

**Productivity Commission
Australia's Urban Water Sector
Coliban Submission - Outline**

Productivity Commission Review

The Productivity Commission is conducting an Inquiry into "Australia's Urban Water Sector". The justification for the Inquiry is stated as being that:

In recent years there have been concerns about the performance of urban water systems in metropolitan and regional areas, related to the capacity of the sector to meet demand in light of challenges such as drought, climate change, population growth and water quality issues. A decrease of water stored in dams has led to prolonged use of water restrictions and increased investment in supply augmentation in many jurisdictions.¹

As a result, the Commission has been asked to *identify the opportunities for efficiency gains, which might be achieved through changes to structural, institutional, regulatory and other arrangements in the sector.*

The Commission intends to consult widely with stakeholders and has invited submissions from interested parties.

This paper provides a concise submission from Coliban Water for that Inquiry. It helps confirm Coliban Water's profile and reputation as a forward thinking player in the sector willing to embrace change, the opportunities it brings and focussed on delivering efficiency in processes and enhanced service for customers.

¹ Productivity Commission (2010), *Australia's Urban Water Sector, Issues Paper*, September, page 5.

1 Coliban Water

Coliban Water is a major Victorian regional water corporation centred on Bendigo. We provide water and wastewater services to 140,000 people, with 60,000 residential and 6,600 commercial properties supplied through our urban supply system. The service area includes 49 towns extending from Cohuna and Echuca in the north to Kyneton and Trentham in the south.

We welcome this Inquiry by the Commission as a valuable opportunity for the sector to take stock after a period of high stress due to the drought. We believe we have experience to contribute to the debate and we would be pleased to learn from initiatives progressed elsewhere.

2 Business Efficiency

Over the last decade, Coliban Water has exposed many of its functions to the discipline of the market by contracting out core services through a range of for for purposes approaches including Build, Own, Operate schemes. Customers have benefited as this approach has driven down costs and driven up standards of service by making outputs an explicit contractual obligation. Coliban Water welcomes insights on how to maintain this drive for business efficiency.

Coliban Water recommends the Productivity Commission investigate competitive reforms including ways in which authorities themselves can achieve, demonstrate and as appropriate benchmark productive efficiency.

3 Third Party Access

The Essential Services Commission in Victoria has recently published a paper on establishing a Third Party Access Regime.

Coliban Water welcomes the rigour and challenge that any Access Regime could provide. Any such mechanism would ensure that water authorities are meeting high standards in customer service at efficient costs.

The implementation of an Access Regime may lead to many benefits for Coliban Water, the broader industry and the community in general. Firstly, the implementation of cost reflective pricing will ensure customers are facing the true costs relating to their consumption decision rather than being under or overcharged. Secondly, any innovative schemes that may increase the number of customers being serviced by assets with fixed costs will necessarily lower customer bills by reducing the sum of fixed costs attributable to the current customer base.

Accordingly, it is likely that a correctly targeted Access Regime will produce benefits to both water authorities and their new and existing customers.

However, it needs to be recognised that there are cross-subsidies embedded in the current tariffs. Under the current “postage stamp” pricing, there is sharing of costs at a regional level with prices the same regardless of where in the network or region a customer is located. This serves the social policy objective of ensuring that water and sewerage services are available to small rural communities at a realistic price. While there are economic inefficiencies in retaining postage stamp pricing, it would be administratively complex (and hence expensive) and socially detrimental to abandon the current approach.

Strict implementation of Third Party Access, using a “Cost of Service” approach, could result in ‘Cherry Picking’ with the potential loss of high volume, low-cost customers. This could result in price increases for the remaining customer base and expose the lack of viability of some smaller supply systems.

Coliban Water believes that this risk argues for the adoption of the “Retail Minus” approach to any TPA agreement as this respects the real costs of supply involved.

Coliban Water recommends the Productivity Commission further investigate the benefits of Third Party Access.

4 Satisfying Demand

Coliban Water, like many authorities, has been subject to severe impacts of the drought. Customers have been exposed to significant restrictions over the last five years. As a result Coliban Water has implemented a suite of arrangements to mitigate this impact:

- Investment in alternative supply arrangements such as the Goldfields Pipeline to enable Coliban Water to access supplementary water supplies out of the Goulburn system.
- Use of recycled water to substitute for potable water where possible.
- Development of an innovative urban trading model to provide customers with the ability to offset risks from restrictions. Under this initiative, customers at high risk from restrictions contract to purchase water out of the Goulburn system with Coliban Water delivering that water to supplement the standard urban supply.

This initiative has provided customers with the ability to express their relative willingness to pay for different levels of supply security. Entities such as commercial car-washes and sporting clubs have been able to maintain important business and social services for the benefit of the wider community.

Coliban Water would support the extension of this approach to give customers the choice between a range of different products that better match their needs and aspirations. That would involve differentiating between:

- The baseline essential service that is available to all customers and is subject to tight external regulation; and
- Alternative, discretionary products that customers could choose to purchase above the baseline service. Many customers already exercise this choice at a high price through purchase of tankered water supplies or rainwater tanks.

It would be more economically efficient and provide a higher level of service for Coliban Water to offer and deliver this choice. Coliban Water has the advantage of having access to the raw water market and so the ability to match future demand by purchasing extra water to meet customers' expressed needs.

Coliban Water recommends the Commission examine measures that ensure water is always available for its highest value use through appropriate markets.

5 Optimising Supply Decisions

Coliban Water has access to a portfolio of different water resources to meet its supply obligations. These different resources have varying characteristics in terms of supply security and cost. Therefore, Coliban Water is currently developing an innovative optimisation model to help drive decision making that leads to the best outcome in terms of the choice as to which water storage to draw down at a specific time.

Implementation of an optimisation model will generate an explicit economic value of water in storage for each alternative supply to allow an optimal choice that balances the varying parameters of cost and security over time.

Associated with this, water trading has become an essential part of our business model, new skills and governance frameworks are required to manage new risks and opportunities with a potentially volatile commodity.

Coliban Water can see benefits in extending this model to a more commercial level by including potential access seekers and market signals. This approach could be

applied to an expanded water grid at a state or regional level helping different water authorities optimise resource access decisions.

The optimisation model will also allow Coliban Water to maximise available environmental flows and ecosystem outcomes within the decision process.

Coliban Water recommends the Commission further investigate the economic value functions associated with optimisation.

6 Conclusions

In summary, Coliban Water believes competitive reforms that offer the potential for enhanced efficiency should be vigorously pursued. These reforms, regardless of whether within the authority (competitive tendering or outsourcing) or outside the authority (Access Regimes), will help drive up service levels and drive down costs.

Coliban Water believes that the industry should focus on the provision of water to customers at the lowest possible cost. Restrictions, except in times of dire shortage, should be a thing of the past and authorities should critically examine their storages to optimise their supply to customers.