

**DEPARTMENT OF TREASURY**

Mr Ian Primrose
Chief Executive Officer
Independent Competition and Regulatory Commission
PO Box 975
Civic Square ACT 2608

Dear Mr Primrose

Thank you for your letter of 28 February 2006, which included a copy of your Report 6 of 2006, "Water and Wastewater Annual price reset 2006-07". The following comments are made in relation to the two of the three projects outlined in the report, which ACTEW Corporation (ACTEW) has requested be included in the calculation of water tariffs for 2006-07.

Future Water Options

The Future Water Options (FWO) project included a comprehensive review of numerous water supply augmentation options for the ACT. The work involved the typical investigative processes and preliminary design planning needed to ascertain the relative merits of the proposals.

Treasury notes that the idea for the Cotter Googong Bulk Transfer (CGBT) project arose from an analysis of ACTEW's current infrastructure, and that this analysis was considered as part of the FWO work. Therefore it is open to the ICRC to treat expenditure related to the FWO as part of the capital cost of the CGBT.

Cotter Catchment Development

There are two separate but related projects taking place in the Lower Cotter Catchment (LCC). The first relates to ongoing catchment management and post bushfire remediation work undertaken by the ACT Government through ACT Forests. The second relates to work necessary to bring the quality of the water in the LCC catchment up to a standard adequate for the CGBT to operate effectively, and to bring water from the Cotter Dam into the ACT water supply system. Expenditure on this project is being incurred by ACTEW.

The ACT Forests budgeted program for remediation and management mainly involves the planting of pines, natives and other trees plus minor works on roads. Improving water quality is an outcome of the rehabilitation work, but the quality of water would not reach the level required by ACTEW for ten years or so. In recognition of this, ACTEW is undertaking work of a much different nature to

ACT GOVERNMENT GPO Box 158 Canberra ACT 2601
T 13 22 81

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achieve the required water quality level in a much shorter time. This work includes large scale construction of culverts, drainage and sediment control, and is in addition to the ACT Forests work program.

The discussion paper asserts that this expenditure may be appropriate to be included in the WAC because it relates to catchment management. To date, all normal catchment management work has been undertaken by the ACT Government. The reason that ACTEW has undertaken additional catchment enhancement work in the Lower Cotter Catchment is that it is a direct requirement of ACTEW's decision to reinstate the Cotter Dam into the ACT's water supply system and subsequent decision to undertake the CGBT scheme. Prior to the bushfires, water from the Cotter dam had not been used in the ACT water supply for 20 years. The CGBT scheme is reliant on capturing the environmental flows required to be released from Bendora Dam in addition to any available excess water in Cotter Dam.

Treasury consider that the work undertaken by ACTEW is not an appropriate cost for inclusion in the Water Abstraction Charge (WAC) because it is not a cost being incurred by the ACT Government. The work is being done by ACTEW to enhance the LCC catchment to a level beyond what is being achieved under the Government's remediation program.

The intention of the WAC is to recoup (amongst other things) "water supply costs – covering the catchment management costs, and all other costs incurred by the ACT Government in the maintenance, regulation and assurance of water supply".¹

The decision to spend funding on enhancing the LCC in order to progress the CGBT was made by the ACTEW Board. If ACTEW had not undertaken this catchment enhancement work to improve water quality, the alternative would have been to spend more on treatment works, which would have been a far more costly exercise. However, if this alternative had been chosen, there would be no case for the ICRC to even consider it as a possible addition to the WAC.

Insurance

In Treasury's view the expenditure incurred by ACTEW should not be recovered via the WAC. Consequently the issue of whether insurance compensation is being used to meet the Government's expenditure on LCC is not relevant to the decision to allow ACTEW to recover its costs via water tariffs. However, the following information makes it quite clear that the costs incurred by the Government far exceed the insurance compensation available for the clean up and rehabilitation of the LCC.

