

6 October 2022

Mr Marcus Crudden
Executive Director Price Monitoring and Regulation
Essential Services Commission
Level 8, 570 Bourke St
Melbourne, VIC, 3000

Dear Mr Crudden

The fair sharing of costs related to the provision of recreational facilities management: Southern Rural Water 2023-28 Price Submission

I am writing in response to Southern Rural Water's (SRW) 2023-28 Price Submission, lodged with the Essential Services Commission (ESC) on 30 September 2022. In particular, with reference the derivation of charges to recover the costs of recreational facilities management and its engagement with our organisation.

The purpose of this formal submission is to ask the ESC to investigate, as part of its 2023 price review:

- SRW's response to our requests to determine a more appropriate basis for charging, including the appropriateness of engagement completed with relevant stakeholders;
- The appropriateness of SRW's approach to:
 - allocating costs between headworks (bulk entitlement charges) and recreational facility management charges;
 - allocating costs to be recovered through recreational charges, including corporate management and governance, corporate support services, overheads and capital expenditure charges;
- The prudence and efficiency of costs recovered by SRW's recreational charges;
- The beneficiaries of the services being provided by SRW; and
- Alignment of the charging approach with the Water Industry Regulatory Order (WIRO) pricing principles.

Our response includes:

- Background to recreational charges paid by our organisation and by extension, our urban customers;
- The evidence that supports necessary change;
- A timeline of the activities undertaken by our organisation to engage with SRW in attempting to resolve the appropriate approach to charging for recreational facility management; and

- Our proposal for the ESC's investigation.

Background

By way of background, SRW is responsible for managing water storages at Blue Rock Reservoir, Cowwarr Weir and Lake Glenmaggie. We hold Bulk Entitlements in each of these waterways for the purpose of producing reticulated drinking water.

To recover these expenses, SRW levies 96.01 per cent of these costs to us, and by extension our urban customers. It does so on that basis that it considers the residents of Willow Grove, Coongulla, Glenmaggie and the broader Gippsland region our urban customers to be the primary beneficiaries of their facilities¹.

The remaining 3.99% is levied on its irrigation customers. SRW has advised that these allocations are based on population split².

SRW has advised our organisation that the Department for Environment, Land, Water and Planning (DELWP) endorsed its approach to charging urban water customers and that the justification for doing so was that "urban water customers provide a good proxy for those receiving the benefits of recreational facilities"³. We dispute this principle. SRW also levies headworks charges to BE holders of the above waterways based on the size of the BE held by each entitlement holder.

The following breakdown has been provided to us by SRW to show the costs for managing recreational facilities at Blue Rock Reservoir, Cowwarr Weir and Lake Glenmaggie:

Table 1 SRW breakdown of costs for recreational facilities (2018-22)⁴

Business segment: 4060 – Recreational Facilities East	Jun-22 Budget	Jun-21 Actual	Jun-20 Actual	Jun-19 Actual
10 – Ops & Maintenance	268,942	212,943	229,009	197,169
15 – Business Mgt	90,117	97,409	56,841	59,788
20 – Corporate Mgt & Governance	48,212	38,666	20,798	20,892
25 – Corporate Support Services	108,432	97,559	72,190	66,522
30 – Overheads	30,471	27,043	24,315	21,838
55 – CapEx charges	61,330	54,155	63,964	65,710
Total	607,504	527,775	467,117	431,918
GW share	583,265	506,716	448,479	414,685

SRW has advised us that there are five bulk entitlement (BE) holders across its two bulk storages (noting that Cowwarr is a weir and not a bulk water storage) as per the table below:

Table 2 BE holders for Blue Rock Reservoir and Lake Glenmaggie⁵

	Blue Rock	Glenmaggie
BE for multiple power stations	52.5%	
BE for GW	17.08%	1.37%
BE for SRW for agriculture	2.1%	91.32%
Environmental Water		7.31%
Drought Reserve	18.87%	

¹ SRW presented an update on the progress of their review – 21 March 2022 (Meeting notes)

² Southern Rural Water, *SRW Price submission – Gippsland Water*, 6 May 2022

³ Southern Rural Water, Letter titled Recreational facility charges, 14 February 2022

⁴ *ibid*

⁵ *ibid*

The remaining BE holder in Blue Rock Lake, not shown in Table 2, is the Victorian Environmental Water Holder, at 9.45%.

Power generators, the Victorian Government (Drought Reserve) and the Victorian Environmental Water Holder are not charged recreational facility maintenance fees, despite holding large entitlements.

In its 2023-28 Price Submission, SRW states that “there are no provisions in the bulk entitlement orders to impose such a fee”⁶.

