



Kempsey Shire Council

Submission

Inquiry into Secure & Sustainable Urban Water Supply & Sewerage Services For Non-Metropolitan NSW

29 April 2008

TERMS OF REFERENCE

OBJECTIVE

- To identify the most effective institutional, regulatory and governance arrangements for the long term provision of water supply and sewerage services in country NSW; and
- Ensure these arrangements are cost-effective, financially viable, sustainable, optimise whole-of-community outcomes, and achieve integrated water cycle management.

THE TASK

The State's 107 local water utilities are facing growing challenges, posed by drought, climate change, environmental water allocations, demographic shifts, technological advances and skill shortages.

In view of the challenges facing the utilities, the Inquiry is to identify the most appropriate institutional and regulatory arrangements for the water supply and sewerage industry in NSW in order to ensure that services are efficient, reliable, affordable and safe.

In particular, the Inquiry should identify arrangements that will enable customers of water utilities in regional NSW to benefit from a secure water supply, professionalism, cost effective service standards and regulatory safeguards in the provision of water supply and sewerage services.

As a minimum, the Government expects water supply and sewerage service providers to:

- respond and plan in advance to the challenges facing the industry;
- be financially self sufficient;
- be able to comply with appropriate stringent environmental and public health standards; and
- implement cost-effective service standards.

In considering the merits of any new industry arrangements, the Inquiry should take into account:

- the historical structure of the industry and its performance record to-date;
- the current and future challenges facing the industry;
- the present capacity of the industry to address those challenges;
- alternative industry arrangements used in other States;
- the impact of any changes on the financial sustainability of Councils;
- the socio-economic impacts on the community, including indigenous communities, of any new institutional and regulatory arrangements;
- the relative performance of other States and their experience with industry reform;
- the institutional and regulatory options available, including the relative merits and drawbacks of each; and
- the role Local, State and Federal Governments should play in further improving services.

The Inquiry is to focus on the provision of urban water supply and sewerage in rural and regional NSW. Sydney Water, Hunter Water, Gosford City Council Water Supply Authority and Wyong Shire Council Water Supply Authority are excluded from the Inquiry.

Submission – Kempsey Shire Council

Organisation Name: Kempsey Shire Council

Submission authorised by: Kempsey Shire Council

Executive Summary of Submission (300 words or less please)¹

Kempsey Shire Council supports the need for a review of water utilities across NSW. Whilst Kempsey Shire is currently among the top fifteen water utilities in the State and meets all Best Practice Guidelines it does recognize that the challenges and issues facing the water industry across the State require expert focused entities to make and implement the necessary changes.

This submission is based on a high level assessment of the water industry and proposes a model that will best meet the long term challenges faced by the water industry, enhance the opportunities for those who work in the industry and best serve the residents of our region into the future.

This submission proposes a model that would entail the establishment of a new regional corporatised water utility with the transfer of assets, staff and operations from current water utilities to the new corporation. Existing local authorities would take a shareholding in the new utility based upon the value of the business they transfer...

Governance of the new corporation would be by a commercially focused professional board with membership based upon expertise and experience. The Board would be selected by ballot by the shareholding local authorities with appointment made by the Governor. Dividends and tax equivalents would be distributed back to the shareholders based upon their shareholding.

This submission proposes that appropriate transitional arrangements are put in place to minimize the impact of these changes on existing water utility and local authority employees. Transitional arrangements are also required for local authorities to make the necessary adjustments to their operations following the changes.

It is also proposed that the new water corporation have a community service obligation to contribute to integrated water cycle management through catchment, estuary, stormwater and flood programs.

Special transitional grant funding arrangements are also recommended to allow the new corporation to address an expected backlog of asset replacement/renewals programmes and staffing transitional implications.

¹ Please provide a concise summary of the key issues or arguments provided in your submission.

1. Challenges / Issues

1a) What are the major water and sewerage management issues in your region?

Kempsey Shire Council is a general purpose council located on the Mid North Coast. The Council has an annual budget of approximately \$70m and a staff of approximately 300. Macleay Water is the water and sewer business unit of Kempsey Shire Council and has an annual operating revenue of approximately \$13m with a staff of approximately 50.

The major water and sewerage management issues in the region are:

- Sustainable outcomes for water cycle management into the future, in particular improving the environmental outcomes of water utilities to date and managing well the concurrent social and financial implications.
- Implementation of IWCM across the whole water cycle including the catchment
- Implementation of sustainable effluent re-use schemes including dual reticulation.
- The next long term water augmentation strategy and the likely significant impacts of climate change.
- Financial sustainability in the light of reducing consumption driven by user charges and the impact of reduced income through BASIX and dual reticulation initiatives in growth areas.
- Financial risk posed due to the DWE portions of pricing component targets within DWE Best Practice Guidelines. Access-charge: usage-charge percentage targets pose poor income levels in wet years leading to operational and capital expenditure implications.
- Capital cash flow management where contributions for growth related infrastructure are received only when the growth occurs whereas the infrastructure is required prior to development. This situation is exacerbated by the lead time required for design, approval and construction of infrastructure.
- The escalating cost of major water & sewer infrastructure projects due to national and international demand for skills and resources.
- Asset management is an issue for all public asset providers in identifying and providing an appropriate level of asset replacement funding.
- Conflicting regulatory approaches to reclaimed water use.
- Attracting suitably qualified and experienced technical and professional staff.
- Impractical, illogical, inflexible portions of some Best Practice Guidelines creating customer division due to perceived inequity of implementation.
- Assurance of water quality to customers, in particular management of algae on off-stream storages (Dams) and intermittent heavy metal river contamination, without the construction of modern water treatment plants at significant capital and ongoing operational costs.

