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WATER INDUSTRY COMPETITION AMENDMENT (REVIEW) BILL 2014

Second Reading

The Hon. DUNCAN GAY (Minister for Roads and Freight, and Vice-President of the Executive Council) [5.40 p.m.]: I move:

That this bill be now read a second time.

I seek leave to have the second reading speech incorporated in *Hansard*.

Leave granted.

I am pleased to introduce the Water Industry Competition Amendment (Review) Bill 2014.

The Water Industry Competition Act—or 'WIC Act'—commenced in 2008. Through a licensing regime and a third party access regime, the Act facilitates new market entrants, and regulates their activities in order to protect public health, consumers and the environment.

The bill before us is the outcome of a comprehensive review of the Water Industry Competition Act that has involved extensive stakeholder consultation. It seeks to address current regulatory gaps, improve customer protection, cut red tape and remove unwarranted barriers to entry.

The bill narrows the scope of the current licensing regime to focus on those higher risk schemes that warrant expert regulatory oversight. It removes duplication with the Local Government Act and addresses an important regulatory gap relating to metropolitan councils.

Many metropolitan councils are currently operating recycling and stormwater reuse schemes that are not subject to any regulatory oversight. This creates risks to water quality and public health.

The bill mitigates these risks by bringing metropolitan councils into the Water Industry Competition Act framework.

Importantly, the bill significantly strengthens the last resort arrangements to ensure essential services are maintained in the unlikely event that either a retailer or an operator fails.

While the current Act includes provisions dealing with the failure of a ***retailer***, there are no such provisions to deal with the failure of a licensed scheme ***operator***.

The bill addresses this gap—and provides a flexible framework to enable a last resort provider to recover its costs.

The bill adds a new clause to remedy the absence of objects in the current Act.

The key objects now include:

- the protection of public health and safety, the environment and the interests of consumers—including in the longer term; and

- the facilitation of competition with a view to encouraging innovation and improved efficiency.

The objects clause refers explicitly to longer term considerations.

Experience in other markets has shown that short term approaches can impose inefficient costs in the longer term, and have adverse impacts for consumers, the broader community, and the environment.

The new objects clause also includes the aim of 'facilitating the efficient, reliable and sustainable provision of water and sewerage services, having regard for financial, environmental and social

considerations'.

This 'triple bottom line' approach is vital given the nature of the water industry and its potential for significant public health, environmental and social impacts.

The bill also includes a new test as to the ***suitability*** of parties seeking a licence or approval. This brings the Act into line with similar legislation, and will ensure that approvals and licences are only granted to appropriate entities.

In addition to the current requirement that applicants have the technical, financial and organisational capacity to undertake the proposed activities, the bill requires consideration of the degree to which an applicant relies on the capacity of contractors and subcontractors, whether those arrangements are suitable, and whether additional conditions are needed to address any issues arising.

This is a new requirement that will enable regulators to consider whether business models pose any risks in relation to the effective and efficient administration and enforcement of the Act, and impose any additional conditions considered necessary.

It is in the interests of all parties that companies entering the water market are reliable and robust—not 'two dollar companies' that may be unwilling to make the ongoing investments needed to maintain their assets and comply with all applicable standards.

For public water utilities who may be appointed as last resort providers, granting approvals and licences to such companies could increase the risk they will need to step in to maintain services to customers.

For private entities operating in the market, community acceptance of alternative providers would be eroded.

And most importantly for consumers, the need to protect public health and maintain essential services underscores the importance of only granting approvals and licences to suitable corporations.

I now turn to the proposed repeal of section 10 (4) (d) of the Water Industry Competition Act, an element of the bill that has received a great deal of attention.

While Section 10 (4) (d) Act does remove the existing requirement to source sufficient water other than from a public water utility, it is incorrect to suggest that the reform will enable Water Industry Competition Act licensees to simply become water re-sellers. In fact, the bill explicitly provides that this cannot occur.

Under the proposed reforms, services can only be provided by water industry competition retailers when they provide the infrastructure to deliver those services.

This requirement is consistent with the original policy intent of the Act to encourage new investment in water infrastructure. It also ensures that we do not see a market develop that would provide an incentive for retailers to increase sales in order to increase profits.

