



Guide to Gas Capital Contributions

Effective October 2024



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1. Introduction

If your home or business connects, or wants to connect, to Powerco's gas distribution network, we may require you to contribute to some of the costs towards the design and installation of the gas assets. This payment is called a capital contribution or a customer contribution. This guide outlines when you may be required to contribute, the process that is followed and how the amount is calculated. If you need one of Powerco's gas pipelines to be moved, we may also ask you to contribute to the capital costs.

Powerco reviews its policy towards capital contributions annually and this guide is updated on the Powerco website (www.powerco.co.nz) after any changes are made.

If you have any questions about this guide or the process, please contact Powerco's Gas office on 0508 427 970.

This guide also contains information required under section 2.4.6 of the Gas Distribution Information Disclosure Determination 2012. Amongst other things, this requires disclosure of Powerco's current policy for determining capital contributions and how the amounts payable for any capital contribution is determined.

2. Definitions

The following terms are used in this guide and their meaning is provided below.

The Gas Hub is Powerco's gas customer team and they provide information to make it easier for people to connect to reticulated gas, via residential and commercial specialists. Contact the Gas Hub at 0508 427 482 or thegashub.co.nz/contact-us.

Customer Initiated Work (CIW) or Customer Work, means work to construct new assets that will form part of Powerco's network (and be owned by Powerco) and/or work to upgrade, alter or relocate existing Powerco assets for any of the following reasons:

- a) The connection of a new customer to Powerco's network
- b) The extension of Powerco's network into new subdivisions
- c) The upgrade of Powerco's network to meet the gas capacity needs for the purposes of: (a) or (b) above, or to meet the gas capacity needs of an existing customer where their load or capacity requirements have increased
- d) The moving, relocating, altering or removal of the existing Powerco network for an existing customer or a third party with an interest in the assets.

Customer Contribution is the amount of money a customer must contribute to the Customer Work to enable the work to proceed. This is often termed a capital contribution.

Gas Measurement System (GMS) means a combined meter and regulator, which is used to record the quantity of gas being supplied to a customer as well as to reduce the network pressure being supplied to the customer's installation.

Incremental Upgrade Assets means the assets upstream of the Customer Work that would be required to meet the capacity or security requirements for the incremental new load.

New Revenue means additional revenue to Powerco as a result of a new customer connection and/or an upgrade to an existing customer's load resulting in new revenue.

Powerco Investment means the amount of money Powerco is prepared to invest into the Customer Work. This is calculated given the future forecast returns from the development and aligned to Powerco's gas asset strategy.

3. Why does Powerco require contributions from customers?

Powerco's gas network is constantly changing as new homes and businesses connect to the network and existing consumers require new assets as their gas demand changes. To be fair to our current gas consumers, who are not changing their load, we sometimes require a contribution:

- When people need extensions or reinforcements to the gas network that will benefit them but no other users of the network
- When people want to connect to the network or change their load and this requires new assets to be built.

The principal objective of the contribution is to create a price signal to incentivise consumers to assess the cost effectiveness of connecting to the network or changing their load, versus alternative options that may be available to them. A secondary objective is to share costs reasonably equitably between customers that require new connections or capacity changes and existing customers that require no additional investment.

An alternative approach would be for Powerco to undertake the full investment and recover the additional costs from the customer as part of regular gas charges over a period of time. However, this approach is not generally practicable for the following reasons:

- The assets built are likely to have a long life (e.g. over 40 years) and it is not reasonable to expect consumers to be locked into a contract for this length of time
- In practice, charging arrangements need to be reasonably simple and consistently applicable to a large number of customers – it is not usually feasible to tailor charges to individual customers, unless they are very large
- How a new connection or new investment will be utilised in the future, and by how many parties, is not always known. In many cases it is not possible to make an accurate calculation of future cash-flows and the return on investment that should be recovered from an individual consumer.

4. What is the process for connection or works?

If you need a new connection(s), capacity change or want to move one of our assets, your first point of contact will depend on the amount of gas you (will) consume, or the size of the asset being moved.

