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Ref: D2011/030357

5 August 2011

Mr James Cox
Chief Executive Officer and Full Time Member
Independent Pricing and Regulatory Tribunal of NSW
PO Box Q290
QUEEN VICTORIA BUILDING NSW 1230

Dear Mr Cox

Sydney Desalination Plant Pty Limited Price Determination 2011

I am writing to you, as the Managing Director of Sydney Water has indicated to me that one of the points that the SCA made in its recent submission to the above Review may have been misinterpreted.

In our comments on the Weighted Average Cost of Capital (Pg 3) we pointed out that SDP Ltd faces low business specific risk.

This comment should be seen within the correct context. SDP Ltd propose a WACC of 7.8% based on "Both market and business specific risks" (SDP Ltd Submission Pg. 20). Business specific risks refer to those risks that are within the control of management. Market risks, on the other hand, occur as a result of market movements beyond the control of management. It is market risk that is priced within the WACC formula through the Beta parameter, not business specific risk.

Issue is not taken with SDP Ltd's proposal of a WACC of 7.8%. The letter accompanying our submission stresses the importance of competitive neutrality in setting prices for SDP Ltd. We would expect that any WACC set for SCA for the upcoming price determination, therefore would similarly take account of market risk, given both the SDP and SCA share similar risks. Consistent with this argument, the SCA will be proposing a WACC that is higher than the current 6.5% in our upcoming price determination.

If IPART requires any further clarification of this issue, please contact Ed Chan on 02 4724 2487.

Yours sincerely

A handwritten signature in black ink, appearing to read "Michael Bullen", written over a horizontal line.

Michael Bullen
Chief Executive