



Looking after water, looking after you

Response to Interim Price Monitoring Information Requirement

**Water and Sewerage Treatment, Distribution
and Retail Activities**

August 2010

Unitywater Interim Price Monitoring Response

Contents

| | | |
|-----------|---|----|
| Section 1 | Executive Summary..... | 6 |
| 1.1 | Emerging capabilities..... | 6 |
| 1.2 | Progress to beyond the interim price monitoring period..... | 7 |
| 1.3 | Information constraints..... | 8 |
| 1.4 | Statutory accounts and budget..... | 9 |
| 1.5 | Revenue..... | 9 |
| 1.6 | Service standards..... | 10 |
| 1.7 | Demand forecasts..... | 10 |
| 1.8 | Regulatory asset base (RAB)..... | 11 |
| 1.9 | Capital expenditure..... | 12 |
| 1.10 | Contributed, donated and gifted assets..... | 13 |
| 1.11 | Depreciation..... | 14 |
| 1.12 | Indexation..... | 15 |
| 1.13 | Return on capital..... | 16 |
| 1.14 | Operating costs..... | 16 |
| 1.16 | Non-regulated services..... | 19 |
| 1.17 | Tax useful lives and asset values..... | 20 |
| 1.18 | Conclusion..... | 20 |
| Section 2 | Introduction..... | 21 |
| 2.1 | Unitywater..... | 21 |
| 2.2 | Characteristics of the area served..... | 22 |
| 2.3 | Emerging and developing capabilities..... | 23 |
| 2.4 | Progress to beyond the interim price monitoring period..... | 24 |
| 2.5 | Information constraints..... | 27 |
| Section 3 | Principles and assumptions..... | 28 |
| 3.1 | Principles..... | 28 |
| 3.2 | Budget assumptions..... | 29 |
| Section 4 | Statutory accounts and budget..... | 32 |
| 4.1 | Summary of Statement of Profit and Loss..... | 33 |

| | | |
|-----------|--|----|
| 4.2 | Summary of Balance Sheet..... | 33 |
| 4.3 | Summary of Cash flow..... | 33 |
| 4.4 | Regulatory Adjustments..... | 34 |
| 4.5 | Accounting Principles and Policies..... | 35 |
| Section 5 | Revenue..... | 35 |
| 5.1 | Pricing Policy | 35 |
| 5.2 | Revenue for each of the Services | 36 |
| 5.3 | Classification by Customer Groups..... | 37 |
| 5.4 | Tariff Structure..... | 38 |
| 5.5 | Forecast Revenue versus MAR | 38 |
| Section 6 | Service standards | 39 |
| 6.1 | Definitional issues..... | 39 |
| 6.2 | Past service standards as approved by other agencies..... | 40 |
| 6.2.1 | Service Standards for Sunshine Coast Regional Council | 40 |
| 6.2.2 | Service Standards for Moreton Bay Regional Council area..... | 41 |
| 6.3 | Service standards 1 July 2010 to 30 June 2013..... | 42 |
| 6.4 | Changes to service standards..... | 44 |
| Section 7 | Demand..... | 47 |
| 7.1 | Water demand..... | 47 |
| 7.2 | Demand for sewerage services..... | 49 |
| 7.3 | Demand Forecasting for Capital Planning | 50 |
| Section 8 | Regulatory asset base | 51 |
| 8.1 | General approach | 52 |
| 8.2 | RAB Information Gaps..... | 52 |
| 8.3 | Initial RAB 1 July 2008..... | 54 |
| 8.4 | RAB roll-forward 1 July 2010..... | 54 |
| 8.5 | RAB roll-forward 30 June 2013..... | 55 |
| Section 9 | Capital Expenditure..... | 56 |
| 9.1 | Council capital expenditure | 57 |
| 9.2 | Forecast capital expenditure..... | 57 |
| 9.3 | Method of determining capital programs | 63 |
| 9.3.1 | Growth | 63 |
| 9.3.2 | Renewals | 65 |
| 9.3.3 | Improvements..... | 66 |

| | | |
|------------|---|----|
| 9.3.2 | Compliance..... | 66 |
| 9.4 | Capital planning process and prioritisation..... | 67 |
| 9.4.1 | Capital Prioritisation Model..... | 67 |
| 9.4.2 | Expenditure approval processes..... | 67 |
| Section 10 | Contributed, donated and gifted assets..... | 68 |
| 10.1 | Overview..... | 68 |
| 10.2 | Receipts for each service for each region..... | 69 |
| 10.3 | Adjustments for actual receipts..... | 69 |
| 10.4 | Change to asset offset method..... | 70 |
| Section 11 | Depreciation..... | 70 |
| Section 12 | Indexation..... | 72 |
| Section 13 | Return on Capital..... | 73 |
| Section 14 | Operating costs..... | 74 |
| 14.1 | Operating costs by region..... | 75 |
| 14.2 | Cost characteristics..... | 78 |
| 14.3 | Cost collection and forecasting..... | 80 |
| 14.4 | Cost allocation..... | 81 |
| 14.5 | Changes in operating costs by service and category..... | 82 |
| 14.5.2 | Historic costs..... | 82 |
| 14.5.2 | Anticipated changes..... | 82 |
| 14.6 | Changes in distribution operating costs..... | 84 |
| 14.6.1 | Overview of distribution operating costs..... | 84 |
| 14.6.2 | Explanation of distribution operating cost variances..... | 85 |
| 14.7 | Changes in retail operating costs..... | 85 |
| 14.7.2 | Reporting of Retail Operating Costs..... | 87 |
| 14.7 | Changes in corporate costs..... | 88 |
| 14.9 | Establishment costs..... | 89 |
| Section 15 | Non-regulated services..... | 89 |
| 15.1 | Moreton Bay..... | 90 |
| 15.2 | Sunshine Coast..... | 90 |
| 15.3 | Financial details..... | 90 |
| Section 16 | Tax Useful Lives and Asset Values..... | 91 |
| Section 17 | Conclusion..... | 91 |

Section 1 Executive Summary

Unitywater is a statutory authority responsible for the delivery of water supply and sewerage services to customers in the Moreton Bay and Sunshine Coast regional area.

Unitywater was established by the Queensland Government as part of its reform of water supply arrangements in South East Queensland. The reform process included divesting Moreton Bay Regional Council and Sunshine Coast Regional Council of their water distribution and sewerage assets and transferring these to Unitywater on 1 July 2010.

The reforms are aimed at providing better outcomes for customers, and include the delivery of:

- Improved water supply co-ordination and management;
- More efficient water supply and sewerage services; and
- Improved management of the associated infrastructure.

Within its geographical area, Unitywater:

- Provides customers with drinking-quality water;
- Collects, treats and disposes of sewage;
- Treats, recycles and supplies water to industry;
- Operates and maintains the infrastructure in a water and sewerage system;
- Plans and delivers new infrastructure to enhance the system;
- Serves customers and levies a charge for its services.

An independent Board has been appointed to decide the strategies for Unitywater and to ensure that the functions of the organisation are delivered. The former owners of the Unitywater assets are entitled to participate in the returns delivered from the efficient operation of the business, which in turn contributes to the quality and availability of social infrastructure within the region.

The area serviced by Unitywater spans more than 5,000 square kilometres with an estimated residential population of 670,000, which represents approximately 21% of Queensland's total population.

This report is Unitywater's first interim price monitoring information return to the Queensland Competition Authority (the Authority).

The information templates provided by the Authority have been populated and have been provided separately to this document.

1.1 Emerging capabilities

Unitywater assumed ownership of its assets on 1 July, 2010. This was preceded by a short, yet intense, period of preparation to take on these new responsibilities, with the entity formally created in November 2009. The creation of Unitywater as a standalone, commercial business presents significant opportunities to adopt new management practices, explore innovation and customise business processes and systems to improve operational performance. While these are longer-term aspirations, the immediate focus is to establish the business, which is in its first year of operations, maintain continuity of service to customers and implement systems and processes that position Unitywater to be able to respond to its regulatory environment. Unitywater must also address legacy issues associated with inherited assets, tariff structures and prices, resources, systems and processes and supplier contracts from the previous Council owners.

This fact is necessary to take into account when assessing the information available from Unitywater. In addition, it is also important to assess the information in light of the infancy of the organisation in that many systems and processes that would be typical of an established business are under development. This was recognised by the Authority's Ministers, in explaining the background to their Direction to the Authority:¹

Over the interim regulatory period, the Ministerial Direction clearly indicates that the QCA should recognise the emerging and developing capabilities of the new entities. With multiple water and wastewater businesses merging into single organisational units, the capacity of the new entities to provide comprehensive regulatory information will be limited, particularly for 2010-11. Moreover, organisation-wide systems and processes will take time to become established.

This early status of development also has implications for pricing and this information return. For example, it is difficult to establish a maximum allowable revenue (MAR) with the precision that normally occurs for a mature regulated business. Furthermore, many factors that influence the opening regulatory asset base (RAB) are yet to be finalised.

Unitywater is in the process of finalising its systems and the resources required to operate the business, including new retail and corporate capabilities. At the same time, the resourcing of the business has needed to occur within the requirements of the operational constraints imposed by the SEQ Urban Water Arrangements Reform Workforce Framework, 2010.

1.2 Progress to beyond the interim price monitoring period

Despite only recently having taken ownership of the assets, Unitywater has achieved much already in preparing itself for the regulatory environment beyond FY2013, including:

- Reducing its reliance upon Council systems and resources, to the point where it is expected that independent resourcing will be achieved, by and large, for FY2012. Already, Unitywater has implemented its own finance and payroll systems;
- Structuring its financial accounts to align with the Authority's data requirements under the interim price monitoring regime;
- Implementing governance processes around the capital expenditure program, including a dedicated sub-committee of the Board to review expenditure and approve variations;
- Developing internal performance indicators and systems of measurement;
- Developed detailed cost allocation methodologies; and
- Identified a pathway to finalise its RAB value, based on final, audited information from Councils.

It is also important to note that the Unitywater Board has only recently appointed, and the strategy for the business is still being developed. The strategy-setting activities of the Board will influence the future direction of Unitywater, including the resourcing arrangements for the business, prioritisation of activities, asset management and development of its capital expenditure program and delivery of that program into the future. The Board also recognises that the strategy for the business must be complementary to its regulatory environment. Indeed its future revenues will be dependent upon the effectiveness of its regulatory strategy and ability to respond to the current and future regulatory regimes.

¹ Letter from the Authority's Ministers to Mr Brian Parmenter, 2 July 2010.

1.3 Information constraints

The price monitoring framework is information intensive and, for the current year, relies heavily upon information obtained from the previous Councils for FY2009 and FY2010. Unitywater has sought to obtain as much of this information as possible from Councils. Where data was not available from Councils directly, Unitywater has sought the reasons why this was not available.² In some cases, Unitywater has sourced information from the Enterprise Financial Model developed by the Council of Mayors (SEQ) water reform program using Council-provided data, on the basis that this was the best information available at the time of lodging this information return. This model was audited by external agencies for data integrity and data quality.

The details of the information constraints and data limitations are set out throughout this information return. In general, these relate to:

- An absence of some statutory account information, particularly for balance sheet or cash flow statements as these were not prepared discretely for the Councils' water and sewerage business;
- The accounting treatment and level of cost disaggregation for amalgamating Councils has shown to be disparate, particularly for FY2009. This is partly attributable to different classifications of Water and Sewerage Businesses under full cost pricing principles. Generally for those Councils where the Water and Sewerage Businesses met the threshold criteria for a type 2 business (Local Government Act requirement), separate accounts existed for revenue, operating costs and capital projects. For those Councils which did not need to report Water and Sewerage as a Business Activity, minimal separate information was collated;
- Historic water demand data, particularly for FY2009; and
- Details for the FY2010 year which are generally based on estimates (using Councils' third quarter forecasts) as final year-end data was not available to Unitywater. However, the forecast year-end position could differ substantially from the actual position, once finalised.

Furthermore, Unitywater has not been able to certify the information provided from Councils, but has instead relied on the audited results (where available) used for external reporting. Unitywater has also relied upon the accuracy and completeness of the data in the Enterprise Financial Model for FY2009, and the Councils in relation to the accuracy and completeness of the forecasts for FY2010.

It is important to note that this has implications for the calculation of the opening RAB, as the final RAB cannot be ascertained until further, final and audited information is available from Councils. The opening RAB presented in this information return is therefore an interim amount.

For the price monitoring period (FY2011 to FY2013) detailed budget information by cost code and natural account was used to populate information for these forecast years. It should be noted that Unitywater's forecasts are based on its best estimates, given current information. These forecasts are likely to change as Unitywater gathers more information and becomes more familiar with its operating environment and assets.

² Refer letters dated 12 August, 2010 from Unitywater to each Council. These letters can be made available to the Authority or its consultants upon request.

1.4 Statutory accounts and budget

Unitywater has provided forecasts of its statutory accounts (balance sheet, profit and loss and cash flow statement) that align with its budget and forward projections. These are set out in the completed templates.

Moreton Bay Regional Council, Sunshine Coast Regional Council and the previous six new amalgamating Councils did not keep separate full financial statements for their water businesses. Consequently, Unitywater is unable to provide statutory balance sheets and cash flow statements for FY2009 and FY2010. A letter has been sent to the participating Councils to confirm that they are unable to supply this information. A profit and loss statement has been compiled from available data by Unitywater staff for this period, and is provided in the completed templates.

1.5 Revenue

The current year is Unitywater's first year of setting prices. In doing so, Unitywater has inherited existing tariff structures and price levels from Councils. Furthermore, Unitywater was required to set prices based on limited historic information about its anticipated MAR, and amidst uncertainty about key parameters such as the opening RAB. This knowledge has grown since prices were originally modelled in March 2010, as the organisation has developed and refined its cost projections. The estimated MAR for this information return is some \$48M above the forecast revenue for FY2011. Unitywater has chosen to limit price increases to those originally calculated, rather than increase prices further to recover the full (anticipated) MAR. The final MAR will be subject to refinement for FY2011 given the opening RAB is indicative and is to be finalised during the year.

Unitywater intends to smooth prices in subsequent years (from FY2012 onwards) so that MAR is achieved over a defined period, on a NPV neutral basis. In determining the level of under-recovery for FY2011, Unitywater will adjust for the final RAB, actual revenues received and actual capital contributions received.

The period of the price smoothing will be determined once the MAR parameters are finalised, including the opening RAB. The three year revenue forecast presented in this information return is not based on an NPV neutral glide path, and is indicative only. Unitywater has little control on water demands given the institutional settings for the SEQ Water Grid. Furthermore, demand is difficult to predict in the current environment where permanent water conservation measures are being applied for the first time, amidst a growing population. Consequently, Unitywater proposes to adopt a revenue cap approach to pricing and adjust prices in subsequent years to account for variations between actual and forecast demand. This approach is to apply for the current year, and will be reviewed for FY2012 onwards.

Unitywater's pricing policy in relation to tariff reform is to limit any changes where possible until such time as the Authority has published pricing principles, as has been foreshadowed. In terms of contributed, donated and gifted assets, Unitywater has retained the revenue offset approach. Unitywater will review this approach in the future. The following table indicates the estimated historic and forecast revenue for each service in each region. Historic information is based on the best data available to Unitywater.

Moreton Bay revenue by service

| Services | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|----------|--------|--------|--------|--------|--------|
|----------|--------|--------|--------|--------|--------|

| | | | | | |
|------------------------------|---------------|---------------|---------------|---------------|---------------|
| Drinking Water | \$65m | \$69m | \$93m | \$106m | \$121m |
| Other Core Water | \$7m | \$6m | \$8m | \$8m | \$9m |
| Sewage via Sewer | \$63m | \$79m | \$107m | \$133m | \$144m |
| Trade Waste | \$1.4m | \$1.2m | \$1.7m | \$1.7m | \$1.8m |
| Other Core Sewage | \$2m | | | | |
| Non Regulated | \$5.3m | \$2.8m | \$3.7m | \$3.9m | \$4.1m |
| Revenue from Services | \$145m | \$158m | \$213m | \$252m | \$280m |

Other Core Water Services includes the provision of recycled water. The majority of revenue here relates to a contract with a commercial customer for the Murrumba Downs Recycled Water Plant.

Sunshine Coast revenue by service

| Services | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|------------------------------|---------------|---------------|---------------|---------------|---------------|
| Drinking Water | \$57m | \$67m | \$80m | \$95m | \$108m |
| Other Core Water | \$0 | \$0 | \$0 | \$0 | \$0 |
| Sewage via Sewer | \$70m | \$78m | \$82m | \$97m | \$113m |
| Trade Waste | \$0.9m | \$0.5m | \$1.2m | \$1.3m | \$1.3m |
| Other Core Sewage | \$0 | \$0 | \$0 | \$0 | \$0 |
| Non Regulated | \$12m | \$0.1m | \$0.1m | \$0.1m | \$0.1m |
| Revenue from Services | \$141m | \$146m | \$163m | \$193m | \$222m |

1.6 Service standards

Unitywater is currently managing to approve service standards inherited from the former Council businesses. These service standards currently reside in the Strategy Asset Management Plan and customer service standards, which are required to be updated by 30 June 2011. Unitywater anticipates that a common set of standards will be developed across its service area from this time.

1.7 Demand forecasts

Water demand forecasts were referenced from the current customer databases and the forecasts supplied by the participating Councils as part of the Water Reform Program due diligence exercise. The later formed the base for the demand in the Enterprise Financial Model. Unitywater also engaged an economic consultancy to undertake forecasts of the equivalent base charge. The forecasts are set out below.

Demand forecasts

| DEMAND | FY2010 | FY2011 | FY2012 | FY2013 |
|--|---------|---------|---------|---------|
| Drinking Water Volumes ML | 47,146 | 48,723 | 49,242 | 51,288 |
| Drinking Water Equivalent Base Charges | 282,118 | 288,235 | 294,670 | 301,156 |
| Sewage via Sewer Equivalent Base Charges | 288,748 | 295,098 | 301,589 | 308,223 |

Expected long term demands are used to plan the future capital works program and long term operational and maintenance strategies. These are based around expected population growth but also take into account State and Council development plans. The maximum likely demand level needs to be taken into account in this forecasting.

1.8 Regulatory asset base (RAB)

The opening RAB as at 1 July 2008 has been reconciled to the asset values as advised by the Minister for Natural Resources, Mines and Energy and Minister for Trade for each Council, and pro-rated based on the written down value. Due to information constraints arising from an absence of final Council data, the opening RAB at 1 July, 2010 is an interim value.

The table below provides a summary of the interim RAB roll-forward estimate to 30 June, 2010.

Summary RAB roll-forward 1 July 2010

| REGION \$(000) | Initial RAB 1 July 2008 as per Ministerial Direction | Add: Capital Expenditure | Less: Disposals | Less: Regulated Depreciation | Add: Indexation | RAB rolled forward 30 June 2010 Interim value |
|-------------------|--|--------------------------------|--------------------|------------------------------------|--------------------|--|
| Moreton Bay | 1,110,017 | 334,863 | | (61,297) | 55,548 | 1,439,131 |
| Sunshine Coast | 919,853 | 94,276 | (1,008) | (52,113) | 43,130 | 1,004,138 |
| Total | 2,029,870 | 429,139 | (1,008) | (113,410) | 98,678 | 2,443,269 |

Unitywater has also forecast the RAB balances over the price monitoring period. This is summarised in the table below.

Summary RAB roll-forward 30 June 2013

| REGION \$(000) | RAB rolled forward 30 th June 2010 | Add: Capital Expenditure | Less: Disposals | Less: Regulated Depreciation | Add: Indexation | RAB rolled forward 30 June 2013 |
|-------------------|---|--------------------------------|--------------------|------------------------------------|--------------------|---------------------------------------|
| Moreton Bay | 1,439,131 | 397,561 | | (119,446) | 142,940 | 1,860,186 |
| Sunshine Coast | 1,004,138 | 384,032 | | (88,141) | 87,690 | 1,387,719 |
| Total | 2,443,269 | 781,593 | | (207,587) | 230,630 | 3,247,905 |

Asset acquisitions for the period were based on Unitywater's budgeted capital expenditure projects in a year assuming 65% capitalisation at year end. This means that the assumed level of incomplete assets is then carried forward to the next year's asset acquisitions.

1.9 Capital expenditure

The table below summarises Unitywater's forecast capital expenditure by year, region and service:

Three year capital expenditure plan \$m

| Region | Services | FY2011 | FY2012 | FY2013 |
|-----------------------------|-------------------------------------|--------------|--------------|--------------|
| Moreton Bay | Non-regulated services | 0.3 | 0.2 | 0.2 |
| | Business Support | 17.0 | 8.3 | 3.8 |
| | Other core water services | 0.8 | 1.8 | 1.4 |
| | Sewage Collection | 63.1 | 29.5 | 17.3 |
| | Sewage Treatment | 78.6 | 21.0 | 7.4 |
| | Water Distribution and Reticulation | 12.3 | 15.0 | 7.0 |
| | Total Moreton Bay | | 172.1 | 75.8 |
| Sunshine Coast | Non-regulated services | 0 | 0 | 0 |
| | Other core water services | 9.0 | 8.8 | 0.6 |
| | Sewage Collection | 26.1 | 26.6 | 40.8 |
| | Sewage Treatment | 34.7 | 89.2 | 93.5 |
| | Water Distribution and Reticulation | 20.1 | 23.5 | 21.6 |
| Total Sunshine Coast | | 90.0 | 148.0 | 156.4 |
| Total Unitywater | | 262.1 | 223.9 | 193.5 |

Notes: Unitywater has populated the data templates with capitalised expenditure for the period. This assumes that 65% of planned capital expenditure will be capitalised in the year.

Unitywater has developed its capital expenditure program for FY2011 and outer years with reference to the need for the expenditure, and has categorised expenditure according to the drivers of growth, renewals, improvements and compliance. Unitywater's program has also been developed having regard to its capacity to deliver, based on past performance and the availability of resources and contractors to perform the work.

Significant investment will be directed to sewage treatment and collection infrastructure. These projects are primarily growth driven and reflect the growing demand for services in both regions.

In particular investment in new sewerage infrastructure for Sunshine Coast is required due to new residential developments and significant capacity issues within the existing network. The three year capital program provides for the upgrade and augmentation of seven sewage treatment plants in the Sunshine Coast region representing a total investment of approximately \$200m.

Other significant projects include upgrades and augmentations of four sewage treatment plants in the Moreton Bay region representing a further \$98m investment.

Capital expenditure for FY2011 was approved by the Board of Unitywater as part of its overall budget approval process. Unitywater has established a sub-committee of the Board to monitor and review the capital expenditure program and its delivery. This committee meets monthly to consider progress against timelines and budget, and make decisions as required on variations or budget changes.

Unitywater is currently establishing further governance structures to underpin the process of approving capital expenditure.

1.10 Contributed, donated and gifted assets

Unitywater has been unable to obtain complete and final information about contributed, donated and gifted assets from Councils for FY2009 and FY2010.

The information for FY2010 is based on Council third quarter estimates, and will need to be updated when final results are provided to Unitywater. This will have an impact on the final RAB and MAR calculations.

For the period FY2011 to FY2013, estimated developer provided assets are forecasted from historic trends taking into consideration expected development growth. The actual level of developer provided assets can vary significantly in an individual year depending on the timing of developments. Forecasts of planning scheme charges are also based on historic trends. Unitywater expects this forecasting will improve in subsequent years.

The following table indicates the level of receipts for each service for the Moreton Bay Region, as currently estimated and presented in the completed templates:

Capital contributions Moreton Bay

| | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|--|---------|---------|---------|---------|---------|
| Drinking Water Donated Assets | \$9.6m | \$6.0m | \$4.5m | \$4.0m | \$4.1m |
| Drinking Water Grants | \$3.6m | \$0.7m | | | |
| Drinking Water Planning Scheme Charges | \$7.5m | \$9.7m | \$11.6m | \$12.2m | \$12.5m |
| Sewage via Sewer Donated Assets | \$9.8m | \$6.9m | \$9.1m | \$8.1m | \$8.3m |
| Sewage via Sewer Grants | \$33.3m | \$24.3m | | | |
| Sewage via Sewer Planning Scheme Charges | \$9.6m | \$12.3m | \$14.9m | \$15.8m | \$17.1m |

The following table indicates the level of receipts for each service for the Sunshine Coast Region, as currently estimated and presented in the completed templates:

Capital contributions Sunshine Coast

| | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|--|---------|---------|---------|--------|--------|
| Drinking Water Donated Assets | \$9.9m | \$6.8m | \$6.9m | \$5.6m | \$5.6m |
| Drinking Water Grants | \$2.1m | \$3.3m | | | |
| Drinking Water Planning Scheme Charges | \$11.3m | \$6.7m | \$10.0m | \$9.9m | \$9.9m |
| Sewage via Sewer Donated Assets | \$19.3m | \$12.4m | \$10.2m | \$8.0m | \$8.0m |
| Sewage via Sewer Grants | \$1.3m | \$0.03m | | | |
| Sewage via Sewer Planning Scheme Charges | \$9.6m | \$6.5m | \$8.5m | \$8.5m | \$8.4m |

The information requirement seeks nomination of any date that Unitywater intends to adopt the asset offset method. For clarity, Unitywater has not nominated a date although this does not mean it will not choose to do so during the price monitoring period. Any nomination will occur as part of a future information return.

