

13 September 2007

Mr Greg Watkinson
Director References and Research
Economic Regulation Authority
6th Floor, Governor Stirling Tower
197 St Georges Terrace
Perth Western Australia 6000

Dear Mr Watkinson,

Attached is a brief submission to your Inquiry into Competition in the Water and Waste Water Services Sector.

My interest in this issue goes back more than a decade, when I was an active member of the Federal Senate prior to the introduction of National Competition Policy. I worked for over two years lobbying for the Senate to conduct an inquiry into its consequences after its introduction. I then travelled the country as a member of the Senate Select Committee which conducted the inquiry into the Socio-Economic Consequences of National Competition Policy until the completion of my Senate term in 1999.

I then undertook research for a Masters Thesis (completed in 2001) at Murdoch University on National Competition Policy, in relation to the way it dealt (or failed to deal with) the public interest issues associated with some of this state's most anti-competitive legislation, State Agreement Acts.

As an MLC, I was a member of the Finance and Public Administration Committee which conducted a major water inquiry. Now, having finished my term as an MLC for the Agricultural Region, (where the National Competition Policy water policy changes are having had a wide range of impacts), I am in my second year of a PhD at UWA on the Outcomes of National Competition Policy, as the first PhD student attached to the new Australian Global Studies Research Unit at UWA.

I therefore appreciate the opportunity of commenting on your issues paper.

Yours sincerely

Dee Margetts

**Comments on the Terms of Reference and Issues Paper for the
ERA Inquiry on the Water and Wastewater Services Sector**

By Dee Margetts

September 2007

Introductory Comments

Firstly, before commenting on the Issues Paper, it should be noted that there are some particular issues associated with such a major policy change as National Competition Policy.

One is the ratchet effect. Any changes which reduce regulation in Australia's utilities are very hard, if not impossible, to reverse under the current administration of National Competition Policy. Even those aspects of legislation and administrative practises which have so far gained an exemption from NCP reform are continually reviewed. It is the affected industry or community sectors which, under the reversal of the onus of proof, have to continually make the (narrowly judged) public interest case for exemption. The assumption is that any effective opposition will diminish in strength over time or eventually disappear.

Another major issue is that, despite the enormity of the policy change, there are no built-in systematic checks to find out whether the NCP changes are achieving their assumed or stated goals. There is no way that even a business would implement a major policy change in this manner.

In 1995, at the time NCP was introduced, the legislative package was limited to just 1 day of committee hearings before being pushed through the Senate. The Institute of Engineers gave evidence expressing concern about the such important impacts such the potential loss of intellectual capital, and offered to provide evidence of the impacts of such changes in the UK, but they were denied the opportunity to obtain and present such evidence.

Altogether, this means that even greater care should be taken before pushing through further major policy changes such as the deregulation (and re-regulation under new market-based rules) of such an essential service as water in Western Australia. Even though this paper makes mention of competition in other countries such as England and Wales, it does not mention the range of problems associated with such policy changes, problems which can be located by a basic internet search!

A few years ago, I attended a seminar on water benchmarking, and I have to say it was horrifying to see how the global corporate sector, was pushing for a lowest common denominator approach to something as vital as water supply.

Terms of Reference

Like many aspects of NCP, the "key areas of focus" are to "enhance competition" in the water and wastewater sectors, with the built-in assumptions that it will bring "enhanced efficiency". This ignores the fact that private profit is exactly that – money which is taken out of the public purse and not necessarily reinvested for the public benefit. There is also no definition of what the state Government mean by "enhanced efficiency" when it comes to such a vital service as water.

Such vital issues as the social and environmental impacts are only dealt with in the terms of reference in a similar way as they are in the original Federal NCP legislative package, that the Authority should "have regard to" the impact of these reforms of

the Government's social, economic and environmental **policy directions**, NOT what the impacts actually are, and how they may affect the cost/benefit balance.

Most notably, in the terms of reference in such a vital service as water, there is no requirement to consider the potential health risks of poor market-based choices in the future.

Foreward

Reflecting the assumptions in the terms of reference, the ERA Chair, Lyndon Rowe goes even further in his assumptions, but stating that the ERA intend to Examine the “**extent** to which increased competition could improve efficiency, effectiveness and sustainability of the provision of water and wastewater services” not “whether” increased competition will achieve such aims.

There would be many people in the community who would be far from convinced that “increased competition” will lead to increased sustainability in such a vital sector as water.

P 1

Again the Authority is “required to have regard to” the impact of the reforms on Government's social, economic and environmental policy objectives” – not what **are** the likely social, environmental or even actual economic outcomes, just whether the decision have effects on **policy objectives** (whatever they may be). And once again NO mention of potential health outcomes of market-based water policies.