Based on the summary information above, we believe the following questions need to be considered:

- Did DELWP endorse this pricing approach? If so, where does this position appear in policy and was there any formal communication?
- What is the basis for the apportionment of shared costs to recreational facilities management?
- As all current entitlement holders benefit from access to the water in these storages, why is an apportionment of recreation cost not made to other entitlement holders?
- How has SRW determined the allocation of costs between headworks and recreational charges, to ensure there is no cross-subsidisation?
- Does SRW’s approach to charging align with the WIRO pricing principles?
- Is it appropriate to have an inconsistent approach to levying headworks and recreational charges?

The evidence that supports change

We have been unable to resolve the following issues through our engagement with SRW:

1. Information provision and transparency

The ESC’s Price Submission Guidance Paper explains that “a water business must provide participants in its engagement process with appropriate information, given the purpose, form and the content of the engagement, and a reasonable and fair opportunity to participate as part of the process”⁷.

Similarly, the PREMO assessment framework seeks for businesses to be an “open book”⁸.

We have initiated several requests for SRW to clarify the basis for cost allocations (e.g. letters dated 13 April 2021, 19 January 2022, 14 February 2022 and 17 February 2022). At this point, no information on the basis for cost allocation has been provided that provides transparency with regards to the allocators and their reasonableness.

Upon our request, SRW undertook to engage with other entitlement holders (power generators in particular) to explore options that would involve them making a fair contribution towards recreational facility maintenance.

We were provided with the opportunity to review draft versions of the engagement materials presented to the power generators and we expressed concern that in our view, the content was leading towards a particular outcome.

⁶ Southern Rural Water 2023-28 Price Submission, 30 September 2022, pages 56 and 114

⁷ Essential Services Commission 2021, 2023 water price review: Guidance paper, 26 October 2021, pg. 20

⁸ Essential Services Commission 2021, 2023 water price review: Guidance paper, 26 October 2021, pg. 42

We were concerned that the materials inferred a continuation of the principle relied upon in the existing apportionment “*provided a good proxy for those receiving the benefits of the recreation facilities*”⁹.

We were also concerned that the only option put to the power generators involved an offer of “co-branded signage around the facilities” in return for a contribution.

There was limited discussion on the arguments we had presented to SRW during the preceding months, nor a presentation of the options we consider appropriate for engagement.

2. Justification for the allocation of shared costs to recreational charges

While we recognise the underlying principle of (amongst other things) the charge recovering a “fair contribution to overheads”¹⁰, the fairness of the apportionment can only be determined through transparency on the basis for cost allocation.

Despite numerous requests (e.g. letters dated 13 April 2021, 19 January 2022, 14 February 2022 and 17 February 2022), SRW is yet to provide any information on the basis for the apportionment of costs.

The quantum of the charge to us exceeds our own costs for managing recreational facilities at our Moondarra Reservoir considerably, which are approximately \$42,000 per annum.

Our Moondarra maintenance includes a reservoir viewing area, dam wall access, a public toilet facility, extensive picnic facilities and public spaces. As such, we are not satisfied that SRW’s recreational charges to us reflect an appropriate allocation of shared costs.

3. Inconsistency with WIRO pricing principles

Part 11 (d) of the *Water Industry Regulatory Order 2014*¹¹ requires that the manner in which prescribed prices are calculated should:

- a. be easy to understand;
- b. provide signals about the efficient costs of service provision (whilst avoiding price shocks); and
- c. take into account the interests of customers.

While the methodology is relatively easy to understand, SRW’s pricing approach contradicts the last two principles.

Firstly, efficiency implies that a charge is reflective of the costs of the provision of that service. SRW has not evidenced the basis for the allocation of shared costs between headworks and recreational charges, or costs to recreational charges.

Secondly, in its 2023-28 submission, where SRW has reduced the recreational charges, it has increased headworks charges, which could create a cross-subsidy.

Thirdly, despite being the customer that pays 96% of all recreational charges, SRW has not taken our interests account. In our view, SRW has demonstrated a clear bias towards maintaining the current arrangements,¹² and is avoiding more challenging conversations with other entitlement holders.

⁹ Southern Rural Water, *SRW Price submission – Power companies*, May 2022

¹⁰ Essential Services Commission 2021, 2023 water price review: Guidance paper, 26 October 2021, pg. 56

¹¹ https://www.water.vic.gov.au/__data/assets/pdf_file/0033/536298/Final-WIRO-2014published-in-GG-on-23-October-2014.pdf

¹² Southern Rural Water 2023-28 Price Submission, 30 September 2022, pages 56, 113 and 114

This brings the prudence and efficiency of the charges into question.

4. *We have a mandate from our customers to act*

Throughout our 2023-28 Price Submission customer engagement process, the majority of some 3,500 customers have told us that they expect our charges to be fair and affordable, and reflective of the services they receive from us.

