



Independent Pricing and Regulatory Tribunal

Assessment of Huntlee Water's network operator's licence (drinking water) application

**Prepared under the *Water Industry Competition
Act 2006 (NSW)***

Report to the Minister
March 2015

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Inquiries regarding this document should be directed to a staff member:

Gary Drysdale (02) 9290 8477

Robert Aposhian (02) 9290 8406

Independent Pricing and Regulatory Tribunal of New South Wales
PO Box K35, Haymarket Post Shop NSW 1240
Level 15, 2-24 Rawson Place Sydney NSW 2000

T (02) 9290 8400 F (02) 9290 2061

www.ipart.nsw.gov.au

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1 Summary

The Independent Pricing and Regulatory Tribunal of NSW (IPART) received and assessed the network operator's licence application from Huntlee Water Pty Ltd (HW) under the *Water Industry Competition Act 2006* (NSW) (the Act).

HW proposes to eventually construct, operate and maintain a drinking water supply network, a sewerage network, recycled water network and water recycling facility at a new residential and commercial development at Huntlee, in the Lower Hunter Valley near Cessnock (identified as Huntlee Stage 1).¹ Huntlee Stage 1 involves the construction of up to 2,345 lots over 15 sub-stages.

Huntlee Stage 1 received planning approval from the Planning Assessment Commission (PAC) under Part 3A of the *Environmental Planning and Assessment Act 1979* (EP&A Act) in 2013.² The development approval included the construction of utilities, roads and other associated infrastructure necessary for a residential sub-division.

The provision of water and sewerage services in the application was based on a water servicing plan with Hunter Water Corporation (**Hunter Water**) as the nominated service provider. The conditions of approval indicated that other service providers may be used, but these would require a WICA licence.³ Further, the planning approval did not provide for the construction and operation of a local recycled water plant. A proposed recycled water plant is now subject to a rezoning request by the developer.

Due to delays in obtaining rezoning approval for the recycled water plant and its need to meet planned development timeframes, HW has requested that its licence application be assessed in two separate phases:⁴

- ▼ Phase 1 involves the construction of the drinking water reticulation infrastructure only for the first 180 lots (the subject of this report).
- ▼ Phase 2 will include construction of the remaining water, sewage and recycled water infrastructure for Huntlee Stage 1, including the recycled water plant.

¹ Huntlee Water network licence application - 1 May 2014. Available at http://www.ipart.nsw.gov.au/Home/Industries/Water/Private_Sector_Licensing_WICA/Huntlee_Water_Pty_Ltd

² Huntlee Water network licence application - Appendix 3 - 1 May 2014. Available at http://www.ipart.nsw.gov.au/Home/Industries/Water/Private_Sector_Licensing_WICA/Huntlee_Water_Pty_Ltd

³ Huntlee Water network licence application - Appendix 3 - 1 May 2014. Available at http://www.ipart.nsw.gov.au/Home/Industries/Water/Private_Sector_Licensing_WICA/Huntlee_Water_Pty_Ltd

⁴ Email dated 21 January 2015 from Flow Systems' (HW's parent), outlining its request to reduce the scope of the application to just include drinking water infrastructure.

Phase 2 of the project will be the subject of a future licence variation application after the rezoning is obtained.⁵

Our assessment is therefore primarily focused on Phase 1, which involves drinking water infrastructure only for the first 180 lots. However, some elements of the larger scheme form part of our assessment, where appropriate.

Key issues from the stakeholder submissions include:

- ▼ The status of the rezoning application for the site, and determining the appropriate planning instrument and consent body for the treatment plant and reticulation network. By limiting the application to Phase 1, HW has effectively postponed the review of these issues until a subsequent licence variation is sought for the whole of the Stage 1 development. The existing Part 3A approval under the EP&A Act includes the construction of the drinking water reticulation network. We have reviewed the environmental assessment conducted for these works under this approval and consider that no further assessment is warranted for Phase 1 of this scheme. For further discussion of this issue, see section 4.2 of this report.
- ▼ The status of negotiations with Hunter Water regarding bulk water supply agreements and the amplification works program necessary to eventually supply the entire development. Hunter Water has advised that negotiations between Hunter Water and Flow Systems are in an advanced stage towards entering a 10-year supply agreement. Hunter Water indicated the utility service agreement could be executed by 31 March 2015.⁶ This will be supported by a site specific agreement for Huntlee, which is expected to be signed shortly thereafter. The amplification works program is specific to Hunter Water and the developer, and does not form part of this licence assessment. For further discussion of this issue, see section 4.1.2 of this report.

