WSAA Submission

to the

Commonwealth Productivity Commission

Review of the

Regulation Impact Statement

National Competition Policy Arrangements

Introduction

The Water Services Association of Australia (WSAA) welcomes this opportunity to comment on the Review of National Competition Policy Arrangements.

WSAA, established in 1995, currently has 28 members and 25 associate members from across Australia and New Zealand that provide water services to more than 15 million urban based customers, including many of Australia's largest industrial and commercial businesses.

WSAA provides a forum to discuss issues of importance to the urban water industry and, where appropriate, is a focal point for communicating the industry's views. In this context WSAA has a major interest in a review of the National Competition Arrangements.

The Productivity Commission lists[1] the key elements of the National Competition Policy (NCP) package as:

- extending the anti-competitive provisions in the Trade Practices Act 1974 to government owned enterprises,
- separating regulatory from commercial functions,
- requiring government owned service providers to operate on similar commercial terms as the private sector (e.g. paying dividends and tax equivalent payments),
- establishing independent authorities to set, administer or oversee prices for monopoly services, and
- introducing third party access regimes for significant infrastructure.

Impact of NCP

The key elements of NCP for the urban water industry have all been implemented. The Trade Practices Act 1974 now extends to the urban water industry. The Act's coverage is in addition to the States' own legislative and regulatory oversight. To date, however, there has been no action taken against any urban water service provider under this Act.

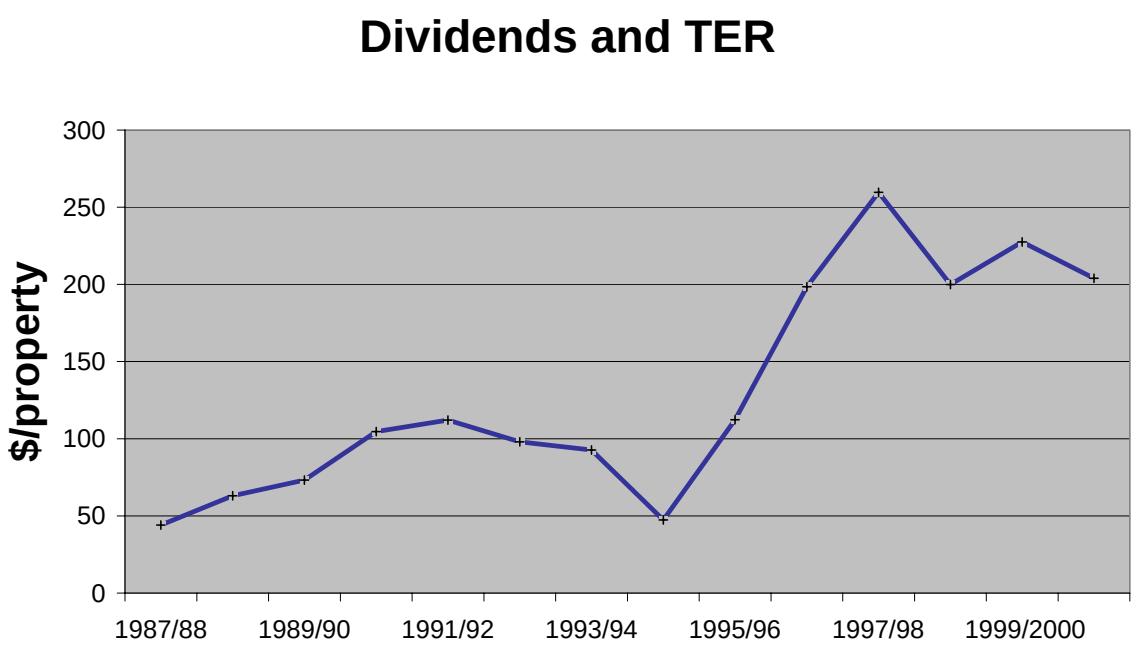
Similarly, the separation of regulatory from commercial functions has also been fully implemented. The regulatory functions (e.g. public health, environmental, customer service and price oversight) have been retained by government while the service provider has been

[1] Productivity Commission 2004, *Review of National Policy Arrangements*, Issues Paper, pg 2

given a commercial focus. The institutional models adopted for urban water service providers differ widely between and within different States. Some service providers have been corporatised, some have been established as authorities while others have been set up as separate divisions of local government.