1b) How does your local water utility currently plan to manage future challenges such as drought, climate change, environmental water allocations, demographic shifts, technological advances and skill shortages (or other issues you have identified)?

Drought

Drought security of the Kempsey Shire's seven water supply schemes has been addressed through the Macleay Water Drought Management Plan. This Plan consolidates strategies to provide an integrated framework for the responsible implementation and monitoring of initiatives to achieve the specified water supply objectives during conditions of drought.

In particular, Kempsey Shire's largest water supply scheme, the Kempsey Water Supply Scheme is drought-secure via the -

- Steuart McIntyre Dam Off-Stream water storage provision
- 30-year water supply capital works infrastructure provision
- Management of water extractions and supplies at critical times (including restrictions)
- Regular monitoring of extraction sources on the grounds of both capacity and quality

The Kempsey Shire Water Supply Scheme has emergency supply capabilities beyond the designed drought security provisions via emergency bores and alternative supply routes.

Long term future interconnections with the South West Rocks, Hat Head and Crescent Head water supply schemes have been scoped with various short to medium term components being included within the capital works programme. The implementation of actions within the Drought Management Plan would enable such work to occur when needed.

The concurrent development of risk-based management plans for the smaller village water supply schemes adds to the water supply security of the Kempsey Shire's water supply schemes.

Climate Change

Macleay Water is currently preparing for the commencement of the first review of our IWCMS. We are currently cooperatively working with the BOM, and monitoring CSIOR predictions, DECC planning guidelines and the water sharing plan developments for the Macleay River and coastal sands. Appropriate data will be included within the review of the IWCMS.

Environmental Water allocations

Council is currently very aware of the riparian flow requirements and subject license constraints/limits imposed on the Macleay River and constantly work within these. River level monitoring consistently occurs and is regularly communicated to customers through Council's monthly Water Happynings page in the Kempsey Shire's Happynings paper (features the local TV guide).

In addition, Council is actively involved in the water sharing plan developments for both the Macleay River and the Coastal Sands aquifers.

To this end, a partnering of Council and other technical investigatory groups were successful in obtaining a national heritage grant to further the understanding of the coastal sands aquifer.

Sustainable Water Cycle Management

Kempsey Shire Council places a high priority on triple bottom line management of its various functions, placing emphasis on obtaining a good balanced outcome for its community. This emphasis was clearly shown in the stakeholder consultation process with the Integrated Water Cycle Strategy and this direction has been confirmed with the recent community development of their community strategic plan. A cultural shift has occurred within Council to achieve such outcomes and this is evident in the management of the water utility.

With this mantle, demand management has been a focus. Macleay Water has developed a Demand Management Strategy that is already delivering very good water consumption outcomes, before the implementation of higher consumption pricing, and without a result bias of water restriction implementation. The Macleay Water Demand Management Plan is allied with other major directional strategies, including the award winning IWCMS, and fundamental for achieving sustainable water consumption levels. The addition of gradual price indicators will only achieve better outcomes.

A recent example of this cultural shift was the South Kempsey petrochemical incident. Despite the opportunity for Macleay water to permit a flow of petrochemical spill through the Sewage Treatment Plant, and directly in the sensitive receiving environment downstream, major efforts were made to contain the spill at the Plant. With the assistance of NSW Fire Brigade the petrochemical containment was addressed and then recovery of the biological sewage process occurred.

Maintenance of this culture is challenging and not as affordable as traditional management, and is particularly challenging in the current climate skill shortages and capital/operational cost increases. However such a culture needs to be maintained to achieve sustainable outcomes for the community into the future.

IWCMS

Council was part of the initial pilot programme to develop the IWCMS and its strategies. The implementation of IWCMS across 7 water supply and 7 sewerage schemes was definitely a challenge. Effectively the hard work rewarded Kempsey Shire Council by significantly lifting it ahead of many utilities in terms of strategic integrated planning of its infrastructure and business. This achievement was recognised with the Green Globe award in 2005.

Since then, this integrated strategic approach has rewarded Council. A dual reticulation opportunity has now been realised as a water recycling scheme that reduces the pressure upon precious water resources in a growing coastal town, and improves the quality and quantity of effluent disposed. The sustainable effluent reuse is a key factor within the implementation of the IWCMS. Shire-wide market research has occurred with a focus on replacing where possible the use of potable supplies. Many exciting future projects have been developed, limited only by the need to spread capital funds to manage the Macleay Water business responsibly within financial constraints.

Management of a major river catchment spanning multiple local government areas and with developments regulated by various state government agencies has proved difficult. The reluctance of various state government agencies to recognise the implications of upper catchment management on water and land quality downstream has been disappointing. Efforts to resolve, or at least open discussions have been considerably time consuming with minimal resulting outcomes to date. Council will continue the interagency negotiations to endeavour to obtain sustainable water cycle outcomes for the Kempsey Shire.

Many other cooperative prospects due to Council's integrated strategic approach within and external to the Kempsey Shire have also eventuated both as investigation into aquifer function and partnering. Partnering with DNR for the placement of aquifer monitoring bores and curriculum-outcome based water education with the NSW Department of Education are examples of great cooperative win-win outcomes for the agencies and the community.