Our full assessment of the licence application is outlined in Section 4 of this report. Based on our analysis, we are satisfied that HW has satisfactorily met the licensing criteria under section 10 of the Act, having regard to the licence application, submissions made, and the licensing principles under section 7 of the Act.

We therefore recommend that the Minister grants a network operator's licence to HW, for the works identified in Phase 1, subject to the conditions as set out in licence number 15_030.

⁵ The rezoning application is currently with the Department of Planning and Environment (DPE). HW anticipates that this approval will be given in the near future.

⁶ Letter from Hunter Water to IPART, dated 2 March 2015.

The Minister must consider, but is not bound to accept, any advice or recommendation in this report in determining the licence application. The Minister may, if circumstances so require, seek further advice from us in relation to the licence application.⁷

We recommend that the standard licence conditions be applied, with an additional clause requiring HW to maintain professional indemnity insurance for a minimum of six years following the completion of the design phase of the infrastructure (see section 4.1.7 of this report for further details). We consulted with the Self Insurance Corporation of NSW (SICorp) on the insurance requirements for this particular application, and agreed that it is appropriate to include this clause in the licence.

Further, we note that we are likely to recommend that this clause becomes a standard licence condition for all new WICA network operator licences.

2 Background

Purpose of this report

In accordance with the Act, IPART must consider the licence application and any stakeholder submissions, and provide a report on the application to the Minister.⁸ The Minister is required to determine an application for a licence by granting the licence or refusing the application.⁹ The Minister may determine the conditions to which the licence (if granted) should be subject.¹⁰

This report therefore summarises our analysis, issues raised by stakeholders through their submissions and our recommendation to grant the licence. It also contains proposed licence conditions to which the applicant should be subject.

The applicant

The applicant corporation, Huntlee Water Pty Ltd (HW), is a subsidiary company of Flow Systems Pty Ltd (Flow Systems). HW has no direct employees and relies on the full support of Flow Systems for operation.

⁷ *Water Industry Competition Act 2006* (NSW), section 10(2).

⁸ *Water Industry Competition Act 2006* (NSW), section 9.

⁹ *Water Industry Competition Act 2006* (NSW), section 10(1).

¹⁰ *Water Industry Competition Act 2006* (NSW), section 13(1)(b).

Flow Systems currently operates three other licensed networks through its subsidiary companies, at Discovery Point, Pitt Town and Central Park. Each network includes the supply and reticulation of recycled water. Central Park and Discovery Point are also licensed for the reticulation of drinking water. In addition, Flow Systems has received a new licence for a development at Wyee, and has several other applications for network and retail licences currently being assessed.

The overall scheme

Huntlee Stage 1 development is divided in 15 sub-stages and includes 2,070 dwellings, and five mixed use town centre sub-stages representing another 275 lots.¹¹ The development received Part 3A approval under the EP&A Act from the Planning Assessment Commission (PAC) in April 2013.

The Part 3A approval includes approval to build the reticulation network for drinking water and sewage, along with other utility services. However, it does not include approval for a local recycled water plant. A separate rezoning application has been submitted to the Department of Planning and Environment (DPE) to rezone the area from B4 Mixed Use to SP2 Infrastructure. The rezoning also has the effect of making the clauses in Division 18 of *State Environmental Planning Policy (SEPP) 2007 (Infrastructure)* relevant. Under clause 106 of the Infrastructure SEPP, the recycled water plant can be built by a WICA licensee on land in a prescribed zone without consent. In the event of an application to vary the licence for Phase 2, we will undertake an environmental assessment when assessing a WICA licence application under the Act.¹²

Proposed water industry infrastructure subject to this application

On 1 May 2014 we received HW's licence application for a network operator's licence under the Act for Huntlee Stage 1. Stakeholder consultation commenced on 1 July 2014 and concluded in August 2014. In response to issues identified by stakeholders and through our assessment, HW subsequently provided additional information.

On 20 November 2014, HW requested that the application be reduced to only include the first 180 lots, to be supplied with sewerage, drinking water and recycled water reticulation infrastructure, and construction of interim flow balance tanks to collect, store and dispose of wastewater offsite.

¹¹ Huntlee Water network licence application - 1 May 2014. Refer IPART website - http://www.ipart.nsw.gov.au/Home/Industries/Water/Private_Sector_Licensing_WICA/Huntlee_Water_Pty_Ltd

¹² *Water Industry Competition Act 2006* - sections 7(1)(a) and 10(4).

On 21 January 2015, this request was further reduced to just drinking water for the first 180 lots. The proposed treatment plant is not permitted under the current land use, as it is not a prescribed zone.

As part of a review of internal assessment processes, including insurance and related entity checks, further information was requested and provided by HW in January and February 2015, which completed the assessment for Phase 1.

