

**INDEPENDENT PRICING AND REGULATORY TRIBUNAL**

**REVIEW OF PRICES FOR WATERNSW**

**Tribunal Members  
Dr Peter Boxall AO, Chairman  
Ms Catherine Jones and Mr Ed Willett, Members**

**Members of the Secretariat  
Mr Hugo Harmstorf, CEO, Mr Matthew Edgerton, Mr John Madden  
and Ms Veronika Henkel**

**SMC Conference and Function Centre,  
66 Goulburn Street, Sydney NSW**

**Tuesday, 10 November 2015, at 9.15m**

.10/11/2015

1

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1 OPENING REMARKS

2  
3 THE CHAIRMAN: Good morning. Welcome to this public  
4 hearing. I would like to begin by acknowledging that we  
5 are meeting on the Gadigal land of the Eora people and wish  
6 to pay my respects to the traditional landowners both  
7 present and past.

8  
9 We are conducting a review to determine the maximum  
10 prices that WaterNSW can charge for bulk water services it  
11 provides to its customers in the Greater Sydney area from  
12 1 July 2016.

13  
14 I am Peter Boxall and I am Chair of the Independent  
15 Pricing and Regulatory Tribunal - IPART. I am joined today  
16 by my fellow tribunal members, Catherine Jones and  
17 Ed Willett. Assisting the tribunal today are IPART  
18 secretariat members, Hugo Harmstorf, who is IPART's CEO,  
19 Matthew Edgerton, John Madden and Veronika Henkel.

20  
21 I would like to thank those who have provided a written  
22 submission in response to our issues paper for this review.  
23 The main customer of WaterNSW Greater Sydney bulk water  
24 supply is Sydney Water, so its prices have a direct impact  
25 on water prices charged by Sydney Water. WaterNSW also  
26 supplies water to three local councils and 61 smaller  
27 unfiltered and raw water customers.

28  
29 Our issues paper set out the key issues that will be  
30 considered as part of the review. It also summarised  
31 WaterNSW's pricing proposal which was submitted to IPART  
32 from 30 June 2015 and set out our preliminary views on some  
33 of the pricing issues. WaterNSW's pricing proposal, our  
34 issues paper and submissions to our issues paper are  
35 available to the public on our website.

36  
37 This public hearing is an important part of our  
38 consultation process for this review. In addition to the  
39 views expressed in written submissions, we will consider  
40 the views you provide today in making our decisions on  
41 WaterNSW prices.

42  
43 Following this public hearing, we will release a draft  
44 determination and report for public comment in late March  
45 2016. People will then have about four weeks to make  
46 further written submissions for consideration by IPART  
47 before we make our final decisions on WaterNSW's prices for

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1 the Greater Sydney area.

2  
3 A final report and determination will be released  
4 in June 2016, which will contain the maximum prices to  
5 apply from 1 July 2016.

6  
7 In general terms, our price review will be seeking to  
8 determine what are WaterNSW's efficient costs of providing  
9 bulk water services and how should these costs be recovered  
10 through prices. We therefore seek your views on these  
11 questions.

12  
13 Before we commence proceedings today, I would like to  
14 say a few words about the process for this hearing. We  
15 will commence today with a presentation by WaterNSW of its  
16 pricing proposal. The hearing will then be divided into  
17 three sessions.

18  
19 The first session will consider WaterNSW's operating  
20 costs, capital costs and its approach to allocating shared  
21 costs between its Greater Sydney area customers and its  
22 rural customers.

23  
24 The second session will consider WaterNSW's prices to  
25 Sydney Water to its three council customers and to other  
26 smaller customers. It will also consider whether a  
27 cost-pass through mechanism should be introduced for  
28 Shoalhaven pumping costs and for bulk water purchases from  
29 the Fish River Water Supply Scheme.

30  
31 The third session will consider other issues  
32 associated with the price review, including the length of  
33 the determination period and whether we should include  
34 WaterNSW's proposed efficiency benefit sharing scheme and  
35 its raw water quality incentive scheme in our pricing  
36 determination. This third session is an opportunity for us  
37 to hear your views on any other issues you wish to raise  
38 that are relevant to this review of WaterNSW's prices for  
39 the Greater Sydney area.

40  
41 For each session, a member of the IPART secretariat  
42 will give a brief presentation on each topic. I will then  
43 invite participants at the table to provide comment on  
44 those topics. Following discussion by those around the  
45 table, I will then invite comments from the floor.

46  
47 Today's hearing will be recorded by our transcriber.

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1 Therefore, to assist the transcriber I ask that, on each  
2 occasion you speak, to identify yourself and, where  
3 applicable, your organisation.  
4  
5 A copy of the transcript will be made available on our  
6 website.  
7  
8 Immediately following this hearing, we will be holding  
9 a public hearing for IPART's review of Sydney Water prices  
10 to its customers which is scheduled to commence at 11.30am.  
11  
12 We commence today with a presentation by WaterNSW of  
13 its pricing proposal. Over to you Elli.  
14  
15 PRESENTATION BY WATERNSW  
16  
17 MS BAKER: My name is Elli Baker. I am the chief  
18 financial officer at WaterNSW. I will quickly introduce  
19 the other people from the organisation who are here with me  
20 today: David Harris, our CEO; Andrew George, executive  
21 manager for strategic engineering; and Ed Chan, senior  
22 manager for economics and business planning.  
23  
24 We have a brief presentation to start today and there  
25 are around six or seven slides in this presentation.  
26  
27 Our goal at WaterNSW is to provide a reliable supply  
28 of high quality water at the lowest possible price. Over  
29 the last particularly 10 or 11 months, we have been going  
30 through a significant period of change as a new  
31 organisation. We became WaterNSW on 1 January this year.  
32  
33 Part of that change has been to develop a three-year  
34 strategic action plan for the business, which will deliver  
35 the government's vision of an efficient customer focus and  
36 commercially minded bulk water utility. That really is the  
37 backbone behind what our organisation is resourced to  
38 deliver over the next three years.  
39  
40 We have designed on the back of that strategic action,  
41 and are currently implementing, a new and efficient  
42 integrated organisation structure. In addition to that, we  
43 have a significant number of new investment processes that  
44 are being developed to rigorously assess spending. The  
45 result of this has been, as per our submissions to IPART,  
46 lower proposed prices for customers in the Greater Sydney  
47 area.

1  
2 As I just mentioned, what we are striving to do is to  
3 deliver the most efficient services to customers. The  
4 significant reforms that we have undertaken have  
5 essentially stripped a significant amount of cost out of  
6 the organisation, while still delivering quality of water  
7 to customers.  
8  
9 This chart here just shows the pre-merger forecasts  
10 for our regulated opex, and that is across our entire  
11 regulated activities not just our Greater Sydney  
12 activities, before the merger of Sydney Catchment Authority  
13 and State Water Corporation and now as WaterNSW. The  
14 difference between the yellow bars and the blue bars just  
15 identifies the costs that we have stripped out, and  
16 essentially what that is is savings to customers in the  
17 form of lower prices.  
18  
19 I think it is very important when we bring multiple  
20 customer prices into one organisation that we ensure that  
21 there is no cross-subsidisation, and we are very aware of  
22 this for our customers. One of the things we did want to  
23 be very upfront with here today is just how we are ensuring  
24 that there is no cross-subsidisation.  
25  
26 We spent some time around about 12 months ago now  
27 really doing some analysis on the most simple and yet  
28 defensible methodology to ensure that we appropriately  
29 allocate costs to customers. We have essentially a  
30 three-step process for doing that. The first step is  
31 around capitalising some of the operational overhead, and  
32 that is to do with projects directly.  
33  
34 The second step then is around looking at analysis of  
35 data from the former separate financial systems of the two  
36 legacy organisations and having a look at what we define as  
37 within-the-region operational overhead, but it is really  
38 looking at overhead that is specific to delivery of  
39 services to specific customers and ensuring that that  
40 overhead is allocated to those customers that it is  
41 relevant to.  
42  
43 We then as a third step have the remaining corporate  
44 overhead, which tends to be operations like finance and IT  
45 and those sorts of very corporate-style overheads. We  
46 allocate those to the customers based on the proportion of  
47 the underlying direct opex and salaries and wages. So what