Implementation of the 30-year capital works programme successfully continues and the first review of this fundamental document has begun. Incorporation of emerging information, particularly with regards climate change is a focus of this review.

Financial Sustainability

Financial sustainability in the light of reducing consumption driven by user charges, and the impact of reduced income, though BASIX, and dual reticulation initiatives in growth areas are becoming an increasing challenge.

The reducing income likely as a result of pricing indicators is difficult to balance with social implications within the Kempsey Shire, due to the disproportionate socio-economic nature of the community. Customer tank water management is an opportunity being developed to partly address new business opportunities arising as a result of BASIX. However the immediate concern of capital infrastructure affordability without considerable pricing changes is a major challenge.

Capital Cash Flow and Financial Risk

The implications of capital cash flow and financial risk are managed within Council by delaying delivery. There is staggered or delayed capital project delivery to ensure good financial management of the available resources. There is delayed delivery of full compliance with Best Practice Guidelines, particularly pricing ratio targets, to minimise financial risk to Council and introduce gradually pricing changes. Within Kempsey Shire, the achievement of sustainable outcomes for the community has taken priority over ticks in a box for immediate compliance with Best Practice Guidelines. The intentions of the Guidelines are being worked towards and often the outcomes are being achieved before the compliance is actually achieved.

Project Cost Escalation

The escalating cost of major water & sewer infrastructure projects due to national and international demand for skills and resources has meant that some capital projects have had to be deferred or reprogrammed.

The level of escalation also has caused a shortfall in developer contributions due to the five year review cycle for development servicing plans.

Best Practice Guidelines

This matter is discussed in detail in question 7.

Water Quality Assurance

Council has faced major challenges with water quality assurance derived from aspects beyond Council's control. These include algae management and intermittent heavy metal contamination.

Algae management in Dams has been an issue across the mid north coast and continues to defy the indicators for escalation. Whilst significant further knowledge capture is required (years) to better understand the characteristics of each Dam and the various algal species, water treatment plants are ultimately required. It is acknowledged that water treatment plants at this point would treat the symptom and not the cause. However lack of available water resources for use is a risk posed to the community as is the significant capital cost. This challenge has been unresolved at present and work continues on both addressing the financial planning for such a capital cost, as well as collectively working on obtaining better knowledge of the algal characteristics.

Similarly, the treatment of the symptom for intermittent heavy metal contamination is the only current solution, as the continued cost of water carting to remote villages is not sustainable and the cause of contamination will take years to address. Again the financial planning for such capital costs and longer term operational costs are progressively being addressed.

Technological Advances and Skill Shortages

Kempsey Shire Council with a staff of approximately 50 currently operates 7 water supply schemes, 7 sewerage schemes and shortly a water recycling (under construction) scheme. Macleay Water includes water/sewer process, construction, maintenance, technicians (trades) and management staff.

Challenges with regards skill shortages and technological advances are further discussed in Question 6 a) & b). In summary, in the current climate Kempsey Shire Council has had to be innovative and flexible in its approach to obtaining and retaining the skills required to operate and manage its water utility's infrastructure. Whilst innovative approaches ultimately achieve objectives, such objectives could be achieved more quickly and with less effort if technical human resources were more readily available.

Council has received several recent awards for its innovative integrated water management work. Some of the more recent major awards are listed below. Some of the practical onground innovations are being considered for Engineering Excellence awards in the upcoming month.

- 2007 National Awards for Local Government - Commendation - Community Water Grants Water Savings
- 2006 NSW Sustainable Water Challenge - Greenfield development
- 2005 Green Globe Award - Integrated Water Cycle Management

2. Governance Arrangements for Local Water Utilities in NSW

2a) What do you or your organisation believe the most effective institutional, regulatory and governance arrangements for the long term provision of water supply and sewerage services in country NSW are/would be, and why?²

Institutional

The single most critical issue affecting the long term sustainability of water utilities is financial sustainability. Whilst governance and regulatory impediments may frustrate and delay advances, without an adequate source of funds, real change and advancement will be illusory.

Financial sustainability of water utilities, in this region will only be achieved through the establishment of a commercially focussed water corporation which is able to provide the necessary professional and technical staff to meet the challenges. This corporation would be governed by appropriately skilled and experienced expert Board.

The Board would be required to comply with Australian Corporations Law. Directors of the Board are bound by the Corporations Law to act in the best interests of the corporation at all times. Any intervention by Government would only be via their normal regulatory roles.

Council's would receive compensation for the transfer of utilities by receiving shares in the new corporation equal in value to the value of the business they are transferring. A detailed financial model will be required to value the businesses they are transferring. Adjustment to the transfer value would need to be made based upon the levels of debt or reserves transferred.

Council's would transfer both debt and reserve funds to the new corporation equal to the value currently held on their water and sewer accounts.

A nominal shareholding would be allocated to any Council transferring a utility with a zero or negative net worth in their transferred business for voting purposes.

Dividend and tax equivalent payments to Councils would be based upon the number of shares they hold. This will ensure that revenue generated by the regional water utility stays within the region.

In addressing the issue of an appropriate size for the proposed corporations and their financial capacity, Minister Rees' comments at Taree on 30 January were considered. Minister Rees stated that the first two of six essential elements of a future water utility model were: 1. Operating financial sustainability; and, 2. Capital sustainability.

This poses the question, What scale of organisation is financially sustainable on an operating and capital basis? To answer this question we have looked at those water utilities not included in the current review.

