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2008 WATER PRICE REVIEW – WATER PLANS ISSUES PAPER
GIPPSLAND WATER SUBMISSION

Gippsland Water (GW) has reviewed the Water Plans Issues Paper released by the Essential Services Commission (ESC) in relation to the 2008 Water Price Review. From a regional water corporation perspective, GW offers the following information for consideration in finalising the review process.

Rather than seek to cover the entire range of issues identified in the Issues Paper, the Gippsland Water response in the following tables concerns itself with those issues which the corporation believes it can provide some insight into to inform the debate.

Yours sincerely,

David Evans
Acting MANAGING DIRECTOR



WORKPLACE EXCELLENCE
AWARDS

WINNER 2004

Subject	ESC page reference	Gippsland Water Comment
Conservative demand forecasts and sharing of risk between business and customers	12-15, and 49-51	<p>Gippsland Water demand forecasts for residential consumption have been based on the Victorian Government's Central Region Sustainable Water Strategy (CRSWS) and Gippsland Water's Water Supply Demand Strategy (WSDS), in response to requirements set out by the Victorian Government and DSE (CRSWS - refer page 39 and action 4.42, page 98). Water saving targets for the period for residential consumption are based on mid 1990s consumption of 244 litres/person/day, with a 25% reduction by 2015. Total consumption targets are consistent with targets for Melbourne. Rather than being conservative, the forecasts reflect changing government and community attitudes towards the use of a critical resource.</p> <p>From a Gippsland Water perspective, "high visibility" Victorian Government initiatives to save water have a very significant focus on residential customers. The continuation of these Victorian Government incentives, together with changes in residential customer behaviour that are evident from the imposition of water restrictions across the region in 2006/07 support the forecasting of reductions in consumption. It should be noted that the intent is to reduce demand, irrespective of the level water restrictions imposed from time to time.</p> <p>Demand forecasts are also an essential component of the demand / supply review process undertaken in the WSDS. Augmentations determined in the WSDS assume the same reductions in demand forecast as the final Water Plan. Increasing demand would trigger a logical requirement to review the implications for augmentation strategies determined in the WSDS, and included as capital projects, and as part of the price path in this final Water Plan.</p> <p>Gippsland Water would be concerned at any attempt to modify demand forecasts with the aim of artificially reducing tariff impacts. Recent evidence in the form of actuals for the first six months of 2007/08 continues to indicate that demand has again reduced, despite the lifting of water restrictions and the return to permanent water saving rules.</p> <p>One comment in the demand section of the Issues Paper that surprised Gippsland Water was -</p> <p style="padding-left: 40px;">"it is worth noting that some of the businesses that have forecast declining average consumption operate in the most water abundant areas in the state...including Gippsland Water..." (page 51)</p>

		<p>In response, Gippsland Water would note that declining consumption already exists, and has been outlined in the historical data provided in the final Water Plan (page 148). In addition, surface water system yields have reduced significantly. As outlined in the final Water Plan (page 129), over the past 10 years, inflows to Gippsland Water’s supply systems have been 21 per cent less than the long term average.</p> <p>The point to be taken from this is that even water corporations and their customers in “water abundant” regions face the real task of reducing consumption in times of significant uncertainty with respect to future system yields. In the Gippsland Water region, this is further compounded by the relatively small size of raw water storages (where storages for residential consumption actually exist) compared to large storages elsewhere in the state.</p>
Water Restrictions	14 (table 2.1)	<p>Please note an error in the ESC Issues paper which indicates that actual levels of restriction for Gippsland Water were limited to permanent water savings in 2006/07. This is incorrect.</p> <p>Gippsland Water applied significant water restrictions across the region in 2006/07. Major residential centres including Morwell, Traralgon, Moe, Warragul and Sale were all placed on level three restrictions in 2006/07. Several smaller towns were placed on level 4 restrictions due to a severe lack of water in small surface water systems, which in some instances required water to be carted into these towns.</p>
Dealing with Uncertainty	20	<p>Gippsland Water identified one major water augmentation, the Latrobe System Investment Strategy, as an uncertain capital project in our final Water Plan. Gippsland Water proposes that any mechanism for dealing with uncertain projects should include –</p> <ul style="list-style-type: none"> • Evidence of government approval to proceed (for major projects over \$5m); • Evidence of approved timeframes for completion of capital expenditure; • Evidence of approved values for capital expenditure; • Evidence of approved values for operational expenditure; and • Details of the changes sought in relation to tariffs for the remainder of the regulatory period, together with evidence to support the revised tariff calculations.

