



27 February 2015

Mr Glenn Appleyard
Chair
Tasmanian Economic Regulator
GPO Box 770
Hobart TAS 7001

Dear Mr Appleyard

TasWater Response to 2015 Price Determination Draft Report

Thank you for the opportunity to provide a response to the 2015 Price Determination Investigation Draft Report.

This investigation and price determination will underpin our ability to sustainably meet the expectations of customers, regulators and other stakeholders within an acceptable timeframe. In this regard it is important for all stakeholders to understand that decisions made now will affect the achievement of this aim.

Our response to the Draft Report has therefore been developed through the lens of not just this coming three year period, but the next ten years.

We are of the view that a number of the recommendations in the Draft Report are based on seriously flawed assumptions and methodologies. Implementation of these recommendations will also materially affect the sustainability of the business and therefore our ability to deliver infrastructure and operational improvements in a manner that allows us to balance the needs of all of our key stakeholders.

In particular we contend that our revenue has only recently exceeded the lower limit of sustainability as determined in the first price determination period, and it is against this backdrop that our Draft Price and Service Plan 2015-18 (Draft Plan) was submitted in August 2014 to balance the need to:

- manage customer pricing outcomes (including for those paying above target tariff and those paying below);
- deliver significant improvements in public health and environmental compliance;
- meet owners expectations as set out in the Shareholders' Letter of Expectations; and
- ensure TasWater maintains an appropriate financial position so that it can meet its obligations and deliver the agreed standards of customer service.



With this in mind we are significantly concerned by the Regulator's view on:

- the recovery of revenue during the 2012-15 period;
- the basis on which the revenue limits for each year of the regulatory period are determined;
- the pricing transition path for customers paying above target tariff; and
- the basis for setting and measuring performance against customer service standards.

We have separated out responses on these issues based on errors of fact, differences in methodology and differences in policy positions.

We remain of the view that our Draft Plan is appropriate and sustainably balances the competing needs discussed above. Should the Regulator's proposals be adopted unchanged, however, our ability to balance those needs (including within the timeframes originally anticipated) would be significantly compromised.

In particular, the Regulator's proposed reduction in revenue will lead to a write down in assets of approximately \$100 million at 30 June 2015. This will result in TasWater reporting a significant after tax loss, eliminate all of TasWater's retained earnings balance, reduce the value of our shareholder equity, and could result in a negative impact on TasWater's credit rating.

Given dividends would not be underpinned by a positive retained earnings balance, the Directors of TasWater will need to consider whether a reduction or cessation of dividend payments to Owners is warranted. We are of the view that a change of this nature arising from unsound assumptions and methodologies compromises our ability to fulfil the requirements of the Water and Sewerage Corporation Act (2012).

We welcome the comments and feedback on areas of policy and those areas that the Regulator has accepted.

We remain committed to working closely with you and your officers to finalise the determination and Price and Service Plan that will underpin our ability to make a long term difference for the Tasmanian community.

Yours Sincerely

A handwritten signature in black ink that reads "Miles Hampton".

Miles Hampton
Chairman



**TASWATER RESPONSE TO
THE ECONOMIC REGULATOR'S
2015 PRICE DETERMINATION INVESTIGATION
DRAFT REPORT**

Document Approval and Issue Notice

TasWater Response to the Economic Regulator's 2015 Price Investigation Draft Report is a controlled document. Recipients should remove superseded versions from circulation. This document is authorised for issue once it has been approved.

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1. Executive summary

TasWater welcomes the opportunity to review the Regulator's draft report on TasWater's proposed prices and service levels for the 2015-18 regulatory period.

This investigation and price determination will underpin TasWater's ability to sustainably meet the expectations of customers, regulators and other stakeholders within an acceptable timeframe. Decisions made now will affect the achievement of this aim.

TasWater's response to the draft report has therefore been developed through the lens of not just this coming three year period, but the next ten years.

TasWater contends that its revenue has only recently exceeded the lower limit of sustainability. It is against this backdrop that the Draft Price and Service Plan 2015-18 (draft plan) was developed to balance the need to:

- manage customer pricing outcomes (including for those paying above target tariff and those paying below)
- deliver significant improvements in public health and environmental compliance
- meet owners expectations as set out in the Shareholders' Letter of Expectations
- ensure TasWater maintains an appropriate financial position so that it can meet its obligations and deliver the agreed standards of customer service.

In reviewing the Regulator's draft report TasWater has identified a number of material differences between the draft plan and the Regulator's draft report.

The key areas of difference relate to:

- the recovery of revenue during the 2012-15 period
- the basis on which the revenue limits for each year of the regulatory period are determined
- the pricing transition path for customers paying above target tariff
- the basis for setting and measuring performance against customer service standards.

The reason for the differences can be categorised in the following three ways:

1. Matters where the Regulator's position is based on errors of fact
2. Matters where there is a difference in methodology
3. Matters where there is a difference in policy position

A summary of TasWater's assessment of the differences listed above is set out in section 3 with a detailed analysis provided in Appendix 1.

It is important to note that the Regulator has used some of its proposals, including those where there are errors of fact, as justification for its major policy proposal regarding the pricing transition for customers paying above target tariff.

TasWater is strongly of the view that the Regulator should acknowledge the first category of differences noted above and make the appropriate corrections in its final report.

TasWater remains of the view that its draft plan is appropriate and sustainably balances the competing needs discussed above.

Should the Regulator's proposals be adopted unchanged, however, TasWater's ability to balance those needs (including within the timeframes originally anticipated) would be compromised, as would the overall sustainability of the business.

More specifically, the Regulator's proposal would decrease TasWater's revenues by \$36.902 million across the 2015-18 period, with the majority of the decrease in revenue (being \$19.779 million), realised in year one.

This would in turn result in 2015-16 net profit after tax (NPAT) being reduced by \$11.813 million (or 40.2 per cent) on the prior year result. The cumulative effect of this is to decrease year 10 NPAT by \$9.731 million (or 21.3 per cent), increase borrowings over that period by \$96.767 million (or 18.6 per cent) and increase the gearing level from 30.4 per cent to 38.3 per cent, a level that is much closer to those of well-established and mature Australian water businesses.

From our preliminary analysis, the reduction in revenue will lead to a write down in assets of approximately \$100 million at 30 June 2015¹. This write down will eliminate all of TasWater's retained earnings balance (the balance will be negative) and could result in a negative impact on TasWater's credit rating.

TasWater also believes that its ability to fulfil all of the principal objectives of the corporation as set out in section 6 of the *Water and Sewerage Corporation Act 2012* will be compromised.

These financial impacts would also mean that TasWater's future capacity to partially or fully self-fund major strategic projects such as rationalisation of Launceston and Hobart's ageing and non-compliant sewage treatment plants and associated infrastructure is diminished.

Should these projects ultimately be signed off by the technical regulators as the most cost effective means of addressing key infrastructure challenges in the State's major cities, TasWater will have to seek agreement to either:

- substantial increases in prices for customers over a number of years, as opposed to the current aim which is to progressively reduce the size of tariff increases over subsequent regulatory periods; and/or
- implement the agreed solutions over a longer timeframe.

While these matters will not be realised until after this next regulatory period, it is our strong contention that they must be considered now in order to ensure that a step change in prices or changes to the delivery of agreed projects/outcomes can be avoided.

Other matters

TasWater notes the Regulator's comments and proposals regarding issues associated with the provision of services to customers. With the exception of developer charges, customer service standards and the guaranteed service level (GSL) scheme, which are discussed further below, TasWater does not have material concerns with the Regulator's position on these matters and is working through each policy to ensure the Regulator's suggestions are appropriately reflected.

¹ We are currently modelling the exact impact on retained earnings and will forward a final set of numbers in due course.

Developer charges

TasWater does not support headworks being charged into the future where capacity has been installed. TasWater remains committed to its proposed policy, particularly in the medium to longer term and is of the view that it provides the most appropriate arrangements for Tasmania.

In recognising, however, that the timing of the development of the Strategic Asset Management Plan creates a degree of uncertainty, TasWater proposes that an interim developer charges policy arrangement based on TasWater's approved serviced land area could apply for this regulatory period.

Customer service standards

TasWater notes the Regulator's intention to change the basis on which these are determined and measured, from averages to actual minimums. While TasWater is of the view that averages provide better incentives for businesses to drive efficiency, particularly at this stage in the business' maturity, TasWater is open to exploring the possibility of actual minimums for some indicators with the Regulator for this regulatory period.

TasWater remains concerned, however, about the quality of its data, and that systems and processes required to fully comprehend its underlying performance, and operate under a more sophisticated framework such as actual minimum service standards, do not yet exist.

It is expected that TasWater will make significant progress with the development and implementation of systems and processes over the coming regulatory period such that consideration of a number of matters, including customer service standards, will be more detailed and based on better data in subsequent regulatory periods.

Guaranteed Service Level (GSL) Scheme

TasWater does not support the Regulator's proposal that the Government consider the introduction of a guaranteed service level scheme.

2. Introduction

TasWater commenced operations on 1 July 2013 as Tasmania's statewide provider of water and sewerage services through the merger of the three regional corporations – Ben Lomond Water, Cradle Mountain Water and Southern Water – and their common service provider Onstream.

TasWater is currently, until 30 June 2015, operating under three Price and Service Plans (PSP) that were approved by the Tasmanian Economic Regulator (the Regulator) in 2012 for the former regional corporations.

In late 2013 the Regulator issued the *Tasmanian Water and Sewerage Industry, 2014-15 Price Determination Investigation, Price and Service Plan Guideline, November 2013* to assist TasWater with the preparation of its proposed PSP for the three year regulatory period commencing on 1 July 2015.

TasWater submitted its draft 2015-18 PSP (draft plan) to the Regulator on 29 August 2014. The draft plan articulates and commits to a set of outcomes and prices to be delivered over the period, which were developed with a view to striking a balance between removing the complexities associated with current pricing arrangements and addressing infrastructure challenges.

The major elements of our draft plan have been endorsed by Owner Councils as an appropriate balance of the competing priorities.

Over the period September to December 2014, TasWater worked closely with the Regulator's office to clarify a number of issues and provide additional information in support of the proposals set out in the draft plan.

The Regulator then released its *2015 Price Determination Investigation – Regulated Water and Sewerage Services in Tasmania Draft Report* on 9 January 2015.

TasWater has reviewed the Regulator's draft report, and in doing so has again worked closely with the Regulator, and the business' responses are presented throughout this report.

TasWater looks forward to working with the Regulator throughout the remainder of the price determination investigation to ensure optimal outcomes for water and sewerage customers and the Tasmanian community are achieved.

3. Key Matters

TasWater’s draft plan was developed in order to balance the competing needs of customers, regulators and stakeholders. In TasWater’s view the suite of proposals contained therein appropriately manages affordability for customers, with delivery of commitments to regulators, customers, communities and owners. The draft plan was also developed within the context that TasWater’s revenue has only recently exceeded the lower limit of sustainability.

The Regulator has released a draft report that differs from TasWater’s draft plan in a number of key areas, including:

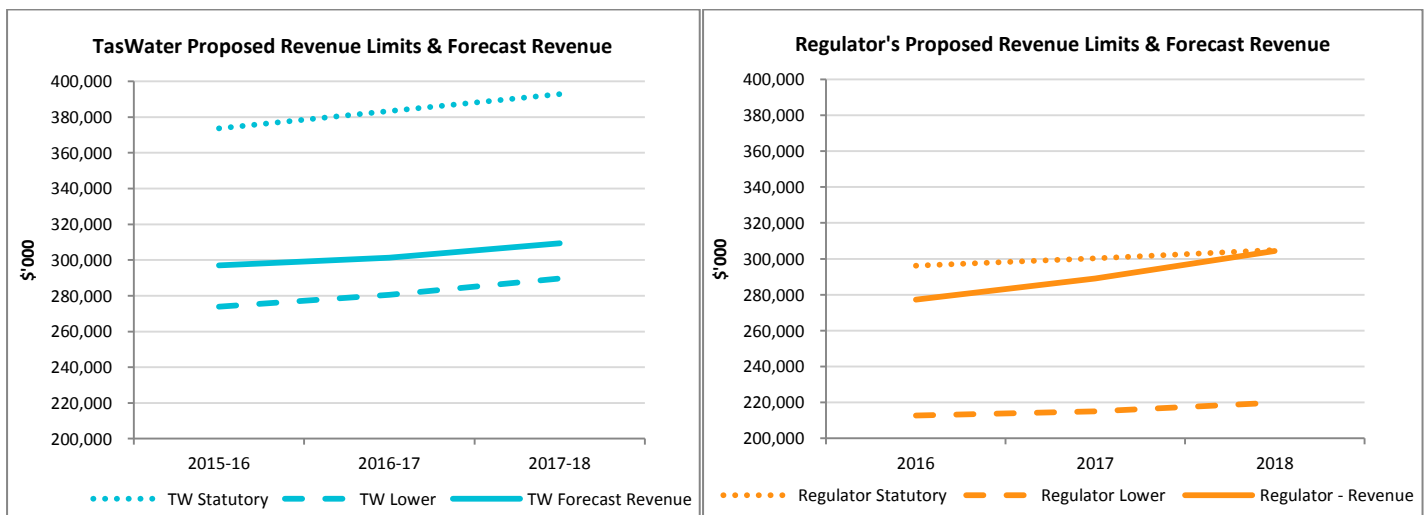
- the recovery of revenue during the 2012-15 period
- the basis on which the revenue limits for each year of the regulatory period are determined
- the pricing transition path for customers paying above target tariff
- the basis for setting and measuring performance against customer service standards.

