

WaterNSW Cost Allocation Manual

June 2024

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1 Version History

Version	Date	Author	Detail of changes
1	December 2021	WaterNSW	First Version
2	June 2024	WaterNSW	Contents structure; Additional description of inclusions and exclusions in the overhead allocation method; Additional description of allocators in section 7.4; Additional diagrams and tables

2 Introduction

WaterNSW is a State-Owned Corporation established under the Water NSW Act 2014 and operates under an Operating Licence issued and monitored by the Independent Pricing and Regulatory Tribunal (IPART).

WaterNSW is responsible for supplying the State's bulk water needs, operating the State's river systems and the bulk water supply system for Greater Sydney, and providing services to its customers with respect to licensing and approvals, water allocation trades ("temporary trades"), water licence trades ("permanent trades") and water resource information.

WaterNSW supplies two thirds of water used in NSW from its 41 major dams, rivers and pipelines to regional towns, irrigators, Sydney Water Corporation, and local water utilities. WaterNSW owns and operates the largest surface and groundwater monitoring network in the southern hemisphere and build, maintain and operate essential infrastructure. WaterNSW plays a vital role in improving the availability of water that is essential for water users and the communities throughout NSW. WaterNSW does this through the delivery of its market functions:

- Source water protection – protection of the Greater Sydney drinking water catchment to ensure safe water is supplied to Sydney Water, local councils and other distributors for treatment and distribution to their customers
- Bulk water supply – supplying water from its storages to customers in the Greater Sydney drinking water catchment and in the State's regulated surface water systems
- System operator – efficient management of the State's surface and groundwater resources to maximise reliability for users through the operation of the State's river systems and bulk water supply systems, in collaboration with the Murray Darling Basin Authority (MDBA) which directs operations of the River Murray system
- Bulk water supply infrastructure planning, delivery, and operation – planning, developing, owning, and operating infrastructure to meet customer-defined levels of service and in support of NSW Government policy and priorities to increase the security and reliability of water supplies to end use customers and the communities of NSW; and
- Customer water transaction services – providing efficient and timely services to end use customers for water licensing and approvals, water trades, billing and to meet their water resource information needs with respect to surface and groundwater quantity and quality.

3 Background

3.1 Scope

The overall scope of this cost allocation manual (CAM) is to provide context and explain the decision-making process on the methodology, which underlies the calculations prepared by WaterNSW within their cost allocation model. The scope of the CAM is limited to the allocation of costs to the four (4) regulated services (i.e., Greater Sydney, Rural Valleys, Water Administration Ministerial Corporation and Broken Hill Pipeline) and non-core or other services.

While there is no regulatory requirement on WaterNSW to prepare a CAM for pricing purposes, we have sought to be consistent with the principles and arrangements set out in IPART's Cost Allocation Guide¹ (Guide) and other principles and reporting requirements.

3.2 Purpose

The purpose of this Cost Allocation Manual (CAM) is to describe the cost allocation method that WaterNSW uses to allocate its costs for its separate regulated service streams.

Allocation of costs in a shared price-regulated environment is a complex exercise. This Manual explains WaterNSW's cost allocation methodology and describes how WaterNSW:

- Distinguishes between direct and indirect costs
- Attributes and allocates costs to and within WaterNSW's price regulated and non-price regulated services; and
- Calculates the costs of the WaterNSW price regulated and non-price regulated services to reflect the costs associated with the provision of each service.

By explaining the accounting basis of how costs have been, or will be, allocated, this Manual will assist WaterNSW in the development of pricing proposals for its four major pricing determinations: Greater Sydney Determination, Rural Valleys Determination, Water Administration Ministerial Corporation (WAMC), and the Broken Hill Pipeline. It also provides more transparency and confidence on how WaterNSW allocates costs.

¹ IPART, "Cost Allocation Guide – Water Industry Competition Act 2006, March 2018."

4 Operational Structure

4.1 Organisational structure

The organisation follows a hierarchy with the Chief Executive Office at the top level with all other business areas at the next level, refer to Appendix F – Organisational structure diagram for further details.

4.2 Regulated services

WaterNSW performs cost allocation to calculate the costs for its four (4) regulated services streams, which include:

- **Core business:**
 - Greater Sydney - WaterNSW is the main supplier of bulk water in the Sydney region. It manages and protects Sydney's drinking water catchments and catchment infrastructure. It supplies bulk water to Sydney Water Corporation (SWC or Sydney Water) and to three councils (Wingecaribee Shire Council, Shoalhaven City Council and Goulburn Mulwaree Council), and raw water and unfiltered water to minor customers.
 - Rural Valleys – WaterNSW provides rural valley bulk water services which relate primarily to the capture store and release of water to licence holders across 13 valleys in NSW.
 - WAMC - WaterNSW carries out on behalf of Water Administration and Ministerial Corporation certain licensing, water monitoring and billing functions formerly carried out by DPI Water on behalf of WAMC.
 - Broken Hill Pipeline Services – WaterNSW provides raw water, via a 270-kilometre pipeline, to the community of Broken Hill and a small number of landholders nearby.

4.3 Non-regulated services

Supplementary activities and Other. These are non-core projects, such as those services which do not form part of IPART's pricing determination and whose costs are excluded from the notional revenue requirements set by IPART. This segment consists of supplementary activities that are not included in the regulated business. These activities are externally funded (e.g., activities funded by Murray Darling Basin Authority, NSW Government Grant Funded project works, and unregulated commercial business opportunities).

5 Governance arrangements

5.1 Accountability

This section outlines the relevant accountabilities within WaterNSW for the implementation, continued application, maintenance/updates, internal monitoring, reporting and quality assurance of the CAM.

Specific responsibilities for updating, maintaining, applying, and monitoring the CAM are managed by Financial Planning, Analysis & Commercial, who are responsible for governance, assurance, and implementation of the CAM. Financial Planning, Analysis & Commercial will ensure that costs are allocated and reported in accordance with the CAM. This includes:

- Maintaining accounts and making records available for review
- Monitoring the appropriateness of causal drivers used
- Allocation of indirect costs, and
- Ensuring application and monitoring of costs is in accordance with the CAM.

The following table sets out the specific accountabilities and responsibilities for updating, maintaining, applying, and monitoring the application of the CAM:

Role	Accountability and/or responsibility
Chief Executive Officer	<ul style="list-style-type: none"> • Accountable for approving the CAM
Chief Financial Officer	<ul style="list-style-type: none"> • Responsible for developing and recommending the CAM to the CEO. • Ensuring systems and processes are in place to support the CAM application. • Monitoring CAM outcomes to provide assurance that the CAM outcomes are in line with the CAM Policy.
Manager Financial Planning & Analysis	<ul style="list-style-type: none"> • Responsible and accountable for applying the detailed principles and policies described in this CAM as the basis for attributing costs to, or allocating costs between WaterNSW's separate regulated service streams • Implement the CAM and maintain associated costing procedures and guidelines for staff • Ongoing responsibility for updating, maintaining, applying, internally monitoring, and reporting on the application of the CAM
All staff	<ul style="list-style-type: none"> • Comply with all relevant costing procedures and CAM guidelines

Table 1: CAM accountabilities and responsibilities

5.2 Duration and review

This CAM will be considered current and will take effect at the date approved by WaterNSW's Chief Executive Officer. The CAM will remain and be considered current until it is periodically updated and re-issued.