1 we are saying is that the overhead is there to support the  
2 delivery of those underlying activities and we are sharing  
3 the overhead or allocating the overhead to customers in  
4 that same proportion.  
5  
6 We then look at our submission for Greater Sydney and  
7 there are two slides here - one is on opex and one is on  
8 capex. This first slide on operating expenditure just  
9 shows you the decline in our proposed operating expenditure  
10 from the 2015-16 year, which is the current year, for  
11 Greater Sydney through the four years of the proposed  
12 pricing determination and illustrates the savings that we  
13 are delivering for customers.  
14  
15 There is a 5 per cent drop in real opex from the 2016  
16 year to the first year of the next determination and then  
17 by the end of the proposed determination pricing period, we  
18 are proposing to deliver 9 per cent in real dollar savings.  
19  
20 In order to achieve this, we have rigorously  
21 scrutinised our operating costs and, as mentioned before,  
22 developed a new organisational structure designed to most  
23 efficiently deliver services to customers.  
24  
25 In regards to capital expenditure - and as we go  
26 through this public hearing, we will talk in more detail  
27 about capital expenditure - this chart shows at a higher  
28 level the proposed capital expenditure.  
29  
30 Since the proposal that we have submitted and the  
31 conversations that we have been having with the independent  
32 efficiency review consultants, we have proposed to remove  
33 around about \$100 million of capex in that final year. This is  
34 really based on our view that there are state initiatives  
35 that are currently being looked at that we believe will  
36 yield a more efficient infrastructure solution than the  
37 proposed Shoalhaven one that was in our June submission.  
38  
39 On that basis, we have decided to propose removing  
40 around about \$100 million from that proposed capital  
41 expenditure profile on the view that customers should not  
42 be asked to fund that while there is remaining uncertainty  
43 and, in our view, some of the other initiatives being  
44 looked at will provide a more efficient solution for  
45 customers. So, on a risk assessment basis, we have decided  
46 to remove that amount of capex.  
47

1 This is the last slide that I have this morning to  
2 give you an overview of our submissions. This then shows  
3 the resulting prices from our proposal. Again, it  
4 highlights that we are striving to achieve the lowest  
5 possible costs to customers while still maintaining  
6 delivery of high quality water. In real dollars we are  
7 proposing a price decline across our customers.  
8  
9 THE CHAIRMAN: Thank you very much, Elli.  
10  
11 I will now call on Veronika from the secretariat to  
12 introduce the discussion on opex, capex and the approach to  
13 cost allocation.  
14  
15 SESSION 1: EXPENDITURE - OPERATING EXPENDITURE,  
16 CAPITAL EXPENDITURE, COST ALLOCATION  
17  
18 MS HENKEL: As Peter pointed out, we start with session  
19 one on operating expenditure followed by capital  
20 expenditure and cost allocation. Session 2 will be on  
21 price structures and prices followed by a session on other  
22 issues.  
23  
24 WaterNSW's initial proposal to IPART included  
25 \$405 million of operating expenditure for the next four  
26 years. This is about 0.2 per cent lower than the current  
27 determination period allowance. In the operating  
28 expenditure, this included \$3 million per year for  
29 Fish River Water Supply Scheme pumping and also  
30 \$2.1 million for Shoalhaven pumping.  
31  
32 WaterNSW later revised its proposal to IPART and  
33 included \$385 million of operating expenditure for the  
34 2016-2020 period. As Elli earlier pointed out, this is  
35 about 5 per cent less than the allowance for the current  
36 determination period and it is driven by the implementation  
37 of the new integrated organisational structure.  
38  
39 Similarly as before, this graph demonstrates the  
40 allowance versus actuals for the past four years and, going  
41 forward, the forecasts. The red line indicates the revised  
42 forecast, which shows the decline in opex over the period.  
43  
44 Looking at the past operating expenditure, in its  
45 proposal, WaterNSW stated that the key drivers of this  
46 underspend was due to no need to pump from the Shoalhaven.  
47 There were some savings in energy costs related to routine

1 pumping. There was a repeal of the carbon tax and there  
2 were lower purchases from the Fish River water scheme and  
3 also some savings in insurance premiums.  
4  
5 Some of these operating savings were partially offset  
6 by higher costs relating to managing incidents and also the  
7 Warragamba Dam risk and reliability investigation. The net  
8 outcome was a total of about \$10 million of underspend  
9 across the four years.  
10  
11 Looking at the forecast, as I mentioned, in its  
12 initial pricing proposal, WaterNSW included about  
13 \$13 million of efficiency savings over the four-year  
14 period. In its revised operating expenditure forecasts,  
15 WaterNSW is proposing an additional \$25 million of  
16 efficiency savings over the next determination period.  
17  
18 Moving on to capital expenditure, again, in the  
19 initial proposal received by IPART, WaterNSW included  
20 \$375 million of capital expenditure over the next four  
21 years. This is about three times the allowance for the  
22 current determination period and included about  
23 \$103 million in the final year for the Shoalhaven transfer  
24 project. Other key projects would be the Upper Canal  
25 refurbishment and the catchment asset renewals.  
26  
27 In its proposal WaterNSW noted that there is an  
28 uncertainty about the outcomes of the Metropolitan Water  
29 Plan and the Hawkesbury-Nepean Valley Flood Management  
30 Review and has based its submission on the Metropolitan  
31 Water Plan 2010 modified with updated information on water  
32 demand.  
33  
34 Again, the graph demonstrates the past capital  
35 expenditure looking forward. Over the 2012 determination  
36 period, WaterNSW, or the former SCA, underspent by about  
37 \$22 million, which is about 16 per cent of the allowance,  
38 and it was largely due to the deferral of the Warragamba  
39 environmental flows construction.  
40  
41 Looking forward, in its initial proposal, we can see  
42 that 2019-20 year with a large increase for Shoalhaven. As  
43 Elli pointed out in her presentation, that is no longer  
44 part of the proposal. In their submission WaterNSW  
45 attributes the spending in the early years of the next  
46 determination period to works focusing on asset reliability  
47 and asset renewal.

1  
2 Moving to cost allocation, as Elli outlined in her  
3 initial presentation, in their proposal the operating cost  
4 between the Greater Sydney area, which is the former Sydney  
5 Catchment Authority, and the rural customers, which is the  
6 former State Water, are apportioned by distinct categories:  
7 Direct costs, overheads, and corporate-wide overheads.  
8 Also the corporate-wide capital costs are based on the  
9 proportional value of each regulatory asset base. In this  
10 case 67 per cent of those costs are allocated to the  
11 Greater Sydney area.  
12  
13 The questions we have for today are:  
14  
15 Is Water NSW's proposed opex prudent and efficient?  
16 Are opex savings from the merger sufficient?  
17 Are the proposed efficiency gains sustainable.  
18 In regard to opex was WaterNSW's capex for 2012-16 and  
19 its proposed capex for 2016-2020 prudent and efficient?  
20 Do you agree with WaterNSW's assessment of the  
21 need for augmentation of water supply; and  
22 Is WaterNSW's proposed approach to allocating shared  
23 expenses between Greater Sydney customers and its rural  
24 customers reasonable?  
25  
26 THE CHAIRMAN: Thank you very much, Veronika. Now, I  
27 will just call for contributions from around the table on these  
28 issues. Would anybody like to start? Kris? Eric?  
29  
30 MR FUNSTON: Kris Funston from Sydney Water. I think that  
31 our big concern when we originally saw the proposal was  
32 probably around the issues of cost allocation and ensuring  
33 that those costs were allocated efficiently. You have a  
34 merger of two entities and two organisations, so it was  
35 making sure that you don't have that cross-subsidisation  
36 between what is effectively the rural bulk water operations  
37 and the urban water operations.  
38  
39 We see the approach that has been put forward as  
40 reasonably pragmatic in looking at this in terms of the  
41 regulatory asset base across each of the utilities. The  
42 issue here is we would need to obviously explore that in  
43 more detail to see whether or not that is appropriate in  
44 terms of the detail, but we see it as sort of a reasonable  
45 way, in the first instance, of looking at how these costs  
46 are allocated.  
47

1 The question for us was also these realised  
2 efficiencies and the extent you are removing corporate  
3 overheads and just getting that understanding and  
4 visibility around what are the corporate overhead savings  
5 that are occurring, because we do understand there is a lot  
6 of restructuring actually going on within the organisation  
7 and just understanding exactly where are those cost savings  
8 being achieved. That is something we would probably be  
9 interested in receiving some more detail on and getting a  
10 greater appreciation of.

