



8 April 2022

Joe Dimasi
Senior Commissioner
Independent Competition and Regulatory Commission
PO Box 161
CIVIC SQUARE ACT 2608

Dear Mr Dimasi

Issues Paper: Regulated water and wastewater services prices 2023–28

Icon Water welcomes the opportunity to submit its response to the Independent Competition and Regulatory Commission (the ICRC) issues paper for its 2023–28 review of Icon Water's regulated water and wastewater (sewerage) services prices.

To support our vision of being a valued partner in the community, Icon Water is committed to providing safe, secure and sustainable water and wastewater services to the ACT and region. To deepen our understanding of what the community values and their experience with Icon Water, we recently undertook our most comprehensive community engagement program to date – *Let's Talk Water and Wastewater*. Through this engagement, Canberrans told us that they value:

- reliable water and wastewater services;
- quality drinking water;
- affordable pricing; and
- responsive customer service.

We also learned the following key insights about what our customer expect when we consider strategic planning and investment decisions:

- The community agrees with the need to continue to **plan for the future**, this includes water security and exploring alternative water sources.
- There is community support for achieving **greater environmental sustainability** and accelerating our achievement of net zero, while limiting impacts on customer prices.
- The community is committed to Icon Water **maintaining quality and reliable core services** and is willing to pay something towards improving network performance equity.

- **Affordability** should underpin any investment decision. If Icon Water needs to invest to avoid causing issues in the future, it should consider support for **vulnerable customers** and other impacted customer segments.
- The community views Icon Water as an essential service provider. To be a **valued partner** in the community they want us to **be more visible** – this means being targeted in our partnering initiatives, educational and supporting activities, and openly talking about it with the community.

These insights will underpin our regulatory proposal for 2023–28, which is due to the ICRC on 1 July 2022. The proposal will outline how we are investing to ensure our water and wastewater system is resilient and provides a level of service that reflects customer preferences. We are committed to balancing affordability for the community while we deliver efficient and sustainable services, including meeting the ACT Government’s climate change target to transition towards net-zero emissions by 2045.

Icon Water is largely supportive of the ICRC framework for regulating water and wastewater prices. The current regulatory framework and pricing principles are suitable for the upcoming price review, noting the significant work undertaken over the past few years to review aspects of the framework outside the usual five-year price review process. This included the ICRC undertaking reviews of incentive mechanisms, the weighted average cost of capital (WACC) and demand forecasting methodologies. These reviews have provided regulatory certainty as we plan for the upcoming regulatory period.

Our attached submission (attachment 1) addresses each of the six questions put forward in the issues paper.

Thank you for the opportunity to provide input into the process now to shape the discussion about key issues in advance of submitting our regulatory proposal for 2023–28. If you have any questions, please contact Cath Pennington at cath.pennington@iconwater.com.au or 02 6180 6979.

Yours sincerely

A handwritten signature in black ink, appearing to read 'R Hezkial', written in a cursive style.

Ray Hezkial
Managing Director



Attachment 1 – Icon Water’s response to questions posed in the Issues Paper

This attachment sets out our responses to the questions asked in the ICRC issues paper. Our regulatory proposal, which is due to the ICRC on 1 July 2022, will provide additional information.

Question 1: How do we balance the trade-offs between affordability and price stability on one side, and Icon Water’s ability to raise enough revenue to maintain service standards, protect water security and manage the impacts of climate change on the other?

