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Mr Sean Crees  
Acting Director Regulation Water  
Essential Services Commission  
Level 2, 35 Spring Street  
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Dear Sean

**GIPPSLAND WATER'S RESPONSE TO 2008 WATER PRICE  
REVIEW CONSULTATION PAPER - DECEMBER 2006**

Thank you for providing the opportunity for representatives of the Commission to meet with Gippsland Water to discuss the *2008 Water Price Review Consultation Paper - December 2006* and to provide a written response.

As an overarching comment Gippsland Water would like to express apprehension at the level of uncertainty that water businesses are currently facing with the drought, the uncertainty with price review framework and the expectations of other regulators, about releasing to the public and engaging in widespread community consultation a document which is essentially committing water businesses for a 5 year period, 14 months prior to the commencement of that 5 year period.

Gippsland Water provides the following comments under each of the key headings contained in the Commission's *Paper*.

1. **Length of regulatory period and dealing with uncertainty**

- Gippsland Water conceptually supports a five year regulatory period, however given we have a national water crisis the level of uncertainty faced by water businesses is greater today than ever before.
- Gippsland Water agrees that businesses are in the best position to deal with the uncertainty associated forecasts and changes in priorities, however water businesses do not have all the mechanisms available to businesses operating in an open market environment to manage all demand and supply events.



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- The Commission needs to clearly articulate a process for businesses to detail major projects that may occur during the five year regulatory period, that have not been factored in to the revenue requirement, due to their potential impact on tariff, and the significant level of uncertainty associated with the implementation of the project. Gippsland Water is concerned that including projects with significant levels of uncertainty may increase tariffs unnecessarily. This process would also need to consider how to establish a trigger, that allows the revenue requirement to be included, and tariff adjusted should the project proceed during the regulatory period.
- Whilst Gippsland Water acknowledges the Determination provides for catastrophic events, Gippsland Water still believes that the current clause on unforeseen events within the Determination should be broadened to include unforeseen events outside the control of businesses, such as natural disasters and acts of terrorism. Clear triggers should be established to ensure the impacts of these events are significant.
- Materiality threshold should be linked to the annual operating expenditure that relates to the unforeseen event, not total revenue.
- The materiality threshold does not clearly indicate whether it is a cumulative amount, or related to each individual event. Discussion with Commission Officers indicated that the intention was for a cumulative approach. This needs to be clarified.
- The Commission should give consideration to extending the price adjustment for variations in licence fees payable to regulators to include the mandatory audit costs directly associated with each of the regulators. Whilst the auditors are engaged directly by each of the businesses, they effectively work for the regulator because the water business has no control over the scope and the auditor needs to be approved by the Commission. If the regulators engaged the auditor directly, which Gippsland Water believes they should, these costs would be treated as a pass through.

## 2. **Service standards and GSLs**

- Gippsland Water does not support harmonising of operational service standard targets across businesses. Each business will have different priorities and operating environments and should be allowed to determine their own targets in consultation with their customers.
- Gippsland Water supports South East Water's suggestion that the Commission give further consideration to the relevance of including planned works service standards. If service targets are to be set for planned works they should not necessarily represent the last three years historical performance but rather the best customer outcome. Constantly striving for improved planned works service standards may result in some customers being faced with multiple planned works over a relatively short period of time to achieve a single outcome, whereas from a customer perspective a single event for a slightly longer duration could have received the same outcome.

- Customer consultation undertaken by Gippsland Water as part of updating the Customer Charter in 2005 didn't show any strong desire from customers for the introduction of GSL's, particularly when customers understood the cost of GSL's would be built into their tariffs. Gippsland Water's impression of the three Commission customer consultation meetings held in 2005 in Melbourne, Wangaratta and Traralgon (which Gippsland Water representatives attended), is that similar views were expressed.
- Gippsland Water is currently consulting with customers on GSL's for the 2008 Water Plan process.

### 3. **Assessing expenditure**

- Gippsland Water seeks clarification of the Commission's expectation in terms of the basis of forecast expenditure for 2006/07 and 2007/08 in the initial draft Plan. Discussion with Commission Officers indicated that businesses should reflect best estimates based upon current information, and should not base forecast expenditure on the benchmark estimates (adjusted for CPI) from the first price review. This issue needs to be clarified, and financial templates need to be reviewed where reconciliations to the first price review is currently factored in to existing templates.
- Gippsland Water seeks clarification from the Commission on how it proposes to treat expenditure identified in the 2005 Price Review as capital, however due to changes in accounting standards is now being treated as operational expenditure through water businesses accounting systems.
- Gippsland Water supports the need for businesses to continually seek productivity improvements however this does not automatically translate to cost reductions, but rather may result in improved customer service outcomes which are difficult to quantify, help assist businesses absorb larger than CPI price rises for key costs and managing the changing priorities due to drought response. Accordingly Gippsland Water does not support the Commission position of imposing an arbitrary 1% per annum productivity improvement on water businesses. Consideration should be given to allowing businesses to propose productivity gains, and demonstrate why such gains are realistic in nature.
- Gippsland Water supports the requirement to contain information on key projects within the Water Plan, however the Commission should allow businesses to determine the number of projects detailed within its Plan.