P 2

There is, at least one mention of the “essential nature” of services such as water, as to why, traditionally such services have been provided by State Governments – no mention, however, of why water is no longer considered a service, which should not be left to the free market, profit motives and “greed”, the factors on which markets are generally based.

There is a mention of the “corporatisation of many government businesses”, assuming that this step was positive in each of the criteria mentioned? In the case of the Water Corporation, one important effect was the separation of many aspects water management policy from the business of water provision, which resulted in, amongst other things, a major push from the Water Corp to get the Government to allow them to thin or clear water catchments to increase their access to water flows, (regardless of the potential impacts on the future quality of the water in those catchments), because the impacts on salinity or other potential water contaminants would be the financial responsibility of the taxpayer via the very underfunded Water and Rivers Commission, as it was.

There is also mention of the “national arrangements” for broad water policy framework, but, of course, those national arrangements were designed largely around the circumstances of the Murray Darling Basin, which is largely a surface-water based system – quite different from the circumstances in Western Australia. No mention

either that the \$10 billion national Water Security Plan was being paid for by the Federal taxpayer to fix up the problems which have been made even worse by the NCP water “reforms” in the face of drought.

Mention is made of the Department of Water’s oversight of water entitlement systems, atwater trading and water metering, following the Irrigation Steering Committee review of 2005, but no mention of the links between irrigation issues and scheme water. For instance, in the period following the 2001 water policy changes in WA, the Water and Rivers Commission freely gave out water licences for crops, which, in many instances were linked to managed investment schemes and which were never likely to be commercially sustainable. They gave out sometimes large allocations of water, to the detriment of real farmers in many instances, without requiring best practice in water use as part of any licence conditiona, on the understanding that once the water was fully allcoated, holders of such licenses could then sell their water allocations, that is make money out of a public asset they never paid for in the first place. Water and Rivers did this without fully consulting the Department of Agriculture and with minimal environmental assessment. Or any overall irrigation management strategy for dry land irrigation. The market is a blunt instrument, and is unlikely to deliver in many policy areas without specific and appropriate regulation especially as private allocations now often compete with the public water system for the same resource.

It is hard to justify assessing the future market directions for scheme water without linking it to the overall water mangement policies, (or lack thereof) in Western Australia. This situation is made worse by the unjustified secrecy relating to water allocations (especially if you compare it to the public nature of mining licenses). The taxpayer, and general community are denied such basic information on the area under cropping even of those who have been allocated large amounts of this public resource. Before going any further with any further market-based polices, ALL of the current water irrigation licences should be fully audited for water use efficiency and whether best practice water efficiency is being implemented. Their “free” allocation should be limited to world’s best practice water efficient usage for the area under cropping. Anything in excess of what their actual crops really need should be redeemed, and not be made available for sale for private speculative profit! Only if irrigators chose to reduce the area under irrigation, should they be permitted to sell the water allocation that they no longer require.

P 3

There is, at least, some recognition that markets can “fail to deliver benefits to consumers”, but as the paper progresses, it shall be seen that most of the emphasis is on price, not on service, reliability, equity or sustainabilty, let alone health risks.

P 5

The section on competition includes a discussion of what the controversial issue generally referred to as “contestibility”;

“Even in situations where a market is served by a single company, the threat of an additional business entering the market can exert competitive pressure leading to efficient outcomes for customers.”

There is also discussion that “*competition for customers*” will lead companies to seek the “*lowest cost way of producing products and services*”. This commoditisation of a vital resource can lead to a distinct conflict in the other policy values such as health and the environment, and may limit the investment in long term infrastructure.

Mention is also made of the market-based assumption that competing companies will lead to resources (water) being allocated to where they are most valuable, however, relying on market signals, can mean that decisions for long term sustainability may not be made in time. In Western Australia, significant water resources have been allocated to eucalyptus plantations on soil which is unsuitable, and to larger numbers of olive plantations than there is currently a market to sustain (and individually allocated more water than what experts agree is needed for high quality olive oil).

There is talk of **manufacturing** a product (water!) so cheaply that the company starts to attract more customers. This is emphasising the commercial desire to sell more of a **product**. This is hardly a sustainable model for a nation suffering the effects of climate change. In areas of dry land irrigation, what are impacts of increased water use on salinity and water logging? That is, making water cheaper with insufficient regulatory control. may create greater environmental costs for the future.

There is mention of the instances where the “ability of competition to deliver benefit to consumers is constrained, but the discussion following that statement refer only to price and profits, not reliability or guaranteed safety etc.

P 6

There is a brief mention of “public health risks” but no details.

There is an unsupported statement which follows; “*Economic efficiency achieved through competition requires that environmental and other related factors are appropriately brought to account to ensure sustainability.*” This statement is certainly not supported by the manner by which the National Competition Council has so far gone ahead with their so-called “public interest” assessments.

