

**SUBCOMMITTEE OF THE STANDING COMMITTEE ON  
ESTIMATES AND FINANCIAL OPERATIONS**

**2012–13 BUDGET ESTIMATES HEARINGS**

**TRANSCRIPT OF EVIDENCE  
TAKEN AT PERTH  
THURSDAY, 5 JULY 2012**

**SESSION THREE  
WATER CORPORATION**

**Members**

**Hon Philip Gardiner (Chair)  
Hon Ken Travers  
Hon Ljiljanna Ravlich**

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**Hearing commenced at 2.07 pm**

**MR BRIAN ROBERTSON**

**Manager, Capital Investment Branch, sworn and examined:**

**MR LLOYD WERNER**

**Manager, Pricing and Evaluation, sworn and examined:**

**MR ROSS HUGHES**

**Chief Financial Officer, sworn and examined:**

**MRS SUSAN MURPHY**

**Chief Executive Officer, sworn and examined:**

**The Chair:** Welcome from us all. Before we begin, I must ask public servants, each of you, to take the oath or affirmation.

[Witnesses took the oath or affirmation.]

**The Chair:** You have signed a document titled “Information for Witnesses”. Have you read and understood that document?

**The Witnesses:** Yes.

**The Chair:** This hearing is being held in public although there is discretion available to the committee to hear evidence in private either of its own motion or at your request. If for some reason you wish to make a confidential statement during today’s proceedings, you should request the evidence be taken in closed session before answering the question.

Government agencies and departments have an important role and duty in assisting government to scrutinise the budget papers on behalf of the people of Western Australia and we value that assistance.

These proceedings are being recorded by Hansard. A transcript of your evidence will be provided to you and it will greatly assist Hansard if, when referring to the budget statements or consolidated account estimates, members, in particular, give the page number, item, program, amount and so on in preface to the questions. If supplementary information is to be provided, I ask your cooperation in ensuring that it is delivered to the committee clerk within 10 working days of receipt of the questions. Should you be unable to meet this deadline, please advise the committee clerk immediately.

Any questions from any of our members? Who would like to go first?

**Hon KEN TRAVERS:** Can you advise me what statement of corporate intent you are operating under at this point in time?

**Mrs Murphy:** Our statement of corporate intent for this financial year was submitted, as is required under our act, on 30 June 2012 to the minister. The minister has to get the concurrence of the Treasurer and then he tables it. At the moment we are operating, I guess, somewhat freeform, but we are operating largely under—the numbers in our SCI are the same numbers in the state budget. So we are operating to the state budget and we are doing the tasks as foreshadowed under our SDP and last year’s SCI as they go forward.

**Hon KEN TRAVERS:** So the 2012–13 statement of corporate intent, when was that submitted to the minister?

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**Mrs Murphy:** On 30 June—29 June, technically, because 30 June was a Saturday.

**Hon KEN TRAVERS:** It was submitted a day before the end of the financial year?

**Mrs Murphy:** Yes.

**Hon KEN TRAVERS:** Is there not an earlier date that you are required to submit it by?

**Mrs Murphy:** No.

**Mr Hughes:** We submit it to assist the Treasury budget process —

**Mrs Murphy:** We submit a draft in December normally.

**Mr Hughes:** Every GTE does it at different dates. Ours goes in around Christmas, mostly for Treasury purposes and budget preparation processes.

**Hon KEN TRAVERS:** Under section 50, my understanding is you are required to table it by a required date and if there is not a fixed date—a number of them I thought it was 14 December last year—then two months before the start of the next financial year is the date by which you are required to submit the statement of corporate intent. That is in accordance with the Water Corporation Act 1995.

**Mr Hughes:** Our understanding, which we can check at another time, is that it is required to be submitted to the minister by 30 June.

**The Chair:** That is something we can take on notice.

*[Supplementary Information No C1.]*

**Hon KEN TRAVERS:** My understanding is that you are supposed to submit it under the act at least two months before or the date on which it is fixed to be submitted, which I thought was normally around December, so it is well in advance of the budgetary cycle. Then under section 53 of your act, you are required to have agreement on it not later than the start of the next financial year. So the 2012–13—you should have had agreement on with the minister by 30 June. I cannot imagine if you only submitted it on 29 June, you are going to get agreement before 30 June.

**Mrs Murphy:** No.

**Hon KEN TRAVERS:** This is a matter that has now been raised by the Auditor General on a number of occasions. Has that not been made with you by the Auditor General in your private briefings with him about the Auditor General's concerns on this matter?

**Mr Hughes:** My understanding of the issues that the Auditor General has raised is the time within which it takes from concurrence by the Treasurer to the point at which it is submitted to Parliament. There is a statutory deadline—statutory number of days—between that concurrence and the release submission into Parliament.

**Hon KEN TRAVERS:** No, I think if you go and have a look at what the Auditor General said, his concern is they are not meeting the time line of having them submitted and signed off before 30 June.

**Mr Hughes:** No, he has not raised it with us.

**Mrs Murphy:** That has not been raised with us.

**Mr Hughes:** What has been raised with us is the speed at which concurrence to Parliament has been done. There are times that he has gone to Parliament or he has completed a report and named those entities which have not complied with that. We can check that.

**Hon KEN TRAVERS:** I assume if it was only submitted to the minister on 29 June—are you aware whether the concurrence of the Treasurer has been sought yet to the statement of corporate intent?

**Mrs Murphy:** I do not know the answer to that, no. But if there are particular aspects covered in the SCI that you would like us to provide any illumination on, we are very happy to do that.

**Hon KEN TRAVERS:** Well, I could say that all of the items listed in section 52(2) of your act, if you wanted to.

**Mrs Murphy:** I might have to ask you for a little bit more clarification.

**Hon KEN TRAVERS:** That is all the items; the act outlines what is supposed to be included in the statement of corporate intent. You made a comment earlier and it may help answer some of it; there is a statement of corporate intent that you submitted as part of the original budget process. Is everything that was in that statement of corporate intent now incorporated into the budget?

**Mrs Murphy:** There are some changes—not verbatim, no. Do you mean in the text or in the financial numbers? I am not quite sure which bit you want.

**Hon KEN TRAVERS:** More the financial numbers.

**Mrs Murphy:** The text will have changed, probably a lot. In the financial numbers, sometimes there are projects that have changed during the year—for example, sometimes the timing of cash. I know last year's SCI foreshadowed a sum of money for a pipeline for Perdaman resources which has rolled forward because that project has not happened. There were some timing issues in the southern seawater desal plant, the second tranche, because when that project started we had a cash flow we had guessed and the actual cash flow is slightly different, so there were some timing issues on that. They were the main changes.

**Mr Werner:** They also reflect the decisions that are made in the budget process.

**Mrs Murphy:** After EERC hearings.

**Mr Werner:** The draft goes in in December; there is the budget process and some things are funded and some things are not and adjustments are made to the draft so that the Treasurer can concur, because we want the SCI to line up with the budget.

**Hon KEN TRAVERS:** I guess that is one of the reasons why we are particularly interested in it, because you may have seen the reports by other committees of the Legislative Council regarding some of the other major trading enterprises, namely, Western Power. I guess the concern that I have is that what I think that has identified is that the board of Western Power were identifying capital works that were required to be undertaken and that the Treasury process was not allowing them to do that because they were not approving that expenditure. So, I guess, what I am interested in is are there areas in the Water Corporation where you have identified the capital works that need to be renewed, replaced, significant maintenance undertaken on that have not been funded in the budget?

**Mrs Murphy:** There are always things that are not funded in the budget. It is a degree of criticality of those things. It became clear some years ago that the state's ability to fund the suite of assets that the Water Corporation were proposing was going to be problematic. So, some years back, about three years ago, we changed the way we do our capital investment prioritisation process. We run a very risk-based process. We can live within the borrowings we are allowed. The capital program that is in this budget is probably not ideal, but it certainly enables us to continue to meet our operating licence requirements and to consider growth. Growth has been the driver for the bulk of our capital program in recent years. In the past few years we have run the capital program out over a 20-year program with a risk-based program and nominated the capital needs over a 20-year period. So, we are having a much more mature discussion with Treasury about a longer-term capital program that does not bounce around based on some of the vagaries of the way different state budgets are constructed. We are pretty comfortable that the 20-year program is okay.

In the first five years, we are spending more on growth than we would choose because the growth is happening in the state, which means that some of the asset replacement and asset upgrade work is pushed out. But it is pushed out in the six to 10 years, which in the life of the assets is still quite

acceptable. So as long as that 20-year funding horizon is met, and that is pretty much—if you look at our forward estimates and take out the lumpiness of the second seawater desal plant, it really is a fairly constant amount of capital going forward, which we believe will meet all of the requirements of that. But if it were to be cut dramatically going forward, then it would be problematic.

**Hon KEN TRAVERS:** What I was hearing out of that is because of the rapid growth, you are having to spend more on growth. That does mean that maintenance work that you would otherwise have wanted to do over the next four years is going to get deferred to future budgets and future generations to actually carry the cost of that.

**Mrs Murphy:** Not maintenance work; maintenance work is happening because maintenance work is the only —

**Hon KEN TRAVERS:** Sorry, replacement.

**Mrs Murphy:** It is asset replacement. We would, in an ideal world, probably do about five per cent more of our capital program on asset replacement now than we are, but there is no risk to our ability to deliver our operating licence on the currently funded strategy. If the currently funded strategy were to change, if the forward estimates program were to change dramatically, that may not be the case.

[2.20 pm]

**Hon KEN TRAVERS:** So if you do not need to do it, then why would it have been a part of your original asset replacement plans?

**Mrs Murphy:** It is not that you do not need to do it, it might just be at a lower whole-of-life cost for the asset. For example, the ERA at the moment are doing our price review. As part of that price review, they have a consultant called Cardno who come in to look at the efficacy of our capital program and the efficiency and whether we are doing the right thing. Their comment was that overall it is really good; they are really pleased. But there have been a couple of examples where we have gone in and done a small upgrade and then two years later another small upgrade and three years later another small upgrade, whereas if you look at the whole-of-life cost, it may have been more cost effective to do a big upgrade in the first place. The fact that we are trying to keep state debt as low as possible and borrow as little money as we can is one of the reasons we chose to do that. So over the 50-year life of the plant, it may be marginally more effective to do one big upgrade. But in the way we are trying to make the capital program cover all of the assets we have got and all of the risks we have got, we are doing some perhaps slightly suboptimal, but I do not think we are putting a risk on any of our service delivery and we are not putting a risk on the asset base for our customers.

**Hon KEN TRAVERS:** But what that says to me is by having a cap on your borrowings, the end result is that it is going to cost us more.

**Mrs Murphy:** Potentially, but at the end of the day —

**Hon KEN TRAVERS:** And we are going to end up paying higher fees and charges for our water rates because we are not allowing you to manage the assets in the most economically efficient and effective manner.

**Mrs Murphy:** The former is true, the latter may not be. I might have to defer to Lloyd here about the model; our pricing model that the ERA follow. But about 70 per cent of our price is based on capital investment. So whilst deferring capital may not be the best value for money over the life of the asset, increased operating costs and deferring capital may still keep the price to customer about the same. I know that sounds complicated and hard to follow, but the net result is at the moment with the capital we are getting, we are keeping it in balance and nothing material is being deferred.

