

# Queensland Competition Authority

Draft Assessment

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## Transition to performance monitoring – Unitywater

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May 2014

We wish to acknowledge the contribution of the following staff to this report:

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## SUBMISSIONS

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Closing date for submissions: 30 June 2014

Public involvement is an important element of the decision-making processes of the Queensland Competition Authority (QCA). Therefore submissions are invited from interested parties concerning its assessment of water retailers' transition to annual performance monitoring. The QCA will take account of all submissions received.

Submissions, comments or inquiries regarding this paper should be directed to:

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### Confidentiality

In the interests of transparency and to promote informed discussion, the QCA would prefer submissions to be made publicly available wherever this is reasonable. However, if a person making a submission does not want that submission to be public, that person should claim confidentiality in respect of the document (or any part of the document). Claims for confidentiality should be clearly noted on the front page of the submission and the relevant sections of the submission should be marked as confidential, so that the remainder of the document can be made publicly available. It would also be appreciated if two copies of each version of these submissions (i.e. the complete version and another excising confidential information) could be provided. Where it is unclear why a submission has been marked 'confidential', the status of the submission will be discussed with the person making the submission.

While the QCA will endeavour to identify and protect material claimed as confidential as well as exempt information and information disclosure of which would be contrary to the public interest (within the meaning of the *Right to Information Act 2009* (RTI)), it cannot guarantee that submissions will not be made publicly available.

### Public access to submissions

Subject to any confidentiality constraints, submissions will be available for public inspection at the Brisbane office, or on the website at [www.qca.org.au](http://www.qca.org.au). If you experience any difficulty gaining access to documents please contact us on (07) 3222 0555.

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## THE ROLE OF THE QCA – TASK, TIMING AND CONTACTS

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The Queensland Competition Authority (QCA) is an independent statutory authority to promote competition as the basis for enhancing efficiency and growth in the Queensland economy.

The QCA's primary role is to ensure that monopoly businesses operating in Queensland, particularly in the provision of key infrastructure, do not abuse their market power through unfair pricing or restrictive access arrangements.

In 2012, that role was expanded to allow the QCA to be directed to investigate, and report on, any matter relating to competition, industry, productivity or best practice regulation; and review and report on existing legislation.

### Task, timing and contacts

The QCA has conducted four price monitoring reviews of distribution-retail water providers in south east Queensland covering the pricing periods from July 2010 to June 2015.

On 28 June 2013, the QCA received a Ministerial Direction to investigate and develop a long-term regulatory framework (and pricing principles). The purpose of the review is to improve the regulatory framework and reduce the regulatory costs for water businesses – while providing protection to water users from monopoly power.

### Key dates

Ministerial Direction	28 June 2013
Position Paper - Regulatory Framework	24 February 2014
Position Paper - Pricing Principles	28 March 2014
Position Paper - Return on Capital	30 May 2014
Submissions due on Position Papers	30 June 2014
Submissions due on Draft Assessments (transition)	30 June 2014
Final Report	30 September 2014

### Contacts

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# 1 INTRODUCTION

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## 1.1 Purpose

This draft assessment outlines whether Unitywater should transition to light-handed long-term performance monitoring. The assessment is based on the information available to the QCA from its price monitoring investigations and the transition criteria outlined in the QCA's position paper on the *Long Term Regulatory Framework for SEQ Water Entities* (QCA 2014a).<sup>1</sup>

Comments are sought by **30 June 2014**. All submissions will be taken into account in the QCA's Final Report, due 30 September 2014.

## 1.2 Background

The Ministers have directed the QCA to investigate and report on a long-term regulatory framework for the monopoly distribution and retail water and sewerage activities of the five south east Queensland (SEQ) distributor-retailers (the retailers) — Unitywater, Queensland Urban Utilities (QUU), and the Logan, Redland and Gold Coast City Councils. If accepted, the framework would apply from 1 July 2015.

The overarching regulatory objective is to protect the long-term interests of the users of SEQ water and sewerage services by ensuring the prices of these services reflect prudent and efficient costs, while promoting efficient investment in and the use of these services, having regard to service reliability, safety and security over the long term.

SEQ water retailers have been subject to different forms of price monitoring since 2008. Over 2010–15, the QCA has reviewed the costs of water and sewerage services, monitored changes in prices and compared the retailers' revenues to the maximum allowable revenue. The maximum allowable revenue reflects the QCA's assessment of prudent and efficient costs.

The Ministers required that the form of prices oversight should minimise the administrative burden on the retailers and facilitate a move to a more light-handed framework over time.

## 1.3 Transition to long-term framework

In its position paper, the QCA recommended a light-handed performance monitoring framework which 'tracks' retailers' performance against:

- (a) CPI-X and certain financial information
- (b) pricing principles
- (c) desired customer engagement practices
- (d) strategic approach to long term investment
- (e) service quality standards (including performance targets).

The QCA also recommended that depending on the outcome of the 2013-15 review, a transition to performance monitoring may be required. The length and nature of the transition may vary between retailers.

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<sup>1</sup> The QCA's Draft Position Paper *Long Term Regulatory Framework for SEQ Water Entities* is available from the QCA website. Comments on this paper are also due by 30 June 2014.

## 1.4 Criteria

The position paper outlined the criteria for an immediate transition to long-term performance monitoring as including:

- (a) absence of public interest or equity issues that may warrant regulatory review
- (b) regulated services are clearly defined and separated from non-regulated services
- (c) evidence that market power is not being exercised
- (d) absence of imminent material changes in circumstances or major infrastructure costs
- (e) a demonstrated capacity to provide the required information accurately and on time, based on prior regulatory processes.

Performance in customer engagement, strategic planning for long term investment, service quality and application of pricing principles would also be relevant in assessing readiness.

It is also considered that water retailers may be required to provide additional information or resolve outstanding issues in the intervening period before commencement of annual performance monitoring from 1 July 2015.

