

25 January 2018

Mr Nathan Petrus
Director Consumer Protection and Pricing
Essential Services Commission
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Business SA
Chamber of Commerce
and Industry South Australia

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Dear Mr Petrus

I write in response to ESCOSA's request for submissions on its draft framework and approach for the SA Water regulatory determination (2020 – 2024).

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Working for South Australia

Executive Summary

- While increases in SA Water's usage charges have moderated in recent years, they remain at a high watermark, and trade waste charges that typically impact manufacturing businesses are still rising at 10 percent per annum.
- For ESCOSA to adequately protect the 'long term' interests of South Australian consumers through its economic regulation of SA Water, it is important that adequate consideration be given to how each aspect of SA Water's pricing structure has moved over the last decade.
- Business SA supports the costs of providing recycled water remaining part of providing sewerage retail services to ensure SA Water demonstrates prudent and efficient means of addressing its environmental discharge obligations and that SA Water customers are adequately compensated for the costs of treating that water.
- While SA Water's services standards do account for regional areas, it is done so on an aggregate basis and consideration should be given to the value of reporting at a more granular level for regions, as per the approach being considered for SA Power Networks' reliability standards.
- Notwithstanding the matter of how SA Water's regulatory asset base (RAB) is determined lies beyond the scope of this specific process, it still has ramifications for longer term planning of SA Water's revenues.

Should you require any further information or have questions, please contact Andrew McKenna on (08) 8300 0000 or andrewm@business-sa.com.

Yours sincerely,

Anthony Penney

Executive Director, Industry and Government Engagement





Why this matter is important to South Australian businesses

As South Australia's Chamber of Commerce and Industry, Business SA is the peak business membership organisation in the State. Our members and the broader business community are affected by this matter in the following ways:

- While water price rises have moderated somewhat in recent years, their absolute level still results in South Australian businesses paying one of the highest water usage rates in Australia.
- A reliable and safe water supply is critical for businesses and Business SA recognises the work SA Water is undertaking to improve its ability to both prevent and respond to bursts and leaks across the network, particularly its investment in technology which can also assist businesses in understanding on site issues.
- Trade waste is a largely unavoidable by-product of a business' production process and while not a retail service covered by SA Water's revenue cap, the rising cost of trade waste treatment is still a significant issue for South Australian businesses.
- Water intensive businesses need to make long term investments in infrastructure to manage water and trade waste costs and need to understand what the underlying cost drivers are for SA Water in order to mitigate against price increases.

Key Policy Points

1. Business SA acknowledges ESCOSA's edict that to promote the long-term interests of SA Water's customers, the proposed framework and approach aims to ensure that SA Water '*should incur only efficient expenditure, taking a long-term approach to its decision making to ensure the essential services it provides are sustainable and customers receive the benefits of that improved efficiency through the prices they pay.*'

To adequately assess whether or not the long-term interests of consumers have actually been protected, ESCOSA should provide analysis as to how SA Water's price structure has evolved over time, particularly across the last decade. While there may be legitimate reasons for particular drivers of price increases, for example the Adelaide De-salination Plant (ADP) and associated pipeline infrastructure, without monitoring price increases over an appropriate timeframe there is no way of adequately determining whether the long-term interests of consumers have actually been protected.

Following considerable cost pressure on electricity consumers over many years, the Federal Government recently instructed the Australian Competition & Consumer Commission (ACCC) to undertake an inquiry into electricity prices. Business SA acknowledges the following statement from the ACCC's draft report executive summary:

One thing is clear from this consultation and information gathering: there is a severe electricity affordability problem across the NEM and the price increases over the past ten years are putting Australian businesses and consumers under unacceptable pressure.

From evidence in sectors such as electricity, it is clear that for regulators to adequately gauge the long-term nature of a price issue impacting consumers, having at least ten years data enables much more robust and definitive conclusions.



Business SA notes the following usage price structure for SA Water’s commercial customers in 2007/08:

- a) First 125 kL - \$0.50/kL
- b) Above 125 kL - \$1.16/kL¹

Compared with 2017/18:

- a) \$3.308 per kL²

Even if we take a conservative view and only work off the top rate of water usage for commercial customers, prices have still increased 185% over the past decade, or nearly triple, which is actually higher than the extent of electricity price rises experienced in South Australia over the same period.

While prices have moderated in recent years and Business SA has been encouraged by ESCOSA's rigorous approach to regulating SA Water since 2013, the longer term perspective still needs to be considered for, particularly as it impacts upon the long term investment decisions businesses make in this state. Furthermore, when considering water usage rates alone across the states as an indicator of South Australia's competitiveness, we are still the most expensive when compared against the following major water utilities:

Water use prices 2017/18		
Jurisdiction	Marginal price per unit (\$/kL)	Supply pricing mechanism
SA Water	3.308	Property value
Sydney Water	2.04	Meter size
Hunter Water (NSW)	2.3	Meter size
City West Water (Vic)	2.7186	Fixed charge per property per annum
South East Water (Vic)	3.2366	Fixed charge
Yarra Valley Water (Vic)	2.8503	Fixed charge
Urban Utilities (Qld)	1.609	Fixed charge
Water Corp (WA)	2.318	Gross rental property value
TasWater	1.0202	Meter size
Source: Price pages for above companies		

2. Business SA acknowledges that ESCOSA sets SA Water’s allowable gearing ratio of 60% based on the competitive entity concept, an inherent feature of economic regulation – and that SA Water’s current gearing is approximately 45%.