1.11 Depreciation

Regulatory depreciation values as at 1 July 2008 have been calculated on the basis of remaining useful life of individual assets applied to the asset value grossed up/down in accordance with the Minister's advised values. Depreciation, relating to asset acquisitions (capitalised and developer provided) during the period 1 July 2008 to 30 June 2010, has been calculated on the basis of Council asset useful life and pro-rated in accordance with the acquisition date. However, complete information was not always available from Councils for some assets,

in which case a useful life of 50 years was assumed. This will be revised once more complete information is available.

Depreciation for assets acquired post 1 July 2010 were based on asset lives provided by engineering consultants during the SEQ water reform phase 2 process. A new Non Current Asset Policy has just been approved by Unitywater's Board. This policy contains asset lives that differ in some cases from those used in the current submission however it is not envisaged that the variation to depreciation values will be material. It is proposed to recalculate depreciation as part of the process to finalise the interim RAB.

Straight line depreciation has been applied in all cases. A summary of depreciation over the analysis period, by region and service, is provided below:

Depreciation by Region and Service

| REGION AND SERVICE (\$000) | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|----------------------------|---------------|---------------|---------------|---------------|---------------|
| Moreton Bay | 30,223 | 31,075 | 35,005 | 40,619 | 43,822 |
| NON REGULATED | 44 | 112 | 208 | 227 | 237 |
| NON REGULATED | | | | | |
| REGULATED | 44 | 112 | 208 | 227 | 237 |
| SEWERAGE | 18,859 | 19,384 | 22,145 | 26,135 | 28,115 |
| TRADE WASTE | 0 | 4 | 7 | 7 | 7 |
| SEWAGE VIA SEWER | 18,859 | 19,381 | 22,138 | 26,127 | 28,107 |
| WATER | 11,320 | 11,579 | 12,652 | 14,257 | 15,470 |
| DRINKING WATER | 11,048 | 10,923 | 11,846 | 13,406 | 14,571 |
| OTHER CORE WATER | 272 | 656 | 806 | 851 | 899 |
| Sunshine Coast | 25,641 | 26,471 | 27,372 | 29,212 | 31,560 |
| NON REGULATED | 18 | 23 | 26 | 26 | 26 |
| NON REGULATED | 18 | 23 | 26 | 26 | 26 |
| SEWERAGE | 16,509 | 17,058 | 17,677 | 19,018 | 20,812 |
| TRADEWASTE | 2 | 5 | 8 | 8 | 8 |
| SEWAGE VIA SEWER | 16,507 | 17,053 | 17,669 | 19,010 | 20,804 |
| WATER | 9,114 | 9,390 | 9,668 | 10,167 | 10,722 |
| DRINKING WATER | 8,484 | 8,760 | 9,005 | 9,430 | 9,928 |
| OTHER CORE WATER | 631 | 631 | 664 | 738 | 793 |
| Grand Total | 55,864 | 57,547 | 62,377 | 69,831 | 75,381 |

The growth in regulatory depreciation occurs due to growth in capital expenditure.

1.12 Indexation

The RAB and capital expenditure has been indexed in accordance with the Ministerial Direction to the Authority and the Authority's requirements. The table below provides a summary

Indexation Parameters

| Indexation rates | | Year Ending 30 June: | | |
|------------------------|------|----------------------|-------|--------------|
| | | 2009 | 2010 | 2011 onwards |
| Annual Indexation rate | % pa | 2.02% | 2.50% | 2.48% |
| | | Historical | | Forecast |

Unitywater intends to revise the indexation assumption for FY2010, to align with the increase in the consumer price index for that period, upon finalising the RAB for 1 July, 2010.

1.13 Return on capital

The Direction from the Minister requires the Authority to consider a weighted average cost of capital (WACC) within a reasonable range of values for FY2011. A joint consultancy between the three retail/distribution entities was commissioned to undertake a detailed study in respect to an appropriate weighted average cost of capital to be applied for calculation of revenue requirements in FY2011. Consultants CEG undertook this analysis, and recommended a range for the WACC. Unitywater has adopted the midpoint of this range being 9.88% (nominal post-tax).

Unitywater notes that some of the underlying assumptions adopted by the consultant depart from those adopted by the Authority in past decisions. Unitywater submits that the above WACC falls within a reasonable range, as there are a number of valid assumptions that can be made in relation to WACC parameters. Furthermore, Unitywater submits that the Authority should not be constrained by its past decisions in assessing a reasonable range, as there are clearly valid assumptions and parameters that lie outside its past decisions that have been adopted by regulators elsewhere.

1.14 Operating costs

Unitywater is in its first year of operations and has inherited assets and cost structures from Councils. Unitywater must also develop new corporate and retail capabilities, while maintaining service continuity. Operating costs for FY2011 represent business as usual costs as well as one-off costs associated with bringing the business together, for example, systems and business integration activities.

The table below shows the forecast operating expenditure \$m by year, activity and cost category as defined by the Authority:

Three year operating expenditure plan \$m

| Activity and cost category | FY2011 | FY2012 | FY2013 | Total | % contribution to total expenditure |
|----------------------------|----------|----------|----------|-----------|-------------------------------------|
| Non-regulated | | | | | |
| Corporate | 1 | 1 | 1 | 3 | |
| Distribution Operating | 6 | 6 | 6 | 19 | |
| Total non-regulated | 7 | 7 | 8 | 22 | 2.8% |
| Sewerage | | | | | |
| Corporate | 26 | 24 | 25 | 74 | |
| Distribution Operating | 62 | 64 | 67 | 193 | |

| Activity and cost category | FY2011 | FY2012 | FY2013 | Total | % contribution to total expenditure |
|----------------------------------|------------|------------|------------|------------|-------------------------------------|
| Retail | 6 | 9 | 9 | 24 | |
| Total Sewerage | 93 | 98 | 101 | 292 | 37.5% |
| Water | | | | | |
| Bulk water costs | 75 | 93 | 114 | 283 | |
| Corporate | 23 | 22 | 22 | 68 | |
| Distribution Operating | 29 | 31 | 32 | 92 | |
| Retail | 6 | 8 | 9 | 23 | |
| Total Water | 134 | 154 | 177 | 465 | 59.7% |
| Unitywater | | | | | |
| Bulk water costs | 75 | 93 | 114 | 283 | 36.3% |
| Corporate | 50 | 47 | 48 | 145 | 18.6% |
| Distribution Operating | 97 | 101 | 105 | 303 | 39.0% |
| Retail | 12 | 18 | 18 | 48 | 6.1% |
| Total Unitywater | 234 | 259 | 286 | 779 | |
| % inc on base year FY2011 | 0 | 11% | 22% | | |

The table below sets out the growth and cost escalation parameters which were applied when forecasting Unitywater's initial budget.

Growth and cost escalation factors

Population Growth

| Year | FY2011 | FY2012 | FY2013 |
|----------------|--------|--------|--------|
| Moreton Bay | 2.52% | 2.29% | 2.29% |
| Sunshine Coast | 2.85% | 2.35% | 2.35% |

Cost Escalation

| Year | FY2011 | FY2012 | FY2013 |
|-----------------------|--------|--------|--------|
| General Escalation | 2.9% | 2.9% | 2.9% |
| Chemicals | 3.5% | 3.5% | 3.5% |
| Electricity | 7.9% | 7.9% | 7.9% |
| Labour (SC 4% FY2011) | 4.5% | 4.0% | 4.0% |
| Bulk water: | | | |
| Moreton Bay | 22% | 18% | 15% |
| Sunshine Coast | 26% | 28% | 22% |

Note: Costs will differ within South East Queensland given location, demographics, workforce and other factors. Hence cost escalation can be expected to be different between the various distribution/retail entities.

Additional costs will be incurred, both recurrent and one-off items, in relation to establishment of new corporate and retail capacity. There are also costs associated with Council based service level agreements and employee costs associated with staff transferred from existing council corporate structures to Unitywater.

Unitywater is governed by the reform workforce framework which guarantees maintenance of employee conditions until 30th June 2013. Estimated salaries and wages which fall within the workforce framework represent 86% of total employee budgeted costs for FY2011.

Unitywater may also incur estimated costs of \$1.7m for FY2011 in relation to labour equalisation between regions. Operational costs for FY2011 show this commitment as a once off impact included in operational corporate projects with the recurrent impact included in the relevant budgets for FY2012 and FY2013.

Efficiencies are planned in line with Unitywater's development path. Strategies are currently being developed to leverage efficiencies from the use of technologies and additionally through the review of existing contracts to identify opportunities to achieve the most cost effective outcomes.

Operating costs have been segregated by region and attributed to activities, services and cost categories at a disaggregated level as required by clause 5.11 of the Information Requirement.

Operating cost data has been sourced as follows:

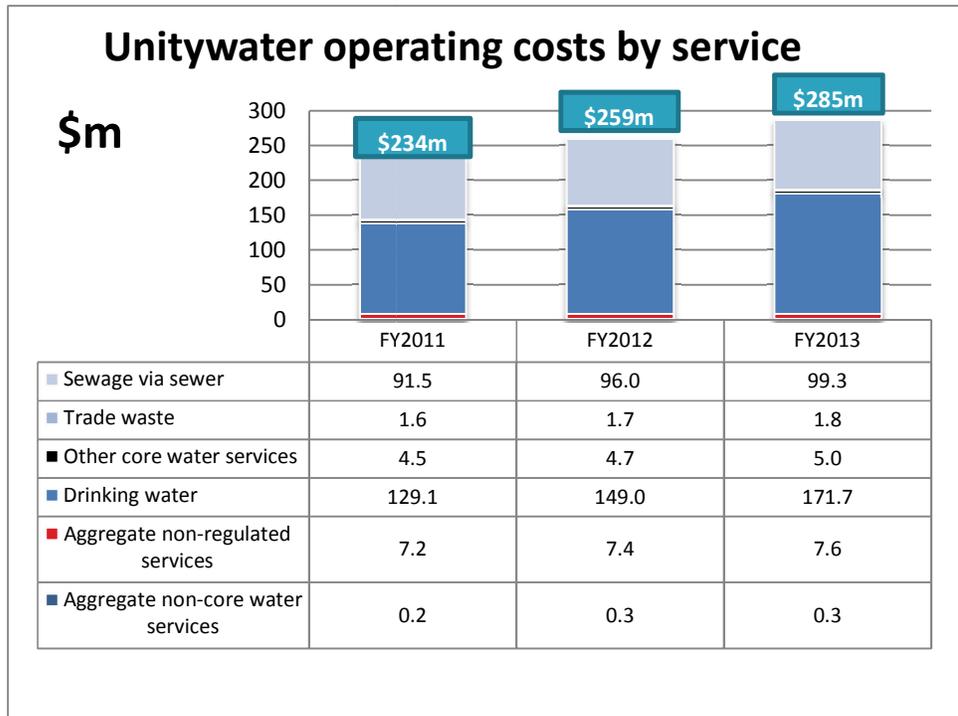
- FY2009 – Due to the disparate information available directly from Councils, the alternate information source used was the Enterprise Financial Model. This model was the tool utilised for the collation of data by the SEQ Water Reform Project. This model is an audited document.
- FY2010 – As the final financial results for the respective Councils were not available at the time of data collection, Councils adopted third quarter budget estimates were used.
- FY2011 to FY2013 – Detailed budget information by cost code and natural account was used to populate information for the forecasted years. The disaggregated data used has been reconciled to Unitywater's initial budget documentation as approved by the Board.

Where costs could not be directly attributed to a service, detail of the cost allocation and associated causal drivers have been provided separately. Unitywater has provided the full allocation model accompanied by a supporting explanatory document.

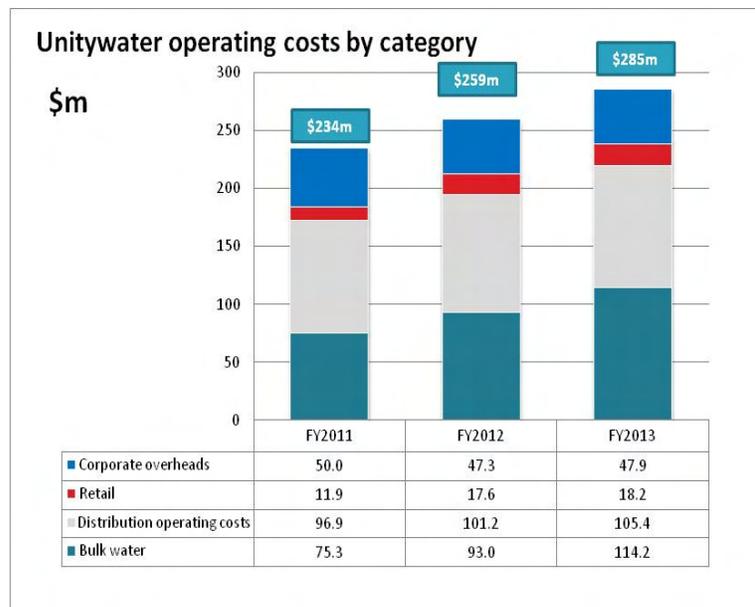
It is difficult to make meaningful comparisons of costs between FY2011 and FY2010 when Councils owned and operated the assets. This is because Councils' water and sewerage businesses operated within the Councils' broader corporate structure, and utilised Council-wide resources. Historic costs for water and sewerage will therefore be heavily influenced by how these corporate and other common costs were allocated, compared to how those costs currently present for Unitywater. Comparisons to FY2010 require further caution as costs in this year are based on a Council estimate only. This estimate may not be exhaustive and may differ significantly from actuals depending on the robustness of the Councils' estimates.

The following graphs set out the anticipated changes to operating costs.

Operating Costs FY2010 to FY2013 by service (\$nominal)



Operating cost by cost type (\$nominal)



Bulk water charges are clearly the main reason for increasing operating costs into the future.

1.16 Non-regulated services

Unitywater has inherited two non-regulated services: laboratory services and private works. The table below presents the financial characteristics of these services in aggregate. Capital expenditure for these services has

been separately identified, as has direct and indirect operating expenditure. Common costs have been allocated to these services in accordance with Unitywater's revenue and cost allocation model.

Non-regulated services – aggregate financial details

| Non Regulated Service | \$M |
|---------------------------|-------------|
| Budgeted Revenue | 3.79 |
| Operating Costs | 7.20 |
| Depreciation | 0.23 |
| Return on Assets | 0.75 |
| MAR Adjustments | -0.06 |
| Full Cost Recovery | 8.11 |
| Under Recovery | 4.32 |

1.17 Tax useful lives and asset values

In all cases tax useful life has been assumed to be the same as the regulatory useful life. This assumption may be revised at a later point by Unitywater pending advice from tax advisors.

1.18 Conclusion

Unitywater assumed ownership of its assets on 1 July, 2010. This was preceded by a short, yet intense, period of preparation to take on these new responsibilities, with the entity formally created in November 2009. The creation of Unitywater as a standalone, commercial business presents significant opportunities to adopt new management practices, explore innovation and customise business processes and systems to improve operational performance. While these are longer-term aspirations, the immediate focus is to establish the business, which is in its first year of operations, and maintain continuity of service to customers. Unitywater must also deal with legacy issues as it has inherited assets, tariff structures and prices, resources, systems and processes and supplier contracts from the previous Council owners.

This is Unitywater's first information return to the Authority under the interim price monitoring regime, and has been made amidst the transition of water and sewerage assets from Councils.

While there currently a number of information constraints for this return, particularly in relation to prior years, this was not unexpected by the Authority nor the Authority's Ministers. Indeed, the Direction notice to the Authority requires the Authority to consider the availability of information from the entity, their emerging capability to provide information and the transitional work required to integrate and establish the entities and accept the operational constraints imposed by the SEQ Urban Water Arrangements Reform Workforce Framework 2010.

Unitywater has set out a program and timetable to remedy these information constraints and in particular in relation to the opening RAB at 1 July, 2010.

Unitywater's forecast revenues are below MAR, based on reasonable allowances for operating costs and return on and return of assets. Unitywater intends to smooth the price increases on an NPV neutral basis. This will be revised and confirmed in subsequent information returns.

Many systems and processes that would be typical of an established business are under development. This early status of business maturity also has implications for pricing and this information return. For example, it is difficult to establish a MAR with the precision that normally occurs for a mature regulated business. Furthermore, many factors that influence the opening RAB are yet to be finalised.

Unitywater is still in the process of finalising its systems and resources required to operate the business, including new retail and corporate capabilities. Nonetheless, Unitywater has made significant progress already towards the post FY2013 regulatory environment, particularly in regard to its financial systems and governance measures for capital expenditure.

Section 2 Introduction

The Premier and Treasurer of Queensland (the Authority's Ministers) have referred the monopoly distribution and retail water and sewerage activities of Unitywater and two other entities in South East Queensland to the Queensland Competition Authority (the Authority), for a price monitoring investigation covering the period 1 July, 2010 to 30 June, 2013 (FY2011 to FY2013).

The Authority has published its information requirements for Unitywater and the other two entities, in the form of a report (SEQ Interim Price Monitoring Information Requirements for FY2011 (the information requirement)), and a template in spreadsheet form. This report has been structured to align with the structure of the information requirement, and particularly chapter 5.

This report, along with the completed templates, forms Unitywater's response to this information requirement.

2.1 Unitywater

Unitywater is a statutory authority responsible for the delivery of water supply and sewerage services to customers in the Moreton Bay and Sunshine Coast regional area.

Unitywater was established by the Queensland Government as part of its reform of water supply arrangements in South East Queensland, in accordance with the *South-East Queensland Water (Distribution and Retail Restructuring) Act 2009*. The reform process included divesting Moreton Bay Regional Council and Sunshine Coast Regional Council of their water distribution and sewerage assets and transferring these to Unitywater on 1 July 2010.

The reforms are aimed at providing better outcomes for customers, and include the delivery of:

- Improved water supply co-ordination and management;
- More efficient water supply and sewerage services; and
- Improved management of the associated infrastructure.

An independent Board has been appointed to decide the strategies for Unitywater and to ensure that the functions of the organisation are delivered. The former owners of the Unitywater assets are entitled to participate in the returns delivered from the efficient operation of the business, which in turn contributes to the quality and availability of social infrastructure within the region.

The creation of Unitywater as a standalone, commercial business presents significant opportunities to adopt new management practices, explore innovation and customise business processes and systems to improve operational performance. While these are longer-term aspirations, the immediate focus is to establish the business, which is in its first year of operations, and maintain continuity of service to customers. Unitywater must also deal with legacy issues as it has inherited assets, tariff structures and prices, resources, systems and processes and supplier contracts from the previous Council owners.

2.2 Characteristics of the area served

The area serviced by Unitywater spans more than 5,000 square kilometres, with an estimated residential population of 670,000, which represents approximately 21% of Queensland's total population. This population is predicted to grow significantly to 804,000 residents by 2016 and 1,024,000 residents by 2031.

Within its geographical area, Unitywater:

- Provides customers with drinking-quality water;
- Collects, treats and disposes of sewage;
- Treats, recycles and supplies water to industry;
- Operates and maintains the infrastructure in a water and sewerage system;
- Plans and delivers new infrastructure to enhance the system;
- Serves customers and levies a charge for its services.

Unitywater has been formed amidst this environment of growth in demand and expansion to its service footprint.

Unitywater has also inherited a significant portfolio of assets, including 18 sewerage treatment plants, over 5,100km of trunk and reticulation main pipelines, 826 sewage pump stations and pressure mains, and around 5,000 km of trunk and reticulation sewers.

The diagram below outlines the geographical area serviced by Unitywater.

Diagram 1 Area serviced



2.3 Emerging and developing capabilities

As set out above, Unitywater assumed ownership of its assets on 1 July, 2010. This was preceded by a short, yet intense, period of preparation to take on these new responsibilities, with the entity formally created in November 2009. This is clearly a factor to be taken into account when assessing the information available from

Unitywater. This also means that many systems and processes that would be typical of an established business are under development. This was recognised by the Authority's Ministers, in explaining the background to their Direction to the Authority:³

Over the interim regulatory period, the Ministerial Direction clearly indicates that the QCA should recognise the emerging and developing capabilities of the new entities. With multiple water and wastewater businesses merging into single organisational units, the capacity of the new entities to provide comprehensive regulatory information will be limited, particularly for 2010-11. Moreover, organisation-wide systems and processes will take time to become established.

This early status of development also has implications for pricing and this information return. For example, it is difficult to establish a maximum allowable revenue (MAR) with the precision that normally occurs for a mature regulated business. Furthermore, many factors that influence the opening regulatory asset base (RAB) are yet to be finalised.

Unitywater is still in the process of finalising its systems and resources required to operate the business, including new retail and corporate capabilities. At the same time, the resourcing of the business has needed to occur within the requirements of the operational constraints imposed by the SEQ Urban Water Arrangements Reform Workforce Framework, 2010.

2.4 Progress to beyond the interim price monitoring period

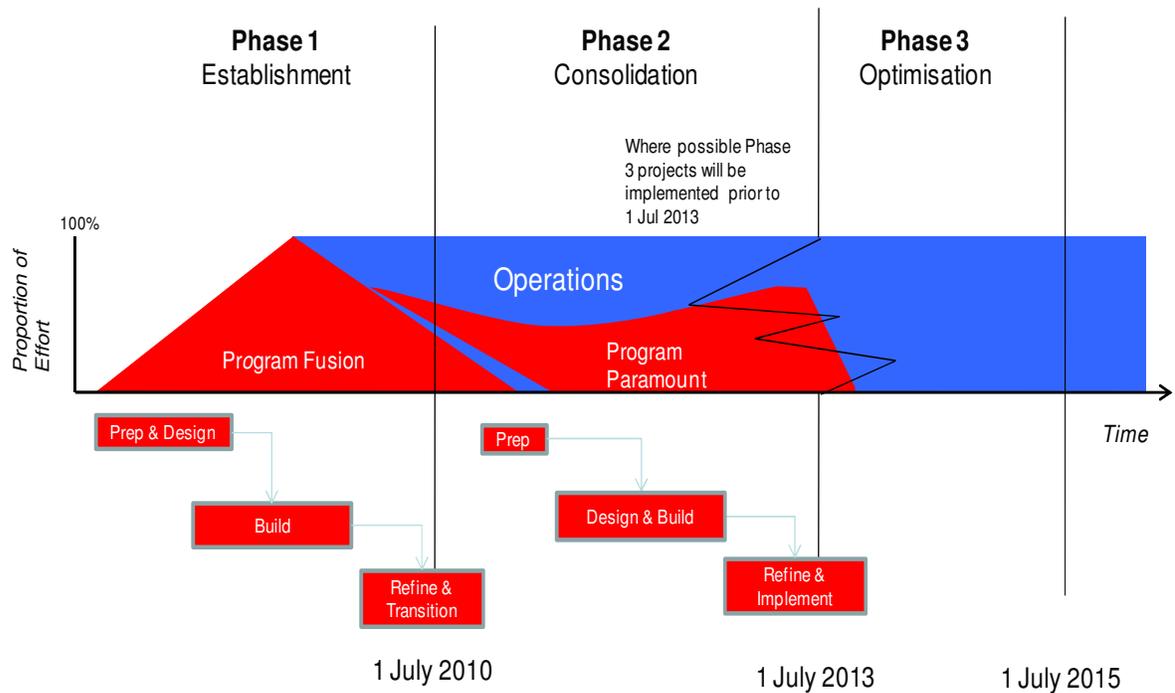
Despite only recently having taken ownership of the assets, Unitywater has achieved much already in preparing itself for the regulatory environment beyond FY2013, including:

- Reducing its reliance upon Council systems and resources, to the point where it is expected that independent resourcing will be achieved, by and large, for FY2012. Already, Unitywater has implemented its own finance and payroll systems;
- Structuring its financial accounts to align with the Authority's data requirements under the interim price monitoring regime;
- Implementing governance processes around the capital expenditure program, including a dedicated sub-committee of the Board to review expenditure and approve variations;
- Developing internal performance indicators and systems of measurement;
- Developed detailed cost allocation methodologies; and
- Identified a pathway to finalise its RAB value, based on final, audited information from Councils.

It is also important to note that the Unitywater Board has only just been established, and the strategy for the business is still being developed. The strategy-setting activities of the Board will influence the future direction of Unitywater, including the resourcing arrangements for the business, prioritisation of activities, asset management and development of its capital expenditure program and delivery of that program into the future. The Board also recognises that the strategy for the business must be complementary to its regulatory environment. Indeed its future revenues will be dependent upon the effectiveness of its regulatory strategy and ability to respond to the current and future regulatory regimes.

Unitywater is implementing a three-phase program to fully develop the business and its operational capability. This is summarised in the diagram below:

³ Letter from the Authority's Ministers to Mr Brian Parmenter, 2 July 2010.

Diagram 2 Development Path

The first phase was completed on 30 June, 2010, and involved the transfer of the two Councils' water and sewerage assets and people to Unitywater and the establishment of necessary Service Level Agreements to ensure business continuity. Unitywater's governance and quality and performance frameworks were also established.