The reason for the differences can be categorised in the following three ways:

1. Matters where the Regulator’s position is based on errors of fact
2. Matters where there is a difference in methodology
3. Matters where there is a difference in policy position

The differences falling under categories 1 and 2 primarily impact on the calculation of TasWater’s revenue limits. As a result, the Regulator has proposed alternate values for each of the lower, statutory and upper revenue limits, and the components thereof, in its draft report. A comparison of the Regulator’s and TasWater’s revenue limits, which are clearly materially different, is set out in the figures below.

Figure 1: Comparison of revenue limits under TasWater’s draft plan and the Regulator’s draft report



The Regulator has used its view on revenue limits and the recovery of revenue as justification for its major policy proposal regarding the price transition for customers paying above target tariff.

In reviewing the Regulator’s draft report, TasWater has not been presented with any information or compelling arguments that its draft plan is fundamentally flawed and would result in inappropriate or unacceptable outcomes, particularly in the context of needing to balance a number of competing needs.

TasWater’s view on the individual matters that fall within each category mentioned above is summarised in the following sections and addressed in further detail throughout the Appendices to this report.

In addition, TasWater’s assessment of the impact of the Regulator’s proposals, should they be adopted unchanged, is also detailed in the following sections.

3.1. Matters where there is error of fact

TasWater considers there are three significant areas in which there are errors in the Regulator’s proposals.

The first issue is the revenue recovered during the 2012-15 period, which has informed the Regulator’s policy position on the price transition for customers paying above target tariff.

The second issue impacts the calculation of TasWater’s lower and statutory revenue limits, which (when considering actual forecast revenue) have also informed the Regulator’s policy position on the price transition for customers paying above target tariff.

3.1.1. Over-recovery of revenue

The Regulator has stated in its draft report that TasWater will have recovered revenue of some \$80 million in excess of the estimated revenues provided by the former regional corporations in 2012 during the first regulatory period.

TasWater considers this conclusion is based on underlying assumptions and a comparison that is factually incorrect, and advises that there will in fact be an under-recovery of revenue for the 2012-15 period when comparing regulated revenue approved by the Regulator in the 2012 determination with the former corporations’ and TasWater’s actual (and budgeted) regulated revenue.

TasWater’s comparison of approved and actual /forecast regulated revenue during the 2012-15 period is set out in the following table.

Table 1: Comparison of approved and actual/forecast regulated revenue for 2012-15

Revenue source ¹	Nominal 3 year Revenue (\$'000) (as per 2012 price determination)	Actual Revenue (\$'000) (including budget for 2014-15)	Variance (\$'000)
Fixed water and sewerage	575,673	593,845	18,172
Variable water and sewerage	131,595	126,892	(4,703)
Trade waste	23,046	27,356	4,310
Supplementary revenue ²	21,232	0	(21,232)
Total	751,546	748,093	(3,453)

Notes:

1. Revenue sources such as grants, contributed assets, interest and other revenue which are detailed in TasWater’s statutory accounts are not included in the comparison as they are not classified as regulated revenues.
2. Southern Water’s approved 2012-15 Price and Service Plan included an allowance for customer revenues that had not been brought into the customer impact model at the time the PSP was prepared (refer page 180 of Southern Water’s 2012-15 Price and Service Plan).

This issue is important as the Regulator’s view that TasWater has over-recovered revenue is used as a key justification to support the proposal that TasWater should and can afford to increase the pace of the price transition for customers above target beyond what was proposed in the draft plan.

Putting aside the matter of whether the policy position on the price transition is appropriate or not, the justification for the policy position should not be based on erroneous information.

TasWater requests the Regulator review the assessment of 2012-15 revenues and make the appropriate corrections in its final report.

3.1.2. Operating expenditure allowance – real vs nominal values and adoption of Jacobs’ recommendations

In its draft report the Regulator has proposed an opex allowance that is \$14.3M lower in year 1, \$18.4M lower in year 2, and \$22.5M lower in year 3 than TasWater’s proposed opex set out in the draft plan.

It is important to note that TasWater’s proposed opex values are presented in nominal dollar terms, consistent with the remainder of the draft plan.

The Regulator’s values appear to be real dollar amounts, given the minimal growth year on year and that the Regulator has proposed the adoption of a growth rate of 0.3 per cent per annum in section 5.5 of the draft report.

As shown in Table 2 the inconsistent use of nominal and real values accounts is a significant part of the difference between TasWater and the Regulator’s proposed opex allowances over the three year period.

In addition, TasWater also notes that in the draft report the Regulator has proposed to accept Jacobs’ recommendations regarding opex, which would include the baseline allowance (being the 2013-14 combined approved allowance less sustainable merger savings) and increasing that amount to account for the impact of the capital program on opex.

TasWater’s draft plan was developed prior to Jacobs’ review and as such its proposed opex values for each year of the period are not inclusive of an uplift as recommended by Jacobs.

In reviewing the draft report, putting aside the issue of comparing nominal values with real values, TasWater is unable to reconcile the Regulator’s proposed allowance with the values recommended by Jacobs. The Regulator’s values appear to be \$3.8M less in each year than Jacobs’ values.

All of this indicates that the Regulator’s proposed opex allowance amounts are too low in each year of the period.

A summary of proposed opex allowances, including the difference between the real and nominally based amounts, is set out in the following table.

Table 2: Comparison of proposed opex allowances

	2014-15 (\$'000)	2015-16 (\$'000)	2016-17 (\$'000)	2017-18 (\$'000)
TasWater proposed opex allowance (nominal\$) (A)		160,301	164,676	169,173
Regional corporations combined allowance less merger savings of \$5.4M (B)	146,135			
Regional corporations post merger allowance adjusted for CPI (B*2.5% pa = C) ¹		149,788	153,533	157,371
Variance – PSP2 to regional corporations adjusted opex (A-C)		10,513	11,143	11,802
Actual opex as per statutory accounts (D) ²	160,322			
Regulator proposed opex allowance (E) ³		145,965	146,265	146,665
Regulator proposed opex allowance (nominal) (E*2.5% pa = F)		149,614	153,670	157,942
Variance –regional corporations adjusted opex to Regulator’s proposed opex (nominal) (C-F)		174	(137)	(571)
Variance – TasWater proposed opex to Regulator’s proposed opex (real) (A-E)		14,336	18,411	22,508
Variance – TasWater proposed opex to Regulator’s proposed opex (nominal) (A-F)		10,687	11,006	11,231

Notes:

1. Adjusted values do not include any allowance for the opex uplift due to the capital expenditure program (as per Jacobs’ calculation and recommendation)
2. Actual costs include unregulated expenditure while all other numbers exclude unregulated expenditure
3. TasWater assumes these values are presented in real dollars given the minimal growth year on year

Table 2 shows that after accounting for the incorrect comparison of nominal and real values there is a difference of approximately \$11 million each year between TasWater’s proposal and the Regulator’s proposal. The reasons for this difference are discussed further in section 3.2.4.

The comparison of nominal values against real values is incorrect and TasWater requests the Regulator review its analysis and amend its final report to ensure the consistent use of nominal and real dollar amounts. Furthermore, TasWater requests the Regulator review its calculations regarding:

- the roll forward of approved opex for the former regional corporations in 2012; and
- the inclusion of an allowance to reflect the impact of the capital program on opex.

3.1.3. Capital expenditure allowance – conversion of nominal to real values

In its draft report the Regulator has stated that it intends to maintain the proposed total capital program of \$330 million over the coming three year regulatory period. In doing so the Regulator has accepted Jacobs’ advice to re-profile the capital expenditure within the period (as set out in section 4.4.1 of the draft report).

TasWater notes, however, that Jacobs’ conversion (tables 4.2 and 4.3) of the proposed expenditure from nominal to real dollars contains an error. TasWater is of the view that there was an error in Jacobs’ calculation, in that the correct method is $Nominal \$ = (Real \$) / (Inflation rate \times t)$ whereas Jacobs have calculated real dollars as $Nominal \$ = Real \$ \times (100 - Inflation rate \times t)$. This difference in approach has an impact in the order of approximately \$373,000 (real) for the 2015-18 period.

A summary of the proposed capex values is set out in the following table.

Table 3: Comparison of proposed capex allowances

	2015-16 (\$'000)	2016-17 (\$'000)	2017-18 (\$'000)
TasWater proposed (nominal)	110,000	110,000	110,000
Jacobs (real 2015\$)	107,250	104,570	101,960
Unregulated capex to be deducted	921	970	0
Economic Regulator's proposed capex ¹	95,609	103,600	112,690
TasWater calculation of correct capex allowance ²	96,640	103,730	111,902
Variance	1,031	130	(788)

Notes:

1. These values reflect Jacobs' recommendation to reduce the allowance by 10 per cent in year one and increase the allowance in year 3. They are also net of unregulated capex.
2. TasWater's calculations reflect the methodology discussed above and is net of unregulated capex.

TasWater requests the Regulator review the methodology for converting the nominal values to real values.

3.2. Matters where there are methodological differences

There are a number of matters throughout the Regulator's draft report where the methodology used to determine allowances differs from that proposed by TasWater in the draft plan.

Each of the methodological differences impacts on the calculation of TasWater's lower and statutory revenue limits, which (when considering the actual forecast revenue for the period) have informed the Regulator's policy position on the price transition for customers paying above target tariff.

3.2.1. Asset Renewal Annuity (ARA)

In its draft report the Regulator has proposed an ARA for the coming period that is less than half that proposed by TasWater in the draft plan and over 40 per cent lower than the amount approved for the regional corporations in 2012.

In its draft plan TasWater proposed an Asset Renewal Annuity (ARA) of approximately \$95 million (being \$45.5 million for water and \$46.7 million for sewerage) for each year of the regulatory period. TasWater's proposed amount compares to a combined ARA total of \$80.2 million that the Regulator approved for the former regional corporations in 2012.

TasWater's proposed ARA is not dissimilar to its proposed calculation of regulatory depreciation on new and existing assets for the regulatory period (with forecast depreciation of \$96.7 million exceeding the proposed ARA in 2017-18). Nor is it dissimilar to the 2014-15 combined regulatory depreciation allowance approved by the Regulator in 2012 for the regional corporations (being \$91.6 million in 2014-15).

The ARA is a key component of the lower revenue limit which was used by TasWater to determine the proposed water and sewerage target charges set out in the draft plan. It is an important issue in that the ARA is a significant determinant of the level of TasWater's minimum operating sustainability.

TasWater's comparison of the proposed ARA values with that approved by the Regulator for the regional corporations in 2012 is set out in the following table.

Table 4: Comparison of Asset Renewal Annuity proposed allowances

Asset Renewal Annuity	2014-15 (\$'000)	2015-16 (\$'000)	2016-17 (\$'000)	2017-18 (\$'000)
Combined regional corporations approved allowance	80,238			
TasWater proposed allowance		95,191	95,191	95,191
Regulator's proposed allowance		45,031	45,031	45,031
Variance		(50,160)	(50,160)	(50,160)

TasWater requests the Regulator review its methodology and rationale for determining the ARA.

3.2.2. Depreciation

The Regulator has proposed an average annual depreciation that is approximately \$20 million per annum lower than that proposed by TasWater in its draft plan and approximately \$16 million per annum lower than the amount approved for the regional corporations in 2012.

In the draft plan TasWater proposed an average annual depreciation of approximately \$93 million per annum for each year of the regulatory period. This compares to an average annual depreciation of approximately \$89 million per annum previously approved by the Regulator for the former regional corporations in 2012.

A comparison of the proposed depreciation allowances with that approved by the Regulator for the regional corporations in 2012 is set out in the following table.

Table 5: Comparison of proposed depreciation allowances

Depreciation	2014-15 (\$'000)	2015-16 (\$'000)	2016-17 (\$'000)	2017-18 (\$'000)
Combined regional corporations approved allowance	91,588			
TasWater proposed allowance		89,741	93,227	96,671
Regulator's proposed allowance		71,437	73,012	74,733
Variance		(18,304)	(20,215)	(21,938)

In calculating its depreciation estimate, the Regulator has used the same data set as that provided by TasWater. However, TasWater and the Regulator have used a differing approach to determining the average useful lives and resultant depreciation charge.

TasWater's methodology was used to calculate the depreciation charge in the 2013-14 Regulatory Accounts. These accounts were audited by the Tasmanian Auditor-General, who did not object to the methodology or the resultant depreciation charge. These accounts were provided to the Regulator in December 2014.

TasWater is of the view that the Regulator's use of TasWater's data set but proposal of an alternative methodology is flawed, and by implication suggests that the audited regulatory accounts for 2013-14 are incorrect.

In addition, TasWater contends that the Regulator's methodology overstates the calculated useful asset life as the longer life assets represent a disproportionate amount of the opening RAB. Effectively this means that the depreciation allowance will be understated.