The structure of the urban water service provider also varies significantly across Australia. Some service providers are vertically integrated (e.g. Hunter Water) while others have been established as wholesalers (e.g. Melbourne Water) and retailers (e.g. City West Water). The functional scope of wholesaler versus retailer also varies in different jurisdictions. For example drinking water treatment in Melbourne is the responsibility of the wholesaler, Melbourne Water, whereas in Sydney this function rests with the retailer, Sydney Water.

Metropolitan water service providers have complied with the NCP requirement to pay dividends and to make tax equivalent payments to their shareholders. The chart below illustrates the increase in such payments on a per property basis in real terms (2000/01 dollars). The amount shown is the national average for Brisbane, Sydney, Newcastle, Melbourne, Adelaide and Perth between 1987/88 and 2000/01. The chart below clearly shows a marked increase in the amount of real dividend and tax equivalent payments (on a per property basis) made to governments since the introduction of NCP. Indeed in 2002/03 the Australian urban water service providers paid in excess of $1 billion in dividends to their government shareholders[2].



It should also be stressed that the number of properties serviced in Australian cities has increased significantly during the same period. Accordingly, the actual increase in real

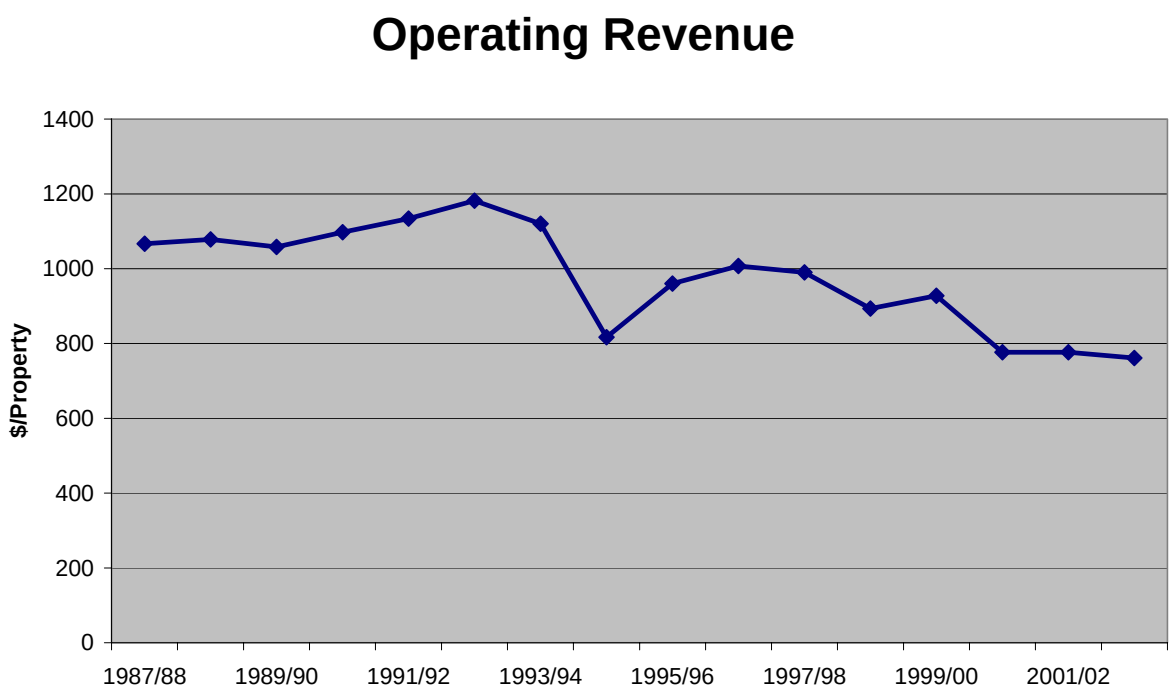
[2] WSAAfacts 2003.

dividend and tax equivalent payments has been even greater than that depicted in the above chart.

