission's views would exclude any benefits associated with facilitating retail competition.] The *Input Methodologies Discussion Paper* is available at http://www.comcom.govt.nz//IndustryRegulation/Part4/ContentFiles/Documents/IM-final.pdf.

10 Ibid at paragraphs 9.21 and 9.52. In the First Consultation Paper the Commission sought to address this issue by providing for distributors to vary from the model approach to a distribution pricing methodology if they had good reason.

11 Ibid at paragraph 9.47.

12 See Commerce Commission, *Authorisation for the Control of Supply of Natural Gas Distribution Services by Powerco Ltd and Vector Ltd, Draft Decisions Paper*, 4 October 2007, p 302; and Commerce Commission, *Input Methodologies Discussion Paper*, 19 June 2009, paragraph 9.22..

adopting a methodology whereby the regulator provides guidance in a less prescriptive manner.

2.4 The Commission's revised view on a model approach

2.4.1 Submissions on the First Consultation Paper reflected widespread support from distributors in particular and, to a slightly lesser extent, retailers for the Commerce Commission's preliminary view, in the context of Part 4 of the Commerce Act, that a principles-based approach to pricing methodologies is appropriate for distributors.

2.4.2 Noting the lack of industry support for a model approach consisting of a prescriptive methodology, coupled with the relatively broad industry support for a principles-based approach, the Commission revisited the intent behind a model approach to a distribution pricing methodology.

2.4.3 The Commission agreed with submitters that, where appropriate, consistency should be sought between itself and the Commerce Commission in respect of the treatment of distribution pricing. Accordingly, the Commission developed a principles-based approach to a distribution pricing methodology and, where practicable, sought to align it with the approach adopted by the Commerce Commission in the Gas Authorisation for Powerco and Vector[13], taking into consideration the Commerce Commission's preliminary views on pricing methodologies, as set out in its 19 June 2009 Input Methodologies Discussion Paper[14].

2.4.4 The Commission noted that the focus of the Commerce Commission on distribution pricing has been in the context of Part 4 of the Commerce Act and has not been related to enhancing retail competition. The Commerce Commission has summarised its current preliminary view, in the context of Part 4 of the Commerce Act, on distribution pricing as follows:

(a) "*a principles based approach to pricing methodologies is appropriate for [distributors that it regulates]; and*

(b) *the principles should be based upon the output of the Electricity Commission's Distribution Pricing Project, to the extent that:*

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[13] See Commerce Commission, *Authorisation for the Control of Supply of Natural Gas Distribution Services by Powerco Ltd and Vector Ltd, Decision Paper*, 30 October 2008, available at http://www.comcom.govt.nz//IndustryRegulation/Gas/CommissionReportsandDocuments/ContentFiles/Documents/[PUBLIC]%20Gas%20Authorisation%20-%20Decisions%20Paper%20-%2031%20October%202008.pdf

[14] See the Commerce Commission, *Input Methodologies Discussion Paper*, 19 June 2009 at Chapter 11.9, paragraphs 11.107-11.129.

(i) *such principles, guidelines and/or model distribution pricing methodology or approaches are consistent with the relevant provisions of the Commerce Act; and*

(ii) *are available in sufficient time for the [Commerce] Commission to take those decisions into account within the statutory timeframes for determining input methodologies*"[15].

2.4.5 Noting its broader mandate in respect of distribution pricing, the Commission reformulated the Commerce Commission's principles set out in the Gas Authorisation into pricing principles, and incorporated:

(a) additional objectives set out in the Act, namely, ensuring electricity is delivered to all classes of consumers in a fair, reliable and environmentally sustainable manner and the promotion and facilitation of the efficient use of electricity[16];

(b) relevant objectives in the TPM[17] and the Distributed Generation Regulations[18]; and

(c) feedback from submissions on the First Consultation Paper and the June 17 workshop.

2.4.6 The Commission prepared draft methodological requirements based on those set out in the Gas Authorisation for Powerco and Vector, and updated these where appropriate to reflect additional requirements specific to the Commission's objectives and specific outcomes.

2.4.7 The Commission was attracted to this approach of specifying an intermediate level of detail in a model approach to a distribution pricing methodology for the following reasons:

(a) The economic efficiency benefits of a pricing principles approach may be greater than under a more prescriptive methodology. In fact, the benefits of a more prescriptive approach may be close to zero where there is no ability to prevent retailers from rebundling distribution price structures in a manner that weakens their economic signalling effect;

(b) Insofar as efficient pricing is concerned, it aligns with the approach that the Commerce Commission has to date adopted for the gas sector, and which the Commerce Commission has provisionally indicated as being

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[15] See Commerce Commission, *Input Methodologies Discussion Paper*, 19 June 2009, paragraph 11.121.

[16] See ss 172N (1) (a) and (b) of the Electricity Act 1992.

[17] The TPM is outlined in Schedule F5 (Transpower's transmission pricing methodology), Section IV, Part F, of the Rules**.**

[18] Refer to the Electricity Governance (Connection of Distributed Generation) Regulations 2007.

appropriate under the input methodologies regime, at least for the gas sector[19]; and

(c) The pricing principles and methodological requirements approach could be adapted to encompass the extended mandate of the Commission.

2.4.8 The Commission set out in the Second Consultation Paper its preliminary view in respect of adopting a principles-based approach to a distribution pricing methodology, coupled with guidelines (methodological requirements) to assist stakeholders with interpreting and implementing the pricing principles. As with the First Consultation Paper, this paper received substantial feedback from submitters. A summary of the submissions received can be found in Appendices 1, 2 and 3.

19 See the Commerce Commission, *Input Methodologies Discussion Paper*, 19 June 2009, under the section entitled “Pricing Methodologies – Approach and level of detail in pricing principles 449.

3. Pricing principles

3.1 A principles-based approach

3.1.1 Significant feedback was received from submitters on the draft pricing principles, with all submissions being supportive, or at least generally supportive, of a principles-based approach. Appendix 1 outlines comments on specific principles and the suggested wording that they contain.

3.1.2 The Commission has noted the feedback from submitters and has adopted suggestions relating to clarifying and simplifying the pricing principles.

3.2 Pricing principles

3.2.1 The table below sets out the Commission's final draft of the proposed pricing principles. The underlined text shows changes to the draft pricing principles proposed in the Second Consultation Paper.

Principle	Comments on changes
(a) Prices are to signal the economic costs of service provision, by: (i) being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), except where subsidies arise <u>from compliance with</u> legislation <u>and/or other regulations</u>; (ii) having regard, to the extent practicable, to the level of available service capacity; and (iii) signalling, to the extent practicable, the impact of additional usage on future investment costs.	Several submitters pointed out that legislation takes precedence over principles so there is no need to include the exception. Others felt there was merit in clarifying the potential for cross subsidies to occur due to legislation or regulations such as the Low Fixed Charge Regulations. The Commission has decided that the revised version provides greater clarity and does not diminish the intent of the principle.
(b) Where prices based on 'efficient' incremental costs would under-recover allowed revenues, the shortfall should	The Commission removed the reference to Ramsey pricing to reduce the potential for stakeholders to believe that they

Principle	Comments on changes
be made up by setting prices in a manner that has regard to consumers' demand responsiveness ~~(i.e of Ramsey pricing) and/or the quality of service that they receive~~, to the extent practicable.	must implement Ramsey pricing per se, which is difficult to do in practice. The quality of service responsiveness can be covered in the amended principle (c).
(c) Provided that prices satisfy (a) above, prices should be responsive to the requirements and circumstances of ~~users~~ stakeholders in order to: (i) discourage uneconomic bypass; (ii) allow for negotiation to better reflect the economic value of services and enable stakeholders to make price/quality trade-offs or non-standard arrangements for services; and (iii) where network economics warrant, encourage investment in transmission distribution alternatives (e.g. distributed generation or demand response) and technology innovation.	The generic term "stakeholder" has been introduced to cover all affected parties. Sub-clause (ii) has been expanded. Sub-clause (iii) has been included to replace previous principle (f). It is slightly amended from the original Commerce Commission clause by the addition of "or demand response" to reflect the fact that investment in demand response can lead to efficient deferral of distribution investment. Transmission has been added as some transmission assets have similar characteristic to distribution assets and are fully funded by distributors.
(d) Development of prices should be transparent, promote price stability and certainty for stakeholders, and ~~lead to prices that are able to be understood by users~~ changes to prices should have regard to the impact on stakeholders.	The generic term stakeholder has been used. The use of "transparent" has been retained to reinforce the concept behind the Information Disclosure Regulations that apply to the pricing methodologies. Transparency should lead to understandable pricing so that

Principle	Comments on changes
	condition has been removed and replaced with the need for consideration of the impact of changes in prices on stakeholders such as retailers and consumers.
(e) ~~Pricing structures should not place undue transaction costs on retailers and consumers,~~ Development of prices should have regard to the impact of transaction costs on retailers and should be ~~competitively neutral and~~ economically equivalent across retailers.	Based on suggestions from submitters, the original wording has been replaced by a clearer expression of the intent of the principle.
~~(f)~~ ~~Prices and pricing structures should promote efficient usage of electricity and encourage investment in distributed generation (including renewable generation), distribution alternatives and technology innovation.~~	As suggested by a number of submitters, this principle has been incorporated into principle (c).