In April 2022, a panel of 30 of our customers came together to learn about, explore and deliberate over a number of key issues relating to affordability and fairness, to help shape our 2023-28 Price Submission. The levying of charges to recover SRW's recreational facility maintenance costs was one of the topics discussed.

They also told us that "major industries should pay their own way"¹³.

Our customers believe that the cost of maintaining SRW's recreational facilities at Blue Rock Reservoir, Lake Glenmaggie and Cowwarr Weir should be shared fairly between all of the BE holders including GW, irrigators and power generators. This was confirmed by our customer summit panel¹⁴.

The panel also recommended that our customers should pay between 17-30 per cent of the cost of maintaining SRW's recreational facilities at Blue Rock Lake, Lake Glenmaggie and Cowwarr Weir¹⁵.

5. *Beneficiaries of the recreational facilities*

SRW has sought to allocate the costs of recreational facilities management according to population.

In its Price Submission, SRW states that "Macalister Irrigation District residents make up 4% of the regional population" and "the remaining population are principally Gippsland Water customers, rather than SRW customers, hence the costs are passed onto Gippsland Water."¹⁶

In our view, this statement overlooks the fact that many users of SRW's recreational facilities reside in areas outside of our service area (in particular metropolitan Melbourne). It also overlooks the fact that other bulk entitlement holders are also beneficiaries of the storages that these recreational facilities are located on.

Consistent with our summit panel's recommendations, we consider the costs of managing recreational facilities should be recovered from all BE holders, and we have committed to advocate for this outcome on their behalf.

Managing recreational facilities is a service that comes with managing bulk storages. The beneficiaries of these bulk storages are the BE holders. In this case, our organisation has a relatively small BE compared with the power generators and irrigators, yet we are burdened with almost the entire cost.

The Victorian Government's *Water for Victoria Water* plan states that "the money water corporations spend to provide recreational infrastructure and facilities should be paid for by the people who benefit"¹⁷.

¹³ Gippsland Water, Price Submission 2023-28, September 2022, pg. 52

¹⁴ Ibid

¹⁵ Ibid,

¹⁶ Southern Rural Water 2023-28 Price Submission, 30 September 2022, page 114

¹⁷ Victorian State Government, *Water for Victoria Water Plan*, 20-16, pg. 120

It is therefore consistent with Government policy that the basis for recovering recreational facilities management costs, should therefore be consistent with the basis for recovering headworks costs (i.e. the percentage share of BE for that storage).

Our engagement with SRW

We have provided the Commission with evidence showing a long history of approaching SRW in an endeavor to resolve our concerns about the apportionment of recreational facilities charges.

In the process of developing our 2023 Price Submission, our Managing Director wrote to SRW's Managing Director three times (once in 2019, and two in 2022) seeking a review of the basis upon which it recovers recreational charges and seeking clarity on the apportionment of shared costs.

Seven meetings were held with members of SRW's executive and senior management team between February and July 2022. A detailed schedule of activities is provided in Attachment 1.

Whilst SRW provided information about BE holders in its storages, as well as the actual costs it had incurred in managing its eastern recreational facilities and the costs allocated to recreational facilities management, we remain concerned about the lack of rigor and transparency SRW has shown through this process. In particular:

- SRW was reluctant to openly consider alternative pricing methods, quickly discounting these on the basis of "unlikely to pass the beneficiaries test"¹⁸;
- SRW was reluctant to engage other BE holders on the potential to review the appropriateness of the charging methodology; and
- SRW did not provide appropriate information about the basis for the allocation of shared costs to recreational facilities management.

We also believe that SRW's approach to engaging on this matter has been inconsistent with the principles described in the ESC's 2023 Price Submission Guidance Paper:

1. *"A water business must provide participants in its engagement process with appropriate information, given the purpose, form and the content of the engagement, and a reasonable and fair opportunity to participate as part of the process"*¹⁹

We have not been provided with appropriate information, and we consider the information provided to power generators by SRW during its engagement to be biased towards maintaining the status quo. Nor did it present the options that we formally asked to be considered.

2. *"The business's justification for how it will address customer and community expectations that will not or cannot be met."*²⁰

In its most recent communication²¹, SRW stated that "we have, on balance, decided to continue to calculate the sharing of remaining costs based on the same allocation method that has been in place under recent price submissions."