**Hon KEN TRAVERS:** Before we go to Lloyd, though, what that says to me is then your ability to make a profit is reduced, which then would change significantly the dividend to government. Where

it is now becoming clear the government is setting targets for you in terms of dividend in absolute terms that they want to recover from you as an agency, that will feed back in some way, whether it is increasing the rate of return that you are required to get off your assets or through some other mechanism, pushing prices up so that the government can still get the actual cash dollars that they are looking for in terms of dividends out of you.

**Mrs Murphy:** There is a pressure on us to reduce our operating costs, which is a way of getting dividends out of us —

**Hon KEN TRAVERS:** Which is on top of what we were talking about.

**Mrs Murphy:** Clearly. But clearly there is also a requirement on us to improve efficiency anyway. The ERA model assumes a two per cent cumulative year-on-year efficiency, so every year our operating costs are reduced by two per cent on the year before.

[Witness's mobile phone rang.]

**Mrs Murphy:** I am so sorry; I thought I had turned it off.

**Hon GIZ WATSON:** A bottle of red wine each, I think!

**The Chair:** It is a bottle of water really!

**Mrs Murphy:** Yes, purest Western Australian tap water! I am so sorry.

**Hon KEN TRAVERS:** I heard about this non-alcoholic halal vodka the other day which sounded awfully like water to me, but anyway!

**Mrs Murphy:** I think we have a marketing opportunity being proposed here that may be a way to meet the operating efficiency dividend!

The fact is, we are always looking for ways to be more efficient and we are highly mindful of the cost impact on our customers. So the trade-off between capital and operating is a juggling act that we are doing over thousands and thousands of assets all the time. We would always in an ideal world like to have more capital to ensure that the risks of failure are lower, but not spending the capital does not mean necessarily that that pipe will fail or that pump will fail. What it does mean is that our asset management regimes have to become slicker and more rapid and we have to get much better at using the data that we are gathering to be able to predict when we are going to have failures and get in there and do just-in-time maintenance, rather than wait for everything to fail, or worse still, routinely replace things that may not have been going to fail for some time. So, yes, there are pressures on the Water Corporation due to capital constraints and, yes, there are pressures on the corporation due to operating constraints, but I do not believe they are any worse than the pressures that are on every business operating in Western Australia at the moment. I think it is reasonably appropriate that we scratch to the bottom of the organisation looking for every form of efficiency we can deliver.

**Hon KEN TRAVERS:** But my experience is that the Water Corp has consistently done that anyway; that is not a new process that is suddenly being foisted upon you as an organisation. That is something that, certainly in the time I have followed the Water Corp, has been a constant ongoing part of the culture and the processes of it.

**Mrs Murphy:** Absolutely, so I think what it means is that you have to just keep looking at the business and look at different ways of doing things. There are some things we can do in technology; for example, the way you interact with your customers. You can put more online and reduce the number of calls you get, which changes the costs of running some parts of your business. I think there is a lot more we can keep doing and we are really looking actively at all parts of our business to see it. Remember, we are not given capital; we borrow capital and we pay back with interest. So if we were given the opportunity to borrow more capital, we would take that opportunity up, but I do not believe we are harming our customers or degrading our assets or operating in an unsafe way

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with the capital constraints we have. If we were heading for a situation such as the one that you outlined that Western Power appear to be in—I am not an expert on Western Power—I can assure you that my board would be jumping up and down very quickly! Our board do not have the protection of the Crown. We are not public servants under our act; none of us have the protection of the Crown. So, it is very much in our interest to make sure that that is very clearly communicated to our one shareholder who is the minister, so that would be happening if we were concerned about those issues.

**Hon KEN TRAVERS:** I think it is possible that the Western Power board was doing that to their minister. What I recognise is that Parliament has an obligation to be also testing those matters, which needs to be there.

Were there some other comments that we —

**Mrs Murphy:** Just about how the economic model works.

**Mr Werner:** You asked whether the fact that we were doing the smaller upgrades rather than the whole-of-life cost would affect the price to customers. We spend \$1 billion a year and that goes into the pricing model—that generates a price and a return. If we get \$900 million a year, the prices will actually be lower to customers because the ERA does not give us a rate of return on the extra \$100 million that we would spend. So, the issue about how does it impact on customers' prices, it depends on the size of our capital program. If it costs more to do something, then what happens is over time we have less to spend on other things. So, as Sue said, it is a balancing of risks and things like that. So the suboptimality either results in the need to spend some more money in the future or it will mean that you will take a couple more risks in the overall scheme of things. It will not flow through into customers' prices—paying more—unless it does lead to spending more in the future.

**Hon KEN TRAVERS:** That is my concern, because it is effectively deferring an expenditure today that ultimately means you either have to spend more or take a higher risk in the future. So that is still not a good outcome for the consumers in that it might look like you are doing okay this year but in two years' time or four years' time your capital expenditure is going to go up and therefore the amount that you are allowed to charge under the ERA modelling goes up, or you are running a higher risk profile on your assets than you would have professionally liked to have done at this point in time.

[2.30 pm]

**Mr Werner:** Yes.

**Mrs Murphy:** That is true, but because of the diversity and suite of assets, there is risk and there is risk. The risk of a major waste water spill into the Swan River is a risk that we are not going to play around with.

**Hon ALISON XAMON:** Good.

**Mrs Murphy:** We might take a different risk profile with a pipeline that leads to one customer in a country area where it is an augmentation in case of a drought to water stock.

**Hon KEN TRAVERS:** At which point the Chair says, "Not good!"

**Mrs Murphy:** No. If we have a contingency back-up plan, we can manage the risk. For instance, you can cart water if there is a catastrophic failure. One of the things we try to build into our capital program is to minimise the risk across our whole program. That is what Brian spends his life doing. If we have a group of customers who are served by one pipeline, be it water in or waste water out, then that is a vulnerable situation. In our capital program as we build capacity we try to always put some duplication in, so if this pipe fails, there is another way to serve those customers. In an ideal world we would have that everywhere and that would keep our risk profile low and keep our operating costs low, but the capital to do that would be prohibitively high and the state could never afford that. It is always this trading and balancing game. We have more customers who are single-

point vulnerable than we would like to have in an ideal world, but that does not mean that those customers are necessarily going to actually experience any adverse situation. We may have another way of servicing them, be it by trucking water or, if a pipe bursts and cannot be fixed for more than an hour, by providing bottled water—those sorts of things. We are looking much more robustly at some of these solutions. Sometimes the risk when you actually define it is worth teasing out. It is part of the whole regulatory push back that we have been trying to engage in with all of our regulators; that you do not just have a one size that fits all, you have to explore the situation and look at the consequences, look at the mitigation and ask whether this is a risk that as a society we want to take. That is a debate kind of outside the role of the Water Corporation as an entity, but because our only shareholder is the Minister for Water and our customers are the people of Western Australia, we feel we need to have that discussion.

**Hon KEN TRAVERS:** In terms of your capital program and your borrowings, what is the difference between what you are looking for and what you have been given in dollar terms?

**Mrs Murphy:** This year over the four-year estimates period it was about \$241 million; that was all that was formally deferred. Nothing is knocked back. Nothing goes away, it just gets moved out. Out of the \$3.6 billion, it was \$241 million. There was another \$80 —

**Mr Werner:** No, there was another \$92 million on top of that as well.

**Mrs Murphy:** That was in the final year. It is not defined to the specific project; well, it actually is, but sometimes those project priorities would change in that four-year period.

**Hon KEN TRAVERS:** All right. So around \$241 million out of the \$3.6 billion.

**Mrs Murphy:** Which I believe we can defer and manage through being clever. We have also been doing a lot of work on how efficiently we can deliver our capital program. We were very heartened by the big tick we got in the preliminary report from our auditors sent in by the ERA. We are probably getting of the order of about five per cent more bang for our buck out of our capital program at the moment than we were in the way we have packaged up some of our contracting arrangements and things.

**Hon KEN TRAVERS:** From all of that, what was your estimated dividend that you expect to get from this monetary year?

**Mrs Murphy:** CFO, have you got the list? Do you mean this year we are in now?

**Hon KEN TRAVERS:** Yes, 2012–13.

**Mr Hughes:** Oh, 2012–13

**Hon KEN TRAVERS:** If you have got the dividend for last year and also what you are estimating will be the dividend for this year.

**Mr Hughes:** The expected dividend from last year out of our SCI then was \$384 million. The forecast dividend for 2012–13 in the latest state budget papers is \$375 million. Bear in mind we also pay tax to the state government as well, but that is the dividend.

**Mrs Murphy:** Then we get back CSOs, but they are now called operating subsidies.

**Hon KEN TRAVERS:** Was that \$375 million what you estimated or is that what you would have been requested to provide by the government?

**Mr Hughes:** It is probably a two-way street, but a lot of our income and expenditure is regulated anyway. It kind of is the consequence of an engine of activity that generates that sort of output. To be clear, the percentage of our after-tax cash profits is 85 per cent, so that is pretty much where the dividend comes from. Ours has been 85 per cent for quite some time, so there has been no adjustment to our dividend pay-out ratio, if that is partly where you were coming from.

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**Mrs Murphy:** We do not set our price. The ERA make a recommendation to government and government chooses price. There is always a bit of toing and froing and fiddling around with the price over the four-year period that goes on. The current budget contains the ERA's price path going forward from three years ago. The ERA is doing a review now and they will recommend to government a price at the end of this—when is it? October?

**Mr Werner:** November.

**Mrs Murphy:** They will make that recommendation to government this year. The ERA will set the weighted average cost of capital, which is really the biggest chunk definer of what the price increases end up being. It is highly likely that the ERA will come up with a number greater than or different from what is in the budget for the out years, but that will not affect this year that we are in at the moment.

**Hon KEN TRAVERS:** You only control, then, in terms of changing the dividend is expenditure?

**Mrs Murphy:** Yes. No, no—we have a number of unregulated customers. We have commercial customers and industrial customers—your BHPs, Rios and Alcoas. We get headworks charges from land developers and property developers, which move with the amount of work. In fact Treasury has now formally linked the amount of money we get from developers' contributions into our capital program, so in a year where there is a lot of development going on we get more capital that year—that is actually matched dollar for dollar. If there is a lot more property development going on, then clearly we need to be doing a lot more investment to support that. Those are now linked directly, so they do bounce around a bit. They vary depending on what is happening in the property sector. We take a best guess of that for the year going forward, but that can vary. Similarly, you always have to be careful what you wish for. We are aggressively campaigning to work with our customers to reduce demand. Last year we were very successful in that, to the extent that it actually reduces revenue as well. Our economic model is totally bizarre in that we spend our entire advertising budget telling our customers not to buy our product and then rejoicing when our revenue goes down because of that, until our CFO adds the numbers up and says, "That was a good plan!"

**Hon SALLY TALBOT:** Sounds like a strong anti-privatisation argument.

**Hon ALISON XAMON:** The planet thanks you.

**Hon KEN TRAVERS:** When you then look at the cost of your next desal plant you will suddenly say it was not a bad strategy after all.

**Mrs Murphy:** Indeed.

**Mr Werner:** That is exactly right.

**Mrs Murphy:** That is exactly the issue with deferring capital for some of the other capital deferrals. I will tell you, the biggest way we can meet our operating efficiency dividend for the state government is to reduce per capita water demand, because that means less energy is used to pump water, we use less chemicals to treat it, we pay less money for all the ancillary things to go with that, and it also defers capital in both the long run and short run. For us, demand management, which you can slightly overdo in any one year, which is really more to do with climate than anything else, is the way that we can lower our costs for the long term.

