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Submissions on Revised Draft ODV Handbook
Network Performance Group
Commerce Commission
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Wellington

This submission is in response to the revised draft ODV Handbook and associated papers issued for consultation on 9 July 2004.

The ENA recognises the Commission has, relative to the initial draft ODV Handbook, improved significantly the transparency and robustness of its approach to setting standard values in the revised draft ODV Handbook. ENA members will be commenting on the actual values used and other aspects of the revised draft.

In this submission the ENA wishes to reiterate a number of issues that remain outstanding in the revised draft and which, in the ENA's view, should and could be addressed in the final ODV Handbook.

Clarity of purpose and use of market prices

The purpose of the ODV valuations remains unspecified. The Commission states in its cover report¹ that (paragraph 19):

"With respect to any post-breach inquiries by the Commission under the targeted control regime, the Commission has previously indicated it would, where appropriate and relevant, use such valuations as the starting point for its inquiry, but may then take into account the business-specific circumstances of any lines business that is the subject of an inquiry."

¹ Regulation of Electricity Lines Businesses, Invitation for Submissions on Handbook for Optimised Deprival Valuation of System Fixed Assets of Electricity Lines Businesses: Revised Draft for Consultation", Commerce Commission, 9 July 2004.

This indicates the ODV valuations may be used for investigations under Part 4A of the Commerce Act. It does not address the issue as to whether these valuations may be used for the setting of prices if the goods or services of a lines business were controlled, and it places no obligation on the Commission to take into account situations where the costs faced by a lines business exceed the standard costs stated in the ODV Handbook.

The ENA has recommended in the past that the Handbook allow for a lines business to use market prices applicable to its situation, in preference to standard costs, where it can demonstrate that special circumstances exist, and that the prices used for the special circumstances conform to a test of efficient costs. The ENA recommends that at a minimum this should apply, and be stated explicitly in the ODV Handbook, where the valuations are to be used as part of any post-breach investigation by the Commission under Part 4A, or in the process of setting prices for goods and services under control.

Valuations will not be comprehensive

The revised draft includes a list of assets that are not to be included in the ODV valuations (paragraph 2.7). It is not clear however how the Commission expects these assets to be included in the wider valuation of the lines business.

The cover report (paragraph 25) indicates this issue will be addressed in the Commission's review of the information disclosure regime and the development of a regulatory accounting framework. However the timing of this review is such that the 2003/04 valuations will need to be reported prior to its completion. Thus these valuations will incorporate the revised ODV valuations, but remain incomplete.

The ENA recommends the Commission clarify how assets (both tangible and intangible) used in the delivery of the electricity conveyance services, but excluded from the ODV Handbook and the current information disclosure regulations, are to be included in the interim in the valuation of lines businesses.

Planning horizons distort investment

The planning horizons for the optimisation test remain those in the original ODV Handbook and they do not reflect engineering best practice. The ENA and its members have raised this issue from the very start of the ODV Handbook review process, with no success. It remains a mystery as to why progress has not been made on this issue.

Under the thresholds regime lines business have financial incentives to minimise cost, as they are rewarded by higher profits from doing so. The Commission notes that dynamic efficiency issues are an important objective of the regulatory regime (paragraph 28 of cover report), but then in the revised draft maintains planning horizons for optimisation that are inconsistent with optimal investment patterns. At a minimum the ENA recommends the planning horizons be set at ten years, to align with the ten-year asset management plan period.

The ENA suggests the Commission consider what, if any additional information it may require in relation to load forecasts in order to provide the necessary rigour to support longer planning periods.

Basis for valuing LV cable

Note (h) of handbook Table A.1 states, with respect to LV cables "Values are based on costs for suburban subdivisions". These values reflect situations where a subdivision is being established. This is in many cases inconsistent with the approach to determining replacement costs as set out in paragraph 2.13 of the draft handbook, that:

"Replacement costs for non-standard assets should be determined on the basis that construction occurs around all existing infrastructure and development (other than the asset being valued)."

The cost of reticulating LV cables where the area is already built-up is considerably higher than in a new subdivision. ENA members have provided the Commission with appropriate values that reflect this. The ENA recommends they be adopted.

EV test re-introduced without justification

The EV test has been re-introduced in the revised draft, but was removed in the initial draft ODV Handbook for rural distribution spurs. No justification is given for its re-introduction.

The ENA recommends the EV test be removed, and at a minimum be removed in relation to rural distribution spurs as it was in the initial draft ODV Handbook.

No procedures for updating the ODV Handbook

The original ODV Handbook did not incorporate procedures for updating it and in fact was not updated for ten years. The revision process the Commission has undertaken over the last year has suffered, in the ENA's view, from the absence of such clear and robust updating procedures.

The ENA recommends that updating procedures be incorporated in the final ODV Handbook.

Transpower optimisation exemption and confusion with purpose

The revised draft exempts Transpower from the ODV optimisation rules in certain circumstances (paragraph 2.35):

“For the avoidance of doubt, optimisation of transmission projects that have been approved by the Electricity Commission is not required.”

The Commission’s cover report does not explain why this exemption is included, but the ENA assumes it is to enable Transpower to shift optimisation risk to its customers via its pricing. If this is the case, this exemption confuses the preparation of ODV valuations as part of the information disclosure regime with the pricing of Transpower’s services.

This exemption highlights the importance of the Commission clarifying the purpose of the ODV valuations. If their purpose is for monitoring lines business performance by way of the information disclosure regime (which appears to be the case, as opposed to the pricing of services), then this exemption is not necessary to enable Transpower to shift optimisation risk to its customers.

Under Part F, as issued by the Electricity Commission, it appears most of Transpower’s investments going forward will be approved by the Electricity Commission. This exemption therefore is likely over time, through the renewal and expansion process, to apply to most of Transpower’s assets. The ENA finds this exemption extraordinary, as it removes one of the key disciplines in the ODV regime. As a practical matter, it would introduce complexity by creating an arbitrary boundary between existing assets and those procured after some arbitrary date.

The ENA recommends this exemption be removed.

We would be happy to discuss the issues raised in this submission with the Commission.

Yours sincerely

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