



**SUBMISSION TO
COMMERCE COMMISSION**

**Regulation of Electricity Line
Businesses Draft Handbook for
Optimised Deprival Value of
System Fixed Assets and Draft
Information Disclosure
Requirements**

9 February 2004

MARLBOROUGH LINES LIMITED

Submissions on Draft ODV Handbook and Draft Information Disclosure Requirements
Network Performance Group
Commerce Commission
PO Box 2351
Level 6, 44-52 The Terrace
WELLINGTON

SUBMISSION OF MARLBOROUGH LINES LIMITED

1. Introduction

- 1.1 The Commerce Commission (“the Commission”) is required under Part 4A of the Commerce Act (“the Act”) to set thresholds with a declaration of control in respect of electricity distribution and transmission services supplied by large Electricity Lines Businesses (“ELBs”). The Commission has released a draft Optimised Deprival Valuation Handbook (“the Draft ODV Handbook”), draft Information Disclosure Requirements (“the Draft Requirements”), and a draft Information Disclosure Requirements Handbook (“the Draft Disclosure Handbook”) pursuant to Part 4A of the Commerce Act 1986. At the same time the Commission has issued an Invitation for Submissions Paper dated 23 December 2003 (“the 23 December Paper”).
- 1.2 Marlborough Lines is party to and fully supports a submission prepared by PricewaterhouseCoopers (“the PWC Submission”) on behalf of 19 large ELBs.
- 1.3 This individual submission from Marlborough Lines expands on some aspects of that group submission.

2. Background

- 2.1 Marlborough Lines is a medium sized ELB, supplying 21,400 consumers over 3,280km of line located throughout Marlborough.
- 2.2 Marlborough Lines also owns:
 - 50% of Nelson Electricity Limited, the network which supplies the city of Nelson;
 - 51% of OtagoNet the network which supplies provincial Otago excluding Central Otago.
- 2.3 Nelson Electricity has the greatest consumer density of any network in New Zealand whilst OtagoNet is the least dense.
- 2.4 The Marlborough network extends to some remote areas which can only be reached by helicopter or boat.

- 2.5 Of the total Marlborough consumer base, 48% are located in Blenheim, a further 18% in smaller townships throughout Marlborough, and the remaining 34% throughout rural and sparsely populated areas such as the Marlborough Sounds and Upper Awatere Valley/Molesworth areas. Overall, 80% of consumers are supplied from 20% of the network.
- 2.6 Marlborough Lines has a single point of supply (GXP) connection with Transpower's system. The company has a significant 33kV sub-transmission system incorporating 325km of 33kV lines and 13 33/11kV zone substations.

3. Objective of Valuations

- 3.1 We reiterate the concerns expressed in the PWC Submission, that the Commission has not, in any of the papers released to date, advised the purpose of the valuations derived from compliance with the Handbook. That is, does the Commission hope to achieve consistent outcomes for comparative monitoring of performance, or is an accurate valuation required for post-breach investigations of individual ELBs. We are also concerned that previous Commission decisions have indicated ELBs will be required to choose either ODV or Depreciated Historic Cost ("DHC") valuation options by April 2004, but as yet the Commission has given no indication of the principles to be adopted should companies choose the DHC option.
- 3.2 The decision regarding which valuation methodology to be adopted by individual ELBs is not one which should be taken lightly or rushed to comply with an unrealistic deadline. There is some seven weeks remaining to the end of the current financial year. We submit the Commission must provide ELBs with significantly more time to consider the as yet unreleased Handbook for the DHC alternative, and to then make a decision regarding the future valuation method to be adopted.
- 3.3 As an example of the potential conflict between the two valuation methodologies, the Draft Handbook includes in Appendix B a requirement for high voltage and low voltage underground cabling, that "*Cables running close together, or on the same side of any road or street must be optimised to a single trench except where this would not meet the ELBs quality of supply requirements.*"
- 3.4 Assuming a DHC Handbook would allow the cost of trenching for a new cable to be included in the "cost", this requirement will inevitable lead to companies adopting the ODV methodology being significantly disadvantaged when compared to those adopting the DHC methodology.

4. Part 2: Practical Valuation and Mandatory Procedures

4.1 Clause 2.13

- 4.1.1 The term "brownfields" used in this clause is not defined, and should either be deleted or a full explanation as to the meaning of the term provided. Further, this clause requires that replacement costs must be "*commensurate with a significant scale of construction rather than with piecemeal additions*", and as

a guide suggests a replacement cost of a distribution feeder should be determined on the basis that the “*feeder is constructed as a single project.*”

- 4.1.2 Marlborough Lines has one 11kV feeder from a zone substation totalling 275km of 11kV line and over 300 distribution substations. We suggest it would be absurd to base a replacement cost on that scale of construction. Given that the “unit” for maximum value and life in Table A1 is, for distribution lines 1km, we suggest it would be more appropriate to use that measure as a definition of “significant scale”.

