



**WATER SERVICES
ASSOCIATION OF AUSTRALIA**



WSAA Submission

**Legislative Council Select
Committee TasWater
Ownership**



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1.0 Introduction

The Water Services Association of Australia (WSAA) is the peak body that supports the Australian urban water industry. Our members provide water and sewerage services to over 20 million customers in Australia and New Zealand and many of Australia's largest industrial and commercial enterprises.

WSAA facilitates collaboration, knowledge sharing, networking and cooperation within the urban water industry. The collegiate approach of its members has led to industrywide advances to national water issues.

WSAA welcomes the opportunity to provide comments on the Water and Sewerage Tasmania Bill 2017 and the Water and Sewerage Tasmania (Consequential and Transitional Provisions) Bill 2017.

WSAA advocates nationally for reforms to the water industry that support the long term interests of customers and the community. Our positions are set out in a number of publications over the last three years. In 2014, we commissioned a report from Frontier Economics on improving economic regulation. It drew on economic regulation both in Australia and internationally to identify the elements of a best practice model. In 2015, we released a paper on national water reform with Infrastructure Partnerships Australia. Most recently the urban water industry's views have been brought together in WSAA's submission to the Productivity Commission's review of national water reform, and WSAA is an active participant in the Commission's inquiry.

Applying the lens of national reform to the urban water industry demonstrates that the right institutional structure for urban water utilities is fundamental to good outcomes for customers. A key feature of national urban water reform was the COAG competition reforms of the 1990's. All state and territory governments and the Commonwealth agreed that government-owned industries such as water and electricity should be set up as Government Business Enterprises under a corporatisation model.

WSAA strongly suggests that any changes to the governance arrangements for water utilities should be assessed against the agreed COAG model of corporatisation. This brief submission sets out the elements of the corporatisation model and comments on consistency of the proposed Tasmanian legislation with the model.

WSAA wishes to emphasise that it has no position on who should own water utilities. In this case we have no opinion on whether TasWater should be owned by the state government or local governments. Our comments relate to the governance in place regardless of ownership.

2.0 The COAG Corporatisation Model

In 1994, the Council of Australian Governments (COAG) unanimously endorsed a reform framework for Australia's water industry as part of a wider package of reforms to the government sector. COAG's explicit reform objectives were to increase competition and to improve the efficiency and effectiveness of service delivery. This framework was incorporated into the 2005 National Competition Policy (NCP) agreements that included undertakings to implement a program for reforms to the government sector.

A key element of the COAG agreement was that urban water utilities should have a commercial focus. The NCP made a direct recommendation that government business enterprises be corporatised to meet the competitive neutrality principles. The corporatisation model was developed to provide government owned businesses with similar incentives for efficiency as private counterparts. Corporatisation improves the discipline facing water utilities as it provides for:

- clear and non-conflicting corporate objectives
- managerial responsibility, authority and autonomy from executive government
- effective performance monitoring by the owner government
- effective rewards and sanctions related to performance

The NCP arrangements referenced the work of the inter-governmental committee responsible for Government Trading Enterprise (GTE) national performance monitoring as an appropriate model for corporatisation from 1991. This set out seven characteristics of a fully corporatised GTE to achieve effective reform, summarised in Box 1. These characteristics may remain the most effective approach for government business to operate under the principles of competitive neutrality.

Independent economic regulation of utilities was one of the key aspects of the competition policy frameworks and reforms. Its aim is to ensure a degree of independent oversight and helps ameliorate the inherent conflict where government is at once the shareholder, rule setter, operator and retailer. The intention was for regulation to reproduce the discipline otherwise provided by competition, to ensure that monopoly businesses do not earn monopoly profits or provide sub-standard services, while still enabling them to cover the efficient cost of operating and maintaining the network assets. A best practice regulatory framework for the water industry would typically entail:

- determination or oversight of the prices and service levels provided by monopoly suppliers
- licensing of suppliers as a means of monitoring and enforcing compliance with these services/prices
- overseeing competition in contestable elements of these industries (e.g. via regulation of third party access to essential facilities)

Economic regulation and independent price oversight has played an important role in the water industry's development and it needs to continue to evolve to meet future challenges. Overall, there is strong evidence of significant benefits from the pricing and institutional reforms undertaken, including the introduction of consumption-based charging in most metropolitan and regional urban areas.

Customers are the ultimate beneficiary of robust and independent governance structures and economic regulation models. Better economic regulation means - prices are kept as low as possible, services and investments are targeted at areas of highest customer value, and there are greater opportunities for customer engagement and more transparent decision making. This requires that all aspects of the broader regulatory framework including economic regulation, environmental regulation and drinking water quality regulation are focused on achieving outcomes at lowest cost in an integrated manner.

Box 1: Characteristics of a Fully Corporatised GTE

- i) **Clear and Non-Conflicting Objectives**
 - a clear understanding of the government shareholder objectives
 - guidance given where there are conflicts between commercial, social and regulatory objectives
 - contractual arrangements covering community service obligations (CSOs) between the entity and government provider and that ideally, the provision of such services should be open to competitive tender to minimise the costs
 - ministerial responsibility for the commercial success of an enterprise should be separated from the responsibility for associated regulatory functions.
- ii) **Managerial Responsibility. Authority and Autonomy**
 - government as owner should operate at arm's length from the Board and management of the enterprise so that managers can be held fully accountable for their performance.
- iii) **Effective Performance Monitoring by the Owner-Government**
 - established independent and objective performance monitoring arrangements, such as a central monitoring unit
 - such a unit would review the GTE's business plans and provide advice to the shareholding Ministers, including on the entity's proposed core activities, rate of return, dividends and capital structure.
- iv) **Effective Rewards and Sanctions Related to Performance**
 - incentive systems and penalties should exist against agreed performance targets and should act to motivate the Board and management to maximise the performance of the enterprise.
- v) **Attaining Competitive Neutrality in Input Markets**
 - GTEs should not enjoy any special competitive advantages or disadvantages over their private sector counterparts because of their government ownership
 - a level playing field is needed on a range of issues, including cost of debt, return on equity, tax arrangements.
- vi) **Attaining Competitive Neutrality in Output Markets**
 - removal of protective barriers that reduce competition faced by government enterprises
 - GTEs should be subject to the same legislative regulations as private sector enterprises.
- vii) **Effective Natural Monopoly Regulation**
 - where GTEs enjoy a natural monopoly, a public policy framework should be established to ensure that natural monopoly powers are not abused

