Australia's Urban Water Sector
Public Inquiry of the Productivity Commission

Submission of:	WATER UTILITIES SHARING GROUP INCORPORATING GWYDIR, MOREE PLAINS AND WALGETT SHIRES
Date:	16 May 2011

INTRODUCTION:

The Water Utilities Sharing Group (the "Group") is a resource sharing alliance that commits Gwydir Shire Council ("GSC"), Moree Plains Shire Council ("MPSC") and Walgett Shire Council ("WSC") to strive for the highest standards of delivery of water and sewerage services to their respective communities.

Enclosed is a copy of the Memorandum of Understanding executed by each member of the Group which, amongst other things, details the vision statement, objectives, membership and areas of resource collaboration of the Group.

This document comprises the response of the Group to the Productivity Commission inquiry into the case for microeconomic reform in Australia's urban water sector (the "Submission"). In particular, this Submission will address the Group's position in relation to the *"Draft recommendations, findings and information requests: Chapter 13 – Reform in regional areas"*.

DRAFT RECOMMENDATIONS, FINDINGS AND INFORMATION REQUESTS: CHAPTER 13 — REFORM IN REGIONAL AREAS

INFORMATION REQUEST
Is the economic real rate of return an appropriate measure to assess full cost recovery? Are there any risks in using this measure, especially in considering whether utilities are properly providing for returns on capital invested to date, and on future capital expenditure? Is there merit in adopting a measure, or at least a benchmark, that reflects full economic cost?

All members of the Group provide water and sewer services to diversely-sized demand centres, often in geographically disparate areas. For example, MPSC provides these services to the largest centre in the Moree Plains Shire (being Moree) as well as a number of smaller surrounding villages of varying sizes (for example, Mungindi and Garah).

As the local utility provider in each Shire, each member Council has a commitment to provide all residents within its Shire with these essential services, which may or may not result in a positive economic real rate of return.

The Group disputes that a critical element of urban water reform is founded in all water and wastewater utilities achieving full cost recovery; for some water utilities this may be utterly unfeasible, as to do so may necessitate passing on exorbitant costs to end-users. The Group considers it inappropriate to effectively penalise those end-users to enable the water utility to operate on a commercially viable basis, particularly when the fundamental tenement of local government is to serve the needs of the whole community. While we strive for an economic return for the whole of the operation, various centres are heavily subsidised by the main centre and therefore, the returns associated with water and wastewater services cannot be considered in isolation.

DRAFT FINDING 13.1
In many areas of regional Australia, water utilities recover their costs and are financially sound.

However, a significant number of regional water utilities are earning negative or very low real rates of return. It is not clear that these utilities are achieving genuine cost recovery (that is, recovering all costs – including asset maintenance and renewal costs – over the capital cycle). This could have

serious implications for water system infrastructure over the longer term, particularly if negative or low returns are sustained over a number of years.

The Group acknowledges that it may be appropriate for regional water utilities to aim to achieve a positive rate of return for these services. It is felt that this approach will incentivise regional water utilities to strive for greater efficiencies and encourage forward planning for this sector in their respective areas.

Equally however, the Group believes it would be wholly inappropriate for a mandated rate of return to be applied to regional water utilities. Such utilities face challenging circumstances, including a declining rates base, geographic dispersion of their end-users and the need to service many small groups of end-users. Such circumstances diminish the economies of scale and commercial recovery rates enjoyed by many metropolitan water utilities.

In many cases, the Group considers that the prices passed onto end-users for these services do not, and cannot, reflect the actual cost of service provision.

INFORMATION REQUEST
Do local government financing policies, including restrictions on rate increases, directly or indirectly influence the price setting or investment behaviour of council owned utilities, and if so how?

The Group considers that local government financing policies do not influence the price setting or investment behaviour of their Councils. However, members of the Group acknowledge that the impact of price rises must always be balanced with the capacity of the community to bear such increases.

INFORMATION REQUEST
As with the major metropolitan utilities, the Commission is interested in views as to whether regional water corporations should be structured as Government Trading Enterprises or corporations under the Corporations Act 2001 (Cwlth). Further, what are the ways that community views could be reflected in the utilities' activities without undermining the principle of board appointment by merit?

For many reasons, the Group does not consider it appropriate for all regional water corporations to be structured as Government Trading Enterprises or corporations under the Corporations Act 2001 (Cwlth).

Such organisational structures (particularly incorporated companies) impose certain duties and obligations upon its officers and senior management, many of which align themselves with the pursuit of commercial benefits and profits for stakeholders which members of the Group find difficult to reconcile with the needs of end-users in their Shires. By way of example, for Council-operated water utilities in the Group's region, it is not an option to cease supply of water services to end-users simply because the returns do not justify the means.

Amongst the Group, there are differing approaches to revenue returns for these services – some have implemented rating strategies which effectively charge uniform rates for all end-users despite service delivery being more expensive to some groups of end-users. For other Councils, differential pricing has been adopted depending on the end-user's locality. Accordingly, a "one size fits all" approach cannot be applied to the Councils within the Group and it is anticipated that a case-by-case analysis of all regional Councils would produce similar disparities.