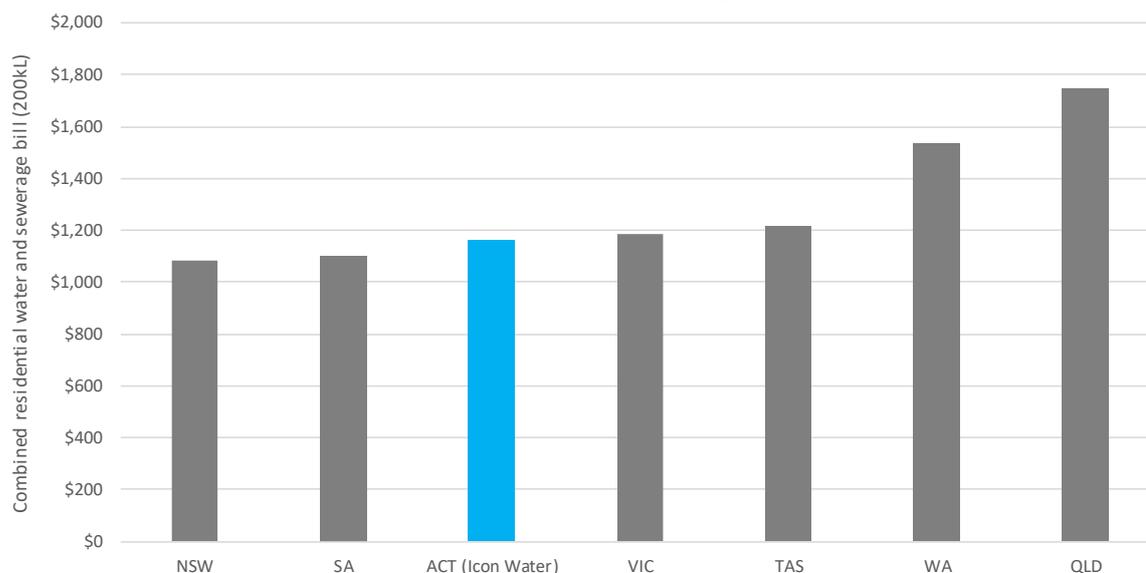
Icon Water understands the cost-of-living pressures facing our community and works hard to deliver high-quality and affordable water and wastewater services to the ACT and region.

Managing the timing of expenditure, and the balance of affordability and service quality, requires customers to be placed at the centre of Icon Water’s decision-making. This allows customers to understand the major factors driving water and wastewater prices, and provides them with an opportunity to give feedback on any trade-offs between service levels, investment and prices. In preparing for the 2023–28 Price Proposal we undertook extensive customer and community engagement to seek feedback and insights from multiple perspectives within the ACT community and Icon Water’s customer groups. The engagement confirmed that our customers generally have high levels of satisfaction with Icon Water’s level of service, and identified key insights to support Icon Water’s planning for 2023–28. It also confirmed that affordability should continue to be central to Icon Water’s decision-making, especially for more vulnerable customers.

*Our customers told us that **affordability** should underpin any investment decision. If an investment is needed to avoid causing issues in the future, support for **vulnerable customers** and other impacted customer segments should be considered.*

Icon Water’s commitment to affordability is reflected in the way we plan and invest in water and wastewater services, ensuring we align with customer priorities for service quality while maintaining affordable pricing. As part of our regulatory submission for 2018–23, Icon Water proposed significant efficiencies in capital and operating costs which have helped keep bill increases, on average, below inflation. This has contributed to Icon Water having amongst the lowest residential water and wastewater bills for major urban water utilities in Australia (Figure 1).

Figure 1: Residential combined water and wastewater bills for major urban water utilities



Source: Bureau of Meteorology, National Performance Report 2020–21.
Amounts represent the average across all major water urban water utilities in each state/territory.

The importance of affordability has been heightened recently by the COVID-19 pandemic and its flow-on economic impacts on ACT families and businesses. To support our customers during the pandemic, Icon Water implemented a range of support measures including a ‘price-freeze’ in 2020–21, payment extensions, flexible payment plans and a pause on credit collection activities. Icon Water has also maintained its ‘Staying Connected’ program, which provides personalised support to help customers who may be struggling to pay their bills, and has expanded the program to support small businesses.

While affordability is at the forefront of our decision-making, Icon Water is increasingly facing an uncertain operating environment and must make investments to ensure affordability and service quality can continue to be maintained over the longer term. Recent experience has demonstrated the need for Icon Water to be resilient to disruptions to the ACT region that can be caused by events such as the COVID-19 pandemic, drought, bushfires, extended wet weather and storms. Financial markets and the broader economy have also shown volatility, with Icon Water’s allowed return on capital falling to near-record lows, and high rates of inflation placing upward pressure on prices across the global economy. This environment creates challenges for businesses like Icon Water which must maintain a large portfolio of major capital assets and provide a high-quality essential service to the community.

The ACT region is at risk from climate change, and we are already seeing some of its effects. This includes rising temperatures, changes to rainfall and run-off patterns, more extreme weather and longer fire seasons. In recent years, the ACT has observed its water storage drop to around 45 per cent in early 2020, before increasing to 100 per cent in 2021. The ICRC recently concluded its review of Icon Water’s demand forecasting methodologies, which acknowledged the impact of climate change on water usage, and included revisions to the demand forecasts to account for the latest available climate change projections. Improving the accuracy of demand forecasts can support affordability by helping to ensure customers pay no more or less than the efficient costs of providing them with water and wastewater services. Through our engagement program, it was apparent that customers expect us to proactively respond to climate change risks, but not at any cost.

