

# WB3 Project

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Mr. E J Hall  
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Dear Mr. Hall

## **WATER BUSINESS THREE FEEDBACK TO SEQ INTERIM PRICE MONITORING- INFORMATION REQUIREMENTS 2010/11**

Thank you for the opportunity to provide comment to the Queensland Competition Authority's (the Authority) SEQ Interim Price Monitoring Information Requirements for 2010/11- Draft Report.

The following are the aggregated comments on the paper from the three Councils of Water Business Three (WB3): Gold Coast, Logan and Redland.

Attached are specific comments are related predominantly to Section 4: Detailed Information Requirements and Appendix E: Information requirements Also provided is the edited document, for Appendix E: Information Requirements with comments and amendments provided therein where relevant.

### **General Comments**

As a general comment, it appears that the Authority will have wide ranging powers to analyse and audit our business as required. The process identified appears to be more than price monitoring and will involve additional costs and resources to meet the requirements. In particular the review of capital expenditure will create uncertainty in business planning and delay the commencement of projects as a result of another layer of approval being added before projects can commence.

From an accounting point of view there will be chart, ledger and system adjustments required with processes and quality systems to be put in place. Additional costs will be incurred in establishing the framework and undertaking the required recording. In addition a regulatory section will be required to be set up in WB3 to manage the process. .

The initial setup will be required at a time when WB3 is establishing the business to start from 1 July 2010 which will put further strain on existing resources.

There is still no clarity on when certain items to be reported will be progressively rolled out. WB3 requires more certainty so it can develop its budgets, structures, and policies for 2010-11 and incorporate these requirements in its financial management system.

WB3 recommends that the Authority develop a methodology to ensure consistency in the allocation of costs into various areas. However WB3 should also be provided with the option of applying its own methodology if it is considered a more realistic indicator of the cost of providing the service. This could perhaps be addressed in the development of the information collection templates. This is to resolve some issues, that have already been identified in discussions, around how to allocate costs from wastewater, such as trade waste.

WB3 will provide its best estimates with regards to pricing policies going forward based on current arrangements in each of its districts. However WB3 may decide to make substantial changes to its pricing policies and tariff structures once established, including convergence of pricing between the three districts. This could cause differences in future reporting periods. WB3 therefore envisages problems developing as tariff structure changes will make comparison of actuals and forecasts difficult and potentially meaningless (Appendix E: Section 5.2.1 (d) & (e)).

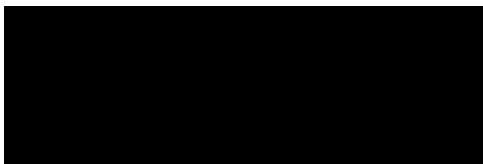
WB3 believes there will be issues around comparing historical data and forecast data. With the information requirements, and the disaggregation required, progressively increasing over the interim period, WB3 is concerned that there will not be like-for-like comparison of some of the information (e.g. may not be in a position to disaggregate historical information), and that this could produce information that is either misleading or not meaningful.

The Draft Report refers to the end of interim arrangements being on 30 June 2013. In the previous submission, it was stated that it is unlikely that a robust ERP system with suitable processes and quality systems can be introduced in the required timeframe at a time when the business is being built. As a result, it will be necessary to use a temporary suite of systems with the permanent solution being introduced at a later date. This will result in additional costs on the business.

Finally, it is not considered reasonable for a Director's sign off that the regulatory accounts which include forecasts and interim financial results are presented as true and fair.

Please contact Sandro Marin, WB3 Project Manager- Finance, Asset Transfers & Corporate Services on 3412 4423 should you require further information.

Yours faithfully



Mark Harvey  
**Chair- WB3 Joint Management Committee**  
*For the Chief Executive Officer's of  
Gold Coast Logan and Redland City Council's*

## **WATER BUSINESS THREE**

### **Specific Comments on Detailed Information Requirements and Appendix E: Information Requirements**

#### **Page 32- Section 3.7**

*The Authority recommends that it report any instance where revenues significantly exceed, or are considered likely to significantly exceed the MAR for sustained period.*

Could clarification be given on what is what constitutes "significantly exceed" and a "sustained period"? Also, if MAR is being calculated on an activity basis ie water and wastewater, will it be deemed significant if for example one product is above for a "sustained period" by MAR, however overall the MAR has not been exceeded? What if one geographic location is above MAR for a product and the other locations are below MAR with the average being below MAR?

#### **Page 35- Section 3.8 (b) & Appendix E (3.4, 5.11-5.14 & Attachment 1)**

*For 2010/11, the relevant items of revenue, capital and cost expenditure should be disaggregated by each entity according to the following deemed categories:*

- a. activity (each of water and wastewater); and*
- b. geography (for each of the 10 amalgamated council boundaries, and by system (catchment) where available); and*
- c. and further, by:*
  - o core service...*
  - o non-core services in aggregate...*
  - o non-regulated services in aggregate*

(i) The Authority requires the entities to establish their information systems by 1 July 2010 to enable disaggregation of costs necessary to provide timely and transparent information to customers on the costs and other factors underlying each price. The Authority has not adequately considered the advice of the Synergies report dealing with legacy issues. To effectively do this will mean restructuring of ledger and reallocation of costs. This will need to be undertaken for the Budget 2010/11 which we are in the process of preparing. This will involve possible changes to the Chart of Accounts, processes and reporting at a time when we are preparing to commence operation of the new entity on 1 July 2010. .