TasWater considers a reduction in the regulatory depreciation allowance for this regulatory period as proposed by the Regulator may impact on the business' ability to undertake renewals going forward, or a step-change in the depreciation allowance may be needed in the next period once additional data and information has been collected.

TasWater requests the Regulator review its methodology for determining useful asset lives and therefore the depreciation allowance.

3.2.3. Weighted Average Cost of Capital – calculation of risk free rate and debt risk premium

In its draft report the Regulator has proposed alternate methodologies for calculating the risk free rate (RFR) and the debt risk premium (DRP) components of the WACC. The difference in methodology results in a reduction in TasWater's nominal pre-tax WACC of approximately 21 basis points.

TasWater, with the assistance of external independent advice, proposed a consistent trailing average methodology be used for both components (based on a combination of 10 year long term data together with 40 day short term data). This methodology has also been adopted by two of Australia's largest and most experienced regulators in the AER and IPART.

TasWater's methodology is considered to appropriately reflect the actual borrowing behaviour of regulated entities and remove the volatility associated with financial markets (including fluctuations in the interest rate cycle which ensures that the WACC is not set too high when rates peak and not too low when rates trough).

The Regulator's approach, particularly the use of a short term average only for the DRP, which is based on an outlying method adopted by the ERA in Western Australia, set the DRP at the low point of the interest rate cycle thereby undesirably creating more exposure for TasWater as and when interest rates go up.

TasWater considers the Regulator's methodology is flawed and requests the calculation of the RFR and DRP be reviewed for the final report.

3.2.4. Operating expenditure allowance – other matters to be taken into account

As discussed earlier, in its draft report the Regulator has proposed an opex allowance that is \$14.3M lower in year 1, \$18.4M lower in year 2, and \$22.5M lower in year 3 than TasWater's proposed opex set out in the draft plan.

After adjustments to account for the incorrect comparison of nominal and real values and to adopt Jacobs' recommendations as proposed by the Regulator, TasWater acknowledges that its proposed opex is above the values recommended by Jacobs.

TasWater considers the difference to be reasonably justifiable in that the former regional corporations, from which the proposed opex allowance is based, developed forecast opex in the early stages of their existence, having only just been through the first phase of industry reform with incomplete asset data and while there were many unknowns about the operation of the businesses.

With a second phase of reform completed, and TasWater now established, many of the previously unidentified costs of operations have become clearer conceptually, and have been incorporated into the

opex forecasts via year on year budget development between 2012 and 2015. This explains the remaining variance between the 2012 allowance and actual opex (and TasWater's proposed opex for 2015-18).

TasWater requests the Regulator review its proposed opex allowance to ensure that previously unidentified costs are appropriately incorporated into the forecasts.

3.2.5. Opening regulated asset base (RAB)

In its draft report the Regulator has proposed an opening RAB value of \$3.0 billion, which is \$36.883 million lower than proposed in TasWater's draft plan, based on an assumption that TasWater has not accounted for the full capex underspend over the 2012-15 period. The Regulator has arrived at its proposed value by adjusting the forecast closing RAB of the former regional corporations by the amount of the underspend.

TasWater has, on the other hand, calculated the opening RAB by tracking actual movements in the RAB from year to year throughout the 2012-15 period. The actual capital underspend (and forecast for 2014-15) is therefore taken into account, as are other relevant factors, including:

- variations in, and substitution of projects undertaken during the period
- the amount and timing of individual capital projects
- the in-service data of the resulting asset(s)
- the individual components of the asset(s) and the useful lives assigned to those components

The Regulator's methodology fails to acknowledge and account for other factors that affect the value of the opening RAB.

TasWater contends that the Regulator's assumptions are flawed and requests the Regulator review its calculation of the opening RAB.

3.2.6. Third party contributions

In its draft report the Regulator has included government grant income within the scope of third party contributions.

TasWater does not object to this approach, however, it is of the view that the Regulator has incorrectly interpreted the nature of some of the income TasWater has included within the scope of grant income. Specifically, grant income includes the Tasmanian Government subsidy for headworks charges and grant funding for non-regulated reuse assets. TasWater believes these amounts should be excluded from the total of third party contributions deducted from the RAB.

When undertaking revenue limit calculations, third party contributions are deducted from capital expenditure. However, to ensure RAB values are not understated, the assets that these contributions generate should be included within gross capital expenditure estimates to ensure the RAB is not understated. TasWater notes that the Regulator does not appear to have included these amounts in the gross capital expenditure estimates in the draft determination.

TasWater requests the Regulator review its treatment of third party contributions. Further, TasWater notes that as the above amounts disclosed in the draft plan were nominal values, the Regulator should ensure, where necessary, that adjustments are made on an accurate and consistent basis.

3.3. Matters where there are differences in policy position

In addition to the differences relating to factual errors and methodology, TasWater considers there are four key policy matters on which the Regulator and TasWater differ.

TasWater's comments and observations on each of these policy positions are set out in the following section.

3.3.1. Water fixed charges

In its draft report the Regulator has proposed target water fixed charges be set at TasWater's proposed 2017-18 rate of \$329.48 for each year of the period.

In the draft plan, TasWater proposed that target water fixed charges increase by 6 per cent each year (consistent with the approach for target sewerage fixed charges) off a base of \$293.24. This base was determined through targeting TasWater's understanding of the lower revenue limit appropriate for it as a single statewide business.

TasWater considers its proposal is appropriate on the basis that this regulatory period, being the first for TasWater as a statewide provider of water and sewerage services, is the best time to reset prices that take account of the benefits associated with having one business which is in turn reflected in a continued price transition journey for customers.

In addition, consistent with the intent set out in the draft plan, TasWater considers that prices will need to continue increasing beyond this regulatory period, albeit at a lesser rate, as a result of the major capital program that still needs to be completed.

Should the Regulator choose to adopt its proposal to set flat water charges in this period it risks sending the wrong message, ie that water fixed charges no longer need to increase, despite TasWater's capital program requirements which clearly demonstrate the need for future price increases.

The Regulator, in proposing flat target water fixed charges, is also in effect introducing another price transition for customers, which is likely to be confusing and an unnecessarily complex 'pricing story' for TasWater to communicate. It means that target sewerage fixed charges are transitioning one way (6 per cent per annum), variable water charges are transitioning in another way (2.5 per cent) and the arrangements for target water fixed charges are different again.

It should also be noted that the Regulator's proposal to move straight to \$329 for fixed price for water on 1 July 2015 will present an increase to customers on fixed tariff in the south of approximately 8 per cent.

In light of this, TasWater requests the Regulator reconsider its proposal to set flat target water fixed charges for the duration of the period.

3.3.2. Price transition arrangements for customers paying above target tariff

In its draft report the Regulator has proposed transitioning all customers above target straight to target on 1 July 2015.

TasWater proposed transitioning these customers down over a three year period, two years ahead of the legislated deadline of 2020, which when combined with the other price transition proposals would mean there is only a small cohort of customers not at target by 2018 (being those who are below and were materially away from target).

TasWater considers that its entire suite of proposed price transition arrangements set out in its draft plan are appropriate, affordable and sustainable, and see customers transitioning to a level playing field quickly while also allowing TasWater to balance other competing priorities and outcomes. The proposal broadly sees the majority of customers both below and above target transition to target over a similar period of time, meaning that the pricing message is manageable in terms of complexity.

As discussed earlier in this response, the Regulator has used its different revenue limits and conclusion about TasWater's recovery of revenue during the 2012-15 period as justification for its proposed price transition arrangements.

TasWater has raised a number of issues with those assumptions that significantly challenge the validity of the Regulator's position. TasWater has further significant concerns about the impact of the Regulator's proposal on its sustainability.

TasWater is therefore of the view that the Regulator should reconsider its price transition proposal in light of the information presented in this response.

TasWater has modelled the Regulator's price transition proposal to understand the materiality of the impacts on the business' sustainability.

Should the Regulator's position be adopted unchanged it reduces TasWater's revenues by \$36.902 million over the 2015-18 period, with the majority of the reduction in revenue (\$19.779 million) realised in year one. This results in 2015-16 net profit after tax (NPAT) decreasing by \$11.813 million (or 40.2 per cent) on the prior year result. The cumulative effect of this is to:

- decrease year 10 NPAT by \$9.713 million (or 21.3 per cent)
- increase borrowings over the period by \$96.767 million (or 18.6 per cent)
- increase the gearing level from 30.4 per cent to 38.3 per cent².

From our preliminary analysis, the reduction in revenue will lead to a write down in assets of approximately \$100 million at 30 June 2015³. This will result in TasWater reporting a significant after tax loss, eliminate all of TasWater's retained earnings balance, dividends (if paid) would not be underpinned by a positive retained earnings balance and the business' credit rating could be negatively impacted.

The impact of the Regulator's proposal on overall business sustainability is that TasWater would not be able to fulfil all of the principal objectives of the corporation as set out in section 6 of the *Water and Sewerage Corporation Act 2012* (the Corporation Act). Specifically, TasWater will not be in a position to fulfil section 6(1)(c)(i) and 6(1)(c)(ii):

- (c) to be a successful business and, to this end –*
- (i) to operate its activities in accordance with good commercial practice; and*
 - (ii) to deliver sustainable returns to its members; and*

An outcome where TasWater is unable to meet these legislative provisions would not be acceptable. Further, it is important to note that the increase in gearing level diminishes TasWater's capacity to self-fund major strategic projects such as the Launceston and Hobart Sewerage Improvement Projects.

² This assumes the Hobart and Launceston Sewerage Improvement Projects do not proceed or they are fully funded by Government. In the event that TasWater partially funds the Projects (by 40 per cent) the gearing level would increase to 53.2 per cent, and were TasWater to fully fund the Projects the gearing level would increase to 71.5 per cent.

³ We are currently modelling the exact impact on retained earnings and will forward a final set of numbers in due course.

In discussing increases in TasWater's gearing, it is important to also consider the gearing levels of other water businesses. The average gearing level⁴ for the Australian water industry is 45 per cent, with many businesses (including Sydney Water, Queensland Urban Utilities, Hunter Water and Yarra Valley Water, all of which are established and mature) falling somewhere between 35 and 50 per cent. While these figures suggest an increase would result in TasWater being in line with other water businesses, TasWater's circumstances, including the quality of data relating to infrastructure and capital program requirements, create uncertainties that may result in increases to the business' gearing level over time. That being the case, and at this early stage in TasWater's existence, it would not be prudent to make policy decisions that leave TasWater with a high gearing level.

In conclusion, TasWater is strongly of the view that the Regulator's proposed price transition and reduction in revenue would result in an unacceptably high gearing level that would not be commensurate with the business' counterparts in other states (given the relative states of maturity). Further, it would compromise TasWater's ability to deliver a capital program that meets the expectations of technical regulators in particular.

3.3.3. Developer charges

In the draft report the Regulator has considered and presented three alternative approaches for developer charges in addition to TasWater's proposed policy and the current IPART methodology. Each alternative involves headworks being charged in some form in the future.

TasWater does not support headworks being charged into the future where capacity has been installed, including post the conclusion of the Government waiver policy in April 2016, and is of the view that there will be very little, if any, other support provided for such a concept.

TasWater remains committed to its proposed developer charges policy, particularly in the medium to long term, as it incentivises development in line with strategic land use planning and continues to deliver price signals (ie relative to the burden the development places upon infrastructure capacity) and therefore provides the most appropriate arrangements for Tasmania.

Notwithstanding this, TasWater does recognise the Regulator's concern that the timing of the development of its first Strategic Asset Management Plan (SAMP) presents some challenges. On this basis TasWater has recommends an alternative interim developer charges policy arrangement be applied for this next regulatory period. The interim arrangement would be based on the approved serviced land area and involve no charge for developments within serviced land and user (ie developer) pays for developments outside serviced land. Consistent with the Regulator's draft report, there would also be no change to the current arrangements for works internal and works external.

TasWater notes that this would be an interim arrangement only, with the proposal as set out in the draft plan to be adopted for the regulatory period commencing 1 July 2018. This would allow sufficient time for TasWater to undertake condition assessments and to more fully work through the detailed methodology for calculating and imposing out of sequence and isolated development charges with the Regulator prior to implementation of the policy.

TasWater requests the Regulator approve this proposed interim policy for the 2015-18 period.

⁴ Data based on information sourced from recent annual reports of other Australian water utilities.

3.3.4. Customer service standards

In its draft report the Regulator has proposed that frequency and duration related customer service indicators be measured on an actual minimum basis as opposed to the current basis of measure which is average.

In the draft plan TasWater proposed targets for each customer service standard indicator that would see the current minimum service standards as outlined in Schedule 1 of the Customer Service Code (noting that they are measured on an average basis) met by 2017-18.

TasWater notes that its proposed targets may be ambitious in some instances, however the business does not yet have the well-developed systems and processes that enable the collection and analysis of asset data necessary for a more robust understanding of customer service standards. In this regard, TasWater is concerned that consideration of actual minimums will drive outcomes that are at odds with the priorities set by the technical regulators and our legislative obligations (eg redirection of capital expenditure from compliance to renewals, particularly on linear assets).

A number of projects are under development to improve our data collection and analysis capability. It is expected that these projects will place TasWater in a better position to provide more accurate and evidence-based customer service standard targets for the next regulatory period.

