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Essential Services Commission
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INQUIRY INTO AN ACCESS REGIME FOR WATER AND SEWERAGE INFRASTRUCTURE SERVICES

This submission is put forward by the Consumer Utilities Advocacy Centre Ltd (CUAC) in response to the Issues Paper released by the Victorian Essential Services Commission (the Commission) on the *Inquiry into an Access Regime for Water and Sewerage Infrastructure Services – Issues Paper* (the Issues Paper).

CUAC is an independent consumer advocacy organisation which ensures the interests of Victorian electricity, gas and water consumers - especially low-income, disadvantaged, rural and regional and Indigenous consumers - are effectively represented in the policy and regulatory debate.

This submission is endorsed by the Consumer Action Law Centre (Consumer Action) and the Victorian Council of Social Services (VCOSS).

We welcome the opportunity to provide comment to the Commission on the Issues Paper. This submission outlines our views and recommendations on an access regime, based on research we have undertaken. We have concentrated on issues that are important for consumers, particularly with respect to the interests of low-income and disadvantaged households, in establishing an access regime in Victoria.

As a preliminary comment, we are aware that third party access regimes are a recent phenomenon in Australia, with New South Wales the predominant State with an access regime for water and sewerage infrastructure¹. The New South Wales water reforms commenced in 2006 and that State is now awaiting certification of its access regime by the National Competition Council. With such limited examples in the Australian market, a full appraisal of consumer impacts is difficult. As a new approach to water management in Australia, and noting documented disadvantages of private participation in water internationally, we strongly encourage the Commission to consult further with relevant agencies in New South Wales and overseas to determine how the regime has specifically brought efficiencies and downstream benefits to consumers, prior to introducing it in Victoria.

We acknowledge that this Inquiry is an outcome of the 2007-08 Inquiry into the *Reform of the Metropolitan Retail Water Sector*, undertaken by the Victorian Competition and Efficiency Commission (VCEC). CUAC, together with Consumer Action, participated in the public consultation process as part of the VCEC Inquiry. In a submission to VCEC, CUAC and Consumer Action indicated support for a third party access regime, where it avoided the implementation of an ad hoc, piecemeal and costly system or which might occur under the

¹ Essential Services Commission 2009, *Inquiry into an Access Regime for Water and Sewerage Infrastructure Services—Issues Paper*, February, p. 32

*Commonwealth Trade Practices Act 1974*². An access regime would relate, in the main, to 'upstream' infrastructure development, wastewater and recycled water undertakings with longer term 'downstream' benefits accruing to consumers. CUAC and Consumer Action also stated that the process to determine pricing methodology must be one in which the views of all relevant stakeholders are sought and prices must be cost-reflective and efficient without impacting on affordability. An access regime must incorporate public and transparent consultation in its development and operation, with consumer protections in place.

We understand that the role of the Commission is now to direct an Inquiry into developing an access regime for water and sewerage infrastructure services. The Commission will make recommendations into how an access regime could operate in Victoria, including an access pricing methodology.

The Department of Sustainability and Environment (DSE) Office of Water also has responsibility for acting on another of the recommendations of the 2007-08 Inquiry into the *Reform of the Metropolitan Retail Water Sector*, which is the migration of metropolitan water businesses from the *Water Industry Act 1994* to the *Water Act 1989*. Under the *Water Act* businesses will become statutory corporations with an enhanced level of public accountability and priority to serve consumers. Third party access, however, may result in benefits to private investors rather than consumers.

Within the context of the Commission's role, the DSE review and considering CUAC's previously stated position on an access regime, we have outlined our key concerns with those issues raised in the Issues Paper, as well as provided specific responses to issues raised for consideration by the Commission. We have not addressed all of the questions in the Issues Paper, but have instead concentrated on those most relevant to CUAC. We look forward to expanding on issues during further consultation with the Commission.

Key Recommendations

Water is an essential service, fundamental for life and health. Ensuring access and equity must be of foremost priority when undertaking regulatory decision making in the water sector.

CUAC has supported cost reflective, efficient water pricing together with a strong consumer protection framework for Victoria, with reviews overseen by a regulatory authority to ensure water remains affordable for consumers. We continue to advocate for adequately resourced hardship programs and a well targeted Government concession framework.

CUAC supports reform measures in the water sector which deliver consumer benefits, with adequate consumer protection including health and safety standards, and reliability of supply. We are concerned, however about the potential impacts of water reform for residential consumers, for low income and disadvantaged households and for vulnerable communities.

