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BULK WATER TARIFF PRESENTATION TO PARLIAMENT – CONCLUSIONS OF SALGA RELATING TO WATER BOARD TARIFF INCREASES ON THE BASIS OF SECTION 42 OF THE MUNICIPAL FINANCE MANAGEMENT ACT 56 OF 2003



Recommendations

Recommendation	Detail	DWAs Response	SALGA Views	Progress
Sustainable growth projections	That utilities prepare capital expenditure budgets within the affordable growth rate of the utility given prescribed debt ceilings and CPI tariff increases.	<ul style="list-style-type: none"> ▪Point noted ▪Reduce Energy costs ▪Attempt will be made to cut cost 	This must form part of the infrastructure planning requirements	Don't see significant attention on this matter
Capital and Operating Cycle Optimisation	Form realistic capital programs and operating cycle performance	<ul style="list-style-type: none"> ▪Infrastructure Development to be informed by the supply agreement including pricing for such ▪Infrastructure to be demand driven 	An independent panel of experts should moderate infrastructure programmes in the short term	Some discussions had started – SALGA still feels this route is important



Recommendations

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Recommendation	Detail	DWAs Response	SALGAs View	PROGRESS
Factoring of local government ability	Regulator to factor the ability of local council's to absorb tariff increases.	LG to utilise Equitable share to pay for water services	The develop a water sector funding strategy	A funding an investment framework is being developed
Tariff Applications Variance	Examination of detailed utility comments for dubious tariff increases and reduce tariff accordingly.	<ul style="list-style-type: none"> ▪ Bloem Water Tariff adjusted downwards ▪ Moderating other boards tariff will require detail investigation ▪ Such moderation to be done by an independent regulator 	For 2012-13 an independent panel of expert will be helpful in the process	Some discussions had started – SALGA still feels this route is important



OTHER RELATED MATTERS

ISSUE	OBSERVATION
Standardisation of bulk tariffs proposals	Some progress but not significant
Municipal inputs into tariffs proposals	Very limited - however in some instances engagements are robust
Feedback to SALGA's comments	Only four WB – gave feedback
Feedback from DWA on the final submission to Minister	No response
Engagement with NT and DWA	Shared our analysis
Norms and standards	SALGA not yet engaged on such
Section 42 process	Inadequate supply of information



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TARIFF REGIME

Status quo remains

DWA

1st Tier
National security
of supply

Tariff regulated by the
raw pricing strategy

**BULK
PROVIDERS**

2nd Tier
Regional supply to
WSA's

Not regulated however the Water
Services and Municipal Finance
Management Acts provides
guidance

MUNICIPALITIES
(Water Services
Authorities)

3rd Tier
Local service delivery
and customer
management

Not regulated however the water
services and Municipal Finance
Management Acts provides
guidance



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Municipal Situational Context 2012/13



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SALGA POSITION ON BULK WATER TARIFFS IN WATER BOARD SECTOR

- SALGA has conducted Review of Proposed Water Board Bulk Water Tariffs for the Financial Year 2013
- This Review is conducted in Terms of S42 of the Municipal Finance Management Act
- SALGA reached conclusions on the Quantum of the Tariffs, as well as Regulation of the Tariff mechanism
- The Conclusions have been communicated to Department of Water Affairs
- Position and recommendations of SALGA is presented to Parliament ⁷