11  
12 THE CHAIRMAN: Sure thank you, Kris. How about DPI  
13 Water? Cathy?

14  
15 MS COLE: Cathy Cole from DPI Water. I would say that we  
16 do agree with WaterNSW's revised assessment on the capex,  
17 noting Elli's presentation about pulling back on the  
18 \$100 million roughly for the Shoalhaven transfers pending,  
19 I guess, further information and an understanding of the  
20 timing and needs for water supply augmentation and  
21 environmental flows which are impacted by other government  
22 review processes.

23  
24 The Hawkesbury-Nepean flood management review and the  
25 metro water plan are closely interlinked. They are not  
26 ideally aligned with the IPART price review, but we will  
27 continue to provide the best advice that we can as things  
28 go along. So, yes, I was pleased to see that change.

29  
30 THE CHAIRMAN: Thank you, Cathy. For WaterNSW, what  
31 sort of comfort can you give us that these savings are  
32 sustainable and, in a sense, some of the points that Kris  
33 raised about the overheads and things like that?

34  
35 MR HARRIS: David Harris, WaterNSW. Peter, as Elli  
36 outlined in her presentation, we have spent almost the  
37 entirety of this calendar year taking a step back looking  
38 at our legislative objectives. We have developed a very  
39 comprehensive three-year strategic action plan where we  
40 have allocated targets - three-year targets - together with  
41 rolling one-year actions to support achievement of those  
42 targets. We have taken that work and then we flowed that  
43 through and created a new organisational structure that is  
44 aligned to delivering on those.

45  
46 I think too in her presentation, Elli pointed out the  
47 much more rigorous processes that we have also put in place

1 around our opex and capex spend. By way of example, those  
2 processes require all opex and capex of over \$200,000 to be  
3 reviewed by two executive-level committees and, where  
4 required, then going up to the board, which was not in  
5 place before. They are both investment review type and  
6 executive level oversight together with project  
7 implementation risk type oversight from a second executive  
8 committee.

9  
10 We are very confident about this. With the rigour in  
11 which we have set out our strategic action plan, the way we  
12 have then aligned our specific organisational structure to  
13 those specific deliverables together with the processes we  
14 have put in place - together, I might say, with the talent  
15 that we have internally in terms of our people in  
16 leadership positions within the company - we are very  
17 confident that we will achieve what we have set out to do  
18 over that three-year time frame.

19  
20 THE CHAIRMAN: Thank you very much, David. Are there  
21 any questions or comments from the floor? No? Is there  
22 anything else around the table? Eric

23  
24 MR DE ROOY: Yes, if I may. Eric De Rooy from Sydney  
25 Water. We are encouraged to see the approach taken by  
26 WaterNSW in looking at the outcomes for our customers. We  
27 encourage the two organisations to continue to work in a  
28 way that we interact to optimise the outcomes for our  
29 customers. We will continue to work at the operational  
30 level to achieve that and to have the lowest possible price  
31 pass-through to our customers.

32  
33 Also with that, we will continue to work with WaterNSW  
34 to ensure that the appropriate skills are available through  
35 the value chain to manage the risks on behalf of our  
36 customers. With every reform and restructure, there are  
37 risks and opportunities and we will continue to work with  
38 WaterNSW to manage those so that together we can provide  
39 assurances to our customers that their water is safe to  
40 drink.

41  
42 THE CHAIRMAN: Thank you very much, Eric.

43  
44 In that case we might move on to session 2 and I will  
45 call on Veronika again. This session is on price  
46 structures, prices and cost pass-through mechanisms.

1 SESSION 2: PRICE STRUCTURES, PRICES AND COST-PASS  
2 THROUGH MECHANISMS

3  
4 MS HENKEL: Starting with price structures and prices,  
5 under the proposal, WaterNSW is proposing price structure  
6 for Sydney Water as follows today: they are intending to  
7 maintain the current fixed to volumetric charge ratio of  
8 80:20 and they are proposing to incorporate a mechanism to  
9 allow adjustment of the volumetric charge to reflect the  
10 Sydney desalination plant mode of operation.

11  
12 With the price structures for the raw and unfiltered  
13 water customers, the proposal is to maintain the current  
14 price structure and price level so the cost of water to  
15 customers is similar to that of the retail network.

16  
17 Our preliminary view in the issues paper is to accept  
18 WaterNSW's proposal. Just as a way of background in the  
19 2012 determination, we introduced the SDP schedule in  
20 recognition of the revenue destabilisation that the SDP  
21 operation would inflict on the SCA.

22  
23 This is just a summary of the proposed charges. These  
24 charges are based on the initial proposal made by WaterNSW.  
25 As you can see, there is a decline in price from the  
26 current level for Sydney Water and the prices are kept  
27 constant for the unfiltered water and raw water customers.

28  
29 In regards to prices to councils, as we mentioned  
30 earlier, WaterNSW provides bulk water to three local  
31 councils. The total revenue requirement from the three  
32 councils is based on the estimated cost of the bulk water  
33 supply network to service these customers. The costs are  
34 then allocated to each council based on their respective  
35 demand forecasts.

36  
37 The proposal from WaterNSW is to change the current  
38 price structure from 25 per cent fixed and 75 per cent  
39 volumetric to 80 fixed and 20 volumetric. This would align  
40 the structure of these prices to those of Sydney Water.

41  
42 This is a summary of the proposed charges on that  
43 slide. As you can see, in the year 2016-17 and onwards,  
44 the fixed component for each of the councils increases. It  
45 is worth noting that for Goulburn there is a reduction;  
46 however, that is driven by the reduced demand.

47

1 In regards to the cost pass-through mechanism, in its  
2 initial proposal to IPART, WaterNSW proposed to include all  
3 non-core expenditure in its operating expenditure. This  
4 included, as we mentioned earlier, the \$2.1 million per  
5 annum for Shoalhaven pumping and also \$3 million per year  
6 for pumping and the purchase of bulk water from the Fish  
7 River Water Supply Scheme.

8  
9 In our issues paper our position was that we remain  
10 interested in pricing approaches that better reflect  
11 scarcity value of dam water. In this context, we are  
12 proposing to introduce a cost pass-through mechanism for  
13 the Shoalhaven and also for the Fish River.

14  
15 In its submission to our issues paper, WaterNSW  
16 supported our introduction of a cost pass-through mechanism  
17 for Shoalhaven pumping; however, WaterNSW did not support  
18 introducing the cost pass-through mechanism for the Fish  
19 River water supply. The rationale there is because these  
20 purchases are relatively small and incur relatively high  
21 transaction costs compared with the amount being  
22 reimbursed.

23  
24 The questions for today are:

25  
26 Is WaterNSW's proposed structure of bulk water prices  
27 to the councils - 80 per cent fixed and 20 per cent  
28 volumetric - reasonable?

29 Is WaterNSW's proposed allocation of the costs to each  
30 of the councils aligned with its costs of servicing these  
31 customers?

32 Should the volumetric price include a cost  
33 pass-through mechanism for Shoalhaven pumping costs?

34 Similarly should the volumetric price include a cost  
35 pass-through mechanism for the Fish River scheme?  
36 Should the cost pass-through mechanism(s) apply to council  
37 customers?