The CAM will be reviewed at the beginning of each regulatory pricing period. A review of the CAM may also occur in the event of major changes to WaterNSW's business that could impact the provision of services or the capture and recording of costs.

These reviews include a comprehensive assessment of the compliance of recorded expenditures with the cost allocation method outlined in the CAM.

5.3 Source data maintenance and reconciliation

Reconciliation

Upon the completion of the cost allocation process, the entries are loaded into Power BI for data analysis. In Power BI, there is a check to see that all the direct overhead (OVH) segment costs total to zero after allocation. Additionally, costs tagged as "Core" and "Not Applicable" (NOTA) and Rural All Valleys costs are also checked to ensure that they are total to zero after cost allocation.

6 Cost Allocation Principles

WaterNSW has adopted key principles in the development of its CAM. These include the principles outlined in IPART's Cost Allocation Guide, and applicable reporting requirements that reflect good practice and regulatory precedent.

6.1 IPART's Cost Allocation Guide

The causality principle in allocating costs

WaterNSW understands and interprets this principle to be that all costs (capital and operating) must be allocated to the relevant service which causes those costs to be incurred. More specifically, WaterNSW's four separate determinations are defined both by the type of service and by geographic boundaries.

As a result, direct causal costs are identified at a service level, geographic system level and an activity level. This concept is extended to a high proportion of operating costs, and further attributed to the specific services within the separate service areas. For example, the cost of maintenance activities used to maintain bulk water storage and delivery infrastructure through the Greater Sydney supply system are directly costed to this service.

Allocating costs where a causal relationship cannot be established

WaterNSW interprets this principle to mean where a causal relationship does not exist, or where it is not practicable to precisely identify and measure causal allocators, it is then necessary to substitute a close approximation to an ideal causal allocation. We use this approach for allocating our indirect common shared costs. This CAM sets out the method for allocating indirect common costs.

Total costs to be allocated

WaterNSW interprets this principle to be that the sum of costs allocated to each service must reconcile with the total costs outlined in our audited statutory financial accounts. Accordingly, we have embedded a cross-check in into our cost allocation model, as part of broader governance and quality assurance processes.

A cost should only be allocated once

WaterNSW interprets this principle to be those costs within a service, as well as between services, should only be counted or allocated once. There should be no double counting or duplication of costs across WaterNSW's separate determinations and service areas.

As with the cross-checks/governance outline in the 'Total costs to be allocated' principle, a separate reconciliation of costs with IPART's determined costs ensures that costs are only allocated once, precluding double counting or over allocation, demonstrating that cost have been neither created nor lost as a result of the allocation.

Periodic review of the basis for cost allocation

WaterNSW understands this principle to be one in which allocators should not be regarded as static or permanent, and as such causal allocators should be updated as often as is practical, to ensure casual relationships remain relevant. As part of WaterNSW's governance process, we will update allocators periodically as technologies and operations trigger change or improved allocators become available. The updating of allocators will occur through a periodic review of the allocators.

6.2 Additional principles adopted

Can be practically implemented

This principle is in addition to those outlined by IPART in its guidance. WaterNSW interprets this principle to mean that although ideal allocators are always preferred, in some cases it may not be practicable to precisely identify and measure causal allocators of cost without undue cost and effort. In such cases, WaterNSW will adopt a proxy allocator based on our understanding of the nature of the expenditure and an expectation that the proxy will result in allocations that are consistent with those that would result from an ideal causal allocator.

6.3 Basis of preparation

The financial statements for financial reporting of actual balances are general purpose financial statements that have been prepared on a going concern basis in accordance with:

- applicable Australian Accounting Standards (which include Australian Accounting Interpretations);
- applicable International Financial Reporting Standards
- the requirements of the *Government Sector Finance Act 2018 (GSF Act)*;
- Treasurer's Directions issued under the GSF Act; and
- the requirements of the *State Owned Corporations Act 1989*.

Furthermore, the budget has been prepared in accordance with NSW Treasury's Statement of Corporate Intent guidelines for State Owned Corporations. This includes, but not limited to, adherence to the following Commercial Framework Policies:

- TPG 22-02 Ownership and Portfolio Expectation Policy;
- TPG 24-27 Performance Reporting and Monitoring Policy for Government Businesses;
- TPG 21-10 Capital Structure and Financial Distribution Policy for Government Businesses; and
- TPG 23-19 Guidelines for Community Service Obligations.

7 Cost Allocation Methodology

7.1 Overview

Cost allocation is a step-by-step process that involves:

- Identifying and defining the cost objects to which costs will be assigned;
- Identifying and classifying costs as direct or indirect;
- Tracing direct costs and attributing them to the cost objects;
- Applying a method of relating indirect costs to the cost objects – i.e., allocating these to cost objects using appropriate allocators or cost drivers.

Terminology

Cost allocation relates to the attribution and allocation of a service provider's costs to its regulated and non-regulated services. In developing this manual, we have used the definitions set out in the IPART Guide and the key terms used are:

- A **cost object** is any activity or item for which costs are separately measured. Cost allocation is the process of identifying, aggregating, and assigning costs to specific cost objects. For the purpose of this CAM, each cost object represents an individual component required to provide a service. Hence each cost object can be assigned to both a system and a service level.
- **Direct costs** are costs that can be directly traceable to a specific cost object and can be attributed to a particular cost object and hence a service; and
- Costs that cannot be directly traceable to a specific cost object are **indirect costs**. These indirect costs are allocated across our services based on causal relationships.
- **Cost (or causal) drivers** are activities or attributes that triggers a cost to be incurred.

