

Your ref.

Our ref AH/lt 850/9

Contact: Andrew Hunt (03) 5434 1302

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Essential Services Commission
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Dear Sean

2008 Water Price Review – Guidance on Water Plans (Guidance)

I refer to the 2008 Water Price Review – Guidance on Water Plans document and wish to make some observations and request for clarifications in a number of sections of that report.

Our review of the document indicates that Guidance could be improved, in some areas to:

- *Minimise ambiguity.*
- *Give clearer guidance to staff in the businesses undertaking investment appraisals and prioritisation, and*
- *Facilitate consistent outcomes and therefore the ability to undertake meaningful inter-business comparison.*

Coliban Water has identified two specific areas where improvements could be made, being Service Outcomes (Chapter 4) and Capital Expenditure (Chapter 5 Section 3).

Our concerns and proposals together with examples that highlight the concerns are outlined below:

Section 4 - Service Outcomes

1. Regulatory and government obligations (sub section 4.2) is divided into 3 groups:

- *4.2.1 Statement of obligations*
- *4.2.2 Environmental obligations*
- *4.2.3 Water quality obligations*

The Statement of Obligations provides broad guidance to the business as to the whole of its modus operandi but does not provide for any specific measurable outcomes. Coliban Water would argue that everything it does is to comply with its Statement of Obligations.

As an example, the Statement of Obligations requires the business to:

“Manage risks to protect the safety, quality and security of supply”

Compliance with the Department of Health and Safety’s drinking water quality guidelines achieves this. Under the Guidance, Coliban Water could classify this as either Statement of Obligation or Water Quality Obligation.

Therefore, Coliban Water believes that the Guidance should refer to the Statement of Obligations as the overarching objectives of the business which require the Obligations and Service Standards to be achieved and to be used as a framework for a prudent business to set Additional Service Standards.

2. It is unclear as to whether a service outcome (not being an environmental, water quality or service standard outcome) is an Other Obligation (Section 4.2.4) or an Additional Service Standard (Section 4.3.3).

Some examples of these are:

Other Obligations vs Additional Service Standards

- OH&S requires Coliban Water to provide a safe working environment. There are specific OH&S based regulations in some areas that define the environment – expenditure to comply with these specific needs has a service outcome of Other Obligation – in other areas where Coliban Water establishes its own OH&S framework has a service outcome of Additional Service Standard.
- Coliban Water has set its own target for recycled water under the auspices of government policy. These would be classified as Additional Service Standard outcomes.
- Coliban Water, as a prudent operator, is considering adopting certain operating standards recommended by Water Services Association of Australia. Whilst these are empirical standards they are self-imposed and would therefore be classified as Additional Service Standards outcomes.

Coliban proposes that the distinction between Other Obligations and Additional Service Standards should be defined by:

Other Obligations: Legislation, regulation or government policy that has empirical targets

Additional Service Standards: Legislated or regulated obligations that do not include empirical targets

Government policy that has no empirical targets and for which the business has established self-imposed targets

Prudent self-imposed service targets

Section 5.3 Capital Expenditure

Section 5.3.1 identifies cost drivers as:

- Renewal
- Growth/augmentation
- Improved services
- Compliance
- Government contributions
- Customer contributions

Coliban does not believe that these are cost drivers, but are better classified as expenditure types. Cost drivers tend to be the overarching legislation or regulation requirement and would be better defined as the service outcome headings as in Section 4.

In attempting to apply these definitions to our capital program, Coliban believes that the classification of expenditures into cost drivers (expenditure type) is ambiguous.

- Renewal vs compliance

Coliban Water, in general, renews assets to ensure continued compliance with its Obligations/Service Standards/Additional Service Standards - it is a rarity for assets to be renewed without this driver. There is therefore ambiguity for Coliban Water in appropriately distinguishing between renewal and compliance (expenditure type). If the definition refers to the replacement of an existing asset as being a renewal this would not appropriately classify expenditure made to replace an asset solely to ensure compliance.

Coliban is currently preparing its capital expenditure forecasts for the next Water Plan. In the absence of clarity on this issue, we have provided the following guidance to our staff:

Cost driver definitions

- *Replacing a section of sewer main in an area where the currently defined Service Standard is achieved – Renewal.*
- *Replacing a section of sewer main in an area where the currently defined Service Standard is not achieved – Compliance.*
- *Installation of a standby pump to comply with a self-imposed standard - Compliance.*
- Improved services

Coliban makes investments where the targeted outcome is improved efficiency. This should be included in this cost driver (expenditure type).

- Government and customer contributions

Coliban is of the opinion that these are not cost drivers (expenditure types) but, where received, are subsets of other cost drivers (expenditure types) and should therefore be removed from the list. (Coliban recognises the necessity of being able to identify the levels of government and customer contributions for assets.)

A present example of the problems defining contributions as a separate cost driver is our Goulburn Campaspe Link project.

Coliban Water is anticipating receipt of a significant level of government contribution for its Goulburn Campaspe Link project.

If the definitions in the Guidance are adopted Coliban Water would record in its regulatory assets register 2 assets for each asset installed as part of the project; one asset would be given a cost driver (expenditure type) of government contribution and the second would have cost driver (expenditure type) of augmentation; in its financial assets register, a single asset record would be created for each asset installed.

In practice Coliban Water records the asset acquired as a single asset in both the regulatory and financial records with a cost driver (expenditure type) of augmentation and negative assets in the regulatory records representing the government contribution.

In the case of customer contributions the difficulty is even greater as a result of timing differences of cash expenditure and customer contribution which can be a number of years.

Coliban would propose the following clarification:

Renewals

Replacement/enhancement of facility/asset in a situation of current compliance with Obligations/Service Standards/Additional Service Standards to reduce the risk of future non compliance

Growth/Augmentation

Increase in the capacity of the facility/asset/process in response to increased demand

Improved service

Upgrading of service outcomes e.g. provision of potable water to communities receiving filtered water, provision of sewerage reticulation to an unsewered community
Expenditure to improve the efficiency of the business
Expenditure to increase the anticipated life of an asset

Compliance

Bringing a facility/asset that currently does not comply with Obligations/Service Standards/Additional service Standards into compliance


Contributions

Government and customer contributions should not be classified as cost drivers (expenditure types) but the Guidance must require the businesses to appropriately identify these contributions.

As we have already commenced work in preparing information for the Water Plan a prompt response to our issues raised would be appreciated.

Should the ESC find it beneficial we would be happy to discuss these proposals further.

Yours faithfully



Andrew Hunt
Executive Manager Business Services