

THE HOUSE OF ASSEMBLY SELECT COMMITTEE ON WATER AND SEWERAGE MET IN COMMITTEE ROOM 2, PARLIAMENT HOUSE, HOBART ON TUESDAY 22 MARCH 2011.

Mr MILES HAMPTON, ONSTREAM BOARD CHAIR, AND **Ms CAROLYN PILLANS**, CORPORATE SECRETARY, WERE RECALLED AND FURTHER EXAMINED, AND **Dr CHRISTINE MUCHA**, CHIEF EXECUTIVE OFFICER, ONSTREAM, WAS CALLED, MADE THE STATUTORY DECLARATION AND WAS EXAMINED.

DEPUTY CHAIR (Mr Morris) - Welcome, everyone. Miles, is there anything you would like to say, wearing your Onstream hat this time?

Mr HAMPTON - I don't think I have anything to add to that which I have already said. I think at the first hearing in Hobart I very specifically addressed Onstream and expressed some views about the governance arrangements and the prescription of the activities undertaken by Onstream.

Mr HIDDING - For the sake of people reading a transcript of this hearing, knowing it is about Onstream, could you give a two-paragraph precis of where you are and we can then go back to your evidence to fill that out?

Mr HAMPTON - The four boards put in a joint submission and in respect of Onstream they highlighted two aspects: governance and its activities in respect of governance. Onstream is currently a proprietary limited company that is jointly owned by the three regional corporations and it has its own board. On that board are the three chief executives of the regional corporations, together with a common chair, an independent director and one of the other common directors. The view of the board was that there was no need for a separate legal entity and shared services do not need that form of structure to work. A number of councils across the State share resources and I'm certain that they don't set up separate legal entities to do it. Equally, in terms of the composition of the board, you would almost say, with the exception of one director, we are all at times conflicted. A very clear view of the four boards is that there is no need for it to be a separate legal entity and the form and constitution ought to be left to the regional corporations.

As regards the activities, effectively the regional corporations are banned from undertaking certain activities that fall to Onstream. It is quite prescriptive. The view of the boards is that there should not be any prescription and the regional corporations should be free to decide what they want to do on an individual basis and what they want to undertake on a shared basis. That is not to say that the current boards of the regional corporations have a specific view as to what they would or would not leave with Onstream. That has not been discussed. The principal reason for not believing that prescription is appropriate is that it doesn't open the door for any competitive tension and, as a result, we will never know whether we are in fact getting the most cost-effective solution.

DEPUTY CHAIR - Could you run through in order of volume of activity within Onstream where you are now? Obviously the billing system has been a big thing for you in the last 12 months. You also do a significant human services component for the three corporations, as I understand it. Can you run through those key things and roughly what proportion of the business they currently are and where you think they're going at the moment? If things were to stay the same, the billing system is bedding down, hopefully that will be less of your effort.

Mr HAMPTON - The two principal areas at this point in time are information technology and billing - the provision of an IT platform and IT services to the three corporations. In terms of the billing to the three corporations last year, about \$5 million was on IT and almost a similar amount on billing. So the two core principal activities are IT and billing.

Mr HIDDING - And they cross over into each other?

Mr HAMPTON - Yes, they cross over into each other because the billing system uses the IT system. When it gets away from that, it drops away very quickly. The third-largest activity in terms of the cost that we charge the corporations is accounts payable/financial services, which is about \$1 million. Then it drops away to procurement, secretariat and human resources. So the two big areas are IT and billing.

Mr HIDDING - This is not a rude question, but Ms Mucha is a senior player in Tasmania in terms of water and services. I am interested in whether Ms Mucha saw the management of Onstream as being different to what it turned out to be. We all took it on faith to see how it would go and as it has turned out, it's an IT and billing company. Is this something that you saw yourself managing or did you see yourself more in policy development for the corporations?

Dr MUCHA - You've made that valid comment about it being an evolution process and when we started - and you have to remember, we only had about four months to get up and running - you needed to have a very good understanding of the water industry to understand what the key drivers were. IT has always been a big driver in the water industry. If you don't have IT, you can't do the monitoring of the reservoirs et cetera, so that was always a key element.

Mr HIDDING - I see, on the technical side as well?

Dr MUCHA - Yes, the technical side also. It's not just about running servers and things like that, it's about providing communication links, right down to where the reservoirs are. It is a very complex IT. When it originated at Onstream it took on some of the other aspects as well; we did do some research and development for them in the area of monitoring water because we had a significant fund from the Bureau of Meteorology. So that aspect was there. You could say, 'Let's look at it from the other side'. If you had someone there who did not understand the water industry, then I do not think they would have been able to get it up in four or five months, so that was a critical element. We had a good understanding of that.

I still think that whilst, yes, we tend to talk about it as a backroom corporation, basically you do need to have an understanding of your clients because otherwise you could be

going off at a complete tangent to what their needs are. Even for understanding this State, for instance, with the payroll, the payroll system when it was started comprised of 29 councils plus the three bulk water and there were 32 different enterprise agreements. You needed to understand the uniqueness, and that was my background as well, of how the people in the field operated. I do not think there has been that.

It is the same with the billing; I think you needed to understand the difficulties with the billing. As we move forward obviously that has been one of our key drivers because no-one has wanted to be in the space that we have been in with the billing. Really now it is about working through, making it as streamlined as we can.

IT, I think, has one of the greatest avenues of growth because IT is very strong in how it can help the water industry and that is going to be a big driver into the future, both nationally and locally. IT is one of the key drivers.

I do not think I have wasted my time in that area.

Mr HIDDING - No, and that was not the suggestion. I can see why it was good to have you there.

Dr MUCHA - The four CEOs have regular meetings or forums. With the four of us together with all of our different ideas and background experience - obviously there were some new ones that came from Victoria - I think we have come up with a very good system in a relatively short time.

Mr HIDDING - So they were not able to snow you, is that what you are saying?

Dr MUCHA - That is right.

Laughter.

Mr HAMPTON - You opened your remarks using the words 'policy development'. Picking up on what Christine has said, over the last two years in that area in large measure the former chair has guided the corporations to allow the person with the best skillset to effectively be a lead person in respect of the area, whether or not it fell in their domain necessarily, and I think that has been a productive use of the skills that have been brought together.

Mr HIDDING - Because the CEOs are on Onstream, I guess in terms of policy development, good, sound public policy as it relates to the operation of a public utility, it is all very well having a good idea in your head but articulating that into a policy plan and then a set of management principles is, from somebody who comes from politics, pretty difficult. It is the articulation from strong thinking into management rules. How does that happen and where does that happen within all the corporations or Onstream?

Mr HAMPTON - It does not officially happen in Onstream.

Mr HIDDING - No, it does not. So it is in the group?

Mr HAMPTON - It is in the group. So if we are looking at two-part pricing and how we are going to implement it, it is done as a group and it might be at the CEO level or it might be with one CEO's involvement with people at a lesser level or it might be people at a lesser level, trying to bring together the best people across the four corporations who can contribute to it. Onstream did not have and does not have a specific lead role in that area of global policy development. Clearly, it has a lead role in guiding the corporations down the path of IT and the use of IT and Christine brought unique skills, having led Hobart Water, to use IT in a very sophisticated way to manage the assets. Not all of the other organisations who transfer their assets to us were managing their assets in that way. I do not want to make it clear that the board did not give Onstream a policy brief across the industry. Onstream does not have a chief engineer, it does not have a chief asset manager; each of the three regional corporations has an asset manager.

Mr HIDDING - Is that so? I suppose it is in line with government policy to set up the three but is it the best corporate model?

Mr HAMPTON - My view is that it is the best corporate model today given the issues that we have in front of us at present. Whether in five or 10 years' time - when, hopefully, a lot of the work that needs to be done is done - it will still be the appropriate model, I am not sure.

Mr BEST - We had a witness who felt that what we have is a Rolls-Royce model. Basically it is over-complicated or it is over-supported - however you may want to describe it. Is that the case? Have we got a Rolls-Royce or a Holden? There is no way that you could do anything any cheaper than you are. Obviously, you will create more efficiencies as you move on but what you have set up with Onstream is a very efficient way of going about it with the challenges that you have had.

Mr HAMPTON - My view as chair and my view as a common director for the past two years is that, just like the other corporations, we had certain employees transferred to us and we had to take them whether they collectively brought all the skills that we needed or not. It was the same issue that the other three corporations faced.

Mr HIDDING - Who decided which employees you got? They floated to the top, did they?

Mr HAMPTON - They floated to the top.

Laughter.

Mr HAMPTON - Clearly in a large measure the administrative people ended up in Onstream's space and some of them ended up in the regional corporation space, but even so we did not have all the skills. We were looking, for example, for a much more sophisticated IT approach because we were trying to cover the State so we have had to go out and recruit a significant number of people to make sure that we have the skillsets. We are basically 18 months into operations, two years since we started.

To answer your question directly, do I think that we are today as efficient as I had hoped we would be in a year's time and two years' time, my answer would be no, but I think it is actually reflective of being thrown together with some monstrous tasks to tackle. In the same way that the boards of the regional corporations have said to their CEOs, 'We now

want some productivity benefits; we want costs to be going up less than the CPI, we have said the same thing to our CEO at Onstream. I am not sitting here saying that I think it is the most efficient.

Mr BACON - You think it can be more efficient over time?

Mr HAMPTON - I think it can be.

Dr MUCHA - The submission that we gave to you was obviously in December and I think in there we talked about savings of \$4.8 million. We did a figure the other day and we are now up to \$5.3 million. That is per year so if you multiply that in 10 years that is \$53 million. Yes, you could argue that some of those savings may have been achievable without Onstream but what it really is about is the driver and the expertise to achieve those savings.

I refer back to that earlier comment about why was I involved in Onstream. As part of the constitution and part of the act it talks about also providing opportunity of services to the councils. I am not sure if the chairman's model, as he has pointed out, may be appropriate or able to be done, but to me that was one of the really big benefits of the Onstream model - helping local government - because a number of the services would then actually give benefit both to local government and to the corporations, which are owned by local government. Effectively, any savings you make you can multiply. A number of the savings obviously are made because you're talking about three large corporations, but if you then added the councils to that there are some significant savings that could be made. We haven't had the opportunity to investigate that further at the moment because we've been heads down and let's get it right for the corporations. I think the chairman is perfectly right when he talks about working through and making it more efficient. I think that can happen and I think we have illustrated that. Even with the corporations getting into one enterprise agreement and away from the messy environment they're in, that will bring efficiencies.

Also where you can really add the benefit is working with the councils because you are then reducing your overheads. The interesting thing about the question of overheads is that a lot of those costs would still be there irrespective of whether we existed or not. In fact only a very small component - which would be reflected in the board and myself as well - would disappear; the larger overhead costs would still remain. I believe that it was set up with the view to give that support and development for the councils.

Mr BEST - So you're confident to say that the principles here have been strategic and accurate and as efficient as you could possibly do it, given the challenges of starting up and what you've had to address?

Dr MUCHA - I would say we have been. Revenue services or billing have probably been the biggest challenge for us. Now that we have a new system and are already recognising improvements with the call centres, they are able to access and view things so that's creating efficiencies. When you talk about the efficiencies within us, it is now about the efficiencies from end to end. It is efficiencies within the corporations, allowing them to capture those as well. It is multiplier effect of efficiencies.