If you are a residential consumer or a small or medium business, your first point of contact should be your gas retailer or the Gas Hub. A list of gas retailers is available at <https://www.thegashub.co.nz/get-connected/find-a-gasfitter-or-retailer>. You may also want to visit the Consumer NZ website <https://www.powerswitch.org.nz/> to find the best pricing plan for your circumstances.

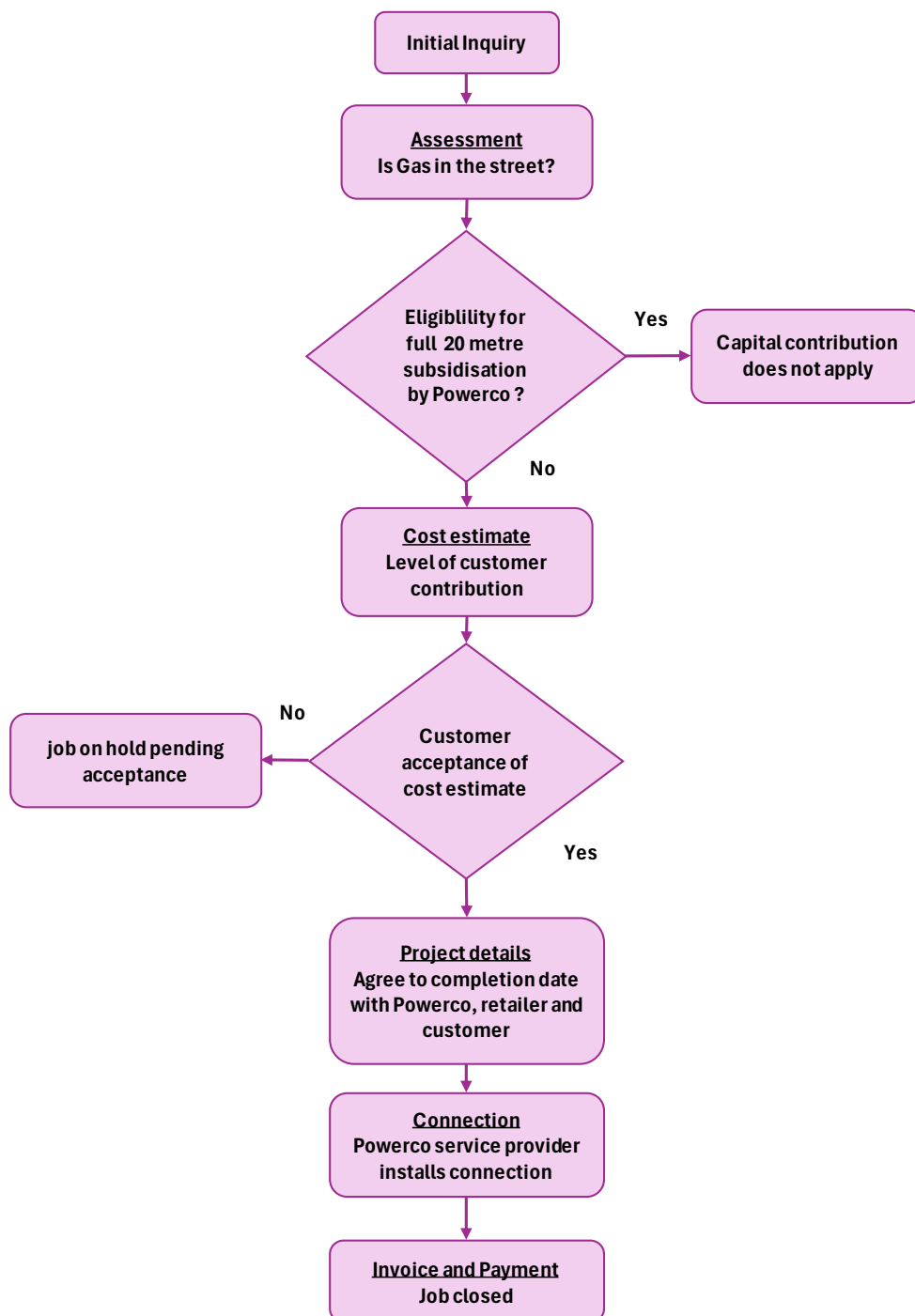
If you are a larger commercial customer, or require major works, you can contact Powerco directly on 0508 427 970, and a Powerco account manager will discuss options and facilitate the process for you.