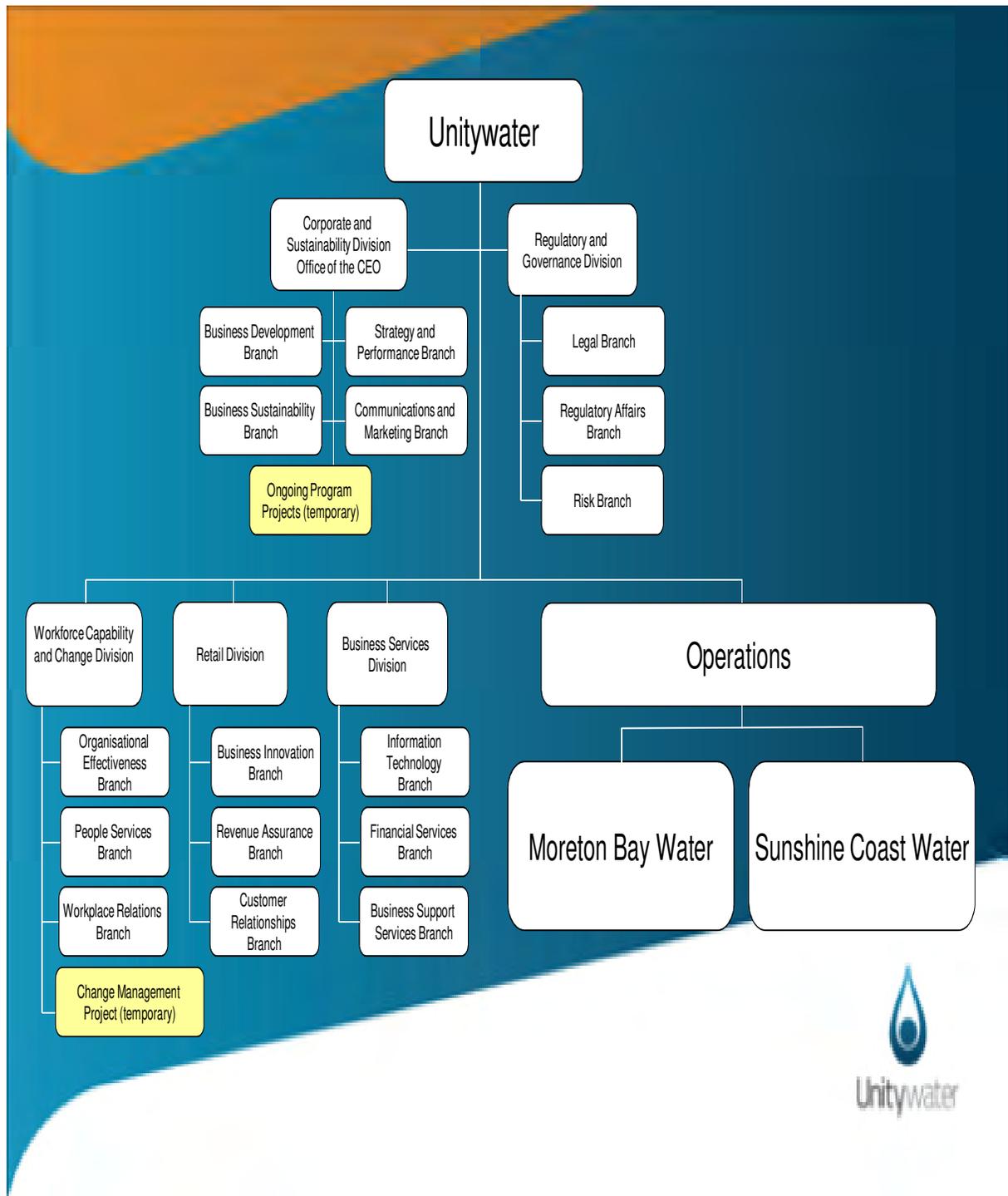
The second phase, which aligns with the price monitoring period (1 July 2010 to 30 June, 2013), is currently underway and involves progressing the consolidation of Unitywater, and fully implementing systems and processes. In doing so, an important part of this phase is to identify and capture opportunities for efficiencies from the new organisation and large service area and asset base.

The final phase reflects the activities of a fully developed business, including the refinement and optimisation of business systems and processes.

Diagram 3 outlines the Unitywater's current organisational structure from a functional perspective.

The Unitywater budget approved by its Board for FY2011 reflects the structure below and represents approximately 941 full time equivalent staff.

Diagram 3 Business Structure



2.5 Information constraints

The price monitoring framework is information intensive, and for the current year relies heavily upon information obtained from the previous Councils for FY2009 and FY2010. Unitywater has sought to obtain as much of this information as possible from Councils. Where data was not available from Councils directly, Unitywater has sought the reasons why this was not available. In some cases, Unitywater has sourced information from the Enterprise Financial Model developed by the Council of Mayors (SEQ) water reform program using Council-provided data, on the basis that this was the best information available at the time of lodging this information return. This model was audited externally for data integrity and data quality.

The details of the information constraints and data limitations are set out throughout this information return. In general, these relate to:

- An absence of some statutory account information, particularly for balance sheet or cash flow statements as these were not prepared discretely for the Councils' water and sewerage business;
- The accounting treatment and level of cost disaggregation for amalgamating Councils has shown to be disparate particularly for FY2009. This is partly attributable to different classifications of the Councils' water and sewerage businesses under full cost pricing principles. Generally for those Councils where the business met the threshold criteria for a type 2 business (Local Government Act requirement), separate accounts existed for revenue, operating costs and capital projects. For those Councils which did not need to report water and sewerage as a business activity, minimal separate information was collated;
- Historic water demand data, particularly for FY2009; and
- Details for the FY2010 year, which are generally based on estimates (using Councils' third quarter forecasts) as final year-end data was not available to Unitywater. The forecast year-end position could differ substantially from the actual position, once finalised.

Accordingly, data templates for past years have been populated from the following source documents:

- FY2009 – Due to the disparate information available directly from Councils', the alternate information source used was the Enterprise Financial Model. The model values were used to populate operating result data for this information return with the exception of developer provided assets and other capital contributions. This information was based on actual reported data to maintain integrity of information used in the calculation of the regulatory asset base.
- FY2010 – As the final financial results for the respective Councils were not available at the time of this data collection, Councils adopted quarter three estimates were used.

Furthermore, Unitywater has not been able to certify the information provided from Councils, but has instead relied on the audited results (where available) used for external reporting. Unitywater has also relied upon the accuracy and completeness of the data in the Enterprise Financial Model for FY2009, and the Councils in relation to the accuracy and completeness of the forecasts for FY2010.

It is important to note that this has implications for the calculation of the opening regulated asset base (RAB), as the final RAB cannot be ascertained until further, final and audited information is available from Councils. The opening RAB presented in this information return is therefore an interim value.

For the price monitoring period (FY2011 to FY2013) detailed budget information by cost code and natural account was used to populate information required for these years. The disaggregated data used has been reconciled to Unitywater's initial budget documentation as approved by the Board. It should be noted that Unitywater's forecasts are based on its best estimates, given current information. These forecasts are likely to change as Unitywater gathers more information and becomes more familiar with its operating environment and assets. Accordingly, the forecasts presented in this information return will not be to the level of precision and with the amount of rigour that would normally accompany a regulatory submission. Indeed, Unitywater notes that this is not a regulatory submission (in so far as the Authority is not setting prices on the basis of this information), but rather a point-in-time estimate of current and future costs to provide the background to monitoring revenues.

Unitywater also notes that new cost imposts may arise over the price monitoring period that are unforeseen, or uncertain and not able to be quantified.⁴ Unitywater has not sought to speculate about new cost imposts at this stage, but has made forecasts in relation to known increases for key inputs such as electricity.

Section 3 Principles and assumptions

This section sets out the principles and assumptions used in compiling the response to the information requirement.

3.1 Principles

Information provided by Unitywater reflects the substance and economic reality of each transaction in order to disclose a complete, relevant and accurate picture of events with best known knowledge at the time of the preparation of its budget and this information return, subject to the information constraints discussed in the various sections throughout this document.

Information provided by Unitywater is consistent with Council records to the extent of information made available to Unitywater and consistent with Unitywater's Board-approved budget. Information provided by Unitywater adheres to generally accepted accounting principles and satisfies accounting concepts of relevance and reliability to the extent of records and information provided by Councils. Information provided in the completed templates is at a disaggregated level and detailed models have been developed to facilitate cost allocations. Revenue and asset information has also been disaggregated, where possible.

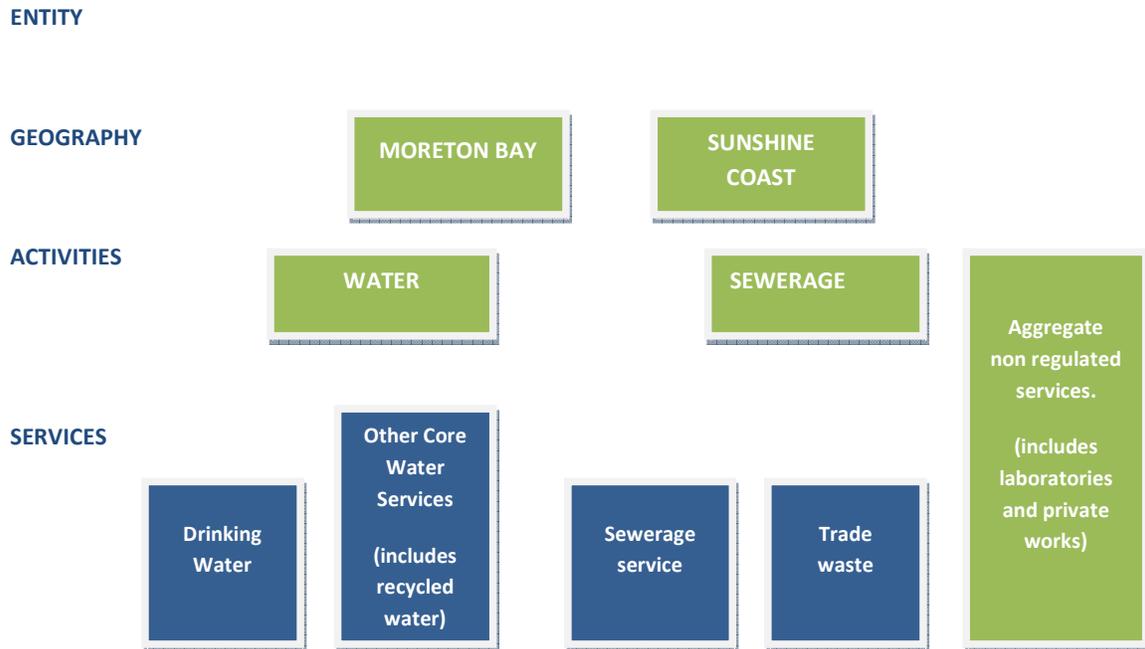
The diagram below sets out how Unitywater has applied the disaggregation required by the Authority. The forecast data underlying each service is collated at a cost centre/project code/natural account level.

Diagram 4 Disaggregation of information.

⁴ This would include, for example, any levies or chan



relation to regulation by the Authority.



The precise application of the above disaggregation for costs, assets and revenues is set out in the following sections. These sections also describe data constraints, where these exist. The alignment with statutory accounts is set out in the following section, including discussion on the information constraints in sourcing certain statutory accounts from Councils for past years. For the current information return detailed data has been provided by Unitywater to natural account level and full disclosure has been provided for the allocation of revenues and costs to service levels.

In the future the financial report for Unitywater will be a general purpose financial report which will be prepared in accordance with:

- Applicable Australian Accounting Standards (including Australian Interpretations) adopted by the Australian Accounting Standards Board;
- The Financial and Performance Management Standard 2009;
- Queensland Treasury's Financial Reporting Requirements for Queensland Government agencies; and
- Other authoritative pronouncements.

The financial statements will be authorised for issue by the Board and details will be available to be provided to the Authority on all items to a natural account level. Policies and procedures, including an accounting manual, are currently being prepared by Unitywater.

3.2 Budget assumptions

Unitywater's initial Board approved budget has been attached to the completed template as part of the supporting work papers, along with a statement of budgeted operating performance, cash-flow and balance sheet. Additionally as part of the revenue and cost allocation model, the revenues and costs are disaggregated to the lowest level of natural account and mapped to the respective regulatory reportable activities.

Unitywater has constructed its initial budget based on a combined methodology of zero based costs and historic values escalated for growth and price factors.

The table below provides a summary of the budget approach for key revenue and cost items.

Table 1 Budget Methodology

| ELEMENT | ZERO BASED | HISTORICAL/ZERO BASED |
|--|------------|-----------------------|
| Revenue | | |
| Utility Revenue | ✓ | |
| Fees and Charges (including trade waste) | | ✓ |
| Other Revenue | | ✓ |
| Capital Revenue | | ✓ |
| Operating Costs | | |
| Bulk water costs | ✓ | |
| Retail operating costs | ✓ | |
| Corporate costs | ✓ | |
| Distribution operating costs: | | |
| - Employee expenses | ✓ | |
| - Electricity costs | | ✓ |
| - Chemical costs | | ✓ |
| - Contractor expenses | | ✓ |
| - Materials and services | | ✓ |
| - Licence or regulatory fees | | ✓ |
| - Indirect taxes | | ✓ |
| Capital Expenditure | ✓ | |

Unitywater has developed a new Chart of Accounts to facilitate the rigorous financial reporting requirements to address capture of data for regulatory purposes. This means that the structure aligns with information requirements for cost categorisation as advised by the Authority.

The account string used for reporting purposes comprises an organisation unit, project code, activity and natural account:

- The organisation unit assigns a unique identity code to various areas of business. Examples of organisational codes are Mechanical Services, Electrical Services, Plumbing, Finance, etc;
- The project code identifies separate capital projects, continuing service delivery projects and operational projects;

- The activity code allows the differentiation of costs based on various activities of the business; and
- Natural accounts are grouped by revenue, expenses, assets, liabilities and equity and further categorised as per sub groups and account types for reporting purposes.

For the purposes of preparing Unitywater's initial budget, elements were budgeted for using a combination of historical and zero based methods, and required mapping of the Councils' old chart structures to Unitywater's new chart structure.

Similarly the cost categories required to align budget reporting to regulatory classifications were mapped on an individual basis. To promote transparency of disaggregated revenues and costs to the Authority, a copy of Unitywater's chart of account structure mapped to regulatory classifications has been provided as part of the working papers in the Revenue and Cost Allocation Model.

The following budget rules were applied:

- All expenses and revenues were budgeted in FY2010 dollars;
- Indexation for price and growth factors were applied universally on budget consolidation;
- Capital and operational projects were assumed to have internal labour and material costs included in the total project cost estimates;
- The labour budget was based on the respective labour establishments of Moreton Bay Water and Sunshine Coast Water (including vacancies). Labour budgets reflected various working arrangements of employees and included on-costs, overtime and annualised allowances;
- For retail and corporate business functions, labour establishments were created including staff costs for employees transferred from the two regional Councils. It is envisaged that further refinement of staff establishments will be required during Unitywater's quarterly budget review process. Changes will occur primarily due to the fluidity of services provided in-house compared to services provided under service level agreements with the respective Councils. Additional functional realignments will mean that functional reporting will change. No material impact on service allocations are expected to result from functional realignments;
- The capital budget was based on the planning databases of the respective water businesses as well as some zero based calculations for IT equipment, plant and fleet; and
- Operational projects of a non-recurring nature were budgeted in accordance with the requirements of phase 2 of Unitywater's development path.

The following table outlines the general growth and cost escalation assumptions (in nominal terms) used for determining costs as part of Unitywater's initial approved budget. Further comment regarding operating and capital costs are included in the relevant sections of this report. As set out above, new cost imposts⁵ have not been included, except to the extent of those inputs described below.

⁵ Including any levies made in relation to regulation by the Authority.

Table 2 Growth and cost escalation factors**Population Growth**

| Year | FY2011 | FY2012 | FY2013 |
|----------------|--------|--------|--------|
| Moreton Bay | 2.52% | 2.29% | 2.29% |
| Sunshine Coast | 2.85% | 2.35% | 2.35% |

Cost Escalation

| Year | FY2011 | FY2012 | FY2013 |
|-----------------------|--------|--------|--------|
| General Escalation | 2.9% | 2.9% | 2.9% |
| Chemicals | 3.5% | 3.5% | 3.5% |
| Electricity | 7.9% | 7.9% | 7.9% |
| Labour (SC 4% FY2011) | 4.5% | 4.0% | 4.0% |
| Capital Expenditure | 5.0% | 5.0% | 5.0% |
| Bulk water: | | | |
| Moreton Bay | 22% | 18% | 15% |
| Sunshine Coast | 26% | 28% | 22% |

Note: Costs will differ within South East Queensland given location, demographics, workforce and other factors. Hence cost escalation can be expected to be different between the various distribution/retail entities.

All values expressed in this report are in nominal dollars.

Section 4 Statutory accounts and budget

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section describes the statutory account information available to Unitywater from Councils, and Unitywater's budget and forecast financial statements.

As specified in the information requirement, Unitywater is expected to provide the requested information 'to the extent that records and information have been provided to the entities by the participating Councils'.

Moreton Bay Regional Council, Sunshine Coast Regional Council and the previous six amalgamated councils did not keep separate full financial statements for their water businesses for this reporting period. Due to this Unitywater is unable to provide statutory balance sheets and cash flow statements for FY2009 and FY2010. Unitywater has sought clarification from Councils about these matters.

As Unitywater did not exist until 1 July, 2010 composite information for a balance sheet and cash flow prior to this point are not available for analysing the plans for the future. The Councils did however separately report on the operating performance of their water businesses hence Unitywater has been able to combine these results for the first two years and create an indicative profit and loss statement.

4.1 Summary of Statement of Profit and Loss

The following is a high level summary of the profit and loss statement. Comparisons in expenditure between FY2010 and FY2011 should be made with caution, as the FY2010 data is based on Councils' forecast. Increases in expenditure across years are also affected by increases in bulk water charges.

Table 3 Summary of profit and loss

| | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|---------------------------|--------|--------|--------|--------|--------|
| Revenue | \$416m | \$400m | \$454m | \$520m | \$579m |
| Expenditure | \$284m | \$294m | \$428m | \$480m | \$528m |
| Earnings after tax | \$132m | \$106m | \$26m | \$40m | \$51m |

Note: data for FY2009 and FY2010 is indicative only, and is largely drawn from notes to Councils' financial accounts.

4.2 Summary of Balance Sheet

The following table is a high level summary of the balance sheet for the five years:

Table 4 Summary of Balance Sheet

| | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|--------------------|---------------|---------------|----------|----------|----------|
| Assets | Not Available | Not Available | \$3,172m | \$3,449m | \$3,670m |
| Liabilities | Not Available | Not Available | \$1,449m | \$1,615m | \$1,728m |
| Equity | Not Available | Not Available | \$1,723m | \$1,834m | \$1,942m |

The significant rise over the three years is primarily due to the investment in new capital due to growth.

4.3 Summary of Cash flow

The following table is a high level summary of the cash flow for the five years:

Table 5 Summary cash flow

| | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|----------------------------|---------------|---------------|---------|---------|---------|
| Opening Balance | Not Available | Not Available | \$25m | \$28m | \$30m |
| Operating Cash flow | Not Available | Not Available | \$117m | \$166m | \$191m |
| Investing Cash flow | Not Available | Not Available | -\$200m | -\$173m | -\$146m |
| Financing Cash flow | Not Available | Not Available | \$86m | \$9m | -\$36m |
| Closing Balance | Not Available | Not Available | \$28m | \$30m | \$39m |

4.4 Regulatory Adjustments

The adjustment of 1 July 2008 accounting values to match the valuation advised by the Minister for Natural Resources, Mines and Energy and Minister for Trade (the Minister) for the Regulatory Asset Base (RAB) and the roll forward of this RAB according to the formula outlined by the Authority has led to the identification of two regulatory adjustments as set out in the table below:

Table 6 Summary regulatory adjustments

| Items Adjusted | Budget Financial Statement FY2011 | Regulatory Adjustment | Regulatory Financial Statement FY2011 |
|--------------------------------------|-----------------------------------|-----------------------|---------------------------------------|
| Property, Plant and Equipment | \$2,834m | \$93m | \$2,741m |
| Depreciation | \$68.0m | \$5.6m | \$62.4m |

These changes to depreciation and property, plant and equipment in FY2011 are also reflected in templates 5.1.7 and 5.1.8 respectively. Consequential changes to the same items for years FY2012 and FY2013 have also been made in these templates which are the Regulatory Financial Statements. These changes are shown in the following table:

Table 7 Summary of changes

| Items | FY2011 | FY2012 | FY2013 |
|--|----------|----------|----------|
| Financial Statement Property, Plant and Equipment | \$2,834m | \$3,072m | \$3,279m |
| Adjustment | \$93m | \$60m | \$30m |
| Regulatory P, P & E Template 5.1.8 | \$2,741m | \$3,012m | \$3,248m |
| Financial Statement Depreciation | \$68.0m | \$74.6m | \$81.8m |
| Adjustment | \$5.6m | \$4.8m | \$2.9m |
| Regulatory Depreciation Template 5.1.7 | \$62.4m | \$69.8m | \$78.9m |

4.5 Accounting Principles and Policies

The previous section discussed the accounting principles and policies used for this information return. Unitywater will provide information on any changes to accounting principles and policies in future information returns.

Section 5 Revenue

Note:

The historic information set out in this chapter is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section describes Unitywater's approach to pricing, and sets out its forecast revenues. Historic revenue information is also provided, which has been sourced from Councils.

5.1 Pricing Policy

Unitywater has adopted a pricing policy to achieve full cost recovery at or near its best estimate of MAR. However, MAR for FY2011 and subsequent years is subject to the finalisation of some key assumptions, including the opening RAB. For FY2011, the current estimate of MAR is above that anticipated when setting prices. Unitywater's policy in this instance has been to retain the original prices, as announced, and to smooth prices in subsequent years (from FY2012 onwards) so that MAR is achieved over a defined period, on a NPV neutral basis. In determining the level of under-recovery for FY2011, Unitywater will adjust for the final RAB, actual revenues received and actual capital contributions received.

The period of the price smoothing will be determined once the MAR parameters are finalised, including the opening RAB. The three year revenue forecast presented in this information return is not based on an NPV neutral glide path, and has been provided to present an indication of potential growth in revenue over the price monitoring period.⁶

Unitywater has little control on water demands given the institutional settings for the SEQ Water Grid. Furthermore, demand is difficult to predict in the current environment where permanent water conservation measures are being applied for the first time, amidst a growing population. Consequently, Unitywater proposes to adopt a revenue cap approach to pricing and adjust prices in subsequent years to account for

⁶ This is not Unitywater's proposed price path, and accordingly the information return does not set any details about the price path.

variations between actual and forecast demand. This approach is to apply for the current year, and will be reviewed for FY2012 onwards.

Unitywater's pricing policy in relation to tariff reform is to limit any changes where possible until such time as the Authority has published final pricing principles, as has been foreshadowed. In terms of contributed, donated and gifted assets, Unitywater has retained the revenue offset approach, although it will review this position annually.

5.2 Revenue for each of the Services

In reporting revenues, actual revenues have been obtained for FY2009, Council forecasts have been used for FY2010 and Unitywater's forecasts for FY2011 to FY2013.

The following table indicates the level of revenue for each service for the Moreton Bay Region:

Table 8 Moreton Bay revenue by service

| Services | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|------------------------------|---------------|---------------|---------------|---------------|---------------|
| Drinking Water | \$65m | \$69m | \$93m | \$106m | \$121m |
| Other Core Water | \$7m | \$6m | \$8m | \$8m | \$9m |
| Sewage via Sewer | \$63m | \$79m | \$107m | \$133m | \$144m |
| Trade Waste | \$1.4m | \$1.2m | \$1.7m | \$1.7m | \$1.8m |
| Other Core Sewage | \$2m | | | | |
| Non Regulated | \$5.3m | \$2.8m | \$3.7m | \$3.9m | \$4.1m |
| Revenue from Services | \$145m | \$158m | \$213m | \$252m | \$280m |

Other Core Water Services is provision of recycled water with the great majority of the revenue from a contract with commercial entity for the Murrumba Downs Recycled Water Plant.

The following table indicates the level of revenue for each service for the Sunshine Coast Region:

Table 9 Sunshine Coast revenue by service

| Services | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|------------------------------|---------------|---------------|---------------|---------------|---------------|
| Drinking Water | \$57m | \$67m | \$80m | \$95m | \$108m |
| Other Core Water | \$0 | \$0 | \$0 | \$0 | \$0 |
| Sewage via Sewer | \$70m | \$78m | \$82m | \$97m | \$113m |
| Trade Waste | \$0.9m | \$0.5m | \$1.2m | \$1.3m | \$1.3m |
| Other Core Sewage | \$0 | \$0 | \$0 | \$0 | \$0 |
| Non Regulated | \$12m | \$0.1m | \$0.1m | \$0.1m | \$0.1m |
| Revenue from Services | \$141m | \$146m | \$163m | \$193m | \$222m |

Note: all values are in nominal dollars.

For Drinking Water the rise in revenue is primarily due to the pass through of higher bulk water costs, growth (including capital expenditure), and the indicative revenue path.⁷

For Sewage via Sewer the rise is due to the same factors, with the exception of bulk water charges. Accordingly the increases are less than for Drinking Water.

