

wellington  
electricity™



## **Customer Contribution Policy**

Pursuant to:

Electricity Distribution Information Disclosure Determination 2012 (Clause 2.4.6)

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## Introduction

The purpose of this document is to disclose a description of Wellington Electricity Lines Limited's (we\*) policy for determining customer capital contributions in accordance with the *Electricity Distribution Information Disclosure Determination 2012*, clause 2.4.6.

## 1. Background

we\* is a supplier of electricity lines function services and is regulated by both the Commerce Commission and Electricity Authority.

### Tariffs are set by the Commerce Commission

we\* is a regulated supplier of electricity lines function services and as such is subject to price control under Part 4 of the *Commerce Act 1986*. Specifically we\* is currently subject to the Commerce Commission's *Electricity Distribution Services Default Price-Quality Path Determination 2012*.

A Default Price-quality Path (DPP) Determination is made by the Commerce Commission every 5 years based on a forward looking model that forecasts we\*'s future capital and operating expenditure (see below). The forecast of future capital expenditure included in the Commerce Commission's building block model is net of we\*'s forecast capital contributions.

The DPP determination specifies the maximum weighted average prices we\* can charge customers over the 5 year period.

### Capital and operating expenditure

we\*'s operations are focused on maintaining the existing high levels of safety, reliability, service and performance of the network assets that we\* provides to its customers. The types of expenditure that we\* incurs are listed below.

Capital expenditure	Operating expenditure
Consumer connection	Service interruptions and emergencies
System growth	Vegetation management
Asset replacement and renewal	Asset replacement and renewal
Asset relocations	Routine and corrective maintenance and inspection
Reliability, safety and environment	System operations, network support and business support

Any investment that is not included in the capital expenditure forecasts used by the Commission to set prices for the 5 year period is therefore not recovered by we\* through the tariffs charged to customers during the 5 year period.

### Return on investment

Under the DPP determination we\* earns a Weighted Average Cost of Capital (WACC) return on the specified forecast level of investment and its existing regulated asset base. Any customer funded assets (capital contributions received by we\*) are excluded from we\*'s regulated asset base to ensure that we\* does not include this investment cost in its future tariffs as it has already been paid for.

we\* capital contributions policy covers the following matters:

- **Section 2 – Customers’ contributions**

- **Section 2.1 – Customers’ contributions:** details how the customer contribution is calculated depending on the nature of the assets and the size of the project.

- **Section 3 - Other charges**

- **Section 3.1 - Network connection / disconnection fee:** details the network connection /disconnection fees for those activities associated with any augmentation of the network that can only be provided by we\*;
- **Section 3.2 - Headworks fee (marginal cost of existing network reinforcement to meet customer price/quality requirements):** details the charges that are levied to address augmentation to the shared network required due to new customer connection requirements which include capacity and security of supply;
- **Section 3.3 - Cost reapportionment for shared assets:** details the current cost sharing process; and
- **Section 3.4 - Recoverable costs for damage to existing works:** details when we\* is able to recover costs from third parties.

- **Section 4 - Pricing principles**

## **2. Customers’ contributions**

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Within the electricity industry, it is standard business practice for distribution businesses to secure contributions from customers towards the cost of carrying out customer initiated augmentation<sup>1</sup> works that are not recovered through standard lines function services charges (tariffs). This ensures other customers remain cost neutral from the new connection.

The alternative process is to have no customer contribution for new works and all existing customers face an increase in lines function services charges to recover new connection costs of the new connection. we\* consider that the “causer pay” approach is an acceptable practice so that existing customers can maintain standard charges.

we\* requires a capital contribution when the cost of the works will not be fully recovered through ongoing tariffs and/or requires expenditure that is not compensated for (through existing tariffs) under the DPP determination set by the Commerce Commission.

Customer contribution arrangements are entered into between we\* and the customer(s) requesting the capacity required for their connection and the security of supply from the network. The customer contribution represents the amount paid by a customer to contribute to the cost of work necessary for the customer to obtain a supply of electricity at the price and quality choices they determine. For example, the contribution could relate to additional assets necessary for the customer to connect to the network. Examples of the additional assets are:

- Overhead lines;
- Underground cables;
- Pillars;

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<sup>1</sup> Augmentation means either new works to the network and/or works to extend the network.

- Pits;
- Switchgear; and
- Transformers.