According to the applicant,¹³ the developer needs to obtain subdivision registration as soon as possible to commence construction and meet its development timetable. HW has therefore proposed to construct, operate and maintain water industry infrastructure within the Huntlee Stage 1 development in two phases:

- ▼ Phase 1 - drinking water reticulation, with water supply accessed from Hunter Water Corporation (Hunter Water), to the first 180 lots.
- ▼ Phase 2 includes all the remaining works as shown below, including a new recycled water treatment plant, referred to as the Local Water Centre (LWC), for all of Huntlee Stage 1:
 - drinking water: reticulation, storage, treatment
 - sewage: collection, treatment, disposal, and
 - recycled water: treatment, storage and reticulation.

Phase 1 is the focus of this report. Phase 2 will be the subject of a separate licence variation application and assessment. Drinking water will be supplied to HW by Hunter Water under a bulk water supply agreement. Hunter Water has advised that negotiations between Hunter Water and Flow Systems are in an advanced stage towards entering a 10-year supply agreement. Hunter Water indicated the utility service agreement could be executed by 31 March 2015.¹⁴ This will be supported by a site specific agreement for Huntlee, which is expected to be signed shortly thereafter.¹⁵

The existing drinking water system has capacity for 550 lots prior to the need to construct the next trunk supply main. The current proposed 180 lots in Phase 1 is within the current system capacity.¹⁶

¹³ Email dated 17 October 2014; Letter from Flow Systems to IPART – 21 November 2014.

¹⁴ Letter from Hunter Water to IPART, dated 2 March 2015.

¹⁵ Letter from Hunter Water to Flow Systems, dated 17 October 2014.

¹⁶ Letter from Hunter Water to SMEC Australia, who prepared the water and wastewater servicing strategy for Huntlee New Town, dated 26 June 2013.

3 Consultation and submissions

Ministers and their departments

On 1 July 2014, we provided the licence application for Huntlee Stage 1 to, and invited submissions from, the following Ministers and their relevant departments:

- ▼ Minister administering the *Public Health Act 2010* (NSW) (Minister for Health).
- ▼ Minister administering Chapter 2 of the *Water Management Act 2000* (NSW) (Minister for Primary Industries).
- ▼ Minister administering the *Protection of the Environment Operations Act 1997* (NSW) (POEO Act) (Minister for the Environment).
- ▼ Minister administering the *Environmental Planning and Assessment Act 1979* (NSW) (EP&A Act) (Minister for Planning).¹⁷

We also provided a copy of the licence application to the Minister for Natural Resources, Lands and Water, as the Minister administering the Act, at the same time.

The closing date for the submissions was 1 August 2014. We received four submissions. These submissions are available on our website. The issues raised, and how these issues were addressed, are described below. Please note that these submissions were based on the larger Huntlee Stage 1 development.

- ▼ NSW Health supported the application, and requested consultation during:
 - i) the detailed risk assessment and technology assessment (if conducted)
 - ii) following the compliance audit and before retail supply commences, and
 - iii) the development of the water quality management plans.

We have guidelines and procedures in place to ensure NSW Health is consulted after the licence is granted when the above tasks will be undertaken.

- ▼ The DPE has no objection to the application, provided all necessary approvals have been obtained. In this regard, we note that drinking water infrastructure will be constructed in accordance with the Part 3A approval under the EP&A Act. Other issues raised by DPE regarding the permissibility of the construction of a recycled water treatment plant in the current land zoning will be assessed in a subsequent licence variation request, once the rezoning approval has been obtained.

¹⁷ *Water Industry Competition Act 2006*, section 9(1)(b).

- ▼ The NSW Environment Protection Authority (EPA) has advised that HW will require an environment protection licence (EPL) for the scheduled activity of ‘sewage treatment’ in accordance with the POEO Act. We note that this is not required for Phase 1 of this project, which only involves drinking water infrastructure. Further, an EPL will not be required initially as the plant capacity will be below the EPL licensing threshold for many years.
- ▼ The Minister for Natural Resources, Lands and Water advised that stormwater captured by the detention basins may require a water access licence and water supply work approval. In addition, one of the permanent water bodies proposed for the development is proposed to be used for water quality control purposes. These ponds may exceed current harvestable rights limits and therefore may also require a water access licence and water supply work approval. We have been advised that the use of these ponds will only be required if the recycled water plant requires additional volume. HW will be required to liaise with the NSW Office of Water if/when it decides to incorporate these ponds into the scheme. We understand that this issue is unlikely to occur for many years and therefore does not form part of the Phase 1 proposal being considered within this report.

Public water utility

Hunter Water was notified of the licence application. It advised that it supported the application, provided that negotiations concerning bulk water supply were completed, and the water servicing strategy was revised to take into account revised potable water demands.¹⁸ These concerns are addressed in section 4.1.2 below.