**The CHAIR:** Hon Ken Travers, I will just halt you there and come back to you, because I know Hon Giz Watson —

**Hon GIZ WATSON:** No, I am fine, thank you very much.

**The CHAIR:** I will just move around and then come back to Hon Ken Travers at the end. I think Hon Sally Talbot was first.

**Hon SALLY TALBOT:** I am happy to go next.

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**Hon ALISON XAMON:** I have to go at three.

**The CHAIR:** Sorry, can we go to Hon Alison Xamon?

**Hon ALISON XAMON:** Thank you. I have some more questions about specific line items. I refer to the southern seawater desalination —

**Mrs Murphy:** Stage 2.

**Hon ALISON XAMON:** Yes. How confident are you that the additional water supply is going to ensure that Water Corp will be able to achieve its target of reduced extraction for the 2012–13 year? Also, if you think it is likely to be successful, understanding that we still do not know what sort of rainfall we are going to be looking at for winter, what sort of estimate are you looking at in terms of requiring abstraction?

**Mrs Murphy:** Our long-term abstraction plan, which has been developed in conjunction with the Department of Water, is that the long-term sustainable take from all the aquifers is about 120 gigalitres a year.

**Hon ALISON XAMON:** That is including the Jandakot mound?

**Mrs Murphy:** That is including Jandakot. Our plan over the next five years is to remove almost all of the bores from the superficial aquifer, which is the one that tends to be linked to the environmental wetlands, and be looking long-term at more permanent non-moving yields, if you like, from the Perth Yarragadee, the Leederville and a bit from Jandakot. The only superficial that we are looking to continue to take and maybe develop is just on the coast near Eglinton, as the superficial is flowing out to sea, so there is a possibility of taking some water there. Our aim is to keep that 120 as a baseload.

**Hon ALISON XAMON:** Can I just clarify that? Are you talking about 120 being the baseload in five years' time?

**Mrs Murphy:** No, as of this year. Assuming there is some rain over winter, we are very hopeful that next year we will take only 120. This year we have taken a lot. Southern seawater desal stage 2 will be coming online and that is our plan, because that is where we want to be for the long haul. Over and above that, the big issue for us for next year is to move groundwater replenishment from a trial to a full-scale approved project.

**Hon ALISON XAMON:** That was my next question.

**Mrs Murphy:** It is the 120, plus whatever we put in. The concept for the long term is a 120 base and the water we are putting into a deep aquifer. We will be injecting into the Leederville and the Yarragadee, not the superficial. For every gigalitre in, a gigalitre is to be added to our abstraction licence.

**Hon ALISON XAMON:** If you get down to 120, I, for one, will be very pleased. That is obviously a step in the right direction. The concern has been that we have been looking at very serious extractions occurring, particularly over the last few years. I am also concerned that Perth is growing, so we have population pressures. What I am trying to get from you is how confident you are actually feeling—it sounds like you are fairly confident —

**Mrs Murphy:** Very confident.

**Hon ALISON XAMON:** —that the extra 50 gig coming online is not just going to have to meet increased demand, but is also going to be able to deal with pulling back extraction to sustainable levels.

**Mrs Murphy:** Absolutely. Even though we have been taking a lot more than we would choose out of the groundwater system in the last couple of years, we have moved our abstraction pattern and we are taking the bulk of the water from the deeper aquifers now and very little from the superficial.

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**Hon ALISON XAMON:** It has been too late for some of the wetlands though, as you are aware.

**Mrs Murphy:** I know. But we are not the only people removing water. In fact, the superficial aquifer is used by a lot of people.

**Hon ALISON XAMON:** I am aware of that.

**Mrs Murphy:** Every one of our bores is licensed. I think my staff do an amazing job. I think this year, touch wood, at the moment it appears with all of the Perth borefield that no individual bore will over-abstract at all. It is a huge juggling act.

**Hon ALISON XAMON:** You are probably aware of the work I have been doing in hounding the DOW about the rest of the bores over the Gnangara, so I recognise that the Water Corp is only one of them, but it is the main one.

**Mrs Murphy:** Yes. We are a big and visible target and we must be good corporate citizens and do exactly what we can. I absolutely agree.

**Hon ALISON XAMON:** Okay. I wanted to ask about the groundwater replenishment as well. Obviously, we are hoping that the trial is ultimately deemed to be successful. Do you want to give some comment on that?

**Mrs Murphy:** Certainly. I think it is one of the most exciting possibilities for Perth water supply that I have ever seen, because your source of water grows with your population so it gives you the ability to actually be truly climate independent. The aim of the trial is not to get water but to get a regulatory framework that enables a full-scale project to go ahead. So far with the MOU and the work that we have done with Health and the Department of Environment and Conservation, everything is looking really prospective. There has been nothing untoward. Everything is going well. That trial completes at the end of December. There is then a bit of processing time. We would hope that by around April we will be in a position to get a formal go ahead from government. That, by coincidence, fits the political timetable well, because I doubt we will get a decision in March. Hopefully by April we can get a decision to move ahead to a full-scale scheme. The first stage we would be looking at is a seven-gigalitre project, because we can do all of that on the existing footprint of our Beenyup waste water treatment plant. So there would be no impact on anybody around us as there are no pipeline routes, there is no clearing, no nothing—it is on that same footprint.

We would be treating then seven gigalitres of water and injecting that into the Leederville. With one bore—one Yarragadee bore—proposed as we get that going, we would then augment in lots of seven gigalitres as we gain confidence and as we need the water.

[2.45 pm]

**Hon ALISON XAMON:** Could you please explain to me the time frames that are intended with that, particularly when the end of the stage 1 is anticipated to be?

**Mrs Murphy:** Stage 1 is 2015, to have it totally complete.

**Hon ALISON XAMON:** Yes. When in 2015?

**Mrs Murphy:** I think it is the end of 2014–15 financial year, is it not?

**Mr Robertson:** Yes.

**Mrs Murphy:** So the middle of —

**Mr Robertson:** The middle of the year, so in time for the summer.

**Mrs Murphy:** We worry about summers —

**Hon ALISON XAMON:** Yes.

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**Mrs Murphy:** So for the summer at the end of 2015. But the timing for the next tranches is climate dependent, so what we will do is—if we get rain we will always use the rainwater first. So if we were to get more rain, we would delay augmenting the plant; if the weather is dryer—if it just stays dry like it is—we would probably keep going straight on and augment. So it gives us a bit of flexibility in how we deliver the capital. Also, the people of Perth have been doing a very good job in the demand management stakes. At the moment we are saving more water than Perth is growing, so the delivery of water has been dropping. We are actually delivering less water this year than we did last year, even though Perth is growing. So we are absorbing quite a lot of growth at the moment. Clearly that has an endpoint, but at the moment I think there is still a long way to go in that space and we will be keeping going with that as well.

So the aim for Perth, hopefully by the end of five years, is that if we get rain we will always use it, and that we can use the lowest-cost source water first. But if we have a winter when we get no rain we still survive as a city—no, we do not survive; we thrive as a city in the same way we do now. We are embedding water efficiency legislation in the way things happen; the two-day-a-week that keeps Perth green and enables gardens to survive is permanent. The winter sprinkler ban, so you do not water when it is raining, is permanent, and you do not water in the day, when the water just evaporates, is permanent. By embedding those and keeping demand down and working with the garden industry and landscapers and developers we can actually absorb a lot of the growth anyway, and then we can use groundwater replenishment in increasing blocks to meet future demand. I do not see Perth needing another major new source other than the ground water replenishment for 15 or 20 years.

**Hon ALISON XAMON:** I do not know whereabouts I can look in the line items so I just want to ask about it, and that is the water pressurisation trials. What has happened with that? We have not been hearing much about that recently. Could you tell me if that has fallen off the agenda or if there is a suggestion that that might start to look at being rolled out going into the future?

**Mrs Murphy:** The reason you have not heard anything about it is because nothing has happened, so that is not surprising. It has not fallen off the agenda; it is not something we have been pursuing aggressively—we have had a whole lot of other things happening—but I think next year there is some money in the —

**Mr Robertson:** Yes, funding being provided for it.

**Hon ALISON XAMON:** Do you mind telling me which line item it is?

**Mrs Murphy:** It will be in a bundle.

**Hon ALISON XAMON:** You can see that it is very broad.

**Mrs Murphy:** Is it opex or capex?

**Mr Robertson:** It is capex.

**Mr Hughes:** It will be somewhere on page 860.

**Hon ALISON XAMON:** Okay; I refer to page 860!

**Mrs Murphy:** I realise you are asking questions based on the budget, and because we are a corporatised entity the budget has capital revenue and CSO, so it does not necessarily give you the detail.

**Hon ALISON XAMON:** Are you able to give me the detail in —

**Hon KEN TRAVERS:** The SCI would give us more detail.

**Mrs Murphy:** No, it would not; the SCI does not have very much detail.

**Hon ALISON XAMON:** So I was not wrong then when I thought it had fallen off the agenda, but I am glad to hear that it is probably going to be coming back.

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**Mrs Murphy:** It is funded in this current financial year to get started again.

**Mr Robertson:** Yes.

**Hon ALISON XAMON:** Could I please get the amount for that funding, and also forward estimates? I am happy to take that on notice if that is easier. The other thing is, if you could also identify which areas have been identified for further rollout, because I am aware that it cannot occur everywhere; and also the time frames for when those areas are going to be rolled out? I am happy to take all that on notice.

*[Supplementary Information No C2.]*

**Mrs Murphy:** So it is the pressure reduction work; what areas; timing; and dollars for the forward estimates periods?

**Hon ALISON XAMON:** Yes, please.

**Mrs Murphy:** The timing may be a little bit flexible, because as you do it, sometimes areas that look prospective are not when we get into the engineering. We will give you what we have.

**Hon ALISON XAMON:** Because of course I am aware there are capital costs potentially involved with that as well.

**Mr Robertson:** Yes.

**Hon ALISON XAMON:** So, I am assuming that some preliminary work on that has already been identified as well.

**Mrs Murphy:** Yes. We did do a trial in the Rossmoyne area.

**Hon ALISON XAMON:** Yes, I know. I know it was successful, so that is why I have been keen to see it rolled out.

**Mrs Murphy:** We agree.

**Mr Hughes:** Unless you are a Rossmoyne resident!

**Mrs Murphy:** He is a Rossmoyne resident.

**Hon ALISON XAMON:** You do not like it?

**Mrs Murphy:** He has no choice but to like it!

**Hon ALISON XAMON:** That is right!

Can I also have the actual figures for the last financial year, for this financial year and for the forward estimates for the programs for water conservation? By that I mean the public education programs, such as the save six buckets. Do you have that on hand or do you need to take that on notice?

**Mrs Murphy:** I would have to take that on notice because that is all operating, none of that is capital. The operating line items are not in the budget, but we can certainly dig those out for you.

**Hon ALISON XAMON:** Are you able to give —

**Mrs Murphy:** Some are co-funded federally.

**Hon ALISON XAMON:** Sure. Are you able to indicate—again I am happy to take it on notice—what percentage is federal funding and what percentage is Water Corp? I am also interested to know generally whether there has been increasing funding for these sorts of public education campaigns or if it has remained fairly constant or if it has been going down.