38  
39 THE CHAIRMAN: Thank you, Veronika. Are there any  
40 contributions on pricing from around the table? Sydney  
41 Water? DPI?

42  
43 MS COLE: As a general principle, DPI Water supports  
44 mechanisms for drought response measures and the cost  
45 pass-through of elements that are triggering by a  
46 particular event, and there are criteria that IPART has  
47 identified in its issues paper for cost pass-through

1 mechanisms. Broadly we do support that in terms of passing  
2 on that water scarcity and conservation signal to the  
3 customers.

4  
5 THE CHAIRMAN: I was just wondering what happens in the  
6 case of the councils where there is a proposed change to  
7 80 per cent fixed to 20 per cent volumetric, which would  
8 align them with the price of Sydney Water. I understand  
9 there is some government regulation, which I suspect  
10 emanates from your area, that councils, when they charge  
11 their customers, can only charge 25 per cent fixed and  
12 75 per cent volumetric or something like that. Is that the  
13 case?

14  
15 MS COLE: I would have to take that on notice, Peter. I'm  
16 not sure off the top of my head.

17  
18 THE CHAIRMAN: Okay, thanks. So, Chris? Eric?

19  
20 MR FUNSTON: We might come in on the cost pass-through  
21 issue. I think we have raised this on our issues paper, so  
22 our view is on the record. We looked at the Shoalhaven  
23 pumping costs and said that, in principle, we agree that  
24 the preference would be that this is done through a cost  
25 plus, so we have proposed a similar cost pass-through  
26 mechanism for SDP costs.

27  
28 I think what happened was when we actually came to  
29 look at the magnitude of those costs, it was a relatively  
30 low cost estimate and we looked at what the price signal  
31 would be in terms of the increased usage pricing and  
32 estimated it to be around 2 cents. I think that led us to  
33 question the value of that price signal to customers given  
34 the potentially administrative complexity around doing that  
35 pricing adjustment across our customer base. That was  
36 really our query.

37  
38 We have said in principle what we actually support is  
39 a symmetry of approach in terms that whatever approach is  
40 taken in relation to WaterNSW is also actually the approach  
41 that is also taken to Sydney Water. So if you do get this  
42 Shoalhaven transfer cost based on some sort of property  
43 listing sort of estimate of it being on and off, then we  
44 will obviously accept that and we will pass that through in  
45 our costs.

46  
47 Similarly if you have this as a cost pass-through, we

1 will put this as a cost pass-through. But when we looked  
2 at it, we did question whether or not this was really  
3 providing the value of the price signal - the appropriate  
4 price signal to customers

5  
6 THE CHAIRMAN: Thank you, Kris. WaterNSW, would you  
7 like to make any comments at this stage?

8  
9 MS BAKER: I think that from our perspective, Shoalhaven  
10 pumping is not immaterial necessarily in terms of the bill  
11 that we charge to Sydney Water, but it is then immaterial  
12 with Sydney Water billing that on to their customers.

13  
14 I believe that we had more concerns with Fish River,  
15 namely, that the administration of trying to pass through  
16 the small cost of Fish River would outweigh the benefit.  
17 So definitely for the Fish River, we didn't support cost  
18 pass-through.

19  
20 THE CHAIRMAN: Thanks, Elli. Any comments from the  
21 floor at this stage? There is someone down the back?

22  
23 MS KROGH: I am Carmel Krogh and I am the director of  
24 Shoalhaven Water. I would like, on behalf of Cathy, to add  
25 to the reply to your question regarding the 75 per cent.

26  
27 DPI Water, previously the Office of Water, have what  
28 is known as best practice guidelines. Councils are  
29 required to meet those best practice guidelines for their  
30 pricing. Those guidelines include the fact that the  
31 councils should receive 25 per cent of their residential  
32 income from the fixed charges. That's where the difference  
33 is.

34  
35 THE CHAIRMAN: Thank you very much, Carmel. Yes, Matt?

36  
37 MR EDGERTON: Elli, could I follow on on the points you  
38 made. You suggested that the administrative costs of a  
39 pass-through mechanism for the Fish River scheme is an  
40 argument against a cost pass-through mechanism in that  
41 instance. I note that you are forecasting Fish River costs  
42 of about \$3 million and Shoalhaven pumping costs at about  
43 \$2 million. Could you tell us a little bit more about why  
44 not a pass-through mechanism for the Fish River scheme, why  
45 the additional administrative complexity associated with  
46 those costs?



1 MS BAKER: I would need to go back to that, but I think a  
2 substantial amount of that Fish River cost that you are  
3 talking about is infrastructure charge not the pumping.  
4 I don't think it is the pumping cost - that is the  
5 \$3 million. I would need to go back and have a closer look  
6 at numbers, but the proposed pass-through of the pumping is  
7 a much smaller amount. I would need to go back and check  
8 the exact number.

9  
10 MR McINNES: Excuse me, I can answer that question.

11  
12 THE CHAIRMAN: Sorry, could you please identify yourself.

13  
14 MR McINNES: Rod McInnes, WaterNSW. I am an economist  
15 there. The \$2 million cost that you are referring to,  
16 Matt, is on an insurance basis, actuarial basis. The  
17 actual cost that would be incurred could be as much as  
18 \$20 million and it would be incurred quite rarely, so the  
19 pass-through would be quite substantial and it would have  
20 a price effect if passed through to Sydney Water customers.

21  
22 With the \$3 million, there is not much response to  
23 scarcity. There is not a change there that would create a  
24 demand response according to principles that you are  
25 espousing of getting a price response, a demand response  
26 from customers. With regard to administrative cost,  
27 I think, as Kris referred to, there is a lot of work in  
28 getting that out to the individual customers.

29  
30 MR EDGERTON: Thank you, Rod. Could I ask as well then:  
31 in IPART's issues paper we have expressed an interest in a  
32 pass-through for the Shoalhaven pumping costs because it  
33 does reflect the relevant scarcity of water in times of  
34 drought. Could you tell us a bit about whether pumping  
35 from the Fish River scheme is used in a similar way? Is it  
36 in response to water scarcity or is it also used for other  
37 operational reasons?

38  
39 MR CHAN: Ed Chan from WaterNSW. Following on what Rod  
40 was saying, the principal difference between the Shoalhaven  
41 pumping and the Fish River is the way it is used.  
42 Shoalhaven pumping, as Rod said, is very much about drought  
43 response whereas the Fish River water scheme and the way  
44 we use the water is very much tied in with the operation of  
45 the system in the Blue Mountains area.

46  
47 Depending on the water operations in the dams

1 up there, it is an operation that occurs on a very regular  
2 basis regardless of the season. So, yes, during drought  
3 periods we may actually draw more water from the Fish River  
4 Water Supply Scheme, but there is no set supply rules where  
5 we have to operate when the dam gets to 75 per cent level.

6  
7 From that regard, WaterNSW, at some point in time,  
8 might only have to pass through a very small amount for  
9 Fish River and that is really depending on the operating  
10 system, balancing storages and ensuring that the Blue  
11 Mountains system has the same reliability level of supply  
12 compared with the rest of the network. That's why we say,  
13 on balance, it is actually a more costly administrative way  
14 to pass through Fish River costs compared with Shoalhaven  
15 where, if we moved to a cost pass-through mechanism,  
16 certainly a significant amount would be passed through and  
17 would show an impact to Sydney Water.

18  
19 THE CHAIRMAN: I think an implication in what you are  
20 saying is that Shoalhaven is used as a drought response and  
21 the Fish River is not basically.

22  
23 MR CHAN: Correct.

24  
25 MS BAKER: Yes.

26  
27 THE CHAIRMAN: And Fish River is just part of your  
28 ongoing operations?

29  
30 MS BAKER: That's right.

31  
32 MR CHAN: Correct.

33  
34 MS BAKER: For us to calculate the incremental amount to  
35 have in a pass-through is quite administratively difficult.

36  
37 MR HARRIS: It's a mode of operation.

