



2021 Review of Water NSW's Murray River to Broken Hill Pipeline prices

Issues Paper

September 2021

Water >>



Tribunal Members

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Invitation for submissions

IPART invites written comment on this document and encourages all interested parties to provide submissions addressing the matters discussed.

Submissions are due by Friday, 22 October 2021

We would prefer to receive them electronically via our online submission form [Lodge a submission](#)

You can also send comments by mail to:

2021 Water NSW Murray River to Broken Hill Pipeline review
Independent Pricing and Regulatory Tribunal
PO Box K35
Haymarket Post Shop, Sydney NSW 1240

Late submissions may not be accepted at the discretion of the Tribunal. Our normal practice is to make submissions publicly available on our [website](#) as soon as possible after the closing date for submissions. If you wish to view copies of submissions but do not have access to the website, you can make alternative arrangements by telephoning one of the staff members listed above.

We may choose not to publish a submission - for example, if it contains confidential or commercially sensitive information. If your submission contains information that you do not wish to be publicly disclosed, please indicate this clearly at the time of making the submission. However, it could be disclosed under the *Government Information (Public Access) Act 2009* (NSW) or the *Independent Pricing and Regulatory Tribunal Act 1992* (NSW), or where otherwise required by law.

If you would like further information on making a submission, IPART's submission policy is available on our website.

The Independent Pricing and Regulatory Tribunal (IPART)

We make the people of NSW better off through independent decisions and advice. IPART's independence is underpinned by an Act of Parliament. Further information on IPART can be obtained from [IPART's website](#).

Acknowledgment of Country

IPART acknowledges the Traditional Custodians of the lands where we work and live. We pay respect to Elders, past, present and emerging.

We recognise the unique cultural and spiritual relationship and celebrate the contributions of First Nations peoples.

IPART is reviewing prices for transporting water to Broken Hill region

IPART sets prices for water transport services supplied by Water NSW via the Murray River to Broken Hill Pipeline (the Pipeline). These prices apply to Water NSW's 2 main customers:

- **Essential Water**, the supplier of water and wastewater services to customers in the Broken Hill region
- **a small number of landowners** who may take water from specific parts of the pipeline for their own use (offtake customers).

IPART last set prices for these services in 2019,¹ shortly after the Pipeline was built and first came into use. Since then, the Pipeline has helped to secure water supply in the Broken Hill region, which had experienced drought and water restrictions for many years.

Prices that Water NSW charges Essential Water for transporting water from the Murray River are a key factor when reviewing the prices that Essential Water customers in the Broken Hill region pay for water and wastewater services. For this reason, IPART is reviewing both sets of prices at the same time. For more information about this review see our [Essential Water Issues Paper](#).

The first step of this review is to consider [Water NSW's pricing proposal](#) which it submitted to IPART in June 2021, and is available on our website. This Issues Paper sets out the key issues from that proposal and what prices would be if IPART was to accept the proposal. It also outlines how we will go about this review, including how you can provide input and key questions we would like you to answer.

When we set prices for a regulated business like Water NSW, we generally aim to set prices that will cover the costs of providing services to customers. This ensures that water businesses can continue to provide safe and reliable water services into the future. We will also consider if there are any opportunities to reduce costs.

Water NSW is proposing a small bill decrease for Essential Water

We want to know your views on Water NSW's proposed price changes. While Water NSW is proposing a small bill decrease for Essential Water, it is proposing to slightly increase bills for offtake customers. Throughout this review we will look closely at the costs Water NSW has proposed and decide whether they are reasonable and no higher than they need to be. We will then use this information to set prices that apply from 1 July 2022.

Prices would vary for Essential Water and offtake customers

IPART sets prices that cover Water NSW's costs for building, operating and maintaining the Pipeline shown in Figure 1. Water NSW has proposed we continue setting different prices for Essential Water and offtake customers. It has proposed that these price changes would occur from 1 July 2022 and then remain the same for the next 5 years, as shown in Table 1 and Table 2.^a

Throughout this Issues Paper, we have presented current prices in \$2021-22. We have converted future prices over the next 5 years into \$2022-23. This is because the prices we set will start applying from next year. Our approach is different from Water NSW's proposal because Water NSW has presented all prices in \$2021-22, including all future prices. For more information please see Box 1 on page 10 of this document.

Figure 1 The Murray River to Broken Hill Pipeline



Source: Adapted from Water NSW schematic of the Broken Hill Pipeline, see [Pricing proposal by Water NSW – Plain English Summary - June 2021](#).