*Our customers told us that there is community support for achieving **greater environmental sustainability** and accelerating to net zero greenhouse gas emissions while limiting the impacts on customer prices.*

A key challenge for Icon Water is that our revenues can be highly variable, due to the influence of weather on water demand. In contrast, Icon Water's costs do not change significantly from year to year since they are mostly comprised of expenditure on major long-lived assets (although increasingly Icon Water is investing in digital assets which tend to have shorter asset lives). To manage the potential mismatch between revenues and costs, the ICRC applies a demand 'deadband' which helps to share water demand risk between Icon Water and its customers. The deadband allows Icon Water's revenues and prices to be adjusted (up or down) if its water sales revenue differs by more than \pm six per cent of the forecast for the regulatory period. This helps to promote affordability and bill certainty for customers, whilst ensuring that Icon Water can still recover its efficient costs if water demand varies significantly from the forecast. Icon Water supports the deadband mechanism, and considers that the current six per cent threshold is appropriate. However, there may be a case to reconsider the threshold value in future if there is a material increase in the uncertainty surrounding water demand or other elements of our regulatory framework.

Improving the accuracy of our water demand forecasts is just one part of how Icon Water must meet the challenges of climate change. We understand the urgency to mitigate greenhouse gas emissions, and are committed to meeting the ACT Government's target of achieving net zero emissions by 2045. The [Icon Water Climate Change Adaptation Plan](#) identifies priorities to further build our resilience to climate change impacts in the ACT region while minimising disruptions to essential service delivery. This includes the need to invest in meeting climate-related challenges such as:

- tree root incursions due to droughts;
- more frequent leaks and bursts due to thermal expansion, corrosion and subsidence;
- heavy rains causing stormwater incursion into sewers; and
- the risk of bushfire damage to the network.

Icon Water has incorporated climate change projections in its planning since the early 2000's, including under the ACT's *Think Water, Act Water* strategy released in April 2004, and more recently under the *ACT Water Strategy 2014–44*. However, continued investment is required to maintain water security and climate resilience as the territory experiences growth in urban development and an increase in climate related impacts on the network. This sentiment is also shared by our customers.

*Our customers told us that the community agrees with the need for Icon Water to **plan for the future**, including investing in water security and exploring alternative water sources.*

Icon Water recently developed our Drought Management Plan (DMP), which outlines multiple actions and responses in drought conditions, with various trigger points. The DMP includes a list of activities to be undertaken to enhance our drought response readiness, which are to be implemented in the 2023–28 regulatory period. We also recently developed our Water and Wastewater system strategies. These strategies take a holistic and systematic view, examining the current state of our water and wastewater system in terms of safety, security and level of sophistication in its efficiency, prudence and ongoing improvement. A set of actions has been identified for the ongoing development and improvement of our water and wastewater systems, which will be implemented in the 2023–28 regulatory period. This includes a long-term water security plan which will ensure our water supply can support future growth and development of our region and considers the integration with wastewater management. Icon Water intends to engage with the ACT community as part of the continued development of the DMP, water and wastewater system strategies.

Icon Water also faces challenges associated with ageing infrastructure, alongside pressure from ACT's growing population and increasing urban density. A significant proportion of Icon Water's assets were built in the 1960's and 70's at the time some of Canberra's major districts were first developed (including Woden Valley, Belconnen, Weston Creek and Tuggeranong). Many of these assets are now reaching the end of their economic and engineering life, including multiple drinking water reservoirs in the ACT. Icon

Water has also observed the Lower Molonglo Water Quality Control Centre (LMWQCC) approaching maximum capacity during wet weather events, which has led to three instances of partially treated effluent being released in 2021. These challenges mean that significant capital investment is required in the coming years to renew and grow Icon Water's assets.

Our customers told us that the community is committed to Icon Water **maintaining quality and reliable core services**, and is willing to pay something towards improving network performance equity.