TasWater is of the view that averages (particularly for response times) have demonstrably driven increased performance across the water sector nationally and therefore serve as a better basis for driving improved service outcomes. However should the Regulator determine that the use of minimum standards are appropriate, we would recommend they are limited to frequency and duration related customer service indicators.

Notwithstanding our concerns regarding the use of minimum standards as opposed to averages, TasWater is open to further discussions with the Regulator regarding minimum targets for the following indicators for the 2015-18 regulatory period:

- Average time taken to attend bursts and leaks – Priority 1 (minutes)
- Average time taken to attend bursts and leaks – Priority 2 (minutes)
- Average time taken to attend bursts and leaks – Priority 3 (minutes)
- Average time taken to attend sewer spills, breaks and chokes (minutes).

As part of these discussions TasWater is seeking to revisit the targets proposed in the draft plan for these indicators. Those proposals assumed averages would continue to be the basis of measure and a move to actual minimums requires additional time for further consideration.

3.3.5. Guaranteed Service Level (GSL) Scheme

TasWater is not in a position to implement a guaranteed service level scheme and is firmly of the view that following experience in electricity and other regulated businesses it is questionable whether the introduction of such a scheme at this time or in the near future would result in improved service levels for customers.

Having given the concept careful consideration TasWater is deeply concerned at the impact on operational and capital priorities such a scheme may drive, particularly given the large compliance capital focus for TasWater.

4. Appendix 1 – Detailed Analysis of Key Matters

Section 3 of this report summarises TasWater’s analysis of the key matters raised in the Regulator’s draft report where there are differences from the draft plan. More detailed analysis on a number of those key matters is provided throughout this appendix.

4.1. Over-recovery of revenue

The Regulator stated in its draft report that TasWater will have recovered revenue of some \$80 million in excess of the estimated revenues provided by the former regional corporations in 2012 during the first regulatory period.

TasWater considers this conclusion is based on underlying assumptions and a comparison that is factually inaccurate, and is of the view that there will in fact be an under-recovery of revenue for the 2012-15 period when comparing regulated revenue approved by the Regulator in the 2012 determination with the former corporations’ and TasWater’s actual (and budgeted) regulated revenue.

Section 3.1.1 provides a summary of TasWater’s analysis and position on this matter.

The former regional corporations and TasWater reported total revenues in their Statutory Financial Statements for the financial years ending 30 June 2013 and 30 June 2014 that exceeded the estimated revenues provided in 2012. In addition, TasWater has budgeted to exceed the estimated revenues for the financial year ending 30 June 2015.

However, total revenues per TasWater’s Statutory Financial Statements are not directly comparable to the estimated revenues provided in 2012 as the Statutory Financial Statement revenues include a number of items that are not treated as revenue from a regulatory pricing perspective. For instance, items such as contributed assets and government grants are treated as offsets to TasWater’s Regulated Asset Base (RAB) by the Regulator and thus are not returned as revenues in the price determination.

A like for like comparison should consider the revenues of the former regional corporations and TasWater in the following categories:

- Fixed Water Charges
- Volumetric Water Charges
- Fixed Wastewater Charges
- Fixed Trade Waste Charges
- Volumetric Trade Waste Charges.

The outcomes of such a like for like comparison for each year of the 2012-15 period are set out in the following tables. The first table sets out the year on year outcomes, with the following table showing the aggregated amounts over the period.

Table 6: Year on year comparison of revenue approved by the Regulator in the 2012 determination against actual revenue outcomes (and forecast for 2014-15)

Revenue source ¹	2012-13			2013-14			2014-15		
	Nominal Revenue ³ (\$'000)	Actual Revenue ⁴ (\$'000)	Variance (\$'000)	Nominal Revenue ³ (\$'000)	Actual Revenue ⁵ (\$'000)	Variance (\$'000)	Nominal Revenue ³ (\$'000)	Budget Revenue ⁶ (\$'000)	Variance (\$'000)
Fixed water & sewerage	179,087	183,218	4,131	192,950	199,305	6,355	203,636	211,322	7,686
Variable water & sewerage	41,753	41,292	(461)	43,816	41,296	(2,520)	46,026	44,304	(1,722)
Trade waste	7,233	7,741	508	7,671	8,245	574	8,142	11,370	3,228
Supplementary revenue ²	6,605	0	(6,605)	7,068	0	(7,068)	7,559	0	(7,559)
Total	234,678	232,251	(2,427)	251,505	248,846	(2,659)	265,363	266,996	1,633

Notes:

1. Revenue sources such as grants, contributed assets, interest and other revenue which are detailed in TasWater's statutory accounts are not included in the comparison as they are not classified as regulated revenues.
2. Southern Water's approved 2012-15 Price and Service Plan included an allowance for customer revenues that had not been brought into the customer impact model at the time the PSP was prepared (refer page 180 of Southern Water's 2012-15 Price and Service Plan).
3. Combined for regional corporations as per 2012 determination
4. Combined for regional corporations as per the financial statements for the relevant year
5. Actual revenue as per TasWater's 2013-14 financial statements
6. Budgeted revenue for TasWater

Table 7: Comparison of total revenue approved by the Regulator in the 2012 determination for the three years of the period against actual total revenue generated by the regional corporations and TasWater (and forecast for 2014-15)

Revenue source ¹	Nominal 3 year Revenue (\$'000) (as per 2012 determination)	Actual Revenue (\$'000) (including budget for 2014-15)	Variance (\$'000)
Fixed water and sewerage	575,673	593,845	18,172
Variable water and sewerage	131,595	126,892	(4,703)
Trade waste	23,046	27,356	4,310
Supplementary revenue ²	21,232	0	(21,232)
Total	751,546	748,093	(3,453)

Notes:

1. Revenue sources such as grants, contributed assets, interest and other revenue which are detailed in TasWater's statutory accounts are not included in the comparison as they are not classified as regulated revenues.
2. Southern Water's approved 2012-15 Price and Service Plan included an allowance for customer revenues that had not been brought into the customer impact model at the time the PSP was prepared (refer page 180 of Southern Water's 2012-15 Price and Service Plan).

When these revenue categories are compared to the estimated revenues provided in 2012 it reveals that the former regional corporations and TasWater have under-recovered revenue over the first regulatory period in the order of \$3 million.

This issue is important as the supposed over-recovery of revenue is a key justification used by the Regulator to support its proposal that TasWater should and can afford to increase the pace of the price transition for customers above target beyond what was proposed in the draft plan.

TasWater requests the Regulator review the assessment of 2012-15 revenues and make the appropriate corrections in its final report.

4.2. Operating expenditure

In its draft report the Regulator has proposed an operating expenditure (opex) allowance that is \$14.3 million lower in year 1, \$18.4 million lower in year 2 and \$22.5 million lower in year 3 than TasWater's proposed opex in the draft plan.

TasWater is concerned that the Regulator has compared nominal values with real values (which explains some of the difference in the proposals), has not fully adopted Jacobs' proposed values as indicated in the draft report, and has not taken account of opex costs that have emerged since the 2012 determination was finalised.

Sections 3.1.2 and 3.2.4 provide a summary of TasWater's analysis and position on this matter.

This issue is important in that it establishes TasWater's (not the former regional corporations) baseline operating expenditure using information that is available and known at this time.

In developing its proposed opex allowance for the draft plan, TasWater drew on its experience during the 2013-14 financial year when a number of 'operating expenditure unknowns' started to emerge.

4.2.1. Adoption of Jacobs' proposed opex values

The Regulator, in arriving at its proposed opex allowance, has stated in the draft report that it has accepted Jacobs' recommendations in relation to the allowance. Jacobs, in section 4 of their report, use the approved expenditure in year 2 of the first pricing period for the former regional corporations as their starting point for determining the allowance for the second regulatory period. Jacobs then deducted the sustainable per annum merger savings and added the opex impact from the capital expenditure projects to be undertaken in the second pricing period that were reviewed in the course of the review.

This resulted in an operating and maintenance expenditure allowance in real 2015 dollars that is \$3.8 million higher in each year of the second pricing period than the Regulator's draft determination (see table 10 in the Jacobs report and Table 4.18 of the draft determination).

TasWater's analysis indicates that the Regulator has not included Jacobs' estimate of the opex impact from the capital expenditure projects to be undertaken in the second pricing period.

In its report to the Regulator, Jacobs recommended that the impact of the forward capital program (based on an analysis of 38 per cent of the projects proposed to be undertaken during the period) should be specifically allowed for in TasWater's opex allowance. In this regard, Jacobs recommended increases of \$0.7 million in 2015-16, \$1.0 million in 2016-17 and \$1.4 million in 2017-18.

4.2.2. Unidentified Opex in 2012

In adopting Jacobs' recommendations the Regulator has based the opex allowance in the second pricing period on the approved expenditure for the former regional corporations in 2012.

TasWater is of the view that there would be strong argument for the Regulator's approach if the former corporations had reached a steady state of operations with a suite of mature systems and processes for the collecting, monitoring and reporting of asset and operational performance data.

However, in 2012 the former corporations had only just come through the first phase of industry reform with incomplete asset data, a recently implemented billing system with minimal historical data and the majority of customers still to be metered for water consumption. Since then the industry has undergone a second phase of reform to establish TasWater, with many of the challenges regarding asset data and billing history still prevalent. Between 2012 and 2015 many of the unidentified costs of operations have become clearer conceptually, and have been incorporated into the operating and maintenance expenditure forecasts via year on year budget development during that period. This explains the remaining variance between the 2012 allowance and the actual expenditure.

These unidentified opex items in 2012 include, but are not limited to, the following:

- **Capital expenditure program in the second pricing period** – Jacobs analysed as part of their investigations a number of capital expenditure projects to be undertaken in the second pricing period and estimated the impact of those projects on TasWater’s opex. Jacobs recommended, and the Regulator accepted, increasing the opex allowance for these costs. However, the projects that Jacobs reviewed only represented 38 per cent of the total capital expenditure program in the second regulatory period. TasWater is of the view that the opex impact identified by Jacobs should be scaled up for the full capital expenditure program.
- **Capital expenditure program in the first pricing period** – the analysis that Jacobs undertook of the opex impact of the capital expenditure projects to be undertaken in the second pricing period was not undertaken by either the former corporations or an independent third party in 2012. As there has been significant capital expenditure undertaken by the former corporations and TasWater prior to the commencement of the second regulatory period it would be expected that the 2012 opex allowance would be impacted.
- **Upfront costs of the capital program** – experience has informed us that there is a significant cost incurred to develop the capital expenditure program and the individual business cases within the program. These costs include the costs of internal labour and external capability and are predominantly engaged in feasibility studies, environmental monitoring, option analysis, community and stakeholder consultation and the development of the business case. Under the Accounting Standards these costs are generally unable to be capitalised to the resulting asset that is created and thus are absorbed in the opex allowance. The extent of these costs was not fully understood in 2012.
- **Unidentified compliance programs** – experience has informed us that there is a significant cost incurred in meeting the commitments made within the business’ quality management plans and safety management plans. For instance, with respect to the dam safety management plan those dams with a significant or higher consequence category have a major financial impact on TasWater as the cost of management rises from an annual cost of \$10,000 for a low category dam to \$110,000 for a high category dam. Overall TasWater has 201 confirmed water and wastewater storages, lagoons and weirs which fall under the definition of a dam, of which 34 are rated as having a significant or higher consequence category, and a further 105 water bodies on the dam master list are to be further investigated which will most likely further increase the operating cost base . The extent of these costs was not fully understood in 2012.

In conclusion, TasWater requests the Regulator undertake a review of their calculation of opex, in particular:

- the consistent use of nominal and real dollar amounts
- the rolling forward of the approved expenditure for the former regional corporations in 2012

- consideration of an allowance for the opex impact of the full capital expenditure program undertaken in the first pricing period and to be undertaken in the second pricing period, including the upfront costs of developing the capital expenditure program
- consideration of an allowance for the opex impact of the unidentified compliance programs in 2012.

4.3. Asset Renewal Annuity

In its draft report the Regulator has proposed an ARA for the coming period that is less than half that proposed by TasWater in the draft plan and over 40 per cent lower than the amount approved for the regional corporations in 2012.

In its draft plan TasWater proposed an Asset Renewal Annuity (ARA) of approximately \$95 million (being \$45.5 million for water and \$46.7 million for sewerage) for each year of the regulatory period. This compares to a combined ARA total of \$80.2 million that the Regulator approved for the former regional corporations in 2012. In addition, it is not dissimilar to its proposed calculation of regulatory depreciation on new and existing assets for the regulatory period (with forecast depreciation exceeding the proposed ARA in 2017-18).

Section 3.2.1 provides a summary of TasWater's analysis and position on this matter.

The ARA is a key component of the lower revenue limit which was used by TasWater to determine the proposed water and sewerage target charges set out in the draft plan. It is an important issue in that the ARA is a significant determinant of the level of TasWater's minimum operating sustainability.

The Regulator's draft report states four key explanations for the way in which it has built up its proposed ARA. TasWater does not consider the changes to be valid in that they do not appropriately recognise the level of investment required for TasWater to operate sustainably into the future.