**Mrs Murphy:** I can tell you that the public education component—I do not have the dollars off the top of my head—is pretty constant; it goes on forever. There is an opportunistic nature to the federally funded programs; we have a suite of programs that we would like to run, and as funding becomes available or they fit a funding criteria we will always try to access that funding. There has

been a big tranche of those that are just coming to an end at the moment. But federal government has been very helpful in, for example, the showerhead swap program we have been running—it has funded that all the way through—and we have had some other water efficiency program work where we have come in under budget and it has allowed us to roll those unspent funds into some work going forward. But generally the federal funding, apart from rolling forward some unspent funds, has finished. There is a little bit there, but most of it going forward is all Water Corp funding.

*[Supplementary Information No C3.]*

**Hon ALISON XAMON:** Can I confirm then that showerhead swap scheme has now ended?

**Mrs Murphy:** No.

**Hon ALISON XAMON:** It is ongoing, is it?

**Mrs Murphy:** It is ongoing, but we do not have that many left. I think we swapped 100 000, which was the original program, and I think we have another 20 000 we are going with now.

**Mr Hughes:** We feel like we are getting closer to a saturation point.

**Mrs Murphy:** The take-up has slowed a lot. But when bills go out, which is happening as we speak—the rates bill—there is usually a flurry again.

**Hon ALISON XAMON:** Which leads me on to my next point, and I am picking up on your comment about it reaching saturation point. Of course, a whole range of programs were axed in 2009; is it coming around to that time when it is actually going to be useful to start rolling out some of those water conservation measures again? I am aware that we have a whole bunch of people who are now living in homes who would probably want to take advantage of various water conservation measures.

**Mrs Murphy:** Everything has a use-by date and a point at which the law of diminishing returns kicks in. I do not think we would start the washing machine one again because that program actually changed the washing machine availability. You really have to look to find a water-inefficient washing machine in Perth now, so I do not think there is much to be gained by —

**Hon ALISON XAMON:** But there are a whole range of areas—plants and garden areas and all sorts of things like that—so I was wondering if there is any appetite to actually reinvigorate some of those programs?

**Mrs Murphy:** We look all the time at where the best bang for our buck is. For us at the moment we have to be very careful that we are not pushing costs onto our customers that we could meet cheaper in some other way; the water we save has to be cheaper than the long-run marginal cost of the water we are supplying, or we are asking our customers to pay for something we can supply cheaper. There has to be an economic justification as well as a “it is a good thing to do” kind of justification. We are looking at those programs all the time. The showerhead swap was a really good one because it saves a lot of water, and once it is in place it keeps saving water. We have some other programs where we have partnered with private sector, such as the Toilets to Go program that does not cost the state or the Water Corporation any money. By getting a competitive price from the private sector, they will guarantee to replace your water-inefficient toilet with a brand-new toilet at a very low cost—it is actually cheaper than just buying the hardware fittings—and they will come and fit it for that. So, what we are looking at is more innovative ways along the way. I do not think just putting your hand in the pocket is always the right answer, and I think we have to keep the story changing. We blitzed gardens for a while because that was where the big water use was. We have now, in the last home water use survey, found that it used to be 45 per cent inside, 55 per cent outside; in the last survey that swapped around, so it is 55 per cent inside, 45 per cent outside—I hope I said that right. Anyway, it has gone the other way. What we thought was we would do a blitz on the in-house, which is why we did the showerhead swaps, and we have done a lot of stuff about

not running your dishwasher until it is full and those sorts of things. So I think what it means is that coming into summer, we will move back into ex-house campaigns.

**Hon ALISON XAMON:** I suppose it is always the tension between needing to get favourable economic outcomes with the fact that we have to have favourable environmental outcomes as well.

**Mrs Murphy:** Yes, but I am not talking about Water Corp making money.

**Hon ALISON XAMON:** No, no.

**Mrs Murphy:** What I am saying is, like a rainwater tank; a rainwater tank costs, per kilolitre, more than the water we supply, so for me to say to my customers that they have to have a rainwater tank would be cost-shifting. Now, to say, “By all means put one in, because it is a great visual signal, you learn a lot, it is great and it is a fabulous idea”, is a totally different thing. But with the rainfall patterns in Albany a rainwater tank is actually more cost-effective, so we actually do offer a Water Corp rebate in Albany for a rainwater tank plumbed into your house, but we do not in Perth. There is no silver bullet; it is lots and lots of things. There are lots of campaigns we will run, there are lots of things we will subsidise, there are lots of things other people will subsidise, and we just need to keep changing the message but keep the general direction going.

**Hon ALISON XAMON:** I also just wanted to ask about the Kwinana industry water recycling program; I wanted to know how that is going. I think the last time I heard, they were recycling about six gigalitres, and I was wanting to know whether there was any scope to increase that or any proposals to increase that beyond that area.

**Mrs Murphy:** Not at the moment. The foundation customer for that plant—which is to take treated waste water from the Woodman Point treatment plant, treat it to boiler-feed quality and sell it back to industry—was Hismelt. Hismelt went into care and maintenance and so they were not taking any water, and now Hismelt has gone altogether. We have sold all the Hismelt water now to other customers.

**Hon ALISON XAMON:** Is it still the six gigalitres that we are talking about?

**Mr Werner:** Yes. The plant has not expanded, because the customer who was taking up the capacity left. We have had to actually had to go and sell that capacity to other customers in the area, so that is what has been engaging us over the last year or two for that project.

**Hon ALISON XAMON:** So it is continuing to be six gigalitres that you are managing to recycle though?

**Mrs Murphy:** Yes.

**Mr Werner:** Yes.

**Hon ALISON XAMON:** And you have been able to find customers?

**Mr Werner:** Yes.

**Mrs Murphy:** Yes.

**Mr Werner:** There are customers who are taking it opportunistically. They have the pipes in place and they have use, so we have been trying to sell it to those customers and we have been successful at that. We are trying to get those customers onto long-term contracts so that we can be assured that they will be taking that six gigalitres year in, year out.

**Hon ALISON XAMON:** It sounds like there is no expansion in the pipeline, so to speak.

**Mrs Murphy:** It is ready to be expanded, the gist of the engineering is there, but we need customers. We did go out looking for further customers and we have done expressions of interest a couple of times, and that is how we made up the six gigalitres, but we have not got further customers at this stage.

**Hon ALISON XAMON:** Can I ask at what price that water is actually being sold to industry for?

**Mr Werner:** The stuff that is under contract is probably confidential, I think.

**Mrs Murphy:** Roughly the long-run marginal cost of water-ish.

**Mr Werner:** When we first wrote those contracts the price was higher than the potable water supply, and that is because it is a higher quality —

**Mrs Murphy:** It is a higher quality water.

**Mr Werner:** —in terms of salinity and stuff like that. So for industrial uses it had higher value.

We have changed the structure of the tariffs so the volumetric component for industry has gone up out of the potable scheme. That is heading towards a couple of dollars a kilolitre.

**Hon ALISON XAMON:** So it is equivalent?

**Mr Werner:** The commercial stuff is lower than the potable now, so that has switched around. The discussion we are having with industry is about probably selling that water for about \$1.75 if they sign on to long-term contracts, or at \$2 if they are just taking it opportunistically. But what is in the actual existing contracts is lower than that.

**Mrs Murphy:** It is an unusual water recycling scheme in that it is selling boiler quality water. People always assume that recycled water is somehow inferior; this is superior, if you like. I am not sure that water has a personality, but it is a much purer water!

**The CHAIR:** I think your observation is correct!

**Hon SALLY TALBOT:** I will carry on my line of questioning from the previous line because it segues quite nicely. One of those potential customers, presumably, would be Alcoa, which is desperate for water.

**Mrs Murphy:** In Kwinana?

**Hon SALLY TALBOT:** In Pinjarra and on to Wagerup. Can I start by asking you about your involvement in the Peel waste water reuse scheme project?

**Mrs Murphy:** We have been in discussion with Alcoa for years and we have a signed agreement for them to take waste water from Gordon Road. The original plan was for them to build a pipeline, and that was nothing to do with us; we were just selling the water at the gate of the waste water treatment plant.

**Hon SALLY TALBOT:** They were taking your product and putting in their own pipe, which they would have owned.

**Mrs Murphy:** Yes. They have not proceeded with that. I am aware that there are a whole lot of other possibilities being spoken about and a whole lot of other ideas; I do not think they have landed anywhere at this stage.

**Hon SALLY TALBOT:** The interesting thing is that the documentation I have seen talks about quite an extensive public sector component of that, and I would be a bit intrigued if they have not been talking to you about that.

**Mrs Murphy:** No-one is asking the Water Corporation to fund anything. If we were to fund a pipeline, we would then charge a commercial rate to recover the cost of that pipeline to a customer, but our limit is our borrowing. If I am constrained for capital to do the things we have to do for our customers, then for me to use that capital for a commercial deal for Alcoa is inappropriate. But if someone else wanted to finance it, for us to build it and for us to borrow the money—if we could borrow the money off the state's balance sheet somehow, and do a commercial deal with Alcoa, that would be a great solution.

**Hon SALLY TALBOT:** Nobody is talking to you about that?

**Mrs Murphy:** Everybody is talking to us about that, but not in a way that —

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**Hon KEN TRAVERS:** No-one is opening their cheque book for you.

**Mrs Murphy:** No. It has not reached a point —

**Hon SALLY TALBOT:** You mean it is all talk?

**Mrs Murphy:** At this stage, yes. It has not reached a point of anything being triggered into a project.

**Hon SALLY TALBOT:** Would you expect Water Corporation to be involved if there were public sector funding of the easements?

**Mrs Murphy:** Do you mean buying the pipeline route?

**Hon SALLY TALBOT:** Yes. I assume it is the easement for the pipeline.

**Mrs Murphy:** It depends who owns the pipeline. The bigger issue would be who owns the pipeline; if the private sector owned the pipeline, then I would not expect Water Corporation to go near it, ideally. That would be someone else's; I would not want to inadvertently take any risk on anything that we do not own. If we owned it—we do not have to own the easement, but we would have to have an interest in the land. To me, it is the ownership of the pipeline more than the easements, but other public sector entities could own it; we do not have a monopoly.

**Hon SALLY TALBOT:** But not Water Corporation?

**Mrs Murphy:** We would be happy to own it if I could borrow the funds off the state's balance sheet—not having that borrowing on the state's balance sheet.

**Hon SALLY TALBOT:** But you would not be looking at putting Water Corporation money into buying easements for a pipeline that Water Corporation did not own?

**Mrs Murphy:** No, not unless we were going to use it for some other pipeline that we did own or there was some other reason for the Water Corporation to buy it.

**Hon SALLY TALBOT:** What about Water Corp's involvement in funding for additional water capture or treatment or storage initiatives along the pipeline route?

**Mrs Murphy:** Unless we get a customer who is going to pay for it—if it is a commercial customer, unless there is commercial deal for us in it that someone is going to cover the costs and we are going to make a return on it, then we would not get involved. If there were a community good purpose, if it was for the good of the community and the government chose to fund it, we would get involved if the government asked us to, but —

**Hon SALLY TALBOT:** Which would be a policy decision.

**Mrs Murphy:** It would be a policy decision; it is not really a —

**Hon SALLY TALBOT:** Does Water Corp make any funding provision for agricultural production precincts, or agri-industry precincts?

