

19 May 2009

Dr Ron Ben-David  
Chairman  
Essential Services Commission  
Level 2  
35 Spring Street  
MELBOURNE VIC 3000

Dear Ron,

Please find enclosed South East Water's response to the Commission's 2009 Water Price Review Draft Decision.

Generally, South East Water has sought to respond to issues that have been raised rather than comment on matters that appear to have been resolved.

The specific areas of focus for South East Water include:


- Service Standards – South East Water has developed an alternative approach to service standards to better reflect the current climate.
- Expenditure – Key issues include water main renewals, the Northern Victorian Irrigation Renewal Project (NVIRP), VCEC implementation costs and savings and the expenditure auditor's approach which has resulted in double counting of reductions in some areas.
- Demand Forecasts – Exclusion of the impacts of price elasticity, the timing of changes to restrictions and the overall impact of the T155 program.
- WACC – Consistency between the Commission's estimate of the debt margin and the borrowing costs imposed by Treasury.
- Tariff Structures – South East Water has developed a pricing structure that places greater emphasis on water volumetric charges and less emphasis on sewage volumetric charges. South East Water is also proposing to retain its current sewage disposal charge seasonal indices.

South East Water has made amendments to Melbourne Water's bulk charges to remove the impacts of NVIRP as well as include the relevant capital expenditure in our Water Plan. South East Water understands that the Commission will replace South East Water's estimate of Melbourne Water's bulk charges with the final amount payable. At this stage, South East Water would like to be consulted to ensure that the adjustments to retail tariffs that are made are consistent with our intentions.

Given the need to communicate with customers and other stakeholders as well as update business systems, South East Water would like to emphasise the importance of receiving the Commission's Final Decision as soon as possible.

Should you require any information in addition to the attached, please feel free to contact Ian Johnson on 9552 3725 or [ian.johnson@sewl.com.au](mailto:ian.johnson@sewl.com.au).

Yours sincerely

A handwritten signature in blue ink, appearing to be 'S. Cox', with a stylized flourish at the end.

Shaun Cox  
Managing Director

## **South East Water Response to:**

**2009 Water Price Review**

**Draft Decision**

***May 2009***

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# 1. Introduction

Following is South East Water's response to both the Essential Services Commission's (Commission) Water Plan Draft Decision and the final reports of the Commission's auditor's in relation to Expenditure and Demand.

Generally, South East Water has sought to respond to issues that have been raised rather than comment on matters that appear to have been resolved. In addition, South East Water will raise any issues that have arisen after the release of the Draft Decision.

In summary, South East Water would like to focus on:

- Service Standards – an alternative approach for deriving service standard measures.
- Operating Costs – Focusing on double counting of savings, Victorian Competition and Efficiency Commission initiatives, bulk charges, T155 management costs and non-prescribed costs.
- Capital Costs – Focusing on water mains, cost escalation and the Northern Victorian Irrigation Renewal Project.
- Demand Forecasts – Issues relating to price elasticity, timing of changes to restriction and the impact of restrictions.
- Tariff Structures – Increased emphasis on water volumetric tariffs.

As an overall comment however, it would appear as if the Commission has made a major shift in risk from our original balanced approach to one more weighted towards customers with respect to cost and demand.

## 2. Service Standards

### 2.1 Draft Decision

The Commission approved four of South East Water's proposed core service standards and proposed that the remainder be reset to reflect the average of the period 2005/06 to 2008/09.

## 2.2 South East Water Response

Ongoing drought, poor rainfall, drying soil conditions, customer expectations on water wastage and consequent changed worked practices have created service outcomes over the last four years that would not match a more longer term set of average outcomes.

Therefore in preparing its 2009 Water Plan, and in anticipation of conditions returning to normal, South East Water set targets for a range of measures that reflected a longer term view rather than the three years of the 2005 Water Plan period.

While we understand the Commission's desire the ensure service standards do not deteriorate, South East Water believes that a more pragmatic approach to setting targets is required rather than adopting the three years of the 2005 Water Plan. That is, service measures that are significantly impacted by climate change need separate consideration.

In response to the Draft Decision therefore, we have proposed new targets for activities directly related to climate change and accept all others proposed by the Commission.

The two key measures are unplanned water interruptions per 100 km (a direct function of bursts, etc resulting from drying soil conditions over the last few years) and sewer blockages per 100 km (a direct result of tree root intrusion). As outlined in the charts below there has been a significant increase from a low base year in 2005/06.

It is our view that the three years average including current forecasts for 2008/09 will reflect likely ongoing dry conditions over the next four years.

Further there are a number of other measures that link directly to bursts / blockages; namely measures like frequency, duration and minutes off supply. We therefore propose the adoption of the last three years including 2008/09 be applied to those measures as well.

The revised tables of standard measures is as follows.

Note that all additional measures are accepted as per the Draft Decision.

Service Standard	3 yr avg 2005- 08	Draft Decision					Revised Proposal based on 2006-2008 Average			
		2009- 10	2010- 11	2011- 12	2012- 13	Comment	2009- 10	2010- 11	2011- 12	2012- 13
Water										
Unplanned water supply interruptions (per 100km)	29.6	29.6	29.6	29.6	29.6	Impacted by climate change – refer to Note 1 below.	31.2	31.2	31.2	31.2
Average time taken to attend bursts and leaks (priority 1) (minutes)	37.2	40	40	40	40	Accepted				
Average time taken to attend bursts and leaks (priority 2) (minutes)	110.5	120	120	120	120	Accepted				
Average time taken to attend bursts and leaks (priority 3) (minutes)	945.8	550	550	550	550	Accepted				
Unplanned water supply interruptions restored within 5 hours (%)	99.7	99.6	99.6	99.6	99.6	Accepted				

Service Standard	3 yr avg 2005- 08	Draft Decision				Comment	Revised Proposal based on 2006-2008 Average			
		2009- 10	2010- 11	2011- 12	2012- 13		2009- 10	2010- 11	2011- 12	2012- 13
Planned water supply interruptions restored within 5 hours (%)	78.5	78.5	78.5	78.5	78.5	Accepted				
Average unplanned customer minutes off water supply (minutes)	17.2	17.2	17.2	17.2	17.2	Impacted by climate change – refer to Note 2 below	17.6	17.6	17.6	17.6
Average planned customer minutes off water supply (minutes)	7.7	7.7	7.7	7.7	7.7	Accepted				
Average frequency of unplanned water supply interruptions	0.20	0.20	0.20	0.20	0.20	Impacted by climate change – refer to Note 3 below	0.21	0.21	0.21	0.21
Average frequency of planned water supply interruptions	0.04	0.04	0.04	0.04	0.04	Accepted				

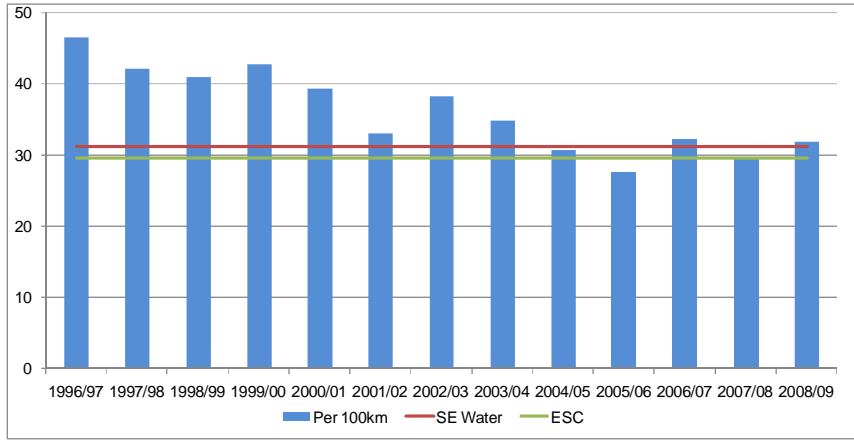


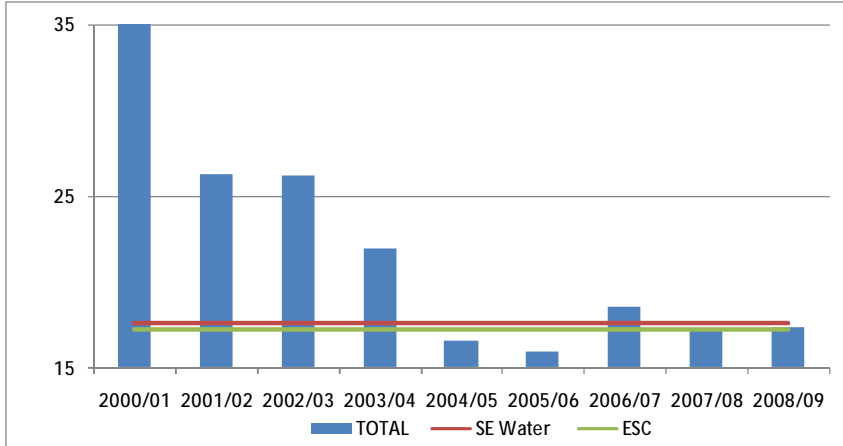
Service Standard	3 yr avg 2005- 08	Draft Decision				Comment	Revised Proposal based on 2006-2008 Average			
		2009- 10	2010- 11	2011- 12	2012- 13		2009- 10	2010- 11	2011- 12	2012- 13
Average duration of unplanned water supply interruptions (minutes)	87.8	87.8	87.8	87.8	87.8	Accepted				
Average duration of planned water supply interruptions (minutes)	205.6	205.6	205.6	205.6	205.6	Accepted				
Customers experiencing more than 5 unplanned water supply interruptions p.a. (number)	139	139	139	139	139	Impacted by climate change – refer to Note 4 below	209	209	209	209
Unaccounted for water (%)	9.5	9.5	9.5	9.5	9.5	Accepted				
<b>Sewerage</b>										
Sewerage blockages (per 100km)	19.5	19.5	19.5	19.5	19.5	Impacted by climate change – refer to Note 5 below	21.3	21.3	21.3	21.3