38  
39 MR CHAN: Historically the Sydney Catchment Authority  
40 showed that as a separate cost because we are a bulk water  
41 supplier supplying water to the end customer, so the  
42 question was why are we purchasing water as a bulk water  
43 supply? There was really just a way of expressing that we  
44 do have to purchase water from systems outside of us. It  
45 is a clear way of showing where our costs are in terms of  
46 servicing that system.

1 THE CHAIRMAN: Thank you very much, Ed. Matt?  
2  
3 MR EDGERTON: Just another question then to WaterNSW.  
4 You have supported a cost pass-through mechanism for the  
5 Shoalhaven scheme presumably on the basis that that would  
6 be added to your usage price to Sydney Water. Should that  
7 pass-through also be reflected in the usage price to your  
8 three council customers?  
9  
10 MR CHAN: No. The way we calculate council prices is  
11 based on their usage share of the system. So in  
12 calculating the prices, we have already allocated the cost  
13 of the system. Again from an administrative perspective,  
14 the councils' share of our operating costs are relatively  
15 low, even when we are pumping. To calculate that cost  
16 through to the councils, I think is again administratively  
17 higher than what it would be for the councils.  
18  
19 Also the drought pumping is primarily for servicing  
20 the needs for Sydney customers and --  
21  
22 THE CHAIRMAN: But the drought pumping would be also  
23 for servicing your other customers.  
24  
25 MR CHAN: Primarily, it's for --  
26  
27 THE CHAIRMAN: Yes, because Sydney is your biggest  
28 customer. Is this because the councils are relatively  
29 small customers --  
30  
31 MR CHAN: They are. They are and --  
32  
33 THE CHAIRMAN: -- therefore a percentage of any Shoalhaven  
34 pumping costs would also be very small?  
35  
36 MR CHAN: With our revenue requirement, as a proportion  
37 the councils only make up about \$1.4 million versus the  
38 200-odd for Sydney Water, so the proportions are relatively  
39 small. Economically there are benefits for council  
40 customers in the assets there. We have already priced that  
41 in our asset price - in our normal prices to the councils.  
42  
43 MR EDGERTON: Just on the prices to the councils, you are  
44 proposing quite a significant change in their price  
45 structure. I note there might be some council stakeholders  
46 here, but can you tell us what consultation you had with  
47 the council customers and is there anything you can tell us

1 about their views on those price structures?  
2  
3 MR CHAN: We had consulted with all three of the major  
4 councils before we put our submission into IPART in June.  
5 In general they are supportive of the move - or should  
6 I say they are not against it. They do recognise that it  
7 is a big jump from 25 per cent to 80 per cent.  
8  
9 As a way of history, prior to the current  
10 determination period, the SCA charged a fully variable  
11 charge to council customers. The conversation we started  
12 with the councils then is recognising the fixed cost nature  
13 of the Greater Sydney business and we actually commenced  
14 moving the tariff structure towards a higher fixed charge.  
15 In the 2012-16 determination we started with a 25:75 and  
16 for this period we are proposing that it align with Sydney  
17 Water.  
18  
19 Again the rationale for moving to a higher fixed  
20 charge is because of the reliability of service we provide  
21 to the councils and also the fixed cost nature of our  
22 assets. So in pricing the councils, the majority of the  
23 cost is on the Shoalhaven system side, which is largely  
24 fixed costs, and the operating costs side of it is  
25 relatively small. We would like as much as possible to  
26 reflect the fixed cost nature of the business in those  
27 prices.  
28  
29 MS BAKER: I think it is worth saying in addition that the  
30 analysis showed that we would have received less revenue  
31 from customers had we had the fixed 80:20 over this current  
32 four year period.  
33  
34 MR WILLETT: Could I go back to the question of Shoalhaven  
35 pumping. Did I hear correctly that there is an inclusion  
36 of \$2 million on a probabilistic or insurance basis and  
37 then there is a possibility of a pass-through according to  
38 demand need of up to \$20 million. Isn't there some  
39 doubling accounting there?  
40  
41 MR CHAN: The arrangement under the current determination  
42 is that the Shoalhaven cost borne by the SCA is calculated  
43 on a probability basis, so that under the current  
44 arrangement, WaterNSW, or the Greater Sydney portion,  
45 receives roughly about \$2 million a year as an insurance  
46 premium. Should we have to pump, yes, 20 or \$30 million,  
47 WaterNSW at the moment would not get additional cost

1 pass-through for that.  
2  
3 MR WILLETT: They won't?  
4  
5 MR CHAN: No. So what is being proposed is moving away  
6 from that insurance scheme where there is no cost  
7 allowance but when we do pump, it becomes a cost  
8 pass-through and whatever we incur we will pass on.  
9  
10 MR WILLETT: So you are moving from an insurance basis to  
11 a pass-through basis?  
12  
13 MR CHAN: Correct, yes.  
14  
15 MR WILLETT: Thank you.  
16  
17 THE CHAIRMAN: Are there any other comments from the  
18 floor? Yes, Carmel?  
19  
20 MS KROGH: I can't speak on behalf of my other council  
21 counterparts. However, on the change from the variable to  
22 the fixed, as Elli said, in the quantum of it for the  
23 councils, and I think it is for each of the councils, the  
24 actual dollar value is reduced over that price path anyway.  
25 So, in essence, we have no issue with the change from the  
26 fixed and variable percentage.  
27  
28 THE CHAIRMAN: Thank you, very much, Carmel. Is there  
29 anybody else? Are there any other comments? Thank you.  
30  
31 Let's move on to session 3, which is to hear views on  
32 any other issues. We have identified a number of issues.  
33 One issue is the length of time that new prices should  
34 apply - that is, the length of the determination - whether  
35 we should include an efficiency benefit sharing scheme and  
36 also a raw water quality incentive scheme in the pricing;  
37 and what values to adopt for projected water sales and  
38 customer numbers. I will ask Veronika to introduce this  
39 session.  
40  
41 SESSION 3: OTHER ISSUES  
42  
43 MS HENKEL: Thank you, Peter. The last session is on  
44 other issues, as Peter outlined, starting with the length  
45 of the determination period.  
46  
47 Under WaterNSW's proposal, it is a four-year

1 determination period starting from 1 July 2016 and ending  
2 30 June 2020. WaterNSW believes that it provides a balance  
3 between a stable and certain operating environment while  
4 allowing sufficient flexibility to respond to changes in  
5 the water industry. It is their proposal to remain aligned  
6 with Sydney Water's determination.  
7  
8 Our preliminary position in the issues paper is to  
9 accept the proposal.  
10  
11 I turn next to form of regulation. In their proposal,  
12 WaterNSW outlined the efficiency benefit sharing scheme  
13 for operating expenditure. This would allow WaterNSW to  
14 hold efficiency savings or losses for a fixed number of  
15 years regardless of when the savings or losses are  
16 achieved.  
17  
18 Our position in the issues paper is that our decision  
19 will be informed by our Sydney Water review and that we  
20 will then consider potential benefits relative to risks and  
21 costs when we apply to it to WaterNSW. There will be a  
22 session on the efficiency benefit sharing scheme in the  
23 Sydney Water public hearing following this.  
24  
25 Next is the proposal to include the raw water quality  
26 incentive payment scheme. It is currently contained in the  
27 raw water supply agreement between WaterNSW and Sydney  
28 Water. Under the scheme, WaterNSW can receive a payment  
29 of up to \$1 million per annum from Sydney Water, if it  
30 supplies water that is better than the rolling five-year  
31 average of specified water quality indicators.  
32  
33 In our issues paper, our preliminary position was that  
34 we support the rationale and that we will investigate its  
35 application in our determination.  
36  
37 Moving on to water sales and customer numbers, as we  
38 pointed out, WaterNSW's customer base is made up of  
39 Sydney Water, three local councils and 61 smaller retail  
40 customers. WaterNSW has adopted Sydney Water's forecast  
41 water sales to its end-use customers and it has consulted  
42 with the council customers on water sales.  
43  
44 Again our preliminary position in the issues paper is  
45 to accept WaterNSW's proposal; however, we will be informed  
46 through our decision in the Sydney Water review on sales  
47 for Sydney Water.