**Mrs Murphy:** No. We do sell bulk water to irrigators. That is our only agri-anything.

**Hon SALLY TALBOT:** I have some other questions involving regional facilities, if I can keep going. I would like to ask you some questions about the announcement earlier this year of the project to establish the viability of the water supply for the West Canning Basin, about 120 kilometres out of Port Hedland. Can you tell us how much Water Corp is contributing to that investigation? Where is it up to? I understand the announcement was around the beginning of this year. Where is it up to, what is Water Corp paying for, and what budget stream are you funding it from?

**Mrs Murphy:** The Department of Water believes there is at least 10 gigalitres available in the West Canning Basin that is allocated, at the moment, to the Water Corporation. No-one has done the drilling to know exactly where you put the bores, how they work, where a pipeline would be, or

anything. We have worked with BHP, Atlas Iron, and FMG to co-fund the drilling to see how much water there is there, and we are sharing the costs of that drilling program based on the amount of water that we would get as a percentage of the 10 gigalitres there. If there is five gigs there, we would all get that percentage of it; if it is more than 10 gigs, we would still only get the percentage of the 10 gigs; we would preserve anything above 10 gigs for the Water Corporation.

**Hon SALLY TALBOT:** A sort of pro bono deal?

**Mrs Murphy:** It is, a bit. The whole thing is about six million and our share is about half a million. BHP is doing the most; I think BHP is six gigs out of the 10 gigs, FMG is two and we have one—something like that.

**Hon SALLY TALBOT:** Is it about a twelfth share in the overall project?

**Mrs Murphy:** Yes, but the joy of the project, if you like, is that the water, without treatment, is not potable, but without treatment it would be suitable for dust suppression, so by building that pipeline we would be able to take pressure off the existing bore fields to supply the town of Port Hedland. Our interest, as the Water Corporation, is less about getting water from the West Canning Basin for ourselves and more about getting the dust suppression users off the town scheme, but the reason we are involved with it is because those mining companies do not always play nicely together, and by the Water Corporation being involved, no one private sector agency would own the infrastructure, so a future user coming in, another mining company, would still be to get involved because we could broker a deal through them. The half a million dollars for the drilling is not a huge investment for us, but it preserves some flexibility and some commercial rights for people who have not yet started working in the East Pilbara.

**Hon SALLY TALBOT:** That is very interesting; what is Water Corp's formal role in the deal?

**Mrs Murphy:** We are leading the deal. We are pulling it together.

**Hon SALLY TALBOT:** So you are going to be the broker of the unfolding of the deal, if people wanted to leave or join? Water Corp would be the broker?

**Mrs Murphy:** Yes.

**Hon SALLY TALBOT:** Why is it a comparatively small share? Is it because it is not potable?

**Mrs Murphy:** Yes. We have two goals in the whole process in the whole process. The first goal is to get non-potable users off the scheme in Port Hedland town, if we can, which actually allows us to use the existing bore fields and existing infrastructure for the town.

**Hon SALLY TALBOT:** So you are recovering potable water?

**Mrs Murphy:** Yes, a sort of backwards recovery. The second is that we are there to preserve the rights of future investors or future proponents who may want to be part of the scheme from being shut out, because if BHP were to build it all by itself, it would then have an asset that would not be a common user infrastructure; it could keep other people out of it and have some sort of pre-emptive right on the pipeline, even if it did not have a pre-emptive right on the water, and no-one else would ever be able to get in and justify building it for a small quantity of water. So our aim is to keep it fair for the future, for the people who are not there yet but might be, and to move non-potable use off the scheme.

**Hon SALLY TALBOT:** I bet they wish they had gotten involved with the train lines!

**Mrs Murphy:** I have enough problems, thank you!

**Hon SALLY TALBOT:** Just a further question on that part of the world. There is a remote communities program being rolled out. I wondered if Water Corp has any investment in that. I am looking at an announcement, again in February, of \$12 million of royalties for regions funding to upgrade essential water services at remote Aboriginal communities.

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**Mrs Murphy:** Not in the top line. We are, as almost a subcontractor, doing work in two remote communities at the moment. The Department of Housing is the lead agency, and it contracts that work out. Some of it is done by the private sector, and we are doing some work in that, but we are not the proponent.

**Hon SALLY TALBOT:** Which are the two that Water Corp is involved in?

**Mrs Murphy:** I would have to check. There are seven that we have looked at; I will have to take that as a question on notice. Which are the Aboriginal communities that we are doing work for the Department of Housing on.

*[Supplementary Information No C4.]*

**Hon SALLY TALBOT:** Because I have mentioned the “R for R” words, I will ask you about page 861. I notice that there is royalties for regions money from the regional infrastructure headworks fund. Can you just take us through each of those years? I am referring to the last line item under “Funded By”—“Drawdowns from Royalties for Regions Fund”.

**Mrs Murphy:** Sorry?

**The CHAIR:** The line item at the bottom of page 861, “Drawdowns from Royalties for Regions Fund”.

**Mrs Murphy:** Do we have a different page 861? I do not know. That is not in our copy; I am sorry. The totals are the same.

In respect of those small amounts from the royalties for regions funds, there are a number of modest projects we are doing for them. There is the Roebourne waste water treatment plant; that has got a bit this year. There is a big lump of \$42 million, which is to move the Port Hedland waste water treatment plant. At the moment in Port Hedland, there are two waste water treatment plants: one in Port Hedland and one in South Hedland. The one in Port Hedland was in a fabulous place when Port Hedland was created, but —

**Hon SALLY TALBOT:** I do remember that we covered this in some detail in estimates last year.

**Mrs Murphy:** Yes. There is \$42 million for that over the forward estimates, and there is about another \$6 million of royalties for regions money over everything else and a couple of regional recycling schemes.

**Hon SALLY TALBOT:** Perhaps what I could do, seeing as we have the rather odd circumstance of you not having the same numbers as me—in fact, me having more than you —

**Mrs Murphy:** I like yours better!

**Hon SALLY TALBOT:** I am a bit worried about the bottom line being the same. Can I ask you to take that as the next supplementary question? We have got this line item, “Drawdowns from Royalties for Regions Fund”, which is footnoted as regional infrastructure and headworks fund. It is \$2.6 million, \$1.8 million, \$1.9 million, \$1.9 million, and then nothing in the 2015–16 year.

[3.15 pm]

**Mrs Murphy:** So you want the royalties for regions funding.

**Hon SALLY TALBOT:** Why is there none for 2015–16? Is it simply that you have not got that far ahead in applying or being offered money?

**Mrs Murphy:** There is not a lot of royalties for regions funding that is appropriate for Water Corporation projects, because most of our projects are baseline projects anyway. It is only for something that we would not have done in the normal course of business that is perceived as having a benefit to the region that is funded through royalties for regions. I do not think royalties for regions has allocated a great deal of funding in the out years. They tend to release tranches of funding.

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**Hon SALLY TALBOT:** If I could have the breakdown of the figures.

**Mrs Murphy:** A breakdown of what is in those figures, sure.

*[Supplementary Information No C5.]*

**Hon SALLY TALBOT:** My notes say that the Kalbarri waste water scheme upgrade is due to commence in September this year and completed within the financial year. I wonder whether that is funded under the heading “Works in Progress”, the line item “Wastewater Program” for country wastewater treatment and conveyance on page 860.

**Mr Robertson:** Kalbarri is an active project that will be included in those works in progress at this point in time.

**Hon SALLY TALBOT:** How much is that costing?

**Mrs Murphy:** Brian has the project details.

**Mr Robertson:** It is \$3.34 million. That is the funding available in 2012–13 for that project and excludes previous expenditure.

**Hon SALLY TALBOT:** What else is covered under the line item for country waste water treatment and conveyance?

**Mr Robertson:** The projects feeding into that equation include waste water treatment plants and upgrades in the goldfield and agricultural region at Beverley and Toodyay. There will be a number of pump station upgrades to meet growth in those areas and some conveyance system works, so a number of projects will comprise that total line item.

**Hon SALLY TALBOT:** Could you take that as another supplementary please and give us a breakdown there?

*[Supplementary Information No C6.]*

**The CHAIR:** On that same question: are there any royalties for regions funding contributing to funding the assets in that line item?

**Mr Robertson:** There is none from royalties for regions, but there is commonwealth funding for the Kalbarri waste water treatment plant.

**The CHAIR:** Is there only commonwealth funding?

**Mr Robertson:** All that I am aware of, yes.

**Mrs Murphy:** Just to be clear, it is a breakdown of the country waste water project line.

**Hon SALLY TALBOT:** It is that line item, and the projects that includes?

**Mrs Murphy:** You want what is not funded by us?

**The CHAIR:** I think I have that answer already, thank you.

**Mr Robertson:** I will double-check and confirm that back as part of the answer.

**Hon SALLY TALBOT:** My last question on specific projects is about the biosolids program. Is that covered in the item “Support Programs” on page 860?

**Mrs Murphy:** When you refer to a biosolids program, do you mean the lime amended biosolids program trial at Ellenbrook or those biosolids being stored in the wheatbelt and used as a fertiliser in Moora?

**Hon SALLY TALBOT:** I have two here—Moora and the Myalup pipe plantation.

**Mrs Murphy:** Myalup will not be in the budget papers at all, because that would be an operating cost; there is no capital in that. Myalup would be in straight operations, so that would not appear in any of those numbers.

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**Hon SALLY TALBOT:** What about the Moora trial?

**Mrs Murphy:** The Moora trial is probably all operations now too. A building was constructed to store the biosolids, which would have been capitalised already. That would have been completed, so I doubt there is any capital there at all for Moora; it would be an operational issue and would be trucking and handling now.

**Hon SALLY TALBOT:** Is it covered in another part of your budget papers?

**Mrs Murphy:** Because we are corporatised entity our operating lines do not appear. It is clearly in the Water Corporation's own budget, but the government process only has capital in it.

**Hon SALLY TALBOT:** Are you involved in operating funding for the biosolids projects?

**Mrs Murphy:** Yes.

**Hon SALLY TALBOT:** How much have you committed to that?

**Mrs Murphy:** That will have to be taken on notice.

**Hon SALLY TALBOT:** I have a couple of questions about it. What is Water Corporation's budget for the biosolids program? How much does it cost to produce? What is the product? I assume it is compost?

**Mrs Murphy:** They are like little pellets of fertiliser. It is not so much how much it costs to produce it, because we do not have a choice but to produce it. Our waste water treatment plants produce biosolids, and they have to go somewhere. So we choose to heat and dry them and, in the Moora example, use them as a fertiliser. The Myalup example is different because they are not totally dried, so that is not a dried pelleting process; it is a wettish sludgy stuff which is spread around the pine trees as a fertiliser. This is the last year that was done, so that program does not continue.

**Hon SALLY TALBOT:** Was that a trial?

**Mrs Murphy:** Everything is, sort of—yes, it was a trial.

**Hon SALLY TALBOT:** So it is not going to continue?

**Mrs Murphy:** It is not going to continue. There were mixed views from the local community; they were not pleased.

**Hon SALLY TALBOT:** You mean they did not like dirty brown sludge being spread around their pine trees?

**Mrs Murphy:** Some, although the pine trees were quite some distance from the community.

**Hon KEN TRAVERS:** I am sure they might have called it something other than dirty brown sludge!

**The CHAIR:** I think it was the horsefly problem that got people excited.

**Mrs Murphy:** The pellets appear to be a much better solution, but we are also doing a trial, which I think is really prospective, of taking something that is not dissimilar to the pellet solution, blending it with lime, which kills the microbes and pathogens in it, and then blending that further with clay to form a product which is, surprisingly, called lime amended bioclay, and we are doing some trials. It is very innovative. We may have to work on the marketing.