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EQUITABLE SHARE FOR WATER

2013	2014	2015	TOTAL
7 201	7 717	8 297	23 251

EQUITABLE SHARE FOR SANITATION

2013	2014	2015	TOTAL
6 204	6 648	7 149	26 649

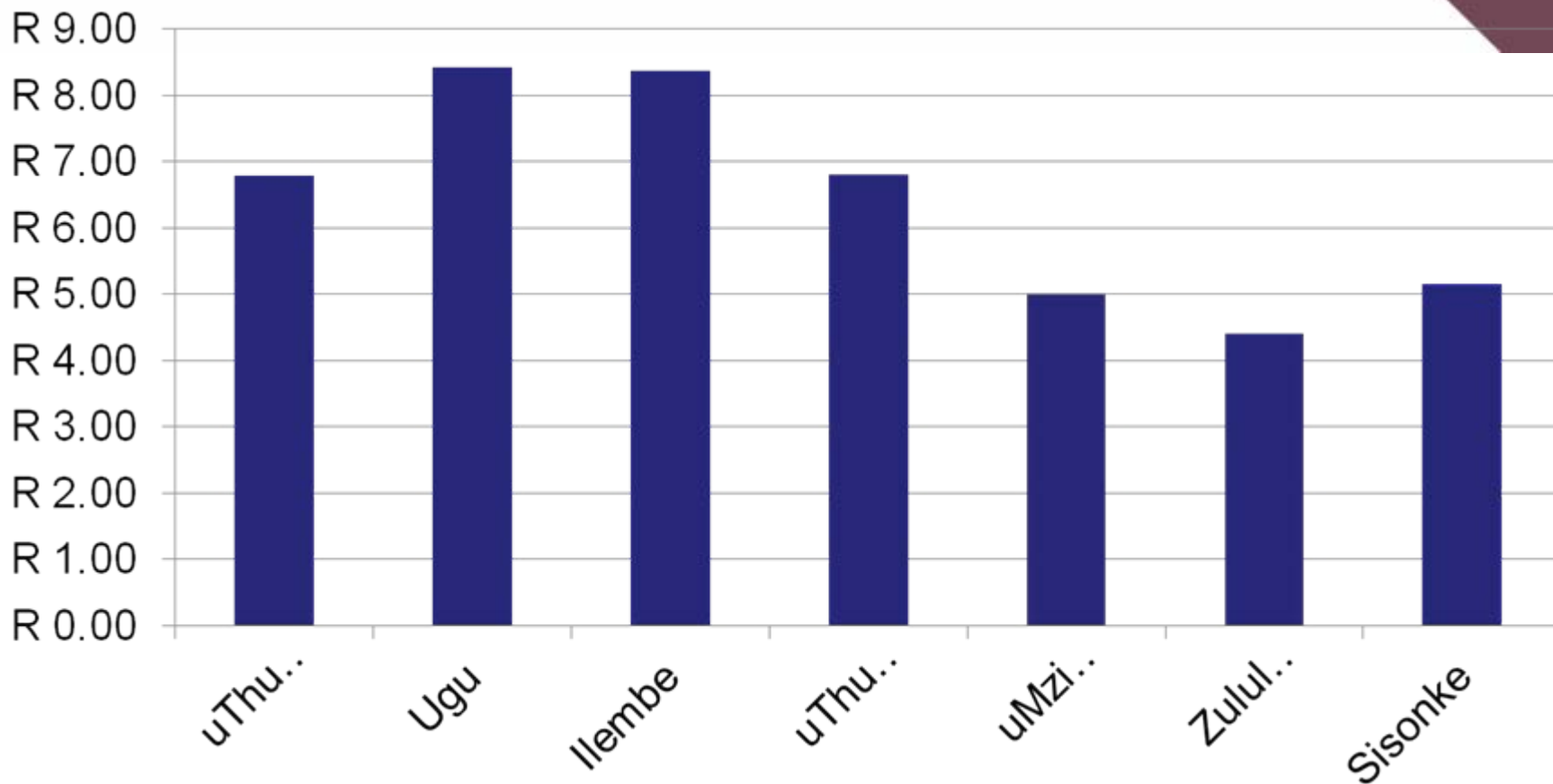


REVIEW OF LG FISCAL FRAMEWORK (MUNICIPAL FINANCE)

- The LGES will need to be re-conceptualised in its entirety rather than through minor adjustments to parameters.
 - Underlying data under-pinning LGES formula is now severely **out-dated & out of touch with dynamically changing service delivery** context (e.g. migration patterns).
- In poorer municipalities, expansion of infrastructure to poor communities through the MIG has resulted in greater pressure on operating and maintenance budgets.
- The comprehensive LGFF review should explore ways in which to explicitly link the LGES to the MIG.



