



10 October 2001

Dr Tom Parry
Chairman
Independent Pricing and Regulatory Tribunal of NSW
Level 2, 44 Market Street
SYDNEY NSW 2000

Attention: Mr Michael Sedwell

Dear Dr Parry,

I refer to your recent call for public submissions for the review of Hunter Water's Operating Licence. Accordingly, please find attached Sydney Water's submission to the review.

Sydney Water looks forward to working with the Tribunal to share any insights gained from its recent Operating Licence, system performance and Customer Contract reviews.

Sydney Water apologises for the delay in providing our submission and wishes to *thank* the Tribunal for their extension of time.

This matter is being conducted for Sydney Water by Mr Gavin Morrison, Manager Regulatory Strategy, who can be contacted on 9350 5827. In addition, I would be happy to discuss this matter further with you at any time.

Yours sincerely,

Richard Birrell
A/General Manager Corporate Affairs

IPART's review of Hunter Water's Operating Licence

Submission by Sydney Water

Overview

Sydney Water is a statutory state-owned corporation, wholly owned by the people of NSW. Sydney Water provides drinking water, wastewater services and some stormwater services to 4 million people in Sydney, Illawarra and the Blue Mountains by utilising assets in excess of \$13 billion.

Sydney Water has three equal statutory objectives – to protect public health, to protect the environment and to be a successful business. These objectives reflect customers' expectations of how Sydney Water should provide its water, wastewater and stormwater services.

Introduction

In 2000, the NSW Government introduced amended Operating Licences for Sydney Water and the Sydney Catchment Authority (SCA). The licences contain significant requirements regarding public health, system performance, customer protection and environmental performance. The licences also reflect the findings of the **McClellan Inquiry**, which addressed matters specific to Sydney's water supply and put in place arrangements for regulating the separate roles of Sydney Water and the SCA.

Since that time, IPART has assumed the role of Licence Regulator for the NSW water utilities and has conducted operational audits on Hunter Water and the SCA, with Sydney Water's audit currently underway. IPART has also set price paths for the NSW water agencies (October 2000 for the Sydney agencies), reviewed Sydney Water's system performance standards (April 2001) and is currently finalising the review of Sydney Water's Customer Contract (October 2001). These reviews have involved significant stakeholder consultation. IPART will also conduct the mid-term review of Sydney Water and the SCA's Operating Licences in January 2002.

IPART is required to determine appropriate regulations for the monopoly aspects of the NSW water agencies' operations. These regulations set compliance requirements for large asset bases that were constructed and managed before such regulations were contemplated. In addition to this, IPART must consider the significant development of other regulations that now apply to the water agencies, such as comprehensive environmental legislation administered by the EPA and DLWC. The water agencies' operating licences require them to comply with such requirements.

These developments underpin the principles that define the role of the operating licence in regulating the NSW water utilities. These principles are articulated in Hunter Water's submission for this review and include that:

- the principal focus of the operating licence should be standards of service and customer protection;
- regulation should be focussed on outputs and performance;
- regulated requirements must be important to customers and the community, within the control of the regulated agency, verifiable and able to be audited;

- licence standards should specify requirements to achieve system performance;
- licences should not duplicate the requirements of other legislation or regulatory mechanisms; and
- licences should not impose obligations on parties other than the regulated agency.

Sydney Water would add that the Operating Licence is essentially a franchise agreement with the Government that enables the water agency to provide water, wastewater and stormwater services in the long-term interest of the community.

Hunter Water's Operating Licence should be reviewed against these principles with regulatory requirements developed that reflect local conditions rather than cherry picking new or appealing regulatory requirements from other jurisdictions. Sydney Water also disagrees with any suggestion that Hunter Water should be required to comply with the same licence requirements that apply to Sydney Water without consideration of local factors, given the specific circumstances that applied to the development of Sydney Water's Operating Licence.

The review also provides an opportunity for stakeholders to further consider the best form of economic regulation for the NSW water agencies. For example, how can IPART use its broad powers under Part 3 of the *IPART Act 1992*, which relate to its price determination powers, to require agencies to provide robust performance information on an annual basis, thereby avoiding the inclusion of highly prescriptive requirements in the Operating Licence. This issue is particularly important in light of IPART's interest in more effective regulations for asset management to ensure the robustness of the water, wastewater and stormwater systems.

Drinking Water Quality Standards

Sydney Water views drinking water quality standards as one of the minimum customer requirements for inclusion in the Operating Licence. As such, Sydney Water supports Hunter Water's recommendation that it be required to meet the 1996 Australian Drinking Water Quality Guidelines (Guidelines) and any further iteration of them. Sydney Water also supports Hunter Water's recommendation that its 5-year Drinking Water Quality Management Plan and Incident Management Plan be included in the Operating Licence.

Sydney Water believes there should be clear arrangements within Government for determining the application of the Guidelines to the NSW water agencies. At present, both NSW Health and IPART are responsible for applying the health-related values of the Guidelines to the water agencies. The **1996** Guidelines are imposed directly by the Operating Licence with IPART assessing compliance with the Guidelines through the annual operational audit. NSW Health is responsible for specifying the application of any amendments, updates or supplements to the Guidelines, and through the Annual Monitoring Plan, defining how compliance against the health parameters of the Guidelines is to be applied. Sydney Water supports Hunter Water's proposal that its water quality standards be updated immediately or at the mid or end-term review, depending on the cost implications of compliance.