**Mr Werner:** It is why we are called the Water Corporation.

**Mrs Murphy:** Yes, marketing may not be our long suit! Despite the lime amended bioclay's somewhat pedestrian name it is really promising and we are doing some trials in the Ellenbrook area. One of the problems with Western Australian sandy soils is the acid sulfate soil, so the lime helps with the soil conditioning, and the lime amended bioclay helps with water retention in the soil and the biosolids provide a natural, very slow releasing fertiliser. The trials we have done have been

very prospective for farmers with grazing lands, so they are getting a lot more grass. We are also looking at it for turf growers as a fertiliser and soil agent. It appears to hold the nutrients very firmly into the soil, so the fertiliser run-off is much lower. We see it as a great way of reducing run-off into the upper reaches of the Swan and as a potential commercial product. Now, it may be the Water Corporation that commercialises it or we could partner with someone in the private sector to do it, because clearly naming products may not be for us—someone may come up with a catchier name. We have been doing it as a trial, so we have a trommel where we are mixing it. It is probably even more prospective than the Moora trial. Everyone agrees that the nutrients contained in biosolids are a resource and something that is really important for the community and that the word waste is a misnomer. However, when individual members of the community come in contact with biosolids, they are not usually thrilled, so there is a bit of a marketing and sales job to be done to get the community to understand it is a valuable resource.

**Hon SALLY TALBOT:** I heard of an interesting trial that was done recently in which people were given two glasses of water and asked which one they would like to drink. One is recycled sewage and one is tap water, and they all drank the tap water. But if you say one is purified water and one is tap water, they will drink the purified water. I have probably doubled your stock of knowledge!

**Mrs Murphy:** You are absolutely right. The corollary to that though is when you use cute language the public can turn on you. With our groundwater replenishment trial, we have a community facility that takes school groups through and we are very overt that it is sewerage water and it does come from your toilet and this is what happens to it and why you can drink it. In the Queensland experience, they spent all that money and the whole thing got thrown out.

*[Supplementary Information No C7.]*

**Mrs Murphy:** That is on the biosolids program funding.

**Hon SALLY TALBOT:** I think you just pulled yourself back from saying that it is all trials.

**Mrs Murphy:** They are all trials to a certain extent. I do not think that we have landed on an optimum long-term way to get the best out of the biosolids we have.

**The CHAIR:** You are certainly getting closer.

**Mrs Murphy:** Good.

**Hon SALLY TALBOT:** I would like to get a sense of what sort of money is going into the trials that you are running, both in capital and operational expenditure. Are you proposing anymore?

**Mrs Murphy:** The biosolids just keep coming, so we have to dispose of them. Disposing of them in a non-beneficial way kind of goes against the grain through the entire corporation. We will keep doing trials until we come up with a solution. I believe it is a revenue source for the corporation.

**Hon SALLY TALBOT:** Perhaps we could merge you with the Waste Authority.

**Hon KEN TRAVERS:** The ultimate BS pellet!

**The CHAIR:** What capital was required to build the plant for the pelletisation of the biosolids?

**Mrs Murphy:** It is before my time. It was done quite a while ago. It comes from Subiaco. Moora operates with waste from Subiaco largely. I understand it is just a drying kiln. I do not think it would be particularly expensive.

**The CHAIR:** So the pelletisation of the biosolids is not that big a cost. I always figured it might have been.

**Mrs Murphy:** The big cost in the whole process is transportation. When you pelletise it, it becomes lighter because all you are really doing is removing all the water, so you are not transporting water. There are costs in drying it out, but they are probably offset by the cost of not transporting water around.

**Hon SALLY TALBOT:** How many FTEs does Water Corporation have?

**Mrs Murphy:** Roughly about 3 000. There are roughly 3 000 people paid through the Water Corporation payroll.

**Hon SALLY TALBOT:** So that is bodies?

**Mrs Murphy:** Yes.

**Hon SALLY TALBOT:** What does that translate to in FTEs?

**Mrs Murphy:** No, that is FTEs and not bodies.

**Hon SALLY TALBOT:** What does that translate to in bodies?

**Mrs Murphy:** I do not know off the top of my head.

**Mr Hughes:** I would be estimating.

**Mrs Murphy:** We deliver Perth regional operations, and have done for years, in a partnership with the private sector. We have just re-awarded those contracts, so we have about 500 employees who work for another company but are permanently in a shared partnership with the Water Corporation.

**Hon SALLY TALBOT:** Is that the Transfield consortium?

**Mrs Murphy:** There are two contracts. One is a contract with Programmed Maintenance Services and one is a joint venture between Transfield and Degremont. That only applies to a few people in the management team. The actual blue collar workers are in a holding company that stays the same. Fifteen years ago they were water authority employees, then they were put in a holding company and those holding companies go with whoever has those maintenance contracts. I am not explaining that very well. But the blue collar workforce is paid by Programmed in the Perth region and by the Aroona alliance, which is Transfield and Degremont for the water and waste water treatment plants. But the individual people are the same people that move along; it is not like it is a new company coming with new people at a grass roots level. Then there is the capital business where we are delivering about a billion dollars of capital, which is in partnership with either the design companies or construction companies and there are probably about 2 000 people employed across our capital business as well—not Water Corp people.

**Hon SALLY TALBOT:** Whose payroll are they on?

**Mrs Murphy:** That would be Leighton, GHD, John Holland, Georgiou, Tecnicas Reunidas or someone like that.

**Hon SALLY TALBOT:** I am glad you said you were not sure whether you were explaining it very well. I thought it might be me. We are talking about 3 000 Water Corporation FTEs, and over and above that you have these 500 in admin positions.

**Mrs Murphy:** No, the 500 are the men with spanners fixing things around Perth—blue collar largely.

**Mr Hughes:** They are employed by other people on our assets—so, if there is a waste water overflow in your street.

**Hon SALLY TALBOT:** They are over and above the 3 000?

**Mr Hughes:** Correct.

**Hon SALLY TALBOT:** I notice you say that you recently re-signed the contracts. Has it been a quantitative change in the latest round—Transfield–Suez–Degremont?

[3.30 pm]

**Mrs Murphy:** There have been changes. There are two distinct chunks of work. One is fixing pipes that break, and pump stations and things like that. That work used to be in two contracts: everything north of the river for the Perth metro area, which was a contract that we had with Thiess called

Swan Water; and one south of Perth, which was a contract with the United Group, which was called Western Water. We have taken those two contracts, which came to an end, and we now have one contract instead of the two, which is for all of Perth. The people who were employed by Thiess and the people who were employed by the United Group are now employed by Programmed Facility Management. Programmed are our partners for that work. That alliance has Water Corp people in it and Programmed people in it. Then we have another alliance. For the last 15 years we outsourced the mechanical and electrical maintenance work in our big water and waste water treatment plants in Perth. It had been with the same company but the company had changed names over many years. Its most recent incarnation was PSN Water. That contract came to an end and we have created a new relationship with Transfield Degremont called the Aroona Alliance. The people who were working for PSN Water are now in the Aroona Alliance. We have taken the Water Corp people who remain Water Corp people and stay on our payroll who were operating the plant and doing the civil maintenance and moved them all together into one alliance working together. Previously the plants operated and the maintenance happened separately. One of the efficiency ways forward that we identified years ago was that mixing maintenance and operations into one whole of plant concept to maximise the output of the plant was a way of getting more out of our existing assets and that is what the Aroona Alliance has been created to do. In the Programmed alliance, which is called the Perth Region Alliance, about 70 per cent of the employees are paid on payroll by Programmed and about 30 per cent are paid on the Water Corp payroll. On the Aroona Alliance, about 70 per cent are on the Water Corp payroll and 30 per cent on the Aroona payroll. With these alliances we share risk. If we can do the work together and be more efficient and save money, our partner will get a higher margin and the Water Corp will save money. If it costs more, they lose their margin so they are incentivised to work with us to become more efficient. The two per cent cumulative efficiency dividend that is built into our ERA model is built into those contracts so their budgets reduce.

**Hon SALLY TALBOT:** Is it not precisely that sharing of risks that alarms the community? Will we get to a stage where a water pipeline bursts and the Water Corp stands around and says, “It’s not our problem; it’s a private company”?

**Mrs Murphy:** No, because it absolutely is our problem. The operating licence we have with the ERA and the relationship with our customers is with the Water Corporation. The man who is running the Perth Region Alliance at the moment has been with the Water Corporation for 30-plus years. It is an integrated team. We are partnering with the private sector in the absolute meaning of partner—to bring in ideas. They are incentivised to help us find more efficient ways of doing things but it is still our name on the line and it is still our obligation to service our customers. We are trying to bring in the best of the Water Corporation, which has depth of knowledge and experience, but also the best of the private sector, which is about workforce renewal. One of the big issues across utilities is an ageing workforce. We are never going to compete with the mining companies in dollars so we need to be able to access workforce renewal in a way that we are aiming to bring people through and see working in the water industry as maybe part of a career not a lifetime career.

**Hon SALLY TALBOT:** You have an ageing workforce but also skills shortages. Do you feel you are able to pay higher wages by going into these kind of arrangements with private companies?

**Mrs Murphy:** No, not at all. We are able to access a workforce that may be part of their workforce. At different stages of people’s working lives, they want different things out of their work. They may have a stage where they want to work fly in, fly out in the remote Kimberley area or a mine site in the Kimberley. There may be another stage where they would rather work in a domestic stage around Perth where they go home at night and may earn less money. Water Corp is never going to have a business where we can roll our workforce through those multiple opportunities. Some of our partners can. The contracts that we have with our partners links them into our operating licence requirements. If they are not meeting the KPIs that we are required to meet, they are in default; it is a breach of contract and the contract can be terminated. We have a lot of teeth to make it work.



Because they are alliance contracts and we are working together, there is also a lot of scope. It is a great way to develop our staff as well.

**Hon SALLY TALBOT:** Do you need more teeth or do you have enough?

**Mrs Murphy:** We have plenty of teeth.

**Hon SALLY TALBOT:** I put it to you that the community makes a big distinction between an enterprise like Water Corp saying, “We use private contractors to fix pipes and do the mechanical and electrical maintenance” and Water Corp selling part of its operation to the private sector.

**Mrs Murphy:** We have not sold part of our operation.

**Hon SALLY TALBOT:** So you are saying that it is the first category that Water Corp is operating?

**Mrs Murphy:** Absolutely, and has done for 15 years. The only change is that we have taken multiple contracts and made them into less contracts.

**Hon SALLY TALBOT:** That was my question about the qualitative and quantitative change. You are saying there has been no qualitative change.

**Mrs Murphy:** The qualitative change is really in the treatment plant areas of bringing the operations people and the maintenance people under one shared boss so that they are working together as a team and not as two parallel streams. That is not necessarily a contractual arrangement; that is just the way we choose to structure our business.

**Hon SALLY TALBOT:** Do you have a line item for the operational costs of hiring or contracting people to do this work?

**Mrs Murphy:** We have a line item for delivering the operations and maintenance for the Perth region. The Perth region, which is run by the Perth Region Alliance, manage their workforce, some of whom are paid by Programmed and some of whom are paid by the Water Corporation.