Q1. Do you agree with the wording of these proposed principles? Please give reasons where you do not agree.

3.2.2 Where conflicts arise in applying the pricing principles, they should be resolved with the objective of best satisfying the Commission's principal objectives under section 172N of the Act.

3.3 Terminology

3.3.1 Various submitters on the Second Consultation Paper provided suggestions on how to designate those parties affected by distribution pricing methodologies.

The Commission used "consumer", as defined in the Rules[20], to refer to those parties who are supplied with electricity and "user" to describe those who pay (or could be paid by) the distributor for distribution services. These users could include retailers, distributed generators, demand aggregators and direct purchasers that could contract directly with distributors. All of these parties have a stake in the development of the prices for distribution services.

3.3.2 One alternative could be to use the term "customer" for those who contract directly but this may cause confusion, as the definition of customer in the Rules is "a person who purchases or has agreed to purchase, electricity from a retailer at a specific ICP", which would exclude retailers and also end users who purchase electricity directly from the clearing manager. Another suggestion was to add "connected parties" as this would include distributed generators.

3.3.3 Some submitters suggested using "stakeholder" as a generic term to cover all affected parties. The Commission has adopted that approach except where a specific stakeholder category should be identified separately.

[20] Part A of the Rules defines "consumer" as "any person who is supplied electricity for consumption and includes a distributor, retailer or generator where the distributor, retailer or generator is supplied with electricity for its own consumption".

4. Information disclosure guidelines

4.1.1 Most submissions received on the Second Consultation Paper expressed concern about the requirement for distributors to comply with the methodological requirements. The Commission agrees that being prescriptive about pricing methodologies is not required and to clarify its intention, proposes to establish information disclosure guidelines in the place of the methodological requirements it had previously proposed.

4.1.2 The information disclosure guidelines are intended to assist distributors with the preparation of the information disclosure on their distribution pricing methodology and to assist an independent expert reviewer to assess distributors' compliance with the pricing principles. Use of the information disclosure guidelines by distributors in the 2011-2012 financial reporting year and beyond will result in an easier comparison across distributors of compliance with the pricing principles. .

4.1.3 The information disclosure guidelines are designed to reflect, as closely as is appropriate, the Commerce Commission's preliminary view on the direction of the pricing methodology information disclosure requirements and what the minimum disclosure should include[21].

4.1.4 The Commission's view is that the level of reporting on a distributor's distribution pricing methodology should be consistent with the obligations on distributors under the relevant information disclosure requirements contained in subpart 4 of Part 4 of the Commerce Act or subsequent developments[22] (i.e. a distributor would submit the same information to the Commission as it would submit to the Commerce Commission, but include a section on how the distribution pricing methodology has met or had regard to the pricing principles).

4.1.5 Currently, the distribution pricing information disclosure requirements under the Commerce Act are as follows:

> ***22. Disclosure of pricing methodologies—***
>
> *Every disclosing entity must publicly disclose,-*

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[21] See the Commerce Commission's preliminary view of what the minimum disclosure should include in the commerce Commission's *Information Disclosure Discussion Paper*, published 29 July 2009, at paragraph 484.

[22] These are provided for in subpart 4 of Part 4 of the Commerce Act (which came into force on 14 October 2008) and will be set out in a section 52P determination made by the Commerce Commission. The Commerce Commission is required to make a determination specifying how information disclosure regulation applies to each EDB and Transpower "as soon as practicable" after 1 April 2009. The Electricity Distribution (Information Disclosure) Requirements 2008 and the Electricity Information Disclosure Requirements 2004 continue to apply until the determination takes effect.

(a) At the beginning of each financial year, the methodology used at the beginning of that financial year to determine the line charges payable or to be payable; and

(b) Any change in the methodology or adoption of a different methodology, within 1 month of the change or the different methodology taking effect.

23. Contents of pricing methodology disclosures—

Every disclosure under requirement 22 must—

(a) Describe the methodology used to calculate the prices charged or to be charged; and

(b) Include the key components of the revenue required to cover costs and profits of the disclosing entity's line business activities, including cost of capital and transmission charges, which must include the numerical value of each of the components; and

(c) State the consumer groups used to calculate the prices charged or to be charged, including—

(i) The rationale for the consumer grouping; and

(ii) The method by which the disclosing entity determines which group consumers are in; and

(iii) For each of these consumer groups, the statistics relating to that group which were used in the methodology; and

(d) Describe the method by which the disclosing entity allocated the components of the revenue required to cover the costs of its line business activities amongst consumer groups, which must include the numerical values of the different components allocated to each consumer group and the rationale for allocating it in this manner; and

(e) Describe the method by which the disclosing entity determined the proportion of its charges which are fixed and the proportion which are variable, and the rationale for determining the proportions in this manner

4.1.6 For the 1 April 2010 - 31 March 2011 financial year, the Commission proposes that distributors report against the pricing principles prior to 1 April 2010, using the information disclosure requirements ***currently*** provided for in the Commerce Act. However, distributors should use the information disclosure guidelines published by the Commission to report against the pricing principles for the 1 April 2011 - 31 March 2012 financial year (see section 5). Provided that the information sought by the Commission is the same as the information submitted by distributors to the Commerce Commission with respect to the information disclosure, in an effort to avoid duplication, the Commission would get a copy of the information from the distributor's website. If further information is required the Commission would seek the information directly from distributors.

4.1.7 After the 2011 - 2012 financial year, if no changes to a distributor's pricing methodology occur, the distributor's information disclosure will be unchanged (unless the distributor wished to change it by providing additional information). Changes to price levels need not be reported.

4.1.8 The Commission will work with the Commerce Commission to ensure consistency between the information disclosure requirements of the two entities in respect of distribution pricing. The Commission notes that this is likely to be an iterative process, and that there may be therefore some further refinements to the proposed information disclosure guidelines set out in this consultation paper.

4.1.9 Based on submissions received on the Second Consultation Paper and the Commerce Commission's preliminary view of what minimum disclosure should include[23], the Commission's proposed information disclosure guidelines are now as follows:

Information Disclosure Guidelines		
(a)	Prices should be based on a well-defined, clearly explained and published methodology, with any revisions notified and clearly marked.	
(b)	The pricing methodology disclosed should include sufficient information on the following for an independent expert to assess compliance with the pricing principles, including:	
	(i)	how the methodology links to the pricing principles and any non-compliance;
	(ii)	the rationale for consumer groupings and the method for determining the allocation of consumers to the consumer groupings;
	(iii)	quantification of key components of costs and revenues;
	(iv)	an explanation of the cost allocation methodology and the rationale for the allocation to each consumer grouping; and
	(v)	pricing arrangements that will be used to share the value of any deferral of investment in distribution and transmission assets with the investors in alternatives such as distributed generation or load management, where this is practicable.
(c)	The pricing methodology should:	
	(i)	employ industry standard tariff formats and nomenclature, where possible; and

23 See the Commerce Commission's *Information disclosure discussion paper,* 29 July 2009, chapter 9 (in particular paragraph 484).

(ii) where a change to the existing pricing methodology is proposed, describe the details of the impact on consumer classes and the transition arrangements proposed to mitigate the effect of redistribution of costs and "rate shock".

Q2. Do you support the concept of information disclosure guidelines rather than the more prescriptive methodological requirements?

Q3. Do you agree with the wording of these proposed information disclosure guidelines? Please give reasons where you do not agree.

5. Pricing methodology review

5.1.1 Several submitters suggested that the Commission undertake a review of pricing methodologies and some distributors suggested that the Commission adopt a compliance review process similar to the process used by the Commerce Commission in assessing the Asset Management Plans (AMP) produced annually by distributors.

