SEQWATER'S 27 JULY SUBMISSION / RESPONSE TO QCA REQUEST OF 23 JULY

23 July 2012

The Authority provides, herewith, another formal (consolidated) information request to Seqwater. [Questions outlined below prior to Seqwater responses.]

A response would be appreciated by **Friday 27 July 2012**.

**From:** Damian Scholz [redacted]
**Sent:** Friday, 27 July 2012 11:59 AM
**To:** Angus MacDonald
**Cc:** Economic Regulation Staff
**Subject:** response to request

Hi Angus

Please see our initial responses below to your request received 23 July 2012.

**QCA Question 1**

The non-direct costs you have submitted to QCA on 29 June 2012 have been reviewed at the officer level and were compared to the non-direct costs provided to QCA in February of this year as part of Seqwater submission to the bulk prices review. There were some discrepancies in the numbers identified for some cost items as per attached. Could you please provide justification or reasons for these discrepancies by Monday 23 July 2012.

**Seqwater Response to Item 1**

As a first cut explanation, the numbers in the February submission were for the CBD (including Karalee) plus locations which are assets. The numbers in June are CBD only and do not include costs budgeted directly to assets.

**QCA Question 2**

Questions on the forecasting of electricity costs:

Looking at attached "Summary of Seqwater's responses" we notice that Seqwater has undertaken to provide additional information on electricity costs for Pie Creek and Central Lockyer. However, you do not propose to provide details for the other schemes (unless we request it) on the basis that the electricity costs for those other schemes is immaterial. Please provide us the basis for your general forecasting approach to electricity (that is, applied in each scheme) including how you came up with your $100,000 estimate for off stream storages. As the prudency & efficiency of electricity costs are NOT being looked at as part of the opex/renewals consultancy, we will need your submission on this point. Regarding electricity cost escalation (or equivalent) please clarify your position in light of the following new draft text from Chapter 2: Regulatory Framework:

> "Seqwater faces cost risks due to market conditions for inputs and regulatory imposts. To achieve revenue certainty under a regime of stable prices, there are a range of mechanisms that could be adopted.

Most cost variations are expected to be most appropriately resolved through end-of-period review adjustments.*Electricity*

Unlike for SunWater, the Authority notes that electricity is a particularly small cost for Seqwater (mainly bulk schemes) and the potential for improvements is less than for SunWater.

It is therefore proposed to pass-through electricity costs (including the cost of carbon which is outside Seqwater's control) which are not material. Any adjustments to prices for this purpose should only occur annually.

Actual costs incurred should then be reviewed as part of an end-of-period review of their efficiency. *Off-Stream Storages*

In response to Seqwater's submission regarding off stream storage electricity pumping costs, the Authority accepts that such pumping costs are outside of Seqwater's control (as pumping requirements are specified in the ROP or IROL and cannot be predicted due to their high variability), rather than to meet customer demand. Seqwater should be able to recover the prudent and efficient costs of meeting ROP and IROL obligations.

This differs from the circumstances of SunWater, where the Authority concluded that off stream pumping costs relate to water use (therefore, a variable cost) and should be recovered through the volumetric charge.

However, some Seqwater electricity pumping costs do not vary with water use and should be recovered through the fixed charge.

The Authority accepts that actual pumping costs may vary materially from those forecast by Seqwater.

Therefore, the Authority is prepared to accept the prudent and efficient fixed pumping costs (established in Chapter 6) and review it at the end of regulatory period. Seqwater must retain records of actual pumped volumes and costs over the 2013-17 regulatory period for this purpose.

**The Authority recommends that:**

**(a) end-of-period adjustments, price review triggers or cost pass-through mechanisms be used to manage risks due to market conditions for inputs and regulatory imposts;**

**(b) electricity costs, including the carbon cost, which are not material should be passed through during the regulatory period (not more than once annually). The actual costs incurred should then be subject to an end-of-period efficiency review;**

**(c) in relation to off stream storage pumping costs incurred in a manner that does not relate to meeting customer demand (water use), Seqwater should apply for an end of period adjustment to the nominated amount which has been incorporated in costs."**

**Seqwater Response to Item 2**

*Electricity – first, we are still finalising the document setting out the forecasting approach to operating costs, including electricity. Secondly, Seqwater accepts that an end of period adjustment mechanism is sufficient to manage electricity cost risk in relation to the assets that provide irrigation services, given electricity costs (with the exception of Lake Clarendon) are not material. However, given a variable charge now applies at Pie Creek to recover electricity costs, we see merit in retaining the suggested provision for an annual adjustment for actual changes in electricity costs in this tariff group. This will ensure the variable charge is properly reflecting actual variable costs, thereby sending accurate price signals to customers. It can also be easily implemented by updating the variable charge by the annual percentage change in the variable energy tariffs applicable to the pump station.*

**QCA Question 3**

Basically (re above) we support Seqwater's suggestion (inflation + 'unders & overs'), on the basis that the small proportion of electricity costs justifies only end-of-period adjustments. However, we also appear (deviating from SunWater but consistent with the Bulk GSC report) to contemplate annual pass-through of electricity costs (including the cost of carbon which is outside Seqwater's control) which are not material. Does this make sense to you? Surely carbon is already in your forecast base year costs?? Please illuminate me further on this topic, particularly how you forecast electricity (including 4 years of carbon) and whether you would avail of immaterial annual pass thru??

**Seqwater Response to Item 3**

**QCA Question 4**

For internal labour costs, Seqwater uses an escalation factor of 4% pa for the regulatory period 2013-17. It mentions that the current Enterprise Bargaining Agreement (EBA) expired on **30 June 2012** (4% for the period 1/7/2009 to 30/6/2012). Please provide details of any new EBA as part of our consideration of cost escalation.

**Seqwater Response to Item 4**

Internal Labour - The wage increase for 2012-13 has not yet been approved, although this is likely to occur before the QCA publishes its draft report in November 2012. Future increases, as well as conditions for a new EBA for the merged business are yet to be negotiated.

**QCA Question 5**

For Pie Creek losses. We think you should have the costs of 100% of the 60ML of high priority loss WAE recovered from customers. However, we think you are should not have 100% of the 483ML of medium priority loss WAE recovered from customers – we think this is an inefficient volume of MP loss WAE. We think you should determine the efficient amount, apply to DNRM to covert the unneeded amount to any and sell it. Prior to selling it we think Seqwater should bare the holding cost. To determine this amount the data you have provided is not adequate or appropriate, mainly as it is incomplete and too long ago. Also it is inconsistent with the period used for SunWater (that is, 1975 to 1983 do not accord with the SunWater period, which was the nine years to 2010-11).

We now seek from you the most recent past 9 or 10 years of actual losses deliveries in Pie Creek.

Failing this we seek from you: (a) the highest ML of actual losses delivered during the past 9 or 10 years (perhaps you can ask SunWater); and (b) for that year the announced allocation – or preferably (as a proxy for announced allocation) the total actual water delivered to customers in Pie Creek also expressed as a portion of total customer WAE in that year. On this basis, you should please (and we will also) estimate the efficient level of losses WAE for Pie Creek (as per the method adopted by the Authority for SunWater, for this purpose).

**Seqwater Response to Item 5**

Pie Creek losses - we will be able to respond next week following a further search for more data as requested.

**Damian Scholz**
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seqwater
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