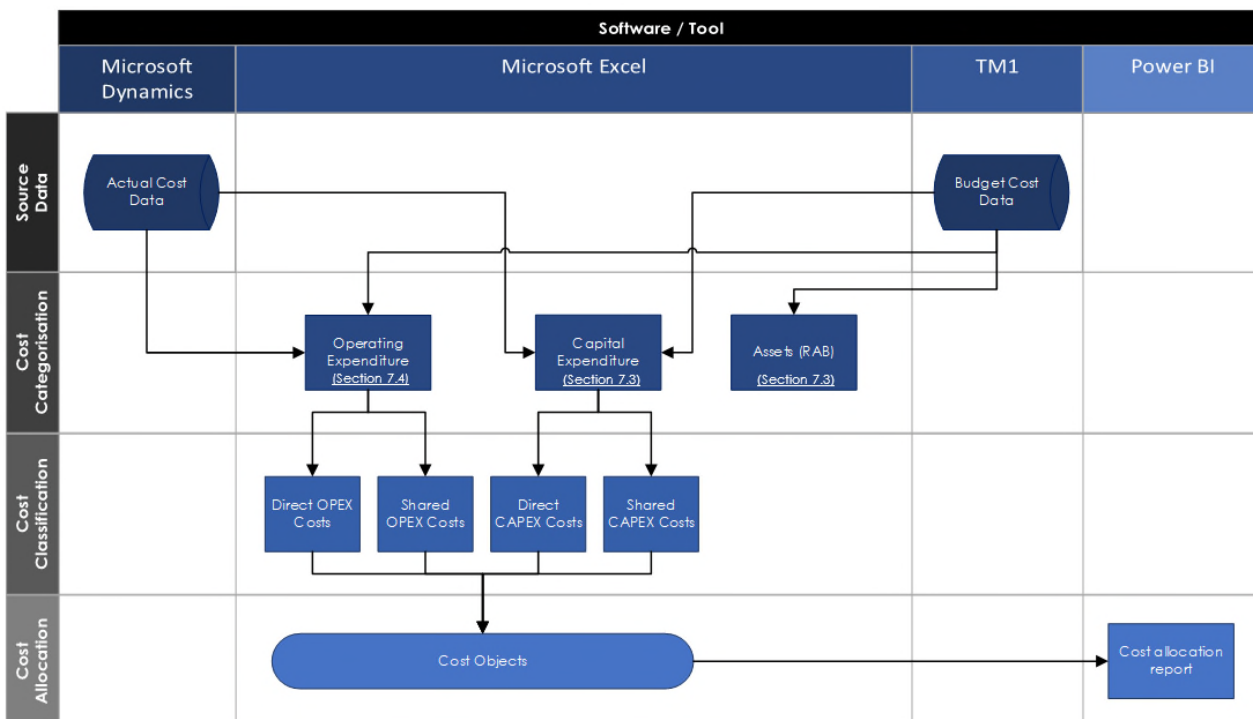


Figure 1: Cost disaggregation process

7.2 Reporting system

7.2.1 System

WaterNSW's Microsoft Dynamics 365 Financial Management System is used to capture all costs, with TM1 used for budgeting costs.

7.2.2 Chart of accounts

WaterNSW's chart of accounts and costing systems have been established such that costs (both operating and capital) can be separately accounted for and reported in accordance with the CAM and regulatory requirements. The chart of accounts structure enables costs to be attributed directly to, or to easily allocate costs between the following service categories:

- Greater Sydney services
- Rural Valleys services
- WAMC
- Broken Hill Pipeline services; and
- Non-core projects.

Each account string in the general ledger comprises 8 pieces of information, whereby each piece assists in grouping of costs for reporting by: Project, Valley, Segment, Activity as well as other reporting segments as outlined in Table 2 below.

Level	Segment	Format	Description
1	Responsibility centre	4 digit code	The area of financial responsibility assigned to a manager or supervisor, i.e. managing business unit.
2	Project and Phase	11 digit code	8 digits project, "." separator, 2 digits for phase. .1x phases are Capital Expenditure (Capex), .2x and .3x are Operating Expenditure (Opex) phases
3	Valley	2 digit code	This is the location where the project will be delivered according to mapped valleys
4	Activity centre	2 digit code	Type of work being performed (e.g., asset inspections)
5	Pricing service	4 digit code	Identifies the service category (e.g., Greater Sydney), i.e. regulatory determination
6	Business Segment	4 digit code	Identifies the segment (e.g., Core, core plus)
7	Capability	3 digit code	Identifies whether Opex or Capex and if Capex what capability
8	Cost item	4 digit code	Type of expenditure (e.g., labour, energy, chemicals), i.e. main account groupings

Table 2: General ledger account information

Projects can have multiple levels using either sub-projects or work orders to capture transactions across project phases. Projects are linked to managing responsibility centres or business units that are responsible for delivery.

7.2.3 Cost objects hierarchy

Determination	Valley	Segment	Area	Category	Business Unit (Sample ²)
Broken Hill	All Valleys	Core	Chief Executive	Catchment	Analytics & Modelling Infrastructure
	Broken Hill		Strategy & Performance		
Greater Sydney	All Valleys	Core Plus	Strategy & Performance	Dam Safety	Asset Capability
	Blue Mountains	Other	Digital	Fleet	Asset Delivery
	Shoalhaven system	Overhead	Finance Legal & Risk	Hydrometrics	Audit and Assurance
	Upper Nepean	Pass Through	Corporate Affairs	Major Projects	Board Secretariat
	Warragamba		Safety People & Culture	SCADA	BSI Analytics
	Woronora	Operations	Water Infrastructure	Catchment Protection	
	All Valleys	WNSW	NOOVH	Chief Executive Officer	
Rural Valleys	Border			Opex core	Commercial services
	Fish River			Opex non-core routine	Communications and community Media
	Gwydir			Opex non-core special	Construction Services
	Hunter				Customer Experience
	Lachlan				Digital Transformation Office
	Lowbidgee				Financial Accounting
	Macquarie				Financial Planning & Analysis
	Murrumbidgee				General Counsel
	Murray				Government Projects
	North Coast				Government Relations and Regulatory Strategy
	Namoi				Health Safety and Environment
	Peel				ICT Infrastructure delivery
	South Coast				Major Infrastructure Delivery
	WAMC	All Valleys			
Border					Operations Leadership and Support
Coastal					People and Culture
Far West					Performance and Support
Gwydir					Major Infrastructure Delivery
Hunter					Major Projects
Inland					Renewable Energy
Lachlan					Regional Contracts
Macquarie					Water Monitoring
Murrumbidgee					Water Quality
Murray					
North Coast					
Namoi					
Peel					
South Coast					
Not Applicable	All the above				

Table 3: Cost object hierarchy

² This list is a sample of the business units of WaterNSW.

7.2.4 Methodology to capture costs in system

Costs are identified as either capital expenditure or operating expenditure based on the capital expenditure policy and procedures (Refer to CD2020/66[v2]).

WaterNSW has developed a by-project approach to allocating costs into appropriate categories for the IPART price reviews.

WaterNSW's Microsoft Dynamics 365 Financial Management System is used to capture direct and indirect costs.

