



# Prices for Hunter Water Corporation from 1 July 2020

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Independent Pricing and Regulatory Tribunal

October 2019

Suite 1, Level 1  
165 Lambton Road  
Broadmeadow, NSW 2292

Phone: 02 49699 600

[info@hunterbusinesschamber.com.au](mailto:info@hunterbusinesschamber.com.au)  
[www.hunterbusinesschamber.com.au](http://www.hunterbusinesschamber.com.au)

## Introduction

The Hunter Business Chamber (The Chamber) is the largest regional business chamber in Australia, established in 1886. The Chamber independently represents about 2,000 member organisations to all levels of government and is the peak business and industry association in the region, reflecting the interests of all sectors.

The Chamber works as an integral part of the NSW Business Chamber (NSWBC) network. We advocate to government at local, state and federal level for business-positive policies that promote investment and growth to deliver flow-on benefits to all in our community.

The Hunter Region is Australia's largest regional economy, with a Gross Regional Product of more than \$50 billion per year, driving more than one quarter of the total economic output of NSW. The Hunter is an economically diverse region encompassing strong foundations in resources, manufacturing and agriculture, but with fast-growing services and knowledge sectors. Mining, manufacturing and construction are the key industries by output, while health care and social assistance is the highest employing sector, followed by education and training and retail.

## Overview

Our comments to the IPART review stem from our interest and advocacy for business in the Hunter region. The NSWBC conducts quarterly Business Conditions Surveys that report on business performance and confidence in regions across NSW, as well as highlighting the impact of factors that affect business operations such as operating costs, staff retention and consumer sentiment. Our business surveys for the past year have shown a softening of business confidence across the Hunter region, from relative highs (in comparison with the rest of NSW) in late 2018.

In Newcastle and Lake Macquarie Statistical area, business confidence slipped from being "relatively strong" in December 2018 to "below average" in the June 2019 survey, with business performance indicators also down<sup>1</sup>. These results were echoed in the Hunter Research Foundation Centre's Hunter Economic Indicators for January-June 2019<sup>2</sup>.

Based on the outcomes of these surveys, business confidence, performance and sentiment in the Hunter Region could best be described as patchy and is not forecast to change in the short term. Businesses have reported through our surveys that rising operating costs, including that of utilities, are a significant constraint to businesses wishing to grow and expand. While the Chamber is supportive of many of the objectives outlined in the Hunter Water pricing proposal to increase efficiency and improve water conservation, we also recognise the imposition of rising costs on business and the variable ability of business to absorb such changes in service arrangements.

The Chamber supports Hunter Water's plans to invest \$871 million on infrastructure, technology and service delivery over next five years as long as it can be achieved under a regime of reasonable price increases that do not have a significant impact on customers, particularly business.

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<sup>1</sup> NSWBC Business Conditions Survey June 2019 [https://www.nswbusinesschamber.com.au/NSWBC/media/Policy/BCS-JUN2019-Report\\_1.pdf](https://www.nswbusinesschamber.com.au/NSWBC/media/Policy/BCS-JUN2019-Report_1.pdf)

<sup>2</sup> Hunter Research Foundation, Hunter Economic Indicators Jan-June 2019. <http://www.hrf.com.au/uploads/publications/Hunter-Economic-Indicators-June-2019-FINAL.pdf>

## **Location-based charges**

The biggest single impact on customers will be the phasing out of location-based charges for the 20 large water users that currently receive an historic discount on water usage charges. As outlined in Table 2.10 of Technical Paper 8 in the Hunter Water pricing proposal bringing these users to a common rate of \$2.51 per kL, in line with that charged to other customers, by 2024-25, will involve phased increases for individual users of between 12 cents and 59 cents per kL. The Issues Paper indicates that the proposal will be accepted “subject to consideration of customer impacts”. It is difficult to ascertain the likely impact on individual users from the information provided but the Chamber has received anecdotal advice from industrial customers among the cohort of large water users that the overall costs to some will be quite substantial – in the realm of hundreds of thousands of dollars per year.

The Chamber supports the rationale behind bringing all customers to a common water usage rate and the process of phasing in the cost increase over five years to mitigate the financial impact, but believes it is important that comprehensive engagement be undertaken with the affected users to ensure that all avenues to reduce water use or convert to recycled water are explored, including options that may originate from the users. We have received feedback from some users in this cohort that engagement has not yet reached this level and take on good faith that Hunter Water will follow through on its commitment to work closely with those affected by the cessation of location-based charging to minimise impacts. We note that this may involve the need for additional capital investment by Hunter Water that will accelerate change in water usage by these users, which may require a contingency in the price plan to facilitate projects not otherwise defined.

We also raise the matter of community support for the cessation of location-based charges, which was discussed in the Technical Paper. We note there was not overwhelming support for the cessation of the charges, despite the reported impact it has in increasing the bills of residential customers by about \$10 a year. The results to the same question from the survey of non-residential users were referenced but not provided in the same detail in the Technical Paper. We also note that the Technical Paper does not reference any response from the individual users who will be affected, which may have been useful in helping to ascertain the overall impact and fairness of the proposal.

