



**SUBMISSION TO
COMMERCE COMMISSION**

**Development of a Handbook for the
Optimised Deprival Valuation of Electricity
Lines Business System Fixed Assets**

November 2003

NELSON ELECTRICITY LIMITED

14 November 2003

Submissions on ODV Handbook Issues Paper
Network Performance Group
Commerce Commission
PO Box 2351
Level 6, 44-52 The Terrace
WELLINGTON

Dear Sir

SUBMISSION OF NELSON ELECTRICITY LIMITED (NEL)

1. Introduction

- 1.1 NEL is a small electricity network company, which distributes electricity to some 8,600 consumers in the central Nelson area.
- 1.2 NEL was originally incorporated by the Nelson City Council and in 1996 the shares in Nelson Electricity were purchased by Marlborough Electric Limited and Tasman Energy Limited. These companies in their present form (Marlborough Lines Limited and Network Tasman Limited) continue to own the shares of NEL, each holding 50%.
- 1.3 The NEL network comprises a total of 241 circuit kilometres of reticulation. Of this some 83% is located underground. Whilst the Nelson region in general is experiencing strong growth the constrained nature of the Nelson reticulation has led to low growth in electricity consumption in recent years although there are signs presently that this is increasing.
- 1.4 NEL is involved with the submission prepared by PriceWaterhouseCoopers on behalf of 19 large electricity lines businesses and supports the industry group submission.
- 1.5 This short submission focuses on the issue of how NEL is disadvantaged by the ODV valuation process and the ODV replacement values and associated multipliers with particular regard to underground cabling.

1. Questions 7 and 10 (Standard maximum asset replacement costs, lives and multipliers)

1.1 The Commission is already aware of the unique attributes of NEL's network construction, being predominantly underground and being the densest electricity network by consumers per km of line. It is these attributes that give rise to NEL having an issue with the ODV Handbook values and multipliers and how they do not reflect the true costs NEL is faced with.

2.2 The attached table below demonstrates the current costs on a per metre basis for NEL to install underground cables on the network as an example to support this NEL submission. It is clear that the ODV Handbook values including multipliers are not high enough to reflect true replacement costs. Note: values do not include design and project management costs. All of these jobs were or are being built by independent contractors, on a competitive tender basis. There are no multipliers applied to the Handbook values as all these sites are outside the CBD area and not laid in rocky ground.

CABLE AND TRENCH COST BREAKDOWN

Project	HV/LV	Cable Size	Road or Footpath per metre	Trench Rate per metre	Cable Rate per metre	Total Rate per metre	ODV Handbook 4th Ed per metre
Actual Cost Examples							
GPO-Coll'wood Br (2003)	HV	300	Road	\$147	\$62	\$209	\$120
Hastings St (2003)	HV	300	Footpath	\$139	\$62	\$201	\$120
Sussex St (2003)	LV	300	Road	\$133	\$38	\$171	\$55

2.3 Reasons for the disparity between actual costs of installing underground cables and the ODV handbook value can be explained in part by the following:

- Stringent Local Body requirements on excavations in the footpath and roadway reinstatement cause additional costs.
- Almost all underground work requires excavating in road or footpath.
- Increased Traffic Management Costs.

1.4 Regions around New Zealand will be affected by these or similar issues to a greater or lesser degree. To have all regions restricted to a handbook value may not reflect the true replacement cost of a network. We believe that it would be appropriate for there to be an allowance not necessarily in the replacement cost section but in the multipliers to reflect the regional cost differences between networks.

- 2.5 This may give rise to the issue of how to ensure a multiplier of this nature is applied fairly across the industry. As all ODV valuations require auditing, the electricity network could be required to demonstrate to the auditors satisfaction real differences between ODV Handbook replacement costs and actual replacement costs.
- 2.6 Networks undertaking capital expenditure must carefully weigh their obligation to maintain supply and reliability against their inability to earn an appropriate rate of return on that capital expenditure through the inability to reflect full value in the ODV. In the case of NEL, the company has placed on hold a programme to complete undergrounding of the entire network because of the inability of the shareholders to achieve an appropriate rate of return for this investment.
- 1.7 The denominator in the statistical ROI calculations is substantially the average value of system fixed assets at ODV value. To have the true costs of installation for NEL included in the ODV handbook would increase NEL's overall ODV to a more realistic level as presented in previous submissions to the Commerce Commission. ROI is overstated when ODV undervalues network investment.
- 1.8 The present ODV Handbook also limits the level of cost which can be capitalised where overhead reticulation is converted to underground reticulation and where additional cables or capacity are being located underground. This is a disincentive to investment and not at all in the longer-term interests of consumers.
- 2.9 ODV concerns here relate to:
- The "Greenfields" requirements in the current Handbook, whereby cables laid in the same area at different times (often 10-20 years apart) must be valued as if there was only one trench dug for these cables.
 - The unreasonable requirement that plant whose life exceeds the standard life for that asset has no value (in ODV terms), notwithstanding it is still being used for the purpose it was constructed to serve. This encourages networks to replace assets for economic reasons rather than for security of supply reasons. It is suggested that assets that are older than the asset life as specified in the handbook be assigned a residual life to reflect the asset still in use on the network where it can be demonstrated that these assets are still in good operational condition.

We thank the Commission for the opportunity to comment on the Paper, and would welcome further discussion with the Commission on the points raised in this letter.

Yours sincerely

Phil Goodall
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