^a Price changes proposed by Water NSW have not factored in the impacts of inflation. IPART sets prices to update automatically each year to factor in inflation, based on the Consumer Price Index (CPI).

Proposed bills for Essential Water to decrease by around 3%

The overall bill Essential Water pays for water from the Pipeline is expected to be around 3% lower than it is currently. Table 1 shows that Water NSW has proposed continuing to charge Essential Water:

- A fixed charge, which covers fixed costs for building and maintaining the pipeline. Water NSW proposes to decrease this charge by around 3%
- A usage charge per ML of water supplied, which covers variable costs of transporting water through the pipeline. Water NSW proposes to increase this charge by around 6%²

While there is a small increase in the average price for Essential Water, because usage charges make up a small component of the bill, overall bills will decrease by around 3%.

Table 1 Essential Water's forecast bill (\$2022-23)

	2021-22 ^a	2022-23	2023-24	2024-25	2025-26	2026-27
Fixed charge (\$/day)	67,281	65,290	65,112 ^b	65,290	65,290	65,290
Variable charge (\$/ML) - non-drought	213	227	226	226	226	225
Forecast bill for Essential Water (\$'000s)	25,747	25,099	25,088	25,081	25,074	25,068

a. Bill in 2021-22 is presented in \$2021-22 and forecast bills for 2022-23 to 2026-27 are presented in \$2022-23.

b. The proposed daily fixed charge is lower in 2023-24 because it is a leap year, the annual fixed charge would be the same as other years.

Source: Water NSW, Pricing Proposal to IPART, June 2021, p 76 and IPART analysis.

Seek Comment



1. What are your views on the proposed prices for Essential Water?

Proposed bills for offtake customers to increase by around 1%

The overall bill for a small existing offtake customer using 10ML of water a year is expected to be around 1% higher than it is currently. Table 2 shows that for existing offtake customers, Water NSW has proposed continuing to charge:

- a fixed charge to cover Water NSW's additional fixed cost for providing the offtake^b, which is expected to decrease by less than 1%
- a usage charge per kilolitre of water supplied, the same as paid by Essential Water which is expected to increase by around 6%³

Water NSW has proposed that any new offtake customers over the next 5 years would have the option to either:

^b Water NSW levies a fixed charge to all but one offtake customer. This customer allowed a bulk storage facility to be built on their land in exchange for an offtake.

- pay the same fixed and usage prices as existing off take customers, or
- pay the capital cost of their offtake up-front and then pay only the usage charge.⁴

Table 2 Offtake customer prices (\$2022-23)

	2021-22 ^a	2022-23	2023-24	2024-25	2025-26	2026-27
Fixed charge (\$ per year)	7,585	7,566	7,566	7,566	7,566	7,566
Usage charge (\$/kL)	0.21	0.23	0.23	0.23	0.23	0.23
Upfront capital charge for new offtakes (\$) ^b	77,319	79,252	79,252	79,252	79,252	79,252

a. Prices in 2021-22 are presented in \$2021-22 and forecast prices for 2022-23 to 2026-27 are presented in \$2022-23.

b. Currently Water NSW can install additional offtakes for new offtake customers through an unregulated pricing agreement.

Source: Water NSW, [Pricing Proposal to IPART](#), June 2021, p 78, IPART analysis.

Seek Comment



2. What are your views on the proposed prices for offtake customers?



3. Should new offtake customers pay the same prices as existing customers? Or should they also have the option to pay the capital cost of their offtake up-front and then only pay the usage charge?

Prices for shutdown, standby or restart proposed to remain unregulated

Under certain circumstances, Essential Water can request Water NSW shut down and restart the pipeline, which creates additional costs for Water NSW that can be recovered through prices. Water NSW has proposed IPART continue to leave these prices unregulated for the next 5 years, as is currently the case.⁵

In 2019 we decided it was up to Water NSW and Essential Water to negotiate shutdown, standby and restart prices. This was to encourage Essential Water to only request a shut down when the benefit of doing so outweighs the cost.⁶ We are seeking your views on whether these prices should continue to be unregulated.

Seek Comment



4. Should shutdown, standby or restart charges remain unregulated?

Overall proposed costs for the Pipeline are decreasing

To set prices, we will look at whether Water NSW's costs for the Pipeline are reasonable and no higher than they need to be for both:

- costs incurred during the 2019 determination period
- costs proposed for the 2022 determination period.