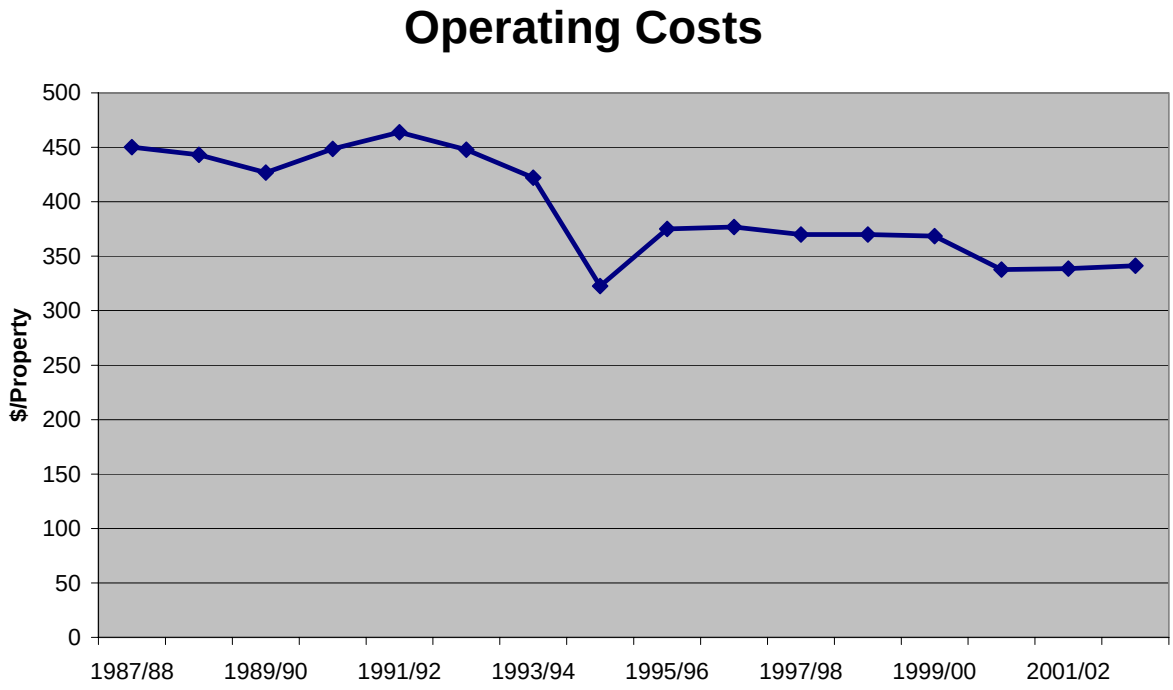
As noted above, the Commission also identifies the establishment of independent authorities to set, administer or oversees prices for services remaining under monopoly control as a key element of NCP. In actual fact the Water Resource Policy of the COAG agreement[3] stated that water "[P]rices will be set by the nominated jurisdictional regulators (or equivalent) who, in examining full cost recovery as an input to price determinations, should have regard to …". The amended agreement notes that "[T]he reference to *or equivalent* … is included to take account of those jurisdictions where there is no nominated jurisdictional regulator for water pricing". Accordingly, a careful reading of the NCP indicates that the establishment of independent price regulators was not required but rather that price determination/oversight was to be undertaken either by an independent price regulator or by government.

Nevertheless, independent price regulators for urban water have been established in all State and Territory jurisdictions with the exception of South Australia (where the State Government currently determines urban water prices). Again, the economic regulation models established in different jurisdictions vary.

The performance of the urban water industry in terms of real (in 2002/03 dollars) revenue per property and real operating costs per property for the period from 1987/88 to 2002/03 can be seen from the two charts below.



[3] As amended by the ARMCANZ meeting in Hobart in 1998.



Again, both charts suggest that the real average revenue and operating costs per property have decreased significantly since the introduction of NCP for urban water.

The last key element of NCP of relevance to the urban water industry identified by the Commission refers to third party access for infrastructure services. By extending the coverage of the Trade Practices Act 1974 to include the urban water industry, part IIIA of the Act allows for applications from third parties to declare such services as infrastructure of national significance and, accordingly, to enable third parties to seek access to these services.

The current application by Services Sydney to the NCC for a declaration of the Sydney Water sewage transmission and interconnection services is the first such application under Commonwealth provisions. However, it should be emphasised that there are already other third party access arrangements in place. For example in South East Queensland, Logan Water and Ipswich Water[4] purchase bulk water from SEQW through negotiated third party access treatment and transmission arrangements with Brisbane Water.