WaterNSW applies the following process to allocate costs across its IPART determinations:

- Work is undertaken on a project basis. Before a project is created in Microsoft Dynamics 365, the principles and procedures outlined in the Business Case Framework (BCF) have to be complied with. A Business Case should split proposed costs into direct costs and note the estimated overheads (including capitalised interest costs, indirect portfolio overhead costs and corporate overhead costs) in the Business Case. Estimated overhead rates will be provided by the relevant Portfolio Finance Business Partner (FBP). Direct costs can be directly attributable to the provision of services based on the Portfolio / valley / activity combination.
- A project is created in Microsoft Dynamics 365 after the project is approved. The project is mapped to an IPART activity code (such as 'Renewals and Replacements' or 'Environmental Planning and Protection') and a price determination (such as Greater Sydney or Rural Valleys). The project manager consults with the finance team on the appropriate classification for the project. The project classification must align with the project drivers identified in the BCF. For example, a project to construct a Fish Passage structure in Greater Sydney will be mapped to the 'Environmental Planning and Protection' IPART activity code and the Greater Sydney determination. This mapping will be supported by a BCF document identifying environmental compliance as a key driver for the project.
- Staff allocate their direct costs (e.g., time and materials) to a project. Direct costs predominately relate to labour, materials, and contractors' costs. Direct labour costs are captured in Microsoft Dynamics 365 and allocated to projects using WaterNSW's timesheet systems. Employees record their labour hours for each fortnight using KRONOS. Employees select a project for each timesheet 'punch'. Timesheets are reviewed and approved by the line manager. Contractor costs and materials are captured and allocated to projects by raising a purchase order in Microsoft Dynamics 365. The project manager selects the appropriate project for the purchase order.
- By mapping a project to an IPART funding source (pricing determination), the cost of the project is allocated to the appropriate IPART determination and incorporated into costs for the relevant determination.

7.3 Capital expenditure

Under IPART's building block approach to determining total allowed costs and setting prices, capital costs comprise a return on assets and a return of assets (regulatory depreciation), plus return on working capital and a tax depreciation allowance.

Allocating the Regulated Asset Base

WaterNSW maintains separate regulatory asset bases (RABs) for each of its regulated services. The opening asset values for these RABs were set by IPART in its initial determinations for each service.

The RABs for each service are rolled forward over the course of the regulatory period to reflect direct and indirect / shared capital expenditure in accordance with IPART's standard approach as set out in each respective determination.

Allocating direct capital expenditure

Capital expenditure that is directly attributable to a service is allocated to that service consistent with the process described in allocating direct cost for Opex, refer to [7.4.1](#).

Allocating shared corporate capital expenditure

Corporate capital projects are allocated between regulated business segments by the proportional value of Total (Opex and Capex) salary costings. IT SaaS projects are excluded from the following methodology, for further details on the IT SaaS methodology, refer to [7.4.3](#).

- The adoption of salary costing (e.g., as a proxy for FTEs) as a basis for allocation reflects the close correlation between the expenditures for the majority of corporate capital projects and the number of FTEs associated with each project. It should be noted that Broken Hill does not share in these costs.
- Corporate capital projects support the ongoing operation of the business as a whole, and include costs such as ICT renewals, ICT telecommunications, ICT Analytics, ICT automation, ICT corporate systems, office refits and refurbishments and procurement.

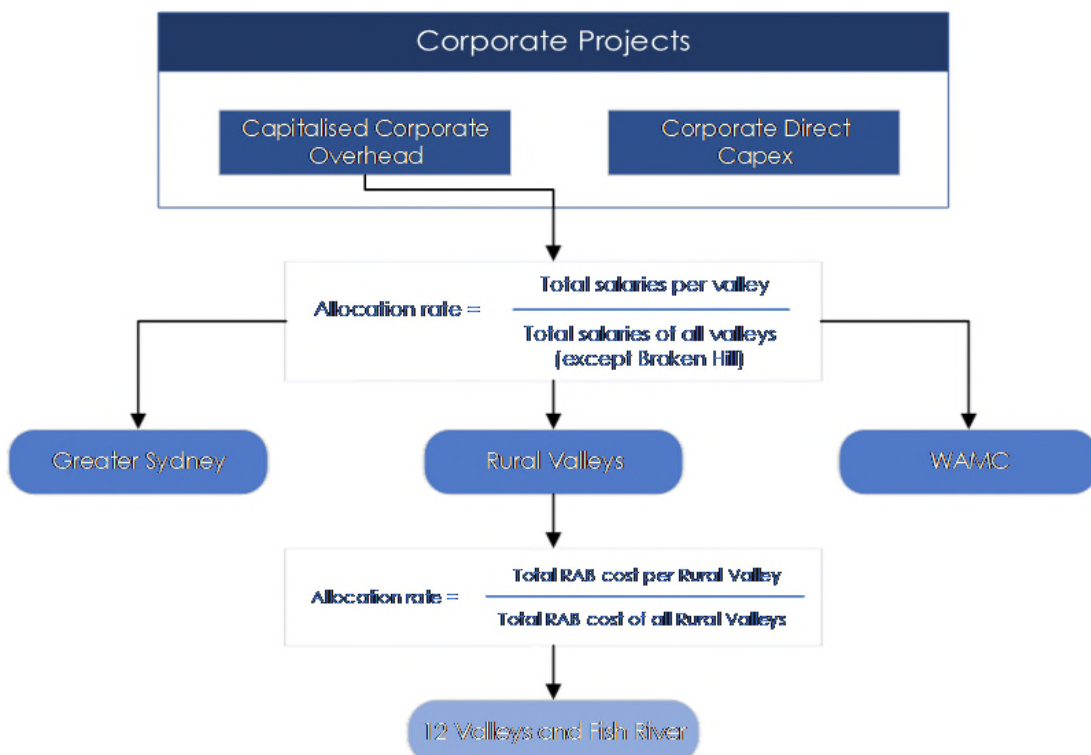


Figure 2: Allocation of Capex

7.4 Operating expenditure

7.4.1 Direct costs

Labour costs

Timesheets are used to directly attribute labour cost to projects/work orders. Staff members are responsible for attributing labour hours to appropriate projects on a regular basis accounting for all days of activity.

Based on the labour hours charged, direct labour costs are attributed to the appropriate project or responsibility centre by multiplying the number of hours charged by the individual staff member's labour rate per hour.

Non labour costs

Ring-fencing through activity-based costing

All operating costs are allocated into the following four segments:

1. **Core.** This segment consists of the regulated business activities of Greater Sydney and Rural Valleys, WAMC, and the Broken Hill Pipeline. Activities include non-contestable activities such as build / own / operation of bulk water infrastructure and water delivery⁵. The direct costs of these businesses are tagged and allocated to each of the rural valleys (Bulk water and WAMC services) and Greater Sydney/Broken Hill as appropriate.
2. **Core Plus.** This segment consists of supplementary activities that are not included in the regulated business. These activities are externally funded and include investments such as those funded by MDBA and the NSW Government.
3. **Other.** This segment represents unregulated business, whereby activities are fully contestable, and the market determines prices and volumes³. The direct costs are allocated accordingly to the segment.
4. **Overhead.** This includes the overhead costs from business units which are the operational areas within WaterNSW that are responsible for specific functions and service delivery, and corporate overheads which relate to whole of business functions.

