URBAN DEVELOPMENT INSTITUTE OF AUSTRALIA (VICTORIA)

Suite 411, Level 4, 434 St Kilda Road, Melbourne Vic 3004
Tel 03 9832 9600 Fax 03 9832 9650
E: info@udiavic.com.au W: www.udiavic.com.au
abn 69 005 125 280

8th March, 2007

Essential Services Commission
Level 2, 35 Spring Street
Melbourne VIC 3000

2008 WATER PRICE REVIEW CONSULTATION PAPER
FRAMEWORK AND APPROACH

We thank you for the opportunity to respond to the Consultation Paper in which the framework and approach to the 2008 Water Price Review is outlined and discussed.

The Urban Development Institute of Australia (Victoria) is an independent association of over 270 organistions directly involved in the production, financing and marketing of all facets of property development.

UDIA Victoria is:

- A forum for discussion of industry problems and objectives
- An active political lobbyist for industry causes and goals
- An active collator and disseminator of information and data relating to urban development
- A monitor of Government and Public Authority activities that affect urban development and the viability of the industry.

Our approach to the Consultation Paper is to provide initial comments in relation to the principles outlined. It is our intention to respond more fully in time. That may be upon the release of the Exposure Draft expected to be made public on or around the 1st May 2007.

The UDIA provides the following general comments in respect to infrastructure pricing.

2005 PRICE DETERMINATION - NEW CUSTOMER CONTRIBUTIONS
While the UDIA welcomed the approach determined by the ESC in the 2005 Price Determination, several of the concerns raised by our organisation in our submissions to that process have, we believe, been borne out.

The issue of sequencing, or the financing of bring forward costs, has been a particular matter of concern for the urban development industry. While the approach of the ESC to this issue is understood, the practical reality of determining what is, and what is not, out of sequence development has been far more difficult to determine.

In certain growth areas several development fronts have been simultaneously active, while the determinants of “sequencing” have in several instances, been unrelated to water infrastructure. Similarly, and as foreshadowed, land ownership patterns and intentions have in other instances altered what might have otherwise represented a logical sequencing of development. Hence, despite the best efforts of stakeholders, there remains - two years after the initial Price Determination - no accepted methodology to determine an equitable apportionment of bring forward costs, if and when, they occur.

EQUITABLE ARRANGEMENTS
The urban development industry remains concerned at the approach of upfront infrastructure charging in general and its impact on the affordability of new homes. As noted in our earlier submissions prior to the 2005 Price Determination, there is a strong view that new home buyers are today financing infrastructure through upfront charges, in contrast to earlier generations who were afforded the same through general usage charges.

We believe there is still a case to be made for this today, whereby the cost of infrastructure should be recovered over the life of the infrastructure. In other words, while there is an upfront cost in connecting a new household, that household also will contribute through the retail price of water for the lifetime of the household.

Moreover we note our ongoing concern that home owners in established areas are afforded infrastructure upgrades and maintenance through the revenues raised by the retail price of water, a situation at odds with that of the new home buyer.

CERTAINTY
While the urban development industry has demonstrated general support for the changes brought about by the 2005 Price Determination, an overriding concern remains that of certainty. The development cycle for broadhectare land – that is the elapsed time between site identification and purchase and the release of developed lots to the market - can take up to a decade, and sometimes longer. When dealing with timeframes of this nature the need for economic certainty is paramount. The prospect of ever-changing infrastructure funding principles does little to engender the economic certainty required when undertaking long term investment decisions.

THE CONSULTATION PAPER
In respect to the Consultation Paper, we provide the following specific comments:

<u>Item 7.3 Approaches to setting customer contributions</u>

- Upfront contributions are requiring developers to fund business growth of water companies – that is to say, each new customer connection provides long term business growth to the relevant water utility. Recovery of growth related capital expenditure through the retail price of water represents a fairer outcome.
- The funding of infrastructure up front by the water company has “no material long term financial impact” on the water company. It does however represent a significant cost impost built into the price of a housing lot.
- The $1,000 per lot charges suggested for water and for sewage proposed by some is rejected by the development industry. The result is an additional $1,300 per lot cost to home buyer and more when viewed as part of a 30 year mortgage.
- Further to our general comments regarding equitable arrangements, we note that a new property on the urban fringe, with new infrastructure (and therefore very low maintenance cost) will require low recurrent spending for the next 30-40 years. Those home owners will effectively cross subsidise upgrades and maintenance in established urban areas through the retail price of water. Older or existing areas have substantially higher maintenance costs and in many cases require replacement of local infrastructure – all paid for out of water company tariffs. If new home buyers on the fringe are paying for their infrastructure, but have lower costs over the next 30-40 years should they then pay a lower water tariff?

- As noted earlier in this submission, there are ongoing difficulties in structuring charges on the basis of locational signals. Additional cost will only enhance the value of the property “next in line”. If the structure of the contributions creates too great a disincentive for anyone other than the next in line then there is the potential (or likelihood) that speculators or unwilling private land owners can hold up development in a corridor for years (and potentially decades).

Item 7.5 Current Arrangements

- The $500 per lot charge brought in as a result of the 2005 Price Determination has received a certain level of acceptance from development industry.
- Since the 2005 Price Determination, the State Government Infrastructure Levy has been announced with likely charges between $3,000 and $8,000 per lot.
- The suggested increase in the water and sewage levies to $1,000 (as suggested by other stakeholders) would be opposed by the development industry on affordability and equity grounds.
- The continued referral of applications for increases is critical.

Item 7.6 Further Issues

- Under the current arrangements where a developer is required to fully fund reticulation infrastructure there is the situation of cross subsidy in the water tariffs where the tariff component for maintenance and short term replacement costs is transferred to existing and older areas.
- "Temporary" infrastructure (such as temporary pump stations) is shared by several developers and therefore must be treated as shared assets under the definitions. Often the temporary assets provide a benefit to the water company in deferring capital expenditure while the water company collects revenue. The water company should meet such costs rather than the developer.
- The current arrangements in respect to bring forward costs do not appear to include an allowance for the bringing forward of the revenue component.
- In respect to infrastructure costs associated with recycled water schemes the urban development industry believes funding arrangements must take into account the broader community benefit derived from recycled water schemes.

We look forward to making additional and further comments during the consultation phase following the Exposure Draft anticipated for release in May of this year.

Yours sincerely

Tony De Domenico

Tony De Domenico
CEO