DRAFT RECOMMENDATION 13.1

There is a strong case for undertaking aggregation of small water and wastewater utilities in regional areas of New South Wales and Queensland. The precise approach – including identification of affected councils and the preferred grouping of councils – should be assessed and determined by relevant State Governments, in consultation with Local Governments and affected communities.

This process should consider the relative merits of alternative organisational structures, including:

- *county council*
- *regional water corporation*
- *regional alliance (or regional organisation of councils).*

The Group recognises the value of aggregation of certain aspects of water and sewer services in regional areas and to this end, has independently formed the Group, which covers the Gwydir, Moree Plains and Walgett Shire Councils. As set out in the enclosed Memorandum of Understanding, the Group has been set up as a voluntary resource sharing alliance that commits its members to strive for the highest standards of delivery of water and sewerage services to their respective communities.

The Group was established at the instigation of its members, rather than as a result of higher government intervention. As a consequence, members have been primarily involved in establishing the purposes and objectives of the Group and determining the level of co-operation deemed appropriate for the region. The Group meets regularly to share information and experiences and in the future, it is likely that high-level strategic co-operation and management for the region will be sought by members.

However, the Group considers that full aggregation of members' water and sewerage assets is not feasible nor desirable for this region. Accordingly, each member has control and ownership of their assets (including in respect of maintenance and investment decisions) so that each member is free to pursue its own objectives and reinvest the fruits of those services in their own community.

DRAFT RECOMMENDATION 13.2

The New South Wales Government should provide a formal response to the recommendations of the Armstrong and Gellatly inquiry as a matter of priority.

The Queensland Government should commence a similar process, in consultation with Local Governments and communities, to consider the costs and benefits of different structural reform options for the urban water sector in regional Queensland (outside of south-east Queensland).

The Group considers that it would be appropriate for the NSW Government to formulate its position in relation to these findings and recommendations so that regional Councils can understand the NSW Government's intent regarding these matters.

DRAFT RECOMMENDATION 13.3

Jurisdictions should identify those regional utilities that are unable to provide safe and secure water and wastewater services for economic reasons. In doing so, the relative merits of alternative supply options (including moving to a system of self-supply) should be considered.

State and Territory Governments should subsidise the provision of water supply and wastewater services in regional areas where it is uneconomic for the utility to provide these services safely and efficiently. This funding should be granted via an explicit Community Service Obligation, and subject to periodic review.

The case for providing subsidy funding for capital works, financial incentives for reform and assistance for affected local councils should be determined by State and Territory Governments.

The Group acknowledges that there are challenges to providing safe and secure water and wastewater services to all parts of regional communities, particularly having regard to the economic cost of doing so. In fact, members of the Group face these very challenges in certain parts of their Shires and consider that they are not alone in these endeavours.

As this is a very real issue for members of the Group, there have been discussions regarding the merits of alternative supply options, for example, the provision of water tanks and filtration systems to smaller localities. Whilst this might be more economical on paper, members are not entirely comfortable that such an approach will ensure safe water supply as the responsibility of water standards is then delegated to the end-user.

The Group considers that low-interest loans advanced to communities facing water supply and wastewater service issues would be beneficial for those communities having the capacity to take responsibility for such services and the ability to service those loans. This ensures that ownership of the asset is always retained by the relevant community, which experience suggests results in a better outcome for those end-users.

However, the Group acknowledges that for certain communities within regional Australia (including some villages within members' Shires), this approach would be untenable. For these areas, State Governments should subsidise the provision of water supply and wastewater services where it is uneconomic for the local water utility to provide these services safely and efficiently.

Amongst the Group, there is agreement that the local water utility rather State Government is best placed to administer the provision of low-interest loans and allocation of subsidies. Knowledge of the potential alternative water supply options, future plans for the community and other local concerns and issues are entrenched within local water utilities. Accordingly, funding for loans and subsidies will be utilitised most efficiently and effectively by such utilities. It is felt that this produces a more sustainable approach to water supply. In the experience of members of the Group, local decision-making regarding water supply tends to produce better and more sustainable outcomes, with those "on the ground" better positioned to allocate the funding.

DRAFT RECOMMENDATION 13.4
State and Territory Governments should undertake regular, public reviews of water and wastewater outcomes in Indigenous communities. Water and wastewater services should be assessed against the same metrics that are used to measure service quality in non-Indigenous communities.

It is agreed that water and wastewater outcomes in Indigenous communities need to be periodically reviewed. This ensures accountability so that the most effective and sustainable supply methods are being pursued.

However, the Group questions whether such services should be assessed against the same metrics used to measure service quality in non-Indigenous communities. Often, the issues associated with supply and management to indigenous communities are vastly different from those of non-Indigenous communities. By way of example, some of the challenges include staff/skills shortages, significant financial costs and the relationship between the Aboriginal community and the local utility.

