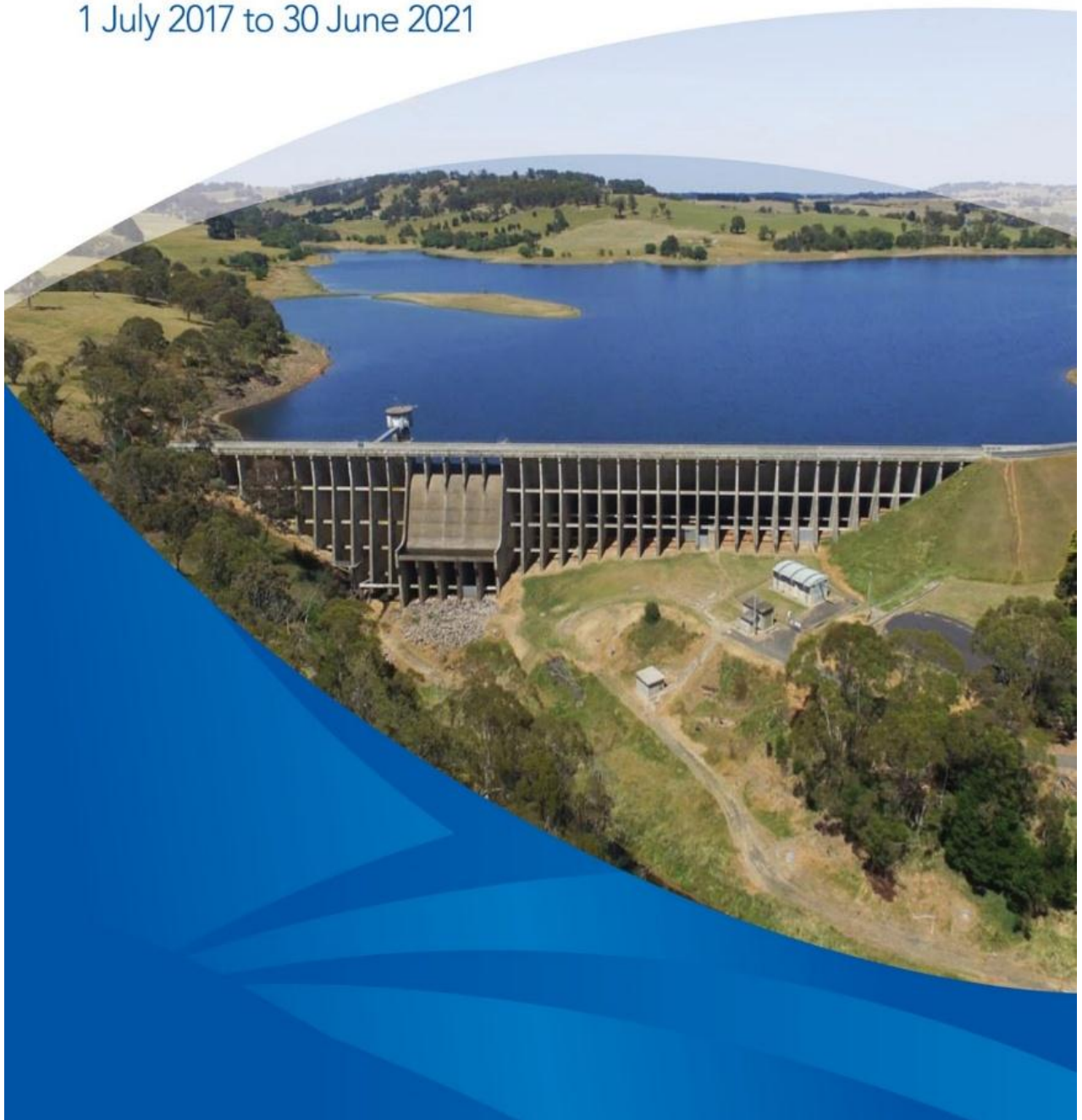




Response to the IPART Draft Determination Supplementary Submission

Regulated prices for NSW Rural Bulk Water Services from
1 July 2017 to 30 June 2021



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1. Introduction

This is a supplementary submission in response to the Independent Pricing and Regulatory Tribunal of NSW (IPART):

- Draft Determination of Prices for rural bulk water services from 1 July 2017 (Draft Determination); and
- Draft Report on its review of prices for rural bulk water services from 1 July 2017 to 30 June 2021 (Draft Report).

This supplementary submission is provided to IPART to inform its Final Determination for the period 1 July 2017 to 1 July 2021 (Final Determination). It is specific to the issue of the payback of the unders and overs mechanism (UOM) balance and IPART's draft decision to write off most of the UOM balance in the Fish River Scheme. IPART stated at page 83 of the Draft Report:

We consider the shutdown of Wallerawang power station represents a structural change in water consumption, which is different to ordinary volatility and represents a step change to a new permanent lower level of usage. We do not consider that it is appropriate for the general customer base to bear the resulting shortfall in usage revenue.