TasWater supports the use of forecast renewal and compliance capex as per the data collection template for the three years of the regulatory period, however it is critical to recognise that these figures are not an appropriate reflection of the level of investment required by TasWater to operate sustainably into the future. TasWater is making provision for a base level of renewals over the second regulatory period to try and ensure that the most critical/pressing asset renewals are still completed at a time when the need to focus on compliance issues is so great. TasWater is also using this base level of investment to build a library of asset criticality, condition and performance data to better understand the level of capital investment required to comply with the Customer Service Code and customer expectations.

TasWater is of the view that the Regulator's proposal to reduce compliance expenditure to zero over a seven year period post this regulatory period (to reflect Jacobs' final report reference that compliance capex is required for a decade) is not appropriate. The information used to inform the Jacobs Report is the 10 year capital works program, which does not contain all future compliance projects that will require completion.

TasWater considers that compliance expenditure can be broken into three major categories, with the relevant regulator noted in brackets:

- drinking water (DHHS)
- wastewater treatment (EPA and LGA)
- dam safety (DPIPWE).

This aligns with the Regulator's definition of compliance capital expenditure contained within the Ring Fencing Guidelines. TasWater has made substantial progress in addressing drinking water compliance and the stated 10 year completion period for compliance is an achievable target.

However TasWater will not have completed all necessary capital works to achieve compliance for wastewater treatment and dam safety by 2025. Compliance capital expenditure will continue to form an integral component of the capital works program for the foreseeable future.

Wastewater treatment compliance projects are needed at almost all 112 Sewerage Treatment Plants (STP) across the state. TasWater has found that completing a major capital works project at a STP has typically taken a minimum of two years. This means TasWater will be delivering compliance works for STPs well beyond the time horizon of the 10 year capital works program reviewed by Jacobs for their report.

The capital cost associated with delivery of these compliance works can be broadly forecast based on the capital cost associated with projects completed to date. TasWater has found that small level 2 STP projects can be delivered at a cost of \$3-5 million and medium-larger plants on a case by case basis (\$15-20 million is a conservative figure). The level 1 STPs will typically require a lesser value of investment than level 2 STPs. This will mean that TasWater will need to invest capital expenditure in the order of \$500-\$600 million to achieve full compliance for wastewater treatment. It is worth noting that this figure does not include major strategic projects such as the Greater Launceston Sewerage Improvement Program, the Greater Hobart Sewerage Improvement Program and a potential Greater Devonport Sewerage Improvement Program which may need to be partially or fully funded outside of future PSPs.

Dam safety projects are currently underway with TasWater having a long term dam safety program in place that will look to invest \$50M of dam safety upgrades over a 15 year period. This level of capital investment will bring TasWater's dam portfolio risk level below the ANCOLD level of tolerability but will not result in all dams having an ALARP (As Low As Reasonably Practicable) residual risk. This is the long term objective for dam safety at TasWater and will require further capital investment. It is considered that compliance works for dams will need to continue over a prolonged period.

The third element of the Regulator's ARA build is to "after three years, use the forecast renewal capex for the five financial years from 2013-14 to 2017-2018 as provided in the Data Collection Template and then eight years of adding the annual reduction in compliance capex to the renewals capex over the previous eight years."

As noted above it is not an appropriate assumption that the capital works program is a rolling ten year program of works put together with the best information available at the time. It does not contain, nor purport to contain, the full quantum of capital works that require completion. TasWater knows that there is still substantial compliance capital investment required in the long term for STPs and dams. Furthermore, the current focus on completing compliance projects and revenue limits imposed impact on TasWater's ability to fund an expected appropriate level of asset renewal.

As noted in the draft plan, TasWater considers that the development of a 'bottom-up', more comprehensive and accurate annuity calculation is not possible at this point in time with the data limitations that TasWater faces. TasWater is committed to improving the quality of asset data however this will take time. Until TasWater is in a position to use accurate asset data for criticality, condition and performance to inform asset renewals the determination of the asset annuity will remain a theoretical calculation based on installation dates and weighted useful asset lives.

The final element of the Regulator's ARA build is to "from 2032 onwards use the combined renewal and compliance capex from 2016 onwards thereby creating an approximate 17 year renewals cycle based on TasWater's own data which the Economic Regulator considers is within TasWater's financial and logistical capabilities."

TasWater is developing an asset renewal profile as part of the consolidated asset management plan. The asset renewal profile will initially be governed by year of installation and weighted useful asset lives. As data quality projects proceed and improved asset data is obtained the renewal profile will be revisited and determined based on asset condition and performance.

TasWater anticipates that there will be an asset renewal cycle/pattern that will come out of the strategic asset management plan however the profile will be over a much longer cycle than 17 years due to the long lived nature of the majority of TasWater's infrastructure. TasWater's expectation is that the renewal profile is more likely to be shaped by societal, regulatory and demographic factors. By way of example it is expected that there will be a significant requirement for renewal works during the 2030s for water pipelines that will reflect a significant capital investment in water infrastructure post World War II and similarly there will be a marked spike in sewer renewals in the 2040-50s following legislative/regulatory changes in the 1960-70s that led to the creation of a large number of sewerage schemes across the state.

TasWater also notes that the Regulator is of the opinion that the annual annuity payments detailed in TasWater's ARA are not achievable with respect to TasWater's financial and logistical capabilities. TasWater contends that its proposal is in fact achievable particularly given its proposed capital program for the 2015-18 period, the majority of which is made up of compliance and renewal expenditure, and which the Regulator is intending to accept (albeit re-profiled in the first and last years). If it is the case that the Regulator is of the view that TasWater could not meet the ARA then this appears to be at odds with the Regulator's view of TasWater's ability to deliver the capital program as proposed.

The final determination of an accurate asset annuity built from the bottom up is not possible for this price investigation, however TasWater is firmly of the belief that the figure proposed in the draft plan (\$95 million) is much closer to the long term investment required than the Regulator's view which is less than half that amount.

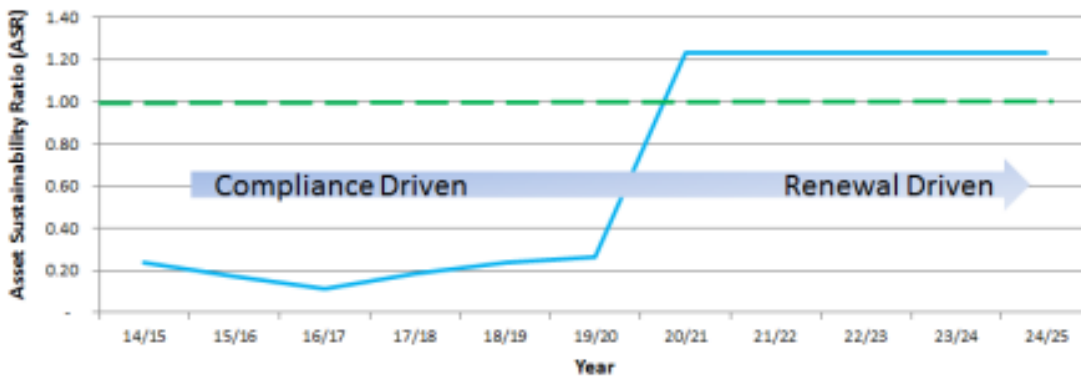
TasWater provided information to Jacobs as part of their review to support the view about renewals requirements into the future, and the work done by the former regional corporations in developing their asset management plans also supports this view. It was well understood internally that the cost of achieving compliance would force asset renewals to be deferred for the medium-long term. This decision was made with the intention of making up the gap over time through beginning the implementation of an Asset Management Information System (AMIS) and data improvement works to better understand asset criticality, condition and performance and the level of investment that would be required to maintain a viable business into the future. This can be demonstrated through the calculated sustainability index of the regional corporations, for example in the north over the first ten years of operation the sustainability index was approximately 0.5. An asset sustainability ratio of 0.8 – 1.2 is the target range for a sustainable and efficient business. Similar work has since been completed for TasWater indicating a significant underinvestment in renewals for both water and sewer pipelines which account for almost 70% of the asset base and are the key assets in terms of service provision to customers.

This point was demonstrated and endorsed by Jacobs in their draft report (refer section 2.3.3). While the charts (which show linear assets only) did not appear in the final report they are shown again below for clarity and completeness.

TasWater

Water Pipeline Asset Sustainability Ratios (ASR)

ASR = $\frac{\$ \text{Renewal}}{\$ \text{Depreciation}}$
 data: 10 Year Capital Plan / TasWater Corporate Plan 2015-17



TasWater

Sewer Pipeline Asset Sustainability Ratio (ASR)

ASR = $\frac{\$ \text{Renewal}}{\$ \text{Depreciation}}$
 data: 10 Year Capital Plan / TasWater Corporate Plan 2015-17



This strongly demonstrates the issues that TasWater faces in trying to balance the conflicting capital priorities of achieving compliance with operating a sustainable water business into the future. It should be noted that this figure is constructed based on the current 10 year capital works program. It is expected that as TasWater improves data quality and captures a more complete cost and timing of compliance works, the shape of the graph will be refined. In addition, and importantly, the graph shows that current renewal practices for water and sewer pipelines are not sustainable and that over time TasWater will need to lift the level of investment in renewal for pipelines by a factor of 4-6 times. Taking the 2017-18 renewal forecast from the draft plan, a four-fold increase would take the expenditure to approximately \$79 million, with a six-fold increase taking the expenditure to over \$118 million.

The Regulator's calculated annuity will not allow TasWater to complete required compliance or renewal works effectively and hence never achieve a satisfactory asset sustainability ratio where depreciation is sufficient to fund renewals. In addition it has informed the Regulator's view of TasWater's ability to 'afford' a faster price transition which may not be valid from a longer term sustainability perspective. Neither of these scenarios would be in the long-term interests of customers and the Tasmanian community.

TasWater requests the Regulator reconsider the methodology used to calculate the ARA.

4.4. Depreciation

The Regulator has proposed an average annual depreciation that is approximately \$20 million per annum lower than that proposed by TasWater in its draft plan and approximately \$16 million per annum lower than the amount approved for the regional corporations in 2012.

TasWater is concerned that the Regulator's methodology, including the approach to determining average useful lives, which is different to the one used by TasWater, understates the necessary depreciation in each year of the regulatory period.

Section 3.2.2 provides a summary of TasWater's analysis and position on this matter.

In the draft plan TasWater proposed an average annual depreciation of approximately \$93 million per annum for each year of the regulatory period. This compares to an average annual depreciation of approximately \$89 million per annum previously approved by the Regulator for the former regional corporations in 2012.

An increase in TasWater's depreciation estimate from the first regulatory period to the second regulatory period is to be expected given the significant capital expenditure program undertaken in the first and second regulatory periods that is driving an increase in the RAB.

In calculating its depreciation estimate, the Regulator has used the same data set as that provided by TasWater. However, both TasWater and the Regulator have used a differing approach to determining the average useful lives and resultant depreciation charge.

TasWater has calculated the annual depreciation charge for each asset category using an average useful life for the assets within that category. The result of all of the individual asset category depreciation estimates is summed to provide the total annual depreciation estimate. The overall estimated average useful life is an outcome, being simply the opening RAB value divided by the annual depreciation estimate, rather than an input into the annual depreciation calculation.

It should be noted that TasWater's methodology was used to calculate the depreciation charge in the 2013-14 Regulatory Accounts. These accounts were audited by the Tasmanian Auditor-General, who did not object to the methodology or the resultant depreciation charge. These accounts were provided to the Regulator in December 2014.

The Regulator's approach is to calculate a weighted average useful life for each asset category and then summing those useful lives to get the overall useful life of the RAB. The depreciation estimate is then simply the opening RAB divided by the average useful life. TasWater contends that under this methodology the calculation of the average useful life is flawed as it fails to present the weighting factor, being the opening RAB for the individual asset category, on a consistent basis across all of the asset categories. This is because for the shorter life assets the expenditure on renewals at the end of their useful lives is not incorporated into the calculation. The calculated useful life under this methodology will be overstated as the longer life assets represent a disproportionate amount of the opening RAB.

Additionally, the RAB values by category and associated asset life data provided by TasWater was effective as at 1 July 2013. The Regulator has used this data to estimate average asset lives as at 1 July 2015.

Accordingly under their calculation methodology the depreciation estimates made by the Regulator have been understated as the Regulator's remaining useful lives are two years longer than the actual remaining useful lives.

The issue of regulatory depreciation, and the allowance provided to TasWater, is important in the long term as it affects the business' ability to fund necessary asset renewals going forward. Consistent with the discussion below on the Asset Renewal Annuity, TasWater faces significant data limitations and is in the process of building an asset renewal profile as part of the consolidated asset management plan. What is known at this time, however, is that TasWater's asset sustainability ratio is well below the target range for a sustainable and efficient business, and that renewals expenditure needs to increase over time to achieve that operating state. Given this, TasWater considers a reduction in the regulatory depreciation allowance for this regulatory period may impact on the business' ability to undertake renewals going forward, or a step-change in the depreciation allowance may be needed in the next period once additional data and information has been collected.

TasWater requests the Regulator review its methodology.

