



29 September 2005

Mr James Cox
Chief Executive Officer and Full-Time Member
Independent Pricing and Review Tribunal of NSW
Level 2, 44 Market Street
Sydney NSW 2000

Dear Mr  Cox

Response to the draft report, *Investigation into Water and Wastewater Service Provision in the Greater Sydney Region*

Sydney Water Corporation welcomes the opportunity to comment on the draft report and submits the attached response.

Please contact Dr Chris Guest, Director, Regulatory Strategy and Reform on (02) 9350 4819 if you need any further information.

Yours sincerely



David Evans
Managing Director

Sydney Water Submission to the
Independent Pricing and Regulatory
Tribunal of NSW on the Draft Report,
*Investigation into Water and
Wastewater Service Provision in
the Greater Sydney Region*

September 2005

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Sydney Water Corporation welcomes the release of the draft report and submits the following comments on the recommendations of the draft report.

There are twenty-three recommendations in the draft report, which have been grouped into six categories for conciseness of response.

1. OUTSOURCING

Summary of recommendations

- Water authorities should use competitive sourcing to procure additional water supplies (R1)
- Water authorities should separate competitive sourcing activity from the rest of their operations (R2)
- Sydney Water should use outcomes-based procurement in other areas of service delivery (R3).

The greater use of outcomes-based competitive procurement is supported, providing its use is determined by reference to the relative cost effectiveness of external provision compared with internal provision, and is subject to Government policy.

To allow the use of outcomes-based procurement, Sydney Water supports the development of transparent costing systems. This would provide the information needed to benchmark the cost of internal provision of services against external provision, and thereby enable potential areas for outcomes-based competitive procurement to be identified.

Consistent with the adaptive management approach proposed in the draft report, use of outcomes-based competitive procurement should commence in areas where there is a need, the outcomes being sought can be clearly defined, and there are net benefits compared to internal provision and competitive sourcing of inputs.

In relation to bulk water supplies, Sydney Water is proceeding with competitive procurement arrangements for a desalination plant. So the next opportunities for competitive sourcing by outcomes may lie in other areas.

2. INDUSTRY STRUCTURE

Summary of recommendations

- Establish a state-based access regime for water and wastewater infrastructure, based initially on an 'negotiate and arbitrate' model (R4)
- Incorporate IPART's recommended framework into the access regime (R5)
- Access to water and wastewater be priced using the Efficient Component Pricing Rule (R6)
- Not undertake structural disaggregation of Sydney Water at this time (R7).

Sydney Water supports the introduction of a state access regime as recommended in the draft report.

A state access regime has benefits compared to an access regime established under the Commonwealth Trade Practices Act, as consumer protection and price regulation would be integrated with the other aspects of an access regime.

The framework outlined in the draft report sets out appropriate rules for an access regime, including: the maintenance of postage stamp pricing using the Efficient Component Pricing Rule; the use of a negotiate-arbitrate model, in the first instance; continued regulation of prices by the Independent Pricing and Regulatory Tribunal; and directed initially to large commercial and industrial users.

More work needs to be done regarding the potential gains and costs of the structural disaggregation of Sydney Water before any conclusion could be drawn. Further examination is needed to ascertain whether the benefits of either the horizontal or vertical disaggregation of Sydney Water would outweigh the costs. In particular, further investigation is required regarding the impact of disaggregation on the efficiency of service provision and operational management, and how to address differential cost structures. Sydney Water supports this work being undertaken.

It is noted that the implementation of a state access regime would of itself be a considerable structural change to the industry. The experience with a state access regime should be taken into account when other kinds of structural change are being considered.

3. REGULATORY REFORM

Summary of recommendations

- Identify and, where warranted, remove legal and regulatory impediments to private sector involvement and competition in water and wastewater markets (R8)
- Improve arrangements for collecting and disseminating information about the water and wastewater market (R9)
- Establish property rights for sewage and stormwater, and possibly the injection and removal of water from storage facilities (R10)
- Develop and apply across agencies guidelines for valuing environmental impacts associated with water services (R13)
- Ensure appropriate regulatory obligations are placed on incumbents and new entrants to protect consumers and the public interest (R17)
- Use IPART's proposed principles for the revised policy and regulatory framework to guide: short-term decisions under the existing framework and; a comprehensive review of the existing regulatory framework (R18)
- In the above review, take into account principles of best practice regulation, national competition reform principles and other characteristics (R19).