Firstly, Sydney Water, operating revenue 06/07 \$1.68bn, operating result \$335m, net assets \$7.2bn. Secondly, Hunter Water, operating revenue 06/07 \$257m, operating result \$89m, net assets 1.34bn. And finally, the proposed Central Coast Water Corporation (aggregation of Gosford & Wyong Water Utilities), operating revenue 06/07 \$98m, operating result \$8.8m with net assets of \$1.7bn.

² You may provide your answer in reference you a specific geographical region only if desired.

An assumption was therefore made that a utility in the order of magnitude similar to the proposed Central Coast Corporation would have the capacity to meet the Minister's criteria.

The next issue in terms of determining future water utilities areas again came from the Minister in his address at Taree. Points 3 & 4 of his essential six part criteria were: 3. Utilities must be able to attract and retain appropriate professional and technical staff; and, 4. Must protect and enhance the employment of existing water industry employees.

The region is a lifestyle region with excellent health, sporting, leisure, primary, secondary, technical and university education facilities. Housing is affordable, the region is conveniently located mid way between Sydney and Brisbane and is an employment area of choice.

In terms of protecting and enhancing existing employment, it is our view, that existing operational staff numbers are unlikely to be affected by this review. Should this not be the case transitional employment provisions should be made to protect affected employees for up to three years.

Larger utilities will offer the benefits of providing greater opportunities for training, career paths and progression. In addition these utilities will create a significant number of new jobs in regional areas at the technical and professional level.

The aggregations arrived at and presented as part of this submission are based upon a combination of meeting the first four criteria required by the Minister and catchment boundaries, historical regional groupings and areas of common interest also played a part.

A corporation for the Mid North Coast could comprise nine existing utilities. The area extends from Gloucester/Great lakes to Grafton. This area had an operating revenue for 06/07 of \$170m an operating result of \$60m and net assets of \$2 billion.

It is believed that a corporation of this scale would have the appropriate balance sheet, profit & loss and cash-flow strength to enable access to debt funding to the level required to support the required investment and to fund all business activities on a sustainable basis. Being classed as an infrastructure corporation the risk profile will be lower thereby giving access to more competitive borrowing rates.

This corporation model could be adapted to other areas in the State.

It is proposed that the corporation be a vertically integrated business providing extraction, storage, distribution and retail water and sewerage services.

It is proposed that bulk water together with management of rivers, streams and major storages remain with the State Water.

Regulatory

The proposed change will require new regulations stipulating the establishment, governance, taxation arrangements, customer protection, pricing controls and transitional arrangements.

A total review of the existing regulatory environment is warranted. Under the existing regulatory regime there is inconsistency between the Local Government Act, Environment Planning & Assessment Act, Water Act and other legislation.

Quite clearly it is beyond expectation that all regulation relating to water utilities be administered by a single statutory authority. What is expected is that all legislation and guidelines are consistent in delivering Government policy and its application.

At the present time local water utilities are faced with dealing with the Department of Local Government, Department of Water & Energy, Department of Planning, Department of Environment & Climate Change, Department of Primary Industry and Department of Health. Often to achieve endorsement or approval across all these regulators a less than optimum outcome is achieved.

Consideration needs to be given to creating some sort of hierarchy or lead agency approach to the regulation of the water utility industry.

In terms of separation of powers, the proposal that the utility corporation be owned by the local government entities from which they are derived, provides a clear separation between the utility and the State authorities which regulates it.

One major benefit for the State Government with this proposal is that the regulatory effort by State Government Departments should be reduced in dealing with less water utilities.

Governance

Assets and staff from existing water utilities would be transferred to the new corporation. Each Council contributing assets to the new corporation will receive a shareholding in the new corporation based upon the value of the business they transfer. Dividend and tax equivalents will be distributed back to the owning Councils based upon the value of the business each contributed to the new corporation.

It is proposed that the corporation would be governed by a commercially focussed professional board. Potential board members will be nominated based upon their professional expertise and experience. Boards will be appointed by the Governor following a ballot process involving the owning Councils. A seven member Board including a Chairman is proposed. No more than two Councillors from owning Councils can be elected to the Board. Councillors who are nominated must also meet the professional expertise criteria required for Board membership.

It is proposed to operate the Board on a commercial basis, together with a standard charter and a mandatory code of conduct. The provisions of the standard charter and code of conduct need to be considered in the regulatory changes proposed.

The Board needs to meet certain community service obligations (CSO's) in relation to contributions to catchment management, integrated water cycle management and water sensitive urban design.

Transitional arrangements are required to ensure the Board and senior management of the proposed corporation are selected from the best available nominees or applicants.

2b) How would you or your organisation's preferred model assist to better manage the challenges identified in Question 1a to ensure that services are efficient, reliable, affordable and safe? *[In your response, please provide concrete examples of alternate arrangements that would assist local water utilities to manage future challenges]*

The corporatised model will be better able to address the identified challenges in the following ways:

IWCM

It is proposed that community service obligations (CSO's) be imposed on the corporation to contribute to catchment management, flooding, stormwater and estuary management all of which form part of an integrated water cycle. Additionally, the new corporation will be better resourced with specialist environmental, engineering and technical staff to identify and address IWCM issues.

Sustainable effluent reuse schemes

Better use and reuse of available water resources will increasingly become a more critical issue for water utilities. Environmentally and technologically advanced reuse treatment plants and schemes are becoming more complex for both approval and operational requirements. A larger water corporation will be able to provide the necessary specialist staff and financial resources to carry these schemes to fruition and achieve the maximum benefit available.