NSW Treasury, Characteristics of a Fully Corporatised Government Trading Enterprise, August 1991

3.0 Comments on the Tasmanian legislation

Assessed against the Nationally agreed model of corporatisation, WSAA has three broad concerns with the proposed Tasmanian legislation.

1. The removal of the commercial objective from the utility set out in the Government Business Enterprises Act 1995.
2. The blurring of the lines of accountability between the Minister and the utility through the Infrastructure Investment Plan
3. Removing the independent economic regulators ability to set prices.

3.1 Objectives of the utility

The objectives of the corporation are set out in clause 6 of the Water and Sewerage Tasmania Bill 2017. WSAA supports the objectives relating to the efficient and effective delivery of services and investment. However, clause 6 removes the application of clause 7 of the Government Business Enterprises Act 1995 from the corporation. Clause 7 is the principal objectives of the GBE and is set out in Box 2.

It would appear that removing this clause removes one of the key pillars of the corporatisation model — for the utility to act commercially, balanced with delivering any community service obligations specified by the owner government.

Box 2: Principal objectives of a Government Business Enterprise

- (1) The principal objectives of a Government Business Enterprise are –
 - (a) to perform its functions and exercise its powers so as to be a successful business by –
 - (i) operating in accordance with sound commercial practice and as efficiently as possible; and
 - (ii) achieving a sustainable commercial rate of return that maximises value for the State in accordance with its corporate plan and having regard to the economic and social objectives of the State; and
 - (b) to perform on behalf of the State its community service obligations in an efficient and effective manner; and
 - (c) to perform any other objectives specified in the Portfolio Act.
- (2) On the request of the Portfolio Minister, the Treasurer may, by notice published in the Gazette, specify the economic and social objectives of the State relevant to the Government Business Enterprise specified in the notice.

3.2 Infrastructure Investment Plan

Another element of the corporatisation model was clear roles and responsibilities and making water utilities accountable for the delivery of services. Section 15 of the Water and Sewerage Tasmania Bill 2017 requires the Board of the utility to prepare an infrastructure investment plan at the same time it prepares its corporate plan.

However, the Bill requires:

- the plan to be in a form specified by the Treasurer
- the Board consult with the water Minister and Treasurer in preparing the plan
- a draft of the plan is to be provided to the Minister and Treasurer
- that a draft of the plan becomes the plan of the Corporation when it is approved by the Minister and Treasurer
- the Minister and Treasurer approve any amendments to the plan
- the Corporate Plan is to be consistent with the Infrastructure Investment Plan

Although it will depend on how the Infrastructure Investment Plan is implemented, on the face of it, section 15 is unlikely to promote the separation of roles and Board accountability that was part of the original COAG corporatisation model.

3.3 Independent Price Regulation

For monopoly industries such as water, independent price regulation is important to protect consumers. WSAA’s previous work in this area has demonstrated that best practice is for a regulator to set prices independently from government.

Currently in Tasmania, like other states across Australia outlined in Box 3, prices and revenue are independently determined by the Tasmanian Economic Regulator. In contrast under the new arrangements it is proposed that while the economic regulator will advise on maximum prices, it will be the Treasurer who is responsible for setting maximum prices.

As set out in the second reading speech:

This new regime makes the Treasurer responsible for setting maximum prices, which the Government have committed to being in the range of 2.75% to 3.5%, in the form of a pricing order, following a pricing investigation by the Regulator. The Minister and the Treasurer will set the terms of reference for the investigation.

The new regime appears to significantly weaken the role of independent regulation.

Box 3: Independent Price Regulation in Australia

Most economic regulators of the urban water industry across Australia do have powers to regulate services which are provided under conditions of market power, and this power has been appropriately bestowed on them by government. Economic regulators should be given clearly defined powers and functions (set out in legislation) necessary to undertake their role and achieve their regulatory objectives.

Economic regulators in NSW, Victoria, and South Australia have deterministic powers where the independent regulator determines prices (or allowable revenues) with legal effect.

Region	Regulator	Description
SA	Essential Services Commission of South Australia (ESCOSA)	Determines prices, conditions relating to prices, and price-fixing factors for water retail services. Specific prices set must comply with the Commission’s allowed revenues.
NSW	Independent Pricing and Regulatory Tribunal New South Wales (IPART)	Reviews and determines the maximum prices that can be charged for bulk and retail water by most major water utilities across NSW.
VIC	Essential Services Commission (ESC)	Review and approves water pricing and annual tariffs to ensure consistency with determinations.

In our submission to the Productivity Commission on their inquiry into the reform of Australia’s water resources sector, we further outline our reform agenda. We review the progress of national reform since its inception and set out the main reforms necessary to meet future challenges. A key element of this is economic regulation’s role in the urban water industry’s development.

4.0 Contact Details

WSAA welcomes the opportunity to discuss this submission further.

If there are any details you wish to follow up on please contact:

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5.0 Reference Material

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