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Mr. Sean Crees
Acting Director Regulation (Water)
Essential Services Commission
Level 2, 35 Spring Street
Melbourne 3000

12 February 2007

Dear Sean

2008 Water Price Review Consultation Paper

Goulburn-Murray Water is responding to the ESC's request for feedback on key issues for the second regulatory period. A detailed response to the consultation paper is attached. Key issues for G-MW are:

Length of Regulatory Period and Dealing with Uncertainty

Goulburn-Murray Water supports the ESC's preference for a five year regulatory period providing that an appropriate mechanism is put in place to allow for unforeseen events on an annual basis.

G-MW is operating in a dynamic and changing environment due to Government water reforms (particularly the significant change in the national agenda), the impact of the worst drought on record and higher expectations of compliance with existing obligations, and Government policies and directives.

G-MW believes that the approach to dealing with uncertainty in the current regulatory period is too narrow and fails to recognize the high degree of uncertainty that exists in the rural water sector and that rural water businesses operate on a cost recovery basis with limited ability to absorb or reprioritise the cost of significant unforeseen events. In addition to changes in legislation and obligations, unforeseen events needs to include Government directions, drought, significant unforeseen asset management costs (e.g. water savings projects, changes in asset standards, major asset failures), customer supported changes in service standards and MDBC contributions or changes to MDBC arrangements under the Federal Government's proposal.

The level of uncertainty could be reduced with increased communication by stakeholders within the water sector of plans and expectations for the next regulatory period. This is one of the stated objectives of the regulatory approach and the Water Plan process. The ESC is encouraged to be more proactive and take a coordinating role to improve the level of understanding of the regulatory approach and the communication of stakeholder plans and expectations under its MoU's with various water sector stakeholders. The ESC should not manage this through applying a rigid regulatory approach on water businesses.

The regulatory approach should include a process each year for the Water Plan to be amended for unforeseen events within the regulatory period for implementation within the regulatory period and that the definition of 'unforeseen events' should be widened.

Materiality Threshold

G-MW supports the ESC's decision not to apply a materiality threshold to rural water businesses on the basis of limited flexibility to deal with unforeseen events due to low opening RAVs and the district based approach to pricing. It is expected that a materiality threshold will not be applied to rural water businesses for the next regulatory period.

Price Review Process

G-MW's Water Plan development process was discussed with the ESC during a meeting on 27 November 2006. At this meeting we outlined a process that schedules consultation with water services committees in May/June 2007 and the broader customer base from 1 July 2007 ie customer consultation would commence after submission of the exposure draft version of the Water Plan to the ESC. It was explained that the consultation has been rescheduled due to the difficulty in engaging with customers on important water issues and prices during a harsh one in one thousand year drought.

Further, it was requested that during the May/June 2007 WSC consultation period G-MW's draft Water Plan would not be released publicly, by G-MW or the ESC.

Greg Wilson has already given support to G-MW's approach providing that DSE was also supportive of the approach. We wrote to DSE on 5 December 2006 explaining G-MW's Water Plan development process and highlighting the consultation approach. To date DSE has not communicated any dissatisfaction with this approach. Accordingly our current work plans are now committed to this approach.

G-MW has now proceeded with its Water Plan development process as discussed last November 2006. We therefore expect continued support from the ESC and DSE that will ensure G-MW's draft Water Plan will not be publicly released until consultation with WSCs has been completed.

G-MW welcomes the involvement of the ESC during the public consultation phase of the process.

Yours sincerely

(Original signed by Trevor Ierino 12/2/07)

Trevor Ierino
EXECUTIVE MANAGER BUSINESS AND FINANCE

cc Russell Cooper, CHIEF EXECUTIVE G-MW

ESC 2008 Water Price Review Consultation Paper – G-MW’s Response

Length of Regulatory Period and Dealing with Uncertainty

G-MW supports a five year regulatory period provided that a mechanism is put into place to allow for unforeseen events on an annual basis and that the definition of “unforeseen events” is widened.

Halcrow highlighted in its review of G-MW’s expenditure for the current Water Plan that G-MW is operating in a dynamic and changing environment. The uncertainty is due to implementation of Government water reforms, the varied seasonal impact of the worst drought on record and increasing responsibilities to comply with existing obligations and Government policy and directives.

Due to this varied and high level of uncertainty, the definition for “unforeseen events” should be widened from just changes to legislation and Statement of Obligations (SoO), to include:

- Unforeseen significant asset management costs, eg:
 - Water savings projects:
 - Projects such as the Strategic Measurement Program (SMP) and Shepparton Modernisation have been identified and developed within 6 months. These projects have significant operating costs and may have RAV implications as well. The ESC accepted that the SMP project could not have been planned by G-MW when it amended its draft determination for the 2006 – 2008 regulatory period.
 - Changes in asset standards – changes in asset standards such as the Australian National Committee On Large Dams guidelines (as required by the SoO) will not result in a change to the SoO but may result in changes to asset management expenditure.
- Customer supported changes in service standards
- MDBC contributions/costs – The level MDBC contributions are determined by River Murray Water’s (RMW) annual costs which G-MW has no direct control over and annual negotiations with the Victorian Government. RMW costs are set on a year by year basis with approval by the Murray Darling Ministerial Council.