Sydney Water also notes the slight inconsistencies resulting from the duplication of reporting requirements in the *Sydney Water Act 1994*, memorandum of understanding (MOU) with NSW Health and the Operating Licence. This point is also

made in Hunter Water's submission for this review and that the MOU can change over the period of the Operating Licence.

Sydney Water does not oppose the requirements of Hunter Water's **MOU** with NSW Health being reflected in the Operating Licence. However, consideration should be given to making NSW Health solely responsible for setting all the health-related values of the Guidelines under a separate instrument.

System performance standards and measures

Sydney Water believes that system performance standards are fundamental to the Operating Licence as they ensure the integrity and robustness of the water, wastewater and stormwater services. IPART has previously identified the following as basic customer requirements for these services: drinking water quality, water reliability, water continuity, water pressure, sewage overflows, stormwater flooding and customer service.

Sydney Water supports the consideration of each of these basic customer requirements in this review, noting that very clear statements from the community and Government were made on these matters during the review of its system performance standards. IPART should consider these outcomes before recommending similar arrangements for Hunter Water's Operating Licence.

IPART's Issues Paper for this review notes that little is known at present about customer expectations and levels of satisfaction with the various performance measures and the relative importance of each standard to customers. It also commented that customer research on willingness to pay for higher levels of service is required if higher standards are to be introduced. Sydney Water notes the Commonwealth Scientific and Industrial Research Organisation's (CSIRO) current research on developing a methodology for determining customer service standards for water continuity. Sydney Water believes that developing a **straightforward** methodology for determining customer preferences for system performance standards is a key area where economic regulation in NSW can be improved. Until such a methodology is agreed, Sydney Water does not support higher standards being set in Hunter Water's Operating Licence. In the absence of effective techniques for determining customer preferences, Sydney Water believes that Hunter Water's standards should be required to reflect historic performance levels, below which service performance can not deteriorate. Hunter Water's submission for this review outlines areas where the current standards can be raised to historic performance. Hunter Water has also offered to collect indicator data to provide more information on the appropriateness of raising standards.

Sydney Water also supports the developing of a common method of standards measurement for NSW water agencies, noting that this does not mean that the same standard should be set for each agency. An effective methodology for determining standards should account for factors such as topography, customer density, age and configuration of assets, design standards, local economic facts, climate, etc. The Hunter Water submission outlines how existing standards can be retained with new measures recommended to allow comparison with other NSW water agencies.

Sydney Water does not support any recommendation that its standards and indicators should simply be transferred into Hunter Water's Operating Licence. It would also be useful if IPART's consultants for this review clarify at the public workshop for this review how it will approach the cost-benefit assessment it is required to undertake in recommending amendments to Hunter Water's standards.

Also, Sydney Water does not support asset management requirements being included in Hunter Water's Operating Licence. The price determination process is the most appropriate method for IPART to consider water agencies' asset management practices and associated expenditures. In line with the SCA's practices, Sydney Water has an Asset Management Strategy that it has prepared for its Minister in line with the Government's Total Asset Management Manual. This Strategy addresses the linkages between customer impact and service performance and system management plans. IPART might consider recommending a similar requirement for Hunter Water's Minister's consideration, if such action has not already been undertaken.

Environmental requirements

Environmental indicators and reporting

Sydney Water supports consistency in Operating Licence requirements regarding the environment, particularly with respect to developing a shared understanding of industry environmental issues, State of the Environment reporting and benchmarking between water and potentially other industries.

Best practice environmental planning and reporting is not only undertaken for compliance purposes. Effective environmental management (indicators, planning and reporting) needs to identify emerging issues, respond to them through internal planning processes and gauge the success of the reaction, irrespective of which regulator imposed the requirement.

The problems in regulating this area are highlighted by Sydney Water's environmental requirements, which have been built up and imposed on Sydney Water over time. At present, Sydney Water has to report on the special objectives required in the ***Sydney Water Act 7994*** plus the environmental and separate ecologically sustainable development (ESD) indicators and the Environment Plan requirements contained in the Operating Licence. This has required Sydney Water to invest considerable effort in interpreting these multiple requirements into a framework that makes sense of Sydney Water's environmental management practices.

Sydney Water believes that the environmental requirements set in Hunter Water's Operating Licence should avoid this ad hoc approach and reflect accepted international practice, such as the United Nations Environment Program's Global Reporting Initiative.

Sydney Water also supports the development of high level **ESD** indicators, with environmental indicators forming a subset of these requirements. These indicators should seek to show progress in specific areas when compared with performance in previous years. However, it is only by considering ESD indicators as a suite and analysing the trends over time that allow agencies to assess whether they are putting the principles of **ESD** into action. It is important that such indicators are not developed or used to assess indicator by indicator performance or short-term trends.