The whole notion that the amendments to the Act are opening the door for water re-sellers shows a distinct lack of understanding of the urban water market.

Due to the small margins in the urban water—retail margins in the electricity sector are around three times higher—there is little incentive to act as a re-seller, even if it was allowed.

In addition, the pricing principles set out in the Water Industry Competition Act require consistency with postage stamp pricing, meaning that private providers cannot undercut the public water utilities.

The claims that the amendments represent a step toward privatisation of water assets are similarly unfounded.

If privatisation was the objective, we would be seeking to stymie rather than facilitate competition with existing utilities.

During debate in the other place, a number of misleading statements were made about the consequences of repealing this provision.

The Government rejects those assertions.

We have specifically adopted a market model that is designed to ***protect*** water efficiency improvements, and does not incorporate full retail contestability. We have done this despite calls by some stakeholders that all limits on competition should be lifted.

Concern was also expressed that private operators will be able to purchase large amounts of water from public utilities and on-sell it to retail customers for a significant profit. This is based on a misconception that private entrants can get a discount if they buy in 'bulk' from Sydney Water.

In fact, all customers who buy drinking water from Sydney Water pay the same price per kilolitre—there is no discount for buying 'in bulk'. Under IPART's Act, Sydney Water and Hunter Water cannot legally sell water for less than the price set by IPART, unless the Treasurer grants approval—and the Treasurer has never done so.

Similarly, if a new entrant was to use the Water Industry Competition Act's access regime to enter into a water supply agreement with another water authority—rather than just buying water direct from Sydney Water—there are provisions to ensure that access prices are in line with IPART's pricing determinations and 'postage stamp pricing'.

Provisions will also be retained to prevent a new entrant from undercutting Sydney Water. These were included in 2011 to ensure that all in Sydney Water's area of operations contribute fairly to the cost of infrastructure that secures our water supply.

In short, you cannot get a discount for buying in 'bulk'.

It is also wrong to suggest—as several did in the other place—that private licensees will be able to charge whatever they like, to the detriment of households across New South Wales. In fact, the bill makes a number of changes designed to boost customer protection.

For example, it introduces a new test whereby IPART ***must not grant*** construction approval unless satisfied that a proposed greenfield or infill development—called a 'category A scheme' in the bill—will not have significant adverse financial implications for residential and small commercial customers. IPART must also be satisfied that the scheme is financially viable.

This turns the current licensing principle in section 7 of the Act into a concrete test that the proponent must meet before approval can be granted. In addition, for customers of such schemes, contract terms will be prescribed in the regulation to ensure customer interests are protected.

The bill also requires new information to be included in planning certificates to notify purchasers if a property will be serviced by a water industry competition licensee. In this way, buyers can find out about water and sewerage charges upfront.

Licensees will be required to publish their prices, and customers must be notified at least six months in advance of any increase.

IPART must also be notified of any price variation, and licensees cannot lawfully recover the new charges if they have not given the required notice.

If a private licensee is charging high prices for their services—and the customer has the option of switching back to a public water utility ¬they will be able to 'vote with their feet' and change supplier. In these circumstances, private licensees will have a strong incentive to conduct their business in a way that does not turn customers away.

If the customer does not have the option of switching supplier, the Minister may issue a monopoly supply declaration under section 51 of the current Act, and request IPART to determine the price to be charged.

The Minister also has power to impose licence conditions on retailers to protect the interests of customers. For example, the Minister could impose conditions if licensees were considered to be 'price gouging'.

Another view expressed in the other place is that consumers will be 'left high and dry' as private companies do whatever they want.

Customers ***will not be left high and dry*** under these reforms.

However, they could be if the bill is not passed—and the proposed reforms to licensing, scheme approval and last resort arrangements are not strengthened. Customers—and the broader community—could also be adversely affected if metropolitan councils continue to go unregulated.

Concern was also expressed that the reforms will jeopardise water quality. This too is unwarranted.

The Government is very conscious of the need to ensure that infrastructure is built to appropriate standards and is appropriately maintained over time. The bill includes a number of provisions to do just that.

