

26 February 2018



Mr Marcus Crudden
Director of Water
Essential Services Commission
Level 37, 2 Lonsdale Street
Melbourne VIC 3000

Dear Marcus,

Regarding – The Financial Modelling Treatment of New Customer Contributions Revenue

North East Water has historically included New Customer Contributions (NCCs) as prescribed revenue and therefore have included this item in tariff revenue to recover the determined Revenue Requirement. We acknowledge that this treatment is inconsistent with the approach preferred by the Commission. We note that we also offset NCCs against the Regulatory Asset Base consistent with the Commission's preferred approach. The following commentary outlines North East Water's proposed correction to this treatment.

Management have assessed the 8 year impact on the financial model based on the following changes;

- Removing NCC revenue from the recovery of the Revenue Requirement for the 8 years.
- Assessing the Deloitte's draft Expenditure review paper and only removing \$3,000,000 from administration expenditure relating to the implementation of Smart Metering. All other expenditure and capital proposals remain consistent with our Price Submission.
- Applying minor amendments to the original model based on ESC information requests.

8 Year Revenue Requirement	\$440,140,000
Revenue Recovered from Tariffs	\$430,860,000
Under Recovery	(\$9,280,000)
% of Revenue Requirement	(2.1%)

The North East Water Board met and discussed this item on Tuesday 20 February 2018 and endorsed the approach to under-recover on the total revenue requirement for the 8-year


Price Submission as submitted. In effect this will see the Corporation continue to meet its commitment to customers to constrain real price increases to 0.45% per annum.

The Board is comfortable that this 2.1% under-recovery (noting the model already has a tolerance for up to 1% under-recovery) can be managed internally and would not impact on our ability to deliver all of our customer outcomes and the capital delivery program.

North East Water's has had a long-term focus on the ability to generate strong cash-flows from operations, has delivered a financial position with low debt and the capacity to respond to any unforeseen financial challenges and opportunities. This has been recognised through the Corporation's AA credit rating — one of only a couple awarded throughout the Victorian Water Industry. It is from this strong position that North East Water believes it can accommodate this under-recovery proposal without any long term financial impacts or reduction in our capacity to respond to emerging opportunities and obligations.

Should you wish to discuss this proposal further please contact myself directly on [REDACTED] or by email [REDACTED]

Yours Sincerely



Anthony Hernan
Executive Corporate Services