It did not provide any detailed justification for this decision, other than to present that the

¹⁸ Southern Rural Water, Letter titled Recreational facility charges, 14 February 2022

¹⁹ Essential Services Commission 2021, 2023 water price review: Guidance paper, 26 October 2021, pg. 20

²⁰ Essential Services Commission 2021, 2023 water price review: Guidance paper, 26 October 2021, pg. 21

²¹ Southern Rural Water, Southern Rural Water Price Submission 2023/24-2028/29, 12 September 2022

power generators are “not supportive of a change to the method for calculating recreational charges, to a model that involves the power companies in part funding these activities”²².

3. *"A business must make available, or provide on request, resources and materials provided to customers during its engagement, and any customer feedback about the engagement program."*²³

Despite several requests, SRW did not provide us with access to the basis for the allocation of shared costs recreational charges.

We encourage the ESC to seek access to this information, as well as copies of the presentations provided by SRW to both ourselves and the power generators.

Our ask of the ESC

We request that the ESC undertakes the following as part of its review of SRW's 2023-28 Price Submission:

1. Review the appropriateness of engagement completed by SRW with our organisation including the level of transparency of information shared;
2. Review the appropriateness of engagement completed by SRW with the power generators, and whether there was any genuine attempt to openly (and without bias) discuss the alternative options we proposed;
3. Review the appropriateness of the allocation of costs between headworks and recreational charges to ensure that there are no cross subsidies;
4. Review the cost allocation approach for both headworks and recreational charges to determine whether it supports your criteria for prudence and efficiency;
5. Review whether SRW has appropriately identified the primary beneficiaries of the provision of recreational facilities management at Blue Rock Reservoir, Cowwarr Weir and Lake Glenmaggie; and
6. Seek for SRW to establish a pricing framework that more appropriately reflects the pricing principles contained in the WIRO, and one that reflects the clear feedback provided by our organisation and our customers.

Thank you for considering our submission and we appreciate the time it will take to consider and evaluate our feedback through your price review.

Should you wish to discuss this matter further or seek additional information as listed in the table below, please contact Melissa Thek, General Manager Business Transformation on telephone 5177 4735 or email melissa.thek@gippswater.com.au and we will be happy to assist.

Kind regards



Simon Aquilina
Acting Managing Director

²² ibid

²³ Essential Services Commission 2021, 2023 water price review: Guidance paper, 26 October 2021, pg. 22

Attachment 1 – Table of engagement activities with SRW

Topic	Mode of Engagement	Date	Internal File Reference
Letter to SRW – Follow up on request to review rec facility charges (MD to MD)	Letter	19 January 2022	COR/22/3094
Letter -- SRW MD response to GW - GW & SRW Recreation facilities	Letter	14 th Feb 2022	COR/22/5667
Letter to SRW regarding review of recreational facility charges	Letter	17 February 2022	COR/ 22/6317
Letter to DELWP regarding SRW's review of recreational facility charges	Letter	February 2022	COR/22/6316
SRW presented the best possible way of sharing costs to beneficiaries.	Meeting	17 February 2022	COR/22/6396
Discuss pathway forward for both agencies	Meeting	22 February 2022	COR/22/7181
Discuss Price Submission next steps	Meeting	8 March 2022	COR/22/38411
E-mail to SRW to respond to their presentation in February and their proposal.	Email from GW to SRW	E-mail 10 March 2022	COR/22/40915
SRW presented an update on the progress of their review.	Meeting	21 March 2022	COR/22/40971 (Meeting notes)
GW Request for SRW to set up follow up meeting and develop a schedule of upcoming activities for this work	-mail from GW to SRW	28 March 2022	COR/22/40916
SRW MD attended customer summit	Attendance at GW Customer Summit	26 March 2022	COR/22/18565
Discuss progress of SRW review	Phone Discussion	1 April 2022	
Meeting between SRW &GW MD's and Exec	Meeting	27 April 12022	COR/22/40918
SRW provided with customer summit recommendations.	Email	17 May 2022	COR/22/40959
Progress meeting	Phone Discussion	30 May 2022	
SRW provided a copy of proposed presentation to power companies, to GW	Email	1 June 2022	COR/22/20847
GW Response to proposed presentation to power companies	Email	2 June 2022	COR/22/20937
SRW presented to GW further progress of their review	Meeting	29 June 2022	COR/22/40954 (Meeting Notes)
SRW presented options being considered for the ongoing recreational facility charges	Meeting	25 July 2022	COR/22/40955 (Meeting notes)
Thank you for contributions at customer summit, update on Price Submission engagement process and invitation to provide feedback on Directions Paper	Email	Letter/ email sent July 2022	COR/22/27303
Email from GW to SRW requesting them to confirm their outcome	Email	12 September 2022	COR/22/40961
Response from SRW to GW on outcome	Email/Letter	Monday 12 September 2022	COR/22/39441
Letter to SRW on outcome	Email/Letter	Tuesday 27 September 2022	COR/22/39518