Expert consultants

We approached two agencies to assist us with the assessment of the licence application.

The Self Insurance Corporation of NSW (SICorp) provided assistance to assess the adequacy of HW’s insurance requirements. SICorp also provided advice as to whether the structure of insurances appears to be appropriate given the level of risk and the activities expected from the scheme. SICorp’s findings are addressed in section 4.1.7.

Vincent’s Chartered Accountants (Vincent’s) was engaged to assess the financial capacity of the applicant and the viability of the proposed scheme. As HW is a new entity, the assessment focused on the parent company, Flow Systems. Vincent’s findings are addressed in section 4.1.3.

¹⁸ Letter from Hunter Water to IPART, dated 1 August 2014.

The Deed of Guarantee and Indemnity (the Deed) and Corporate Services Agreement (CSA) between HW and its parent, Flow Systems, were provided to both Vincents and SICorp as background information to support their analysis. Their findings are addressed in sections 4.1.3 and 4.1.7. The Deed and the CSA were subsequently reviewed and amended to provide added clarity in relation to the scope and protection of the rights of HW's beneficiary.

General public and local council

We also called for submissions on the application from the public.¹⁹ We advertised in the Sydney Morning Herald, Daily Telegraph, and Newcastle Herald on 9 July 2014 for public submissions. Submissions closed on 1 August. One submission was received from Cessnock City Council, which raised a number of concerns related to the environmental and regulatory aspects of the proposed recycled water and sewage management scheme. These issues do not concern the provision of drinking water to the development. The rezoning application and additional assessment information provided should allay the majority of Council's concerns. However, any residual matters will be considered as part of the licence variation process for Phase 2 of the scheme.

4 Assessment of application

This section of the report contains our assessment of HW's network operator's licence application and our justifications for recommending the granting of the licence.

Information assessed

In making our recommendations we have undertaken analysis of the information that HW provided in its licence application, stakeholder submissions and discussions, specialist consultants' findings, and additional information submitted by the applicant through subsequent requests.

¹⁹ *Water Industry Competition Act 2006*, section 9(1)(c).

Basis of our assessment

Our assessment is based on each of the licensing criteria and principles outlined in the Act. The Minister may not grant the licence unless satisfied that the applicant:

- ▼ is not a disqualified corporation
- ▼ is not a corporation that is a related entity (within the meaning of the *Corporations Act 2001* of the Commonwealth) of a disqualified corporation, but only if the disqualified corporation would have a direct or indirect interest in, or influence on, the carrying out of the activities authorised by the licence
- ▼ has, and will continue to have, the technical, financial and organisational capacity to carry out the activities to be authorised by the licence
- ▼ has the capacity to carry out its activities in a manner that does not present a risk to public health or a significant risk of harm to the environment
- ▼ has made, and will continue to maintain, appropriate insurance arrangements
- ▼ in the case of a licence to supply water, will supply sufficient quantities of water obtained otherwise than from a public water utility, and
- ▼ such other matters as the Minister considers relevant, having regard to the public interest.²⁰

Further, in considering whether or not to grant the licence, and what conditions (if any) to impose on the licence, regard is to be had to the following licensing principles:

- ▼ the protection of public health, the environment, public safety and consumers generally
- ▼ the encouragement of competition in the supply of water and the provision of sewerage services
- ▼ the ensuring of sustainability of water resources
- ▼ the promotion of production and use of recycled water
- ▼ the promotion of policies set out in any prescribed water policy document
- ▼ the potential for adverse financial implications for small retail customers generally arising from the activities proposed to be covered by the licence, and
- ▼ the promotion of the equitable sharing among participants in the drinking water market of the costs of the water industry infrastructure that significantly contributes to water security.²¹

Our assessment is provided in section 4.2 of this report. Section 4.3 contains additional matters that we considered relevant to this licence application.

²⁰ *Water Industry Competition Act 2006* (NSW), sections 10(3) and (4).

²¹ *Water Industry Competition Act 2006* (NSW), section 7.

Scope of the assessment

Although this report assessed Phase 1 of the licence application only, some licensing criteria and principles have been considered in respect to the whole scheme. Criteria and principles that only apply to Phase 1 are stated and explained in the relevant sections.

4.1 Licensing criteria

4.1.1 Disqualified corporation and related entities

Huntlee Water Pty Ltd is not a disqualified corporation. Its directors and Chief Operating Officer are not disqualified individuals. Huntlee Water is not a related entity of a disqualified corporation.