The Pipeline's costs include:

- **Financing costs** which mostly cover how much Water NSW would need to pay its lenders and shareholders for funding the construction of the Pipeline. These costs are known as 'return on assets'.
- **Depreciation costs** which recover the capital cost of the Pipeline over a long period of time
- **Ongoing maintenance and repair costs** which are expected to be low since the Pipeline was built recently
- **Direct operating costs** such as contractor costs, energy costs and corporate support costs
- **Other costs** such as paying taxes.

This Issues Paper outlines the key costs from Water NSW's proposal that are impacting prices. We will review these costs to ensure they are reasonable and no higher than they need to be.

Lower interest rates expected to reduce the cost of financing the Pipeline

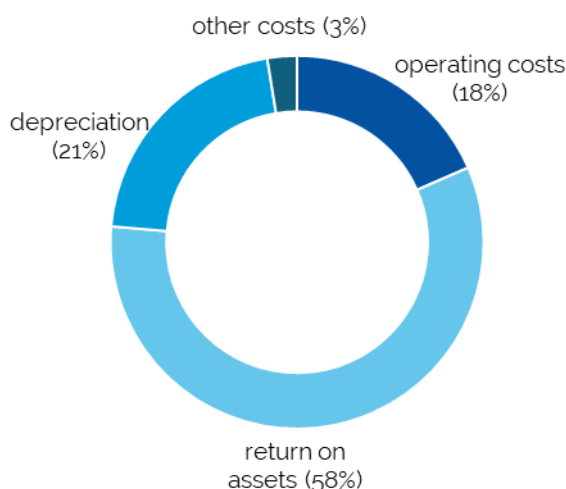
Like many businesses, Water NSW needs to finance its operations so it can continue to provide services. It does this by borrowing money from lenders and by attracting shareholders to invest in its business.

Over the next 5 years, Water NSW expects to have lower financing costs partly due to current low interest rates.⁷ Financing costs (or return on assets) make up around 58% of the Pipeline's total proposed costs (see **Figure 2**). Therefore, the decrease in financing costs is the key driver of the proposed decrease in prices for Essential Water.⁸

When setting prices, IPART makes an allowance using a standard method to cover these financing costs. Throughout this review we will look at whether the costs proposed by Water NSW for the Pipeline reflect this method and decide how much we should allow.

For more information on these costs see [Water NSW's proposal for the Pipeline](#).

Figure 2 Water NSW's proposed costs over the next 5 years



Source: Water NSW pricing proposal, IPART analysis

Higher operating costs are expected to offset some reductions in financing costs

Water NSW expects operating costs for the Pipeline will increase. These costs include paying its contractor to operate and manage the Pipeline, energy bills, corporate support costs and other costs such as taxes and insurance premiums.

Around 40% of the Pipeline's proposed operating costs relate to paying its contractor who operates and maintains the Pipeline.^c In our 2019 review, we assessed the cost of this contract and decided it provided good value for money for customers.⁹ Over the next 5 years, Water NSW expects these contract costs to increase.¹⁰

Energy costs represent around a third of operating costs. These costs vary depending on when the Pipeline requires energy to pump water, the volumes of water being pumped and what the energy price is at the time. When we last set prices, we extensively reviewed the approach for estimating energy costs to ensure good value for money. Over the next 5 years, Water NSW proposes a similar approach and expects energy costs to decrease as result of lower energy prices.¹¹ However, if energy costs change over the next 5 years, Water NSW proposes to recover these costs from customers next time we review prices.¹²



Water NSW proposes to pass on changes in energy costs to customers next time we review prices for the Pipeline. This means future prices for the Pipeline could increase or decrease depending on changes in energy costs.

^c John Holland Pty Ltd Joint Ventures has a 20-year contract with Water NSW.

Around 15% of the Pipeline's operating costs relate to corporate support costs and other costs. Water NSW expects these costs to be higher than what was allowed the last time we set prices.

We will look at the operating costs Water NSW has proposed for the Pipeline to ensure they are reasonable and no higher than they need to be.

