

COMMISSION OF THE EUROPEAN COMMUNITIES

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DRAFT COUNCIL RECOMMENDATION
ON ELECTRICITY TARIFF STRUCTURES IN THE COMMUNITY

(presented by the Commission to the Council)

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Electricity Tariff Structures

Communication from the Commission to the Council

I. INTRODUCTION

1. In its Resolution of 13 February 1975, the Council emphasised "the need to make it possible for prices to cover gradually and to the fullest extent possible, the cost of making energy available and the amortisation of the necessary investments"⁽¹⁾. On several occasions the Council has emphasised the need to save energy by optimising the use of resources.
2. The achievement of these objectives in the electricity sector can be facilitated through the adoption of an adequate and rational electricity tariff policy based on common principles agreed at Community level.
3. The Commission keeps under review the development of prices and pricing structures in the energy sector. In 1979 the Commission, together with the electricity supply industry, examined the electricity tariff structures in the Community and the possibilities of their alignment. It is now opportune for the Council to review the position and to adopt an agreed policy.

II. PRINCIPLES

4. Tariff structures should guarantee that consumers receive electricity supplies at prices that ensure that costs are covered and that sound financial balances are achieved. Tariffs should take account of the production, transmission and distribution costs of supplying the different categories of consumer. Artificially low rates for certain sectors at the expense of higher charges for others involve the risk of distortions in the structure of demand. So the requirement to cover costs should be fulfilled separately for each consumer sector. Tariffs should also be as clear and straight-forward as possible for obvious reasons of commercial, public relations and management policy.
5. Tariff structures should also be designed with the rational use of energy in mind by avoiding, in particular, inducements that could encourage energy wastage. A clear and coherent tariff policy for energy sources enables the consumer to make correct choices and leads to the optimum utilization of resources.

(1) O.J. N° C 153/6 of 9.7.1975

III. FIVE GUIDELINES

6. The Commission believes that a rational tariff structure for the electricity sector should be based on these principles which lead to the following five guideline proposals :

a) General application of two-part tariffs

Two-part tariffs consist of payment of a periodical fixed charge (*), independent of consumption; and a payment for the kilowatthours actually consumed.

As bulk electricity cannot be stored, it is produced when demanded. Electricity production, transmission and distribution plant is of course therefore installed to meet the maximum load which may be expected at a specific time. As consequent heavy investment is committed independently of the actual period during which plant on the system is used, the overheads (capital, payroll, plant costs) therefore account for 50 %- 80 % of total costs, depending on circumstances. Costs resulting from an increase in consumption using existing plant (essentially fuel costs) account for a smaller proportion of total costs. The average cost per Kwh therefore decreases the more Kwh a given plant produces. The cost structure is thus the inescapable logical basis for two-part tariffs. Where tariffs are such as to align prices with costs, the price moves in step with the costs incurred, thus producing a decreasing unit price with increasing consumption. In addition, however, in the sharing of fixed costs among the different categories of consumer, account needs to be taken of the contribution of each category to the forming of peak electricity demands. This should be taken into consideration particularly to ensure that fixed costs are fairly allocated at low levels of consumption (e.g., in the domestic sector).

Although most electricity suppliers in the Community are turning towards two-part tariff structures, the Commission believes this trend should continue at a faster rate. This should reduce disparities with other tariffs in which the price of electricity is reduced too sharply as consumption grows (See paragraph b).

(*) The fixed component is related to maximum demand (Kilowatt) and, consequently, to the investment which the electricity supplier has to make.

b) Elimination of block (*) tariffs of a promotional nature

Some tariffs promote electricity demand by dividing consumption in a specific period into successive fixed amounts of Kwh, to which reducing prices apply. These are thus structured in a way that accentuates artificially a diminishing level of costs and therefore stimulates unnecessarily high consumption. Although this type of tariff may have been justified in the past, it is no longer acceptable now that the rational use of energy resources is paramount. This kind of promotional tariff structure must now be eliminated.

c) Avoidance of tariffs based on type of use of electricity

The cost of supplying electricity is independent of how it is used by the consumer. Cost depends solely on quantity and on the times at which the consumption takes place (i.e. peak and off-peak).

Certain tariff structures, however, still apply to the specific use of electricity for such purposes as lighting, cooking, motive power and heating. The application of tariffs of this type to consumers who, in increasing numbers, are using electricity for different purposes, causes separate supply circuits to be installed on the same premises, and to be monitored by separate meters needed for separate invoicing, which thus leads to additional costs. Such procedures are to be avoided.

d) The provision of multiple tariffs (**) incorporating different price levels

Consumption of electricity at periods of maximum demand gives rise to a need for new investment in electrical plant. On the other hand a consumer who takes electricity during off-peak periods could receive supplies from existing plant. It is therefore desirable to restrain demand for electricity during peak periods and to transfer it to off-peak. This can be achieved by applying multiple tariffs incorporating different prices to different load periods such as : peak periods, off-peak periods, winter and summer periods and, in particular, in the home, during the day and night.

(*) Block tariff : a tariff in which the charge is based on a series of different kilowatt-hour rates applying to successive kilowatt-hour blocks of given size, supplied during a specific period.

(**) Multiple tariff : a tariff comprising different rates according to the periods of the day (e.g. rates for peakload hours, for day-time hours, or for low-load hours) or according to the season of the year.