Disaggregation will be particularly difficult for services with multiple prices such as Trade Waste which has up to three different categories of pricing. The provision of separate costing for these categories will not be any easy task. This will also apply to residential and non residential water prices in some areas. This disaggregation would largely be achieved through cost allocation which may be difficult to substantiate using subjective allocation methods.

Entities should be provided with a robust allocation framework from which to differentiate such costs in a consistent manner.

(ii) It is stated that in the initial year geographic costing will be provided. It mentions that over the balance of the price monitoring period that information systems focus on systems (catchments). WB3 will be costing by geographic area initially ie Gold Coast, Logan and Redland, however, costing by catchment is not currently undertaken. Considering the large number of catchments, this will result in additional complexity, particularly in labour costing, as well as an increased cost to provide the information. In addition, a large amount of cost allocation will be required resulting in difficulties in substantiating costs within each catchment. Costing by catchment may not be applicable if a geographic location price or a combined area WB3 price is used. In addition there is a significant cost driver associated with the water grid and delivering a greater level of security

of supply which benefits all users which is better reflected in a total water area costing rather than a dissection by catchment.

iii) As discussed above, disaggregation of the costing of some core services e.g. trade waste, would be difficult, and would require the use of arbitrary allocations.

**Page 37- Section 3.9**

*a) Should a final price monitoring report find that an entity's revenues significantly exceed or are considered likely to significantly exceed, the MAR for a sustained period...*

As raised for page 32, could please provide clarification on what is considered significant and sustained?

**Page 38- Section 3.10**

*(b) The entities provide any information relating to price and revenues that may be reasonably required by the Authority.*

Could clarification please be given on what constitutes information 'reasonably required'?

**Page 41- Section 4.2 & Appendix E( 3.4, 5.11 and Attachment 1)**

*The Authority recommends that for 2010/11, the new entities be required to provide details, for each deemed category of:*

- a. actual revenues for each year from 1 July 2008 to 30 June 2010 (The Authority also invites comment on the most appropriate degree of disaggregation, consistent with the proposed categories, considered feasible by the entities)*

The degree of disaggregation on prior year information could be an issue depending on the deemed categories agreed to. This is largely because of the need to undertake cost allocations in prior periods. It may be difficult to historically "back-apply" disaggregation, especially if new allocation categories are used for future revenues. Access to historical information from council systems may also cause difficulties.

**Page 43- Section 4.3 & Appendix E (5.3)**

*b) The Authority and relevant agencies work together to establish an integrated performance monitoring framework (incorporating standards of service) relevant to the new entities.*

The Authority will be relying on information provided by entities under the National Performance Reporting (NPR) framework through the SWIM database until the service standards and integrated performance framework is completed. There are some items in the SWIM / NPR framework that some districts that are currently not able to be reported on.

The main issue is that not all of the indicators are reported as adequate systems are not in place to provide an indicator which would pass audit. Will it be necessary to improve processes and introduce systems so WB3 can report on all indicators?

It is likely that each district will have separate information using different systems. It may be difficult to consolidate these together particularly as each geographic location uses different processes and assumptions. It should be noted that an audit of indicators is required every three years. The next audit is at the end of the June 2010 financial year. Issues are anticipated in Logan's case in the 2010 audit due to the inclusion of areas under the council amalgamations.

On the financial side, WB3 could probably achieve gradual increase in the reporting arrangements. However, from the asset, environmental, and customer information perspective, this is not something that all of WB3 will be in a position to report on until an ERP is in place in some years.

It is therefore considered that for 2010-11 reporting on specific indicators will need to be similar to current arrangements of each district. Reporting on the indicators not provided can be introduced over time as required systems are introduced.

**Page 45- Section 4.4 & Appendix E (5.4 c)**

*4.4 c) Demand forecasts used to substantiate proposed capital expenditure, to the extent that it differs from (b) above and corresponding non-revenue water and bulk water purchases*

There may be difficulty in providing some linkages between demand forecasts and capital expenditure, as not all capital expenditure is demand / growth related.

**Page 47- Section 4.5 & Appendix E (5.5.1)**

*Details of the initial RAB value allocation must be provided by individual assets or groups of assets of common type and function to which an existing useful life has been attached and audited.*

WB3 may not be capable to allocate at asset value level and prefer allocation at the group level at individual assets.