1  
2 The general questions we have to end the session are:  
3  
4 What are your views on:  
5 The length of the determination;  
6 The efficiency benefit sharing scheme for  
7 WaterNSW;  
8 The raw water quality incentive payment scheme;  
9 Water NSW's forecast water sales.  
10  
11 This concludes my presentation, thank you.  
12  
13 THE CHAIRMAN: Thank you very much, Veronika. Are  
14 there any comments from the table? Sydney Water?  
15  
16 MR DE ROOY: I want to address the incentive payment  
17 scheme - the raw water quality incentive payment scheme.  
18 In principle, we support the idea or the principle of an  
19 incentive scheme. What we would like to do is work through  
20 with the joint review on how that may work under the raw  
21 water supply agreement as part of the determination  
22 process.  
23  
24 Given the recent changes with WaterNSW from the SCA  
25 and also the water filtration contractors with whom we have  
26 just renegotiated their contracts or rather extensions, a  
27 joint review could consider those changes and give us a  
28 better assessment of the risks, the treatment capability  
29 and costs borne by all parties.  
30  
31 We note in our submission that follows in the next  
32 session that we have not included any incentive payment  
33 costs in our proposal because we are of the opinion that it  
34 needed to be offset by equivalent savings.  
35  
36 THE CHAIRMAN: Thank you, Eric. Kris?  
37  
38 MR FUNSTON: I might comment on the efficiency benefit  
39 sharing scheme. I think we will discuss this when we deal  
40 with Sydney Water's proposal. We are supportive of  
41 incentive mechanisms. More broadly, anything that  
42 encourages businesses to lower their costs we think is  
43 important.  
44  
45 In this issue I think the question is about ensuring  
46 that that opex level is baselined appropriately.  
47 Especially given the changes and the cost allocation that

1 is having to be done between the two entities, it is about  
2 ensuring that that is actually set at the right level. We  
3 would be keen to ensure that that cost has actually been  
4 set at the right level before this sort of scheme is put in  
5 place.  
6  
7 If there is confidence that that cost has been set at  
8 the right level and these costs are being appropriately  
9 apportioned, then we don't see any issue with what is being  
10 proposed and we look at it as a scheme that will actually  
11 incentivise WaterNSW to lower its costs.  
12  
13 THE CHAIRMAN: Thank you very much, Kris. Cathy?  
14  
15 MS COLE: Nothing to add to those issues, thanks.  
16  
17 THE CHAIRMAN: Thank you. Are there any comments or  
18 questions from the floor?  
19  
20 WaterNSW would you like to respond to any of those  
21 comments or add anything?  
22  
23 MR HARRIS: No, I don't think so. We agree with  
24 Sydney Water. As a matter of principle we see that raw  
25 water quality incentive scheme as a good thing and we are  
26 happy to work through with our customer in terms of  
27 reviewing risk and so on.  
28  
29 MS JONES: Based on what you have just said there David  
30 and Sydney Water's comments on that scheme, is it realistic  
31 that it would happen in the next four years? If you are  
32 thinking of putting it in the proposal, is it to happen at  
33 a certain time or would you like it to happen sometime in  
34 the next four years?  
35  
36 MR HARRIS: We would like it to happen in this coming  
37 determination period. Noting Eric's comments, by the way,  
38 about changes since the provision was drafted, the  
39 provision is there in the agreement and we were  
40 recommending that effectively that provision be turned on,  
41 but there may need to be discussion around that provision  
42 in light of subsequent events at Sydney Water's end, and  
43 that is fine, but we would like that to be in effect during  
44 the determination.  
45  
46 MS JONES: Thank you.  
47

1 THE CHAIRMAN: Thank you, Catherine. Matt?  
2  
3 MR EDGERTON: We will obviously talk about Sydney Water's  
4 proposed efficiency benefit sharing scheme in a little bit  
5 more detail in the hearing that follows this one, but I was  
6 wondering if WaterNSW could just provide us with a  
7 high-level argument as to why you are proposing this scheme  
8 and why you think it is necessary.  
9  
10 MS BAKER: I think broadly we have the same view as Kris.  
11 I think a scheme which incentivises a business to be as  
12 efficient as possible is good for customers. That is  
13 really broadly why we are proposing the scheme. Are you  
14 after more --  
15  
16 MR CHAN: If I may add to that, our proposal for the  
17 efficiency benefit sharing scheme as an incentive mechanism  
18 allows us as a business to actually make continuous  
19 improvement rather than be, I suppose, confined within a  
20 determination period where every four years we come to the  
21 tribunal with savings that go forward on the next four  
22 years.  
23  
24 We believe as a business that it is actually good  
25 discipline for us to continually seek savings as the  
26 determination periods go, but as part of doing that, some  
27 of that benefit should be shared with the business. Our  
28 proposal, similar to Sydney Water based on what we put  
29 forward, is 25 per cent to the business and 75 per cent  
30 share to the customer.  
31  
32 In our view, that is a good mechanism to insure that  
33 customers continue to get the benefits from the business  
34 and it is a continuation, not something that happens once  
35 every four years. That is very much how the business is  
36 being structured to move forward. It is about continuous  
37 improvement and continuous efficiency gains rather than  
38 sort of on a period-by-period basis.  
39  
40 THE CHAIRMAN: John?  
41  
42 MR MADDEN: I have a question that is back to the  
43 incentive scheme, the quality incentive scheme, and the  
44 baselining, which I think is an important point. In your  
45 proposal on operating expenses, does that include the  
46 activities that are a part of that scheme, or if the scheme  
47 didn't go ahead, do those activities have to be taken off?

1 There is \$1 million up for grabs. Do you know the cost of  
2 your activities with or without the scheme?  
3  
4 THE CHAIRMAN: Is this the EBSS?  
5  
6 MR MADDEN: No, the quality incentive scheme.  
7  
8 MR HARRIS: I think the concept here, and Eric in fact  
9 referred to it in his comment around treatment plant costs,  
10 is that in providing a particular quality of water to  
11 end-use customers that are, broadly, catchment bulk water  
12 costs, relevantly, and treatment costs, there can be a  
13 trade-off. As Eric was referring to, there can be a  
14 trade-off in terms of the quality of the water that we  
15 provide which can obviously reduce the treatment costs at  
16 any given point in time for Sydney Water or vice versa.  
17 I think we see this as a mechanism for economically  
18 incentivising both parties to come to an optimal outcome in  
19 that regard.  
20  
21 THE CHAIRMAN: I think I have a similar question. Let's  
22 say you are able to deliver water which is of a superior  
23 quality and you receive the \$1 million from Sydney Water.  
24 For them I agree that if the water is a better quality,  
25 they will be able to spend less on treatment so, in a  
26 sense, that will wash through. In the case of WaterNSW, do  
27 you anticipate you will have to undertake additional  
28 expenditure to produce that better quality water and get  
29 the \$1 million, or is this \$1 million that goes to your  
30 bottom line?  
31  
32 MS BAKER: I am not sure we can --  
33  
34 MR MADDEN: I think it's a bit more to the point because  
35 it's what the incentive is to you.  
36  
37 MR HARRIS: I would characterise this more from our  
38 perspective as a risk measure. In other words, and I'm  
39 using very broad terms here --  
40  
41 THE CHAIRMAN: Yes, sure.  
42  
43 MR HARRIS: -- we have the ability on a day-by-day basis  
44 to deliver water of varying qualities to Sydney Water  
45 and that is the operational cooperative arrangement that  
46 Eric referred to earlier. However, query whether, over the  
47 long run, for us to continuously deliver the best quality

1 water is actually then leaving us with a risk in terms of  
2 quality of supply over the long term.  
3  
4 I think what we are saying there is that should be  
5 driven at any point in time - that is the quality of the  
6 water. Of course, we are talking about above baseline  
7 here, let's be very clear about that; we are not talking  
8 about below but anywhere above baseline. I think that we  
9 probably need to have greater incentive and greater regard  
10 to look at our long-run risks around just constantly  
11 pumping out the best quality above baseline water and where  
12 is that leaving us in the long run? Currently there is no  
13 financial incentive around that decision.