### Where criteria are not met

Should a retailer be considered not ready to move to annual performance monitoring, the existing arrangements should continue until outstanding elements are addressed. This would require a further detailed review - for a one-year period (2015-16). The scope of the one-year review would depend on the nature of the outstanding issues.

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## 2 ASSESSMENT

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### 2.1 Introduction

The QCA has assessed Unitywater against the criteria using the outcomes of the 2013-15 investigation and from publicly available sources.

### 2.2 Assessment against core criteria

#### 2.2.1 Public interest and equity

The criteria require that there be an absence of public interest or equity issues that may warrant regulatory review for a retailer to transition to long-term performance monitoring.

The QCA is not aware of any public interest or equity issues that would warrant further regulatory review and prevent Unitywater from transitioning to long-term performance monitoring.

In previous reviews, the QCA has been required to assess whether Unitywater complied with a CPI cap when council rebates and subsidies were taken into account (QCA 2013 and 2012). In 2011-12 and 2012-13, Moreton Bay Regional Council provided a rebate on the fixed water and sewerage charges for the residents in its council area. The QCA concluded that Unitywater had complied with the CPI price cap in both 2011-12 and 2012-13.

In its 2013-15 review, the QCA noted that the Moreton Bay Regional Council rebate expired on 30 June 2013. Further, the State Government bulk water rebate that applied to the bulk water component of the residential bill also expired on 30 June 2013.

Unitywater also provides a haemodialysis rebate which provides customers using haemodialysis machines at home with an allowance (at no charge) of 200 kilolitres per annum.

The Department of Energy and Water Supply (DEWS) is undertaking a review of the Water and Sewerage Services Code for Small Customers in South East Queensland and will consider the water businesses' current policies (including hardship) in relation to supporting customers.

#### 2.2.2 Regulated services are defined

The criteria require that regulated services are clearly defined and separated from non-regulated services.

In previous reviews, the QCA requested retailers to list all regulated services, their tariffs and corresponding volumes and revenues. Unitywater complied with this requirement, providing the (average) tariffs, volumes and revenues from their price setting process. Further, Unitywater provided a detailed price list for its services.

The QCA also requested retailers to exclude the revenues and costs of non-regulated services, with only the regulated revenues and costs falling under review. The retailers were also required to provide explanation of the basis of any allocations made to non-regulated services that would assist the QCA in its assessment of their submissions. Relevant definitions were as follows:

- (a) a non-regulated service was defined to mean a service provided by a retailer that is not required to satisfy any specified legal obligation or is provided by other service providers in a competitive market in which the business has no legal power to influence a



customer's selection of the business as the service provider. For example, this could include laboratory services. Non-regulated services are not to be disaggregated between water and wastewater.

- (b) non-regulated revenue includes interest on investments, but not interest paid by customers on overdue accounts.

In previous reviews, the delineation between regulated and non-regulated services has not been specifically investigated by the QCA: non-regulated services have not been a material segment of costs and revenues. The precise boundary of regulated and non-regulated services may change over time as the nature of relevant services and markets develops.

Unitywater has identified its non-regulated services, costs, revenues and assets. For the 2012-13 review, Unitywater listed its non-regulated services as laboratory services, private works, facilities management and other non-regulated services. For the period 1 July 2013 to 30 June 2015, Unitywater submitted information templates indicating that:

- (a) non-regulated revenues are \$10.2 million, regulated revenues are \$979.0 million
- (b) non-regulated operating costs are \$10.7 million, regulated operating costs are \$582.8 million
- (c) non-regulated assets are \$1.1 million, regulated assets are \$3,305.2 million (as at 30 June 2015) (Unitywater 2013b).

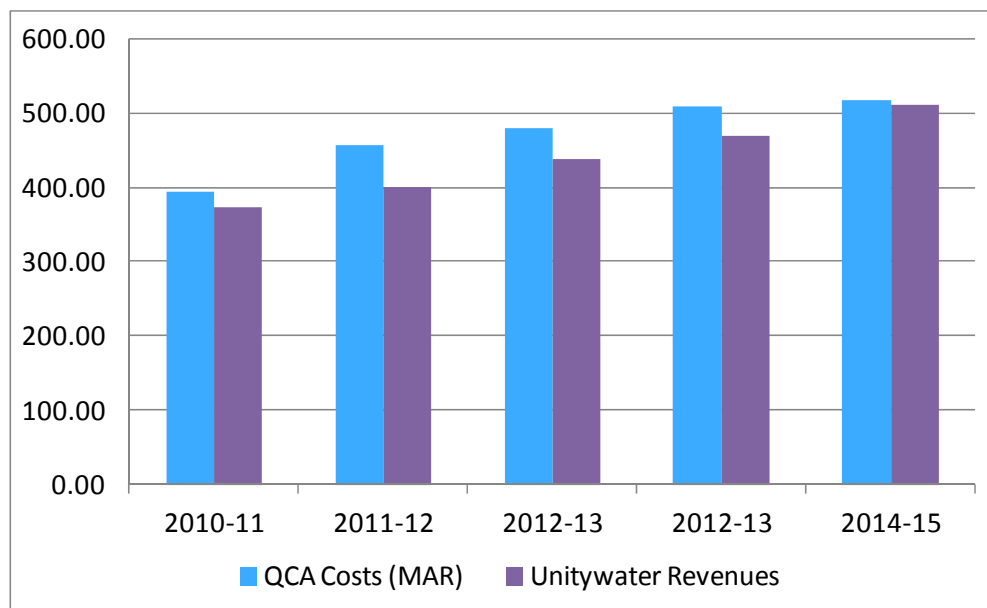
Overall, the QCA considers that regulated services are clearly defined and sufficiently separated from non-regulated services. The revenues and costs of non-regulated services are not material enough to warrant further investigation.