5.1.2 The Commission believes that the suggestion has merit and that an independent review should be conducted periodically to assess the compliance of each distributor's distribution pricing methodology with the pricing principles. Each distributor would have an opportunity to comment on the review of its own distribution pricing methodology. A summary of the reviews would be published by the Commission to provide an indication of compliance trends, problem areas, examples of best practice and advice to the Commission on improvements to the information disclosure guidelines.

5.1.3 Due to the comparatively stable nature of distribution pricing structures, an annual review of all distribution pricing methodologies would probably not be justified. However, distributors would still be required to publish their distribution pricing methodologies on an annual basis and provide details of changes of, or to, their methodologies within 1 month of the change, as required by the information disclosure requirements under Part 4 of the Commerce Act.

5.1.4 Where a distributor amended its methodology, the Commission would have the discretion to initiate a review of that methodology.

Proposed process and timetable for reporting

5.1.5 The Commission proposes that distributors first use the information disclosure guidelines to report against the pricing principles in March 2011 (for the 1 April 2011 – 31 March 2012 financial year).

5.1.6 For the 1 April 2010 - 31 March 2011 financial year, the Commission proposes that distributors report against the pricing principles, using the current Commerce Act's information disclosure requirements.

5.1.7 This first review will be a learning exercise. It will be a benchmarking exercise to assess the need for changes and/or enhancements to the information disclosure guidelines, as well as to develop assessment criteria for future reviews. The Commission anticipates dialogue with, and input from, the industry during this development.

5.1.8 By 31 July 2010, each distributor will receive an independent expert's draft report on the compliance of the distributor's distribution pricing methodology against the pricing principles, and should respond to the Commission on the findings of this report by 31 August 2010. The Commission will publish a summary of the independent reviews by 30 September 2010, with a score for compliance with the pricing principles.

5.1.9 The Commission proposes to repeat this process in 2011 (including the independent review of pricing methodologies), but with distributors reporting against the pricing principles using the information disclosure guidelines.

5.1.10 Subsequent reviews by an independent expert will occur only when a distributor amends its pricing methodology or has not amended a materially non-compliant pricing methodology.

5.1.11 Provided that the information sought by the Commission is the same as the information submitted by distributors to the Commerce Commission with respect to the information disclosure, in an effort to avoid duplication, the Commission would get a copy of the information from the distributor's website. If further information is required the Commission would seek the information directly from distributors.

5.1.12 The intention of these reviews of distributors' distribution pricing methodologies is to improve the efficiency of distribution pricing, facilitate retail competition and enhance the quality of information disclosure.

5.1.13 If at any time the Commission considered that a distributor had not provided sufficient information or was materially non-compliant with the pricing principles, the Commission would seek to persuade the distributor to comply.

5.1.14 If there was no improvement in a distributor's compliance with the pricing principles, the Commission would consider whether targeted regulation was appropriate. It is the Commission's expectation that distributors will voluntarily comply given that the Commission has adopted many of the significant suggestions put forward by distributors on its approach to distribution pricing. As noted in the Second Consultation Paper:

> "The Commission considers that this is an opportunity for distributors to show that a light-handed approach will result in improvements. Improvements to the way distributors set their prices therefore need to be demonstrated in a transparent manner so that the Commission and interested parties can confirm that distributors have set or are in the process of setting their prices in accordance with the pricing principles."[24]

[24] See the Second Consultation paper at Paragraph 5.1.2.

Q4.	**Do you agree with the proposed process and timetable for reporting? Please give reasons where you do not agree.**

6. Process to complete the distribution pricing methodology approach

6.1.1 The timetable for completing the Commission's approach to a distribution pricing methodology is set out in the following table.

Table 2 Process to complete the distribution pricing methodology approach

Date	Event
December 2009	Industry working group reports back on administrative issues that can be bilaterally addressed by retailers and distributors
1 December 2009	Final consultation paper published on pricing principles and information disclosure guidelines (Third Consultation Paper)
22 December 2009	Submissions due on Third Consultation Paper
February 2010	Publication of final pricing principles and information disclosure guidelines

Appendices

Appendix 1 Submissions regarding the proposed principles (The revised draft principles based on submissions are contained in paragraph 3.2.1)

1.1 Submissions from distributors on proposed principles[25]

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
(a) Prices are to signal the economic costs of service provision, by:						
(i) being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), <u>except where subsidies arise from legislation;</u>	Remove added words. Legislation will and must take precedence over any and all of these principles, so the addition is redundant. **Eastland Energy** notes that Electricity services into remote areas are generally	Recommend deleting the added words, as legislation takes precedence over the Commission's regulation.	Change to read as follows to clarify that compliance obligations may distort economic signals: *being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), except where*	Add '*or other regulations'* after legislation. Mention of legislation is not strictly necessary, as legislation must always take precedence over principles. However, useful for lay readers to be reminded that there are considerations other	Add to end of sentence so it reads: *'except where subsidies arise from compliance with legislation or other regulations.'* **Wellington Electricity** supports this principle, but suggests in	Agree with Unison and Vector. The revised version with reference to regulation provides greater clarity and does not diminish the intent of the principle.

[25] For the purpose of keeping the summary table as readable as possible the Commission has summarised the most comprehensive submissions and included other comments where appropriate.

Draft Principle	**Orion**	**Powerco**	**PWC**	**Unison**	**Vector**	**Commission Response**
	at a level that does not signal the true costs of supply due to the relation of length of line and consumers on that line. Agree that excessive subsidisation is not desirable, but for remote consumers for example, consider a reasonable of cross subsidisation as acceptable.		*subsidies arise from <u>compliance with</u> legislation <u>or other regulations</u>;*	than the just the pricing principles that must be taken into account.	addition to legislation it also refers to the GPS.	
(ii) signalling, to the extent practicable, the impact of additional usage on future investment costs.						
(b) Where prices based on 'efficient' incremental costs would under-	Specific mention of Ramsey pricing is unnecessary. Commerce	Recommend deleting the added words – economic concepts have been confused.	The proposed insert is not necessary, is inconsistent with a	Amend as follows: *'Where prices based on 'efficient' incremental costs*	Amend the bracketed sentence to read: *'(i.e. qualitatively*	The Commission wished to identify that the principle is related to applying

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
recover allowed revenues, the shortfall should be made up by setting prices in a manner that has regard to consumers' demand responsiveness <u>(i.e. Ramsey pricing) and/or the quality of service that they receive</u>, to the extent practicable.	Commission has recognised that while Ramsey pricing may provide qualitative guidance there are significant practical difficulties in applying Ramsey pricing in a quantitative manner. Quality of service is logically misplaced in this principle which is about non-distortion of principle a) (iii) in the recovery of residual revenue. Recommend removing the added words. **Wellington Electricity** made similar points about not supporting the use of Ramsey	Price quality trade off and demand responsiveness are different economic concepts. The Commission may be referring to using the price quality trade-off as a proxy for demand responsiveness.	'principle' approach, can be included in supplementary guidance, and as set out in the Commerce Commission's Input Methodology paper, there are practical limitations to Ramsey Pricing which need to be considered. The introduction of quality of service is confusing (better addressed in c).	*would under-recover allowed revenues, the shortfall should be made up by setting prices in a manner that has regard to consumers' demand responsiveness (i.e. <u>is qualitatively consistent with</u> Ramsey pricing) ~~and/or the quality of service that they receive~~, to the extent practicable.'* Introduction of the concept of a price/quality trade-off is confusing when the principle is looking at demand elasticities. 'Efficient incremental costs' should take account of the level of quality delivered. Well recognised that	*consistent with the economic principle of Ramsey Pricing)'* The Commerce Commission, recognising the difficulties with quantitatively applying Ramsey pricing provided guidance that this principle should be considered as qualitative guidance. The proposed addition of quality of service extends the principle beyond the fundamental economics behind Ramsey pricing and is already captured by principle (c)(ii). Recommends the	the principle behind Ramsey pricing, but has adopted the suggested Vector wording to reduce the potential for stakeholders to believe that they must implement Ramsey pricing per se, which is difficult to do in practice. The quality of service responsiveness can be covered in the amended principle (c).