Ms PILLANS - I can provide an example that explains whether we are overengineered or not. One of the earlier decisions of the combined boards was to set up the central secretariat. In previous examples at Hobart Water we had perhaps half a person in a small organisation who looked after legal compliance and legal services, half a person who looked after internal audit, half a person who looked after insurance, and a board and secretariat and a governance manager. Since we have moved to the common model, we still have one corporate secretary, one legal counsel, one internal audit specialist, one insurance specialist and a couple of support staff. They now look after all four corporations, the equivalent of the water and sewerage governance of 32 contributing entities. We also pick up the internal governance of Onstream. As an example of that, in the 2009-10 year we prepared, serviced and facilitated 88 board and committee meetings from our small team. We also provided the legal compliance framework and the legal services. Some of that was facilitation rather than delivery in itself. We have brought one batch of expertise that lives centrally and is readily accessible and shareable by all CEOs and executive management teams. We had an independent review this time last year to see whether the model that we built was the best model and it turned out that those results were that we had developed as fit-for-purpose. We used simple technology that was as efficient as it could be - electronic board portals and those sorts of things. They made a couple of suggestions around the edges but it got a tick and moved on. That is an example of what Onstream can deliver on behalf of all the corporations.

Mr BEST - The \$2.4 million of savings in the first year, they are real savings?

Dr MUCHA - Yes.

Mr HIDDING - Based on what Ms Pillans has just said, do you see yourselves genuinely as a service organisation to three corporations or vice versa, and how do they see you? Do they see you increasingly as head office because in a corporate sense that is what head office does - it provides the stuff that the divisions are unable to do because of scale?

Mr HAMPTON - I don't think they see us as head office. I don't think that was what was intended. I think, however, some people outside might view Onstream as head office and that is reflective of their not completely understanding its role.

Mr HIDDING - Given your corporate background, though, isn't it behaving as a head office?

Mr HAMPTON - No, because in fact each of the corporations has their own CEO, each of the corporations has their own senior financial person and each of the corporations has their asset manager and their operations manager. There are certain activities that are normally undertaken within a corporation that typically would fall under the ambit of the chief financial officer, the chief information officer or the chief HR manager.

Mr HIDDING - Can we look at CFOs. Originally it was set up with a central CFO, but I note that Hobart now has its own CFO.

Mr HAMPTON - Indeed. The description of activity does have financial services in the ambit of Onstream. After we had been going about 12 months the CEOs of the regional corporations effectively said to the boards, 'We think we need some more strength in the financial area within each corporation' and I think it was largely a matter of being able to

have access to Conrad Lennon, who was the CFO within Onstream and at that point in time the CFO of the three regional corporations as well.

Mr HIDDING - Is he not now?

Mr HAMPTON - The role is still within Onstream, but what we have done is taken certain aspects of that role and put it back into the corporations where it ought to have properly been from day one. While we have honoured the spirit of the legislation, we have sought to find a more commonsense solution. That has also freed up the CFO in Onstream to play a more proactive role in the implementation of the new billing system.

Mr HIDDING - Which brings me to my next question. Given that billing will be sorted - I have a good feeling about this from everything I have heard; you guys are on to this compared to some other utilities around the place and you will nail your IT -

Mr BEST - They would be better organised than the Liberal Party dues.

Mr HIDDING - Dues - what are they?

Dr MUCHA - Is that a service opportunity we should look at?

DEPUTY CHAIR - Yes, I think so.

Mr HIDDING - If it is then a good idea that the three divisions have their own CFOs, Onstream surely does not need a CFO?

Mr HAMPTON - I am happy to express the view that in the fullness of time the CFO functions that are needed for Onstream could well be provided by a CFO within one of the other corporations.

Mr HIDDING - Because Onstream itself being a service organisation is not going to have a large -

Mr HAMPTON - Today, tomorrow - probably inappropriate. In 12 to 18 months' time - completely appropriate to have it on the table for consideration.

Dr MUCHA - I think what it does show is the evolutionary approach that we have had to take. As I say, we had four months to set up and that was all the corporations as well so we had to at that time divvy and decide who was doing what to make sure that we were servicing the needs, that obviously the community still received their water and sewerage and there also were the appropriate support mechanisms behind, particularly for the payroll. We got a payroll system up - I think we had two errors, which was pretty incredible.

The main thing about this is we recognise its evolution and even as we formulate budgets each year or as we look at our services we are discussing and changing them as we improve the efficiencies or we have the IT. For instance, it is now recognised that IT is a growing area, particularly in that communication side. If you took a snapshot in 12 months' time, I think you'll find it will be different again.

Mr HAMPTON - There is one other area that we made a change on and that was in relation to call centres.

DEPUTY CHAIR - Yes, if you can take us through that. I have a grumpy customer of yours who has given me some correspondence again which I have here somewhere.

Mr HAMPTON - If you read the prescription of our activities, you would conclude that four centres would fall under the domain of Onstream and we set up a common call centre approach under Onstream. The CEOs came to their boards and said, 'We are not quite sure that this is the right model.' We have resources in the individual corporations that could take up some of the slack and what the then chair brought to the boards and was signed off was that the call centres, the actual staff, would be in the corporations but to honour the spirit of what we required, the platform on which they were working was an Onstream platform. We tried to find the solution that best worked rather than follow the prescription.

DEPUTY CHAIR - As in a single number for entry and that is still the case is it?

Dr MUCHA - Yes.

Mr HAMPTON - But the actual human resource who are answering those telephones are in fact sitting inside the regional corporations.

DEPUTY CHAIR - Is there a triage system right at that very high level entry for people, so that they get -

Dr MUCHA - When you ring in it will pick up where you are located and so then it goes straight through.

DEPUTY CHAIR - I see. So it is an automatic triage system there?

Dr MUCHA - That is my understanding of it, yes, it is automatic. When it was set up I think we had two months to set up a call centre. Immediately we set up a 12 months' completely outsourced one, except that we installed some systems to work and I think it was a good learning curve and a number of those people then transferred to the individual corporations at the end of that 12 months.

Mr HIDDING - What was the benefit of having them in those corporations?

Dr MUCHA - There are a number of benefits, particularly the fact that the corporations felt they could utilise staff on other activities as well because sometimes you get the peaks and the troughs, so it is a good opportunity to do other work.

Mr HIDDING - Are you suggesting there are periods where there are no complaints?

Dr MUCHA - You would like to hope so!

Mr HAMPTON - Not all calls, sir, are complaints.

Mr HIDDING - I could ring up to congratulate you.

Laughter.

Mr HIDDING - So there are other things they can do. So that is one good reason?

Dr MUCHA - Yes, there are other things. That is one and the other one is that obviously it also provides that extra redundancy if there is an overload in one site. That is something we are working on the moment from a technology point of view, that can redirect to another corporation. Also, the other thing is that if you are in your regional area you understand the community and hopefully you are employing people who are part of that community so they understand the systems - as with Ben Lomond, they are a part of the Launceston and the Tamar community, versus the Cradle Mountain Water. It is important that you have someone who understands on the other end of the line and that, again, takes time to train them.

Mr HIDDING - Who understands the local parochial matters?

Dr MUCHA - That is right.

Mr HIDDING - As commonality strengthens, however - let us say in five years' time, when platforms are generally the same - what is an answer in Hobart will be the same as an answer in Devonport. I suppose it is always good to have somebody on the other end of the phone who, when somebody says 'It is freezing, isn't it?' he or she is able to say, 'Yes, it is' rather than saying, 'Well, down here in Hobart it is beautiful.' It is bit like the Indian call centre syndrome - there is that sort of feeling about a personal thing. But even that, as commonalities increase, will become less and less of an issue, I would have thought.

Dr MUCHA - In five years' time, yes, there will still be call centres but I think there will also be more and more people going to the web. This was evident, for instance, in that comment recently from TT-Line. We have not yet pursued that because obviously our interim billing system has not been sophisticated enough and that is part of the new system that will allow that. I think in five years' time you find more and more people who obviously have just the normal inquiries, probably will not go to call centres. For specific, really difficult inquiries, they will still need people. But whether you have one central or several individual in five years' time, well -

DEPUTY CHAIR - It's a long way off.

Dr MUCHA - Yes.

Mr HIDDING - You could say, 'You can wait or you can go online and fix this'. Is there an interim step - I think Qantas was going to go there but I don't think they ever did - whereby you can go online but there is someone watching you online as you ask questions and they can intervene?

Mr HAMPTON - I think that technology is there but I'm not sure that we have explored it.

Dr MUCHA - I think the key element - and it's been very clear from the corporations and also our board and staff - is to get the current billing right. I think that is the move that will happen as we move forward.

Mr HIDDING - It's all billing, isn't it?

Dr MUCHA - There are online queries.

Mr BEST - Online is cheaper, though, isn't it. On the weekend I went to pay my Telstra bill over the phone and they have a message. I worked it out on a calculator and it was \$5 to pay over the phone so that's the last time I am doing that. Online is faster and cheaper.

Mr HAMPTON - I was in the Hobart call centre last week and they had a big whiteboard and on it was 'This is out on this street and will be reconnected at such-and-such a time'. If we tried to do that on a State basis, I am not quite sure it would work. We are trying to provide a level of service to the various communities. I think we have the optimum; I think we have a common platform but distributed functionality. I think in the area of CFO and Onstream and in one other area we have responded in terms of the mandate for Onstream, as Christine alluded to in her opening comments, the possibility of doing other activities for other organisations. Christine touched on the councils. The remit that the board gave to Christine as CEO was broader, but during the course of our first 12 to 18 months it became clear to us that some people were unhappy with that remit being broader.

DEPUTY CHAIR - They felt you had an unfair advantage, I think.

Mr HAMPTON - People took it that we had an unfair advantage. The fact that we might have had proper cost attribution was beside the point. It did not matter, it was perception.

Mr BACON - But also they can't compete with you for the billing for the water corporations, can they? You can compete with them but they can't compete with you.

Mr HAMPTON - Some did express that view to us. The board took the view - and I'm happy to say that I'm not sure that our CEO of Onstream was overly happy at the time - that we are all in one space. If Onstream's head is being shot on this issue, then we are all being shot on this issue. The best thing we can do is put our heads down and focus on the principal activity - let's face it, these other activities in the short term were very low value. We are a \$15-million cost centre and we are picking up \$100 000 or \$200 000. Christine's plan was that they would be built over time, but we had to start somewhere and we were being popped off on that basis. The board of Onstream came to the very firm view that we needed to get our head down and we contracted to saying we would continue with that which we had already agreed to do, which is minimal, and focus on our owners, if they wish us to do something, but at this point in time we will not choose anybody else. I think in those three areas the corporations and Onstream in particular have shown considerable flexibility to adapt to our circumstance.

Mr HIDDING - Can I check with the chairman as to whether he has the same impression as I do, that most of the people complaining about those matters were in fact local government, the very people who own the organisation, who saw this as some kind of competition, in spite of the fact that they own it?

Mr HAMPTON - There were some local government representatives who were expressing that view but there were also a number of people who were running small business around the State -

Mr HIDDING - Who felt threatened?

Mr HAMPTON - who felt threatened and we did not need the noise; we were creating enough noise ourselves.

DEPUTY CHAIR - It was my impression at the time that the complaints out of local government reflected as much as anything the fact that they did not really have a strong sense of ownership.

Mr BACON - Control.

DEPUTY CHAIR - Yes, they did not have much control but the feeling of ownership of the corporations is something that is still not very strong.

Mr HIDDING - Having rebalanced their businesses or handed them over.

DEPUTY CHAIR - Yes.