The only outstanding issue associated with the previous negotiated NCP reform package for urban water relates to the inclusion of externalities in water pricing. This omission is not due to negligence, or unwillingness to act, on the part of the industry but, rather, to the uncertainties surrounding the identification and valuation of the environmental externalities associated with the urban water cycle. The NCC has effectively acknowledged as much by not penalising State and Territory governments through the withdrawal of any competition payments for failure to deliver on this front. Nonetheless, WSAA is aware of the importance of this issue and the outcome of this work will hopefully provide sufficient information for a workable framework on externalities to be developed.

[4] Other local governments in the area also have similar third party access arrangements with Brisbane Water.

Further Reform

The current drought across the country and the uncertainties about water yield impacts from climate change are focussing the next stage of water reform on improving water entitlement security, improving trading systems, formalising environmental water entitlements and, specifically for the urban sector water, conservation and reuse[5].

In relation to the urban sector, while the public media commonly report Australian households are among the highest water users in the world, this is misleading. Australian cities have typically developed on the "quarter acre block", with low population densities and significant garden areas. Many would argue this a desirable trait of Australian cities. In this context in comparison to European countries and developed Asian countries, external water for gardens comprises between 30 to 60% of total domestic water use depending on the city.

Despite this, an analysis of comparable cities in the United States with similar climate, household block sizes and demographics, shows that Australian cities use *one half* of the water these US cities use.[6] Despite a hotter climate, Australian indoor water use is similar to UK household water use[7].

Therefore the Australian urban water industry can rightly justify a proud track record in the area of water conservation. Some examples are detailed below.

Australia has been at the forefront in respect of developing a nationally consistent water efficiency labelling scheme for water appliances and equipment. WSAA administers the scheme on behalf of its Members. This currently voluntary national scheme is unique in the world and, by the end of calendar year 2005, will be overtaken by a mandatory scheme run by the Commonwealth government. Australia was also the first country in the world to mandate the introduction of the dual flush toilet to reduce water consumption (a new model with lower flushing volumes will be introduced shortly).

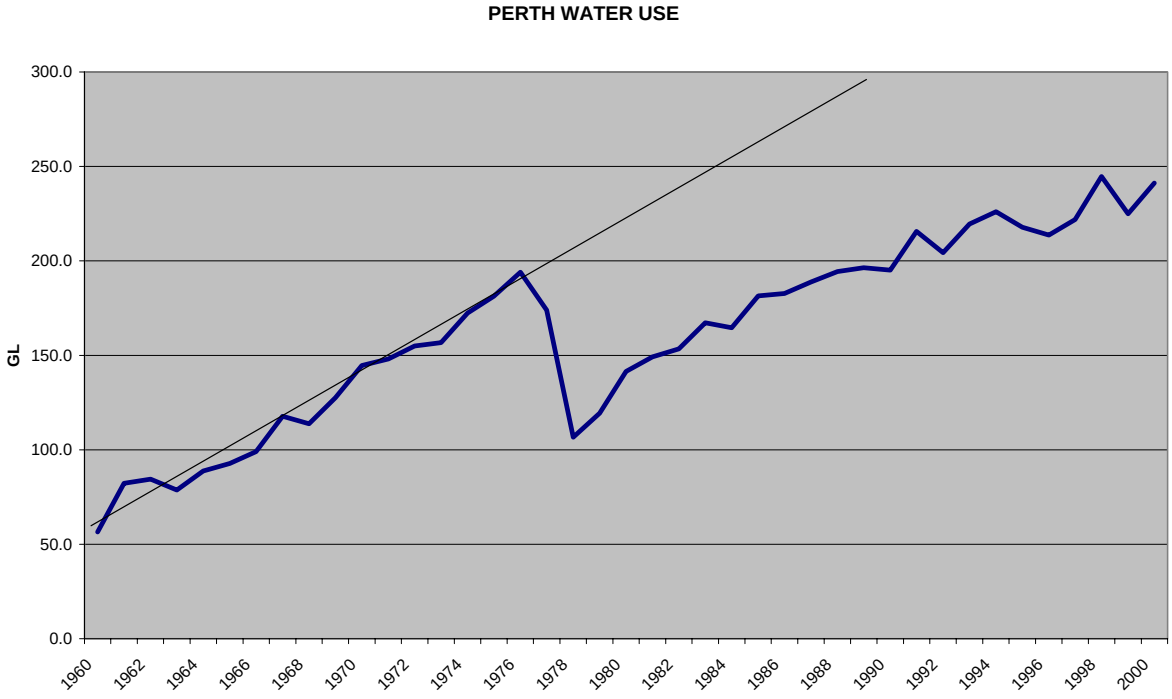
Australian water utilities are highly regarded for their efforts to educate the urban community about responsible water use and there are numerous examples of such public campaigns and educational programs. The extreme variability of rainfall in Australia has repeatedly led to the imposition of water restrictions and the need for new publicity campaigns to educate Australian households regarding their water consumption.