However, the QCA has not reviewed whether costs have been appropriately allocated between service categories. The QCA needs to be confident that prices reflect the cost of providing services. This is an issue to be addressed in assessing retailers' compliance with pricing principles.

### 2.2.3 Market power

The criteria require evidence that market power is not being exercised, that is, the opening cost base is efficient and further cost increases comply with the CPI-X mechanism (with above referenced qualifications) and service quality is in line with expectations.

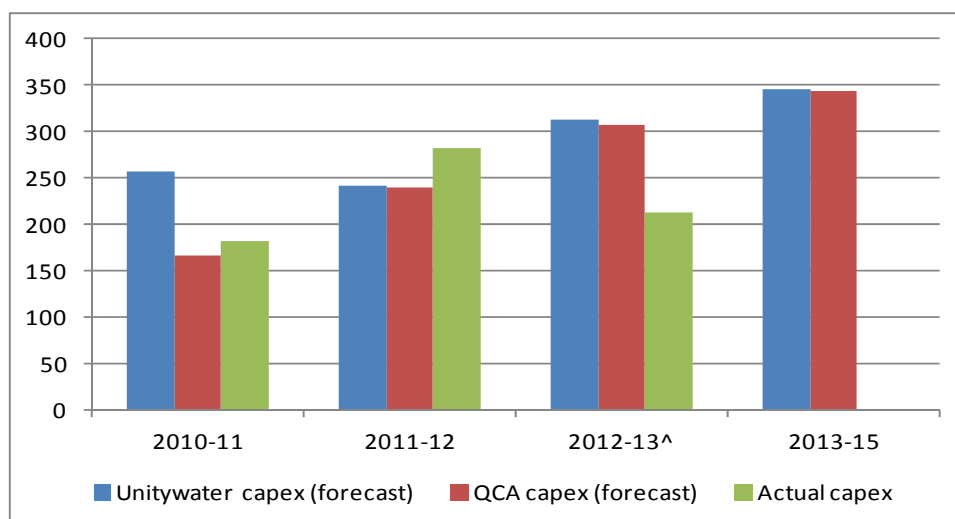
In previous reviews of costs and revenues, the QCA did not find any evidence that Unitywater was exercising its monopoly power. Unitywater's revenues have been below the aggregate maximum allowable revenue (MAR) (2010-15) (see Figure 1 below).

**Figure 1 Forecasts of Unitywater costs (MAR) and revenues (\$m)**

Source: QCA past price monitoring revenues 2010-15.

It is noted that:

- (a) Unitywater's MARs have been above the QCA MAR, with the difference in 2013-15 mainly due to Unitywater's higher weighted average cost of capital (WACC) of 7.62% compared to the QCA benchmark WACC of 6.57%. However, while differences exist, the QCA proposes to use its MAR as a basis for performance monitoring from 2015. Unitywater's revenues have been below the QCA MAR.
- (b) capital expenditure proposals have been reviewed four times over the period 2010-2015 by two different independent groups of consultants. Over 2010-15, the sample of capital projects subject to prudence and efficiency review has averaged 33% of forecast capital expenditure (excluding contributed assets). Over 2010-15, the QCA's prudent and efficient capital expenditure was lower than Unitywater's by 35.2% (predominantly due to deferrals identified by Unitywater and the QCA (see Figure 2). However, actual capital expenditure for 2010-13 was below the level of forecasts previously found to be prudent and efficient and therefore actual capital expenditure was used to roll forward the RAB in the 2013-15 review.

**Figure 2 Unitywater capital expenditure (\$m)**

- (c) for the 2013-15 review, Unitywater has adopted a starting RAB as at 1 July 2010 rather than at 1 July 2008 as required by the Ministerial Direction.

The QCA adopted the 1 July 2008 RAB and 2008-10 data (including capital expenditure and asset lives) from Unitywater's previous submissions. Unitywater provided revised capital expenditure data for 2010-15. The QCA allocated this data to services and asset classes in some instances, where this was not readily available from the Unitywater data.

The QCA opening RAB as at 1 July 2013 was slightly (0.4%) lower than that estimated by Unitywater. The QCA closing RAB as at 30 June 2015 was (1.4%) below that estimated by Unitywater. The QCA is working with Unitywater to seek to further reconcile differences in the RAB.<sup>2</sup> This is expected to result in only minor changes to the RAB. Therefore, the opening cost base as set by the QCA MAR is considered suitable as a basis for future performance monitoring.

- (d) non-bulk operating expenditure has also been reviewed four times (by two different independent groups of consultants). Over 2010-15, the QCA's estimate of prudent and efficient non-bulk operating expenditure was lower than Unitywater's. As noted above, while differences exist, Unitywater's revenues have been below the QCA MAR.

Overall, there is no evidence to suggest that market power is being exercised.

#### 2.2.4 Imminent change in circumstances

The criteria require that there is an absence of imminent material changes in circumstances or major infrastructure costs.

Unitywater's cost information requested for the 2013-15 review did not provide information on post-2015 costs. Bulk water prices until 2017-18 are publicly available on the DEWS website.

<sup>2</sup> As part of this process, Unitywater proposed an alternate method to allow QCA to validate the RAB via reliance on Unitywater's corporate asset register that has been subject to audit by the Queensland Audit Office. Unitywater considered this would be more accurate and cost-effective than providing the data template for the QCA model.

An independent and consistent validation of the RAB using the framework set out in past price monitoring requires a data template that can be verified against supporting documents. The QAO does not apply the rules set out in the Direction for price monitoring in the conduct of its audit.

The QCA is not aware of any imminent material changes in circumstances or major infrastructure costs that would impede Unitywater's transition to the long-term framework.

### 2.2.5 Information provision

The criteria require that there is demonstrated capacity to provide information accurately and on time.

In general, Unitywater has provided its submissions to price monitoring accurately and on time. Unitywater has responded to further requests for information in a reasonable timeframe.