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
	Pricing, and drew attention to the Commerce Commission's Discussion Paper on Input Methodologies. Also made similar comments about reference to quality of service.			Ramsey Pricing is difficult to apply in practice, particularly because it is very difficult to accurately measure demand elasticities (hence the addition).	statement be removed.	
(c) Provided that prices satisfy (a) above, prices should be responsive to the requirements and circumstances of users in order to:						
(i) discourage uneconomic bypass; and						
(ii) allow for <u>price/quality tradeoffs.</u>	Do not support the proposed change, 'price/quality trade-off' needs to be	Delete this principle. Include the following	Do not support this change as it is not defined and may mean different	Delete this sub-clause and add in: *'(ii) allow negotiation*	Amend as follows: *'Allow negotiation to better reflect the*	Agree. Clause (ii) expanded. A new sub-clause (iii) has been included to

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
	defined. The alternative wording in the gas principles in relation to allowing negotiation to better reflect the economic value of specific services is an appropriate principle. Not clear how this could be applied in a meaningful way as a general pricing principle for an integrated electricity distribution network. More appropriate to have a principle that encourages investment in distribution alternatives when network economics warrants it.	instead: *'allow negotiation to better reflect the economic value of specific services.'* No rationale for inclusion of this, so difficult to comment – prefers original wording as it is broader and specifically mentions consultation with the customer.	things to different EDBs or consumers. 'Economic value of specific services' is more valid as this links the service requirement to its value. Concept of negotiation also useful as it reflects the reality of setting service standards for those consumers which are able to consider alternatives.	*to better reflect the economic value of specific services; and* *(iii) where network economics warrant; encourage investment in distribution alternatives (e.g. distributed generation) and technology innovation.'* Good business practice to have consultation with customers, and to cater for their specific business requirements.	*economic value of specific services, including price/quality tradeoffs.'* There may be other less tangible elements than the price/quality trade-off that need to be considered in the development of non-standard contracts (e.g. the desire for more or less fixed pricing to have regard to risk). The original text captured these elements and also placed greater emphasis on consultation with individual customers through negotiation. It should therefore be	replace principle (f). It is slightly amended from the original Commerce Commission clause by the addition of "or demand response" to reflect the fact that investment in demand response can lead to efficient deferral of distribution investment in network enhancement.

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
	Wellington Electricity made similar comments about this already being required under the Commerce Commission's Price-Quality regulations, and the gas authorisation principle being more appropriate.				retained, but acknowledge that negotiation may involve price quality tradeoffs.	
(d) Development of prices should <u>be transparent</u>, promote price stability and certainty for <u>consumers</u>, and <u>lead to prices that are able to be understood by users.</u>	Transparency should not be included as a principle; transparency is the underlying rationale of a disclosure regime. The rest of this proposed principle is unclear. What is meant by stability and certainty? No time of use pricing?	Delete this principle, as transparency is covered by information disclosure so there is no need for it to be included. Include the following instead: *'Consultation with retailers should be undertaken before material changes in price structure are undertaken. Changes to prices should have*	No need for transparency requirement as this is what disclosures are attempting to achieve. Remainder is also not required, as it is unreasonable to expect stability and certainty, when innovation is important, and price signals are an	Delete this clause and replace with: *'Development of prices should be transparent, promote price stability and certainty for stakeholders, and changes to prices should have regard to the likely impact on customers.'* Consider that	Amend to read as follows: *'Development of prices should be transparent, promote price stability and certainty for stakeholders, and changes to prices should have regard to the impact on customers.'*	The generic term "stakeholder" has been introduced to cover all affected parties. The use of "transparent" has been retained to reinforce the concept behind the Information Disclosure requirements that apply to the pricing

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
	No changes in structure of pricing? No dynamic pricing? Who are users? Recommend this wording: *'(d) Consultation with retailers should be undertaken before material changes in price structure are undertaken. Changes to prices should have regard to the likely impact on consumers.'* **WEL Networks** also note that retailers can re-bundle distributor tariffs which could stifle or negate the intentions behind the price drivers designed by the	*regard to the likely impact on consumers.'* With regards to replacing customer with consumer: the main difference is that a consumer includes people using electricity at an ICP, but not purchasing electricity from a retailer. As the principle refers to pricing, recommends it refers to the purchaser of electricity, rather than all users of electricity. The Commission has also removed "and changes should have regard to the impact on customers". Assumes this is because "promote price stability" is already mentioned. Prefers the Authorisation approach as "impact on	important mechanism to influence behaviour. 'Users' not defined. **Wellington Electricity** made similar comments about this principle and suggested it be amended to read: *'Development of prices should be transparent and regard should be given to the impact changes to prices have on consumers.'* In addition noted that there is an inherent conflict between achieving other principles such as being subsidy free and with the principles being	transparency will be demonstrated through compliance with the Information Disclosure regime. To clarify recommend "consumers" is changed to "stakeholder", to recognise that price stability and certainty is important to retailers as well as end-consumers. Recommend the removal of "and lead to prices that are able to be understood by users" on the basis that this would be a subjective test, depending on the level of consumer engagement. With the roll out of advanced metering infrastructure and the	Assume the use of "consumer" over "customer" implies that distributors should ensure price stability and certainty for end consumer, not retailers. However, price stability and certainty will also be important for retailers, especially in minimising any transaction costs resulting from material changes in price structures, which are inevitable when shifting to a new methodology. Suggests substituting "stakeholders" for "consumers". With regards 'able	methodologies. Transparency should lead to understandable pricing so that condition has been removed and replaced with the need for consideration of the impact of changes in prices on stakeholders such as retailers and consumers.

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
	distributor.	customers" has a broader meaning and better serves customers' requirements. The Commission has added that the development of prices should "lead to prices that are able to be understood by users". It is unclear who "users" are. Retailers are the predominant users of electricity prices, and this principle could relate to retailer consultation. Not supportive of this principle if "users" referred to electricity consumers, as most electricity consumers have little interest in distribution price structures.	easily understood. The principles must allow EDBs to manage such trade-offs.	view to have distribution charges being transparent to customers, EDBs strategies are moving towards educating customers on pricing. This is important as over simplified pricing will be at the expense of other efficiencies which will have a greater benefit to the end customer. Do not support the deletion of "and changes to prices should have regard to the impact on customers". This is an important aspect of flexibility that needs to be retained, and allows EDB to apply a transitional approach to mitigate price shocks.	to be understood by users': customer understanding of pricing is a subjective test; and the phrase, as it currently reads, implies that distributors should "dumb-down" pricing to facilitate customer understanding. This may be at the expense of other pricing principles and more general efficiency considerations. A better strategy would be to educate customers about pricing. Does not support the deletion of the phase "and	

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
					changes to prices should have regard to the impact on customers". Having the flexibility in pricing to account for the impact on customers is extremely important.	
(e) <u>Pricing structures should not place undue transaction costs on retailers and consumers, and should be competitively neutral across retailers.</u>	The term 'undue' is inherently uncertain and subjective. 'Economically equivalent' treatment of retailers is the appropriate definition for economically-based pricing principles rather than 'competitively neutral'. Recommend this wording: *(e) Changes to prices*	Delete this principle. Include the following instead: *Changes to prices should have regard to the likely cost impact on retailers.* The word 'undue' sets a level of costs, which must somehow be measured. 'Have regard to' suggests that it should be given genuine attention and consideration of the	'Undue' is ambiguous. More appropriate to refer to economically equivalent in the context of the economic pricing principles than competitively neutral. **Wellington Electricity** made similar comments noting that 'Undue transaction costs'	Replace with: *'Development of prices should, to the extent practicable, have regard to the transaction costs that impact various stakeholders.'* Have seen no material evidence that transaction/ administrative costs incurred by retailers due to EDB pricing methodologies are exorbitantly high	Replace with: *'Development of prices should, to the extent practicable, have regard to the transaction costs that impact various stakeholders.'* Rewrite to align more closely with language of other principles and recognise that transaction costs may also be	Based on suggestions from submitters, the original wording has been replaced by a clearer expression of the intent of the principle.

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
	should have regard to the likely cost impact on retailers. Retailers should be treated in an economically equivalent manner.	issue.	was not relevant in relation to economic principles. Suggested it should be amended to read: *'Changes to prices should have regard to the likely cost impact on retailers. Retailers should be treated in an economically equivalent manner.'*	resulting in barriers to retail competition. Important when changing prices to have regard to the cost impact on retailers – demonstrated by the consultation process that occurs each year. The use of "have regard to", requires EDBs to demonstrate that they have considered the cost impact on retailers. Neither the requirement that prices "should be competitively neutral across retailers" nor the requirement that retailers "should be treated in an economically	incurred by distributors. The equitable treatment of retailers is a contractual issue and isn't required as a pricing principle. It is unclear how distributors would determine competitive neutrality, beyond establishing that prices are available to all retailers.	