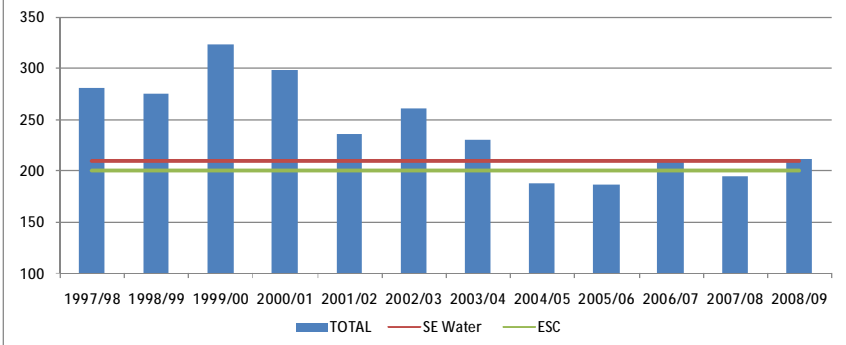
Service Standard	3 yr avg 2005- 08	Draft Decision				Comment	Revised Proposal based on 2006-2008 Average			
		2009- 10	2010- 11	2011- 12	2012- 13		2009- 10	2010- 11	2011- 12	2012- 13
Average time to attend sewer spills and blockages (minutes)	45.9	45.9	45.9	45.9	45.9	Impacted by climate change – refer to Note 6 below	48.3	48.3	48.3	48.3
Total time taken to rectify blockage (minutes)	161	161	161	161	161	Accepted				
Sewer spills contained within 5 hours (%)	100	100	100	100	100	Accepted				
Customers receiving more than 3 sewer blockages p.a. (number)	2.7	2.7	2.7	2.7	2.7	Changed definition refer to Note 7 below	0	0	0	0
<b>Customer service</b>										
Complaints to EWOV (per 1000 customers)	0.15	0.15	0.15	0.15	0.15	Refer to Note 8 below	0.164	0.164	0.164	0.164
Telephone calls answered within 30 seconds (%)	97.2	97.2	97.2	97.2	97.2	Refer to Note 9 below	94	94	94	94

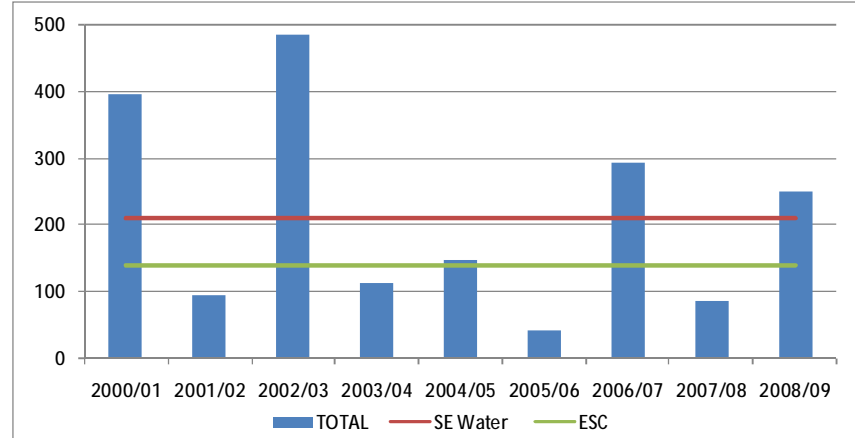
## Notes

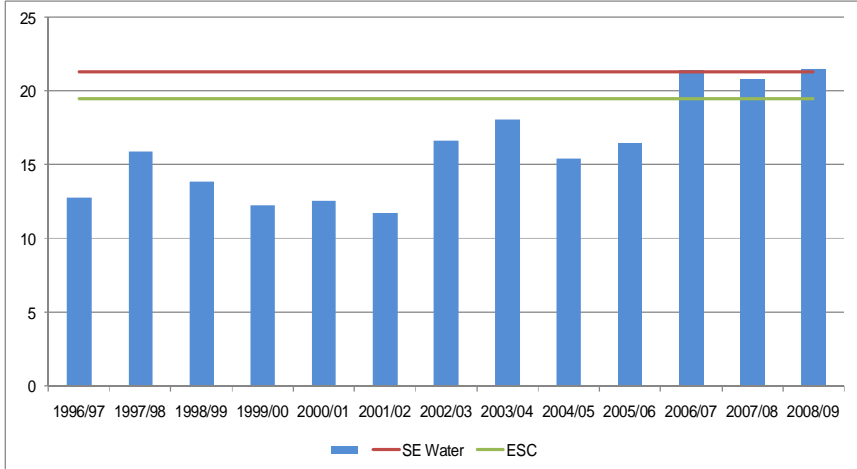
	2008/09 Forecast does not meet Draft Decision Target
	2008/09 Forecast does not meet Proposed Target

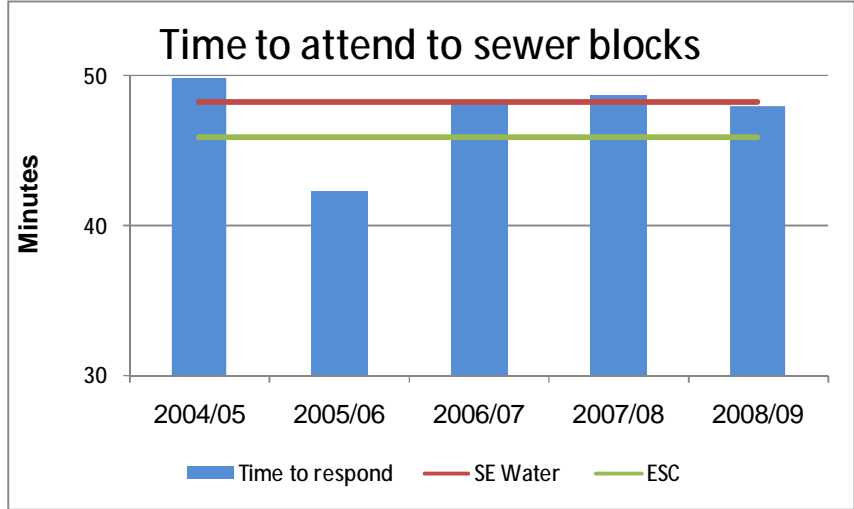
Water	Water Plan	Draft Decision	2008/09 forecast	Revised	
<b>1. Unplanned water supply interruptions (per 100 km)</b>  <u>Averages</u>  06/09 = 31.2  03/08 = 31.0  00/08 = 33.2	35	29.6	31.8	31.2	
<p>The current continued dry period has resulted in relatively stable ground conditions and, as a result, the 2005/2008 three year average is based on two of the three lowest annual interruption rates experienced by South East Water.</p> <p>South East Water's strategies for operations, remediation and renewal are based on maintaining a relatively steady level of interruptions that optimises whole of community costs over the long term. However if there is a return to wetter conditions bursts will increase closer to long term average, as extreme moisture changes in the soils move and stress some of the more vulnerable pipes.</p>					

Water	Water Plan	Draft Decision	2008/09 forecast	Revised																																									
<b>2. Average unplanned customer minutes off water supply (minutes)</b>  <u>Averages</u>  06/09 = 17.6  03/08 = 18.0  00/08 = 22.2	22	17.2	17.3	17.6	 <table><caption>Approximate data from the bar chart</caption><thead><tr><th>Year</th><th>TOTAL (minutes)</th><th>SE Water (minutes)</th><th>ESC (minutes)</th></tr></thead><tbody><tr><td>2000/01</td><td>35</td><td>17.5</td><td>16.5</td></tr><tr><td>2001/02</td><td>26</td><td>17.5</td><td>16.5</td></tr><tr><td>2002/03</td><td>26</td><td>17.5</td><td>16.5</td></tr><tr><td>2003/04</td><td>20</td><td>17.5</td><td>16.5</td></tr><tr><td>2004/05</td><td>15</td><td>17.5</td><td>16.5</td></tr><tr><td>2005/06</td><td>15</td><td>17.5</td><td>16.5</td></tr><tr><td>2006/07</td><td>18</td><td>17.5</td><td>16.5</td></tr><tr><td>2007/08</td><td>16</td><td>17.5</td><td>16.5</td></tr><tr><td>2008/09</td><td>16</td><td>17.5</td><td>16.5</td></tr></tbody></table>	Year	TOTAL (minutes)	SE Water (minutes)	ESC (minutes)	2000/01	35	17.5	16.5	2001/02	26	17.5	16.5	2002/03	26	17.5	16.5	2003/04	20	17.5	16.5	2004/05	15	17.5	16.5	2005/06	15	17.5	16.5	2006/07	18	17.5	16.5	2007/08	16	17.5	16.5	2008/09	16	17.5	16.5
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If unplanned interruptions increase, as discussed above, minutes off supply will increase as well.																																													