Mr HAMPTON - In my very opening remarks to you a few weeks ago I said, 'As corporations we need to be closer to our owners'. If the Government decide that our owners will be the Government then we should be close to the Government. If our owners are the councils, we need to be close to them.

Dr MUCHA - I think it is a valid point and I think I commented earlier that our focus has been to make sure we get it right with the water corporations - again, obviously IT billing but payroll as well. But I think that where we probably did not have the resources or the time to do it was to go and talk to the councils about understanding Onstream. I know that at times where I have spoken to them more recently they have better understood what our opportunities are and where maybe they could work together.

Mr HIDDING - Are you doing any work for any councils anywhere?

Dr MUCHA - Not at the moment. We are doing a bit of work with the State Government with some small GBEs and things.

Mr HIDDING - Do you have any contracts or any work with any other organisations in the private sector?

Dr MUCHA - It is a bit hard how you describe it. It is an interesting one. We have joint contracts when we use private sector to work jointly on a project we are doing for the corporations. Likewise, when we are doing some work for one of the State Government entities, the Tasmanian Planning Commission, basically that is a joint venture with the private sector. We do capture the local private sector in our role, so we do not exclude them. In fact, a number of our activities have a component of outsource to them because we are not out there going to create some things that we are not efficient at doing. So that is the benefit of where we do capture working with the private sector.

Mr HAMPTON - But I do not think we have contracts with individual outside firms where we are providing services to them today.

DEPUTY CHAIR - It is pretty obvious where we are heading with all of this in terms of the information that is coming into us.

Mr HIDDING - Is it?

DEPUTY CHAIR - To me it is starting to become clear.

Mr BACON - You only have one vote though, Tim.

DEPUTY CHAIR - That is correct; I absolutely acknowledge that. But what I am interested in is firstly understanding where the new billing system is at the moment and where you think it is progressing over the next two years or so, just the medium term. Is it fully implemented?

Mr HAMPTON - No.

DEPUTY CHAIR - Where are we at the moment?

Mr HAMPTON - Again, I will ask Christine to expand on it, but we went live with our new billing system on 1 February. We have not made a lot of publicity about it. We do not wish to make a lot of publicity about it because of the concerns and issues with other billing systems. Staff in call centres now have access to it. When they first had access they could just see it. Increasingly, they will be able to do things on it and the functionality, like any major IT system, is never all there on day one. In fact, you do not plan it to be there on day one, you plan to bring the functionality in over a period of time. Get the people using the system comfortable with a base level of functionality and then expand it and broaden it. What we will see in six months' time will be a material difference to that which we went live with. I would hope that by six months' time we would be largely fully functional. What you might see in 18 months to two years' time is some sophisticated applications being brought to it. So we are not fully functional today.

DEPUTY CHAIR - So you are running a dual billing system at the moment?

Mr HAMPTON - No, we are not running a dual billing system.

DEPUTY CHAIR - Can you explain?

Dr MUCHA - I will explain, and basically the Chairman is right, but in February we went live with what we call phase 1A. Phase 1B at the moment is due to go live in the next few weeks and that is really about working with the call centres so they can interact more and take on a number of the activities we were currently having to manage. Then phase 2, which is by June, is all the integrations with all the systems that you need. We stopped using our interim solution shortly after we went live -

DEPUTY CHAIR - So all the customers are on the new billing system?

Dr MUCHA - Yes, and so the legacy is really picking up all the matters right up until the current system. We are running through and confirming and verifying the data through the new system and it is working quite effectively.

DEPUTY CHAIR - So basically by the end of the next financial year, for example, you expect it to be pretty well bedded down and you might start doing add-ons by then?

Dr MUCHA - Yes.

DEPUTY CHAIR - This financial year not quite so?

Mr HAMPTON - Not quite so.

Dr MUCHA - The important thing about the add-ons is they will only be done if they work out to be cost effective. One of the things that we have managed very tightly is that we decided to start off with a Vanilla product and build on that otherwise we would never have got anything up in time. We also had to be conscious of the price because the community has to pay that so why go to something beyond what we need to do for service.

DEPUTY CHAIR - If, for example, we were to recommend to the Government that it become less prescriptive as far as Onstream is concerned, and also potentially eliminating the board and revising the corporate structure, what time frame would not create a shock to the organisation? If we were to say that they should do it tomorrow obviously there would be no time for planning on your side. Is it better that it be sooner or is it better that it may take effect from 1 July this year or 1 July next year in order for you to plan such activity, given that we would need legislative change as well which is not going to happen overnight?

Mr BEST - They have just got the thing up and going.

Mr HIDDING - It is your own recommendation.

Mr BEST - Yes, I know.

Mr HAMPTON - Each of the four corporations has their own CEO and has a competent and experienced management team. The board at Onstream is there simply from a governance point of view and for overall strategy and direction. As you have gathered, we have actually steered that. We have not just sat there and accepted it. We have done our best to steer it within the confines of the legislation and regulations that prescribe us. My view is the sooner the better.

Mr HIDDING - What would be the cost savings from a model such as the chairman has just alluded to? In other words, what are the costs of the board? How many outsiders are on this board and not currently in the corporations?

Dr MUCHA - Three, and I think we worked out last night it was about \$68 000.

Mr HAMPTON - The additional cost of directors is less than \$70 000. The governance saving is not the real issue; the real issue is the individual corporations having, in the

same way we have talked about our councils not feeling ownership and the regional corporations being free to determine which path that they want to go down. If they chose to exit billing, which I think is unlikely, but if they chose to go down that path then they would want an orderly transition. That orderly transition might be a two-year time frame, whereas there is no reason why the governance arrangements could not change fairly quickly, and a prescription.

Mr HIDDING - One of the central reasons for water and sewerage reform in Tasmania was the fact that 29 different units were doing 29 different things. The Government wanted to bring them all together and then it morphed out to three separate corporations. However, there appeared to be some logic that certainly with technical matters there would be a corporate view around Tasmania. In my electorate of Lyons there was one on the east coast. One engineer had his favourite small package plant - an Italian plant - for \$1 million. It was just the fix for Scamander, whereas down the road there was another council who had an almost identical issue and his favourite by a long shot was a completely unrelated plant that cost \$2 million. That is just the way it was. That is what the engineer says so that is what the council has to run with. If we were to decorporatise, how much central logic remains or is that already out the window? Cradle Mountain Water, for example, can choose another billing system from somewhere and an entirely different thinking on pump systems, water and sewerage management and so on.

Mr HAMPTON - The reality is that Onstream is not providing input - the equipment side of it is not in the policy development. I wouldn't like to drift into the reasons for the reform but I think I have already said that one of the real pluses is that on a regional basis we are looking at regional solutions.

Mr BACON - Would statewide solutions be an improvement?

Mr HAMPTON - Perhaps in the fullness of time but given the scale of the work that's to be done at this point in time I don't think it would be appropriate.

Mr HIDDING - But aren't we just talking about cultural matters here? For example, the north-west coast has a problem with headworks charges so we need to tread carefully. Isn't that the problem, that we can't have one statewide view on headworks and development charges? Aren't they just cultural issues?

Mr HAMPTON - No, I don't think they are cultural because there are operational issues that are quite different. The solutions to the various issues in the north, south and north-west that have evolved over time are quite different. The expertise is regional, so finding a regional solution to a problem is a better solution, say, in the south than having 12 different solutions. We are part-way down the track. Going to 29 different solutions would be challenging in the short term. One of the areas that we have been criticised on by our owners is that they don't think we have ramped up our capex programs as fast as they might have understood.

Mr HIDDING - Or that they would have us believe they would have done.

Mr HAMPTON - I won't go there.

Laughter.

Mr HAMPTON - They have criticised us. Sitting across the three regional corporations, it is really challenging. The time frame to get the momentum going: my view would be that if you're trying to do that in one corporation now the time frame would be even harder; we would be even more challenged.

Mr HIDDING - It was put to us in the development of the policy that eventually came to Parliament in the form of legislation that one of the reasons we needed reform was that there were 29 different views and that if we went to the three-corporation model we would resolve those matters of different thinking on different technology by having common directors. Do you see a common-director model as having any control at all over favourites - the northerners like this kind of technology so let them go that way? Does the common-director model allow a common director to say, 'Why is this costing so much? Why are you going this way? In Hobart we know they went this way and we think it's cheaper.'? Does it come down to that level of management by the common directors?

Mr HAMPTON - First of all, when the common director sits on one board they are just a director. There might be four common directors there and two regional directors, but they are there for that corporation. If that corporation's CEO brings forward a preferred approach, then obviously the board would test it. Those who are aware of different approaches in the other corporations may want that CEO's preferred approach tested against those, but may well still land on that CEO's preferred course of action, even though in another region where they sit as common directors they would land with a different solution. Boards by and large, with appropriate checks and balances, like to give management the sense that they're the ones who are bringing forward the proposals and solutions that will be appropriately challenged and questioned.

Mr HIDDING - You're saying there is protection under the common-director model of intellectual property learned at one corporation, or two other corporations, that the common director can bring into play to have a proposal tested against those because he or she has learned that elsewhere? What I am testing is whether this common director thing is just a load of nonsense.

Mr HAMPTON - First of all, as Christine has alluded to, there is a CEO forum where the CEOs meet every month and they cover a diverse range of subjects when they meet. Below the CEO level there are technical groups across the State that work together to talk through what solution they have to this or that problem and, indeed, it is probably far better that the solutions be worked bottom-up rather than be top-down driven. I can see that some may argue that having common directors might mean that you have a more consistent approach across the State but I think it is more a matter of making sure that we get the best solution for the particular part of the State and that does not need common directors. What it does need is a balanced board with appropriate skills and experience.

DEPUTY CHAIR - Is it true that at least part of the cost of having those common directors is the lost opportunity of having more input from people selected because the directors would be selected by the owners?

Mr HAMPTON - The directors may be selected by the owners but I think the issue of input comes down to the rep model and it is not an input to individual directors that is

appropriate, it is a communication from the owners to the board and at the moment that is through three reps as distinct from a rep from each corporation, which I have already commented on.

Mr BEST - That leads me on to the next question about executive management strategy and development.

Mr HAMPTON - Sorry, can I just go back to make one comment. In relation to the boards and the costs of the boards, if there were three corporations and no Onstream board and you had the board of the right size - at the moment we have six because we have four common and two regional - my own view is that Hobart Water, a board size of five, worked very well and if you did the arithmetic, I would think that the aggregate board fee across three corporations with a board size in the regional corporations of five would approximate the same board fee that might be applying today.

Mr HIDDING - Thank you, I wanted that.

Mr BEST - I am interested in executive management strategy development and in particular where you have talked about identifying business development opportunities and driving innovation within Tasmanian water and sewerage. You have here, 'The division has undertaken a range of projects to assist further development'. I am wondering what those might be regarding the building on existing systems and process. I think there is some mention of geospatial knowledge.

Dr MUCHA - Basically part of that group, which I alluded to earlier, was also about doing that work on the Bureau of Meteorology project across the corporations with the water quality data. That was one of them. The other one was the spatial information system which we have now been developing with the corporations because they are seeing it as a useful forecasting tool as well as it fitting in very well with the metering project so we can do some spatial data and information quick-checking and for the implementation of the meters, linking it to the call centres so the call centres can see what meters and what stage they are at particularly, as you know, people are being told that meters will be installed on this particular day so people can ring up. That is part of the spatial information.