In making this recommendation, we have considered the following information:

- ▼ The statutory declaration made by the Managing Director and Chief Operating Officer, stating that:
 - neither HW, nor any director or person concerned in the management of HW is, or would be, a disqualified corporation or disqualified individual within the meaning of the Act, and
 - HW is not a related entity of a disqualified corporation that would have a direct or indirect interest in, or influence on, the carrying out of activities that the licence would authorise if granted.
- ▼ Information provided by the applicant regarding details of the:
 - trustees (past and current) of any trusts in relation to which the applicant is a beneficiary
 - current beneficiaries of any trusts in relation to which the applicant is a trustee, and
 - names of the Chief Financial Officer and Chief Executive Officer for each of the applicant's related entities.
- ▼ Related entity checks undertaken showed that four corporations are related to HW, and would have a direct or indirect interest in, or influence on, the carrying out of activities that the licence would authorise if granted. These companies are Flow Systems, Brookfield Water Holdings Pty Ltd, Brookfield Utilities (Australia) Pty Ltd and BPIH Pty Ltd.
- ▼ Results of the ASIC and Dun & Bradstreet reports that we have obtained for HW, and these four related corporations, confirmed that these companies are not disqualified nor are their directors, Chief Executive Officers, and Chief Financial Officers, disqualified individuals.

- ▼ Results of our search of the Act licence database²², confirming the above..

4.1.2 Technical capacity

We are satisfied that Huntlee Water Pty Ltd has the technical capacity to construct, operate, and maintain water industry infrastructure of the type subject to this application.

In making this recommendation, we have considered the following:

- ▼ The reports, plans and procedures that Flow Systems²³ prepared for similar projects demonstrated its technical understanding of operation and maintenance of drinking water reticulation and treatment. Flow Systems operates Discovery Point Water Factory and Central Park Water, which both have a drinking water component.
- ▼ The results of licence plans audits carried out for Discovery Point and Central Park schemes showed no significant non-compliances, which demonstrated Flow Systems' capacity to safely and reliably construct, operate and maintain infrastructure.
- ▼ HW's preliminary risk assessment demonstrated technical capacity to understand and implement the Australian Drinking Water Guidelines.
- ▼ HW's preliminary design of its potable and non-potable reticulation networks and treatment plant demonstrated technical capacity to design, operate and maintain water industry infrastructure. HW was able to provide a detailed breakdown of its peak and average water treatment and supply calculations, with the assumptions used in line with best practice in NSW.
- ▼ Flow Systems' previous technical experience (within Australia), evident from a review of the CVs of specific personnel nominated to the project in the application.

The applicant is responsible for design, operation and maintenance of all water industry infrastructure within the scheme, as well as construction of the treatment plant. The developer is responsible for construction and handover of the reticulation pipework to the applicant.

Further, we note that Hunter Water advised that it supported the application, provided negotiations concerning bulk water supply were completed and the water servicing strategy was revised to take into account revised potable water demands. These issues have been resolved, and a Utility Services Agreement (USA) between Flow Systems and Hunter Water is being finalised. Negotiations between Hunter Water and Flow Systems are in an advanced stage towards entering a 10-year supply agreement. Hunter Water indicated the utility service

²² There are currently no disqualified corporations or individuals on the register pursuant to the *Water Industry Competition Act 2006*, section 16(e) and 16(f).

²³ Flow Systems will be undertaking these activities on behalf of HW.

agreement could be executed by 31 March 2015.²⁴ An additional agreement specific to the Huntlee site will then be concluded.²⁵

We received no submission regarding HW's technical capacity to operate and maintain drinking water infrastructure.

We conclude that HW has the required technical capacity to be granted a network operator's licence for Phase 1, subject to Flow Systems being specified as an authorised person in the licence.

We recommend that the standard ministerially imposed licence conditions should apply.

4.1.3 Financial capacity

We are satisfied that Huntlee Water Pty Ltd has the financial capacity to construct, operate and maintain the water industry infrastructure. This applies to the whole of Huntlee Stage 1.

We engaged an external financial consultant, Vincents, to assess the financial capacity of the applicant and the viability of the scheme. Since HW is a newly formed subsidiary of Flow Systems, we asked Vincents to review both companies.

We provided the Deed of Guarantee and Indemnity (the Deed) and the Corporate Services Agreement (CSA) between HW and Flow Systems to Vincents as part of its financial assessment. The Deed provides the financial guarantee for the subsidiary company, whilst the Corporate Services Agreement provides the contractual arrangements between parent and subsidiary regarding the provision of services necessary to complete the works. The Deed has no cap on liability and no sunset date. Flow Systems will ensure that HW will perform and observe the guaranteed obligations necessary to meet any claim during the term and, if required, Flow Systems will perform or observe any guaranteed obligation or otherwise procure its performance.