For Trade Waste the rise in revenue is due to the impacts of harmonisation, forecast growth and the indicative revenue path. Harmonisation is required to address the current situation where different rates are charged between the regions for the same type of discharge.

Revenues from Non Regulated Services in the Sunshine Coast region were not addressed in depth during the budget preparation due to establishment issues and are likely to have been understated. This has not affected the allocation of costs to these services. In the Moreton Bay region the level of income for Non Regulated Services in FY2009 is impacted by internal Community Service Obligations income that does not continue under the new arrangements for Unitywater. In Sunshine Coast the level of income for Non Regulated Services in FY2009 is impacted by Internal Sales revenue. Again this will not continue under Unitywater. In both cases care should be taken when comparing the forecast years to FY2009. Non Regulatory Services for FY2011 are covered in more detail in later sections.

Revenues from non-core and non-regulated activities are set out in the completed templates.

Unitywater has also provided a lower level of detail in the completed templates for FY2011 with each of the major revenue items within Utility Charges (e.g. Water Access), fees and charges (e.g. Connection Fees) and other revenue specified. Where possible the quantity and average price are also given. Minor items are grouped together (e.g. Other Fees and Charges). The current legacy billing systems do not allow easy identification of the number of customers or other quantifiable information in relation to these other fees and charges, although the amount of revenue is minor when compared to utility charges.

The information requirement calls for entities to allocate revenue from other sources to deemed categories, and identify revenues that will offset prices/revenues and those that will not.

There are some other revenues received such as fees and charges for water connections that are used to offset revenue requirements from Utility Charges.

5.3 Classification by Customer Groups

For the Utility Charge Revenue in the Sunshine Coast region the sourced Council database information used in the price modelling provided the split between Residential and Non Residential customers. For Utility Charge Revenue in the Moreton Bay region the sourced Council database information used in the price modelling did not provide the split between Residential and Non Residential customers. The percentage split of revenue between residential and non residential customers from the most recent utility charge invoices issued by the Councils for both water and sewerage was obtained and applied to the revenue projections.

The only Commercially Negotiated Agreements were in relation to recycled water and this category has only been used for this service.

Information on the split of other revenue between the categories is not available from the previous Council systems so for this submission this has all been allocated to the 'Other' category.

⁷ Unitywater is yet to determine its proposed price path.

5.4 Tariff Structure

For FY2011, Unitywater retained the tariff structures that were applied by the Moreton Bay and Sunshine Coast Regional Councils in FY2010, with the exception of:

- Separating out the bulk water charge on the utility charge notice;
- Moving to equalise the pricing level for residential customers within each region (leading to different percentage price increases within each district in the Moreton Bay region due to the need to bring together different water base charges and different sewerage charges);
- Increasing the pricing level for non-residential customers within each district by the percentage increase applicable to residential customers in the respective district; and
- Passing on the increase in the bulk water charge in full (which will differ between the Moreton Bay region and Sunshine Coast region in accordance with the established price path advised by the Queensland Government).

Unitywater will make decisions about changes to tariff structure once pricing principles have been established by the Authority.

5.5 Forecast Revenue versus MAR

The current year is Unitywater's first year of setting prices. In doing so, Unitywater inherited existing tariff structures and price levels from Councils.

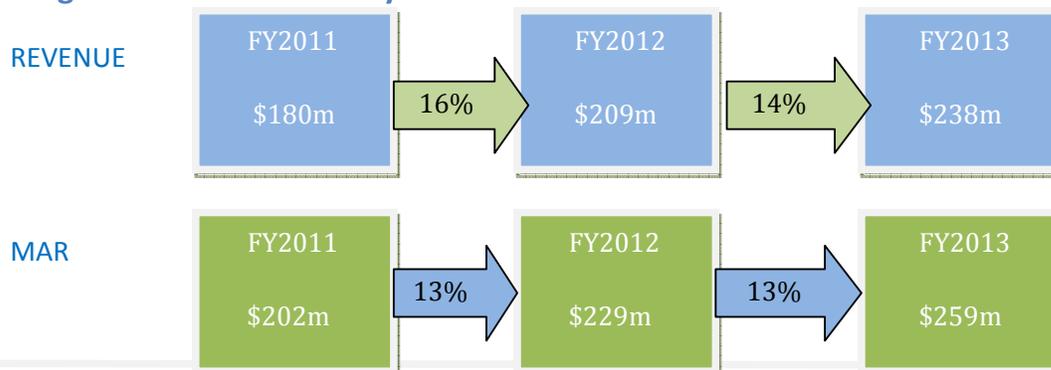
Furthermore, Unitywater was required to set prices based on very limited information about its anticipated MAR, and amidst uncertainty about key parameters such as the opening RAB. This knowledge has grown since prices were originally modelled in March 2010, as the organisation has developed and refined its cost projections. Changes until the adoption of the budget in June 2010 are reflected in final expenditure budgets, the estimated MAR and this information return.

The estimated MAR for this information return is some \$48M above the forecast revenue for FY2011. Unitywater has chosen to limit price increases to those originally calculated, rather than increase prices further to recover the estimated MAR. The final MAR will be subject to refinement for FY2011 given the opening RAB is indicative and is to be finalised during the year.

As set out above, it is intended to recover the shortfall (based on actual revenues received and the MAR based on the final RAB) through a NPV neutral price path, which is yet to be determined. In the meantime, an indicative revenue path is provided for the interim price monitoring period.

The level of under recovery for the three years of budget forecasts for the Water Activity is indicated in the following illustration (based on the indicative revenue path):

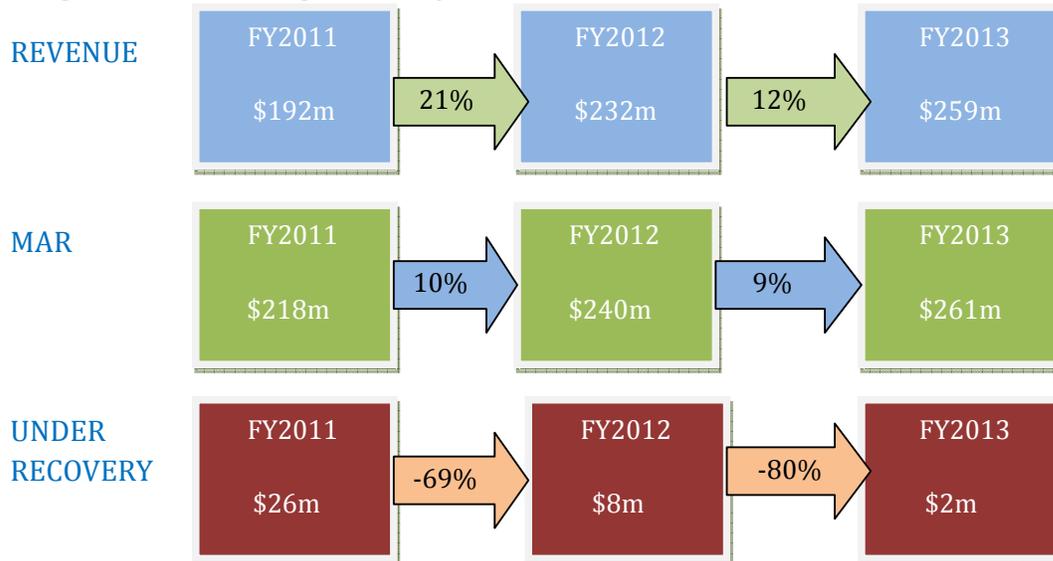
Diagram 5 Water Activity – Forecast revenue Vs MAR





The level of under recovery for the three years of budget forecasts for the Sewerage Activity is indicated in the following illustration (based on an indicative revenue path):

Diagram 6 Sewerage Activity – Forecast revenue Vs MAR



These figures are prior to finalisation of the price path strategy as discussed above.

Section 6 Service standards

This section sets out Unitywater’s current approved service standards, the past service standards approved by the regulator, and information about the date at which service standards may change.

6.1 Definitional issues

Unitywater is required to provide details relevant to each deemed category and for customer groups.

In terms of the *information for deemed categories*, this section provides details of service standards, and presents those service standards by activity (water and sewerage) and geographic area, and in relation to core services.

In terms of *customer groups*, in general the same service standards apply across all customer groups. The Authority’s definition of Customer Group includes customers with commercially-negotiated arrangements or where customers’ prices are not included in the entity’s pricing schedule. Unitywater does not have separate contractual arrangements with customers in relation to these activities and core services, although it does

have customer-specific arrangements for trade waste in some instances. These agreements are effectively an approval to discharge to the sewer network, and are conditions based. Service standards effectively relate to the acceptable quality and quantities/flow rates accepted. This information return does not set out the details of each agreement, although these can be provided if required.

Unitywater does have a contract in relation to the supply of recycled water to a commercial customer (classified as other core services). This contract sets contract-specific service standards that are specific to the recycled water plant, and hence do not have implications beyond that asset to the remaining customer base.

Unitywater does not have, nor intends to have, formal service standards in relation to unregulated services, although it should be noted that laboratory services must comply with the standards required for accreditation.

The Authority's guideline for templates states that the Authority has not predetermined the service standards and that entities should provide information about the service standards that are approved by other agencies or otherwise required by councils. Accordingly, the scope of service standards considered in this section relates to the Customer Service Standards (CSS) required under the *Water Supply (Safety and Reliability) Act* and those expressed in Strategic Asset Management Plans (SAMPs).

Drinking water quality standards have been interpreted as outside of the scope of the information requirement, and not included, as this is a non-discretionary regulatory requirement. Furthermore, water treatment and quality management occurs upstream in the supply chain.

Levels of service as defined in the SEQ Water Strategy have also been interpreted as out of scope as they are not controlled by Unitywater, but rather managed by the QWC through its central planning function.

There are also design standards aimed to generate asset performance outcomes, some of which relate to service aspects such as supply continuity. These standards were set through codes or policies under Council planning schemes, and include the water and sewerage design manual for each former Council. Subsequent amendments to the *SEQ Water Supply (Distribution Retail) Restructuring Act 2009* require Unitywater and the other distribution/retail businesses to collaborate on the preparation and implementation of a single SEQ Design and Construction Manual to be adopted before 1 July 2013. However, these are not considered service standards for the purpose of this information requirement.

Unitywater is also required to provide details of contractual service standards, or changes in contractual service standards, between the WGM and the distribution/retail entity. These are addressed in the sections below.

6.2 Past service standards as approved by other agencies

Unitywater is required to provide details of service standards for each year 1 July 2008 to 30 June, 2010, as approved by other agencies.

The following sections set out the service standards as applied in each of the two Councils.

6.2.1 Service Standards for Sunshine Coast Regional Council

Service standards approved by other agencies

Following the amalgamation of the former Noosa, Maroochy and Caloundra councils in March 2008, a single CSS was approved by the Sunshine Coast Regional Council in February 2009. Sunshine Coast Regional Council

then submitted those standards to DERM for approval by March 2009, and DERM approved the new CSS in June 2009.

The details of these standards and how they evolved over time are set out in working papers to the information return.

In addition, the Sunshine Coast Regional Council adopted the following as their CSS (these measures are not included in the SAMP):

- Standard water connection: within 10 working days;
- Standard sewerage connection: within 10 working days;
- Repair to water service: 5 working days; and
- Answer to enquiries: promptly.

WGM contractual service standards

The Grid Market Rules and associated contract between the Sunshine Coast Regional Council and the WGM set out the requirements for the supply of water into the network. Sunshine Coast Regional Council was a customer under this contract.

There are a variety of service arrangements that are set in these rules and subordinate documents, including Operating Protocols. Importantly, the Grid Market Rules also require various grid entities to share and consult on their SAMPs.

The Grid Market Rules are public documents, and Unitywater can provide to the Authority (along with other related documents) upon request.

6.2.2 Service Standards for Moreton Bay Regional Council area

Service standards approved by other agencies

Each of the former councils of Caboolture, Redcliffe and Pine Rivers had different CSS in March 2008. Moreton Bay Region Council did not adopt a unified CSS for FY2009, but continued to maintain the CSS of the former councils on a district basis. These CSS were previously approved by DERM.

A single service standard across the region was adopted for FY2010, and approved by DERM as part of its approval of the SAMP, on 7 April, 2009.

The details of these standards and how they evolved over time are set out in working papers to the information return.

SEQ Water Grid Manager

The same arrangements apply with the SEQ Water Grid Manager as for Sunshine Coast Regional Council.

6.3 Service standards 1 July 2010 to 30 June 2013

Unitywater is required to describe its service standards to apply over the course of the interim price monitoring period.

Service standards approved by other agencies

The legislation for the water reform will transition the SAMPs and related service standards and CSS from both Councils to Unitywater. Accordingly, these service standards apply from 1 July, 2010 until changed. Expenditure forecasts are also based on these standards continuing. The CSS described above continue to apply in relation to connections, enquiries and repairs.

In respect to complaint handling, the AS ISO 10002-2006 Customer satisfaction – Guidelines for complaints handling in organisations (ISO 1002:2004, MOD) continues to apply. The other aspects to service standards contained in the SAMP are set out in the table below.

Table 10 Current Service Standards

| Description | Service | Region | Unit of measurement | Standard |
|--|----------------|-----------|--------------------------|----------|
| Number of incidents per 100 km of main causing unplanned interruptions | Drinking water | MBRC Area | incidents/100km main/ yr | <10 |
| Percentage of unplanned service interruptions restored within 5 hrs | Drinking water | MBRC Area | % | >95 |
| Percentage of connections experiencing 1 interruption | Drinking water | MBRC Area | % | <10 |
| Percentage of connections experiencing 2 interruptions | Drinking water | MBRC Area | % | <3 |
| Percentage of connections experiencing 3 interruptions | Drinking water | MBRC Area | % | <1 |
| Percentage of connections experiencing 4 interruptions | Drinking water | MBRC Area | % | <0.2 |
| Percentage of connections experiencing 5 or more interruptions | Drinking water | MBRC Area | % | <0.1 |
| Average interruption duration | Drinking water | MBRC Area | Hours | <3 |
| Percentage of times response on-site were within 3 hrs | Drinking water | MBRC Area | % | >95 |
| Percent of connections with verified deficient flow or pressure | Drinking water | MBRC Area | % | <0.1 |
| Compliance with Australian Drinking Water Guidelines – Microbiological | Drinking water | MBRC Area | % | >98 |
| Compliance with Australian Drinking Water | Drinking water | MBRC Area | % | >98 |

| Description | Service | Region | Unit of measurement | Standard |
|---|-----------------------|-----------|-----------------------------------|----------|
| Guidelines - Colour < 15 NHU | | | | |
| Compliance with Australian Drinking Water Guidelines - Turbidity <1 NTU | Drinking water | MBRC Area | % | >98 |
| Compliance with Australian Drinking Water Guidelines | Drinking water | MBRC Area | % | >98 |
| Drinking water quality complaints per 1000 connections | Drinking water | MBRC Area | complaints/ 1000 connections/ yr | <10 |
| Drinking water quality incidents per year | Drinking water | MBRC Area | Number | <250 |
| Sewerage overflows to customer property per 1000 connections per year | Waste-water via Sewer | MBRC Area | overflows/ 1000 connections/ yr | <10 |
| Odour complaints per 1000 connections per year | Waste-water via Sewer | MBRC Area | complaints/ 1000 connections/ yr | <3 |
| Percentage of times response on-site were within 3 hrs | Waste-water via Sewer | MBRC Area | % | >95 |
| Water main breaks per 100 km main per year | Drinking water | MBRC Area | breaks/100km main/ yr | <15 |
| Water losses in litres/connection/day | Drinking water | MBRC Area | litres/ connection/ day | <100 |
| Sewer main breaks/blockages per 100 km main per year | Waste-water via Sewer | MBRC Area | breaks/ blockages/ 100km main/ yr | <18 |
| Sewer inflow/infiltration - ratio of peak day flow to average day flow | Waste-water via Sewer | MBRC Area | ratio | <5:1 |
| Number of incidents causing an unplanned interruption per 100 km of main per year | Drinking water | SCRC Area | number/ 100km main/yr | <30 |
| Restoration of services within 5 hours following a Priority 1 Event | Drinking water | SCRC Area | % | >90 |
| Ratio of planned to unplanned maintenance | Drinking water | SCRC Area | Ratio | 0.5 |
| Response time to Priority 1 Events within 1 hour | Drinking water | SCRC Area | % | >95 |
| Minimum flow expectation at boundary | Drinking water | SCRC Area | metres | 20 |
| Percentage of tests that comply with Australian Drinking Water Guidelines for the reticulation systems over twelve months: e coli | Drinking water | SCRC Area | % | >98 |
| Percentage of tests that comply with Australian Drinking Water Guidelines for the reticulation systems over twelve months: | Drinking water | SCRC Area | % | >99 |

| Description | Service | Region | Unit of measurement | Standard |
|--|---------------------------------|-----------|-------------------------------------|----------|
| Colour <15NHU | | | | |
| Percentage of tests that comply with Australian Drinking Water Guidelines for the reticulation systems over twelve months: turbidity <5NTU | Drinking water | SCRC Area | % | >99 |
| Number of drinking water quality complaints per 1000 connected water properties per year | Drinking water | SCRC Area | number/1000connected properties/ yr | <10 |
| Number of drinking water quality incidents, per 1,000 connected water properties, per year | Drinking water | SCRC Area | number/1000connected properties/ yr | <5 |
| Total sewage overflows per 100km of main per year | Waste-water via Sewer | SCRC Area | number/ 100km of main/ yr | <8 |
| Number of sewage overflows to customer property per 1000 connected sewerage properties per year | Waste-water via Sewer | SCRC Area | number/1000connected properties/ yr | <2 |
| Number of odour complaints per 1000 connected sewerage properties per year | Other Core Waste-water Services | SCRC Area | number/1000connected properties/ yr | <3 |
| Response time to Priority 1 Events within 1 hour | Waste-water via Sewer | SCRC Area | % | >95 |
| Restoration of services within 5 hours following a Priority 1 Event | Waste-water via Sewer | SCRC Area | % | >90 |
| Number of water main breaks and leaks per 100 km of main per year | Drinking water | SCRC Area | number/ 100km of main | <25 |
| Reticulated water supply system loss percentage (unaccounted for water) | Drinking water | SCRC Area | % | <11 |
| Number of sewer main breaks and chokes per 100 km of main per year | Waste-water via Sewer | SCRC Area | number/ 100km of main / yr | <40 |
| Sewer inflow / infiltration – ratio of peak day flow to average day flow | Waste-water via Sewer | SCRC Area | Ratio | <3 |

SEQ Water Grid Manager Contract

To date, no material changes in service standard have occurred for the supply of water from the grid to Unitywater, although this is subject to any changes to the Grid Market Rules.

6.4 Changes to service standards

Unitywater is required to provide details of the expected date at which any change to service standards is to take place, and the standards that would apply before and after that change.

Changes initiated by Unitywater

Unitywater is required to submit an updated SAMP (including CSS) by FY2012 under the *Water Supply (Safety and Reliability) Act 2008*. Unitywater has commenced the development of a common service standard across its service area, and expects these will commence from 1 July, 2011. In development these new standards, Unitywater has considered a range of matters including:

- DERM's "Guidelines for Preparing Customer Service Standards"
- Historic and projected performance against current standards
- Benchmarking of performance against the Queensland Water Directorate State-wide Water Information Project (SWIM) 2008/2009 comparative data report
- Benchmarking of performance against the WSAA National Performance Report (NPR) for 2007/2008
- Review of GHD Water Reform Program Final Report Due Diligence - Technical Module (Key Activities 1.4.11 Levels of Service and 1.4.13 Technical Performance Indicators)
- Review of other SEQ water service provider's service standards
- Determining specific measures in terms of accuracy, realistic application and achievability, cost and timeliness in terms of what would be reasonably acceptable to the customer

Until this review is complete and the new service standards approved by DERM, the standards set out above will continue.

The information return requires information about the standards that would apply after the change. The table below describes the changed service standard as is currently being considered. This should only be considered indicative at this stage, until such time as the final standards are developed by Unitywater and submitted and approved by DERM as part of the SAMP approval.

Table 11 Indicative future service standards

| Description | Service | Region | Unit of measurement | Standard |
|---|----------------|-----------------|---------------------------|-------------|
| Response time to Priority 1 Events within 2 hours | Drinking water | Unitywater Area | % | >85 |
| Restoration of services within 5 hours following a Priority 1 Event | Drinking water | Unitywater Area | % | >85 |
| Unplanned interruptions to supply | Drinking water | Unitywater Area | number/100 km of main/ yr | <20 |
| Ratio of planned to unplanned interruptions – Water | Drinking water | Unitywater Area | Ratio | 0.15 to 0.3 |
| Water main breaks and leaks (SAMP target, not CSS) | Drinking water | Unitywater Area | number/100 km of main/ yr | <20 |
| System water loss (SAMP target not CSS) | Drinking water | Unitywater Area | litres/connection/ day | <100 |
| Water pressure at property boundary | Drinking water | Unitywater Area | kPa | >200 |
| Percentage of tests that comply with Australian Drinking Water Guidelines for the reticulation systems over twelve months: e coli | Drinking water | Unitywater Area | % | >98% |
| Percentage of tests that comply with | Drinking water | Unitywater | % | >98% |

| Description | Service | Region | Unit of measurement | Standard |
|--|-----------------------|-----------------|--|-------------|
| Australian Drinking Water Guidelines for the reticulation systems over twelve months: Colour <15NHU | | Area | | |
| Percentage of tests that comply with Australian Drinking Water Guidelines for the reticulation systems over twelve months: turbidity <1NTU | Drinking water | Unitywater Area | % | >98% |
| Drinking water quality complaints | Drinking water | Unitywater Area | number/1000 connections/ yr | <5 |
| Water quality incidents | Drinking water | Unitywater Area | number/1000 connections/ yr | <2 |
| Response time to Priority 1 Events within 2 hours | Waste-water via Sewer | Unitywater Area | % | >85% |
| Restoration of services within 5 hours following a Priority 1 Event | Waste-water via Sewer | Unitywater Area | % | >85% |
| Sewage overflows | Waste-water via Sewer | Unitywater Area | number/100 km of main / yr | <20 |
| Sewage overflows to customers property | Waste-water via Sewer | Unitywater Area | number/1000 connected properties/ yr | <5 |
| Odour complaints | Waste-water via Sewer | Unitywater Area | number/1000 connection / yr | <3 |
| Sewer main breaks and chokes (SAMP target, not CSS) | Waste-water via Sewer | Unitywater Area | number/100 km of main / yr | <40 |
| Sewer inflow and infiltration (SAMP target, not CSS) | Waste-water via Sewer | Unitywater Area | Ratio of peak day flow to average day flow | 3.5 |
| Response time to Priority 1 Events within 2 hours | Drinking water | Unitywater Area | % | >85 |
| Restoration of services within 5 hours following a Priority 1 Event | Drinking water | Unitywater Area | % | >85 |
| Unplanned interruptions to supply | Drinking water | Unitywater Area | number/100 km of main/ yr | <20 |
| Ratio of planned to unplanned interruptions – Water | Drinking water | Unitywater Area | Ratio | 0.15 to 0.3 |
| Water main breaks and leaks (SAMP target, not CSS) | Drinking water | Unitywater Area | number/100 km of main/ yr | <20 |
| System water loss (SAMP target not CSS) | Drinking water | Unitywater Area | litres/ connection/day | <100 |
| Water pressure at property boundary | Drinking water | Unitywater Area | kPa | >200 |
| Percentage of tests that comply with Australian Drinking Water Guidelines for the reticulation systems over twelve months: e coli | Drinking water | Unitywater Area | % | >98% |

Other change triggers

Unitywater is required to compile a unified service standard to be articulated in its Water Netserv plan, which will replace the SAMP and other plans. The implications of this plan are unclear at this early stage, and expenditure forecasts do not incorporate any assumptions about changes to standard of cost.

It is also possible that a Customer Code will be introduced for SEQ, which may necessitate changes to the CSS. Changes to the Grid Market Rules and subordinate arrangements could also have implications for service standards, although Unitywater is not aware of any such changes at this point in time.

Contract with the WGM

The SEQ Water Market Rules define the obligations of water grid participants, including Unitywater. From 1 July 2010, Unitywater is a customer of the WGM. The service standards detailed in the SEQ Water Grid Rules are general or overarching requirements. Specific, detailed service standards will be specified in the Operational Protocol, Grid Instructions, and Water Grid Performance Standard.

Section 7 Demand

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section describes Unitywater's demand forecasts used to set its budgeted revenues, and for planning for growth capital expenditure.

In terms of historic data, demand information is not yet available from both Councils for FY2009, and Unitywater is currently engaging with Councils on this matter. Accordingly, no demand data for that year has been provided.

7.1 Water demand

The following table summarises the available historic information on water demands, and Unitywater's current forecasts.

Table 12 Water demand (ML)

| | | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|-----------------------|------------------|-------------------|-------------------|--------|--------|--------|
| Moreton Bay Region | Demand | Not Yet Available | 21,329 | 21,992 | 22,198 | 24,096 |
| | Change in Demand | Not Applicable | Not Yet Available | 3.1% | 0.9% | 8.6% |
| Sunshine Coast Region | Demand | Not Yet Available | 23,817 | 26,729 | 27,043 | 27,191 |
| | Change in Demand | Not Applicable | Not Yet Available | 3.5% | 1.2% | 0.5% |

The forecasts were referenced from the current customer databases and the forecasts supplied by Councils as part of the Water Reform Program due diligence exercise. The later formed the base for the demand in the Enterprise Financial Model.