Water	Water Plan	Draft Decision	2008/09 forecast	Revised																																																					
<div>3.      <b>Average frequency of unplanned water supply interruptions (number)</b></div> <div><u>Averages</u></div> <div>06/09 = 0.205</div> <div>03/08 = 0.202</div> <div>00/08 = 0.226</div>	0.23	0.20	0.211	0.21	<div><table><caption>Unplanned Water Supply Interruptions (Number)</caption><thead><tr><th>Financial Year</th><th>TOTAL</th><th>SE Water</th><th>ESC</th></tr></thead><tbody><tr><td>1997/98</td><td>280</td><td>210</td><td>200</td></tr><tr><td>1998/99</td><td>275</td><td>210</td><td>200</td></tr><tr><td>1999/00</td><td>320</td><td>210</td><td>200</td></tr><tr><td>2000/01</td><td>295</td><td>210</td><td>200</td></tr><tr><td>2001/02</td><td>235</td><td>210</td><td>200</td></tr><tr><td>2002/03</td><td>260</td><td>210</td><td>200</td></tr><tr><td>2003/04</td><td>230</td><td>210</td><td>200</td></tr><tr><td>2004/05</td><td>185</td><td>210</td><td>200</td></tr><tr><td>2005/06</td><td>185</td><td>210</td><td>200</td></tr><tr><td>2006/07</td><td>210</td><td>210</td><td>200</td></tr><tr><td>2007/08</td><td>195</td><td>210</td><td>200</td></tr><tr><td>2008/09</td><td>210</td><td>210</td><td>200</td></tr></tbody></table></div>	Financial Year	TOTAL	SE Water	ESC	1997/98	280	210	200	1998/99	275	210	200	1999/00	320	210	200	2000/01	295	210	200	2001/02	235	210	200	2002/03	260	210	200	2003/04	230	210	200	2004/05	185	210	200	2005/06	185	210	200	2006/07	210	210	200	2007/08	195	210	200	2008/09	210	210	200
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2008/09	210	210	200																																																						
<div>South East Water has a valve insertion program in place to, where practicable, reduce the number of customers affected by an interruption. However, if unplanned interruptions increase, as discussed above, average frequency will increase as well.</div>																																																									

Water	Water Plan	Draft Decision	2008/09 forecast	Revised																																									
<b>4. Number of customers experiencing more than 5 unplanned water supply interruptions in the year (number)</b>  <u>Averages</u>  06/09 = 209  03/08 = 135  00/08 = 206	235	139	250	209	 <table><caption>Estimated data from the bar chart</caption><thead><tr><th>Year</th><th>TOTAL</th><th>SE Water</th><th>ESC</th></tr></thead><tbody><tr><td>2000/01</td><td>400</td><td>210</td><td>140</td></tr><tr><td>2001/02</td><td>100</td><td>210</td><td>140</td></tr><tr><td>2002/03</td><td>480</td><td>210</td><td>140</td></tr><tr><td>2003/04</td><td>120</td><td>210</td><td>140</td></tr><tr><td>2004/05</td><td>150</td><td>210</td><td>140</td></tr><tr><td>2005/06</td><td>50</td><td>210</td><td>140</td></tr><tr><td>2006/07</td><td>300</td><td>210</td><td>140</td></tr><tr><td>2007/08</td><td>90</td><td>210</td><td>140</td></tr><tr><td>2008/09</td><td>250</td><td>210</td><td>140</td></tr></tbody></table>	Year	TOTAL	SE Water	ESC	2000/01	400	210	140	2001/02	100	210	140	2002/03	480	210	140	2003/04	120	210	140	2004/05	150	210	140	2005/06	50	210	140	2006/07	300	210	140	2007/08	90	210	140	2008/09	250	210	140
Year	TOTAL	SE Water	ESC																																										
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2007/08	90	210	140																																										
2008/09	250	210	140																																										
<p>Measures for managing this have included decreasing shut off block sizes by installing additional valves. Although these programs continue, further opportunities for improvement are now limited. The results for this measure also vary significantly.</p> <p>It should be noted that the forecast for this year is 250, which would make South East Water's three year (2006/2009) average closer to the longer term target of 235 than the 139 provided for in the Draft Decision.</p>																																													

Sewerage	Water Plan	Draft Decision	2008/09 forecast	Proposed Target 2006/09 average																													
<div>5. Sewerage blockages (per 100km)</div> <div>Averages</div> <div>06/09 = 21.3</div> <div>03/08 = 18.5</div> <div>00/08 = 16.7</div>	22.5	19.5	21.5	21.3	<div><table><caption>Sewerage Blockages (per 100km) Data</caption><thead><tr><th>Year</th><th>Blockages (per 100km)</th></tr></thead><tbody><tr><td>1996/97</td><td>13.0</td></tr><tr><td>1997/98</td><td>16.0</td></tr><tr><td>1998/99</td><td>14.0</td></tr><tr><td>1999/00</td><td>12.5</td></tr><tr><td>2000/01</td><td>12.8</td></tr><tr><td>2001/02</td><td>12.0</td></tr><tr><td>2002/03</td><td>16.8</td></tr><tr><td>2003/04</td><td>18.2</td></tr><tr><td>2004/05</td><td>15.5</td></tr><tr><td>2005/06</td><td>16.5</td></tr><tr><td>2006/07</td><td>21.5</td></tr><tr><td>2007/08</td><td>21.0</td></tr><tr><td>2008/09</td><td>21.5</td></tr></tbody></table></div>	Year	Blockages (per 100km)	1996/97	13.0	1997/98	16.0	1998/99	14.0	1999/00	12.5	2000/01	12.8	2001/02	12.0	2002/03	16.8	2003/04	18.2	2004/05	15.5	2005/06	16.5	2006/07	21.5	2007/08	21.0	2008/09	21.5
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<div>The Commission’s proposed target has not been achieved in the last two years of the three year average. There has been an increasing trend in blockages caused by tree roots over the past couple of years. This is due to tree roots entering trenches and pipes in search of moisture as a result of the drought. Additional cleaning activities recently introduced were intended to stabilise blockages at around current levels and will require some time to reduce blockages below this level.</div>																																	

Sewerage	Water Plan	Draft Decision	2008/09 forecast	Proposed Target 2006/09 average	
<b>6. Average time to attend sewer spills and blockages (minutes)</b>  <u>Averages</u>  06/09 = 48.3  04/08 = 47.9	56	45.9	48	48.3	
<p>The Commission's proposed target was not achieved in the last two years of the three year average. Also the 2008/09 result is forecast to be 48. An exceptional year in 2005/06, due to the low rate of blockages experienced in that year, has adversely impacted on the Commission's proposed target. The increasing number of blockages will also lead to increases in times to attend because of the extra call on resources.</p>					



<b>7. Customers receiving 3 sewer blockages in the year (number)</b>	8	2.7	6	0	<p>The Commission's definition for this indicator relates to blockages in the sewer reticulation system, while South East Water pays a GSL for blockages in the reticulation system and in House Connection Branches. The figures provided incorrectly related to the GSL definition. In order to match the other businesses definition, South East Water proposes to report reticulation blockages only and therefore our three year average results are zero and the target should be zero.</p>
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Customer Service	Water Plan	Draft Decision	2008/09 forecast	Proposed Target 2006/09 average																																					
8. EWOV complaints  <u>Average</u>  06/09 = 0.164	0.15	0.15	0.196	0.164	<table><caption>EWOV Complaints Data (Estimated)</caption><thead><tr><th>Year</th><th>TOTAL</th><th>SE Water Target</th><th>ESC Target</th></tr></thead><tbody><tr><td>2001/02</td><td>0.33</td><td>0.164</td><td>0.15</td></tr><tr><td>2002/03</td><td>0.12</td><td>0.164</td><td>0.15</td></tr><tr><td>2003/04</td><td>0.11</td><td>0.164</td><td>0.15</td></tr><tr><td>2004/05</td><td>0.13</td><td>0.164</td><td>0.15</td></tr><tr><td>2005/06</td><td>0.16</td><td>0.164</td><td>0.15</td></tr><tr><td>2006/07</td><td>0.15</td><td>0.164</td><td>0.15</td></tr><tr><td>2007/08</td><td>0.15</td><td>0.164</td><td>0.15</td></tr><tr><td>2008/09</td><td>0.19</td><td>0.164</td><td>0.15</td></tr></tbody></table>	Year	TOTAL	SE Water Target	ESC Target	2001/02	0.33	0.164	0.15	2002/03	0.12	0.164	0.15	2003/04	0.11	0.164	0.15	2004/05	0.13	0.164	0.15	2005/06	0.16	0.164	0.15	2006/07	0.15	0.164	0.15	2007/08	0.15	0.164	0.15	2008/09	0.19	0.164	0.15
Year	TOTAL	SE Water Target	ESC Target																																						
2001/02	0.33	0.164	0.15																																						
2002/03	0.12	0.164	0.15																																						
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2004/05	0.13	0.164	0.15																																						
2005/06	0.16	0.164	0.15																																						
2006/07	0.15	0.164	0.15																																						
2007/08	0.15	0.164	0.15																																						
2008/09	0.19	0.164	0.15																																						
Increased EWOV complaints in recent years are believed to be as a result of increase awareness amongst customers of the EWOV scheme, rather than changes to work practices. Therefore South East Water proposes a higher target taking into account the actual level of complaints recorded recently.																																									

Customer Service	Water Plan	Draft Decision	2008/09 forecast	Proposed Target 2006/09 average	
9. Calls answered within 30 seconds (per cent)	94	97.2	96.7	94	<p>The Draft Decision has included a combined target of 97.2% as an approved target for both account calls and fault calls but has also accepted the two as additional service standards with the proposed targets of 96% and 93% respectively.</p> <p>South East Water proposed the two separate targets to try to balance call waiting times with the time needed to properly assist customers meet their needs, particularly in terms of providing water saving solutions. As such, a slight drop off in call answering times will be needed if existing resourcing levels are to be maintained.</p> <p>Should it be the case that the Commission intends to approve a single service core service standard, the number needs to reflect the relative weightings between fault and account calls. In this case the standard proposed would be 94%.</p>

### **3. Guaranteed Service Levels (GSLs)**

#### **3.1 Draft Decision**

South East Water originally proposed to maintain the existing GSL events and amounts payable in order to minimise price increases. The Commission's Draft Decision concludes that the current GSL events be approved but proposes to double the amount payable for each event.

