



QCA Pricing Practices Recommendations
December 2014 Update on
SunWater Implementation Plan

December 2014

SunWater has continued implementing the QCA's Pricing Practices Recommendations according to the Implementation Plan. This is the final update reporting on the last few deliverables from the plan. It covers the work completed between July 2014 and Dec 2014.

Review Renewals Planning Process (1.2)

Disseminate New Renewals Planning Process (1.2.8)

As previously reported in the update from April 2014, the major change to SunWater's planning processes that has arisen from the renewals planning review is the requirement to perform options analyses for all material projects. SunWater's processes have been amended accordingly.

The options analysis requirement can be separated into two process changes:

1. The identification of material projects, and
2. The completion of required options analyses.

Training in material projects identification has been completed with the material project lists being successfully generated in November, February and June of each financial year. The Planning Team and Service Managers are aware of the requirement to complete options analyses for the material projects and have had training on completing options analyses in workshops and meetings held during November 2014. Individual options analyses are also reviewed in the course of normal business with the aim of continuous improvement in the quality of these documents.

SunWater continues to improve condition and risk data quality within SunWater's Works Management System (WMS). Gaps in the quality of electrical asset condition and risk data have been significantly addressed over the past six months and further improvement in this area will occur. In addition, a recent review has identified some assets with inadequate condition and risk data. Again, these gaps are being progressively addressed, focussing initially on the higher risk assets. These improvements in the condition and risk data are contributing to improved renewals program forecasts which are being used as inputs for the current LMA and Infrastructure Pipeline asset investigations, and will ultimately lead to better forecasts for the next Irrigation Pricing Review.

Review Operating Costs Planning (1.3)

Disseminate New Agreed Operating Planning Process (1.3.6)

As previously reported in the update from April 2014, the most significant change to SunWater's operating processes is the requirement to produce Annual NSPs and Performance Reports. SunWater's operating planning process documentation has been updated accordingly and Service Managers have demonstrated their understanding of this process through their contributions to the NSPs and Performance Reports produced over the past two years. These new reporting obligations were also discussed in workshops and meetings held during November 2014.

Other actions from the operating review involve better execution of existing processes. This includes better adherence to the cost allocation methodology and improved tracking of labour costs. While these actions have not necessitated changes to process documentation, the importance of improved cost allocations has been re-iterated during the November 2014 workshops and meetings.

Separate Identification of Irrigation Working Capital Requirements (3.5)

Separate Identification of Irrigation Cash Flows (3.5.1)

The QCA's recommendation on estimating working capital was seeking two main changes in the calculation of SunWater's working capital requirements:

1. Separately identifying working capital cash flows for Irrigation service contracts only, not whole-of-business, and
2. Using forecasts of each of the working capital cash flows, not historical information.

The QCA presented Deloitte's approach to calculating working capital in a report¹ tabled as part of the last Irrigation Price Review. SunWater has applied Deloitte's methodology in producing an example working capital forecast using forecasts of cash flows for irrigation service contracts only, as recommended by Deloitte. These cash flows were able to be separately identified using SunWater's Financial Model and an Infrastructure Pipelines model developed to support the proposed lease of these assets.

Forecast Working Capital requirements (3.5.2)

The components required to estimate working capital requirements were described in Deloitte's report². SunWater followed Deloitte's methodology to estimate the cash flows tabled below:

Table: Working Capital Analysis of BW & IS of SunWater

	Forecast 2017-18	Forecast 2018-19	Forecast 2019-20	Forecast 2020-21	Forecast 2021-22
	\$000	\$000	\$000	\$000	\$000
Current Assets					
Trade debtors	13,181	13,511	13,849	14,195	14,550
Term trade debtors	85	85	85	85	85
Provision for impairment	(1,854)	(1,911)	(1,697)	(1,747)	(1,760)
Receivables	11,413	11,685	12,237	12,533	12,875
Inventories	1,646	1,606	1,568	1,530	1,492
GST Receivable	785	807	491	437	555
Accrued Revenue	7,157	7,360	7,251	7,457	7,451
Other current assets	7,942	8,167	7,742	7,894	8,006
Total current assets	21,001	21,459	21,547	21,956	22,373
Current Liabilities	2017-18	2018-19	2019-20	2020-21	2021-22
	\$000	\$000	\$000	\$000	\$000
Trade creditors	3,874	3,979	2,343	2,062	2,676
Other creditors & accruals	6,198	6,439	7,262	8,106	8,970
Payables	10,072	10,418	9,605	10,167	11,646
Employee benefits	2,420	2,635	2,671	2,746	2,822
Provisions	2,420	2,635	2,671	2,746	2,822
Total current liabilities	12,492	13,053	12,277	12,913	14,468
Working Capital	8,509	8,406	9,270	9,042	7,904

¹ Deloitte – Final Report: Working Capital Allowance, 15 Aug 2011, QCA Website.

² “Other Current Liabilities” cash flow category is currently not relevant to the next price path.

The above table demonstrates SunWater's application of Deloitte's methodology. However, this estimate does not represent SunWater's forecast for use at the next price determination because the operating cost forecasts will not be established until the next review and are likely to be very different due to the substantial changes proposed for SunWater's business structure. In particular, the Industrial Pipelines business and some of the Irrigation Systems business may not be a part of SunWater by the time of the next pricing review.

Working capital requirements will need to be estimated at the time of the next review based on SunWater's forecast of cash flows for the re-structured business as it exists at that time.

Document Working Capital Forecasting Methodology (3.5.3)

This update report, along with the Deloitte report, represents the supporting documentation for production of the working capital forecast at the next price review.

The working capital estimate provided above has been produced by taking the forecasts from SunWater's Financial Model (V1205) and differencing off a separate model representing the Industrial Pipelines business. As such, it is an estimate of the working capital requirements for a combined Bulk Water and Irrigation Systems business (BW & IS).

Some further notes relevant to the estimate include:

- The forecast has been based on SunWater Financial Model (version 1205) less an Industrial Pipelines forecast model to provide a forecast for the BW & IS business.
- Trade debtors forecast is based on the most recent six months closing balances for the BW & IS business (Jun 14 to Nov 14) to get to an average debtor position. This average debtor balance has then had 2.5% CPI applied each year from 2014 out to 2022.
- Term trade debtors have been taken from the model forecasts.
- The provision for impairment is taken from the models. It equates to approximately 2.5% of the annual credit sales of BW & IS.
- Inventories is taken from the model forecasts.
- Accrued revenue is taken from the model and when combined with trade debtors is comparable year on year with the 2014 actuals.
- Trade creditors have been taken from the two forecast models identifying the trade creditors only and removing any other liabilities.
- Other creditors are taken from the model forecasts and it includes items such as accruals and deferred revenue. It does not include the Annuity liability as this is not considered relevant working capital. It also excludes any intercompany tax sharing balances.
- Employee benefits have been taken from the two forecast models.