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
				equivalent manner" are a necessary part of the pricing principles, as they are already required by section 36 of the Commerce Act 1986. **WEL Networks** made similar comments about retailer transaction costs suggesting that if some retailers don't want to transparently pass through the distributor costs other retailers may want to, and therefore are welcome to, add complexity so they can offer a cheaper product to their customers.		
(f) <u>Prices and pricing structures should promote efficient</u>	The economics of a network supporting distributed generation is	Delete this principle – the ideas of distributed generation and technology innovation	These objectives are better met using other forms of regulation and	Fits better with principle (c). Pricing should not specifically	Remove this principle. It does not seem	As suggested by a number of submitters, this principle has been

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
usage of electricity and encourage investment in distributed generation (including renewable generation), distribution alternatives and technology innovation.	extremely site-specific. This is not a principle but an outcome that is conditional upon network economics at a particular site. 'Electricity' is much more than energy (kilowatt-hours). It includes the delivery system (grid, networks) and all related services (fault calls etc). Note that the Electricity Governance (Connection of Distributed Generation) Regulations 2007 include a specific set of pricing principles. Recommend that this clause be	should be removed or moved to principle c. **ENA** also agree that this is partly provided for under principle (a), while the Commerce Commission is tasked (s54Q) with developing specific regulatory mechanisms to incentivise and avoid disincentives to energy efficiency, demand side management and load control. In addition, other regulations (such as the Distributed Generation Regulations) already impose legislative incentives on distributors in this respect. Pricing methodologies are a very blunt tool for this purpose and do not support the inclusion of	place undue limitations on distributors' ability to recover their costs. Distributed Generation is adequately covered by the Distributed Generation Regulations. Distribution alternatives and technology innovation are not objectives which are readily achieved through pricing methodologies. Innovation is best dealt with through the price quality path and is being explicitly	encourage investment in distributed or renewable generation, or in distribution alternatives, unless it is efficient to do so. A more appropriate principle is that prices and pricing structures should promote efficient use of delivered electricity, including existing electricity infrastructure, distributed and renewable generation, and distribution alternatives.	necessary to develop a separate pricing principle at this stage on energy efficiency, demand side management, distribution alternatives or innovative technology. The Commission should at least wait until the Commerce Commission has deliberated on regulatory incentives mechanisms that promote these initiatives so that any principle is more targeted. At a minimum, distribution pricing should only be required to	incorporated into principle (c).

Draft Principle	Orion	Powerco	PWC	Unison	Vector	Commission Response
	deleted as fits better under principle c.	this principle.	considered by the Commerce Commission. **Wellington Electricity** made similar comments with regards to this principle and **WEL Networks** suggested that emphasis should be placed on <u>when</u> efficient usage is preferred and that pricing should signal <u>economic</u> investment in alternatives to reduce loads during peak periods.		promote efficient use of electricity network services, not electricity, since this is the domain of retailers. Additionally, distributors should not have to encourage distributed generation, or technological innovation, rather pricing structures should be neutral to such matters, and promote allocatively efficient use of existing sunk networks.	

1.2 Submissions from retailers on proposed principles[26]

Draft Principle	Contact	Meridian	TrustPower	Commission Response
(a) Prices are to signal the economic costs of service provision, by:				
(i) being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), <u>except where subsidies arise from legislation;</u>	Use of the words "subsidy free" suggests purity in pricing that incentivises complexity. Some distributors may use this principle to justify their pricing approaches, when a more pragmatic approach accepting a level of cross subsidy will still provide appropriate network investment signals. Network pricing signals are passed through by retailers unless the pricing structure is unnecessarily complex or unbillable given widely deployed metering, in which	Queries whether the lines companies should be required to be transparent about where cross subsidies lie if they are material. There is still an expectation in the GPS that changes in rural line charges are in line with changes in urban line charges.	Replace 'being subsidy free' with the following less prescriptive phrase: *'reflecting the true cost of supply'*	The Commission agrees that this principle needs clarification. The Commission has decided that the revised version provides greater clarity and does not diminish the intent of the principle. If cross subsidies exist they should be disclosed through the information disclosure.

[26] For the purpose of keeping the summary table as readable as possible the Commission has summarised the most comprehensive submissions and included other comments where appropriate.

Draft Principle	Contact	Meridian	TrustPower	Commission Response
	case the retailer ends up repackaging to ensure appropriate retail pricing for the various consumer categories and ability of consumers to shift load to lower cost periods. Suggested amendment: *‘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.’*			
(ii) signalling, to the extent practicable, the impact of additional usage on future investment costs.			Add additional principle: ‘*(iv) Price signalling to take into consideration the ability of the consumer to take advantage of any such signals.’* This additional point requires	

Draft Principle	Contact	Meridian	TrustPower	Commission Response
			the distributor to have a practical approach to price signalling no just a purely theoretical approach. A purely theoretical approach could mean substantial costs for the consumer and retailer to take up the pricing signals being promoted.	
(b) Where prices based on 'efficient' incremental costs would under-recover allowed revenues, the shortfall should be made up by setting prices in a manner that has regard to consumers' demand responsiveness <u>(i.e. Ramsey pricing) and/or the quality of service that they receive</u>, to the extent practicable.		Understand the Commerce Commission is discussing problems with the availability of data to be able to effectively undertake Ramsey pricing (eg data on price elasticity). Query whether the "shortfall" should refer to "unallocated" costs. **Todd Energy** suggests replacing 'consumers' with 'connected parties'.		The Commission has adopted the suggested Vector wording to reduce the potential for stakeholders to believe that they must implement Ramsey pricing per se, which is difficult to do in practice. The quality of service responsiveness can be covered in the amended principle (c).
(c) Provided that prices satisfy (a) above, prices should be responsive to the requirements and circumstances of users in				

Draft Principle	Contact	Meridian	TrustPower	Commission Response
order to:				
(i) discourage uneconomic bypass; and				
(ii) allow for <u>price/quality tradeoffs.</u>				.
(d) Development of prices should <u>be transparent</u>, promote price stability and certainty for <u>consumers</u>, and <u>lead to prices that are able to be understood by users.</u>	Is intended to address consumer interests, but fails to take into account retailer interests. Not clear what is trying to be achieved. The key requirements are price structure stability and certainty for retailers, and not passing on unrecoverable network costs to retailers. Suggested amendment: *'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*	Queries who the "customer" or user is in this context – with interposed use of system agreements the customer of the lines company is the retailer. Refers to previous submission regarding consistency of price signals which does not appear to be picked up in any of the proposed pricing signals. **Todd Energy** suggest replacing 'consumers' with 'retailers, consumers and other connected parties' and 'users' with 'users of the assets'.	After consumers add: '*and retailers'*. Pricing stability, certainty and clarity are just as critical for the retailer, in most instances the retailer is interposed between the consumer and the distributor. The practice of GXP pricing does not provide transparency through to the individual consumer or predictability for the retailer when setting consumer charges.	The generic term "stakeholder" has been introduced to cover all affected parties. The use of "transparent" has been retained to reinforce the concept behind the Information Disclosure requirements that apply to the pricing methodologies. Transparency should lead to understandable pricing so that condition has been removed and replaced with the need for consideration of the impact of changes in prices on stakeholders such as retailers and consumers.

Draft Principle	Contact	Meridian	TrustPower	Commission Response
	billing systems and widely deployed metering in the network area, and be able to be easily understood by consumers.'			
(e) Pricing structures should not place undue transaction costs on retailers and consumers, and should be competitively neutral across retailers.		Suggests the lines companies pricing structures must be competitively neutral across retailers – especially given that a lines company can now be a retailer of electricity. Perhaps there should be a requirement for a lines company that is an electricity retailer to publish in percentage terms the number of customers on each of their published line tariffs. This would assist in ensuring transparency of competitive neutrality. **MRP** suggests that this warrants further prescription and detail in order to be effective. **Todd Energy** suggest replacing "retailers and consumers" with "retailers, consumers and other connected parties", and replace the second incidence of "retailers" with		Based on suggestions from submitters, the original wording has been replaced by a clearer expression of the intent of the principle.