The Commission also requires retailers to develop an additional GSL that relates to compliance with hardship policies.

#### **3.2 South East Water Response**

South East Water accepts the Commission's proposal to double the payment levels, but expects the Commission to double the operating costs previously estimated to pay GSL's. This is equivalent to an additional \$30k pa.

South East Water is currently investigating the best mechanism for introducing a hardship related GSL, in conjunction with the other retailers. However, given the short amount of time available to consult customers and other stakeholders prior to the commencement of the 2009/10 financial year, South East Water proposes to introduce this GSL at the commencement of the 2010/11 financial year. South East Water has not proposed any additional expenditure to fund this GSL.

### **4. Operating Expenditure**

#### **4.1 Cost Escalation**

##### **4.1.1 Draft Decision**

The Commission proposed a \$5.2m reduction to a range of miscellaneous activities from South East Water's original Water Plan.

#### **4.1.2            *South East Water Response***

South East Water's Water Plan was based on labour escalation of 2.5% in real terms. However, based on subsequent advice from Treasury, South East Water has accepted labour escalation of 1.5%. As this category predominately relates to contract labour based costs some of the adjustment is warranted.

However, a small component of this category relates to plant costs for which the Commission has assumed no real price increase over the regulatory period. South East Water remains of the view that plant costs will exceed CPI over the regulatory period as approx 40% of leases associated with the field maintenance truck fleet used by South East Water's alliance partners (Thiess) are expiring in 2009/10. Recent quotes indicate increases in lease rates in the order of 15%. This represents a one-off increase in operating cost forecasts for plant in 2009/10 of approximately \$80k.

### **4.2            *Victorian Competition and Efficiency Commission (VCEC) Inquiry***

#### **4.2.1            *Draft Decision***

The Draft Decision combined the costs of implementing all the VCEC recommendations with the proposed shared services savings. The Draft Decision recommended a \$2.5m reduction in costs compared to South East Water's Water Plan. The Commission assumes that full savings will be achieved by 2011/12.

#### **4.2.2            *South East Water Response***

South East Water considers that the two aspects of VCEC (implementation costs and shared services savings) should be treated differently. Firstly, additional costs will be incurred to implement the VCEC outcomes including the transition to a statutory authority, the implementation of third party access and financial ringfencing. As a consequence South East Water included \$1m in the original Water Plan submission to account for these expenses. Our view remains that \$1m is a fair estimate and appropriate to be recovered through regulated tariffs.

Secondly, on the basis of the status report included as Attachment 1, South East Water continues to believe that the savings resulting from shared services need to be scaled up to \$2mpa in 2012/13 over the course of the regulatory period, not within two years.

## **4.3 Labour**

### **4.3.1 Draft Decision**

The Draft Decision proposed a reduction of \$8.8m in labour costs over four years with respect to the Water Plan.

### **4.3.2 South East Water Response**

South East Water originally proposed labour escalation of 2.5% in real terms. While the Commission's assumption of 1.5% real increase per annum is considered satisfactory on the basis of advice from Treasury, the Commission's method of recalculating labour forecasts creates a significant variance.

The variance predominantly relates South East Water's labour forecasts for field operations and maintenance. The reason for the variance lies within the methodology used by South East Water to allocate field operations and maintenance forecasts across labour inputs (eg, labour, materials, plant, electricity, chemicals, etc).

Forecasts for field operations and maintenance were developed at an activity level (ie preventative maintenance, remedial maintenance, operations etc.) for each major service (ie water, sewer, sewage treatment plants and recycling). In order to break-down the activity forecasts into cost inputs (eg, labour, materials, plant, electricity, chemicals, etc), they were allocated in proportion to 2008/09 cost input budgets.

The result is that movements in cost input forecasts are correlated to movements in each major service total. For example, if the total STP opex forecast for 2009/10 increases by 10% from 2008/09, then it was assumed that every cost input increased by 10%. Therefore, notionally, labour forecasts increase by 10% even though there may not be additional staff numbers forecast.

The impact is that whilst total operating expenditure has been estimated appropriately at a major service level (eg total STP opex), there is likely to be a 'mix' issue between cost inputs (ie between labour, materials, plant, electricity, chemicals, etc).

## **4.4 Electricity**

### **4.4.1 Draft Decision**

The Draft Decision proposes a \$3.4m reduction in electricity costs over the four years.

### **4.4.2 South East Water Response**

South East Water has factored both price and volume increases into its estimates. Whilst the Commission's growth factors are considered low in respect of electricity volumes, South East Water is comfortable that all electricity costs can be accommodated provided the issues raised in 4.3 above are addressed.

## **4.5 Vehicle Operating Costs**

### **4.5.1 Draft Decision**

The Draft Decision proposed a reduction of \$0.6m in vehicle operating costs over four years with respect to the Water Plan.

### **4.5.2 South East Water Response**

South East Water's Water Plan was based on a 20% increase in fuel costs in year 1 and 10% pa thereafter. Given the changed economic circumstances, South East Water is prepared to accept the Commission's proposal for no real increase.

## **4.6 Chemicals**

### **4.6.1 Draft Decision**

The Draft Decision proposed a reduction of \$0.2m in chemical costs over four years with respect to the Water Plan.

#### **4.6.2            *South East Water Response***

South East Water is prepared to accept this change which reflects no real increases in costs.

### **4.7            *Billing and Collections***

#### **4.7.1            *Draft Decision***

The Commission has proposed that \$6.4m that was included in this category for bad debts be moved from operating expenditure to revenue not collected. The Commission has also proposed an additional \$1.5m reduction over the four year period in relation to costs that were originally estimated on the basis of overall price increases rather than transaction levels.

#### **4.7.2            *South East Water Response***

South East Water is prepared to accept a reduction in the level of increase applied to transaction based costs. However, South East Water has recently advised the Commission that an additional \$0.3m pa is required in the last two years of the Water Plan to account for expected increases in bill print costs. This amount was not included in the original Water Plan estimate.

The current bill printing contract was tendered and awarded in 2005/06 for a term of 5 years at a price which was significantly below market rates. A new contract will commence from 2011/12 which will be preceded by a market tender process. Printing costs are expected to increase significantly under the new contract for the following reasons:

- The current contract was awarded at rates significantly lower than the service provider's competitors; and
- Mergers in the printing industry since the last tender has resulted in less competition in the market place.



It is for these reasons that South East Water proposes to allow for an increase in bill printing costs from 2011/12 of 30%. (This equates to approximately an additional \$0.3M in 2011/12 and \$0.3M in 2012/13).

## **4.8 Conservation**

### **4.8.1 Draft Decision**

The Draft Decision combined the costs associated with water conservation and restrictions management and proposed a reduction of \$8.1m over four years, with respect to the Water Plan.

### **4.8.2 South East Water Response**

South East Water is of the view that the costs of managing restrictions and Target 155 (T155) should be treated separately from water conservation.

Whilst comfortable with the Commission's revisions in respect of water conservation, South East Water believes further consideration is required in relation to the Commission's decreases in restrictions/T155 management costs. Specifically, the Commission has allowed \$2.0M in 2009/10 for undertaking the T155 water conservation campaign which is consistent with forecasts for this year. A large proportion of this expenditure relates to payments to DSE for advertising (\$0.9M). South East Water expects this campaign to continue into 2009/10 and 2010/11 and will require similar investment as 2008/09. South East Water believes a minimum of \$1.0M will be required to adequately deliver the T155 campaign in 2010/11.

## **4.9 Brainwaves Cup**

### **4.9.1 Draft Decision**

The Draft Decision proposed to remove the \$2.0m over four years proposed by South East Water to cover costs associated with the Brainwaves Cup.

### **4.9.2 South East Water Response**

The Brainwaves Cup although highly visible, is only one element of South East Water's innovation program. However in preparing the Water Plan, South East Water included existing labour costs for the overall innovation program (\$0.2m pa) as well as seed funding for the brainwaves program (\$0.3m pa). South East Water believes that the labour component represents business as usual and therefore should be retained in order to deliver efficiency improvements. South East Water is prepared to remove the seed fund allowance.

## **4.10 Environmental Contribution**

### **4.10.1 *Draft Decision***

The Draft Decision proposes a \$0.6m increase over the four year period for the Environmental Contribution.

### **4.10.2 *South East Water Response***

Based on the Commission's assumption of 2.5% inflation for the entire regulatory period, South East Water agrees with the adjustment. If however, Treasury's corporate planning assumptions of 2% inflation for 09/10 and 2.5% thereafter are used, an additional \$0.075M pa must be added to South East Water's Water Plan forecasts.

## **4.11 Guaranteed Service Levels**

The cost of GSL's will increase by an additional \$0.03m pa to fund the increased GSL payment levels.

## **4.12 Financial Reporting Obligations**

From 2009/10 South East Water will be obligated to account for and disclose additional financial information in respect of its infrastructure assets. The Department of Treasury and Finance have mandated that all public sector entities account for infrastructure assets on a fair value basis as stipulated in AASB1049 "Whole of Government and General Government Sector Financial Reporting". System enhancements, process and disclosure changes are expected to cost \$0.2M in 2009/10 and then \$0.1M pa

thereafter. These expenses were not included in our original Water Plan and approval is now sought for its inclusion.

#### **4.13 Double Counting**

Some of the ESC's opex adjustments appear to be 'double counted'. That is, adjustments made to expenditure items (eg labour) appear to have been made by the Commission independently to adjustments to expenditure programs (eg water conservation). The result is that where the affected expenditure accounts appear within the expenditure programs, a double count will occur. For example, the ESC has reduced the total labour forecast in 2009/10 by \$2.10M. Independently to this, the water conservation program has been reduced by \$0.85M, which includes labour costs. This means that the labour associated with water conservation has been reduced on two fronts, hence the 'double count'.

