

CS ENERGY SUBMISSION TO QCA ON GAWB SUBMISSION 2 – EXPENDITURE PROPOSALS

CS Energy has reviewed the GAWB document. It has also been briefed by GAWB personnel on the pricing model and what CS Energy will be expected to pay for raw water supplied under contract from Awoonga Dam.

CS Energy draws water from Awoonga Dam using pumps and pipes owned and operated by SunWater. CS Energy pays SunWater for that service under a long term agreement. Consequently the only costs (capital and operating) reasonably attributable by GAWB to CS Energy are those directly relating to the operation and maintenance of Awoonga Dam.

CS Energy's concern with GAWB's proposals

CS Energy has a fundamental concern about the whole tenor of GAWB's pricing proposal. In its discussions with CS Energy, GAWB has indicated that a price increase of between [REDACTED] [REDACTED] will apply to CS Energy's water purchases from Awoonga Dam, the range of projected prices being dependent on the estimated demand and WACC.

CS Energy is also concerned that GAWB appears not to understand that it doesn't have an open cheque from its existing customers to do as it likes. Those who have to pay expect a less ambitious programme based on realistic expectations for dam yield and demand growth and assessed on stringent commercial criteria that reflect accurately the true risks.

GAWB's proposed WACC is considerably higher than that used by CS Energy. If WACC is indicative of perceived risk, then the clear implication is that GAWB's business is one of extremely high risk. However there is no valid evidence to suggest this is so.

The scale and diversity of risks faced by CS Energy are orders of magnitude greater than for GAWB.

Plant failure alone can cost CS Energy tens of millions of dollars in the space of a few hours. For example if CS Energy supplies electricity under contract to a customer at say \$50/MWh and then has a plant failure, such failure limiting supply in the NEM and causing the pool price to hit \$10,000/MWh, CS Energy can be obliged to purchase replacement MWh from the pool for the contracted customer at that high price.

CS Energy must invest in technically complex long lead time, high capital cost plant with which it is expected to compete for sales in the highly competitive electricity market. Recouping of billion dollar investments takes decades in this competitive environment in which CS Energy is required to deal in the physical as well as the derivative market to manage these considerable risks. Nothing in GAWB's operations and risk profile are even remotely comparable with those faced by CS Energy. GAWB's Awoonga Dam is a relatively simple piece of civil engineering that has low O&M costs, is not subject to obsolescence to make it uncompetitive and has a virtually indefinite life. The customers are tied by contract to an access charge, effectively a take or pay, which would more than cover GAWB's fixed costs.

Demand forecasts

GAWB acknowledges that it erred in its demand forecast which would have had such a damaging impact on its present financial position.

CS Energy agrees that GAWB's latest assessment of demand of 50,000ML/year is a more realistic forecast level compared with its overoptimistic forecasts submitted to previous QCA reviews and presumably used in its budgeting process.

This overestimation would appear to have a twofold effect on GAWB's financial position. Firstly, GAWB would have expended funds on the expectation of higher revenue than it ultimately received. Secondly it would have assessed the need to augment was more imminent than is the case and would have been expending funds, if not unnecessarily then certainly prematurely.

The excessive price increases now being canvassed by GAWB would seem to be intended to recover its financial position having spent in accordance with unrealistic revenue expectations.

The perceived need for augmentation is not accepted by CS Energy as the basis for increasing prices for existing customers. It is CS Energy's view that the cost of augmentation for new customers should be borne by those new customers under terms of new water supply agreements.

It is not acceptable for GAWB to expect its customers to underwrite the combination of unrealistic demand forecasts and overly pessimistic Awoonga Dam yield forecasts.

Pessimistic yield forecasts prematurely trigger the costly action on augmentation for drought mitigation and new demand.

CS Energy does not believe that GAWB should be able to absolve itself of the responsibility for significantly overstated expectations. Having its customers shoulder the financial burden attributable to this situation is not reasonable as there is no incentive for GAWB to be any more diligent and realistic in future.

CS Energy's water requirements for Callide B are made up of supply from GAWB and SunWater.

It is CS Energy's preference to take the Callide Dam water first because it makes a fixed annual payment and does not incur the pumping costs that apply to the water from Awoonga Dam. However the announced allocation for Callide Dam is uncertain from year to year and that factor is the major determinant of the variance in CS Energy's offtake from GAWB in any year rather than the variance in generation. Callide B has a reasonably even load from year to year (apart from maintenance outages every three years).

Capital Expenditure

The only Capex relevant to supplying CS Energy are the flood capacity obligation (\$22 million over 5 years) and the Awoonga Recreational area.

GAWB will need to demonstrate that it has interpreted the statutory safety requirements correctly and that it will meet those requirements in the most cost effective manner. Because GAWB has exhibited what seems to be an overly conservative attitude to risk (in evidence in its previous demand and yield forecasts), CS Energy requests that the QCA ensure that GAWB's interpretation and implementation of statutory requirements is realistic.

CS Energy does not accept that it should bear the cost of any other items listed by GAWB.

Although CS Energy is not affected by the proposal to provide a 14 day system storage and does not accept that it should bear any of the cost, the GAWB submission does not indicate if it has considered, as an alternative to cover the contingency of failure of GAWB's Awoonga pump station, teeing off the SunWater pipeline that supplies CS Energy and CPM power stations. If that were the better alternative (probably a simpler process to implement and one not prone to evaporation losses) and GAWB undertook that alternative, CS Energy would consider bearing some of the cost if done in a manner that provided contingency pumping from Awoonga Dam for CS Energy, but CS Energy would also expect to share in savings it provided for GAWB's other customers.

Operating Expenditure

As with Capex, the only Opex CS Energy accepts it should bear is that specifically related to the cost of running Awoonga Dam to store raw water taken by CS Energy.

Effect of a QCA ruling

It is CS Energy's view that GAWB is not entitled to apply an overall pricing direction by the QCA to raw water supplied from Awoonga Dam to CS Energy under a negotiated contract.

CS Energy and GAWB are now proceeding with negotiation of a new agreement and this will be done independent of the QCA.

It is CS Energy's clear view that any arrangement it completes with GAWB for the supply of raw water from Awoonga Dam will be commercially determined rather than one imposed by a third party. The fundamental commercial aspect, price, is dictated by the Deed of Settlement executed between GAWB and CS Energy on 9 December 2009.

Although the recently executed Deed makes reference to GAWB's standard pricing principles, CS Energy considers that, in its directions on GAWB's pricing principles, the QCA should make specific reference to CS Energy and GAWB negotiating a commercial price. That price will be determined having regard for all the terms and conditions being negotiated in the new water supply agreement which is specific to CS Energy and different from GAWB's standard form of agreement. It is not reasonable to negotiate all the new terms but have a price imposed by a separate process.