4.1 New residential connection

Households seeking a new gas connection can contact a gas retailer or the Gas Hub. The Gas Hub (www.gashub.co.nz) can help make connecting to gas and installing gas appliances as easy as possible.

Once you have made an initial inquiry, Powerco will assess your circumstances and provide an estimate of any capital contribution required. The process is described in Figure 1.

Figure 1 Standard residential connection process



4.2 New commercial connection

If you are a small or medium business, or a new subdivision with five connections or less, you will follow the same process as residential connections.

If you are a large commercial customer, please contact Powerco on 0508 427 970 and a specialist account manager will contact you to discuss your connection requirements. They manage the process for you to make the connection as simple as possible. The process may take longer than a residential connection and may require more investigation by Powerco of the impact of your gas demand on the network. This may require a technical study or design work.

4.3 New commercial or industrial connections, extensions, reinforcements, moving of assets, or reticulating subdivisions with more than five connections

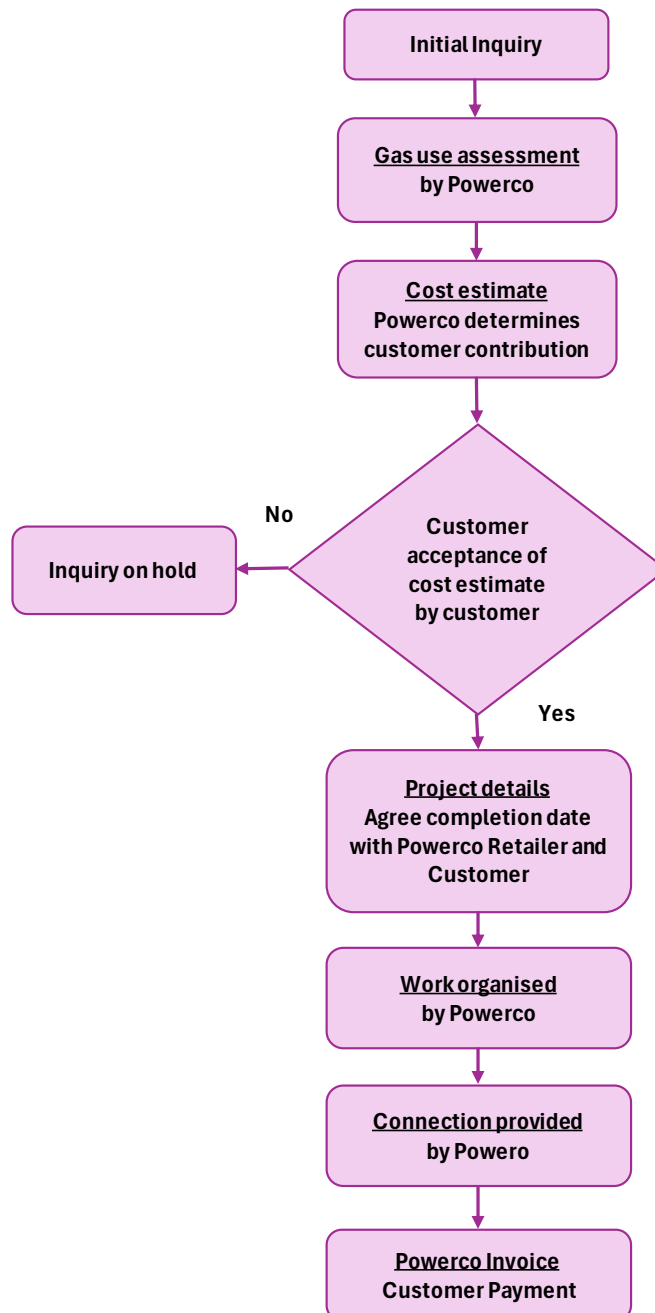
If you are an existing commercial customer, you may already have an existing account manager at Powerco. If you require a major change to your capacity or need Powerco's assets to be moved, contact the account manager in the first instance.