Cost object: Cost item or Account Category

Direct costs per account category or cost item are allocated to a service as follows:

Cost item	Description	Basis for allocation	Costs allocated to
Salary and wages	Salary and wages, associated payroll on-costs and employee/industry allowances	Directly attributed through labour costing to a project	<ul style="list-style-type: none"> • Greater Sydney services • Rural Valleys services • WAMC; • Broken Hill Pipeline; and • non-core projects.

³ WaterNSW, "Chart of Accounts User Guide"

Other Employee related	Other staff related costs such as staff training.	Directly attributed to projects.	<ul style="list-style-type: none"> • Greater Sydney services • Rural Valleys services • WAMC; • Broken Hill Pipeline; and • non-core projects.
Consultancies	Consisting of consultancy fees.	Directly attributed to projects.	<ul style="list-style-type: none"> • Greater Sydney services • Rural Valleys services • WAMC; • Broken Hill Pipeline; and • non-core projects.
Materials, plant and equipment	Inventory and non-inventory (irregular) items. Includes water purchases, general materials and chemicals, ICT costs and energy costs.	The certification process for invoices requires officers to confirm the correct project/ work order is used for the costing	<ul style="list-style-type: none"> • Greater Sydney services • Rural Valleys services • WAMC; • Broken Hill Pipeline; and • non-core projects.
Contractors	Includes hire contracts such as legal services, IT services, professional services, maintenance services among others.	The certification process for invoices requires officers to confirm the correct project is used for the costing	<ul style="list-style-type: none"> • Greater Sydney services • Rural Valleys services • WAMC; • Broken Hill Pipeline; and • non-core projects.
Administration	Incorporating expenditure such as minor energy and utilities, insurances, office supplies, property expenses, land tax, council rates among other administrative costs.	<p>Directly attributed to projects.</p> <p>The certification process for invoices requires officers to confirm the correct project is used for the costing</p>	<ul style="list-style-type: none"> • Greater Sydney services • Rural Valleys services • WAMC; • Broken Hill Pipeline; and • non-core projects.

Table 4: Cost items and basis for allocation

7.4.2 Shared costs or Indirect costs

Allocation of overhead costs

WaterNSW's costs are allocated to activities and to each pricing determination for regulatory purposes. There are, however, costs that are excluded from the allocation. The costs for metering services are excluded and therefore, do not receive any allocated overhead. The following figure is a diagrammatical representation of the broad methodology used to apportion costs across activities and submissions.

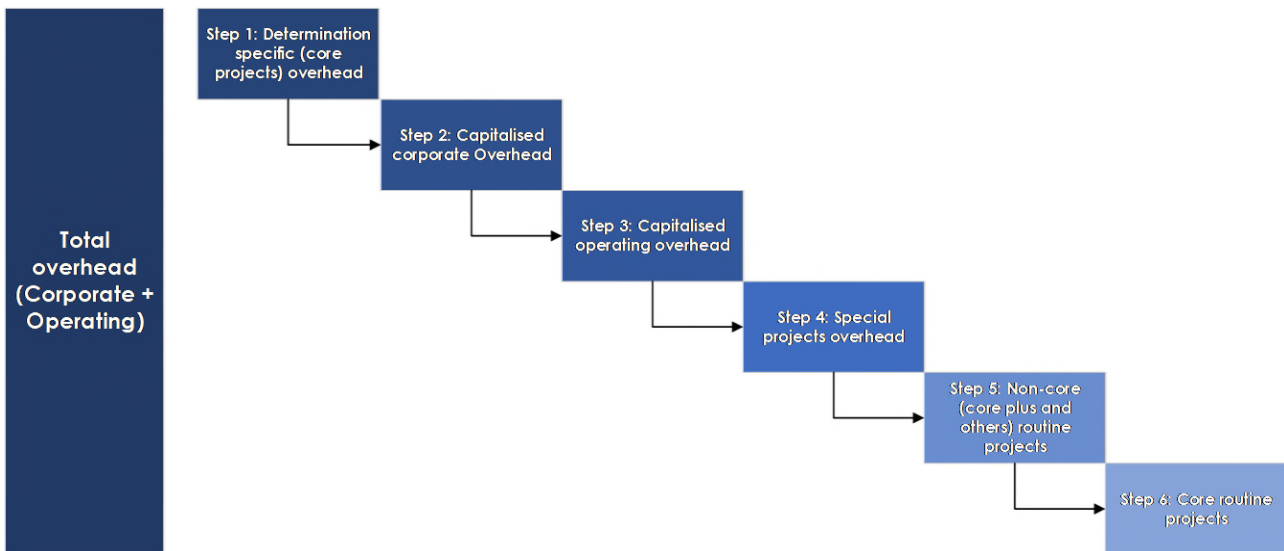


Figure 3: WaterNSW's cost allocation methodology

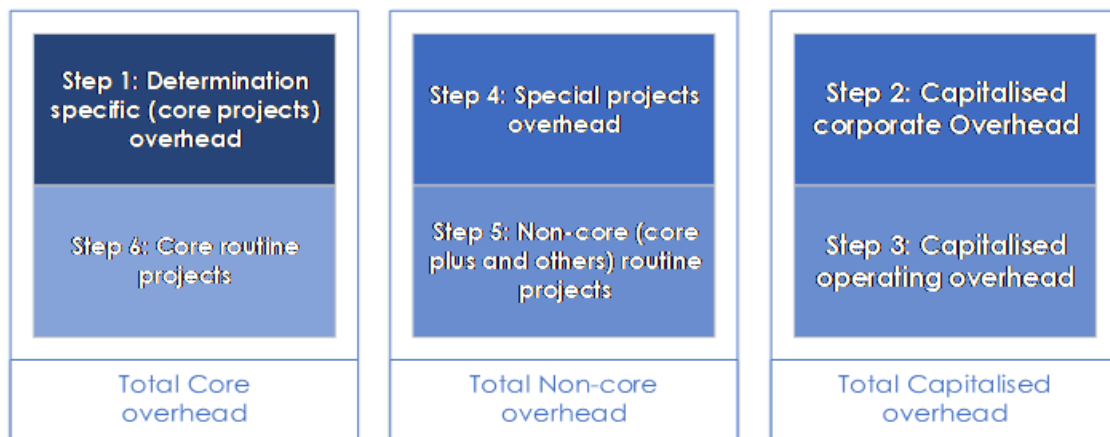


Figure 4: Overhead allocation reconciliation

Gross (or total) overhead is comprised of cost that is not directly attributed (coded) to a project or activity. This Gross Overhead is comprised of operational overhead and corporate services overhead.