Draft Principle	Contact	Meridian	TrustPower	Commission Response
		“retailers and connected parties”		
(f) Prices and pricing structures should promote efficient usage of electricity and encourage investment in distributed generation (including renewable generation), distribution alternatives and technology innovation.		Agrees with the intent of this principle but not if it is applied in a way that makes customers worse off. The Electricity Governance (Connection of Distributed Generation) Regulations 2007 include pricing principles for connection of distributed generation. Queries whether the lines companies pricing should “encourage” distributed generation at the expense of other generation or other customers without distributed generation and considering the GPS states “it is important that there are no unnecessary barriers to its development”. Maybe lines companies pricing should “enable” distributed generation as opposed to encourage it.		As suggested by a number of submitters, this principle has been incorporated into principle (c).
Additional Principles suggested	To deal with annual line charges:			

Draft Principle	Contact	Meridian	TrustPower	Commission Response
	'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.' Pricing schedule completeness: *'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.'*			

1.3 Other Submissions on proposed principles

Draft Principle	DEUN	MEUG	Response
(a) Prices are to signal the economic costs of service provision, by:			
(i) being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), <u>except where subsidies arise from legislation;</u>	This is identified as a key issue, but DEUN has reserved its position until more work can be done on it. Generally supports implementing cross-subsidies that are provided for in legislation, so long as they are applied as cost-effectively as possible. Rural consumers cost more to supply than nearby urban ones, but the regional economy depends on keeping rural businesses (including farming families) viable, and very high electricity bills could make this impossible.		The revised version provides greater clarity and does not diminish the intent of the principle. Material cross subsidies should be disclosed as part of the information disclosure.
(ii) signalling, to the extent practicable, the impact of additional usage on future investment costs.			
(b) Where prices based on 'efficient' incremental costs would under-recover allowed revenues, the shortfall should be made up by setting prices in a manner that has	Does not support Ramsey pricing because it perpetuates price discrimination that keeps domestic prices high and prices to competitive consumers low.		The Commission has adopted the suggested Vector wording to reduce the potential for stakeholders to believe that they must implement Ramsey pricing

Draft Principle	DEUN	MEUG	Response
regard to consumers' demand responsiveness (i.e. Ramsey pricing) and/or the quality of service that they receive, to the extent practicable.			per se, which is difficult to do in practice. The quality of service responsiveness can be covered in the amended principle (c).
(c) Provided that prices satisfy (a) above, prices should be responsive to the requirements and circumstances of users in order to:			
(i) discourage uneconomic bypass; and			
(ii) allow for price/quality tradeoffs.			
(d) Development of prices should be transparent, promote price stability and certainty for consumers, and lead to prices that are able to be understood by users.			
(e) Pricing structures should not place undue transaction costs on retailers and consumers, and should be competitively neutral across retailers.			
(f) Prices and pricing structures should	Supportive of this principle, which	This principle is redundant because of	As suggested by a number of

Draft Principle	DEUN	MEUG	Response
promote efficient usage of electricity and encourage investment in distributed generation (including renewable generation), distribution alternatives and technology innovation.	recognises the potential of distribution pricing to actually promote innovation, small-scale generation, and energy efficiency.	requirements of principle (a). Promotion or encouragement of efficient use practices, distributed generation or technology innovation starts with economically efficient prices. Any suggestion that promotion or encouragement might include tilting the playing field in favour of those options is contrary to principle (a) (i) to be subsidy free.	submitters, this principle has been incorporated into principle (c).

Appendix 2 Submissions regarding methodological requirements

2.1 General comments on methodological requirements

Submitter	Comment	Response
Eastland Network	The requirements as proposed, when applied to small, sparse, rural networks, will illustrate inefficiencies and high levels of cross-subsidisation that are brought about by current legislative requirements. If these are not considered in the context of the legislation or the physical characteristics of the network, they will lead to erroneous or incorrect conclusions being drawn over the nature of the distributor's pricing.	Requirements have been amended to provide information disclosure guidelines. Where legislation or regulation leads to inefficiencies and high levels of subsidisation, these should be disclosed and quantified where practicable
ENA	The methodological requirements are not required, and impose undue limitations on the principles themselves. The Electricity Information Disclosure Requirements for electricity distributors already set out the information that must be disclosed by distributors when publishing pricing methodologies. This, along with a requirement that pricing methodologies must have regard to the pricing principles, is sufficient.	Requirements have been amended to provide information disclosure guidelines.
Mighty River Power	Believes the most critical barrier to competition in the electricity retail market is the existence of an excessive number of distributors each with their own set of terms and conditions or access and pricing – so are supportive of proposals to develop a regulated methodology. Suggest that the problems retailers face with entering small network areas can be compounded by the diversity of electricity distribution tariff arrangements, particularly in small networks with an inordinate number of tariff categories.	Noted.

Submitter	Comment	Response
	Network access arrangements, including pricing, can impact on the level of competition in any market where network access is needed in order to compete. Examples of such markets include airports, electricity, gas, ports and telecommunications. Precisely because of this that the Government introduced access regimes under the Telecommunications Act and the Dairy Industry Restructuring Act, including regulation of price.	Noted.
	Agree that it is up to distributors to demonstrate a voluntary approach would work, and suggest that it would be helpful if some distributors pooled their resources to develop a generic pricing methodology they would all be happy to adopt.	Noted.
	Recommend that the Electricity Commission undertake a review of current tariff setting practices to identify what is industry best practice and what stands out as being of particular concern. This would be particularly helpful in order to operationalise some of the principles. This would be invaluable in providing distributors guidance on the reviews they will need to undertake of their pricing methodologies and how to best comply with the Commission's pricing principles and methodological requirements.	Agree – the proposal is to introduce an independent review of pricing methodologies.
	Do not believe the Electricity Commission's proposals are unreasonable for distributors to comply with. Distributors are natural monopolies and the proposals are at the lower end of the regulatory scale. They leave distributors with considerable discretion over how to set their prices. The onus needs to be on distributors to demonstrate their pricing practices are reasonable and justified. MRP suggest that if distributors cannot demonstrate that there pricing practices best serve the long-term interests of consumers	Noted.

Submitter	Comment	Response
	then greater regulatory intervention is justified.	
Meridian	Methodological requirements appear detailed but do not seem to have a direct reference to the pricing principles. For example – the question "have the pricing principles been applied in the development of the proposed prices?" could be asked in the compliance stage.	Requirements have been amended to provide information disclosure guidelines. The information disclosure should contain a statement by the company on the extent that its distribution pricing methodology complies with the pricing principles.
Network Waitaki	Need to be more specific with regards to definitions in order to ensure that the pricing methodology disclosures deliver on their intent to demonstrate compliance with the pricing principles. EC needs to define the load groups it wants disclosures based on – otherwise distributors will need to test compliance by submitting existing methodology and getting feedback from regulator. AMP disclosure is like this and has been unsatisfactory. Co-ordinate this workstream with smart metering.	Agree. A guideline has been added for distributors to show linkage between pricing principles and their pricing methodology. Process will be evolutionary.
Northpower	Believes that its network already has a very high level of retail competition, and does not think that regulating methodologies will have a positive effect on the level of retail competition.	Noted.
Orion	The minimum disclosure should include: ▪ a description of the methodology used and how the methodology links to any applicable pricing principles; ▪ the rationale for customer groupings and the method for determining the allocation of customers to the customer groupings; ▪ quantification of key components of regulated revenue and	Requirements have been amended to provide information disclosure guidelines which are generally in line with this suggestion.

Submitter	Comment	Response
	costs; ▪ description of the methodology and quantification of allocation of revenues and costs to the customer groupings; and ▪ customer and volume statistics.	
Powerco	Pricing methodologies have a similar degree of information asymmetry to asset management plans. In trying to improve asset management, the Commerce Commission chose to use information disclosure as the regulatory instrument, along with an annual report highlighting poorly performing EDBs. Powerco recommends this approach is adopted for pricing methodologies. The Commission and the Commerce Commission should produce one set of principles, require one annual disclosure and use one expert to assess the pricing methodologies.	The Commission is working with the Commerce Commission to align information disclosure requirement. The proposed methodological requirements have been amended to provide guidelines and the Commission will be developing a compliance monitoring approach based on an independent review of pricing methodologies.
PWC	Adoption of the form of the Pricing Methodology Report which the Commerce Commission required of Vector and Powerco for the Gas Authorisation and a similar compliance review process is not appropriate. These requirements are well in excess of what is required to meet the EC and Commerce Commission mandates and objectives. Given the considerable overlap between the legislative obligations of the two regulatory bodies, the requirements on EDBs for pricing methodologies should be consistent, and can be implemented without duplicating compliance processes. Proposed requirements are too limiting and they presuppose that certain approaches will be applied and exclude other potential	The proposed Pricing Methodology Report was a guide only. The proposal has been amended to provide guidelines, which are generally in line with Requirement 23 of the Information Disclosure requirements.