Experimentation with recycled water using third pipe systems in locations such as Rouse Hill in Sydney and the combination of third pipe systems and stormwater resuse at the Sydney Olympic Park development are other developments that demonstrate the urban water industry's desire to innovate in the area of water conservation. These developments use a "whole of water cycle" context and are virtually unique in the world. Further developments are underway in most States. Some of these are targeting 80% or greater reduction in potable water demand, radically changing the utilisation of this scarce resource. WSAA expects these type of developments to accelerate once the technical, pricing and institutional issues they raise are fully addressed.

---

[5] COAG Communiqué, September 2003
[6] See appendix one – Comparison of domestic water use in Australia and comparable US states.
[7] OFWAT 2002 – See Appendix 2

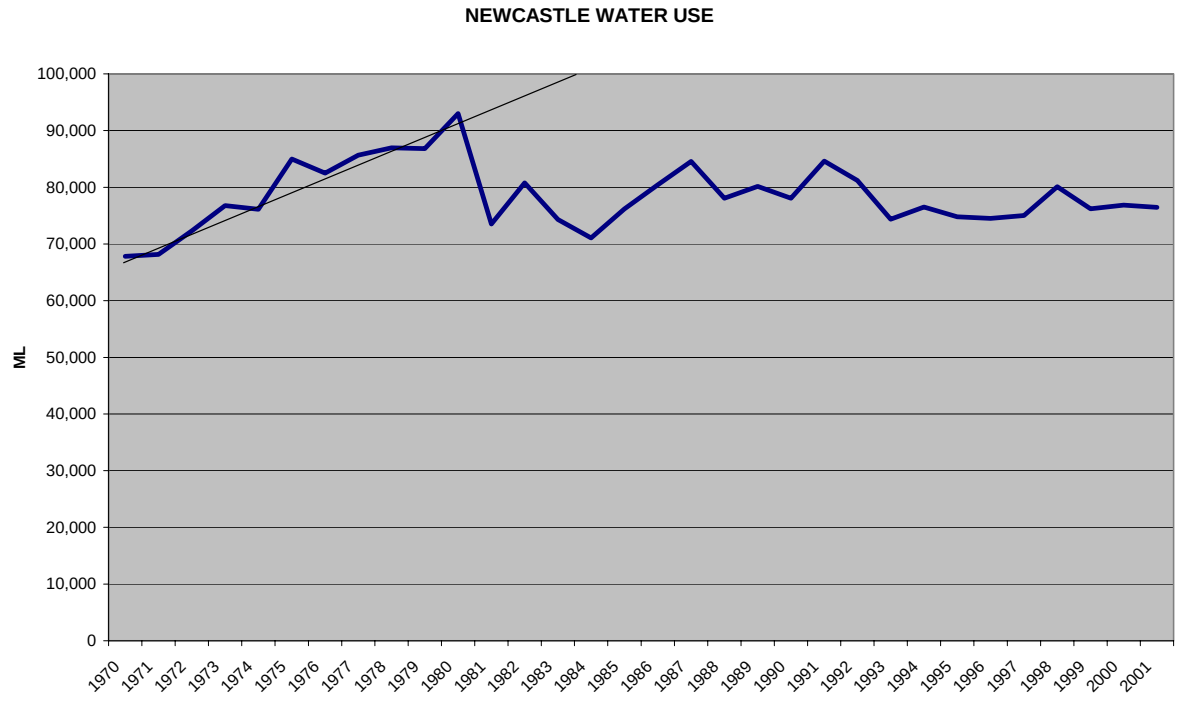
Last, but certainly not least, it is important to recognise that no other country in the world has been able to universally apply usage based pricing in its cities[8]. Starting with Perth in 1978 and progressively spreading to the Eastern cities, universal usage based pricing had a marked impact on water consumption upon its introduction. The chart below shows the marked decrease in total water usage in Perth in the late 1970s. While water consumption increased again in the years following the introduction of usage based pricing, consumption never returned to its previous trend.