### 4. **Incentive mechanisms**

- Gippsland Water does not support the application of an efficiency carryover mechanism from the first regulatory period to the second period. Whilst Gippsland Water agrees businesses should continually strive for productivity improvements, the timing of achieving these improvements should not be influenced by financial decisions around who retains the benefit of the gain and for what period of time.

- The efficiency carryover mechanism outlined by the Commission seems appropriate for businesses which are regulated and profit driven, Gippsland Water questions their value for businesses which are not purely focussed on returns to shareholders. Regional urban water businesses are not profit driven businesses.
- If carryover mechanisms are introduced, will they include materiality thresholds/triggers?
- Gippsland Water does not support the introduction of an s-factor mechanism for water businesses. The theory of s-factor mechanism is potentially at odds with the price of water reflecting the true cost.
- Gippsland Water is a stronger supporter of competition by comparison with the regional urban sector. Performance reporting is an effective method of providing incentives to businesses to improve their level of service.

## 5. Pricing

- Gippsland Water seeks clarification on the Commission's position on the introduction of residential wastewater volumetric charge for water businesses who currently only have a single fixed tariff.
- Gippsland Water supports annual approval of prices as appropriate for third pipe schemes where groups of customers receive a relatively homogenous service.
- Gippsland Water supports pricing principles for large non domestic customers receiving unique recycled water services.
- Gippsland Water supports pricing principles stating prices must not exceed the full efficient cost of providing the service.
- The pricing principles in relation to recycled water currently seek to maximise revenue or recover cost. Gippsland Water questions whether the pricing principles at this time should encourage the use of recycled water rather than pure economic theory, given prevailing conditions.
- The majority of miscellaneous services provided by Gippsland Water are provided by a third party under contract which expires 30/6/07. Gippsland Water is currently in the market to renew this arrangement. If the Commission proposes to make any changes to Gippsland Water's current businesses processes associated with miscellaneous services this needs to be clarified urgently.
- The Commission needs to ensure that it doesn't create an unreasonable burden on water businesses in 2008 Water Plan on miscellaneous charges. They are not significant revenue generators.
- Gippsland Water supports standardisation of definitions relating to 'actual cost' and 'at cost'.
- Gippsland Water has concern that standardisation of fees and definitions may take too long for the 2008 Water Plan.
- Gippsland Water supports and currently provides customers with cost estimates before services are provided.
- Gippsland Water doesn't support the restriction of new miscellaneous charges to the commencement of each regulatory period.

## 6. Customer Contributions

- Whilst Gippsland Water would support increasing the cap on customer contributions to \$1,000 per lot for water and \$1,000 per lot for wastewater under the current operating rules, further clarification is required as to other changes proposed by the Commission in raising the new customer contribution from the current circa \$500 to \$1,000. Gippsland Water understands that currently an industry submission is being prepared and that Gippsland water is generally supportive of an industry approach in an effort to reach a satisfactory outcome.
- Gippsland Water doesn't understand why each business needs to clearly articulate what the proposed new customer contribution is, how it is calculated and identify the underlying pricing principles. Given in the first price review the Commission in its final decision determined the new customer contribution outcome why isn't Commission adopting a uniform approach in the 2008 Water Plan?
- Gippsland Water supports the current size criteria for classifying as either reticulation or shared as it provides clarity, is supported by developers and is simple to manage. The introduction of capacity as a criteria is far too complex to manage. Gippsland Water doesn't support a more complex criteria on the basis business and the "developer" community require more clarity, simplicity and consistency across water businesses, not less.
- Gippsland Water seeks further clarification on what is the Commission's position on water businesses making a contribution to upsizing of reticulation assets? This subject is not addressed in the consultation paper, but is practised by several water businesses, as a fair approach to reticulation and shared assets.
- Gippsland Water supports water businesses developing strategic development plans for major towns which include long term infrastructure requirements and estimated dates when locations will be serviced.
- Gippsland Water supports the development of high level principles to guide the estimation of bring forward periods and proposes the Commission facilitate an industry workshop to develop the principles.

If you require any further information please contact Mr Kevin Enguell, Manager Strategic Planning on telephone (03) 5177 4684 or Mr Tony Staley, General Manager, Finance and Regulation on telephone (03) 5177 4719.

Yours sincerely



John Mitchell  
**CHIEF EXECUTIVE OFFICER**