Note there is some uncertainty with these forecasts. This uncertainty arises not just as a result of climatic conditions, but more significantly from shifting community attitudes towards water. Forecasting over the next 1-3 years will be difficult as the Moreton community exit a regime of severe restrictions to milder, permanent restrictions, whilst the Sunshine Coast face the introduction of permanent water conservation measures in the region. How these communities might respond to the changing circumstances is difficult to gauge. This has resulted in forecasts that are not just a reflection of anticipated population increases.

Unitywater will revise and improve upon these forecasts over the price monitoring period, as the business gains more operational experience and information and as demand under the new permanent conservation measures (applied by the Queensland Water Commission) becomes clearer.

Bulk water purchases due to system losses have also been forecast. The following table shows these losses and the loss factor used:

Table 13 Loss factors (ML)

| | | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|-----------------------|---------------|-------------------|--------|--------|--------|--------|
| Moreton Bay Region | System Losses | Not Yet Available | 3,412 | 3,518 | 3,551 | 3,855 |
| | Loss Factor | | 13.8% | 13.8% | 13.8% | 13.0% |
| Sunshine Coast Region | System Losses | Not Yet Available | 4,130 | 4,276 | 4,327 | 4078 |
| | Loss Factor | | 13.8% | 13.8% | 13.8% | 13.0% |

The 13.8% loss factor is based on an analysis of actual losses during 2009 in Moreton Bay. This loss factor is the best available information to Unitywater, and has been applied across the entire network. Unitywater engaged an economic consultant to undertake indicative price modelling and in doing so, considered a number of assumptions, including a reduction in the loss factor due to system leakage management improvements. This reduction is forecast to start in FY2013 reducing from the loss factor of 13.8% to a factor of 13.0%. These assumptions will need to be validated and refined as Unitywater obtains more information over the following years.

The consultant also undertook forecasts using the concept of 'Equivalent Base Charge Customers' as the basis for estimating access charge revenue. The following table shows the forecast for both regions:

Table 14 Water demand forecast (equivalent base charge for customers)

| Equivalent Base Charge Demand Forecast for Water Customers | FY2010 | FY2011 | FY2012 | FY2013 |
|--|---------|---------|---------|---------|
| Moreton Bay | 141,208 | 144,597 | 148,067 | 151,621 |
| Change in Demand | | 2.4% | 2.4% | 2.4% |
| Sunshine Coast | 140,910 | 143,728 | 146,603 | 149,535 |
| Change in Demand | | 2.0% | 2.0% | 2.0% |

The detailed assumptions used by the consultant in providing this forecast are provided as part of the completed templates.

7.2 Demand for sewerage services

Sewerage demand figures were forecast by the consultant using the same concept of 'Equivalent Base Charge Customers'. The following table shows the forecast for both regions:

Table 15 Sewerage demand forecast (equivalent base charge customers)

| Equivalent Base Charge Demand Forecast for Sewerage Customers | FY2010 | FY2011 | FY2012 | FY2013 |
|---|---------|---------|---------|---------|
| Moreton Bay Region | 143,733 | 147,183 | 150,715 | 154,333 |
| Change in Demand | | 2.4% | 2.4% | 2.4% |
| Sunshine Coast Region | 145,015 | 147,915 | 150,873 | 153,891 |
| Change in Demand | | 2.0% | 2.0% | 2.0% |

No volume forecasts are made because sewerage charges, unlike water, are not volumetrically based. Even in those areas (Sunshine Coast) where volumetric charges apply to selected larger industrial customers, they are calculated as a percentage of measured water consumption, rather than from continuous direct monitoring of sewage flows. The forecast of demand for revenue purposes is by and large based on the number of pedestals.

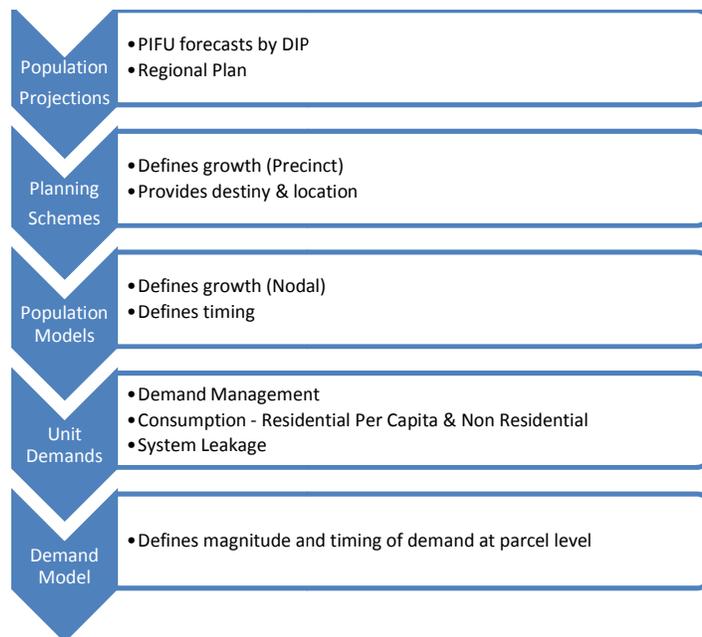
For the purposes of breaking down water and sewerage between customer groupings (Residential and Non-Residential) the percentage split used for capital expenditure planning (described below) has been used. This is reflected in the completed templates.

7.3 Demand Forecasting for Capital Planning

Forecasts are also made to enable planning for capital expenditure. These forecasts are based on projected populations, planning scheme requirements and unit demands for both residential and non-residential consumers.

The method used to derive forecast demands for water and sewerage core services is illustrated in the diagram below;

Diagram 7 Demand Projection Process Chain



**PIFU – Planning and Forecasting Information Unit, DIP – Department of Infrastructure and Planning*

In essence, the process chain can be described as follows;

Link 1

Regional population projections are provided by the Planning and Forecasting Information Unit of the Queensland Department of Infrastructure Planning. These projections, along with the SEQ Regional Plan, set out the population growth and the urban footprint for the region.

Link 2

Overlaying this is the Council Planning Scheme. The Planning Scheme sets out in more detail – down to the precinct level – where development can occur, the type of development, and the acceptable density of

development. In the near future, the Planning Scheme is also likely to incorporate Total Water Cycle Management measures that the Council would like to see adopted.

Link 3

From the Planning Scheme, a Population Model is prepared that defines growth down to the level of individual allotment. Importantly, the population model needs to make assumptions – at the allotment level - about when such growth might occur.

Link 4

Unit demands have been determined for both residential and non-residential consumption. For residential consumption, unit demands are assessed at 230 litres per capita per day. For non-residential consumption, unit demands are expressed in terms of either allotment area for industrial development (i.e. 25 equivalent persons per hectare) or floor area for commercial development (i.e. 5 equivalent tenants per 100 sqm gross floor area).

Link 5

A demand model is prepared that sets out existing and future water and sewerage demands – at the level of the parcel – covering the whole of the serviced region. This demand model becomes the major input to the growth related capital planning process.

Link 6

Demand projections are made by the model for 5 year periods for up to 20 years.

The demand projections derived via this method will generally be more conservative (i.e. higher) than for shorter-term demands because:

- It assumes full occupancy of residential and tourist facilities. This reflects the higher loads experienced during holiday periods which govern the sizing of infrastructure;
- In some locations, a demand factor on the 230 L/c/d has been applied to cover the longer term uncertainty of current consumption trends. This is the case at Moreton, although not presently at the Sunshine Coast. It is anticipated that over time a consistent load factor will be developed and applied across the extended region; and
- It assumes that land with current Development Approval proceeds to market over the next 5 years.

The demand projections used for the purposes of planning future capital infrastructure are not at the granular short term forecast level. Instead, these demands include provisions for higher than average annual populations, and in some cases, where there is uncertainty in relation to consumption trends, they will include higher than average annual consumption.

Section 8 Regulatory asset base

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section sets out how the opening RAB at 1 July, 2010 was calculated, and the reasons that this value has been adopted as an interim RAB. The section also sets out the RAB roll-forward over the price monitoring period.

8.1 General approach

The opening RAB as at 1 July 2008 has been reconciled to the asset values for each Council, as advised by the Minister, and pro-rated based on the written down value. Due to information constraints explained later in this section, the current RAB is an interim value. For the purposes of this information return the revenue offset method for calculation of the RAB has been adopted for FY2011 to FY2013 (noting that revenue offset is deemed for the preceding years).

The Authority has issued a revised model in mid August with amendments to the calculation to the RAB roll-forward, however this was not received in time to utilise for the current information return. Unitywater has therefore performed its own calculation based on the information report requirements.

Unitywater has adopted a disaggregated approach to valuing the RAB for regulatory purposes where possible. This means that individual asset details have been maintained and directly attributed to regulatory services and asset classes. For historic periods the asset values used have been sourced from the Councils' financial statement notes.

It has been assumed (based on historic capitalisation) that 65% of the projected capital expenditure will be capitalised at year end for the forecasted period FY2011 to FY2013. Only capitalised expenditure is added to the RAB roll forward. In calculating the revenue allowance, it was assumed that asset acquisitions and developer provided assets occur mid-year and are added to the opening regulated asset base accordingly.

8.2 RAB Information Gaps

In the process of validating Councils' data for the roll-forward period, a number of interpretation issues and information gaps were identified. These issues are summarised in the table below.

Table 16 Information Gaps

| Issue | RAB Component | Approach | Issue Identified | Information GAP | Required Action |
|-------|---------------|----------|------------------|-----------------|-----------------|
|-------|---------------|----------|------------------|-----------------|-----------------|

| Issue | RAB Component | Approach | Issue Identified | Information GAP | Required Action |
|-------|--------------------------------|--|---|--|---|
| 1 | Opening asset base 1 July 2008 | Opening balances agreed to accounting written down value and grossed up/down to Minister's advised value. | Interim financial statements provided by Moreton Bay Regional Council. Sunshine Coast Regional Council required back-solving from 30 June 2009 as no statements were produced at 30 June 2008. | Interim statement values and back-solved written down values were not all supported by individual asset detail. | Unitywater request to Councils to substantiate reported values with individual asset details and assess the accuracy of individual asset classes. |
| 2 | RAB roll-forward 1 July 2009 | Acquisitions, developer provided assets and disposals agreed to Financial Statements in aggregate. | Moreton Bay asset acquisitions and developer provided assets | Moreton Bay Regional Council assets as provided in Financial Statements not supported by individual asset detail (developer provided assets \$19M and asset acquisitions \$8m – estimate 2% of RAB) | Unitywater request to Councils to substantiate reported values with individual asset details and assess the accuracy of individual asset classes. |
| 3 | RAB roll-forward 1 July 2010 | Estimated acquisitions and disposals based on Q3 estimates and estimated work in progress to be completed as at 30 June 10 | Moreton Bay Regional Council large outstanding balances for work in progress and no developer provided assets recognised at March. No detail for SC acquisitions and developer provided assets. | Linking of work in progress balances to complete transferred assets. Lack of individual asset detail. | Unitywater request to Councils to substantiate reported values with individual asset details and assess the accuracy of individual asset classes. |
| 4 | Establishment Costs | Establishment costs to be recognised when actual FY2010 results become available. | Quantum and treatment of establishment costs are not clear. QCA templates show establishment costs as operating expenditure where as Interim Price Monitoring Requirements classify as capital. | No establishment costs included in information templates but this to be rectified when the value is finalised and the pricing treatment confirmed. | Confirm value of establishment costs with Councils based on actual results, clarify with QCA re treatment of these costs in price monitoring templates and method of amortisation if costs are to be capitalised. |

In general, Unitywater is concerned that the information used to establish the RAB at 1 July, 2010 is accurate and subject to independent audit. This can occur through the process to determine final equity shares for each Council, where the Minister has directed that participating Councils' equity rights will be determined on the basis of Councils' relative proportion of the roll-forward regulated asset base as at 30 June 2010. In order to do this Unitywater is charged with validating the Councils' RAB by the 31st December 2010.

The results of this assessment are then to be issued to the Board of Unitywater and participating Councils for comment. This information will then be passed to the Minister for final determination of the RAB and flowing quantum of equity rights. It is envisaged that such a determination will not be made until February/March 2011. To achieve this outcome Unitywater will be addressing the issues tabled in order to validate the RAB value. For the purposes of this information return Unitywater has submitted the RAB information as provided by Councils with an estimate of FY2010 movements.

8.3 Initial RAB 1 July 2008

Initial RAB values have been reconciled to the Minister's advised values in accordance with the recommended approach by the Authority. This means that the accounting written down values by individual asset have been grossed up or down to the Minister's advised values, being \$2,029,870 for both Councils' assets.

As financial statements were not produced, or required, at 30 June 2008, the Sunshine Coast Regional Council's accounting written down value was rolled forward from financial statements ending 13 March 2008.

In the case of Moreton Bay Regional Council, interim financial statements were provided. As noted above in relation to information gaps, the accounting written down value agrees in aggregate by asset class, however the detailed asset listing did not agree. For the purposes of this information return the statement value was used and unsupported data was categorised as "other distribution infrastructure".

The following table displays the initial RAB as at 1 July 2008.

Table 17 Initial RAB 1 July 2008

| OPENING ASSET BASE | Numeration | Geographic Area | | Total |
|---|---------------|--------------------|---------------------|--------------------|
| | | 1 Moreton Bay | 2 Sunshine Coast | |
| WRITTEN DOWN VALUE as at 1 July 2008 | | | | |
| Total WDV (accounting values) as at 1 July 2008 | \$'000 | 1,019,414.0 | 1,477,807.5 | 2,497,221.5 |
| REGULATORY ASSET BASE VALUES as at 1 July 2008 | | | | |
| Water: | | | | |
| Drinking water | \$'000 | 477,409.4 | 344,103.4 | 821,512.9 |
| Other core water services | \$'000 | 3,657.5 | 24,137.5 | 27,795.0 |
| Aggregate non-core water services | \$'000 | 0.0 | 0.0 | 0.0 |
| Wastewater: | | | | |
| Wastewater via sewer | \$'000 | 628,419.9 | 551,429.4 | 1,179,849.2 |
| Trade waste | \$'000 | 7.9 | 27.8 | 35.6 |
| Other core wastewater services | \$'000 | 0.0 | 0.0 | 0.0 |
| Aggregate non-core wastewater services | \$'000 | 0.0 | 0.0 | 0.0 |
| Non-regulated: | | | | |
| Aggregate non-regulated services | \$'000 | 522.4 | 154.9 | 677.3 |
| Total RAB Value as at 1 July 2008 | \$'000 | 1,110,017.0 | 919,853.0 | 2,029,870.0 |

- Detailed files containing individual asset details allocated to services and asset classes have been provided separately to the Authority, along with supporting work papers.

8.4 RAB roll-forward 1 July 2010

Councils' RAB roll-forward data limitations and gaps are discussed above, and relate to the 1 July, 2010 roll-forward. Despite this, Unitywater has generated an indicative opening RAB at 1 July, 2010, based on indicative acquisition and disposal data for FY2010 from Council estimates sourced from Councils' third quarter budget reviews.

For the purposes of calculating the RAB roll-forward:

- Capital expenditure was identified on an individual asset basis and included estimated completed assets only;

- Indexation was applied globally to assets based on half year capitalised assets, developer provided assets and asset disposals;
Proportionate depreciation was calculated by individual asset based on acquisition date; and
- Establishment costs were not included as information about establishment costs is not yet finalised. These establishment costs will be integrated into the final RAB for 1 July, 2010.

The final opening RAB for 1 July, 2010 will be set once these and other matters discussed above are settled and Unitywater has final, audited information upon which to verify the opening value.

The table below provides a summary of the interim RAB roll-forward estimate to 30 June 2010.

Table 18 Summary RAB roll-forward 1 July 2010

| REGION \$(000) | Initial RAB 1 July 2008 as per Minister's advice | Add: Capital Expenditure | Less: Disposals | Less: Regulated Depreciation | Add: Indexation | RAB rolled forward 30 June 2010 Interim value |
|-------------------|---|--------------------------------|--------------------|------------------------------------|--------------------|--|
| Moreton Bay | 1,110,017 | 334,863 | | (61,297) | 55,548 | 1,439,131 |
| Sunshine Coast | 919,853 | 94,276 | (1,008) | (52,113) | 43,130 | 1,004,138 |
| Total | 2,029,870 | 429,139 | (1,008) | (113,410) | 98,678 | 2,443,269 |

8.5 RAB roll-forward 30 June 2013

The following table summarises the estimated RAB roll-forward for this period.

Table 19 Summary RAB roll-forward 30 June 2013

| REGION \$(000) | RAB rolled forward 30 th June 2010 | Add: Capital Expenditure | Less: Disposals | Less: Regulated Depreciation | Add: Indexation | RAB rolled forward 30 June 2013 |
|-------------------|---|--------------------------------|--------------------|------------------------------------|--------------------|---------------------------------------|
| Moreton Bay | 1,439,131 | 397,561 | | (119,446) | 142,940 | 1,860,186 |
| Sunshine Coast | 1,004,138 | 384,032 | | (88,141) | 87,690 | 1,387,719 |
| Total | 2,443,269 | 781,593 | | (207,587) | 230,630 | 3,247,905 |

Asset acquisitions for the period were based on Unitywater's budgeted capital expenditure projects, assuming 65% capitalisation at year end. This means that the assumed level of incomplete assets is then carried forward to the next year's asset acquisitions.

Negligible asset disposals are expected and Unitywater's initial budget did not provide for asset disposals.

Section 9 Capital Expenditure

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section describes Unitywater's capital expenditure for the current year, forecast expenditure for future years, and sets out the available information about past capital expenditure from Councils. The following table provides a summary of the capitalised expenditure as set out in the completed templates.

Table 20 Summary of assets capitalised

| REGION AND SERVICE \$m | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|---------------------------|-------------|--------------|--------------|--------------|--------------|
| Moreton Bay | 59.8 | 242.8 | 199.1 | 109.5 | 50.7 |
| DRINKING WATER | 20.3 | 40.5 | 18.4 | 19.3 | 12.2 |
| NON REGULATED | 0.0 | 6.2 | 0.5 | 0.2 | 0.2 |
| OTHER CORE WATER SERVICES | 11.9 | 13.1 | 0.9 | 1.5 | 1.6 |
| TRADE WASTE | 0.0 | 0.3 | 0.0 | 0.0 | 0.0 |
| WASTEWATER VIA SEWER | 27.7 | 182.7 | 179.2 | 88.4 | 36.6 |
| Sunshine Coast | 21.7 | 24.2 | 58.5 | 127.7 | 153.5 |
| DRINKING WATER | 7.4 | 9.9 | 13.1 | 22.3 | 22.2 |
| NON REGULATED | 0.1 | 0.4 | 0.0 | 0.0 | 0.0 |
| OTHER CORE WATER SERVICES | 0.0 | 0.0 | 5.9 | 8.9 | 3.5 |
| TRADE WASTE | 0.0 | 0.4 | 0.0 | 0.0 | 0.0 |
| WASTEWATER VIA SEWER | 14.2 | 13.5 | 39.5 | 96.5 | 127.8 |
| Grand Total | 81.6 | 267.1 | 257.5 | 237.2 | 204.1 |

The Authority's Ministers' Direction to the Authority requires that actual capital expenditure for the period 1 July 2008 to 30 June 2009 (including establishment costs and developer provided assets), be accepted as prudent and efficient. Unitywater has inherited a number of projects from Councils (identified as work in progress), although Councils are yet to provide sufficient details at an individual project level at the time the data templates were compiled. Unitywater submits that this expenditure inherited from Councils should be excluded from an assessment of prudence as it is outside Unitywater's control. Furthermore, Unitywater

submits that the cost of these inherited projects should not be subject to review where the costs were largely determined prior to 1 July, 2010 (e.g. contracts have been let).

9.1 Council capital expenditure

Unitywater has agreed Moreton Bay and Sunshine Coast asset acquisitions to Council financial statements in aggregate. The notes to financial accounts however could not be fully supported by individual asset details. In these cases the financial statement notes to accounts provide for water and sewerage activities separately and therefore an allocation of assets to activities was possible. For the purposes of this information return those unidentified assets have been disclosed as the asset class “distribution other”, and the cost driver has been assumed to be growth.

For the Moreton Bay region, specific data issues identified in relation to acquisitions and developer donated assets for the period were:

- Asset acquisitions agreed to statements in aggregate, however detailed acquisitions did not reconcile to financial statements for FY2009 (variance \$8m allocated to Water and Sewerage, 87% and 13% respectively with acquisition date assumed to be mid-year); and
- Although contributed assets (developer provided) agreed to financial statements in aggregate detail was provided therefore allocation between Water/Sewerage and recycled assets was based on notes from the financial accounts).

For FY2010 Councils’ third quarter budget estimates have been used. This information has been provided by project, however there are data issues relating to the correct classification of assets and cost drivers.

Linking of work in progress balances to correct classifications and obtaining reliable completion status for year end has also presented constraints in meeting the precise information requirements. Unitywater, after investigation with Council, has assumed a work in progress balance of \$87m for Moreton Bay region in FY2010. Disparate advice has been received from Sunshine Coast council and work in progress balances were not currently available. This issue will be rectified when actual audited results are received.

In both cases the work in progress value has been excluded from RAB calculations until the asset is complete and capitalised. Additionally, due to insufficient information, *no establishment costs have been capitalised at this point in the forecasted FY2010 results. Unitywater will amend capital expenditure with these values when actual expenditure becomes available.*

Due to data integrity issues as mentioned above, the RAB value, as at 1 July, 2010, will be updated when actual audited financial accounts are made available by Councils. Additionally the RAB value will not be finalised until Unitywater has final, audited information on the components for the opening RAB at 1 July, 2010.

For a list of information gaps, data integrity issues and RAB validation process, refer to Section 9.2 RAB information gaps.

9.2 Forecast capital expenditure

Unitywater has developed its capital expenditure program for FY2011 and outer years with reference to the need for the expenditure, and has categorised expenditure according to the drivers of growth, renewals,

improvements and compliance. Unitywater's program has also been developed having regard to its capacity to deliver, based on past performance and the availability of resources and contractors to perform the work.

Unitywater has provided a detailed breakdown of capital budgets for the forecast period FY2011 to FY2013. Working papers provide information by project. Unitywater expects that supplementary information will be made available once the Authority (and its appointed consultant) commences the review of capital expenditure in detail.

To facilitate consistency of measurement, Unitywater has assumed that capital expenditure incurred during a financial year will represent 65% completion of each asset project by year end. This assumption is based on historic trends of the two Councils.

The table below show how the capital expenditure for the period budgeted translates to the capitalised expenditure, and provides a summary by region of the values capitalised.

Table 21 Capitalisation \$M

| Region | Reconciliation | FY2011 | FY2012 | FY2013 |
|-------------------------|---------------------------------|--------------|--------------|--------------|
| Moreton Bay | WIP from prior year capitalised | 87.3 | 60.2 | 26.5 |
| | Add current year expenditure | 172.1 | 75.8 | 37.1 |
| | Less 35% assumed incomplete | (60.2) | (26.5) | (13.0) |
| | Capitalised | 199.1 | 109.5 | 50.7 |
| Sunshine Coast | WIP from prior year capitalised | | 31.5 | 51.8 |
| | Add current year expenditure | 90.0 | 148.0 | 156.4 |
| | Less 35% assumed incomplete | (31.5) | (51.8) | (54.7) |
| | Capitalised | 58.5 | 127.7 | 153.5 |
| Unitywater Total | WIP from prior year capitalised | 87.3 | 91.7 | 78.3 |
| | Add current year expenditure | 262.1 | 223.9 | 193.5 |
| | Less 35% assumed incomplete | (91.7) | (78.3) | (67.7) |
| | Capitalised | 257.6 | 237.2 | 204.1 |

The following table shows developer and Unitywater capitalised expenditure, by driver.