The same pattern of substantial reduction in water consumption was repeated in other Australian cities when usage based pricing was introduced. For example, the chart below shows water consumption for the city of Newcastle. Usage based pricing was introduced by Hunter Water in 1982[9].

[8] Hobart is the only exception due to the absence of residential meters.

[9] In Brisbane, the last Australian capital city to introduce usage based pricing, residential water consumption per property decreased by 23% between 1997/98 and 2002/03 (WSAAfacts 2003).



While it would be simplistic to expect pricing to bear the entire burden of managing water conservation[10], the urban water industry is nor resting on its laurels. The Sydney and Melbourne water service providers together with WSAA have recently completed a major research project on customer preferences for alternative pricing structures to promote water conservation. The Sydney and Melbourne water service providers are currently using the output of that research to better understand their customers and to develop pricing strategies required by their respective regulators.

The Association is also undertaking a project to develop pricing guidelines for recycled water. To date the focus of pioneering projects utilising recycled water has been to reduce the impacts of the discharge of treated effluent on receiving waters. However, as pressure on our water resources increases, recycled water is increasingly being used as a substitute resource for non potable purposes. This trend raises substantial technical problems and institutional issues with which the industry and regulators are still coming terms. As the use of recycled water becomes increasingly mainstream, the industry needs to focus on the commercial aspects of this product to ensure the most appropriate use of this increasingly valuable resource.

In addition, while third party access applications are the exception rather than the rule at the moment, it should be noted that widespread use of these arrangements is not consistent with the existing postage stamp pricing arrangements. This issue may require a watching brief by the industry and its regulators.

[10] Residential demand for water is very inelastic.

Conclusion

In summary, WSAA notes that the Australian urban water industry has successfully implemented the COAG reform agenda established in the 1990s and, by reducing its costs, has delivered lower prices to its customers as well as significantly higher contributions, through higher dividends and tax equivalent payments, to its shareholder governments.

The Association has also noted COAG's intention to focus the next wave of urban water reforms on water conservation. In this regard, the Australian urban water industry already has a proud track record and will continue to work to apply itself to deliver improved performance in water use.

Appendix 1

WSAA WATER CONSUMPTION FACT SHEET*

City	Population (000s)	Volume Supplied (ML)		L/head/day		Residential Properties	kL/Property	
		Total	Residential	Total	Residential		Total	Residential
Adelaide	1,052	180,760	108,112	471	282	415,000	393	255
Brisbane	835	165,931	106,568	546	351	317,000	463	319
Canberra	325	61,607	34,901	522	295	118,000	497	311
Darwin	96	37,484	14,682	1,078	421	31,000	1,307	618
Melbourne	3,456	496,110	282,861	393	224	1,207,000	373	234
Perth	1,375	235,389	161,344	469	322	497,000	420	323
Sydney	3,923	597,519	324,777	417	227	1,406,000	391	243
Hobart*	47	11,185	322	657	492	19593	509	395
			Average	**440**	**256**			**260**

*Residential consumption figures for Hobart are based on the Mt Nelson suburb only

WATER CONSUMPTION IN COMPARATIVE US STATES[6]

City	Population (000s)	Volume Supplied (ML)		L/head/day	
		Total	Residential	Total	Residential
Arizona	3,920	1,115,012	726,761	780	507
California	30,500	7,765,015	5,126,015	700	462
Florida	12,200	2,860,068	1,740,911	640	390
Hawaii	1,120	295,679	180,999	723	443
Nevada	1,290	646,624	422,793	1,230	806
New Mexico	1,380	429,701	259,755	852	515
Texas	17,600	4,545,712	3,385,104	712	530
			Average	**805**	**522**

