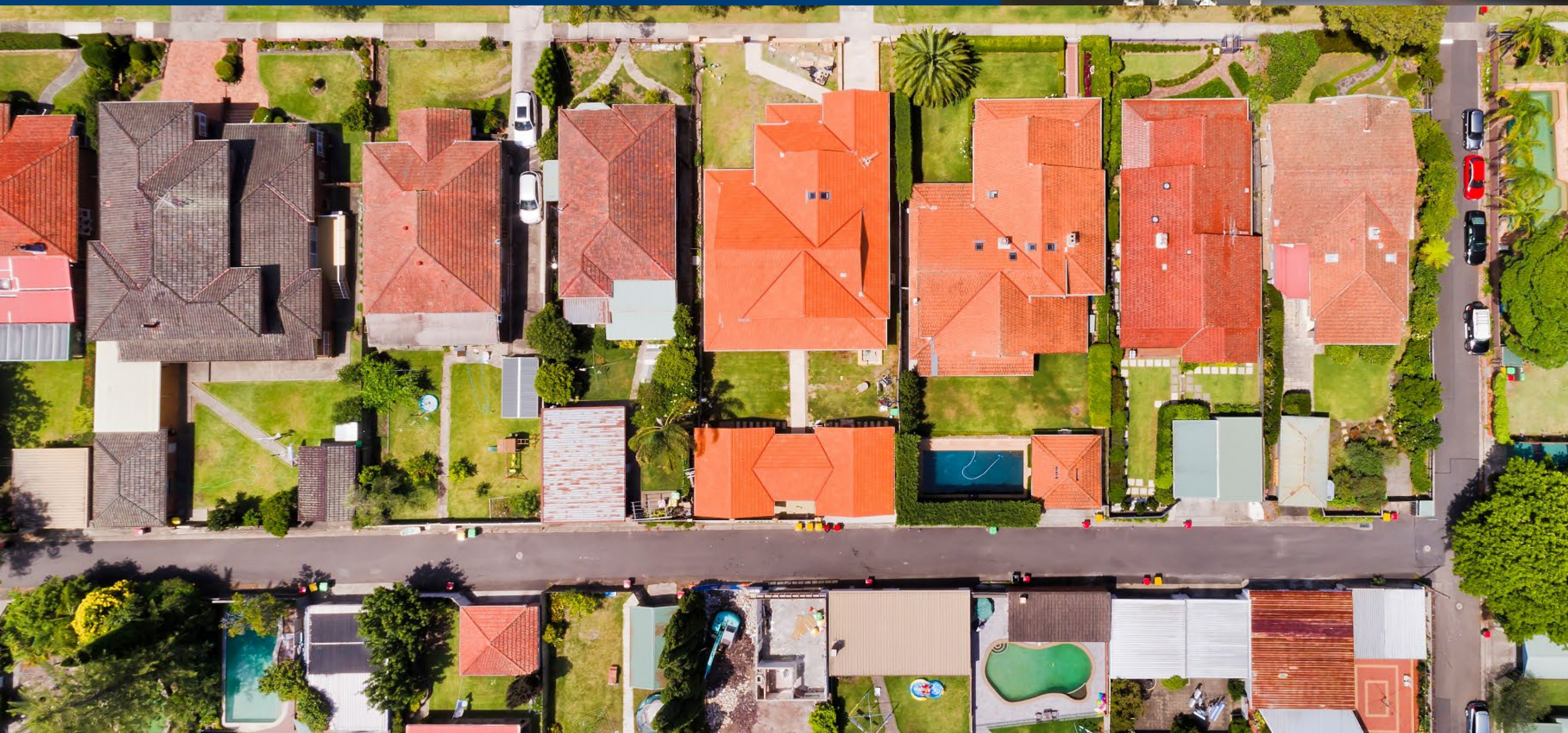
WATER SERVICES
ASSOCIATION OF AUSTRALIA

WSAA SUBMISSION TO IPART DRAFT REPORT – REVIEW OF PRICES FOR SYDNEY WATER

23 June 2025



Submission to IPART Draft Report – Review of prices for Sydney Water

Background

Thank you for the opportunity to provide a submission on IPART's Draft Report – Review of prices for Sydney Water.