We have also been doing a bit of work with the State Government on that because a lot of their databases are basically the ones that are utilised by the water corporations but also they see some merit in a spatial system where you can go in and gather different bits of data and build a picture like a map. That is one of the things we have been doing.

The other thing is that we do provide support and services where needed, particularly in business analysis. We have needed those resources as well to help us with the revenue services and also building our service level agreements with the corporations. It is an interesting one; there is no fine line between the corporations so if someone needs a particular support, we will provide that support or we will help them acquire that support, particularly with the metering project.

Ms PILLANS - Can I summarise what Christine was saying there with an example that was quoted to me by one of the CEOs the week before last. It goes back to your point about head office and direction. We do not give direction. His comment was: 'We

come to you with problems and you send us back solutions.' That is really what we see ourselves doing. They come in with challenges, they come in with opportunities and we throw it around and say, 'Okay, these are the sorts of things that we could examine'. So problems come to us, solutions go back to them is how they are viewing the way that Onstream operates for them.

Mr BEST - We have heard in particular that each region has its own set of circumstances. I suppose there would be some commonality; even though there are separate issues, you are trying to bring about common solutions in some ways.

Dr MUCHA - I think it is also - and I think this was part of the reform process as well - about being able to share ideas cost-effectively. For instance, obviously Southern Water is a very large corporation by nature of where the population is but the other corporations could share some of those benefits, which is what we are doing, particularly with IT. Do the corporations want that? Yes, they do because obviously they have drivers to be cost-effective as well. So they are looking at what is the best cost-effective solution.

Mr HIDDING - In five years' time, though, when the sting has gone out of their need for the billing service because it is there and everybody is blasé about it and their growing need for IT services and what have you, what happens then? I can see in this transition thing there is a bit of a honeymoon right now, everybody needs everybody and it is all working all right. Where does it go when it is all sorted? That flows to my next question. If Onstream is all about IT platforms and billing, what is this IT stuff about? Do we know what it is about? As we have Mr Beswick over there, I wonder whether we could get a five-minute overview on the scope?

Dr MUCHA - If you are comfortable with Andrew speaking; I don't know.

Mr HIDDING - You could do it and Andrew could provide you with advice, if you need it.

Dr MUCHA - I certainly could do it but Andrew might feel frustrated if we do not give him the chance to say it. Andrew might like to talk about the IT strategy that is being building with the corporations that moves it three to five years on anyway.

Mr ANDREW BESWICK, CHIEF INFORMATION OFFICER, ONSTREAM, WAS CALLED, MADE THE STATUTORY DECLARATION AND WAS EXAMINED.

Dr MUCHA - Andrew is the Chief Information Officer and provides the guidance across the corporations.

Mr HIDDING - What do you blow \$5 million a year on, mate?

Laughter.

Mr BESWICK - A combination of things. The provision of the IT hardware, the servers to run the various IT systems on, including the desktop computers that everyone uses.

Mr HIDDING - Are your servers all here in Hobart?

Mr BESWICK - No. Production servers are in Hobart, disaster recovery servers are replicated in Launceston and that provides full disaster recovery for the application of running our core data centres. There are also some small regional servers that are at each of regional corporations which provide access to information in terms of speed and performance and so it funds all the desktop computers, a fleet of those. It funds the software licences for the different software systems that the corporations use, most of which are common, as the major ones are. It also funds the human resources and provides help desk support for the use of those systems and hardware, and finally, the communication links that connect people to those systems and servers.

Mr HIDDING - Do you deal with a principal adviser? I take it, from what I read of you, that you came from up the coast?

Mr BESWICK - From Burnie City Council.

Mr HIDDING - You have strong skills in this area but do you use a central advisor as to what systems you should be using? What's the base of your system?

Mr BESWICK - It's a Windows platform. We use MS SQL as a database server environment, as opposed to Oracle which is another major one. That is the basis of our environment and they are basically virtualised servers that we have in our core data centres. It is quite state-of-the-art in the type of configuration that you would expect.

Mr HIDDING - In terms of dollars, it is a lean, mean -

Mr BESWICK - It is certainly what I would consider appropriately scaled for the size of our corporation customers.

Mr HIDDING - Is the expenditure right now high because you're bringing the whole thing in new? Where do you see yourselves in five years, other than replacement of hardware and continued development of software? You would have a picture in your mind. Is it going to be \$5 million recurring?

Mr BESWICK - I think it is likely to be at least that or in fact an increase on that because the pattern of development in IT has been an increasing dependence on and development of it in businesses. In that cost there is an upward pressure in terms of the number of services. What counterbalances that is the cost of IT services is declining in terms of the cost of hardware. What you get for your money is improving all the time, so there is a counterbalance there that is happening.

Mr HIDDING - So it is getting cheaper?

Mr BESWICK - It gets cheaper on a per unit basis but you do more units of power because you're doing more with it.

Mr HAMPTON - Andrew alerted us to various segments of cost, so would the committee to see that broad categorisation, maybe the hardware, people, software - just maybe four or five broad categories?

Mr HIDDING - It's a very contemporary snapshot of how a modern business has to operate.

Mr HAMPTON - I make the observation that in terms of billing to the regional corporations that is there for the current financial year and that which we are looking at for next year, which we are presently in negotiation left-hand to right-hand as to what they will be, we are at about a 1 per cent cost uplift in IT in the short term. That is reflective of a number of circumstances.

We can provide the break-up and we will do our best to show it in a comparative year-on-year basis.

DEPUTY CHAIR - Thank you, that will be great.

Mr HIDDING - In terms of IT, is the call centre an IT child or a separate entity?

Mr BEST - No, the call-centre platform is provided by our IT and solutions division, so effectively the telephony services are provided through our division, as well as the particular call centre software.

Mr HIDDING - Did you develop that software yourself or is that a package?

Mr BEST - No, that is being purchased. It is leased at the moment.

Mr HIDDING - So call centre staff belong to which division?

Dr MUCHA - They belong to each of the corporations.

Mr HIDDING - You were saying that if they are busy in one they will rotate off to another. How does that work?

Dr MUCHA - Say, for instance, the call centre of Southern Water might be caught up because there's a break and everyone is ringing in, but there are also people who may have queries on accounts so that could then switch to Ben Lomond Water, if they chose

to do that and had that arrangement with Ben Lomond Water. That is where we are talking about the switching and sharing of services.

Mr HAMPTON - But equally, say, in Southern Water if the person in charge of that area needed some additional human resource, he may be able to pull some resource out of accounts payable or another part of the business who have been skilled up in answering the calls. That was significantly the driver for the CEOs believing the call centres within their operations were better, that they would optimise the use of staff.

Mr HIDDING - Mr Chairman, that brings me back to the issues that were put to us as to why we should centralise this business of water and sewerage in Tasmania and then why it should go out to three models and now we are considering the various models. There are obviously some people who have various things in mind already as to what might happen and we discussed that if one of the three regional corporations wanted to do something entirely different with billing, they might do so. It is not beyond the realms of possibility that within five to 10 years' time they could be so different that they do not have any synergies to be able to work together in terms of call centre revolving and that kind of thing. What I am trying to get a handle on is, if there were three completely separate organisations all with CFOs, all with their own boards and no common directors, how long it would take for us to have the 29-sector model become the three-sector model so that we have the same issues and problems? How do we get the best of both? I think everybody up north wants to control their own destiny but how do we actually maintain the best of common thinking and synergies?

Mr HAMPTON - The best way of looking at that is probably the new system that we have for billing and it is called Gentrack. I could go into that but Gentrack sits on our IT platform. We have purchased one set of software, it has been run across the three corporations effectively by Onstream for the corporations on the Onstream IT platform. If the board of Cradle Mountain Water decided that it wanted to explore whether or not it should do something itself presumably it would get a price from somebody else and Onstream, with the shared services CEO, would provide a price for those services and then the CEO of Cradle Mountain Water would make a decision as to what they would recommend. In a completely stand-alone model it would be their decision and, in my judgment, it ought to be their decision because it puts back competitive tension onto Onstream.

Mr HIDDING - This competitive tension is an interesting concept and it is the argument against silos to a degree, but I will give you one example of 15 years ago when we were in government. There were communications for police, ambulance and fire and we would actually have saved money and so much expertise if they all had the same system. They could firewall each other, but still have the same system. Not in a million years - not then and not now - will there ever be the same system for our three emergency services. And the State Emergency Service - different again. That is expensive, clunky and poor management. You simply cannot break down the silos, though, because of the culture within the public service, not until somebody actually waves a big stick and says that -

DEPUTY CHAIR - Don't give people ideas.

Mr HIDDING - within 10 years there will be, because you need to see contracts offered and all that sort of stuff. That is what I am concerned about - that kind of thinking that the regions can do their own thing. Let us say that Cradle Mountain Water goes and gets a price off someone else - we had that argument in Parliament last week, getting a price or going to tender on something means that if somebody else wins it that is where you go because that is what good business tells you to do and, suddenly, we lose the synergies.

Mr HAMPTON - If it is done cheaper maybe you have gained some synergies in an aggregate sense and yes, there is the issue it might be economical for one to move but if two move it drives up the cost on the other side and I understand that. In relation to what might happen down the track - and again Christine and Andrew might be in a better position to expand on this - pre our coming into existence, as I understand it in the south, Property Wise, who are owned by Brighton, were providing billing services to a number of councils and Burnie was a billing hub for a number of councils. The translation and I think the parallel is there. In that case, the 29 councils were happy with the solution that they had; then it continued and probably would still be doing so today if we had not come along. I would expect that because you are only having to deal with three corporations, the opportunity for that to continue for IT and billing and whatever other services are most cost-effectively done on a joint basis.

Mr HIDDING - But you do admit that on that scenario of there being three stand-alone, separate regional models, if one took its billing elsewhere it could substantially drive up the cost for the other two corporations without their having any control over the fact that one other walked. Then it could in fact become non-commercial.

Mr HAMPTON - The reality is, if our billing costs are \$5 million, and they are \$2.5 million to the south - let us leave IT out of it for the moment - and \$1.5 million in the other regions, then yes, if Cradle could do it for \$1.2 million and decided to go its own way to save \$300 000 year, if they could. One would hope they would give Onstream the opportunity to see what it could do to take costs out because if we think we have an efficient platform then we should be competitive. I do not think there is any doubt that in the fullness of time there was an expectation that maybe Onstream might provide more activities for councils, and billing was the most logical area.

Mr HIDDING - Are you supposing, for instance, that Cradle Mountain Water - owned by the north-west councils - would give any consideration to what it would mean to the other two organisations in giving Onstream the opportunity to do whatever? There was never any evidence of that in the past. In fact, it is a statewide sport to do the other lot over.

Mr HAMPTON - I would not propose that. But if in my scenario Cradle Mountain Water were able to get their services at, say, 20 per cent cheaper through a third party, one would also think that then Ben Lomond Water and Southern Water could probably do the same.

Dr MUCHA - It is one of the things that we can get caught up in, just purely on cost efficiencies. When you see a tender, whatever the tender is, there are a lot of measures in there - quality measures as well - and there are performance measures and there is risk management. You would expect that the corporations would with any of their tenders, whether it is a capital project or billing, look at all those elements. It would not just be

about what is the cheapest. They would also have to look at what risks they would be wearing. So on that basis, Onstream would tender exactly the same as the others and you would give those elements. If Onstream could not meet all those elements but another provider did, that would be it because then you have had a robust analysis of the actual activity.

