



*Contact Officer: Mrs Haupt
Reference : WS1.2, JAH*

18 November 2014

Mr Hindmarsh
Chief Executive Officer
Queensland Competition Authority
GPO Box 2257
Brisbane Q 4001

Dear Mr Hindmarsh

RE: GAWB: 2015-2020 PRICE MONITORING SUBMISSION

I refer to your advice on 21st October 2014 advising of the recent submission by GAWB with respect to the Price Monitoring Submission lodged to apply to prices from 2015-2020 and the invitation for Council to provide comment with respect of the components of pricing that is being sought to apply to residents of the Gladstone Region for treated water during this period.

Council key points that it would like to raise are:

- Support for change in methodology regarding WACC;
- Whilst agreeing in principle with the "In System" storage project, Council questions the project alternatives, and the pricing impacts for Council above 4 days o;
- Questioning the attribution of pricing of switchboard upgrades at GWTP to Council, is the upgrade associated primarily with demand associated with industrial demand on Curtis Island;
- Operating costs attributable to the Benaraby Pricing zone
- Residents should not be required to pay a return on investment associated with expenditure on the Contingent Supply Strategy;
- Raise concerns and question applicability of MDQ based pricing to Council's network.

Weighted Average Cost of Capital (Section 7)

Council notes the change in methodology with respect to the determination of the WACC, the move towards a methodology that embraces a trailing average cost of debt over a 10 year period, rather than a "on the day" approach that has applied in previous review, is more

appropriate when determining prices on long lived assets and Council is supportive of this principle.

Capital Expenditure (Section 5)

Council is fully supportive of the implementation and maintenance of a system of asset management and replacement and has no reason to believe that the proposed End of Life replacements planned are not required provided that the investments are timely and prudent.

"In System Storage Project"

With respect to the proposed risk mitigation works in particular the Offline Storage and a Repump Station within the network, a \$21.9m project, whilst agreeing in principle to the project there are some questions that are not raised in the GAWB submission that Council believe need to be considered with respect to the likelihood of the risk, and consideration associated with the recovery through pricing of the project.

Whilst the submission by GAWB states that the project is deemed necessary to overcome key risks with respect to potential failure of the Awoonga Dam Pump Station, and that appropriate pumping redundancies exist in the current network, however, the potential for failure remains and therefore the construction of a suitably sized storage dam within the network would facilitate a redundancy of up to 14 days. The question that remains is what is the likelihood of such an outage that would require a 14 day capacity, \$21.9m project is a considerable project and surely the expenditure of public monies on a project that may only be utilised on the most infrequent of circumstances, should not be funded by residents.

Council can advise that its systems are designed to provide up to a 4 day capacity for its 22,700 connections, it would appear that what this project is "buying" in Council's circumstance is that additional level of service in case of an event or a failure that would take the system offline for a period between 4 and 14 days.

Council questions the need for residents to subsidise through their pricing this project given that Council manages risks for up to 4 days within its network, and would request that pricing strategies are reviewed if this project is required for other customers, and if the project proceeds that residents only be responsible for paying a share of costs in excess of 4 days storage, given that Council has made investments in its own network to provide this level of redundancy. If the need for project is because of the impact of an interruption to supply that will have extraordinary consequences to industrial customers of GAWB, then surely it is those customers that should be funding the project and not residents subsidising large industry.

In addition Council believes that all alternatives should be investigated with respect to redundancy of pumps at Awoonga Dam. Further, it also appears the justification for the proposed timing of these works has been tied to the 5 year maintenance period of the existing pumps rather than obsolescence of the existing redundant pipeline, although this may just be coincidence.

"Low Lift and High Lift Pumps - Gladstone Water Treatment Plant"

Whilst not questioning the need for the project, the project rationale identifies that this need is derived from issues with "peak power demand as experienced in late 2013". If the project is more associated then with mitigating risk due to the industrial demand of customers on Curtis Island, as would appear to be case given the citing of the dates of late 2013 in the project rationale, then this project should be attributable to the Curtis Island customers and not the regions residents.

Operational Expenditure (Section 2)

Table 3 on Page 7 of GAWB's submission identifies that there has been a 14% increase in costs attributable to the Benaraby Pricing Zone. This increase appears abnormal and out of step with the balance of the pricing zones, further, Council has been working with GAWB and are currently in the process of altering the supply to reduce the operation expenses of the Benaraby booster pumps, Council seeks clarification as to whether these proposed reductions in operational expenditure have been taken into consideration.

Contingent Supply Strategy

Council is supportive of the determination made in 2010 by QCA with respect to the recommendation that the Contingent Supply Strategy expenditure incurred after April 2008 should not be included in the Regulated Asset Base (RAB).

The need for investment in any augmentation of a supplementary water source is not a function of Council and its residents demand. Residential customers have proven to be receptive to water conservation measures, and indeed offer the most flexibility in times where demand management measures are required to be implemented.

The inclusion of any costs associated with the Contingent Supply Strategy should be excluded from the asset base attributed to residential water prices.

Maximum Daily Quantity (MDQ) Based Delivery Pricing

GAWB has flagged in its submission that for the subsequent price review that it would like to move towards a pricing system that would move the access component of the GAWB charge to be based on MDQ.

Whilst GAWB officers have provided indicative modelling that there is little impact in moving to a MDQ system for Council, there are several factors that need to be considered that would lead to the conclusion that when servicing a treated water network, MDQ based pricing may not be appropriate from a residential perspective.

It would appear that the methodology is contradictory to the Department of Energy and Water Supply (DEWS) recommendations for sizing of bulk water assets. DEWS planning guidelines for water supply and Sewerage (April 2010) suggest that bulk water mains be sized for the "Mean Day Maximum Month" (i.e. the average day of the worst 30 days) and that high demands on any single day be buffered in the reservoir storage (i.e. reservoirs serve a dual purpose of emergency storage and buffering peak demands). Whilst the MDMM peaking factor for residential is generally higher than industrial use, a MDMM peaking factor would be more in line with the guidelines that have been established for sizing of bulk water assets.

Technical Officers advise that the peak option would also be difficult to accurately interpret since there are varying points of GAWB metering throughout Council's network and "peak demands" will vary dependant on if the metering is on the inlet or outlet of reservoirs. This is further complicated in that "peak day" demands into Council reservoirs will be influenced by operating levels (e.g. over 4 days you empty a reservoir and then fill it on the fifth peak day, this will increase the peak day demand compare to if the reservoir had been partly filled on each of the previous days).

Council is pleased to provide comments on the submission by GAWB with respect to prices for 2015-2020, and whilst Council for the purposes of GAWB is considered as one customer, we are one customer with 22,700 residential connections as at June 2014, and we are mindful that the bulk water network needs to run efficiently and effectively but it should not be at the expense of residential connections bearing the costs of projects that are necessary for the industrial customers of GAWB.

Please do not hesitate to contact Mr Mark Holmes, Chief Financial Officer, if you have any further queries in relation to the issues raised in this letter.

Yours faithfully

A handwritten signature in black ink, appearing to read 'S. Randle', written over a horizontal line.

STUART RANDLE
CHIEF EXECUTIVE OFFICER