<p>Smoothed and moderated approaches to price paths</p>	<p>20 and 58</p>	<p>Gippsland Water customers face the prospect of significant increases in tariffs, given proposed levels of operational and capital expenditure for the 2008-2013 regulatory period, (which are still under review).</p> <p>Based on Gippsland Water’s revenue requirement for the 2008-2013 regulatory period, a “smoothed” price path of approximately 17% per annum was determined using the ESC pricing model. Based on Gippsland Water modelling, the annual average tariff in 2012/13 based on this “smoothed” approach would be more than \$1,514.</p> <p>Out of concern for the impact increased tariffs will have on customers, Gippsland Water chose to evaluate several other approaches to the issue of price paths during the formulation of the Water Plan. Gippsland Water’s goal was to limit the increase in the average annual tariff over the five year regulatory period, whilst requiring customers to pay an up-front contribution in excess of increases ordinarily expected.</p> <p>As outlined in the Water Plan, Gippsland Water also reviewed a “moderated” approach, which proposed annual increases of 23% for the first two years, followed by increase of 10% for the remaining three years. Based on Gippsland Water modelling, the annual average tariff in 2012/13 based on the “moderated” approach would be \$1,369.</p> <p>Gippsland Water also reviewed an “as required” approach, which attempted to match the timing of revenue requirements per annum. Gippsland Water faces a significant step change in operational expenditure in the first two years of the regulatory period. The “as required” approach proposed annual increases of 48% for the first year, followed by an increase of 5% for the remaining four years. Based on Gippsland Water modelling, the annual average tariff in 2012/13 based on the “as required” approach would be \$1,226.</p> <p>Gippsland Water elected to adopt a “moderated” approach in the draft and final Water Plans. This approach balanced the competing needs of limiting the increase in the average annual tariff over the five year regulatory period, whilst requiring customers to pay an up-front contribution in excess of increases ordinarily expected. In addition, the “moderated” approach reduces the potential for a price decrease in the first year of the next regulatory period, by limiting the creep in tariff that the “smoothed” approach produces.</p> <p>Gippsland Water took the opportunity to outline all three proposed approaches to price paths during the six community consultation sessions held across the Gippsland region for the draft Water Plan. While customers who attended the sessions were concerned at the significant increase in tariffs proposed, feedback received from customers was that the limitation of the increase for outlying years was a consideration that Gippsland Water had correctly assessed would be of concern to customers.</p>
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<p>Hardship issues and dealing with customer issues</p>	<p>23</p>	<p>As Gippsland Water outlined in its final Water Plan (refer page 83), it has a Hardship policy that details procedures for assisting our residential customers. Gippsland Water completes an exhaustive process to ensure that we actively identify customers who may be experiencing times of hardship and apply every effort in order to work with and assist them in managing their accounts.</p> <p>Gippsland Water reiterates its submission to the ESC Tariff Structures Review, where we indicated that the Water Industry Regulatory Order includes the principle to take into account the interests of low income earners and vulnerable customers.</p> <p>Low cost essential water is a concern raised by low income and vulnerable members of the community. This issue has been raised repeatedly during recent community consultation on Gippsland Water's draft Water Plan. Gippsland Water's concern is how best to provide for these groups at a time when water prices are expected to rise significantly, but not uniformly, across the state over the next five years in response to climate change, regulatory obligations, new infrastructure requirements, and the ever increasing costs of operating and maintaining water and wastewater services.</p> <p>There is a body of evidence to suggest that tariff structures, whether they be inclining blocks, or a flat rate do not provide for low income and vulnerable groups, such as pensioners and large families. While there appears to be some support for a fourth "low cost" tier to be added to inclining block tariffs (IBT), not all water corporations across the state have IBT's in place, thus not all vulnerable customers would be captured by this approach. A new block would not provide protection for larger families whose normal water requirements may fall outside the volumetric boundaries associated with any new block.</p> <p>Gippsland Water contends that social objectives should be pursued outside the tariff setting structure. We contend that this is a role for government across the state, not for individual water corporations. In determining rebate schemes, which could cater for these groups, government must consider the impact of generally higher tariffs outside metropolitan Melbourne when determining the value of concessions provided. Water corporations should be required to administer these rebate schemes on behalf of government.</p> <p>Gippsland Water thus supports the contention made by EWOV (letter of 15 January 2008 to ESC Water Plan Issues Paper) that the value of current concessions is being eroded and it something that should be addressed (by government).</p>
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Key capital projects table	37 (table 3.5)	Table 3.5 depicts the Gippsland Water Factory (GWF) as a \$170m project, in the current period. For clarification, the GWF project represents a total capex spend of \$173.9m. The final Water Plan assumes that all expenditure will be incurred before the commencement of the second regulatory period, with the exception of \$13m which has been forecast for 2008/09.
Approved 2007/08 expenditure compared with Water Plan forecast	40 (table 3.6)	In table 3.6, Gippsland Water is depicted as having a gap of \$84m between the original Water Plan and the forecast figure. It should be noted that the Water Plan figure is net of a \$25m government contribution, which was actually received in 2006/07. The remaining variance of \$59m is directly attributable to the increase in Gippsland Water Factory capital costs, as outlined by Gippsland Water in the final Water Plan (refer page 117).
Useful lives of assets	43	Gippsland Water has identified asset lives used for all asset classes in the capital expenditure summaries included in the ESC template. Gippsland Water believes that the asset lives used in the final Water Plan are conservative in nature, and do not adversely increase the regulatory depreciation calculations or the total revenue requirement. A comparison with the asset lives used by Gippsland Water in the determination of book depreciation further supports this view.
Classification of assets into shared and reticulation	71	<p>Gippsland Water is one of the majority of businesses that are currently satisfied with the Commission's current procedure for the classification of assets. Gippsland Water would strongly oppose any proposal to change the current asset definitions, as it would -</p> <ul style="list-style-type: none"> • significantly increase the number of shared assets, with water corporations becoming responsible for these works. This would obviously increase capital expenditure, and therefore our tariffs (existing customer base pays); or alternatively, other capital projects already planned would need to be forgone, increasing levels of service/environmental risk; • again confuse the development/water industries. Gippsland Water has made significant efforts to communicate the current rules via developer nights and in one on one meetings, and developers are comfortable with the current arrangement. • make the calculation of "Brought Forward" % very difficult, as there are potentially many developments happening at once. One town in the Gippsland region potentially has more than 10 growth fronts; <p>Gippsland Water has already committed to developers that we will contribute to the cost of reticulation assets, to service the full catchment beyond their development.</p>

