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17 May 2010

Mr John Hall
Chief Executive
Queensland Competition Authority
GPO Box 2257
Brisbane Qld 4001

Dear Mr Hall,

Submission to the Queensland Competition Authority (QCA) in response to QCA Draft Report concerning Gladstone Area Water Board (GAWB) Pricing Practices

Callide Power Management (CPM) would like to thank the QCA for the provision of the Draft Report concerning GAWB's Pricing Practices ("Draft Report") and the opportunity to provide a further response to this report.

CPM notes that the Draft Report provides recommendations and support for a majority of CPM's major areas of concern included in our submission of 5 February 2010.

1. Response to Draft Report

CPM would like to take the opportunity to make the following comments on the key findings and recommendations made in the Draft Report that are relevant to source asset usage:

- CPM supports the position articulated by the QCA that the form of regulation should remain a price cap, as opposed to a revenue cap, because it allocates demand risk to the party in the best position to control and mitigate that risk – GAWB.

- The QCA's view that the planning period should remain at a 20 year horizon for future pricing periods versus a 5 year period is supported by CPM. This will ensure that pricing is not front loaded for capacity that is required in future years and will minimise the risk of significant price shocks to existing customers.

- Recognising recent heavy inflows to Awoonga Dam, CPM supports the QCA's view that the full historic no failure yield should be reset to 78,000ML as opposed to 70,000ML.

- CPM supports the QCA's position with respect to the asset base being a roll-forward approach for the 2010-2015 planning period rather than a full re-valuation. This takes into account the opening value at July 2005, indexation, asset additions, subtractions and depreciation, and, the non-allowance of the proposed $16M upward re-valuation to the opening 2005 asset value.

- CPM support's the Authority's recommendation that GAWB's proposed dam safety works require further justification, as to timing and the most cost-effective option. CPM accepts that GAWB must comply with externally-mandated safety standards, though customers should only be required to fund the most cost-effective response strategy.

- CPM notes the QCA has proposed WACC parameters in line with its recent determinations for other utilities, and CPM expects these would be maintained for the final recommendation (subject to updating of the time-sensitive market parameters etc).

- CPM supports the QCA's view that self insurance is not an appropriate method to mitigate risk under the circumstances.

- CPM is satisfied with the QCA's recommendation with respect to reviews conducted on operating costs and indexation.

2. Price Transition

CPM notes the Draft Reports findings that on the basis of information available, it is estimated that on average (weighted by demand in each segment) prices could increase by 43.4% assuming that the QCA's recommendations were adopted. This compares to an increase of 119% were GAWB's proposed expenditures and forecasts accepted in full.

For CPM specifically, a price increase of that which is foreshadowed in the QCA Draft Report, still represents a major price shift and will result in a 'price shock' for the 2010-2015 planning period and this would have a substantial and material impact on the competitiveness of the Callide C Power Plant . This large operational cost increase will affect only a limited number of power stations and not the vast majority of the Queensland or national electricity generation market, which places the Callide C Power Plant at a competitive disadvantage relative to other market participants.

CPM is not in a position to recover any of this cost increase through the national electricity generation market and long term financing arrangements have been made to support the project based on stable, relatively certain price assumptions over the life of the facility.

CPM supports the recommendation that further discussions are held between GAWB and other stakeholders regarding the issue of transitioning to the recommended pricing practices. Furthermore, CPM would like to indicate our preference for a price transitioning process by drawing on the examples noted in the QCA's submission (ESC 2009). CPM would be supportive of in general, a price transition process that:

- is set with regard to customer preferences and under individual consultation with GAWB; and
- does not result in a significant price shock in the first year of the subsequent regulatory period

CPM preference is for a 10 year (2 planning period) price transition. [redacted] The revenue recovery for the supplier would be NPV neutral.

CPM believes that our transition approach is the fairest way for the supplier to recover costs in an NPV neutral manner as well as preserving the Callide C Power Plant's competitive position and long term future.

Yours sincerely,

[redacted]

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Jamie Maione
Commercial Manager
Callide Power Management