Submitter	Comment	Response
	approaches. Recommends the use of Guidance such as that included in Requirement 23 of the IDRs.	
Todd Energy	Suggest a new guideline (a)(x): development of pricing arrangements that will be used to reflect the value of distributed generation contribution to deferral of investment in transmission assets and transmission costs avoided at the grid exit point.	Guideline amended to include pricing arrangements that will be used to share the value of deferral of investment in distribution assets with investors in alternatives (such as distributed generation or load management), in a similar manner to grid support contracts, where this is practicable.
Unison	Concerned that the Commission is proposing to provide methodological requirements. Non-mandatory guidelines would be more appropriate for assisting EDBs in their pricing methodology disclosures. Consider that the existing Information Disclosure Requirements could be utilised as a basis for these non-mandatory guidelines. The proposed reporting requirements would result in an onerous compliance burden on EDBs. Want to give the form of regulatory monitoring more consideration. Preliminary view is that a self-reporting process, similar to that for Asset Management Plans (AMPs) may be more efficient. Commission is suggesting an unnecessary high level of regulatory intervention. The principles can be adhered to by a form of self-reporting. Care needs to be taken that there is not a duplication of reporting in respect to the requirements under Part 4 of the Commerce Act. There needs to be an effective and practicable approach to monitoring the uptake of the proposed principles,	Requirements have been amended to provide guidelines.

Submitter	Comment	Response
	without the imposition of unnecessary compliance costs.	
Wellington Electricity	Considers that any reference to methodological requirements should be removed. To specify them is not consistent with a principles based approach as it presupposes a pricing based approach and removes flexibility to adapt to changing environments. In place of proposed Methodological Requirements the EC should refer to the Commerce Commission’s existing Information Disclosure requirements relating to Pricing Methodology disclosures.	Requirements have been amended to provide guidelines.

2.2 Specific comments on methodological requirements

Requirement	Comments	Response
(a) Prices should be based on a well-defined, clearly explained and published methodology, with any revisions notified and clearly marked.		
(b) Price development should incorporate, to the extent practicable, an analysis of the cost of service provision that includes:	**ENA:** Opposed to distributors needing to provide cost of supply models and to seek prior approval of prices. **WEL Networks:** Agree with (b) and (c) but many of the terms and technical words used should be defined somewhere.	Provision of cost of service models is not required. Noted.
(i) definition of the classes of service provided and the parameters by which the quality of service in each class are measured;		
(ii) an examination of the cost elements that arise from the use, operation and expansion		

Requirement	Comments	Response
of the network;		
(iii) <u>identification</u> of the relationship between the quality of service provided and the level of current and future cost for each class of service;		
(iv) an allocation of existing and future network costs to <u>service</u> classes, and an explanation of the cost allocation methodology used;		
(v) the translation of allocated costs into service prices at the defi<u>n</u>ed level of quality of service – <u>including the re-allocation of transmission charges while preserving the transmission pricing signal;</u>	**Contact:** Not clear why "preserving the transmission pricing signal" is relevant to methodological requirements. Suggested amendment: *'taking into account the transmission pricing methodology and signal to the extent practicable'.* **TrustPower:** Replace 'including the re-allocation of transmission charges while preserving the transmission pricing signal' with: *'having consideration of transmission pricing methodology and signalling in a manner which is practicable'.* These words are less prescriptive. It is	Reference to transmission pricing has been removed from the guidelines

Requirement	Comments	Response
	important that any translation of allocated costs should only be done if they are able to be passed through to consumers in a meaningful manner by the retailer.	
(vi) analysis of the extent to which costs are marginal, and whether the associated price components in the tariff structure reflect those marginal costs;		
(vii) analysis of the development of time of use prices and critical peak pricing where these can practically be applied;		
(viii) estimates of the range of subsidy-free prices for each service class and the extent to which subsidies, if any, are caused by legislation; and	**Contact:** 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. Suggested amendment: *'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.'*	Noted

Requirement	Comments	Response
(ix) <u>development of pricing arrangements that will be used to reflect the cost / value of deferral of investment in distribution assets, where this is practicable.</u>		
(c) Information relating to standard services on customer class price levels and structures, quality of service standards, underlying costs, price derivation methods and rationale, and medium term price and quality of service strategies should be publicly disclosed.		
(d) Underlying service classifications, cost data, cost allocations and other elements that contribute to pricing decisions should be periodically reviewed and updated where relevant to reflect industry developments and changes in user requirements and preferences,	**WEL Networks:** When methodology is not changed, a simple declaration stating this should be all that is required for disclosure.	Agree. This clause has been removed from the guidelines. Information disclosure should include details of changes to the methodology

Requirement	Comments	Response
methods of service provision and costs.		
(e) Pricing structures should:		
(i) consist only of the minimum number of tariffs necessary to meet the provisions of the pricing principles; and	**MRP:** Warrants further prescription and detail in order to be effective.	Noted
(ii) employ industry standard tariff formats and nomenclature, where possible.	**Eastland Network**: Supports common terminologies and definitions, but does not support common tariff structure between distributors. Suggests an improved definition of domestic premises, that specifically excludes holiday homes, would be beneficial. Holiday homes should not qualify for the Low Fixed Charges or standard domestic tariffs as they bring to the network the issues of low average consumption with seasonal peaks. Believe that each distributor has developed their own tariffs to best suit the requirements of their end consumers as well as sending the correct pricing signals and generating the appropriate level of revenue for the business. Common tariffs could result in increased levels of cross	The industry working group is considering administrative issues that may be addressed bilaterally between retailers and distributors.

Requirement	Comments	Response
	subsidisation and send the wrong pricing signals.	
(f) Where a change to the existing pricing methodology is proposed to improve compliance with the pricing principles, details of the impact on customer classes and the transition arrangements proposed to mitigate the effect of redistribution of costs and "rate shock" should be publicly disclosed.	**ENA:** Do not support the proposed disclosure of variations to the pricing methodology – this is not consistent with the principle approach. **MEUG:** Would be useful to include time requirements for EDBs giving notice of price changes with such notice being sufficient to allow retailers to amend their prices. Similarly a requirement to respond within a certain time to inquiries from parties seeking information on EDB prices and opportunity for customised charges to particular sites would be an improvement on the status quo.	Disclosure of changes to the pricing methodology is a vital element of the pricing principles. The timing for price changes is usually covered by the use of system or other access arrangements.

Appendix 3 Submissions on reporting requirements

Submitter	Comment	Response
Eastland Network	Do not believe that the methodological requirements should be reported on nor used as measure in compliance reporting. They stand in contradiction to the principles based approach. A very high level of detail has been added to the original requirements from the gas determination. Concerned that proposal simply introduces the Commerce Commission's model pricing methodology by proxy since distributors will not only continue to price as they currently disclose but also have to develop the Commission's pricing model and then report on the differences. Will be extremely resource and cost intensive process. Current disclosure requirements of pricing methodologies in combination with threshold compliance statements and information disclosure schedules provide ample information for the regulator and interested parties. Concerned about the requirement to include an audit certificate of a cost of supply model as believe this simply adds excessive levels of audit and compliance reporting.	Requirements have been amended to provide guidelines. The Commission is working with the Commerce Commission to align information disclosure requirements It was a guide only.
ENA	Opposed to the auditing of models and the publication of long term pricing plans.	The proposed Pricing Methodology Report was to provide some guidance as to what would be compliant. .

Submitter	Comment	Response
	Support an approach which involves periodic industry-wide reviews of published pricing methodologies to be undertaken by one of the Commissions. This may be similar to the existing Asset Management Plan review process undertaken by the Commerce Commission. Publication of a review report could lead to improvements over time in the quality of pricing methodologies, as distributors would be able to learn from the experiences of others, and from the observations of the reviewer on any compliance issues, and on where examples of best practice may be found.	Agree. A periodic independent review of pricing methodologies will be introduced.
Northpower	Concerned by additional compliance costs which will arise from any new monitoring regime for distribution pricing. Already, distribution pricing is subject to compliance (and hence compliance costs) through requirements to disclose line charge tariff pricing and methodology, the revenue aspects in the annual Information Disclosure requirements (and associated audits), notification requirements in the Low Fixed Charge regulations, and price/quality thresholds assessments and associated audits. The Electricity Commission and the Commerce Commission are both developing regimes for monitoring distribution pricing methodologies, which has the potential for duplication and/or inconsistencies.	The Commission will work with the Commerce Commission to align the disclosure requirements to keep compliance costs as low as practicable.
Orion	Do not support the Commission's proposals for the publication of annual statements of variance/compliance, submission of a cost of supply model, disclosures of future pricing expectations, Commission	The proposed Pricing Methodology Report was to provide some guidance as to what would be compliant.