Given the large UOM balance in the FRWS is primarily a result of structural change, and not of weather or climate driven variability, we consider that the balance attributable to the closure of Wallerawang power station should be written off. This removes around \$3.2 million from the balance as at 1 July 2016.

WaterNSW made a representation to IPART during the public hearing on the Draft Determination on 4 April 2017 that EnergyAustralia should have to pay the UOM balance attributable to them¹.

2. UOM balance in the Fish River Scheme

Following third quarter water sales figures, WaterNSW has estimated the closing balance of the UOM for the end 16/17 for individual customers in the Fish River Scheme as set out in the table below.

Fish River UOM Closing Balance (\$nominal)	2015-16	2016-17
Raw Water		
EnergyAustralia - Mt Piper	792,717	1,079,335
EnergyAustralia - Wallerawang	3,170,866	4,317,342
Other	261,066	234,326
Sub-total (raw water)	4,224,649	5,631,003
Filtered water		
Lithgow Council and Individual minor customers	354,264	593,012
Sub-total (filtered water)	354,264	593,012
Total (raw and filtered water)	4,578,914	6,224,015

The balance attributable to Wallerawang power station has increased - from approximately \$3.2 million to \$4.3 million. This increase above the already substantial \$3.2 million proposed to be written off by IPART has necessitated this further submission by WaterNSW.

¹ See pages 63 and 64 of the transcript of the public hearing.

3. EnergyAustralia's UOM Balance is the Result of Commercial Decision, not a Water Market Structural Change

The decision to close the Wallerawang power station, resulting in significantly lower water usage in the Fish River valley, was a commercial decision made by EnergyAustralia. It is important to distinguish that EnergyAustralia *caused* a structural change in water consumption, rather than being *impacted* by an external structural change imposed on it. It is EnergyAustralia that *imposed* a structural impact on the other (remaining) customers in the valley.

4. The ACCC UOM Decision Captures All Over/Under Revenue Balances, with No Exclusion

WaterNSW does not agree with the rationale of IPART in the Draft Report on the nature of the balance to be captured by the UOM. The UOM was introduced by the Australian Competition and Consumer Commission (ACCC) in the ACCC Final Decision on State Water Pricing Application 2014-15 – 2016-17, June 2014 at page 20:

The ACCC has determined that a hybrid form of control will apply to State Water's bulk water charges for the 2014-17 regulatory period. Specifically, the hybrid form of price control adopted is a price cap that can be adjusted for under or over collection of revenue.

*The hybrid form of control will allow for a partial rather than full adjustment to prices each year to account for the difference between actual and target revenue. Under this form of control, **any** under or over collection of revenue will be added into a rolling 'unders' and 'overs' account. The value of this account will be multiplied by the weighted average cost of capital (WACC) to determine the amount by which charges can be adjusted in the next year.*

The unders and overs account is a running balance of annual differences between actual and target revenues. As the adjustment to total revenue is equivalent to the WACC multiplied by the balance in the unders and overs account, and not the full difference between actual and forecast revenues, annual price changes will not be as significant compared to State Water's proposed revenue cap.

This form of control is symmetrical, as it will reduce charges if State Water has over collected revenue, and increase them if it has under collected.

The ACCC considers the hybrid form of control will address price stability for customers while also providing State Water with greater revenue certainty. If there are dry periods, State Water will receive a return on the balance in the unders and overs account, thereby recognising any additional borrowing costs needed to help manage its cash flows.

The ACCC's decision references "**any**" over or under collection to revenue. There is no reference to the UOM only applying to "ordinary climate volatility" and no exclusion for "structural change".

If, however, structural change was considered to be a legitimate basis for UOM exclusion, then this should have been:

1. defined as to which risks are borne by which party;
2. taken into account in the regulatory (pricing) framework; and
3. applied consistently across the customer base (rather than only applying to one customer).

Additionally, by providing itself with a broad discretion to exempt a customer from paying the UOM balance, IPART is introducing significant regulatory risk to the price determination process.

5. Conclusion

In our view, EnergyAustralia has *caused* a structural change on other customers in the Fish River valley as a result of its commercial decision, rather than having been impacted by a structural change *imposed* on it. Additionally, there is no reference to exclusion for structural change in the ACCC UOM decision.

There is no rationale to make an exception for structural change for EnergyAustralia with regards to the repayment of its UOM balance. IPART should ensure that the payback of the UOM attributable to the Wallerawang power station shut down is repaid by EnergyAustralia.