Table 22 Assets capitalised by region (including developer provided assets)

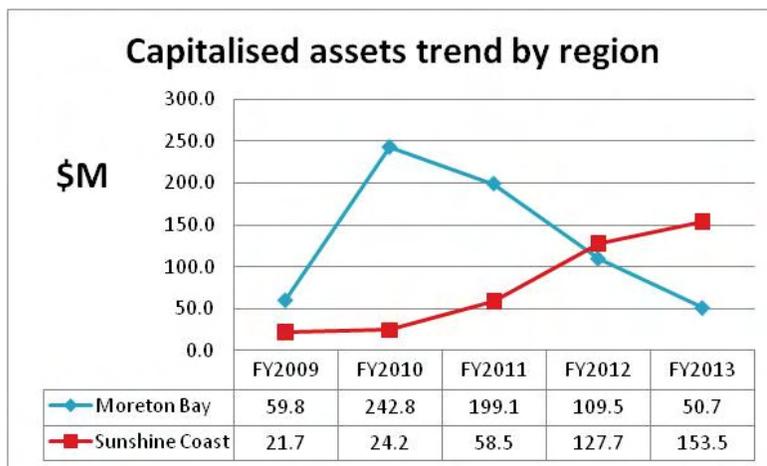
| Capitalised by Region \$m | Cost Driver | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|---------------------------|----------------------------------|-------------|--------------|--------------|--------------|-------------|
| Moreton Bay | New assets | 59.8 | 89.6 | 150.3 | 67.2 | 25.8 |
| | Renewal | 0.0 | 14.8 | 22.6 | 17.7 | 12.1 |
| | Improvements | 0.0 | 135.0 | 0.0 | 0.0 | 0.0 |
| | Business Improvements | 0.0 | 0.0 | 3.3 | 1.0 | 0.0 |
| | Infrastructure Improvements | 0.0 | 0.0 | 0.3 | 0.1 | 0.0 |
| | Compliance | 0.0 | 3.4 | 22.6 | 23.5 | 12.7 |
| | Total capital expenditure | 59.8 | 242.8 | 199.1 | 109.5 | 50.6 |
| | Developer Provided | 19.3 | 12.9 | 13.7 | 12.2 | 12.5 |

| | | | | | | |
|-----------------------|----------------------------------|--------------|--------------|--------------|--------------|--------------|
| | Total Capital Program | 79.2 | 255.7 | 212.8 | 121.7 | 63.1 |
| Sunshine Coast | New assets | 14.0 | 20.0 | 40.5 | 108.6 | 139.4 |
| | Renewal | 7.7 | 4.1 | 9.0 | 12.5 | 12.0 |
| | Improvements | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| | Business Improvements | 0.0 | 0.0 | 6.4 | 3.8 | 0.2 |
| | Infrastructure Improvements | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| | Compliance | 0.0 | 0.2 | 2.6 | 2.8 | 1.9 |
| | Total capital expenditure | 21.7 | 24.2 | 58.5 | 127.7 | 153.5 |
| | Developer Provided | 29.2 | 19.1 | 17.1 | 13.7 | 13.6 |
| | Total Capital Program | 50.9 | 43.4 | 75.6 | 141.4 | 167.1 |
| Unitywater | New assets | 73.8 | 109.6 | 190.8 | 175.8 | 165.2 |
| | Renewal | 7.7 | 18.9 | 31.6 | 30.2 | 24.1 |
| | Improvements | 0.0 | 135.0 | 0.0 | 0.0 | 0.0 |
| | Business Improvements | 0.0 | 0.0 | 9.7 | 4.8 | 0.2 |
| | Infrastructure Improvements | 0.0 | 0.0 | 0.3 | 0.1 | 0.0 |
| | Compliance | 0.0 | 3.6 | 25.2 | 26.3 | 14.6 |
| | Total capital expenditure | 81.6 | 267.1 | 257.6 | 237.2 | 204.1 |
| | Developer Provided | 48.5 | 32.0 | 30.8 | 25.8 | 26.1 |
| | Total Capital Program | 130.1 | 299.1 | 288.4 | 263.0 | 230.2 |

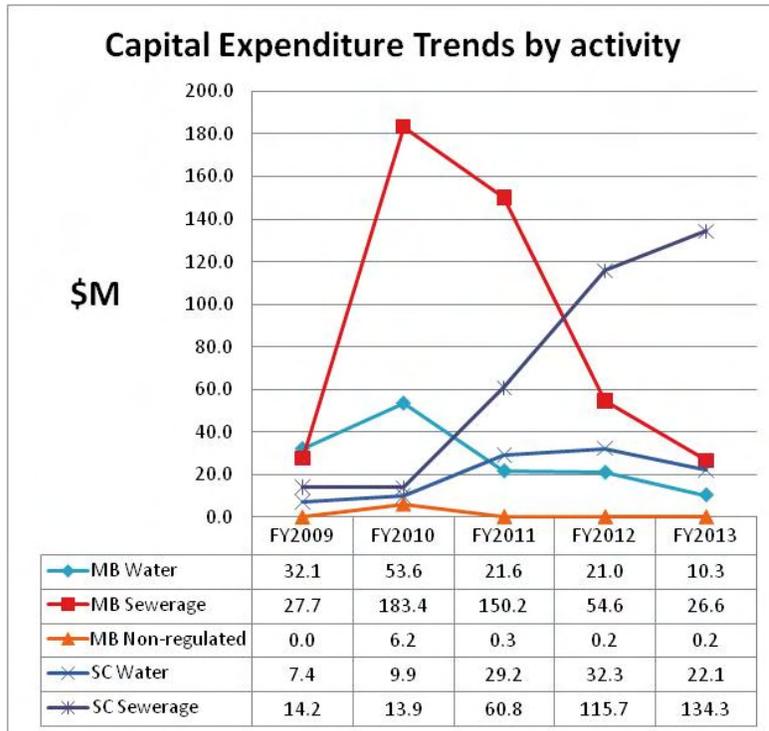
As indicated above there is significant expenditure arising from growth over the period. Minimal improvement capital expenditure is forecast over the period, on the basis that existing service levels are assumed to continue over the period. Unitywater has classified expenditure required to meet existing service levels as compliance expenditure, as it seeks to remedy certain situations where services do not meet current standards.

The following graphs show trends in both assets capitalised over the analysis period and actual capital expenditure. These trends indicate the increasing investment in sewerage infrastructure with FY2009 to FY2011 representing significant investment in the Moreton Bay Murrumba Sewage treatment plant (STP) and recycling facility and FY2011 to FY2013 showing redirection of resources to Sunshine Coast sewerage infrastructure representing augmentation/upgrades of seven STPs.

Graph 5 Assets capitalised by region

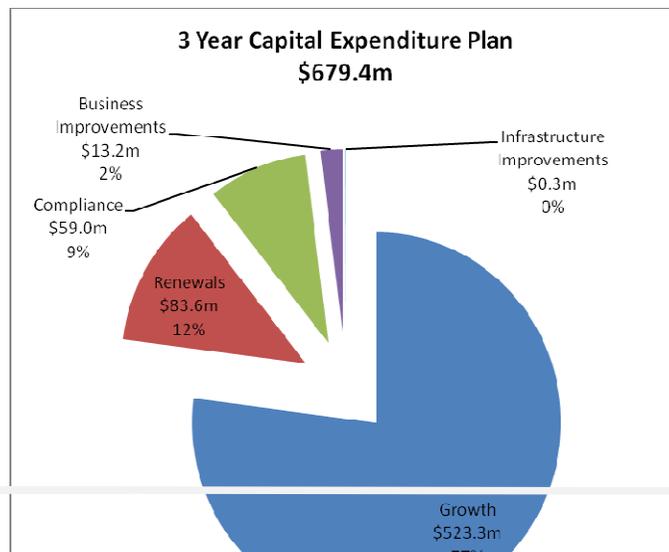


Graph 6 Capital expenditure by region

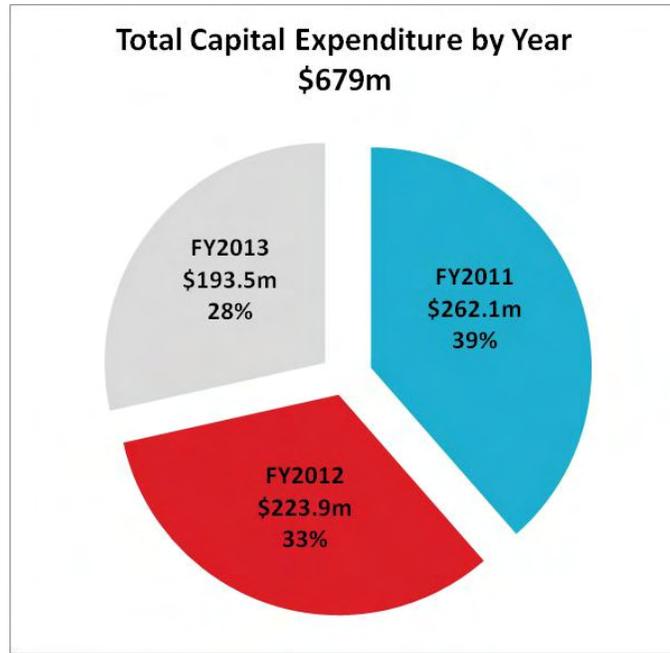


Capital expenditure (not capitalisation) by cost drivers over the three year plan show that significant expenditure will be driven by growth factors. This correlates with projected population growth of 20% to 2016 and the resulting expansion in the asset base required to provide service capacity.

Graph 7 Summary of capital expenditure by cost driver

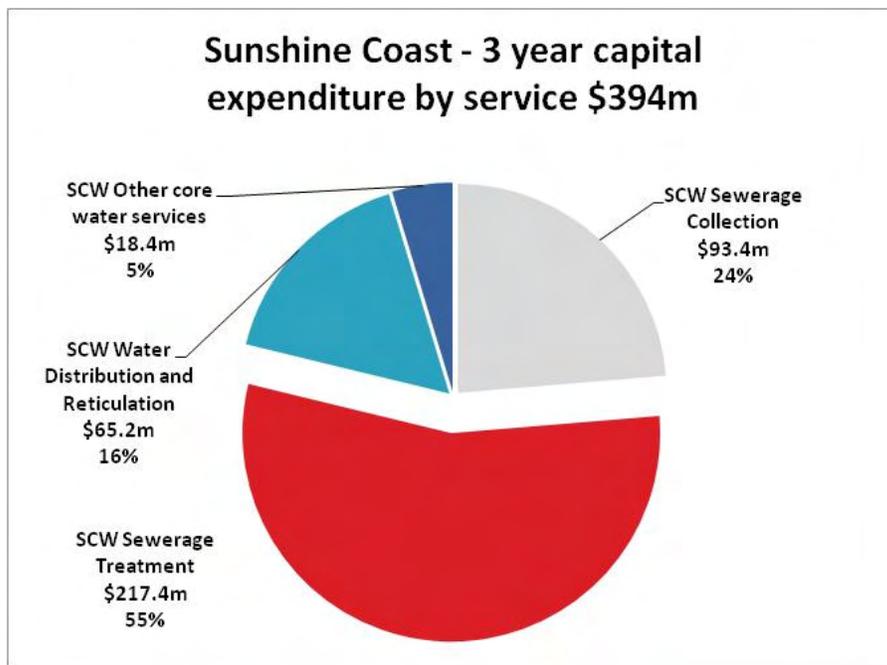
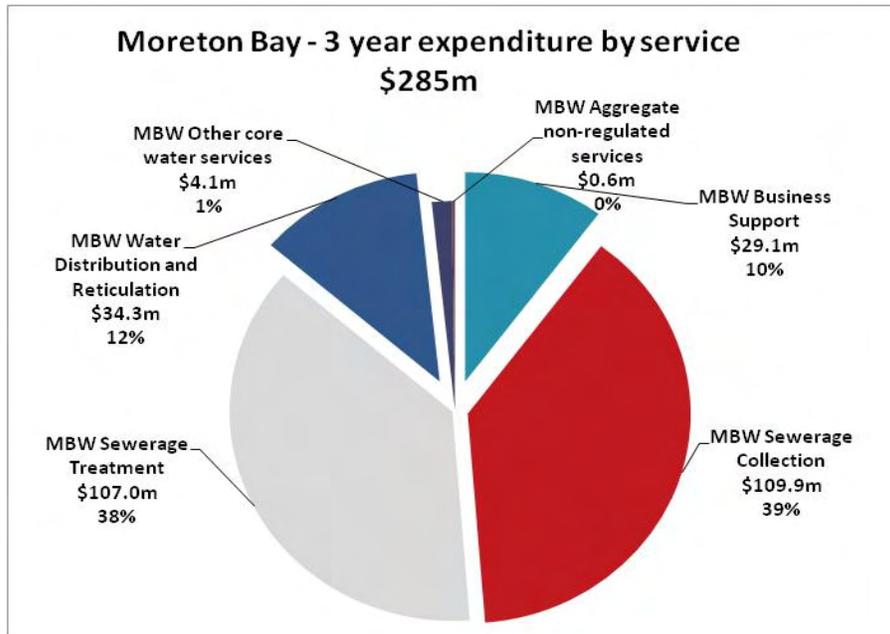


Graph 8 Summary of capital expenditure by year



The following graphs display three years capital expenditure by region and service type. Sewerage services account for 77% of all capital expenditure during the period.

Sunshine Coast expenditure will increase significantly over the three-year period. This is principally due to planned upgrades of seven sewage treatment plants

Graph 9 Capital expenditure by region and service

As evident from the graphs above, the significant portion of capital expenditure over the next three years is for Sewerage Treatment and Collection categories, rather than Water Distribution. This is a result of the following factors:

- Major upgrades to some of the region's sewage treatment plants are scheduled over the next few years. These upgrades involve significant capital expenditure; and
- Falling levels of both residential and business water consumption over the last 5 years have tended to mitigate the impact of growth and allowed future water distribution infrastructure to be deferred.

The table below provides details of capital expenditure by service over the next 3 years. Additionally Unitywater has included as part of the work papers supporting this response a detailed listing of all capital expenditure. Business Support capital expenditure for FY2011 includes \$10.3m of replacement vehicles, \$1.1m of new vehicles, \$1.5m for facility fit outs and \$4.1m for IT related projects. Other items relate to infrastructure projects.

Table 23 Capital Expenditure by Service

| Service \$M | FY2011 | FY2012 | FY2013 | Total | % of Total |
|--|--------|--------|--------|-------|------------|
| Business Support | 17.0 | 8.3 | 3.8 | 29.1 | 4.3% |
| Non Regulated | 10.1 | 0.7 | 0.2 | 11.0 | 1.6% |
| Recycled Water Distribution and Reticulation | 0.6 | 1.7 | 0.7 | 3.0 | 0.4% |
| Recycled Water Manufacture | 9.4 | 9.0 | 1.3 | 19.7 | 2.9% |
| Sewage Collection | 89.4 | 56.0 | 57.4 | 202.7 | 29.8% |
| Sewage Treatment | 103.4 | 109.6 | 100.9 | 313.9 | 46.2% |
| Water Distribution and Reticulation | 32.2 | 38.6 | 29.2 | 100.0 | 14.7% |
| TOTAL | 262.1 | 223.9 | 193.5 | 679.4 | 100.0% |

9.3 Method of determining capital programs

The method for deriving each capital expenditure item within a program varies depending on the *cost driver*.

The process used to derive capital works for each *cost driver* is summarised below.

9.3.1 Growth

Growth related capital projects are those that are primarily about augmenting water and sewerage services to cater for increasing population.

The essential element of the process chain that ultimately defines growth-related capital expenditure is set out schematically below:

Diagram 8 Planning process

*Link 1*

Demand forecasts established in accordance with Demand Forecast Methods provide the load inputs to water and sewerage system network models. Demands are calculated for the current load and generally in 5 year increments for at least 15 years. Ultimate loads under the fully developed planning scheme are also determined.

Link 2

These demand projections are used as inputs to water and sewerage network models. These computer models of the reticulation networks are run for existing and future demands to identify where and when system performance fails to meet the designated standards of service.

Link 3

Network modelling is used to identify solutions to system deficiencies, when such solutions need to be implemented, and what they might cost. For smaller, straightforward pipeline augmentation solutions, this level of detail is often sufficient for the project to be included in the prioritisation process without any further detailed options investigations.

Link 4

For larger pipe and pump system upgrades, further investigations into the options available are generally required before the proposed augmentation can be included in the capital program. These planning investigations typically involve:

- Review of network modelling to confirm system shortfall
- Where possible, validation from field/SCADA data
- Developing and assessing a range of alternative options
- Concept design to identify capital costs
- Route selection and environmental approvals
- Application of whole-of-life cycle costing.
- Recommendation of the preferred solution

Link 5

Capital works identified in the coming financial year also undergo a “prioritisation” process to ensure funding is allocated in an appropriately efficient manner. The current prioritisation process is discussed further in this section.

9.3.2 Renewals

The planning process for asset renewals varies between all prior amalgamated Councils. They also vary between the different asset classes.

In broad terms the process chain for determining renewal driven capital works is as follows:

Diagram 9 Capital Expenditure Process for Renewals



Both Moreton and Sunshine Coast maintain GIS asset databases for all water and sewerage assets. However, there is considerable work still to be done to consolidate both regions databases.

The databases that exist include physical attributes, as well as age and estimates of serviceable life. Although estimates of remaining serviceable life are generally based on desktop assumptions, rather than field condition assessments, the current system does allow a financial assessment to be made in relation to renewal expenditure projections.

Some condition assessment is done on assets, although this varies depending on the asset and the location. There is no common process applicable across the extended region. Some brief comments on the current approach are set out below;

- 1 For smaller passive non-critical water and sewage pipe work, assets are essentially run-to-failure with pipe replacements implemented as and when required. These replacements are typically identified by operations staff.
- 2 For larger critical water pipe assets, occasional condition assessments are done to establish the assets remaining life. Note, in some locations, these condition assessments are being done as part of a broader systematic network-wide approach. However, in most instances, the assessments are generally reactive, and occur as a result of operational concerns or in response to recent failure history.

- 3 In relation to larger critical sewer pipe assets, condition assessments via CCTV inspections are done more frequently, but are still not completed in a systematic manner that would allow asset life to be adjusted within the current asset register database.

Both Moreton and Sunshine Coast areas have recently installed asset maintenance systems involving the implementation of field computing and capture of system operational data. It is expected that the data provided by this system will assist in the development of systematic approaches to asset condition assessment and asset management.

9.3.3 Improvements

Improvements relate to expenditures associated with improving service levels and reliability to meet customer preferences.

Unitywater is currently managing to existing service levels, and its capital expenditure program has been developed accordingly. Hence there are minimal improvements forecast for the period.

9.3.2 Compliance

Compliance relates to expenditure required to meet legislative standards. Unitywater has interpreted this to also include expenditure required to meet pre-existing service levels (rather than improved service levels).

Compliance projects are typically assessed and determined on a case-by-case basis.

Diagram 10 Planning Process for compliance projects



Regulatory and legislative issues that drive Compliance typically include;

- 1 Workplace Health and Safety Act
- 2 Environmental Protection Act (Including EPP Water, Environmental Authorities, etc)
- 3 Water Supply (Safety and Reliability) Act
- 4 Provision of capacity for fire fighting

Compliance issues frequently arise as a consequence of growth. In particular, whilst regulatory compliance is often a driver for the upgrade of a sewage treatment plant (STP), the principal cause of this is growth in the connected catchment exceeding either the STP capacity, or the Environmental Authority (Licence) limit.

Solutions to Compliance related issues are developed through planning investigations. Once the solution has been identified, the proposed works are assessed in the Capital Prioritisation Model before being included in the draft Capital Expenditure Program for approval.

9.4 Capital planning process and prioritisation

9.4.1 Capital Prioritisation Model

A prioritisation model has been specifically developed to assess projects across the region. This model allows each project to be assessed, scored and ranked.

Projects are evaluated and scored against seven weighted criteria, including;

- 1 Public Health
- 2 Workplace Health and Safety
- 3 Environmental Impacts
- 4 Financial Considerations
- 5 Asset Condition
- 6 Legislative/Legal/Corporate Requirements
- 7 Social

Four of these criteria utilise a risk based approach (Likelihood x Consequences) to add additional rigor to the scoring process. Each criterion is assigned a weighting and the combined criteria scores are then used to rank the projects within the draft program.

Note projects that meet the following specific triggers are automatically included in the capital expenditure program. These triggers include:

- Specific statutory or legislative requirements
- Extreme public, WH&S or environmental risks
- Previously commenced projects that must continue

9.4.2 Expenditure approval processes

Capital expenditure for FY2011 was approved by the Board of Unitywater as part of its overall budget approval process. Unitywater has established a sub-committee of the Board to monitor and review the capital expenditure program and its delivery. This committee meets monthly to consider progress against timelines and budget, and make decisions as required on variations or budget changes.

Unitywater is currently establishing further governance structures to underpin the process of approving capital expenditure. These processes will be refined during the coming financial year as structural changes are implemented. Consequently the Authority should consider current practices in light of Unitywater's emerging capabilities. Other information required by the Authority in relation to approval processes, linkages to strategic asset management plans, option analysis and procurement processes will be matters addressed by Unitywater during the Authority's detailed review of capital expenditure.

Section 10 Contributed, donated and gifted assets

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section describes the historic and forecast contributed, donated and gifted assets and related matters. Actual results are supplied for FY2009, the latest Council forecasts for FY2010 and the budget forecasts for FY2011 to FY2013. The information for FY2010 is based on Council third quarter estimates, and will need to be updated when final results are provided to Unitywater. This will have an impact on the final RAB and MAR calculations. In some cases, funds received from individual Infrastructure Agreements have not always been separated by Councils into the level of disaggregation required by the Authority. In allocating developer contributions assumptions needed to be made as contributions are classified as unallocated as at the time of receipt. Records were not always kept by Councils to tie contributions to individual assets or classes, and it will take time to develop a method for this allocation in the future. Accordingly, Unitywater has not been able to allocate donated assets and cash contribution in all cases. All donated assets have been categorised as Distribution Infrastructure as most would be in this category. This is reflected in the templates provided.

10.1 Overview

Data has been collected in relation to historic grants and subsidies from the State Government. These have been discontinued for FY2011, and hence are not included in the forecasts.

The level of developer provided assets for the period FY2009 to FY2010 is based on Council supplied information. The FY2009 values have been agreed in aggregate to the financial statement notes. The FY2010 figures are a Council forecast that will need to be updated once the final results are provided. For the forecasted period FY2011 to FY2013, estimated developer provided assets are forecasted on historic trends taking into consideration expected development growth. The actual level of developer provided assets can vary significantly in an individual year depending on the timing of developments.

Forecasts of planning scheme charges are based on historic trends. The level of receipts forecast is based on expected growth and the current levels of developer charges. All developer cash contributions for water or sewerage infrastructure received on or after 1st July, 2010 will be collected by Council and remitted to Unitywater at which time the final amounts. For priority infrastructure development Unitywater is tied to the participating Councils and relies on Councils' as well as its own views for the level and timing of growth. New arrangements and processes need to be developed with Councils as part of the implementation of the broader water reforms in SEQ.

10.2 Receipts for each service for each region

The following table indicates the level of receipts for each service for the Moreton Bay Region, as currently estimated:

Table 24 Capital contributions Moreton Bay

| | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|--|---------|---------|---------|---------|---------|
| Drinking Water Donated Assets | \$9.6m | \$6.0m | \$4.5m | \$4.0m | \$4.1m |
| Drinking Water Grants | \$3.6m | \$0.7m | | | |
| Drinking Water Planning Scheme Charges | \$7.5m | \$9.7m | \$11.6m | \$12.2m | \$12.5m |
| Sewage via Sewer Donated Assets | \$9.8m | \$6.9m | \$9.1m | \$8.1m | \$8.3m |
| Sewage via Sewer Grants | \$33.3m | \$24.3m | | | |
| Sewage via Sewer Planning Scheme Charges | \$9.6m | \$12.3m | \$14.9m | \$15.8m | \$17.1m |

The following table indicates the level of receipts for each service for the Sunshine Coast Region, as currently estimated:

Table 25 Capital contributions Sunshine Coast

| All figures in \$000's | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|--|---------|---------|---------|--------|--------|
| Drinking Water Donated Assets | \$9.9m | \$6.8m | \$6.9m | \$5.6m | \$5.6m |
| Drinking Water Grants | \$2.1m | \$3.3m | | | |
| Drinking Water Planning Scheme Charges | \$11.3m | \$6.7m | \$10.0m | \$9.9m | \$9.9m |
| Sewage via Sewer Donated Assets | \$19.3m | \$12.4m | \$10.2m | \$8.0m | \$8.0m |
| Sewage via Sewer Grants | \$1.3m | \$0.03m | | | |
| Sewage via Sewer Planning Scheme Charges | \$9.6m | \$6.5m | \$8.5m | \$8.5m | \$8.4m |

10.3 Adjustments for actual receipts

The revenue offset approach requires capital contributions to be offset against the MAR, to determine the residual revenue that can be recovered from other customers through utility charges and other fees and charges.

The MAR described in this information return has been adjusted by the forecasts set out above for capital contributions. Forecasting capital contributions is difficult, and subject to uncertainty. Consequently, Unitywater intends to adjust the MAR and the RAB at the end of the current year to reflect actual capital contributions received. The adjusted MAR will be used to determine the level of under-recovery for the year.

Unitywater intends to revisit this approach annually during the interim price monitoring period where these contributions become more certain or easier to forecast with accuracy.

10.4 Change to asset offset method

The information requirement asks for the nomination of any date that Unitywater intends to adopt the asset offset method. Unitywater has not nominated a date although this does not mean it will not choose to do so during the price monitoring period. Any nomination will occur as part of a future information return.

Section 11 Depreciation

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section presents depreciation as can best be determined historically, as well as the forecast depreciation from future capital expenditure. The completed templates provide more detailed information, as required by the Authority. Information has been provided on an individual asset basis with the exception of information gaps noted earlier in relation to the RAB roll-forward.

The following approach has been adopted:

- Useful lives were applied to the opening asset base as at 1 July 2008 and capitalised assets during the roll forward period to 30 June 2010 based on Council records to the extent that individual asset details were provided. For all other assets which were balanced in aggregate to the financial statement notes, a useful life of 50 years was applied.
- Depreciation relating to asset acquisitions (capitalised and developer provided) during the period 1 July 2008 to 30 June 2010 was calculated on the basis of Council asset useful life and pro-rated in accordance with the acquisition date. Where information was not available from Councils to determine the lives (eg no asset details), a useful life of 50 years was assumed.

