

URBAN WATER UPDATE

New Federal Government

The election of the new Labor Federal Government may see a changing focus in tackling the key issues in the water industry.

The Government has made a number of policy announcements to address the key issues which include:

- Investing in more efficient and sustainable irrigation and farming practices throughout Australia;
- Working with households and businesses to conserve water in towns and cities and to invest in water infrastructure;
- Promoting storm water capture and the use of recycled water – especially by industry;
- Promoting new sources of water which are not dependent on rainfall i.e. desalination;
- Protecting rivers, waterways and the natural environment;
- Investing in water infrastructure in order to restore flows to the Murray Darling Basin;
- Reversing licence over-allocation by buying water entitlements from winning sellers; and
- Bringing forward \$400 million of spending under the \$10 billion plan to fast-track action to secure water.

The Labor Government proposes to work with all State Governments to support practical infrastructure projects including:

- \$1 billion investment in water recycling, desalination and major storm water capture projects;
- National target of recycling 30% of wastewater by 2015;
- \$500 worth of rebates to households to install rainwater tanks or grey water pipes;
- Offering of low interest loans of up to \$10,000 to help families invest in water and energy savings;
- \$250 million to fix pipes and ensure water reaches its destination with minimum loss;
- Ensuring the correct implementation of the 2004 National Water Initiative; and
- The establishment of a National Centre of Excellence in Water Desalination which will develop and commercialise new water technology. Two centres will be built – one in Perth and the other in Brisbane – ensuring that new forms of energy efficient bulk water supplies being developed in Australia are built on and that the skills are kept within the country.

State of Play

With most of the capital cities experiencing severe water deficiency at the moment (as highlighted in the table below), water reforms and the sustainable management of current resources are a high priority.

CITY	Average Percentage of Water Level in main supplying dam/s
Sydney	60%
Melbourne	40%
Brisbane	20%
Hobart	90%
Adelaide	80%
Perth	43%
Darwin	76%

Source: <http://www.switchbanks.com.au/watersaving.html> (December 2007)

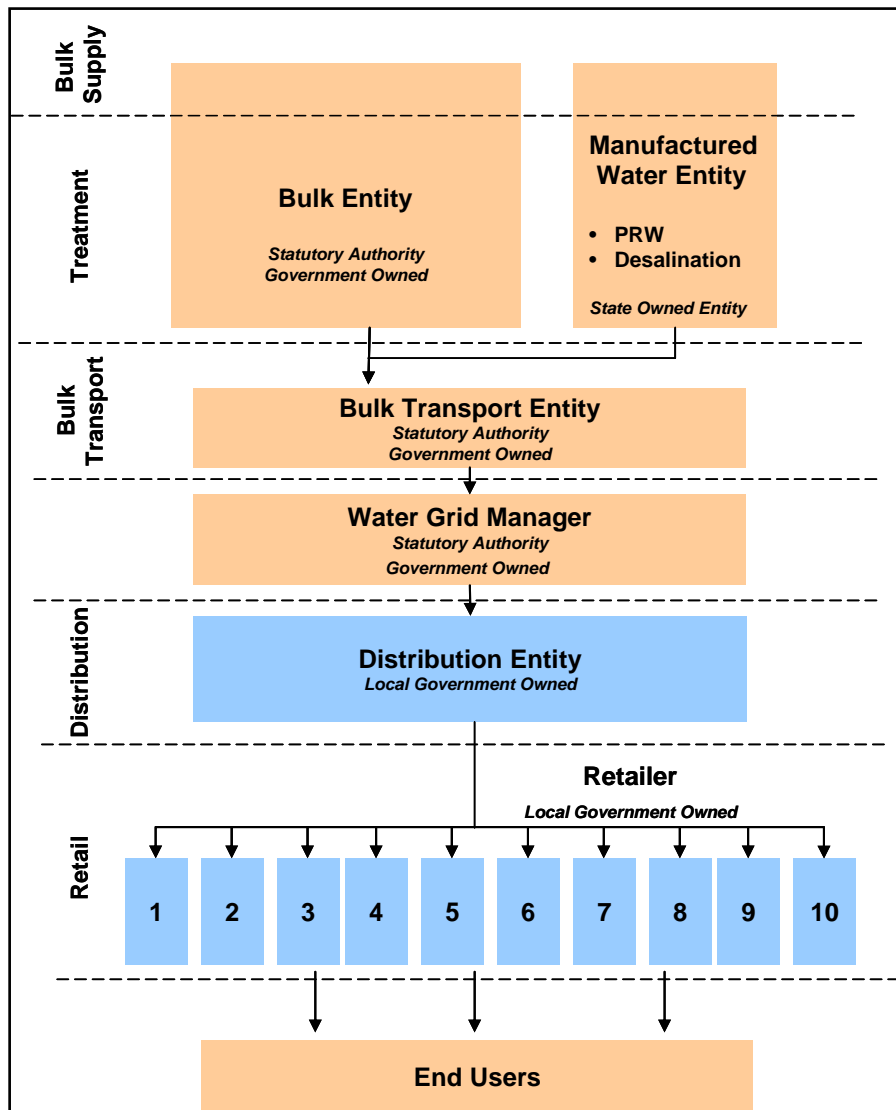
Below is an outline of the major initiatives being investigated, considered, or already undertaken within the states of Queensland, Tasmania, Victoria and Western Australia.