**Page 48- Section 4.6 & Appendix E (2.2, 3.4.4 & 8)**

*A generic template and model may provide further assistance with the technical calculations that are typically involved in rolling forward a RAB. It is proposed to prepare such a template once the Government has made a decision on the interim price monitoring framework.*

WB3 supports the use of a template that will provide consistency across the entities. WB3 requests that it be consulted in its development, with adequate time frames for comments.

**Page 51 Section 4.7**

*a) the expert report to be released for comment separately or as part of a draft price monitoring report*

This states that the Capital Expenditure review will be released for comment with the price monitoring report. This process may delay the installation of infrastructure and cause unnecessary red tape for the operation of the water business. It is assumed there will be adequate processes in place for assessing projects ending in the final sign off by the Board of the new water entities. Shouldn't the review by the QCA therefore be more high level?

**Page 53 Section 4.7 & Appendix (5.6.3)**

*The Authority recommends the following criteria and process for assessing capital expenditure for inclusion in the regulatory asset base:*

*a) only prudent (needed) and efficient (cost-effective) forecasts capital expenditure be included in the regulatory asset base for the purposes of calculating the maximum allowable revenue*

*b) the process for assessing capital expenditure should involve independent review and open consultation. The independent expert should assess the prudence and efficiency of capital expenditure having regard to the entities' policies and procedures and a sample of projects. The expert should identify the value of any expenditure that is not efficient and prudent.*

It is considered that there will be practical risks for the business having the regulator or an independent reviewer determining what is efficient and should be approved. It seems to be quite 'heavy handed' for a price monitoring review, and its timings will make it quite difficult on the business and may create business planning uncertainty and cause delays in the installation of infrastructure.

Also:

- o WB3 is concerned that some capital expenditure that is to be constructed, and has already been approved or under contract, may have to go through this review with no ability to change the projects.
- o Gold Coast has recently had its Priority Infrastructure Plan (PIP) approved. Would this satisfy as having an independent review?
- o As previously discussed, Capital Expenditure is grouped by wastewater- there is no differentiation for trade waste assets.

#### **Page 55 Section 4.8**

*The Authority understands that the entities are to receive all capital contributions previously paid to councils.*

Note this should be the case after 1 July 2010 but is likely that unspent contributions will be held by councils and not passed over to the water businesses

Also what is the level of detail required by QCA in regard to contributed donated assets i.e. asset number, description, asset value and so forth? As discussed at the workshop on 8 December 2009, the need for this level of information is difficult to justify particularly given the effort and costs involved.

#### **Page 56 Section 4.8 & Appendix E 5.6 & 5.7**

*The Authority recommends that a review of the appropriate basis for treating capital contribution and contributed, donated and gifted assets be undertaken as part of the current remit...*

These comments have been included, however may not be relevant if the above recommendation no longer applies. WB3 understands that a process of new capital contributions are treated has been agreed between the State Government and councils and as such should not be reinstated.

What level of detail will be required on capital revenues / contributions? WB3's view is that actual developer charges (and estimates) be aggregated.

Also, what useful lives / depreciation rate will be applied from 1 July 2010 i.e. current rate or agreed rate across WB3? The RAB value will need to be finalised so we can set up new asset register.

*d) Capital contributions (cash and infrastructure charges) received in respect of approvals under the Integrated Planning Act 1997 and details of related assets for each year from 1 July 2008 to 30 June 2010;*

*e) Capital contributions (cash and infrastructure charges) received in respect of approvals under the Integrated Planning Act 1997 and details of related assets for each year from 1 July 2010 to 30 June 2013*

Could clarification please be given on what is actually required under these information requirements. If this WB3 implies that a register of assets that specific infrastructure charges are related to is required, then this would be quite a difficult and arduous exercise.

**Page 58 Section 4.9 & Appendix E 5.8**

*Details of depreciation of RAB values and capital expenditure for the period 1 July 2008 to 30 June 2010 on the physical assets calculated using existing useful lives attaching to individual assets from 1 July 2008.*

Clarification is required on point in time of useful lives to use. Can WB3 use current useful lives? Or do we have to use what they were as at 1 July 2008? 1 July 2008 probably shouldn't be used due to the effects of reform on the districts of WB3, particularly Logan.

**Page 64 Section 4.12 & Appendix E 5.11**

*While the direction refers to these as capital costs, the Authority notes that, for consistency, any allowable establishment costs that were clearly of an operating nature should be included in the MAR as operating costs..*

Is there a divergence of views between the Direction and the Authority in including establishment costs as part of Operating costs for calculation of MAR? Aren't establishment costs treated as part of the regulatory asset base?

**Page 65 Section 4.13 & Appendix E (1.4)**

WB3 considers that 1 July 2010 is considered a tight timeframe for the provision of actuals, especially with the amount of work required in transitioning the new entity. The Authority needs to acknowledge that if 1 July 2010 remains as the date, then this would largely be draft / budget information and will contain many assumptions and caveats on the data. Audited information would not be available until around October / November 2010.

Actual information could not be provided at 1 July as year end processing of source data as well as accruals would be undertaken during July. If required, unaudited information could be provided in August.