- Forecast depreciation of capitalised and developer provided assets for the years FY2011 to FY2013 was calculated on an individual asset basis and half year depreciation assumed. This assumption aligns to the Authority's guidelines. Asset lives for capitalised assets during this period were sourced from an engineering consultancy which performed a detailed asset assessment for the Water Reform Program Stage 2 process.
- Straight line depreciation has been applied in all cases.

A summary of depreciation by region and service is provided below:

Table 26 Depreciation by Region and Service

| REGION AND SERVICE (\$000) | FY2009 | FY2010 | FY2011 | FY2012 | FY2013 |
|----------------------------|---------------|---------------|---------------|---------------|---------------|
| Moreton Bay | 30,223 | 31,075 | 35,005 | 40,619 | 43,822 |
| NON REGULATED | 44 | 112 | 208 | 227 | 237 |
| NON REGULATED | | | | | |
| REGULATED | 44 | 112 | 208 | 227 | 237 |
| SEWERAGE | 18,859 | 19,384 | 22,145 | 26,135 | 28,115 |
| TRADE WASTE | | 4 | 7 | 7 | 7 |
| SEWAGE VIA SEWER | 18,859 | 19,381 | 22,138 | 26,127 | 28,107 |
| WATER | 11,320 | 11,579 | 12,652 | 14,257 | 15,470 |
| DRINKING WATER | 11,048 | 10,923 | 11,846 | 13,406 | 14,571 |
| OTHER CORE WATER | 272 | 656 | 806 | 851 | 899 |
| Sunshine Coast | 25,641 | 26,471 | 27,372 | 29,212 | 31,560 |
| NON REGULATED | 18 | 23 | 26 | 26 | 26 |
| NON REGULATED | 18 | 23 | 26 | 26 | 26 |
| SEWERAGE | 16,509 | 17,058 | 17,677 | 19,018 | 20,812 |
| TRADEWASTE | 2 | 5 | 8 | 8 | 8 |
| SEWAGE VIA SEWER | 16,507 | 17,053 | 17,669 | 19,010 | 20,804 |
| WATER | 9,114 | 9,390 | 9,668 | 10,167 | 10,722 |
| DRINKING WATER | 8,484 | 8,760 | 9,005 | 9,430 | 9,928 |
| OTHER CORE WATER | 631 | 631 | 664 | 738 | 793 |
| Grand Total | 55,864 | 57,547 | 62,377 | 69,831 | 75,381 |

The growth in regulatory depreciation occurs due to growth in capital expenditure.

Unitywater has calculated useful lives on an individual asset basis, instead of adopting the broader categorisation of asset types defined by the Authority, which can result in assets with lives ranging from 20 to 100 years being grouped together and assigned a single average life.

The table below provides the asset lives used for all post 1 July 2010 acquisitions.

Table 27 Useful life of post 1 July 2010 assets

Source - Water Reform Program_Asset Assessment Phase 1 - Water Business 2_GHD Report

WATER ASSETS USEFUL LIFE

Water Infrastructure

Mains 80-100

SEWERAGE ASSETS USEFUL LIFE

Sewerage Infrastructure

Mains 70-100

| | | | |
|----------------------------|----|-------------------------------|----|
| Hydrants | 50 | Manholes | 80 |
| Meters | 15 | Valves | 50 |
| Valves | 50 | | |
| Water Pump Stations | | Sewerage Pump Stations | |
| Buildings | 60 | Buildings | 80 |
| Control Equipment | 20 | Control Equipment | 20 |
| B423 Pipe work | 50 | Pipe work | 50 |
| Pumps | 20 | Pumps | 20 |
| Telemetry | 20 | Pump well | 80 |
| Electrical | 20 | Telemetry | 20 |
| | | SwitchBoard | 20 |
| Reservoirs | | Treatment Plant | |
| | 80 | Buildings | 60 |
| | | Valves | 50 |
| | | SwitchBoard | 20 |
| | | Telemetry | 20 |
| | | Concrete Structures | 60 |
| | | Steel structures | 25 |
| | | Pumps | 20 |
| | | Pipework | 50 |
| | | Dewatering equip | 20 |
| | | Chlorinator | 30 |
| | | Electrics | 20 |
| | | Aerators | 20 |

A new Non Current Asset Policy has recently been passed by the Board. This policy contains asset lives that differ in some cases (although not materially) from those in the table above. It is proposed to recalculate depreciation as part of the process to finalise the interim RAB.

Section 12 Indexation

This section sets out the indexation applied to the RAB roll-forward and capital expenditure.

As required by the Authority, the ABS Consumer Price Index (all groups, Brisbane) has been used for FY2009 and the resultant escalation rate is 2.02% (being the increase over the period 1 July 2008 to 30 June, 2009).

For FY2010, the information requirement allows for the Brisbane All Groups index to apply for FY2010, or alternatively the Queensland State Budget forecast for the period. For the interim RAB, Unitywater has adopted the FY2010 Queensland State Budget Inflation Forecast, which is 2.50%. When the interim RAB is finalised for the FY2010 the CPI increase for FY2010 will be applied instead.

The escalation applied for future years has been calculated using the difference between the RBA return on the market rate for five year bonds and five year capital indexed bonds, in accordance with the Authority's information requirement. The average of the monthly differences over the six months from November 2009 to April 2010 was used and the resultant escalation rate is 2.48%.

The resulting indexation factors applied by Unitywater were as follows:

Table 28 Indexation Parameters

| Indexation rates | Year Ending 30 June: | | |
|-------------------------|----------------------|------------|--------------|
| | 2009 | 2010 | 2011 onwards |
| Indexation rates | | | |
| Annual Indexation rate | % pa | 2.02% | 2.50% |
| | | 2.48% | |
| | | Historical | Forecast |

Section 13 Return on Capital

The Direction from the Authority's Ministers requires the Authority to consider a weighted average cost of capital within a reasonable range of values for FY2011.

A joint consultancy between the three retail/distribution entities was commissioned to recommend an appropriate weighted average cost of capital. The consultant provided a recommended range for WACC, and Unitywater has adopted the mid- point of this range. The table below sets out the parameters adopted

Table 29 Weighted Average Cost of Capital Parameters

| WACC Parameters | Value |
|--|--------------|
| Weighted Average Cost of Capital Parameters | |
| Risk free rate | 5.65% |
| Market risk premium | 6.50% |
| Debt margin | 8.80% |
| Asset beta | 90.00% |
| Capital structure | |
| Debt (D / (D+E)) | 60% |
| Corporate tax rate | 30% |
| Imputation gamma | 50% |
| Inflation rate | 2.54% |
| Weighted Average Cost of Capital | |
| Nominal Post-tax Return on capital | <u>9.88%</u> |

The consultant's report will be made available to the Authority.

Unitywater notes that some of the underlying assumptions adopted by the consultant depart from those adopted by the Authority in past decisions. Unitywater submits that the above WACC falls within a reasonable range, as there are a number of valid assumptions that can be made in relation to WACC parameters.

Furthermore, Unitywater submits that the Authority should not be constrained by its past decisions in assessing a reasonable range, as there are clearly valid assumptions and parameters that lie outside its past decisions that have been adopted by regulators elsewhere.

It is also acknowledged that in setting the WACC for FY2012 and FY2013, the Authority may revert to its precedent assumptions in deriving a point estimate of WACC, and these assumptions may differ from those above.

Section 14 Operating costs

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater's best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section describes Unitywater’s forecast operating costs, and is supported by the completed template which sets out historic operating costs based on the best information available, as well as detailed information on future costs. Historic Council data has been obtained from the Enterprise Financial Model and Councils’ third quarter forecasts. These past operating costs are heavily influenced by the allocation of overhead from the broader Council to the water and sewerage activities.

Unitywater is in its first year of operations and has inherited assets and cost structures from Councils. Unitywater must also develop new corporate and retail capabilities, while maintaining service continuity.

Unitywater’s total operating costs for FY2011 are forecast to be \$234m. This is based on the initial Board approved budget of \$231m amended for an additional \$3m in costs relating to bulk water purchases to more accurately represent this expected cost. The table below shows this adjustment for each of the three years.

Table 30 Changes to initial budget in completed template (\$M)

| | FY2011 | FY2012 | FY2013 |
|--|---------------|---------------|---------------|
| Initial Board approved budget | 231 | 256 | 282 |
| Change to bulk water cost Moreton Bay | 3 | 3 | 4 |
| Revised operating cost reported in completed template | 234 | 259 | 286 |

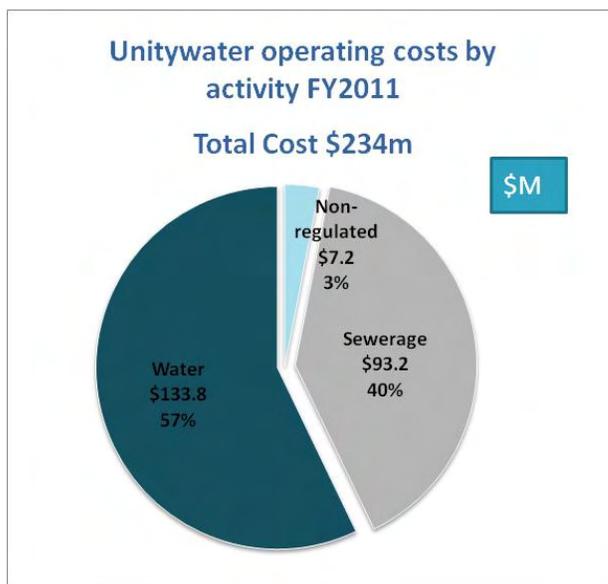
14.1 Operating costs by region

Operating costs relate to the transferred water and sewerage businesses from Councils, and involve the following services:

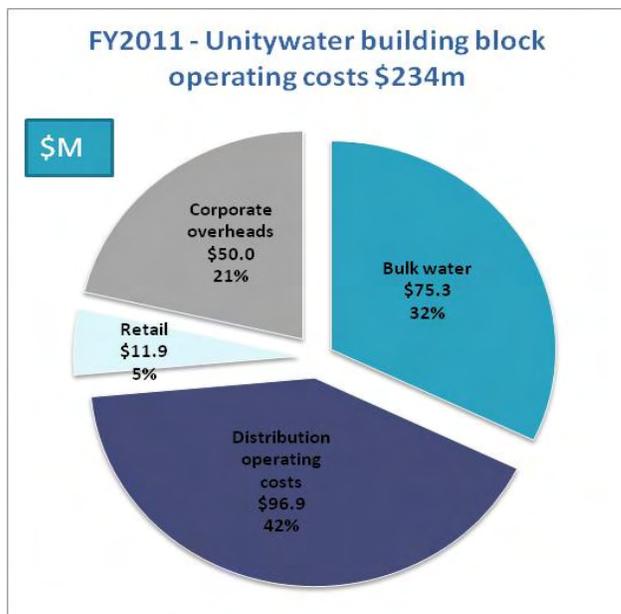
- Core services;
- Other core services (i.e. recycled water treatment and supply to a commercial customer); and
- Unregulated services (i.e. laboratory services and private works).

The data template information shows the operating costs attributable to each activity, service and cost category as provided by the Authority, including the allocation of common costs. The graphs below provide a summary, by regulated water and sewerage activities, and unregulated activities for FY2011. Additionally a breakdown of FY2011 operating costs by major cost components has been provided in the accompanying table.

Graph 10 Operating Costs FY2011 by activity



Graph 11 Unitywater operating costs FY2011 by type



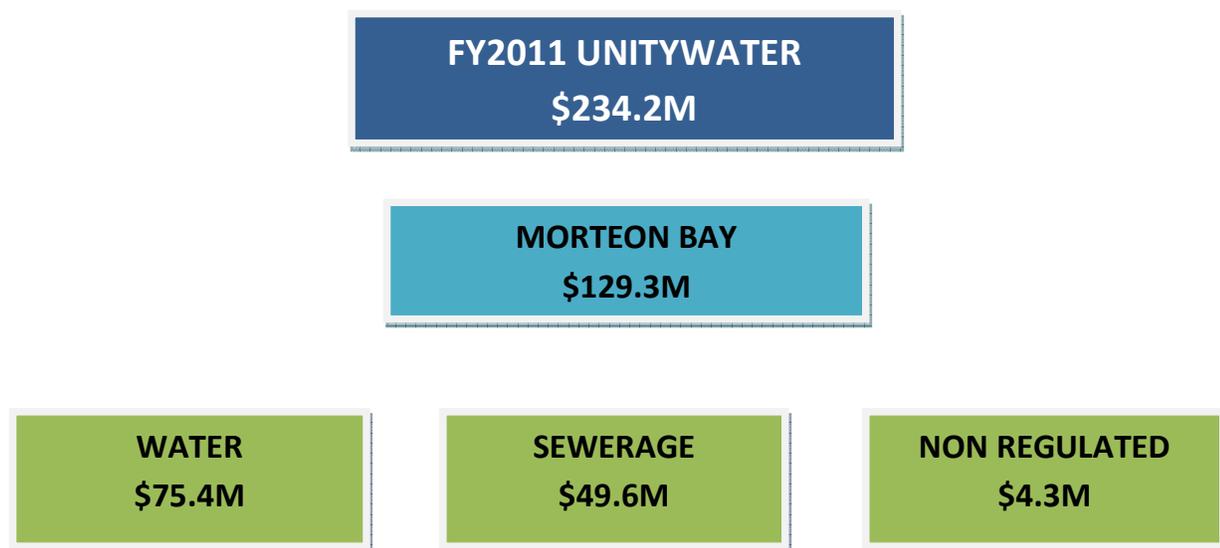
The following diagram provides a breakdown of operating costs at activity level by region. Cost categories attributed to

Breakdown of operating costs

| | \$M |
|---|---------------|
| Bulk water | <u>\$75.3</u> |
| *New Retail costs | <u>\$11.9</u> |
| Corporate costs: | <u>\$50</u> |
| Employee costs | \$13 |
| Non-recurring projects | \$8 |
| SLA's excluding IT costs | \$6 |
| Contractor costs | \$4 |
| IT costs inc SLA's of \$2m | \$4 |
| Fleet costs | \$5 |
| Other new costs | \$9 |
| Indirect taxes | \$1 |
| Distribution costs: | <u>\$96.9</u> |
| Employee costs | \$46.9 |
| Disposal of Bio-solids | \$4.3 |
| Electricity and Chemicals | \$12.9 |
| Contractor costs | \$20.8 |
| Materials & Services | \$11.5 |
| Licence and Reg. Fees | \$0.5 |
| *Note that new retail costs are direct costs including salaries & wages costs but exclude service level agreements of \$2.4m, indicative allocation of overhead \$3.2m and post budget cost reallocations of \$1.2. This would result in an indicative total allocated cost for retail services of \$18.7m. | |
| ** The allocation of operating costs between geographical regions is 55% and 45% respectively being: | |
| Moreton Bay | \$129m |
| Sunshine Coast | \$105m |

water and sewerage activities are shown with % contribution to total costs.

Diagram 11 Region operating costs by activity and cost categories for FY2011



| MORTEON BAY COST CATEGORIES | Water \$m | Water% | Wastewater \$m | Wastewater% |
|-----------------------------|-------------|-------------|----------------|-------------|
| Bulk water costs | 42.1 | 55.9% | | |
| Contractor expenses | 3.1 | 4.1% | 9.5 | 19.2% |
| Corporate costs | 12.9 | 17.2% | 14.1 | 28.4% |
| Electricity & Chemicals | 1.8 | 2.4% | 5.3 | 10.7% |
| Employee expenses | 9.6 | 12.7% | 13.6 | 27.5% |
| Indirect taxes | 0.2 | 0.3% | 0.2 | 0.4% |
| Licence or regulatory fees | 0.01 | 0.02% | 0.24 | 0.48% |
| Materials and services | 2.3 | 3.0% | 3.1 | 6.2% |
| Retail Customer & billing | 1.5 | 2.1% | 1.7 | 3.4% |
| Retail other | 1.7 | 2.3% | 1.9 | 3.8% |
| TOTAL MORETON BAY | 75.4 | 100% | 49.6 | 100% |

SUNSHINE COAST
\$104.9M

| | WATER \$58.4M | SEWERAGE \$43.6M | NON REGULATED \$2.9M |
|-----------------------------|--------------------------------|-----------------------------------|---------------------------------------|
| | | | |
| Corporate costs | 10.1 | 17.2% | 11.0 25.3% |
| Electricity & Chemicals | 0.5 | 0.9% | 5.1 11.8% |
| Employee expenses | 7.0 | 12.0% | 12.5 28.6% |
| Indirect taxes | 0.2 | 0.3% | 0.2 0.5% |
| Licence or regulatory fees | 0.03 | 0.05% | 0.24 0.56% |
| Materials and services | 1.9 | 3.2% | 3.2 7.4% |
| Retail Customer & billing | 1.1 | 1.9% | 1.1 2.6% |
| Retail other | 1.3 | 2.3% | 1.4 3.2% |
| TOTAL SUNSHINE COAST | 58.4 | 100% | 43.5 100% |

The above diagram shows operating costs for water activities comprising of drinking water and other core recycled water services. Sewerage activities include sewage via sewer and trade waste services. Non regulated services operating costs have been shown in aggregate by region and represent laboratory services and private works. Corporate tax has been calculated separately over the interim price monitoring period, and is forecast to be \$11.1m in FY2011 and \$49.5m over the three years from FY2011 to FY2013.

The impact of planned new capital additions on operating costs, particularly in budget years FY2012 and FY2013, requires refinement and Unitywater will be reviewing future year's forecasts to better align operating cost changes with infrastructure expansion.

Other refinements to forecasts will be performed by Unitywater over the next 12 months. This will be aided by automation of budget and cost allocation systems and as a history of actual costs is gathered and analysed.

14.2 Cost characteristics

Operating costs for FY2011 represent business as usual costs as well as one-off costs associated with bringing the business together, such as systems and business integration activities.

Operating costs are also influenced by the staff transition arrangements set under the SEQ Urban Water Arrangements Reform Workforce Framework 2010.

Additional costs will be incurred, both recurrent and one-off items, in relation to establishment of new corporate and retail capacity. There are also costs associated with Council based service level agreements and employee costs associated with staff transferred from existing council corporate structures to Unitywater. Increases for cost inputs such as bulk water, chemicals and electricity and disposal of bio-solids will impact future operating costs and high growth (predicted 20% growth to 2016).

The table below repeats the growth and cost escalation parameters which were applied when forecasting Unitywater's initial budget, as these have a direct bearing on operating costs.

Table 31 Growth and cost escalation factors

| Population Growth | | | | |
|--------------------------|---------------|---------------|---------------|--|
| Year | FY2011 | FY2012 | FY2013 | |
| Moreton Bay | 2.52% | 2.29% | 2.29% | |
| Sunshine Coast | 2.85% | 2.35% | 2.35% | |
| Cost Escalation | | | | |
| Year | FY2011 | FY2012 | FY2013 | |
| General Escalation | 2.9% | 2.9% | 2.9% | |
| Chemicals | 3.5% | 3.5% | 3.5% | |
| Electricity | 7.9% | 7.9% | 7.9% | |
| Labour (SC 4% FY2011) | 4.5% | 4.0% | 4.0% | |
| Bulk water: | | | | |
| Moreton Bay | 22% | 18% | 15% | |
| Sunshine Coast | 26% | 28% | 22% | |

Note: Costs will differ within South East Queensland given location, demographics, workforce and other factors. Hence cost escalation can be expected to be different between the various distribution/retail entities.

Employee direct costs and on-costs (including overtime and allowances and excluding director's fees and labour hire) represent 27% of total operating costs (\$64m) and 15% of total organisation expenses (including depreciation, interest and tax). Employee costs represent a combination of costs relating to employees from the former Council businesses, transferred employees from Councils and new employees.

Unitywater is governed by the reform workforce framework which guarantees maintenance of employee conditions until 30th June 2013. Estimated salaries and wages which fall within the workforce framework represent 86% of total employee budgeted costs for FY2011.

Unitywater may also incur estimated costs of \$1.7m for FY2011 in relation to labour equalisation between regions. Operational costs for FY2011 show this commitment as a once off impact included in operational corporate projects with the recurrent impact included in the relevant budgets for FY2012 and FY2013.

Other efficiencies are planned in line with Unitywater's development path. Strategies are currently being developed to leverage efficiencies from the use of technologies and additionally through the review of existing contracts to identify opportunities to achieve the most cost effective outcomes.

Functional realignment of salary and wages costs post initial budget

Functional re-alignments have been made after the budget was adopted which change the allocation of salaries and wages costs between Corporate, Retail and Distribution Operations. The changes do not impact the overall costs to Unitywater or materially change the attribution of operating costs to activities and services.

The post initial budget changes are not reflected in the information templates provided to the Authority in order to maintain consistency with the Board approved budget. Unitywater has alternatively disclosed the cost movements below.

The movement in costs primarily relate to parts of the operational business overhead included in the operational division budget being reallocated to corporate and retail divisions. Business sustainability functions such as environmental and quality management were moved to the Corporate Division from Distribution Operations. The demand management and water billing functions were moved to the retail function. This explains the major cost shifts, as set out in the table below.

Table 32 Post initial budget re-allocation of costs for FY2011.

| Salaries and wages \$M | Distribution operations | Corporate | Retail | Total |
|------------------------------------|-------------------------|-------------|------------|-------------|
| Salaries and wages reported | 46.9 | 12.8 | 4.1 | 63.8 |
| Post initial budget change | (6.6) | 5.4 | 1.2 | 0 |
| Revised Budget | 40.3 | 18.2 | 5.3 | 63.8 |

14.3 Cost collection and forecasting

Unitywater has provided detailed information regarding operating expenditure relating to services and activities. Operating costs have been segregated by region and attributed to activities, services and cost categories at a disaggregated level as required. Information has been sourced as follows:

- FY2009 – Due to the disparate information available directly from Councils, the alternate information source used was the Enterprise Financial Model. This model was the tool utilised for the collation of data by the SEQ Water Reform Project. This model is an externally audited document.
- FY2010 – As the final financial results for the respective Councils were not available at the time of data collection, Councils' third quarter budget estimates were used.

- FY2011 to FY2013 – Detailed budget information by cost code and natural account was used to populate information for the forecasted years. The disaggregated data used has been reconciled to Unitywater’s budget.

14.4 Cost allocation

Unitywater has developed a detailed revenue and cost allocation model which identifies individual costs to the lowest disaggregated level by natural account. These costs have then been mapped to the relevant regions, activities, services and cost categories as required by the Authority.

Where costs could not be directly attributed to a service, detail of the cost allocation and associated causal drivers have been provided to the Authority. The allocation model provides a transparent audit trail, showing the link between budgeted revenues and costs at a natural account level and the attribution of those revenues and costs to the Authority’s provided categories, services, activities and regions. The allocation model sets out all causal drivers for costs which were not directly attributable to a specific service and shows how these costs were allocated to the relevant categories by individual account.

An account based approach to disaggregating operating expenses was adopted. This means that the underlying principles for allocation of operating costs by Unitywater to specified reporting categories were on an individual account basis as follows:

- Costs directly attributable to Geographic Area, Activity and Service were identified; and
- Indirect costs were identified and allocated to reporting categories on the basis of causal cost drivers.

The table below provides a high level summary of direct and indirect costs. For every indirect cost an allocation driver was assigned to apportion those costs to a service.

Table 34 Direct and indirect operating costs FY2011

| Expenditure Type \$m | Direct Costs | Indirect Costs | Total Operating Costs |
|------------------------------|--------------|----------------|-----------------------|
| Salaries and Wages | 15 | 48.8 | 63.8 |
| Non Salary and Wages | 118 | 52.2 | 170.2 |
| Total Operating Costs | 133 | 101 | 234 |

Financial statements for the 12 month period to 30 June 2009 were not prepared by amalgamating Councils for the Water Business, therefore service level information provided as part of the Water Reform Program due-diligence process has been used (via the Enterprise Financial Model). This data was subject to a review process and externally audited.

For FY2010, forecasted results have been allocated utilising a methodology consistent with the three year budget allocation, however due to varying costing approaches by amalgamated Councils, not all cost groupings were directly translatable to the Authority’s cost categories.

In this case a best fit approach was adopted to improve comparability of financial results for prior years to the three year projected budget. There however still remains some cost categories which show large movements.

Unitywater will refine its cost allocation methodology in the future as further information is available and as Unitywater obtains greater operational history with the assets involved.

14.5 Changes in operating costs by service and category

14.5.2 Historic costs

As set out above, historic operating costs have been obtained through the enterprise financial model for FY2009 and Councils' third quarter forecasts for FY2010. This information is provided in the data templates.