ACT Forests will receive, over a number of years, a total of \$52 million in insurance settlements. The majority of the insurance payment relates to standing timber loss, \$9.1 million of the payment was related to the removal of debris, and \$8.8 million for re-establishment, a total of \$17.9 million. The payment for this rehabilitation work is based on 10,500 hectares of the forest estate, including 4,300 hectares in the LCC, so the allocation of these funds that might be relevant to the rehabilitation of the LCC is in the order of \$7.3 million (based on a pro rata allocation). As shown later in this letter, the Government has already spent more than this amount in funding rehabilitation work in the LCC.

¹ ICRC, Final report – Water Abstraction Charge, October 2003, Recommendation 3, p.41.

ACT Government Remediation Expenditure

In the discussion paper the ICRC notes that the "ACT Government initiated the remediation works". This statement is potentially misleading. The ACT Government initiated remediation work in the area to rehabilitate the land as a result of the damage caused by the 2003 bushfires. It did not initiate any of the work that ACTEW is undertaking.

This is demonstrated in Table 1 below which shows the Government's planned program of rehabilitation works in the LCC as at 2003-04, before the CGBT scheme or use of the Cotter Dam had been proposed. Table 2 shows that the actual Government expenditure on rehabilitation work to date is in line with budget.

Table 1 – ACT Forest's Budgeted expenditure on Lower Cotter Catchment Remediation.

	2003/04 \$'000	2004/05 \$'000	2005/06 \$'000	2006/07 \$'000	2007/08 \$'000	2008/09 \$'000	Total \$'000
Management of ACT Forests' Land	800	800	900	1,002	1,028	1,053	5,583
Re-establishment of selected areas with pine plantation	690	747	645	645	645	645	4,017
Re-establishment of selected areas with natives or exotics	1,140	390	225	225	225	225	2,430
Clean-up and debris removal of the burnt pine plantations	1,600	800	800	800	0	0	4,000
Rehabilitation, improvement and realignment of roads	400	236	224	116	116	116	1,208
Replacement of burnt fencing on public land	0	0	0	0	0	0	0
Reinstatement and enhancement of Deek's Forest park	0	0	0	0	0	0	0
Project management and commissioning expenses	400	224	224	224	224	224	1,520
Total	5,030	3,397	3,008	3,012	2,138	2,263	18,758

Table 2 – ACT Forest's actual expenditure on Lower Cotter Catchment Remediation.

LCC Expenditure \$000	Total ha	Actual spent to Feb 2006	Total Budget to 2005-06	Comments
Management of ACT Forests' Land	N/A	2,500	2,500	
Re-establishment of selected areas with pine plantation	1,300 ha	3,111	2,082	Majority of rehabilitation thus far has been within the catchment
Re-establishment of selected areas with natives or exotics	148 ha	1,100	1,755	Whilst only 148ha have been planted, over 600ha have been cleared and prepared. Drought prevented the 04/05 planting.
Clean-up and debris removal of the burnt pine plantations	2,544 ha	2,325	3,200	So far focused on the easier areas – costs will increase with difficult terrain
Rehabilitation, improvement and realignment of roads	N/A	1,308	850	Roadwork has been focused in the LCC to date
Project management and commissioning expenses	N/A	828	848	
Total		11,172	11,135	

In short, this demonstrates that the ACT Government continues to undertake a comprehensive program of works funded through the WAC. The costs being incurred by ACTEW are over and above those funded from the WAC.

Therefore, Treasury considers that there is no case to consider the catchment enhancement work being undertaken by ACTEW is work on behalf of the Government.


Summary

It is our view that ACTEW's expenditure on the LCC is related to both the need to bring the Cotter Dam into the ACT water system and the establishment of the CGBT. It is therefore appropriate to allocate this expenditure in part as an operational costs and part as capital.

Regardless of how the ICRC views the classification of these costs, Treasury considers that these are ACTEW costs and should be recovered by way of water tariffs.

If you would like to discuss any of the matters raised in the submission please contact Kathy Goth, Manager, Microeconomic Reform Unit on 6207 3949.

Yours sincerely


Paul Grimes
Under Treasurer
30 March 2006