CUAC recommends that, in considering the establishment of a third party access regime, the Commission commit to actioning the following key points:

- Ensure that the process of decision making is underpinned by the primary objective of the Commission as outlined in the *Essential Services Commission Act 2001*, which is to protect the long-term interests of Victorian consumers with regard to the price, quality and reliability of essential services;
- Ensure that the reform process reflects a carefully staged and consultative approach, to maximise benefits to consumers and that any benefits accrued by competition in third party access flow to consumers rather than private shareholders;

² CUAC and Consumer Action 2008, *Inquiry into Reform of the Metropolitan Water Sector*. Submission no: DR 73, 24 January 2008. See VCEC web site: <http://www.vcec.vic.gov.au>

- Undertake a multi staged analysis of the benefits and potential disadvantages to Victorian consumers that may result from introducing a state based access regime. This analysis should demonstrate what the proposed regime would look like and how it might affect the provision of water supply and access by Victorian consumers;
- Present findings of the analysis to the community, as a draft paper for consultation;
- Engage stakeholders in any planning process, with an emphasis on transparency and public consultation;
- Strengthen and extend existing regulatory safeguards and consumer protections, including hardship programs and the concession framework, where these may be necessary, and consult with consumer groups as part of this process;
- Ensure that access benefits outweigh costs and ultimately provides savings for consumers. Access to the water network will require additional infrastructure to be built, and will put additional strain on the existing network, which will result in additional costs to consumers. Benefits must outweigh costs or alternatively, the new provider should pay those costs given they are supplying water to make a profit on a commercial basis;
- Ensure adequate health and safety standards have been clearly established to protect consumers and which entrants must meet, with robust monitoring in place;
- Consider public interest principles, as outlined in Clause 1.3 of the *Competition Principles Agreement*, when undertaking decision making on an access regime. The public test should be expanded for specific inclusion of non-economic factors in consideration of both the public benefit and any counter balancing detriment; and
- Consult with the public regarding the need for access entrants to demonstrate positive public interest outcomes as a condition of participation in an access regime.

Specific responses to questions in the Issues Paper

As stated, CUAC recommends that the next step of the Commission is to develop a draft paper for consultation on what a proposed access regime would look like and what benefits and possible disadvantages would result for Victorian consumers.

In addition, CUAC has referred to some of the issues presented in the Issues Paper which further the argument for a multi staged analysis or have specific relevance for consumers.

Lessons learnt from other industries

CUAC recommends that the process of moving to a third party access regime for water be undertaken with careful foresight and planning in order to deliver consumer benefits. Third party access is most commonly applied to network-based utility industries (telecommunications, gas and electricity)³ and examples of third party access in the water sector are extremely limited in Australia and internationally⁴. Differences between the energy and water sectors collectively suggest that the efficiency successes of third party access in energy may not be repeated to the same extent for water⁵. Central to these differences is the need to address public health concerns and safety of water and sewerage systems as well as the strongly held view in Australia that the provision of clean and safe water is a basic right, priced as prudently as possible⁶.

³ Marsden Jacob Associates 2005, *Third party access in water and sewerage infrastructure: implications for Australia*, p. ii http://www.daffa.gov.au/_data/assets/pdf_file/0019/29260/3_water_sew_infr.pdf

⁴ Marsden Jacob Associates, p. iv

⁵ Marsden Jacob Associates, p. 47

⁶ Marsden Jacob Associates, p. 46

We also recommend the Commission consider the impacts of private participation and competition in the water industry on consumers in the United Kingdom, and develop mechanisms which ensure that Victorian consumers are delivered downstream benefits. Research shows that since privatisation of water in the United Kingdom consumers have faced significant increases in prices. According to the Consumer Council for Water, which represents consumers in England and Wales, since privatisation water bills have risen to around 44% higher in real terms, and by 2010 it is expected that 12% of consumers will face water and sewerage bills which are more than 3% of their disposable income⁷. There has also been an increase in consumer complaints, with record complaints recorded over 2007-08⁸, yet a low level of awareness among consumers about their rights, including the minimum levels of service they are entitled to from their water companies⁹.

The Commission should bear in mind that reform of the energy industry in Victoria has coincided with an increase in customer complaints. We are aware that in comparison water complaints are much lower than those related to the energy sector. For example, figures from the Energy and Water Ombudsman of Victoria (EWOV) show that from 2007-08 1,562 water cases were presented to EWOV while 23,110 related to energy¹⁰. We would like to see the low level of water cases maintained and recommend that the Commission consult with EWOV on reform issues that may impact on customer complaints.