It greatly strengthens the approval process for schemes to ensure that, before construction, scheme designs accord with national water quality guidelines.

This includes a new requirement that scheme designs are signed off by an independent auditor to give confidence all schemes will meet relevant standards.

Licensees will be subject to the same water quality requirements as public water utilities.

As with the current Act, the quality of water produced by a scheme must be rigorously tested after construction and commissioning—and before commercial operation can begin. Again, this involves checking by an independent auditor that the water complies with relevant public health requirements.

It was suggested in the other place, that—if the bill is passed—private operators will be able to purchase water from Sydney Water or another authority, instead of being required to put 'reservoirs and other water harvesting vehicles' in place on a new development site.

A few facts are in order.

The current situation—with section 10 (4) (d) in place—is that every water industry competition licensed scheme providing services to new greenfield and infill developments is sourcing drinking water as a large customer of Sydney Water. None of them have opted to invest in their own supply of ***drinking water*** since that would be hugely costly and inefficient.

Instead, they are recycling effluent and providing it back to customers for non-potable use through dual reticulation schemes. In some instances, they are also harvesting stormwater—but none have installed large reservoirs.

Section 10 (4) (d) says nothing about investments of this sort—it simply refers to sourcing water other than from a public water utility. It does not say what kind of water, or how much is sufficient, or whether the water should be from a new source—and the current regulations are also silent on these matters.

Those opposed to the bill have suggested that the Government thinks there will not be future droughts—hence our willingness to remove section 10 (4) (d). They even went so far as to suggest that Sydney would run out of water if there is a future drought as severe as the millennium drought.

This suggestion is both wrong and irresponsible.

The Government has a robust plan in place to make sure Sydney never runs out of water, and it is wrong to suggest that the reforms before us pose any risks to water security.

The licencing principles ***retained under this bill*** include having regard for 'the promotion of policies set out in any prescribed water policy document'.

The Government's Metropolitan Water Plan is such a policy document. It identifies the optimal portfolio of supply and demand measures to ensure Sydney can meet its water needs, both during drought and for the longer term.

For example, the operating rules for the desalination plant were set out in the 2010 Metropolitan Water Plan, and are given effect through conditions imposed on the Water Industry Competition Act licences held by Sydney Desalination Plant Pty Ltd.

In addition, the current water industry competition regulation empowers the Minister to impose drought restrictions on both public water utility customers and customers of water industry competition licensees. This will not change under the reforms.

The Government is acutely aware of the drought affecting many parts of New South Wales.

We support investment in infrastructure that promotes drought resilience. That is why we want to ensure that requirements are imposed in an effective way—one that cannot easily be avoided, as can the current requirement—and in a way that applies both to public and private utilities.

Placing requirements on private utilities that are not also imposed on public utilities makes it even harder for private utilities to get a foothold in the market.

Experience has shown that when they do, they bring with them innovative and sustainable solutions.

If they do not succeed in entering the market, the section 10 (4) (d) objective of encouraging private investment in alternative water sources *will not be realised*. Business as usual will prevail—and that means public utilities delivering services in what are generally conventional, centralised ways.

There is a range of reasons why private water utilities currently find it difficult to compete with the large public utilities.

The Government acknowledges this and is examining these issues, particularly in connection with their impact on housing supply.

However, many of these matters are outside the scope of the Water Industry Competition Act and cannot be addressed by these reforms.

I note finally the suggestions that removing section 10 (4) (d) is part of a wider plan to 'fatten up Sydney Water for sale'. This assertion makes no sense.

The removal of section 10 (4) (d) is designed to ***facilitate competition*** by creating a more level playing field, allowing new entrants to compete more effectively with incumbent utilities like Sydney Water.

If we wanted to shore up Sydney Water's business, we would be seeking to ***stymie*** competition rather than ***facilitate*** it. We would be ***retaining*** section 10 (4) (d)—making it harder for new entrants to compete—rather than ***removing*** it.

Most importantly, the bill makes important and long overdue changes to ensure that the Water Industry Competition Act can effectively protect public health and consumers, while removing unnecessary red tape.

I commend the bill to the House.