Our 2023–28 Price Proposal will detail our proposed capital expenditure for the regulatory period, which is necessary to continue to meet customer service levels and regulatory obligations both within 2023–28 and into the future. Proactive and measured investment in network resilience can help promote affordability and bill certainty over the long-term because it mitigates sudden and unforeseen price increases when major assets reach end-of-life or fail. However, it is important that Icon Water achieves the right balance of expenditure to ensure that it does not sacrifice affordability in the short-term while targeting savings which may be in the far future or uncertain.

It is also important that investment decisions are not simply driven by considerations of economic efficiency, but also reflect customers' willingness to pay for activities that may extend beyond Icon Water's core mandate to provide water and wastewater services.

Our customers told us that the community considers Icon Water as an essential service provide. To be a **valued partner** in the community, Icon Water should strive to **be more visible** through their partnering initiatives, educating and supporting activities, and openly promoting their initiatives within the community.

The outcomes of the strategic customer and community engagement will be further detailed in Icon Water's 2023–28 Price Proposal, including how they have shaped our plan to continue providing the ACT region with a sustainable, affordable, and high-quality water and wastewater services.

Question 2: Are there other issues relating to the price and quality of water and sewerage services supplied by Icon Water that we should consider during the price investigation?

Icon Water considers that the ICRC issues paper provides good coverage of the major issues relevant to the 2023–28 price investigation.

Icon Water wishes to draw the ICRC's attention to our recent review of miscellaneous fees and charges associated with water and wastewater services. The miscellaneous fees and charges cover services such as water and wastewater main connections, hydrants and meter relocations. Under the current regulatory approach, these charges are updated annually to account for inflation. Icon Water considers that it is timely to re-examine whether the charges continue to be cost-reflective and meet the ICRC's pricing principles.

Any proposed changes to the charges will be included in Icon Water's 2023–28 regulatory submission.

Question 3: We welcome any comments on the pricing principles that we intend to use in addressing and balancing economic, social and environmental objectives.

At this stage, we do not consider any changes are necessary to the overall regulatory framework or pricing principles applied by the ICRC.

Icon Water supports the ICRC's emphasis on economic efficiency as the starting point for achieving the long-term interests of consumers in relation to price, quality, safety, reliability and security of water and wastewater services. Icon Water, like the ICRC, also considers the social and environmental impacts of the services we provide that are essential to the health and wellbeing of the community.

We take into consideration and balance the trade-offs inherent in applying the pricing principles within the context of the ICRC's regulatory framework. For example, while maintaining a focus on economic efficiency, we continue to balance investments in assets and technologies required to transition Icon Water towards net zero emissions by 2045. We are starting to invest now, while exploring the commercial viability of emerging technologies to minimise the impact on consumers and achieve a gradual adjustment of prices, which is consistent with *Pricing Principle 4*.

In addition to our commitment to achieving net zero emissions, our ongoing work to ensure our water sources are safe, secure and sustainable, reflects our commitment to considering and effectively accounting for environmental impacts as part of our decision making (*Pricing Principle 3*).

Icon Water is committed to being a valued partner in our community and our focus on community engagement supports this vision, and ensures we invest in infrastructure that is prudent and efficient. For example, we tested the community's appetite to pay for a roll-out of digital meters as part of a willingness to pay study. Investing in significant new infrastructure without community support would not be efficient and consistent with *Pricing Principles 1 and 2*.

We also support the ICRC's focus on simplicity and transparency (*Pricing Principles 6 and 7*) when setting prices within a focus on prudence and efficiency.

Lastly, as mentioned in response to question 1, affordability for our customers is at the forefront of our decision-making. We heard from our customers that they support our commitment to affordability as part of our investment process (which is consistent with *Pricing Principle 5*).

Question 4: Do you have any comments on our proposed approach to assessing Icon Water's revenue requirement for the next regulatory period?

We agree with the approach put forward by the ICRC to assess Icon Water's revenue requirement for the next regulatory period. The current approach provides an appropriate balance of risks and incentives for Icon Water to deliver efficient and safe services to the community. The current approach is similar to approaches used by regulators in other jurisdictions and reflects good regulatory practice.

The ICRC's 2020 review of incentive mechanisms for water and sewerage services largely addressed the approach used to assess Icon Water's revenue requirement.

As explained in our submission to that review, Icon Water considers the general principles underlying the current approach to incentive-based regulation have been successful in driving affordability and service quality in the long-term interests of our customers¹. Adopting any changes to the regulatory approach now would not be in the long-term interests of customers and would undermine the work we have done to develop a regulatory proposal that is consistent with the current regulatory framework.