In terms of financial capacity, Vincents reported that Flow Systems has a low to medium risk of financial failure. In terms of financial viability of the project, Vincents considered the project low risk. Vincents considered that the Deed was satisfactory to meet the operational financial requirements of the project. Based on its assessment, Vincents recommended approval for HW to be licensed. In Vincents' opinion, HW does not require any additional conditions to ensure it maintains its financial capacity.

²⁴ Letter from Hunter Water to IPART, dated 2 March 2015.

²⁵ Letter from Hunter Water to Flow Systems, dated 17 October 2014.

We reviewed the Deed and CSA. A number of issues were identified to strengthen the documents. Subsequent changes were made in consultation with Flow Systems to revise the Deed and the CSA. We conclude that the Deed is adequate to provide a continuing guarantee and indemnity for all liabilities incurred by HW in carrying out the obligations under the scheme contract. Further, we included a new special licence condition that requires HW to provide prior notification to IPART when the licensee proposes to modify any agreement in connection with the licence application, including the Deed and CSA.

We would like to emphasise that our financial assessment represents the applicant's financial capacity at a point in time. Our recommendation to grant HW a licence should not be viewed as endorsement of the future viability of the corporation. The assessment is based on a combination of information sources, none of which is to be regarded as individually determinative. This assessment is done for our own purpose and for the Minister's purposes in assessing the applicant's application. The conclusion is not to be relied upon for any other purpose by any other person.

We received no submission regarding HW's financial capacity.

We recommend that the standard ministerially imposed licence conditions should apply.

4.1.4 Organisational capacity

We are satisfied that Huntlee Water Pty Ltd has the organisational capacity to construct, operate and maintain the water industry infrastructure subject to this application.

Our analysis showed that, through its relationship with Flow Systems, HW has:

- ▼ Previous experience (within Australia) in the water industry and specific personnel nominated to the project, as shown by the CVs of its key personnel provided to us in its application form.
- ▼ Appropriate organisational structure to manage its nominated third parties to deliver the proposed work based on their contractual arrangements and agreements.
- ▼ Demonstrated that business risks have been identified and will be managed, through the risk assessment it provided.

HW relies on its parent company, Flow Systems, for business support. The CSA and the Deed demonstrated continued organisational support from Flow Systems.

We received no submission regarding HW's organisational capacity.

We recommend that the standard ministerially imposed licence conditions should apply.

4.1.5 Risk to public health

We are satisfied that Huntlee Water Pty Ltd has the capacity to construct, operate and maintain water industry infrastructure in a manner that does not present a risk to public health.

Our analysis showed that HW, through its relationship with Flow Systems, has:

- ▼ Demonstrated previous experience (within Australia) in the water industry and has sufficient technical and organisational capacity to satisfactorily operate and maintain the proposed system, as shown in its application form. Flow Systems currently operates Central Park and Discovery Point drinking water infrastructure under two separate operator's licences.
- ▼ Demonstrated sufficient technical capacity to design and construct the proposed water industry infrastructure to minimise risks to public health.
- ▼ Demonstrated sufficient technical capacity to analyse and manage hazards from source to end use through its risk management plan that it provided, where the Australian Drinking Water Guidelines were applied.

We have also considered NSW Health's submission on HW's capacity to carry out the activities that would be authorised by the licence in a manner that would not present a risk to public health.

NSW Health supports the licence application, subject to the applicant addressing a number of issues,²⁶ including:

- ▼ Consultation with NSW Health during the risk assessments, at the Technology Assessment stage (if undertaken), and before commercial production commences, to ensure all relevant health matters have been addressed.
- ▼ Involvement by NSW Health in the development of the final management plans, including incident notification and management procedures.

We have guidelines and procedures in place to ensure NSW Health is consulted when the above tasks are undertaken, after the licence is granted. The licensee must comply with any requirements of NSW Health that we have agreed to, and that we have notified the licensee about, in writing.

We recommend that the standard ministerially imposed licence conditions should apply.

²⁶ Submission from NSW Health, 30 July 2014. Available at http://www.ipart.nsw.gov.au/Home/Industries/Water/Private_Sector_Licensing_WICA/Huntlee_Water_Pty_Ltd

4.1.6 Risk to the environment

We are satisfied that the Huntlee Water Pty Ltd has the capacity to construct, operate and maintain the water industry infrastructure in a manner that does not present significant risk of harm to the environment. Our current assessment is limited to Phase 1 of the scheme, involving drinking water infrastructure only.