It is normal practice for we\* to undertake all of the work in accordance with the technical standards using approved contractors. we\* may, at its discretion, provide prior approval for a customer to select an independent contractor to undertake **some** of the work based on pre-approved terms and conditions. For example trenching in a new subdivision can be performed by an external service provider based on the appropriate technical standards and certification of the resultant work. we\* will charge a fee (if required) to oversee / review the work undertaken by the external service provider as we\* needs to ensure the integrity of the network is maintained (refer to section 3.1).

The calculation and methodology for determining the amount of a customer contribution that is required to fund the capital cost of new works and augmentation is described in section 2.1 and is based on the size of the project. we\* will provide quotations based on the optimised cost of the assets required. If a customer requests capacity that exceeds the optimised level (e.g. spare capacity) of the asset, the additional cost will be charged to the customer.<sup>2</sup> Likewise if the customer requests high capacity and security and subsequently downgrades their connection requirements, then we\* may seek capital recovery of the stranded assets from the customer if their tariff does not provide an adequate return on the assets employed.

**Even though a customer contributes to the augmentation works, the assets that result from the works are owned and maintained by we\* and not the customer.**

## **2.1. Customers' contributions**

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we\*'s capital contribution policy requires that the customer contribution is received before works commence. In some limited circumstances, we\* may, at its discretion, provide prior approval for the customer contribution to be received subsequent to work starting on site. However, no livening will be permanently provided until all contributions have been received and the customer has a Retail contract for electricity supply.

The customer contribution is calculated in different ways depending on the size and complexity of the project. we\* applies four different project categories to calculate the capital contribution required from the customer, which are listed below.

we\* retains the discretion to select the project category that is applied to the customer. An indication of how we\* expects to allocate projects to categories is outlined below.

- **A – “Standard” pricing** – residential connection or residential sub-division
- **B – “Medium” pricing band** – commercial sub-division (including multi-floor high rise) and single connection via dedicated substation less than 1.5MVA
- **C – “Complex” pricing band** – where neither “standard” or “medium” pricing bands are appropriate to the circumstances of the customer
- **D – “Relocations” pricing band** – where the customer requests a relocation of we\*'s assets

The method for calculating the customer contribution for each project category is described below. In addition to the customer contribution calculated below, other charges will be applied where applicable (refer to section 3).

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<sup>2</sup> we\* does not have a standard schedule of capital contribution charges.

**A. “Standard” pricing** – residential connection or residential sub-division

Developer/owner share of connection costs	Ongoing line charges
Up-front full value of the project costs plus headworks fee (if applicable) less \$750 <sup>1</sup> per lot.	Published tariffs.

The \$750 per lot discount represents we\*'s estimate of average incremental revenue less average incremental costs.

1. Subject to the following conditions:

For clarity, for a rural connection requiring a new or upgraded transformer the customer will not be entitled to the \$750 per lot discount as the transformer cost will be met by we\*.

For new connections supplying low load applications, we\*'s discount may not apply. The threshold required for this discount is at least that of a standard residential load (typically >3kVA ADMD).

When a customer requests a supply upgrade from single to three phases they shall be entitled to we\*'s contribution of \$750 where the load increase would exceed a typical 63amp new connection.

Where the supply directly connects to a customer switchboard, which then supplies multiple properties (e.g., apartment block) the customer is only entitled to a single contribution of \$750 from we\*.

In the case of a larger installation (over 200kVA) we\* may choose to negotiate individually with the developer/owner and in this case the customer contribution will be calculated either under the “Medium” or “Complex” pricing bands.

**B. “Medium” pricing band** – commercial sub-division (including multi-floor high rise) and single connection via dedicated substation less than 1.5MVA

Developer/owner share of connection costs	Ongoing line charges
Up-front full value of the non-recoverable project costs and headworks fee (if applicable).	Published tariffs.

Recoverable costs – are costs that can be recovered through ongoing tariff revenue and/or assets that can be re-deployed or otherwise optimised by we\* if the customer no longer requires the extra capacity. For example, the cost of transformers and HV switchgear where there is sufficient capacity demands for them to be redeployed elsewhere within the network.

Non recoverable costs – are all other costs including installation costs, project management costs and assets that cannot be recovered, redeployed or optimised by we\* if the customer no longer requires the capacity or the lines charge does not recover capital investment of connection or headworks assets.

### C. “Complex” pricing band

The project is classified in the “complex” pricing band if a customer requests a new connection where, the pricing requires non standard terms and conditions and in we\*’s opinion:

- i) the customer represents an unusual credit risk; or
- ii) the customer wants to reserve future network capacity; or
- iii) there are unusual asset ownership or demarcation issues; or
- iv) the customer and/or we\* wish to contract to additional services; or
- v) the site to be connected has unusual locational or security issues; or
- vi) the connection relates to a commercial subdivision (including a multi-floor high rise building) and single connection via a dedicated substation 1.5MVA and above and high voltage connections.