14  
15 THE CHAIRMAN: This agreement between Sydney Water  
16 and the then SCA was struck after the beginning of the last  
17 determination, which was a bit unfortunate in terms of  
18 timing. Therefore, we were not able to have this  
19 discussion before the last determination. It is very good  
20 to have this discussion now before this determination so  
21 that we can take it into account and make a decision about  
22 if and how it would be put in the determination of both  
23 WaterNSW and Sydney Water, so I think it is a very  
24 constructive suggestion.

25  
26 John, do you have anything else?

27  
28 MR MADDEN: This is probably related in a way to catchment  
29 activities. The submission on the revised opex was fairly  
30 high level, even today with the presentation. I wonder if  
31 you could take this opportunity to go through some of the  
32 key drivers of the 9 per cent reduction in opex under the  
33 revised proposal - so, I guess, what's driving it and what  
34 is the build-up of that? Are there activities in  
35 catchment? Is it operations? Is it head office? It would  
36 be good to get some more exploration of those drivers and  
37 the savings and towards the sustainability of them.

38  
39 MS BAKER: It is important to understand, as you said,  
40 John, what is the make-up of those cost savings. I think  
41 the key message we would like our customers, stakeholders  
42 and IPART to understand is that we have not taken two  
43 organisations, put them together and shaved some potential  
44 double-up, but we have actually created a whole new  
45 organisation.

46  
47 Fundamentally - and both David and I talked about this

1 a little bit today - we have a new Act which governs the  
2 organisation. We, as an executive team, have then taken  
3 the nine strategic objectives that the board set following  
4 that new Act coming in and actually built a very rigorous  
5 action plan for the organisation, which was very rigorously  
6 built up to ensure that WaterNSW is only undertaking  
7 activities that actually deliver the services that customer  
8 should have and most efficiently. Then we have resourced  
9 the organisation to deliver that.

10  
11 In understanding how we have done that, we have  
12 actually built a completely new organisation, very much  
13 scrutinised so that with every single position and every  
14 single job in that organisation, we can map it to exactly  
15 what deliverables and outputs that job is delivering as  
16 part of that organisational strategic action plan.

17  
18 There are both direct positions, operational  
19 positions, that have changed as well as, as you say,  
20 overhead-style savings that result from that, and in that  
21 there was a shift - or there are different percentages of  
22 where the savings are allocated to customers. One of the  
23 things that has gone on is - and maybe Andrew can talk  
24 about this a little bit - an increase in the strategic  
25 asset planning for the rural side of the business, which  
26 means that that has an impact on where some of those  
27 savings are.

28  
29 THE CHAIRMAN: It is very encouraging for end-water users,  
30 Sydney Water and the regulator to have an organisation come  
31 forward and put those sorts of savings up on the board, so  
32 that's very encouraging. I am just wondering - this is  
33 following on from John's point - whether either now or  
34 maybe later you could give us a sense of what you have  
35 done.

36  
37 There is a reduction of 9 per cent in opex, I think,  
38 over the four years. For instance, is half that 9 per cent  
39 because of reduced overheads or a quarter? How much is  
40 reduced numbers of staff? It is that sort of stuff we need  
41 to get a feel for the drivers because when you have a feel  
42 for the drivers, you are in a better place to make a  
43 judgment about the sustainability. We wouldn't want to be  
44 in a situation, and I am sure you wouldn't want to be in  
45 that situation, where, in four years time, we observe that  
46 it is starting to go back up again.

1 MR HARRIS: Just in broad terms, because I thought it was  
2 more the numbers that John was asking for, those savings  
3 come out of three areas. They come out of efficiencies  
4 with going through, if you like, shared services  
5 efficiencies. I note that when the government announced  
6 our merger, that was one of the four drivers. So there are  
7 some efficiency gains there.  
8  
9 Secondly, there are efficiency gains through better  
10 targeting our effort towards our customer and our  
11 stakeholder requirements, and that is not just Sydney Water  
12 but also our government shareholder has extremely high  
13 expectations of us in relation to cash management and water  
14 quality and so we have structured ourselves around that.  
15 Also in other areas where we have the opportunity to reduce  
16 those costs, we have taken that.  
17  
18 Thirdly, of course, there is what I might call balance  
19 sheet efficiency as well and that is also an element in the  
20 aggregate cost reduction. We can certainly give you a  
21 breakdown of those, but in broad terms they are the three  
22 areas.  
23  
24 MS BAKER: In a numbers perspective, over the four years  
25 of this next determination, it differs year to year, but it  
26 is around about half overhead, half direct. As I sort of  
27 alluded to before, with the direct savings, the proportion  
28 of those that are applied to Greater Sydney customers  
29 versus rural customers is different depending on our  
30 assessment of where our direct efforts will be spent.  
31  
32 MR HARRIS: The other thing I might add is that we have  
33 been very open and transparent with IPART. We have  
34 provided IPART with a benchmarking study that we procured  
35 during that translation process. In terms of the benefits  
36 or the efficiencies, whatever you want to call them, that  
37 come from a reduction in our staff numbers, you can see  
38 from that that, in my view, we have been entirely  
39 responsible in the way that we have gone about tackling our  
40 oversized numbers.  
41  
42 In that regard in particular, we are highly cognisant  
43 both of the issue that Eric raises on behalf of Sydney  
44 Water today in terms of the level of service - an extremely  
45 high level of service - that that organisation has received  
46 and expects to receive into the future and probably equally  
47 the government's expectation of us in relation to catchment

1 protection and water quality. I think we have gone about  
2 that part of the total efficiency picture in a highly  
3 responsible but very open and transparent way.  
4  
5 MR EDGERTON: Just a follow-on question. I think you have  
6 touched on this, David, but if you could, could you  
7 elaborate on this a little bit more? Your proposed costs  
8 are declining. Does that impact on your end catchment  
9 management and bulk water services in any way?  
10  
11 MR HARRIS: We would like to think that that will actually  
12 improve the level of service we provide because we have  
13 gone right back to square one. We have gone right back  
14 to - this is both on the rural and Greater Sydney side,  
15 however Greater Sydney is relevant here today - what does  
16 our customer expect? What is the standard of that  
17 deliverable? We have got those standards in our strategic  
18 action plan of which you have a copy. We have then  
19 resourced ourselves to deliver those outcomes to those  
20 standards.  
21  
22 We are going about that in perhaps, one might say, a  
23 slightly more sophisticated way or more enlightened way,  
24 however you want to put it, but we have absolutely  
25 resourced ourselves financially and human resource-wise to  
26 achieve those things that we have articulated to the  
27 standard that we have set for ourselves.  
28  
29 MR MADDEN: I guess this question is a follow-up in a way.  
30 The submission which you put in had, I think, the portfolio  
31 risk assessment costs, which were actually an additional  
32 cost over the proposal. This is again an opportunity to  
33 describe what that portfolio risk assessment is about and  
34 why it came up after June 30. It would be good to get some  
35 explanation.  
36  
37 MR HARRIS: I will just make a general comment and I will  
38 than hand over to Andrew for the specifics around that  
39 particular piece of work. We talked about the process that  
40 we went through with our strategic objectives. We are  
41 primarily an organisation that is about Greater Sydney  
42 catchment protection water quality and across the state  
43 around asset management and efficient asset management.  
44  
45 When we took a step back and looked at the systems we  
46 had around our asset management, we believed that they were  
47 not up to the standard that we wanted and, in particular,

1 they would not properly support us in achieving our  
2 objectives. Therefore. The strategic engineering area  
3 is an area where we are now putting more human resources  
4 and more financial resources than previously to build up  
5 our capability around that asset management function.

6  
7 I will now hand over to Andrew.

