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Charles Millstead
Chief Executive Officer
Queensland Competition Authority
GPO Box 2257
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Dear Mr Millstead

Thank you for the opportunity to comment on, and contribute to, the Queensland Competition Authority's (QCA's) Rate of Return Review.

To promote the economically efficient operation of, use of and investment in regulated assets, the rate of return framework applied to regulated businesses needs to enable the recovery of costs incurred in providing regulated services. Sunwater recommends that the QCA consider developing clear and transparent principles for the determination of its rate of return methodology. This approach would better inform the submissions of regulated businesses and facilitate more targeted and meaningful discussion about inputs.

In addition to the above recommendation, Sunwater wishes to highlight our interest in addressing the issues outlined below.

Trailing average cost of debt

Sunwater believes that moving to a trailing arrangement, with an annual adjustment rather than an end of period adjustment, will contribute to reducing regulated businesses' exposure to interest rates.

Regulated businesses with large debt portfolios are likely to issue fixed-rate debt on a staggered maturity basis, rather than refinance their entire debt portfolios at once (or within a very short timeframe) at the beginning of each price path period. This approach minimises the refinancing risk faced by regulated businesses and is a prudent and efficient strategy to managing debt. Sunwater considers that a trailing average approach would better match actual debt management practices and resulting debt costs as, even if the rate applied is still only determined periodically, it would incorporate interest rate changes over time.

A trailing average cost of debt approach would also mitigate the future impact on regulated businesses of rising interest rates, when they occur. This is particularly relevant when the interval between rate of return reviews (if not updated annually) can be quite long.

Beta risk

While Sunwater agrees that other factors (particularly market structure and returns) are likely to be more important, Sunwater considers there should be a reasonable degree of similarity in the physical nature of firms being compared for this purpose.

Regulatory risk

In the case of many regulated entities, the framework in place is subject to explicit legislative triggers and timeframes. In the case of Sunwater, those triggers and timeframes are not captured in either the *Water Act 2000* or the *Queensland Competition Authority Act 1997*. This potential gap between the period assumed by the regulator and the actual period over which those prices may be in effect, creates additional uncertainty for Sunwater that is not present for many other businesses regulated by the QCA.

This uncertainty creates a risk that Sunwater may not have the opportunity to represent our case for appropriate pricing, despite changes in the cost environment potentially leaving us to bear the adverse impacts of how changes in the drivers of our cost profile are reflected in Weighted Average Cost of Capital (WACC) assumptions

Sunwater is of the view that the QCA should consider how this uncertainty might be reflected in an appropriate WACC for Sunwater.

QCA stakeholder engagement

Finally, to facilitate more in-depth consideration of these and other issues, Sunwater submits that there may be value in the QCA separately considering a review of its stakeholder engagement approach, with a view to incorporating:

- more frequent liaison with its regulated entities and their customers
- longer lead times regarding the QCA's upcoming program of works
- longer timeframes for submissions to be delivered.

Essentially, a more flexible, transparent and iterative approach to key stakeholder engagement would be well-received and highly valued by Sunwater. This kind of approach would enable regulated businesses to better plan and dedicate resources and time to the QCA's review processes, given that our regulatory teams are lean and primarily focused on supporting the customer-facing side of our businesses.

Thank you once again for the opportunity to contribute to this process. If you would like additional input or information, or to discuss any element of this submission, please contact Courtney Chester, Regulatory and Pricing Lead.

Yours sincerely



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