QUEENSLAND

In May 2007, the Queensland Water Commission (QWC) released a report relating to institutional arrangements titled *Our Water: Urban Water Supply Arrangements in South East Queensland*. Following this in September 2007, the Queensland Government announced the final model for the institutional reform of water supply arrangements.

The key features of these reforms are highlighted in the diagram below and include:

- The amalgamation of dams, water treatment plants and wastewater treatment plants from the current 22 owners to the establishment of just one bulk supply entity;
- A new manufactured water entity that will be responsible for desalination and recycled water;
- A bulk transport business is to be created which will own all the major pipelines and their associated reservoirs;
- A Water Grid Manager whose role is to purchase services from the bulk supply entities and bulk transport business and sell water to retailers and power stations;
- A single distribution entity that will own all water reticulation and service pipes, meters and sewerage pipes; and
- Between 3-10 retail entities to supply water and wastewater services to end-users.



Source: Based on QWC Urban Supply Arrangements Report (May 2007)

Under the new proposed structure, entities will undertake service provision roles on a regional rather than local basis. The establishment of these new entities will also mean a change in ownership function and arrangements. The State Government will be the owner and operator of the Bulk Water, Bulk Transport and Water Grid Manager functions; and the 9 Councils will jointly own and operate the Distribution and Retail functions.

The new structure is unique in the Australian water industry and has separated each element of the value chain to increase transparency. The framework will also enable third party users to access the network components and may introduce retail competition, subject to a cost/benefit analysis.

Regulatory arrangements will be altered to support the reforms with the development of Regulatory Codes to control the market and asset management. The QWC will initially be in control of the market regulation and will continue to take a long term planning role. The Environmental Protection Agency will continue to license wastewater discharge while the Queensland Health Authority will remain responsible for the regulation of drinking water quality.

Overall, the consolidation of water entities currently in place in South East Queensland intends to ensure clarity around the operation and maintenance of the industry. The proposed structure also foresees long-term planning benefits in relation to water security, service standards, improved customer service, greater control over equitable water pricing, and improved supplier and product options, amongst other advantages.

To read the QWC Urban Supply Arrangements Report (May 2007) see <http://www.qwc.qld.gov.au/Urban+water+supply+arrangements>

TASMANIA

Tasmania covers just one per cent of Australia's land mass, yet has about 14 per cent of Australia's water resource. However, an assessment carried out in 2005 by Engineers Australia found the State to have the worst water and wastewater infrastructure in the entire country, in relation to quality and cost effective water and wastewater services.

In order to achieve sustainable communities and maximise economic development opportunities, a Ministerial Water and Sewerage Taskforce was established in September 2006 to undertake a wide ranging review of the entire sector. This review has an overriding objective to improve their water and sewerage infrastructure with the view of meeting the fast-growing economic progress of the State's other systems and indeed the Nation.

The Taskforce's objectives include:

- Ensuring the long-term sustainability of Tasmania's water resources;
- Improving the quality of water and sewerage services;
- Improving the current water and sewerage infrastructure and planning systems;
- Ensuring economic growth and development in relation to water and sewerage services; and
- Improvement and efficiency of pricing signals.

The Taskforce has already identified that Tasmania's water and sewerage sector is not operating sustainably, and in response has already developed a number of options to be considered in relation to legislative and structural reforms of the system. Many of these options are based around successful operations already being undertaken in other states.

The issues that have been presently identified include:

- Reviewing the structure of the industry to optimise the economics of scale and scope;
- The creation of long term asset management plans;
- The need for a stronger link between economic pricing and other technical regulatory elements (such as environmental, public health, asset management and service standards);
- The need for the regulation of service standards between service providers and customers; and
- The development of independent economic regulation for urban water and sewerage provision.

SAHA have prepared a series of position papers on the Future Regulation of the Tasmanian Water and Sewerage Sector. These papers outline the proposed changes to be made to the regulatory framework currently existing in the Tasmanian water sector.

The proposed changes discussed in the paper include the:

- Specification of regulatory objectives and principles;
- Formalisation and separation of roles and responsibilities in relation to policy development and regulatory roles;
- Review of the long term water demand and supply planning framework;
- Introduction of mandatory asset management planning arrangements;
- Establishment of customer service standard setting framework
- Independent regulation of pricing;
- Establishment of an Ombudsman whose role is to address disputes and complaints; and
- Introduction of a public performance monitoring arrangement to increase accountability.

For more information or to download a copy of the report see

<http://www.treasury.tas.gov.au/domino/df/df.nsf/v-water/3F8B6C67E00092E5CA2573A3000E1C2B>.