Issues arose in the 2013-15 review in relation to the information required to roll forward the 1 July 2008 RAB, as noted above. The QCA has committed to work with Unitywater to reconcile differences in the RAB. The differences are not considered material.

The QCA considers that, on balance, Unitywater has demonstrated it has the capacity to provide information accurately and on time.

### 2.2.6 Summary of assessment against core criteria

On the basis of the above assessment, Unitywater meets the core criteria for moving to the light-handed performance monitoring framework. Issues relating to the RAB roll-forward remain to be resolved.

## 2.3 Assessment against other criteria

### 2.3.1 Introduction

The position paper noted that performance in customer engagement, strategic planning for long-term investment, service quality and pricing principles are relevant to the assessment. Only a partial assessment can be made in relation to many of these criteria, as some were not monitored in the past and complete information is not readily available.

The QCA has sought to identify whether there is any information on these criteria that would delay or impede transition by assessing the entities' performance to date and predisposition to further improvement. To assist entities improve their performance, areas of potential improvement that would be expected to be addressed in subsequent annual performance monitoring are identified.

### 2.3.2 Customer engagement

#### Excerpt of draft recommendations in position paper

- 5.1 Each SEQ entity, in consultation with its customers, develop a strategy for customer engagement based on best practice principles.**
- 5.2 Customer engagement should:**
  - (a) promote understanding of customer's needs and be representative and responsive of customer views**
  - (b) be relevant, evidence based, open and transparent, timely, collaborative, and cost effective.**
- 5.3 The customer engagement strategy should include a customer consultation committee.**
- 5.4 SEQ entities submit by 31 October 2015 an initial statement of their customer engagement strategy.**
- 5.5 The QCA will assess these customer engagement strategies and provide, where appropriate, advice to entities on possible improvements to ensure best practice.**

In its submission to the 2013-15 review Unitywater stated that it is committed to keeping customers and stakeholders informed, including through:

- (a) its community advisory group, which consists of nine members representing community and the business sectors and meets quarterly to provide feedback to Unitywater on customer, community and business needs
- (b) regular briefings to community organisations and other groups on relevant topics
- (c) customers research forums which gauge the effectiveness of communications and gain feedback on planned initiatives
- (d) online material and printed material mailed with customer accounts
- (e) its obligations under the customer charter to inform customers of planned interruptions
- (f) its use of Facebook and YouTube as complementary means of communicating with targeted customers.

In its 2013-15 review, the QCA noted that retailers should explain the reasons for the change in each part of the bill as well as the overall change.

Unitywater has a community advisory group in place and undertakes regulator briefings to the community organisations, customer research and other activities envisaged for a customer consultation committee. The QCA considers that based on available information Unitywater's activities incorporate many of the desired attributes of effective customer engagement.

Accordingly, current performance should not impede Unitywater moving to light-handed annual performance monitoring.

Unitywater will be required to provide more information on customer engagement practices as part of annual performance monitoring.

### 2.3.3 Strategic planning for long term investment

#### Excerpt of draft recommendations in position paper

- 6.1 The council water businesses be subject to the same legislative and regulatory planning requirements as the DRs.**
- 6.2 Entities should provide evidence of board/council approval and Ministerial endorsement of their relevant Water Netserv Plans to the QCA.**
- 6.3 Entities annually report to the QCA on their annual capital works plans or annual performance plans.**
- 6.4 Annual updates to Water Netserv Plans also be submitted.**
- 6.5 SEQ entities provide to the QCA annually, details of their compliance with the asset management standard they have implemented and report on progress in addressing areas of improvement to achieve good industry practice.**
- 6.6 Should a cost of service review be triggered, the QCA assess entities asset management practices against PAS-55.**
- 6.7 Entities report on the project evaluation practices used for significant capex projects.**
- 6.8 Entities submit details of project evaluation, including options analysis and risk analysis, for up to the 6 largest capex items, where required as part of a request for further information.**

As noted above, in the 2013-15 price monitoring review, the QCA made adjustments to one of Unitywater's capital expenditure projects, based on its consultant SKM's advice following their detailed review of six sampled projects. A reduction of \$0.52 million was made to the sampled expenditure of \$61.5 million (total capital expenditure for 2013-15 is \$344.8 million).

SKM also reviewed Unitywater's policies and procedures for capital expenditure, including its Water Netserv Plan for consistency with the SEQ Regional Plan. A summary of SKM's findings is provided in Table 1.

**Table 1 Capital expenditure policies and procedures**

<i>Criteria</i>	<i>Findings</i>
Standardised approach to cost estimating	Unitywater's cost estimating processes were not consistent with good industry practice, due to a capital works cost estimating tool not being mandatory for use.
Gateway review	Unitywater's gateway process includes five review points/gates.
Detailed analysis of options for major projects	Unitywater has processes in place which provide for detailed analysis of options for major projects.
Commissioned capital expenditure from 1 July 2010 in the RAB	Unitywater uses models to translate capital expenditure as-incurred to as-commissioned expenditure. Commissioned values were reflected in the data templates used to roll forward each entity's RAB from 1 July 2010.
Compliance	Unitywater's capital expenditure policies and procedures met the compliance requirement and were robust.
Considers regional perspective	<p>Unitywater's Water Netserv Plan Part B and Capital Works Planning Manual do not include provisions to address regional requirements at key decision points.</p> <p>Unitywater participates in the SEQ Water Service Provider Partnership, SEQ Operations Committee, and SEQ Strategy and Planning Committee. Within its service area, Unitywater takes a whole of region approach to invest in capital projects in Moreton Bay and the Sunshine Coast. Unitywater actively supports investment in alternative nutrient or pollutant reduction initiatives to achieve lower cost environmental benefits in preference to continual focus on STP licences.</p> <p>The QCA considers that the realisation of benefits due to a regional perspective should be captured and reported, to demonstrate regional efficiencies are being pursued and achieved.</p>
Asset management system	<p>Unitywater's asset management system was not consistent with good industry practice and was not robust.</p> <p>Unitywater has not yet fully implemented its Consolidated Asset Management System (CAMS) which will allow it, amongst other things, to:</p> <ul style="list-style-type: none"> <li>(a) more efficiently assess the condition of its properties</li> <li>(b) prioritise maintenance and</li> <li>(c) better manage its fleet of heavy and light vehicles and plant and equipment.</li> </ul> <p>Unitywater participated in the IWA/WSAA 2012 Asset Management Performance Improvement Project.</p>
Procurement	Unitywater's Procurement and Disposals Policy incorporated good industry practices for the procurement of goods and services and was robust

Source: SKM (2014).