Step 1 Determination-specific overhead

The first step in the overhead allocation methodology is to separate the overhead that has been assigned or allocated at source to each determination or regulated service. Gross overhead is analysed and those costs that can be specifically attributable to one of the pricing determinations are attributed directly to that pricing determination. For example, the work done on Greater Sydney submission is attributable to Greater Sydney service. As this overhead has already been identified to be directly caused by a specific determination, this overhead will not be part of the pool of overhead costs to be allocated.

Step 2 Capitalised corporate overhead

Corporate overhead is the amount of overhead that is related to the following areas:

Area Code	Area Description
A	Chief Executive
G	Digital
H & Q	Finance Legal & Risk
R	Strategy & Performance
S	Safety People & Culture
W	WNSW Corporation (a general area used for other corporate costs)

Table 5: Corporate overhead areas

Based on industry benchmarking and accounting standards, we include corporate overheads in the overhead pool for capitalisation. This is primarily based upon the corporate overhead costs being attributable to the capital project. General Ledger accounts that cannot be capitalised in accordance with the capitalisation policy are excluded from the corporate overheads to be capitalised. The excluded general ledger accounts are set out in Appendix B, which include:

- Staff Recruitment, uniforms, and training
- Hospitality and events
- Printing, stationery, and office supplies

Furthermore, intersegment transactions (e.g., Broken Hill fees) are eliminated or excluded from the operating expenses data prior to the overhead allocation to calculate the consolidated WaterNSW group operating expenses, which is the basis for allocation of overhead to the services or determinations.

The amount of overhead “tagged” to the corporate areas (or the corporate business units) in the source system (i.e., Microsoft Dynamics, TM1) form the base amount, from which the amount of capitalised corporate overhead will be calculated. There are two sub-steps under Step 2, which are:

1. Calculate amount of corporate overhead to be capitalised

Cost Driver	Proportion of Direct Capex costs and Direct Opex
Description	Percentage rate of capitalisation of corporate overhead costs
Data Source	TM1/Microsoft Dynamics
Formula	$\text{Corporate Overhead} \times \frac{\text{Direct Capex costs}}{\text{Direct Capex} + \text{Direct Opex costs (excluding overheads)}}$
Update Frequency	Monthly

Total direct Capex includes all capabilities, excluding projects where plant and fleet costs have already been capitalised.

- Allocate the corporate overhead to be capitalised to each determination

Cost Driver	Proportion of each determination's direct Capex costs
Description	Percentage allocation rate for each determination's corporate overhead costs
Data Source	TM1/Microsoft Dynamics
Formula	$\text{Capitalised Corporate Overhead} \times \frac{\text{Direct Capex per project}}{\text{Total direct Capex cost of all projects}}$
Update Frequency	Monthly

The allocated overhead costs are added to the cost base of the related fixed assets and depreciated over the life of these assets based (see section [7.3](#)).

Step 3 Capitalised operating overhead

Operational overhead are costs not directly attributable to specific projects or activities but have a relationship with the operation and delivery of service streams. These costs cannot be directly associated to a single project but are incurred to support the delivery of projects.

Operating overhead is the amount of overhead related to the following areas:

Area Code	Area Description
D	Strategy & Performance
N	Corporate Affairs
O	Operations

Table 6: Operating overhead areas

The amount of overhead "tagged" to the operating areas (or the operational business units) in the source system (i.e., Microsoft Dynamics, TM1) form the base amount, from which the amount of capitalised operating overhead will be calculated. There are two sub-steps under Step 2, which are:

- Calculate amount of operating overhead to be capitalised

Cost Driver	Proportion of total expenses
Description	Percentage rate of capitalisation of operating overhead costs
Data Source	TM1/Microsoft Dynamics
Formula	$\text{Operating Overhead} \times \frac{\text{Total Capex cost of all operating business units}}{\text{Total Expenses (Direct Opex + Capex) of all operating business units}}$
Update Frequency	Monthly

2. Allocate the operating overhead to be capitalised to each determination

Cost Driver	Proportion of total Capex costs
Description	Percentage allocation rate for each determinations operating overhead costs
Data Source	TM1/Microsoft Dynamics
Formula	$\text{Operating Overhead} \times \frac{\text{Total Capex cost per project in operating business units}}{\text{Total Capex costs of all operating business units}}$
Update Frequency	Monthly

The allocated overhead costs are added to the cost base of the related fixed assets and depreciated over the life of these assets based (see section [7.3](#)).

Step 4 Allocation of overhead to special projects

Special projects attract 10% and certain specified projects attract 20% of project direct Opex as overhead, on the basis that they are incremental to current capacity. Examples of these projects are:

- a. Ad-hoc analyses and studies funded by DPI (e.g., Lachlan Valley water security option investigation, preliminary engineering investigation for Hunter Valley); and
- b. National Water Infrastructure Development Fund (NWIDF) (e.g., Mole River Valley and Dungowan Dam feasibility study).

Step 5 Allocation of remaining overhead to core and non-core projects

The remaining balance of overheads, after capitalisation and non-core special allocation (i.e., Steps 2 to 4), is allocated to Core and Non-core projects based upon the Direct Operating Expenses ("Direct Opex") of the projects within each service stream or determination.

Examples of non-core routine projects:

- a. MDBA Constructing Authority
- b. Border Rivers Commission
- c. Mining rectification; and
- d. Third party hydropower

WaterNSW uses Direct Opex of each determination or service stream as the cost allocator for its shared Opex costs.

Direct Opex satisfies the allocation principles set out in Section 6 as:

- Direct Opex as a measure is readily observable
- The use of directly attributable costs as an allocator for indirect/shared costs is a well-established approach with regulatory precedent;
- Direct Opex is subject to independent review by IPART as inputs into WaterNSW's revenue requirement; and
- It is reasonable to expect Direct Opex to be correlated to the cost drivers associated with indirect/shared costs.

Appendix C shows an overall detailed diagram of the overhead cost allocation methodology.

7.4.3 IT Software as a Service (SaaS)

As a result of the IFRS Interpretations Committee (IFRIC) decision in April 2021, WaterNSW changed the methodology for recognition of cloud-based 'software as a service' (IT SaaS) in the financial accounts effective for the financial year ending June 2021. Generally, where a third-party supplier provides the customisation and configuration services, WaterNSW recognises the costs as an expense when the third-party supplier configures or customises the application software - effectively reclassifying these costs from capital to operating expenditure. IFRIC agenda decisions must be followed in order to comply with Accounting Standards. Accordingly, IT SaaS costs are recorded as operating expenses in the general ledger.

IPART is not bound to follow changes in accounting requirements when determining the treatment of expenditure for regulatory purposes (such costs are currently included in RAB). In lieu of guidance from IPART of a change in treatment, we continue to recognise these costs as Capex for regulatory purposes.