Below cost tariffs (water tariffs)





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Bulk Water Tariff Increases 2012/13



Cost Drivers

Cost	Discussion
Raw Water	<p>Deteriorating water quality needing additional chemicals – raw water standards (price relation to quality). Raw water cost increases total 27% of the tariff increases</p> <ul style="list-style-type: none"> •Raw water agreements between DWA and WB
Labour	<p>Labour increases of over 10% are proposed and labour productivity is highly variable.</p>
Power	<p>Eskom's tariff increases are factored into the applications at 25% increase Subsequent to process, Eskom Tariff increase was reduced from 25% to 16%.</p> <ul style="list-style-type: none"> •No Adjustment made as yet that were seen by SALGA •Energy efficiency measures not in place
Chemicals	<p>Wide range of cost increases casts suspicion over the legitimacy of some cost increase projections, control over chemical usage</p>
Depreciation	<p>Declining Productivity of Assets, higher Depreciation Charge due to Replacement of Assets</p>



Cost Drivers Assumptions

Cost	Discussion
Revision	This Revision reduces the forecast Energy Cost for the Water Board Sector from R1,945 b to R1,810 b , or from 29% of Total Water Board costs to 27,5% . Total Overhead Costs reduce from R6,712b to R6,577b - a reduction of 1,2%



PROPOSED TARIFFS

Water Board	Tariff in 2011/12 R/kl	Proposed Tariff in 2012/13 - R/kl	% Increase	SALGA ORIGINAL TARIFF INCREASE
Amatola	5.36	5.90	10.1%	9%
Bloem	3.50	3.94	12.6%	9%
Botshelo	4.48	5.07	13.2%	9%
Bushbuckridge	3.70	3.90	5.4%	5%
Lepelle Northern	3.73	4.06	8.9%	7%
Magalies	3.20	3.49	8.9%	8%
Mhlathuze	2.83	3.10	9.5%	9%
Overberg	3.75	4.11	9.6%	0%
Rand	4.50	5.11	13.6%	9%
Sedibeng	6.36	6.90	8.5%	7%
Umgeni	3.64	4.24	16.6%	9%



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SALGA Recommendations on the bulk potable water tariffs: assumptions based on the 9% decrease on energy

Water Boards planning Increased Borrowings

Water Board	Tariff Increase (%)	Key Issues
??	??	?
Mhlathuze Water SALGA Recommendation Additional Funding Required	9,5% 7,8%	Major Capex Forecast 36% of Assets Entity over-gearred Debt: Equity 133% Return on Equity 2,90% Low but positive Liquidity Issue: Current Ratio 0,9:1 High Loan Repayments Scheduled
?	?	?
Rand Water SALGA Recommendation	13,62% 7,8%	Return on Equity Forecast 9,3% high Cash increases to 3,2 months cover - too high Debt: Equity ratio well below 40% has capacity Significant decline in Asset productivity Entity has large cash reserves Additional submissions considered by SALGA
?	?	?
Umgeni Water (Including Capital Charge) SALGA Recommendation	6,10% 16,6% 7,8%	Significant increases in cost of raw water - 106% Return on Equity 6,2% in 12, 15,69% in 13 High Debt: Equity ratio too high at 55% must reduce Sound expense management shown Significant Capex required Tariff consultation incomplete - thekwini
?	?	?

Water Boards with Significant Capital Expense Drivers

Water Board	Tariff Increase (%)	Key Issues
Amatola Water	10,1%	Operating Deficit in \$29 Business Dependence on \$30 Debt: Equity Ratio rising to 23% Very low water volume sales increases Capex increase in Fixed Assets of 1.19% requires review Return on Equity 1,74% low Expense Productivity Declining - needs attention
SALGA Recommendation	7,8%	
Bloem Water	12,6%	Financial Projections based on 8% tariff increase Moderate Capital Expansion funded by external borrowing Consultation process not fully completed Expense productivity declining Return on Equity 3,89% (at 8%) Debt: Equity Ratio at 5,81% Additional submissions considered by SALGA
SALGA Recommendation	7,8%	
Magalies Water	8,9%	20% Driven by identified cost increases at one plant Entity was trading at Net Deficit Improved productivity and cost management Return on Equity increased from 2% to 3,6% by 16% Cash Reserves moderate Major Capex planned
SALGA Recommendation	8%	