P 7

The discussion of monopolies once again focusses on price assumptions, but there is no discussion of what happens to private profit as opposed to money that has, up until now been reinvested in public infrastructure and services.

The discussion on “vertically integrated businesses” make no reference of the differences of consideration required when considering a vital service such as water.

P 8

Considering the emphasis on price, where a “healthy disease-free environment” is mentioned, it is referred to as “a significant benefit” not an essential requirement of the delivery of a vital asset?!! There is mention of the undesirability of turning off a service such as water for those unable to afford to pay, but evidence from the 2001 Public Services International Research Unit (PSIRU) on Water Privatisation in the UK indicates that the rates of disconnection have considerably increased since putting water services into commercial hands.

P 9

There is mention of the reason why this inquiry is concentrating on potable water, (because there are more dollars to be made from it) but does not make the obvious connection between policies for scheme water and water from the same sources used for other purposes.

P 10

Mention is made of the levels of profits by the Water Corporation but no discussion that at least, as a public corporation, the likelihood is that that profit will or can be invested in future public infrastructure whereas a private corporation have no such obligation. The PSIRU research from the UK also indicates that private corporate profits rose in commercial hands, whilst prices to consumers grew at a higher rate than before.

P 12

In the discussion of the Water Corporation’s responsibilities, there is no mention of what used to be the underfunded Water and Rivers, whose role included is/was to monitor and protect WA’s water resources and that the separation of these functions in 1995 leaving the Water Corporation with the money but Water and Rivers (or their successor) with the responsibilities in water monitoring and protection without a revenue stream has been far from satisfactory.

P 13

There is mention of the outbreak in NSW in 1998 of *Cryptosporidium* and *Giardia* but no mention of how much market factors and profit motives were involved or indeed how these problems may have been associated with the same kinds of loss of intellectual capital which the Australian Institute of Engineers were trying to bring forward before NCP was introduced in 1995.

P 16- 20

The section on New Zealand is very brief and does not mention any of the problems which have been experienced since the contracting out of water services to the private sector. (and how that is impacting on current policy decisions in New Zealand).

The section on England and Wales is longer than that for New Zealand but appears to have left out some of the most important issues. In the PSIRU Report, these are covered under such headings as :

- disconnections and public health
- market failures no incentive to improve efficiency
- profits as fastest growing component
- inadequate investment and regulation
- cut investment to maintain dividends
- droughts
- leakage, low pressure and interruptions
- sewer flooding
- water quality
- environment and pollution
- Ofwat lack of responsibility
- Ownership and takeover
- etc

Why have such important issues, including the impacts on community equity, not been canvassed in this draft paper?

P 21

The above discussion on market-based structure in other countries is followed by a section called “*emerging themes*” but they are only the themes that the report has chosen to mention, not the important issues that have been left out.

P 26

The section on “comparative competition” once again refers to the system adopted by Ofwat in England and Wales, without mentioning the increased problems that consumers have experienced there.

P 29-30

The reference to the some “perceived problems” of market dominance and water hoarding makes no mention that much of these problems have come to light since the 2001 legislative changes and the apparent position taken by Water and Rivers that their role was to allocate as much water as quickly as possible without systematically checking what the long term impacts of such allocations would be on WA long-term water sustainability, on existing industries, neighbouring communities and the environment.

In relation to CSOs, the statement;

“The case of service provision to uneconomic customers is no different to any other instance where goods and services are sought” does not appear to take into consideration the evidence, once again, from the UK (PSIRU, 2001). In a situation where the market was not significantly profitable, taxpayers funds, had then to make up for years of investment shortfalls. That is, private profits, public risk – very relevant for water.

P 35

Under “*Further matters*”, I would like to emphasise that the systematic assessments of the real outcomes in other jurisdictions should be properly considered, and the views of Engineers Australia and the Australian Hydrogeologists Association, environmental scientists sought as well as a balance from a range of affected parties.

This process appears to be moving too quickly to include the proper checks and balances and, as previously mentioned, in the one way ratchet process of Australia’s National Competition Policy, this can be a very dangerous position to take.

If anything, what the experience of other jurisdictions is telling us (not just from the views of the proponents of such change but those affected) is that if you were even to contemplate moving further in this direction, you must INCREASE and not DECREASE your regulatory framework but even that may not be sufficient to prevent social, environmental and health disasters.

This is about water, not just any commodity.

Reference:

Public Services International Research Unit (2001) UK Water privatisation – a briefing by Emanuele Lobina, Research Fellow, PSIRU, University of Greenwich, and David Hall, Senior Research Fellow, University of Greenwich.