We do not intend to propose any major change to the current regulatory framework or approach to assessing Icon Water's revenue requirement as part of our regulatory submission.

We are still assessing the appropriateness of the events identified to trigger a pass through of costs during the upcoming regulatory period. We will provide further information on cost pass through categories as part of our regulatory submission.

¹ Icon Water, *Submission to ICRC review of Incentive Mechanisms for Water and Sewerage Services*, 2020, p1.

Question 5: Do you have any comments on our proposed process for reviewing the prudence and efficiency of capital and operating expenditure proposed by Icon Water?

Icon Water's proposed expenditure is informed by our customers

Icon Water considers the two-step process outlined by the ICRC is a reasonable approach to ensure customers only pay Icon Water's prudent and efficient costs to deliver water and wastewater services. The approach is consistent with the pricing principles and has regard to relevant legislative considerations and government policy. This includes the integration of economic and environmental considerations in the decision-making process through the precautionary principle and the inter-generational equity principal.²

Icon Water supports the inclusion of prudent and efficient expenditure and notes that long-run impacts on customers should be considered in the context of commitments to achieve the ACT Government's net-zero emissions targets and other government policies.³ Without accounting for the impacts of climate change now when making network investments, there is a risk that customer prices will be higher in the long run. Icon Water is committed to enhancing network resilience and investing in long-lived assets to meet customer expectations and regulatory obligations.

The prudence and efficiency of Icon Water's expenditure should be considered holistically

The value for money (efficiency) of providing regulated water and wastewater services needs to be assessed together with prudence. We note that efficiency relates to incurring expenditure, representing the best value for money, which is not always synonymous with the lowest cost option. For example, a utility may procure insurance at the lowest cost, but this may not provide sufficient cover to efficiently mitigate risks.

Prudence relates to expenditure that would reasonably be expected of a utility operating in the relevant circumstances. However, prudence may involve expenses where the benefits do not immediately outweigh the costs but are necessary to meet regulatory obligations and plan for the future as water and wastewater assets are long-lived. For example, having additional measures for maintaining safety and security standards or considering investment decisions that foster increased climate resilience and adaptability may achieve better long-term outcomes. Additionally, regulated utilities may incur prudent expenditure, which is not necessarily the lowest cost option. Therefore, we consider that the prudence and efficiency of expenditure should be considered together, rather than in isolation.

Icon Water has reviewed the service agreements with ActewAGL

Icon Water outsources some of its corporate and customer services to ActewAGL under two contracts – the Corporate Services Agreement (CSA) and Customer Services and Community Support Agreement (CSCSA). Table 1 provides a summary of these services. Both contracts expire on 30 June 2023.

² *Independent Competition and Regulatory Commission Act 1997*

³ For example, the Parliamentary and Governing Agreement, 10th legislative assembly Australian Capital Territory; ACT Government, ACT Water Strategy 2014-44, August 2014.

Table 1 Services under the CSA and CSCSA

Corporate Services	Customer Services and Community Support Services
Information communications technology (ICT) physical hardware, computer software systems and supporting technical services Emergency contact centre Economic regulatory services Human resource services Tax Treasury Accounts payable Procurement Warehouse management Fleet management Property and security Accounting	Meter reading Customer billing Customer account management Customer contact centre Accounts receivable and credit management Customer data storage and protection Community communications Corporate communications Sponsorships

The issues paper mentioned that Icon Water has been reviewing the CSA. It should be noted that this is also the case for the CSCSA. In the 2018–23 regulatory period to date, Icon Water has developed a sourcing strategy to ensure we maintain access to the services required to operate our business efficiently and effectively, so that we can continue to provide high quality and affordable water and wastewater services to our customers. These services are critical to our delivery of essential water and wastewater services to the Canberra community. The program of works to implement the sourcing strategy will provide us with the strategic control, service quality, commercial outcomes and flexibility required to meet the needs of the business into the future. Our decisions have considered value for money and the need to maintain continuity of services for our customers.

We are currently in the implementation stage of the sourcing strategy. At a high-level, services under the CSCSA will continue to be delivered by ActewAGL from July 2023, however no corporate services under the CSA will be provided by ActewAGL post contract expiry. Key points to note in regards to the sourcing strategy includes:

- In 2020, we undertook an initial market review and benchmarking activity for relevant services delivered under the CSCSA. Subsequently, a request for proposal was sought from the incumbent, ActewAGL. Noting the significant number and range of services across the CSA and CSCSA, the decision to secure the CSCSA services as early as possible was based on the need to ensure business continuity and minimise risk of disruption for our customers for one of our most critical areas – billing and retail customer service, thereby enabling focus on the remaining services.

