

30 July 2004

Network Performance Group
Commerce Commission
PO Box 2351
WELLINGTON

Submission on revised draft ODV handbook

Thank you for the opportunity to comment on the draft ODV handbook. We support the application of a consistent valuation methodology for electricity lines businesses.

We would like to comment on the application of depreciated historic cost valuation to Transpower's assets.

At paragraph 27 of the Invitation for Submissions the Commission notes that lines businesses will not be required to commit to a choice between DHC and ODV prior to clarification of the principles and rules that will apply to DHC valuation (and consultation on these principles). In contrast to this, paragraph 16 indicates that Transpower has already indicated that it will adopt a DHC based valuation process.

Transpower has indicated that it wishes to use ODV for the purposes of its opening asset value and then supplement this with historic cost valuations of future investments. We wish to raise two concerns with this:

- It is conceivable that the optimisation process under ODV will result in different network configurations over time. This could occur, for example, if the load or generation composition changes, or generators or consumers install new equipment that changes the need for transmission assets.
- Technological innovation could also result in changes in network engineering and hence the optimal configuration of the network. In addition technological change could alter the replacement cost of system assets, and therefore the ODV valuation.

For these reasons it is desirable that Transpower be required to re-optimize the grid configuration periodically. A specific example of where the optimisation process leads to an illogical result at a point in time is in the optimisation of the Benmore injection point:

- Transpower have optimised the HVDC Pole 1 from a connection at Benmore (BEN) 16kV bus to the 220kV grid. This in turn creates a transmission constraint at BEN (since part of the generation relies on the HVDC Pole 1 for transmission to the North Island grid).
- Transpower have thus noted that an additional interconnection transformer (complete with associated switchgear etc.) is required in the optimal grid configuration. This asset does not exist, and Transpower have no plans to install it (since the constraint is not real).
- However, Meridian pays a substantial amount in its annual transmission charges for this optimised non-existent asset.

If it were possible to remove this constraint by a non-transmission means, but the grid was never re-optimised, Meridian would continue to pay an annual charge for an asset that does not exist. Indeed, it suggests that if Transpower installed an asset to relieve the optimised constraint at Benmore, and that investment was approved by the Electricity Commission, Meridian would pay twice for the constraint relief (since the 'asset' would be in both the opening asset value and the additions).

The handbook indicates (at paragraph 2.35) that transmission projects that are approved by the Electricity Commission will not be required to be optimised. It is not clear why projects which are approved

by the Electricity Commission should be excluded from this process. The approval process will presumably be equally susceptible to under- or over-investment over time as any other rational investment strategy. There is therefore no disadvantage to including these assets in the optimisation process. Not including them could constrain the optimisation of other network assets.

We suggest that Transpower be required to use ODV valuation, like other lines businesses, until full consideration of DHC principles and rules is completed. If DHC valuation is adopted then the current ODV value of the grid is not appropriate as a static starting point for this valuation.

Thank you again for the opportunity to comment on the handbook. If you have any queries, please contact me.

Yours sincerely



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