#### **4.14 Northern Victorian Irrigation Renewal Project (NVIRP)**

The Commission's Draft Decision was based on the premise that Melbourne Water would fund the \$300m payable to fund this project which would be recovered from retailers through bulk charges.

However this arrangement has now been reconsidered. The revised assumption for the Water Plan is to include the capital expenditure in the retailer's regulatory asset value and exclude this amount from Melbourne Water's regulatory asset value. This requires adjustments to be made to increase South East Water's capital expenditure and reduce the amount payable to Melbourne Water as bulk charges. For the purpose of forecasting revenue bulk charges have been reduced by \$20.9m over four years.

South East Water understands that the Commission will amend the amount included for bulk charges taking into account the amendments related to NVIRP as well as other changes.

This amendment will have no material impact on the final charge to customers but will impact on South East Water's cash flow estimates.

#### **4.15 Treatment of Parks and Drainage Billing Fees**

South East Water originally allocated costs equivalent to the revenues received from Melbourne Water and Parks Victoria to non-prescribed. South East Water understands that the Commission has allocated costs differently for the other two retailers and therefore requests that the Commission makes a consistent allocation for South East Water.

This is expected to result in additional prescribed costs in the order of \$0.8m pa.

#### **4.16 Bulk Charges**

In its amendment to bulk charges to reflect adjustments to Melbourne Water's charges, the Commission has omitted some minor expenses originally included by South East Water as bulk charges. These expenses are payable to Goulburn Murray Water, West Gippsland Catchment Management Authority (CMA) and Melbourne Water (Class C recycled water).

The Goulburn Murray charges are an outcome of the of the Commission's 2008 Water Price Review for Regional and Rural Businesses which allowed Goulburn Murray to charge a regional Urban Storage Ancillary Fee. South East Water understands that the Commission is currently reviewing Goulburn Murray Water's 2009/10 tariffs. Therefore the amount allowed for this fee may need to be adjusted in accordance with the Commission's Final Decision. This charge should apply to South East Water on the basis of a one third share and reflect the 75GL savings.

The payment to West Gippsland CMA is in relation to the qualification of environmental flows imposed by the Minister on the Thompson River. This payment is only required when restrictions are more severe than stage 2. Therefore this expense has been included for 2009/10 only.

An allowance has also been made for a payment to Melbourne Water for the purchase of Class C water from the South Eastern Outfall.

Operating Expenditure \$M	2009/10	2010/11	2011/12	2012/13
Draft Decision Operating Expenditure (\$M)	332.9	366.9	439.1	516.7
South East Water Recommended Adjustments				
Operating Cost Escalation	+0.1	+0.1	+0.1	+0.1
VCEC Savings	+1.0	+1.0	+0.5	
Labour Costs Inc Superannuation	+2.6	+2.3	+2.3	+2.3
Electricity	-	-	-	-
Vehicle Operating Costs	-	-	-	-
Chemicals	-	-	-	-
Billing and Collections	-	-	+0.3	+0.3
Water Conservation	-	-	-	-
Restrictions	+0.3	+1.0		
Brainwaves Cup	+0.2	+0.2	+0.2	+0.2
Changes to Accounting Standards	+0.2	+1.1	+1.1	+1.1
GSL's	+0.03	+0.03	+0.03	+0.03
Reallocation from Non-Prescribed to Prescribed	+0.8	+0.8	+0.8	+0.8
Environment Contribution	+0.1	+0.1	+0.1	+0.1
Bulk - NVIRP	-2.3	-3.8	-6.0	-8.9
Bulk – RUFAS, West Gipps & Class C	0.2	0.4	0.4	0.4
<b>Total Revised Operating Expenditure</b>	<b>\$336.2</b>	<b>\$369.0</b>	<b>\$437.8</b>	<b>\$512.1</b>

## 5. Capital Expenditure

### 5.1 Water Mains

#### 5.1.1 *Draft Decision*

The Commission proposed an expenditure reduction of \$10.5m over the four years on the basis of deferring lower priority replacements.

#### 5.1.2 *South East Water Response*

The Halcrow recommendation to defer this expenditure was made on the basis of a moderate risk ranking applied by South East Water, which was interpreted as indicating that these mains are less likely to fail. However, this moderate ranking is actually based on the likelihood of failure and the impact of failure. That is, the distribution mains that were proposed to be renewed all had a high likelihood of failure. The mains that have been proposed to be deferred were expected to have a lower impact of failure than the higher ranked mains.

In addition one of the mains that was recommended to be deferred (Centre Road) has recently undergone a further condition assessment and had its poor condition verified. The likelihood of failure in this instance has increased.

South East Water proposes that expenditure for water main renewals be retained, as follows:

LOCATION	PIPE SIZE	CONST. YEAR	MAT'L	LENGTH (KM)	REMAIN. LIFE	UNIT RATE (\$/m)	COST (\$'000)	2008/09 (\$,000)	2009/10 (\$'000)	2010/11 (\$'000)	2011/12 (\$,000)	2012/13 (\$'000)	COMMENTS
Chapel St Prahran	300/225	1863	CICL	2.45	-23	2600	6370	100	6270				Rate based on Chapel St Project Approval
Jasper Rd, Bentleigh	300	1899	CICL	1.2	-9	1200	1440			1440			Works in quieter traffic streets, day works utilised, outer suburb- still requires extensive traffic management
Centre Rd. East Bentleigh	525	1911	WI	1.46	-7	2500	3650			3650			Rate based on Chapel St, busy shopping district and larger pipe size.
Bluff Rd, Sandringham	300	1911	CICL	2.45	3	1200	2940				2940		Works in quieter traffic streets, day works utilised, outer suburb- still requires extensive traffic management
Yarra St, Sth Yarra	300	1914	CICL	0.32	6	1200	384				384		Local St works - experience tells us rates likely to be expensive due to space constraints and reinstatement costs.
City Rd. Sth Melb	300	1875	CICL	0.3	-11	1200	360				360		Works in quieter traffic streets, day works utilised, still requires extensive traffic management
Warrigal Rd, Oakleigh	600	1911	CICL	0.48	3	2500	1200				1200		Rate based on Chapel St, arterial road and larger pipe size.
St Kilda Rd Stage 2	250	1868	CICL	3.35	-18	1500	5025					5025	Reduced rate based compared to Stage 1 works as main located out of traffic lanes.
<b>TOTALS</b>								<b>100</b>	<b>6270</b>	<b>5090</b>	<b>4884</b>	<b>5025</b>	
<b>LENGH (KM)</b>								<b>0</b>	<b>2.5</b>	<b>2.7</b>	<b>3.6</b>	<b>3.7</b>	

## **Sewer Renewals - Gravity**

### **5.1.3           *Draft Decision***

The Commission proposed an expenditure reduction of \$3.8m over the four years.

### **5.1.4           *South East Water Response***

South East Water accepts this amendment.

## **5.2           Mt Martha**

### **5.2.1           *Draft Decision***

The Commission recommended a minor timing change to the expenditure profile.

### **5.2.2           *South East Water Response***

South East Water accepts this amendment.

## **5.3           Cost Escalation**

### **5.3.1           *Draft Decision***

The Commission proposed no real cost increases for capital expenditure.

### **5.3.2           *South East Water Response***

South East Water remains of the view that there will be capital cost increases during the regulatory period.

One area in which real increases can be justified is labour costs. The Commission has accepted real labour cost increases of 1.5% for operating expenditure. Therefore, as a minimum, South East Water expects that similar increases are allowed for capital expenditure cost categories that involve labour (ie excluding non- labour related categories such as land acquisition).



In order to determine the labour component of capital expenditure, South East Water has analysed a range of typical projects and concluded that on average 30% of the total cost relates to labour. These projects have been recently undertaken and are considered to be representative of the range of projects to be undertaken during the 2009/10 to 2012/13 period. Therefore South East Water has included 1.5% escalation on 30% of its capital works (not including expenditure on non-labour related categories such as land acquisition).

## **5.4 Northern Victorian Irrigation Renewal Project (NVIRP)**

As discussed above, the Commission's Draft Decision was based on the premise that Melbourne Water would fund the \$300m payable to fund this project which would be recovered from retailers through bulk charges.

However this arrangement has now been reconsidered. The revised assumption for the Water Plan is to include the capital expenditure in the retailer's regulatory asset value and exclude this amount from Melbourne Water's regulatory asset value. This requires adjustments to be made to increase South East Water's capital expenditure and reduce Melbourne Water's.

The three retailers have agreed to sharing their investment equally (ie one third contribution) and South East Water's capital expenditure profile over the period has been adjusted to reflect this commitment. No depreciation has been included in relation to this asset.

## **5.5 Cranbourne Treatment Plant**

The Commission has questioned the treatment of the sale of the Cranbourne Treatment Plant land and proposes to remove an amount from the 2007/08 capital expenditure to reflect the amount of regulated capital expenditure spent on rehabilitating the land. The Commission also asked South East Water to provide further information on why the sale value of the property should not be excluded from the asset base.

The Commission should note that the sale of this land has now been deferred. This means that South East Water will have to remove the proceeds from the sale of land

from all estimates until such time as feasibility studies indicate how/when the sale will proceed.

South East Water had previously treated the proceeds of sale as non-prescribed on the basis of past advice from the Commission and as the treatment plant had been decommissioned for a considerable period of time it was not an operating asset at the time the regulatory asset base was determined.

Therefore South East Water proposes that the 2007/08 capital expenditure on rehabilitating the land to original condition remain unchanged until such time as the sale of land is confirmed.