Whilst we talk about opening up and looking at commercial competitiveness, what we do as part of our commitment in moving into this current year but also next year is work out performance measures with our clients. So we do have performance measures and we are building more - basing it around benchmarks. So whilst, yes, you are opening it up to competitiveness, I just want to make sure that when we talk about 20 per cent savings that is assuming this is not the case now. In fact, I think in a number of these areas we are probably quite competitive when we take the four elements - the risk, the cost-effectiveness, the quality of the services and the other performance measures.

DEPUTY CHAIR - You just have nothing to compare it with back there except 29 councils doing their different things.

Dr MUCHA - That is right.

Mr HIDDING - That was a good briefing on the IT thing. I understand now what they do, so thanks for that.

Mr HAMPTON - I would like to make a couple of closing comments specifically in relation to Onstream. We know it's on the record that some councils don't believe Onstream should be there at all. It is also on the record that some councils think the recommendation of the boards is the appropriate path, at the discretion of the regional corporations. We respect those who have the 'no' view just as much as respect those who sit on the same page as we do. One of the things that needs to be understood is that most common service activities evolve from existing corporations and that's why they are successful. Where councils have chosen to have a common services approach in the past, they have made a conscious decision and have had ownership of handling the internal ramifications of the restructuring that goes with it. Our common services with Onstream was imposed, so there was no ownership. It was coming at a time when the real owners of the businesses were feeling quite disenfranchised. My own view is that a number of the comments critical of Onstream were reflective of both the overall upheaval that occurred in the space and a lack of understanding of what Onstream was doing. We have been quite open in saying that I don't believe Onstream is as efficient as we would like it to be, but to the extent that it is inefficient it is reflective of the circumstances of our being thrown together. The board and management will work to take that out until our circumstances are changed by those who might want to change them.

Common services are a challenging space. It is most often best evolved from within rather than from without. We were evolved; it was just put on the table that this will happen. I think the four corporations have made a reasonably good fist of it in the circumstances. I have given examples of where we have tried to optimise solutions that didn't quite work from the prescription, and we will continue to do that. My own view would be that in the fullness of time, given the opportunity to either use the services of Onstream or not, I would be very surprised if the core activities don't stay on a shared-

services basis. Even if there is a cost difference, with the other factors that Christine alluded to I would be very surprised of it did not swing it back.

Dr MUCHA - I will just add to Mr Hidding's question as to why I did it: it was a challenge.

Laughter.

THE WITNESSES WITHDREW.

Mr GLENN APPLEYARD, REGULATOR CHAIRMAN, AND **Mr DEAN BURGESS**, ASSISTANT DIRECTOR, THE TASMANIAN ECONOMIC REGULATOR WERE CALLED, MADE THE STATUTORY DECLARATION AND WERE EXAMINED.

DEPUTY CHAIR (Mr Morris) - Gentlemen, thank you very much for coming and giving some evidence to us. Would you like to commence, Mr Appleyard, with an opening statement perhaps and in particular fill us in on exactly where you fit into the picture of water and sewerage reform?

Mr APPLEYARD - Thank you very much, Mr Deputy Chair, I am happy to do that. I have with me Mr Dean Burgess who is Assistant Director in the Office of the Tasmanian Economic Regulator, who will be assisting me with the more technical and complex issues.

The regulator's job is to administer the economic regulatory framework for the sector as set out in the Water and Sewerage Industry Act and its regulations. The objective of economic regulation is to ensure efficient outcomes that would be reasonably expected from a competitive market thus avoiding monopolistic behaviour.

The key elements of the economic regulatory framework under the industry act include an independent economic regulator for the sector. I should point out I am the Chair and there are in fact two other members who form the Tasmanian Economic Regulator but for the purposes of discussion, I often get saddled with being the regulator but I am in fact the Chair and there is a panel of three.

Mr HIDDING - If you would not mind, so that we get a complete picture, you are not a public servant?

Mr APPLEYARD - No, I am appointed under the legislation and I am a part-time position.

Mr HIDDING - And you have come from the private sector to do that?

Mr APPLEYARD - That is correct. I wear a few hats, Mr Hidding. I was a bureaucrat in a past life but more recently, for the past 10 years, I have been a private sector consultant dealing with public finance issues. I hold a position of member of audit committees for a number of government institutions, including the University of Tasmania. I am on the Accounting Standards Board of Australia and I am a member of the Commonwealth Grants Commission.

Mr HIDDING - Who are the other two on your panel?

Mr APPLEYARD - Mr Peter Hoult, who is probably known to the committee, formerly the Secretary of the Department of Health Services, and Justice, and Chair of the Gaming Commission.

Mr HIDDING - Is he independent as well?

Mr APPLEYARD - Yes, he is.

Mr HIDDING - The same status as you?

Mr APPLEYARD - Yes, indeed. The third member is Mr Alan Smart who resides in Canberra and who has a long background in issues of economic resource pricing and so forth.

The key elements of an independent economic regulator for the sector: we conduct a licensing regime, a customer service standard framework, we undertake price regulation, compliance and performance monitoring and reporting, and complaints handling and dispute resolution. Both the industry act and the draft pricing regulations include a requirement for the regulator when making a price determination to take account of changes in prices upon customers. Therefore the regulator will be required to balance price reform objectives, financial positions of the corporations and regulatory compliance improvement against the need to manage the price impacts upon customers, and some might say 'the wisdom of Solomon' but that is what we are charged to do.

The regulator is not, however, responsible for wider affordability issues such as support for those in socioeconomic difficulties. The economic regulatory framework complements other industry regulators such as for public health, drinking water standards and environment and dam safety. There are independent regulators for those tasks.

Decisions made by the Economic Regulator have been and will continue to be informed in consultation with those other industry regulators and we have a strong consultative arrangement where we meet regularly with those people. However, each industry regulator maintains its own statutory responsibilities and independence.

The industry act sets out a number of reform objectives, including achieving full cost recovery, but does not dictate any time lines for that to be achieved.

The significant challenges facing the water and sewerage industry have, as you are no doubt aware, developed over many years, if not decades. The need to manage price impacts upon customers, along with financial and practical considerations associated with required capital expenditure, means that it is likely to take a similar time to fully reform the industry. Just as an aside, Victoria commenced on this task perhaps 10 years ago and I think still has some distance to go. Therefore for some time the regulator will be required to balance off on competing reform objectives when undertaking price and service regulation.

Under the industry act, price regulation is to be undertaken on a propose-and-respond model. That is, the corporations will present to the regulator price and service plan submissions in line with the requirements in a price and service plan guideline which the regulator will issue. Those guidelines will stipulate what matters are to be addressed in the price and service submissions, what supporting information and analysis is required and what other requirements there are for prior consultation with customers and other stakeholders.

Once the price and service plan is submitted, the regulator will then undertake analysis of the information and prepare a draft determination for public consultation. After the public consultation there will be a final price determination.

The price and service plan guideline will be subordinate to the requirements in the industry legislation and the regulations and therefore we cannot yet issue the price and service plan guideline until the pricing regulations are finalised, and the committee would be aware that those draft regulations are out for comment at the moment. I think the closing date is later this week.

Can I touch on the likely approach that the regulator will take to price regulation. We have a number of options available under the industry act in terms of what approach to take to price regulation but given the current level of under-recovery across the sector and the need to manage price impacts upon customers, it is likely that prices will be determined by side constraints on price movements. This differs from a mature environment where permitted revenues are calculated through a build-up of efficient costs and regulated returns on efficient asset values and depreciation - for example, the process we go through in relation to determining maximum MAIB premiums. That is a process that has been in place for some 20 or 30 years and there is a regular process by which the regulator sets a maximum revenue cap under which the MAIB operates. We are not yet at that stage in relation to water and sewerage.

Nonetheless, the regulator still intends to conduct a building-block approach to determine what full cost-recovery levels are as this is in fact a legislative target under the act. So that is a step we will be doing but, clearly, we will identify that as what is necessary under full cost recovery. However, the focus of the initial price regulation is likely to be limited to constraints on price movements themselves.

The regulator does not intend to specify in the price and service guideline any particular structure or quantum of constraint on price movements. Such constraints will depend on negotiations between the water corporations themselves, their owners and other industry regulators and are to reflect an appropriate balance across the reform objectives. However, given these competing priorities, it is considered that the regulator should specify price reform guidelines for the first determination to reflect any mandatory legislative requirements or matters that are of high priority in terms of building a base for future price reform.

DEPUTY CHAIR - Just to clarify, the first determination will begin on 1 July next year?

Mr APPLEYARD - In 2012, that is correct.

DEPUTY CHAIR - When does that expire; is that three years?

Mr APPLEYARD - It is a three-year price determination.

Whilst still needing to be subject to public consultation, and I emphasise that the regulator goes through extensive public consultation with all of its papers and transparency in terms of publishing draft reports on its website, it is considered that price reform proposals for the first price determination should address the following objectives: at a minimum, achieving a level of revenue that will support the viability of the corporations during the pricing period, and in our most recent state of the industry report you will be aware that we made some comments regarding the longer term financial viability of the corporations. Secondly, achieving two-part pricing for water as from 1 July 2012 -

Mr HIDDING - For the record, what are you referring to?

Mr APPLEYARD - The reference was to the state of the industry report.

Mr HIDDING - So you're back onto this list that you are going through?

Mr APPLEYARD - These are my notes, Mr Hidding, which I am happy to provide later.

Mr HIDDING - That's fine. I was wondering whether you were reading from a Treasurer's Instruction or something like that?

Mr APPLEYARD - No, these are briefing notes which the staff have ably prepared and which focus on some of the issues we think should be put forward in our price and service guidelines. Once the regulations are concluded we will publish those price and service guidelines.

I mentioned the minimum revenues which will maintain viability: achieving two-part pricing from 1 July 2012; transitioning customers to a rational price structure, not necessarily fully cost-effective; preventing any increases in the extent of current cross-subsidies between customer classes; and, importantly, managing the impact of price changes upon customers.

The following price objectives would be considered secondary priorities at this stage, whilst desirable to work towards during the first price determination and will require additional time to fully achieve: that is, achieving full-cost recovery; unwinding all the cross-subsidies between customer classes; achieving fully-cost-reflective prices, and providing full commercial returns to owners. They are secondary priorities, unlikely to be achieved in the first price determination.

The outcomes of the need to manage the impact on customers in conducting price determinations could include some of the following: a lower commercial effective rate of return for the corporations, deferral of increases in dividends to the owners, deferral of regulatory compliance improvement in relation to public health and environmental outcomes, or delays in unwinding the existing cross-subsidies. However, it is important to note that these are not likely to be levers that the regulator will be using but rather outcomes from the negotiation process which will be undertaken.

It is proposed that the corporations will not only be required to put in preferred price constraint proposals but also identify options and their ramifications in terms of the outcomes listed above, relative to the preferred option. This information will also be subject to a public consultation process. The final price determination will require some valued judgments on behalf of the regulator on what the appropriate caps on price movements may be. This decision will be informed by the ramifications of alternative price proposals, as well as community input on all matters.

I will touch briefly on managing the impact of the end of the transitional period. The advice that the regulator provided to the Treasurer in 2010, which is on our website and which the Treasurer has instructed us to make public, amongst other things identified that the 5 per cent price caps combined with the cessation of government assistance after

2011-12 was likely to increase the pressure for price increases after that time, or delay the time by which full-cost recovery could be achieved. It is considered that the best way to manage this issue would be for the IPO to be amended to replace the 5 per cent price caps with alternative price constraints from 1 July 2011. This would enable price reform to commence a year earlier and would prevent another year of increases in the difference between the revenue required by the corporations and the revenue collected from customers. The quantum of any alternative price cap will depend upon a range of matters, not least of which would be any renegotiation of the quantum and timing of the assistance to be provided by government. That is not a matter for the regulator.