If you are a residential consumer who requires Powerco's assets to be moved, please contact your gas retailer. They will liaise with Powerco on your behalf.

If you are developing a subdivision greater than 5 connections, your surveyor or engineering company may contact Powerco on your behalf. If not, then contact Powerco on 0508 427 970.

This process is described in Figure 2.

Figure 2 Process for all larger connections or changes to assets



5. Can I use my own contractor?

In the interests of safety, only Powerco's approved personnel can undertake work upstream of the outlet of a gas metering system (GMS). This includes the capping of the riser valve. However, in certain circumstances retailers may arrange temporary isolation of a gas service by closing and tagging the service valve, including capping of the meter outlet if required, but this work must be undertaken by suitably qualified and appropriately certified gas fitters.

6. Will I have to pay a contribution and how will it be calculated?

This section describes the circumstances when you may have to pay a contribution towards work associated with a gas connection. When you apply to connect to Powerco's network, require additional capacity, or request other changes to the network, Powerco will follow the principles below to determine if you need to pay a customer contribution.

6.1 Principles

1. The level of investment Powerco makes into any Customer Work will be commensurate to the level of return that Powerco will expect to receive as a result of the work, such that:
 - a. New Revenue received from the new customer or existing customer upgrade will provide for Powerco to receive an adequate commercial return on the Powerco Investment into the Customer Work including the Incremental Upgrade Assets after considering the:
 - i. marginal increase in operating and maintenance costs
 - ii. marginal increase in overhead costs
 - iii. potential and/or commitment to gas connection uptake (new subdivisions)
 - iv. the risk of asset stranding.
 - b. The value of the deferment in renewal expenditure as a result of early replacement of existing assets involved in Customer Work will be determined and accounted for in the analysis.
 - c. The allocation of Incremental Upgrade Assets and cost components arising from the customer-initiated work.
2. New Revenue will only be accounted for once for the life of the Customer Work. Consequently, New Revenue for residential subdivisions will be assigned to the development of the reticulation for the subdivision. For commercial and industrial subdivisions, the New Revenue estimated to be derived from the development will be assigned to the development of the reticulation for the subdivision. If commercial/industrial load requirements subsequently exceed the capacity of the development, this will trigger a new Customer Work, with its own New Revenue attributable to that work.
3. The customer may be required to make a Customer Contribution to the cost of the Customer Work where the level of Powerco Investment does not cover the cost of the Customer Work and the Incremental Upgrade Assets. The Customer Contribution will not exceed the cost of the Customer Initiated Work.
4. Where the need for the Customer Work is shared among a number of customers, the Customer Contribution will be apportioned between those customers based on their projected annual consumption or load requirements

6.2 Contributions for new residential connections

Powerco's gas distribution pricing book and GMS pricing book describe the fees Powerco charges for modifications and the charges for new connections. For new connections, the contribution we require depends on the length of the service pipe, associated fittings required to complete the connection; the nature of the load being connected and the complexity of the job.

New residential customers can have the connection fully subsidised by Powerco if they plan to install gas water heating and/or gas central heating and the connection is up to 20 metres from the gas network pipeline to either the home or boundary, whichever is applicable. The customer will pay for the additional length above 20 metres. Even if the length of the new connection is less than 20 metres, occasionally it may be particularly difficult and expensive to install, and we may require a contribution to this cost from the customer. In some circumstances we may only be able to run a service pipe to a property's boundary. If the customer provides a compliant trench, then up to 40 metres may be subsidised by Powerco.

If you do not intend to install gas water heating or gas central heating, please contact the Gas Hub who will discuss your needs. If you require more than 20 metres of service pipe to reach your house gas meter position (as deemed by the gas rules), Powerco will calculate the cost by the method shown in Figure 3.