VICTORIA

Inquiry into Metropolitan Retail Water Sector

The current structuring of Victoria's water sector has allowed for 'competition by comparison' (of the three retailer companies), which in turn encourages the competitor's responsiveness to customers and continual improvement of business services, including water quality and value-for-money supply.

The Victorian Government announced in mid 2007 that the Victorian Competition and Efficiency Commission (VCEC) will undertake a review to assess the metropolitan retail water sector to *identify and evaluate all available options to improve the efficiency, operation and performance of the water sector, including through reforming the structure and/or reducing costs of the sector.*¹

The VCEC have been asked to make recommendations in regards to the:

- Best possible structure that will allow for efficient and the least cost provision of Melbourne's water supply upgrades;
- Reducing costs of the metropolitan sector while improving the level of service in terms of providing safe, reliable and sustainable water and sewerage services; and
- Any related improvements to the governance of the industry, whilst keeping at the forefront the Government's Water Plan and climate change issues.

A finalised report will be released to Government by the end of February 2008, with an interim report to be released in mid December 2007. For further information on this review, please see

http://www.vcec.vic.gov.au/domino/web_notes/vcec/vcecweb.nsf.

Water Tariff Structure Review

The Victorian Government in September 2007 directed the Essential Service Commission (ESC) to conduct an inquiry into tariff structures for the Victorian water sector. The ESC in December 2007 released its draft report and the main conclusions of the review are summarised below:

- Increasing the volumetric component of water charges – the ESC considers that prices in the order of \$1-\$2 per kilolitre are appropriate and proposed charges of \$4 to \$6 per kilolitre for high consumption use are considered to be excessive and not cost reflective;
- Inclining Block Tariffs – pricing based on long run marginal costs (LRMC) is preferred however pricing above LRMC may be supported if benefits associated with balancing demand and supply and capturing externalities can be demonstrated;
- Charging based on meter size – only to be approved if customer impacts can be managed;

¹ Victorian Competition and Efficiency Commission, *Issues Paper – Inquiry into reform of the metropolitan retail water sector*, August 2007

- Connection based charges – setting fixed charges based on per household rather than per title is unlikely to be approved by the ESC unless customer impacts can be addressed;
- Combining water and wastewater charges as a method of simplifying the calculation – supported in principle by the ESC however any premiums would need to closely reflect the actual variable costs of treating sewerage;
- Price paths – ESC is seeking greater justification for significant price increases in the first year of the regulatory period including how customer impacts will be managed;
- Trade waste – the ESC supports differential trade waste charging that represents alternate plant's marginal costs;
- Increasing the share of costs borne by non-residential customers – the ESC is unlikely to approve this without cost-based justification; and
- New customer contributions – the ESC will be consulting further on this matter.

The draft report released by the ESC can be reviewed at <http://www.esc.vic.gov.au/public/Water/Consultations/Water+tariff+structure+review/Water+tariff+structure+review.htm>

WESTERN AUSTRALIA

The main issue that has been highlighted in Western Australia is that of introducing competition into the non-natural monopoly segments of the supply chain (i.e. water and wastewater retailing, water procurement and wastewater treatment and disposal).

Such competitive pressures could lead to new and improved methods of operating and lower prices for customers. In order to initiate action in this area, in July 2007 the Treasurer of Western Australia requested that the Economic Regulation Authority (the Authority) undertake an inquiry into competition in the water and wastewater services sector. Key areas of focus for this inquiry include:

- Introducing greater efficiency in developing and delivering new water sources and other services requiring significant capital investment. This will include looking at issues associated with current market structures and mechanisms to increase competition, diversity and innovation;
- Opportunities for enhanced competition including through the introduction of third party access to existing water and wastewater related infrastructure; and
- Other reforms to the water and wastewater market which may enhance competition, including issues associated with establishing water trading mechanisms, and arrangements for community service obligations paid by the State Government to service providers.²

The Authority released their draft report on 3 December 2007 with the following recommendations:

- Establishment of an Independent Procurement Entity with the responsibility for ensuring least expected cost of balancing supply and demand while maintaining supply security of bulk water;
- Investigations should be made into potential considerable alternative bulk water sources;
- Adjustment of pricing arrangements should be made to allow for water trading; and
- Effective water trading regime should be facilitated with all significant users within a catchment being considered when developing Statutory Water Management Plans and water allocations; and
- The Authority are looking to further consider the potential for anti-competitive behaviour.

In relation to third party access, the Authority has recommended that a State-based third party access regimes be implemented based on the principles of the Competition Policy Agreement. Under this regime, further consideration should be given to prices based on a 'retail minus avoidable cost' approach. The Authority recommends that retail contestability should be introduced for large customers, and for small customers this should be considered on a case-by-case basis.

The effect of the Authority's recommendations are to increase competition by developing opportunities for private enterprise to supply both water and wastewater services and so thereby improving outcomes for customers.

The draft report released by the ERA can be reviewed at http://www.era.wa.gov.au/2/508/46/inquiry_into_co.pm

² http://www.era.wa.gov.au/2/508/46/inquiry_into_co.pm

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