Mr HIDDING - How much of what you have just read out, the scope and task you have, has any settings controlled or advised to you by government? What that goes to is how independent are you when you first took on this role or when water and sewerage was first brought into being? Were you given any guidelines or any settings at all?

Mr APPLEYARD - Only the legislation which came from the Parliament, Mr Hidding.

Mr HIDDING - No Treasury instruction of any note?

Mr APPLEYARD - No. We are truly an independent regulator. The next step will be the determination by government of the pricing regulations.

Mr HIDDING - An independent regulator acts as the market, do they not?

Mr APPLEYARD - Attempts to mimic the market. If we were acting as the market it would all be very simple. In essence you are correct. We try to mimic the market which is absent in a monopoly situation such as this.

Mr HIDDING - Bearing that in mind, what was behind your target to go to full-cost recovery pricing, although you did say there were no time lines so there is not in fact a target?

Mr APPLEYARD - That is correct.

Mr HIDDING - What you are saying is that we must go to full-cost recovery because that is a given. As soon as possible?

Mr APPLEYARD - No. In the legislation, as you would know, one element talks about moving towards full-cost recovery. There is no time frame. As part of our investigations through providing advice to the interim price order and in this first price setting clearly we think it is sensible to see what is required to achieve full-cost recovery, but a timetable is not part of our brief.

Mr HIDDING - Are you leaving that to the corporations?

Mr APPLEYARD - No. Clearly, we have to achieve a balance between each of those elements that I spoke of that is set out in the legislation.

Mr HIDDING - I suppose I should cut straight to the question that is probably higher in my mind. Who demands from a regulator, which is supposed to mimic the market, price-shock management? Someone like me who has been in this job long enough knows that

it is politically most unpalatable to a government when there are price shocks. Why should an economic regulator involve himself or herself in price shock management?

Mr APPLEYARD - Because the regulator is obliged under the legislation to have regard to the impact on customers. It is one of a number of elements to which the regulator has to have regard. There is no indication within the legislation as to whether we give that 20 per cent weight, 50 per cent weight or 100 per cent weight; it is one of a number of elements referred to.

Mr HIDDING - For instance, Metro operates as a government-owned enterprise and it provides a whole raft of subsidies to its customers because those customers demand such - so the aged pensioner has a very cheap fair - but the Government pays an amount of money annually to Metro for those subsidies. That accepts that there is a political cost to not doing so, or there is a social cost in not doing so. They actually write the cheque. Is there not a case for the Government of Tasmania to somehow seek to provide the means by which you could up with some price-shock management?

Mr APPLEYARD - That, Mr Hidding, is a matter for the Government and not for the regulator.

Mr HIDDING - And in the absence of which you need to make your -

Mr APPLEYARD - The regulator has the task of divining between each of these objectives which have been set out in the legislation which the Parliament has given us.

DEPUTY CHAIR - When the original determination was made to accept the 7 per cent or 10 per cent increase as a cap in order to manage price shocks, and then finding that when that 10 per cent flow-through occurred that people identified it as a price shock, how do you think that is going to impact things? Was that a surprise to you, firstly, because the other option was going to 15 per cent annual increases to try to lift the revenues, the lower order was accepted but even that, at least out there in the public, appeared to be a significant price shock and then of course we saw government move in with a 5 per cent subsidy because they must have recognised a price shock as well. How does all that factor in where we go forward in terms of raising revenues from here on?

Mr APPLEYARD - When we undertook the first advice in relation to the interim price order, the one that had the indicative level, I would make two comments. Firstly, the data on which that initial advice was based was -

DEPUTY CHAIR - Preliminary?

Mr APPLEYARD - Preliminary is perhaps the politest word I can apply to it, incomplete, inconclusive because it was -

DEPUTY CHAIR - And not entirely accurate, in hindsight?

Mr APPLEYARD - And not entirely accurate. It was bringing together the best data that we could garner from the 29 existing municipal water and sewerage operations as well as the bulk water authorities. Nonetheless, the size of the under-recovery within the industry was of such proportions that even allowing for variability within the data, it was still

quite clear that there was significant under-recovery and had been for some time and that to get to the nirvana, the national objective of full cost-recovery, was clearly going to take a long time under current pricing arrangements. So it is not as though when the regulator first looked at the water and sewerage industry the regulator discovered that the difference was of the order of 10, 15, 20 per cent, that margin, it was closer to 50 per cent recovery.

DEPUTY CHAIR - That is right.

Mr APPLEYARD - From that point of view, clearly there needed to be drastic action going forward. The Government, as we know, took steps to impose price caps and that is what we have been operating under for the past two years. Where it goes from here is, as I say, a matter for government.

Mr BEST - Do you take into consideration the cost of living, people's ability to pay?

Mr APPLEYARD - No, as I mentioned, Mr Best, socioeconomic impacts are not something that we take into account. But, having said that, whilst we do not specifically look at issues in relation to disadvantage, we do look at impacts on customers per se. If I can put it in the sense that if the regulator were to say we must get full cost recovery and we must do it in two years, the price shocks would be such that any sensible regulator would say that these are too great price shocks for customers because they are way and above the cost of living. If, however, we said that we ought to take 100 years to get to full cost recovery, I think people would say, 'Are you serious about reform within this sector?' So it is a judgment for the regulator, weighing up each of those elements as to where we go.

Mr BEST - We had the Tasmanian Property Council in here and developers and we had an interesting submission from Mr Rockefeller who said that it is very important to get this right - that is, the capital works that need to happen to make things more competitive. He used scenarios with shopping centres in Tasmania and I think New South Wales or somewhere and how much per square metre and all these sorts of things. His view was that to bring this in you are better off to do it in a framework that might take 10 years to balance it out across the residential-commercial, if that means getting it right and it sets Tasmania up to be competitive from a development point of view. I suppose you do not really want to comment on that, do you?

Mr APPLEYARD - I look forward to receiving Mr Rockefeller's submission.

Mr HIDDING - I have a question, as it happens, on precisely the same thing. To finish what Mr Best was saying, he did in fact say that he felt that it was likely that the Property Council would agree to a 10-year transition before they received the full benefits of the policy change. But it seems to me that if a parliament makes a policy change, then it is a good thing for the regulator to try to manage - and obviously it is a mandated job, as I have learned from you now; you reminded me - the upward price shocks. But what about the expectations of those people whose prices will come down? If for years I had been paying far too for much water, in my opinion, and finally the Parliament of Tasmania passes legislation which will radically change the equity levels over who pays for water, who gets to choose that it should be a 10-year transitional period? Is that something the Economic Regulator can do? Has the Parliament not said there should be a policy change?

Mr BACON - There was no time limit in the legislation, and as three people who voted for it I think you were to blame.

Mr HIDDING - We all voted for it.

Mr BACON - Not me.

Laughter.

Mr HIDDING - He likes to point out that it would have been different.

I think that is a key point for me. For those people who are going to benefit by the removal of the inequities -

Mr BEST - You're saying that it's social disadvantage again but on the other end, isn't it.

Mr APPLEYARD - I understand your point, Mr Hidding. In fact, one of the things we have said we will have a look at is that of preventing any increases in the extent of the current cross-subsidies between customer classes. That is shorthand for saying that we are aware that there should be some winners from this process and that, like all winners, they would like to see their gains as quickly as possible. We think that in terms of any constraint, the situation should not get any worse for them, put it that way. If anything, it should start to improve. The Property Council and the commercial sector can expect to see some improvement. How much improvement we will have to balance against these other elements, which you gave us in the legislation.

Mr HIDDING - Yes, but let us pick a small business that pays \$10 000 a year for water; he has the same business up north and on two-part pricing he pays \$4 000. I don't think those sorts of numbers are out of the question. There can be a certain kind of business that is using a lot of water; it is possible. So he cracks a bottle of champagne when he realises the legislation has gone through. He thinks he is going to get a \$6 000 cut on his water bill. Who chooses?

Mr APPLEYARD - When?

Mr HIDDING - When could he expect it? Who decides when he should get it? Is that the Economic Regulator?

Mr APPLEYARD - Yes.

Mr HIDDING - So it is you who decides when he will get the policy benefits?

Mr APPLEYARD - Yes, subject to the terms of reference, which they don't specify a time frame over. We have to do it and we must balance these conflicting elements that you gave us in the legislation to balance.

Mr HIDDING - What are they, diminished price shock? Where is the head of power which would remove from you the duty to give the person the policy benefit?

DEPUTY CHAIR - Is it not the requirement to move towards full-cost recovery, not away from it?

Mr HIDDING - No, he's going downwards.

Mr APPLEYARD - Section 15 of the act, 'Matters to which the Regulator is to have regard - relevant health, public safety and environmental obligations; promotion of efficient, long-term investment; promotion of efficient pricing for regulated services; the impact of rate of change of prices for customers. It is one of nine elements to which the regulator is to have regard.

Mr HIDDING - So that doesn't just refer to upwards, it could be downwards as well?

Mr APPLEYARD - Yes, it could be downwards as well. You, the Parliament, have given us these nine elements to balance, to come to what in theory is an appropriate outcome, and that is what we will endeavour to do to the best of our ability.

Mr HIDDING - Just to cut to the chase, Mr Rockefeller thought about 10 years would be a reasonable transition. I thought it was overly generous of him and, if I was one of his stakeholders, I would object.

Mr APPLEYARD - I would encourage Mr Rockefeller to make a submission, as we would all stakeholders, because it is only by getting that broad cross-section of views that will assist us in the process.

Mr HIDDING - Do you advertise for those views? Do you write to stakeholders? What is the process by which people can say, 'I have a point of view on this'?

Mr APPLEYARD - Normally with these sorts of price investigations we would advertise in the press and on our website, we would issue a media release which is sometimes picked up in the media. We have, I think, a subscription list of stakeholders that we would write to directly saying, 'This has come out, are you interested in giving a submission?' It is quite comprehensive.

Mr HIDDING - And your advertisement to the average Tasmanian, a small business owner or whatever, the advertisement is in language that he or should could understand and be motivated to make a submission?

Mr APPLEYARD - We would like to think so. We also have a creature called the OCCC - the OTTER Community Consultative Committee - at which there are representatives from most of the key stakeholders so they get at first hand a heads-up as to what is coming up and that includes the Property Council, TCCI, the Small Business Association, the Local Government Association of Tasmania, the TFGA, TasCOSS and Anglicare.

DEPUTY CHAIR - And you and I are not on it.

Mr APPLEYARD - You are more than welcome, Deputy Chair, if you would like to come on it.

Mr HIDDING - And a good thing, I suspect.

Mr APPLEYARD - We do go to quite some length to initiate consultation and submissions.

Mr HIDDING - Who decides what is an appropriate return on capital and in particular who set the current 7 per cent return on weighted average costs?

Mr APPLEYARD - There is a fairly exhaustive process by which regulators go about determining the weighted average cost of capital. There is fairly extensive discussion amongst economic regulators in all States and at a national level as to just what constitutes that. It bounces around 7 per cent, depending on some of the inputs.

Mr HIDDING - If there is that much effort and work that goes into it, it is obviously a very serious and weighty determination because it has ramifications for every business.