ActewAGL responded with a proposal, and following evaluation and negotiation, in September 2021, we successfully re-appointed ActewAGL with a new contract commencing on 1 July 2023 for a term of 4 years, with extension options.

- In 2021, we went to the open market for two components of the CSA:
 - Information communications technology (ICT) infrastructure and operations services, and
 - Financial information management systems (FIMS).

Following evaluation and negotiation, in early April 2022 we successfully appointed vendors for most of these services and expect to appoint the remaining vendor imminently.

- For all other remaining services, we continue to determine the most appropriate way for achieving desired outcomes to ensure seamless transition within the time permitted to maintain continuity of services for our customers.

Icon Water will work closely with ActewAGL throughout the transition of corporate services, with the intent of minimising any disruption to customers and staff in both organisations.

We will provide the ICRC with the outcomes of the review and evidence to support the prudence and efficiency assessment as part of their investigation. In the meantime, further information on the review and outcomes can be found on our [website](#).

Question 6: Do you consider the current water tariff structure remains appropriate or is there scope for further rebalancing?

During the 2018–23 regulatory period Icon Water has been gradually rebalancing its water tariffs so that fixed charges make up a greater proportion of customer bills. We did this for three main reasons:

- Icon Water is a fixed cost business, with a relatively low marginal cost of water supply. Increasing fixed charges better reflects Icon Water’s costs and helps achieve allocative efficiency by sending a price signal to customers that better reflects their cost of use.
- Icon Water’s Tier 2 price is amongst the highest in Australia; and this can affect large water users and non-residential customers with little/no discretionary water use. Rebalancing the tariffs helps maintain affordability for these customers.
- Water demand can be highly variable and influenced by climate from year to year. In turn, so is the revenue Icon Water can collect to maintain its network. Having higher fixed charges means Icon Water’s revenue is more stable over time, allowing us to better plan for and undertake long-term investments required for a safe and reliable network.

However, we also note that economic efficiency is just one of the objectives that must be considered when setting prices. The ICRC’s pricing principles include, in addition to economic efficiency, the need to account for environmental considerations and community impacts. Indeed, Icon Water’s Tier 2 price was originally introduced as a price signal for water conservation, and there has been broad support amongst residential customers for maintaining a tiered tariff structure. Furthermore, keeping usage charges above marginal cost allows Icon Water to charge a reduced fixed charge which improves affordability for small water users for whom the fixed charge makes up a greater proportion of the bill. It also reflects a general preference by the community towards ‘pay-for-use’ pricing, with smaller fixed charges.

Nonetheless, we recognise Icon Water’s Tier 2 price remains among the highest in Australia, which continues to create challenges for some large customers.

Icon Water believes that strong community input is required to determine a tariff structure that is perceived as fair and meets the needs of different customer segments. Tariff reform cannot be done by reference to economic principles alone, and should be equitable and meet the needs of different customer segments. Icon Water’s position is that any further rebalancing of tariffs should only occur if there is strong community support and understanding of the impacts on different customer segments.

For the 2023–28 price review, we have engaged extensively on our water tariff structure, including various options for further rebalancing fixed and variable charges. Overall, while most stakeholders consider the two-tier tariff structure to be appropriate, preferences were generally split on the balance of fixed and variable charges. Larger customers tended to prefer higher supply charges (lower usage charges) while smaller customers favoured lower supply charges (higher usage charges). Most participants agreed that affordability is a major consideration, particularly as it relates to small and vulnerable customers. There was also a strong view among residential customers that a higher Tier 2 price is important for encouraging

water saving behaviours. In contrast, among larger water users, there was a perception that the Tier 2 price is unfair since many large users (such as sporting clubs) have limited ability to reduce their water usage.

Icon Water is committed to supporting affordability for all our customers, including both small and large water users, and understands the challenges of creating an equitable and efficient tariff structure. We also note that the tariff structure is just one part of achieving affordability for our customers, as discussed in the response to Question 1.

We will present the full outcomes of the strategic customer and community engagement on tariffs as part of our 2023–28 Price Proposal.