Environment Plan

Sydney Water supports Hunter Water being required to prepare an Environment Plan under its Operating Licence. An Environment Plan is also a requirement for an accredited Environment Management System and is used as an internal planning document for responding on an annual basis to environmental performance and the

success of identified actions and targets in achieving objectives. It is agreed that an Operating Licence requirement for a 5-year Environment Plan gives a longer term commitment to the environment as well as a greater degree of stability and assurity. It does, however, also mean that the Plan can become dated, wrongly promoting actions contrary to continual improvement and the changing needs of the community, regulators and the environment. IPART should consider arrangements that allow agencies to be responsive and adaptive in their Environment Plan whilst meeting the consultation and compliance requirements of the Operating Licence.

Sydney Water supports Hunter Water's request that performance and progress against its Environment Plan targets (rather than compliance) to be assessed in the annual operational audit.

Demand management

In relation to demand management, Sydney Water cautions IPART and the community against setting arbitrary water conservation targets. It is also very important that the purpose of such targets is made clear, for example, are they primarily to ensure that new and expensive dams are not required or do they have a broader resource management purpose. Sydney Water's experience in implementing its demand management requirements is that it is possible to meet prescribed targets, the question is how much money is the community prepared to spend to do this.

Hunter Water's submission makes clear that DLWC is the appropriate regulator of its demand and catchment management requirements. The vertical separation of Sydney Water and the SCA make it more important that IPART play a role in this important area of Sydney's water supply.

Sydney Water and the SCA are required to work on developing a water reliability standard for further consideration at the end-term review of both operating licences. The issues of security of supply, environmental flows, demand (and drought) management, water efficiency and water reuse are all caught up in this issue. Hunter Water has suggested that it develop a Security of Supply Plan, which would include a range of benchmarks and water recycling and demand and drought management requirements. It has also suggested that it develop a Water Conservation Strategy, which would encourage customers to continue to reduce water usage. Performance against these plans would be reported through the annual Environment Report.

Sydney Water believes that IPART needs to work with the water agencies to develop appropriate measures of water reliability in the lead-up to Hunter Water's mid-term review and Sydney Water and the SCA's end-term review of the Operating Licence.

Customer and consumer rights

Sydney Water is currently participating in IPART's review of its Customer Contract. The revised Customer Contract is to be considered by Sydney Water's Minister in October 2001 and renewed by Sydney Water in early 2002. The review has identified the role and purpose of the Customer Contract. There has been a high level of agreement between IPART, Sydney Water and key stakeholders on this matter and on the basic contents of the new Contract.

The review of Sydney Water's Customer Contract has sought to streamline the existing document and to simply reflect the requirements placed on Sydney Water and its customers under the ***Sydney Water Act 1994***, Regulations and Operating

Licence. This process has sought to limit the amount of unnecessary explanatory or technical detail in the Customer Contract on the basis that it can be communicated to customers in a summary pamphlet, which is required under Sydney Water's Operating Licence. It has been important to focus on the Customer Contract being largely for the majority of customers, while allowing individual customers to enter into special arrangements regarding service delivery and protecting the rights of special classes of customers, such as those experiencing financial hardship. Sydney Water has also sought to recognise the rights of consumers, as opposed to customers who are defined as property owners under the Customer Contract, to redress if they receive poor service. The only distinction made is that consumers do not have a financial relationship with Sydney Water. The clear articulation of Sydney Water's redress policy has also been important.

Other important elements of the review has been to clearly articulate the tiers of response for restricting or disconnecting customers for non-payment of bills, outlining customers' rights under the complaints handling process and clarifying customers' role in maintaining their own plumbing assets.

Sydney Water also supports Hunter Water's proposal to develop customer service indicators with IPART for further consideration at the end-term review of its Operating Licence in 2007.

Public reporting and other issues

Sydney Water supports the SCA's proposal that IPART consider biennial audits of the water agencies' operating licences. Audit methodologies should also be agreed on to ensure consistency in assessing the performance of each agency and further consideration should be given to the extensive reporting requirements that are placed on Sydney Water and the SCA in the lead-up to the annual operational audit.

In particular, Sydney Water would like to investigate other means of briefing IPART on its performance other than through the production of the annual compliance reports and recommends that more work be undertaken on streamlining IPART's information requests under Parts 3 and 4B of the *IPART Act 1992*.

A key matter coming out of the review of Sydney Water's system performance standards was the establishment of accuracy requirements for the amended standards and a Monitoring and Reporting Protocol with IPART for ensuring that these accuracy requirements are met. Sydney Water believes that IPART's consultants to this review need to further clarify the purpose of these requirements and how they can be implemented by the water agencies, where required.

Term of the Licence

Sydney Water believes that the Operating Licence and price path processes for the NSW water agencies need to be aligned to allow quality of service and price requirements to be set together. Sydney Water supports a 5-year licence term with a mid-term review, which should be used to make minor amendments and to identify issues requiring further consideration in the lead-up to the end-term review. Sydney Water **also** supports consideration being given to biennial audits to be staggered between each of the agencies.

Sydney Water supports the comments made by the SCA on this matter in its submission for this review.