Developer/owner share of connection costs	Ongoing line charges
Contributions are calculated using a net present value (NPV) model using the formula below.	Case-by-case negotiated non standard contract based on complexity, credit risk, additional services etc.

Customer contribution = total NPV of the initial costs + incremental costs (IC) + other charges - incremental revenue (IR). The model inputs are described in the following table.

Input	Input detail
Initial costs	Up front full value of the directly attributable project costs.
Incremental costs	<ul style="list-style-type: none"> <li>• <b>Transpower transmission charge</b> - using the customer’s expected usage and the applicable Transpower transmission charges.</li> <li>• <b>Maintenance costs</b> - directly relating to the project.</li> <li>• <b>Headworks fee (marginal cost of reinforcement)</b> - charges that are levied to address augmentation to the shared network required due to a new customer connecting (refer to section 3.2 for further details on this charge).</li> <li>• <b>Tax</b> - incremental revenue less initial and incremental costs and other charges multiplied by the tax rate.</li> </ul>
Other charges	<ul style="list-style-type: none"> <li>• <b>Excess demand charge</b> - payable, at we*’s discretion, if demand exceeds contracted capacity. The quantum of the charge will vary with connection and relevant network asset utilisation and value.</li> <li>• <b>Termination charge</b> - takes the form of a customer bond or up-front contribution and is set at the total value of the connection project. This charge is only applied at term, or at early termination, of the contract. It covers we*’s risk relating to the connection’s new investment costs. The Termination Charge does not attract an annual CPI adjustment. The Termination Charge is reduced at each successive contract term renewal based on “straight line” project cost amortisation. The Termination Charge applicable to successive renewals will be the straight line reduction value applicable at the time of Agreement renewal execution.</li> <li>• <b>Reconnection charge</b> - applicable charge for reconnection to the Distribution</li> </ul>

Input	Input detail
	Network. <ul style="list-style-type: none"> <li>• <b>Capacity change request fee</b> - this amount reflects we*'s estimated actual administrative costs in determining availability and terms on which excess capacity would be made available.</li> </ul>
Incremental revenue	Revenue using the customer's expected usage and the applicable negotiated prices.

The NPV is calculated over the average expected life of network fixed assets using the estimate of vanilla WACC (75<sup>th</sup> percentile estimate) set by the Commerce Commission for the relevant DPP regulatory period.

#### D. "Relocations" pricing band

The customer contribution is classified in the "relocations" pricing band if a customer requests a relocation of we\*'s network assets. For example if a customer requests we\* to relocate a pole on their own private land to a new alignment or to transfer overhead lines to underground cables.

Developer/owner share of relocation costs	Ongoing line charges
Up-front, full value.	Published tariffs.

Where it is technically and legally possible for we\* to relocate network assets at the request of a customer, then all costs incurred will be charged to the customer.

In the case of a third party owned pole (e.g. Telecom or public transport overhead network) that supports we\*'s assets and is being relocated by the third party, then the third party pays for the cost of relocating the pole and we\* pays for the cost of relocating we\*'s assets.

we\* may charge on a case by case basis the customer for the book value of the disposed assets if the existing assets are not utilised in the relocation nor have a remaining life that warrants economic reuse of the asset.

For overhead assets being transferred underground, these projects are typically considered when the remaining overhead asset life has expired. Councils will pay all costs for the underground conversion project, with we\* making a contribution equal to the apportionment of the replacement cost for the affected overhead line section.

### 3. Other charges

Other charges that may be applicable are listed below.

#### 3.1. Network connection / disconnection fees

Network connection / disconnection fees are for those activities associated with any augmentation of the network that can only be provided by we\*. Augmentation may form part of the connection / disconnection services we\* provides to a customer to allow the supply of electricity from we\*'s distribution network to an electrical installation of the customer. The fees can be classified into two components:

- Project fees; and

- Other fees and charges.

The project fee is used to recover costs in relation to preparation of the Offer for Network Connection Services including network planning, preparation of the design and associated administration costs. The amount of the fee will differ depending on the nature and the size of the project. If the project goes ahead the project fee is included in the initial costs in the customer contribution calculation (refer to section 2.1).

The project fee is non-refundable (irrespective of whether the project goes ahead) and is paid when the request is made for an Offer for Network Connection Services.