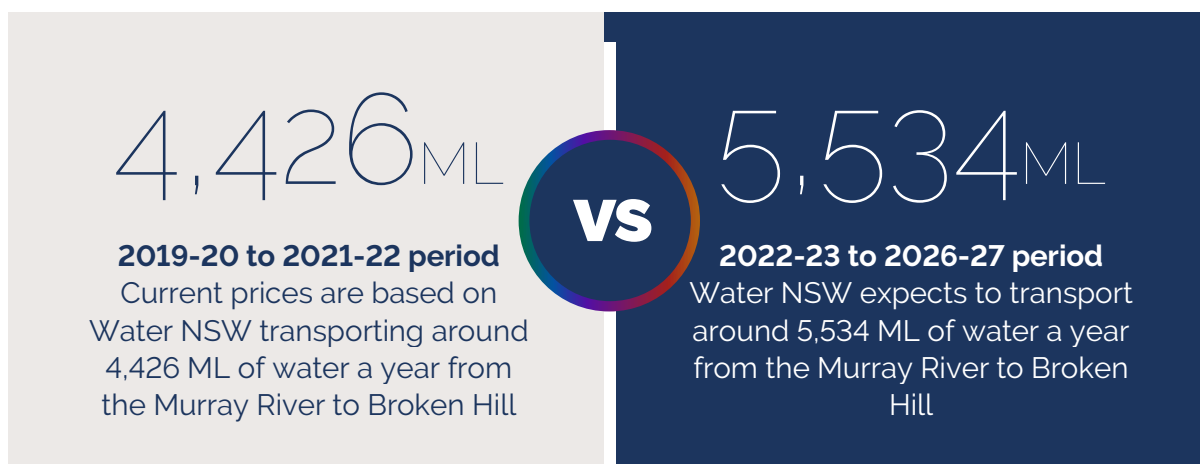
Water NSW expects to transport more water from Murray River to Broken Hill using the Pipeline

Once we decide if the Pipeline costs are reasonable, to set prices we will divide those costs by the amount of water we expect the Pipeline to transport over the next 5 years. Our expectations about water volumes need to be reasonably accurate so that prices generate enough money to cover costs.

Water NSW expects Essential Water to transport more water from the Murray River to the Broken Hill community using the Pipeline. This is different to what we expected in our 2019 review. At the time, we estimated Essential Water would need less water transported by the Pipeline to meet 70% of the community's water demand. We understand that Essential Water needed the Pipeline to transport water to meet almost 100% of the community's water demand from the Pipeline since 2019. Over the next 5 years, Water NSW expects Essential Water to continue to rely on the Pipeline to transport majority of water for the Broken Hill community.¹³

There may be many reasons for Essential Water to use the Pipeline. For example, transporting water from the Murray River using the Pipeline may be cheaper, provide greater water security particularly during drought or the water from Murray River could be better quality than what is available from Essential Water's reservoirs. For this review, we will assess the reasoning behind the water demand assumptions and ensure that customers (Essential Water and the Broken Hill community) do not pay more than they need to. We will set prices to represent the best value for your money.

Figure 3 Comparison of historical and proposed water sale volumes



Source: IPART analysis.

Seek Comment



5. What affects how much water is transported from the Murray River to Broken Hill to meet the water needs of Essential Water and offtake customers? Why might these customers be transporting water from the Murray River less or more water?
6. What are the barriers or opportunities to transport more water from the Murray River using the Pipeline new customers in the Broken Hill region?

We may set Water NSW's prices for a longer period

In the 2019 review, we set Water NSW's prices for 3 years. Since then, the Pipeline has been in use and Water NSW can more easily forecast demand and costs. Therefore, it proposed we now set prices for 5 years and allow it to pass the costs of certain unforeseen events through to customers.¹⁴

There are benefits and risks from a longer pricing period

We see the following benefits in setting prices for 5 years:^d

- it locks in prices for longer, so customers can budget their future bills,
- it provides funding certainty for Water NSW, so it can better plan its projects,
- it encourages Water NSW to become more efficient, which will benefit customers through lower prices in future periods.

However, a long pricing period also creates a risk that if unexpected costs arise during the pricing period, Water NSW may not be able to cover them through its existing prices.

Water NSW proposes to re-allocate risk to its customers

Water NSW wants to reduce the risks it faces from a longer pricing period. It proposes to 'pass-through' the costs of the following unexpected events to its customers by changing prices during the period:¹⁵

- Changes to its regulatory environment, taxes or required service standards
- Natural disaster or terrorism events
- Issues with its insurance coverage or an insurer becoming insolvent.

It considers this will allow it so to recover the costs of events beyond its control.

^d We are currently reviewing the way we regulate water businesses and set prices. As part of the regulation review, we are seeking feedback on moving to a 6-year determination period, with a formal 'health check' at the 3-year mark. For further information, please refer to our [Discussion Paper](#) on encouraging innovation in the water sector. Since we will not finalise the regulation review until 2022, we are not looking to bring in a 6-year determination period for the Water NSW Pipeline review.