<p>Value of GSL schemes questioned</p>	<p>27, 108</p>	<p>Rather than question the value of GSL schemes, as noted in the Issues Paper, Gippsland Water in the draft Water Plan indicated that it would need to consider the cost of providing a GSL scheme. Gippsland Water also noted that it proposed to survey customers in relation to GSL schemes.</p> <p>In the final Water Plan Gippsland Water outlined the results of the customer survey undertaken during the consultation period. 2,100 customer surveys (representing a 3.5% response) were returned. Specifically, in section 4.5.4 (p81), Gippsland Water noted that the findings of the customer survey contrasted significantly with the strong focus group support for the introduction of GSLs. Responding to a question in relation to the introduction of GSL's,</p> <ul style="list-style-type: none"> • 45% indicated that GSLs should be introduced; • 28% indicated that GSLs should not be introduced; and • 27% indicated that they were undecided. <p>In responding to a question in relation to customers paying an additional amount to fund rebates for a GSL scheme:</p> <ul style="list-style-type: none"> • 85% indicated that they would not be willing to pay more; • 8% indicated that they would be willing to pay more; and • 7% indicated that they were undecided. <p>Based on the results of this more significant sample, and the lack of any conclusive positive sentiment, Gippsland Water determined that it would not seek to introduce GSLs during the period of this Water Plan.</p>
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