Overall, while Unitywater has a Netserv Plan, and demonstrated good practice in options analysis and procurement procedures, there are some shortcomings in cost estimating processes, requirements relating to regional planning and asset management practices.

However, given that capex savings identified by SKM were not substantial (0.8% of sample), the shortcomings are not considered material enough to prevent Unitywater moving to annual performance monitoring.

The QCA proposes to seek evidence that the issues raised by SKM (Table 1) are being progressed as part of future performance monitoring.

### 2.3.4 Service quality

The position paper recommended 38 service quality indicators to be used as a basis for initial service quality reporting: 8 on baseline information, 13 on water and sewerage reliability and service, 4 on water quality, 5 on water consumption, recycling and reuse, 4 on customer responsiveness and service, and 4 on the environment.

These indicators were released after the price monitoring reviews from 2010-15 were finalised. Therefore, the price monitoring reviews to date have not investigated Unitywater's service quality against these principles and have not requested relevant information to do so.

However, a preliminary assessment can be made based on information that is publicly available.

Unitywater Customer Service Charter outlines its commitments, responsibilities and standards for water and sewerage services. Unitywater has identified 11 quantitative performance indicators in relation to service quality. Other qualitative standards also apply.

Unitywater annually reports on its performance against eight parameters as shown in Table 2.

**Table 2 Unitywater's reported performance**

WATER		
Parameter	Target	Achieved
Australian Drinking Water Guidelines compliance	>98%	99.9%
Drinking water quality complaints per 1000 connected properties/year	<10	0.05
Unplanned water supply interruptions per 100 km/year	<10	3
Water main breaks and leaks per 100 km/year	<25	6.5
SEWERAGE		
Parameter	Target	Achieved
Odour complaints per 1000 connected sewerage properties	<65	20
Sewage treatment plant compliance	98%*	97.4%
Dry weather sewage overflows per 100 km of mains/year	<2.2	1.7
Sewer main breaks and chokes per 100 km/year	<40	18.8

Source: Unitywater 2013d.

While some of the Unitywater's service standards overlap with some of those identified by the QCA for performance reporting, some of the precise indicators and measures differ. Unitywater reports on six of the QCA's 38 recommended indicators.

Therefore, 32 additional indicators are recommended by the QCA. Many (23) of these are already required under the National Water Commission (NWC) performance reporting process. Unitywater has provided information for NWC performance reporting since Unitywater's inception in 2010-11. However in 2012-13 national performance reporting, Unitywater did not report on key network reliability and customer service indicators (NWC 2014).

There is therefore evidence that Unitywater has set and is monitoring and publicly reporting on its service quality. Unitywater has substantially met the performance targets for its own nominated indicators.



The QCA has not previously monitored service quality performance and Unitywater has not been required to report against all of the QCA's indicators.

Having regard to Unitywater's commitment to service quality performance monitoring, the QCA considers that the identified shortcomings should not impede Unitywater moving to light-handed annual performance monitoring.

However, the QCA proposes that Unitywater will be required to report against the full range of indicators as part of the light-handed framework. Unitywater should also participate in national performance reporting of key network reliability and customer service indicators.

### 2.3.5 Pricing principles

The QCA position paper *SEQ Long Term Regulatory Framework - Pricing Principles* (QCA 2014c) recommended pricing principles to apply to urban water, sewerage, trade waste, recycled water and stormwater reuse.

These principles were released after the price monitoring reviews from 2010-15 were finalised. Therefore, the price monitoring reviews to date have not investigated Unitywater's prices against these principles and have not requested relevant information to do so.

The QCA has not previously reviewed Unitywater's pricing practices and there is insufficient available information in many instances to allow a detailed assessment (see Table 3).

Pricing is important both to ensure customers are aware of the implications of their consumption and to allow Unitywater to manage its risks.

Nevertheless, previous detailed price monitoring has not required adherence to the proposed pricing principles. It would therefore seem inappropriate to impede Unitywater from moving to more light handed performance monitoring.

The QCA notes that for all retailers this is considered a priority issue for attention.

**Table 3 General pricing objectives and principles**

		<i>Draft Recommendations - Unitywater Assessment</i>
Pricing objectives	1.1	That pricing of urban water, sewerage, trade waste, recycled water and stormwater re-use services provided by SEQ entities: (a) promotes economic efficiency (b) ensures revenue adequacy (c) takes account of the public interest (including fairness and equity) (d) is transparent, predictable, simple and cost-effective to apply. <i>Comment: Insufficient information for assessment. Past price monitoring has adopted annual water and sewerage cost/revenue comparisons.</i>
Pricing Principles	1.2	Entities initially establish that the pricing principles are being applied and subsequently advise of any departures, the reasons for the departure and provide relevant supporting analysis. <i>Comment: Insufficient information for assessment. Past price monitoring has adopted annual water and sewerage cost/revenue comparisons.</i>
	1.3	Pricing reflects marginal cost, together with a two-part tariff where necessary to achieve revenue adequacy. <i>Comment: Insufficient information for assessment. Prices generally based on legacy council pricing with some harmonisation and changes in tariff structure designed to allow customers more control over bills. Unitywater (2013b) has a two-block inclining block tariff (IBT) for residential customers of Moreton Bay and Sunshine Coast regions for 2013-14. A three-tier IBT previously applied in 2012-13 in the Moreton Bay region.</i>
	1.4	Prices be set between incremental (marginal) cost and stand-alone cost. <i>Comment: Insufficient information for assessment.</i>
	1.5	Prices reflect the long run marginal cost (LRMC) of providing a particular service. <i>Comment: Insufficient information for assessment.</i>
	1.6	Prices reflecting short run marginal cost (SRMC) be considered when SRMC for a particular period significantly exceeds the LRMC (estimated for a longer period) for a particular service. This is sometimes referred to as scarcity charging. <i>Comment: Unitywater does not charge based on scarcity. Bulk water prices are set by the Queensland Government (not Unitywater) and do not vary with supply constraints.</i>
	1.7	LRMC be estimated on the basis of the perturbation or AIC method. <i>Comment: Insufficient information for assessment.</i>