Water NSW's cost pass-throughs increase its customers' exposure to risk and may lead to price increases if certain events arise

These cost pass-throughs are similar to measures other utilities have requested for recent pricing reviews, but we did not consider were appropriate. At this stage, Water NSW has not provided us with new information which would appear to change our position from previous reviews.


Allowing costs that are so unknown to be passed through unconditionally would create poor incentives for the businesses – they are assured of cost recovery regardless of their actions. Customers risk paying too high a price for an event that is vastly different to what was expected when the pass-through was allowed.

The risk of unexpected events occurring is not new. Rather than implementing cost pass-throughs, it is important for Water NSW to have an incentive to manage this risk. For example, planning for and engaging with potential regulatory changes, insuring against risks where possible and taking actions to limit the impact of events if they occur.

If an unexpected event does have a large negative impact on Water NSW's financial position, it may be more appropriate for it to request an early price review.

Seek Comment

 7. Should we set Water NSW's prices for 5 years?

 8. Do Water NSW's cost pass-through events place too much risk on customers?

We will consider your views in our price review for the Pipeline

We are seeking submissions to this Issues Paper from all interested stakeholders by 22 October 2021. [Page ii](#) at the front of this document explains how to make a submission. In March 2022 we will release a Draft Report with our draft prices for the Pipeline. In setting draft prices we will consider stakeholders' submissions and responses to the questions in this Issues Paper (see list below), and the results of our analysis of Water NSW's proposal. All stakeholders, including Water NSW, will have another opportunity to provide comments on our draft prices and participate in our public hearing.



Seek Comment

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Box 1 IPART's approach to converting prices to account for inflation

We conduct the review of Water NSW's Broken Hill pipeline prices over the current year (the 2021-22 financial year). Therefore, we present final prices and costs in this financial year's dollars (\$2021-22). However, since the prices we set are for the 2022 determination period and will start applying next year, we will need to inflate the prices to the next financial year's dollars (\$2022-23).

The applicable rate we will use to inflate the prices are based on the March inflation rate (which will be released April 2022). At this point we do not know what the March inflation rate is, so we have assumed it to be 2.5%.

Box 1 IPART's approach to converting prices to account for inflation

In this Issues Paper, we have presented the prices and bill impacts consistent with the pricing approach that we will use to set prices in the Final Report. That is, current prices are presented in \$2021-22 and future prices (for years 2022-23 to 2026-27) in \$2022-23 (including a 2.5% inflation rate).

Our prices are different to Water NSW's proposal. This is because Water NSW has presented all prices and bills in \$2021-22. That is, their proposal does not include the impact of inflation (i.e. forecast 2.5% inflation rate).

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References

- ¹ IPART, [Prices for Water NSW's Murray River to Broken Hill Pipeline services from 1 July 2019](#), accessed 15 September, 2021.
- ² Water NSW, [Pricing Proposal to IPART](#), June 2021, p 72.
- ³ Water NSW, [Pricing Proposal to IPART](#), June 2021, p 77.
- ⁴ Water NSW, [Pricing Proposal to IPART](#), June 2021, p 78.
- ⁵ Water NSW, [Pricing Proposal to IPART](#), June 2021, p 78.
- ⁶ IPART, [Murray River to Broken Hill Pipeline Water NSW - Final Report](#), May 2019, p 89.
- ⁷ Water NSW, [Pricing Proposal to IPART](#), June 2021, pp 53 and 59.
- ⁸ Water NSW, [Pricing Proposal to IPART](#), June 2021, pp 53 and 59.
- ⁹ IPART, [Murray River to Broken Hill Pipeline Water NSW - Final Report](#), May 2019, p 22.
- ¹⁰ Water NSW, [Pricing Proposal to IPART](#), June 2021, pp 35-36.
- ¹¹ Water NSW, [Pricing Proposal to IPART](#), June 2021, pp 36-37.
- ¹² Water NSW, [Pricing Proposal to IPART](#), June 2021, p 36.
- ¹³ Water NSW, [Pricing Proposal to IPART](#), June 2021, pp 67-68.
- ¹⁴ Water NSW, [Pricing Proposal to IPART](#), June 2021, p 3.
- ¹⁵ Water NSW, [Pricing Proposal to IPART](#), June 2021, p 30.