Submitter	Comment	Response
	audit and review and possible regulation. This is not justified and inconsistent with the regulatory mandate of both the Commerce Commission and the Commission in respect of pricing methodologies. The cost of compliance of such a process will be excessive, and inconsistent with the potential benefits (if any) of such an intrusive compliance process. Propose an alternative compliance process, based on the well-established AMP disclosure process established by the Commerce Commission as part of the existing information disclosure requirements for EDBs and more consistent with the regulatory objectives for pricing methodology disclosures. This should form part of the Commerce Commission's information disclosure requirements and be accessible to the Commission. The key aspects of the AMP compliance process and a suggested pricing methodology compliance process are included in Orion's submission.	Agree. A periodic independent review of pricing methodologies will be introduced.
Powerco	Compliance with the methodological requirements does not need to be assessed. The requirements would be a constraint, limiting Powerco's ability to innovate. Recommend the Commission consults further on non-mandatory guidelines as there has not been adequate time to consider these in this stage of consultation.	The Commission is introducing information disclosure guidelines and expects these to evolve over time based on experience and the outcomes of the periodic reviews of pricing methodologies
Powerco	The increase in consumers' outcomes from pricing regulation is likely to be fairly small, and correspondingly, the compliance costs of implementing regulation should be small.	The Commission will seek to keep compliance costs as low as practicable in pursuing its objectives.

Submitter	Comment	Response
	Would like further consultation to consider what level of information on the principles could be provided at a low compliance cost. Recommends the following approach (which is similar to the Commerce Commission's approach to Asset Management Plans): ▪ The Commission's principles are adopted by the Commerce Commission's pricing methodology information disclosure requirement. An EDB discloses its pricing methodology each year in line with the Commerce Commission requirements. This should include a description of the methodology and how the methodology has had regard to the pricing principles (in line with the Commerce Commission's current proposals). ▪ The Commission would not produce methodological requirements or a hypothetical/ model pricing methodology, but instead, would publish non-mandatory guidelines. These would provide the Commission's interpretation of the pricing principles and the issues that would need to be considered to show an EDB has had regard for the principles. ▪ The pricing methodology must be publicly disclosed (inline with current Commerce Commission requirements). ▪ The Commission and the Commerce Commission jointly engage a pricing methodology expert to review each pricing methodology and to produce a published report. This report: o assesses each pricing methodology for compliance and	The Commission will work with the Commerce Commission to align the information disclosure requirements of each organisation and will adopt an approach which is generally in line with this proposal.

Submitter	Comment	Response
	best practice o describe overall trends in industry; and o make observations on best practice or innovative developments. ▪ Assuming the reviews are available before the next pricing methodology is prepared; EDBs are able to address any issues raised in the report and consider the approaches adopted by others which are deemed to represent best practice. (Note, have listed benefits of recommended approach)	
PWC	Do not believe that a compliance process that was developed for the Gas Control Authorisation is appropriate for pricing methodology guidance to apply to a large number of entities who are not subject to the same level of regulatory intervention as that implied by the control authorisation. The cost of compliance with the proposed process will be excessive, and inconsistent with potential benefits (if any) of such an intrusive process. Propose an alternative compliance process, similar to the AMP review process.	See comments above. The compliance process will be light handed and regulation would only be considered where there is blatant disregard of the process and the principles.
Unison	The proposed compliance reporting requirements, and the proposed Pricing Report if the Commission considers that the EDB has not met	See comments above.

Submitter	Comment	Response
	the criteria for compliance, would be onerous and costly to EDBs. Further to the suggestion that the proposed methodological requirements be amended to guidelines, recommend a lower cost option would be more appropriate than such highly detailed disclosure reporting requirements.	Agree. Any change to the methodology should be disclosed based on the requirements of the Information Disclosure requirements. This should also include a statement that the change does not alter the compliance with the principles but this need not be audited.
	Need to reconsider the proposed reporting requirements in light of the Gas Authorisation experience. Vector and Powerco's experience of complying with the Commerce Commission's Gas Authorisation has proved to be a costly compliance exercise. A compliance statement every time you change your pricing methodology would be a high cost to an EDB, and therefore a barrier to innovation.	Agree
	Recommend that a description of how the pricing principles have been applied should be part of the pricing methodology documentation required under the Commerce Commission's Information Disclosure requirements. Preliminary view is that such a disclosure could incorporate the 'statement of variation/compliance' that was discussed at the recent workshop. This statement does not need to be audited – the cost of an independent audit would outweigh any potential benefits.	Agree.
	To assess whether the EDB is compliant either the Commission or the Commerce Commission could appoint an external consultant to produce a compliance report. (Unison needs to give this form of regulatory monitoring more consideration). Preliminary view is that this external review process resulting in a report could be similar to the AMP review process. In our experience to date the AMP process has encouraged compliance by EDBs and highlighted their best practices and innovative procedures. This self-reporting process has benefits for	Agree.

Submitter	Comment	Response
	all stakeholders, at the same time minimising compliance costs. Agree that if the regulatory body monitoring the compliance with the pricing principles believes an EDB is consistently and deliberately not taking those principles into account, then the regulatory body should have the ability to request further information from the EDB. However, the regulatory body needs to clearly specify what they believe to be non-compliance, and there needs to an opportunity for the EDB to change its methodology.	
Vector	The Commission proposal seems to unnecessarily maintain some aspects of the Gas Authorisation compliance approach that led to significant compliance costs. Would prefer to see a least cost approach targeted to providing only the necessary information required for the Commission and Commerce Commission to monitor how distributors have had regard to the pricing principles. The key test of compliance should be that an EDB should describe how they have had “regard to” the pricing principles and other pricing objectives in developing their pricing methodology. This would include describing holistically any analysis or decision making that took place as part of the pricing process in relation to each of the pricing principles. Proposal that a distributor should also show compliance with the methodological requirements should be removed. The key test of compliance needs to be against the pricing principles and parties should maintain sufficient flexibility to weight principles and other	Agree Agree Agree. The methodological requirements have been replaced by voluntary guidelines.

Submitter	Comment	Response
	pricing objective to derive efficient and innovative prices without further restrictions. More useful guidance on completing the pricing methodology is already available under Requirement 23 of the Information Disclosure requirements. The additional utilisation of the proposed methodological requirements only duplicates and confounds the provisions of this requirement. Generally supports the reporting approach but submits that compliance against the pricing principles should be shown as a section of the pricing methodology document required under Information Disclosures, rather than as a separate report as proposed. That is, a section of the pricing methodology should be devoted to the key test of how an EDB has had regard to the pricing principles. This would represent the "statement of compliance". Many of the methodological requirements proposed in the discussion paper will already be captured in other sections of this pricing methodology disclosure under Requirement 23. Proposed annual updates of this statement of compliance seem unnecessary, as pricing structures and methodologies are unlikely to materially change often, although actual prices will - due to CPI-X regulation. Propose that the Commission produce a monitoring report, similar in style to the AMP review, at set intervals (perhaps every two years), which provides and assessment and summary of how distributors have had regard to the pricing principles, highlighting best practice and any	The guidelines are generally line with Requirement 23 but provide more guidance on the specific information that would be useful. The Commission is working with the Commerce Commission in aligning the disclosure requirements. The process would allow for this approach. Agree. Update would only be necessary where there were material changes to the methodology. Agree. A periodic independent review will be introduced.

Submitter	Comment	Response
	areas of concern. Should the above monitoring and review process highlight consistent and deliberate non-compliance by an individual distributor over several monitoring periods, then further action may be warranted against that distributor. But the grounds for any charge of non-compliance need to be clearly explained. Supports the concept of the distributor being required to explain their pricing approach more rigorously but does not support the proposed pricing report or view that it needs to be defined at this stage. Apart from in cases of blatant non-compliance, it is unlikely that the Commission will ever find a distributor in breach of the pricing principles so a full report may not even be necessary. The focus of debate should be on the process to encourage compliance.	Agree
Wellington Electricity	Does not consider the Commerce Commission's compliance process in the gas authorisation, which was set-up for the implementation of controlled prices and which incorporates a highly prescriptive format, detailed reviews and audit criteria, is appropriate for the purposes of verifying compliance with a non-mandatory Distribution Pricing Methodology. Recommend that the same type of compliance and review process that applies now to Asset Management Plans should be adopted by the EC instead. An AMP "type" review process would be much lower cost than the EC's proposed process.	See comments above.

Submitter	Comment	Response
WEL Networks	The compliance costs for enforcing this regulation must be less than the improvement in outcomes to consumers for the regulation. What do these regulations provide that the Commerce Commission disclosure regulations do not already achieve?	There are common objectives between the Commissions and the Commission is working with the Commerce Commission to align information disclosure requirements to keep compliance costs down. The Commission's approach is more targeted towards facilitating retail competition.