**Table 4 Application of pricing principles**

<i>Chapter</i>	<i>Topic</i>	<i>No</i>	<i>Draft Recommendation - Unitywater Assessment</i>
Urban Water	Demand forecasting	2.1	Long term forecasts used for capital planning be based on SEQ Water Strategy forecasts. <i>Comment: In the 2013-15 review, Unitywater provided information on its long-term demand for capital planning: it uses 230l/p/d for low and medium density development and 200l/p/d for high density development. Further, Unitywater's capital planning reflects the SEQ Design and Construction Code.</i>

<b>Chapter</b>	<b>Topic</b>	<b>No</b>	<b>Draft Recommendation - Unitywater Assessment</b>
		2.2	<p>Short term demand forecasts be based on estimated water use per customer/connection and population forecasts (number of connections) and take account of any bounce-back effect as well as local circumstances.</p> <p><i>Comment: Unitywater has applied this principle in setting water prices, as noted in past price monitoring reports.</i></p>
		2.3	<p>Demand forecasting practices and alternative models (including demand elasticities) be reviewed by a working group including the entities, QCA and other relevant parties.</p> <p><i>Comment: Unitywater made this suggestion to past price monitoring reviews.</i></p>
	Volumetric charges	2.4	<p>The volumetric charge for urban water services should reflect LRMC.</p> <p><i>Comment: Unitywater introduced changes in tariff structure in 2013-14 designed to allow customers more control over bills. Unitywater (2013b) has a two-block IBT for residential customers of Moreton Bay and Sunshine Coast regions for 2013-14.</i></p> <p><i>The QCA requested but was not provided with Unitywater's fixed and variable costs underpinning its changes to tariff structure in 2013-14.</i></p>
		2.5	<p>Where prices exceed average costs, short-term over-recovery of revenues be addressed by ex-post rebates with adjustments made to the fixed charge.</p> <p><i>Comment: Insufficient information for assessment. Past price monitoring has adopted annual water and sewerage cost/revenue comparisons.</i></p>
	Fixed charges	2.6	<p>Fixed charges be set to recover the MAR not covered by the volumetric charge.</p> <p><i>Comment: Insufficient information for assessment.</i></p>
		2.7	<p>Charges not encourage customers to bypass or disconnect from the network.</p> <p><i>Comment: No information to indicate customers are seeking to bypass or disconnect from Unitywater's network. Past price monitoring has not investigated cost allocation, including to customer types.</i></p>
	Inclining and declining block tariffs	2.8	<p>Inclining and declining block tariffs not be introduced, and where they are in place be phased out over time to a single volumetric charge.</p> <p><i>Comment: In 2013-14, Unitywater reduced the number of tiers in Moreton Bay from three to two for standalone residential dwellings. Multi-dwelling residential and non-residential customers still have a three tier inclining block tariff (this is intended to transition to two tiers).</i></p>
	Location-based or nodal pricing	2.9	<p>Location-based charges for urban water services be applied where the location cost differences are material and where it is practical and cost effective.</p> <p><i>Comment: Unitywater has two location-based pricing areas, based on previous council boundaries.</i></p>
	Peak period and seasonal charges	2.10	<p>Time of day or seasonal charges be considered for urban water services where there are identified economic efficiency benefits and where practical and cost effective.</p> <p><i>Comment: Unitywater has no time of day or seasonal charges.</i></p>

<b>Chapter</b>	<b>Topic</b>	<b>No</b>	<b>Draft Recommendation - Unitywater Assessment</b>
	Self-selecting tariffs	2.11	<p>Self-selecting tariff options be considered where there is sufficient information for customers to make choices, provided they do not result in cross-subsidies or introduce unmanageable revenue risks for the entity.</p> <p><i>Comment: Unitywater does not offer self-selecting tariff options.</i></p>
	Service quality differentials and interruptible tariffs	2.12	<p>Price/service quality tariff options are supported, where material cost differentials are associated with different levels of service.</p> <p><i>Comment: Unitywater does not offer tariffs differentiated by service quality.</i></p>
	Metering and billing arrangements	2.13	<p>Individual metering of flats and units be adopted where economic and practical.</p> <p><i>Comment: As of 1 Jan 2008 all new unit/apartment complexes are required to be fitted with individual meters per dwelling. For existing complexes with shared meters, individual water usage is charged according to the property share percentage of the total water usage by all residents. This reflects an apportionment based on the original plans submitted for approval by the builder. Therefore, those flats and units with more bedrooms/bathrooms are allocated a greater proportion of water and wastewater charges.</i></p>
2.14		<p>Where water is separately metered, and where practical, tenants be billed the fixed and variable charges for water and sewerage.</p> <p><i>Comment: Landlords are entitled to pass the volumetric proportion of a bill to a tenant provided the premises are individually metered and meet water efficiency standards.</i></p>	
2.15		<p>Customers with unmetered connections be charged a deemed amount for usage, reflecting average use for similar property types.</p> <p><i>Comment: Insufficient information for assessment.</i></p>	
2.16		<p>Customers with unmetered connections be given the option of paying for meter installation.</p> <p><i>Comment: A Unitywater fact sheet on sub-metering notes that if the owners of an existing development decide to proceed with the installation of a sub-meter, a body corporate resolution is required and the installation is at the cost of the property owner or body corporate (Unitywater 2014a).</i></p>	
2.17		<p>For vacant land where water and services are available for connection, the water access charge that applies to connected properties (the relevant domestic or commercial charge) be applied.</p> <p><i>Comment: Unitywater charges vacant land the same water and sewage access charge that applies to residential connected properties.</i></p>	

