

9 February 2004

Network Performance Group
Commerce Commission
P O Box 2351
WELLINGTON

Dear Sir / Madam

Submission on Draft ODV Handbook

Meridian welcomes the opportunity to make submissions on the Draft ODV Handbook. Meridian supports the requirement for consistent application of a valuation methodology by natural monopoly electricity lines businesses and transparency, especially with respect to valuation assumptions.

Meridian notes submissions on the draft ODV Handbook should be made on the basis that ODV will be used for the opening regulatory valuation of system fixed assets and that the Commission is indifferent as to whether lines businesses consistently apply ODV or DHC on an ongoing basis. Meridian submits that lines businesses that adopt DHC should be required to implement a valuation methodology determined and published by the Commerce Commission. Meridian is also concerned by the impact on prices charged by lines businesses of a change in valuation methodology and how the Commerce Commission will account for this under its control threshold regime.

Asset Management Plan

Meridian suggests the Commerce Commission consider if further information should be required in the Asset Management Plan to reflect the information the Commission is seeking to demonstrate compliance with the consumer engagement criterion under the targeted control regime. Further specification of what the Commission is looking for in this regard would assist retailers / customers as well as lines businesses.

Economic Value test

Application of an economic value test is an integral part of determining the Optimised Deprival Value of lines companies fixed assets. The Commission highlights the significance of this test in its own introduction to the draft Handbook (paragraph 1.9).

Meridian is concerned by the change in application of the Economic Value (EV) test whereby "the Commission reserves the right to require an EV test to be applied in situations where it considers that a valuation prepared in accordance with this handbook may materially exceed the economic value".

Meridian submits the Commission is likely to be in a position of information asymmetry. The Commission could be expected to be less informed than the lines business doing the valuation about whether an EV test should be applied. Further, the lines business can be expected to avoid doing an EV test if that is to its advantage.

Further, Meridian queries what is meant by "materially exceed"? Is this going to be defined by the Commission?

The current ODV Handbook states that

“System fixed assets are valued at their economic value when it would not be possible for them to earn sufficient long-run profits to provide an appropriate return on the ODRC of the assets.”

While the report by Parsons Brinckerhoff Associates states that EV adjustments to 2001 valuations resulted in a total writedown of asset values of less than 0.25%¹, prices charged by lines businesses are calculated by applying an adequate return to the valuation of system fixed assets. Meridian would be concerned if the valuation of system fixed assets increased, and thus prices, as a result of there being less focus on the economic value of a lines business fixed assets.

If you have any queries please contact me, or Mary Ann Mitchell (DDI 04 381 1380).

Yours sincerely

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¹ Parsons Brinckerhoff Associates Draft report prepared for the Commerce Commission “Development of a Handbook for Optimised Deprival Valuation of system fixed assets of Electricity Lines Businesses”, 23 December 2003, Section 7 Page 21