The existing legislative and regulatory framework is premised on Sydney Water being the sole provider of water and wastewater services. This framework comprises regulation of Sydney Water as a monopoly provider, in addition to regulation of water and wastewater service provision for the purposes of public health and securing desired environmental outcomes.

As described in the draft report, a legislative and regulatory review would be a substantial undertaking. To ensure resources are well used, such a review needs to be well targeted.

The aim of a review of the legislative and regulatory framework for water and wastewater service provision should be to identify unjustified barriers to entry into the water and wastewater market. However, a decision about which barriers to entry are "unjustified" cannot be taken without first deciding on the desired industry structure and the kinds of public policy protections required in relation to public health and environmental outcomes.

A state access regime, were it implemented, would require legislative changes so that responsibility for provision of services does not lie solely with Sydney Water, and to ensure that public policy requirements apply to all providers of water and wastewater services. Designing and implementing the required changes would be a substantial project. A decision on whether other changes should be made should await the outcome of the further work on industry structure reforms referred to in Recommendation 7.

4. RECYCLING

Summary of recommendations

- Ensure clear and robust guidelines are in place for all potential sources and applications of recycled water (R11)
- Review these guidelines regularly (R12).

Sydney Water agrees that gaps exist in the current regulatory framework for recycled water; which, in some cases, could hinder uptake of recycled water. As noted in the draft report, a number of guidelines and regulations are currently under review by the Natural Resources Management Ministerial Council and the Environment Protection and Heritage Ministerial Council, and Sydney Water is a key participant in these reviews.

5. PRICING

Summary of recommendations

- IPART continue to regulate prices for water and wastewater services to small customers (R14)
- Where regulated services are not provided by a government agency, establish the legal basis for price regulation (R15)
- Prices of water and wastewater services to large customers continue to be regulated, but reviewed if competition for large customers emerges (R16).

Sydney Water endorses the continued regulation by IPART of prices for services to both large and small customers to protect consumers, ensure equity of access and efficiency in the supply of services.

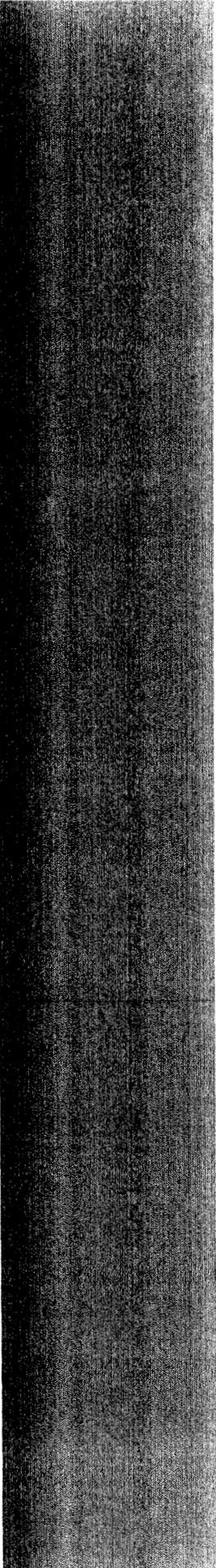
Sydney Water would support a review of the arrangements for price regulation for large customers, if competition for large customers emerges.

6. IMPLEMENTATION

Summary of recommendations

- Establish a central agency for one year to coordinate implementation of reform, reporting to a Cabinet Committee (R20)
- Develop an implementation plan for reform (R21)
- Progress implementation in accordance with a pragmatic approach and timetable that recognises the magnitude of potential gains, the relative ease of effecting change and a logical sequencing of decisions (R22).

Specific implementation arrangements would depend on the kind of changes determined by Government. If these changes were confined initially to a state access regime, competitive outsourcing by outcomes and recycling guidelines, then a new institutional arrangement may not be necessary. Sydney Water supports a gradual approach for progressing implementation of reforms, informed by experience. The



pace of change and lessons of experience should guide whether further reforms are necessary.

CONCLUSION

Sydney Water welcomes the directions set out in the draft report, *Investigation into Water and Wastewater Service Provision in the Greater Sydney Region*.

The key themes of the recommendations in the draft report – greater use of competitive procurement, development of a state access regime and no major industry restructuring, at this time – are supported.

Given the limited experience of competition in the industry and the need to ensure continued protection of consumers and the broader public interest, Sydney Water supports the measured and adaptive management approach proposed in IPART's draft report.