<b>Chapter</b>	<b>Topic</b>	<b>No</b>	<b>Draft Recommendation - Unitywater Assessment</b>
		2.18	<p>Concessions and rebates:</p> <ul style="list-style-type: none"> <li>(a) reflect a consistent approach between the entities</li> <li>(b) be set to apply to either the fixed charge or as a total direct adjustment to the gross invoice amount</li> <li>(c) be capped so as not to subsidise discretionary use</li> <li>(d) be transparent with acknowledgement of the source of, and purpose for, particular concessions/rebates.</li> </ul> <p><i>Comment: The Moreton Bay regional Council rebate expired 30 June 2013.</i></p> <p><i>Unitywater provides a haemodialysis rebate which provides customers using haemodialysis machines at home with an allowance (at no charge) of 200 kilolitres per annum.</i></p>
		2.19	<p>Concessions associated with excess water use caused by leaks, be determined by the entities in consultation with customers.</p> <p><i>Comment: Unitywater has a concealed leak policy that is publicly available (Unitywater 2014b).</i></p>
		2.20	<p>Hardship arrangements be consistent with legislative or operating requirements and avoid cross-subsidies where practical.</p> <p><i>Comment: Unitywater has a financial hardship policy, as noted in 2013-15 price monitoring. DEWS is undertaking a review of the SEQ Customer Code and will consider the water businesses' policies (including hardship) in relation to supporting customers.</i></p>
		2.21	<p>Meter-reading and billing be undertaken at least quarterly.</p> <p><i>Comment: Unitywater applies quarterly billing.</i></p>
	Tradeable water entitlements	2.22	<p>Tradeable urban water entitlements be considered only where the efficiency gains are sufficient to justify the administration and transactions costs.</p> <p><i>Comment: No tradeable urban water entitlements.</i></p>
Sewerage	Demand forecasting	3.1	<p>Demand for sewerage services be based on forecast growth in connections, linked to population growth.</p> <p><i>Comment: Unitywater has applied this principle in setting sewerage prices, as noted in past price monitoring reports.</i></p>
	Efficient pricing	3.2	<p>For residential customers:</p> <ul style="list-style-type: none"> <li>(a) sewerage charges generally be based on a single part tariff with a fixed charge per customer or connection</li> <li>(b) volumetric charges (based on discharge factors) be applied where the LRMC is significant and should be based on discharge or return factors linked to the LRMC of providing the water volumes.</li> </ul> <p><i>Comment: Unitywater introduced two-part tariffs for residential sewage service customers in 2013-14 consisting of a fixed access charge and a discharge factor based volumetric charge. The information provided by Unitywater to explain the introduction of the discharge factor focussed on allowing customers more control over bills and did not refer to LRMC or cost-reflectivity.</i></p>

<b>Chapter</b>	<b>Topic</b>	<b>No</b>	<b>Draft Recommendation - Unitywater Assessment</b>
		3.3	<p>For non-residential customers:</p> <p>(a) fixed sewerage charges be based on the impact of the customer on the system. In the absence of direct metering, water connection size is considered a reasonable proxy</p> <p>(b) if appropriate, volumetric charges be applied based on relevant discharge factors established by customer type. Customers should be able to negotiate a variation in the discharge factor.</p> <p><i>Comment: Unitywater applies a fixed access charge to non-residential sewage customers. Unitywater has indicated that the pricing structure for non-residential customers will be reformed in 2014-15.</i></p>
		3.4	<p>Nodal pricing for sewerage services be applied where cost effective.</p> <p><i>Comment: Unitywater has two location-based pricing areas, based on previous council boundaries.</i></p>
Trade Waste	Demand forecasting	4.1	<p>Where the customer base changes in line with growth, trend information be used to provide reasonable forecasts of demand for trade waste services.</p> <p><i>Comment: Insufficient information for assessment.</i></p>
		4.2	<p>Entities consult with large customers to monitor any step changes in demand for trade waste services.</p> <p><i>Comment: Insufficient information for assessment.</i></p>
	Efficient pricing	4.3	<p>Trade waste prices be based on the impactor pays principle.</p> <p><i>Comment: Insufficient information for assessment.</i></p>
		4.4	<p>Charges be based on the LRMC of transport, treatment and disposal of trade waste, with variable charges based on volume and contaminant load.</p> <p><i>Comment: Insufficient information for assessment. Unitywater's trade waste charges are based on three categories of customers, with permit fees, volume charges (assumed or metered depending on category) and strength charges (assumed or measured depending on category).</i></p>
		4.5	<p>Specific charges for the management of trade waste services (inspection and monitoring) be applied on a cost reflective basis.</p> <p><i>Comment: Insufficient information for assessment.</i></p>
		4.6	<p>Charges be differentiated according to customer type and risk factors, and by location (as part of risk assessments) if considered cost effective.</p> <p><i>Comment: Unitywater's trade waste charges are based on three categories of customers, with permit fees, volume charges (assumed or metered depending on category) and strength charges (assumed or measured depending on category).</i></p>
	Compliance	4.7	<p>Consistent with regulations, entities to apply penalty charges for non-compliance and recover costs associated with breaches.</p> <p><i>Comment: Unitywater relies exclusively on applying the penalty units outlined in the Water Supply (Safety and Reliability) Act 2008.</i></p>
Recycled Water	Efficient pricing	5.1	<p>The revenue requirement for recycled water services be based on the total additional cost of recycling less avoided costs and less developer contributions.</p> <p><i>Comment: Insufficient information for assessment.</i></p>