Process of allocating IT SaaS costs:

1. The IT SaaS projects are set up as All Valley Opex Core projects in the system and therefore do not form part of Gross Overheads referred to in Figure 3.
2. These projects are then allocated to the determinations based on allocation rates provided by the Finance Business Partners for each project as shown in Figure 5 below, which shows a sample allocation rate. Overhead will be allocated to these projects in accordance with the step-by-step methodology in section [7.4.2](#).

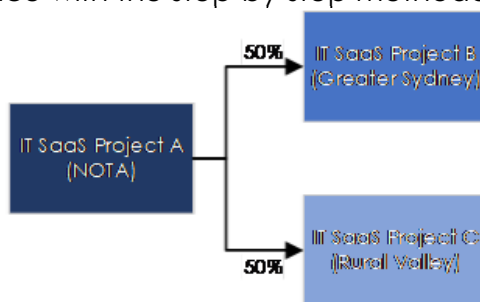


Figure 5: IT SaaS project allocation

3. "All Valley Opex projects" or projects that are not tagged specifically to a valley are distributed to each valley based upon Direct Opex share of each valley. After allocating the IT SaaS Opex costs to each valley and determination, these are re-classified as Capex in the corporate model for regulatory reporting.

8 Appendices

8.1 Appendix A - WaterNSW's regulated services⁴

WaterNSW manages a complex network of dams, storages, and pipelines to supply water to its customers across Greater Sydney and Regional NSW. WaterNSW's services include capturing and storing water, releasing and delivering water, monitoring the raw water quality and the protection of Greater Sydney's water catchment.

IPART conducts its pricing determination review for WaterNSW's Greater Sydney and rural bulk water services where WaterNSW is responsible for the management and supply of raw water in NSW across Greater Sydney, Rural Valleys, WAMC and Broken Hill.

Greater Sydney

WaterNSW is the main supplier of bulk water services to Greater Sydney, additionally WaterNSW provides managing services of Greater Sydney's drinking water catchments, dams, pipelines and other infrastructure, which includes protecting 16,000 square kilometres of drinking water catchments.

WaterNSW's major customers include Sydney Water, Wingecaribee Shire Council, Shoalhaven City Council and Goulburn Mulwaree Council. The supply of raw water is provided to urban water utilities for treatment and then consumption by Sydney, Illawarra, Blue Mountains, Southern Highlands and Shoal communities. Additionally, WaterNSW provides raw, unfiltered water to over 60 smaller customers throughout Greater Sydney.

Rural Valleys

WaterNSW manages dams, pipelines and other infrastructure which are used to provide water to meet community needs such as for domestic use and stock. The bulk water services provided consist of around 6,300 customers which include irrigators and irrigation companies, environmental water holders and local councils. The Rural Valleys consist of 13 different valleys which include 9 Murray-Darling Basin (MDB) rural valleys, 3 coastal valleys and the Fish River Water Scheme, see below for list of valleys:

MDB rural valleys:

- Border
- Gwydir
- Namoi
- Peel
- Lachlan
- Macquarie
- Murray
- Murrumbidgee
- Lowbidgee
- Fish River Water Scheme (Part)

⁴ WaterNSW, "WaterNSW_Annual-Report-2022-23"

3 Coastal valleys:

- North Coast
- Hunter
- South Coast; and
- Fish River Water Scheme (Part).

Water Administration and Ministerial Corporation (WAMC)

WaterNSW carries out a subset of functions and activities on behalf of WAMC. The activities performed include certain licensing, water monitoring and billing functions. The services provided to WAMC are shared with the Department of Planning and Environment – Water (DPE-Water) and Natural Resources Access Regulator (NRAR).

Broken Hill Pipeline

WaterNSW provides raw water to the community and owns and operates a bulk water storage facility that can supply Essential Water's need for water for around 22 days. The raw water is supplied via a 270-kilometre pipeline to the community of Broken Hill and a small number of landholders nearby.

8.2 Appendix B – General ledger accounts excluded

The following general ledger accounts are excluded from overhead costs capitalised.

General Ledger Account	Account Name
2019	Employee Redundancy
2100	Employee Recruitment
2101	PPE & Uniforms
2102	Employee Training
2104	Other Employee Related
2307	Printing and stationary
2311	Advertising and Media
2312	Sponsorships and donations
2313	Grants
2317	Office supplies
2612	WAMC - DOI/NRAR Expense
2701	MV Expenses - Repairs and Services
2807	Computer software licence / subscription
3994	Budget Adjustment Salary
2808	Computer hardware - services
2809	Computer software - services