8  
9 MR GEORGE: Andrew George, WaterNSW. Holistically  
10 speaking, we are adopting a risk-based approach to asset  
11 management for our entire portfolio of assets. We have  
12 previously undertaken a comprehensive portfolio risk  
13 assessment in one half of the business, being the rural  
14 part of the business. To ensure that we are managing the  
15 assets prudently and efficiently across the business, we  
16 need to ensure we are benchmarking ourselves using the same  
17 stick.

18  
19 The PRA is a recognised methodology. It is on the  
20 more leading edge of methodologies. We need to undertake  
21 the review of the Greater Sydney basin to ensure that when  
22 we commit resources and expenditure to dam safety  
23 compliance in the Greater Sydney area, we are doing so in  
24 a prioritised and efficient manner looking at our entire  
25 portfolio across the state of New South Wales.

26  
27 MR MADDEN: I guess for background, it's around  
28 \$4 million, is it?

29  
30 MR GEORGE: Around that order, yes.

31  
32 MS JONES: Does that mean you have done rural and the  
33 money is in there because you're going to do Sydney?

34  
35 MR GEORGE: Correct.

36  
37 THE CHAIRMAN: Matt?

38  
39 MR EDGERTON: In the last few minutes we have primarily  
40 been talking about operating expenditure. At the beginning  
41 of today's proceedings, you mentioned that you have  
42 essentially significantly revised your capital expenditure  
43 for the upcoming period and that you have actually taken  
44 out, I think, close to \$100 million for the upcoming period  
45 relative to your June 30 proposal. You touched on this  
46 a little bit, but could you, please, talk us through in a  
47 bit more detail the decision-making process around that

1 revised estimate given that it is such a significant  
2 adjustment?

3  
4 MR HARRIS: Yes, I will have the first go, and in fact  
5 Elli touched on this in her presentation.

6  
7 At a policy level, there are number of moving parts at  
8 the moment. From our perspective, depending on where those  
9 separate but related parts may drop out - and none of us  
10 are in a position to know that right at this point - when  
11 we looked at those things from our unique perspective of  
12 asset planner, asset builder and asset operator, we felt  
13 that there were possibly some outcomes that may eventuate  
14 and, on that basis, we felt that proceeding to project  
15 execution stage of the Shoalhaven transfer within the next  
16 determination period may not be warranted and so we removed  
17 that project execution spend from the back end of the last  
18 year of our four-year determination.

19  
20 As I say, there are several matters that are uncertain  
21 for all of us at the moment and how they play out over the  
22 next while will determine whether in fact that scheme is  
23 the most efficient way forward or whether there is some  
24 alternative.

25  
26 MR GEORGE: The only thing to add to that would be that we  
27 did look at what are the likely or possible scenarios that  
28 we would be faced with in the determination period. We  
29 constructed a profile in our revised costs that, in some  
30 respects, was agnostic to the specific solution, but when  
31 you think about the processes that you go through, through  
32 a project planning, design phase, there are a lot of common  
33 elements and when we looked at the projects that might be  
34 on the table, there was enough commonality between the  
35 scope in deliverables that we were able to come up with,  
36 I guess, a normalised view of what happen.

37  
38 MR HARRIS: John, in a sense, maybe we have made that  
39 change on a risk basis. So far as any of us can see at  
40 this point, proceeding to execution on that project may not  
41 be the optimal way forward. However, given the demand  
42 numbers that Sydney Water have generated, given the lead  
43 time to our asset project, it would not be sensible for  
44 us to delay project initiation and planning so that those  
45 costs are still in our submission for this determination  
46 period. We think at the moment, in this period of  
47 uncertainty and, therefore for many of us difficulty, that



1 is a responsible balance.  
2  
3 MR MADDEN: So, in a sense, it is a deferral?  
4  
5 MR HARRIS: Well, it is a deferral of the third --  
6  
7 MR MADDEN: But you are still planning?  
8  
9 MR HARRIS: It is a deferral of the third gateway, the  
10 project execution gateway for the Shoalhaven, but it is not  
11 a deferral because our customers in Sydney Water are best  
12 placed of any government entity to forecast demand. We  
13 accept that and our responsibility is to then develop an  
14 asset strategy to enable us to supply water to meet our  
15 customers' projected demand.  
16  
17 Given the lead timing in our projects and given where  
18 those demand numbers have come out, we do not think it is  
19 responsible to defer the initiation of the planning phases  
20 of that project. However, on a balanced balancing basis we  
21 have taken the view not to include the third phase  
22 execution costs - which are, as you saw from the slide, the  
23 very large element of the costs - and to defer that beyond  
24 this determination period.  
25  
26 THE CHAIRMAN: Would anybody else like to comment or  
27 ask a question?  
28  
29 MR NANCE: Phillip Nance is my name. I am just a member  
30 of general public. The incentive payment scheme seems to  
31 me to be a very good thought. There are two things about  
32 it, though. The volume which goes in, is that  
33 significantly invariable so not to worry about it? In  
34 other words, do you worry about the volume or just say, "On  
35 an annual basis that's near enough, so we wouldn't bother  
36 how much went through"?  
37  
38 The other point is just in case, say, Sydney Water and  
39 WaterNSW have a disagreement about it, how about some  
40 prearranged arbitration? Who sorts it? Thank you.  
41  
42 THE CHAIRMAN: Thank you very much very much, Phillip.  
43 Is there any response to Phillip's suggestions?  
44  
45 MR DE ROOY: As I said earlier, I think the scheme needs a  
46 joint review. We will work those ideas as we go through in  
47 terms of making sure it is a sustainable model and that is

1 clear and transparent as to what basis it would be  
2 determined.  
3  
4 THE CHAIRMAN: Thank you, Phillip. Okay, I think that is  
5 it. Is there anybody else? Carmel?  
6  
7 MS KROGH: I could not let the opportunity pass without  
8 making a comment on the Shoalhaven transfer scheme. There  
9 is obviously a lot of debate about that. The scheme is  
10 based upon the 2010 Metropolitan Water Plan. It was  
11 included in that plan.  
12  
13 I would like to make the point that the Shoalhaven  
14 community are very, very interested in what happens to the  
15 transfer scheme. I have made this comment both to WaterNSW  
16 and to DPI Water that, on the issue of the Shoalhaven  
17 transfer scheme, there needs to be significant consultation  
18 with the local community before that goes any further  
19 because there was a huge gap in time before it was actually  
20 initially discussed. In principle, the deferral out of the  
21 pricing path is very consistent with what is actually  
22 happening on the ground.  
23  
24 THE CHAIRMAN: Thank you, Carmel. Is there anything else?  
25 No further questions or comments?  
26  
27 CLOSING REMARKS  
28  
29 THE CHAIRMAN: On behalf of IPART, I would like to thank  
30 you all very much for your participation and your  
31 contribution. It has been of great benefit to hear your  
32 views and participate in the discussion.  
33  
34 A transcript of today's proceeding will be available  
35 on our website in a few days.  
36  
37 We will consider all that has been said today when we  
38 make our decision on WaterNSW's prices for the Greater  
39 Sydney to apply from 1 July 2016.  
40  
41 As previously mentioned, we plan to release a draft  
42 report for public comment in March 2016. People will then  
43 have about four weeks to make further written submissions  
44 for consideration by IPART before we make our final  
45 decisions on WaterNSW's prices.  
46  
47 A final report and determination will be released

1 in June 2016 and the maximum prices that we set will apply  
2 from 1 July 2016.

3  
4 I encourage you to monitor IPART's website for updates  
5 and further information on our timetable, including the  
6 actual release date for the draft report and the date by  
7 which submissions are due in response to that report.

8  
9 Finally, I note the public hearing for IPART's review  
10 of Sydney Water's prices will commence here at 11.30 and  
11 invite anybody interested to stay around and attend that  
12 hearing. Thank you very much.

13  
14 AT 10.40AM, THE TRIBUNAL ADJOURNED  
15 ACCORDINGLY

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