## 5.6 Capital Expenditure Summary

Capex (\$M)	2008/09	2009/10	2010/11	2011/12	2012/13
Draft Decision Capital Expenditure	123.0	153.6	148.0	136.2	128.4
South East Water Recommended Adjustments					
Water Main Replacements	-	+0.3	+4.0	+3.3	2.9
Dual pipe recycled Water	-	-	-	-	-
Sewer Renewals - Gravity	-	-	-	-	-
Sewer Renewals - Pressure	-	-	-	-	-
Hastings Industrial Project	-	-	-	-	-
Reduced scope of works 2008/09	-2.0				
<b>Baseline Total</b>	<b>121.0</b>	<b>153.9</b>	<b>152.0</b>	<b>139.5</b>	<b>131.3</b>
Capital Cost Escalation		0.6	1.4	1.9	2.3
<b>Revised Capital Expenditure</b>	<b>121.0</b>	<b>154.5</b>	<b>153.4</b>	<b>141.4</b>	<b>133.6</b>
<b>NVIRP</b>		56.67	26.67	6.67	10.00
<b>Total revised Capital Expenditure</b>	<b>121.0</b>	<b>211.2</b>	<b>180.0</b>	<b>148.0</b>	<b>143.6</b>

## **6. Weighted Average Cost of Capital (WACC)**

### **6.1 Draft Decision**

The Commission proposed a WACC of 4.8%, on the basis of a 2.55% debt margin. South East Water understands that in calculating this debt margin the Commission assumed that Treasury would be charging South East Water a financial accommodation levy of 110 basis points.

### **6.2 South East Water Response**

South East Water has correspondence from Government indicating that subject to the Commission's final decision, a financial accommodation levy of 200 basis points is to be charged for 2009/10. South East Water seeks to ensure that either the Commission's assumption for the debt margin is revised or confirmation is provided that the financial accommodation levy will be no more than 110 basis points.

South East Water has not made amendments to the WACC in its revised templates on the basis that the Commission is expected to recalculate the WACC on the basis of the most recent information available at the time of the Final Decision. It is expected that this amendment will also include changes to the debt margin.

### 6.3 Regulatory Asset Value (RAV)

Regulatory Asset Value (\$M 08/09)	2008/09	2009/10	2010/11	2011/12	2012/13
Opening RAV	\$1,871.3	\$1,929.5	\$2,070.9	\$2,180.5	\$2,253.8
<i>Plus</i>					
Gross Capital Expenditure	\$148.9	\$234.1	\$206.1	\$174.5	\$170.6
<i>Less</i>					
Customer Contributions – cash	\$27.9	\$27.9	\$26.6	\$27.0	\$27.2
Customer Contributions-gifted assets	\$28.0	\$22.9	\$26.1	\$26.5	\$27.0
Government Contributions	\$2.3	\$4.0	\$0.0	\$0.0	\$0.0
Disposals	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Regulatory Depreciation	\$32.5	\$37.9	\$43.8	\$47.7	\$49.6
<b>Closing RAV</b>	<b>\$1,929.5</b>	<b>\$2,070.9</b>	<b>\$2,180.5</b>	<b>\$2,253.8</b>	<b>\$2,320.7</b>
<b>Average RAV</b>	<b>\$1,900.4</b>	<b>\$2,000.2</b>	<b>\$2,125.7</b>	<b>\$2,217.2</b>	<b>\$2,287.3</b>

Note The regulatory depreciation calculated above is based on a weighted average remaining life of 62 years for existing assets and specific assets lives for new assets.

## 6.4 Revenue Requirement

Based on South East Water's proposed amendments to the Commission's Draft Decision and the amended RAV as shown above, South East Water's revenue requirement is as follows:

Revenue Requirement (\$M 2008/09)	2008/09	2009/10	2010/11	2011/12	2012/13
Return on Assets	\$91.2	\$96.0	\$102.0	\$106.4	\$109.8
Regulatory Depreciation	\$32.5	\$37.9	\$43.8	\$47.7	\$49.6
O&M Expenditure (inc Bulk)	\$289.2	\$336.2	\$369.0	\$437.8	\$512.1
Efficiency Carry-Over	-	-	-	-	-
Carryforward from 1st Period	-	-	-	-	-
Tax Wedge	\$9.3	\$9.2	\$10.4	\$11.1	\$11.4
<b>Benchmark Revenue Requirement</b>	<b>\$422.2</b>	<b>\$479.3</b>	<b>\$525.2</b>	<b>\$603.0</b>	<b>\$682.9</b>

## 7. Demand

### 7.1 Draft Decision

The Draft Decision proposed increased customer numbers (5,800 by 2012/13) to take into account the revised Victoria in Future forecasts and sales volumes (29GL over four years) based on the removal of price elasticity impacts, adjusting changes to restriction levels at 1 July instead of 30 November and reducing the overall impact of restrictions.

### 7.2 South East Water Response

**Customer Numbers** - While consistent with Victoria in Future 2008 (VIF08), the estimates of customer numbers provided by the Commission maintain customer growth at levels greater than those experienced during the recent building boom. South East

Water does not consider these levels of growth to be sustainable into the future given the declining levels of building approvals and the recent cuts to the first home buyers grant.

However, given the difficulty associated with justifying an alternative to the VIF, South East Water has based its estimates on the numbers provided by the Commission and reforecast demand on this basis. South East Water has also used this revised number of customers for the purpose of calculating the increased revenue received from new customer contributions.

**Demand** – There are four main discrepancies between South East Water’s estimates of sales volumes and that provided by the Commission.

1. Customer numbers – As noted above, South East Water has reforecast demand taking into account the higher customer numbers recommended by the Commission.
2. Price elasticity – The Commission has assumed that customers will not respond to price increases by reducing consumption at all. The Commission’s basis for this assumption is that price elasticity impacts are accounted for within South East Water’s estimates of water conservation. However, South East Water has always made specific adjustments to its forecast model to account for this potential overlap and the adjustments by the Commission have consequentially over estimated demand.

For residential customers, South East Water did not include any cumulative price elasticity from year to year in order to only add the price elasticity that results from behaviour change (ie shorter showers). The elements of price elasticity that accumulate as a result of the installation of new appliances (eg washing machines or shower heads) have specifically been excluded. South East Water has then compared price elasticity to restrictions and excluded elasticity where it is of a lesser impact. Therefore while no residential price elasticity was included in South East Water’s forecasts for the Water Plan, South East Water supports its inclusion in an environment where prices are rising and water use is unrestricted.

For non-residential customers South East Water has included cumulative price elasticity as these customers generally are only able to make savings of a more

permanent nature (ie new equipment or changes to production processes). The Commission is of the view that this double counts the impacts of the WaterMap program. However, South East Water had not included the ongoing impacts of Water Map in its original forecasts. South East water has only included the Water Map savings realised in 2007/08. Therefore, no double counting has occurred and the elasticity reduction needs to be reinstated.

3. Timing of restriction changes – Recent Government policy has been to announce changes to restriction levels in November after the winter/spring rain period. Therefore, where the restriction level is expected to change during the year, South East Water has included 5 months at the old level and 7 months at the new level. South East Water expects government to continue this practice and seeks re-instatement of the relevant volume reductions.
4. Impact of Restrictions on Demand – The Commission has concluded that the outcome of the T155 program is consumption averaging 155 litres per person per day across the customer base, while South East Water has based its estimate of water savings on the Drought Response Plan. South East Water has two issues with the Commission’s approach:

- The T155 program was designed by Government to achieve the savings required under stage 4, as indicated by the following quote from the Premier’s press release:

“Target 155 combined with Stage 3a water restrictions will achieve similar savings to Stage 4 while offering the community greater flexibility on how to achieve the target.”.

Should it be the case that Target 155 is not successful in achieving a level of water saving equivalent to stage 4, then it is reasonable to expect, if storage levels continue to decline, that the Government will revise the program, not accept that less savings are made; and

- Experience from Queensland also indicates that such a program can result in lower than expected consumption (T140 program resulted in 128 litres per person per day).

The T155 program is asking customers to limit their consumption to 155 litres per person per day. If those customers that are already using less than 155 litres per person per day do nothing and the customers who are using more



than 155 litres per person per day reduce their consumption, then mathematically, the average across the customer base is likely to be less than 155.

For the above reason's South East Water is of the view that the Drought Response plan estimate of savings is the most valid number.

South East Water's revised demand forecasts taking into account all of the above are as follows:

Sales Volumes (GL)	2009/10	2010/11	2011/12	2012/13
South East Water Revised Water Plan	109.4	116.3	120.5	123.8
Draft Decision	112.7	126.2	126.2	133.6
South East Water Revised – Post Draft Decision	110.8	118.2	123.0	127.0

CUSTOMER NUMBERS				
	2009/10	2010/11	2011/12	2012/13
Number Of Water Customers - Residential	576,630	587,009	597,575	608,331
Number Of Water Customers - Non Residential	53,211	54,457	55,725	57,015
Number Of Sewer Customers - Residential	549,370	559,440	570,353	581,621
Number Of Sewer Customers - Non Residential	44,751	45,915	47,171	48,451
Recycled Customers - Residential Total	1,580	2,474	3,733	5,075
Trade Waste – Number of Customers by Category				
Annual Charge (<2,500kl)	7,378	7,599	7,820	8,041
Annual Charge (>2,500kl<OR=25,000kl)	282	290	298	307
Annual Charge (>25,000kl<OR=100,000kl)	38	39	40	42
Annual Charge (>100,000KL)	22	23	24	24
DEMAND (INCL RESTRICTIONS)				
	2009/10	2010/11	2011/12	2012/13
Volume Of Water Consumed Within Block 1 (kL) - Residential	64,195,829	64,572,532	64,567,521	64,437,153
Volume Of Water Consumed Within Block 2 (kL) - Residential	12,872,739	15,940,103	17,705,284	19,136,727
Volume Of Water Consumed Within Block 3 (kL) - Residential	4,034,743	6,575,284	8,060,782	9,279,123
Volume Of Water Consumed (kL) - Non Residential Total	29,680,765	31,086,245	32,653,314	34,191,431
Volume Of Sewerage Discharged (kL) - Residential	56,752,194	59,832,857	61,371,676	62,512,203
Volume Of Sewerage Discharged (kL) - Non Residential	14,227,080	15,006,722	15,695,199	16,224,663
Volume Of Trade Waste (kL)	5,520,490	5,507,520	5,476,170	5,443,361
Billable BODs (kg)	8,602,010	8,581,800	8,532,951	8,481,828
Billable SS (kg)	3,118,873	3,111,546	3,093,834	3,075,298
Billable TKN (kg)	463,698	462,609	459,975	457,220
Volume Of Recycled Water Consumer (kL) - Residential	166,472	296,355	420,133	566,853

## 8. Tariffs

### 8.1 Form of Price Control

South East Water accepts the Commission's proposal to introduce a hybrid form of price control which provides scope for adjustments to tariffs and/or prices during the period.