This kind of tariff is already adopted in some countries and can with benefit be expanded, particularly for supplies to industry, where consumption is heavy. Deferment of investment in new plant and savings on operation of existing plant will be especially significant where contracts for interruptible supplies are developed, in particular in the industrial and commercial sector.

e) Exclusion of outside influences in drawing up tariffs

As the supply of electricity is a public service, electricity utilities are on occasion under pressure to offer uneconomic tariffs to certain categories of consumers. If this is done, for whatever desirable social motives or anti-inflationary policy reasons, electricity and energy demand as a whole is distorted. Other consumers may then be asked to pay higher tariffs. Policy should ensure that appropriate and economic tariffs are charged to all consumers and that where subsidies may be warranted on social grounds to those on low income, separate Government action is taken to provide support grants.

7. The guidelines in the five areas set out above could provide a common basis for tariff structures for electricity consumers in the Community. The necessary diversity in tariff structures, owing to the specific characteristics of consumer groups in each country and the structure of power station capacity, may need to be taken into account in the adoption of these guidelines. In addition, it is desirable, in times of rapidly rising costs, that prices should be frequently up-dated to avoid large changes and the political problems which they may cause. Tariff structures will need to ensure that this is feasible.

IV. A COMMUNITY TARIFF POLICY

8. Consistent and rational tariff structures are an important factor in the continued development of Community energy policy.

Although the ownership and organization of electricity utilities take different forms in the Community, the supply of electricity is a public service which aims at the equal treatment of consumers. Within the Community these aims require a common alignment of tariffs in order to provide homogeneous supply conditions, i.e. to ensure equality of treatment of consumers, avoiding distortions in pricing. In this way the securing of appropriate competition in the industrial sector can be helped, and consumers will be enabled to choose the right options, with the availability of clearer information on supply conditions.

9. Nevertheless, attention must be drawn to the fact that any changes to the tariff structures for electricity involve the solution of economic, technical, legal and administrative problems. Although price adjustments are relatively easy to implement, this may not be the case when changes to tariff structures are proposed : the merits of altering long-established tariff structures may not be immediately clear to all. Consumers will need to be advised about the reasons for, and consequences of, such changes.
10. The Commission's objective with this Recommendation is only to get agreement on some basic tariff structure principles. Further action in tariff and price policy must be carefully studied and developed in collaboration with Member States.

V. TARIFF RESEARCH

11. In addition it will be wise to continue and intensify research into the demand characteristics of the various consumer categories and their long-term development. This entails highly complex and expensive survey and assessment work. Exchanges of information on methodology and results, and collaboration between Community countries in this field should be increased.

V. RECOMMENDATION

12. The Commission invites the Council to approve the attached draft Recommendation.

DRAFT

COUNCIL RECOMMENDATION

on electricity tariff structures in the Community

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community,

Having regard to the draft Recommendation submitted by the Commission,

Having regard to the opinion of the European Parliament,

Whereas the Council, in its Resolution of 13 February 1975 (1), emphasised the need to make it possible for prices to cover, gradually and to the fullest extent possible, the costs of making energy available and the amortization of the necessary investments;

Whereas consistent energy pricing is a fundamental element of economic and energy policy;

Whereas rational tariff structures allow better utilization of resources;

Whereas the provision of electricity is a public service, irrespective of the legal status of the undertakings involved, and whereas for this reason undertakings must ensure equality of treatment of consumers under comparable supply conditions;

Whereas tariff structures founded on common principles lead to more homogeneous conditions of supply and are a step in the direction of more coherent electricity prices throughout the Community;

Whereas electricity supply undertakings must cover their costs on the basis of an objective allocation of these costs among the various categories of users;

Whereas tariff structures should not be used for the redistribution of resources among electricity consumers;

Whereas promotional tariff structures likely to prevent the rational use of energy should be avoided;

(1) OJ No C 153, 9.7.1975, p. 6

Whereas the principles underlying electricity tariff structures are not yet in general use in the Community, although certain of these structures already reflect a common approach, and whereas efforts to bring about simplification and unification must be pursued ;

HEREBY RECOMMENDS TO THE MEMBER STATES :

That they adopt, where these do not already exist, the requisite laws, regulations and administrative provisions to ensure that electricity tariff structures are based on the following common principles :

1. Tariff structures should be drawn up and adopted so as to allow the application of a rational price policy for electricity and so as to reflect the costs incurred in supplying the various categories of consumer; tariff structures should be designed with the rational use of energy in mind, avoid inducements that could encourage unjustifiably high consumption, and be as clear and simple as possible.
2. The two-part tariff system, which of the various tariff options available, best reflects the cost structure of providing electricity, should be generally used.
3. Promotional tariff structures which encourage unnecessary consumption and in which the price of electricity is artificially lowered as increasing amounts of electricity are used should be discontinued.
4. Tariffs based on the use to which electricity is put should be eliminated.
5. Tariff systems should provide for multiple tariffs, with differential rates which aim to transfer demand for electricity to off-peak periods, and for contracts for interruptible supplies.
6. Tariffs should not be kept artificially low, for example for social motives or anti-inflationary policy reasons; in such cases, separate action, where warranted, should be taken.
7. Tariff structures should ensure that it is possible to up-date prices at regular intervals;

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That research be pursued and developed, in close cooperation at Community level, into the characteristics of electricity demand for different categories of consumers and their evolution in the long-term, with the objective of further improving tariff structures;

That electricity prices on the market be characterised by the greatest possible degree of transparency, and that these prices and the cost to the electricity consumer should be made known to the public as widely as possible.