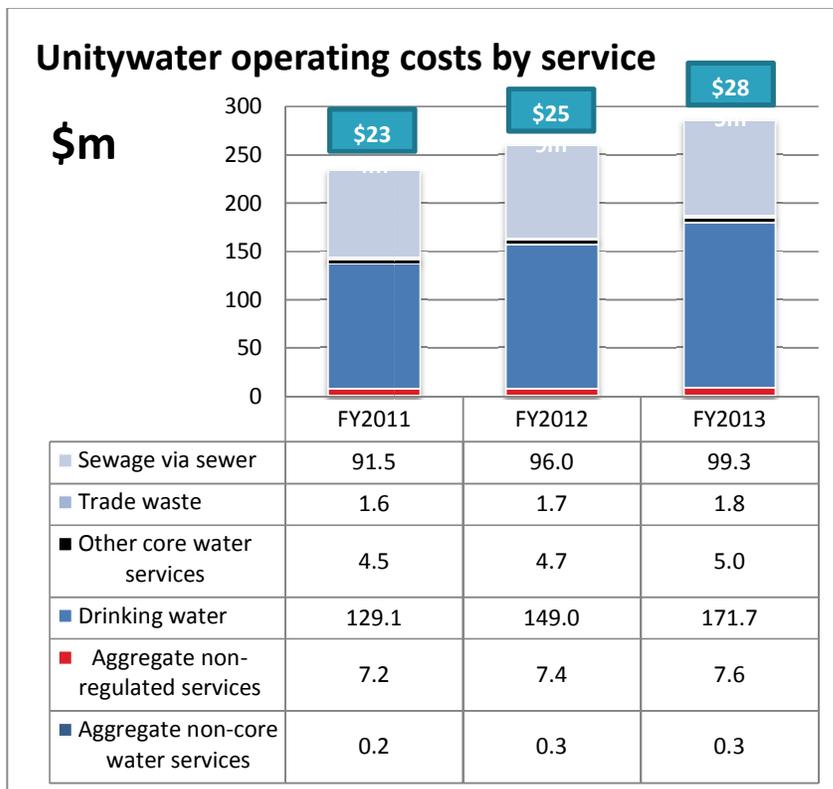
It is difficult to make meaningful comparisons of costs between FY2011 and FY2010 when Councils owned and operated the assets. This is because Councils' water and sewerage businesses operated within the Councils' broader corporate structure, and utilised Council-wide resources such as procurement, human resource management and information technology and systems such as billing, payroll and financial management. Historic costs for water and sewerage will therefore be heavily influenced by how these corporate and other common costs were allocated, compared to how those costs currently present for Unitywater. Additionally, Councils' approach to cost categorisation does not align with that required by the Authority further highlighting the difficulties in making meaningful comparisons.

Comparisons to FY2010 require further caution as costs in this year are based on a Council estimate only. This estimate may not be exhaustive and may differ significantly from actuals depending on the accuracy of the Councils' estimates.

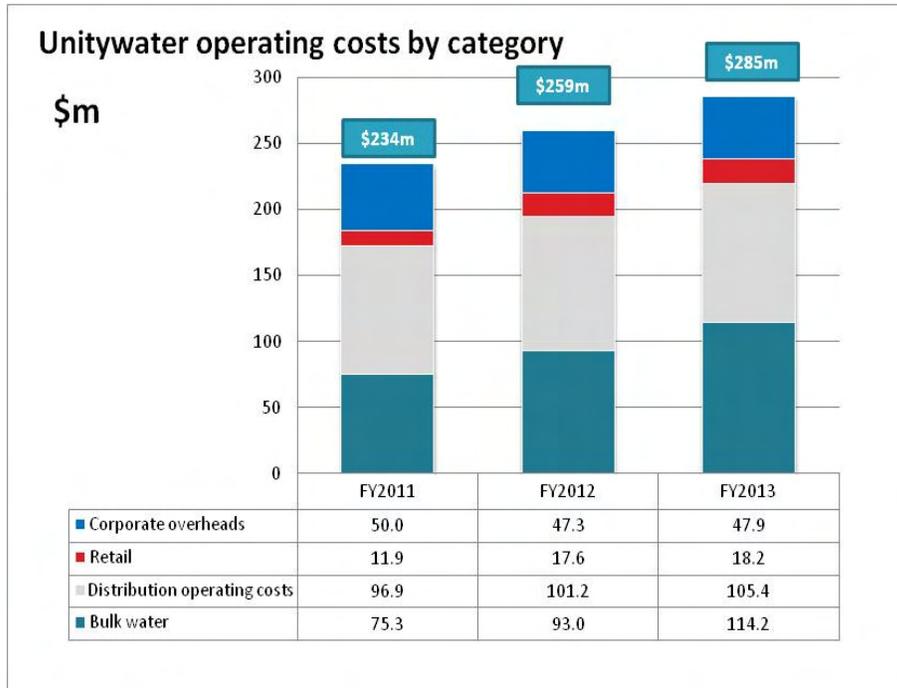
14.5.2 Anticipated changes

The information requirement asks for reasons for anticipated changes in operating costs and taxes over the period 1 July 2010 to 30 June 2013. The graphs below provide an overview.

Graph 12 Operating Costs by service FY2010 to FY2013.



Graph 13 Operating Costs to FY2013 by cost category.



Below is a summarised table highlighting changes between years.

Table 35 Variances in forecast operating costs

| Explanation of Variances | FY2012 | FY2013 |
|--|----------|---------|
| Increase % | 12% | 10% |
| Increase value \$m | \$25m | \$26.6m |
| Represented by: | | |
| Increase in bulk water charge | \$17.7m | \$21.2m |
| Retail costs | \$5.7m | \$0.6m |
| Corporate costs | \$(2.7)m | \$0.6m |
| Increase in Distribution operating costs | \$4.3m | \$4.2m |

Bulk water charges used in Unitywater's initial budget reflect pass through costs of potable water from the water grid manager. For FY2011, the increases in potable water charges are 22% and 26% respectively for the Moreton Bay and Sunshine Coast regions. The projected increases for operating costs for FY2012 and FY2013 align to provided growth and cost escalations with the exception of retail costs. The decrease in corporate costs represents a decrease in once-off project costs.

The following sections provide further explanation of future cost variations for:

- Distribution operating costs
- Retail costs
- Corporate costs

14.6 Changes in distribution operating costs

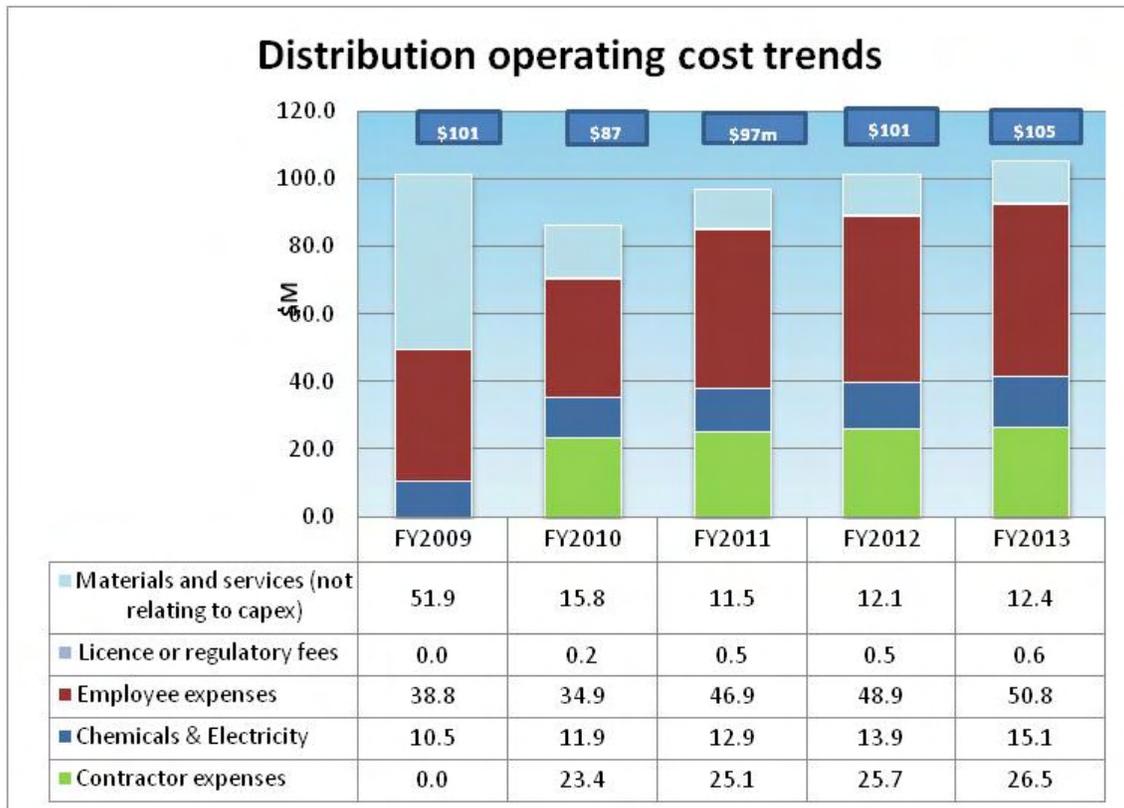
14.6.1 Overview of distribution operating costs

Distribution operating costs relate to the operation of the assets, and exclude bulk water, corporate and retail costs.

As set out above, caution is required when comparing cost information for FY2009 and FY2010 with Unitywater's forecasts. While it remains difficult to make any valid comparisons of distribution operating costs, historic information has been provided below as there is a greater degree of comparability compared to corporate and retail costs.

The following graph provides trends in distribution operating costs over the period of analysis by cost categories.

Graph 14 Distribution operating costs



14.6.2 Explanation of distribution operating cost variances

The above graph shows that a fall between actual distribution operating costs between FY2009 and the Council projected forecasts cost for FY2010, and increase between the Council FY2010 forecast and Unitywater's forecasts in future years. The increase between the Council FY2010 forecast and Unitywater's FY2011 forecast is 12.4% in nominal terms. This apparent increase should be considered with caution, as it is Council's third quarter forecast and well below FY2009 actual.

14.7 Changes in retail operating costs

Moreton Bay and Sunshine Coast water and sewerage businesses did not perform stand-alone retail functions, instead using systems and resources in the corporate areas of each of the Councils. Consequently, retail costs for each of these businesses in the past have been merely allocated on an activity-based or other cost apportionment method by way of corporate overhead charging regimes.

Unitywater has had to develop a retail capacity of its own. The budgeted retail operating costs for FY2011 have not been based on historical data given the very different arrangements in place previously. At the time of the budget submission to the Board, the budgeted retail operating costs were in line with the retail business delivery model that was planned to be in place at that time. This business delivery model has undergone significant changes since this date.

At the time of the initial budget, the retail operating costs were divided across the following teams within retail:

- Retail Directorate
- Business Sustainability & Improvement
- Revenue Assurance
- Customer Service

The retail business delivery model at the time of budget adoption involved a combination of internal and external resourcing. Internal resources for retail functionality were to be sourced through a combination of existing staff transferred from Councils and some proposed new staff as required. Adjustments to the retail staff establishment have been made since the budget and continue to be made, and further changes are likely to take place as the business delivery model is refined. The table below provides a summary of the current position, which varies from the original budget

Table 36 Retail staff establishment (initial view)

| \$(’000) | Direct Salaries and wages | On-cost | Total | FTE |
|--|---------------------------|--------------|--------------|-----------|
| Existing staff from water business. | 891 | 365 | 1,256 | 15 |
| Council staff transferred | 1,406 | 598 | 2,004 | 29 |
| New staff (existing and proposed) | 1,446 | 506 | 1,952 | 19 |
| TOTAL | 3,743 | 1,469 | 5,212 | 63 |

The budget was also based on systems access and support maintenance of existing property data bases and provision of revenue services was being provided by Councils under a service level agreement, along with call centre functionality. The budget was also based on debt collection and meter reading being outsourced to external providers with some in-house capability in relation to data cleansing and validation and credit and collection policies. The budget assumed that billing and receipting was to be supported by a combination of external and in-house resources. Although this is still the transitional arrangement, there are no longer any service level agreements with Councils for these revenue services. The mix and cost of internal and externally provided retail functionality at present is fluid and a significant number of changes have occurred post the initial budget.

The budget also assumed the service delivery model for Retail Revenue Assurance was a blended mix of some functions being performed by transferring staff and other functions being provided by Councils via a service level agreement. It was assumed that this would be the case for the first half of FY2011. It was anticipated that in the second half of the financial year, that Councils would exit from their service level agreement for revenue services and that external contractors would be engaged to do this work. To this end, \$5m of external service provider costs were included in the FY2011 budget. However no allowance has been made for Council’s service level agreement for the first six months of FY2011. This results in an understatement of FY2011 budget costs for retail and will be addressed in Unitywater’s quarterly budget review. Post budget functional structure changes that were known prior to the approval of the budget were included in the final figures. These changes resulted in additional costs, meaning that retail costs may yet increase by \$1.1m (offset by decreases in

Councils SLA costs) from that which is reported in this information return. This is shown separately in the section below.

Unitywater will during the next 12 months further refine service functionality, provider mix and budget for retail activities. Additionally, changes to functional structures post initial budget have meant that retail costs increase by \$1.2m from that reported in the completed templates. This is shown separately in the section below. This impact represents a transfer from the operations budget but does not change total salary costs for Unitywater or materially impact the allocation of costs to services.

14.7.2 Reporting of Retail Operating Costs

In accordance with the Information Requirements final report, retail operating costs have been disclosed separately below. Direct retail operating costs have been reported, and separated from corporate costs as required. It is noted that the final report requires all retail costs including direct labour and materials and allocated overhead to be disclosed. This information is provided separately as part of this report.

Retail direct costs include employee and employee on-costs and all direct non salary and wages costs including contractors.

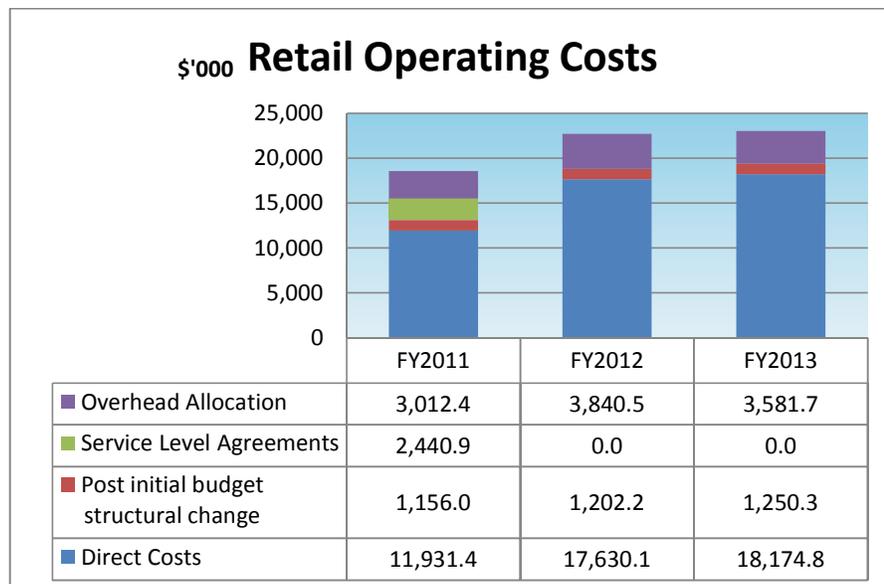
The costs below are sourced from Unitywater's budget with overheads allocated based on percentage of retail direct costs to total entity direct costs.

Retail costs have been allocated to services on the basis of total revenue by geographic region.

It is noted that for this information return, Unitywater has focussed on allocation to services and will be developing over the next year functional based allocations of overheads based on refined cost drivers. This process will be automated and progressed as detailed structures are refined and cost driver information becomes available.

The following graph sets out the forecast retail operating costs by cost categories.

Graph 15 Changes in Retail operating costs (\$nominal)



As can be seen from the above graph, retail costs increase between FY2011 and FY2012. This is primarily related to the full implementation of the retail function and underestimation of Council service agreement costs for FY2011. . The table below summarises explanations for changes in retail operating costs over the period of analysis.

Table 37 Increase in full retail operating costs (\$nominal)

| Explanation for increases in forecasted expenditure: | % | Value (\$M) |
|--|--------|-------------|
| Increase FY2011 to FY2012 | 21.29% | 4.0 |
| <i>Represented by:</i> | | |
| Increase in contractor costs (ext outsource) | | 5.4 |
| Decrease in SLA's | | -2.4 |
| CPI and EBA escalations | | 0.3 |
| Overhead alloc | | 0.7 |
| | | |
| Increase FY2012 to FY2013 | 1.43% | 0.3 |
| represents some savings and CPI & EBA esc | | |

14.7 Changes in corporate costs

Corporate costs include all once-off project costs associated with consolidating the business and the service level agreement costs associated with services that Councils will provide Unitywater to maintain business continuity through the transition period.

New corporate functionality exists from 1 July 2010. Past corporate costs were calculated as an apportionment from Councils of an overhead charge which is not directly comparable to corporate costs reported for FY2011 to FY2013.

The following table provides a dissection of corporate costs for FY2011 to FY2013.

Table 38 Forecast Corporate Costs \$m

| Expense Type \$M | FY2011 | FY2012 | FY2013 | %FY2011 |
|------------------------------|-----------|--------------|-------------|-------------|
| Salaries and Wages | 12.78 | 13.32 | 13.85 | 26% |
| Once-off project costs | 8.27 | 6.02 | 5.11 | 17% |
| Service level agreements | 8.04 | 6.42 | 6.61 | 16% |
| Contractor costs | 5.9 | 5.92 | 6.09 | 12% |
| Fleet and Fuel | 4.91 | 5.16 | 5.54 | 10% |
| Indirect Taxes | 0.9 | 0.9 | 0.9 | 2% |
| Other costs | 9.2 | 9.52 | 9.8 | 18% |
| Total Corporate Costs | 50 | 47.26 | 47.9 | 100% |

It is important to note while the above costs are classified as corporate, they are required to operate the assets and manage the business' operations.

The table above clearly shows that the main contributor to corporate costs is represented by salary and wages expenditure. Although corporate functionality is new, the labour force has been partially sourced from transferred employees from councils who are covered by the current workforce arrangements in force until 2013.

The second largest contribution to corporate costs is represented by once-off project expenditure. Post budget adjustments have been made to the allocation of some once off project costs. This includes approximately \$950k transferred to distribution operating costs in relation to planning initiatives. These costs have been attributed to Water and Sewerage activities equally and categorised as corporate costs. Once off project costs include:

- Salary equalisation in FY2011;
- Project “Paramount” which represents costs for tasks required to be completed in order to align and bring services together;
- Other distribution operating projects which represent costs associated with development of master plans, network modelling and asset management plans; and
- Standards and specifications development and review.

After 1 July 2011 corporate costs are forecast to decline, primarily because of decreasing once off project costs.

14.9 Establishment costs

The information requirement calls for details about approved establishment costs for FY2009 and FY2010, and forecasts of approved establishment costs over the interim price monitoring period.

As discussed in earlier sections, the information template treats these costs as operating costs. In accordance with the Authority’s Ministerial direction, these costs are rather to be treated as additions to the RAB.

Unitywater has been unable to include establishment costs for this information return as these are not yet finalised, but will do so once final information is available from Councils. These establishment costs will be integrated into the final RAB for 1 July, 2010.

Section 15 Non-regulated services

Note:

The historic information set out in this section is based on information provided directly to Unitywater from Councils or obtained from other sources containing Council data (eg the Enterprise Financial Model). Unitywater is not able to confirm the completeness or accuracy of this data, and where possible has relied upon information that has been subject to prior independent audit.

Where information was not available from Councils or other Council sources, Unitywater has sought the reasons for this from each Council.

In undertaking forecasts from FY2010 to FY2013, Unitywater faced considerable information constraints. The original budget was made prior to taking possession of the assets, and with only limited historic information upon which to base projections. Accordingly, the forecasts represent Unitywater’s best estimates when preparing the budget. In some instances, better information has emerged since the original budget, and this information has been described in this information return.

This section describes Unitywater’s non-regulated services inherited from Councils, and provides information at an aggregate level about the revenue and expenditure relating to these services. As set out below, there are information constraints in assigning historic costs and revenues to these services based on limited Council

information, particularly for Sunshine Coast. Common costs have been assigned to these services in accordance with Unitywater's general approach to cost allocation.

A non regulated service is defined by the Authority as a service provided by an entity that is not required to satisfy any specified legal obligation or is provided by other service providers in a competitive market in which the business has no legal power to influence a customer's selection of the business as the service provider.

Unitywater has inherited two such services: laboratory services and private works. These are discussed below for each council.

15.1 Moreton Bay

The laboratories in the Moreton Bay region have previously provided their water testing and other related services to a number of external clients including Seqwater, Linkwater and Moreton Bay Regional Council. Unitywater will continue to provide these services from these facilities.

These same facilities have also provided these services to the drinking water, sewerage and recycled water services provided by the Moreton Bay region. The costs for this have been separately captured and an internal charge made against these services. How this will be treated in the future will depend on the new allocation model as it is developed.

The maintenance crews in the Moreton Bay region also provide what are termed private works services. Private works services are those utilising Unitywater resources on work requested by private customers. An example would be moving a manhole on a customer's property at their request.

15.2 Sunshine Coast

Laboratory and private works services were also inherited from Sunshine Coast Regional Council.

Although it was possible to allocate costs to the non regulated category for the Sunshine Coast the previous Council costing systems did not allow the allocation to specific services. Thus in the template only one generic line titled 'Non Regulated Services – Sunshine Coast' has been shown. A small amount of revenue is shown and this is for laboratory services. It is much smaller than costs because the Sunshine Coast region provided these services to their Council but did not charge for them.

Some level of private works is also undertaken on the Sunshine Coast but no revenue was included in the FY2011 budget. This will be adjusted in future budgets if this service continues.

15.3 Financial details

The table summarises the revenue and costs assigned to non-regulated services at an aggregate level, and summarises financial performance in terms of the building blocks approach. More details are provided in the completed templates.

Based on the information provided in the previous Council format, direct costs have been allocated to services where possible. The allocation methodology has however had to be used to allocate a substantial level of costs between the regulated and non regulated services.

Capital expenditure details on non-regulated services are set out in Section 10, and also provided in the completed template.

Table 42 Non-regulated services – aggregate financial details

| Non Regulated Services | \$M |
|-------------------------------|-------------|
| Budgeted Revenue | 3.79 |
| Operating Costs | 7.20 |
| Depreciation | 0.23 |
| Return on Assets | 0.75 |
| MAR Adjustments | -0.06 |
| Full Cost Recovery | 8.11 |
| Under Recovery | 4.32 |

Section 16 Tax Useful Lives and Asset Values

Section 5.15.1 of the information requirements provides for written down asset values and remaining useful lives for tax purposes to be provided, along with tax lives for new assets or asset classes.

In all cases tax useful life has been assumed to be the same as the regulatory useful life. This assumption may be revised at a later point by Unitywater pending advice from tax consultancies. Accordingly, Unitywater has adopted the regulatory RAB for tax values.

These lives are specified in the template provided to the Authority.

Section 17 Conclusion

Unitywater assumed ownership of its assets on 1 July, 2010. This was preceded by a short, yet intense, period of preparation to take on these new responsibilities, with the entity formally created in November 2009. The creation of Unitywater as a standalone, commercial business presents significant opportunities to adopt new management practices, explore innovation and customise business processes and systems to improve operational performance. While these are longer-term aspirations, the immediate focus is to establish the business, which is in its first year of operations, maintain continuity of service to customers and implement measures to prepare for price regulation.

Unitywater must also deal with legacy issues as it has inherited assets, tariff structures and prices, resources, systems and processes and supplier contracts from the previous Council owners.

This is Unitywater's first information return to the Authority under the interim price monitoring regime, and has been made amidst the transition of water and sewerage assets from Councils.

While there currently a number of information constraints for this return, particularly in relation to prior years, this was not unexpected by the Authority nor the Authority's Ministers. Indeed, the referral notice requires the Authority to consider the availability of information from the entity, their emerging capability to provide information and the transitional work required to integrate and establish the entities and accept the operational constraints imposed by the SEQ Urban Water Arrangements Reform Workforce Framework 2010.

Unitywater has set out a program and timetable to remedy these information constraints and in particular in relation to the opening RAB at 1 July, 2010.

Unitywater's forecast revenues are below MAR, based on reasonable allowances for operating costs and return on and return of assets. Unitywater intends to smooth the price increases on an NPV neutral basis. This will be revised and confirmed in subsequent information returns.

Many systems and processes that would be typical of an established business are under development. This early status of business maturity also has implications for pricing and this information return. For example, it is difficult to establish a MAR with the precision that normally occurs for a mature regulated business. Furthermore, many factors that influence the opening RAB are yet to be finalised.

Unitywater is still in the process of finalising its systems and resources required to operate the business, including new retail and corporate capabilities. Nonetheless, Unitywater has made significant progress already towards the post FY2013 regulatory environment, particularly in regard to its financial systems and governance measures for capital expenditure.

Finally, it is important to note that the Unitywater Board has only just been established, and the strategy for the business is still being developed. The strategy-setting activities of the Board will influence the future direction of Unitywater, including the resourcing arrangements for the business, prioritisation of activities, asset management and development of its capital expenditure program and delivery of that program into the future. The Board also recognises that the strategy for the business must be complementary to its regulatory environment. Indeed its future revenues will be dependent upon the effectiveness of its regulatory strategy and ability to respond to the current and future regulatory regime.