WSAA made a submission in response to IPART's Issues Papers for the Hunter Water and Sydney Water pricing proposals. Our submission made a clear case that the Australian water sector needs to significantly increase investment to meet the challenges of population growth, ageing assets and climate change. We noted that this will require customers to pay more. Our submission made three central points:

1. **Investment is increasing significantly across the water sector**

   It represents a step change, rather than a once off peak. The proposals from the NSW water utilities are typical of what we expect to see across the sector at this time.
2. **There are risks if investment is not made**

   The UK provides lessons in the risks of not matching investment to the needs of customers.
3. **Cost of living is a significant issue, but we should not kick the investment tin down the road**

   There are several ways of handling a cost-of-living crisis. Deferring investment carries significant risks.

The previous submission is available here and on IPART's website.

In light of IPART's draft decision this submission focuses on the issue of risk, specifically the risk of deferring investment in water infrastructure for Sydney.

IPART's draft Sydney Water determination

Under IPART's Draft Report prices would increase by an average 4.6 per cent a year in real terms over the next 5 years. The price increases reflect increases in operating and capital costs. IPART's draft decision is that the revenue Sydney Water needs to cover its efficient costs is around $3.5 billion a year on average across the 5-year determination period. IPART states:

> *"it is $300 million per year or 9% higher than we used when we set its prices in 2020, which reflects our view that efficient expenditure needed to deliver services has increased."*

However, IPART has reduced allowed operating and capital costs well below the level proposed by Sydney Water. It has reduced:

- core operating expenditure by $438 million or 6% over the 5-year determination period
- capital expenditure on infrastructure by $5.9 billion or 35% over the 5-year determination period.

Focussing on capital expenditure IPART has reduced:

- proposed growth expenditure to service new homes by from $10.1 billion to $6.7 billion
- expenditure on renewals from $5.5billion to $3.7 billion.

The reduction in renewals includes excluding most of the Pretreatment Program costs for water treatment plants ($957 million or 75 per cent of the program costs).

In forming this judgement IPART and the Efficiency Reviewers have not found that Sydney Water's proposed capital expenditure is unnecessary. Rather they have found that it is not necessary at this time and can be deferred to future pricing periods.

Different assessment of risk

At the heart of the differences between IPART's Draft Report and Sydney Water's proposal is a different assessment of risk.

WSAA considers it is appropriate that economic regulators examine the trade-off between risk and affordability made by utilities. For their part utilities are continually making these assessments. Managing and prioritising capital expenditure to the areas of highest risk is a key part of the planning processes for water utilities as complex infrastructure providers.

Considering risk forms an integral part of the Efficiency Review conducted as part of the determination. For example, the third objective in the scope of the Efficiency Review was:

> *an overall assessment of whether the level of risk each business is taking (both financially and operationally) is appropriate.*

The scope of work sets this out in more detail.

> *The consultant should look at Sydney Water's approach to risk wholistically, and comment on:*
>
> *e. Whether Sydney Water is optimising trade-offs between prices and service levels efficiently (that is, in a way that a competitive business might)*
>
> *f. Employing an appropriate level of risk when planning for asset renewals and service growth. This may include whether:*
>
> - *Sydney Water's risk appetite is appropriate*
> - *Sydney Water's actual and/or forecast risk position is in line with the efficient risk appetite.*
>
> *g. The sophistication of any risk systems that Sydney Water uses to inform decision-making.*

The Efficiency Review (and the Draft Report) do not have a separate section dealing explicitly with this part of the scope. However, the Efficiency Review makes many comments in relation specific programs or projects. For example, in relation to renewals capex the Reviewers said:

> *In general we have found that Sydney Water has not justified that current levels of asset risk are too high and that customers should pay to increase expenditure and reduce risk.*

And IPART's Draft Report states:

> *We found that Sydney Water will need to spend more than it has previously on building new, and replacing existing, infrastructure. But we are not persuaded that Sydney Water's proposed level of future expenditure was justified or achievable. In making our draft decision, we considered the appropriate level of risk Sydney Water should accept, the needs of customers, environmental performance, the provision of infrastructure to service growth, water security and other emerging issues. We also considered the independent expert advice provided to us by AtkinsRéalis.*

Therefore, the Efficiency Review and the Draft Report has formed a view that Sydney Water is being too risk averse in its approach to investment, and $5.9 billion in capital expenditure can be deferred without material impact on customers or service delivery.

