Coolum Beach Progress & Ratepayers Association Inc.
PO Box 121
Coolum Beach Q 4573

25th May 2004

The Director
Queensland Competition Authority
GPO Box 2257
Brisbane Qld.4001

Dear Sir/Madam,

You have invited public comment on aspects of the 2004 investigation of the Gladstone Area Water Board's pricing policies. The Coolum Beach Progress and Ratepayers Association Inc. (CBP&RA) in May 2003 requested a prices oversight investigation of Maroochy Shire Council's Maroochy Water Services that is currently under review by Queensland Treasury. Your issues paper addresses some of the areas of concern to this Association, and we are pleased to offer the following public comment submission regarding Section 5 - Elements of Maximum Revenue Requirement.

5.2 The Asset Base

Water and sewerage service provision is a capital intensive business activity. For such activities an efficient operator balances the scale effect gains of adding capacity in large increments against the uncertainty implicit in demand forecasting that favors flexibility by adding capacity in smaller increments. A measure of investment decision efficiency in this trade-off is higher ongoing levels of system capacity utilization as overall service demand increases. Meaningful benchmarking of system utilization against those of enterprises experiencing similar climatic conditions, end use patterns and demand growth, and service standards, can be considered when determining the appropriate DORC asset valuation.

DORC assets will include contributed assets and works constructed with State Government subsidy payments. Such assets would need to be removed from the capital base considered eligible for Rate of Return as inclusion would result in an unwarranted return on capital not actually invested by the business entity.

Under the principle of user pays, a Council's water and sewerage infrastructure investment should eventually be fully recovered through headworks contributions. It would be only the time related unrecovered investment then that is deserving of consideration for inclusion in the DORC asset base for the ROR component of maximum revenue requirement at any particular time.

5.3 Rate of Return

Use of WACC methodology assuming a significant proportion of equity financing does not represent a practical financing situation for most Local Government natural monopoly entities in Queensland. A prudent business manager must surely minimize cost of capital. Debt capital is available from Queensland Treasury Corporation (QTC) at rates considerably lower than theoretical equity capital sources considered in the WACC calculation because of the low risk nature of public sector infrastructure investment. This is the lowest practical cost of capital for Local Government natural monopoly entities and a post tax ROI based on this cost of capital seems appropriate for use in the maximum revenue assessment. Use of WACC methodology may inadvertently encourage excessive capital expenditure due to the profit incentive created from cost of capital difference between 100% QTC debt financing and the theoretical WACC based on assumed substantial equity financing (50 – 70%).

5.4 Return of Capital

Realistic depreciation schedules based on actual useful life and efficient maintenance practices are this Association's preferred approach. Again, meaningful benchmarking relative to those enterprises experiencing similar climatic conditions, end use patterns and demand growth, and service standards, can also be considered when determining the appropriate use life assumptions and depreciation approach.

The renewal annuities approach favored by QCA has the disadvantage of encouraging continued use of present day technological approaches to service delivery and exacerbates the barrier to entry for smaller scale innovative decentralized technologies.

5.5 Operating Expenditures

This Association considers that for a capital intensive business enterprise, allocation of general administration costs should follow the patterns of efficient capital investment. Reticulation related assets amount to some 80% of fixed assets for Maroochy Council's water and sewerage enterprise. Dams, treatment plants, etc. are less than 20%. The SMEC allocation recommendation may then be appropriate for Gladstone, but would of course differ for different entities.

Yours sincerely

Peter M. Brown
President