**Hon SALLY TALBOT:** The way the Water Corp does its accounting, does it just show as, “This is our contract obligation with company A” or can you say what the cost was of hiring and contracting certain maintenance services over a financial year?

**Mrs Murphy:** I should ask the CFO. We are on SAP. We have more information on every line item than common sense might dictate! Sorry. The key point from Water Corp alliances is that the chief financial officer for every alliance we operate, be it a capital alliance or an operating alliance—we deliver a lot of our capital in these sorts of partnerships too—is a Water Corporation employee, and that is a condition of all our contracts. The person who signs the cheques is still a Water Corp person, even in the entity. However, we are working in partnership and we are trying very hard. There is no point partnering with the private sector and then saying, “You are going to do it this way and you are going to wear this outfit and do this” because there is no benefit. You are paying a margin to someone for nothing. What we want is the value add that they bring for the margin, the fact that they are working for other utilities in other countries, in other parts of Australia, the different ideas, things that work and things that do not work. We are buying that expertise by paying them a margin for the work that they are doing in partnership but we are also locking them into the obligations that Water Corp has. I honestly think it is a best of both worlds model.

**Hon SALLY TALBOT:** Do the vans that pull up to do the maintenance say “Water Corp” on them or do they say “Transfield”?

**Mrs Murphy:** They say “Water Corporation”. They may say both but they still say “Water Corporation”. We did a bit of customer work about what our customers want. It was pretty clear that our customers want to see the words “Water Corporation” there, otherwise they think we are hiding.

**Hon SALLY TALBOT:** Otherwise they think you have sold it.

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**Mrs Murphy:** If a pipe bursts in front of your house or in your back lane and someone came to fix it last year, they would not have been someone paid on my payroll. Fourteen years ago they would not have been someone paid on my payroll, and now they are not necessarily but they would still have said “Water Corporation” in all of those cases.

**Hon SALLY TALBOT:** You are saying that that amount of outsourcing or privatisation or whatever word you want to use has not changed in the last financial year?

**Mrs Murphy:** As in the number of people employed, it has not changed. In fact, it is probably slightly less because by merging the two in the Perth region, we have dropped some contractors. The mindset of partnering has probably moved further in that our people work in a much more sharing and partnering arrangement than they were before.

**Hon SALLY TALBOT:** Who do you mean by “our people”?

**Mrs Murphy:** Water Corp people.

**Mr Hughes:** Just to be clear in case you are focusing on the Transfield Degremont one, the truck that turns up outside your house to fix your water pipe is Programmed Facility Management.

**Hon SALLY TALBOT:** So that would be another contract.

**Mr Hughes:** That is the Perth region one that was combined from two into one.

**Mrs Murphy:** The Transfield Degremont one is working within our plant so the public would not see them anyway, really. I hope not. If so, that would mean something very bad had happened.

**Hon SALLY TALBOT:** Does Water Corp make a net profit?

**Mrs Murphy:** Yes.

**Hon SALLY TALBOT:** Does that go into consolidated revenue?

**Mrs Murphy:** Yes, 85 per cent of our profit goes into consolidated revenue. It is \$87 million next year.

**Mr Hughes:** We pay taxes and dividend to the state government, which is the consequence of revenue less operating expenditure.

**Hon SALLY TALBOT:** That is a beautiful handball to my colleague at the other end of the table.

**Hon KEN TRAVERS:** It is a perfect segue. I was looking at budget paper No 3 that shows your total dividend and tax contribution to government climbing from \$590 million this year out to \$1.36 billion in the forward estimates. What is the glide path for water rates to achieve that?

**Mrs Murphy:** These are based on the ERA’s previous price path. We have no idea if that is what the ERA is going to recommend. We take their price path that they have but they are doing a new piece of work now.

**Hon KEN TRAVERS:** The ERA makes a recommendation but cabinet ultimately signs off on it.

**Mrs Murphy:** Correct.

**Mr Werner:** In the budget for 2012–13 we talk about the average customer. It was 6.8 per cent. That included the 0.8 per cent for carbon.

**Mrs Murphy:** Clean energy.

**Mr Werner:** For the next three years, that is nine per cent.

**Hon KEN TRAVERS:** Nine per cent each year?

**Mr Werner:** Yes.

**Hon KEN TRAVERS:** How much of that nine per cent is to generate that additional tax and dividend and how much of it is to actually cover increases in your operating costs?

**Mrs Murphy:** We have a regulated rate of return on our assets. That is kind of set by the economic regulator. That is built into the price. The increase is to cover the costs largely.

**Mr Werner:** The pricing model that the ERA has does not have tax and dividends in it.

**Mrs Murphy:** They do not care.

**Mr Werner:** They look at our regulatory asset value and they say, “What is the rate of return and depreciation on that and what is the operating cost that you have for the business?” The model that they have models in two per cent real reduction in the operating cost per service for the operating costs and it takes the capital program —

**Hon KEN TRAVERS:** Even with a two per cent reduction in operating costs, that is still giving you a nine per cent growth year on year in your charges.

**Mr Werner:** The main driver for our price is capital. Operating is about 30 per cent of the revenue target; capital is about 70 per cent. Fifty per cent is the rate of return on our investment, 20 per cent is depreciation of the investment and 30 per cent is the operating cost of the investment. When the ERA sets the prices, the weighted average cost capital in 2009 was 6.6 per cent and they built that in. You then have a cost structure and a revenue base and a profit comes out of that on which you pay tax and dividends.

**Hon KEN TRAVERS:** What is your rate of return?

**Mrs Murphy:** On our assets?

**Hon KEN TRAVERS:** What is your rate of return on equity and what is your rate of return on assets?

**Mr Hughes:** The pricing model is based on six per cent return on assets broadly.

**The Chair:** Fifty per cent?

**Mrs Murphy:** No, six per cent. I wish! We are not an oil company.

**Mr Hughes:** Six per cent return on assets is what we typically —

**Hon KEN TRAVERS:** You have not been achieving that in recent years.

**Mr Hughes:** For a couple of reasons. One is that the pricing model does not deliver an increase in prices on the same day that you increase the capital. To use desal 2, for example, the operating cost and the capital cost of desal 2 we are currently incurring but the price impact of that is smoothed over a period of time.

On day one we take a full cost. By day number six we are starting to get a full return on that asset.

[3.45 pm]

**Hon KEN TRAVERS:** What is the driver of the dividend and tax basically doubling over the next four years?

**Mr Hughes:** The majority of it is the consequence of the increased capital program over the prior couple of few years, bearing in mind we probably spent \$3 billion over the past, I do not know, 10 or eight years replacing surface water with desal water. The consequence of that higher capital base drives, obviously, higher prices, which then generate a stronger return. The other thing to think about probably in other parts of the budget papers is the expenditure incurred by government on operating subsidies or what was called CSOs. If you consider it from a whole-of-community point of view, there are also the areas of the system that are loss making or are not generating profits, so the operating subsidies that are incurred as a result of running our business offset a lot of that dividend and tax.

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**Hon KEN TRAVERS:** Except that they do not, because this year the difference between your dividend tax and your operating subsidy is \$128 million over the forward estimates. That climbs to a \$446 million.

**Mr Hughes:** They are not growing at the same rate; that is true.

**Hon KEN TRAVERS:** Your operating subsidy goes from \$462 million to \$590 million. They are not growing anywhere near as rapidly as your dividends.

**Mr Hughes:** That is true.

**Mrs Murphy:** The metro costs are almost cost reflective. The only part of Perth that is not really cost reflective is the lag of rolling in new assets—the desal over a couple of years, so we are cost reflective. In the country we are not cost reflective but we are moving incrementally towards it every year. The other reason that goes up is that every year we are getting slightly more cost reflective in the country so the CSOs, as a percentage of revenue, drop as well.

**Hon KEN TRAVERS:** What is your estimated rate of return on assets for this year?

**Mrs Murphy:** It is in the SCI.

**Mr Hughes:** The return on asset for the 2011–12 year was forecast to be 4.3 per cent. Return on equity in the 2011–12 year was in the SCI at 5.6 per cent.

**Hon KEN TRAVERS:** For the 2012–13 year?

**Mr Hughes:** I do not have the numbers with me, but they would not be a lot different.

**Mrs Murphy:** They are pretty much the same.

**Mr Hughes:** It would take a lot to make a significant difference considering the size of the denominator.

**Hon KEN TRAVERS:** By the time you get to the fourth year of the forward estimates, will you be up around the six per cent then?

**Mr Hughes:** Probably not. I would be guessing mid to high fours.

**Hon KEN TRAVERS:** Can you take on notice what your rate of return will be for both the 2012–13 and the estimated rate of return for the 2015–15 financial years?

*[Supplementary Information No C8.]*

**Hon KEN TRAVERS:** From what I am hearing, if you continue to have a high capital investment program, because of that lag effect, you will never be able to get to your six per cent rate of return.

**Mr Hughes:** Pretty much.

**Mrs Murphy:** Pretty much. However, the whole thing is predicated too on whatever the WACC is that the ERA believes is the appropriate weighted average cost of capital for our business. If they vary that, it will vary our profitability quite a lot.

**Hon KEN TRAVERS:** I still do not see how you get that massive growth in and almost doubling of your profitability and your tax over the four years.

**Mr Hughes:** Bearing in mind that 70 per cent of the price is associated with the capital program, the capital program has been significantly higher over the last, say, three years and then forecast to continue to be so, so you are seeing quite a shift in the profile, if you like, of the balance sheet.

**Hon KEN TRAVERS:** It is still only getting it at four per cent with the lag involved.

**Mr Hughes:** Probably, yes.

**Hon KEN TRAVERS:** In theory, that \$1 billion, if you did nothing, would continue to grow to reasonably substantial amounts over the forward estimates beyond that.

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**Mrs Murphy:** If the current WACC stays the same, but I think that is highly unlikely; the whole market has moved.

**Mr Werner:** The ERA is looking at our prices at the moment. Every time it looks at our prices—every three years—it does a recalculation of the weighted average cost of capital based on the market rates that are occurring at that time. The assessment they have made in their recent decisions of the risk-free rate of return that gets built into that calculation is substantially less than it was three years ago. Our expectation now till the next price inquiry is that they will come up with a weighted average cost of capital that is lower than what was in the previous recommendations they made, so that will have an impact on our price path going forward. We have not seen —

**Hon KEN TRAVERS:** That would then lead to a lower dividend out-of-tax profit in the forward estimates.

**Mrs Murphy:** It could. If it is a lower price, it will be a lower profit, yes, so a lower dividend. We do not know what they will recommend. No-one knows. Well, they might know. It is not our vote.

**Hon KEN TRAVERS:** Interesting impact on the state budget if they do.

**Mrs Murphy:** The government does not have to do what the ERA says. That is a whole set of discussions that are well outside our orbit.

**The Chair:** Do you make a suggestion about what your weighted average cost of capital is to the ERA when you make your submission?

**Mr Werner:** In our submission to the ERA this time we said, “The way you calculate the weighted average cost to capital is stock standard approach that everyone takes all across Australia for both water utilities, power companies, private companies. They make an assessment of the parameters that apply to a water business and they come up with an assessment. We said, “If you do that the same way as did you last time, that’s fine.” We do not really have anything to add to the debate about how they go about doing it because it is a standard way. We said, “You do the calculation, tell us what you think we are and then we’ll comment back on what you’ve suggested.” If we were a private company we probably would be trying to eke out the last point, one per cent in your WACC because there is a lot of money associated with that.