4.2 Optimisation

4.2.1 *Appendix A: Valuing Assets and Maximum Asset Costs and Lines*

- 4.2.1.1 Clause A.3 excludes the costs of land use consents, easements and compensation. Then clause A.29 allows easement rights obtained and registered against a land title to be valued at the purchase cost, “*provided that the sum paid has not already been expensed.*”
- 4.2.1.2 We submit it is not appropriate to consider the accounting treatment of expenditure on easements in deciding whether or not they should be included in the ODV. We believe easements are an asset, and where they are associated with system fixed assets, should properly be treated as system fixed assets. In our experience over recent years, easements over private land are becoming more expensive and more difficult to obtain. There is little doubt that under current legislation, the right to upgrade or add to a line, granted by the presence of an easement, will be of significant benefit and therefore value to ELBs in the future.
- 4.2.1.3 Clause A.10 continues to define remote areas as those situated “*more than 75km from the nearest works depot*”. As we have submitted on several occasions in the past, distance from works depots to remote areas is more properly measured in time. It can take more than two hours to travel 75km on a narrow windy gravel road, typical in the more remote parts of our network.
- 4.2.1.4 Additionally, the definition should include reference to travel by means other than normal vehicles. Where access to an area is for example by boat only, that area should be classified as remote irrespective of its distance from the nearest work depot.

4.2.2 *Appendix B: Optimisation for Electricity Lines Businesses*

Network Configuration

(d) High Voltage Distribution Network – Issue 3 – Valuation of Single Wire Earth Return Circuits

- 4.2.2.1 We submit it would be more appropriate for the table of standard values to include SWER lines and isolating transformers/substations, rather than the current proposal of valuing these SWER circuits as two wire circuits and

optimising out the isolating transformers.

- 4.2.2.2 Note “o” to Table A.1 includes reference to transformer earthing being included in the cost of distribution substations. However, the earthing requirements for SWER isolating and distribution substations are significantly more stringent than for two wire substations. In many areas, particularly those with very low soil resistivity, the cost of earthing SWER substations to achieve the required 5 ohm earth resistance can be greater than the cost of constructing the other works associated with that substation.
- 4.2.2.3 We fail to see how this type of factor can be taken into account in one single standard value for distribution substations.
- 4.2.2.4 It would be patently erroneous to suggest that the additional cost of this substation earthing is taken into account in the difference in construction cost between two wire and single wire lines, since the number of distribution substations per kilometre of line will vary from area to area.

4.2.3 *Optimisation of Network and Engineering*

(d) High Voltage Distribution

- 4.2.3.1 We fail to see the rationale for continuing the previous practice of requiring “*Cables running close together or on the same side of any road or street must be optimised to a single trench except where this would not meet the ELBs quality of supply requirements*”.
- 4.2.3.2 As mentioned earlier, this requirement alone will inevitably lead to significant differences between valuations on an ODV or DHC basis.
- 4.2.3.3 We submit that this requirement, and the similar requirement in Part (g) of this section should be deleted.

(f) Distribution Transformers

- 4.2.3.4 We note continuation of the 30% total distribution transformer capacity utilisation requirement.
- 4.2.3.5 Whilst we accept 30% capacity utilisation may be appropriate in urban and dense rural areas, we submit it is totally inappropriate for consideration of capacity utilisation in sparsely populated remote areas.
- 4.2.3.6 This is because in sparsely populated areas, it is common to have one transformer for one or two consumer connections. And since the smallest MEA single phase distribution transformer is 15kVA, where the consumers are domestic installations with an After Diversity Maximum Demand (“ADMD”) of 1 to 1.5kVA per installation, capacity utilisation factors of 10% would not be unusual.
- 4.2.3.7 Since transformer manufacturers will generally charge the same for a single phase 15kVA as for a non-standard single phase 5 or 10kVA transformer, there is no benefit to the ELB in purchasing transformers more matched to the consumers ADMD.
- 4.2.3.8 Similarly, areas with a significant level of irrigation consumption, which by its very nature is a summer only load, will often have a capacity utilisation of less than 30%. This is because if the maximum load on that feeder is a winter load, the irrigation transformers do not contribute to the maximum demand. Conversely if the maximum load on that feeder occurs during the summer, the non-irrigation transformers will not be contributing to that maximum demand to the extent they would be during the winter.
- 4.2.3.9 We therefore submit that provision must be included in the optimisation provisions for capacity utilisation of less than 30% where an ELB can show to an auditors satisfaction that the nature of loads on that feeder or section of the network justify a lower factor.

5. The Draft Disclosure Requirements

- 5.1 In Part 7, Derivation Table, symbol “m” is required to be added to the denominator for calculation of ROE. However the formula in Part 3 for this measure requires symbol “m” to be deducted.
- 5.2 This is a drafting error present in the existing regulations, which appears to have flowed through into the new draft.
- 5.3 Part 5, sections 3, 10, 14 and 18 refer to “average” targets for the following financial year and subsequent four financial years etc. There has obviously been some confusion among ELBs as to what is required with regard to these targets, with some companies reporting targets for each of the subsequent five years. However we understand from the Ministry of Economic Development that the current requirement is for a target for the following year and then one figure as target for the average of the next five years. We suggest some clarification of requirements is required.

- 5.4 We note the continued requirement for Marlborough Lines to consolidate the data for OtagoNet into its disclosed information, and agree this is the correct and appropriate treatment.

6. Conclusion

- 6.1 We thank you for the opportunity to comment on the Draft Handbook.

DA Waters
Deputy Chief Executive