Factors to be considered in the design of an access regime

As noted by the Commission, implementing a strategy to enable greater competition in an industry dependent on natural monopoly facilities is a lengthy and evolving process and there is limited experience of implementing such reform strategies in water industries¹¹. A full analysis of benefits and disadvantages to consumers of an open access regime, with extensive consultation and feedback to the community is imperative and must consider, at minimum, issues of:

- Accountability - Public concern for accountability has been identified as an issue of major significance in the third party access debate¹². Unbundling of the wastewater sector and breaking up obligations along the supply chain, for example, may make it easier for businesses to avoid responsibility for supply failures¹³. Ensuring that water is safe for public health, is reliable and secure¹⁴ is paramount to successful implementation of third party access and the accountability of governments;
- Cost – The increasing costs associated with network augmentation and infrastructure requirements will place further pressure on water prices for consumers. Efficient network planning and design and placing the onus on the water supplier to pay for these costs needs to be considered to ensure benefits flow to consumers;
- Efficiencies – scepticism from industry has been noted as to whether efficiencies may be gained from third party access, particularly to the level derived from competition in the energy sector¹⁵. In regards to access pricing determinations, consumers will ultimately have to pay for any economic inefficiency¹⁶; and
- Transparency – a transparent planning process, with public involvement in decision making, has been identified as a key driver in the success and sustainability of water

⁷ Consumer Council for Water, 2008, *Affordability and bills*, <http://www.ccwater.org.uk/server.php?show=ConWebDoc.1779>

⁸ BBC 2008, *Record complaints to water firms*, <http://news.bbc.co.uk/2/hi/business/7604644.stm>

⁹ Consumer Council for Water, 2009, *Awareness low on rights*, <http://www.ccwater.org.uk/server.php?show=ConWebDoc.2025>

¹⁰ Energy and Water Ombudsman of Victoria, 2008, *Annual Report*, p.16

¹¹ ESC, p. 17

¹² Marsden Jacob Associates, p. 89

¹³ Janice Gray & Alex Gardner 2008, *Exploiting the unspeakable: Third-party access to sewage and public-sector sewerage infrastructure in Troubled waters: confronting the water crisis in Australia's cities* ed. Troy, P. p. 145 http://epress.anu.edu.au/troubled_waters/mobile_devices/ch07s14.html

¹⁴ Marsden Jacob Associates, p. x

¹⁵ Marsden Jacob Associates, p. 87 and p. 88

¹⁶ Public Interest Advocacy Centre 2006, *Submission to Consultation Paper on Introducing a dynamic and competitive metropolitan water industry*, p. 10.

http://www.waterforlife.nsw.gov.au/data/assets/pdf_file/0007/1501/PublicInterestAdvocacyCentre_070606.pdf

sector projects.¹⁷ A comprehensive public consultation process is imperative. The public must be able to have meaningful participation and fully understand how third party access will impact on service provision, including quality of supply and prices.

Customer protection framework and EWOV scheme

We recommend that the Commission deliberate over the Customer Service Code to assess whether it may need to be strengthened before commencement of a third party access regime. The Commission also needs to consider the obligations of third parties to reporting and accountability in relation to the size and type of service they provide. This is particularly important as the service provision of a third party entrant may potentially impact on public health or water quality.

The Victorian water sector has demonstrated a culture of service delivery that emphasises customer service, continuous improvement, collaboration and innovation. Competition by comparison has allowed the Commission to publicly monitor and report on the performance of water retailers in order to encourage businesses to further improve their performance relative to others, and has provided incentives for businesses to improve their own performance over time. This has led to a transparency and accountability of a wide variety of aspects of services and service delivery contributing to improvements in options and outcomes for consumers.

We strongly agree with the Commission's suggestion that new entrants to the water industry should be required to join the EWOV scheme relating to water and sewerage services, where these entrants have retail consumers.

The Commission must ensure that there are disincentives for market entrants which enter for short term financial gains or to test the market. Regulations should ensure continuity of residential drinking water supply and sewage services in the long term.

Public interest

CUAC recommends the Commission specifically consult on whether an approach which places a greater obligation on proponents of access to demonstrate positive public interest outcomes would be successful.

Under Part IIIA of Trade Practices Act access seekers that apply for third party access to services provided by significant infrastructure must show that the access is not contrary to the public interest, being that the costs do not outweigh the benefits¹⁸. Currently, the public interest is not a defined term in the Trade Practices Act and the National Competition Council and Australian Competition Tribunal uses a case-by-case approach to determine whether a particular access arrangement would be contrary to the public interest, against factors in clause 1.3 of the *Competition Principles Agreement*¹⁹.

We support the use of these principles, which take into account social welfare and equity considerations, ecological sustainable development, regional considerations and health and safety.

We note the position of a consumer group in New South Wales which have argued that entrants should be obligated to demonstrate how access would result in positive public interest outcomes²⁰. The benefits and disadvantages of emphasising a positive onus on access seekers is also explored in literature on third party access in Australia²¹.