Mr APPLEYARD - Indeed, every business we regulate.

Mr HIDDING - In the case of the three corporations that are before us that we are looking at at the moment so many of their decisions come back to being hamstrung by the 7 per cent mandate. What would happen if you could wave a wand and make it 5 per cent? What would happen to the world? Where is the risk?

Mr APPLEYARD - Not so much in relation to these corporations but where others are operating in terms of attracting investment dollars it makes them a less attractive investment for superannuation funds and other legals of this world if they cannot get what is an appropriate return on capital.

Mr HIDDING - Again, in mimicking the market it is important to set that to get the market right.

Mr APPLEYARD - Exactly.

Mr HIDDING - But for these three corporations - and we have had them all before us and they have all got the same chairman but they have different CEOs and different debts and different levels - it appears that the strictures in their thinking come from something that nobody really gets why it is where it is and they therefore wish it could be otherwise. I just wonder why you could not recognise that this is a special market in which it operates - well, there is no competition thus far -

Mr APPLEYARD - No, but there is not for transmission and for some of these other things which regulators look after.

Mr HIDDING - They ought to be special.

Mr APPLEYARD - I understand what you are saying, Mr Hidding.

Mr HIDDING - Is that what you are saying, they all want to be special?

Mr APPLEYARD - They all want to be special but at the end of the day, I think as I mentioned, in terms of our initial price determination the constraint is unlikely to be this

so-called building block approach which has regard to the weighted average cost of capital. It is more likely to be pricing constraints around what people are effectively calling the 'cap and collar approach'.

Mr HIDDING - I think that is true so that is number one but everybody gets that. Everybody knows you cannot wave a wand and have the pricing structure that you want, there is going to be a transition before you get there. But this 7 per cent does appear to be somewhat arbitrary.

Mr APPLEYARD - I would not say 'arbitrary', it is fairly carefully calculated.

Mr HIDDING - Yes, it is carefully calculated but is it arbitrarily applied in this case?

Mr APPLEYARD - Sorry, I do not follow you. If it is carefully calculated it is not arbitrarily -

Mr HIDDING - I understand that a bunch of regulators sit around and gnash their teeth at what it should be, whether it should be 6.3 or 7 per cent or whatever, and you can come up with 7 per cent but clearly it is important that you people have sat around and talked about that but why is it important to the people of Tasmania that our three corporations operate at 7 per cent rather than 5 per cent?

Mr APPLEYARD - Sorry, they are not operating at that 7 per cent.

Mr HIDDING - No, you are setting an appropriate return on capital.

Mr APPLEYARD - We would if that were to be the determinant on price but, as I say, it is unlikely to be in the first instance. We will go through the steps of establishing maximum revenues and we have not yet determined what we will use for an average cost of capital. My guess is it probably will not be far away from 7 per cent, but that will not be the constraint on prices for at least the first price determination.

DEPUTY CHAIR - Historically though the councils received only in the order of 2 per cent to 3 per cent from their bulk water authorities and that was what they were used to. Is that part of your consideration as well in what might be finally achieved?

Mr APPLEYARD - Well, again the legislation says 'have regard to full cost recovery'. Full cost recovery says use an appropriate weighted average cost of capital.

DEPUTY CHAIR - Right, okay.

Mr APPLEYARD - That is where it comes from.

Mr HIDDING - Otherwise it is not full then it is arbitrary.

DEPUTY CHAIR - Okay thank you.

Are you done with that line?

Mr HIDDING - I am going to have to think about that.

DEPUTY CHAIR - You think about that and I would be very interested to know where we are with the prices -

Mr HIDDING - It is arcane - it sounds like a dark art this regulating business.

Mr APPLEYARD - I do hear that when I wear another hat on the Grants Commission.

Mr HIDDING - Ah, that is a dark secret.

Laughter.

DEPUTY CHAIR - The price and service plans. We know that they are being drafted and we gather the drafts are close to completion. Can you fill us in on the time lines and what you expect from the corporations?

Mr APPLEYARD - As I mentioned, I think, Treasury has issued draft price and service regulations. Once they are completed the regulator then has the task of issuing price and service guidelines for the corporations to react to. We are getting slightly ahead of ourselves because there have been delays in the process to date and we will shortly issue a consultation paper on price and service guidelines. As soon as the regulations are finished we can say well here is what we think about price and services, what do you think? My hope is that we will issue this maybe in the next week or so. Once the pricing regulations are then finalised we can finalise this document and it will then up to the corporations.

DEPUTY CHAIR - We had better not move a disallowance motion on the fifteenth day on these ones! That would throw a spanner in the works in the middle of next year.

Mr APPLEYARD - It would be a further delay.

DEPUTY CHAIR - It would be a further delay.

Mr HIDDING - Not that Mr Appleyard would be worried about that it would just be another thing to deal with.

DEPUTY CHAIR - What are the expected time lines in terms of looking at the pricing from 1 July next year?

Mr APPLEYARD - We would expect that the price and service plans would come back from the corporations to the regulator some time in the third quarter. If we said grand final weekend I think people would understand when we were talking about -

DEPUTY CHAIR - Yes.

Mr APPLEYARD - Then, having those price and service plans, the regulator would then move to produce a draft report for public consultation perhaps by the end of this year, maybe by 1 February 2012. There would then be consultations with both the public and the corporations on that draft report extending over March, April with perhaps the final

report and determination occurring in May of next year. May is really almost a drop-dead time for the corporations because they then have to issue their accounts.

Mr HIDDING - It becomes a major billing issue.

Mr APPLEYARD - It does. That is as best as we can see at this stage but, of course, 1 July 2012 was always the date by which it had to happen. We are being squeezed through the delays and having to compress the consultation.

DEPUTY CHAIR - Sure, that is right. It does not matter what happens from here on, that end date still remains the same and just everything else gets squeezed. That will be the trigger point for the whole State going to two-part pricing?

Mr APPLEYARD - That is as we understand the intention.

Mr HIDDING - When you say 'we' need to do this and that, you are talking about the office of the regulator?

Mr APPLEYARD - The office does the work but the regulator finalises discussion papers and issues draft reports, yes.

Mr HIDDING - Tell me about the structure. You have the Office of the State Regulator; does that sit out there on its own?

Mr APPLEYARD - It receives pay and rations from Treasury in the same way that perhaps the State Grants Commission does, or the Gaming Commission. It sits as an independent office..

Mr HIDDING - So you set the time lines and what you need?

Mr APPLEYARD - Yes, we set the time lines and we tell the staff to do extraordinary things in extraordinary time, and most of the time they do it. Sometimes they bridle a bit.

Mr HIDDING - Obviously overstaffed if they didn't.

Mr APPLEYARD - You might think that, Mr Hidding.

Laughter.

Mr HIDDING - You are obviously getting the work.

Mr APPLEYARD - It has been a very intense period with our electricity pricing in the first half of this year.

Mr HIDDING - What sort of staff does the office have?

Mr APPLEYARD - About eight or 10.

Mr HIDDING - Is it 10 FTEs?

Mr APPLEYARD - Yes.

Mr HIDDING - Are these economists?

Mr APPLEYARD - A mixture - economic skills, legal skills, accounting skills, spreadsheet skills. We have state-of-industry reports to produce. We have competitive neutrality complaints to deal with. We have finished with MAIB for the time being, and Metro, but they will come around in the cycle in terms of further price investigations at some stage. There is always some sector that we have on our radar.

Mr HIDDING - Generally does the office manage its time line? As you say, for this one coming up, particularly for an organisation such as Onstream that is trying to get its billing right, it is going to be a massive issue whether you get it there or there.

Mr APPLEYARD - I, like every organisation, would like more time to accommodate things.

Mr HIDDING - Do you generally meet your time lines?

Mr APPLEYARD - Yes.

DEPUTY CHAIR - I would like to explore with you the theories around setting price increases. We have just been through a process with electricity, which now has significant future price rises built into it. Is that taken into consideration? No-one escapes that really, so is that something you take into consideration when you're dealing with water, the fact that you know there is a cost-of-living increase above CPI for electricity consumers? We also know the same pressure lies here but obviously you have a consideration around what the people can reasonably bear. Does the fact that electricity got in first give them a bit of an advantage and then mean that there is a limit to what could be increased here? Presumably this is only the difference between the actual prices and CPI, assuming an underlying CPI there.

Mr APPLEYARD - Not directly. From time to time essential services jump in cost and they are a component of the CPI, so the extent to which electricity prices prop up the CPI in years ahead will flow through. When we do water and sewerage determination we will not say there has already been a hit on the CPI from electricity. It will be an independent assessment. Having regard to what consumers will pay, clearly we have regard to movements in the overall cost of living. If cost of living is going up by 8 per cent, we would be foolish to say we can afford a further 5 per cent real rise on top of that. If cost of living is going up by 1.5 per cent, perhaps a further 2 percentage points on that is within the ballpark. Don't quote me on the numbers, though.

DEPUTY CHAIR - No, no. We have the magic \$1 billion that has been mentioned from day one in this process as being the approximate shortfall in infrastructure. If only we had \$1 billion and we spent it we would have full regulatory compliance with the health guidelines, there wouldn't be any boil-water alerts and the pipes wouldn't be busting in the way they are. Obviously once that money is theoretically spent, we then don't have the need for that effort of capital works because that is dealing with the backlog. We do not know what the ongoing need is. At the moment in all the stuff that I am seeing around pricing, it tends to, in my mind at least, assume that this extra effort is going to go on forever and a day, rather than the extra effort being aligned with a catch-up bit on top.

Is there any reason why, for example, that backlog should not be dealt with as a surcharge with a sunset clause of 10 years? It was spruiked as \$1 billion over 10 years. Is there any reason why that should not be dealt with in that way so that there is transparency for the customer to see that this is paying for the backlog but that this is underlying cost, and when we catch up with the backlog you will go back to the underlying, ongoing costs?

Mr BEST - I was going to put it a different way: do you consider the debt-level ratios?

Mr APPLEYARD - If I can go to the Deputy Chair's comment first, there was \$1 billion touted as being the necessary amount. Unfortunately, as we find with all essential infrastructure, what we are talking about is having to lift the level of ongoing capital expenditure. I do not think there is a point where you say, 'Thank goodness for that, we are all done', because you then have replacement of capital expenditure. There has been underinvestment in this sector. There needs to be more investment but not more investment to get to a point where you then sit back and start underinvesting again.

DEPUTY CHAIR - No, but surely we only drop back to the level of replacement on the increased investment, not on the original?

Mr APPLEYARD - There is certainly a catch-up element which needs to occur. How much you can then take your foot off the accelerator, for want of a better word, remains to be seen. But, clearly, once that new infrastructure is in place, the depreciation and the replacement costs themselves will be substantial

Mr BEST - We heard from the different corporations. I think Ben Lomond has 4 per cent level of debt ratio, Southern Water has 10 per cent and Cradle Mountain Water had 24 per cent, but they said that if they had to act on all their capital works because of environmental requests then that would take them up to 50 per cent. Do you make any considerations for that when you are looking at pricing?

Mr APPLEYARD - We will have to wait until the corporations respond back to us on these price and service plans, which we will clearly take into account their expectations for future capital expenditure. They will have to set out for us their intentions regarding capital expenditure, having already had conversations with the other regulators, both public health and environment. So we will take those into account.

Mr BEST - So it is up to the corporations to have those discussions?

