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Queensland Competition Authority  
GPO Box 2257  
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Dear Sir

## RESPONSE TO THE QUEENSLAND COMPETITION AUTHORITY

### Introduction

Fitzroy River Water (FRW) appreciates the opportunity to provide its responses to the QCA on the QCA issues paper *Technical Review of the Cost of Capital Methodology*. FRW has tailored its response to this paper from a perspective of a commercialised entity under the *Local Government Act 1993*.

In response to the issues raised by the QCA discussion paper FRW considers the findings by the authors of the report to be substantive, logical and with useable recommendations that will benefit the regulated entities in their application of full cost pricing and appropriate recovery of costs through the application of an accepted and approved Cost of Capital methodology for pricing purposes.

Rockhampton City Council (RCC) and Fitzroy River Water (FRW) have developed pricing for water from its storage on the Fitzroy using the Weighted Average Cost Of Capital Methodology (WACC). These pricing models have been developed by Australian Economic Consultants (AEC) and Queensland Treasury Corporation (QTC) due to their expertise in this area.

### Application of the WACC

The CAPM / WACC has been used as an input of pricing models, consistent with the organisation's maturity and the development of its systems and people. Part of this organisational maturity is reflected in its revised determination of:

- Asset Condition,
- Asset Valuations,
- Contributed Assets,
- Values applied to Contributed Assets,
- Asset lives (compared to tax and accounting concepts), and
- Depreciation rates.

While the WACC is an important input the improvement in systems and related data management to assist in the determinations of the base asset values, their life expectancy, and replacement costs has taken precedence.

The pricing structure for water and the proposed two part tariff have been developed by FRW and considered by Council based on:

- o Infrastructure ownership,
- o Asset valuations (DORC)
- o Contributed Asset values
- o Depreciation rates

using assumptions on specific issues and modelling from QTC and AEC using the WACC to determine:

- o Projected return on capital,
- o Profit, and
- o Water pricing

in the context of a purely commercial arrangement.

### Conclusion

FRW appreciates the opportunity for input into this matter and trust that their response identifies the emphasis it has given to ensuring that the most up to date base data, premised on the latest asset identification and valuation information available, is used in its pricing model and that it regards the professional advice of organisations like QTC and AEC integral in its use of this data.

The approach by the QCA is welcomed and the work undertaken by Dr Martin Lally is recognised for its quality and applicability. The adoption by the QCA of the Brennan - Lally CAPM by the Authority will provide a firm basis for future pricing analysis and structure within the regulated industries.

Yours faithfully



David Traylen  
Commercial Manager