WSAA is unaware of a larger reduction in investment from that proposed by the utility in any recent regulatory determination. It is a significant reprofiling of Sydney Water's proposed investment. WSAA considers this also represents a fundamental reprofiling of the risk in Sydney Water's operations and ultimately the risk faced by the current and future customers of Sydney Water.

In view of the scale of this deferral, WSAA believes the proposition that Sydney Water, has across the board, been too risk averse in its approach to investment needs to be much more widely tested beyond the Efficiency Review between now and the Final Determination. Specific questions are:

- Can Sydney Water meet the NSW Government's housing targets with the reduced expenditure proposed by IPART?
- Can Sydney Water continue to meet environmental performance and service standards if critical sewer mains investment is deferred?
- Is there acceptable water system resilience and capacity if pre-treatment works are deferred at major water treatment plants?

Sydney Water has the opportunity to provide detailed analysis on the impact of details of operating cost and capital expenditure reductions. Nevertheless, WSAA also has some high-level observations as outlined below.

Sydney Water's expenditure has been efficient to date

IPART has found that Sydney Water's expenditure over the last determination period is efficient. This included a significant planned increase in capital expenditure. Indeed, as set out in the Draft Report, Sydney Water exceeded its capital expenditure allowance set by IPART for 2019-2025 to meet the needs of its regulatory and customer obligations. It has published its Long Term Operating and Capital Plan (LTCOP) which is the most comprehensive long-term plan released publicly by an Australia utility.

If Sydney Water has got its investment and risk trade-off right in the past, it begs the question, on what basis has Sydney Water got it wrong for the future?

The expenditure is necessary

As noted above, neither IPART nor the Efficiency Reviewers have questioned the need for the increased investment. It is only the timing of that expenditure which is in question.

Deferring expenditure does not make the need for investment go away, it shifts it to the next regulatory period. The savings from deferral are not $5.9 billion. Rather, the amount saved is the rate of return (and depreciation) on the additional investment for the relatively short period of the deferral. It is these limited savings which must be weighed against greater levels of risk. On WSAA's, albeit simple, calculations the bill impact of the total deferral is around 7 per cent by the end of the determination (see attachment 1 at end of submission). This is the risk return trade-off which stakeholders should keep top of mind.

Deferring expenditure can compound future problems

Sydney Water's proposal sequenced its investment according to its LTCOP. The primary driver of that investment is the need during the current period and the risk to the environment and customers if the investment is not undertaken.

However, WSAA notes that the LTCOP does not show a once-off peak in investment, rather a significant step change. This is the pattern of future investment we see across Australia. There is evidence of a permanent increase in investment necessary to provide housing, maintain ageing assets and provide water security.

If there was a once off peak, deferring expenditure, while exposing the community to greater risk, could at least smooth bill and customer impacts. But this is not the future of water investment in Sydney or elsewhere in Australia. In this environment, deferring necessary investment exposes the community to both an increase in current risk and compounds future investment needs and pricing impacts. As WSAA has reasoned many times before, kicking the tin down the road is not in the long-term interests of consumers.

Transparency is key to the final determination

While it is an unintended outcome of the Draft Report, WSAA considers that customers' views have inadvertently been left behind. When there is a small difference between a utility proposal and a regulator's decision the nexus between what customers were consulted on and what they receive is maintained. However, the consequence of such a large deferral of capex is that the proposition in the Draft Report is significantly different to what Sydney Water consulted on with its customers. There has been little opportunity for customer input into their willingness to pay for potentially lower customer outcomes. The survey approach IPART has undertaken following its Draft Report does not appear to meet all the expectations of IPART's CCC framework for customer engagement.