Water augmentation strategy

The recent drought has shown this to be an area where a number of existing water utilities have particularly failed their communities. The reasons for this are manifold however, parochialism, indecision, lack of expertise, lack of planning and funding would figure prominently.

The recommended model of a corporatised water utility with a professional board and professional management focussed upon water management will overcome all of these issues.

Financial sustainability

A large corporatised water utility would have both a revenue and capital funding base from which to address the financial challenges ahead. This coupled with professional financial management expertise will allow for long term financial modelling to be developed and sustainable revenue and expenditure programs to be developed.

The opportunity to investigate and consider more public private partnership (PPP) or other innovative funding and project delivery options will be better suited to the future capability of the proposed larger corporatised water utility.

Capital cash flow management

A larger better resourced water corporation would be better able to manage the large scale capital projects required to meet the future needs within the area. Financial planning and project management expertise will be better able to address this problem. Projects that would represent a huge expenditure for the current small scale utilities will become just part of a much larger capital program.

Escalating cost of major water & sewer infrastructure projects

This is one issue over which a larger corporate utility will have little control. However through appropriate financial and project planning, delays in implementing projects will be avoided thereby reducing exposure to this risk.

A larger corporate utility would also have greater buying power in the market which will see projects implemented at more cost competitive levels.

Asset management

A larger corporate water utility would have the necessary technical staff to develop and implement the required asset management plans. The corporation will also have far greater financial capability to meet appropriate asset maintenance and renewal programs.

Regulation of reclaimed water use

This is an issue that needs to be addressed as part of the regulatory reform undertaken to implement the structural changes to the water industry recommended by this submission.

Attracting suitably qualified and experienced technical and professional staff

This is one of the major premises stipulated by the Minister. A regional corporation on the Mid North Coast with its lifestyle and high service provision will provide the necessary attraction for staff to want to live and work in this regional area.

For generation X & Y individuals, the opportunity to work in a large corporate entity in a lifestyle location in regional NSW, will be a significant attraction. More and more people in this demographic are looking to move from metropolitan areas but need professional career opportunities to do so.

3. Financial Sustainability

3a) What are the current impediments to financial sustainability and self-sufficiency for local water utilities?

Most water utilities in NSW are managed by general purpose Councils whose major focus is on issues other than water and sewer. This situation often leads to water and sewer issues only receiving secondary consideration.

This situation is exacerbated in smaller Councils where management and technical staff also share general purpose roles. In these situations the level of focus on water issues is often minimal due to external pressures, rather than the needs of the water utility operation.

Many local water utilities pricing decisions for water services are influenced by political and parity considerations and not necessarily the long term financial needs of the utility. For example, developer contributions are kept low to encourage development or to appease pressure from the development lobby or water and sewer increases are kept in line with rate pegging limits rather than being based upon long term financial modelling or service level considerations.

3b) How would your/your organisations preferred model/s assist to remove the impediments to financial sustainability and self-sufficiency for local water utilities?

There are a number of elements that will allow a corporatised model to provide for financial sustainability and self sufficiency.

Firstly the proposed corporation will have a single focus professional board with appropriate qualifications and expertise which will lead to better decision making. The corporation proposed will be of a sufficient size to employ appropriately skilled financial and technical staff to undertake the required strategic and operation financial modelling upon which decisions can be made.

Secondly, it is proposed that pricing oversight be undertaken by IPART on a 3 - 5 year review basis which will bring a level of rigour to financial sustainability and pricing decisions whilst at the same time protecting consumers from overpricing.

Restructuring of water utilities will provide for a level of soft competition between the corporations in relation to pricing and financial performance.

3c) What are the current impediments to local water utilities offering cost-effective service standards?

Many local utilities, due to their size, are unable to provide the necessary expertise or capital required to achieve optimum cost effective service standards.

Through limitations on budgets and failure to provide adequate replacements and renewals, many schemes have outdated technology and rundown assets. As a result system failures and service interruptions are higher.

On a simple economies of scale basis, smaller water and sewerage schemes suffer on a unit cost basis due the relatively small number of customers they serve.

Due to environmental, regulatory and market factors water supply and sewerage scheme capital costs have escalated to such an extent that they are unaffordable for many water utilities without significant external assistance.

3d) How would your preferred model/s improve the ability of local water utilities to offer cost-effective service standards?

A larger corporate utility as proposed is able to attract the necessary financial and technical skills to address the complex issues revolving around asset management, financial planning and project implementation.

A larger entity will be able to spread corporate and other fixed costs over a much larger customer base and thereby reduce their impact on customers.

A large corporate water utility will offer the ability to spread the benefits and costs of major capital schemes across a much larger customer base with much lower per capita capital and future operating costs.

4. Integrated Water Cycle Management (IWCM)

4a) What are the most effective institutional, regulatory and governance arrangements to ensure all local water utilities achieve integrated water cycle management now and in the future?

Institutional

It is proposed that community service obligations (CSO's) be imposed on the corporate utility to contribute to catchment management, flooding, stormwater and estuary management all of which form part of an integrated water cycle.

Additionally, the new corporation will be better resourced financially and have specialist environmental, engineering and technical staff to identify and address IWCM issues. IWCM targets could also be applied to the corporation, ie KPI's and include compliance with Best Management Practice Guidelines.