Water Boards with Sustainability Challenges

Water Board	Tariff Increase (%)	Key Issues
Botshelo Water	13,2%	Entity trading under insolvent conditions Inadequate documentation supplied Negative business trajectory
SALGA Recommendation Additional funding required	9%	
Bushbuckridge Water	5,4%	Entity forecasting very large expense increases Doubtful debts major issue Figures supplied are unreliable Recommended interim increase Control issues to be addressed
SALGA Recommendation	5%	
Overberg Water	9,6%	Tariff consultation incomplete - objections Entity trading at loss Additional funding required High Debt:Equity ratio at 4,5% Expense management requires review Return on equity negative - marginal sustainability
SALGA Recommendation (Pending resolution of objections)	7%	

Water Boards with Unused Financial Capacity

Water Board	Tariff Increase (%)	Key Issues
Lepelle Northern Water	8,9%	<ul style="list-style-type: none"> Capital Expenditure to be funded from Operating Profits Significant R30 Income & profit not reported Return on Equity very high at 13% Debt: Equity ratio is negative 35% Short-term investment very high Entity is over-funded Entity has high cash balances
SALGA Recommendation	7%	
Sedibeng Water	8,5%	<ul style="list-style-type: none"> Low Debt: Equity ratio at 10,2% High levels of cash - R89m Modest Capex Program Very high Debtors days at 130 Return on Equity 6,3%
SALGA Recommendation	7%	



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Recommendations to

Parliament and DWA



Top 6 Key Points

1. Effective and Efficient MT and LT Capital Investment programme
2. Effective, efficient and pro-active management of Expenses, within Parameters
3. Tariff Policy to guide WB Funding and Tariff approach
4. Rational and effective Treasury management process to optimise funding of Water Boards
5. Enhanced control over Tariff determination process
6. Managed Progression towards Implementation



1. Capital Investment Programme

- Water Boards must demonstrate effective and efficient Medium and Long Term Capital Investment programme to improve asset productivity while balance growth in supply of services with borrowing capacity of Water Boards and affordability of Water to customers



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2. Effective Management of Expenses

- Water Boards must demonstrate effective, efficient and pro-active management of Expenses, specifically in the Staff and Energy cost areas and Expense parameters should be set by DWA



3. Tariff Policy to guide WB Funding and Tariff approach

- A Tariff Policy to guide the Funding of Water Board Assets and the recovery of Capital and Operating Costs, dealing with the standardisation of the approach to funding of assets and expenses (pre-funding, matching or arrears funding)
- A Review of the Funding Structure of Water Boards (Debt: Equity Ratio, Financial Asset Levels, Current Ratio levels, Cash Balances) and a Rationalisation Plan for each Water Board



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4. Rational Treasury management process to optimise funding of Water Boards.

- A rational and effective Treasury management process must be developed to optimise funding of Water Boards, accessing capital funds, provision of Government subsidies/grants, and optimising use of funds between Water Boards within Sector



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5. Enhanced control over Tariff determination process

- Tariff-setting process should begin with DWA Approval of Planned Capital and Expense parameters
- DWA should ensure that Tariff Proposals are in line with approved WB Corporate Plans
- Tariff Proposal documentation should be standardised and include motivation for increases in Expenses and Capex
- S42 Consultation Process should be documented in Standardised format, and formally approved by DWA
- S42 Consultation Process should include Capital Expenditure Plan



6. Managed Progression towards Implementation

It is suggested that:

- A Centralised Water Demand Planning function be established, to match water needs with MT and LT Infrastructure Investment, and to review proposed Capex Projects of WB to enhance productivity
- A set of Expense Targets for MT and LT be constructed for the Sector, and for each Water Board, the Targets managed, and Water Boards be incentivised to reach the Targets
- A centralised Cash Management function be implemented to optimise the funds utilisation within the Sector



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Conclusion

- Parliament note the 6 key Points raised by SALGA
- DWA considers these recommendation for implementation in the next tariff cycle



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Thank You!