



SUBMISSION by NORTHPOWER

to the

INDEPENDENT PRICING and REGULATORY
TRIBUNAL OF NSW

PRICING OF CAPITAL CONTRIBUTIONS TO
ELECTRICITY **NETWORKS**

1 May 2000

CAPITAL, CONTRIBUTIONS

NorthPower supports the views expressed in the **IPART** discussion paper that capital contributions need to be considered in the light of an overall **pricing** regulatory **framework**.

In **particular**, the arrangements need to be consistent with the setting of revenue caps and with the principles and key issues espoused in the Tribunal's discussion paper for efficiency, equity and simplicity.

NorthPower participated in the discussions on the Capital Contributions Working Group ("CCWG") and the implementation guidelines. These documents incorporate the philosophy that **locational** signals **are** essential for efficient investment and **for** the equitable allocation of costs between customers.

The key philosophy of the CCWG was that Distributors should **contribute** to the costs of new connection in **accordance** with the future revenues expected to be derived **from** those customers, Network prices would provide contributions towards equivalent levels of investments for every customer.

The Economic Test developed by the CCWG ensured the appropriate relationship **between tariffs** and customers' **contributions** towards new connections.

Difficulties with Current Capital Contribution Determination

NorthPower has been particularly outspoken in regard to the existing capital contribution arrangements which potentially allow customers who will share new network **infrastructure** to receive these assets for **free**, paid for by other customers through **general** tariffs.

NorthPower has received a number of applications over the last few years which have resulted in substantial distributor investment which was not paid for by those individual customers. This removes the price signal from those customers and does not allow adequate ownership of the investment by the customer. It is **NorthPower's** view that customers should be made aware of, **and** accountable for, the **net** costs they impose as a result of their connections to the system, This is consistent with the Economic Test approach recommended by the CCWG. To gain some appreciation of the magnitude of **NorthPower's** exposure to shared asset new connection investments, **there** are some **15,000** rural properties across our area that do not currently have connection to the network. Based on average cost of connection for remote customers this would amount to **\$400M** to connect these customers. **If** they **all** connected, averaging these **costs** across the projected volume of sales means that average prices would need to **increase** by 25%.

Limiting distributor exposure to connection costs based on a comparison with stand-alone systems has proven to be a difficult concept to apply in practice. The cost of a **stand-**



alone system varies dramatically in relation to the level of reliability they deliver, Whilst basic stand-alone systems supplying a limited number of domestic appliances could cost as little as say, \$15,000. In order to achieve levels of reliability commensurate with urban grid connected customers would cost up to \$60,000,

It would not be economic for the distributors to invest **these** levels of expenditure for customers on domestic tariffs where the annual network revenues are around **\$350pa**. It should be noted that the rural cost of supply for most **rural** customers would constitute the average revenue they contribute, based on current **tariffs**.

NorthPower has in a couple of recent cases offered groups of customers specific prices which reflected **the** costs of connection, **This is consistent** with the **comments** in the Tribunal's discussion paper that states that "in some circumstances, cost **information** provided through network charges may prove to be **more** effective in achieving the efficient allocation of network investment." **NorthPower recognises** that specific location **prices can** deliver appropriate **signals** for investments. These can be administratively **complex** over time as new customers connect or load **requirements** change.

Other Options

Option 3, as described in the discussion paper, would remove the major problems experienced by NorthPower under the present determination.

Under the CCWG report the concept of a 'dominant load' is recommended when looking at augmentation costs, **NorthPower** would be concerned that under option 3 the responsibility for augmentation **costs** would rest with **the** distributor and that these costs would be recovered through network tariffs,

Major dominant spot loads such as mines, irrigation loads and food-processing industries can impose **substantial** augmentation requirements, which relate predominantly to their specific load,

NorthPower is concerned that this approach would remove the economic pricing signal and result in an increase in average prices.

Option 4 also addresses the major problems **experienced under the present determination and recommends the use of network charges** to send pricing signals for uneconomic augmentations,

NorthPower is concerned that in conjunction with a reimbursement scheme the use of specific network tariffs would be administratively **complex**.

NorthPower's Preferred Option

A review of interstate approaches to capital contributions has been included in the **IPART discussion** paper.

In each other state the costs associated with augmentation are included in the customers capital contribution and most states appear to have developed a capital **contributions** policy based on **the** commercial viability of the customer.

The **use** of an economic test that identifies the existing distributor contribution to assets and allows a similar level of assets for all connecting customers is equitable and provides efficient pricing signals. To carry out **an** economic test for all new customers would however be complex and confusing.

NorthPower would prefer Option 2, however, would support the adoption of a simplified economic test as described in the **IPART** discussion paper.

A menu approach

It is important that the capital contribution policy is consistent throughout NSW.

Previous capital contribution policies which were **different** between distributors, resulted in **uncertainty** and **confusion**. To be equitable the basis of the policy should be the same between distributors for customers, developers and contractors.

The use of the simplified economic test would provide the platform for a common approach, which would be transparent and relatively simple to administer.

NorthPower would not favour the use of "a menu approach" and believes that **such** an approach will result in **confusion** and complaints,