Regulatory

The regulatory arrangements will need to obligate water utilities and local councils to consult and work together to achieve coordinated servicing of development and the provision of water and sewerage services that meet community expectations eg reclaimed water.

The most effective means to achieve this is through legislation that governs the core activities of both water utilities and local councils.

Any new model for the delivery of water services needs to consider the link between water & sewerage and stormwater. The current system whereby local councils manage all infrastructures has many benefits from an integrated water cycle management perspective. The removal of water & sewerage operations from councils will impair these benefits and suitable arrangement to ensure effective management will be necessary.

Currently IWCM is primarily driven through the DWE Best Practice Guidelines. There is no mandatory requirement to meet the Guidelines, however they do offer the "incentive" of dividends and/or eligibility for grants. For the corporatised approach being recommended, some form of regulation is required to support this initiative.

The EP&A Act through the BASIX SEPP provides some incentives and obligations for certain developments to meet criteria in the SEPP. Some provisions of the SEPP have been found to be limiting factors when attempts have been made to implement Water Sensitive Urban Design (WSUD).

The provisions in the Local Government Act (LGA) in relation to water restrictions in time of drought have limited Council's ability to impose community accepted water conservation measures at other times to reduce demand. Similar conflicts arise when dealing the Department of Health on reclaimed water issues, best practice guidelines and LGA rating provisions.

A total review is required of the legislation and guidelines covering water utilities to ensure there is a consistency of approach across all legislation.

Conflicts have also arisen with the DWE in relation to Section 60 approvals under the Water Act where community engagement has led to schemes with high environmental outcomes and the DWE driven by "least cost" complying option mentality.

It is recommended that a total review of regulatory arrangements affecting water utilities be undertaken.

Governance

It is proposed that the new water utility have CSO's in relation to IWCM and in particular catchment, flooding, stormwater & estuary management. In this regard consideration needs to be given to a mechanism that would allow the shareholders (local Councils) to raise issues with the Board to undertake non-commercial activities aimed at improving water cycle management and natural resource management in the region.

It is Kempsey Shire Council's view that urban consumers of water and sewerage services should contribute to the maintenance and improvement to those elements of the water cycle upon which these services rely. This contribution should be included within water services billing, perhaps as an IWCM levy.

Consideration could also be given to a legislated percentage of any surplus or dividend being devoted to IWCM activities. These proposals will require some further analysis and financial modelling to determine appropriate levels and sustainability.

5. Environmental & Health Standards
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5a) What issues are you aware of in terms of local water utilities ability to adhere to environmental and public health standards? How would your preferred model address these issues?

Environmental and public health standards have led to a significant increase in the capital and operating costs of water utilities.

For many proposals, the environmental assessment alone is significant, which coupled with the time involved means a considerable escalation in costs. It is not unusual for the investigation and approval time frame for major undertakings to extend 5-10 years.

Community expectation in relation to protection of the environment has also increased significantly over a number of years. This expectation has led to increased costs in a number of areas to achieve those outcomes.

Smaller utilities will be increasingly finding it difficult to address and meet these changing standards and expectations. In many instances these utilities lack the technical skills and the financial resources to meet this challenge.

A large corporate utility as proposed will have the capacity to attract and retain the necessary technical skills and have the financial resources to implement the required programs to meet this challenge.

6. Skills & Staff

6a) How many staff in your council are employed for both water/sewerage services, and general services? [i.e. their role is split between water/sewerage and general fund duties such as an engineer whose responsibilities are for water/sewerage and roads] Please also provide the percentage split for each ie 50% water/sewerage and 50% roads.

All of Council's water and sewerage employees are engaged fully on water and sewerage works. There are however a number of corporate support areas such as IT, GIS, payroll, accounts, workshop & depots and general finance functions which would need to be downsized with the loss of water and sewer operations.

In general terms water and sewerage represents approximately 29% of Council's total operating income, whilst water utility staff represent approximately 20% of total staff.

It is estimated that the following equivalent General Fund staff are engaged by Macleay Water:

Function	No of Staff
Fleet Management	1.5
Computer Services	1.5
Corporate Buildings	0.2
Customer First	0.5
Financial Services	3.0
Organisational Effectiveness	0.2
Purchasing	1.2
Sustainable Development	0.6
Shire Services Management	1.0
Human Resources	1.0
Public Relations	0.1
Total	10.8

Fractions of staff would be unable to be transferred which will be a burden on General Fund. It should also be recognised that General Fund will also bear the loss of office and depot rentals unless continuing arrangements can be made. If these costs are borne by General Fund the Department of Local Government needs to be receptive to Special Rate Variation applications.

It is recommended that existing non-direct water utility staff affected by any restructuring be afforded the opportunity to move to any new utility under the transitional arrangements.

6b) What skills shortages have been identified in your local water utility (for now and in the future)?

Macleay Water has first hand experience of the skills shortages within the water industry and the retention of those staff. Those experiences have included professional specialist staff, higher level contract management staff, professional/technical process staff and trades. Alternative means to fill those roles have occurred to avoid long term deferment of projects and address risk exposure. Affordability of such staff remains of concern.

Outsourcing professional specialist roles have met with mixed success as the private consulting sector is experiencing similar skill shortages. Several major projects were

deferred and/or restructured as major consulting firms identified that they were unable to soundly provide the expertise required.

Partnering and secondments with larger water utilities has provided some relief. These alternative methods remain resource hungry to manage and have been identified as adequate for specific projects but not sustainable for the normal multi-faceted technical and professional roles.