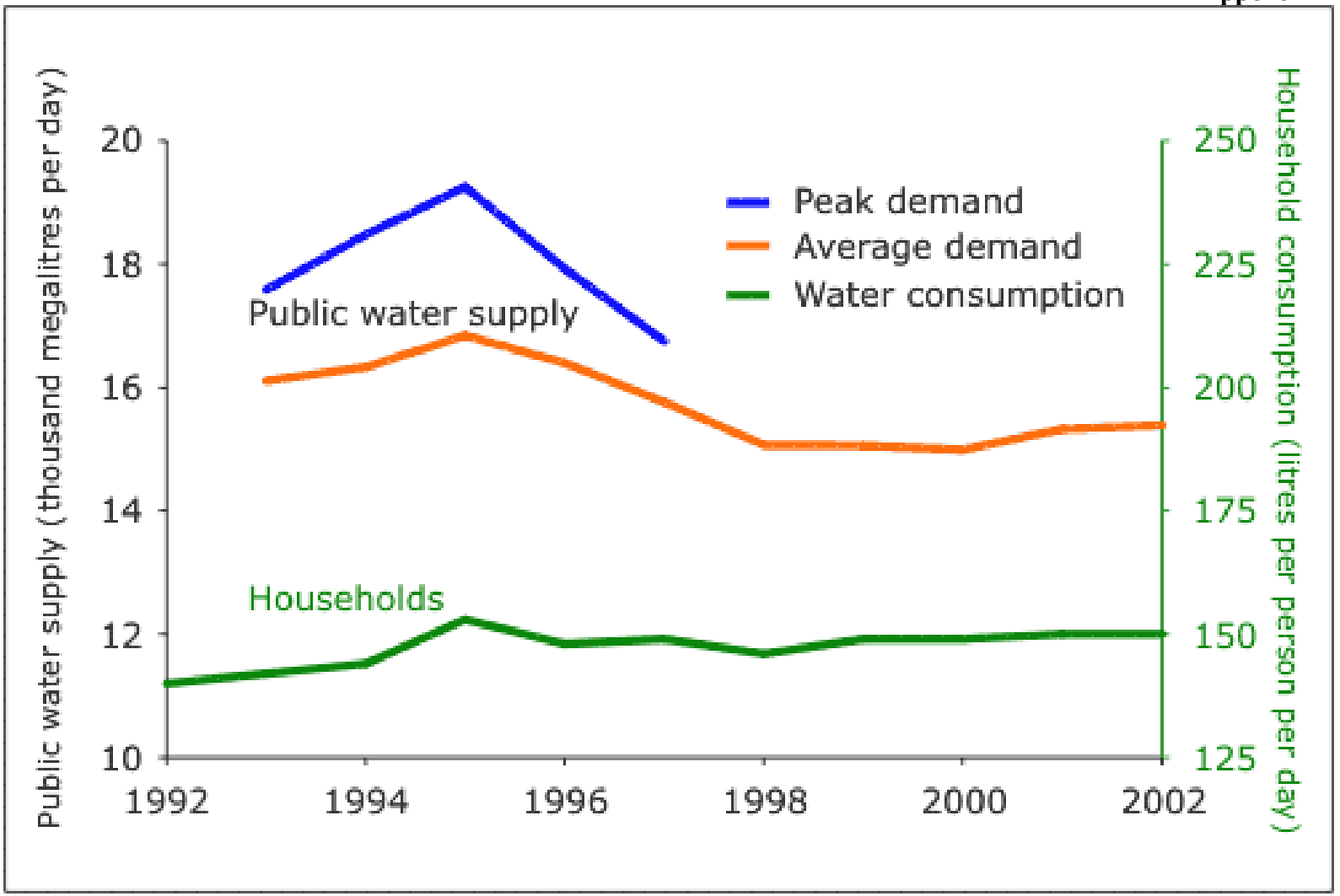
Average Australian per head residential use is half (256L/head/day cf 522 Litres/head/day) comparative United States use.

Sources/Notes:

* WSAA*facts* 2001 (Averaged data 1995/1996 to 2000/2001)

1. Indoor consumption figures derived from CSIRO Perth Domestic Water Use Study, 1999
2. Outdoor consumption is subject to climatic conditions and varies nationally
3. United States Geological Survey - Public and Domestic 1995. (http://water.usgs.gov/watuse/). 2000 Survey Data under preparation.

Appendix 2



Household Consumption and Demand in the UK – OFWAT 2002