4.5. Weighted Average Cost of Capital

In its draft report the Regulator has proposed alternate methodologies for calculating the risk free rate (RFR) and the debt risk premium (DRP) components of the WACC. The difference in methodology results in a reduction in TasWater's nominal pre-tax WACC of approximately 21 basis points.

TasWater is concerned that the Regulator's methodology creates exposure for the business as and when interest rates go up.

Section 3.2.3 provides a summary of TasWater's analysis and position on this matter.

The Regulator has agreed with TasWater's view set out in the draft plan that the methodologies and rationale behind the majority of the components of the WACC that were adopted in 2012 remain sound and a similar approach for the second regulatory period is appropriate. Those components are as follows:

- market return
- equity beta
- gearing level
- corporate tax rate
- gamma.

With regard to the remaining components, being the risk free rate (RFR) and the debt risk premium (DRP) TasWater proposed moving away from the previous 'on-the-day' methodology to a 'trailing average' methodology.

The 'trailing average' methodology is considered to more appropriately reflect the actual borrowing behaviour by regulated entities, the restrictions on activity placed by financial markets and the overriding requirement for organisations to prudently manage financial market risk outside of any regulatory framework. This methodology also overcomes the major flaw in the 'on-the-day' methodology, namely that TasWater would have all its debt repriced around the time that the Regulator assesses the risk free rate and the debt risk premium.

The approach involves calculating a long term average over 10 years combined with an average over 40 days of the same reference dataset. Each of the long term and short term averages is given equal weighting to

determine the RFR and DRP. The use of a long term average in the calculation smooths out the fluctuations in the interest rate cycle and ensures that the WACC is not set too high when interest rates peak, and potentially encourages overinvestment, or is not set too low when interest rates trough, and potentially encourages underinvestment.

While the Regulator supports the 'trailing average' approach TasWater notes that it has inconsistently applied the approach in determining the RFR and the DRP. For the RFR the Regulator has applied TasWater's proposed approach, albeit it is utilising a time weighted average of the 10 year Commonwealth Government security instead of a straight arithmetic average for its long term average.

However, for the DRP calculation the Regulator is solely using a short term average. The impact of this is to set the DRP near the low point of the interest rate cycle which understates TasWater's WACC. Using the dataset that formed the draft determination TasWater estimates that the inconsistent calculation of these components has reduced the nominal pre-tax WACC by approximately 21 basis points.

TasWater can find only limited use of the Regulator's approach under a 'trailing average' methodology of only using a short term average amongst other regulators. Research undertaken in developing the draft plan confirmed that two of the largest regulators, IPART and the AER, have moved to the 'trailing average' approach proposed by TasWater, albeit that the AER is transitioning to the full adoption of the methodology to ensure that no regulated entity is disadvantaged.

TasWater requests the Regulator review its approach to the calculation of the RFR and DRP components within the WACC calculation.

4.6. Opening RAB

The Regulator has proposed an opening RAB value of \$3.0 billion, which is \$36.883 million lower than proposed in TasWater's draft plan, based on an assumption that TasWater has not accounted for the full capex underspend over the 2012-15 period.

TasWater contends that it has accounted for the capex underspend by tracking actual movements in the RAB from year to year throughout the period. That tracking also takes a number of other relevant factors into account that the Regulator's methodology does not.

Section 3.2.5 provides a summary of TasWater's analysis and position on this matter.

TasWater contends that the difference between its opening RAB and the Regulator's stems largely from the opening RAB for the first regulatory period, which was a forecast at the time of the preparation of the first pricing determination.

In forecasting the opening RAB for the second regulatory period TasWater has accounted for the actual opening RAB in 2012, actual capital expenditure in the financial years ending 30 June 2013 and 30 June 2014, and the budgeted level of capital expenditure for the financial year ending 30 June 2015. Under this approach the capital underspend over the first regulatory period is incorporated into the opening RAB for the second regulatory period. Differences will also arise on account of:

- variations in, and substitution of projects undertaken over the first regulatory period
- the amount and timing of the individual capital expenditure projects
- the in-service dates of the resulting asset(s)
- the individual components of the asset(s) and the useful lives assigned to those components.

The Regulator appears to be assuming that the only reason for a difference between the forecast closing RAB from the first regulatory period and the forecast opening RAB for the second regulatory period is the amount of capital expenditure in the first regulatory period. TasWater contends that assumption is flawed and requests the Regulator reviews the forecast opening RAB.

4.7. Third Party Contributions

In its draft report the Regulator has included government grant income within the scope of third party contributions.

TasWater does not object to this approach, however, it is of the view that the Regulator has incorrectly interpreted the nature of some of the income TasWater has included within the scope of grant income.

Section 3.2.6 provides a summary of TasWater's analysis and position on this matter.

TasWater does not object to the Regulator's approach on third party contributions, however it is of the view that the Regulator has incorrectly interpreted the nature of some of the income included within the scope of grant income. Specifically, grant income includes the Tasmanian Government subsidy for headworks charges and grant funding for non-regulated reuse assets. TasWater believes these amounts should be excluded from the total of third party contributions deducted from the RAB.

TasWater notes that the amounts of third party contributions are deducted from capital expenditure when undertaking revenue limit calculations. However, to ensure RAB values are not understated, the assets that these contributions generate should be included within gross capital expenditure estimates to ensure the RAB is not understated. The Regulator does not appear to have included these amounts in the gross capital expenditure estimates in the draft determination.

TasWater requests the Regulator review its treatment of third party contributions. Further, TasWater notes that as the above amounts disclosed in the draft plan were nominal values, the Regulator should ensure, where necessary, that adjustments are made to record the above as real values.

4.8. Customer Service Standards

In its draft report the Regulator has proposed that frequency and duration related customer service indicators be measured on an actual minimum basis as opposed to the current basis of measure which is average.

TasWater is concerned about the poor quality of data that currently underpins the consideration of customer service standards. In addition, TasWater is concerned that consideration of actual minimums will drive outcomes that are at odds with the priorities set by technical regulators and legislative obligations. TasWater is, however, open to further discussions with the Regulator regarding absolute minimum targets for 'response time' indicators.

Section 3.3.4 provides a summary of TasWater's analysis and position on this matter.

TasWater notes the Regulator's position with respect to customer service standards, particularly the intention to "approve the current minimum service standards as outlined in Schedule 1 of the Code as actual minimum standards for the second regulatory period."

TasWater is not fundamentally opposed to the notion of actual minimum targets for frequency and duration related customer service indicators. It is TasWater's view, however, that averages (particularly for response

times) have demonstrably driven increased performance across the water sector nationally. TasWater notes that the Essential Services Commission continues to measure Victorian water businesses using averages for response times, and frequency and duration related indicators (refer ESC *Customer Service Code, Urban Water Businesses*, September 2014).

The key value of averages is the ability to nullify outliers that corrupt data and skew results. Averages, when taken over a broad pool of results provide significant incentives for businesses to drive efficiency and equally identify the most economic point of service delivery.

The “cost to serve” argument when based on minimum service standards 100 per cent of the time has been demonstrated to drive perverse behaviours that seek to mask any failings for fear of punitive outcomes. Minimum service standards that are contemplated on Pareto style principles allows a supplier to operate with a level of freedom to drive the best customer outcomes in a way that acknowledges the wider community of drivers and outcomes needed.

One potential perverse outcome of actual minimum standards could be that capital expenditure is redirected from compliance to renewals, particularly in linear assets, in order to meet standards and avoid penalties. In TasWater’s case, this is something that would be of interest to the EPA, DHHS and DPIPW given compliance challenges and the proposed capital program which aims to address the technical regulators’ priority areas/projects.

With respect to a number of the current standards/indicators, TasWater notes that they are either not attributable to specific customers (eg total water and sewerage complaints per 1,000 properties) or not able to be attributed to specific customers given limited data quality and systems and processes that either do not exist or are not yet integrated (eg average duration of unplanned minutes off water supply). Data issues aside, it is important to note that water and sewerage networks are unlike electricity networks in this regard. Comparisons between the two are, therefore, not meaningful in many ways.

The example above regarding the identification of specific customers impacted by an unplanned outage is something that a mature water business would expect to be able to do. However, consistent with the information set out in the draft plan, TasWater does not have the detailed knowledge of its assets or data confidence to achieve this at this time. An example of this is the recent (early February) unplanned water outage in Hobart that impacted a number of central suburbs. TasWater would not have been able to identify and confirm which customers were affected by the outage with any degree of certainty.

A higher level of data collection and analysis, which TasWater is seeking (and needs) to achieve, requires development of systems and process. The pathway to change is populated by many facets of organisational and customer need. Previously, local knowledge and disparate legacy systems have been relied upon, however this approach is not appropriate for an organisation of the size and scope of TasWater to achieve its organisational and regulatory goals.

As stated in the draft plan, TasWater has a number of projects underway that will form the building blocks for a more robust understanding of customer service standards including:

- Asset Management Information System (AMIS)
- Field Service Management System
- Statewide Geographic Information System (GIS)
- Network Operations Centre
- Customer Records Management system.

As noted above, and stated in the draft plan, TasWater is of the view that development and integration of the above systems is a necessary prerequisite for consideration of both differentiation and actual minimums.

Notwithstanding the above, TasWater is open to further discussions with the Regulator regarding absolute minimum targets for the following indicators for the 2015-18 regulatory period:

- Average time taken to attend bursts and leaks – Priority 1 (minutes)
- Average time taken to attend bursts and leaks – Priority 2 (minutes)
- Average time taken to attend bursts and leaks – Priority 3 (minutes)
- Average time taken to attend sewer spills, breaks and chokes (minutes).

As part of these discussions TasWater is seeking to revisit the targets proposed in the draft plan for these indicators. Those proposals assumed averages would continue to be the basis of measure and a move to actual minimums requires additional time for further consideration.

TasWater notes that Queensland Urban Utilities, which services a mix of urban and rural areas/customers, operates with minimum service standard targets and considers those arrangements would be a useful reference point for both TasWater and the Regulator to consider in proposing and setting minimum targets.

In addition, TasWater intends to discuss a number of other matters that are unclear or lacking in detail in the Regulator's draft report. These include:

- the framework and reporting arrangements that will support actual minimum targets
- the incentive/penalty regime that is mooted by the Regulator in the draft report
- the Regulator's expectations of what happens if any of the minimums were to be breached, for example would TasWater be required to pay customers or the Regulator and if so how much and within what timeframe.

Another matter requiring further discussion is the non-frequency and duration related indicators. TasWater seeks to understand whether it is intended that they remain on an average basis or they will be reworded to reflect a change in approach. TasWater is unclear of the Regulator's intentions from the draft report.

Given the commencement of the new regulatory period is only four months away, and TasWater assumes the Regulator's intention is that actual minimums will be measured from 1 July 2015, TasWater considers it is critical to resolve these issues as soon as possible.

4.8.1. Review of draft plan targets

Notwithstanding that additional time is required to review the majority of targets set out in the draft plan, TasWater is in a position to propose alternative targets for two of the three customer related indicators as a result of a number of initiatives that have been undertaken since the draft plan was submitted in August 2014.

With respect to customer related indicators, TasWater is proposing an amendment to the targets set out in the draft plan for Total Water and Sewerage Complaints (per 1,000 properties) and Percentage of calls answered by an operator within 30 seconds. No change is proposed to the number of water and sewerage complaints to the Ombudsman (per 1,000 customers).

Total Water and Sewerage Complaints (per 1,000 properties)

TasWater conducted internal complaints training in December, after which there has been heightened organisational awareness, transparency and monitoring of complaints received across the business. This has resulted in better identification and definition of complaints and therefore higher numbers being managed in accordance with the Complaints, Enquiries and Disputes Management Policy, which provides further opportunities to continually review and improve customer processes.

As a result, TasWater considers that the current target minimum service standard for this indicator as set out in the Customer Service Code, being 9, is appropriate for each of the 2015-18 period, rather than the 7 proposed in the draft plan.

Percentage of calls answered by an operator within 30 seconds

TasWater considers that a realistic target of 85 per cent of call answered within 30 seconds is a more appropriate utilisation of resources and aligns more closely with the overall performance of other more mature water businesses. The average performance for Australian Water Utilities is 81.4 per cent (refer National Performance Report 2012-13). Given this, TasWater considers that the current target minimum service standard for this indicator as set out in the Customer Service Code, being 85 per cent, is appropriate for each year of the 2015—18 period, rather than the 90 proposed in the draft plan.

TasWater is developing a customer focussed approach across the business, with a particular emphasis to resolve customer issues at first point of contact. It is hoped that this will provide a better customer experience and allow customer issues to be resolved quickly and efficiently. The development of a customer service centre of excellence with well trained customer service staff will be a key enabler. The measurement of operators to answer calls within 30 seconds is in some ways counter active to providing first point resolution to customers as it supports a service geared to record an issue rather than provide a resolution.

TasWater requests the Regulator approve the amended targets for these indicators as per the following table.

Table 8: Revised targets for indicators specifically relating to customers

Indicator	Minimum	2015-16	2016-17	2017-18
Total Water and Sewerage Complaints (per 1,000 properties)	9	9	9	9
Percentage of calls answered by an operator within 30 seconds	85	85	85	85

4.8.2. Guaranteed Service Level scheme

TasWater notes the Regulator’s view that the State Government should consider the introduction of a Guaranteed Service Level scheme (GSL) for the Tasmanian water and sewerage industry.