'Labour hire' of trades persons was worthwhile for short periods. It was found that non water industry experienced trades persons, particularly fitters and electricians, required transitional learning curves to enable full utilisation for the expenditure.

Analysis of the future staffing requirements identified major shortfalls in staff capabilities and a significant loss of expertise due to retirement over the next 5-10 years. Capabilities to operate higher technology treatment plants are required as a result of the increasing quality and quantity demand for potable water, recycled/reclaimed water and effluent returns to the environment. Treatment Plant operators must be practical, computer literate and comfortable with the various dosing equipment and laboratory testing regimes. A significant transition of water process staff from dosing plant capabilities to SCADA controlled treatment plants was identified. The identified aged workforce that exists particularly within sewage process was identified as a mentoring opportunity yet difficultly to fill when occurring in a short timeframe.

An inability to 'buy-in' expertise meant Macleay Water became innovative and began to 'grow our own expertise'. Macleay Water restructured along functional lines to facilitate the 'grow our own' process. Whilst again resource hungry on management and existing technical staff, it has been apparent that specific staff are capable of such succession and the short term buy-in of expertise for mentoring and training is more affordable and practical. Significant inroads have occurred in the transition of process staff for SCADA controlled treatment plants. The retention of potential retirees as mentors under flexible work arrangements is being considered. Macleay Water has established -

- a trainee in water process and will shortly supplement this with a sewage process trainee
- a trades apprentice role that cycles between the various trades upon completion of the indenture
- work and project experience for Kempsey's Unisys cadet engineers in various stages of University engineering studies
- 10 staff in TAFE Cert II training, various staff involved in mentored Cert IV Management training, various staff involved in Cert IV industry specific training
- a mentored training programme to address skill deficits in water/sewer process

6c) Do you have difficulty attracting and retaining experienced technical staff?

See 6b) above.

7. Regulation

7a) What is and isn't working with the current regulatory framework for local water utilities in NSW? [Eg Best Practice Management Guidelines, Local Government Act 1993, role of NSW Government]

The Local Government Act governs water & sewerage accounting and billing arrangements. With the introduction of IWCM by the then DLWC in 2004 it was proposed that local utilities would be able to establish a single fund and a single "water services" account for customers.

Unfortunately no agreement could be reached between the DLWC and DLG on this issue and as a result there has been no progress on this issue since then.

It is also apparent that the regulatory environment applying to metropolitan areas varies from that applying to water utilities in regional NSW. This particularly appears to be the case in relation to reclaimed water use and regulation of STP discharges. A prime example would be the non-acceptance of bubble EPA licences available to Sydney Water but not available to regional utilities on a large river such as the Macleay.

Despite utilities following the Best Practice intentions of integrated water cycle management it is apparent that the state government departments are still struggling with this implementation. Section 60 approvals for integrated infrastructure are an example where until recently, approvals for Water Recycling Plants in conjunction with Sewage Treatment augmentations were fragmented and delayed. Macleay Water is thankful for recent endeavours to resolve this aspect.

The suite of Best Practice Documents whilst offering a beneficial consistent approach across the state do not offer implementation flexibility. This is Macleay Water's experience for both the Liquid Trade Waste Guidelines and the Water/Sewerage/ Liquid Trade Waste Pricing Guidelines.

Co-ordination of strategic planning for growth also works well in a general purpose Council environment. With the separation of water utilities, specific legislation will be required to ensure local Councils and water utilities co-ordinate planning for growth.

At the present time local water utilities are faced with dealing with the Department of Local Government, Department of Water & Energy, Department of Planning, Department of Environment & Climate Change, Department of Primary Industry and Department of Health. Often to achieve endorsement or approval across all these regulators a less than optimum outcome is achieved.

Consideration needs to be given to creating some sort of hierarchy or lead agency approach to the regulation of the water utility industry.

7b) What are the impacts of the current regulatory system on your Council/organisation?

Section 68 approvals & regulation

The delay and fractured response on s.60 approvals caused delayed movement of a \$17m project to tender process for the construction of the integrated Sewage Treatment plant augmentation and Water Recycling Plant. In the current period of escalating construction

prices, delays are costly. Timeframes for the delivery of this project have been set by DECC and extensions for third party delays are difficult to negotiate.

Technically complicated guideline compliance is difficult to communicate to both customers and Councillors. Apparent illogical inconsistencies have occurred with the Liquid Trade Waste Guidelines and the Water/Sewerage/ Liquid Trade Waste Pricing Guidelines that when implemented place Councils in a bad light. An example is the implementation of liquid trade waste excess mass charges, where a national company who is a considerable liquid trade waste customer pays less per kilolitre than a small restaurant owner. Another example is where stepped water pricing means that each unit in a multi-unit residential development obtains an equivalent water allocation of a residential house, negating the opportunity of pricing influenced water demand management and comparatively unfairly cost burdening the house owner.

7c) How would your preferred model improve on the current regulatory framework?

The establishment of a regional water corporation and the recommended review of the total regulatory environment should overcome many of the areas of conflict between the Local Government Act and other regulatory instruments under which water utilities operate.

A regional water corporation and its professional board would have more influence to negotiate flexibility into best practice guidelines.

Upon a decision being taken to restructure the water utility industry, a review of the legislation affecting the industry and including all stakeholders would be a priority to be undertaken.

8. Socio-Economic Impacts

8a) What would be the socio-economic impacts of your preferred model on the community, including indigenous communities?