Two high profile debt swaps from the State Government’s balance sheet to SA Water have occurred in the last few years, the first a \$2.7 billion swap in the 2014/15 state budget, and the second a \$71.2 million swap which occurred in July 2017.

¹ State Government, Transparency Statement Water and Wastewater Prices in Metropolitan and Regional South Australia 2007-08, January 2007.

² SA Water, 2017-18 Pricing Schedule, P4.



The latest transaction followed the direction of the State Government to set SA Water's debt to asset ratio at 45%, as opposed to the 44% it sat at previously.³ Subsequently, SA Water borrowed money 'it didn't need to' to satisfy this shareholder direction.⁴

The Chief Executive of SA Water was recently asked in Parliament whether the additional \$71 million debt would affect water and sewerage charges and responded:

No. To keep it short, we are in a regulating environment, so when ESCOSA did its determination two years ago for the period of 2016-2020, they gave us a cap on revenue. This cap doesn't change anymore, so it doesn't translate into an additional tariff or whatever. It is completely separate.⁵

While Business SA recognises that ESCOSA's approach to SA Water's economic regulation is indifferent to the actual level of gearing SA Water decides to operate, there is still concern from businesses and water consumers at large as to what impacts result from Government directives on SA Water's level of gearing. Subsequently, ESCOSA's framework should address the competitive level of gearing for comparable water utilities and also reassure consumers about any impact of the State Government's debt swaps on water prices.

3. In response to the second question posed at [3.3], Business SA submits the pricing principles approach should be continued for SA Water's other retail services – particularly trade waste services. However, this is an area in which service standard objectives and further analysis may be appropriate.

Many members have expressed to us that they are concerned by increasing trade waste prices; an SA Water retail service excluded from the revenue cap and regulated under a pricing principles approach. Trade waste is a largely unavoidable by-product of a business' production process, particularly those businesses in the manufacturing, industrial, and food and beverage industries. These businesses have been exposed to significant trade waste service price increases over the past decade, including periods of 10% growth per annum. Trade waste exposed businesses must either absorb these increasing trade waste costs, jeopardising future investment and employment, or pass the increased costs into their customers, jeopardising sales and making themselves less competitive.

Business SA recognises that trade waste pricing is made up of many different parameters and that the resource intensity required to treat these parameters will vary. We further recognise that SA Water has competitively priced some trade waste parameters compared to providers in other jurisdictions. However, this is no reason to significantly change how trade waste parameters are priced.

³ Evidence to Budget and Finance Committee, Legislative Council, Adelaide, 4 December 2017, [16024]-[16026] (Roch Cheroux).

⁴ Ibid [16031].

⁵ Ibid 16134].



While movement to fully cost-reflective trade waste parameter prices should occur in principle, this was also supposed to have happened in 2007/08⁶. In its 2014 Water Price Reform Options Report, which did not allow for review of SA Water's RAB, ESCOSA identified extreme price increases to allow a switch to fully cost-reflective trade waste pricing. Volume and Load Based (VLB) trade waste customers, a group well represented in Business SA's membership, would have faced an average increase in their trade waste bill of 434%, with prices for Total Dissolved Solids predicted to increase by 1,087%.⁷ Presuming treatment technologies and practices should become more efficient over time, Business SA queries the underlying cost drivers of trade waste treatment costs for SA Water, and encourages ESCOSA to give them adequate consideration in this process.

Numerous member businesses have invested in on-site water treatment to minimise or reduce their trade waste costs. The difficulty these members face is that the true cost for SA Water to handle these parameters is unclear and parameter prices are subject to significant change from period to period. Members have expressed reluctance to undertake further investment where the costs imposed on them by SA Water are uncertain from year to year; where the 'goal posts' are constantly shifting. Business SA has previously identified a member who engaged a local supply of waste water treatment plants to build and operate a plant on site to treat trade waste at a lower cost than it would be charged to discharge trade waste to Bolivar.⁸ Business SA commented then, and questions again now, that it seems improbable that it is more efficient for individual businesses to operate small scale on-site water treatment plants than for SA Water, with its considerable resources, specialist expertise and economies of scale, to treat trade waste itself.

Certainty regarding the true cost (and therefore the likely on-going cost) to treat trade waste parameters will be of significant benefit to members. An independent assessment of SA Water's real costs to treat trade waste parameters should be implemented before any consideration be given to altering the pricing approach for SA Water's trade waste services.

For the purposes of this draft framework, Business SA submits trade waste services should continue to be priced according to pricing principles.