While TasWater is willing to explore the concept of actual minimum standards further at this time, for many of the reasons raised and discussed above in relation to the customer service standards, TasWater does not consider the introduction of a GSL scheme to be appropriate, feasible or achievable in the near future, particularly within the next regulatory period.

The integration of systems and processes, and the necessary detailed understanding of not only the physical infrastructure but the customer base, does not yet exist to the extent necessary for TasWater to be able to accurately measure customer outages both by volume (time) and number (geographical spread).

For a GSL scheme to work effectively and to the benefit of customers, which is the intention of such a scheme, it should be automated such that customers do not need to apply for payments. The example of

the recent unplanned water outage in Hobart discussed above is a case in point for why a GSL scheme is not possible for TasWater to introduce in the near future.

As already highlighted, it is also important to recognise that water businesses are significantly different to electricity distribution. TasWater is of the view that at this time in the formative part of the business' development, to move to GSLs based on expectations driven by another industry such as electricity would be counter-productive to both the organisation and customers.

The introduction of a GSL scheme for the Tasmanian water and sewerage industry is a significant policy issue and TasWater urges caution from all parties in the consideration of this matter. TasWater considers that a cost benefit analysis would need to be undertaken prior to a scheme being introduced. Such analysis would likely demonstrate that a GSL scheme introduced at the wrong time may not fact be beneficial for customers, as would be the intention, as it may drive the wrong behaviours and shift the focus of the business away from other priority areas. This is particularly relevant for Tasmania at the moment given the compliance challenges TasWater faces and the plans in place to improve water quality and wastewater compliance.

TasWater will engage with the State Government on this matter to ensure the best outcomes can be achieved for water and sewerage customers and the Tasmanian community.

5. Appendix 2 – Other matters raised in the draft report

There are a number of other important matters raised and proposals set out in the Regulator’s draft report. TasWater’s comments, observations and responses to those matters are provided throughout this appendix.

5.1. Debt Servicing Costs

TasWater notes the Regulator’s proposed approach of allocating debt servicing costs in proportion to regulated and unregulated assets. TasWater is not opposed to the Regulator’s proposal to reduce the allowance for debt servicing costs by 8 per cent within the lower limit revenue calculation.

5.2. Pricing matters

TasWater notes the Regulator’s intention to approve:

- postage stamp pricing
- the proposed customer classes set out in the draft plan
- the basis for pricing of fixed water target tariffs, limited supply customers, fire service customers, fixed sewerage charges, variable water charges, private and public filling stations, trade waste, motor home dump points, miscellaneous fees and charges and development assessment services fees.

Notwithstanding the above, TasWater notes that the Regulator’s draft report (at pages XIV and 74) incorrectly states the target variable water charge for 2015-16. TasWater’s proposed variable water charge is \$0.9711 per kilolitre for 2015-16.

With respect to the scenarios set out in Table 48 of the draft plan TasWater acknowledges that the draft plan did not fully explain the basis of the scenarios for customers moving directly to target tariff. TasWater can advise that the direct move to target tariff will be based upon the following factors:

- Change in customer at the property
- Change in property through development process including reconfiguration and change of use
- Change in connection or service including installation of sub meters.

A high-level summary of these scenarios listed in the draft plan, together with the basis for change for each, is set out in the following table.

Table 9: Summary of customer transition to target scenarios (including the basis for transition)

Scenario	Basis of change	Target Tariff/s Applied	Transition to Target Tariff/s under price constraints
Existing customer changes their property’s predominant use	Property change	✓	
Existing customer requires altered connection arrangements through a successful development application process	Connection change	✓	
Previously unconnected properties connect to water and/or sewerage infrastructure (including new sub-divisions)	Connection change	✓	
Where a customer’s property is already connected to water and /or sewerage infrastructure, but is currently not receiving charges (newly discovered customer)	Customer change	✓	
Newly discovered connection(s) to existing installations	Connection change		✓

Scenario	Basis of change	Target Tariff/s Applied	Transition to Target Tariff/s under price constraints
Changes to existing connection points, i.e. change of connection size, including installation of sub-meters	Connection change	✓	
Existing water service customer who is discovered should also be receiving a fire service charge	Connection change		✓
New trade waste customer (applying for a consent)	Customer change	✓	
Existing sewerage service customer who should also be receiving a trade waste charge – trade waste discovery)	Customer change		✓
Adhesions/consolidations (unless part of a development application)	Property change	✓	
Amalgamation	Property change	✓	
Demolition	Property change	✓	
Unconnected vacant lot to connected lot	Connection change	✓	
Change of ownership	Customer change	✓	
Improvement from permanent boil alert to potable water supply (applies to variable charge only)	Connection change	✓	

TasWater will include this additional detail in the final plan.

5.3. ET methodology

TasWater acknowledges the Regulator’s requirements for the final plan to include specific information regarding the ET methodology.

With respect to a schedule detailing the ET rates to be applied to different industries and property uses, the draft plan included such a schedule at Attachment J. TasWater will ensure this is also included in the final plan.

A clear explanation of the ET methodology used to calculate the various ET rates will also be included in the final plan. It is expected that this will be based on Attachment I of the draft plan and include further detail on the methodology, particularly with respect to the WSA and NSW Water Directorate supporting information that is not publically available.

It is also anticipated that this information and the schedule of rates will be published on TasWater’s website throughout the course of the 2015-18 regulatory period.

Caravan Parks

TasWater acknowledges that Caravanning Industry Australia-Tasmania (CIAT) has raised concerns about the calculation of sewerage charges for various caravan parks in their group around the state and requested a review of the way ETs are charged.

TasWater officers have had a number of meetings with CIAT stakeholders over recent months during which possible alternative methodologies, including a discharge factor approach (water in/sewerage out), have been discussed.

Agreement on an appropriate methodology has not yet been reached and TasWater is of the view that this issue requires further discussion with all relevant stakeholders, ie CIAT representatives, the Regulator and TasWater. Additional, more detailed information about the current methodology, possible alternative methodologies and jurisdictional comparisons will be separately provided by TasWater for the purpose of those discussions should the Regulator consider it to represent an acceptable way forward.

5.4. Demand, Customer and Miscellaneous Services Forecasts

In the draft report the Regulator proposes adopting an annual growth rate of 0.3 per cent instead of 0.5 per cent as set out in the draft plan.

TasWater notes that the growth rates it used to develop the draft plan were determined based on the best information available at the time.

The Department of Treasury and Finance’s December 2014 population projections for Tasmania, to which the Regulator refers in its draft report, were not available at the time of preparing the draft plan. On this basis TasWater is not opposed to the Regulator’s proposal to adopt a lower annual growth rate.

Miscellaneous Fees and Charges

TasWater welcomes the Regulator’s intention to approve the miscellaneous fees and charges proposed in the draft plan. It should be noted, however, that there is a transposing error in Table 5.8 of the Regulator’s draft report regarding the proposed charges for a 20mm meter supply and installation. The charges as proposed in TasWater’s draft plan are \$253.86 for 2015-16, \$260.21 for 2016-17 and \$266.72 for 2017-18.

TasWater notes the Regulator’s comments regarding forecasts of miscellaneous transactions. These forecasts have been reviewed (to consider the appropriateness of the starting point and the annual growth rate) since earlier forecasts were provided on 31 October 2014. The revised forecasts, which would effectively replace those set out in Table 5.14 of the Regulator’s draft report, are as follows.

Table 10: Revised miscellaneous transaction forecasts for 2015-18

Transaction Type	2015-16	2016-17	2017-18
Special Read	5,100	5,115	5,131
Section 56ZQ request	7,000	7,021	7,042
Section 56W consent	140	140	141
Service Locator Fee	492	493	495
Pressure & Flow Testing	5	5	5
Property Information Plan	3	3	3
Restriction Charge	350	351	352

Note: all revised forecasts have been calculated using the Regulator’s proposed annual growth rate of 0.3 per cent.

The major differences are associated with the previously provided forecasts for section 56ZQ requests and restriction charges. It should be noted that the revised forecasts have been based on the actual number of transactions for the first half of the 2014-15 year extrapolated out for a full year.

With respect to forecast revenue, the revised forecasts result in additional revenue of approximately \$186,000 in 2015-16, \$179,000 in 2016-17 and \$170,000 in 2017-18.

With respect to the determination of development assessment services charges TasWater can advise that the table on page 93 of the draft plan incorrectly referenced Equivalent Population as the basis for setting the classification thresholds. While Appendix A of the *Water Services Association of Australia – Sewerage Code 2002* defines Equivalent Population, TasWater’s supplement to that Code (a copy of which is available on TasWater’s website) replaces EPs with ETs. The amended table, which will be included in the final plan, is as follows:

Table 11: Revised thresholds for classifying development applications

Non-subdivision applications/plumbing applications	
Classification	Thresholds
Minor	0 - 2 ET typically including: <ul style="list-style-type: none"> • Single dwelling/extension/alteration • One or two units/town houses • Auxiliary dwelling/dependence unit • Shed/garage/carport • Demolition • Shop refit • Light industrial/commercial/retail site / <0.15Ha • Minor extension to commercial / light industrial/retail • New connections • Change of use
Medium	>2 - 10 ET typically including: <ul style="list-style-type: none"> • Three (3) to10 dwellings/units/town houses/dependence units • Light industrial/commercial/retail site/0.15-0.Ha • New/modified backflow protection devices • New/modified fire protection/metering services • Restricted or wayside water connection
Major	>10 - 30 ET typically including: <ul style="list-style-type: none"> • 11-30 dwellings/units/townhouses/dependence units • Industrial/commercial/retail site/>0.3Ha - 1.5Ha
Significant	>30 ET typically including: <ul style="list-style-type: none"> • >30 dwellings/units/town houses/dependence units • Heavy industrial/commercial/retail site/>1.5Ha • Effluent reuse/development within buffer areas

5.5. Service Provision

5.5.1. Serviced Land

Minimum flow and pressure

As noted in the Regulator’s draft report, TasWater has adopted a desktop-based approach to determine the serviced land area, and in doing so has proposed the following minimum flow and pressure:

- design flow: 20 L/minute
- static pressure: 250 kPA (25 m).

TasWater notes the Regulator is seeking justification for the methodology used to derive the minimum flow and pressure figures. In this regard, TasWater can provide the following information.

With respect to minimum pressure, section 2.5.3.3 (Minimum service pressure) from the TasWater Supplement to Water Supply Code of Australia WSA 03-2011-3.1 Version 3.1 MRWA Edition V2.0 (DRAFT 03), which is published on TasWater's website, specifies that the minimum pressure at peak hour demand is:

- 220 kPA (22 m) for residential flat grade ($\leq 18\%$)
- 250 kPA (25 m) for residential steep grade ($> 18\%$)
- 250 kPA (28 m) for non-residential.

These minimum pressures at peak hour demand are based on Section 3 (Sizing of Water Services) and Appendix C of AS/NZS3500.1.2:2003.

The TasWater Supplement does not specify if the minimum pressure is dynamic or static. It is also noted that the minimum pressure specification is dependent on the slope of the terrain.

Dynamic pressure has not been used as part of this desktop-based approach, as this data is not consistently available for all water systems across the state.

A static head of 25 metres has been consistently used, rather than assessing serviced land based on gradient and dynamic pressure. Static head has been utilised as TasWater does not yet have all the information available to determine dynamic pressure across all of the systems. In addition, ten metre contour data has been used for the majority of the state to determine pressure, as such the inaccuracy with this contour data is far greater than the pressure difference between a flat grade and a steep grade.

With respect to flow, section 2.12 (System review) from the TasWater Supplement (as referred to above) specifies the minimum flow rate to be 15 litres per minute. For the purpose of Serviced Land, however, TasWater has used a more conservative rate of 20 litres per minute as it provides a contingency over the 15 l/min for errors in the asset data (for example there are only 10 metre contours in some areas and interpolation is required) whereas during the design process a greater level of asset information is known, for example specific internal diameters and accurate levels.

Publication of final serviced land maps

TasWater supports the Regulator's intention to require the finalised versions of its state-wide serviced land maps to be provided in the final plan, as well as an undertaking to make the final version of those maps available to the public from 1 July 2015.

Finalised versions of the serviced land area maps as at the end of February 2015 based on the asset knowledge and data available at this time are provided with this response as committed to by TasWater through the investigation.

As asset data and knowledge improves over time, the serviced land maps will be updated and republished. Accordingly, the maps include the following disclaimer:

The serviced land area is subject to the asset data and knowledge available at the time of publication. While all reasonable care has been taken to ensure the accuracy of the information portrayed in these maps, its purpose is to provide a general indication of the location of TasWater-

serviced land. The information provided may contain errors or omissions and the accuracy may not suit all users. Any feedback on omissions or errors would be appreciated.

TasWater will make this serviced land area information available to the general public from 1 July 2015.

Identification of serviced land by title

It is noted that the Regulator has identified on a number of maps lines showing different levels of service crossing land title boundaries. It is also noted that the Regulator has requested that in these instances the full title boundary is demarcated as either serviced or unserviced.