Our analysis showed that HW, in conjunction with Flow Systems, has:

- ▼ Demonstrated capacity to comply with environmental regulations, through their previous experience (within Australia) in preparing environmental impact assessments and implementing mitigation measures for the construction and operation of drinking water reticulation infrastructure.
- ▼ Demonstrated understanding of regulatory approval requirements, as confirmed by our own assessment and advice from DPE. In 2013, the developer obtained approval under Part 3A of the EP&A Act from the PAC for Huntlee Stage 1.²⁷
- ▼ Demonstrated capacity to implement environmental management processes, through their site-specific environmental risk assessment and impact assessments. We will audit the adequacy of these controls prior to HW commencing commercial operation of the scheme.

We therefore consider that HW has demonstrated sufficient capacity to not cause significant risk of harm to the environment in Phase 1.

We recommend that the initial licence contain the standard ministerially imposed licence conditions.

4.1.7 Insurance requirements

We are satisfied that Huntlee Water Pty Ltd has made, and will continue to maintain, appropriate arrangements with respect to insurance.

We consulted SICorp to assist us with this assessment.

As part of the review, SICorp examined the applicant's proposed scope of work, the risk assessment, insurance coverage in the areas of professional indemnity, public liability and product liability, as shown in the applicant's insurance certificates. SICorp also reviewed the product disclosure statements for each insurance certificate, and examined the financial rating of the various underwriters providing the insurance. The Deed and the CSA between Flow Systems and HW were also provided to SICorp for review.

²⁷ Huntlee Water network licence application - Appendix 3 - 1 May 2014. Available at http://www.ipart.nsw.gov.au/Home/Industries/Water/Private_Sector_Licensing_WICA/Huntlee_Water_Pty_Ltd

SICorp concluded that sufficient insurance coverage has been demonstrated, subject to an additional requirement on the applicant to maintain professional indemnity insurance during the design phase of the infrastructure and for a minimum of six years following the completion of the design phase of the infrastructure:²⁸

- ▼ Our review of the agreements between Flow Systems and HW showed that they imposed no monetary limits on obligations to HW and its beneficiaries.
- ▼ Further, we intend to consult with SICorp in reviewing an Insurance Expert's report on the proposed insurance arrangements provided by HW, prior to commercial operation of the scheme. Such a report would be required under our recommended terms of the licence.²⁹

We received no submission regarding HW's insurance arrangements.

We recommend that the standard ministerially imposed licence conditions should apply, which requires the licensee to obtain and maintain appropriate insurance.

We also recommend a modification to the standard licence conditions to require the maintenance of professional indemnity insurance during the design phase of the infrastructure and for a minimum of six years following the completion of the design phase of infrastructure.

4.1.8 Additional public interest considerations

No additional matters were raised with regard to public interest during the stakeholder consultation process.

4.2 Licensing principles

We are satisfied that granting a network operator's licence to Huntlee Water Pty Ltd is consistent with the licensing principles.

We had regard to each of following licensing principles in making a recommendation as to whether or not the licence should be granted, and what licence conditions to impose:

²⁸ Email dated 13 February 2015, from SICorp to IPART.

²⁹ Proposed Huntlee network operator's licence – clause B3.4.

- ▼ **Protection of public health, environment, public safety and consumers generally** - We consider that HW has the technical capacity and experience to undertake the activities in a way that will satisfactorily manage risks, subject to Flow Systems being named as authorised persons in the licence. The drinking water supplied through Hunter Water's network is subject to rigorous monitoring. Currently, there are no Operator of Last Resort provisions in place, however drinking water supply is being sourced from Hunter Water, and sewage can be trucked offsite for disposal in emergency situations. We have reviewed the environmental assessment conducted for the scheme, which occurred as part of the approval process under Part 3A of the EP&A Act. We consider that no further assessment or mitigation measures are warranted for Phase 1 of the scheme, provided the conditions of the development approval are adhered to. We therefore consider the proposed activity does not present a significant risk of harm to the environment, and is consistent with Clause 7 of the *Water Industry Competition (General) Regulation 2008* (WIC Regulation) and Section 7 of the Act.
- ▼ **Encouragement of competition** - Although this licence is initially limited to the supply of drinking water to the first 180 lots, it is envisaged the overall scheme will eventually provide sewerage services, drinking water and recycled water to the customers within the Huntlee Stage 1 development. Historically, Hunter Water had a monopoly on sewerage services and drinking water supply in the Newcastle and Hunter regions. Under the applicant's proposal, the overall project will eventually enable a new entity to provide drinking water, sewerage services and recycled water to a discrete development, thus encouraging competition in the provision of these services.
- ▼ **Ensuring sustainability of water resources** - This is Phase 1 of a larger proposed scheme to reduce reliance on drinking water. In Phase 2, the recycled water will be sourced from sewage that would have otherwise been treated and discharged to the environment. It will replace drinking water for toilet flushing, cold water clothes washing, irrigation, car washing, cooling tower use and general wash-down water.
- ▼ **Promotion of production and use of recycled water** - As mentioned above, this is Phase 1 of a larger proposed scheme to reduce reliance on drinking water. In Phase 2, recycled water will be produced for reuse following treatment of collected sewage from the new development. Under the applicant's broader proposal, all homes within the development will be supplied with recycled water, minimising the demand for potable water.

