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Australia's property industry

Creating for Generations

28 October 2019

Dr Paul Paterson
Chair
Review of Sydney Water Corporation prices
Independent Pricing and Regulation Tribunal
PO Box K35
Haymarket Post Shop
Sydney NSW 1240

Dear Dr Paterson

Review of Sydney Water Corporation prices for 2020-2024

The Property Council welcomes the opportunity to provide comments to the Independent Pricing and Regulatory Tribunal (IPART) on Sydney Water's pricing proposal for 2020-2024.

The Property Council of Australia, as Australia's peak representative of the property and construction industry, has members from parts of the sector including owners, developers and investors of all asset classes. Our members own and develop property across most of Sydney Water's area of operations, including Western Sydney and the Illawarra.

We are pleased to provide the following comments for your consideration.

Introduction

Sydney Water delivers a monopoly service for the supply of water, wastewater and stormwater services. A major component of Sydney Water's budget is capital investment for servicing new urban growth within its area of operations. This investment involves Sydney Water building and operating new water, wastewater and stormwater infrastructure. Costs are also incurred when the existing network is augmented to serve increasing populations in established areas.

For 2020-2024, Sydney Water is seeking \$10.7 billion of revenue over the next four years which is a 2% increase on the 2016-2019 determination. Sydney Water has forecast \$5.4 billion of expenditure for operating costs and \$5 billion for capital costs.

IPART's role is to set the maximum prices that Sydney Water can charge for water, wastewater and stormwater drainage services that it provides to residential and non-residential customers. IPART has released an issues paper and in March 2020 will release a draft report and determination for consultation. A final report and determination will be released by June 2020 and the new pricing structure will come into force on 1 July 2020.

Growth Servicing Plan 2019

Sydney Water recently released the 2019-2024 update of its Growth Servicing Plan (GSP). This indicates that Sydney Water is responding to the NSW Government's plan for Sydney's long-term future. The GSP has been aligned to the Greater Sydney Commission's (GSC) Regional Plan for Greater Sydney that envisages the need for an additional 725,000 homes before 2036. The GSP has been informed by the forecasts and approvals set by the Department of Planning, Industry and Environment (DPIE) and local councils.

It is important that Sydney Water is resourced to enable it to deliver infrastructure to new housing being built around Sydney. Failure to allow Sydney Water to fund and deliver key enabling infrastructure in Sydney's growth areas puts at risk the new homes that Sydney needs to meet its growing population.

Productivity Commission discussion paper

IPART should be aware of the discussion paper "*Kickstarting the productivity conversation*" released by the NSW Productivity Commission in October 2019. Section 5.3 of this paper is focused on improving governance in the rural and urban water sectors. It notes that NSW has improved governance in urban water markets over the past few decades, including corporatizing major utilities and establishing independent economic regulation through IPART. The Productivity Commissioner sees potential to further clarify roles and responsibilities, better integrate water and land use planning and improve transparency in the water planning process. The Property Council supports further clarity of the role of Sydney Water in the urban water planning to better integrate with land use planning.

Sydney Water's Proposed Capital Expenditure

The issues paper states that Sydney Water is about to enter into a period of significant capital investment that will well exceed its historical 30-year average. Factors responsible for this increase include compliance with existing mandatory standards, record levels of new growth and the setting of new mandatory standards such as those required by the Environment Protection Authority (EPA).

Sydney Water's proposed capital expenditure during the 2020-2024 period is \$4.5 billion and wastewater services account for the largest proportion of that figure (about \$3 billion). The issues paper indicates that \$572 million is proposed to be allocated to rehabilitation and condition assessment of major sewers and \$305 million on replacement and renewal of wastewater treatment plants. This expenditure is supported as it supports Sydney's continued growth.

The issues paper indicates that IPART has not formed a preliminary view on Sydney Water's proposed capital expenditure for 2020-2024. IPART has stated that it will decide whether Sydney Water's longer-term capital investment strategy is the most efficient. It is vital that Sydney Water is given the financial resources that it needs to support planning decisions being made by the NSW Government and implemented by the GSC, DPIE and local councils.

Section 2.4.3 of the issues paper has noted that Sydney's expansion requires Sydney Water to build and operate new water, wastewater and stormwater infrastructure. Unlike most of the other water utilities in NSW, Sydney Water is prevented from levying developer charges to proponents of new development. Since 2008, the NSW Government has set water, wastewater and stormwater developer charges for Sydney Water to zero. That means the cost of servicing new development is borne by Sydney Water's existing customer base.

The 2020-2024 proposal involves approximately \$1.6 billion of infrastructure solely intended to service the needs of Sydney's growth areas, which represents 36% of the corporation's total capital expenditure over the four-year period. The issues paper warns that keeping developer charges set at zero will place upward pressure on prices over time. The residential development industry has a strong view that these charges must stay set at zero. Any move to re-introduce these charges would have detrimental impact on both the supply and affordability of housing within Sydney.

Demand and Customer Numbers

Following identifying Sydney Water's revenue requirement for 2020 determination period, IPART must decide the Corporation's forecast water sales and customer numbers and forecast chargeable wastewater volumes.