<b>Chapter</b>	<b>Topic</b>	<b>No</b>	<b>Draft Recommendation - Unitywater Assessment</b>
		5.2	Direct and avoidable costs be allocated between relevant parties on a beneficiary pays basis. <i>Comment: Insufficient information for assessment.</i>
		5.3	Recycled water volumetric prices be based on LRM for the established recycled water scheme where possible, based on marginal operating costs less marginal avoided costs. Where the volumetric charge is then higher than the potable water volumetric charge, it may be necessary to reflect demand sensitivities to ensure demand clears supply. <i>Comment: In 2013-14, Unitywater provides Class A water (\$1.30/k) and B Water (\$0.65/k) through its reticulation system, both are below the bulk water price.</i>
		5.4	If still required to ensure revenue adequacy, fixed charges in a two-part tariff should be set to recover remaining revenues, also subject to willingness to pay. <i>Comment: See above, no fixed charges apply for recycled water.</i>
		5.5	If the revenue requirement is still not achievable, unrecovered amounts should be allocated to potable and sewerage charges in proportion to avoided cost allocations. <i>Comment: Insufficient information for assessment.</i>
		5.6	Charges to be periodically reviewed, as customer acceptance increases. <i>Comment: Insufficient information for assessment.</i>
	Sewer mining	5.7	Charges for sewer mining be set on a case-by-case basis to reflect relevant direct costs, a share of sewerage system common costs, service costs for any returns, less avoided costs. <i>Comment: There is no sewer mining undertaken within Unitywater's sewer network.</i>
	Stormwater Reuse		6.1
		6.2	Rate-based charges continue to be used for recovery of stormwater drainage costs. <i>Comment: Rate-based charges are used for recovery of stormwater drainage costs. Unitywater does not provide stormwater drainage services.</i>
Industry-wide issues	Externality pricing	7.1	The inclusion of externality prices be supported where material impacts can be valued accurately and cost effectively. <i>Comment: Insufficient information for assessment.</i>
		7.2	Prices incorporating estimates of externalities avoid duplication with other mechanisms and be transparent. <i>Comment: Insufficient information for assessment.</i>
		7.3	Licences and market mechanisms (where practical) be considered by Government where the benefits are considered to justify the costs. <i>Comment: Insufficient information for assessment.</i>
	Third party access	7.4	Third party access prices be based on the cost of service methodology, and take account of relevant joint or common costs. Any departure from this methodology (such as applying the retail minus

<b>Chapter</b>	<b>Topic</b>	<b>No</b>	<b>Draft Recommendation - Unitywater Assessment</b>
			methodology) is to be justified. <i>Comment: Insufficient information for assessment.</i>
		7.5	Where retail prices are averaged across user groups (postage stamp tariffs) an adjustment apply to ensure that access prices do not result in increased costs of service delivery for remaining customers. <i>Comment: Insufficient information for assessment.</i>
	Cost allocation	7.6	Common costs be allocated to services and customers on the basis of a causal relationship between the costs incurred and the water, sewerage, recycled water or other service performed. <i>Comment: Insufficient information for assessment.</i>
		7.7	If a causal relationship cannot be established between costs incurred and the relevant service, a reasonable cost allocator needs to be established. <i>Comment: Insufficient information for assessment.</i>
	Price paths	7.8	Price paths be applied where there are substantial price increases, having regard to customers' ability to pay and the impacts on the service provider's financial viability. <i>Comment: Unitywater has not published a future price path. Insufficient information for assessment.</i>
		7.9	Price paths be set on a revenue neutral basis. <i>Comment: Unitywater has not published a future price path. The QCA is publishing a separate paper on under and over-recovery mechanisms.</i>

Source: QCA 2014c.

## 2.4 Conclusions

On the basis of its assessment against core criteria (see Table 5), the QCA considers that Unitywater should immediately transition to long-term annual performance monitoring as from 1 July 2015. Outstanding issues relating to RAB roll-forward are expected to be resolved.

It is also noted that apart from the application of proposed pricing principles (where a detailed assessment has yet to be undertaken), Unitywater has showed a commitment to and performed well against other elements of the proposed performance monitoring framework.

Potential areas of improvement with respect to the non-core criteria are identified in Table 5.



**Table 5 Summary of draft assessment - Unitywater**

<i>Criteria</i>	<i>Achieved?</i>
Core Criteria	
Absence of public interest or equity issues that may warrant regulatory review	Yes
Regulated services are clearly defined and separated from non-regulated services	Yes
No evidence of an exercise of market power and opening cost based is efficient	Yes
Absence of material changes in circumstances or major infrastructure costs	Yes
Demonstrated capacity to provide information accurately and on time	Yes – notwithstanding some issues in 2013-15 review in relation to the 1 July 2008 RAB roll forward
Other criteria	
Performance in customer engagement	Existing customer engagement practices are consistent with many desired features. Unitywater is well placed to build on these to achieve best practice.
Strategic approach to long term investment	Broadly addressing many desired elements. Areas of improvement have been identified including the capture and reporting of benefits due to a regional perspective and implementation of the Consolidated Asset Management System.
Service quality	Unitywater has committed to and is reporting on a limited number (6) of the QCA's 38 recommended measures.
Pricing principles	Insufficient information for full assessment. Prices generally based on legacy council pricing. This is considered a priority area for consideration in future performance monitoring.

Submissions on this assessment are due **30 June 2014**. All submissions will be taken into account in the QCA's Final Report, due 30 September 2014.

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