### 8.2 Uncertain Events

South East Water continues to support introduction of a mechanism for within-period or end-of-period price adjustments to take account of uncertain and unforeseen events. However, South East Water considers that the operation of this mechanism would be enhanced by specification in advance of the degree of divergence from original estimates required before an application for an adjustment could be made.

### 8.3 Price Increases

In order to recover the above revenue, South East Water proposes average real price increases as follows for the 2009/10 to 2012/13 regulatory period:

Real Price Increase (%)	2009/10	2010/11	2011/12	2012/13
Average Price Increase	16	15	11.5	7.4

### 8.4 Sewage Disposal Charge (SDC)

#### 8.4.1 *Draft Decision*

The Commission has proposed to approve a proposal by Yarra Valley Water to vary the seasonal indices used to calculate the SDC, according to the level of restrictions in

place. The Commission has also asked South East Water and City West Water to consider making a similar amendment.

#### **8.4.2 South East Water Response**

South East Water proposes to maintain the current indices during the Water Plan period as:

- A change will make it more difficult for customers to understand their bills with regular index changes;
- The proposed change will have greater impacts on some customer groups than others (tenants and high users);
- The indices proposed by Yarra Valley Water do not match South East Water's disposal profile;
- South East Water does not want to pre-empt the review of tariff structures planned for the coming regulatory period;
- This change would necessitate a change to volume forecasts; and
- South East Water would need sufficient time to make changes to its billing system.

South East Water will, in conjunction with the other retailers, undertake a full review of all tariff structures during the regulatory period. This review will pay specific attention to the SDC.

### **8.5 Recycled Water**

#### **8.5.1 Draft Decision**

The Commission proposed to set the price of residential dual pipe recycled water at the bottom tier of potable water.

### 8.5.2 South East Water Response

This proposal is consistent with South East Water's Water Plan. South East Water considers that this proposal provides appropriate incentives to encourage customers to use recycled water at present as:

- Restrictions are expected to be in place throughout the regulatory period. Recycled water customers will be able to water lawns and gardens regardless of restrictions; and
- Generally, detached homes that water average sized gardens will consume water into the second or third tariff blocks. Recycled water customers will save the difference between the first and second/third block prices. For example, records indicate that over the last four quarters, South East Water's recycled water customers would on average have consumed an additional 45kL in Block 2 and an additional 35kL in Block 3 if they had not been supplied with recycled water.

Residential Reticulated Class A Recycled Water Tariffs (\$2008/09)	2008/09	2009/10	2010/11	2011/12	2012/13
Recycled Water Service Charge	20.00	23.20	26.56	28.29	29.56
Recycled Water Variable Charge (per kL) (as per first tier potable water)	1.0052	1.1861	1.3759	1.5410	1.7105

## 8.6 Recycled Water SDC

### 8.6.1 Draft Decision

The Commission asked retailers to clearly identify the methodology to be used for charging recycled water customers for sewage disposal.

### 8.6.2 South East Water Response

South East Water's current SDC formula for recycled water is stated as follows:

$$(\text{metered potable water} + \text{metered recycled water}) \times \text{Discharge Factor (90\%)} \times \text{Seasonal Factors}$$

South East Water proposes to leave this formula unchanged and reconsider it as part of the tariff review during the regulatory period.

## 8.7 Volumetric Charges

### 8.7.1 *Draft Decision*

The Commission has required businesses to respond with a pricing proposal that increases water volumetric charges at a faster rate than other charges. The Commission has also subsequently indicated that they would expect the sewage volumetric charge to increase by a lesser amount than other charges.

### 8.7.2 *South East Water Response*

South East Water has developed a revised pricing proposal that includes a greater than average increase for water volumetric charges. Given the reductions to Melbourne Water's charges and other factors this can be done while meeting Government expectations that prices no more than double. However, given the uncertainty around demand forecasts and in the absence of other adjustments, this approach changes the overall revenue risk profile. This change alone would also have a greater impact on customer groups such as tenants and large families

However, a decrease in emphasis on the variable sewage charge would help to both offset the changes to risk profile as well as mitigate the overall bill impact for tenants and high users.

<b>Real Price Increase (%)</b>	<b>2009/10</b>	<b>2010/11</b>	<b>2011/12</b>	<b>2012/13</b>
Price Increase – Water Volumetric	18	16	12	11
Price Increase – Sewage Volumetric	14	10	7	4
Price Increase – Residential Sewage Fixed	16.8	17.8	14	8.9
All Other Tariffs	16	14.5	6.5	4.5

## **8.8 Higher Price Increase in Year 1**

### **8.8.1 Draft Decision**

The Commission intends to allow businesses a higher price increase in year 1.

### **8.8.2 South East Water Response**

South East Water proposed a higher price at the beginning of the regulatory period and therefore accepts the Commission's approach.

## **9. Trade Waste**

### **9.1.1 Draft Decision**

The Commission intends to approve the proposed change in Melbourne Water's charging parameters from total nitrogen to total kjeldahl nitrogen (TKN).

The Commission also intends to approve Melbourne Water's proposed change from total dissolved solids to inorganic total dissolved solids (ITDS), but will ask Melbourne Water to reconsider the amount of this charge. The Commission expects retailers to pass this charge on to customers during the regulatory period.

### 9.1.2 *South East Water Response*

South East Water intends to pass the change to TKN through to customers now and will consider the proposed change to ITDS as part of the forthcoming tariff review.

## 9.2 **Proposed Tariff Schedule**

South East Water proposes the following tariffs for the 2009/10 to 2012/13 regulatory period:

### 9.2.1 *Residential*

(\$ 2008/09)	2008/09	2009/10	2010/11	2011/12	2012/13
Water Service Charge	56.96	66.08	75.66	80.58	84.20
Sewer Service Charge	192.67	225.00	265.00	302.00	329.00
Variable Charge (Water)					
Block 1 (0-440 litres/day)	1.0052	1.1861	1.3759	1.5410	1.7105
Block 2 (440 – 880 litres/day)	1.2206	1.4403	1.6708	1.8712	2.0771
Block 3 (880 – 2000 litres/day)	1.9745	2.3299	2.7027	3.0270	3.3600
Variable Charge (Sewer)	1.2565	1.4324	1.5757	1.6859	1.7534

Note: - These prices are expressed in real 2008/09 dollars (ie not including inflation)



### 9.2.2 *Non-Residential*

(\$ 2008/097)	2008/09	2009/10	2010/11	2011/12	2012/13
Water Service Charge	56.96	66.08	75.66	80.58	84.20
Sewer Service Charge	228.81	265.42	303.90	323.66	338.22
Fire Service Charge	37.00	42.92	49.14	52.34	54.69
Variable Charge (Water)	1.2206	1.4403	1.6708	1.8712	2.0771
Variable Charge (Sewer)	1.2565	1.4324	1.5757	1.6859	1.7534

Note: - These prices are expressed in real 2008/09 dollars (ie not including inflation).

### 9.3 Trade Waste

(\$ 2008/09)	2008/09	2009/10	2010/11	2011/12	2012/13
Annual Agreement Fee					
<2,500kl	341.51	396.15	453.60	483.08	504.82
>2,500kl,<OR=25,000kl	990.34	1148.79	1315.36	1400.86	1463.90
>25,000kl,<OR=100,000kl	3301.34	3829.56	4384.84	4669.86	4880.00
>100,000kl	9904.18	11488.84	13154.73	14009.78	14640.22
Vol of Trade Waste (kl)	0.5589	0.6483	0.7423	0.7906	0.8262
BOD (kg)	0.5303	0.6151	0.7043	0.7501	0.7839
SS (kg)	0.2974	0.3450	0.3950	0.4207	0.4396
TKN (kg)	1.1645	1.3508	1.5467	1.6472	1.7213
Oxidised Sulphur (kg)	0.9918	1.1505	1.3173	1.4029	1.4661

Note: - These prices are expressed in real 2008/09 dollars (ie not including inflation)

## 9.4 Customer Impact Analysis

Based on the above prices, South East Water expects to see the following changes to the average residential customer's bill. Note, these increases have been calculated on the basis of a customer using 165kL of water per annum and are expressed in 2008/09 dollars (ie not including inflation).

Average Residential Bill (165kL pa)	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	% Increase 2007/08 to 2012/13
Water & Sewer Bill	\$492.46	\$565.35	\$657.85	\$756.23	\$838.95	\$906.21	84.0%

The expected increase for a range of other customer profiles is shown below.