MDBC costs may change considerably under new arrangements being proposed by the Federal Government.

- Drought
 - The cost to manage the water distribution system during extreme dry conditions will be higher than during ‘normal’ conditions.
 - During extreme dry conditions (below 100% water right allocations) ‘dead’ water has in the past been pumped from some storages (with the support) from customers, examples are pumping Waranga basin, and pumping Buffalo dam.
 - The cost to manage unregulated streams and aquifers are significantly higher during drought conditions.

Materiality Threshold

G-MW supports the ESC's decision not to apply a materiality threshold to rural water businesses on the basis of limited flexibility to deal with unforeseen events due to low opening RAVs and the district based approach to pricing. It is expected that a materiality threshold will not be applied to rural water businesses for the next regulatory period.

Service Standards and GSLs

The core rural service standards are appropriate.

Harmonising service targets across rural water businesses would be difficult due to the specific characteristics of the infrastructure in each irrigation scheme and the involvement of customers in developing their own service levels.

Water Plan outcomes can be monitored by:

- Audit of Statement of Obligations on a cyclic basis
- Annual monitoring of service standards performance
- Annual business and industry performance reporting

GSLs are not appropriate for the rural water sector.

Assessing Expenditure

As previously acknowledged by the ESC and Halcrow during the review of expenditure for the current regulatory period, historical expenditure levels are not a reasonable indicator of future expenditure levels due to the dynamic and changing operating conditions that has existed for over ten years in the rural water sector. (Discussed in the 'Uncertainty Section').

Operating expenditure may vary year to year due various reasons that are not attributable to changes in legislation or obligations, e.g.:

- Implementing water savings projects

- Impact of drought – pumping dams, increased resource management, deferring expenditure

- Climatic conditions more generally – timing of rainfall events within the irrigation season may impact on demand and on the length of the irrigation season.

- Government directives –
 - Increased water resource management in the Diversions business under existing legislation and obligations, e.g. metering, management of unregulated water
 - Upgrade the Environmental Management System to meet the existing SoO
 - Storage perimeter land management to comply with various existing legislation
 - Bulk Entitlement loss management

- Improving OH&S performance as a result of the age of infrastructure

- Asset management strategy
 - Cyclic maintenance
 - Strategic maintenance – AMP
 - Opportunity maintenance – low storage levels

- Asset life cycles – increased operations and maintenance on ageing infrastructure
- Cyclic expenditure – dam safety audits and testing of dam safety emergency plans

Capital expenditure programs have different drivers which have had and will have different impacts on the level of expenditure:

- Water savings projects
- Resource management projects – loss management initiatives
- Different ages of infrastructure in each irrigation district
- Assets where the AMP strategy has been applied will change the useful life of those assets.
- Rationalisation – This activity is expected to increase as a result of the reconfiguration project
- Reconfiguration of infrastructure
- Risk management – OH&S, Dam safety program
- Customer service

A review of capital expenditure should take into consideration external funding.

Incentive Mechanisms

Not applicable to G-MW as it operates on a full cost recovery basis (no profit objective). All efficiency savings are passed on to customers.

Tariff Structures

Pricing principles:

- Adequate signals to rural customers relates to the cost of services and not to directly influencing consumption.
- The impact on rural customers should be reviewed in the context of a business input and not as an essential supply to a household. Consideration should be given to the proportion of the water charge to the total costs of the business.
- The impact should also consider the total dollar change in the charge and not just the % change.

Tariffs

- Tariffs should provide a signal to customers about the cost of providing a service – provides the information required for good decision making.
- Tariffs should not distort customer trading decisions.

In response to Government and customer requests G-MW is undertaking a review of its tariff. This review will not be finalised until March 2007. The recommendations from this review may change G-MW's tariff.

The ACCC's review and recommendations on access and termination fees may result in changes to G-MW's tariff.

Miscellaneous Services

Only miscellaneous services that are exactly the same should be standardised. As these miscellaneous service prices are based on cost, the cost structures of each business would need to be considered. The introduction of the water register will standardise some miscellaneous fees.

Miscellaneous fees are charged on a 'pay as you use' basis and may relate to potential customers rather than existing customers. G-MW's customers would not support the transfer of miscellaneous services into water fees.

Clear and precise definitions should be developed for miscellaneous fees to enable review and comparison.

As the ESC has been involved in the water industry for a relatively very short period of time, past experience should not be used solely to base decisions on. The ESC should allow the introduction of new services during the regulatory period on an as needed basis. This should not be burdensome.

Customer Contributions

G-MW negotiate contributions under commercial arrangements to recover costs so that existing customers are not disadvantaged