Mr APPLEYARD - Yes, they have to have bilateral conversations with environment and with public health to come to an appropriate schedule of capital works to keep those other regulators satisfied, for want of a better word. Clearly they cannot do everything at once so they have to come to some accommodation as to the priorities. Having done that, we then have the process of determining the quantum of capital works to see what is appropriate.

Mr HIDDING - In setting your pricing orders, will the recommendations that come before you come from the staff, obviously working to instructions from your panel?

Mr APPLEYARD - That is generally the process. We might have an initial discussion, as the three-member regulator, as to what the broad framework or the strategy might be but then we would send the staff away to prepare position papers, issues papers, surrounding the each of the elements and report back to the regulator. The regulator then says, 'Yes, that's fine' or 'No, do more work there'. We then put that out as a consultation paper.

Mr HIDDING - What guides the office then in providing recommendations to you in terms of what is a fair thing on pricing? What is an industry figure, interstate for instance? Is that of interest at all to the office, what everybody else in Australia pays for water?

Mr APPLEYARD - Once we have reached the more mature stage, things such as benchmarking the performance of other corporations is something we would certainly look at.

Mr HIDDING - You haven't been before to date?

Mr APPLEYARD - We have done some preliminary desk-top looks at that but it's not horses for courses. As everyone says, we are special. There are unique circumstances regarding where water and sewerage is here in Tasmania compared with the other States, so it is hard to draw comparisons.

Mr BURGESS - There is also a lack of data in a lot of the performance elements currently, particularly around customer service.

Mr HIDDING - Lack of data that you can compare with?

Mr BURGESS - No, lack of data that is able to be collected by the corporations. They need to implement systems to get right down into how long it takes to do each job and to feed it back up.

Mr HIDDING - And that will present itself in due course?

Mr BURGESS - Yes. We have a guideline that sets up a timetable for that.

Mr HIDDING - We have been told over the last month or two while we have been doing this inquiry that the average cost of water in an area should be around \$850 per annum for an average household. It struck me that I should ask where that figure has come from. When we were up the coast they said it should be, but while ever the inequities are in, they need to be currently be paying \$1 014 or \$1 114.

Mr BACON - Wasn't that just the average price across all the customers for Cradle Mountain Water?

Mr HIDDING - That was the \$1 200 figure, but then we were told that eventually everybody should be paying about \$850 a year, so I wonder where that came from as a figure that seems to be bandied about the three corporations.

Mr APPLEYARD - I can't help you.

Mr HIDDING - If the figure is wrong, that could have quite some ramifications if they're running their numbers on that. Is this tested against other States? That doesn't ring a bell, those sorts of numbers?

Mr BURGESS - No. The only thing I would say is that sometimes the use of raw averages can be somewhat misleading when you have different costs for different customer classes. We're careful in looking at figures or using figures such as that.

Mr APPLEYARD - I do recall many, many years ago when I had a role on the State Grants Commission and we used to go to Ulverstone and look at water and sewerage prices there. There was an equivalent tenement average charge but it was so dominated by McCain at the time that it was nonsensical. You have to look at both the mix between residential and commercial and also whether it is an urban area such as Melbourne.

Mr HIDDING - It's out there, though, isn't it. We have heard about \$850 a year.

DEPUTY CHAIR - I have the transcript here but I can't remember the full story on that.

Mr BURGESS - You could easily calculate it using some of the advice that is published to the Treasurer.

Mr HIDDING - I reckon that is what has happened.

DEPUTY CHAIR - Can I move on to the issue around the two-part pricing, and that is the balance between the two parts of the pricing and what involvement you have there. How much in thinking and influence will you have in regard to that?

Mr APPLEYARD - I don't think we have had much to date other than the reference to it within the legislation and the fact that the draft regulations refer to two-part pricing and in the National Water Initiative I think it refers to a requirement for two-part pricing. Our expectation is that the corporations, when they come to us, will set out their initial plans in relation to that.

DEPUTY CHAIR - There are a number of models that can be adopted under two-part pricing depending on how much weight you put to various objectives.

Mr APPLEYARD - And in fact already is around various parts of the State, some of the legacies they got from local governments.

DEPUTY CHAIR - Yes, that's right. There is the so-called 'free' component up-front that goes effectively in your fixed component. There is a flat cost per litre. We have heard certainly - and I do not know whether it is universal from the corporations, but I think it might be - that they are looking at having a single flat rate per litre on the second part, irrespective of how many litres, which suggests to me that they do not have a high conservation valuation there in terms of trying to drive down consumption by having an increasing step system or conversely going the other way and having it the more litres you use, the cheaper it gets, to drive up consumption and up revenues in some senses. Will you have an involvement in that or will you wait until you see what comes from the corporations?

Mr APPLEYARD - We will wait and see what comes from the corporations but that would clearly be an area where we will say something in our draft report, I imagine.

Mr BURGESS - The draft regulations talk about this in terms that they require it to be at least short-run marginal cost so that provides some avenue for the corporations to potentially load some of their fixed costs into the variable charge which would provide a conservation incentive and provide potentially a greater ability for customers to control their bill through usage, so that potential exists under the draft regulations.

Mr HIDDING - Which could have a remarkable effect on revenues as well.

DEPUTY CHAIR - If you were to get it wrong.

Mr HIDDING - This is one of the great challenges of a utility - it is a ridiculous thing - you have to use less power and use more power on the other hand. Your marketing department is telling you -

Mr APPLEYARD - Use less power, use less water, defer capex.

DEPUTY CHAIR - That is right.

Mr HIDDING - On that two-part thing, Southern Water will come up with a proposal for you as to how they would bring in two-part pricing without meters because they will not be in place?

DEPUTY CHAIR - Yes, they will be.

Mr HIDDING - By when?

DEPUTY CHAIR - 1 July next year.

Mr HIDDING - Will they be installed?

DEPUTY CHAIR - Yes. In fact bizarrely enough, they are out there flat out installing them at the moment and we have not heard a peep. We did have the launch.

Mr BURGESS - I don't think they are quite started but they are very close.

Mr HIDDING - It just goes to show it was all about the aldermen and not the constituents.

DEPUTY CHAIR - Will you require all the corporations to have the same tariff or fixed component? Sorry, we are using postage-stamp pricing assuming across each area, although there is an opportunity for having a different -

Mr APPLEYARD - That is to be determined.

DEPUTY CHAIR - That is the assumption.

Mr APPLEYARD - To go to the substance of your question no, I do not think we would expect the three corps to come up with identical pricing service plans.

DEPUTY CHAIR - Essentially water in the south could be cheaper than water in the north?

Mr APPLEYARD - It is possible, or vice versa.

DEPUTY CHAIR - Yes, or the volume entry charge so there is no requirement for statewide consistency?

Mr BURGESS - No, and I think this was pointed out earlier. Each corporation is facing very different challenges, both in their own finances and in their regulatory compliance, that has the potential to lead to different - and in terms of the geography to some extent -

Mr APPLEYARD - And in terms of the level of catch-up in water versus sewerage.

DEPUTY CHAIR - Have you had to revise any recommendations or information in light of the fact that in particular Cradle Mountain Water has a much more significant debt load than was originally calculated in the initial assumptions and that that is obviously providing a serious constraint to it? Has that changed the information that you have pushed out there or will be?

Mr APPLEYARD - In the advice to the Treasurer dated November 2010 we indicated that we had undertaken some revisions to that first round of data.

Mr BEST - Was that published?

Mr APPLEYARD - Yes. That would have incorporated the more up-to-date information that we got from the corporations but I think at that stage we were using 2009-10.

Mr BURGESS - I think Cradle Mountain were at about 20 per cent.

DEPUTY CHAIR - The next one was around the compliance for sewerage in particular. We have heard that they have very low levels of compliance right across the State with existing licence conditions on sewage treatment plants and that many of those licence conditions go back decades and are seriously out of date, and that if they were contemporary licence conditions they would be significantly further behind with compliance. That is obviously one of the considerations: how long is it before they are going to be compliant, if ever? Where is the thinking at?

Mr APPLEYARD - In that space we rely on advice coming from the other independent regulator - that is, EPA. The corporations will need to have a conversation with EPA as to which priorities they address first in terms of getting the best bang for their capital buck. So whilst we report on it in our state-of-the-industry report it is pretty much information we get from EPA regarding the current status and what needs to occur.

DEPUTY CHAIR - But if the EPA says we are going to issue new licence conditions for all waste water treatment plants and we expect you to be in compliance in five years with all of those, obviously that is going to have a significant impact on the revenue requirements of the corporations?

Mr APPLEYARD - Sure; that is why there needs to be these bilateral conversations with each of the regulators, because if Roscoe Taylor from Public Health were to say, 'I equally expect you to be fully compliant with drinking water standards within three years', the corporations would throw up their hands and say, 'We cannot spend all this money quickly enough'. The regulator would say that your appetite for capital expenditure is too big, so go away and have another conversation about priorities.

DEPUTY CHAIR - So those conversations really need to happen at least in the interim sense before they come to you. Again, we are not yet at the position of knowing how long it will take us to meet the backlog so that all our drinking water supplies are in compliance with the current requirements or how long it will be before our sewerage systems are in compliance with existing licence conditions, let alone contemporary ones were they to be imposed. We have no idea.

Mr APPLEYARD - That is an accurate statement at this point in time, but hopefully we will get greater clarity over the years ahead.

DEPUTY CHAIR - All we know is that on the path we are going we are moving faster towards that compliance than we were under the old council model?

Mr APPLEYARD - Yes. Anecdotally, the corporations have been to us and said they are still doing investigations as to the nature of the infrastructure. It could well be that in some instances, if the existing plant were to perform better or be used to its capacity, again we could defer capex. To be fair to them, they are still going through a process of discovering the nature of the assets, how well they can perform and what they really do need to do. Some things are obvious and they are getting on with those but for others they need a bit of time to sort out what those priorities are.

DEPUTY CHAIR - You said that the IPO should be amended from July 2011 because we know that the 5 per cent which the Government threw into the system will skew things quite significantly the moment it comes to an end, on current trajectory, at 30 June 2012. We have certainly heard from the corporations that they are screaming for the Government to not let them fall off the end of that cliff. Do you have any suggestions as to what recommendations we might make? There is still a year there and there is \$27 million on the table, unless it gets whipped off and disappears altogether. What would be the most efficient mechanism of winding out that government support?

Mr APPLEYARD - To be honest, Deputy Chair, I would rather not comment on that because it is not within our brief -

DEPUTY CHAIR - Okay.

Mr APPLEYARD - other than to say it would be better that there was a change made sooner rather than later, because with the price caps we have lost time in terms of where we want to get to. The quantum and the nature by which it is spent is a matter for government policy.

DEPUTY CHAIR - Would it be helpful if the Government were to use the money that is available to back itself out in the way it has come in, which is 10 per cent this year, back to 5 per cent next year? Obviously better than falling off a cliff, perhaps.

Mr APPLEYARD - Again, I would rather not comment on the numbers other than to say that the more flexibility it can offer the corporations in terms of whatever cap and collars it suggests, the better. To have a 5 per cent cap for everyone has delayed the processes which ought to have occurred. You can get around that by so-called caps and collars, with the winners not getting a huge advantage and somehow restraining the extent to which they might get some gain, but that is for Government to decide.

DEPUTY CHAIR - Yes, we heard of some very perverse outcomes from this process. Thank you very much for coming and giving evidence.

Mr APPLEYARD - Thank you very much. We wish the committee well in its endeavours.

THE WITNESSES WITHDREW.