<b>Residential Water &amp; Sewer Bill (\$)</b>	<b>2007/08</b>	<b>2008/09</b>	<b>2009/10</b>	<b>2010/11</b>	<b>2011/12</b>	<b>2012/13</b>	<b>% Inc 2007/08 to 2012/13</b>
Pensioner Couple (80kL)	\$183.69	\$210.85	\$249.75	\$296.91	\$329.54	\$345.43	88.0%
Tenant – Family of four – house (230kL)	\$395.00	\$453.46	\$526.79	\$596.91	\$655.54	\$708.20	79.3%
2 adults, 2 children small garden (230kL)	\$612.45	\$703.09	\$817.87	\$937.57	\$1,038.12	\$1,121.40	83.1%
Family 6, average garden (370kL)	\$911.36	\$1,046.23	\$1,217.88	\$1,393.22	\$1,540.74	\$1,667.81	83.0%
Recycled Water Customer	\$505.56	\$576.45	\$672.26	\$775.64	\$862.04	\$933.78	84.7%

Note: - These prices are expressed in real 2008/09 dollars (ie not including inflation).

- Concessions have been assumed to increase by 11.8% in 2010/11 2011/12 and 2012/13 equivalent to the increase for 2009/10

Annual Non Residential Water & Sewer Bill <sup>1</sup>	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	% Increase 2007/08 to 2012/13
Small Business Customer	\$740.53	\$850.12	\$986.57	\$1,120.88	\$1,217.50	\$1,299.65	75.5%
Large Business Customer	\$1,859.46	\$2,134.62	\$2,488.01	\$2,838.14	\$3,118.45	\$3,376.20	81.6%
Large Trade Waste Customer	\$27,076.14	\$31,080.96	\$36,319.72	\$41,775.72	\$45,602.35	\$49,104.93	81.4%

Note - These prices are expressed in real 2008/09 dollars (ie not including inflation).

## 10. Melbourne Water

### 10.1.1 Draft Decision

The Commission proposed to approve a proposal by Melbourne Water to introduce a single volumetric sewage charge (combining domestic strength and trade waste).

### 10.1.2 South East Water Response

It is South East Water's understanding that combining these two charges results in recovery of the cost of treating domestic strength pollutant loads via a volumetric charge. This volumetric charge is used as a contributor to trade waste charges and may therefore result in over recovery of costs through pollutant charges. The materiality of this change is uncertain but may have ramifications under future access pricing regimes.

## 11. Other

### 11.1 Miscellaneous Services

South East Water proposes that its pricing for miscellaneous charges prices be approved in nominal terms to ensure consistency throughout the regulatory period in order to provide administrative ease in dealing with this particular industry segment.

Prior to the commencement of the current financial year the costs to provide these products and services were reassessed. This resulted in the need to increase some prices and reduce others. The products and services that could be moved to the cost reflective price without significant changes were moved immediately and those that couldn't were proposed to be transitioned over a period of time. The transition of these items to their cost reflective prices is included in the table below.

As part of their review of Regional and Rural Water Plans, the Commission concluded that only those miscellaneous charges that are “core” should be approved specifically with the remainder set subject to pricing principles. Therefore South East Water is proposing the following key charges for approval.

Miscellaneous Services	2008/09	2009/10	2010/11	2011/12	2012/13
20 mm meter + delivery and installation	\$120.00	\$93.00	\$93.00	\$93.00	\$93.00
20 mm service connection to mains of up to 300 mm	\$320.00	\$320.00	\$320.00	\$320.00	\$320.00
Removal and testing of water meters	\$64.60	\$76.00	\$88.00	\$98.00	\$108.00
Application fee for connection of single residential property to water and/or sewer	\$80.00	\$60.00	\$45.00	\$45.00	\$45.00
Plan showing sewer location within a Property (Property Sewerage Plan)	\$20.00	\$20.00	\$20.00	\$20.00	\$20.00
Information Statements – All forms of lodgements	\$20.00	\$18.00	\$18.00	\$16.00	\$14.00
Restoration of supply at the meter	\$53.85	\$63.00	\$70.00	\$70.00	\$70.00
Application fee to build over South East asset or easement	\$31.00	\$36.00	\$41.00	\$45.00	\$49.00
Application fee for connection –works not required	\$108.90	\$128.00	\$148.00	\$165.00	\$183.00

Note: - These prices are expressed in nominal dollars (ie including inflation)

## 11.2 New Customer Contributions

### 11.2.1 *Treatment of Changes to Customer Numbers*

South East Water recommends that the Commission amend its number of new lots used to calculate the value of customer contributions to ensure that it is consistent with the number of new customers assumed as part of the demand forecasts.

### 11.2.2 *Backlog Bring Forward Charges*

South East Water supports the Commission's recommendation.

### 11.2.3 *Proposed New Customer Contributions*

Category (\$2008/09)	2008/09	2009/10	2010/11	2011/12	2012/13
<b>Water per lot</b>					
Category 1 – less than 450m <sup>2</sup>	\$550	\$550	\$550	\$550	\$550
Category 2 - between 450m <sup>2</sup> and 1,350m <sup>2</sup>	\$1,100	\$1,100	\$1,100	\$1,100	\$1,100
Category 3 – greater than 1,350m <sup>2</sup>	\$2,200	\$2,200	\$2,200	\$2,200	\$2,200
<b>Sewer per lot</b>					
Category 1 – less than 450m <sup>2</sup>	\$550	\$550	\$550	\$550	\$550
Category 2 - between 450m <sup>2</sup> and 1,350m <sup>2</sup>	\$1,100	\$1,100	\$1,100	\$1,100	\$1,100
Category 3 – greater than 1,350m <sup>2</sup>	\$2,200	\$2,200	\$2,200	\$2,200	\$2,200

Note: - These prices are expressed in real dollars (ie not including inflation)

Category (\$2008/09)	2008/09	2009/10	2010/11	2011/12	2012/13
<b>Dual Pipe Recycled Water Developments</b>					
<b>Water per lot</b>					
Category 1 – less than 450m <sup>2</sup>	\$275	\$275	\$275	\$275	\$275
Category 2 - between 450m <sup>2</sup> and 1,350m <sup>2</sup>	\$550	\$550	\$550	\$550	\$550
Category 3 – greater than 1,350m <sup>2</sup>	\$1,100	\$1,100	\$1,100	\$1,100	\$1,100
<b>Recycled Water per lot</b>					
Category 1 – less than 450m <sup>2</sup>	\$550	\$550	\$550	\$550	\$550
Category 2 - between 450m <sup>2</sup> and 1,350m <sup>2</sup>	\$1,100	\$1,100	\$1,100	\$1,100	\$1,100
Category 3 – greater than 1,350m <sup>2</sup>	\$2,200	\$2,200	\$2,200	\$2,200	\$2,200
<b>Sewer per lot</b>					
Category 1 – less than 450m <sup>2</sup>	\$550	\$550	\$550	\$550	\$550
Category 2 - between 450m <sup>2</sup> and 1,350m <sup>2</sup>	\$1,100	\$1,100	\$1,100	\$1,100	\$1,100
Category 3 – greater than 1,350m <sup>2</sup>	\$2,200	\$2,200	\$2,200	\$2,200	\$2,200

Note: - These prices are expressed in real dollars (ie not including inflation)

DSE has required that the Backlog connection charge remain at \$500 throughout the period. Therefore, as for miscellaneous charges, South East Water requests that the Commission approve this charge on a nominal basis.



Backlog Connection Charge (\$2008/09)	2008/09	2009/10	2010/11	2011/12	2012/13
Backlog Connection Charge	\$500.00	\$500.00	\$500.00	\$500.00	\$500.00

Note: - These prices are expressed in real dollars (ie not including inflation)

## Attachment 1

Following is a status report prepared by South East Water's project manager on behalf of the broader industry working group:

### VCEC Shared Services Project

#### Status Report – 1 May 2009

#### Background

The Shared Services Project was established with two phases for the 2008/09 financial year. The first phase was to examine well known common spend areas where it was expected joint procurement may be possible. Phase 2 is to prepare a spend map across the four businesses and investigate those areas of major spend not reviewed in Phase 1.

#### Phase 1 Spend Analysis

The following is an update to the status of Phase 1 analysis spend categories. The analysis is being undertaken by sub-groups from the four Melbourne Metropolitan Water Businesses.

Joint Procurement Approved *	Options under Consideration	No Savings Potential
Electricity	Vehicles	Fuel
Banking Services	IT/Telecommunications	Over the Counter Collections
Meter Purchasing	Insurance	Internal Audit Services
	Laboratory Services	
	Meter Reading	
	Chemicals	
	Legal Services	
	Media Monitoring	
	Bill Printing	

\*For those categories where joint procurement has been approved, tenders are currently underway.

## Phase 2 Detailed Analysis

Ernst & Young (project consultant) have completed the detailed data capture and analysis work across the four water businesses. This work has included mapping the spend of the four Melbourne Metropolitan Water Businesses over a 12 month period, categorising that spend for easier comparison and identifying common suppliers.

Following this analysis, workshops have been held in the following spend categories:

- Capital Works and Engineering Services
- Human Resources – Recruitment and Temporary Labour
- Information Technology
- Marketing and Media

Following these workshops, a number of areas have been targeted for follow up to assess opportunities for joint procurement and future strategy development.

Ernst & Young have also commenced drafting the report of their findings across both the opportunities in common spend areas and potential areas for benchmarking and have scheduled meetings across the four water businesses to discuss the findings.

## Savings Identified

Note that no cost savings have been identified to date. This will not be possible until tenders are completed or new pricing contracts assessed.

## Project Costs

The Shared Services Project has a budget through to 30 June 2009 of \$400K. This cost includes consultants, a project manager and incidental expenses.

The cost of water business staff apart from the project manager has not been included in the project costings.

Beyond June 2009, further stages of the project will be planned to cover implementation of those categories where joint procurement has been approved. Further investigation work will also be required in some areas such as capital works and IT. Benchmarking activity is also being assessed for completion in the 2009/2010 financial year to facilitate identification of future savings from Shared Services.

Estimated costs for the 2009/2010 financial year are in the range of \$600K - \$700K which includes project management and consulting time.