¹⁷ Meena Palaniappan et al., 2006, *Assessing the long-term outlook for current business models in the construction and provision of water infrastructure and services*, OECD p. 37.

http://www.pacinst.org/reports/oecd_water_report/oecd_water_paper.pdf

¹⁸ ESC, p. 22

¹⁹ Public Interest Advocacy Centre, p.11

²⁰ see Public Interest Advocacy Centre 2006, *Submission to Consultation Paper on Introducing a dynamic and competitive metropolitan water industry*, p. 11.

http://www.waterforlife.nsw.gov.au/_data/assets/pdf_file/0007/1501/PublicInterestAdvocacyCentre_070606.pdf

²¹ Gray & Alex Gardner p. 132-333 http://epress.anu.edu.au/troubled_waters/mobile_devices/ch07s08.html#d0e3383

We recommend the Commission specifically explore if this approach could be undertaken in Victoria. However, as identified in a report by Consumer Action²² the scope of the public benefit test should be expanded for specific inclusion of non-economic factors in consideration of both the public benefit and any counter balancing detriment.

Protecting public health and water quality

Safe water is paramount for public health. CUAC is concerned about potential health and environmental risks involved with further entrants seeking to inject water into the water supply network.

While we support the Commission's proposal that appropriate compensation mechanisms should be in place in the event of breaches of quality standards, including the proposal that new entrants seeking to inject water must have risk management plans and undertake monitoring and sampling to demonstrate that the water to be injected into the system is of water quality standards, we strongly recommend clear establishment of minimum quality standards and robust monitoring upfront. This will reduce the likelihood that consumers are exposed to risk.

Transitional arrangements

CUAC strongly supports transitional arrangements as part of an access regime. In particular, we support measures which ensure that disadvantaged and low income consumers do not face adverse pricing consequences, such as price shocks.

Access disputes

We support an independent arbitrator to make a determination in an access dispute. We agree that the independent arbitrator must have sufficient resources and expertise to carry out its dispute resolution role and that arbitration is binding. We do not think the Commission should be appointed as arbitrator as this would impinge upon the independent status required for the position.

Commission as Regulator

We believe that the Commission possesses the necessary expertise to be granted responsibility as regulator of an access regime, mandated to operate with transparency and wide reaching consultation.

Review of institutional framework

We urge the Commission to commence a full review of the existing framework on the basis that it is possible that the existing institutional framework contains gaps that could limit its coverage or that the relevant regulatory agency lacks sufficient powers to effectively regulate a new entrant²³. We stress the necessity for strong regulatory rules and monitoring for consumer protection, including health and safety.

Access pricing

CUAC supports a cost reflective pricing model, with safeguards in place so that consumers do not have to indirectly fund the costs of competition. The model should generate sufficient margins and only efficient entry should be encouraged. We would support the regulator in choosing the best access pricing model, subject to a full cost benefit analysis and the inclusion of regulatory guidance on prices, such as indicative tariffs or reasonable price boundaries, to provide a framework for access negotiations between infrastructure operators and access seekers.

Environmental protection regulatory framework

As a minimum, the current environmental protection regulatory framework should be reviewed. The framework should be strengthened on the basis of the review to fully consider the implications on health and water quality from a range of water suppliers. These should be linked to upfront license requirements.

²² See Consumer Action Law Centre 2007, *Defining "public benefit" - social and environmental considerations in Part VII of the Trade Practices Act 1974 (Cth)*. <http://www.consumeraction.org.au/downloads/DefiningpublicbenefitReportfinal.pdf>

²³ ESC, p. 64

Licensing system

CUAC recommends a licensing system, rather than a registration framework, as it would provide stronger protections and monitoring. Access seekers would have to meet specific criteria to successfully be issued with a licence. Licence applications would need to address public interest principles, including water quality and consumer protection.

The Commission should be responsible for assessing licence applications and granting of licences. Licences must also be reviewed by the Commission on a periodic basis.

Consistency with current regulatory framework

The process for determining access prices and prices for new water and sewerage services should be consistent with the current process of price determination, except where some adaptation is required.

Government policy needs to take into account access issues for low income and disadvantaged consumers. The concession framework must be extended to cover retail services offered by new entrants.

Reviews

We recommend a review to be undertaken in the first instance after one year of operation of the access regime. Subsequent reviews should be linked in to water pricing reviews and benefits for consumers.

Information collection, reporting and auditing requirements

We recommend that access seekers be subject to rigorous information collection, reporting and auditing requirements. Some new auditing systems may be required to accommodate innovative services.

We agree that arrangements need to be made to ensure that access seekers are subject to the information provisions relating to other relevant regulators, such as the Environmental Protection Agency and the Department of Human Services.

Legislative and regulatory barriers

CUAC has no comment on legislative and regulatory barriers at this stage as we would prefer to address the issue when there is further information provided as to a proposed access regime.

Should you wish to discuss any matters raised in this submission, please do not hesitate to contact me on (03) 9639 7600.

Yours sincerely



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