**Hon KEN TRAVERS:** One per cent is a big return to shareholders. Going to page 861 where you have got the funding sources of your capital works program—the internal funds and balances listed there, where do you source those from?

**Mrs Murphy:** Customers, in simple terms.

**Hon KEN TRAVERS:** It is certainly not retained profits is it? You have retained 15 per cent, but that is probably only, this year, what, \$66 million or something?

**Mr Hughes:** We retain 10.5 per cent after tax and dividends—30 per tax, 85 per cent dividends. The other internal funds and balances and the way the depreciation works is right.

**Hon KEN TRAVERS:** With your depreciation do you put cash away for that before you determine it or do you have to borrow to fund your internal funds?

**Mr Hughes:** No. The borrowings there—take 2012–13, for example; that is new borrowings of \$570 million; the other sources of funding for us for the capital program come from the other forms of cash that are going through the system. This is a cash perspective, not an accounting perspective. The cash that comes through the system from customers, receivable, accounts payable, ends up with \$499 million, \$299 million being available for us to fund the \$1 071 000.

**Hon KEN TRAVERS:** I cannot quite understand how that works if, in terms of your profit, you are retaining only \$60 million.

**Mrs Murphy:** Revenue is about \$2 billion.

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**Mr Werner:** Effectively, the depreciation is not a cash item in our accounts, but it reduces our profit so we do not pay tax and dividends on the depreciation, but that gets retained in the business. That is available to invest back into the capital program. A big chunk of that money is the depreciation.

**Hon KEN TRAVERS:** Effectively, it is converted from an appropriation amount into a cash amount through the book keeping process.

**Mr Hughes:** Indirectly.

**Hon KEN TRAVERS:** Can you give us a breakdown of that—I am happy if you take it on notice—over those forward estimates because, again, I see that growing. I am intrigued to understand how that grows under the forward estimates period from where it is currently at \$499 million to \$575 million.

*[Supplementary Information No C9.]*

**Hon KEN TRAVERS:** That drop off in the capital works program over the forward estimates is basically predicated on your estimation of a slowdown in the increased demand for your services?

**Mrs Murphy:** It is really the completion of the big lump of southern seawater desal money going through. The groundwater replenishment, which is the next source, is not as lumpy. You do more small things as you go. If you pull the lumpiness of a couple of big projects out, it is actually fairly stable.

**Mr Hughes:** One of those lumps is Mundaring water treatment plant on page 860. Because it goes through as PPP, it shows in only one year. If you look on page 860, it is \$268.121 million in the 2013–14 year. Under the title of “Water Programs” “East Metropolitan—Mundaring Water Treatment Plant”, if you back out \$268.121 of the total on page 861 and if you back out SSDP, you will find a much smoother program.

**Hon KEN TRAVERS:** Then the following year you have east Rockingham waste water treatment coming in as well, \$168 million, so that is a big lump.

**Mr Hughes:** Sure; there are a couple of lumpy bits. SSDP, Mundaring and east Rockingham in this forward estimates period and its slight history are probably the three really chunky bits.

**Hon KEN TRAVERS:** Once east Rockingham is finished and you have completed Alkimos, what does that give us in capacity going forward before we need a big lump on Bayswater treatment?

**Mrs Murphy:** We should not need a big lump for a while. We are looking at how we can modularise east Rockingham and do the bare minimum up front and spend it as we go, and not build too much anticipation in growth. We are not too bad for quite a long time. If you look at wastewater revenue, the wastewater price customers have paid over the past 10 or 15 years, the increases every year for wastewater have been within 1.8 per cent more than CPI. Generally, they are basically CPI. Because wastewater has grown with population, it is pretty much CPI growth. Water has been where the big lumpy expenditure has been because we used to get 380 gigalitres of water in the dams and now we are lucky to get 40 in run-off terms. That has changed. We have had this huge capital injection in the water space. In the wastewater space, the capital injection has largely been keeping up with growth. It is not catching up with climate issues. It is a bit smoother.

**Hon KEN TRAVERS:** I guess my other question is: on the change from 0.2 per cent to 0.7 per cent you have your lending guarantee figure, what impact does that have through your figures? I think you have got the figure there. You are paying a fair chunk of that amount. What impact does that have on your bottom line?

**Mr Hughes:** A broad estimate, \$20 million a year, increases our op ex, or increases our interest line, so our profit has fallen as consequence.

**Hon KEN TRAVERS:** They pick it up today but they lose it in a dividend next year.

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**Mrs Murphy:** You will have to ask the Treasurer.

**Mr Hughes:** Ask Treasury to pass it through Treasury Corporation.

**Mr Werner:** From our business, the loan guarantee reduces the profit and it just flows straight through. Our budget has been increased so that we can pay. It does not appear in the pricing, so it will not impact on the pricing. But from Treasury's perspective—you can ask them—but it is a competitive neutrality thing. If you have got utilities that are getting a free kick in accessing cheap money, it is a policy decision that they want government-owned entities competing on an even footing with private entities.

**Mrs Murphy:** If someone wanted to build an asset and supply a part of the community, we do not have a financial advantage.

**Hon KEN TRAVERS:** That does not ultimately come back into any of the things such as the average weighted cost of capital; the borrowing cost of that does not get included back in there?

**Mr Werner:** ERA has already done a separate calculation of borrowing costs for what used to be PB.

**Mr Hughes:** They apply a notional rating to us, if for the pricing purposes, and a notional gearing ratio. The pricing model is based on an independently owned water corporation, if you like. The 70 points is probably a more commercial cost of funds for an entity like ours.

[4.00 pm]

**Hon KEN TRAVERS:** So they would have already factored in —

**Mr Hughes:** Something like that. Not literally, no.

**Hon KEN TRAVERS:** — or something around that amount into the one in which they have calculated all your cost structures. That would have already have been calculated here.

**Mr Hughes:** For the purposes of the weighted average cost of capital.

**Mr Werner:** So that decision will not affect the prices.

**Mrs Murphy:** The price is not based on what we actually pay. It is based on the notional.

**Hon KEN TRAVERS:** So on that basis, it just cleans it up and probably gets them \$36 million this year rather than the \$80 million they would have got through dividends.

**Mrs Murphy:** No. They lose 85 per cent of that.

**Hon KEN TRAVERS:** Get some extra money this year and then less money next year as it flows into dividends.

**Mr Werner:** No, it just makes 10 per cent difference. It is really very —

**Hon KEN TRAVERS:** If you are the Treasury and you needed cash this year, now is the year to have done it because it gives them a bit of a cash bonus this year.

**Mrs Murphy:** We just do what we are told.

**Hon KEN TRAVERS:** No, I understand that.

**The Chair:** But if it is that you are doing what your customers want, which is lower prices —

**Mrs Murphy:** It does not affect prices.

**The Chair:** No, not that particular part but your structure seems to me to be just the normal typical corporate structure, which is how most people think; they do not go beyond that. Whereas a cooperative where you have got your users and your contributors of money, being the government, being one and the same people just about, cooperatives structures seem to be much more relevant. We have raised that with the ERA and they were not too sure which way to go on it either, but from

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your perspective it would be intriguing to me to actually consider the two structures. It would mean that there would not be any dividends being paid to government.

**Mrs Murphy:** Correct.

**The Chair:** And your average weighted cost of capital might rise marginally—it does not with CBH, which is the best example—and you would be giving cheaper prices to your customers.

**Mrs Murphy:** At the end of the day, I cannot speak for the ERA or the government, but I am assuming it is do with the ability of the private sector to compete.

**The Chair:** The private sector can compete in whichever model they chose to complete with, just the same as CBH. So, CBH has chosen to have a structure that suits their constituency, if you like, which is a similar model to what you could do if you considered it.

**Hon KEN TRAVERS:** The five per cent efficiency dividend and the efficiency dividend going forward, which is I think \$17 million this year and then \$28 million, how did you achieve the five per cent and how are you intending to achieve the dividend going forward?

**Mrs Murphy:** Two per cent of the five per cent was deemed to be the ERA's two per cent. So, we were asked to deliver a further three last year.

**Hon KEN TRAVERS:** Two per cent was already factored into your budget effectively.

**Mrs Murphy:** Yes. There are a few things. We have certainly done a major piece of efficiency work, including the way we are doing our outsource alliances and we are also doing a big piece of work across our country regions. We have done a lot of standardisation across the way we operate our country regions. Historically, each of our regions was operated quite differently and there was a perception that they would compete, but what we found was that has not necessarily delivered a business that makes sense holistically across the state. So, now we have done a big piece of work to line up the structures within each of the country regions, the job descriptions and the way the different regions work so that people can actually move from region to region quite easily. That has delivered some savings and we are hoping to deliver some more going forward. We have also had a bit of luck.

**Hon KEN TRAVERS:** Does that alter staffing levels in country areas?

**Mrs Murphy:** No, it does not alter staffing levels in country areas, but it affects some of the support services to them. So, it might change the number of HR people you need in Perth to run the regions. We are not making anyone redundant or anything like that, but as we move on it is possible that we do not replace things. So, I can see no scenario where we ever have less people with spanners; the physical work has to be done. For us, it is about how you organise the work to minimise the overhead costs that you have got to put on the people with the spanners and making sure the trained people with the spanners are being used to do that work, not other work. So, you do not want those people doing other tasks that somebody who does not have those skills could do. It is more about lining up and kind of removing internal red tape, which happens in big organisations; it is a perpetual kind of war to make it go away. So, we have done quite a bit in that space and we believe there is more to go. We have also had a good year. Last summer was not too bad, the summer we have just gone through. We did not have as much carting as we had forecast. So, we have slightly over-delivered on our efficiency dividend, partly through skill and always there is an element of luck in these matters too.

**Hon KEN TRAVERS:** Have you identified how you are going to achieve this going forward?

**Mrs Murphy:** We have identified how we are going to achieve some of it and we are still working on some of it. The year we are starting, this year, we are pretty comfortable that we can do that.

**Mr Hughes:** Which is pretty much through a continuation of the areas that Sue mentioned. The integrated alliances, which we have talked about before, we are confident can deliver some savings

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over and above the two per cent ERA target and the work in the regional areas and various other reviews of really our shared services units.

**Mrs Murphy:** In the meantime, we are looking at some things to do in the way we structure our interest and how we do some of our borrowings. We have got a few other projects bubbling along that we think can deliver some savings for the future.

**The Chair:** We will close there. I must say that I sense much less anxiety amongst you from the hearing that we had May last year just after the budget had been released and it was after a very dry year. I sense that things are moving forward.

**Mrs Murphy:** Indeed.

**The Chair:** If there are any additional questions that the committee has, they will be asked of you via the minister in writing in the next a couple of days together with the transcript of evidence, which includes the questions you have taken on notice. If we have any unasked questions—we have just a couple of us here now— we will submit to these via the committee clerk. Responses to the questions that we ask will be requested within 10 working days of receipt, as is normal. Should you be unable to meet this due date, please advise the committee as soon as possible before the due date. We are getting quite finicky on this particular aspect. The advice is to include specific reasons as to why the due date cannot be met.

On behalf of the committee, thank you very much for your attendance this afternoon.

**Hearing concluded at 4.06 pm**

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