

Our Ref: F084876
Your Ref: C/15/4191
Enquiries To: Denis Musaefendic

4 November 2016

Water Team – Pricing Approach Review
Essential Services Commission
Level 37, 2 Lonsdale Street
Melbourne VIC 3000

Dear Water Team,

Re: Barwon Water Response - Assessing and Rating PREMO Price Submissions (October 2016)

I am writing to you in response to the Commission's request for businesses to provide feedback to the *Assessing and Rating PREMO Price Submissions (October 2016)* consultation paper.

Feedback on topics requested by the Commission is provided below.

PREMO assessment tool

Barwon Water accepts the Commission's point that providing specific criteria may result in a tick-the-box approach, however language such as 'significant improvement', 'very significant improvement', 'clearly above industry benchmark' still leaves a broad degree of ambiguity and guess work for businesses.

Barwon Water believes that the Guaranteed Service Level (GSL) assessment criteria are better placed in the 'Outcomes' section of PREMO rather than 'Risk'. The GSLs result in an output of higher quality of service received by customers as well as a direct output that customers experience if these standards are not achieved through a GSL payment.

Barwon Water notes the inclusion in the 'Management' element which guides businesses to mitigate or absorb, for Standard or Advanced respectively, the costs of new regulatory obligations. The uncontrollable nature of these costs makes them difficult to mitigate or absorb, which is why Barwon Water believes the Commission's position thus far has been to treat them as a direct revenue requirement component. This position is also made in the ESC's latest *Water Pricing Framework and Approach – Final Paper (October 2016)* stating that *"The pricing framework and approach will continue to allow water businesses to recover efficient costs for the delivery of policy or regulatory obligations. Policy and regulatory obligations will generally be specified in a Statement of Obligations, or in separate instruments administered by the Environment Protection Authority (Victoria) and the Department of Health and Human Services"*.

Another implication made by this inclusion is that businesses have the ability to mitigate or absorb these costs which implies that there is some inefficient expenditure that can be replaced with these new obligations. Barwon Water believes that there should be a correlation between the ambition rating and the efficiency of expenditure which makes these uncontrollable costs even more difficult to absorb.

PREMO scoring system

Barwon Water's assessment of the KPMG scoring system is that it appears to be relatively rigid considering the lack of full certainty about what it takes to achieve a certain level of ambition which makes it difficult for both the businesses and the Commission to justify an integer score. Because of this, any downward revisions in the score have a much higher impact and likelihood in resulting in a downgrade. In addition, by using an averaging approach to calculate an overall rating, the scoring system assumes that each REMO element has an equal impact on the customers and community which may not be the case depending on different businesses circumstances, proposals and community engagement.

Having said that, Barwon Water believes that the alternative scoring approach recommended by the Commission addresses both of the concerns noted about KPMG's approach. The ability to state the degree of confidence would add transparency and accuracy to the businesses and Commissions assessment for each REMO element. Being able to score higher or lower than an integer is also a pseudo way of weighting the impact of each REMO element differently. Barwon Water therefore supports the Commissions alternative scoring approach.

Thank you for the opportunity to provide feedback on the Commission's new water regulatory pricing framework. Please do not hesitate to contact Denis Musaefendic (ph: 5226 2582) should you require any clarifications.

Yours faithfully

A handwritten signature in black ink, appearing to read 'S Butcher'.

Seamus Butcher
Manager Strategy, Environment and Regulation