Table 7: General Ledger accounts excluded

8.3 Appendix C – Allocation detailed diagram

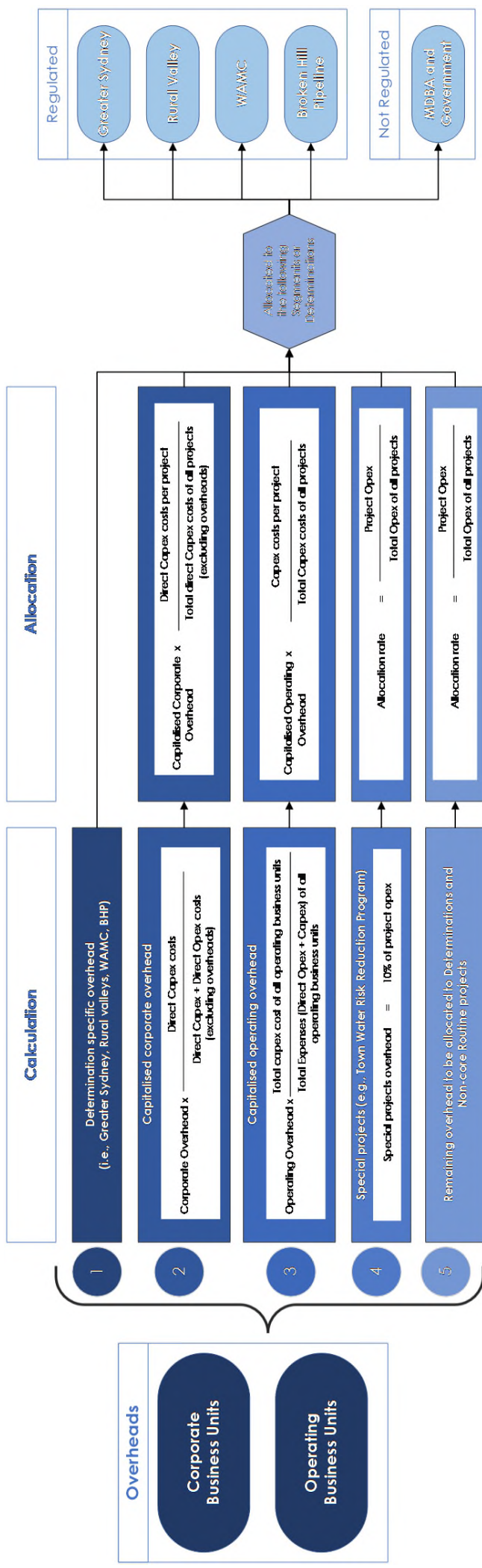


Figure 6: Allocation detailed diagram

8.4 Appendix D – Organisational structure table

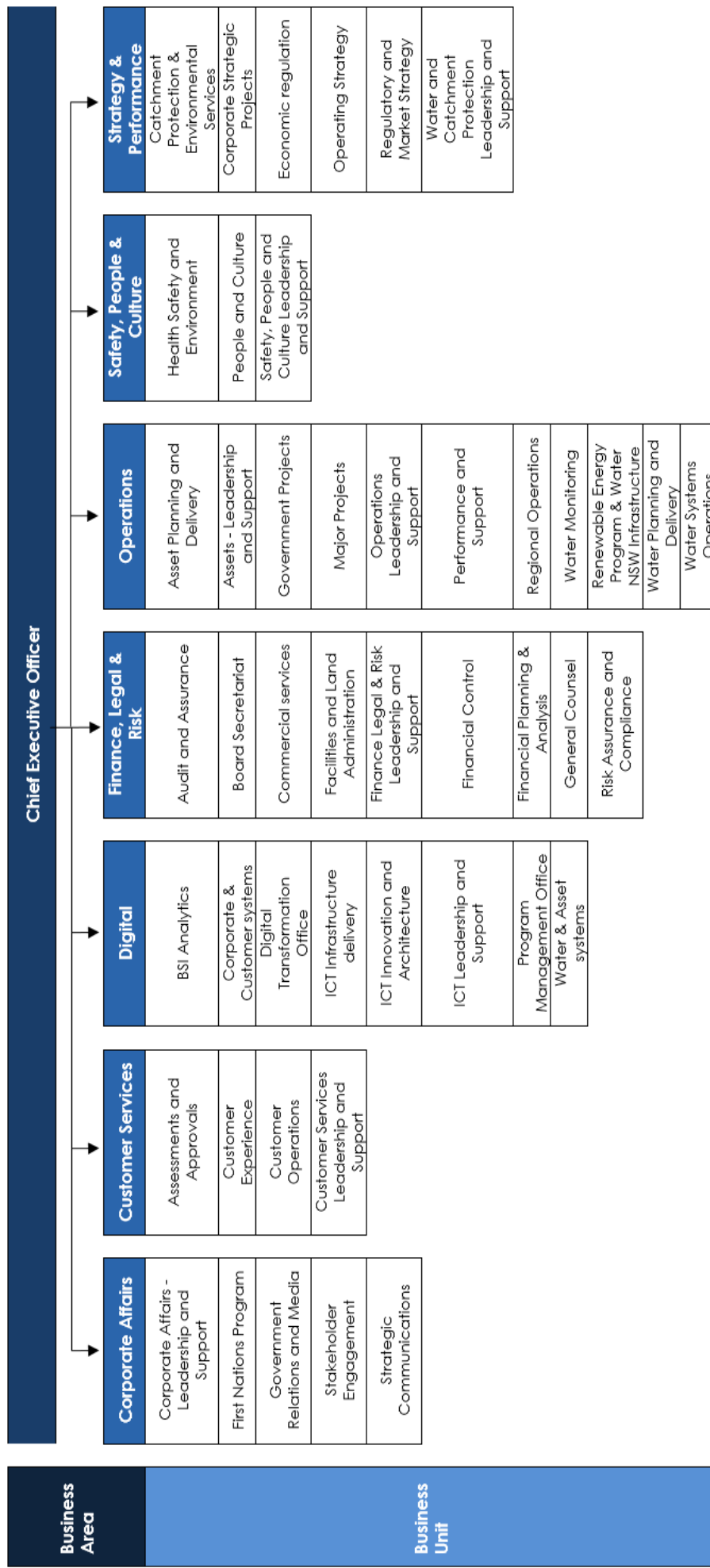


Table 8: Organisational structure

8.5 Appendix E - Definitions

Overhead cost: cost that is not directly attributed (coded) to a project or customer. For example, corporate business unit overhead.

Operational Business Unit: System Operations, Water and Catchment Protection, Assets, Water Solutions and Market Strategy.

Corporate Business Unit: Chief Executive, Safety, Legal Governance and Risk, Finance and Commercial Services, People and Culture, Business Systems, and Information

Software-as-a-Service (SaaS): These refer to arrangements that are service contracts, which provide WaterNSW with the right to access the cloud provider's application software over a contract period.

Non-core routine project (attracts a full share of overhead): Completed alongside WaterNSW Core (regulated) activities. Examples of non-core routine projects:

- MDBA Constructing Authority
- Border Rivers Commission
- Mining rectification; and
- Third party hydropower

Non-core special project (attract a percentage of 10% of project direct costs as overhead): Incremental to current capacity, for example:

- Warragamba Dam Raising
- ad-hoc analyses and studies funded by DPI, e.g., Lachlan Valley water security option investigation, preliminary engineering investigation for Hunter Valley
- Government funded projects such as National Water Infrastructure Development Fund (NWIDF), e.g., Mole River Valley and Dungowan Dam feasibility study; and

Determination-specific Overhead: Non identifiable activity costs but they can be identified to a specific pricing determination.

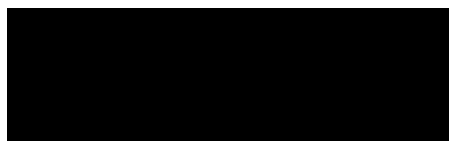
8.6 Appendix F - Chief Executive Officer's and Chief Financial Officer's statement

Section 2 of IPART's Cost Allocation Guide - Water Industry Competition Act 2006, requires WaterNSW's Chief Executive Officer and Chief Financial Officer to confirm that the information contained in the cost allocation manual is accurate and confirms WaterNSW's intention to comply with the cost allocation methodology.

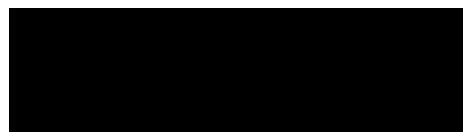
On behalf of WaterNSW, we confirm that:

- This document "WaterNSW Cost Allocation Manual" dated June 2024 sets out WaterNSW's cost allocation method in accordance with Section 42 of the Water Industry Competition Act (2006).
- WaterNSW intends to comply with the cost allocation methodology set out in this Manual.
- WaterNSW will review and update the manual as appropriate.

For and on behalf of WaterNSW.



Andrew George
Chief Executive Officer



Paul Denmeade
Acting Chief Financial Officer

20 September 2024
Date

20 September 2024
Date