Employment

Due to the hands on operation nature of water supply and sewerage schemes and the fact that they tend to be provided on locality-by-locality basis it is argued that there will be very little impact of the preferred model on operational staff levels. Over time there may be some rationalisation due to the introduction of technology and the aggregation of some schemes. It is recommended that transitional arrangements provide for transfer opportunities and job protection arrangements for an appropriate period, say 3 years, to allow for readjustments to be made.

In the smaller Councils where there are shared professional and technical roles there will be some rationalisation of roles for various positions. While this is unlikely to reduce numbers in these roles it will have a financial impact on these Council's General Funds. In this regard it is recommended that transitional arrangements provide for some level of industry adjustment funding for local Council's.

There will also be some employment impacts in the corporate support areas of existing Councils. Again it is recommended that transitional arrangements provide for transfer opportunities and job protection arrangements for an appropriate period, say 3 years, to allow for readjustments to be made.

It is expected that significant employment and career progression opportunities, with a greater investment in training and development will accrue from this proposed model.

Pricing

This submission recommends that pricing oversight of water utility services across NSW be undertaken by IPART. The prices justification process should provide for recognition and assessment of socio-economic impacts across the State and in particular any vulnerable groups such as indigenous communities.

Transitional arrangements should also provide for the maintenance of nodal pricing with a stipulated phase out period to minimise socio-economic impacts on any affected community.

The establishment of a corporation will see the establishment of a new organisation with its own infrastructure. Unless this infrastructure can be paid for by Government subsidy and increased operational efficiencies, increased water and sewerage charges could result. As mentioned in Question 6 if the shareholding councils General Funds are adversely affected constituent councils rates could increase.

The transfer of Macleay Water staff and some General Fund staff would involve the transfer of employee leave entitlements to the new corporation. Those entitlements amount to \$1.3 million as at 30th June 2007. Council does not have a reserve of any substance so presumably a levy will need to be placed on customers during any transitional period or a liability transferred if government funding is not forthcoming.

Service Levels

Providing water security to communities in regional NSW has the potential to provide a positive socio-economic impact for communities. Based upon anecdotal evidence, the

security of water supply in any given area during the last drought became a significant factor in people's minds when making relocation changes.

Added to this is the fundamental principle that safe water and environmentally sustainable sewerage schemes underpin the socio-economic lifestyle expected in our society. The preferred model presented in this proposal will ensure this benefit is enjoyed by all water utility customers across NSW.

There will be times when customers will need to attend the regional headquarters which could involve additional travel. Currently customers who are undertaking development have a council one stop shop where planning, building, engineering and water and sewerage requirements can be addressed at the one location. Water and sewerage enquiries would not now be part of this process.

9. Other Comments on the Inquiry

9a) What other comments would you like to provide in relation to the Terms of Reference for the Inquiry?

Need for change

In the majority of cases across the State, Council water and sewerage activities are not individually of a size to meet the future challenges and large scale development required to address water and sewerage infrastructure needs. Ongoing ad-hoc funding from the State Government is not going to fix the long-term structural problems that face the industry address the looming liability associated with infrastructure asset renewals.

Sustainability of remaining general purpose Councils.

The ongoing financial viability of general purpose Council's currently providing water utility services needs to be considered and transitional arrangements put in place to allow sufficient time for Council's to make the necessary structural and financial adjustments.

In this regard options such as one-off extra-ordinary rate adjustments or industry re-adjustment grants may need to be considered.

Change in other States

A review has been undertaken of the structural changes made and being made in other States.

Whilst Queensland has adopted a corporatised approach with ownership being vested in Councils, the disaggregation of the businesses as adopted in Queensland is not supported in the NSW context. South east Queensland may have the economies of scale and customer base to fragment these businesses between, bulk supplies, reticulation and retail, such a model is unlikely to produce sustainable scale businesses across NSW.

Additionally it is argued that a direct customer focus is required due to the nature of the potential impacts from reticulation and infrastructure adjustments undertaken by water utilities. Infrastructure providers operating remotely from customers will lose an essential element of customer focus for any business.

The recently proposed Tasmanian model is similar to that proposed in this submission, however there is concern in relation to the scale of these businesses and their sustainability. The level of control over proposed Boards by the Treasurer as detailed in the draft legislation is of concern.

The Victorian structure, again based upon a corporatised model appears to be working well with appropriately scaled commercial entities. The two-tiered approach in Victoria is not warranted in NSW as it is proposed that bulk water management continues to be undertaken by the State Water.

10. Other Issues

10a) Are there any other issues related to water management you would like to comment on that are not part of the Terms of Reference?³

Timing

The changes to the water industry and local government incumbent in this submission are significant. Change also brings with it a level of uncertainty for all involved.

For this reason it is recommended that the changeover to any new regional water industry structure occur as quickly as possible rather than being implemented over an extended period of time. A long implementation timeframe has the potential to unnecessarily delay the implementation and planning of many essential infrastructure projects. In addition the personal impacts of a long implementation period could well see a significant loss of corporate, technical and operational knowledge from the industry.

On Site Sewerage Management

It is recommended that responsibility for on-site sewerage management be transferred to the regional water utilities as part of this proposal. Issues relating to on-site sewerage management need to be considered in the same light as other water utility issues.

³ Whilst issues such as water restrictions regimes and water trading are not directly the focus on the Inquiry, your comments are invited and may be used to inform other relevant NSW Government policy processes.