Figure 3 Residential customer contribution where more than 20 metres of service pipe to meter position

	Total Cost of Customer Work
Less:	<u>Powerco Investment (up to 20 metres subsidised from gas main to meter)</u>
=	Customer Contribution (for Customer Work)
Plus:	<u>GST</u>
=	<u>Total Quotation for Customer</u>

Example: A resident has moved into a new home without gas and wants to replace their electric hot water cylinder with instant gas water heating

The resident has checked www.gashub.co.nz and found there is a gas main in their area, they then contact The Gas Hub on 0508 427 482 to confirm that it is in their street and passing their property.

The resident and the Gas Hub determine that the house is approximately 15 metres from the gas service pipe in the road. As the resident is using the gas supply for water heating and the connection appears standard (no complexity such as rough terrain), Powerco will cover the cost to install the connection and no customer contribution is required.

6.3 Contributions for new commercial and industrial connections, extensions and reinforcements of existing connections and reticulating subdivisions of more than 5 connections

The customer contribution for commercial and industrial connections is determined by Powerco using a more detailed methodology. This methodology is also applied if you are an existing customer and need an extension or reinforcement of the network due to an increase in your gas demand, or are installing connections to new subdivisions of more than 5 lots.

The process for Powerco to calculate your contribution follows four steps:

- a) **Information collection and completion of analysis of impact on network of the new connection:** A range of information needs to be collected in order for Powerco to complete an analysis. This includes information such as the number of new connections needed, the type of gas meter(s) that needs to be installed, the expected life of the assets being installed, the length of service pipe required, if the network will need to be reinforced or extended, the forecast annual gas consumption of the connection(s), if there will be any salvage value if equipment is reused, and the expected life of the connection (including a risk assessment of the business).
- b) **Calculation of the total cost of the Customer Work:** Powerco determines the new assets and installation works required and this is costed based on Powerco's competitively tendered service provision contract. The salvage value of any equipment removed is deducted from this cost.
- c) **Powerco Investment:** The amount Powerco is prepared to invest into the Customer Work is calculated, based on the cost of the Customer Work and the forecast revenue from the connection and the life of the project. The revenue generated by the new connection is based on a defined period of time, determined by criteria Powerco use to assess a new connection.
- d) **Customer contribution level:** The customer contribution required is the amount required in addition to the Powerco Investment to meet the total cost of the Customer Work, as shown in Figure 4.

Figure 4 Customer contribution calculation

	Total Cost of Customer Work
<i>Less:</i>	<u><i>Powerco Investment</i></u>
=	Customer Contribution (for Customer Work)
<i>Plus:</i>	<u><i>GST</i></u>
=	<u>Total Quotation for Customer</u>

If your contribution is calculated on a minimum term of connection or minimum annual gas consumption, this will be specified in your contract with Powerco. Powerco may pursue breaches of contract as per our standard commercial operating procedures.

7. What if I disagree to the level of contribution?

If you have concerns or questions about the level of the contribution, please contact Powerco on 0508 427 970. We will respond to your query within ten working days of receiving the.

8. Consistency with Commerce Commission pricing principles

This section discusses the consistency of Powerco's approach to customer contributions with the Commerce Commission's pricing principles¹. This section should be read alongside Powerco's Gas pricing methodology², which has a wider discussion of Powerco's pricing approach.

The Commerce Commission pricing principles are based on economic theory. Powerco considers that we balance a complex mix of factors when considering how the principles should be applied in practice. Our view is that current policy around the application of capital contributions is fully compliant with the pricing principles.

Principle 1(a) – Prices are to signal the economic costs of service provision, by 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

Incremental cost

The term "incremental cost" is the cost of the next additional unit of production and "long run incremental cost" is the cost of providing an additional unit, including, if necessary, the capital cost of increasing the capacity of the network to enable an additional network to be provided. The long run incremental cost may be the present value of the cost of a future addition to the network.

There are two aspects of incremental cost that are relevant to a new connection or increase in capacity. First, there are the direct additional costs that result from the additional assets that are required to join the consumer to the network or expand capacity. Powerco's approach to capital contributions ensures that this cost is fully covered by the consumer through the contribution they are required to make and their regular gas charge.

Second, there is the incremental cost imposed on the existing network by additional load. This is difficult to evaluate in a meaningful way as much of the time it is zero, meaning that the next unit of gas can be distributed to a customer within the existing capacity of the network.