The best way forward would appear to be a transparent process between now and the Final Report.

As noted above WSAA considers that given the scale and importance of the Draft Report wider testing should take place on the prudency of deferring $5.9 billion in capital expenditure. We believe this should involve the views of a wider range of Government stakeholders to provide customers and the community with assurance that the trade-offs in the final determination are correct – or flag what adjustments are necessary. The views of the health and environment regulators of Sydney Water appear to represent the best proxy for customer and community views at this stage.

IPART and the Efficiency Reviewers have been explicit and transparent in the expenditure they think should be deferred. WSAA considers, if they have not already done so, that IPART should formally and transparently seek the views of other regulators on the deferrals within their remit. For example:

- Is NSW Health comfortable that Sydney Water can maintain a sufficient quantity and quality of water during the well documented and increasingly severe extreme events impacting the Warragamba Dam catchment and the Hawkesbury Nepean River?
- Is the NSW Environment Protection Authority comfortable that Sydney Water will be able to meet its environmental obligations with deferred renewal expenditure?
- Is the NSW Department of Planning, Housing and Infrastructure and NSW Minister for Housing confident that Sydney Water can meet both Federal and State housing targets with reduced expenditure?
- Is the Australian Department of Infrastructure, Transport, Regional Development, Communications and the Arts comfortable Sydney Water will be able to meet the terms of its authorisation to pollute?

As just one example IPART seeks comment on pretreatment costs, saying:

> *Our draft expenditure decision excludes most of the Pretreatment Program costs ($957 million or 75% of the program costs) in the capital allowance, as the case for the program in this determination period is not strongly justified. Are you comfortable with this trade-off of costs and benefits? Or would you prefer to pay higher water prices to ensure higher water quality in exceptional or unusual events?*
>
> *What are the respective benefits and risks associated with the proposed Pretreatment Program?*

These are the sort of questions where we consider NSW Health should have a specific view.

WSAA considers that the Final Report would benefit from in person public hearings or roundtables with all the stakeholders present, including NSW and Australian Government agencies and regulators. Without this input, our strong view is that IPART, Sydney Water, customers and the community are unable to be confident that the appropriate risk and affordability trade-offs are being made.

Indeed, if significant investment is to be deferred, WSAA considers that economic, environment and health regulators have a collective responsibility for the outcome. Sydney Water cannot be held solely responsible to delivering outcomes with a level of expenditure that they did not propose or endorse.

But Sydney Water will continue meet its core customer requirements

Stakeholders should not take comfort from the fact that Sydney Water will do the right thing for its customers regardless of the determination. Sydney Water spent more than its capital expenditure allowance in the last determination because it was necessary. IPART subsequently found that this was justified. It may well be that if faced with similar circumstances Sydney would spend what was necessary to protect customers, water quality and the environment.

However, this is not a robust model to operate under. Making investments that are not covered by prices (for the determination period), is not costless. It will significantly increase debt levels. Increases in debt are another way of saying that the costs are being transferred to future customers. These costs will be reflected in even higher prices in future periods or weaker financial viability for the utility.

Contact

WSAA welcomes the opportunity to discuss this submission further.

[redacted]

[redacted]

Attachment 1

Estimated bill impact from deferring $5.9 billion in capital expenditure

Year	2025-26	2026-27	2027-28	2028-29	2029-30
Amount capital deferred	$ 1,200,000,000	$ 1,200,000,000	$ 1,200,000,000	$ 1,200,000,000	$ 1,200,000,000
Cumulative capital deferred	$ 1,200,000,000	$ 2,400,000,000	$ 3,600,000,000	$ 4,800,000,000	$ 6,000,000,000
Capital cost saved by deferral	$ 50,400,000	$ 100,800,000	$ 151,200,000	$ 201,600,000	$ 252,000,000
Average annual revenue	$ 3,500,000,000	$ 3,500,000,000	$ 3,500,000,000	$ 3,500,000,000	$ 3,500,000,000
Bill impact	**1.4%**	**2.9%**	**4.3%**	**5.8%**	**7.2%**

Capital cost (WACC plus 1% Depreciation) 4.2%