During the 2016 determination period, there was an unexpected high period of dwelling growth that led to a larger than expected growth in Sydney Water's residential customers. Sydney Water has indicated that the number of dwellings it serves with water was higher than forecast in both June 2017 (1.6%) and June 2018 (2.6%) and by June 2020 will be about 4% higher than the original forecast.

During the current determination period Sydney Water anticipates a starting customer base of 1,889,000 rising to:

- 1,927,000 (2.01%) in 2020/21,
- 1,964,000 (1.92%) in 2021/22,
- 2,002,000 (1.93%) in 2022/23 and
- 2,038,000 (1.79%) in 2023/24.

A factor behind the ongoing increase in the Corporation's water sales is an increase in residential dwellings that DPIE forecast to increase by around 37,000 or 1.7% annually. The Property Council recommends these figures be reviewed in December 2019 following release of updated housing supply forecast by DPIE that are currently being updated for 2019.

A reduction in water consumption per dwelling is forecast during the 2020 determination period from 200.3 kL to 199.5 kL. Sydney Water expects this reduction due to a greater proportion of apartments being produced at present compared to detached houses and greater water efficiency through the Government's BASIX targets. As Sydney Water commenced the development of its pricing proposal in late-2018 and early 2019, some of these forecasts may no longer be accurate. The Property Council recommends that the dwelling number and water consumption forecasts be reviewed the fall in dwelling approvals and completions in the last twelve months.

Stormwater drainage services (except Rouse Hill)

About 520,000 customers of Sydney Water are located within a declared stormwater catchment area and pay stormwater charges to Sydney Water. For the 2020 to 2024 period these prices will increase by 8% in 2020 and remain constant in real terms for the remainder of the period. It is noted that IPART has not formed a preliminary view on stormwater charges and have sought more information from Sydney Water on the relationship between property size and the cost of providing stormwater services. These charges should be consistent with the charges imposed by local councils for providing the equivalent trunk stormwater charges in other parts of Sydney.

Currently stormwater charges are generally based on the land area of a customer's property. Since 2012, charges have been set so that owners of larger properties pay proportionally less on a square metre basis than smaller properties. This is referred to as "constrained area pricing". A shift away

from constrained area pricing could see charges for large non-residential customers increasing between 5% to 196%.

The Property Council supports Sydney Water's position regarding the calculation of these charge and we recommend the continuation of constrained area pricing for the 2020-2024 determination.

Prices for Other Minor Services

Rouse Hill drainage charges

Because Sydney Water owns and manages trunk drainage in the Rouse Hill area, it is responsible for managing large areas of open space to accommodate flood flows, natural creeks and grass lined channels and artificial wetlands.

Sydney Water's proposal is to gradually reduce the charges it imposes on customers in Rouse Hill. In 2016, IPART increased the Stormwater Drainage Charge to reflect Sydney Water's costs for providing these services. The proposal seeks to lower the charge from \$151 per year in 2019/20 to \$114 per year in 2023/24.

Sydney Water has indicated that the operating cost deficit from earlier years will be diminished by 2023/24 and that the price reductions proposed can be accommodated. The Property Council supports the gradual reduction in this charge.

Form of Regulation Issues

Section 9 of the IPART issues paper addresses the way IPART regulates Sydney Water's operations. Key points identified here are considered below:

Length of determination period

Sydney Water and IPART both favour a continuation of the current four-year pricing determination period as it strikes an appropriate balance between providing certainty to the regulated business and limiting delays in customers benefiting from efficiency gains. The Property Council supports continuation of the current four-year pricing cycle.

Unregulated pricing agreements.

The issues paper indicates that in 2016's pricing determination, Sydney Water was permitted to enter into unregulated pricing agreements with large non-residential customers. Sydney Water has proposed retaining the ability to enter into unregulated pricing agreements over the 2020-2024 determination period. The Property Council supports this aspect of the proposal and agrees with IPART's view that this will incentivise Sydney Water to engage with its customers to develop mutually beneficial arrangements that are specifically targeted to better match customer preferences.

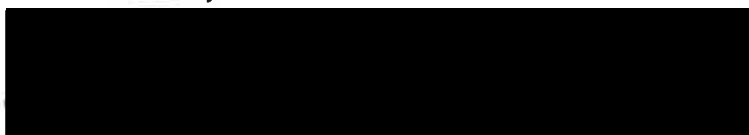
Non-regulated revenue

Sydney Water may derive non-regulated revenue from regulated assets. An example of this is Sydney Water's participation in the NSW biodiversity offset scheme. Between 2020 and 2024, Sydney Water have estimated revenue in the order of \$20 million from its land holdings participating as biodiversity stewardship sites. Sydney Water is proposing to share 10% of that revenue with its customers. The Property Council support's IPART's proposed approach regarding the use of revenue from participation in this program.

We look forward to reviewing IPART's final report and determination in March 2020 (and if publicly released, the additional information being provided to IPART by Atkins Cardno) so that we can provide more feedback if required. We also look forward to IPART's final report and determination in June 2020.

Should you have any questions, please do not hesitate to contact Troy Loveday, Senior Policy Advisor on (02) 9033-1907.

Yours sincerely



Jane Fitzgerald
NSW Executive Director
Property Council of Australia