Urban Water the Future – price monitoring or regulation?

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IPART Conference, 10 August, Sydney
How the Commission came to this issue

• The Commission completed a broad ranging public inquiry into Australia’s Urban Water Sector in 2011
• Inquiry was to assist COAG to advance urban water reform
Key problems in the Urban Water Sector

• Inefficient investment in supply augmentations
• Inefficient allocation of water
• Undue reliance on costly water restrictions
• Costly water use efficiency and conservation programs
• Addressing affordability by distorting prices

These problems occurred with and without price regulation
Why?

- Unclear, conflicting, inappropriately assigned objectives and policies
- Unclear responsibilities and accountabilities
The Commission proposed a reform package

• Proposed a package of reforms to overcome these problems
  – *focus on improved institutional & governance arrangements*
  – *once these arrangements in place, move to price monitoring*

• Not simply price regulation vs price monitoring
Price regulation – current arrangements

Metropolitan areas
• Prices set by independent regulators in NSW, Victoria, SA and the ACT
• Elsewhere regulators have an advisory role

Non-metropolitan areas
• Regulatory price setting less common
Rationales for price regulation

• Preventing the exercise of market power
• Avoiding the politicisation of utility pricing
• Ensuring full recovery of efficient costs
• Community reassurance
Potential advantages

- make utilities more efficient
- provide reassurance to consumers
- reduce politicisation
Price regulation

Potential disadvantages
• high transaction costs
• costs from regulatory error
• impediment to innovative procurement (real options) & pricing (multiple tariff offerings)
• cost recovery
Price regulation vs price monitoring

- Neither price monitoring nor price regulation on its own will overcome key problems in water sector
So what is needed?

- Clarification of objectives, roles & responsibilities
- Retailer-distributors with responsibility for competitive procurement & water security
- Incorporation of utilities
- Government charter with utility
- Public reporting against the charter
- Periodic public review of utility performance vs charter
- Greater consumer involvement
- ... and then a move to price monitoring
Charter between a government and its water utility

- Obligation to serve and procure supply
- Obligations regarding environment and public health
  - utilities must comply with these conditions
- Retail-distribution utilities apply portfolio manager framework
- Transparent processes and procedures for choosing supply augmentation
  - tenders for supply, public consultation, public reporting of decision, audit of decision by independent body
- Transparent principles, process and procedures for setting prices
  - public consultation, public reporting, periodic review, use marginal opportunity cost of supply to set volumetric prices
- Borrowings and dividends policies
- Customer service standard/hardship policies
- Risk allocation (consumers, government, private)
- Clearly specified and funded CSOs
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