Notwithstanding this, the Group recognises the importance of securing quality water services for such communities and believes that local water utilities have a stronger, more prevailing social conscience to the provision of such services. Such a commitment is generally inconsistent with the commercial and profit-driven motives of a corporate entity.

DRAFT RECOMMENDATION 13.5

Compliance with the health critical elements of the Australian Drinking Water Guidelines should be mandatory, and implemented via legislation.

Utility performance against all elements of the Australian Drinking Water Guidelines should be publicly reviewed and reported on annually by State and Territory Governments. Sanctions should apply if water utilities do not comply with the mandatory elements of the guidelines, and directors or other accountable persons such as councillors should be personally liable for the risks associated with non compliance.

Utilities that do not comply with the non-health critical elements of the guidelines must develop and implement a risk management plan (approved by the relevant health department) that will move the utility toward full compliance with all elements of the guidelines.

The Group is very concerned with the suggested sanctions for non-compliance with mandatory elements of the Australian Drinking Water Guidelines and considers that attaching personal liability to directors and other accountable persons wholly unacceptable.

Whilst the Group acknowledges the importance of the mandatory elements of such Guidelines, there have been times that members of the Group have been unable to comply with such standards through no fault of the Council water service provider. A recent example of this involved the effects of the Queensland floods on water quality in the cross border river systems and therefore, water provision to certain members' communities.

All members of the Group share a genuine concern regarding the impact such sanctions would have on the ability of local utilities to provide water services to their communities. It is felt that such an approach would impose greater impediments to recruitment in this sector for regional councils – there are enough difficulties in attracting skilled professionals in regional areas, particularly for senior positions – without subjecting such individuals to personal liability.

In addition, the Group believes that this would have consequences upon the economic cost of service delivery. Such a regime would force local water utilities to be conservative in their approach to compliance with the mandatory Guidelines, which would be likely to significantly increase the cost of service provision. Further, members anticipate that accountable persons would be insistent on the water utility obtaining appropriate insurance coverage against such risk, which brings additional economic burden.

The Group believes that a preferable and workable approach to compliance with mandatory standards would be through the risk management plans of water utilities. These plans, through continuous improvement, are developed and refined over time.

DRAFT RECOMMENDATION 13.6

The Governments of Western Australia, South Australia and the Northern Territory should consider the costs and benefits of replacing the single, jurisdiction-wide public corporation model with a regional water corporation approach (horizontal disaggregation).

In undertaking this analysis, relevant State and Territory Governments should consider factors other than scale, including opportunities for yardstick competition, the proximity of utilities to the customers they serve, opportunities for more location-specific pricing arrangements and the effectiveness of water resource management and water system planning.

As this does not involve the NSW State Government, this recommendation is noted by the Group.

INFORMATION REQUEST
What are the likely sources of costs and benefits of undertaking structural reform of the urban water sectors in Western Australia, South Australia and the Northern Territory?

As this does not involve the urban water sector in NSW, this information request is noted.

DRAFT FINDING 13.3
There may be scale and scope benefits for water supply and wastewater services to be provided by a single utility in regional areas. This should be considered by jurisdictions as part of the reform process.

As noted throughout this Submission, the benefits which can potentially accrue by approaching certain aspects of water supply and wastewater services regionally have already been recognised by the Moree Plains, Walgett and Gwydir Shires through the formation of the Group.

Given the diverse challenges faced by members of the Group, many such services remain with local utilities but it is felt that the natural development of the Group will be to adopt a more regional basis to strategic and asset management issues. Presently, the Group is discussing how certain duplicative aspects of water services in the region may be more efficiently delivered collectively (which is likely to result in greater economies of scale) and steps are being taken as to the most appropriate way to investigate these matters.

Other local utilities in the region have also been invited to form part of the Group.

INFORMATION REQUEST
Is there a case for reintegrating water supply and wastewater services in regional areas where they are currently provided separately? In which regions? What are the principle costs and benefits of separate, as compared to integrated, water supply and wastewater service provision?

For the region represented by members of the Group, the value of integration of certain aspects of water supply and wastewater services has already been recognised. Members of the Group feel that the hybrid voluntary alliance formed in this region (hybrid in the sense that assets remain owned and controlled by local utilities but there is a common approach to higher level strategic issues) works effectively. This demonstrates that a "one size fits all" approach is unlikely to be practically achievable and workable; rather, aggregation must be viewed as a case-by-case exercise to have regard to the factors affecting water supply and wastewater services.

CONCLUSION:

The Water Utilities Sharing Group strongly affirms that the role of managing country towns' water supply and sewerage should remain with Local Government in the States of New South Wales and Queensland.

The Group acknowledges that there may be some benefits to the community derived from Local Governments working together in voluntary alliances at a strategic level.

Mayor, Cr Katrina Humphries
CHAIR, WATER UTILITIES SHARING GROUP