Occasionally the incremental cost will be a very large number, because the next unit of gas to be distributed would require additional capacity to be installed. The additional income Powerco derives from the increased consumption may be too low to justify the cost of providing the additional capacity. Our policy is to require the customer who initiates the need for the additional work to pay a share of the cost in proportion to the amount of capacity they require.

¹ The pricing principles are set in the Gas Distribution Services Input Methodologies Determination 2012 (section 2.5.2)

² Available on Powerco's website: powerco.co.nz/who-we-are/disclosures-and-submissions/gas-pricing

Standalone cost

Cross subsidisation exists when customers pay more for a service than the costs another firm would incur if it served those customers on a stand-alone basis. As Powerco's policy is that customers never pay more than the total costs of customer work, the contribution will always be below the stand-alone cost.

Subsidy free zone cost

As contributions are above incremental cost and below stand-alone cost, they will be in the subsidy free zone. Powerco's use of a cost of supply model also provides additional reassurance that this will be the case by allocating actual costs of supply to individual price categories. By regularly reviewing the costs of supply and revenue by price category Powerco ensures that our contribution requirements fall within the subsidy free zone.

Principle 1(b) and (c) – Prices are to signal the economic costs of service provision, by

- **having regard, to the extent practicable, to the level of available service capacity**
- **signalling, to the extent practicable, the impact of additional usage on future investment costs.**

These two principles essentially reflect opposite sides of the same coin, both requiring that prices should look to the future and be based on long run marginal costs. In essence, prices should be low where future investment is low (and spare capacity exists); and prices should be high where capacity is constrained and investment is needed. The criteria that Powerco take into account when calculating contributions ensures this principle is met.

Principle 2 – 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

The level of capital contribution directly relates to the cost of the work, and therefore is unlikely to lead to the under recovery of allowed revenues. There is no shortfall that needs to be made up through pricing having regard to consumers' demand responsiveness.

Principle 3(a) – Provided that prices satisfy principle 1 above, prices should be responsive to the requirements and circumstances of consumers in order to discourage uneconomic bypass

The main risk of bypass of the distribution network is large consumers opting to use a bypass gas network or choosing an alternative energy source. Powerco's practice is to offer non-standard pricing and individual account management to industrial and large commercial customers to address the risk of uneconomic bypass and to enable arrangements that are tailored to customers' needs. Powerco's approach to non-standard pricing includes taking into account customers' individual capacity and demand to ensure, to the extent practicable, that the price is cost reflective.

Principle 3(b) – Provided that prices satisfy principle 1 above, prices should be responsive to the requirements and circumstances of consumers in order to allow for negotiation to better reflect the economic value of services and enable consumers to make price/quality trade-offs or non-standard arrangements for services

For non-standard customers, Powerco offers a service more tailored to their individual requirements. Powerco continues to consult with these customers through one-to-one liaison with key account managers. This works well as large customers are usually familiar with the issues involved in price/quality trade-offs and strong relationships provide a firm foundation for discussing all aspects of quality and price.

Principle 4 – Development of prices should be transparent, promote price stability and certainty for consumers, and changes to prices should have regard to the impact on consumers

This capital contributions guide is published on Powerco's website, along with Powerco's gas pricing schedule, gas pricing methodology, gas pricing book, and versions of these documents from previous years for comparison.

The impact on customers of changes to the established allocation methodology is a central consideration in the pricing process, including capital contributions.

Powerco consults with retailers and other customers throughout the year to discuss all aspects of our pricing approach (including potential improvements). This provides a mechanism to enable customers to communicate any concerns they may have about the impact of prices on them. A description of this process is available on request from Powerco.

For standard residential connections, we have received feedback that defining the Powerco Investment as a maximum length (20 m) provides certainty. In reviewing approach to cost allocation and impact on customers we have therefore retained this approach. We have analysed the impact on customers of changing the amount of Powerco Investment and determined that 20 m offers reasonable stability and minor impact.

For non-standard customers, Powerco continues to consult with customers through one-to-one liaison with key account managers, which provides a channel for discussions of all aspects of quality and price.

