

Mr Joe Dimasi
Senior Commissioner
Independent Competition and Regulatory Commission
PO Box 161
Civic Square ACT 2608

Via email: icrc@act.gov.au

Dear Senior Commissioner Dimasi

Issues Paper - Incentive Mechanisms for Water and Sewerage Price Regulation

The ACT Council of Social Service (ACTCOSS) represents not-for-profit community organisations and advocates for social justice in the ACT.

We welcome the opportunity to provide feedback on the Independent Competition and Regulatory Commission's (ICRC's) Issues Paper on Incentive Mechanisms for Water and Sewerage Price Regulation.

About our submission

ACTCOSS plays a role as a consumer advocate on energy in the ACT. In this role we have engaged in discussions with ACT consumers about incentive mechanisms for electricity and gas networks. Incentive mechanisms for electricity and gas networks are based on similar principles to incentive mechanisms for water and sewerage. The information collected through our consultations on energy has helped to inform this submission.

ACTCOSS also has a broader concern with the affordability of energy, water and sewerage, and telecommunications, as essential services for people living on low incomes or experiencing disadvantage.

We welcome the fact that, under its regulatory objectives and pricing principles for water and sewerage tariffs, the ICRC needs to balance economic efficiency considerations related to pricing with environmental and social considerations. This includes the following pricing principle:

Community impact – fair outcomes for low-income households

Adverse impacts on households with low incomes need to be limited or moderated by phasing and other compensating mechanisms or limits on changes to regulated prices or other regulatory arrangements.

The Issues Paper

Through the Issues Paper, the ICRC is seeking stakeholder input on the current incentive mechanisms and on how the Commission proposes to approach the Review. This is being conducted ahead of the ICRC's next price investigation for the regulatory period from 1 July 2023.

Our submission responds to the three of the questions in the Issues Paper.

Do you have any comments on the overall approach the Commission has proposed to adopt for its review of incentive mechanisms?

The ICRC's planned approach involved:

- Release of an issues paper (4 December 2019)
- Submissions on issues paper (28 February 2020)
- Workshop (Late March 2020)
- Draft report (Late April 2020)
- Submissions on draft report (July 2020)
- Final report (Late August 2020).

ACTCOSS supports this approach. We understand that due to the COVID-19 pandemic the ICRC decided to cancel the workshop. In late March 2020, the ICRC contacted ACTCOSS in order to seek a consumer group perspective. Subsequently, ACTCOSS and the ACT Civil and Administrative Tribunal (ACAT) met with ICRC staff via videoconference on 14th April 2020 to discuss the Issues Paper and provide verbal feedback. This submission reiterates the feedback ACTCOSS provided at the videoconference as well as some further considerations.

A workshop would have provided a useful opportunity for stakeholder discussion of the issues and options identified in the

Issues Paper. Given the technical nature of the issues, there would have been value in providing an opportunity for a 'deep dive' into the current incentive mechanisms and others adopted by other regulators. We would encourage the ICRC to consider the option of utilising its Consumer Consultative Committee as an established forum through which to explore such issues in future.

ACTCOSS would recommend that the ICRC keeps open the option to convene a videoconference with stakeholders following the release of the Draft Report should any concerns be raised or identified during the interim period. This could be done through a meeting of the ICRC Consumer Consultative Committee.

Given the technical nature of this review, some additional independent analysis would have provided valuable support for consumer engagement. To assist consumers in providing feedback through consumer engagement forums, the presentation of evidence on the relative performance of Icon Water under the current incentive mechanisms (e.g. efficiency and/or price comparison with other regions) would have been valuable. Providing this analysis and evidence would also have helped build consumer confidence in the process and outcome.

We recommend that the ICRC's Draft Report include an assessment of the strengths and weaknesses of current incentive mechanisms and if/how any other incentive mechanisms used by other regulators might address any weaknesses and be appropriate to the ACT.

Ideally, this would include evidence of the relative benefits and costs for consumers, including any anticipated price impacts. If possible, it would also be useful to compare Icon Water's performance on price and service quality with other regions/water and sewerage services providers.

Are the current incentive mechanisms used by the Commission appropriate?

The purpose of the current review is to ensure that the ICRC's approach to determining water and sewerage prices provides appropriate incentives for Icon Water to operate efficiently. Incentive mechanisms are an important tool in the ICRC's approach to regulation as they encourage regulated businesses to pursue efficiency improvements (such as improved services and financial outcomes) that can be shared between the business and consumers. Any changes to the incentive mechanisms will be implemented in the regulatory period after 30 June 2023.

The ICRC's current approach to incentive mechanisms include:

- an 'efficiency dividend' for **operating expenditure** – if Icon Water can exceed the efficiency dividend and lower its operating costs below the level of costs that was accepted by the Commission, Icon Water will increase its profits in the regulatory period.
- assessment of the prudence and efficiency of Icon Water's proposed and actual **capital expenditure** at the beginning of the regulatory period (ex-ante review) and as part of the assessment for the next regulatory period (ex-post review).
- minimum **service standards** imposed through the Customer Protection Code as guaranteed service levels (GSLs). The GSLs require Icon Water to provide rebates (payments) to customers when service standards are not met. Further, the Commission requires Icon Water to report on actual outcomes for service standards against the targets set in the Code.
- The 'deadband' **price control mechanism** provides an incentive for Icon Water to manage demand risk carefully, including by identifying potential efficiency gains. It also provides greater incentives for Icon Water to invest in more accurate models for forecasting demand.

Our understanding is that the ICRC's regulatory objectives and pricing principles have been relatively successful in the ACT and have helped drive improvements to affordability and service quality for ACT water and sewerage customers. As indicated above, we recommend that the ICRC present any available evidence on this in the Draft Report – for example, the benchmarking of Icon Water's performance against providers in other jurisdictions.

A risk that arises with incentive mechanisms, for operating and capital expenditure, is that efficiency may be pursued at the expense of service quality. We are reasonably confident that this risk is effectively mitigated through the GSLs. We believe that this has been further strengthened through the recent amendment of the Consumer Protection Code requiring automatic payment of rebates to customers where GSLs are not met.

For ACTCOSS, a further and fundamental strength of the current approach is that the ICRC must take account of equity and other social impacts, including fair outcomes for low-income households.

What factors should the Commission consider in judging whether an incentive mechanism is suitable for Icon Water? Are there any ACT specific considerations?

The ICRC's legislated objectives require it to facilitate an appropriate balance between efficiency and environmental and social considerations. The ICRC must also promote the efficient investment in, and efficient operation and use of, regulated services for the long-term interests of consumers in relation to the price, quality, safety, reliability and security of the service.

In order to achieve these objectives, ACTCOSS considers the following three factors as being critical to achieving social justice in relation to the efficient provision of water and sewerage services in the ACT:

- equitable distribution of risk so that those exposed to risk to have the ability and incentive to manage it
- fair outcomes for consumers – especially for low-income households – in terms of price, quality, safety, reliability and security of the service
- sustainable use and management of water resources – including ensuring cultural flows for Traditional Custodians.

If you have any questions in relation to our submission, please contact [REDACTED], Senior Policy Officer, ACTCOSS on [REDACTED]

Yours sincerely

[REDACTED]

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Chief Executive Officer

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22 April 2020