Other fees may be levied when we\* is required to perform work that is not covered by the customer contributions or project fee. Such fees generally arise where construction work is undertaken by an external service provider.

### ***3.2. Headworks fee (marginal cost of reinforcement)***

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The headworks fee (marginal cost of reinforcement) is a charge levied to the new customer connection to address the augmentation to the existing network to meet the capacity and/or security of supply requested by the customer which is not available from the existing network.

Specifically, there are network areas which can become capacity constrained based on the new connection demand or security of supply requirements. To manage the new load demand, the existing network needs to be strengthened with a larger capacity infrastructure. The customer making the new connection will be required to pay an appropriate proportion of the capacity reinforcement works.

we\* will charge the headworks fee on the “Residential” “Medium” and “Complex” pricing band customers where existing network capacity becomes constrained from a new connection. The headworks fee is included in the NPV model of the “Complex” pricing band refer to section 2.1C.

we\* will determine, on a case by case basis whether the headworks fee is required for other network areas based on scale. Headworks fees may include augmentation at the substation level or investment in a new substation for large customer load requirements and may also result in higher transmission charges.

### ***3.3. Cost reapportionment for shared assets***

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we\* may at it's discretion, employ on a case-by-case basis a process for re-apportioning the costs of a customer funded network extension that is subsequently connected to by other customers within a defined period. The reapportionment will be on a pro-rata basis and subject to depreciation. Any payment by the new connecting customer will be made to we\* and we\* will make a payment to the customer who funded the initial works. we\* will determine the reapportionment and payment process.

### ***3.4. Recoverable costs for damage to existing works***

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we\* is required from time to time to perform remediation work on its assets to ensure public safety and continuity of the supply of electricity following an adverse event which impacts the resilience of the asset (e.g. repair and relocation of assets. Where damage has been identified as being caused by a third party, we\* will recover such costs from the third party responsible for the damage or loss.

Recoverable works include:

- Restoration of damage, including theft or loss, to we\*'s supply network and associated property (for example a pole hit by a car or damage caused to a we\* vehicle); and
- Relocation of we\* assets as requested by third parties and outlined in section 2.1D above.

#### 4. Pricing principles

The Electricity Authority's Pricing Principles are contained in the Distribution Pricing Principles and Information Disclosure Guidelines 2010. we\* understands that Pricing Principles consist of well accepted, high level principles and were introduced on a voluntary compliance basis.

Where relevant, we\*'s customer contribution policy is consistent with the pricing principles for the following reasons:

- Customer contributions are based on incremental costs and discourage cross-subsidisation from existing customers for new customer connections;
- Customer contributions are responsive to the circumstances of the customers and are calculated based on the capacity required by the customer, the security of supply required by the customer, the level of available capacity, security of the present network configuration and the impact on upstream investment costs;
- Customer contributions are recovered when the cost of the works will not be recovered through ongoing standard tariffs and/or requires expenditure that is not compensated for under the relevant DPP determination set by the Commerce Commission; and
- The customer contribution policy is transparent and the impact on stakeholders is considered when setting / updating the policy.

The following table sets out the Electricity Authority's Pricing Principles.

<b>Pricing Principles</b>	
(a)	Prices are to signal the economic costs of service provision, by:
(i)	Being subsidy free (equal to or greater than incremental costs, and less than or equal to standalone costs), except where subsidies arise from compliance with legislation and/ or other regulation; and
(ii)	Having regard, to the extent practicable, to the level of available service capacity; and
(iii)	Signalling, to the extent practicable, the impact of additional usage on future investment costs.
(b)	Where prices based on 'efficient' incremental costs would under-recover allowed revenues, the shortfall should be made up by setting prices in a manner that has regard to consumers' demand responsiveness, to the extent practicable.
(c)	Provided that prices satisfy (a) above, prices should be responsive to the requirements and circumstances of stakeholders in order to:
(i)	Discourage uneconomic bypass; and

<b>Pricing Principles</b>	
(ii)	Allow for negotiation to better reflect the economic value of services and enable stakeholders to make price/quality trade-offs or non-standard arrangements for services; and
(iii)	Where network economics warrant, and to the extent practicable, encourage investment in transmission and distribution alternatives (e.g. distributed generation or demand response) and technology innovation.
(d)	Development of prices should be transparent, promote price stability and certainty for stakeholders, and changes to prices should have regard to the impact on stakeholders.
(e)	Development of prices should have regard to the impact of transaction costs on retailers, consumers and other stakeholders and should be economically equivalent across retailers.