## **Interest rate assumptions**

The Chamber notes comments relating to the current interest rate environment potentially offsetting the impact on the cost of the proposed capital expenditure program. These assumptions should be examined closely by IPART as interest rate changes are beyond the control of Hunter Water. It is noted revenue increases are programmed to be higher than the foreshadowed rate of inflation. Potential price pressures on Hunter Water and for that matter, customers, could be produced by a change (upward) in interest rates and the program outcomes need to have a buffer by using a conservative approach in relation to the assumptions around future interest rates.

## **Recycled water**

IPART has flagged a litmus test in consideration of pricing arrangements for recycled water based on customer willingness to pay. The Chamber recognises that this forms only a small part of the overall expenditure regime proposed and that the principle of making greater use of recycled water is widely

supported, but cautions that getting consensus from businesses on willingness to pay may be problematic on the following grounds:

- There are significant differences in the incidence (relative proportion) of the cost of HWC charges across businesses in relation to usage and rate costs;
- The difference across businesses in their capacity to pay based on the variable ability to pass on some or all parts of the cost increases;
- Perspectives of different businesses on their levels of future profitability attributable to current performance and sentiment.

This needs to be considered in assimilating policy and practice outcomes should engagement of this type be put into practice.

### **Issues for Stakeholder Comment**

#### **Question 5: Is it appropriate to move from reactive to proactive asset management, given the additional cost?**

The Chamber supports this change in principle and believes it reinforces sound business practice. However, the rate and staging of this change must acknowledge impact on customers so that the current generation of customers is not unduly penalised for the shortcomings of past practices. This might mean cost increases on the implementation program need to be staged over a longer period.

#### **Question 8: How much emphasis should be put on benchmarking with other utilities in terms of performance standards and hence required capital expenditure?**

The Chamber believes this is an important element. Hunter Water programs and consequential charges are an important consideration of in keeping business in the Hunter competitive and pricing must have regard to this. It is false economy to be lax on capital works programs in order to keep costs down, however it is also important to consider relativities to ensure that where expansive programs are proposed and charged to customers, they do not make the region uncompetitive in a business sense.

#### **Question 11: Should we update prices annually for the cost of debt, or pass these changes through via true-up in the subsequent regulatory period?**

In situations where interest rate volatility is going to have a significant impact on interest costs, the adjustment mechanism needs to be regular. This does not appear to be the situation currently. However, it would be prudent to have buffers or contingencies in place in the event volatility did increase within the currency of the regulatory period.

#### **Question 16: Is there another way to gauge support from non-residential customers whose willingness to pay has not been tested, or should non-residential customers be excluded from paying for the proposed discretionary expenditure?**

While it is difficult to argue non-residential customers should be excluded from paying for proposed discretionary expenditure, it is equally difficult to get a clear consensus on the willingness to pay. This is based not only on the communication difficulties but also the elements outlined earlier concerning the variability businesses have in the capacity to pay. Where this category of expenditure remains

modest (as is now the case) we would support the principle of inclusion with a caveat that should it ever be a significant percentage of the overall expenditure regime (say more than 5 per cent) and the benefits of the incidence of the expenditure not otherwise attributable to a narrow band of customers.

**Question 26: Is a phase out of location-based prices over five years warranted or could it be done sooner, given the customers impacted are large users and may benefit from water conservation measures?**

The Chamber does not believe a shorter phase-out period is warranted given the potential substantial financial impact on the largest water users. The phase-out also needs to allow for detailed ongoing consultation with the customers affected and the investigation, development and implementation of programs to improve water efficiency and therefore mitigate financial impact on individual businesses.

**Question 32: Is Hunter Water's proposal to not equalise the water service charge for apartments with houses until the next regulatory period reasonable?**

The Chamber believes there should be transparent equity in the way customers are charged. Where inequity is identified, it should be addressed respective of capacity to pay. The Chamber does not believe apartments should continue to be considered in a different manner to houses and note that this anomaly has a flow-on impact on other customers including businesses. We support this anomaly being addressed as soon as is reasonable and practical.

**Question 34: Is there value in retaining the deemed discharge for non-residential customers?**

As has been noted earlier in this submission, there is considerable diversity in the nature of HWC's non-residential customers. The deemed discharge should remain in place until more detailed analysis is available and the impact of change clearly understood.

The Hunter Business Chamber appreciates the opportunity to provide comment on the Hunter Water pricing proposal and welcomes further engagement on these matters.

## **Contacts**

Amy De Lore  
Policy and Public Affairs Manager  
P: 4969 9600  
E: [amy.delore@hunterbusinesschamber.com.au](mailto:amy.delore@hunterbusinesschamber.com.au)

Bob Hawes  
CEO  
P: 4969 9600  
E: [bob.hawes@nswbc.com.au](mailto:bob.hawes@nswbc.com.au)