While able to comply with this requirement, TasWater is of the view that the current maps provide additional relevant information to customers. The title boundaries that are partially intersected by the serviced land area are serviced as indicated, however (for example) there may be limitations to supplying large sloping title boundaries above a certain contour level (i.e. will not receive the minimum pressure/flow service on some portions of the title). Accordingly, TasWater considers it appropriate, and good practice, to make these title owners aware of such limitations, especially for current vacant land which may assist with positioning of a house.

In order to be consistent with the draft plan, TasWater will update the map legend to refer to the following terms:

- Titles with full service (instead of “Serviced”)
- Titles with limited service (instead of “Partial service”)
- Titles that are unserviced (instead of “Not serviced”).

Additional categories will also be included within the map legend to provide further information, such as:

- Further investigation required (water and sewer)
- Wayside (water)
- Potential wayside (water)
- Untreated supply (water)
- Low pressure connection (sewer)
- Private pump station connection (sewer).

Regular update of description of serviced land

TasWater supports the Regulator’s intention to require TasWater to provide an undertaking in its final plan to ensure that the description of serviced land is regularly updated, published and made available to the public.

In concluding the development of the serviced land area for submission to the Regulator for approval, TasWater is establishing and documenting “business as usual” processes to maintain the serviced land area and publish the information to the public.

With respect to the frequency of updating the serviced land area, TasWater recommends that this be undertaken no more frequently than on a quarterly basis. TasWater is of the view that a higher frequency of releasing changes as proposed by the Regulator will create additional administrative overheads to maintain such a service.

Regardless of the timeframes for providing updated serviced land area, TasWater will establish KPIs to monitor and review the compliance to the specified timeframes.

5.5.2. Customer contract

TasWater has reviewed the Regulator's comments and made a number of amendments to the draft Customer Contract as a result.

5.5.3. Connection policy

TasWater notes the Regulator's comments and has amended the Connections Policy to:

- outline the circumstances in which TasWater will permit an owner of land to relocate or adjust a connection to its infrastructure
- specify the connection charges to apply to properties within serviced land.

TasWater also notes that the Regulator intends to approve TasWater's proposed connection fees and relocation of connection fees for 20mm and 25mm water connections and 100mm sewerage connections.

These charges will be included in the final plan. An undertaking to determine connection and relocation of connection charges for non-standard and larger water and sewerage connections on a cost recovery basis will also be included in the final plan.

5.5.4. Service charges policy

TasWater notes the Regulator's intention to accept the proposed service charges tariff structure for the 2015-18 regulatory period.

With respect to the comments in the Regulator's draft report regarding advice from TasWater about the intention to not impose service charges on property owners in limited service or limited supply areas, TasWater wishes to clarify this issue and advise that it does in fact currently impose service charges.

TasWater regrets to advise that the informal advice provided to the Regulator on this matter was incorrect and that TasWater does not propose changing its current practice for the 2015-18 regulatory period. This is consistent with the intent of the draft plan which stated the following:

... service charges will vary according to the type of service (ie full or limited) a customer might expect to receive upon connection, which will be informed by the identification and classification of serviced land.

This shows a clear intent notwithstanding all of the differentiated charges were not explicitly set out in the draft plan. In the same way that service charges for unconnected properties able to connect to a full water service are linked to the target fixed water service charge for connected properties, service charges for properties able to connect to a limited water service are linked to the discounted (by 10 per cent) target fixed water service charge for connected properties.

TasWater proposes amending the final plan to more explicitly reflect to whom service charges will be applied and the relevant amount of those service charges. In doing that Table 49 from the draft plan will be updated consistent with the following table.

Table 12: Revised service charges for 2015-18

	2015-16	2016-17	2017-18
Water service charge (full service)^	\$293.24	\$310.84	\$329.48
Water service charge (limited service)^	\$263.92	\$279.76	\$296.52
Sewerage service charge (0.6 ET)	\$337.60	\$357.88	\$379.32

Note ^: These are the proposed charges for a 20mm water connection, with all other connection sizes leveraging off this rate according to the scaling factors set out in Table 35 of the draft plan.

In addition, the draft service charges policy will also be updated to clear identify that service charges will be levied on properties able to connect to a limited water service.

5.5.5. Sub-metering policy

TasWater notes the Regulator’s comments regarding the draft water metering policy that was submitted as part of the draft plan and that the regulatory obligation is for a sub-metering policy only. In this regard, TasWater has redrafted the policy to address sub-metering matters alone. The amended policy also includes additional information regarding the process for strata title owners to follow in deciding whether or not to proceed with sub-metering.

For the 2015-18 regulatory period, TasWater is proposing a continuation of the approach to sub-metering that has applied during the 2012-15 period. For completeness, this approach involves TasWater providing fixed and volumetric charges to individual lot owners within strata arrangements.

New strata schemes will be metered using a master meter with sub-meters or individual lot meters. Where there is no common property, no shared connecting pipe work and no requirement for a master meter, TasWater may, at its discretion, approve each lot being individually connected to TasWater’s water main.

For existing strata developments that have not previously had water meters, the default will be to install a single boundary meter and if all lot owners agree, sub meters can be installed with costs to be allocated accordingly.

Where the strata arrangement has only a single meter at the boundary, the target tariff for the fixed water charge will be based on the boundary meter connection size (eg 32mm = \$750.68 in 2015-16). This charge will then be allocated between the individual titles on the basis of general or special unit entitlement (as defined under the Strata Titles Act). For example, each lot owner within a four unit strata development with a 32mm boundary meter connection would each have a fixed charge target tariff for water of \$187.68 (if each lot has equal unit entitlement). The volumetric usage will also be split in the same manner and itemised on the lot owner’s bill. If agreed by all lot owners in writing (or their body corporate), the unit entitlement allocation can be varied.

For strata arrangements that elect to install sub-meters (and this requires all lots to agree to the install), each lot owner will have a target tariff of a standard 20mm metered connection (\$293.24 in 2015-16) and will receive their own volumetric usage bill measured by their individual sub-meter.

The increased fixed cost of having a sub-meter reflects the additional meter reading and depreciation costs when compared to sharing the cost of one boundary meter.

5.5.6. Developer charges policy

With respect to the developer charges proposal set out in the draft plan, TasWater notes the Regulator’s concerns about the linkage to the as yet incomplete Strategic Asset Management Plan (SAMP). TasWater

also notes the Regulator's view that "in principle, most aspects of TasWater's proposed approach to headworks charges are consistent with the Pricing Principles."

While the Regulator has considered and proposed three alternative approaches to headworks, in addition to the current IPART methodology and that proposed in the draft plan, TasWater does not support headworks being charged into the future where capacity has been installed, including post the conclusion of the Government waiver policy in April 2016, and is also of the view that there will be very little, if any, other support provided.

TasWater remains committed to its proposed developer charges policy, particularly in the medium to long term, as it incentivises development in line with strategic land use planning and continues to deliver price signals (ie relative to the burden the development places upon infrastructure capacity) and therefore provides the most appropriate arrangements for Tasmania.

Notwithstanding this, TasWater does recognise that the timing of the development of its first SAMP presents some challenges, particularly given it will not be possible to complete condition assessments for all systems and assets by 1 July this year or in fact by the time the Government's waiver policy finishes. In turn, this creates some uncertainty with respect to the calculation and application of out of sequence charges in particular.

On this basis TasWater has considered an appropriate interim developer charges policy arrangement that could apply for this next regulatory period. The interim arrangement would be based on the approved serviced land area and would involve no charge for developments within serviced land and user (ie developer) pays for developments outside serviced land. Consistent with the Regulator's draft report, there would also be no change to the current arrangements for works internal and works external.

TasWater notes that this would be an interim arrangement only, with the proposal as set out in the draft plan to be adopted for the regulatory period commencing 1 July 2018. This would allow sufficient time for TasWater to undertake condition assessments and to more fully work through the detailed methodology for calculating and imposing out of sequence and isolated development charges with the Regulator prior to implementation of the policy.

5.5.7. Trade waste charges policy

TasWater notes the Regulator's trade waste comments in the draft report and the Regulator's support of the proposed approach, including charges, set out in the draft plan.

With respect to the intended requirement to amalgamate the Liquid Trade Waste Policy and the draft Liquid Trade Waste Charges Policy, TasWater does not consider this to be an appropriate or sensible outcome on the basis that the liquid trade waste policy, which has already been approved by TasWater's Board, provides information about the business' overall approach to the management of trade waste. It addresses principles other than costs, including safety, asset and environment protection, the importance of which may be lost on customers if combined with the detail of the charges policy. TasWater proposes to remove the Liquid Trade Waste Policy from the final plan and amend the draft liquid trade waste charges policy, taking account of the detailed comments provided by the Regulator.

TasWater is supportive of the Regulator's requirement that the methodology on which TasWater has based its trade waste customer categorisation be clearly outlined and published. It is intended, however, that this be done via a standalone supporting guideline (a copy of which will be attached to the final plan) within a suite of guidelines created to support the policy, rather than the detail sitting within the policy itself. The suite of guidelines will provide detail on application process, sampling and monitoring programs, site audits,

and minimum pre-treatment standards, among other things, to provide clarity and understanding for customers.

TasWater also notes the Regulator's requirements regarding the trade waste category calculator, including making it available to trade waste customers and the public generally and that it links to relevant policies and other supporting materials. TasWater can confirm that the calculator, which will be linked to supporting materials, has been under development for some time with a view to it being activated on the website for use from 1 July 2015.

In relation to the Regulator's requirement for prices negotiated with Category 3 and 4 trade waste customers, TasWater can confirm that the final plan and trade waste charges policy will include an undertaking that the prices will reflect a reasonable transition period recognising the time it would take for a trade waste customer to implement appropriate pre-treatment.

Finally, it is important to note that TasWater is proposing some minor amendments to the business activities for trade waste codes BE08P and BE09. These amendments are based on feedback from site audits that have been undertaken since the draft plan was submitted in August 2014 and provide more clarity for customers on specific use.

5.5.8. Service extension and expansion policy

TasWater notes the Regulator's comments regarding the draft service extension policy that was submitted as part of the draft plan and recognises that it has a legislative obligation to address the matter of service expansion. The draft policy has, therefore, been amended to:

- clarify who is liable for the cost of extensions
- address service expansion, including that costs will be charged in accordance with the Developer Charges Policy
- clarify that connection of properties outside serviced land will be dealt with in accordance with the Service Introduction Charges Policy.

With respect to the first point above, for the 2015-18 period TasWater proposes a continuation of the approach that has applied through the current regulatory period, ie

- TasWater bears the cost of extension for customers who are currently paying a service charge
- the customer is liable to pay an extension charge (in addition to the applicable connection charge) in the event that they are not paying a service charge.

Where the customer is liable, the extension charge would be based on recovering costs.

5.5.9. Service introduction charges policy

TasWater notes the Regulator's comments and has amended the draft service introduction charges policy accordingly, ie the definitions of service introduction and service introduction charge now mirror those set out in the PSP Guideline and the Pricing Regulations and an undertaking regarding the calculation and publication of service introduction charges has been included.

With respect to the preconditions for imposing service introduction charges, TasWater proposes that the service introduction charge will be levied from the date on which the property is able to connect to TasWater's water and/or sewerage infrastructure. This is consistent with the definition of service introduction charge as set out in the Pricing Regulations.

In the event that a service introduction proposal goes ahead, TasWater can confirm its intention that service charges will be imposed on property owners who choose not to sign-up (and pay the service introduction charge) initially.

5.5.10. Other policies

TasWater has considered the Regulator's feedback in relation to the draft "Customer complaints, enquiries and disputes management policy" and has amended the policy to adopt all suggested amendments.

With respect to the Financial Hardship policy, TasWater has also considered the Regulator's feedback and made a number of amendments to the policy, particularly to ensure complete alignment with the *Tasmanian Water and Sewerage Industry Customer Service Code*, April 2013.

5.5.11. Service replacement

TasWater notes the Regulator's comments in the draft report regarding service replacement it is broadly supportive of the proposed approach set out in the draft plan.

TasWater supports the implementation of an end-to-end service replacement process to provide clarity and certainty to customers and stakeholders. In relation to the series of flowcharts that are set out in the draft report to depict the process, TasWater offers the following comments:

- In relation to Figure 6.1, to provide certainty to customers and TasWater it would be preferable to have another step between the current boxes 1.2 and 1.3 to reflect approval from the Economic Regulator for the service replacement proposal to proceed prior to customer offers and the review process (based on feedback from other regulators and the community consultation). This would necessitate a change to the current box 1.4 in that it would then only relate to the process of implementation of the amendments to serviced land.
- There is no discussion within Figure 6.3 of what constitutes discussions with community and regulators revealing that supply replacement is feasible/viable. It is unclear whether the Regulator considers majority support is necessary to proceed and if so whether TasWater has flexibility in determining what support or feasibility/viability looks like.
- The inclusion of a 'right of review' for customers with respect to the offer made by TasWater is a positive addition and it is appropriate that this be undertaken through the Ombudsman. To the extent that this review process is needed and utilised, it would also provide a point of validation for the way in which TasWater has gone about determining compensation or an opportunity for refinement of the approach if necessary.

TasWater considers clarity on the first two issues is important to resolve prior to the commencement of the new regulatory period.