- ▼ **Promotion of policies set out in any prescribed water policy document** - The eventual supply of recycled water by HW to the Huntlee development is consistent with the objectives of the Lower Hunter Water Plan. The Lower Hunter Water Plan contains various water supply and demand measures to ensure the region can withstand extreme drought. This plan includes the supply of recycled water and notes that “private sector suppliers are likely to play a bigger role in providing water supply, wastewater and recycled water services to new developments, particularly in areas remote from urban centres”.³⁰ Flow Systems’ supply of drinking water, recycled water, and provision of sewerage services at Huntlee Stage 1 therefore promotes the policies set out in the Lower Hunter Water Plan. The Metropolitan Water Plan is the only prescribed water policy document in the WIC Regulation. It does not apply to the development in Huntlee Stage 1.
- ▼ **Potential for adverse financial implications for small retail customers generally arising from the activities proposed to be covered by the licence** - This principle applies to retail supplier licence applications. It will be considered in any future retail licence application by the applicant or its parent company for this scheme.
- ▼ **Promotion of equitable sharing among participants in the drinking water market of the costs of water industry infrastructure that significantly contributes to water security** -The Lower Hunter Water Plan states that “...the current water supply system can supply an average of around 75 billion litres of water each year to the people of the lower Hunter. Taking account of forecast population growth of just over 100,000 people, and water consumption trends, there will be enough water to supply the region for around 20 years under typical climate conditions.”³¹ As a consequence, there is currently no significant expenditure on water infrastructure to improve water security in the region.

4.3 Additional matters considered

4.3.1 Monopoly supplier

We consider that Huntlee Water Pty Ltd should not be subject to pricing regulation through being declared a monopoly supplier, at this time.

Under section 51 of the Act, the Minister may declare a licensed retail supplier or licensed network operator to be a monopoly supplier in relation to a specified water supply or sewerage service, area and class of customers.

³⁰ 2014 Lower Hunter Water Plan, NSW Department of Finance and Services, January 2014, p 2.

³¹ 2014 Lower Hunter Water Plan, NSW Department of Finance and Services, January 2014, p 10.

The Minister can declare a monopoly supplier after the licence has been granted. If declared a monopoly supplier, the Minister may then refer the monopoly services to IPART for determination of prices and/or periodic review of the pricing policies.

A monopoly declaration can only be made in relation to a service if the Minister is satisfied that:

- ▼ it is a service:
 - i) for which there are no other suppliers to provide competition in the part of the market concerned, and
 - ii) for which there is no contestable market by potential suppliers in the short term in that part of the market, and
- ▼ in the case of a water supply service for recycled water, that connection of land to that service is required by or under some other Act.³²

We consider the service to be licensed could be considered a monopoly service. However, at this time, we do not recommend that the network operator be declared in relation to a water supply or sewerage service, nor subject to price regulation.

We note that Flow Systems has indicated that it will match its charges to those of Hunter Water for drinking water and sewerage services, and will provide recycled water at a price below the drinking water price.

This matter will be reconsidered when assessing the retail supplier's licence application for this scheme and/or when a variation to this network application is made.

5 Recommendations

We are satisfied that Huntlee Water Pty Ltd has satisfactorily met the licensing criteria under section 10 of the Act, having regard to the licence application, submissions made, and the licensing principles under section 7 of the Act.

We recommend that the Minister grants a network operator's licence to Huntlee Water Pty Ltd, subject to the conditions as set out in licence number 15_030.

Further, we consider that Huntlee Water Pty Ltd should not be declared a monopoly supplier in respect of a water supply or sewerage service, nor subject to pricing regulation, at this time.

³² *Water Industry Competition Act 2006* (NSW), section 51(2).

The Minister must consider, but is not bound to accept, any advice or recommendation in this report in determining the licence application. The Minister may, if circumstances so require, seek further advice from us in relation to the licence application.

The Minister is required to provide us with a notice of his decision to grant or refuse a licence application and of the reasons for that decision.³³ We will then make the information in the notice available to the public on our website, in accordance with the requirements of the Act.³⁴

³³ *Water Industry Competition Act 2006*, section 10(5).

³⁴ *Water Industry Competition Act 2006*, section 10(6).