Service standards could also be introduced regarding trade waste customer engagement. Business SA notes ESCOSA's focus on improving SA Water's long-term perspective and the intention to encourage SA Water to 'engage with its customers on the long-term implications of its proposals.'⁹ Long-term trade waste parameter predictions should be communicated to customers promptly and effectively. Such communication would better enable businesses to assess their on-site treatment requirements and budget accordingly.

⁶ Government of South Australia, Transparency Statement Water & Wastewater Prices in metropolitan and regional South Australia 2007-08, page 35

⁷ Ibid 91.

⁸ Business SA, 'Submission – ESCOSA inquiry into reform options for SA Water pricing (Draft Report)', September 2014, 9.

⁹ ESCOSA, 'SA Water Regulatory Determination 2020 – Draft Framework and Approach', November 2017, p 5.



4. Business SA supports the costs of providing a recycled water scheme remaining part of the costs of providing sewerage retail services. For several years Business SA has been encouraging SA Water to further develop water recycling schemes for expanded primary production, and we have been a strong proponent of the Northern Adelaide Irrigation Scheme (NAIS). Initial conversations we had with SA Water in 2014 related to how it could better support economic growth in South Australia, not only through ensuring competitively priced services, but what further industrial opportunities could be developed using excess recycled water. All along Business SA has been keen to ensure SA Water uses NAIS to realise the best possible economic outcome for the State, and in doing so covers the costs of its sewerage customers who pay for that water to be treated, and who have experienced significant increases in water prices over the past decade. There is no doubt that NAIS needs to meet the market, which includes local growers, but ultimately the water should go to the growers able to use it most efficiently and consequently, able to absorb the highest price to make an adequate return.

Business SA supports assistance to help local growers be competitive for that water, but that needs to be separately considered to ensuring the costs of treating waste water are minimised through SA Water providing recycled water at a market rate.

5. Business SA has long argued that consumer engagement through regulatory determination processes is typically enhanced when the regulated business can provide impact of any changes beyond just the level of the average residential consumer. While bill changes for residents needs to be carefully considered, the same quantum of bill change for a water intensive business with a bill in the tens of thousands is likely to be felt in a much more significant manner, and those impacts need adequate consideration.

Business SA is encouraged by feedback from SA Water that total bill impacts for each consumer will be considered for in upcoming consumer 'willingness to pay' surveys for the 2020-24 regulatory period. Accordingly, the framework to SA Water's regulatory determination should formally consider bill changes across a range of consumer classes.

6. While Business SA supports ESCOSA taking a long term approach to its regulation of SA Water, we acknowledge that the value of SA Water's RAB is a primary determinant of the majority of SA Water's revenues and that eventually some independent analysis of how the RAB value is determined will need to be undertaken.
7. Business SA recognises that under the *Water Industry (Third Party Access Amendment) Act 2015*, third parties can legally access SA water's water and sewerage infrastructure services. Considering ESCOSA's approach to ensuring SA Water pursues future cost efficiencies, with a focus on continuous improvement, consideration should be given to the publication of more granular information around SA Water's costs of treating sewerage to ensure adequate competitive pressure on SA Water to deliver a least cost solution. Although potential competitors to the provision of sewerage/trade waste treatment can gather information on prices directly from customers, they cannot necessarily see on aggregate what are the market opportunities for accessing South Australia's sewerage/trade waste treatment market, including in regional areas.



8. In relation to the electricity sector, the recent spate of reliability issues in regional areas (particularly on the Eyre Peninsula) has highlighted the issue of having reliability and service standards which are not granular enough to ensure appropriate accountability on monopoly utility operators. While Business SA is not necessarily raising concern about SA Water's performance between metropolitan and regional areas, considering the services standards are under review through this process, adequate consideration should be given to whether regions could be disaggregated rather than just separated for regional and metropolitan standards. South Australia's regions have many different characteristics, both economic and otherwise, as well as being represented in various boundaries throughout the political system. Consequently, to ensure adequate accountability and understanding of issues, SA Water should be incentivised to ensure it meets expectations across key regions which could be defined on the following basis:

Whyalla/Port Augusta/Far North

Eyre Peninsula

Barossa/Mid-North/Pt Pirie/Yorke Peninsula

Adelaide Hills

Murraylands & Riverland

Kangaroo Island

Fleurieu Peninsula/McLaren Vale

South East

9. Business SA supports ESCOSA's focus on engaging other regulators in the process of SA Water's next regulatory determination, particularly to ensure SA Water can efficiently meet a range of regulatory requirements imposed at least cost to consumers. For example, considering trade waste costs are largely associated with the cost of treating and discharging sewerage to satisfy environmental obligations, the EPA should be engaged to look at all options to ensure the environmental outcomes they require are not unnecessarily imposing costs on SA Water and its customers. For example, is there another way to meet the EPA's requirements which might lessen the need for SA Water to incur particular costs treating sewerage?

Business SA would also like to see appropriate transparency on SA Water's industry licence fees which tripled to \$9.5 million for the current regulatory determination. While at the time we acknowledged this was a State Government decision involving some transfer of functions from SA Water to Government, it is ultimately paid for by water users who have a right to know whether such costs are comparable to those incurred in other jurisdictions.